

**Financial Statements
and Supplemental Information**

Naval War College Foundation, Inc.

December 31, 2009 and 2008



Mayer Hoffman McCann P.C.
An Independent CPA Firm
Tofias New England Division

NAVAL WAR COLLEGE FOUNDATION, INC.

Financial Statements and Supplemental Information

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Independent Auditors' Report

The Board of Trustees
Naval War College Foundation, Inc.
Newport, Rhode Island

We have audited the accompanying statements of financial position of the Naval War College Foundation, Inc. (a non-profit organization) as of December 31, 2009 and 2008, and the related statements of changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of the Naval War College Foundation, Inc.'s management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with U.S. generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Naval War College Foundation, Inc. as of December 31, 2009 and 2008 and changes in its net assets and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

Mayer Hoffman McCann P.C.

June 2, 2010
Newport, Rhode Island

NAVAL WAR COLLEGE FOUNDATION, INC.

Statements of Financial Position

December 31,
2009 2008

Assets

Cash and cash equivalents	\$	1,425,747	\$	3,095,966
Interest receivable		33,793		33,903
Contributions and grants receivable, net		269,560		601,749
Life memberships receivable, net		23,801		34,312
Investments		15,009,929		10,986,993
Inventory		173,043		167,487
Prepaid expenses		478		875
Furniture and equipment, net		74,750		32,819
Historical collections		67,598		67,598
		<u> </u>		<u> </u>
Total assets	\$	<u>17,078,699</u>	\$	<u>15,021,702</u>

Liabilities and Net Assets

Liabilities:

Accounts payable and accrued expenses	\$	101,599	\$	145,802
Capital lease obligation		6,052		10,899
Gift annuities		76,733		49,949
		<u> </u>		<u> </u>
Total liabilities		<u>184,384</u>		<u>206,650</u>

Net assets:

Unrestricted		5,816,756		3,442,669
Temporarily restricted		3,137,488		2,333,942
Permanently restricted		7,940,071		9,038,441
		<u> </u>		<u> </u>
Total net assets		<u>16,894,315</u>		<u>14,815,052</u>
		<u> </u>		<u> </u>
Total liabilities and net assets	\$	<u>17,078,699</u>	\$	<u>15,021,702</u>

See accompanying notes to the financial statements.

NAVAL WAR COLLEGE FOUNDATION, INC.

Statements of Changes in Net Assets

	<i>Years Ended December 31,</i>	
	<i>2009</i>	<i>2008</i>
Changes in unrestricted net assets:		
Support:		
Corporate members	\$ 190,200	\$ 192,500
Individual members	186,150	226,013
Graduate members	111,960	115,380
Unrestricted contributions	496,530	673,858
Total support	984,840	1,207,751
Revenues (expenses):		
Museum store sales, net	72,624	67,977
Investment income (loss), net, and for 2008 reclassification to permanently restricted net assets to maintain historical purchasing power	788,018	(2,265,672)
Special events, gross	55,927	37,768
Publication royalties	685	1,731
Total revenues (expenses)	917,254	(2,158,196)
Net assets released from restrictions and transferred:		
Net assets released from restrictions	487,210	597,897
Reclassification from temporarily restricted for prior year endowment loss charged to temporarily restricted	1,507,233	-
Net reclassifications at donors' requests	(1,000)	2,292
Total net assets released from restrictions and transferred	1,993,443	600,189
Total unrestricted support and revenues (expenses)	3,895,537	(350,256)
Expenses:		
Foundation grants	693,903	847,823
Program services	383,874	387,589
Management and resource development	443,673	479,373
Total expenses	1,521,450	1,714,785
Change in unrestricted net assets	2,374,087	(2,065,041)

See accompanying notes to the financial statements.

NAVAL WAR COLLEGE FOUNDATION, INC.

Statements of Changes in Net Assets (Continued)

	<i>Years Ended December 31,</i>	
	<i>2009</i>	<i>2008</i>
Change in temporarily restricted net assets:		
Contributions	\$ 225,214	\$ 444,570
Gifts in kind	9,007	-
Investment income (loss)	1,353,995	(1,012,174)
Reclassification from unrestricted for prior year endowment losses charged to unrestricted	(1,507,233)	-
Net assets released from restrictions	(487,210)	(597,897)
Reclassification of accumulated earnings due to change in law	1,208,773	-
Net reclassifications at donor's requests	<u>1,000</u>	<u>(2,292)</u>
Change in temporarily restricted net assets	<u>803,546</u>	<u>(1,167,793)</u>
Change in permanently restricted net assets:		
Contributions	110,403	39,150
Investment income	-	89,103
Reclassification of accumulated earnings due to change in law	<u>(1,208,773)</u>	<u>-</u>
Change in permanently restricted net assets	<u>(1,098,370)</u>	<u>128,253</u>
Change in net assets	2,079,263	(3,104,581)
Net assets, beginning	<u>14,815,052</u>	<u>17,919,633</u>
Net assets, ending	<u>\$ 16,894,315</u>	<u>\$ 14,815,052</u>

See accompanying notes to the financial statements.

NAVAL WAR COLLEGE FOUNDATION, INC.

Statements of Cash Flows

	<i>Years Ended December 31,</i>	
	<i>2009</i>	<i>2008</i>
Cash flows from operating activities:		
Changes in net assets	\$ 2,079,263	\$ (3,104,581)
Adjustments to reconcile changes in net assets to net cash provided by (used in) operating activities:		
Depreciation	19,093	8,243
Bad debt expense	2,034	15,425
Net realized and unrealized (gains) losses on investments	(1,706,057)	3,704,145
Investments received as contributions	(106,915)	(110,465)
Reclassification of investment income restricted for long-term investment	-	(89,103)
Contributions restricted for long-term investment	(110,403)	(39,150)
Changes in:		
Interest receivable	110	9,443
Contributions and grants receivable	271,983	(438,977)
Life memberships receivable	8,477	(6,317)
Inventory	(5,556)	(54,889)
Prepaid expenses	397	6,177
Accounts payable and accrued expenses	(44,203)	54,308
Other liabilities - gift annuity	26,784	(13,815)
Total adjustments	<u>(1,625,750)</u>	<u>3,045,025</u>
Net cash provided by (used in) operating activities	<u>453,513</u>	<u>(59,556)</u>
Cash flows from investing activities:		
Acquisition of furniture and equipment	(61,024)	(26,196)
Purchase of investments	(4,603,930)	(5,284,348)
Proceeds from the sale/maturities of investments	2,393,966	7,242,030
Deposits	-	6,420
Net cash provided by (used in) investing activities	<u>(2,270,988)</u>	<u>1,937,906</u>
Cash flows from financing activities:		
Contributions and reclassification of investment income restricted for long-term investment	152,103	153,583
Payments on capital lease obligation	(4,847)	(3,967)
Net cash provided by financing activities	<u>147,256</u>	<u>149,616</u>
Increase (decrease) in cash and cash equivalents	<u>(1,670,219)</u>	<u>2,027,966</u>
Cash and cash equivalents, beginning of year	<u>3,095,966</u>	<u>1,068,000</u>
Cash and cash equivalents, end of year	<u>\$ 1,425,747</u>	<u>\$ 3,095,966</u>

See accompanying notes to the financial statements.

NAVAL WAR COLLEGE FOUNDATION, INC.

Notes to Financial Statements

Note 1 – Organization and Summary of Significant Accounting Policies

The Naval War College Foundation, Inc. (the “Foundation”), organized in 1969, is a charitable organization whose purpose is to provide a source of support to assist the Naval War College in carrying out its mission to enhance the professional capabilities of its students and conduct research in the development of advanced strategic and tactical concepts. The Internal Revenue Service has determined that the Foundation is a non-profit organization exempt from income taxes under Sections 501(c)(3) of the Internal Revenue Code.

Cash and Cash Equivalents

The Foundation considers all short-term investments with an original maturity of three months or less to be cash equivalents.

Investments

Investments in marketable debt and equity securities are valued at their fair values, based on quoted market prices. Unrealized gains and losses are included in the changes in net assets.

Classification of Net Assets

Net assets, support and revenues, and expenses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, the net assets of the Foundation and changes therein are classified and reported as follows:

Unrestricted Net Assets

Net assets that are not subject to donor-imposed stipulations. Included in unrestricted net assets at December 31, 2009 and 2008 are \$25,431 and \$21,530, respectively, of assets directed by the Board of Trustees to be segregated from the general operating assets and to be known as the Strasser International Leadership Award.

Temporarily Restricted Net Assets

Net assets subject to donor-imposed stipulations or state law that will be met by the passage of time or fulfillment of donor stipulated purposes.

Permanently Restricted Net Assets

Net assets subject to permanent donor-imposed stipulations are maintained in perpetuity by the Foundation. Generally, the donors of these assets permit the Foundation to use all or part of the income earned on related investments for specific purposes.

NAVAL WAR COLLEGE FOUNDATION, INC.

Notes to Financial Statements

Note 1 – Organization and Summary of Significant Accounting Policies (Continued)

Contributions and Recognition of Donor Restrictions

Contributions received are recorded as unrestricted, temporarily restricted, or permanently restricted support depending on the existence and/or nature of any donor restrictions. Contributions that are restricted by the donor are reported as an increase in unrestricted net assets if the restriction expires in the reporting period in which the contribution is given. All other donor-restricted contributions are reported as an increase in temporarily or permanently restricted net assets depending on the nature of the restriction. When a restriction expires, temporarily restricted net assets are released to unrestricted net assets. The Foundation carries its contributions and grants receivable at cost less an allowance for doubtful accounts. On a periodic basis, the Foundation evaluates its contributions and grants receivable and establishes an allowance for doubtful accounts, when deemed necessary, based on its history of past write-offs and collections and current credit conditions.

Membership Support

Since members receive only nominal tangible benefits from their membership payments, these dues are contributions in substance. As such, they fall under the treatment of contributions as described in the note on contributions and recognition of donor restrictions.

The Foundation carries its membership receivables at cost less an allowance for doubtful accounts. On a periodic basis, the Foundation evaluates its membership receivables and establishes an allowance for doubtful accounts, when deemed necessary, based on its history of past write-offs and collections and current credit conditions.

Inventory

Inventory consists of museum store merchandise held for resale. The inventory is valued at the lower of cost or market determined on first-in, first-out basis.

Furniture and Equipment

Furniture and equipment is stated at cost and depreciated using the straight-line method over estimated useful lives ranging from three to five years. It is the policy of the Foundation to capitalize those items with a fair value at date of donation or cost exceeding \$1,000.

Occupancy Expense

The Department of the Navy, consistent with its internal regulations, does not charge the Foundation for rent or utilities. The rental value of the offices has not been determined and, accordingly, is not included in the Foundation's operating results.

NAVAL WAR COLLEGE FOUNDATION, INC.

Notes to Financial Statements

Note 1 – Organization and Summary of Significant Accounting Policies (Continued)

Concentration of Credit Risk

The Foundation maintains its cash and securities in bank and investment deposit accounts which, at times, may exceed insured limits. The Foundation has not experienced any losses in such accounts.

Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

Historical Collections

In accordance with accounting standards for contributions received and contributions made, the Foundation does not recognize contributions of works of art or historical treasures, which meet the following conditions. They are: (1) held for public exhibition, education, or research in furtherance of public service rather than financial gain, (2) protected, kept unencumbered, cared for, and preserved, and (3) subject to an organizational policy that requires the proceeds from sales of collection items to be used to acquire other items for collection.

Allocation of Expenses

The cost of providing program and other services has been summarized on a functional basis in the statements of changes in net assets. Accordingly, management has allocated certain costs among the program and supporting services benefited. Personnel and other costs have been allocated based upon actual time spent or usage.

NAVAL WAR COLLEGE FOUNDATION, INC.

Notes to Financial Statements

Note 1 – Organization and Summary of Significant Accounting Policies (Continued)

Fair Value Measurements

The Foundation measures its financial instruments at fair value. Fair value standards require an entity to maximize the use of observable inputs and minimize the use of unobservable inputs to determine value. Fair value standards also require the Foundation to classify its financial instruments into a three-level hierarchy, based on the priority of inputs to the valuation technique as follows:

Investments measured and reported at fair value are classified and disclosed in one of the following categories:

Level I – Quoted prices are available in active markets for identical investments as of the reporting date. The Foundation's Level I assets are common stocks, preferred stocks, and mutual funds.

Level II – Pricing inputs are other than quoted prices in active markets, which are either directly or indirectly observable as of the reporting date, and fair value is determined through the use of models or other valuation methodologies. The Foundation has corporate and government bonds and gift annuities considered to be Level II investments.

Level III – Pricing inputs are unobservable for the investment and includes situations where there is little, if any, market activity for the investment. The inputs into the determination of fair value require significant management judgment or estimation. The Foundation has no Level III investments.

Subsequent Events

The Foundation has evaluated subsequent events through June 2, 2010, the date the Audit Committee of the Board of Trustees approved and authorized the financial statements to be issued.

Reclassification

Certain reclassifications have been made to the 2008 financial statements to conform with 2009 presentation.

NAVAL WAR COLLEGE FOUNDATION, INC.

Notes to Financial Statements

Note 2 – Contributions and Grants Receivable, Net

The Foundation recognizes promise-to-give contributions and grants in the year in which such promises are made. Promise-to-give contributions are recorded at net realizable value less an allowance for doubtful accounts.

At December 31, contributions and grants receivable consist of:

	<i>2009</i>			
	<i>Unrestricted</i>	<i>Temporarily Restricted</i>	<i>Permanently Restricted</i>	<i>Total</i>
Gross contributions and grants:				
Due within one year	\$ 137,335	\$ 32,687	\$ -	\$ 170,022
Due within two to four years	<u>98,504</u>	<u>10,000</u>	<u>-</u>	<u>108,504</u>
Total	235,839	42,687	-	278,526
Allowance for pledges receivable	(1,600)	-	-	(1,600)
Discount to present value	<u>(6,890)</u>	<u>(476)</u>	<u>-</u>	<u>(7,366)</u>
Contributions and grants receivables, net	\$ <u>227,349</u>	\$ <u>42,211</u>	\$ <u>-</u>	\$ <u>269,560</u>

	<i>2008</i>			
	<i>Unrestricted</i>	<i>Temporarily Restricted</i>	<i>Permanently Restricted</i>	<i>Total</i>
Gross contributions and grants:				
Due within one year	\$ 68,073	\$ 280,945	\$ 26,700	\$ 375,718
Due within two to four years	<u>198,504</u>	<u>50,000</u>	<u>15,000</u>	<u>263,504</u>
Total	266,577	330,945	41,700	639,222
Allowance for pledges receivable	(11,600)	-	-	(11,600)
Discount to present value	<u>(25,873)</u>	<u>-</u>	<u>-</u>	<u>(25,873)</u>
Contributions and grants receivables, net	\$ <u>229,104</u>	\$ <u>330,945</u>	\$ <u>41,700</u>	\$ <u>601,749</u>

Approximately 89% of gross contributions and grants receivable are collectible from three donors as of December 31, 2009. Approximately 98% of gross contributions and grants receivable were collectible from four donors as of December 31, 2008.

NAVAL WAR COLLEGE FOUNDATION, INC.

Notes to Financial Statements

Note 3 – Life Memberships Receivable, Net

Life memberships receivable consists of the unpaid balances of individual life membership dues, net of an allowance for uncollectible amounts.

These unpaid memberships are expected to be received as follows:

Year ending December 31,	2009	2008
2009	\$ -	\$ 21,850
2010	18,976	13,962
2011	<u>6,825</u>	<u>-</u>
Total	25,801	35,812
Less allowance	<u>(2,000)</u>	<u>(1,500)</u>
Life memberships receivable, net	\$ <u>23,801</u>	\$ <u>34,312</u>

Note 4 – Investments

Investments are carried at fair values and are summarized as follows as of December 31:

	2009	2008
Common stocks	\$ 11,368,261	\$ 8,000,466
Preferred stocks	121,150	106,900
Bonds	3,087,600	2,719,439
Mutual funds	<u>432,918</u>	<u>160,188</u>
Investments	\$ <u>15,009,929</u>	\$ <u>10,986,993</u>

NAVAL WAR COLLEGE FOUNDATION, INC.

Notes to Financial Statements

Note 4 – Investments (Continued)

The following schedule summarizes the net investment income for the year ended December 31, 2009:

	<i>Unrestricted</i>	<i>Temporarily Restricted</i>	<i>Permanently Restricted</i>	<i>Total</i>
Interest and dividends	\$ 200,718	\$ 335,550	\$ -	\$ 536,268
Net realized gains	45,130	74,920	-	120,050
Net unrealized gains	595,530	990,477	-	1,586,007
Management fees	<u>(53,360)</u>	<u>(46,952)</u>	-	<u>(100,312)</u>
Total	\$ <u>788,018</u>	\$ <u>1,353,995</u>	\$ <u>-</u>	\$ <u>2,142,013</u>

The following schedule summarizes the net investment loss for the year ended December 31, 2008:

	<i>Unrestricted</i>	<i>Temporarily Restricted</i>	<i>Permanently Restricted</i>	<i>Total</i>
Interest and dividends	\$ 465,752	\$ 1,050	\$ 89,103	\$ 555,905
Net realized gains	556,001	-	-	556,001
Net unrealized losses	(3,157,829)	(1,013,224)	-	(4,171,053)
Management fees	<u>(129,596)</u>	<u>-</u>	<u>-</u>	<u>(129,596)</u>
Total	\$ <u>(2,265,672)</u>	\$ <u>(1,012,174)</u>	\$ <u>89,103</u>	\$ <u>(3,188,743)</u>

For the year ended December 31, 2008, the allocation of investment income to permanently restricted net assets was a result of the historic dollar value adjustment.

Note 5 – Fair Value Measurements

The Foundation follows the fair value measurement standards for its financial instruments, these standards require enhanced disclosures about instruments that are measured and reported at fair value and establish a hierarchal disclosure framework, which prioritizes and ranks the level of market price used in measuring instruments at fair value. Market price is affected by a number of factors, including the type of instrument and the characteristics specific to the instrument. Instruments with readily available quoted prices or for which fair value can be measured for actively quoted prices generally will have a higher degree of market price observability and a lesser degree of judgment used in measuring fair value.

NAVAL WAR COLLEGE FOUNDATION, INC.

Notes to Financial Statements

Note 5 – Fair Value Measurements (Continued)

The valuation of the Foundation's financial instruments using the fair value hierarchy consisted of the following at December 31:

2009	<i>Quoted prices in active markets Level 1</i>	<i>Significant observable inputs Level 2</i>	<i>Significant unobservable inputs Level 3</i>	<i>Total</i>
Common stocks	\$ 11,368,261	\$ -	\$ -	\$ 11,368,261
Preferred stocks	121,150	-	-	121,150
Bonds	-	3,087,600	-	3,087,600
Mutual funds	-	432,918	-	432,918
	\$ 11,489,411	\$ 3,520,518	\$ -	\$ 15,009,929
2008				
Common stocks	\$ 8,000,466	\$ -	\$ -	\$ 8,000,466
Preferred stocks	106,900	-	-	106,900
Bonds	-	2,719,439	-	2,719,439
Mutual funds	-	160,188	-	160,188
	\$ 8,107,366	\$ 2,879,627	\$ -	\$ 10,986,993

Fair values of financial instruments for which the Foundation did not elect the fair value option are included in the table below. The fair values of such instruments have been derived, in part, by management's assumptions, the estimated amount and timing of future cash flows and estimated discount rates. Different assumptions could significantly affect these estimated fair values. Accordingly, the net realizable values could be materially different from the estimates presented below at December 31, 2009 and 2008. In addition, the estimates are only indicative of the value of individual financial instruments and should not be considered an indication of the fair value of the Foundation.

Cash and cash equivalents	Carrying amount approximates fair value
Contributions and grants receivable, net	Carrying amount approximates fair value
Life memberships receivable, net	Carrying amount approximates fair value
Accounts payable	Carrying amount approximates fair value

NAVAL WAR COLLEGE FOUNDATION, INC.

Notes to Financial Statements

Note 6 – Furniture and Equipment, Net

Furniture and equipment, net, consists of the following:

	<i>2009</i>	<i>2008</i>
Furniture and equipment	\$ 106,683	\$ 45,658
Less accumulated depreciation	<u>(31,933)</u>	<u>(12,839)</u>
Furniture and equipment, net	<u>\$ 74,750</u>	<u>\$ 32,819</u>

Note 7 – Capital Leases

In December 2007, the Foundation entered into a capital lease for office equipment for which the equipment was not received until January 2008. The lease expires in December 2010. The capital lease is payable in monthly installments of \$504, including interest, beginning in February 2008. The interest rate on the lease is 13.7%

The following is a schedule of future minimum payments required under the lease with the present value as follows:

2010	\$ 6,043
2011	<u>504</u>
Total minimum lease payments	6,547
Less: amount representing interest	<u>(495)</u>
Present value of minimum lease payments	<u>\$ 6,052</u>

Note 8 – Historical Collections

The Foundation has a collection, which consists of paintings, sculptures, charts, memoirs, letters and other rare books and memorabilia of historical significance to the Navy and the Naval War College. This collection is currently loaned to the Naval War College for display in the Naval War College Museum and in the various Naval War College buildings. Post 1991 collection items donated to the Foundation are not capitalized as no estimation of fair value is readily determinable.

NAVAL WAR COLLEGE FOUNDATION, INC.

Notes to Financial Statements

Note 9 – Gift Annuities

The Foundation was named administrator of a charitable remainder annuity trust during the year ended December 31, 2004. The charitable remainder annuity trust provides for the payment of quarterly distributions to the designated beneficiary over the life of the beneficiary. At the end of the trust's term, the remaining assets are available for the Foundation's use. The portion of the trust attributable to the present value of the future benefits to be received by the Foundation was recorded in the statements of changes in net assets as an unrestricted contribution in the period the trust was established. Assets held in the charitable remainder annuity trust totaled \$50,000 when the trust was created in 2004 and are reported at fair market value as part of the investments balance in the Foundation's statements of financial position. On an annual basis, the Foundation revalues the liability based on actuarial assumptions. The present value of the estimated future payments, \$6,269 at December 31, 2009, is calculated using a discount rate of 8.3% and applicable mortality tables.

The Foundation was named administrator of a charitable remainder annuity trust during the year ended December 31, 2006. The charitable remainder annuity trust provides for the payment of quarterly distributions to the designated beneficiary over the life of the beneficiary. At the end of the trust's term, the remaining assets are available for the Foundation's use. The portion of the trust attributable to the present value of the future benefits to be received by the Foundation is recorded in the statements of changes in net assets as an unrestricted contribution in the period the trust is established. Assets held in the charitable remainder annuity trust totaled \$66,111 when the trust was created in 2006 and are reported at fair market value as part of the investments balance in the Foundation's statements of financial position.

On an annual basis, the Foundation revalues the liability based on actuarial assumptions. The present value of the estimated future payments, \$8,644 at December 31, 2009, is calculated using a discount rate of 9.5% and applicable mortality tables.

The Foundation was named administrator of a charitable remainder annuity trust during the year ended December 31, 2007. The charitable remainder annuity trust provides for the payment of semi-annual distributions to the designated beneficiary over the life of the beneficiary. At the end of the trust's term, the remaining assets are available for the Foundation's use. The portion of the trust attributable to the present value of the future benefits to be received by the Foundation is recorded in the statements of changes in net assets as an unrestricted contribution in the period the trust is established. Such contributions totaled \$20,064 for the year ended December 31, 2007. Assets held in the charitable remainder annuity trust totaled \$48,055 when the trust was created in 2007 and are reported at fair market value as part of the investments balance in the Foundation's statements of financial position. On an annual basis, the Foundation revalues the liability based on actuarial assumptions. The present value of the estimated future payments, \$21,722 at December 31, 2009, is calculated using a discount rate of 6.0% and applicable mortality tables.

NAVAL WAR COLLEGE FOUNDATION, INC.

Notes to Financial Statements

Note 9 – Gift Annuities (Continued)

The Foundation was named administrator of a charitable remainder unitrust during the year ended December 31, 2009. The charitable remainder unitrust provides for the payment of quarterly distributions to the designated beneficiary over the life of the beneficiary. At the end of the trust's term, the remaining assets are available for the Foundation's use. The portion of the trust attributable to the present value of the future benefits to be received by the Foundation is recorded in the statements of changes in net assets as a permanently restricted contribution in the period the trust is established. Such contributions totaled \$84,902 for the year ended December 31, 2009. Assets held in the charitable remainder unitrust totaled \$125,000 when the trust was created in 2009 and are reported at fair market value as part of the investments balance in the Foundation's statements of financial position. On an annual basis, the Foundation revalues the liability based on actuarial assumptions. The present value of the estimated future payments, \$40,098 at December 31, 2009, is calculated using a discount rate of 5.0% and applicable mortality tables.

Note 10 – Museum Store Sales, Net

The Foundation operates a store in the Naval War College Museum, which sells souvenirs and memorabilia. Sales and cost of goods sold were as follows:

	<i>2009</i>	<i>2008</i>
Sales	\$ 161,308	\$ 148,573
Cost of goods sold	<u>88,684</u>	<u>80,596</u>
Net sales	<u>\$ 72,624</u>	<u>\$ 67,977</u>

Additionally, the museum store incurs other operating costs consisting primarily of personnel costs and bank charges. These operating costs amounted to \$62,254 and \$57,848 for the years ended December 31, 2009 and 2008, respectively, and are included in program services on the statements of changes in net assets.

NAVAL WAR COLLEGE FOUNDATION, INC.

Notes to Financial Statements

Note 11 – Net Assets

The following represents required disclosures relative to the composition of investments and net assets at December 31, 2009 and 2008:

<i>2009</i>	<i>Unrestricted Net Assets</i>	<i>Temporarily Restricted Net Assets</i>	<i>Permanently Restricted Net Assets</i>	<i>Total</i>
Endowment assets and those functioning as endowment assets, beginning of year	\$ 21,530	\$ -	\$ 8,996,741	\$ 9,018,271
Reclassification based on change in law	-	1,208,773	(1,208,773)	-
Gifts and additions	-	-	152,103	152,103
Long-term investment returns, net:				
Interest and dividends	965	335,550	-	336,515
Realized gains	216	74,920	-	75,136
Unrealized gains	2,855	990,477	-	993,332
Management fees	(135)	(46,952)	-	(47,087)
Total long-term investment returns, net	3,901	1,353,995	-	1,357,896
Expenditures:				
Amounts appropriated for expenditure	-	(361,807)	-	(361,807)
Change in endowment assets and those functioning as endowment assets	3,901	2,200,961	(1,056,670)	1,148,192
Endowment assets and those functioning as endowment assets, end of year	\$ 25,431	\$ 2,200,961	\$ 7,940,071	\$ 10,166,463

NAVAL WAR COLLEGE FOUNDATION, INC.

Notes to Financial Statements

Note 11 – Net Assets (Continued)

2008	<i>Unrestricted Net Assets</i>	<i>Temporarily Restricted Net Assets</i>	<i>Permanently Restricted Net Assets</i>	<i>Total</i>
Endowment assets and those functioning as endowment assets, beginning of year	\$ 25,875	\$ -	\$ 8,843,158	\$ 8,869,033
Gifts and additions	-	-	64,480	64,480
Long-term investment returns, net:				
Interest and dividends	1,068	-	89,103	90,171
Realized gains	811	-	-	811
Unrealized losses	(6,082)	-	-	(6,082)
Management fees	(142)	-	-	(142)
Total long-term investment returns, net	(4,345)	-	89,103	84,758
Expenditures:				
Amounts appropriated for expenditure	-	-	-	-
Change in endowment assets and those functioning as endowment assets	(4,345)	-	153,583	149,238
Endowment assets and those functioning as endowment assets, end of year	\$ 21,530	\$ -	\$ 8,996,741	\$ 9,018,271

Endowment

The Foundation's endowment consists of approximately 34 individual funds established for a variety of purposes by donors. As required by U.S. generally accepted accounting principles, net assets associated with endowment funds, including funds designated by the Board of Trustees to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions.

Interpretation of Relevant Law

The State of Rhode Island has signed into law the Uniform Prudent Management of Institutional Funds Act (UPMIFA), effective for the year ended December 31, 2009 and thereafter, requiring the preservation of the original value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. The Foundation is applying this law as passed. As a result of this law, the Foundation classifies as permanently restricted net assets: (a) the original value of gifts donated to the permanent endowment, (b) the original gift value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Foundation in a manner consistent with the standard of prudence prescribed by UPMIFA. UPMIFA allows the Board of Trustees to appropriate a percentage of net appreciation as is prudent considering the Foundation's long- and short-term needs, present and anticipated financial requirements, and expected total return on its investments, price level trends, and general economic conditions.

NAVAL WAR COLLEGE FOUNDATION, INC.

Notes to Financial Statements

Note 11 – Net Assets (Continued)

Investment Objectives and Spending Policy

The Foundation has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding for the annual operations while seeking to maintain the purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the Foundation must hold in perpetuity or for a donor-specified period as well as board-designated funds. Under this policy, as approved by the Board of Trustees, the endowment assets are invested in a manner that is intended to produce results that exceed the price and yield results of various indexes while assuming a moderate level of investment risk. Actual returns in any given year may vary. To satisfy its long-term rate-of-return objectives, the Foundation relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The Foundation targets a diversified asset allocation that places a greater emphasis on equity-based investments to achieve its long-term objectives within prudent risk constraints.

Distributions from long-term investments are made using the total return method. Under the total return method, distributions consist of interest, dividends and realized and unrealized gains. The Board of Trustees has established a spending rate of five percent (5%) of a rolling twelve-quarter average fair market value of the long-term investments. Distributions up to this spending rate are used to support operations. The Foundation has adopted this spending policy in order to protect the nature of the original corpus of gifts as well as to preserve the purchasing power of these funds into the future.

Funds with Deficiencies

From time-to-time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level that the donor requires the Foundation to retain as a fund of perpetual duration. In accordance with U.S. generally accepted accounting principles, deficiencies of this nature are reported in unrestricted net assets. There were no such deficiencies at December 31, 2009 and 2008.

Note 12 – Related Parties

Contributions received from members of the Board of Trustees and employees totaled \$355,167 and \$445,372 for the years ended December 31, 2009 and 2008, respectively. Contributions and grants receivable include amounts due from Board members and employees totaling \$208,104 and \$232,594 at December 31, 2009 and 2008, respectively.

Note 13 – Fundraising Costs

Management and resource development on the statements of changes in net assets includes approximately \$94,000 and \$102,000 of fundraising costs for the years ended December 31, 2009 and 2008, respectively. These amounts represent printing, mailing and promotion costs as well as an allocation of employees' costs for salary, taxes, and benefits based on time spent on fundraising activities.

NAVAL WAR COLLEGE FOUNDATION, INC.

Notes to Financial Statements

Note 14 – Pension Plan

The Foundation has a tax sheltered retirement plan (the “Plan”) covering all employees who meet certain eligibility requirements. Employees may elect to defer a percentage of their compensation into the Plan. The Foundation contributes 1% of an employee’s compensation. Additionally, matching contributions are made by the Foundation equal to 100% of the first 4% deferred by an employee, and for employee deferrals in excess of 4%, at the rate of one half percent per year of employment, limited to a maximum matching contribution of 9% of an employee’s compensation. Contributions made by the Foundation were \$25,361 and \$23,499 for the years ended December 31, 2009 and 2008, respectively.

Note 15 – Operating Leases

The Foundation leases office equipment under non-cancelable operating leases through October 2013. Future minimum lease payments required under the non-cancelable operating leases are as follows:

2010	\$	6,111
2011		3,460
2012		3,219
2013		<u>2,682</u>
Total	\$	<u>15,472</u>

Lease expense was approximately \$8,000 for each of the years ended December 31, 2009 and 2008.

Note 16 – Uncertain Tax Positions

The Foundation accounts for the effect of any uncertain tax positions based on a “more likely than not” threshold to the recognition of the tax positions being sustained based on the technical merits of the position under scrutiny by the applicable taxing authority. If a tax position or positions are deemed to result in uncertainties of those positions, the unrecognized tax benefit is estimated based on a “cumulative probability assessment” that aggregates the estimated tax liability for all uncertain tax positions. Interest and penalties assessed, if any, are accrued as income tax expense. The Foundation has identified its tax status as a tax exempt entity as a tax position; however, the Foundation has determined that such tax position does not result in an uncertainty requiring recognition. The Foundation is not currently under examination by any taxing jurisdiction. Its Federal tax returns are generally open for examination for the past three years.

Note 17 – Cash Flows Information

During the year ended December 31, 2008, the Foundation financed the purchase of computer equipment totaling \$14,866 through a capital lease.

Supplemental Information



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Independent Auditors' Report on Supplemental Information

The Board of Trustees
Naval War College Foundation, Inc.
Newport, Rhode Island

Our report on our audit of the basic financial statements of Naval War College Foundation, Inc. for the years ended December 31, 2009 and 2008 appears on page one. The audits were conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The accompanying supplemental schedules are presented for purposes of additional analysis and are not a required part of the basic financial statements. The supplemental information has been subjected to the auditing procedures applied in the audits of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Mayer Hoffman McCann P.C.

June 2, 2010
Newport, Rhode Island

NAVAL WAR COLLEGE FOUNDATION, INC.

Selected Financial Information

Composition of Assets

	<i>December 31,</i>			
	<i>2009</i>	<i>of %</i>	<i>2008</i>	<i>of %</i>
	<i>Amount</i>	<i>Assets</i>	<i>Amount</i>	<i>Assets</i>
Cash	\$ 1,425,747		\$ 3,095,966	
Investments	<u>15,009,929</u>		<u>10,986,993</u>	
Total cash and investments	16,435,676	96%	14,082,959	94%
Other assets	<u>643,023</u>	<u>4%</u>	<u>938,743</u>	<u>6%</u>
Total assets	\$ <u>17,078,699</u>	<u>100%</u>	\$ <u>15,021,702</u>	<u>100%</u>
Total assets, end of year	\$ 17,078,699		\$ 15,021,702	
Total assets, beginning of year	<u>15,021,702</u>		<u>18,074,891</u>	
Increase (decrease) in assets	<u>\$ 2,056,997</u>		<u>\$ (3,053,189)</u>	
% increase (decrease)		<u>14%</u>		<u>-17%</u>

Museum Store Operations

	<i>Years Ended December 31,</i>			
	<i>2009</i>	<i>% of</i>	<i>2008</i>	<i>% of</i>
	<i>Amount</i>	<i>Sales</i>	<i>Amount</i>	<i>Sales</i>
Gross sales	\$ 161,308	100%	\$ 148,573	100%
Cost of goods sold	<u>88,684</u>	<u>55%</u>	<u>80,596</u>	<u>54%</u>
Gross profit	<u>72,624</u>	<u>45%</u>	<u>67,977</u>	<u>46%</u>
Personnel costs	54,860	34%	50,886	34%
Other store expenses	<u>7,394</u>	<u>5%</u>	<u>6,962</u>	<u>5%</u>
Total operating costs	<u>62,254</u>	<u>39%</u>	<u>57,848</u>	<u>39%</u>
Net income from museum store	\$ <u>10,370</u>	<u>6%</u>	\$ <u>10,129</u>	<u>7%</u>

NAVAL WAR COLLEGE FOUNDATION, INC.

Schedule of Permanently Restricted Net Assets

Year Ended December 31, 2009

	<i>Beginning Balance</i>	<i>Contributions</i>	<i>Reclassification Based on Change in Law</i>	<i>Ending Balance</i>
Adelaar Book Fund	\$ 19,843	\$ 300	\$ (2,443)	\$ 17,700
Annenberg Regional Endowment	267,871	-	(17,871)	250,000
Asia Pacific Study Group	115,746	-	(15,746)	100,000
Batemans NCC Essay Award	26,565	-	(4,961)	21,604
Brecker Library Support Fund	21,277	-	(1,277)	20,000
Carr Lecture Fund	51,031	-	(9,660)	41,371
Daley Family Award	50,143	200	(4,744)	45,599
D'Luhy Prize	-	25,000	-	25,000
EMC Information Technology Chair	1,679,855	-	(179,855)	1,500,000
Evening Lecture Endowment	50,500	-	(500)	50,000
Fairchild International Lecture Fund	115,746	-	(50,746)	65,000
Foster Endowment	-	84,903	-	84,903
Freund International Student Fund	63,660	-	(13,660)	50,000
Hayward CDE Award	23,423	-	(3,914)	19,509
John Nicholas Brown Chair & Study Group	1,627,672	-	(196,229)	1,431,443
Kurth Fund	127,134	-	(2,134)	125,000
Larkin USMC Award	29,196	-	(696)	28,500
Levy Chair	1,448,432	-	(235,863)	1,212,569
Lowry Visiting Professorship	44,880	-	(13,107)	31,773
McGinnis Family Award	22,120	-	(339)	21,781
Military Operations/International Law Award	13,314	-	(3,314)	10,000
Miller Lecture Fund	136,114	-	(26,339)	109,775
Naval Order Book Fund	11,416	-	(1,391)	10,025
Naval War College Foundation Award	31,646	-	(6,799)	24,847
Nolan Award Fund	25,000	-	-	25,000
Polk Holiday Lunch Fund	2,200	-	-	2,200
Polk Sailors of the Year Award	33,379	-	(2,731)	30,648
Reinauer Award	21,897	-	(1,120)	20,777
Ruger National Security Economics Chair	2,800,591	-	(401,202)	2,399,389
Strasser Counter-Terrorism Lecture Fund	101,101	-	(1,001)	100,100
Strasser International Leadership Awards Fund	11,327	-	(111)	11,216
Thys Fund	26,134	-	(1,134)	25,000
Wheeler NCC Fund	15,454	-	(6,112)	9,342
Woodson Memorial Award	23,774	-	(3,774)	20,000
Total	\$ 9,038,441	\$ 110,403	\$ (1,208,773)	\$ 7,940,071

NAVAL WAR COLLEGE FOUNDATION, INC.

Schedule of Temporarily Restricted Net Assets

Year Ended December 31, 2009

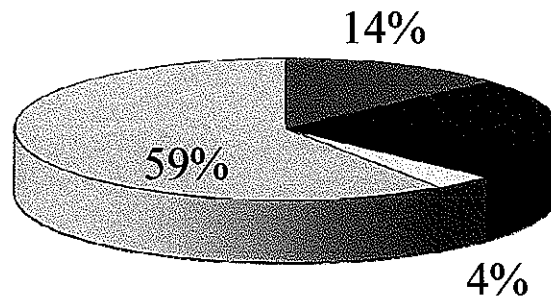
	Beginning Balance	Contributions	Net Investment Income	Released from Restriction	Reclassification Based on Change in Law	Transfer to Unrestricted Restricted Net Assets	Reclassification at Donor's Request	Ending Balance
Adelaar Book Fund	\$ 1,343	\$ -	\$ 3,034	\$ (1,000)	\$ 2,443	\$ (3,375)	\$ -	\$ 2,445
Annenberg Regional Endowment	(5,168)	-	40,086	-	17,871	(46,027)	-	6,762
Asia Pacific Study Group	33,911	-	17,334	(11,157)	15,746	(19,945)	-	35,889
Batemans NCC Essay Award	3,225	-	3,900	(1,000)	4,961	(4,603)	-	6,483
Bradley Foundation Genest Grant	150,000	-	-	(36,544)	-	-	-	113,456
Brecker Library Fund	610	-	3,250	(212)	1,277	(3,682)	-	1,243
Carnes Lord Grant-Smith Richardson	2,215	-	-	-	-	-	-	2,215
Carr Lecture Fund	19,296	-	7,584	(2,000)	9,660	(8,899)	-	25,641
CDE	-	500	-	-	-	-	-	500
Classroom Upgrades	4,673	3,090	-	-	-	-	-	7,763
CMSI	-	9,815	-	-	-	-	-	9,815
Crown CCL Lecture	1,000	-	-	(1,000)	-	-	-	-
Daley Family Award	12,886	-	7,584	(500)	4,743	(8,592)	-	16,121
Doyle Prize	-	50	-	-	-	-	-	50
EMC Information Technology Chair	440,686	-	251,564	(95,198)	179,855	(288,132)	-	488,775
Ethics Program	15,000	-	-	(5,000)	-	-	-	10,000
Evening Lecture Endowment	-	-	7,584	-	500	(5,584)	-	2,500
Fairchild International Lecture Fund	88,785	-	17,334	(5,000)	50,746	(19,945)	-	131,920
Freund International Student Fund	5,245	-	9,534	(2,955)	13,660	(11,047)	-	14,437
Green Room	-	7,496	-	-	-	-	-	7,496
Hayward CDE Award	2,375	-	3,467	(1,000)	3,914	(3,989)	-	4,767
Jim Hayes Fund	11,250	4,500	-	-	-	-	1,000	16,750
John Nicholas Brown Chair & Study Group	230,925	-	243,764	(49,800)	196,229	(279,233)	-	341,885
Kurth Fund	(5,085)	-	19,068	(11,907)	2,134	-	-	4,210
Larkin USMC Award	(2,876)	-	4,334	(1,151)	696	-	-	1,003
Levy Chair	292,122	-	217,329	(55,984)	235,863	(248,548)	-	440,782
Library Support	818	-	-	(818)	-	-	-	-
LM Chairmen's Classroom 2/Mahan Reading Room	250,000	-	-	(24,390)	-	-	-	225,610
Lowry Visiting Professorship	48,350	-	6,717	(5,000)	13,107	(7,671)	-	55,503
McGinnis Family Award	1,408	-	3,250	(1,000)	339	(2,997)	-	1,000
Military Operations/International Law Award	2,914	-	1,950	-	3,314	(2,148)	-	6,030
Miller Fellowship	1,000	-	-	(1,000)	-	-	-	-
Miller Lecture Fund	33,868	-	20,368	(6,000)	26,339	(23,321)	-	51,254
Museum Support	-	11,190	-	-	-	-	-	11,190
Naval Historic Treasures	5,060	5,075	-	-	-	-	-	10,135
Naval Order Book Fund	495	-	1,733	(650)	1,391	(1,841)	-	1,128
Nolan Award	-	-	5,634	(250)	-	-	-	5,384
NWCF Award	2,001	-	4,767	(1,000)	6,799	(5,523)	-	7,044
NY Navy League Russian Elective 2008	5,000	-	-	(5,000)	-	-	-	-
NY Navy League Russian Elective 2009	-	5,000	-	-	-	-	-	5,000
Piracy Conference	-	8,000	-	-	-	-	-	8,000
Polk Holiday Lunch	260	1,000	-	(122)	-	-	-	1,138
Polk Model Classroom	-	30,000	-	-	-	-	-	30,000
Polk Sailors of the Year Award	1,132	9,000	4,984	(1,800)	2,731	(5,523)	-	10,524
Pollack/MacArthur Foundation Grant	100,000	-	-	(12,000)	-	-	-	88,000
Raytheon Asia Pacific Forum	3,125	-	-	-	-	-	-	3,125
Raytheon China Conference	2,000	-	-	-	-	-	-	2,000
Regional Electives Cluster	188,565	-	-	(30,000)	-	-	-	158,565
Regional Studies Library-Foreign Language	-	500	-	-	-	-	-	500
Regional Studies Library	-	7,216	-	-	-	-	-	7,216
Regional Studies Library-VB grant	-	120,000	-	-	-	-	-	120,000
Reinauer Award Fund	1,231	2,000	1,050	(1,000)	1,120	-	-	4,401
Ruger National Security Economics Chair	340,607	-	419,491	(101,012)	401,202	(480,526)	-	579,762
Sofrenko Lectures	2,500	2,000	-	(2,500)	-	-	-	2,000
Spruance Lectures	4,000	3,000	-	(4,000)	-	-	-	3,000
SR Genest Grant	-	4,265	-	-	-	-	-	4,265
Strasser Counter-Terrorism Lecture Fund	-	-	15,168	(1,518)	1,001	(17,490)	-	(2,839)
Strasser International Leadership Awards Fund	2,715	-	2,383	(1,000)	112	(1,841)	-	2,369
Student Memorial Fund	544	-	-	-	-	-	-	544
Thys Award Fund	(2,600)	-	3,900	(1,392)	1,134	-	-	1,042
Thys Lecture Fund	26,000	-	-	(2,150)	-	-	-	23,850
Wheeler NCC Fund	5,037	-	2,383	(1,200)	6,112	(2,762)	-	9,570
Woodson Memorial Award	4,494	-	3,467	-	3,774	(3,989)	-	7,746
Zimmerman-Gray Award	1,000	1,000	-	(1,000)	-	-	-	1,000
Discount on gross contributions and grants receivable	-	(476)	-	-	-	-	-	(476)
Total	\$ 2,333,942	\$ 234,221	\$ 1,353,995	\$ (487,210)	\$ 1,208,773	\$ (1,507,233)	\$ 1,000	\$ 3,137,488

NAVAL WAR COLLEGE FOUNDATION, INC.

Charts

Year Ended December 31, 2009

Support and Revenues



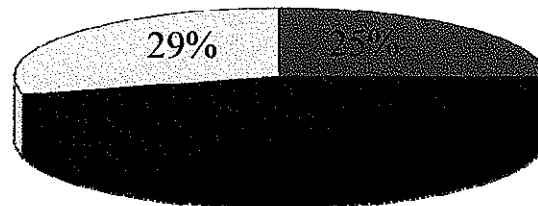
■ Memberships \$488,310

■ Contributions \$841,154

□ Net Store Sales and Other \$129,236

□ Net Investment Income \$2,142,013

Expenses



■ Program Services \$383,874

■ Foundation Grants \$693,903

□ Management & Development \$443,673

NAVAL WAR COLLEGE FOUNDATION, INC.

Charts

Year Ended December 31, 2008

