



THE ESTATE OF STEPHEN GIRARD, DECEASED

Financial Statements

June 30, 2016 and 2015

(With Independent Auditors' Report Thereon)

THE ESTATE OF STEPHEN GIRARD, DECEASED

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KPMG LLP
1601 Market Street
Philadelphia, PA 19103-2499

Independent Auditors' Report

The Board of Directors of City Trusts
Philadelphia, Pennsylvania:

We have audited the accompanying financial statements of The Estate of Stephen Girard, Deceased (the Estate), which comprise the statements of net assets – FASB basis as of June 30, 2016 and 2015, and the related statements of changes in net assets – FASB basis and cash flows – FASB basis for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with the basis of accounting described in note 1(c); this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position – FASB basis of the Estate of Stephen Girard, Deceased, as of June 30, 2016 and 2015, and the changes in its financial position – FASB basis and its cash flows – FASB basis for the years then ended, on the basis of accounting described in note 1(c).



Basis of Accounting

We draw attention to note 1(c) of the financial statements, which describes the basis of accounting. As described in note 10, the Board of Directors of City Trusts is an agency of the Commonwealth of Pennsylvania and, as such, the Estate is subject to the accounting standards promulgated by the Governmental Accounting Standards Board (GASB). The financial statements are prepared in accordance with the standards promulgated by the Financial Accounting Standards Board (FASB), which collectively represent another comprehensive basis of accounting. Our opinion is not modified with respect to this matter.

KPMG LLP

Philadelphia, Pennsylvania
October 25, 2016

THE ESTATE OF STEPHEN GIRARD, DECEASED

Statements of Net Assets – FASB Basis

June 30, 2016 and 2015

(In thousands)

Assets	2016	2015
Cash	\$ 1,222	1,328
Receivables, net	1,928	2,180
Prepaid and other assets	8,320	8,595
Investments	263,905	270,504
Note receivable	—	3,500
Assets held under indenture agreements	35,685	29,011
Property, plant and equipment, net	129,789	134,521
Total	<u>\$ 440,849</u>	<u>449,639</u>
Liabilities and Net Assets		
Liabilities:		
Accounts payable	\$ 1,388	1,099
Accrued expenses	2,957	2,942
Line of credit	3,500	—
Interest rate swap liability	32,185	25,302
Advance rents and other liabilities	91,596	85,062
Long-term debt	77,166	77,705
Total liabilities	<u>208,792</u>	<u>192,110</u>
Net assets – unrestricted	<u>232,057</u>	<u>257,529</u>
Total	<u>\$ 440,849</u>	<u>449,639</u>

See accompanying notes to financial statements – FASB basis.

THE ESTATE OF STEPHEN GIRARD, DECEASED

Statements of Changes in Net Assets – FASB Basis

Years ended June 30, 2016 and 2015

(In thousands)

	<u>2016</u>	<u>2015</u>
Revenues:		
Realized and unrealized investment (losses) gains	\$ (1,728)	4,153
Income from investments	5,091	7,166
Real estate	25,177	25,420
Girardville area	1,982	2,117
Reimbursements under government programs and other income	676	815
Contributions to Girard College	1,111	949
	<u>32,309</u>	<u>40,620</u>
Total revenues		
Expenses:		
Girard College	19,465	19,381
Management of Girard Estate:		
Real estate	15,964	16,779
Girardville area	599	578
Administration	1,319	1,460
Interest expense	4,205	4,196
Other	40	187
	<u>41,592</u>	<u>42,581</u>
Total expenses		
Loss on extinguishment of debt	—	496
Unrealized loss on interest rate swaps	6,883	3,677
Increase (decrease) in pension benefit obligations	9,306	(809)
	<u>(25,472)</u>	<u>(5,325)</u>
Decrease in net assets		
Net assets, beginning of year	<u>257,529</u>	<u>262,854</u>
Net assets, end of year	\$ <u><u>232,057</u></u>	\$ <u><u>257,529</u></u>

See accompanying notes to financial statements – FASB basis.

THE ESTATE OF STEPHEN GIRARD, DECEASED

Statements of Cash Flows – FASB Basis

Years ended June 30, 2016 and 2015

(In thousands)

	<u>2016</u>	<u>2015</u>
Cash flows from operating activities:		
Change in net assets	\$ (25,472)	(5,325)
Adjustments to reconcile change in net assets to net cash used in operating activities:		
Depreciation and amortization	7,858	7,767
Loss on early extinguishment of debt	—	496
Realized and unrealized investment losses (gains)	1,728	(4,153)
Interest rate swap liability	6,883	3,677
Change in operating assets and liabilities:		
Rent and other receivables	252	282
Prepays and other assets	258	29
Accounts payable and accrued expenses	304	(1,108)
Advance rents and other liabilities	6,534	(3,667)
Net cash used in operating activities	<u>(1,655)</u>	<u>(2,002)</u>
Cash flows from investing activities:		
Property additions	(3,109)	(4,351)
Proceeds from asset sales	—	3,493
Proceeds from sales of investments	—	5,694
Purchases of investments	(5,982)	(3,022)
Investments in joint ventures	(16,625)	(4,000)
Repayment of note receivable	3,500	—
Proceeds from joint ventures	19,595	3,144
Net cash (used in) provided by investing activities	<u>(2,621)</u>	<u>958</u>
Cash flows from financing activities:		
Assets held under indenture agreements	1,209	391
Proceeds from line of credit	6,000	—
Payments on line of credit	(2,500)	—
Proceeds from new debt	—	59,200
Payments on long-term debt	(539)	(59,718)
Net cash provided by (used in) financing activities	<u>4,170</u>	<u>(127)</u>
Net decrease in cash	(106)	(1,171)
Cash, beginning of year	<u>1,328</u>	<u>2,499</u>
Cash, end of year	\$ <u>1,222</u>	\$ <u>1,328</u>
Supplemental disclosures of cash flow information:		
Interest paid	\$ 4,187	3,812

See accompanying notes to financial statements – FASB basis.

THE ESTATE OF STEPHEN GIRARD, DECEASED

Notes to Financial Statements – FASB Basis

June 30, 2016 and 2015

(1) The Estate and Summary of Significant Accounting Policies

(a) *The Estate*

Upon his death in 1831, Stephen Girard bequeathed cash and real estate to the City of Philadelphia for the primary purpose of establishing a boarding school for orphans (Girard College). Girard College, in continuous operation since 1848, is now a full scholarship boarding school for grades 1 through 12 situated on a 43-acre campus in Philadelphia for academically capable students from qualified families of limited financial resources. The City of Philadelphia serves as Trustee under the will of Stephen Girard, Deceased, acting by the Board of Directors of City Trusts (hereinafter referred to as the Girard Estate or the Estate) and retains ownership of the assets and obligations of the Estate, which it administers for the benefit of the Estate. The Estate comprises personal property and real estate, principally acquired properties and improvements thereto in Philadelphia and throughout the Commonwealth of Pennsylvania (the Commonwealth) and anthracite coal lands in Schuylkill, Columbia, and Northumberland counties in the Commonwealth in the general vicinity of Girardville, Pennsylvania. The primary operations of the Estate include the funding and operation of Girard College. The funding is derived primarily from the Estate's investment portfolio, real estate assets and anthracite coal assets.

(b) *Petition to Orphans' Court of Philadelphia*

In June 2013, the Board of Directors of City Trusts (the Board) approved the following plan, subject to the approval of the Orphans' Court of Philadelphia (Orphans' Court), regarding the long-term sustainability of Girard College:

- 1) Girard College would temporarily convert its residential program to an extended day program beginning in the 2014–2015 academic year;
- 2) Girard College would temporarily suspend its operation of grades 9–11 beginning in the 2014–2015 academic year;
- 3) Girard College would temporarily suspend its operation of grade 12 beginning in the 2015–2016 academic year.

This plan was a temporary change and, subject to milestones established by the Board, the intent was to grow the school back to a residential academic program serving students from grades 1 through 12 as growth became sustainable. The plan did not involve any plan to close or relocate Girard College. The savings in staff and resources by temporarily suspending the five-day residential program and the high school would enable Girard College to reduce its expenses, repair its buildings, and replenish its investment endowment fund so that the income would be sufficient to maintain the school's operations in the future. The petition requesting approval of the operating plan was submitted to the Orphans' Court on July 29, 2013.

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Notes to Financial Statements – FASB Basis

June 30, 2016 and 2015

In October 2013, the Board determined that for the benefit of the children and to end any uncertainties that existed for the students, parents, staff and faculty associated with the implementation of the planned transition for the 2014–2015 academic year, Girard College would continue to operate as a residential boarding school for students in grades 1 through 12 until the 2015–2016 academic year. Also, for the 2015–2016 academic year only, Girard College would offer a nonresidential, extended day academic program serving students in the 12th grade. The Board presented its case to Orphans' Court in July 2014.

In August 2014, the Orphans' Court denied the Board's petition to temporarily suspend the residential and high school programs at Girard College. In September 2014, the Board filed a set of exceptions in the case, essentially asking the Court to reconsider its decision given the weight of the evidence presented during the hearing. Oral argument on the exceptions took place in October 2014. However, in November 2014, the Court maintained its position and denied the Board's exceptions.

In December 2014, the Board filed an appeal of the Orphans' Court ruling to Commonwealth Court. It also announced that Girard College would continue to operate the high school program until the completion of the 2018–2019 academic year regardless of the outcome of the appeal so that all current students in grades 9–12 would be able to graduate. The Board presented its oral argument on the appeal to Commonwealth Court in October 2015. However, in January 2016, the Commonwealth Court affirmed the Orphans' Court ruling, which denied the Board's petition. The Board accepted the Commonwealth Court ruling and continues to operate Girard College as a residential boarding school for students in grades 1 through 12.

(c) ***Basis of Accounting***

As described in note 10, the Board is an agency of the Commonwealth of Pennsylvania and, as such, the Estate is subject to the accounting standards promulgated by the Governmental Accounting Standards Board (GASB). However, to prepare the financial statements and notes thereto, the Estate has chosen to follow accounting standards promulgated by the Financial Accounting Standards Board (FASB) applicable to not-for-profit organizations to reflect a presentation that is consistent with historical practices and that is followed by other trusts. Estate management believes that the FASB format presents the results of its diversified educational, investment and real estate activities in a manner that is more meaningful to third parties and to the Board.

If the Estate's financial statements were prepared in accordance with GASB standards rather than FASB standards, the following significant differences would exist:

- Management's discussion and analysis would be required supplementary information.
- Net position, rather than net assets, would be presented. Net position would include, in addition to an unrestricted component, a component for net investment in capital assets.
- Recorded obligations for retirement plans would be accounted for similar to pension obligations under FASB standards, with differences in the rate used to discount future pension benefits to their present value and the method used to attribute pension liabilities to specific periods. Additionally, information on funding progress for the plans would be required supplementary information.

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Notes to Financial Statements – FASB Basis

June 30, 2016 and 2015

- The Estate would be required to evaluate the effectiveness of its interest rate swaps as potential hedging derivative instruments. If deemed effective, changes in fair value of the swaps would be recorded as a deferred outflow of resources or a deferred inflow of resources rather than unrealized gain or loss on the statements of changes in net assets – FASB basis.
- Gains and losses related to debt defeasance would be deferred and amortized over the life of the debt rather than recorded as gain or loss at the time of the defeasance.
- Debt issuance costs, except any portion related to prepaid insurance costs, would be recognized as an expense in the period incurred, rather than amortized over the life of the related debt.
- Additional disclosures would be provided regarding:
 - interest rate risk, credit risk, custodial credit risk and concentrations of credit risk related to the Estate’s investments and the Estate’s policies for managing such risks;
 - a description of the risks of loss to which the entity is exposed and the ways in which the risks of loss are managed;
 - pledged revenues under the Estate’s debt agreements;
 - additions to and deductions from the Estate’s capital assets and long-term debt and maturities of interest payments on long-term debt.

(d) Net Assets

In accordance with accounting standards promulgated by the FASB applicable to not-for-profit organizations, net assets, revenues and expenses are classified based on the existence or absence of donor-imposed restrictions. Temporarily and permanently restricted net assets are not significant and, therefore, all net assets and changes therein are classified and reported as unrestricted net assets in the accompanying financial statements.

(e) Receivables

Receivables include investment income receivable and accounts receivable. Accounts receivable are net of an allowance for bad debts which is estimated based upon the Estate’s assessment of factors related to the collectibility of such receivables. Actual losses may vary from current estimates. These estimates are reviewed periodically and if changes to such estimates are deemed necessary they are recorded in the period in which they become reasonably estimable.

THE ESTATE OF STEPHEN GIRARD, DECEASED

Notes to Financial Statements – FASB Basis

June 30, 2016 and 2015

(f) Investments

At June 30, 2016 and 2015, the Estate's investments were primarily invested in the Collective Legal Investment Fund (the CLIF), which is a pooled investment fund of the assets of all the trusts administered by the Board. Such investments are stated at fair value. Units of the CLIF are normally purchased and sold based on the available cash and cash requirements of the Estate. Gains and losses from the sales of such units, determined on the last-in, first-out method, are included in the statements of changes in net assets – FASB basis. The change in the difference between aggregate market value and the cost of investments from the beginning to the end of the year is reflected in the statements of changes in net assets – FASB basis. Earnings from the CLIF are allocated based on units held.

The CLIF participates in a securities lending program as a means to generate incremental income. Through this program, the CLIF may lend its securities to qualified borrowers, through its lending agent, that meet certain guidelines as established by the Board. All borrowings are initially secured by collateral in an amount equal to at least 102% of the fair value of the securities loaned and are marked to market daily. Each business day, the amount of collateral is adjusted based on the prior day's closing fair value. The collateral is invested in cash and cash equivalents. Income from lending activity is determined by the amount of interest earned on the invested collateral, a portion of which is allocated to the lending agent. The CLIF also is entitled to receive interest and dividends from securities on loan.

As of June 30, 2016 and 2015, the CLIF had loaned out certain securities, returnable on demand, with a market value of \$214,144,000 and \$41,976,000, respectively, to several financial institutions that have deposited collateral with respect to such securities of \$219,802,000 and \$43,033,000, respectively.

The Estate is the minority partner in several joint ventures which are accounted for on the equity method.

(g) Assets Held Under Indenture Agreements

The Collateral Pledge and Security Agreement related to the Series of 2014 Refunding Bonds requires funds to be deposited with a trustee as security for outstanding debt obligations related to the Estate's associated interest rate swap agreement. Assets held under indenture agreements consist of cash equivalents and securities segregated for this purpose within the CLIF.

(h) Interest Rate Swaps

The Estate's interest rate swaps related to its debt are measured at fair value and are recognized as assets or liabilities in the statements of net assets – FASB basis. Changes in the fair value from year to year are recognized in the Statement of Changes in Net Assets – FASB Basis.

(i) Property, Plant, and Equipment

Property, plant, and equipment comprise land, equipment, and real estate improved and acquired for investment purposes, Girard College real property and facilities and construction-in-progress.

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Notes to Financial Statements – FASB Basis

June 30, 2016 and 2015

Expenditures for property, plant, and equipment are recorded at cost. Improvements to buildings and Girard College capital assets are stated at cost less accumulated depreciation calculated on a straight-line basis over the estimated useful lives, ranging primarily from 5 to 35 years. Alterations for tenants are stated at cost less accumulated depreciation calculated on a straight-line basis over the terms of the respective leases. Equipment is stated at cost less accumulated depreciation calculated on a straight-line basis over the estimated useful lives, ranging primarily from 5 to 20 years.

Long-lived assets to be held and used are assessed for impairment whenever events or changes in circumstances indicate that their carrying amount may not be recoverable. If circumstances indicate a long-lived asset is impaired, the asset value will be reduced to fair value. Fair value is determined through various valuation techniques including quoted market values and third-party independent appraisals, as considered necessary.

(j) ***Fair Value***

Fair value is the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date.

There are three levels of inputs that may be used to measure fair value:

Level 1: Quoted prices in active markets for identical assets or liabilities. Level 1 assets and liabilities include debt and equity securities that are traded in an active exchange market and U.S. Treasury securities.

Level 2: Observable inputs other than Level 1 prices such as quoted prices for similar assets and liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities. Level 2 assets and liabilities include debt securities with quoted market prices that are traded less frequently than exchange-traded instruments. This category generally includes certain U.S. government and agency mortgage-backed debt securities and corporate debt securities.

Level 3: Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies or similar techniques as well as instruments for which the determination of fair value requires significant management judgment or estimation.

The Estate measures its investments and interest rate swaps related to its debt at fair value in accordance with other accounting pronouncements. The Estate's valuation methodology for each of these items is described in the paragraphs below. The inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such cases, for disclosure purposes, the level in the fair value hierarchy within which the fair value measurement falls in its entirety is determined based on the lowest-level input that is significant to the fair value measurement.

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Notes to Financial Statements – FASB Basis

June 30, 2016 and 2015

Collective Legal Investment Fund

At June 30, 2016 and 2015, the Estate's investments include shares owned in the CLIF which invests in the following types of securities:

Equity Securities

Securities traded on a national securities exchange (or reported on the NASDAQ national market) are stated at the last reported sales price on the day of valuation. To the extent these securities are actively traded, they are categorized in Level 1 of the fair value hierarchy.

Debt Securities

U.S. government securities are generally valued at the closing price reported in the active market in which the individual security is traded, if available (Level 1 inputs), or yields currently available on comparable securities (Level 2 inputs)

Listed asset-backed securities are valued based on quoted market prices from the active market in which the instrument is principally traded and are categorized in Level 1 of the fair value hierarchy. If such quoted prices are not available, the fair value of the security is estimated based on models considering the estimated cash flows and expected yield. Such investments are categorized as Level 2 or Level 3 based on the extent inputs are observable and timely.

Other debt securities are valued at the closing price reported in the active market in which the security is traded, if available. If such information is not available, debt is valued based on yields currently available on comparable securities for issuers with similar credit ratings (Level 2 inputs).

Private Equity Funds

Net asset values provided by limited partnership investees are based on the net asset value per share as reported by the investee as a practical expedient. Net asset value may differ from fair value as otherwise calculated. Such investments, which are measured at net asset value per share as a practical expedient to fair value, have not been categorized in the fair value hierarchy table below.

Interest Rate Swaps

The fair value of the Estate's interest rate swaps related to its debt obligations is based on a discounted cash flow model with Level 3 inputs including the value of the relevant market index upon which the swap is based.

(k) 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, 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. The

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Notes to Financial Statements – FASB Basis

June 30, 2016 and 2015

Estate’s most significant estimates include actuarial assumptions used to determine pension benefit obligations and interest rate swaps. Actual results may differ from those estimates and assumptions.

(l) Asset Retirement Obligation

Substantially all of the Estate’s asset retirement obligations represent estimated costs to remove asbestos within the Estate properties. The following is a reconciliation of the Estate’s remaining asset retirement obligation for the years ended June 30, 2016 and 2015 (in thousands):

Balance, June 30, 2014	\$	836
Remediation		(3)
Accretion expense		50
		<hr/>
Balance, June 30, 2015		883
Remediation		(13)
Accretion expense		40
		<hr/>
Balance, June 30, 2016	\$	<u>910</u>

The liability is recorded as a component of advance rents and other liabilities in the statements of net assets – FASB basis.

(m) New Accounting Pronouncements

FASB Accounting Standards Update (ASU) No. 2015-07, Disclosures for Investments in Certain Entities that Calculate Net Asset Value per Share (or its Equivalent), was effective for December 31, 2015. ASU No. 2015-07 removes the requirement to categorize within the fair value hierarchy all investments for which fair value is measured using the net asset value per share as a practical expedient. The presentation in note 2 reflects the implementation of the provisions of ASU No. 2015-07.

(2) Investments and Assets Held Under Indenture Agreements

The following summarizes the Estate’s investments as of June 30, 2016 and 2015 (in thousands):

	<u>2016</u>	<u>2015</u>
3,105,341 and 3,036,756 Collective Legal Investment		
Fund units, respectively	\$ 242,406*	252,609*
Joint ventures	21,304	17,701
Money market funds	195	194
	<hr/>	<hr/>
Total investments	\$ <u>263,905</u>	<u>270,504</u>

* Amounts exclude \$35,685,000 at June 30, 2016 and \$27,802,000 at June 30, 2015 that are segregated within the CLIF to comply with the requirements of certain debt, line of credit and swap agreements. Such amounts have been included in assets held under indenture agreements to reflect the restriction on their use.

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Notes to Financial Statements – FASB Basis

June 30, 2016 and 2015

The composition of the Estate's investment returns for the years ended June 30, 2016 and 2015 are as follows (in thousands):

	<u>2016</u>	<u>2015</u>
Net realized gain on sales of CLIF investments	\$ 394	1,596
Unrealized appreciation (depreciation) in fair value of CLIF investments	(8,697)	2,823
Dividend and interest income, net	4,736	6,169
Total CLIF (loss) income	<u>(3,567)</u>	<u>10,588</u>
Gain on sales of joint ventures	7,615	—
Share in joint ventures' operating (loss)	(1,040)	(266)
Total joint venture income (loss)	<u>6,575</u>	<u>(266)</u>
Other	355	997
Total investment income	<u>\$ 3,363</u>	<u>11,319</u>

(a) ***Collective Legal Investment Fund***

The CLIF is a balanced portfolio composed primarily of equity, fixed-income and short-term investment securities. It is intended to be more aggressive than income-oriented portfolios and less aggressive than equity-oriented portfolios. All asset classes, other than alternative investments, must have a readily ascertainable market value and must be readily marketable. The Board's investment policy does allow private investment funds on a limited basis. As of June 30, 2016, 1.7% of the CLIF assets have been invested in this asset class.

The equity portfolio is well diversified to avoid undue exposure to any single economic sector, industry group or individual security.

Risk, volatility and the possibility of loss in purchasing power are present to some degree in all types of investment vehicles. While high levels of risk are normally avoided, the assumption of risk is warranted and encouraged in order to allow the opportunity to achieve satisfactory long-term results consistent with objectives and fiduciary character of the CLIF. The volatility of returns are monitored and evaluated on a continuing basis.

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Notes to Financial Statements – FASB Basis

June 30, 2016 and 2015

At June 30, 2016 and 2015, the Estate owned approximately 58.73% and 57.80%, respectively, of the total units in the CLIF. The total investments of the CLIF at fair value as of June 30, 2016 and 2015 are as follows (in thousands):

	<u>2016</u>	<u>2015</u>
Short-term investments	\$ 18,475	12,230
Equities:		
Common stock	205,405	228,438
Exchange-traded funds	46,990	55,082
International equity mutual funds	29,154	30,530
Fixed income:		
U.S. government and agency obligations	31,003	30,873
Corporate and other bonds	86,924	84,165
Asset-backed securities	2,839	3,844
Mutual Funds	20,419	—
Global tactical asset allocation mutual funds	24,037	29,376
Private equity	8,259	10,618
Total investments in the CLIF	<u>\$ 473,505</u>	<u>485,156</u>

The CLIF's accounting policy is to recognize transfers between levels of the fair value hierarchy on the date of the event or change in circumstances that caused the transfer. There were no transfers into or out of Level 1, Level 2, or Level 3 for the years ended June 30, 2016 or 2015 other than the effect of ASU 2015-07 as described in note 1(n).

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Notes to Financial Statements – FASB Basis

June 30, 2016 and 2015

The following table presents the CLIF’s fair value hierarchy for assets held in the CLIF measured at fair value on a recurring basis as of June 30, 2016 (in thousands):

	2016 Fair value	Fair value measurements at June 30, 2016 using	
		Level 1	Level 2
Short-term investments	\$ 18,475	18,475	—
Equity securities:			
U.S. common stocks:			
Industrials	25,940	25,940	—
Consumer discretionary	32,297	32,297	—
Consumer staples	18,149	18,149	—
Energy	11,448	11,448	—
Financial	33,057	33,057	—
Materials	7,774	7,774	—
Information technology	35,489	35,489	—
Utilities	4,109	4,109	—
Healthcare	28,454	28,454	—
Telecommunications and other	8,688	8,688	—
Total U.S. common stocks	<u>205,405</u>	<u>205,405</u>	<u>—</u>
Exchange traded funds:			
S&P 500 Index SPDR	25,535	25,535	—
Select Sector SPDRs	21,455	21,455	—
Total exchange traded funds	<u>46,990</u>	<u>46,990</u>	<u>—</u>
International equity mutual funds	<u>29,154</u>	<u>29,154</u>	<u>—</u>
Total equity securities	<u>281,549</u>	<u>281,549</u>	<u>—</u>
Fixed income:			
Debt securities issued by the United States			
Treasury and other U.S. government corporations and agencies	29,773	29,610	163
Debt securities issued by states of the United States and political subdivisions of the states	1,164	—	1,164
Debt securities issued by foreign governments	66	—	66
Corporate debt securities	86,924	—	86,924
Asset-backed securities	1,189	—	1,189
Residential mortgage-backed securities	852	—	852
Commercial mortgage-backed securities	798	—	798
Mutual Funds	<u>20,419</u>	<u>20,419</u>	<u>—</u>
Total fixed income	141,185	50,029	91,156
Global tactical asset allocation mutual funds	<u>24,037</u>	<u>24,037</u>	<u>—</u>
Total	<u>465,246</u>	<u>374,090</u>	<u>91,156</u>
Private equity funds reported at net asset value per share as a practical expedient	<u>8,259</u>		
Total investments in the CLIF	<u>\$ 473,505</u>		

THE ESTATE OF STEPHEN GIRARD, DECEASED

Notes to Financial Statements – FASB Basis

June 30, 2016 and 2015

The following table presents the CLIF’s fair value hierarchy for assets held in the CLIF measured at fair value on a recurring basis as of June 30, 2015 (in thousands):

	2015 Fair value	Fair value measurements at June 30, 2015 using	
		Level 1	Level 2
Short-term investments	\$ 12,230	12,230	—
Equity securities:			
U.S. common stocks:			
Industrials	26,702	26,702	—
Consumer discretionary	39,176	39,176	—
Consumer staples	10,138	10,138	—
Energy	12,913	12,913	—
Financial	41,338	41,338	—
Materials	7,891	7,891	—
Information technology	47,159	47,159	—
Utilities	2,157	2,157	—
Healthcare	34,155	34,155	—
Telecommunications and other	6,809	6,809	—
Total U.S. common stocks	<u>228,438</u>	<u>228,438</u>	<u>—</u>
Exchange traded funds:			
S&P 500 Index SPDR	34,869	34,869	—
Select Sector SPDRs	20,213	20,213	—
Total exchange traded funds	<u>55,082</u>	<u>55,082</u>	<u>—</u>
International equity mutual funds	<u>30,530</u>	<u>30,530</u>	<u>—</u>
Total equity securities	<u>314,050</u>	<u>314,050</u>	<u>—</u>
Fixed income:			
Debt securities issued by the United States Treasury and other			
U.S. government corporations and agencies	29,152	26,665	2,487
Debt securities issued by states of the United States and political subdivisions of the states	1,159	—	1,159
Debt securities issued by foreign governments	562	—	562
Corporate debt securities	84,165	—	84,165
Asset-backed securities	2,019	—	2,019
Residential mortgage-backed securities	29	—	29
Commercial mortgage-backed securities	1,796	—	1,796
Total fixed income	<u>118,882</u>	<u>26,665</u>	<u>92,217</u>
Global tactical asset allocation mutual funds	<u>29,376</u>	<u>29,376</u>	<u>—</u>
Total	<u>474,538</u>	<u>382,321</u>	<u>92,217</u>
Private equity funds reported at net asset value per share as a practical expedient	<u>10,618</u>		
Total investments in the CLIF	<u>\$ 485,156</u>		

THE ESTATE OF STEPHEN GIRARD, DECEASED

Notes to Financial Statements – FASB Basis

June 30, 2016 and 2015

(b) *Joint Ventures*

The Estate has invested in various joint ventures which own diversified real estate assets including an office building leased as an automotive research facility, student housing, apartment complexes, a parking garage and retail/office/industrial facilities for lease in several states. The Estate is entitled to preferred cumulative dividends and/or operational cash flow from net operating income. These investments are accounted for on the equity method.

The following table summarizes the Estate's investments in joint ventures as of June 30, 2016 and 2015 (in thousands):

	<u>2016</u>	<u>2015</u>
Joint venture beginning balance	\$ 17,701	17,111
Additional investments	16,625	4,000
Proceeds from sales of joint ventures	(15,328)	—
Cash distributions	(2,749)	(1,838)
Return of capital	(1,520)	(1,306)
Gain on sales	7,615	—
Share in joint ventures	(1,040)	(266)
Joint venture ending balance	<u>\$ 21,304</u>	<u>17,701</u>

(c) *Assets Held Under Indenture Agreements*

Assets held under indenture agreements at June 30, 2016 and 2015 were \$35,685,000 and \$29,011,000, respectively. Of these amounts, \$35,685,000 and \$27,802,000, respectively, were segregated within the CLIF while the remainder at June 30, 2015 was held in cash and cash equivalents in a separate account with a trustee.

(3) **Note Receivable**

In November 2013, the Estate provided \$3,500,000 in mezzanine financing for the construction of a multi-story apartment building in Philadelphia, Pennsylvania. The note had a not to exceed term of 36 months with interest payable monthly. As part of the same transaction, the Estate provided, for a fee, a \$2,500,000 completion of construction letter of credit through a bank to support the primary construction loan. The bank required the Estate to post collateral equal to the face amount of the letter of credit.

In July 2015, the Estate received \$3,500,000 and all interest due in satisfaction of the note receivable and subsequently thereafter the \$2,500,000 letter of credit was canceled and all collateral was released by the bank.

THE ESTATE OF STEPHEN GIRARD, DECEASED

Notes to Financial Statements – FASB Basis

June 30, 2016 and 2015

(4) Property, Plant and Equipment

Property, plant, and equipment of the Estate as of June 30, 2016 and 2015 are as follows (in thousands):

	2016	2015
Real estate operations:		
Land	\$ 28,152	28,169
Buildings and improvements	127,306	128,034
Tenant alterations	6,236	11,721
Equipment	510	177
	162,204	168,101
Accumulated depreciation	(58,577)	(60,859)
	103,627	107,242
Coal operations:		
Equipment	295	321
	295	321
Accumulated depreciation	(220)	(240)
	75	81
Girard College operations:		
Capital assets	59,093	58,643
Equipment	1,209	1,765
	60,302	60,408
Accumulated depreciation	(34,215)	(33,210)
	26,087	27,198
Total property, plant, and equipment, net	\$ 129,789	134,521

Land and other real estate received under the will of Stephen Girard after his death in 1831 have been assigned no value in the accounts of the Estate and represent various properties in Philadelphia, Schuylkill and Columbia counties in Pennsylvania. Subsequent improvements to buildings and real estate have been capitalized and depreciated.

The Estate recorded depreciation expense of \$7,841,000 and \$7,745,000 in 2016 and 2015, respectively.

THE ESTATE OF STEPHEN GIRARD, DECEASED

Notes to Financial Statements – FASB Basis

June 30, 2016 and 2015

(5) Retirement Plans

(a) Defined-Benefit Plans

Non-union employees of the Estate and Girard College hired prior to September 1, 2010 and certain union employees participate in the Board of Directors of City Trusts Girard Non-Contributory Retirement Plan (Non-Contributory Plan). Certain other union employees participate in the Board of Directors of City Trusts Contributory Retirement Plan (Contributory Plan). Contributions to the Contributory and Non-Contributory plans (the Plans) provide for the payment of estimated normal cost and amortization of the unfunded prior service liability over a 25-year period.

The Estate recorded a liability of \$10,153,000 and \$2,570,000 at June 30, 2016 and 2015, respectively, for the Estate’s unfunded status, which is included as a component of advance rents and other liabilities in the statements of net assets – FASB basis.

The following presents the projected funded status and accrued cost of the Plans for the year ended June 30, 2016 (in thousands):

	Contributory plan	Non- contributory plan
Projected benefit obligations – June 30	\$ (6,780)	(40,233)
Fair value of plan assets – June 30	5,421	31,439
Funded status	\$ (1,359)	(8,794)
Accrued cost recognized in the Estate’s statement of net assets	\$ (1,359)	(8,794)
Accumulated benefit obligation	6,517	38,762
Benefit expense	77	48
Employer contribution	238	1,927
Plan participants’ contribution	38	—
Benefits paid	319	1,352
Weighted average assumptions used to determine benefit obligation and net periodic benefit cost:		
Discount rate	3.48%	3.51%
Expected long-term return on plan assets	7.75	7.75
Rate of compensation increase	3.00	3.00

The expected rate of return on Plan assets was changed to 7.75% at June 30, 2016 and has been employed for both Plans based on their investment in the CLIF. It is a reasonable estimate based on (a) the CLIF’s actual annual rates of return in the past and (b) reasonable expectations with regard to the future annual returns.

THE ESTATE OF STEPHEN GIRARD, DECEASED

Notes to Financial Statements – FASB Basis

June 30, 2016 and 2015

The following presents the projected funded status and accrued cost of the Plans for the year ended June 30, 2015 (in thousands):

	Contributory Plan	Non- Contributory Plan
	<u> </u>	<u> </u>
Projected benefit obligations – June 30	\$ (5,856)	(33,746)
Fair value of plan assets – June 30	<u>5,610</u>	<u>31,422</u>
Funded status	\$ <u>(246)</u>	<u>(2,324)</u>
Accrued cost recognized in the Estate’s statement of net assets	\$ (246)	(2,324)
Accumulated benefit obligation	5,625	32,578
Benefit expense	123	400
Employer contribution	412	1,927
Plan participants’ contribution	38	—
Benefits paid	401	1,255
Weighted average assumptions used to determine benefit obligation and net periodic benefit cost:		
Discount rate	4.20%	4.27%
Expected long-term return on plan assets	8.00	8.00
Rate of compensation increase	3.00	3.00

The components of net periodic benefit cost for the years ended June 30, 2016 and 2015 are as follows (in thousands):

	2016	2015
	<u> </u>	<u> </u>
Amounts recognized in net assets but not yet recognized in net periodic benefit cost:		
Prior service costs	\$ 171	208
Net loss	<u>16,725</u>	<u>7,064</u>
Total amount recognized in net assets	\$ <u>16,896</u>	<u>7,272</u>
Components of net periodic benefit cost:		
Service cost	\$ 1,056	1,245
Interest cost	1,647	1,628
Expected return on plan assets	(2,924)	(2,786)
Amortization of prior service cost	37	56
Recognized actuarial cost	<u>309</u>	<u>380</u>
Net periodic benefit cost	\$ <u>125</u>	<u>523</u>

THE ESTATE OF STEPHEN GIRARD, DECEASED

Notes to Financial Statements – FASB Basis

June 30, 2016 and 2015

The Estate expects to contribute \$353,000 and \$1,247,000 to the Contributory and Non-Contributory Retirement Plans, respectively, in fiscal year 2017.

The expected benefit payments from the Plans for the next 10 years are as follows (in thousands):

	Contributory Plan	Non- Contributory Plan
2017	\$ 389	1,670
2018	378	1,705
2019	367	1,774
2020	390	1,821
2021	378	1,847
Years 2022–2026	1,821	10,183
	\$ 3,723	19,000

The Plans' investments were held in the CLIF at June 30, 2016 and 2015.

	June 30, 2016		June 30, 2015	
	CLIF units held	Percentage of CLIF held	CLIF units held	Percentage of CLIF held
Contributory Plan	59,805	1.13%	59,830	1.09%
Non-Contributory Plan	345,621	6.54	334,370	6.08

(b) Defined Contribution Plan

Girard Estate and Girard College nonunion employees hired after August 31, 2010 participate in the Girard Estate/Girard College Retirement Plan, a 403(b) defined contribution retirement plan. Employees may choose to defer a portion of their compensation in accordance with Internal Revenue Services regulations. Employee contributions are immediately fully vested and are not subject to forfeiture for any reason. Eligible participants receive a discretionary annual employer contribution, which is determined each year. The employer contributions for fiscal years 2016 and 2015 were set at 3% of eligible compensation and in the aggregate were \$27,000 and \$27,000, respectively.

(6) Line of Credit

In April 2016, the Estate entered into a secured revolving line of credit agreement with a bank which provides that the Estate may borrow up to \$15,000,000. Amounts outstanding under this line bear interest at the Daily LIBOR plus 0.90%. If the average amount of the unused line is greater than 50% of the total available line, an unused fee equal to 0.15% on the average daily amount of the unused portion is due annually. The Estate is required to pledge as collateral certain marketable securities with an adjusted (as defined) market value at least equal to the monthly outstanding balance. Such collateral is held in the CLIF and presented as assets

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Notes to Financial Statements – FASB Basis

June 30, 2016 and 2015

held under indenture agreements in the statements of net assets – FASB basis. The line expires on April 19, 2017 with an option to renew by the bank, in its sole discretion. At June 30, 2016, the Estate had outstanding borrowings of \$3,500,000 under this line.

(7) Long-Term Debt

(a) *1101 Market Street Financing*

In May 2012, an insurance company issued a \$20,000,000, 3.95% fixed rate, 10-year term, 25-year amortization note as a partial refinancing of the fee and leasehold interest in the office building located at 1101 Market Street in Philadelphia, Pennsylvania. Repayments of principal and interest began in July 2012 and are due monthly for 10 years up to and including June 2022. At that time, a significant portion of the principal will remain outstanding and will require refinancing or satisfaction.

(b) *Series of 2014 Revenue Refunding Bonds*

On December 1, 2014, The Philadelphia Authority for Industrial Development issued \$59,200,000 of Tax-Exempt Revenue Bonds (Girard Estate Project) Series of 2014 Revenue Refunding Bonds (the 2014 Bonds) with a bank being the sole holder. The proceeds were used to refinance and redeem the Series of 2001 and Series of 2002 Bonds. The loan agreement is a general obligation of the Estate payable from the unrestricted revenues of the Estate.

The bank, in its sole discretion, has the option within 90 days prior to and 90 days after the 10 year anniversary following the bond issuance date to declare the entire principal balance and accrued and unpaid interest of the 2014 Bonds payable in full. If exercised, payment on this call option would be due within 90 days of such written notification from the bank.

In connection with the issuance of the 2014 Bonds, the Estate entered into an interest swap contract in order to convert the variable interest rate for the 2014 Bonds to a synthetic fixed rate plus the applicable credit spread. The swap contract has a notional amount of \$59,200,000 with a final maturity of June 1, 2032. The fair value of the rate swap at June 30, 2016 and 2015 was \$32,185,000 and \$25,302,000, respectively.

(c) *Debt Covenants*

The Estate has covenanted that it will not lease, sell or otherwise dispose of all or a part of the project facilities of the facilities leasing projects to a person other than a governmental unit. In the event that the Commonwealth or any other lessee of all or a portion of the 2014 project facilities assigns its rights as lessee to an assignee that is not a governmental unit, the Estate is required to take remedial action (if any) in order to maintain the exclusion of interest on the 2014 Bonds from gross income for federal income tax purposes.

The debt covenants under the bond purchase and loan agreement require that the Estate maintain a ratio of market value of unrestricted cash and investments to funded debt equal to or greater than 1.50 as those terms are defined in the agreement. Also, the Estate may not issue or incur any additional general obligation indebtedness without the prior written consent of the swap counterparty, which consent will not be unreasonably withheld.

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June 30, 2016 and 2015

Under the Collateral Pledge and Security Agreement to the 2014 swap master agreement, the Estate is required to pledge as collateral certain marketable securities with an adjusted (as defined) market value equal to the monthly net fair value loss of the Estate’s rate swap. Such collateral is held in the CLIF and presented as assets held under indenture agreements in the statements of net assets – FASB basis. In addition, the counterparty has a priority secured position, in the event of default, against the Estate’s marketable securities.

The Estate was in compliance with the Bond covenant, letter of credit agreement, swap agreement, line of credit agreement and mortgage note as of June 30, 2016 and 2015.

Long-term debt consists of the following at June 30, 2016 and 2015:

	<u>2016</u>	<u>2015</u>
	(In thousands)	
2014 Bonds, interest paid monthly, variable rate swapped to a fixed rate of 4.9035%, no principal payments until \$23,200,000 in 2031 and \$36,000,000 in 2032. The loan agreement is a general obligation of the Estate.	\$ 59,200	59,200
Mortgage payable, 3.95% fixed rate note, 10-year term to June 2022, 25-year amortization.	<u>17,966</u>	<u>18,505</u>
	<u>\$ 77,166</u>	<u>77,705</u>

Maturities of the long-term debt outstanding are as follows (in thousands):

Year ended June 30:	
2017	\$ 561
2018	583
2019	607
2020	631
2021	656
Thereafter	<u>74,128</u>
	<u>\$ 77,166</u>

(8) Interest Rate Swap

The following is a summary of the Estate’s interest rate swap agreement (in thousands):

<u>Series</u>	<u>Effective date</u>	<u>Notional amount</u>	<u>Estate pays</u>	<u>Estate receives</u>	<u>Expiration date</u>
2014 Bonds	12/01/2014	\$ 59,200	4.9035% plus 69% of 30-day LIBOR	69% of 30-day LIBOR	6/1/2032

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Notes to Financial Statements – FASB Basis

June 30, 2016 and 2015

The fair value of the interest rates swap is recorded in the financial statements as follows (in thousands):

	<u>Balance sheet location</u>	<u>Location of gain (loss)</u>	<u>Fair value 2016</u>	<u>Fair value 2015</u>	<u>(Loss) 2016</u>	<u>(Loss) 2015</u>
Interest rate swap agreement	Interest rate swap liability	Unrealized loss on interest rate swaps	\$ 32,185	25,302	(6,883)	(3,677)

The following table presents the fair value hierarchy classification of the Estate’s swap obligations as of June 30, 2016 with a comparative total for 2015 (in thousands):

	<u>Fair value 2016</u>	<u>Fair value measurements at June 30, 2016 using</u>			<u>Fair value 2015</u>
		<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	
Financial liabilities:					
Interest rate swap obligation	\$ 32,185	—	—	32,185	25,302

(9) Real Estate Leases

Tenant leases have various expiration dates ranging through fiscal year 2025. Minimum rentals on non-cancellable operating leases at June 30, 2016, which represent future income to the Estate, are as follows (in thousands):

2017	\$ 16,489
2018	14,927
2019	6,205
2020	3,075
2021	1,986
Thereafter	<u>74,730</u>
	\$ <u>117,412</u>

In September 2016, the largest tenant in the Estate’s 1101 Market Street office building in Philadelphia announced it would be relocating when its lease expires in September 2018. The tenant occupies approximately 367,000 square feet of office space representing 59% of the combined retail and office components of the building. Anticipating the announcement, in July 2016 the Estate retained the services of an international commercial real estate brokerage firm to assist it in the repositioning strategy and lease-up of the building in advance of the anticipated fiscal 2019 vacancy.

In 2007, the Estate entered into a long-term ground lease with a lessee, in the form of two leases, for the land and existing buildings located in the City of Philadelphia, between Market and Chestnut Streets and between 11th and 12th Streets and received an up-front payment of \$90,000,000. In addition, the Estate will receive basic net rent, for each lease, of \$1 per year.

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June 30, 2016 and 2015

The leases are triple net leases with all income, expenses, taxes and liabilities transferring to the lessee for a term of 75 years. At the lessee's option, the lease term can be extended for an additional term of 75 years for the then current market rate to be determined by binding arbitration in either the 50th, 60th or 74th year of the lease. Title to the property remains with the Estate and, as a result, the lease is accounted for as an operating lease. The \$90,000,000 up-front payment at June 30, 2007 was recorded as unearned rental income and is included in advance rents and other liabilities in the statements of net assets – FASB basis. The unamortized balances at June 30, 2016 and 2015 were \$79,137,000 and \$80,337,000, respectively. The lessee has been granted the right to perform property improvements up to and including the demolishing of current structures and the development of new properties. Title to new properties and improvements passes to the Estate at the end of the lease term. The leases do not contain bargain purchase options. In July 2008, the leases were assigned by the lessee, with the Estate's consent, to a third party. In September 2014, the ground lease covering the land and existing buildings fronting on Market, 11th and Chestnut Streets was divided into three separate ground leases, each of which was then assigned, with the Estate's consent, to an affiliate of the then-existing ground lessee.

(10) Tax Status

The City of Philadelphia, Trustee Under the Will of Stephen Girard, Deceased, Acting by the Board of Directors of City Trusts, statutory agent for the City of Philadelphia, has been determined to be an agency of the Commonwealth of Pennsylvania and, as such, is exempt from federal income taxes.

U.S. generally accepted accounting principles require management to evaluate income tax positions taken by the Estate and recognize a tax liability (or asset) if the Estate has taken an uncertain tax position that more likely than not would not be sustained upon examination by the IRS. Management has analyzed the tax positions taken by the Estate and has concluded that, as of June 30, 2016 and 2015, there are no uncertain positions taken or expected to be taken that would require recognition of a liability (or asset) or disclosure in the financial statements. The Estate is subject to routine audits by taxing jurisdictions; however, there are currently no audits for any tax periods in progress.

(11) Commitments and Contingencies

The Estate is party to various claims and legal proceedings which arise in the normal course of business. Management, after consultation with legal counsel, does not believe that the resolution of these matters will have a material adverse effect on the Estate's financial condition or results of operations.

(12) Related-Party Transactions

The Estate has a written conflict of interest policy that requires, among other things, that no member of the Board can participate in any decision in which he or she (or an immediate family member) has a material financial interest. When such relationships exist, measures are taken to mitigate any actual or perceived conflict, including requiring that such transactions be conducted at arm's length, for good and sufficient consideration, based on terms that are fair and reasonable and for the benefit of the Estate, and are in accordance with applicable conflict of interest laws.

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Notes to Financial Statements – FASB Basis

June 30, 2016 and 2015

(13) Subsequent Events

In connection with the preparation of the financial statements, the Estate evaluated subsequent events after the balance sheet date of June 30, 2016 through October 25, 2016, which was the date the financial statements were issued.