

# **Institute for Defense Analyses**

**Report of Independent Auditors on Financial  
Statements and Schedule of Expenditures of  
Federal Awards in Accordance with the OMB  
Uniform Guidance**

**For the Year Ended September 27, 2019**

**EIN#: 53-0233247**

# Institute for Defense Analyses

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September 27, 2019

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**Part I**

**Financial Statements and Schedule of  
Expenditures of Federal Awards  
For the Fiscal Year ended September 27, 2019**



## **Report of Independent Auditors**

To the Board of Trustees Institute for Defense Analyses

### **Report on the Financial Statements**

We have audited the accompanying financial statements of the Institute for Defense Analyses, which comprise the balance sheets as of September 27, 2019 and September 28, 2018, and the related statements of activities and cash flows 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 the financial statements in accordance with accounting principles generally accepted in the United States of America; 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 the financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. 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 our 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, we consider internal control relevant to the Institute for Defense Analyses' 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 Institute for Defense Analyses' 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 of the Institute for Defense Analyses as of September 27, 2019 and September 28, 2018, and the changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

### ***Emphasis of Matter***

As discussed in Note 13 to the financial statements, the Institute changed the manner in which it presents certain aspects of its financial statements as a not-for-profit entity in 2019. Our opinion is not modified with respect to this matter.

### ***Other Matters***

#### ***Other Information***

Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The accompanying schedule of expenditures of federal awards for the year ended September 27, 2019 is presented for purposes of additional analysis as required by Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance) and is not a required part of the financial statements. The information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures, in accordance with auditing standards generally accepted in the United States of America. In our opinion, the schedule of expenditures of federal awards is fairly stated, in all material respects, in relation to the financial statements taken as a whole.

### ***Other Reporting Required by Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated December 20, 2019 on our consideration of Institute for Defense Analyses' internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters for the year ended September 27, 2019. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the effectiveness of internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Institute for Defense Analyses' internal control over financial reporting and compliance.

*PricewaterhouseCoopers LLP*

McLean, Virginia  
December 20, 2019

**Institute for Defense Analyses**  
**Balance Sheets**  
**As of September 27, 2019 and September 28, 2018**

	2019	2018
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 6,992,833	\$ 18,587,332
Contract receivables billed, less allowance of \$50,000 for 2019 and 2018	5,697,725	12,033,238
Contract receivables unbilled, less allowance of \$250,000 and \$100,000 for 2019 and 2018, respectively	27,567,188	14,815,030
Prepaid expenses and other current assets	10,783,289	11,096,691
Total current assets	51,041,035	56,532,291
Prepaid ground rent	946,400	982,800
Property, plant and equipment - net	110,975,040	107,124,350
Investments	211,704,974	208,843,952
Project fund investments	13,521,539	-
Total assets	\$ 388,188,988	\$ 373,483,393
<b>Liabilities and Net Assets</b>		
Current liabilities:		
Accounts payable and accrued expenses	\$ 11,535,656	\$ 12,352,157
Accrued salaries	6,891,732	6,623,917
Accrued interest payable	962,240	980,783
Accrued paid time off	11,522,918	11,052,254
Accrued pension and postretirement costs	5,663,723	5,668,976
Bonds payable	3,515,000	3,510,000
Total current liabilities	40,091,269	40,188,087
Long-term liabilities:		
Accrued postretirement benefits costs	3,999,478	3,408,295
Interest rate swap agreements	8,891,029	5,453,703
Notes payable	-	15,000,000
Long-term debt:		
Bonds payable	100,254,336	78,305,000
Less unamortized debt issuance cost	3,162,711	890,663
Total long-term debt	97,091,625	77,414,337
Total liabilities	150,073,401	141,464,422
Net assets without restrictions	238,115,587	232,018,971
Total liabilities and net assets	\$ 388,188,988	\$ 373,483,393

*The accompanying notes are an integral part of these financial statements.*

# Institute for Defense Analyses

## Statements of Activities

For the fiscal years ended September 27, 2019 and September 28, 2018

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	2019	2018
Operating revenue, including fixed fees of \$6,429,134 and \$6,097,063 respectively	<u>\$ 256,263,463</u>	<u>\$ 247,445,206</u>
	<u>256,263,463</u>	<u>247,445,206</u>
Contract expenses:		
Direct salaries and benefits	133,965,572	127,515,589
Other direct costs	50,426,301	54,383,039
Indirect costs	<u>63,309,483</u>	<u>57,603,113</u>
Total contract expenses	<u>247,701,356</u>	<u>239,501,741</u>
Non-contract expenses:		
Salaries and benefits	774,009	534,066
Other costs	2,417,596	2,318,878
Indirect costs	667,799	458,802
Interest	<u>2,657,199</u>	<u>3,093,145</u>
Total non-contract expenses	<u>6,516,603</u>	<u>6,404,891</u>
Total operating expenses	<u>254,217,959</u>	<u>245,906,632</u>
Operating income	<u>2,045,504</u>	<u>1,538,574</u>
Investment and other income:		
Investment income	7,434,548	12,773,751
Unrealized (loss)/gain on swap agreements	(3,437,326)	3,018,088
Miscellaneous income	<u>53,890</u>	<u>94,618</u>
Total investment and other income	<u>4,051,112</u>	<u>15,886,457</u>
Change in net assets	6,096,616	17,425,031
Net assets, beginning of year	<u>232,018,971</u>	<u>214,593,940</u>
Net assets, end of year	<u>\$ 238,115,587</u>	<u>\$ 232,018,971</u>

*The accompanying notes are an integral part of these financial statements.*

# Institute for Defense Analyses

## Statements of Cash Flows

For the fiscal years ended September 27, 2019 and September 28, 2018

	2019	2018
<b>Cash flows from operating activities:</b>		
Change in net assets	\$ 6,096,616	\$ 17,425,031
Adjustments to reconcile change in net assets to net cash and cash equivalents provided by operating activities:		
Loss on disposal of equipment	8,589	8,260
Depreciation and amortization of property, plant, and equipment	6,903,778	6,330,374
Unrealized loss (gain) on investments	802,767	(5,014,985)
Realized gain on investments	(2,661,076)	(3,381,817)
Unrealized loss (gain) on swap agreements	3,437,326	(3,018,088)
Amortization of prepaid ground rent	36,400	36,400
Amortization of bond issuance costs	50,543	62,483
Loss on extinguishment of debt	131,351	-
Increase/(decrease) resulting from changes in assets and liabilities:		
Contract receivables	(6,566,645)	(2,782,993)
Prepaid expenses and other current assets	313,402	(1,359,531)
Accounts payable and accrued expenses	(666,500)	(940,387)
Accrued salaries	267,815	436,740
Accrued interest payable	(18,543)	11,140
Accrued paid time off	470,664	713,540
Accrued pension cost	(5,253)	586,785
Accrued postretirement benefits costs	591,183	130,958
Net cash and cash equivalents provided by operating activities	<u>9,192,417</u>	<u>9,243,910</u>
<b>Cash flows from investing activities:</b>		
Purchases of investments	(8,066,081)	(56,292,674)
Proceeds from sales of investments	7,063,367	51,959,011
Net purchases of project fund investments	(13,521,539)	-
Capital expenditures	(10,763,408)	(5,615,623)
Proceeds from sale of equipment	351	-
Net cash and cash equivalents used in investing activities	<u>(25,287,310)</u>	<u>(9,949,286)</u>
<b>Cash flows from financing activities:</b>		
Payment of debt	(3,510,000)	(3,385,000)
Proceeds from issuance of bonds	27,639,336	-
Extinguishment of debt	(17,175,000)	-
Payment of bond issuance cost	(2,453,942)	-
Net cash and cash equivalents provided by/(used in) financing activities	<u>4,500,394</u>	<u>(3,385,000)</u>
Net (decrease) in cash and cash equivalents	(11,594,499)	(4,090,376)
Cash and cash equivalents at beginning of year	<u>18,587,332</u>	<u>22,677,708</u>
Cash and cash equivalents at end of year	<u>\$ 6,992,833</u>	<u>\$ 18,587,332</u>
<b>Supplemental disclosure of cash flow information:</b>		
Interest paid	\$ 3,443,121	\$ 3,146,777
Capital expenditures in accounts payable	\$ 3,394,120	\$ 6,028,684

*The accompanying notes are an integral part of these financial statements.*



# Institute for Defense Analyses

## Notes to Financial Statements

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### 1. Description of business and summary of significant accounting policies

#### Description of business

The Institute for Defense Analyses (the "Institute") is a private not-for-profit corporation which administered three federally-funded research and development centers (FFRDC) during the fiscal years ended September 27, 2019 and September 28, 2019. The Institute's largest FFRDC is for the Office of the Secretary of Defense, the second for the National Security Agency and the third for the White House Office of Science and Technology Policy.

#### Reporting year

The Institute's fiscal year is the 52- or 53-week annual accounting period ending the last Friday in September. The Institute's current fiscal year ended on September 27, 2019; the prior fiscal year ended on September 28, 2018.

#### Cash equivalents

The Institute classifies readily-convertible liquid investments with maturities of three months or less when purchased as cash equivalents, except that such investments purchased with funds held by external investment managers are classified with investments. Cash equivalents are maintained in an interest-bearing checking account.

#### Prepaid ground rent

In September 1991, the Institute paid the City of San Diego \$1,200,000 for a 55-year ground lease for the Center for Communications Research (CCR) in La Jolla. The Institute is amortizing the ground rent on a straight-line basis over its term of 55 years.

In October 2005, the Institute exercised an option with the City of San Diego under the 1991 lease to allow expansion to 50,000 square feet of building area for the Center for Communications Research building. The \$598,640 cost for the expansion rights is being amortized on a straight-line basis over the remaining years of the original 1991 agreement.

#### Investments

Investments are stated at fair value. The fair value of investments is based on quoted market prices with realized and unrealized gains and losses included in the Statement of Activities.

#### Debt

The Institute used the proceeds from the sale of tax-exempt bonds to finance construction of two office buildings, to refinance, renovate and expand the La Jolla, California building and to purchase land adjacent to the Institute's headquarters. One building serves as the Institute's current headquarters in Alexandria, Virginia; the other as an office in Princeton, New Jersey. In August 2019, the Institute issued additional tax-exempt bonds through the Industrial Development Authority of the City of Alexandria to construct a new headquarters building located in Alexandria, Virginia. Additional information about the debt is disclosed in note 6.

The Institute uses interest rate swap agreements to effectively fix the interest rates on two of its variable rate bonds. The fair value of the swaps is based on a calculation specified in the agreements and any gain or loss is included in statement of activities.

#### Property, plant and equipment

The Institute carries property, plant and equipment at cost and depreciates them on a straight-line basis over the following estimated useful lives:

Buildings and improvements	5 to 40 years
Office furniture and equipment	5 to 10 years
Computer equipment and software	3 to 5 years

# **Institute for Defense Analyses**

## **Notes to Financial Statements**

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The Institute amortizes leasehold improvements on a straight-line basis over the lesser of the improvement's useful life or the remaining life of the lease. The Institute expenses repairs and maintenance as incurred; it capitalizes betterments which materially extend the lives of related assets. When it sells or retires assets, the Institute removes the related costs and accumulated depreciation from its accounts and includes any gain or loss in operations. The Institute reviews its property and equipment assets for impairment in value whenever events or circumstances indicate that the carrying value may not be recoverable.

### **Capitalization of interest**

Interest costs related to qualifying assets are capitalized during the period which the related assets are constructed and prepared for their intended use.

### **Bond issue costs**

Bond issue costs represent expenses incurred in connection with issuing bonds and are being amortized on a straight-line basis over the terms of the related bond issues.

### **Paid time off**

The Institute accrues paid time off leave as earned. The Institute permits employees to accumulate unused leave subject to certain limitations. The Institute pays employees for unused leave at termination or retirement.

### **Net assets without restrictions**

Net assets represents the accumulated excess of contract revenue and other income over total costs and expenses. Net assets also represents the unrestricted net assets of the Institute in accordance with provisions for "Financial Statements of Not-for-Profit Organizations." The Institute has only unrestricted net assets.

### **Operating revenue**

The Institute performs research primarily for U.S. government agencies. The majority of the Institute's revenue is from cost-plus-fixed-fee (CPFF) contracts with a smaller portion related to fixed price contracts. The Institute recognizes revenue from CPFF contracts on the basis of direct and indirect costs incurred, plus a fixed fee determined as a percentage of cost. Whenever the Institute can determine that a contract will result in a probable loss which it can reasonably estimate, the Institute charges the entire estimated loss against contract revenue.

Contract costs for services provided to the U.S. government, including indirect expenses, are subject to audit and subsequent adjustment by negotiations between the Institute and government representatives. All contract revenues are recorded in amounts that are expected to be realized upon final settlement. Management is of the opinion that adjustments, if any, arising from such audits will not have a material effect on the accompanying financial statements.

### **Income taxes**

Under section 501(c)(3) of the Internal Revenue Code and the laws and regulations of the states of Virginia, Maryland, New Jersey, California, and District of Columbia, the Institute is exempt from taxes on income. The Institute is subject to unrelated business income as a result of parking benefits provided to its employees. The Institute had unrelated business income during the year ended September 27, 2019 of \$222,121 and no unrelated business income during the year ended September 28, 2018.

# Institute for Defense Analyses

## Notes to Financial Statements

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### Management estimates and uncertainties

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent 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 those estimates.

### Concentration of credit risk

The Institute's financial instruments that are exposed to concentrations of credit risk consist primarily of its cash and cash equivalents, investments and accounts receivable. The Institute's excess cash and cash equivalents are deposited in high quality financial institutions. Deposits may be redeemed upon demand and are considered to be a minimal credit risk. Investments are held mainly in the form of high quality publicly traded mutual funds and exchange traded funds. The Institute performs periodic evaluations of these institutions for relative credit standing. The composition and maturities of investments are regularly monitored by management. The Institute limits the amount of credit exposure to any one financial institution or commercial issuer. The accounts receivable are primarily due from U.S. government agencies.

## 2. Contract receivables

Contract receivables at September 27, 2019 and September 28, 2018 consisted of the following:

	2019	2018
Billed receivables	\$ 5,747,725	\$ 12,083,238
Unbilled receivables	<u>27,817,188</u>	<u>14,915,030</u>
	<u>\$33,564,913</u>	<u>\$26,998,268</u>

Most of the Institute's business is with U.S. Government departments and agencies and is subject to government audit. These costs and fees are included in unbilled receivables, as well as any costs recorded after the billing cycle. Cost recorded after the billing cycle is billed in the subsequent period. The government has completed audits for all years through September 29, 2017. Management of the Institute believes that disallowed costs, if any, for the period not yet audited will not have a material adverse impact on the financial statements. A management reserve is maintained for potential losses from certain areas of risk associated with performing contract work with the federal government. The management reserve balance as of September 27, 2019 and September 28, 2018 amounted to \$350,000 and \$250,000 respectively. The Institute has reserved \$50,000 of the management reserve for government audits, which is included in accounts payable in the Balance Sheets.

# Institute for Defense Analyses

## Notes to Financial Statements

### 3. Investments

Investments as of September 27, 2019 and September 28, 2018 are set forth below at cost and fair value by investment type:

	2019		2018	
	Cost	Fair Value	Cost	Fair Value
Long-term investments				
Equity				
Small Cap Growth	\$ 14,324,063	\$ 16,319,452	\$ 13,660,205	\$ 17,484,054
International Fund	28,081,193	31,606,575	26,628,101	31,277,861
Large Cap Growth	41,493,914	75,396,864	38,910,842	73,002,800
Diversifying Strategies	11,719,647	8,557,547	11,719,647	10,128,303
Subtotal - equity	<u>95,618,817</u>	<u>131,880,438</u>	<u>90,918,795</u>	<u>131,893,018</u>
Fixed income				
Money market funds	2,667,771	2,667,488	1,710,149	1,710,144
Certificate of Deposit	-	-	4,400,000	4,400,000
Fixed income - Total Return	75,739,428	77,157,048	73,333,283	70,840,790
Subtotal - fixed income	<u>78,407,199</u>	<u>79,824,536</u>	<u>79,443,432</u>	<u>76,950,934</u>
Total investments	<u>\$ 174,026,016</u>	<u>\$ 211,704,974</u>	<u>\$ 170,362,227</u>	<u>\$ 208,843,952</u>

On August 29, 1997, the Board of Trustees of the Institute resolved to use available funds and future earnings thereon to establish a capital reserve pool. Based upon the intent of the Institute, assets of the capital reserve pool of \$211,704,974 and \$204,443,952 are classified as long-term as of September 27, 2019, and September 28, 2018, respectively. Market values of investments may change for a number of reasons, including changes in prevailing market and interest rates, increases in defaults and credit rating downgrades. See note 4 for further discussion of fair value measurements. Interest and dividends are reinvested into the capital reserve pool. Previously, the Institute held \$4,400,000 in a Certificate of Deposit. These funds were to be used to pay the remaining balance of the 2016 land purchase in Alexandria, Virginia. At the 2019 maturity date, the Institute transferred these funds to cash. See note 5 for further details about the land purchase.

Total net investment gain for the years ended September 27, 2019 and September 28, 2018, respectively, consists of the following:

	2019	2018
Interest and dividends	\$ 5,405,213	\$ 4,336,163
Realized gains and (losses), net	2,661,076	3,381,817
Unrealized gains and (losses), net	(802,767)	5,014,985
Less - investment management expenses	<u>(82,088)</u>	<u>(81,450)</u>
Total net investment gain	<u>\$ 7,181,434</u>	<u>\$ 12,651,515</u>

Total net investment gain is included in investment income on the Statement of Activities.

# Institute for Defense Analyses

## Notes to Financial Statements

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### 4. Fair value measurements

The Institute previously adopted FASB Accounting Standards Codification 820-10 "Fair Value Measurement" (ASC 820-10) which establishes a framework for measuring fair value, establishes a fair value hierarchy based upon the observability of inputs used to measure fair value, and expands disclosures about fair value measurements. Under ASC 820-10, fair value of an investment is the price that would be received to sell an asset or to transfer a liability in an orderly transaction between market participants at the measurement date.

ASC 825-10 gives entities the option, at specific elections dates, to measure certain financial assets and liabilities at fair value. The election may be applied to financial assets and liabilities on an instrument basis, is irrevocable, and may only be applied to entire instruments. Unrealized gains and losses on instruments for which the fair value option has been elected are reported in earnings at each subsequent reporting date. The Institute did not elect fair value accounting for any assets or liabilities that are not currently required to be measured at fair value.

The hierarchy gives the highest priority to investments with readily available quoted prices in an active market and the lowest priority to unobservable inputs which require a higher degree of judgment when measuring fair value. The three categories of the fair value hierarchy are as follows:

**Level 1** – Quoted prices in active markets for identical assets or liabilities as of the measurement date.

**Level 2** - Quoted prices in markets that are not active or other pricing inputs that are either directly or indirectly observable as of the measurement date.

**Level 3** – Prices or valuation techniques in which one or more significant value drivers are unobservable as of the measurement date. The determination of fair value for these financial instruments requires one or more inputs subject to significant management judgment or estimation.

Items not subject to fair value reporting include cash deposits of \$6,992,833 and \$18,587,332 as of September 27, 2019 and September 28, 2018, respectively.

In cases where inputs used to measure fair value fall into different categories within the fair value hierarchy, an investment's level is based on the lowest level of input that is significant to the fair value measurement.

In general, for Level 2 and Level 3 investments, the Institute utilized the investment manager of the asset to provide a valuation estimate based on previously disclosed techniques and processes which have been reviewed by management for propriety and consistency given the asset type and investment strategy. In addition, the Institute may also use established processes for determining the fair value of such securities which reflects the Institute's own assumptions to value the assets as well. Management makes best estimates based on information available. The following estimates and assumptions were used to determine the fair value of each class of financial instrument held by the Institute at September 27, 2019 and September 28, 2018. There have not been any changes to the method used to determine the fair value of the assets and no changes to the level of the assets. The levels associated with the securities are not an indication of the risk associated with investing in those securities.

# Institute for Defense Analyses

## Notes to Financial Statements

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**Investments** – The assets included are funds purchased to provide returns to the Institute's Capital Reserve Pool as well as money market accounts for the debt service reserve fund associated with the Institute's tax-exempt bonds.

**Equities** – Small Cap, International, Large Cap and Natural Resources equity investments include but are not limited to commingled funds that track US and non-US index funds. These funds generally seek results similar to indexes such as the S&P or Russell. These securities are traded in an active market and are priced using available quotes as of the reporting date. They are classified as Level 1.

**Fixed Income** – Total Return include but are not limited to US government and corporate debt securities and commingled funds investing in US government and non-government debt securities. The Institute primarily invests in funds consisting of intermediate term bonds with a moderate risk rating. These assets are traded in an active market and are priced using available quotes as of the reporting date. They are classified as Level 1.

**Certificate of Deposit** – Consist of investments in a certificate of deposit, which are restricted for the 24 month term at a fixed rate of .75%. They are classified as a Level 2.

**Money Market** – Cash equivalent consist of investments in money market accounts, which are actively traded. These are priced by independent market prices in the primary trading market and are classified as Level 2.

**Deferred Compensation Plan Assets** – Retirement funds purchased to provide returns to those employees who are participating in the Institute's deferred compensation plan. The plan is administered and investments are restricted to TIAA (Teachers Insurance and Annuity Association), CREF (College Retirement Equities Fund) and TIAA-CREF. The individual investment is selected by the participant and the value of the investment is available to the employee upon termination.

**TIAA Guaranteed Fixed Annuity** – Valued at contract value which is the amount that would be received at the reporting date if amounts were withdrawn or funds transferred prior to maturity. A participant can only withdraw according to predetermined installment plan. Contract value represents fair value. These assets are classified as Level 3 due to lack of observable transactions of similar investment instruments at or around the balance sheet date.

**Pooled Separate Account** – Valued at quoted price of accumulation units held at year end. Transfers out of this account are limited to once per quarter. These assets have a publicly quoted price but are not publically traded and carry some restrictions with regard to movement in or out of the account and are therefore classified as Level 2.

**CREF Variable Annuities** – These assets include funds that invest in governmental, non-governmental debt securities, stocks and other investments categories that at the quoted price for accumulation units held at the year end. These assets have a publicly quoted price but are not publically traded and carry some restrictions with regard to movement in or out of the account and therefore classified as Level 2,

**TIAA-CREF Retirement Mutual Funds** – These assets include funds that invest in international equity and other investment categories valued at the NAV of shares held at year end. Because these funds are traded on an active exchange and are valued primarily on the basis of market quotations, official closing prices or other basis of information furnished by a pricing service, they are classified as Level 1.

# Institute for Defense Analyses

## Notes to Financial Statements

**Interest Rate Swap Agreements** – The fair value of the interest rate swaps are based on quotes received from the counterparties to the agreements. The Institute does not have access to specific valuation models used by the counterparties; however, the Institute does receive an independent third-party valuation of these agreements. Based on the lack of observable inputs, these agreements are classified as a Level 3.

The following table presents the Institute's assets and liabilities that are measured at fair value by level within the hierarchy as of September 27, 2019:

	Level 1	Level 2	Level 3	Total
<b>Assets:</b>				
Investments				
Equities:				
Small Cap	\$ 16,319,452	\$ -	\$ -	\$ 16,319,452
International	31,606,575	-	-	31,606,575
Large Cap	75,396,864	-	-	75,396,864
Natural Resources	8,557,547	-	-	8,557,547
Fixed Income:				
Total Return	77,157,048	-	-	77,157,048
Certificate of Deposit	-	-	-	-
Money Market	-	2,667,488	-	2,667,488
Subtotal - investments	<u>209,037,486</u>	<u>2,667,488</u>	<u>-</u>	<u>211,704,974</u>
Deferred Compensation Plan Assets				
TIAA Guaranteed Fixed Annuities	-	-	816,506	816,506
Pooled Separate Account:				
Real Estate	-	278,300	-	278,300
CREF Variable Annuities:				
Fixed Income	-	204,122	-	204,122
Equities	-	301,841	-	301,841
Other	-	121,916	-	121,916
TIAA-CREF Retirement Class Mutual Funds:				
Target Date Retirement Funds	1,895,654	-	-	1,895,654
Other	1,278,979	-	-	1,278,979
Subtotal - deferred compensation	<u>3,174,633</u>	<u>906,179</u>	<u>816,506</u>	<u>4,897,318</u>
Total assets at fair value	<u>\$212,212,119</u>	<u>\$ 3,573,667</u>	<u>\$ 816,506</u>	<u>\$216,602,292</u>
<b>Liabilities:</b>				
Interest Rate Swap Agreements	\$ -	\$ -	\$ 8,891,029	\$ 8,891,029
Total liabilities at fair value	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 8,891,029</u>	<u>\$ 8,891,029</u>

# Institute for Defense Analyses

## Notes to Financial Statements

The following table presents the Institute's assets and liabilities that are measured at fair value by level within the hierarchy as of September 28, 2018:

	Level 1	Level 2	Level 3	Total
<b>Assets:</b>				
Investments				
Equities:				
Small Cap	\$ 17,484,054	\$ -	\$ -	\$ 17,484,054
International	31,277,861	-	-	31,277,861
Large Cap	73,002,800	-	-	73,002,800
Natural Resources	10,128,303	-	-	10,128,303
Fixed Income:				
Total Return	70,840,790	-	-	70,840,790
Certificate of Deposit	-	4,400,000	-	4,400,000
Money Market	-	1,710,144	-	1,710,144
Subtotal - investments	<u>202,733,808</u>	<u>6,110,144</u>	<u>-</u>	<u>208,843,952</u>
Deferred Compensation Plan Assets				
TIAA Guaranteed Fixed Annuities	-	-	1,126,780	1,126,780
Pooled Separate Account:				
Real Estate	-	342,037	-	342,037
CREF Variable Annuities:				
Fixed Income	-	142,982	-	142,982
Equities	-	394,534	-	394,534
Other	-	87,424	-	87,424
TIAA-CREF Retirement Class Mutual Funds:				
Target Date Retirement Funds	1,651,636	-	-	1,651,636
Other	1,180,864	-	-	1,180,864
Subtotal - deferred compensation	<u>2,832,500</u>	<u>966,977</u>	<u>1,126,780</u>	<u>4,926,257</u>
Total assets at fair value	<u>\$ 205,566,308</u>	<u>\$ 7,077,121</u>	<u>\$ 1,126,780</u>	<u>\$ 213,770,209</u>
<b>Liabilities:</b>				
Interest Rate Swap Agreements	\$ -	\$ -	\$ 5,453,703	\$ 5,453,703
Total liabilities at fair value	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 5,453,703</u>	<u>\$ 5,453,703</u>



# Institute for Defense Analyses

## Notes to Financial Statements

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The following table is a reconciliation of the Institute's Level 3 assets and liabilities measured at fair value for the fiscal year ended September 27, 2019:

	<u>Guaranteed Fixed Annuities</u>
Beginning Balance	\$ 1,126,780
Interest credited	26,912
Total purchases	26,694
Total sales	(363,880)
Ending Balance	<u>\$ 816,506</u>

	<u>Interest Rate Swaps</u>
Beginning Balance	\$ (5,453,703)
Total unrealized loss	(3,437,326)
Ending Balance	<u>\$ (8,891,029)</u>

Amount of loss recognized on the Statement of Activities

Total unrealized loss	\$ (3,437,326)
Net interest expense	(834,609)

Net interest expense is a result of interest paid of \$1,579,565 and interest received of \$744,956 which is included on the Statement of Activities.

The following table is a reconciliation of the Institute's Level 3 assets and liabilities measured at fair value for the fiscal year ended September 28, 2018:

	<u>Guaranteed Fixed Annuities</u>
Beginning Balance	\$ 825,986
Interest credited	28,659
Total purchases	293,583
Total sales	(21,448)
Ending Balance	<u>\$ 1,126,780</u>

	<u>Interest Rate Swaps</u>
Beginning Balance	\$ (8,471,791)
Total unrealized gain	3,018,088
Ending Balance	<u>\$ (5,453,703)</u>

Amount of gain recognized on the Statement of Activities

Total unrealized gain	\$ 3,018,088
Net interest expense	(1,093,793)

Net interest expense is a result of interest paid of \$1,652,254 and interest received of \$558,461 which is included on the Statement of Activities.

# Institute for Defense Analyses

## Notes to Financial Statements

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### 5. Property, plant and equipment

Property and equipment balances as of September 27, 2019 and September 28, 2018 are summarized as follows:

	2019	2018
Land	\$ 41,341,225	\$ 41,377,394
Buildings and improvements	107,031,670	106,920,835
Construction in progress	9,115,959	1,898,956
Computer software, equipment, and furniture	34,943,191	33,291,363
	<u>192,432,045</u>	<u>183,488,548</u>
Accumulated depreciation and amortization	<u>(81,457,005)</u>	<u>(76,364,198)</u>
Property, plant and equipment - net	<u>\$110,975,040</u>	<u>\$107,124,350</u>

In April 2016, the Institute purchased land in Alexandria, Virginia for future development of the Institute's headquarters facility. The purchase price of the land was \$12,863,512 of which the Institute has paid \$8,515,072. The remaining balance is to be paid upon the construction of the Potomac Yard Metro Station. In 2018, the Institute recognized the remaining purchase price of \$4,348,440, since the Potomac Yard Metro Station construction is likely to occur. The land purchase was originally financed with a seven year variable rate note maturing December 2022 for \$15,000,000. The land purchase has been refinanced with proceeds from the Series 2019 bonds and the variable rate note has been extinguished. Costs associated with the construction of the new headquarters facility were previously included in prepaid expenses on the Balance Sheet. In 2019, the Institute reclassified these costs to construction in progress for both 2019 and 2018.

# Institute for Defense Analyses

## Notes to Financial Statements

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### 6. Debt

Debt as of September 27, 2019 and September 28, 2018, is as follows:

	2019	2018
New Jersey Education Facilities Authority (NJEFA) Variable Rate Revenue Bonds, Series 2000D issued in the original principal amount of \$16,695,000 and a new principal amount of \$11,070,000 in fiscal year 2016 in connection with the construction of an office building in Princeton, New Jersey, November 16, 2000; interest payments are monthly resulting in a weighted average interest rate of .0266; annual principal payments ranging from \$500,500 to \$705,000 beginning October 1, 2016 and ending October 1, 2030.	\$ 7,750,621	\$ 8,286,356
California Statewide Communities Development Authority Variable Rate Revenue Refunding Bonds Series 2000 issued in the original principal amount of \$4,015,000 and a new principal amount of \$2,920,000 in fiscal year 2016 in connection with the refunding of the Center for Communications Research (CCR) La Jolla facility on June 1, 2000; interest payments are monthly resulting in a weighted average interest rate of .0254; annual principal payments ranging from \$108,500 to \$245,000 beginning October 1, 2016 and ending October 1, 2030.	-	2,163,649
California Association of Bay Area Government (ABAG) Authority Variable Rate Revenue Bonds Series 2005 issued in the original principal amount of \$11,945,000 and the new principal amount of \$11,945,000 in fiscal year 2016 to finance the expansion and renovation of the Center for Communication Research (CCR) La Jolla facility on September 1, 2005; interest payments are monthly resulting in a weighted average interest rate of .0266; annual principal payments ranging from \$2,000,000 to \$2,310,000 beginning October 1, 2031 to October 1, 2035.	10,610,728	10,624,204
The Industrial Development Authority of the City of Alexandria Variable Rate Revenue Bonds Series 2015A issued in the original principal amount of \$69,935,000 for purposes of (i) refunding Series 2000B issued in the principal amount of \$26,445,000 in connection with the construction of the Institute's headquarter facility in Alexandria on June 1, 2000 (ii) refunding Series 2005 issued in the original principal amount \$53,925,000 for the purpose of advance refunding of Series 2000A (iii) refunding Series 2006 issued in the original principal amount \$14,875,000 in connection with the acquisition of land at the Institute's headquarters facility in Alexandria on March 1, 2006; interest payments are monthly resulting in a weighted interest rate of .0250; annual principal payments ranging from \$2,663,000 to \$2,840,000 beginning October 1, 2016 and ending October 1, 2035.	\$ 56,918,425	\$ 59,850,128

# Institute for Defense Analyses

## Notes to Financial Statements

	2019	2018
The Industrial Development Authority of the City of Alexandria Variable Rate Revenue Bonds Series 2019 issued in the principal amount of \$249,400,000 in connection with the construction of the Institute's new headquarters facility in Alexandria issued on August 8, 2019 ; interest payments are monthly resulting in a weighted interest rate of .02455; annual principal payments ranging from \$2,870,000 to \$10,000 beginning October 1, 2023 and ending October 1, 2054.	\$ 25,326,851	\$ -
	<u>\$ 100,606,625</u>	<u>\$ 80,924,337</u>

Total debt and unamortized debt issuance cost as of September 27, 2019 and September 28, 2018

	2019			2018		
	Debt	Unamortized Debt Issuance Cost	Debt less Unamortized Issuance Cost	Debt	Unamortized Debt Issuance Cost	Debt less Unamortized Issuance Cost
New Jersey Education Facilities Authority Variable Rate Revenue Bond Series 2000D	\$ 7,865,000	\$ 114,379	\$ 7,750,621	\$ 8,395,000	\$ 108,644	\$ 8,286,356
California Statewide Communities Development Authority Variable Rate Revenue Refunding Bond Series 2000	-	-	-	2,295,000	131,351	2,163,649
California Association of Bay Area Government Authority Variable Rate Revenue Bond Series 2005	10,750,000	139,272	10,610,728	10,750,000	125,796	10,624,204
The Industrial Development Authority of the City of Alexandria Variable Rate Revenue Bond Series 2015A	57,515,000	596,575	56,918,425	60,375,000	524,872	59,850,128
The Industrial Development Authority of the City of Alexandria Variable Rate Revenue Bond Series 2019	27,639,336	2,312,485	25,326,851	-	-	-
	<u>\$103,769,336</u>	<u>\$ 3,162,711</u>	<u>\$100,606,625</u>	<u>\$81,815,000</u>	<u>\$ 890,663</u>	<u>\$ 80,924,337</u>

The Institute's debt is financed with tax-exempt variable rate bonds which are privately held by BB&T Bank. Interest is paid monthly.

In 2019, the Institute issued \$249,400,000 of tax-exempt variable rate bonds to finance the construction of a new headquarters facility. These bonds are structured as a bank drawdown facility. The bond proceeds are made available to the Institute through periodic draws during construction period up to \$249,400,000. As of September 27, 2019, the Institute has recognized debt of \$27,639,336 associated with the Series 2019 bonds, which is reflected on the balance sheet as long-term debt. These bonds are also privately held by BB&T Bank and carry an interest rate of 79% of 1-month Libor plus not more than 1.10%. Interest is calculated and paid monthly on the recognized debt balance. The Institute also used \$2,295,000 of corporate equity to extinguish debt associated with

# Institute for Defense Analyses

## Notes to Financial Statements

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the California Association of Bay Area Government Authority Variable Rate Revenue Bond Series 2005. The Institute recognized a \$131,351 loss associated with unamortized bond issuance cost related to this debt, which is included in interest on the Statement of Activities.

The bonds require that the Institute meet certain financial covenants, including maintaining a debt service coverage ratio of 1.1 to 1.0 and certain other liquidity ratios at the end of each fiscal year. These bonds are uncollateralized as long as the Institute meets the financial covenants. Interest expense related to long-term debt was \$2,807,495 and \$2,691,771 for the years ended September 27, 2019 and September 28, 2018, respectively. In the opinion of management, the Institute was in compliance with all covenants of the bonds as of September 27, 2019 and September 28, 2018.

The annual bond principal payments required are as follows:

<b>Fiscal Year</b>	<b>Total</b>
2020	\$ 3,515,000
2021	3,650,000
2022	3,780,000
2023	3,925,000
2024	6,945,000
Thereafter	303,715,000
	<u>\$ 325,530,000</u>

### 7. Interest rate swap

During the year ending September 30, 2005, the Institute entered into three interest rate swap agreements to effectively fix interest rates on outstanding variable debt. Two of the Swap agreements collectively hedge the cash flow associated with the series 2005A bond. Both agreements are in the amount of \$18,485,000 and carry a fixed rate of 3.475% which the Institute pays. In return, the Institute receives interest based on a variable rate equal to the USD-BMA municipal Swap Index. The agreements are set to expire October 1, 2030.

The third Swap agreement is to hedge \$11,945,000 of the ABAG Series 2005 Bond. The Swap agreement carries a fixed rate of 3.416% which the Institute pays. In return the Institute receives interest based on a variable rate equal to 70% of LIBOR. The agreement is set to expire October 1, 2035.

The Swaps are recognized as Interest Rate Swap Agreements at fair value in the Balance Sheet. The changes in fair value are recorded as unrealized gains or losses in the Statement of Activities. The fair value of the swap agreements was \$(8,891,029) as of September 27, 2019 and \$(5,453,703) as of September 28, 2018. The Swaps resulted in unrealized loss of \$(3,437,326) and an unrealized gain of \$3,018,087 for September 27, 2019 and September 28, 2018, respectively.

# Institute for Defense Analyses

## Notes to Financial Statements

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### 8. Commitments and contingencies

The Institute has several operating leases for the rental of office space with noncancellable remaining terms of more than one year. All operating leases expire by the year 2029.

Minimum annual rental commitments are as follows:

#### Fiscal years

2020	\$ 1,218,097
2021	1,245,492
2022	1,273,581
2023	1,302,225
2024	1,331,471
Thereafter	6,742,360
	<u>\$ 13,113,226</u>

Operating lease rent expense was \$1,219,641 and \$747,148 for the years ended September 27, 2019 and September 28, 2018, respectively.

The Institute maintains a revolving credit agreement maturing on March 10, 2020, that allows borrowings up to \$20,000,000. The agreement is not collateralized; however, so long as the agreement is in effect, the Institute may not encumber its accounts receivables which must remain free and clear of all liens, encumbrances and pledges. Interest accrues on outstanding balances at the Institute's choice of the London Inter-Bank Offered Rate plus the applicable Interest Margin, as defined, or prime rate minus one-half of one percent. The Agreement requires the Institute to maintain a net worth of not less than \$75,000,000 and certain financial ratios. As of September 27, 2019 and September 28, 2018, the Institute had no outstanding borrowings under this agreement. The Institute also has a compensating balance agreement of \$5,000,000.

### 9. Postretirement benefits

#### Defined contribution retirement plan

The Institute maintains a defined contribution retirement plan in which eligible employees participate. Under the Plan, the Institute contributes a fixed percentage of participating employees' eligible compensation to an insurance company or a mutual fund to purchase annuities or mutual fund units of participation. The Plan requires a six-month waiting period for all new employees. Contributions vest fully after two years' service. The Institute funds retirement costs as they accrue. Institute contributions to the Plan were \$14,471,374 and \$13,795,868 for the years ended September 27, 2019 and September 28, 2018, respectively.

#### Other postretirement benefits

The Institute provides limited medical insurance benefits for eligible retirees. Employees with 15 years' service who retire after age sixty-two may continue their medical insurance at group rates until age sixty-five. The Institute accrues the cost of postretirement benefits during each employee's service. It funds postretirement benefits on a pay-as-you-go basis. The measurement date is October 1, 2018.

# Institute for Defense Analyses

## Notes to Financial Statements

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In accordance with provisions of FASB Accounting Standards Codification (ASC) 715-60 and 958-715-25, the Institute recognizes the funded status of a defined benefit postretirement plan on the Balance Sheet. An overfunded plan is recognized as an asset and an underfunded plan is recognized as a liability. The Institute uses the Citigroup Pension Index to determine the discount rate.

The accumulated postretirement benefit obligation for the years ended September 27, 2019 and September 28, 2018 are as follows (in thousands):

	2019	2018
Accumulated postretirement benefit obligation at the beginning of year	\$ 3,609	\$ 3,466
Service cost	253	255
Interest cost	139	116
Plan participants' contribution	16	20
Actuarial gain	254	(161)
Benefits paid	(68)	(87)
Accumulated postretirement benefit obligation at the end of year	<u>\$ 4,203</u>	<u>\$ 3,609</u>

The plan assets for the years ended September 27, 2019 and September 28, 2018 were (in thousands):

	2019	2018
Fair value of plan assets at beginning of year	\$ -	\$ -
Employer contribution	52	67
Plan participants' contribution	16	20
Benefits paid	(68)	(87)
Fair value of plan assets at end of year	<u>\$ -</u>	<u>\$ -</u>

The Institute's policy is to fund postretirement benefits as payments are made.

Funded status of benefit plan as of September 27, 2019 and September 28, 2018 were (in thousands):

	2019	2018
Fair value of plan assets	\$ -	\$ -
Funded status	(4,203)	(3,609)
Unrecognized net actuarial loss	-	-
Unrecognized prior service cost	-	-
Accrued postretirement liability reflected in the accrued postretirement benefits costs	<u>\$ (4,203)</u>	<u>\$ (3,609)</u>

# Institute for Defense Analyses

## Notes to Financial Statements

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The components of the net periodic benefit cost and amounts recognized in net assets without restrictions for the years ended September 27, 2019 and September 28, 2018 were (in thousands):

	2019	2018
Service cost	\$ 253	\$ 255
Interest cost	139	116
Amortization of (gain)	(63)	(57)
Amortization of prior service cost	(12)	(12)
Recognized net actuarial loss	-	-
Net periodic benefit cost	<u>\$ 317</u>	<u>\$ 302</u>

	2019	2018
Prior year unrecognized amounts in unrestricted net assets	\$ (1,425)	\$ (1,332)
Current year unrecognized (gain)	(980)	(1,296)
Current year unrecognized prior service cost/(credit)	(116)	(128)
Current year unrecognized transition obligation	-	-
Total unrecognized current year in unrestricted net assets	<u>\$ (1,096)</u>	<u>\$ (1,424)</u>
Change in unrestricted net assets	\$ 329	\$ (92)

The assumptions used to determine the benefit obligation for 2019 and 2018 are as follows:

	2019	2018
Discount rate - weighted average	3.00%	4.00%
Assumed health care cost trend rate	7.00%	7.00%
Ultimate trend rate	5.0%	5.0%
Year that the rate reaches the ultimate trend rate	2027	2027
Assumed dental cost trend rate	4.00%	4.00%
Ultimate trend rate	4.00%	4.00%
Year that the rate reaches the ultimate trend rate	2019	2018

The assumptions used to determine the net periodic benefit cost for 2019 and 2018 are as follows:

	2019	2018
Discount rate - weighted average	4.00%	3.50%
Assumed health care cost trend rate	7.00%	6.00%
Ultimate trend rate	5.0%	5.0%
Year that the rate reaches the ultimate trend rate	2027	2022
Assumed dental cost trend rate	4.00%	4.00%
Ultimate trend rate	4.00%	4.00%
Year that the rate reaches the ultimate trend rate	2019	2018



# Institute for Defense Analyses

## Notes to Financial Statements

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The assumed medical cost trend rate for next year is 7.0% and the assumed dental trend rate for next year is 4.0%. The pattern of change for each rate is -0.5% per year to 5%, then 5% thereafter.

The ultimate trend rate is expected to be achieved for medical cost in 2027 and for dental cost in 2019. The assumed health care cost trend rates have a significant effect on the amounts reported for health care plans. A one-percent-point increase in the rates would increase the postretirement service plus interest cost by \$65,853 and increase the year-end accumulated postretirement benefit obligation by \$499,744. A one-percent-point decrease in the rates would decrease the postretirement service plus interest cost by \$53,606 and decrease the year-end accumulated postretirement benefit obligation by \$425,350.

Amounts recognized in net assets without restrictions (in thousands):

	2019	2018
Net actuarial (gain)	\$ (980)	\$ (1,296)
Prior service credit	(116)	(128)
Net periodic benefit cost	<u>\$ (1,096)</u>	<u>\$ (1,424)</u>

Estimated amount that will be amortized from net assets without restrictions into net periodic benefit cost in 2020 (in thousands):.

	2020
Actuarial loss/(gain)	\$ (36)
Prior service cost/(credit)	(12)
Total	<u>\$ (48)</u>

### Cash Flows

#### *Contributions*

The Institute expects to contribute approximately \$15,194,942 to its defined contribution retirement plan and to spend approximately \$206,618 on its other postretirement medical benefit plan in 2020.

#### *Estimated Future Postretirement Benefit Payments*

The following benefit payments, which reflect expected future service, as appropriate, are expected to be paid over the next fiscal years ending as of September:

2020	\$ 206,618
2021	183,623
2022	269,756
2023	311,815
2024	320,388
Years 2025-2029	1,780,086

### Deferred compensation

The Institute provides a deferred compensation plan for trustees and certain key employees regulated by Section 457(b) of the Internal Revenue Code. The plan is funded through participant deferrals with no additional contributions from the Institute. Plan assets consist of money market funds and equity securities and are held for the benefit of the participant. Assets are recorded at fair value

# Institute for Defense Analyses

## Notes to Financial Statements

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based upon quoted market prices, and are included in prepaid expenses and other current assets. The related liability is included in accrued pension costs. At September 27, 2019 and September 28, 2018, deferred compensation was \$4,897,318 and \$4,926,257 respectively.

### 10. Functional classification of expenses

Total operating expenses for the years ended September 27, 2019 and September 28, 2018 consist of:

	2019	2018
Research and development		
Program and non-program cost	\$ 190,240,678	\$ 187,846,820
Support costs, principally general and administrative	63,977,281	58,059,812
	<u>\$ 254,217,959</u>	<u>\$ 245,906,632</u>

### 11. Natural classification of expenses

Total operating expenses for the year end September 27, 2019 consist of:

	Program Expenses	Non-Program Expenses	Management and General	Total
Salaries	\$ 110,748,894	\$ 8,889	\$ 27,304,108	\$ 138,061,891
Benefits	42,644,994	765,101	12,072,751	55,482,846
Travel	10,453,563	974,480	1,616,849	13,044,892
Materials	6,042,003	30,769	3,681,868	9,754,640
Consultants/Subcontractors	4,106,425	-	144,432	4,250,857
Facilities	6,284,783	331,100	9,147,370	15,763,253
Services	3,415,159	620,506	7,660,798	11,696,463
Other	696,052	642,655	2,000,200	3,338,907
Insurance	-	-	348,905	348,905
Interest	-	2,475,305	-	2,475,305
	<u>\$ 184,391,873</u>	<u>\$ 5,848,805</u>	<u>\$ 63,977,281</u>	<u>\$ 254,217,959</u>

Program expenses are directly related to the Institute's current contracts. Non-program expenses are ordinary and necessary business expenses which are not allowed to be charged directly or indirectly to a government contract. Management and general administrative expenses are related to both contract and non-contract functions. Benefit costs are allocated as a percentage of salary expense.

# Institute for Defense Analyses

## Notes to Financial Statements

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### 12. Liquidity and availability of financial assets

Financial assets and liquidity resources available within one year to meet cash needs for general operating expenditures consist of cash of \$6,992,833 and accounts receivable of \$33,564,913. The Institute also has an available line of credit of \$20,000,000.

### 13. New Accounting Pronouncements

In 2019, the Institute adopted ASU 2016-14, Presentation of Financial Statements of Not-For-Profit Entities ("ASU 2016-14"). Under the new guidance, changes were made to accounting rules that would enable not-for-profit organizations to better report and explain their financial position and results of operations. The most significant changes for the Institute are to report expenses both by the function and nature and to provide quantitative and qualitative information about the management of liquid resources and availability of financial assets. This information is presented in notes 11 and 12.

In February 2014, the Financial Accounting Standards Board ("FASB") issued ASU No. 2014-09, Revenue from Contracts with Customers ("ASU 2014-09"). ASU 2014-09 supersedes the revenue recognition requirements in Topic 605, "Revenue Recognition" and most industry-specific guidance. The core principle of ASU 2014-09 is that a company will recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the company expects to be entitled in exchange for those goods or services. In July 2015, the FASB deferred the effective date of ASU 2014-09. The new revenue standard is effective for annual periods beginning after December 15, 2018 for non-public entities. Management is currently evaluating the impact of ASU 2014-09 on the Institute's financial statements.

In February 2016, the FASB issued ASU 2016-02, Leases ("ASC 2016-02"). Lessees will need to recognize on their balance sheet a right-of-use asset and a lease liability for virtually all of their leases (other than leases that meet the definition of a short-term lease). The liability will be equal to the present value of lease payments. The asset will be based on the liability, subject to adjustment, such as for initial direct costs. For income statement purposes, the FASB retained a dual model, requiring leases to be classified as either operating or finance. Operating leases will result in straight-line expense (similar to current operating leases) while finance leases will result in a front-loaded expense pattern (similar to current capital leases). The standard is effective for periods beginning after December 15, 2018 for not-for-profit entities. Management is currently evaluating the impact of ASU 2016-02 on the Institute's financial statements.

### 14. Subsequent events

The Institute is not aware of any additional subsequent events or transactions that would affect the financial statements as of September 27, 2019 through the date the financial statements were available to be issued.

**Institute for Defense Analyses**  
**Schedule of Expenditures of Federal**  
**Awards For the fiscal year ended**  
**September 27, 2019**

<u>Federal Grantor/ Program Title</u>	<u>CFDA Number</u>	<u>Contract Number</u>	<u>Pass-through Entity</u>	<u>Pass-through Entity Award number</u>	<u>Federal Expenditures</u>	<u>Pass-through to Subrecipients</u>
<b>RESEARCH AND DEVELOPMENT CLUSTER</b>						
<u>Department of Defense</u>						
Washington Headquarters Service Acquisition Directorate	12.RD	HQ0034-14-D-0001			\$ 155,373,057	\$ 1,149,858
Washington Headquarters Service Acquisition Directorate (Studies & Analyses FFRDC)	12.RD	HQ0034-19-D-0001			21,896,618	255,895
Maryland Procurement Office (Communications & Computing FFRDC)	12.RD	H98230-16-D-0030			68,256,448	-
Johns Hopkins University/Applied Physics Lab	12.RD	152711	Johns Hopkins University	N00024-13-D-6400	237,894	-
IPA-Intergovernmental Personnel Act	12.RD	Various			960,949	-
<b>TOTAL DEPARTMENT OF DEFENSE</b>					<b>246,724,966</b>	<b>1,405,753</b>
<u>Central Intelligence Agency</u>						
MITRE	13.RD	BOA - 53125	MITRE	2009-0917826-000	17,927	-
ODNI (E11)	13.RD	2015-15063000008			667,910	-
<b>TOTAL CENTRAL INTELLIGENCE AGENCY</b>					<b>685,837</b>	<b>-</b>
<u>National Science Foundation</u>						
Office of Science and Technology Policy Institute (Science and Technology Policy Institute FFRDC)	47.RD	OIA-0408601			8,448,277	38,012
<b>TOTAL NATIONAL SCIENCE FOUNDATION</b>					<b>8,448,277</b>	<b>38,012</b>
<u>Department of Energy</u>						
Sandia National Laboratories	81.RD	1920605	Sandia National Laboratories	DE-NA0003525	9,884	-
<b>TOTAL DEPARTMENT OF ENERGY</b>					<b>9,884</b>	<b>-</b>
<b>TOTAL RESEARCH AND DEVELOPMENT CLUSTER</b>					<b>255,868,964</b>	<b>1,443,765</b>
<b>TOTAL EXPENDITURES OF FEDERAL AWARDS</b>					<b>\$ 255,868,964</b>	<b>\$ 1,443,765</b>

The accompanying notes are an integral part of the Schedule of Expenditures of Federal Awards.

**Institute for Defense Analyses**  
**Notes to the Schedule of Expenditures of Federal Awards**  
**For the fiscal year ended September 27, 2019**

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**1. Presentation and Basis of Accounting**

The accompanying Schedule of Expenditures of Federal Awards (the Schedule) for the Institute for Defense Analyses (IDA) has been prepared on the accrual basis of accounting which conforms to accounting principles generally accepted in the United States of America and is consistent with the IDA's basic financial statements. The information in this Schedule is presented in accordance with the requirements of applicable guidance, therefore some amounts presented in the Schedule may differ from amounts presented in, or used in the preparation of, the financial statements.

For purposes of the Schedule, federal awards include all grants, contracts and similar agreements entered directly between IDA and agencies and departments of the federal government and all sub-awards to IDA by non-federal organizations pursuant to federal grants, contracts and similar agreements. For the purpose of the Schedule, expenditures for federal award programs are recognized on the accrual basis of accounting.

Negative numbers in the schedule represent adjustments to amounts previously reported in the normal course of business.

**2. Indirect Cost Rate**

The Institute has negotiated an indirect cost rate with the Defense Contract Management Agency as our cognizant agency for indirect costs. As such, the Institute did not elect to use the 10 percent de minimis indirect cost rate allowed under the Uniform Guidance.

**Part II**  
**Reports on Compliance and Internal Control**



## **Report of Independent Auditors on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with Government Auditing Standards**

To the Board of Trustees Institute for Defense Analyses

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the financial statements of the Institute for Defense Analyses, which comprise the balance sheet as of September 27, 2019, and the related statements of activities and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated December 20, 2019, which includes an emphasis of matter paragraph as the Institute changed the manner in which it presents certain aspects of its financial statements as a not-for-profit entity in 2019.

### **Internal Control over Financial Reporting**

In planning and performing our audit of the financial statements, we considered the Institute for Defense Analyses' internal control over financial reporting ("internal control") to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Institute for Defense Analyses' internal control. Accordingly, we do not express an opinion on the effectiveness of the Institute for Defense Analyses' internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

### **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the Institute for Defense Analyses' financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an



opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

#### **Purpose of this Report**

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

*PricewaterhouseCoopers LLP*

McLean, Virginia  
December 20, 2019





**Report of Independent Auditors on Compliance with Requirements  
That Could Have a Direct and Material Effect on Each Major Program and on Internal Control  
Over Compliance in Accordance with the Uniform Guidance**

To the Board of Trustees  
The Institute for Defense Analyses

**Report on Compliance for Each Major Federal Program**

We have audited the Institute for Defense Analyses' compliance with the types of compliance requirements described in the *OMB Compliance Supplement* that could have a direct and material effect on each of the Institute for Defense Analyses' major federal program for the year ended September 27, 2019. The Institute for Defense Analyses' major federal program is identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

***Management's Responsibility***

Management is responsible for compliance with federal statutes, regulations and the terms and conditions of its federal awards applicable to its federal program.

***Auditors' Responsibility***

Our responsibility is to express an opinion on compliance of the Institute for Defense Analyses' major federal program based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the audit requirements of Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Those standards and the Uniform Guidance require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Institute for Defense Analyses' compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for the major federal program. However, our audit does not provide a legal determination of the Institute for Defense Analyses' compliance.

***Opinion on Each Major Federal Program***

In our opinion, the Institute for Defense Analyses complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on its major federal program for the year ended September 27, 2019.



## Report on Internal Control Over Compliance

Management of the Institute for Defense Analyses is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the Institute for Defense Analyses' internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with the Uniform Guidance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Institute for Defense Analyses' internal control over compliance.

*A deficiency in internal control over compliance* exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A *material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. A *significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of the Uniform Guidance. Accordingly, this report is not suitable for any other purpose.

A handwritten signature in black ink that reads "PricewaterhouseCoopers 22P". The signature is written in a cursive, flowing style.

McLean, Virginia  
July 31, 2020

## **Part III**

### **Findings**

**Institute for Defense Analyses**  
**Schedule of Findings and Questioned Costs**  
**For the fiscal year ended September 27, 2019**

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**Section I – Summary of Auditor’s Results**

*Financial Statements*

Type of auditor’s report issued:

Unmodified

Internal control over financial reporting:

- Material weakness (es) identified? \_\_\_\_\_ yes   x   no
- Significant deficiency (ies) identified that are not considered to be material weaknesses? \_\_\_\_\_ yes   x   none reported
- Noncompliance material to financial statements noted? \_\_\_\_\_ yes   x   no

*Federal Awards*

Internal control over major programs:

- Material weakness (es) identified? \_\_\_\_\_ yes   x   no
- Significant deficiency(ies) identified that are not considered to be material weaknesses? \_\_\_\_\_ yes   x   none reported

Type of auditor’s report issued

Unmodified

on compliance for major programs:

Any audit findings disclosed that are required to be reported in accordance with 2 CFR 200.516(a)? \_\_\_\_\_

yes   x   no

Identification of major programs: CFDA Number(s)	Name of Federal Program or Cluster
Various	Research and Development Cluster
Dollar threshold used to distinguish between type A and type B programs:	\$3,000,000
Auditee qualified as low-risk auditee?	<u>  x  </u> yes <u>      </u> no

**Institute for Defense Analyses**  
**Schedule of Findings and Questioned Costs, Continued**  
**For the fiscal year ended September 27, 2019**

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**Section II – Financial Statement Findings**

No findings to be reported.

**Section III – Federal Award Findings and Questioned Costs**

No findings to be reported.

**Institute for Defense Analyses**  
**Summary Schedule of Prior Audit Findings**  
**For the fiscal year ended September 27, 2019**

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There were no prior audit findings which require an update in this report.