

MAY AND STANLEY SMITH CHARITABLE TRUST

FINANCIAL STATEMENTS

December 31, 2016 and 2015

MAY AND STANLEY SMITH CHARITABLE TRUST

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INDEPENDENT AUDITORS' REPORT

To the Trustees
May and Stanley Smith Charitable Trust

We have audited the accompanying financial statements of May and Stanley Smith Charitable Trust, which comprise the statements of financial position as of December 31, 2016 and 2015, and the related statements of activities and changes in net assets, 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 these 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 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 audits 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 auditors consider 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 of May and Stanley Smith Charitable Trust as of December 31, 2016 and 2015, and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

BPM LLP

San Francisco, California
June 8, 2017

MAY AND STANLEY SMITH CHARITABLE TRUST

STATEMENTS OF FINANCIAL POSITION

December 31, 2016 and 2015

| | <u>2016</u> | <u>2015</u> |
|--|-----------------------------|-----------------------------|
| ASSETS | | |
| Cash and cash equivalents | \$ 457,890 | \$ 380,081 |
| Investments | 398,808,771 | 407,882,906 |
| Dividends and interest receivable | 546,896 | 486,872 |
| Prepaid other tax | 4,956 | 22,307 |
| Contribution receivable from May Smith Trust | - | 660,000 |
| | <u> </u> | <u> </u> |
| Total assets | <u>\$ 399,818,513</u> | <u>\$ 409,432,166</u> |
| LIABILITIES AND NET ASSETS | | |
| Liabilities: | | |
| Grants payable | \$ 7,107,000 | \$ 4,882,000 |
| Accounts payable | 509,412 | 511,433 |
| Federal excise taxes payable | 32,175 | 2,705 |
| | <u> </u> | <u> </u> |
| Total liabilities | 7,648,587 | 5,396,138 |
| Net assets - unrestricted | <u>392,169,926</u> | <u>404,036,028</u> |
| | <u> </u> | <u> </u> |
| Total liabilities and net assets | <u>\$ 399,818,513</u> | <u>\$ 409,432,166</u> |

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

MAY AND STANLEY SMITH CHARITABLE TRUST
STATEMENTS OF ACTIVITIES AND CHANGES IN NET ASSETS

For the years ended December 31, 2016 and 2015

| | 2016 | 2015 |
|---|----------------|-----------------|
| Net investment income: | | |
| Net realized and unrealized gains (losses) on investments | \$ 3,663,729 | \$ (20,305,349) |
| Dividends | 10,348,441 | 9,990,325 |
| Interest, capital gains, and other income | 604,406 | 1,272,366 |
| Custodial and investment related expenses | (3,598,180) | (2,896,961) |
| Net investment income (loss) before federal excise tax | 11,018,396 | (11,939,619) |
| Federal excise and other taxes | (556,782) | (485,205) |
| Net investment income (loss) | 10,461,614 | (12,424,824) |
| Support: | | |
| Change in value of May Smith Trust | 68,502 | (420,382) |
| Net investment income (loss) and support | 10,530,116 | (12,845,206) |
| Expenses: | | |
| Grants | 20,625,054 | 17,952,626 |
| Grants administration | 1,771,164 | 1,484,606 |
| Total expenses | 22,396,218 | 19,437,232 |
| Change in net assets | (11,866,102) | (32,282,438) |
| Net assets - unrestricted, beginning of year | 404,036,028 | 436,318,466 |
| Net assets - unrestricted, end of year | \$ 392,169,926 | \$ 404,036,028 |

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

MAY AND STANLEY SMITH CHARITABLE TRUST

STATEMENTS OF CASH FLOWS

For the years ended December 31, 2016 and 2015

| | 2016 | 2015 |
|---|-----------------|-----------------|
| Cash flows from operating activities: | | |
| Change in net assets | \$ (11,866,102) | \$ (32,282,438) |
| Adjustments to reconcile change in net assets to net cash used in operating activities: | | |
| Net realized and unrealized (gains) losses on investments | (3,663,729) | 20,305,349 |
| Net (increase) decrease in value of contribution receivable from the May Smith Trust | (68,502) | 420,382 |
| Changes in operating assets and liabilities: | | |
| Dividends and interest receivable | (60,024) | 261,526 |
| Prepaid other tax | 17,351 | (3,303) |
| Grants payable | 2,225,000 | (380,500) |
| Accounts payable | (2,021) | (40,641) |
| Federal excise taxes payable | 29,470 | (20,740) |
| Contribution receivable from May Smith Trust | 728,502 | 3,644,618 |
| Net cash used in operating activities | (12,660,055) | (8,095,747) |
| Cash flows from investing activities: | | |
| Purchase of investments | (119,109,941) | (266,820,463) |
| Proceeds from sale of investments | 131,847,805 | 275,050,254 |
| Net cash provided by investing activities | 12,737,864 | 8,229,791 |
| Increase in cash and cash equivalents | 77,809 | 134,044 |
| Cash and cash equivalents, beginning of year | 380,081 | 246,037 |
| Cash and cash equivalents, end of year | \$ 457,890 | \$ 380,081 |
| Supplemental disclosures of cash flow information: | | |
| Federal excise and other taxes paid | \$ 509,961 | \$ 517,818 |

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

MAY AND STANLEY SMITH CHARITABLE TRUST

NOTES TO FINANCIAL STATEMENTS

December 31, 2016 and 2015

1. Organization

The May and Stanley Smith Charitable Trust (the “Trust”) was established in 1989 to provide grants to organizations that serve the needs of children, the elderly, the disabled and the disadvantaged. The Trust makes grants primarily to organizations serving people in the Western Region of the United States and in British Columbia, Canada. A small number of grants are made to organizations in the Bahamas, the United Kingdom, Hong Kong and Australia. The Trust has been classified by the Internal Revenue Service (“IRS”) as a private foundation, as defined in Section 509(a) of the Internal Revenue Code (“IRC”). The Trust has been recognized by the IRS as a foreign organization for purposes of IRC Section 4948. For the years ended December 31, 2016 and 2015, the Trust complied with the IRS requirement to spend or distribute for charitable purposes a minimum of five percent of the average fair value of its investment assets for the preceding year. The trustees may distribute principal or income, or both, for the purposes defined in the Trust agreement. The Trust is supported through investment income and contributions.

2. Summary of Significant Accounting Policies

Basis of Accounting

The accompanying financial statements have been prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America (“U.S. GAAP”).

Use of Estimates

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

Cash and Cash Equivalents

The Trust considers all highly liquid investments with a maturity of three months or less when purchased to be cash equivalents.

Concentration of Credit Risk

The Trust maintains cash balances with multiple banks under a bank deposit program. Cash balances are insured by the Federal Deposit Insurance Corporation up to \$250,000 per insured bank. Cash and investment balances are insured through the Securities Investor Protection Corporation up to \$500,000 and by Lloyd’s of London up to \$900,000. Cash and investment balances may at times exceed these limits. To date, the Trust has not experienced any losses in these accounts.

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MAY AND STANLEY SMITH CHARITABLE TRUST

NOTES TO FINANCIAL STATEMENTS

December 31, 2016 and 2015

2. Summary of Significant Accounting Policies, continued

Investments

Investments are stated at quoted market prices or estimated fair values. Gains or losses that result from market fluctuations are recognized in the period such fluctuations occur. Realized gains or losses that result from sales or maturities of investments are calculated on an adjusted cost basis. Dividend and interest income are accrued when earned.

Fair Value Measurement

Fair value is determined based on 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.

Receivables and liabilities are measured at carrying value which approximated fair value due to their short maturity.

Covered Calls

The use of call options is a part of the Trust's investment strategy. Covered calls are recorded at fair value and generally expire within one to three months from the original dates. Cash flows from covered calls are classified as an investing activity on the statement of cash flows.

Grants

Grants are expensed when the unconditional promise to give is approved by the Board of Trustees.

Income Taxes

The Trust is a private foundation and is exempt from federal income taxes under Section 501(c)(3) of the IRC and from the California franchise and/or income taxes under Section 23701(d) of the California Revenue and Taxation Code. The Trust maintains its accounts and files its tax returns using the accrual method of accounting.

The Trust, a private foundation, has been recognized by the IRS as a foreign organization for purposes of IRC Section 4948 and as such is subject only to a federal excise tax of 4% on its gross U.S. sourced interest and dividends. All excise taxes are considered to be current taxes and no deferred taxes are necessary.

Continued

MAY AND STANLEY SMITH CHARITABLE TRUST

NOTES TO FINANCIAL STATEMENTS

December 31, 2016 and 2015

2. Summary of Significant Accounting Policies, continued

Risks and Uncertainties

The Trust invests in various investment securities. Investment securities are exposed to various risks such as interest rate, market and credit risk. The Trust invests in bond funds whose durations are typically less than 5 years. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect investment values reported in the statements of financial position.

Reclassifications

Certain reclassifications have been made to the 2015 financial statement presentation to correspond to the current year's format. Net assets and changes in net assets are unchanged due to these reclassifications.

3. Fair Value Measurements and Investments

Generally accepted accounting principles establish a hierarchy to prioritize the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The following is a brief description of these three levels:

Level 1 – Quoted prices in active markets for identical assets. Investments in this level have been valued at the closing price on the active market on which the securities are traded at December 31, 2016 and 2015.

Level 2 – Observable inputs other than quoted prices in active markets for identical assets, quoted prices for identical or similar assets in inactive markets, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets. Investments held in this level, including the contribution from the May Smith Trust, have been calculated using the most recent trading activity for identical or similar securities and changes in interest rates.

Level 3 – Inputs that are generally unobservable and typically reflect management's estimates of assumptions that market participants would use in pricing the asset.

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MAY AND STANLEY SMITH CHARITABLE TRUST

NOTES TO FINANCIAL STATEMENTS

December 31, 2016 and 2015

3. Fair Value Measurements and Investments, continued

The following table presents the Trust's assets measured at fair value on a recurring basis as of December 31, 2016:

| December 31, 2016 | Quoted Prices in Active Markets (Level 1) | Total |
|--|--|----------------|
| Investments by fair value level: | | |
| U.S. common stocks: | | |
| Energy | \$ 13,641,101 | \$ 13,641,101 |
| Materials | 5,435,900 | 5,435,900 |
| Industrials | 13,905,705 | 13,905,705 |
| Consumer discretionary | 29,822,094 | 29,822,094 |
| Health care | 47,255,432 | 47,255,432 |
| Financials | 32,969,370 | 32,969,370 |
| Information Technology | 57,740,878 | 57,740,878 |
| Total U.S. common stocks | 200,770,480 | 200,770,480 |
| U.S. preferred stock | 13,172,340 | 13,172,340 |
| International equity funds | 67,673,679 | 67,673,679 |
| Marketable alternatives | 21,707,121 | 21,707,121 |
| Money market funds | 10,050,407 | 10,050,407 |
| Bank deposit program and cash | 2,667,592 | 2,667,592 |
| U.S. fixed income: | | |
| ETF | 8,176,000 | 8,176,000 |
| Mutual funds | 55,038,222 | 55,038,222 |
| Total U.S. fixed income | 63,214,222 | 63,214,222 |
| Liabilities: | | |
| Covered calls | (74,421) | (74,421) |
| Total investments by fair value level | \$ 379,181,420 | 379,181,420 |
| Investments measured at the net asset value ("NAV"): | | |
| Private equity: real estate funds | | 19,627,351 |
| Total investments | | \$ 398,808,771 |

Continued

MAY AND STANLEY SMITH CHARITABLE TRUST

NOTES TO FINANCIAL STATEMENTS

December 31, 2016 and 2015

3. Fair Value Measurements and Investments, continued

The following table presents the Trust's investments measured at fair value on a recurring basis as of December 31, 2015:

| December 31, 2015 | Quoted Prices in Active Markets (Level 1) | Significant Other Observable Inputs (Level 2) | Total |
|--|--|---|----------------|
| Investments by fair value level: | | | |
| U.S. common stocks: | | | |
| Industrials | \$ 28,472,480 | \$ - | \$ 28,472,480 |
| Consumer discretionary | 14,191,888 | - | 14,191,888 |
| Consumer staples | 6,423,489 | - | 6,423,489 |
| Health care | 65,447,446 | - | 65,447,446 |
| Financials | 41,016,096 | - | 41,016,096 |
| Information Technology | 46,760,835 | - | 46,760,835 |
| Total U.S. common stocks | 202,312,234 | - | 202,312,234 |
| U.S. preferred stock | 13,752,900 | - | 13,752,900 |
| International equity funds | 73,796,983 | - | 73,796,983 |
| Marketable alternatives | 19,274,784 | - | 19,274,784 |
| Money market funds | 18,454,641 | - | 18,454,641 |
| U.S. fixed income: | | | |
| ETF | 25,290,944 | - | 25,290,944 |
| Mutual funds | 28,137,081 | - | 28,137,081 |
| Business development companies | 8,725,000 | - | 8,725,000 |
| Total U.S. fixed income | 62,153,025 | - | 62,153,025 |
| Liabilities: | | | |
| Covered calls | (100,695) | - | (100,695) |
| Total investments by fair value level | \$ 389,643,872 | \$ - | 389,643,872 |
| Investments measured at the NAV: | | | |
| Private equity: real estate funds | | | 18,239,034 |
| Total investments | | | \$ 407,882,906 |
| Contribution receivable from May Smith Trust | \$ - | \$ 660,000 | \$ 660,000 |

Continued

MAY AND STANLEY SMITH CHARITABLE TRUST

NOTES TO FINANCIAL STATEMENTS

December 31, 2016 and 2015

3. Fair Value Measurements and Investments, continued

The Trust uses the NAV to determine the fair value of all the underlying investments which do not have readily determinable fair values and prepare their financial statements consistent with the measurement principles of an investment company, or have attributes of an investment company. The following table lists the investment in the real estate fund as of December 31, 2016 and 2015:

December 31, 2016

| <u>Asset</u> | <u>Strategy</u> | <u>NAV in Fund</u> | <u>Number of Funds</u> | <u>Remaining Life</u> | <u>Unfunded Commitments</u> |
|----------------------|-------------------------------------|------------------------|----------------------------|---------------------------|---------------------------------|
| Private equity: | | | | | |
| Real estate fund II | Domestic real estate related assets | \$ 19,676,879 | 1 | 7 years | \$ 6,470,050 |
| Real estate fund III | Domestic real estate related assets | <u>(49,528)</u> | 1 | 9 years | <u>9,962,500</u> |
| | | <u>\$ 19,627,351</u> | | | <u>\$ 16,432,550</u> |

December 31, 2015

| <u>Asset</u> | <u>Strategy</u> | <u>NAV in Fund</u> | <u>Number of Funds</u> | <u>Remaining Life</u> | <u>Unfunded Commitments</u> |
|---------------------|-------------------------------------|------------------------|----------------------------|---------------------------|---------------------------------|
| Private equity: | | | | | |
| Real estate fund II | Domestic real estate related assets | \$ 18,239,033 | 1 | 8 years | \$ 6,822,300 |

As a limited partner in the closed-end real estate funds, the Trust may not withdraw from the real estate funds prior to a fund's dissolution.

4. Covered Calls

The Trust has written covered calls as part of its investment strategy. Included in equity securities as of December 31, 2016 and 2015 were short calls on various securities. The short calls constituted covered calls and entitled the holder to acquire 625,900 and 198,400 shares at various set prices per share for the years 2016 and 2015. The 2016 calls expire on January 20, 2017.

The notional and fair values of the calls as of December 31, 2016 and 2015 are as follows:

| | <u>2016</u> | | <u>2015</u> | |
|---------------|---------------------------|-----------------------|---------------------------|-----------------------|
| | <u>Notional Value</u> | <u>Fair Value</u> | <u>Notional Value</u> | <u>Fair Value</u> |
| Covered calls | \$ (29,809,700) | \$ (74,421) | \$ (28,656,000) | \$ (100,695) |

Continued

MAY AND STANLEY SMITH CHARITABLE TRUST

NOTES TO FINANCIAL STATEMENTS

December 31, 2016 and 2015

4. Covered Calls, continued

All of the Trust's derivative instruments are marked to current value as a change in net assets. The fair values of these instruments are included in investments in equity securities. The Trust recognized \$1,773,080 and \$1,560,734 of net gains related to derivative activity for the years ended December 31, 2016 and 2015, respectively. These net gains are reported as net realized and unrealized gain on investments in the statements of activities.

5. Contribution Receivable

May Smith established the May Smith Trust, a personal trust, on October 10, 1982, to provide for May Smith's support and maintenance during her life and certain charitable gifts and donations after her death. Following her death in July 2006, the May Smith Trust was distributed in accordance with her wishes, and ultimately dissolved in November 2016.

During the years ended December 31, 2016 and 2015, respectively, the Trust received \$747,597 and \$3,644,618 in cash and securities from the May Smith Trust. As of December 31, 2015, the receivable to the Trust from the May Smith Trust was \$660,000.

6. Net Assets

Net assets on the statements of financial position are comprised of original and subsequent capital contributions to the Trust, anticipated contributions, and increases in value through investment activity. Net assets are all considered unrestricted.

Net assets as of December 31, 2016 and 2015 are as follows:

| | <u>2016</u> | <u>2015</u> |
|---|-----------------------|-----------------------|
| Contributed capital | \$ 135,970,395 | \$ 135,970,395 |
| Contributed capital from the May Smith Trust | 65,365,606 | 65,297,104 |
| Contribution receivable from the May Smith Trust | - | 660,000 |
| Net increase in value since inception of the Trust, net of grants and operating expenses | <u>190,833,925</u> | <u>202,108,529</u> |
| Total net assets - unrestricted | <u>\$ 392,169,926</u> | <u>\$ 404,036,028</u> |

Continued

MAY AND STANLEY SMITH CHARITABLE TRUST

NOTES TO FINANCIAL STATEMENTS

December 31, 2016 and 2015

7. Grants Payable

The Trust sometimes approves grants that have a payment or payments in future years, or that are paid when certain future requirements are met by the grantee. Grants authorized but unpaid at year-end are reported as liabilities. Discounting of grants payable over multiple years would be immaterial and is not reflected in the financial statements. The following is a summary of grants authorized and payable:

| | | |
|--------------------------|----|-------------------------|
| Year ending December 31: | | |
| 2017 | \$ | 7,032,000 |
| 2018 | | <u>75,000</u> |
| Total grants payable | \$ | <u><u>7,107,000</u></u> |

8. Net Realized and Unrealized Gains and Losses on Investments

Realized gains and losses from the sale of investments are recognized as the difference between sales proceeds and original cost. Unrealized gains and losses include changes in the fair market value during the year. Gains and losses (realized and unrealized) included in earnings are reported in the statements of activities and changes in net assets as follows for the years ended December 31, 2016 and 2015:

| | <u>2016</u> | <u>2015</u> |
|---|----------------------------|-------------------------------|
| Realized (losses) gains from the sale of investments, net | \$ (10,253,553) | \$ 30,520,043 |
| Unrealized gains (losses) on investments held, net | <u>13,917,282</u> | <u>(50,825,392)</u> |
| Net realized and unrealized gains (losses) on investments | <u><u>\$ 3,663,729</u></u> | <u><u>\$ (20,305,349)</u></u> |

9. Federal Excise and Other Taxes

Federal excise tax expense was calculated at a rate of 4%. The Trust pays foreign taxes on foreign dividends and unrelated business income tax ("UBIT") as applicable. Federal excise and other taxes are included in the statements of activities as follows as of December 31, 2016 and 2015:

| | <u>2016</u> | <u>2015</u> |
|----------------------------------|--------------------------|--------------------------|
| Federal excise and other taxes: | | |
| Current federal excise tax | \$ 351,482 | \$ 336,353 |
| Foreign tax | 200,756 | 139,387 |
| UBIT | <u>4,544</u> | <u>9,465</u> |
| Total federal excise tax benefit | <u><u>\$ 556,782</u></u> | <u><u>\$ 485,205</u></u> |

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MAY AND STANLEY SMITH CHARITABLE TRUST

NOTES TO FINANCIAL STATEMENTS

December 31, 2016 and 2015

10. Tax Payout Requirement

The IRC requires private foundations to annually disburse approximately 5% of the market value of investment assets, less the federal excise tax, for the current year by the end of next year. This payout requirement may be satisfied by payments for grants, program-related investments, direct conduct of charitable activities, and certain administrative expenses. As of December 31, 2016 and 2015, the Trust has met the required minimum distributions, but has undistributed income amounts that must be distributed before the end of the next fiscal year of approximately \$16,600,000 and \$17,866,124 as of December 31, 2016 and 2015, respectively.

11. Related Parties

The Trust Instrument authorizes trustees to use the services of a business or professional firm with which a trustee may be associated, and to compensate the firm for those services. A trustee is the managing member of the company that provides administrative services to the Trust. Fees paid to the administrative services company were \$1,536,870 and \$1,425,000 for the years ended December 31, 2016 and 2015, respectively. There were no fees due to the administrative services company at December 31, 2016 or 2015.

Another trustee is the managing partner of the accounting firm that provides tax return preparation services to the Trust. Expenses related to the accounting firm were \$9,625 and \$9,970 for the years ended December 31, 2016 and 2015, respectively. Fees due to the accounting firm were \$8,100 and \$7,815 at December 31, 2016 and 2015, respectively.

The trustees were paid trustee fees of \$375,000 for the years ended December 31, 2016 and 2015, which are included under custodian and investment related expenses on the statements of activities and changes in net assets.

12. Subsequent Events

The Trust evaluated subsequent events for recognition and disclosure through June 8, 2017, the date which these financial statements were available to be issued. Management concluded that no material subsequent events have occurred since December 31, 2016 that required recognition or disclosure in the financial statements.