

# **The Charles Stark Draper Laboratory, Inc.**

**Report on State Awards in Accordance with State of  
Florida Rules of the Auditor General**

**June 28, 2013**

**The Charles Stark Draper Laboratory, Inc.**  
**Summary of Reports**  
**June 28, 2013**

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**Report Title**

Report of Independent Auditors

Consolidated Financial Statements and Notes to Consolidated Financial Statements

Schedule of Expenditures of State Financial Assistance

Notes to Schedule of Expenditures of State Financial Assistance

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*

Report of Independent Auditors on Compliance with Requirements That Could Have Direct Have a Direct and Material Effect on Each Major State Program and Internal Control Over Compliance in Accordance with Chapter 10.650 of the Rules of the Auditor General, State of Florida

Schedule of Findings and Questioned Costs



## Report of Independent Auditors

To the Board of Directors of  
The Charles Stark Draper Laboratory, Inc.:

We have audited the accompanying financial statements of The Charles Stark Draper Laboratory, Inc. and its subsidiaries (collectively referred to as the "Laboratory"), which comprise the consolidated balance sheets as of June 28, 2013 and June 29, 2012, and the related consolidated statements of activities and changes in net assets and of cash flows for the years then ended, and the related notes to the financial statements.

### ***Management's Responsibility for the Consolidated Financial Statements***

Management is responsible for the preparation and fair presentation of the consolidated 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 consolidated financial statements that are free from material misstatement, whether due to fraud or error.

### ***Auditor's Responsibility***

Our responsibility is to express an opinion on the consolidated financial statements based on our audits. We conducted our audit 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 consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the Company's preparation and fair presentation of the consolidated 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 Company'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 consolidated 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 consolidated financial statements referred to above present fairly, in all material respects, the financial position of The Charles Stark Draper Laboratory, Inc. and its subsidiaries at June 28, 2013 and June 29, 2012, and the results of their operations and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

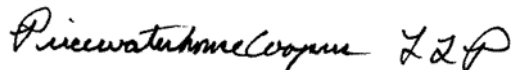
## **Other Matters**

### *Other Information*

Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The accompanying Schedule of Expenditures of State Financial Assistance for the year ended June 29, 2012 is presented for purposes of additional analysis as required by *Florida Single Audit Act*, Audits Nonprofits and For-Profits Organizations, Chapter 10.650, Rules of the Auditor General, and is not a required part of the basic consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated 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 consolidated financial statements as a whole.

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

In accordance with *Government Auditing Standards*, we have also issued our report dated September 20, 2013 on our consideration of the Laboratory's 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 June 28, 2013. The purpose of that report is 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 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 the Laboratory's internal control over financial reporting and compliance.

A handwritten signature in cursive script that reads "PricewaterhouseCoopers LLP".

September 20, 2013, except with respect to Note 2 to Schedule of Expenditures of State Financial Assistance as to which the date is April 29, 2014

**The Charles Stark Draper Laboratory, Inc.**  
**Consolidated Balance Sheets**  
**June 28, 2013 and June 29, 2012**

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	<b>2013</b>	<b>2012</b>
<b>Assets</b>		
Current assets		
Cash and cash equivalents	\$ 52,110,559	\$ 46,898,012
Accounts receivable - net of allowance of \$575,106 and \$573,112 in 2013 and 2012, respectively	39,571,589	32,090,927
Unbilled contract costs and fees, net of allowance of \$700,171 and \$553,879 in 2013 and 2012, respectively	47,147,309	46,829,863
Other current assets	<u>6,775,166</u>	<u>4,917,287</u>
Total current assets	145,604,623	130,736,089
Long-term investments	202,173,270	167,556,950
Deferred charges and other assets	8,380,687	5,555,509
Deferred financing costs, net	539,060	570,461
Prepaid pension benefits	5,405,595	3,581,461
Property and equipment, net	<u>185,751,513</u>	<u>188,845,275</u>
Total assets	<u>\$ 547,854,748</u>	<u>\$ 496,845,745</u>
<b>Liabilities and Net Assets</b>		
Current liabilities		
Accounts payable and accrued contract costs	\$ 35,775,056	\$ 37,135,781
Accrued compensation and related expenses	23,851,302	23,785,366
Other accrued expenses	<u>9,335,085</u>	<u>9,124,728</u>
Total current liabilities	68,961,443	70,045,875
Accrued post retirement benefits	38,943,752	54,472,238
Bonds payable, net	79,240,115	79,182,924
Deferred revenue and other long-term liabilities	<u>26,925,710</u>	<u>11,075,766</u>
Total liabilities	214,071,020	214,776,803
Commitments and contingencies	-	-
Unrestricted net assets	<u>333,783,728</u>	<u>282,068,942</u>
Total liabilities and net assets	<u>\$ 547,854,748</u>	<u>\$ 496,845,745</u>

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

**The Charles Stark Draper Laboratory, Inc.**  
**Consolidated Statements of Activities and Changes in Net Assets**  
**June 28, 2013 and June 29, 2012**

	2013	2012
<b>Operating revenues</b>		
Net Revenue	\$ 526,169,726	\$ 513,478,968
Other income	1,468,727	580,514
Total operating revenues	<u>527,638,453</u>	<u>514,059,482</u>
<b>Operating expenses</b>		
Direct costs		
Subcontracts	216,791,822	212,670,022
Salaries and wages	95,527,375	94,374,344
Employee benefits	27,545,433	26,109,208
Materials, services and rentals	21,473,746	19,622,345
Other, principally travel and equipment	29,204,793	27,171,763
Total direct costs	<u>390,543,169</u>	<u>379,947,682</u>
Indirect costs		
Salaries and wages	58,538,031	55,494,086
Employee benefits and vacations	29,419,543	27,661,677
Materials, services and rentals	16,662,118	15,616,285
Depreciation and amortization	18,479,582	18,371,531
Other	9,498,771	13,628,149
Total indirect costs	<u>132,598,045</u>	<u>130,771,728</u>
Interest expense and fees	<u>4,472,637</u>	<u>4,470,678</u>
Total operating expenses	<u>527,613,851</u>	<u>515,190,088</u>
Increase/(Decrease) in unrestricted net assets from operations	<u>24,602</u>	<u>(1,130,606)</u>
Non-operating gains/(losses)		
Dividend and interest income	2,038,151	1,527,484
Realized and change in net unrealized gains on long-term investments	20,541,273	1,557,850
Other non-operating income, net	7,705,604	8,382,733
Other changes in pension and post retirement benefits	21,405,156	(31,140,970)
Total non-operating gains/(losses), net	<u>51,690,184</u>	<u>(19,672,903)</u>
(Decrease)/increase in unrestricted net assets	51,714,786	(20,803,509)
Unrestricted net assets, beginning of year	<u>282,068,942</u>	<u>302,872,451</u>
Unrestricted net assets, end of year	<u>\$ 333,783,728</u>	<u>\$ 282,068,942</u>

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

**The Charles Stark Draper Laboratory, Inc.**  
**Consolidated Statements of Cash Flows**  
**June 28, 2013 and June 29, 2012**

	<b>2013</b>	<b>2012</b>
<b>Cash flows from operating activities</b>		
Increase/(Decrease) in unrestricted net assets	\$ 51,714,786	\$ (20,803,509)
Adjustments to reconcile change in unrestricted net assets to net cash provided by operating activities		
Depreciation and amortization	18,479,582	18,371,531
Realized and net change in unrealized gains on long-term investments	(20,541,273)	(1,557,850)
Other changes in pension and post retirement benefits	(21,405,156)	31,140,970
(Gain)/loss on disposal of property and equipment	(39,708)	35,440
Other non-cash adjustments	(45,602)	(231,515)
Changes in operating assets and liabilities		
Accounts receivable	(7,480,662)	(4,162,676)
Unbilled contract costs and fees	(317,446)	(133,985)
Other current assets	(1,857,879)	(305,532)
Deferred charges and other assets	(3,462,076)	2,702,915
Accounts payable and accrued contract costs	(1,360,725)	5,035,811
Accrued compensation and related expenses	4,112,360	276,767
Deferred revenue	16,082,690	21,209
Other accrued expenses	453,884	(814,694)
Net cash provided by operating activities	<u>34,332,775</u>	<u>29,574,882</u>
<b>Cash flows from investing activities</b>		
Additions to property and equipment	(15,163,042)	(14,580,514)
Proceeds from sale of property and equipment	42,832	23,194
Purchase of investment securities	(46,894,338)	(37,324,130)
Proceeds from sale of NTV investments	119,113	8,263
Proceeds from sale of investment securities	<u>32,718,016</u>	<u>33,539,205</u>
Net cash used in investing activities	<u>(29,177,419)</u>	<u>(18,333,982)</u>
<b>Cash flows from financing activities</b>		
Change in bond discount	<u>57,191</u>	<u>54,133</u>
Net cash provided by financing activities	<u>57,191</u>	<u>54,133</u>
Net increase in cash and cash equivalents	5,212,547	11,295,033
Cash and cash equivalents, beginning of year	<u>46,898,012</u>	<u>35,602,979</u>
Cash and cash equivalents, end of year	<u>\$ 52,110,559</u>	<u>\$ 46,898,012</u>
<b>Supplemental disclosure of cash flow information</b>		
Interest paid	\$ 4,134,712	\$ 4,219,306
Property and equipment included in accrued costs	333,374	3,486,628

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

# The Charles Stark Draper Laboratory, Inc.

## Notes to Consolidated Financial Statements June 28, 2013 and June 29, 2012

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### 1. Summary of Significant Accounting Policies

#### **Corporate Organization and Purpose**

The Charles Stark Draper Laboratory, Inc. (The Laboratory) is a membership (nonstock), nonprofit Massachusetts Corporation. The Laboratory engages in activities that contribute to the support and advancement of scientific research, technology and development and in educational activities in the sciences and related subjects. The Laboratory's sponsors are primarily agencies of the U.S. Government.

The Laboratory intends to continue to be exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code. In the event of either liquidation or dissolution of the Laboratory, its net assets would be distributed to one or more charitable tax-exempt organizations or governmental agencies.

#### **Fiscal Calendar**

The Laboratory's fiscal calendar (DFY) ends on the Friday closest to June 30<sup>th</sup>. Due to this policy, the fiscal calendar may result in the last day of a fiscal year falling on a date other than on June 30. Approximately every fifth year the Laboratory's fiscal year will contain 53 weeks. There are 52 weeks in fiscal year 2013 and 52 weeks in fiscal year 2012.

#### **Capitalized Software**

Certain costs, as they relate to purchased hardware, software, and implementation activities have been capitalized in accordance with ASC 350-40, *Intangibles – Goodwill and Other – Internal-Use Software*.

#### **Revenue Recognition**

The Laboratory performs research primarily under cost-type contracts for its various sponsors. Under these contracts, reimbursement is received for direct and indirect contract costs plus a fixed or incentive fee. Costs are reimbursed and recognized as revenue as they are incurred. Contract fees are recognized in proportion to costs incurred as the contracts are performed or otherwise as specified in the contract.

Some contracts are long-term, meaning that the projects will continue for one year or more. For long-term contracts, GAAP allows revenue to be recognized on a percentage-of-completion basis if "circumstances are such that total profit can be estimated with reasonable accuracy and ultimate realization is reasonably assured."

Current income recognized under the percentage-of-completion method is based upon (a) the total income projected for the contract at the time of completion and (b) the expenses incurred to date. The percentage-of-completion can be measured using the proportion of costs incurred versus the total estimated cost to complete the contract. The Lab receives advances, performance-based payments from customers that may exceed costs incurred on certain contracts. The Lab classifies advance payments and billings in excess of costs incurred as deferred revenue and other long-term liabilities. Costs incurred in excess of billings as classified as unbilled contract costs and fees, net.

The Laboratory receives royalty payments in accordance with the terms of technology agreements. Royalty payments are recorded as other income in the statements of activities and changes in net assets.

# **The Charles Stark Draper Laboratory, Inc.**

## **Notes to Consolidated Financial Statements June 28, 2013 and June 29, 2012**

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### **Net Assets**

The net assets of the Laboratory primarily consist of the excess of operating revenues over operating expenses since commencement of operations, the changes in gains and losses on investments and other non-operating income. All net assets are unrestricted in nature.

### **Use of Accounting Estimates**

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

### **Deferred Financing Costs**

The costs of securing financing are capitalized and amortized, on the straight-line method, over the life of the associated indebtedness. This method approximates the expense that would have been recognized using the effective interest method.

### **Deferred Charges**

The Laboratory recovers overhead costs associated with U.S. Government-sponsored projects under construction in accordance with Cost Accounting Standards (CAS). As permitted under CAS, overhead costs associated with the development of software systems are recorded as deferred charges and amortized, on the straight-line method, over five years. In 2011 and prior, the Laboratory had elected to recognize the expense of the Supplemental Retirement Plan for Corporate Officers (SRPCO) over 15 years. In 2012, the Laboratory changed SRPCO methodology and expensed the balance of the deferred charges for retired officers. In future years, the Laboratory plans to expense any officer's paid charge in the year of retirement.

### **Property and Equipment**

Depreciation of owned equipment (including data processing equipment and software) is computed on the straight-line method using three- to five-year lives. Leasehold improvements are amortized on the straight-line method over the shorter of the useful lives of the assets or the lease term. Building costs are depreciated on the straight-line method over lives of thirty-nine to forty-two-years.

When assets are retired or otherwise disposed of, the assets and related allowances for depreciation and amortization are eliminated from the accounts and any resulting gain or loss is reflected in the statements of activities and changes in net assets.

In addition to the equipment and buildings acquired by the Laboratory and investments it makes in leasehold improvements, all of which are reflected in the accompanying balance sheets, the Laboratory also uses certain government-furnished equipment for which it is accountable to the U.S. Government.

### **Independent Research**

The Laboratory engages in independent research programs authorized by its Board of Directors. The expenses of such programs are charged to operations as incurred.

**The Charles Stark Draper Laboratory, Inc.**  
**Notes to Consolidated Financial Statements June 28, 2013 and June 29, 2012**

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**Cash and Cash Equivalents**

Cash and cash equivalents consist of amounts on hand and highly liquid investments with maturities of three months or less when purchased. The Laboratory maintains the majority of its cash and cash equivalents at one institution.

**Long-Term Investments**

Investments are primarily in equity securities and mutual funds with readily determinable fair values based on quoted market prices and collective trust funds. The fair value of the collective trust funds are based on net asset value (NAV). Certain investments in debt securities are recorded at amortized cost as it is the Laboratory's intent to hold these investments until maturity. The investment goal for the various portfolios is capital preservation while generating returns sufficient to offset the impact of inflation. Realized gains and losses on investment securities are determined by the specific identification method. Dividends are recorded on the ex-dividend date and interest income is recorded on the accrual basis.

**Prior Year Balance Sheet Reclassification**

In fiscal 2013, certain immaterial reclassifications have been made to the accompanying prior period Consolidated Balance amounts to conform to the current period's presentation.

**New Accounting Pronouncement**

On July 2, 2011, The Laboratory adopted new guidance enhancing the *Fair Value Measurement* standard. This standard requires disclosure on the activity in the Level 3 rollforward to be reported on a gross, rather than net, basis.

2. Long-Term Investments

The Laboratory's long-term investment portfolio consists of the following at June 28, 2013 and June 29, 2012:

	<b>2013</b>	<b>2012</b>
Investment securities		
Cash and money market mutual funds	\$ 2,340,152	\$ 695,488
U.S. investment-grade fixed income funds	43,175,962	59,120,870
U.S. large cap equity holdings	71,821,868	43,215,040
U.S. small cap mutual fund	25,664,182	20,410,088
U.S. Treasury and fixed income holdings	22,055,096	10,042,271
Global equity funds	36,528,798	33,516,075
Insurance contracts and other	280,530	403,537
Total investment securities at fair value	<u>201,866,588</u>	<u>167,403,369</u>
Other investments	<u>306,682</u>	<u>153,581</u>
Total investment securities at amortized cost	<u>306,682</u>	<u>153,581</u>
 Total long-term investments	 <u>\$ 202,173,270</u>	 <u>\$ 167,556,950</u>

**The Charles Stark Draper Laboratory, Inc.**  
**Notes to Consolidated Financial Statements June 28, 2013 and June 29, 2012**

The following tables present information about the assets that are measured at fair value on a recurring basis as of June 28, 2013 and June 29, 2012, and indicate the fair value hierarchy of valuation techniques we utilized to determine such fair value.

	<b>June 28, 2013</b>	<b>Level 1 Assets</b>	<b>Level 2 Assets</b>	<b>Level 3 Assets</b>
Investment securities				
Cash and money market funds	\$ 2,340,152	\$ 2,340,152	\$ -	\$ -
U.S. investment-grade fixed income funds	43,175,962	-	43,175,962	-
U.S. large cap equity holdings	71,821,868	71,821,868	-	-
U.S. small cap mutual fund	25,664,182	-	25,664,182	-
U.S. Treasury and fixed income holdings	22,055,096	-	22,055,096	-
Global equity funds	36,528,798	-	36,528,798	-
Insurance contracts and other	280,530	-	83,508	197,022
	<u>\$ 201,866,588</u>	<u>\$ 74,162,020</u>	<u>\$ 127,507,546</u>	<u>\$ 197,022</u>

	<b>June 29, 2012</b>	<b>Level 1 Assets</b>	<b>Level 2 Assets</b>	<b>Level 3 Assets</b>
Investment securities				
Cash and money market funds	\$ 695,488	\$ 695,488	\$ -	\$ -
U.S. investment-grade fixed income funds	59,120,870	-	59,120,870	-
U.S. large cap equity holdings	43,215,040	43,215,040	-	-
U.S. small cap mutual fund	20,410,088	-	20,410,088	-
U.S. Treasury and fixed income holdings	10,042,271	-	10,042,271	-
Global equity funds	33,516,075	-	33,516,075	-
Insurance contracts and other	403,537	-	73,874	329,663
	<u>\$ 167,403,369</u>	<u>\$ 43,910,528</u>	<u>\$ 123,163,178</u>	<u>\$ 329,663</u>

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. In determining fair value, the use of various valuation approaches, including market, income and cost approaches, is permitted.

A fair value hierarchy has been established based on whether the inputs to valuation techniques are observable or unobservable. Observable inputs reflect market data obtained from sources independent of the reporting entity and unobservable inputs reflect the entities' own assumptions about how market participants would value an asset or liability based on the best information available. Valuation techniques used to measure fair value must maximize the use of observable inputs and minimize the use of unobservable inputs. The standard describes a fair value hierarchy based on three levels of inputs, of which the first two are considered observable and the last unobservable, that may be used to measure fair value.

In general, fair values determined by Level 1 inputs utilize quoted prices (unadjusted) in active markets for identical assets or liabilities. The Laboratory's Level 1 assets consist of equity holdings and money market funds. Fair values determined by Level 2 inputs utilize data points that are observable, such as quoted prices, interest rates and yield curves. The Laboratory's Level 2 assets consist of variable annuities, mutual funds, and a collective trust fund, all of which are recorded at the net asset value (NAV) provided by the investment company.

**The Charles Stark Draper Laboratory, Inc.**  
**Notes to Consolidated Financial Statements June 28, 2013 and June 29, 2012**

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Fair values determined by Level 3 inputs utilize unobservable data points for the asset or liability, and include situations where there is little, if any, observable market activity for the asset or liability. The Laboratory's Level 3 assets as of June 28, 2013 consist of insurance contracts associated with the deferred compensation plan discussed above. There are no liquidity restrictions associated with any of the Laboratory's investments recorded at fair value.

The change in the fair value of the Laboratory's investments with unobservable data points is shown below:

<b>Fair Value Measurements Using Significant Unobservable Inputs (Level 3)</b>		
	<b>Insurance Contracts</b>	<b>Total Investment Securities</b>
<b>June 28, 2013</b>		
Balance at beginning of year	\$ 329,663	\$ 329,663
Transfers to Level 2	-	-
Unrealized appreciation of deferred compensation	(132,641)	(132,641)
Balance at end of year	<u>\$ 197,022</u>	<u>\$ 197,022</u>
	<b>Insurance Contracts</b>	<b>Total Investment Securities</b>
<b>June 29, 2012</b>		
Balance at beginning of year	\$ 281,127	\$ 281,127
Transfers to Level 2	-	-
Unrealized appreciation of deferred compensation	48,536	48,536
Balance at end of year	<u>\$ 329,663</u>	<u>\$ 329,663</u>

There were no unfunded commitments as of June 28, 2013. The Laboratory had no transfers from Level 2 to Level 1 in the current year.

**The Charles Stark Draper Laboratory, Inc.**  
**Notes to Consolidated Financial Statements June 28, 2013 and June 29, 2012**

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3. Property and Equipment

Property and equipment are stated at cost. The following is a summary of property, plant and equipment, at cost less accumulated depreciation at June 28, 2013 and June 29, 2012:

	2013	2012
Data processing equipment	\$ 23,976,671	\$ 23,214,541
Other equipment	110,325,217	107,160,591
Building and leasehold improvements	64,750,533	54,262,973
Building	123,709,047	123,709,047
Land	32,984,487	32,984,487
Construction in progress	938,174	7,013,855
	<u>356,684,129</u>	<u>348,345,494</u>
Less: Accumulated depreciation	<u>170,932,616</u>	<u>159,500,219</u>
Property and equipment, net	<u>\$ 185,751,513</u>	<u>\$ 188,845,275</u>

Depreciation expense was \$18,299,282, and \$18,196,500, for the years ended June 28, 2013 and June 29, 2012, while amortization expense was \$180,300 and \$175,031, for the years ended June 28, 2013 and June 29, 2012, respectively. The Laboratory capitalizes interest cost incurred during the period of construction of capital assets. Interest costs capitalized during the years ended June 28, 2013 and June 29, 2012 were \$301,237, and \$211,870, respectively.

In December 2008, the Laboratory purchased a facility in St. Petersburg, Florida at a total cost of \$7,931,895. Certain costs to fit-out this location, as well as costs incurred to fit-out a leased facility at the University of South Florida in Tampa, Florida were recorded in construction in progress in 2009 and were placed into service in 2010. In addition, the Laboratory entered into a contract with Hillsborough County, Florida, wherein the County has agreed to fund \$976,000 of rent obligations pursuant to a ten year lease with the University of South Florida. The rent subsidies are stipulated to fund the rent obligations due in years 4 and 5 of the rental agreement (see Note 11). This pledge for future benefits has been classified as deferred charges on the balance sheets and will be recognized into revenue during years 4 and 5 of the lease. Fiscal year 2013, includes 12 months of year 5 lease, therefore the Laboratory recognized \$488,000 of this deferred charge.

In December 2012, the Laboratory entered into an agreement with Akamai Technologies to lease the 5th floor of One Hampshire at Kendall Square Condominium. The lease will run through fiscal year 2019. Although the lease commenced in February, construction associated with the remodeling kept the space from being occupied until July 2013 at which time the lease payments will commence. Pursuant to ASC 840-20-25-1 (FASB 13) rental income shall be recognized on a straight-line basis over the term of the lease even though rental payments are not made on a straight-line basis. The Laboratory has agreed to contribute up to \$2,492,749 of Akamai's remodeling costs and so has recorded a liability. Pursuant to ASC 840-20-25-6 and ASC 840-20-25-7 payments made to or on behalf of the lessee are deemed to be lease incentives and shall reduce rental income on a straight line basis over the term of the lease. This amortization began in February 2013. In fiscal year 2013, the Laboratory recognized \$658,882 in rental revenue and \$150,166 in amortized lease incentive, netting to \$508,716. In fiscal year 2019 Akamai has the option to extend the lease an additional 5 years. Also exercisable is an option allowing Akamai to rent an additional 23,500 sq ft; which becomes available in fiscal year 2016.

**The Charles Stark Draper Laboratory, Inc.**  
**Notes to Consolidated Financial Statements June 28, 2013 and June 29, 2012**

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In December 2006, the Laboratory completed an addition to the Hill Building at a total cost of \$64,383,119. The Hill Building and addition together comprise the One Hampshire at Kendall Square Condominium. In total, the Laboratory has leased 77.5% of the space available in the combined Hill Building and addition. The Laboratory occupies the remainder of this space. Rental income, including parking revenue, included within other non-operating income in the statement of activities and changes in net assets was \$8,181,834 and \$8,823,666 for the years ended June 28, 2013 and June 29, 2012, respectively. In addition, the Laboratory incurred \$1,524,699 and \$1,852,212 for its share of common area maintenance costs for the year ended June 28, 2013 and June 29, 2012, respectively. Generally accepted accounting principles require lease income to be recognized on a straight-line basis, which differs from the timing of rental payments in certain of the Laboratory's lease agreements. Revenue recorded in advance of rental payments was \$3,607,073 as of June 28, 2013 and is included in deferred charges and other assets in the accompanying balance sheet. Minimum future rental payments on noncancelable leases to be received as of June 28, 2013 are as follows:

Year	
2014	\$ 6,857,613
2015	5,559,854
2016	5,255,940
2017	5,445,772
2018	5,540,688
Thereafter	36,141,702
	<u>\$ 64,801,569</u>

4. Capital Facilities Allowances and Unreimbursable Expenses

Capital facilities allowances of \$1,843,614 in 2013 and \$3,145,044 in 2012 are included in the statements of activities and changes in net assets.

During 2013 and 2012, certain expenses were either subsidized by the Laboratory or were not reimbursed under the terms of the Laboratory's contracts with its various sponsors. Total unreimbursed expenses included in indirect costs were \$6,693,362 and \$9,639,958 for 2013 and 2012, respectively, and consist principally of otherwise allowable overhead costs as well as unallowable personnel related and administrative expenses and charges incurred in excess of funded contract amounts. Total Laboratory funded projects and cost sharing was approximately \$1,363,000 and \$1,096,000 in 2013 and 2012, respectively.

5. Commitments and Contingencies

The Laboratory leases office space, laboratory facilities and certain equipment. Such leases expire at various dates through the year 2021, with options to extend for additional periods. The office space and laboratory facility lease payments are subject to escalation for increases in real estate taxes and operating expenses. Certain equipment is also rented on a short-term basis and charged to contracts. Total rental expense (exclusive of certain equipment rentals which are charged directly to contracts) was \$1,496,493 and \$1,833,760 in 2013 and 2012, respectively.

Minimum annual rental commitments under such leases (subject to certain escalation provisions) are as follows:

**The Charles Stark Draper Laboratory, Inc.**  
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<b>Year</b>	<b>Building</b>	<b>Equipment</b>	<b>Total</b>
2014	\$ 1,447,315	\$ 118,251	\$ 1,565,566
2015	1,298,007	96,624	1,394,631
2016	1,288,505	96,624	1,385,129
2017	1,362,905	1,696	1,364,601
2018	1,391,271		1,391,271
Thereafter	1,854,962		1,854,962
	<u>\$ 8,642,965</u>	<u>\$ 313,195</u>	<u>\$ 8,956,160</u>

All payments to the Laboratory for work performed on contracts with agencies of the U.S. Government are provisional payments which are subject to adjustment upon audit by the Defense Contract Audit Agency (DCAA). Audits through fiscal year 2012 have been completed and rates have been finalized and recorded through fiscal year 2011.

In 2007, the Laboratory established a liability for environmental cleanup costs associated with soil contamination at a test facility under the requirements of ASC 410-30, *Asset Retirement and Environmental Obligations – Environmental Obligations*. The Laboratory has compiled estimates of the cleanup costs under various scenarios and will update those estimates as conditions change in future periods. Due to the long-term nature of the remediation activities, the Laboratory has discounted the expected future expenditures to the current period, using a rate of 6.80%. At June 28, 2013 the Laboratory's recorded liability was \$2,527,279.

The Laboratory is subject to routine legal proceedings incidental to its business. While the ultimate liability from the proceedings is difficult to determine, in the opinion of management, the results of these proceedings will not have a material adverse effect on the Laboratory's financial position or results of operations.

**The Charles Stark Draper Laboratory, Inc.**  
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6. Pension and Other Post-retirement Benefit Plans

The Laboratory has three defined benefit pension plans and one post-retirement benefit plan providing health care benefits to retired employees. The current period cost of administering these benefit plans is included within operating activities as an indirect cost. The remaining changes to the benefit obligations are recorded in other changes in pension and post retirement benefits as a part of non-operating activities in the statement of activities and change in net assets.

The following schedules provide summary information concerning the Laboratory's benefit plans for the years ended June 28, 2013 and June 29, 2012:

	<b>Pension Benefits</b>		<b>Medical Benefits</b>	
	<b>2013</b>	<b>2012</b>	<b>2013</b>	<b>2012</b>
<b>Benefit obligation at end of year</b>	\$ 137,198,157	\$ 142,531,472	\$ 27,395,930	\$ 30,380,540
<b>Fair value of plan assets at end of year</b>	117,874,170	110,257,239	12,659,762	10,681,996
Unfunded status of the plans	<u>\$ (19,323,987)</u>	<u>\$ (32,274,233)</u>	<u>\$ (14,736,168)</u>	<u>\$ (19,698,544)</u>
<b>Consolidated balance sheets</b>				
Current liabilities	\$ (522,000)	\$ (1,082,000)	\$ -	\$ -
Noncurrent assets	5,405,595	3,581,461	-	-
Noncurrent liabilities	(24,207,582)	(34,773,694)	(14,736,168)	(19,698,544)
Unfunded status of the plans	<u>\$ (19,323,987)</u>	<u>\$ (32,274,233)</u>	<u>\$ (14,736,168)</u>	<u>\$ (19,698,544)</u>
<b>Net period benefit cost</b>	<u>\$ 5,285,099</u>	<u>\$ 1,850,562</u>	<u>\$ 1,613,822</u>	<u>\$ 1,719,287</u>
<b>Amounts not yet reflected in net periodic benefit cost and included in unrestricted net assets:</b>				
Accumulated actuarial loss (gain)	\$ 25,525,059	\$ 41,472,433	\$ (3,368,409)	\$ 1,961,387
Prior service costs (benefits)	79,878	184,935	-	(82,095)
Transition Obligation	735,167	840,191	-	-
	<u>\$ 26,340,104</u>	<u>\$ 42,497,559</u>	<u>\$ (3,368,409)</u>	<u>\$ 1,879,292</u>

The Retirement Plan for Employees (RPE) provides retirement benefits paid from the net assets available for plan benefits. Retirement benefits are paid to participants in equal monthly payments beginning in the month following retirement and continue until death. Payments to a surviving spouse are made at a reduced level. This plan comprises approximately 85% of the Laboratory's pension benefit obligations and plan assets.

The Retirement Plan for Staff Members (RPSM) provides a Surviving Spouse's Benefit, which provides a supplement for married participants who transferred to the Laboratory from the Massachusetts Institute of Technology prior to July 2, 1976, and a Minimum Pension Benefit, which provides a minimum level of retirement benefits based upon years of service and final average salary, through a group annuity; the plan was frozen during 2009. This plan, together with the Supplemental Retirement Plan for Corporate Officers and Retiree Medical Benefit Plan (RMP), comprises the remainder of the Laboratory's benefit obligations and plan assets.

**The Charles Stark Draper Laboratory, Inc.**  
**Notes to Consolidated Financial Statements June 28, 2013 and June 29, 2012**

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The Retiree Medical Benefit Plan provides post-retirement Medicare supplemental health insurance and prescription drug benefits. The Laboratory's contributions to the plan are capped.

**Benefit Obligations**

The components of the change in total benefit obligation and the applicable assumptions for determining benefit obligations are shown below:

	<b>Pension Benefits</b>		<b>Medical Benefits</b>	
	<b>2013</b>	<b>2012</b>	<b>2013</b>	<b>2012</b>
Benefit obligation at beginning of year	\$ 142,531,472	\$ 115,578,329	\$ 30,380,540	\$ 26,801,799
Actuarial loss/(gain)	263,963	657,000	-	528,218
Service cost	2,857,478	1,992,263	1,353,616	1,137,124
Interest cost	4,909,923	5,414,625	1,113,374	1,363,187
Plan participants' contributions	-	-	3,154,931	3,146,209
Change in assumptions	(7,929,372)	22,856,411	(4,448,103)	1,745,023
Benefits paid	(5,435,307)	(3,967,156)	(4,158,428)	(4,341,020)
Benefit obligation at end of year	<u>\$ 137,198,157</u>	<u>\$ 142,531,472</u>	<u>\$ 27,395,930</u>	<u>\$ 30,380,540</u>
Accumulated benefit obligation	<u>\$ 135,505,247</u>	<u>\$ 140,706,092</u>		
<b>Weighted-average assumptions</b>				
Discount rate	4.11%	3.55%	4.35%	3.75%
Rate of compensation increase	3.04%	3.04%	n/a	n/a

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**Notes to Consolidated Financial Statements June 28, 2013 and June 29, 2012**

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**Benefit Cost**

The components of the net periodic benefit cost recognized in the statements of activities and changes in net assets, and the applicable assumptions for determining benefit costs, are shown below:

	<b>Pension Benefits</b>		<b>Medical Benefits</b>	
	<b>2013</b>	<b>2012</b>	<b>2013</b>	<b>2012</b>
Service cost	\$ 2,857,478	\$ 1,992,263	1,353,616	\$ 1,137,124
Interest cost	4,909,923	5,414,625	1,113,374	1,363,187
Expected return on plan assets	(6,713,936)	(6,651,140)	(771,073)	(698,926)
Amortization of prior service cost	105,057	105,057	(82,095)	(82,098)
Amortization of transition obligation	105,024	105,024	-	-
Amortization of net actuarial loss	4,021,553	884,733	-	-
Net periodic benefit cost	<u>\$ 5,285,099</u>	<u>\$ 1,850,562</u>	<u>\$ 1,613,822</u>	<u>\$ 1,719,287</u>
Changes in plan assets and benefit obligations recognized in unrestricted net assets				
Net loss (gain)	\$ (11,925,821)	\$ 29,178,848	\$ (5,329,796)	\$ 2,974,838
Amortizations	(4,231,634)	(1,094,814)	82,095	82,098
Total recognized in unrestricted net assets	<u>\$ (16,157,455)</u>	<u>\$ 28,084,034</u>	<u>\$ (5,247,701)</u>	<u>\$ 3,056,936</u>
Total recognized in net periodic benefit cost and unrestricted net assets	<u>\$ (10,872,356)</u>	<u>\$ 29,934,596</u>	<u>\$ (3,633,879)</u>	<u>\$ 4,776,223</u>
Weighted-average assumptions				
Discount rate	3.55%	4.92%	3.75%	5.25%
Expected long-term return on plan assets	7.00%	7.00%	7.00%	7.00%
Rate of compensation increase	3.08%	3.85%	n/a	n/a

Amortizations of pension benefit prior service costs, transition obligations and actuarial gains and losses in 2014 are expected to be \$73,701, \$105,024, and \$2,351,699, respectively. Amortization of medical gains and losses in 2014 is expected to be \$52,842 .

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**Assumptions**

The discount rate is determined annually based on census information, the timing of future benefit payments and yield curve data from the Mercer Yield Curve as of the valuation date for calculating net periodic benefit cost, and as of year-end for financial statement disclosure.

The expected long-term rate of return assumption represents the expected average rate of return on current and future funds invested to provide for benefit obligations. This assumption is determined based on a number of factors, including historical market index returns, historical plan return data, anticipated long-term asset allocation of the plans and plan expenses. The Laboratory recognizes differences between the expected return on assets and the actual return over the remaining service life of the applicable participants. This amount is included in net periodic pension cost as a component of the amortization of actuarial gains and losses and is expected to be \$2,404,541 in 2014.

Assumed health care cost trend rates at June 28, 2013 and June 29, 2012 were as follows:

	<b>2013</b>	<b>2012</b>
Health care cost trend rate for pre-65 coverage assumed for next year	7.44%	7.62%
Health care cost trend rate for post-65 coverage assumed for next year	7.44%	7.62%
Rate to which the cost trend rate is assumed to decline (the ultimate trend rate)	4.50%	4.50%
Year that the rate reaches the ultimate trend rate	2027	2027

Assumed healthcare costs trend rates can have a significant effect on the amounts reported for health care plans. A one-percentage point change in the assumed health care cost trend rates would have the following effects at June 28, 2013 and June 29, 2012:

	<b>Medical Benefits</b>	
	<b>2013</b>	<b>2012</b>
Impact of 1% increase in assumed health care cost trend rates		
Effect on total of service and interest cost components	\$ 173,146	\$ 146,905
Effect on postretirement benefit obligation	1,012,812	1,201,071
Impact of 1% decrease in assumed health care cost trend rates		
Effect on total of service and interest cost components	(147,085)	(125,599)
Effect on postretirement benefit obligation	(886,573)	(1,047,297)

The Medicare Prescription Drug, Improvement and Modernization Act of 2003 (providing Medicare Part D – Prescription Drug benefits) was reflected in the Laboratory’s accounting results assuming that the Laboratory will continue to provide the same (capped) level of contributions for each participant of the post-retirement medical plan; however any federal subsidy received will be applied to reduce the retiree participants’ share of the cost.

**The Charles Stark Draper Laboratory, Inc.**  
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**Plan Assets**

The components of the change in total plan assets are shown below:

	<b>Pension Benefits</b>		<b>Medical Benefits</b>	
	<b>2013</b>	<b>2012</b>	<b>2013</b>	<b>2012</b>
Fair value of plan assets at beginning of year	\$ 110,257,239	\$ 109,781,693	\$ 10,681,996	\$ 9,984,664
Actual return on plan assets	10,984,166	1,131,841	1,652,766	(2,668)
Employer contributions	750,000	3,457,000	1,328,497	1,894,811
Plan participants' contributions	-	-	3,154,931	3,146,209
Benefits paid	(4,107,417)	(3,967,156)	(4,158,428)	(4,341,020)
Fair value adjustments	(9,818)	(146,139)	-	-
Fair value of plan assets at end of year	<u>\$ 117,874,170</u>	<u>\$ 110,257,239</u>	<u>\$ 12,659,762</u>	<u>\$ 10,681,996</u>

The investment objectives for the assets of the plan are to meet or exceed current and future benefit payments while minimizing employer contributions. Investment policies and strategies governing the assets of the plans are designed to achieve investment objectives within the constraints of a prudent level of portfolio risk and diversification. Risk management practices include the use of investment managers and maintenance of a portfolio diversified by asset class, investment approach and securities holdings, and the maintenance of sufficient liquidity to meet benefit obligations as they come due.

The Laboratory's pension plans weighted-average asset allocations by asset category are as follows:

	<b>RPE</b>			<b>RPSM</b>			<b>Total Pension</b>
	Fair Value	Asset Allocation		Fair Value	Asset Allocation		
		Range	Actual			Range	Actual
<b>June 28, 2013</b>							
U.S. fixed income	\$ 21,905,662	16-30%	22%	\$ -	-	-	\$ 21,905,662
Global equity funds	50,889,094	45-60%	51%	10,175,089	40-60%	53%	61,064,183
U.S. real estate fund	6,674,319	5-10%	7%	-	-	-	6,674,319
Insurance contracts	19,267,414	15-30%	20%	8,962,592	40-60%	47%	28,230,006
	<u>\$ 98,736,489</u>			<u>\$ 19,137,681</u>			<u>\$ 117,874,170</u>
<b>June 29, 2012</b>							
U.S. fixed income	\$ 25,241,303	16-30%	27%	\$ -	-	-	\$ 25,241,303
Global equity funds	42,509,955	45-60%	46%	8,569,146	40-60%	50%	51,079,101
U.S. real estate fund	5,998,281	5-10%	6%	-	-	-	5,998,281
Insurance contracts	19,333,963	15-30%	21%	8,604,591	40-60%	50%	27,938,554
	<u>\$ 93,083,502</u>			<u>\$ 17,173,737</u>			<u>\$ 110,257,239</u>

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The disclosure provisions of ASC 820, *Fair Value Measurements and Disclosure*, were adopted as of fiscal year 2010 for benefit plan assets. The following tables present information about the assets that are measured at fair value on a recurring basis as of June 28, 2013, and indicate the fair value hierarchy of the valuation techniques we utilized to determine such fair value.

	<b>June 28, 2013</b>	<b>Level 1 Assets</b>	<b>Level 2 Assets</b>	<b>Level 3 Assets</b>
Investment securities				
U.S. fixed income	\$ 21,905,662	\$ -	\$ 21,905,662	\$ -
Global equity fund	61,064,183	-	61,064,183	-
U.S. real estate fund	6,674,319	-	6,674,319	-
Insurance contracts	28,230,006	-	-	28,230,006
	<u>\$ 117,874,170</u>	<u>\$ -</u>	<u>\$ 89,644,164</u>	<u>\$ 28,230,006</u>

	<b>June 29, 2012</b>	<b>Level 1 Assets</b>	<b>Level 2 Assets</b>	<b>Level 3 Assets</b>
Investment securities				
U.S. fixed income	\$ 25,241,303	\$ -	\$ 25,241,303	\$ -
Global equity fund	51,079,101	-	51,079,101	-
U.S. real estate fund	5,998,281	-	5,998,281	-
Insurance contracts	27,938,554	-	-	27,938,554
	<u>\$ 110,257,239</u>	<u>\$ -</u>	<u>\$ 82,318,685</u>	<u>\$ 27,938,554</u>

In general, fair values determined by Level 1 inputs utilize quoted prices (unadjusted) in active markets for identical assets and liabilities. Fair values determined by Level 2 inputs utilize data points that are observable, such as quoted prices, interest rates and yield curves. The Laboratory's Level 2 assets consist of variable annuities, all of which are measured at the NAV provided by the investment company.

Fair values determined by Level 3 inputs utilize unobservable data points for the asset or liability, and include situations where there is little, if any, observable market activity for the asset or liability. The Laboratory's Level 3 assets as of June 28, 2013 consist of an insurance contract, the value of which was provided by the insurance company and reviewed for reasonableness by the Laboratory. There are no liquidity restrictions associated with any of the Laboratory's plan assets measured at fair value.

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The change in the fair value of the Laboratory's benefit plan assets with unobservable data points is shown below:

**Fair Value Measurements Using Significant Unobservable Inputs (Level 3)**

	<b>Insurance Contracts</b>
<b>June 28, 2013</b>	
Balance at beginning of year	\$ 27,938,554
Purchases	3,334,443
Total gains	1,064,426
Benefits paid	<u>(4,107,417)</u>
Balance at end of year	<u>\$ 28,230,006</u>
<b>June 29, 2012</b>	
Balance at beginning of year	\$ 23,700,885
Purchases	7,252,762
Total gains	1,268,783
Benefits paid	<u>(4,283,876)</u>
Balance at end of year	<u>\$ 27,938,554</u>

The Laboratory's Retiree Medical Benefit Plan weighted-average asset allocations by asset categories are as follows:

	Fair Value	Asset Allocation	
		Range	Actual
<b>June 28, 2013</b>			
Investment-grade fixed income fund	\$ 2,274,228	12-26%	18%
High-yield bond fund	831,918	3-11%	6%
Domestic equity funds	7,159,879	33-73%	57%
International equity funds	1,782,023	3-24%	14%
Real estate securities fund	<u>611,714</u>	5-11%	5%
	<u>\$ 12,659,762</u>		
<b>June 29, 2012</b>			
Investment-grade fixed income fund	\$ 1,961,009	12-26%	18%
High-yield bond fund	707,128	3-11%	7%
Domestic equity funds	5,806,592	33-73%	54%
International equity funds	1,675,014	3-24%	16%
Real estate securities fund	<u>532,253</u>	5-11%	5%
	<u>\$ 10,681,996</u>		

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All of the Retiree Medical Benefit Plan assets are mutual funds traded in active markets for identical assets (Level 1 assets).

**Contributions and Benefits**

The Laboratory does not anticipate making any contributions to the RPSM in 2014. The Retiree Medical Plan was funded on a “pay as you go” basis in 2012 and 2013. However, the Laboratory anticipates contributing an additional \$435,000 to the plan in 2014 to meet funding requirements calculated under U.S. Government Cost Accounting Standards. The Laboratory does not anticipate making any contributions to the RPE in 2014.

Estimated future benefit payments, which reflect future service as appropriate, are as follows:

	<b>Pension Benefits</b>	<b>Medical Benefits</b>
2014	19,868,000	1,451,636
2015	8,071,000	1,526,999
2016	6,404,000	1,582,580
2017	6,145,000	1,643,630
FY2018	6,183,000	1,719,514
FY2019-FY2023	37,657,000	10,444,285

7. **Deferred Charges and Other Assets**

As permitted under CAS, overhead costs associated with the PeopleSoft software implementation projects are recorded as deferred charges and are being recovered over five years as charges to indirect contract costs. At June 28, 2013 and June 29, 2012, the balance of these costs was \$264,995 and \$381,252, respectively. In fiscal 2012, overhead costs of \$469,234 associated with the Service Procurement Module implementation was recorded as deferred charges. In 2012, the Laboratory changed its accounting methodology for SRPCO expensing the balance of the deferred charges in year the benefit is paid, see Note 1.

8. **Line of Credit**

In 2013 and 2012, the Laboratory did not make any withdrawals or payments under its short-term line of credit arrangements. Currently, the Laboratory has short term lines of credit with Bank of America and BNY Mellon. At June 28, 2013 and June 29, 2012, there were no balances outstanding under the credit facilities. The lines of credit may be renewed annually.

9. **Bonds Payable**

Effective October 23, 2008, the Laboratory issued \$80,000,000, net of a discount of \$970,946, of Massachusetts Development Finance Agency (MDFA) Fixed Rate Demand Revenue Bonds, Draper Laboratory Issue, Series 2008 (the “Series 2008 Bonds”); the Series 2008 Bonds are uncollateralized. The proceeds of the Series 2008 Bonds were used to extinguish the outstanding Series 2000 Bonds as well as provide funding for additional facility and computer upgrades as needed.

The Series 2008 Bonds have no restrictive covenants of a financial nature. The estimated fair value of the Series 2008 Bonds was \$89,989,336 and \$91,645,648 at June 28, 2013 and June 29, 2012, respectively.

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The Series 2008 Bonds have been issued in four groups with varying maturity dates and interest rates, as follows:

Maturity Date	Interest Rate	Maturity Amount
September, 2015	4.75%	\$ 22,500,000
September, 2020	5.50%	10,000,000
September, 2025	5.75%	25,865,000
September, 2030	5.88%	<u>21,635,000</u>
		<u>\$ 80,000,000</u>

The following is a summary of the Laboratory's bonds payable at June 28, 2013 and June 29, 2012:

	2013	2012
Outstanding bonds	\$ 80,000,000	\$ 80,000,000
Less: bond discount	<u>(759,885)</u>	<u>(817,076)</u>
Total bonds payable	<u>\$ 79,240,115</u>	<u>\$ 79,182,924</u>

10. Asset Retirement Obligations

During 2013 and 2012, the Laboratory recognized the following changes to the fair value of its conditional asset retirement obligations:

	2013	2012
Fair value of liability at beginning of year	\$ 6,207,544	\$ 6,018,308
Liabilities settled	(40,544)	(186,908)
Accretion of fair value	<u>387,972</u>	<u>376,144</u>
Fair value of liability at end of year	<u>\$ 6,554,972</u>	<u>\$ 6,207,544</u>

11. Deferred Grant Revenue

The Laboratory entered into an agreement with the Office of Tourism, Trade and Economic Development in the State of Florida on June 30, 2008. The total value of this agreement is approximately \$15,000,000 substantially all of which has been received by the close of 2012. The Laboratory also secured an additional \$15,000,000 in matching awards from various other parties described below. These matching awards will be received in the form of equipment, donated facilities, and rent incentives over the next ten years. These agreements include several provisions that require the initial deferral of revenue as described below.

In 2013 and 2012, the Laboratory received \$0 and \$1,000,000 respectively, from the State of Florida under this arrangement. The terms of the award stipulate that the Laboratory needs to create a specified number of salaried positions, generate a specified level of proposals, and incur costs related to equipment purchases at specified milestone dates during the contract period. Provided that the Laboratory has met the related conditions of the award, revenue will be recognized in proportion to costs incurred under the agreement. If the Laboratory fails to meet its

## **The Charles Stark Draper Laboratory, Inc.**

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stipulated terms at the milestone dates, there may be a risk that future funding under the agreement could be forfeited. The additional funding of \$1,000,000 from the State of Florida is deferred until reaching the target goal of 165 jobs. At June 28, 2013, the Laboratory was not in compliance with its most recent milestones. In 2013, the Laboratory failed to meet its headcount goal pursuant to the terms of agreement with the State of Florida, Pinellas County, and Hillsborough County. Therefore, the Laboratory reserved \$1,000,000 deferred charge for potential clawback. Pinellas County agreed to amend the headcount goal target date for July 2016. Similarly, Hillsborough County and the Laboratory are in early stage discussion for a three year extension. The Laboratory expects a three year extension in place before December 31, 2013. The next milestone date for the State of Florida is September 30, 2013. Accordingly, under this agreement the Laboratory has recorded revenue of \$0 and \$2,310,980 in each of the years ended June 28, 2013 and June 29, 2012 respectively, under this agreement and has deferred approximately \$0 in each of the years ending June 28, 2013 and June 29, 2012, respectively, to be recognized as costs are incurred in future periods.

Pursuant to the terms of an agreement with the Laboratory, Pinellas County, Florida, provided \$2,000,000 to the Laboratory to be used for the purchase of equipment. These funds have been recorded in deferred revenue as of June 26, 2009 and are being amortized into revenue over the equipment's useful life of five years since it was placed into service beginning in 2010. Accordingly, the Laboratory has recorded \$400,000 of revenue under this agreement in each of the years ending June 28, 2013 and June 29, 2012.

Pursuant to the terms of an agreement with the Laboratory, Hillsborough County, Florida, provided \$604,566 and \$685,025 of equipment to the Laboratory in 2013 and 2012, respectively. These funds have been recorded in deferred revenue as of June 28, 2013 and June 29, 2012, respectively and are being recognized as revenue over the equipment's useful life of five years. Accordingly, the Laboratory has recorded \$452,446 and \$317,913 of revenue under this agreement during 2013 and 2012, respectively.

Pursuant to the terms of an agreement with the Laboratory, Hillsborough County, Florida, provided \$161,899 for purchase of leasehold improvements to be capitalized by the Laboratory. These funds have been recorded in deferred revenue as of July 1, 2011 and are being recognized as revenue over the useful life of the leasehold improvements; the Laboratory recorded \$22,574 and \$24,052 of revenue during 2013 and 2012 respectively.

Pursuant to the terms of an agreement with the Laboratory, Florida High Tech Corridor Council provided \$985,873 of equipment to the Laboratory. These funds have been recorded in deferred revenue as of July 2, 2010 and are being amortized into revenue over the equipment's useful life of five years since it was placed into service beginning in 2010. Accordingly, the Laboratory has recorded \$197,175 of revenue under this agreement in each of the years ended June 28, 2013 and June 29, 2012, respectively.

In accordance with the Laboratory's lease with the USF Research Foundation (the Landlord), the Landlord provided \$2,000,000 to the Laboratory to be used for the purchase of leasehold improvements to be capitalized by the Laboratory. These funds have been recorded as deferred revenue at June 26, 2009. The Laboratory recorded \$301,413 and \$110,079 as an offset to depreciation in each of the years ended June 28, 2013 and June 29, 2012.

In addition, the Laboratory entered into a contract with Hillsborough County, Florida, wherein the County has agreed to fund \$976,000 of rent obligations pursuant to a ten year lease with the University of South Florida. The rent subsidies are stipulated to fund the rent obligations due in

**The Charles Stark Draper Laboratory, Inc.**  
**Notes to Consolidated Financial Statements June 28, 2013 and June 29, 2012**

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years 4 and 5 of the rental agreement (see Note 3). This pledge for future benefits has been classified as deferred charges on the balance sheets and will be recognized into revenue during years 4 and 5 of the lease. In fiscal year 2013, year 5 of the lease the Laboratory recognized \$488,000 of this deferred charge.

12. Results of Operations

Total operating revenue is \$527,638,453 in 2013 and \$514,059,482 in 2012. The majority of our revenue is with the U.S. Government and related agencies. A contract change order is included in the operating revenue total. There is a pending change order that totals approximately \$264,230 at the end of fiscal 2013.

Direct expenses are \$390,543,169 in 2013 compared to \$379,947,682 in 2012.

Indirect costs are \$132,598,045 in 2013 and \$130,771,728 in 2012. The increase is due primarily to employee related costs. These costs include merit increases and employee benefit costs.

13. Subsequent Events

The Laboratory has performed an evaluation of subsequent events through September 20, 2013, which is the date the consolidated financial statements were available to be issued.

**The Charles Stark Draper Laboratory, Inc.**  
**Schedule of Expenditures of State Financial Assistance**  
**June 28, 2013**

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<b>State Agency</b>	<b>CSFA Numbers</b>	<b>Contract Number</b>	<b>Direct</b>	<b>Total 2013 Expenditures</b>
State of Florida Executive Office of the Governor	31.054	OT08-166	<u>\$ 1,842,264</u>	<u>\$ 1,842,264</u>
<b>Total Expenditures of State Financial Assistance</b>			<u>\$ 1,842,264</u>	<u>\$ 1,842,264</u>

The accompanying notes are an integral part of the Schedule of Expenditures of State Financial Assistance.

# The Charles Stark Draper Laboratory, Inc.

## Notes to Schedule of Expenditures of State Financial Assistance

### June 28, 2013

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#### 1. Basis of Presentation

The accompanying Schedule of Expenditures of State Financial Assistance (the "Schedule") has been prepared in accordance with the requirements of *Florida Single Audit Act*, Audits Nonprofits and For-Profits Organizations, Chapter 10.650, Rules of the Auditor General using the accrual basis of accounting. The purpose of the Schedule is to present a summary of The Charles Stark Draper Laboratory, Inc.'s (the "Laboratory") research program for the year ended June 29, 2013, which has been funded by the State of Florida ("State Awards"). For purposes of the Schedule, state awards include all state contracts entered into directly between the Laboratory and the State of Florida. Because the Schedule presents only the state award activity of the Laboratory, the Schedule is not intended to, and does not, present either the financial position or changes in net assets of the Laboratory.

#### 2. Description of the Award

The Laboratory entered into an agreement with the Office of Tourism, Trade and Economic Development in the State of Florida on June 30, 2008. The total value of this agreement is approximately \$15,000,000 substantially all of which has been received by the close of 2012. The Laboratory also secured an additional \$15,000,000 in matching awards from various other parties described below. These matching awards will be received in the form of equipment, donated facilities, and rent incentives over the next ten years. These agreements include several provisions that require the initial deferral of revenue as described below.

In 2013 and 2012, the Laboratory received \$0 and \$1,000,000 respectively, from the State of Florida under this arrangement. The terms of the award stipulate that the Laboratory needs to create a specified number of salaried positions, generate a specified level of proposals, and incur costs related to equipment purchases at specified milestone dates during the contract period. Provided that the Laboratory has met the related conditions of the award, revenue will be recognized in proportion to costs incurred under the agreement. If the Laboratory fails to meet its stipulated terms at the milestone dates, there may be a risk that future funding under the agreement could be forfeited. The additional funding of \$1,000,000 from the State of Florida is deferred until reaching the target goal of 165 jobs. At June 28, 2013, the Laboratory was not in compliance with its most recent milestones. In 2013, the Laboratory failed to meet its headcount goal pursuant to the terms of agreement with the State of Florida, Pinellas County, and Hillsborough County. Therefore, the Laboratory reserved \$1,000,000 deferred charge for potential clawback. Pinellas County and Hillsborough County agreed to amend the headcount goal target date for July 2016 and December 2016, respectively. Accordingly, under this agreement the Laboratory has recorded revenue of \$0 and \$2,310,980 in each of the years ended June 28, 2013 and June 29, 2012 respectively, under this agreement and has deferred approximately \$0 in each of the years ending June 28, 2013 and June 29, 2012, respectively, to be recognized as costs are incurred in future periods.



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

To the Board of Directors of  
The Charles Stark Draper Laboratory, Inc.

We have audited the consolidated financial statements of The Charles Stark Draper Laboratory, Inc. and its subsidiaries (the "Laboratory") as of and for the year ended June 28, 2013, and have issued our report thereon dated September 20, 2013. We conducted our audit 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.

**Internal Control over Financial Reporting**

In planning and performing our audit, we considered the Laboratory's internal control over financial reporting as a basis for designing our auditing procedures 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 Laboratory's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Laboratory's internal control over financial reporting.

*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 Laboratory's financial statements are free of 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*

September 20, 2013



**Report of Independent Auditors on Compliance with  
Requirements That Could Have a Direct and Material Effect on Each Major State Program and  
on Internal Control over Compliance in Accordance with Chapter 10.650 of the Rules of the  
Auditor General, State of Florida**

To the Board of Directors of  
The Charles Stark Draper Laboratory, Inc.:

**Compliance**

We have audited the Laboratory's compliance with respect to the compliance requirements of eligibility and matching as described in the Rules of the Auditor General, State of Florida Matrix of Compliance Requirements that could have a direct and material effect on its major state program for the year ended June 28, 2013. The Laboratory's major state program is identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirement of laws, regulations, contracts and grants applicable to each of its major state program is the responsibility of the Laboratory's management. Our responsibility is to express an opinion on the Laboratory's compliance based on our audit.

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 Chapter 10.650 of the Rules of the Auditor General, State of Florida. Those standards and the Chapter 10.650 of the Rules of the Auditor General, State of Florida 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 state program occurred. An audit includes examining, on a test basis, evidence about the Laboratory's 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. Our audit does not provide a legal determination of the Laboratory's compliance with those requirements.

In our opinion, the Laboratory complied, in all material respects, with the compliance requirements applicable to its major state program for the year ended June 28, 2013.

**Internal Control over Compliance**

Management of the Laboratory is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to state programs. In planning and performing our audit, we considered the Laboratory's internal control over compliance with the requirements that could have a direct and material effect on a major state program in order to determine our auditing procedures with respect to the matching and eligibility requirements for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with Chapter 10.650 of the Rules of the Auditor General State of Florida, 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 Laboratory's internal control over compliance.

A deficiency in an entity's internal control over compliance 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 noncompliance with a type of compliance requirement of a state 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 state program will not be prevented or detected and correct on a timely basis.

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 deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

This report is intended solely for the information and use of the Laboratory's Board of Directors, management, and state awarding agencies and is not intended to be and should not be used by anyone other than these specified parties.

*PricewaterhouseCoopers LLP*

April 29, 2014

**The Charles Stark Draper Laboratory, Inc.**  
**Schedule of Findings and Questioned Costs**  
**June 28, 2013**

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**I. Summary of Results**

**Financial Statements**

Type of auditor's report issued Unqualified

Internal control over financial reporting

• Material weakness(es) identified?  yes  no

• Significant deficiency(ies) identified that are not considered to be material weaknesses?  yes  none reported

Noncompliance material to the financial statements noted?  yes  no

**State Awards**

Internal control over major programs

• Material weakness(es) identified?  yes  no

• Significant deficiency(ies) identified that are not considered to be material weaknesses?  yes  none reported

Type of auditor's report issued on compliance for major programs Unmodified

Any audit findings disclosed that are required to be reported in accordance with Chapter 10.650 of the Rules of the Auditor General, State of Florida  Yes  no

**Identification of Major State Program**

CSFA Number  
31.054

Name of State of Florida Program  
Innovation Incentive Program

**The Charles Stark Draper Laboratory, Inc.**  
**Schedule of Findings and Questioned Costs**  
**June 28, 2013**

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**II. Financial Statement Findings**

None noted. In addition, there are no management letter items related to State Financial Assistance.

**III. State Award Findings and Questioned Costs**

None noted.

**IV. Prior Year State Award Findings and Questioned Costs**

None noted.