



**AMERICAN DIABETES ASSOCIATION
RESEARCH FOUNDATION, INC.**

Financial Statements

December 31, 2017

(With Independent Auditors' Report Thereon)



KPMG LLP
1676 International Drive
McLean, VA 22102

Independent Auditors' Report

The Board of Directors
American Diabetes Association
Research Foundation, Inc.:

We have audited the accompanying financial statements of the American Diabetes Association Research Foundation, Inc., which comprise the balance sheet as of December 31, 2017, and the related statements of activities, functional expenses, and cash flows for the year 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 U.S. generally accepted accounting principles; 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 audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

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

Opinion

In our opinion, the financial statements referred to above present fairly in all material respects, the financial position of the American Diabetes Association Research Foundation, Inc. as of December 31, 2017, and the results of its operations and its cash flows for the year then ended, in accordance with U.S. generally accepted accounting principles.



Report on Summarized Comparative Information

We have previously audited the American Diabetes Association Research Foundation, Inc.'s 2016 financial statements, and we expressed an unmodified opinion on those audited financial statements in our report dated May 26, 2017. In our opinion, the summarized comparative information presented herein as of and for the year ended December 31, 2016 is consistent, in all material respects, with the audited financial statements from which it has been derived.

KPMG LLP

McLean, Virginia
May 29, 2018

**AMERICAN DIABETES ASSOCIATION
RESEARCH FOUNDATION, INC.**

Balance Sheet

December 31, 2017

(with comparative information as of December 31, 2016)

Assets	2017	2016
Cash and cash equivalents	\$ 858,474	—
Receivable from the American Diabetes Association (note 3)	63,289,465	54,991,558
Contributions receivable, net (note 5)	417,163	3,760,849
Interest in perpetual trust (note 4)	85,626	81,751
Total assets	\$ 64,650,728	58,834,158
Liabilities and Net Assets		
Research grants payable	\$ 26,897,799	18,987,565
Net assets:		
Unrestricted	5,732,502	—
Temporarily restricted	31,934,801	39,764,842
Permanently restricted	85,626	81,751
Total net assets	37,752,929	39,846,593
Total liabilities and net assets	\$ 64,650,728	58,834,158

See accompanying notes to financial statements.

**AMERICAN DIABETES ASSOCIATION
RESEARCH FOUNDATION, INC.**

Statement of Activities

Year ended December 31, 2017

(with summarized information for the year ended December 31, 2016)

	<u>Unrestricted</u>	<u>Temporarily restricted</u>	<u>Permanently restricted</u>	<u>2017 Total</u>	<u>2016 Total</u>
Revenue:					
Donations, bequests, and change in value of perpetual trusts	\$ 2,737,459	448,500	3,875	3,189,834	2,666,456
Contributed professional services	817,451	—	—	817,451	750,090
Grant from the American Diabetes Association (note 3)	29,669,030	2,268,488	—	31,937,518	34,227,945
Total contributions and grants	33,223,940	2,716,988	3,875	35,944,803	37,644,491
Net assets released from restrictions	10,547,029	(10,547,029)	—	—	—
Total revenue	43,770,969	(7,830,041)	3,875	35,944,803	37,644,491
Expenses:					
Program activities – research:					
Research grants	36,557,070	—	—	36,557,070	32,179,317
Contributed professional services	817,451	—	—	817,451	750,090
Total program activities	37,374,521	—	—	37,374,521	32,929,407
Supporting services:					
Management and general	248,980	—	—	248,980	518,538
Fundraising	414,966	—	—	414,966	864,231
Total supporting services	663,946	—	—	663,946	1,382,769
Total expenses	38,038,467	—	—	38,038,467	34,312,176
Change in net assets	5,732,502	(7,830,041)	3,875	(2,093,664)	3,332,315
Net assets, beginning of year	—	39,764,842	81,751	39,846,593	36,514,278
Net assets, end of year	\$ 5,732,502	31,934,801	85,626	37,752,929	39,846,593

See accompanying notes to financial statements.

**AMERICAN DIABETES ASSOCIATION
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Statement of Functional Expenses

Year ended December 31, 2017

(with summarized information for the year ended December 31, 2016)

	Program activities research	Supporting services		2017 Total	2016 Total
		Management and general	Fundraising		
Research grants	\$ 36,557,070	—	—	36,557,070	32,179,317
American Diabetes Association management fee	—	248,980	414,966	663,946	1,382,769
Contributed professional services	817,451	—	—	817,451	750,090
Total expenses	\$ <u>37,374,521</u>	<u>248,980</u>	<u>414,966</u>	<u>38,038,467</u>	<u>34,312,176</u>

See accompanying notes to financial statements.

**AMERICAN DIABETES ASSOCIATION
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Statement of Cash Flows

Year ended December 31, 2017

(with comparative information for the year ended December 31, 2016)

	2017	2016
Cash flows from operating activities:		
Change in net assets	\$ (2,093,664)	3,332,315
Adjustments to reconcile change in net assets to net cash provided by (used in) operating activities:		
(Increase) decrease in interest in perpetual trust	(3,875)	284
Adjustments for changes in operating assets and liabilities:		
Increase in receivable from the American Diabetes Association	(8,297,907)	(9,542,096)
Decrease in contributions receivable	3,343,686	330,614
Increase in research grants payable	7,910,234	5,507,496
Net cash provided by (used in) operating activities	858,474	(371,387)
Cash and cash equivalents, beginning of year	—	371,387
Cash and cash equivalents, end of year	\$ 858,474	—

See accompanying notes to financial statements.

**AMERICAN DIABETES ASSOCIATION
RESEARCH FOUNDATION, INC**

Notes to Financial Statements

December 31, 2017

(with comparative information as of and for the year ended December 31, 2016)

(1) Organization

The American Diabetes Association (the Association) is a not-for-profit voluntary health agency that works to prevent and cure diabetes and to improve the lives of all people affected by diabetes. In October 1994, the Association's board of directors established the American Diabetes Association Research Foundation, Inc. (the Foundation), as a subsidiary of the Association. The objective of the Foundation is to fund diabetes-related research leading to:

- The prevention and cure of diabetes
- The prevention and cure of the complications of diabetes
- New and improved therapies for individuals affected by diabetes

The Foundation is generally exempt from income taxes under Section 501(c)(3) of the Internal Revenue Code (the Code) and charitable contributions to the Foundation qualify for charitable tax deductions as described in the Code. The Foundation is subject to taxation on any net unrelated business income and has been classified as an organization that is not a private foundation under Section 509(a) of the Code.

The Foundation recognizes the effect of income tax positions only if those positions more likely than not would not be sustained upon examination by the Internal Revenue Service. The Foundation has analyzed the tax positions taken and has concluded that as of December 31, 2017, there are no uncertain tax positions taken or expected to be taken that would require recognition of a liability (or asset) or disclosure in the financial statements.

On December 22, 2017, the president signed into law H.R.1, originally known as the Tax Cuts and Jobs Act, which includes several changes relevant to tax exempt organizations, primarily related to unrelated business income, net operating losses, certain new excise taxes, and changes affecting the deductibility of certain expenses. Management is currently in the process of evaluating the new law and the impact it may have on the Foundation.

The Foundation has been and continues to be dependent on the continued financial support of the Association to operate its core programs. The Association is committed to continue such support as necessary in order for the Foundation to sustain its research activities and to continue as a going concern.

(2) Summary of Significant Accounting Policies

(a) Basis of Accounting

The Foundation prepares its financial statements on an accrual basis in accordance with U.S. generally accepted accounting principles.

The net assets and revenues, gains, and losses of the Foundation are classified for accounting and reporting purposes into three classes of net assets based on the existence or absence of donor-imposed restrictions. A description of the three classes follows:

Permanently Restricted – Net assets subject to donor-imposed stipulations that they be maintained permanently. For the Foundation, this net asset class relates to an interest in a perpetual trust.

**AMERICAN DIABETES ASSOCIATION
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Notes to Financial Statements

December 31, 2017

(with comparative information as of and for the year ended December 31, 2016)

Temporarily Restricted – Net assets subject to donor-imposed stipulations that may or will be met either by actions of the Foundation and/or the passage of time.

Unrestricted – Net assets that are not subject to donor-imposed stipulations.

(b) Cash and Cash Equivalents

Cash and cash equivalents are defined as currency on hand, demand deposits with banks or financial institutions, and financial instruments with original maturities of less than three months.

(c) Fair Value of Financial Instruments

As of December 31, 2017 and 2016, the carrying value of cash and cash equivalents and research grants payable approximated their fair value based on the short-term maturities of these instruments.

(d) Recognition of Revenues

Contributions, including unconditional promises to give, are recognized when received. The research program is the sole program of the Foundation. Therefore, all contributions to the general research program are reported as unrestricted revenues unless further restricted by the donor. Generally, there is no time restriction presumed on unconditional promises to give as it is the practice of the Foundation to spend these contributions on the research program in the same year as received. Temporarily restricted contributions recognized in 2017 are more specifically restricted than the broad research mission of the Foundation.

Unconditional promises to give are reported at their net realizable value. These unconditional promises to give are reported at fair value based on nonrecurring measurements classified as Level 3 (note 4). Unconditional promises to give that are expected to be collected in future years are recorded at the present value of the amounts expected to be collected. The present value discount is calculated using a risk-adjusted rate at the time of the contribution ranging from 1.4% to 1.6%.

(e) Contributed Services

Contributed services are reported in the statement of activities at the fair value of the services received. Contributions of services are recognized if the services received create or enhance nonfinancial assets or if the services require specialized skills and would typically need to be purchased if not provided by donation. Contributed services reported by the Foundation relate to the panel review of research grant applications and are recorded as both contributed professional services revenue and expense on the statement of activities.

(f) Research Grants

Research grants awarded by the Foundation generally extend over a period of one to five years, subject to renewal on an annual basis. The liability and related expense is recorded when the recipient is notified of the annual award amount, and the liability is recorded as research grants payable in the balance sheet.

**AMERICAN DIABETES ASSOCIATION
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December 31, 2017

(with comparative information as of and for the year ended December 31, 2016)

(g) Management Estimates and Uncertainties

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

(h) Comparative Financial Statements

The statements of activities and functional expenses include certain summarized comparative information for the year ended December 31, 2016. Such information does not include sufficient detail to constitute a presentation in conformity with generally accepted accounting principles. Accordingly, such information should be read in conjunction with the Foundation's financial statements for the year ended December 31, 2016, from which the summarized information was derived.

(3) Transactions with the American Diabetes Association

(a) Research Program

The Foundation facilitates the Association's research program. Accordingly, all contributions for research raised by the Association are granted to the Foundation. These research restricted contributions to the Association totaled \$2,893,465 and \$1,264,158 in 2017 and 2016, respectively. The Foundation also receives gifts for research directly from donors, which are reported as contributions in the statement of activities.

(b) Grants from the American Diabetes Association and Management Fee

The Association provides grants to the Foundation for its research purpose as determined annually based on a formal budgeting process, which is approved by the Association's board of directors. The Foundation is reliant on this grant support, as well as donor support, for its continued operations.

The Foundation pays a management fee to the Association equal to twenty percent of contributions. This fee compensates the Association for staff and other administrative services provided to the Foundation. The management fee assessed on contributions for the Pathway to Stop Diabetes research campaign is spread over five years to align with the grant award schedule.

The Association transfers assets to the Foundation based on the timing of grant payments due. As of December 31, 2017 and 2016, the Association owed the Foundation \$63,289,465 and \$54,991,558, respectively.

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(4) Fair Value Measurements

Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. Those fair value measurements maximize the use of observable inputs. However, in situations where there is little, if any, market activity for the asset or liability at the measurement date, the fair value reflects the Association's own judgments about the assumptions that market participants would use in pricing the asset or liability. Those judgments are developed by the Association based on the best information available in the circumstances.

A fair value hierarchy prioritizes the inputs into 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 lowest priority to unobservable inputs (Level 3 measurements). The level of the hierarchy for the Foundation is as follows:

Level 3: Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the asset or liabilities. The Association's interest in perpetual trusts is carried at the fair value of the Association's share of the trust assets, which was \$85,626 and \$81,751 for 2017 and 2016, respectively. These were presented as Level 3 for both 2017 and 2016. Distributions from the trusts are recorded as investment income and the trust values are adjusted annually for changes in the fair value of the trust assets.

(5) Contributions Receivable

Contributions receivable as of December 31, 2017 and 2016, are expected to be received as follows:

	<u>2017</u>	<u>2016</u>
Within one year	\$ 1,198,023	1,144,201
In one to five years	102,150	276,550
Total contributions receivable	1,300,173	1,420,751
Less:		
Allowance for doubtful accounts	(1,063,000)	(452,000)
Present value discount	(1,570)	(5,652)
Subtotal	235,603	963,099
Funds held in remainder trusts	181,560	2,797,750
Contributions receivable, net	<u>\$ 417,163</u>	<u>3,760,849</u>

(6) Subsequent Events

For the year ended December 31, 2017, the Association has evaluated subsequent events through May 29, 2018, the date the financial statements were available to be issued, and determined that no items required disclosure.