



AMERICAN DIABETES ASSOCIATION

Consolidated Financial Statements
and Consolidating Schedules

December 31, 2016

(With Independent Auditors' Report Thereon)



KPMG LLP
1676 International Drive
McLean, VA 22102

Independent Auditors' Report

The Board of Directors
American Diabetes Association:

We have audited the accompanying consolidated financial statements of the American Diabetes Association and its subsidiaries, which comprise the consolidated balance sheet as of December 31, 2016, and the related consolidated statements of activities, functional expenses, and cash flows for the year then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated 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 consolidated 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 consolidated 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 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 the auditors' 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, the auditor considers internal control relevant to the entity'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 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 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 American Diabetes Association and its subsidiaries as of December 31, 2016, and the results of their operations and their 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 and its subsidiaries' 2015 consolidated financial statements, and we expressed an unmodified opinion on those audited consolidated financial statements in our report dated May 27, 2016. In our opinion, the summarized comparative information presented herein as of and for the year ended December 31, 2015 is consistent, in all material respects, with the audited consolidated financial statements from which it has been derived.

Other Matter

Our audit was conducted from the purpose of forming an opinion on the consolidated financial statements as a whole. The supplementary information included in schedules 1 and 2 is presented for the purposes of additional analysis and is not a required part of the 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 information is fairly stated in all material respects in related to the consolidated financial statements as a whole.

KPMG LLP

McLean, VA
May 26, 2017

AMERICAN DIABETES ASSOCIATION

Consolidated Balance Sheet

December 31, 2016

(with comparative information as of December 31, 2015)

(In thousands of dollars)

Assets	2016	2015
Cash and cash equivalents	\$ 18,622	25,065
Investments (notes 4 and 5)	51,175	51,258
Accounts receivable, net (notes 6 and 18)	10,375	10,376
Inventory and supplies, net	2,254	2,077
Prepaid expenses and other assets	4,980	4,405
Contributions receivable, net (note 7)	41,945	47,803
Fixed assets, net (note 8)	18,784	10,173
Interest in perpetual trusts (note 5)	9,806	9,709
	\$ 157,941	160,866
Liabilities and Net Assets		
Accounts payable and accrued liabilities (notes 15 and 17)	\$ 29,160	14,696
Research grants payable	18,988	13,480
Deferred revenues	10,995	14,304
	59,143	42,480
Net assets (note 11):		
Unrestricted	1,085	21,169
Temporarily restricted (note 9)	83,552	83,148
Permanently restricted (note 10)	14,161	14,069
	98,798	118,386
Total liabilities and net assets	\$ 157,941	160,866

See accompanying notes to consolidated financial statements.

AMERICAN DIABETES ASSOCIATION
Consolidated Statement of Activities
Year ended December 31, 2016
(with summarized information for the year ended December 31, 2015)
(In thousands of dollars)

	<u>Unrestricted</u>	<u>Temporarily restricted</u>	<u>Permanently restricted</u>	<u>2016 Total</u>	<u>2015 Total</u>
Revenue:					
Contributions and grants:					
Donations	\$ 33,325	33,970	—	67,295	67,308
Special events	44,385	4,601	—	48,986	56,704
Less costs of direct benefits to donors	(8,288)	—	—	(8,288)	(8,795)
Bequests	12,578	1,921	(4)	14,495	19,045
Federated and nonfederated organizations	5,019	207	—	5,226	5,895
Total contributions and grants	<u>87,019</u>	<u>40,699</u>	<u>(4)</u>	<u>127,714</u>	<u>140,157</u>
Fees from exchange transactions:					
Subscriptions and other income from periodicals	15,344	—	—	15,344	15,987
Sales of materials	3,703	—	—	3,703	3,615
Program service fees	16,716	—	—	16,716	17,185
Investment income (note 4)	2,996	323	96	3,415	1,393
Miscellaneous revenues	4,179	(9)	—	4,170	3,949
Total fees from exchange transactions	<u>42,938</u>	<u>314</u>	<u>96</u>	<u>43,348</u>	<u>42,129</u>
Net assets released from restrictions	<u>40,609</u>	<u>(40,609)</u>	<u>—</u>	<u>—</u>	<u>—</u>
Total revenue	<u>170,566</u>	<u>404</u>	<u>92</u>	<u>171,062</u>	<u>182,286</u>
Expenses (note 13):					
Program activities:					
Research	45,474	—	—	45,474	43,012
Information	51,917	—	—	51,917	47,768
Advocacy and public awareness	40,839	—	—	40,839	41,826
Total program activities	<u>138,230</u>	<u>—</u>	<u>—</u>	<u>138,230</u>	<u>132,606</u>
Supporting services:					
Management and general	11,475	—	—	11,475	9,566
Fundraising	40,945	—	—	40,945	41,152
Total supporting services	<u>52,420</u>	<u>—</u>	<u>—</u>	<u>52,420</u>	<u>50,718</u>
Total expenses	<u>190,650</u>	<u>—</u>	<u>—</u>	<u>190,650</u>	<u>183,324</u>
Change in net assets	<u>(20,084)</u>	<u>404</u>	<u>92</u>	<u>(19,588)</u>	<u>(1,038)</u>
Net assets, beginning of year	<u>21,169</u>	<u>83,148</u>	<u>14,069</u>	<u>118,386</u>	<u>119,424</u>
Net assets, end of year	<u>\$ 1,085</u>	<u>83,552</u>	<u>14,161</u>	<u>98,798</u>	<u>118,386</u>

See accompanying notes to consolidated financial statements.

AMERICAN DIABETES ASSOCIATION

Consolidated Statement of Functional Expenses

Year ended December 31, 2016

(with summarized information for the year ended December 31, 2015)

(In thousands of dollars)

	Program activities				Supporting services			2016 Total	2015 Total
	Research	Information	Advocacy and public awareness	Total	Management and general	Fundraising	Total		
Grants	\$ 32,231	140	55	32,426	—	—	—	32,426	31,281
Employee costs	4,010	21,399	20,382	45,791	5,597	17,676	23,273	69,064	66,042
Professional fees	1,712	7,674	4,968	14,354	1,737	4,509	6,246	20,600	17,842
Supplies	48	2,795	607	3,450	53	447	500	3,950	4,116
Telecommunications	117	611	592	1,320	134	506	640	1,960	1,914
Postage and shipping	238	2,176	2,339	4,753	218	4,613	4,831	9,584	9,620
Occupancy cost	646	5,643	3,082	9,371	711	2,643	3,354	12,725	12,651
Equipment rental and maintenance	63	478	449	990	80	366	446	1,436	1,203
Printing and publications	1,803	5,825	4,122	11,750	463	6,903	7,366	19,116	20,164
Travel	141	1,471	1,251	2,863	189	959	1,148	4,011	2,578
Conferences and meetings	3,989	1,084	992	6,065	15	229	244	6,309	6,680
Data processing	94	777	332	1,203	17	716	733	1,936	1,989
Depreciation and amortization	95	658	645	1,398	1,047	558	1,605	3,003	2,687
Miscellaneous	287	1,186	1,023	2,496	1,214	820	2,034	4,530	4,557
Total expenses	\$ 45,474	51,917	40,839	138,230	11,475	40,945	52,420	190,650	183,324
Costs of direct benefits to donors								8,288	8,795
Total expenses and costs of direct benefits to donors							\$ 198,938	192,119	

See accompanying notes to consolidated financial statements.

AMERICAN DIABETES ASSOCIATION

Consolidated Statement of Cash Flows

Year ended December 31, 2016

(with comparative information for the year ended December 31, 2015)

(In thousands of dollars)

	<u>2016</u>	<u>2015</u>
Cash flows from operating activities:		
Change in net assets	\$ (19,588)	(1,038)
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation and amortization	3,003	2,687
Net unrealized and realized (gain) loss on investments	(364)	1,739
Loss on disposal of assets	81	37
Provisions for doubtful receivables and obsolete inventory	943	1,096
Adjustments for changes in operating assets and liabilities:		
Increase in accounts receivable	(8)	(185)
Increase in inventory and supplies	(607)	(332)
(Increase) decrease in prepaid expenses and other assets	(575)	348
Decrease in contributions receivable	5,354	3,216
Increase in accounts payable and accrued liabilities	5,510	5,432
Increase in research grants payable	5,508	4,672
Decrease in deferred revenues	(3,309)	(1,057)
Net cash (used in) provided by operating activities	<u>(4,052)</u>	<u>16,615</u>
Cash flows from investing activities:		
Purchases of investments	(35,153)	(34,693)
Sales or maturities of investments	35,503	30,939
Proceeds from sale of fixed assets	12	—
Purchase of fixed assets	(2,753)	(3,306)
Net cash used in investing activities	<u>(2,391)</u>	<u>(7,060)</u>
Net (decrease) increase in cash and cash equivalents	(6,443)	9,555
Cash and cash equivalents, beginning of year	<u>25,065</u>	<u>15,510</u>
Cash and cash equivalents, end of year	\$ <u><u>18,622</u></u>	<u><u>25,065</u></u>
Non cash investing activities:		
Fixed assets purchased by landlord	\$ 8,954	—

See accompanying notes to consolidated financial statements.

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Notes to Consolidated Financial Statements

December 31, 2016

(with comparative information as of and for the year ended December 31, 2015)

(1) Consolidation and Organization

The consolidated financial statements include the American Diabetes Association, the American Diabetes Association Research Foundation, Inc., and the American Diabetes Association Property Title Holding Corporation (consolidated, the Association). All significant inter-Association transactions have been eliminated.

The American Diabetes Association and the American Diabetes Association Research Foundation, Inc. are exempt from income taxes under Section 501(c)(3) of the Internal Revenue Code (the Code) and charitable contributions to these organizations qualify for tax deductions as described in the Code. The American Diabetes Association Property Title Holding Corporation is exempt from income taxes under Section 501(c)(2) of the Code. These entities have been classified as organizations that are not private foundations under Section 509(a) of the Code.

The Association 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 Association has analyzed the tax positions taken and has concluded that as of December 31, 2016, 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 consolidated financial statements.

(2) Program Activities

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. This mission is accomplished through programs in communities throughout the country. The principal program activities of the Association are:

Research – The Association provides financial support to researchers who are seeking knowledge in the following areas:

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

Information – The Association conducts programs that provide diabetes information to individuals with diabetes, their families, and their healthcare providers.

Advocacy and public awareness – The Association acts as an advocate for people with diabetes by delivering programs with important diabetes messages to the general public and to all levels of the government.

(3) Summary of Significant Accounting Policies

(a) Basis of Accounting

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

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Notes to Consolidated Financial Statements

December 31, 2016

(with comparative information as of and for the year ended December 31, 2015)

The net assets and revenues, gains, and losses of the Association are classified for accounting and reporting purposes in 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 by the Association. Generally, the donors permit the Association to use the income earned on related investments for general or specific purposes.

Temporarily Restricted – Net assets subject to donor-imposed stipulations that will be met either by actions of the Association 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, federally insured certificates of deposit with original maturities of less than three months, money market funds of U.S. government securities, and other amounts that have the general characteristics of demand deposits. The Association has classified any cash or money market accounts held by external investment managers as investments as these funds are intended to be part of the Association's long-term investment strategy.

(c) Investments

Investments in marketable equity securities and all debt securities are recorded at fair value, which is based on quoted market prices or dealer quotes. The real estate investment is reported at the appraised value at the time of the donation and is evaluated for impairment on an annual basis. Unrealized and realized gains and losses are reported as investment income on the consolidated statement of activities. Investments are exposed to certain risks, such as interest rate, credit, and overall market volatility. Due to the level of risk associated with certain investment securities and the volatility in the capital markets, changes in the value of investment securities could occur in the near term, and those investment values could materially differ from the amounts reported in the accompanying consolidated financial statements.

(d) Fair Value of Financial Instruments

As of December 31, 2016 and 2015, the carrying value of cash and cash equivalents, accounts receivable, accounts payable, and research grants payable approximated their fair value, based on the short-term maturities of these instruments. Additional fair value information is presented in note 5.

(e) Inventory

Inventory comprises primarily publications and is valued at the lower of cost (first-in, first-out method) or market at net realizable value.

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Notes to Consolidated Financial Statements

December 31, 2016

(with comparative information as of and for the year ended December 31, 2015)

(f) Fixed Assets

All fixed assets are stated at cost or fair value on the date of receipt and are depreciated on a straight-line basis over the following useful lives:

Leasehold improvements	10 years or life of lease, if shorter
Furniture, fixtures, and equipment	5 years
Software	5–7 years

If donors stipulate the purpose for which the assets must be used and/or how long the assets must be held, the contributions are recorded as temporarily restricted, otherwise such donations are reported as unrestricted contributions.

(g) Recognition of Revenues

Contributions, including unconditional promises to give, are recognized when received. All contributions are considered to be available for unrestricted use unless specifically restricted by the donor.

Contributions that are restricted by the donor for a specific time or purpose are reported as temporarily or permanently restricted contributions based on the nature of the restriction. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction has been fulfilled, temporarily restricted net assets are reclassified to unrestricted net assets and are reported in the consolidated statement of activities as net assets released from restrictions. In the event a donor makes changes to the nature of a restricted gift, which affects its classification among the net asset categories, such amounts are reflected as reclassifications in the consolidated statement of activities.

Unconditional promises to give are initially recorded at their fair value. These unconditional promises to give are reported at fair value based on nonrecurring measurements classified as Level 3 in the fair value hierarchy (note 5). 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 1.1% to 2.1%. The carrying value of contributions receivable approximates the fair value.

Fees from exchange transactions are recognized as earned from reciprocal transfers of goods and services. Subscription revenue is deferred upon receipt and then recognized over the term of the subscription, which is generally twelve issues, beginning with the mailing of the first issue to the subscriber.

(h) Split-Interest Agreements

The Association receives certain planned gift donations that benefit not only the Association, but also the donor or another beneficiary designated by the donor. These contributions are termed split-interest agreements and are generally gifts to be received by the Association in the future. The Association benefits from the following types of split-interest agreements: perpetual trusts, charitable lead and remainder trusts, gift annuities, and a pooled income fund.

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Notes to Consolidated Financial Statements

December 31, 2016

(with comparative information as of and for the year ended December 31, 2015)

The Association's share of split-interest agreements is included in investments, contributions receivable, or interest in perpetual trusts. Assets of approximately \$23,349,000 and \$24,304,000 are reported on the consolidated balance sheets as of December 31, 2016 and 2015, respectively. When applicable, amounts to be received in future periods are discounted using a risk-adjusted rate based on the expected term of the split-interest agreements. The rate for 2016 and 2015 was 2.7% and 2.2%, respectively.

Amounts payable to beneficiaries, gift annuities payable, and pooled income fund liabilities of approximately \$1,295,000 and \$1,428,000 are reported as accrued liabilities or deferred revenues on the consolidated balance sheets as of December 31, 2016 and 2015, respectively.

(i) Contributed Services and Materials

Contributed services and materials are reported in the consolidated statement of activities at the fair value of the services and materials 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.

(j) Research Program

The research program of the American Diabetes Association is administered through the American Diabetes Association Research Foundation, Inc. Research grants awarded by the Association generally extend over a period of one to five years, subject to renewal on an annual basis. The liability and related expenses are recorded when the recipients are notified of their annual award amount, and the liability is recorded as research grants payable in the consolidated balance sheet.

(k) Management Estimates and Uncertainties

The preparation of consolidated 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 as of the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

(l) Functional Allocation of Expenses

Expenses have been summarized on a functional basis in the consolidated statement of activities. Accordingly, certain costs have been allocated among program activities and supporting services.

(m) Comparative Financial Statements

The consolidated statements of activities and functional expenses include certain summarized comparative information for the year ended December 31, 2015. 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 Association's consolidated financial statements for the year ended December 31, 2015, from which the summarized information was derived.

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Notes to Consolidated Financial Statements

December 31, 2016

(with comparative information as of and for the year ended December 31, 2015)

(4) Investments

Investments as of December 31, 2016 and 2015, consist of the following (in thousands):

	<u>2016</u>	<u>2015</u>
U.S. government securities	\$ 15,423	11,590
Real estate	12,818	12,818
Fixed-income bonds	7,895	12,251
Fixed-income mutual funds	4,888	4,751
Corporate equities	4,373	4,054
Equity mutual funds	3,343	3,134
Money market funds	2,435	2,629
Other	—	31
Total investments	\$ <u>51,175</u>	<u>51,258</u>

Investments as of December 31, 2016 and 2015, include gift annuity investments of approximately \$2,672,000 and \$2,696,000, respectively, and the fair value of gift annuity obligations under those agreements was approximately \$1,295,000 and \$1,428,000, respectively. Reserves for gift annuities are held in separate investment accounts at a value equal to the original gift plus accrued income less beneficiary payments.

The investment in real estate represents a 1998 donor bequest that restricted the Association from selling the property for 25 years. A portion of the property is leased to corporations and derives monthly rental income that is reported in investment income in the consolidated statement of activities.

Investment income for the years ended December 31, 2016 and 2015, includes (in thousands):

	<u>2016</u>	<u>2015</u>
Property rental income, net	\$ 1,676	1,671
Net realized and unrealized gains (losses)	364	(1,739)
Interest and dividends	1,610	1,727
Investment fees	<u>(235)</u>	<u>(266)</u>
Total investment income, net	\$ <u>3,415</u>	<u>1,393</u>

(5) 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

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Notes to Consolidated Financial Statements

December 31, 2016

(with comparative information as of and for the year ended December 31, 2015)

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 three levels of the hierarchy are as follows:

Level 1: Unadjusted quoted prices in active markets for identical assets or liabilities.

Level 2: Observable inputs other than Level 1, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities. Split-interest obligations are measured as the present value of future cash flows expected to be paid to the donor or the donor's designee. These obligations are adjusted during the term of each annuity for payments to donors, accretion of discounts and changes in life expectancies of the donors.

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. 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. Funds held in remainder trusts are measured at the present value of future distributions projected to be received over the expected remaining term of the trust, or upon the trust's expiration. note 3(h) includes information about the discount rates used in determining the value of the assets.

The following table presents the fair value hierarchy for the Association's financial assets and liabilities that are measured at fair value on a recurring basis as of December 31, 2016 (in thousands):

	<u>Total</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
Financial assets:				
Investments:				
Fixed-income bonds	\$ 7,895	—	7,895	—
U.S. government securities	15,423	—	15,423	—
Fixed-income mutual funds	4,888	4,888	—	—
Equity mutual funds	3,343	3,343	—	—
Money market funds	2,435	2,435	—	—
Corporate equities	4,373	4,373	—	—
Interest in perpetual trusts	9,806	—	—	9,806
Funds held in remainder trusts	10,871	—	—	10,871
Financial liabilities:				
Split-interest obligations	\$ 1,295	—	1,295	—

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Notes to Consolidated Financial Statements

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(with comparative information as of and for the year ended December 31, 2015)

The following table presents the fair value hierarchy for the Association's financial assets and liabilities that are measured at fair value on a recurring basis as of December 31, 2015 (in thousands):

	<u>Total</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
Financial assets:				
Investments:				
Fixed-income bonds	\$ 12,251	—	12,251	—
U.S. government securities	11,590	—	11,590	—
Fixed-income mutual funds	4,751	4,751	—	—
Equity mutual funds	3,134	3,134	—	—
Money market funds	2,629	2,629	—	—
Corporate equities	4,054	4,054	—	—
Other	31	31	—	—
Interest in perpetual trusts	9,709	—	—	9,709
Funds held in remainder trusts	11,831	—	—	11,831
Financial liabilities:				
Split-interest obligations	\$ 1,428	—	1,428	—

Changes in perpetual trusts and funds held in remainder trusts for the years ended December 31, 2016 and 2015, are as follows (in thousands):

	<u>Perpetual Trusts</u>	<u>Funds Held in Remainder Trusts</u>
Balance, December 31, 2014	\$ 9,999	13,189
New trusts	—	57
Investment gains (losses)	78	(387)
Distributions	(368)	(1,028)
Balance, December 31, 2015	9,709	11,831
New trusts	—	—
Investment gains	466	221
Distributions	(369)	(1,181)
Balance, December 31, 2016	\$ <u>9,806</u>	<u>10,871</u>

(6) Accounts Receivable

The Association's receivables consist of amounts due for program service fees, publications, advertising, land rental (note 18), and other exchange transactions. The receivables are reported net of an allowance for doubtful accounts of approximately \$1,372,000 and \$1,439,000 as of December 31, 2016 and 2015,

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Notes to Consolidated Financial Statements

December 31, 2016

(with comparative information as of and for the year ended December 31, 2015)

respectively. Of the allowance amount, \$1,027,000 and \$1,054,000 as of December 31, 2016 and 2015, respectively, relate to the land rental.

(7) Contributions Receivable

Contributions receivable consist of the following amounts due as of December 31, 2016 and 2015 (in thousands):

	<u>2016</u>	<u>2015</u>
Within one year	\$ 26,459	30,967
In one to five years	6,549	7,150
Total contributions receivable	33,008	38,117
Less allowance for doubtful accounts	(1,798)	(1,963)
Less present value discount	(136)	(182)
Subtotal	31,074	35,972
Funds held in remainder trusts	10,871	11,831
Contributions receivable, net	\$ <u>41,945</u>	<u>47,803</u>

(8) Fixed Assets

Fixed assets consist of the following as of December 31, 2016 and 2015 (in thousands):

	<u>2016</u>	<u>2015</u>
Land	\$ 67	67
Leasehold improvements	6,283	1,108
Software	20,381	19,853
Furniture, fixtures, and equipment	18,573	16,454
Total fixed assets	45,304	37,482
Less accumulated depreciation and amortization	(26,520)	(27,309)
Fixed assets, net	\$ <u>18,784</u>	<u>10,173</u>

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December 31, 2016

(with comparative information as of and for the year ended December 31, 2015)

(9) Temporarily Restricted Net Assets

Net assets were temporarily restricted for the following as of December 31, 2016 and 2015 (in thousands):

	<u>2016</u>	<u>2015</u>
Research	\$ 39,150	37,490
Information	3,285	5,354
Advocacy	4,554	4,767
Sponsorship for fundraising activities	4,129	3,245
Future periods (otherwise unrestricted)	<u>32,434</u>	<u>32,292</u>
Total temporarily restricted net assets	<u>\$ 83,552</u>	<u>83,148</u>

(10) Permanently Restricted Net Assets

In accordance with donor stipulations, permanently restricted net assets are held (and invested) in perpetuity. The income derived from these net assets at December 31, 2016 and 2015, is to be used as follows (in thousands):

	<u>2016</u>	<u>2015</u>
Research	\$ 3,924	3,892
Information	2,017	1,999
Advocacy and public awareness	193	194
Discretion of the Association	<u>8,027</u>	<u>7,984</u>
Total permanently restricted net assets	<u>\$ 14,161</u>	<u>14,069</u>

(11) Endowment

The Association's endowment consists of 46 individual donor-restricted endowment funds and donor-restricted term endowment funds established for a variety of purposes. The Association has no board-designated endowment funds.

The net assets associated with these funds are classified and reported based on the existence or absence of donor-imposed restrictions. Accordingly, the historic dollar value of donor-restricted endowment contributions is reported as permanently restricted net assets. The portion of a donor-restricted endowment fund that is not classified as permanently restricted net assets and the term endowment funds are classified as temporarily restricted net assets until appropriated for expenditure.

At times, the fair value of assets associated with an individual donor-restricted endowment fund may fall below the historic dollar value of the fund. A deficiency of \$78,000 existed as of December 31, 2015.

AMERICAN DIABETES ASSOCIATION

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December 31, 2016

(with comparative information as of and for the year ended December 31, 2015)

Changes in endowment net assets for the years ended December 31, 2016 and 2015, are as follows (in thousands):

	<u>Unrestricted</u>	<u>Temporarily restricted</u>	<u>Permanently restricted</u>	<u>Total</u>
Endowment net assets, December 31, 2014	\$ —	18,179	4,362	22,541
Investment return:				
Investment income	1,973	—	—	1,973
Net depreciation	(380)	—	—	(380)
Contributions	—	—	(2)	(2)
Appropriation for expenditure	<u>(1,671)</u>	<u>—</u>	<u>—</u>	<u>(1,671)</u>
Endowment net assets, December 31, 2015	(78)	18,179	4,360	22,461
Investment return:				
Investment income	1,747	177	—	1,924
Net appreciation	49	—	—	49
Contributions	—	—	(5)	(5)
Appropriation for expenditure	<u>(1,718)</u>	<u>(177)</u>	<u>—</u>	<u>(1,895)</u>
Endowment net assets, December 31, 2016	<u>\$ —</u>	<u>18,179</u>	<u>4,355</u>	<u>22,534</u>

The Association has adopted an investment policy for endowment assets that provides continued financial stability for the Association and a revenue stream for spending on the Association's mission.

Under this policy, as approved by the board of directors, the Association relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The Association targets a diversified asset allocation that utilizes fixed-income and equity-based investments to achieve its long-term objectives within prudent risk constraints. The Association expects its endowment funds, over time, to provide an average rate of return of approximately 7.5% annually.

The Association's endowment spending policy permits spending at a rate of 4% of the endowments' market value over a rolling five-year average. The long-term return of 7.5% and a spending rate of 4% are intended to maintain the purchasing power of the endowment.

(12) Contributed Services and In-kind Contributions

The Association recognizes as contribution revenue and as professional fees expense the fair value of services donated by volunteers in conjunction with the peer review process by the Grant Review Panel of the American Diabetes Association Research Foundation, Inc. and medical services provided in conjunction with the Association's program activities, primarily camps held for children with diabetes.

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December 31, 2016

(with comparative information as of and for the year ended December 31, 2015)

Contributed services for occupancy are recorded in occupancy expenses. The Association recognized approximately \$2,437,000 and \$2,055,000, in donated services provided in conjunction with the Association's activities during the years ended December 31, 2016 and 2015, respectively.

Many other volunteers made significant contributions of time to the Association's program and supporting functions. The values of those contributed services do not meet the criteria for recognition and, accordingly, are not recognized as revenues and expenses in the accompanying consolidated statement of activities.

In-kind contributions of supplies are recognized as contribution revenue and supplies expense and totaled approximately \$2,074,000 and \$2,268,000 for the years ended December 31, 2016 and 2015, respectively.

(13) Allocation of Joint Costs

The Association conducts activities to distribute information related to diabetes and a call to action, such as assessing a person's risk for diabetes and seeking appropriate health services, as well as an appeal for funds. The joint costs incurred through these activities for the years ended December 31, 2016 and 2015, were allocated as follows (in thousands):

	<u>2016</u>	<u>2015</u>
Advocacy and public awareness	\$ 8,543	9,942
Management and general	827	247
Fundraising	<u>16,008</u>	<u>17,489</u>
Total joint costs	<u>\$ 25,378</u>	<u>27,678</u>

(14) Pension Plan

The Association has a defined-contribution pension plan that covers most salaried employees who have reached the age of 21 and completed one year of service. Pension expense for the years ended December 31, 2016 and 2015, was approximately \$1,529,000 and \$1,754,000, respectively.

(15) Self-Insured Benefits

The Association self-insures its employee medical and dental benefits. Losses from claims identified under the incident reporting system, as well as provisions for estimated losses for incurred but not reported incidents, are accrued based on estimates that incorporate the past experience of the Association, as well as other considerations, including the nature of the claims or incidents and relevant trend factors.

Self-insured risk for employee health benefits is secured through stop loss insurance policies that protect the Association should total claims exceed a specified limit in a plan year. This limit was approximately \$9,060,000 and \$9,971,000 in 2016 and 2015, respectively.

The liability as of December 31, 2016 and 2015, was approximately \$542,000 and \$433,000, respectively, and is included in accounts payable and accrued liabilities in the consolidated balance sheets. Benefit expense under this plan was approximately \$7,537,000 and \$6,228,000 for the years ended December 31,

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Notes to Consolidated Financial Statements

December 31, 2016

(with comparative information as of and for the year ended December 31, 2015)

2016 and 2015, respectively. The benefit expense includes claims paid and changes to the reserve for future claims.

(16) Line of Credit

The Association has an unsecured line of credit with a bank at interest rates of the London Interbank Offered Rate (LIBOR) plus 2.25% points. The line of credit of \$5,000,000 was renewed in September 2015 and was subsequently renewed for \$10,000,000 in February 2016. The Association expects to renew the line of credit each year. The outstanding balance on the line of credit as of December 31, 2016 and 2015, was \$0. Interest and fees for each of the years ended December 31, 2016 and 2015, were approximately \$47,000 and \$18,000, respectively.

The line of credit is available for working capital and for financing the purchase and implementation costs of computer equipment and software. The Association was required to maintain a level of unrestricted, unencumbered marketable securities, cash and cash equivalents of not less than \$10,000,000 as of December 31, 2016.

(17) Lease Commitments

The Association is obligated under various noncancelable operating lease agreements for facilities expiring at various dates through July 2030. The Association has received improvement, equipment and other incentives from landlords and many of these agreements contain cost escalations providing for increases in rental rates. The Association recognizes rent expense on a straight-line basis over the life of the lease. The Association is also obligated under noncancelable operating leases for telephone and other equipment through March 2021.

As of December 31, 2016, the future minimum lease payments under operating leases with noncancelable lease terms in excess of one year were (in thousands):

Year ending December 31:		
2017	\$	7,248
2018		6,283
2019		5,702
2020		4,575
2021		4,281
2022 and thereafter		<u>32,441</u>
Total minimum lease payments	\$	<u><u>60,530</u></u>

Rent expense totaled approximately \$8,926,000 and \$8,951,000 for the years ended December 31, 2016 and 2015, respectively.

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Notes to Consolidated Financial Statements

December 31, 2016

(with comparative information as of and for the year ended December 31, 2015)

(18) Lease Payments Receivable

The Association holds leases on land that was donated in 1998 through a bequest. As part of the bequest, the donor restricted the Association from selling the land for 25 years from the date of the donation. As of December 31, 2016, the future minimum lease payments due to the Association under these leases were (in thousands):

Year ending December 31:		
2017	\$	1,483
2018		1,551
2019		1,634
2020		1,643
2021		1,240
2022 and thereafter		<u>41,937</u>
Total minimum lease receipts	\$	<u><u>49,488</u></u>

The accumulated difference between the rental income recognized and the straight-line value of the leases was approximately \$7,613,000 and \$7,412,000 as of December 31, 2016 and 2015, respectively, and is included in accounts receivable on the consolidated balance sheet. Due to market conditions, management believes a significant risk exists that future rent revenue will not be recognized; therefore, an allowance against the deferred rent has been recorded in the amount of \$1,027,000 and \$1,054,000 as of December 31, 2016 and 2015, respectively.

(19) Subsequent Events

For the year ended December 31, 2016, the Association has evaluated subsequent events through May 26, 2017, the date the consolidated financial statements were available to be issued, and determined that no items required disclosure.

AMERICAN DIABETES ASSOCIATION

Consolidating Schedule – Balance Sheet

December 31, 2016

(In thousands of dollars)

Assets	American Diabetes Association	Research Foundation	Property Title Holding Corp	Intercompany Eliminations	Consolidated Association
Cash and cash equivalents	\$ 18,622	—	—	—	18,622
Investments	51,175	—	12,818	(12,818)	51,175
Intercompany receivables	5,930	54,992	—	(60,922)	—
Accounts receivable, net	3,649	—	6,726	—	10,375
Inventory and supplies, net	2,254	—	—	—	2,254
Prepaid expenses and other assets	4,980	—	—	—	4,980
Contributions receivable, net	38,184	3,761	—	—	41,945
Fixed assets, net	18,784	—	—	—	18,784
Interest in perpetual trusts	9,724	82	—	—	9,806
Total assets	<u>\$ 153,302</u>	<u>58,835</u>	<u>19,544</u>	<u>(73,740)</u>	<u>157,941</u>
Liabilities and Net Assets					
Accounts payable and accrued liabilities	\$ 29,071	—	89	—	29,160
Research grants payable	—	18,988	—	—	18,988
Intercompany payables	54,992	—	5,930	(60,922)	—
Deferred revenues	10,288	—	707	—	10,995
Total liabilities	<u>94,351</u>	<u>18,988</u>	<u>6,726</u>	<u>(60,922)</u>	<u>59,143</u>
Unrestricted net assets	1,085	—	—	—	1,085
Temporarily restricted net assets	43,787	39,765	12,818	(12,818)	83,552
Permanently restricted net assets	14,079	82	—	—	14,161
Total net assets	<u>58,951</u>	<u>39,847</u>	<u>12,818</u>	<u>(12,818)</u>	<u>98,798</u>
Total liabilities and net assets	<u>\$ 153,302</u>	<u>58,835</u>	<u>19,544</u>	<u>(73,740)</u>	<u>157,941</u>

See accompanying independent auditors' report.

AMERICAN DIABETES ASSOCIATION

Consolidating Schedule – Statement of Activities

Year ended December 31, 2016

(In thousands of dollars)

	<u>American Diabetes Association</u>	<u>Research Foundation</u>	<u>Property Title Holding Corp</u>	<u>Intercompany Eliminations</u>	<u>Consolidated Association</u>
Revenue:					
Contributions and grants:					
Donations	\$ 64,577	2,718	—	—	67,295
Special events, net	40,698	—	—	—	40,698
Bequests	13,890	605	—	—	14,495
Federated and nonfederated organizations	5,136	90	—	—	5,226
Total contributions and grants	<u>124,301</u>	<u>3,413</u>	<u>—</u>	<u>—</u>	<u>127,714</u>
Fees from exchange transactions:					
Subscriptions and periodicals	15,344	—	—	—	15,344
Sale of materials	3,703	—	—	—	3,703
Program service fees	16,716	—	—	—	16,716
Investment income	1,736	3	1,676	—	3,415
Miscellaneous revenues	4,170	—	—	—	4,170
Total fees from exchange transactions	<u>41,669</u>	<u>3</u>	<u>1,676</u>	<u>—</u>	<u>43,348</u>
Intercompany revenues	3,059	34,229	—	(37,288)	—
Total revenue	<u>169,029</u>	<u>37,645</u>	<u>1,676</u>	<u>(37,288)</u>	<u>171,062</u>
Expenses:					
Program activities	105,301	32,929	—	—	138,230
Management and general	11,475	—	—	—	11,475
Fundraising	40,945	—	—	—	40,945
Intercompany expenses	34,229	1,383	1,676	(37,288)	—
Total expenses	<u>191,950</u>	<u>34,312</u>	<u>1,676</u>	<u>(37,288)</u>	<u>190,650</u>
Change in net assets	(22,921)	3,333	—	—	(19,588)
Net assets, beginning of year	81,872	36,514	12,818	(12,818)	118,386
Net assets, end of year	<u>\$ 58,951</u>	<u>39,847</u>	<u>12,818</u>	<u>(12,818)</u>	<u>98,798</u>

See accompanying independent auditors' report.