SANSUM DIABETES RESEARCH INSTITUTE

FINANCIAL STATEMENTS

DECEMBER 31, 2017

SANSUM DIABETES RESEARCH INSTITUTE
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December 31, 2017

DAMITZ
BROOKS
NIGHTINGALE
TURNER
MORRISSET

INDEPENDENT AUDITOR'S REPORT

Board of Trustees
Sansum Diabetes Research Institute

We have audited the accompanying financial statements of Sansum Diabetes Research Institute (the Institute) which comprise the statement of financial position as of December 31, 2017, and the related statements of activity, 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 accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's 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 of 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 auditor's 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 financial statement presentation.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a reasonable 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 Sansum Diabetes Research Institute as of December 31, 2017, and the changes in net assets and cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Report on Summarized Comparative Information

We have previously audited Sansum Diabetes Research Institute's 2016 financial statements, and we expressed an unmodified audit opinion on those audited financial statements in our report dated August 25, 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.

Damitz, Brooks, Nightingale, Turner & Morrisset

Damitz, Brooks, Nightingale,
Turner & Morrisset
August 24, 2018

SANSUM DIABETES RESEARCH INSTITUTE
Statement of Financial Position
December 31, 2017
(With Summarized Comparative Totals for the Year 2016)

Assets	Unrestricted	Temporarily Restricted	Permanently Restricted	Total 2017	Total 2016
Cash and cash equivalents	$ 884,516	$ -	$ -	884,516	$ 361,144
Accounts receivable	570,848	-	-	570,848	669,219
Bequests and pledges receivable, net	-	2,273,692	-	2,273,692	1,656,090
Investment income receivable	34,159	-	-	34,159	27,910
Prepaid expenses and deposits	48,531	-	-	48,531	42,959
Other assets	-	66,665	-	66,665	20,346
	1,538,054	2,340,357	-	3,878,411	2,777,668
Investments-					
Marketable securities					
Cash and cash equivalents held for investment	716,003	-	-	716,003	899,473
Annuity funds	165,378	-	-	165,378	168,008
Other	1,873,154	2,266,375	3,188,962	7,328,491	5,773,199
Marketable securities held in trust					
Assets held in split interest trusts	-	136,891	-	136,891	137,782
Non-trustee remainder interests in split interest trusts, net	-	520,098	3,592	523,690	212,581
Beneficial interest in perpetual trust	-	-	1,718,546	1,718,546	1,578,816
Cash surrender value of life insurance	112,801	-	-	112,801	110,176
	2,867,336	2,923,364	4,911,100	10,701,800	8,880,035
Property and equipment, net	1,668,936	-	-	1,668,936	1,722,241
	$ 6,074,326	$ 5,263,721	$ 4,911,100	$ 16,249,147	$ 13,379,944
Liabilities and Net Assets					
Liabilities					
Accounts payable	$ 100,771	$ -	$ -	$ 100,771	$ 57,263
Accrued liabilities	329,724	-	-	329,724	287,259
Annuities payable	71,420	-	-	71,420	74,669
Present value of future payments on split-interest trusts	-	30,296	-	30,296	39,076
Total liabilities	501,915	30,296	-	532,211	458,267
Net Assets					
Unrestricted					
Board designated	2,659,712	-	-	2,659,712	2,085,330
Other unrestricted net assets	2,912,699	-	-	2,912,699	3,041,369
Temporarily restricted	-	5,233,425	-	5,233,425	2,737,885
Permanently restricted	-	-	4,911,100	4,911,100	5,057,093
Total net assets	5,572,411	5,233,425	4,911,100	15,716,936	12,921,677
	$ 6,074,326	$ 5,263,721	$ 4,911,100	$ 16,249,147	$ 13,379,944

SANSUM DIABETES RESEARCH INSTITUTE

Statement of Activity

Year Ended December 31, 2017

(With Summarized Comparative Totals for the Year 2016)

	Unrestricted	Temporarily Restricted	Permanently Restricted	**Total 2017**	**Total 2016**
Revenues, Gains (Losses), and Other Support					
Contributions	$ 222,573	$ 68,750	$ -	$ 291,323	$ 898,258
Bequests and pledges	131,687	3,224,817	-	3,356,504	286,156
Annuities and actuarial adjustments	(7,622)	-	-	(7,622)	43,002
Clinical studies	1,390,579	-	-	1,390,579	898,158
Research grants	69,688	589,213	-	658,901	403,921
Rental income	108,964	-	-	108,964	103,200
Investment income, net	344,252	470,861	-	815,113	394,222
Change in the value of charitable trusts	-	38,678	(87)	38,591	27,365
Change in the value of beneficial interest in perpetual trust	-	-	139,730	139,730	1,447
Distributions from perpetual trust	-	80,321	-	80,321	81,670
Patient care fees	32,386	-	-	32,386	26,848
Other	82,756	-	-	82,756	57,894
Net assets released from restrictions	2,262,736	(1,977,100)	(285,636)	-	-
Special event:					
Special event - gross	167,884	-	-	167,884	126,820
Direct special event costs	(100,946)	-	-	(100,946)	(63,125)
Net special event proceeds	66,938	-	-	66,938	63,695
Total revenues, gains, and other support	4,704,937	2,495,540	(145,993)	7,054,484	3,285,836
Expenses					
Research	3,035,688	-	-	3,035,688	2,462,775
Management and general	723,715	-	-	723,715	702,871
Annuity program	-	-	-	-	395
Fundraising	499,822	-	-	499,822	389,420
Total expenses	4,259,225	-	-	4,259,225	3,555,461
Increase (decrease) in net assets	445,712	2,495,540	(145,993)	2,795,259	(269,625)
Net assets, beginning of year	5,126,699	2,737,885	5,057,093	12,921,677	13,191,302
Net assets, end of year	$ 5,572,411	$ 5,233,425	$ 4,911,100	$ 15,716,936	$ 12,921,677

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

SANSUM DIABETES RESEARCH INSTITUTE
Statement of Functional Expenses
Year Ended December 31, 2017
(With Summarized Comparative Totals for the Year 2016)

	Program Services	Supporting Services		Total	
	Research and Education	Management and General	Special Events and Fundraising	2017	2016
Salaries	$ 2,026,887	$ 325,767	$ 308,620	$ 2,661,274	$ 2,274,336
Payroll taxes and benefits	332,960	57,273	50,137	440,370	384,946
Total salaries and benefits	2,359,847	383,040	358,757	3,101,644	2,659,282
Outside services	135,979	82,159	104,443	322,581	228,461
Clinical research	207,600	-	-	207,600	82,915
Supplies	92,951	25,460	1,618	120,029	101,495
Printing and postage	2,535	709	11,857	15,101	14,048
Dues and publications	14,218	3,406	7,393	25,017	24,083
Travel and meetings	44,983	9,650	3,600	58,233	52,102
Insurance	28,066	23,954	1,927	53,947	52,942
Occupancy	40,056	34,187	2,751	76,994	68,667
Telephone	11,216	9,572	770	21,558	19,233
Repairs and maintenance	186	43,987	199	44,372	37,728
Professional services	7,394	40,295	-	47,689	48,730
Depreciation	77,033	65,747	5,290	148,070	153,250
Miscellaneous	13,624	1,549	1,217	16,390	12,525
	$ 3,035,688	$ 723,715	$ 499,822	$ 4,259,225	$ 3,555,461

SANSUM DIABETES RESEARCH INSTITUTE

Statement of Cash Flows

Year Ended December 31, 2017

(With Summarized Comparative Totals for the Year 2016)

	2017	2016
Cash flows from operating activities		
Increase (decrease) in net assets	$ 2,795,259	$ (269,626)
Adjustments to reconcile decrease in net assets to net cash provided by operating activities:		
Depreciation	148,070	153,250
Loss on disposal of intangible assets	17,701	-
Net realized gain on investments	(235,774)	(137,999)
Unrealized gain on investments	(415,250)	(109,092)
Change in remainder interests in trusts	(310,218)	(19,323)
Change in present value of future payments on split-interest trusts	(8,780)	(8,042)
Unrealized gain on life insurance policies	(2,489)	(2,645)
Change in cash and cash equivalents held for investment	183,470	790,580
Change in beneficial interest in perpetual trusts	(139,730)	(1,447)
(Increase) decrease in:		
Accounts receivable	98,371	(335,279)
Bequests and pledges receivable	(617,602)	(234,355)
Investment income receivable	(6,249)	13,107
Prepaid expenses and deposits	(5,572)	(15,008)
Increase (decrease) in:		
Accounts payable	43,508	(2,249)
Accrued liabilities	42,465	80,338
Annuities payable	(3,249)	(53,873)
Net cash provided (used) by operating activities	1,583,931	(151,663)
Cash flows from investing activities		
Purchase of property and equipment	(94,765)	(52,056)
Purchase of investments	(1,538,462)	(196,596)
Library development	(64,020)	(2,645)
Website development	-	(17,701)
Proceeds from sales of investments	636,688	565,135
Net cash provided (used) by investing activities	(1,060,559)	296,137
Net increase in cash and cash equivalents	523,372	144,474
Cash and cash equivalents, beginning of year	361,144	216,670
Cash and cash equivalents, end of year	$ 884,516	$ 361,144

SANSUM DIABETES RESEARCH INSTITUTE
Notes to Financial Statements
December 31, 2017
(With Summarized Comparative Totals for 2016)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

This summary of significant accounting policies of Sansum Diabetes Research Institute (the Institute) is presented to assist in understanding the Institute's financial statements. The financial statements and notes are representations of the Institute's management, who are responsible for their integrity and objectivity. These accounting policies conform to accounting principles generally accepted in the United States of America (GAAP) and have been consistently applied in the preparation of the financial statements.

Nature of Activities

The Institute is a non-profit charitable corporation and has been at the forefront of helping to improve the lives of people living with diabetes since its creation in 1944 through research education and care. William Sansum, MD was the first physician in the United States to manufacture and administer insulin to a patient with diabetes in 1922. Today the Institute has an established world reputation in the field of research, artificial pancreas and diabetes in pregnancy. The Institute's office and research facilities are located in Santa Barbara, California.

Financial Statement Presentation

Information regarding the Institute's financial position and activities is reported according to three classes of net assets: unrestricted net assets, temporarily restricted net assets, and permanently restricted net assets.

<u>Unrestricted net assets</u> generally result from unrestricted contributions and investment income less expenses incurred in providing services, fundraising and other administrative expenses.

<u>Temporarily restricted net assets</u> are classified as such based on donor stipulations that they be used in a later period or for a specific purpose. They also include unrestricted investment income on permanently restricted assets where the income has not yet been appropriated for expenditure. When a restriction expires or is met, temporarily restricted net assets are reclassified to unrestricted net assets and are reported in the accompanying statement of activities as net assets released from restriction.

<u>Permanently restricted net assets</u> consist of assets where the donor has imposed permanent restrictions on use of the principal of assets donated. The unrealized gains and investment income on funds not restricted by the donor are classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Institute in a manner consistent with the standard of prudence prescribed by Uniform Prudent Management of Institutional Funds Act (UPMIFA). (Note 9)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Cont.)

Cash and Cash Equivalents

For purposes of the statement of cash flows, cash and cash equivalents consists of cash on hand, cash in banks, and cash in money market funds and excludes cash and cash equivalents held for investment. Cash equivalents classified as investments include money market funds and certificates of deposit.

Contributed Services

During the years ended December 31, 2017 and 2016, the value of contributed services meeting the requirements for recognition in the financial statements was not material and has not been recorded. Although many individuals volunteer their time and perform a variety of tasks that assist the Institute in various activities these services do not meet the GAAP criteria for recognition as contributed services. The Institute receives approximately 1,100 volunteer hours per year.

Prior-Year Summarized Comparative Information

The financial statements include certain prior-year summarized comparative information in total but are not presented by net assets class. Such information does not include sufficient detail to constitute a presentation in conformity with GAAP. Accordingly, such information should be read in conjunction with the Institute's financial statements for the year ended December 31, 2016 from which the summarized information was derived.

Accounts Receivable

The Institute has made no provision for an allowance for doubtful accounts as of December 31, 2017 and 2016 based on management's analysis of the potential credit risk of funding agencies, historical trends, and other information. The Institute does not require collateral from its funding agencies.

Contributions and Bequests and Pledges Receivable

Contributions are recorded when received. Bequests and pledges receivable are measured at fair value on the date a written unconditional promise to give is received from the donor. On this date, the fair value is measured using an income approach which incorporates inputs including estimated credit risk, estimated timing of cash receipts, and an appropriate present value discount factor.

Revenue Recognition – Clinical Studies

The Institute recognizes revenues and related costs using the percentage-of-completion method measured by labor and direct costs incurred.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Cont.)

Investments

In accordance with GAAP, the Institute accounts for its marketable equity securities at fair value. Information about the unrealized gains is presented in Note 3. Information about fair value of investments is discussed in Note 4.

Fair Value Measurements

The Institute follows Accounting Standard Codification (ASC) No. 820, *Fair Value Measurements and Disclosures,* issued by the Financial Accounting Standards Board (FASB). This standard defines fair value, establishes a framework for measuring fair value, and requires certain disclosures about fair value measurements. Pursuant to ASC No. 820, assets and liabilities recorded at fair value are categorized based upon the level of judgment associated with the inputs used to measure fair value. ASC No. 820 establishes a three-level fair value hierarchy that describes the inputs that are used to measure the fair values of respective assets and liabilities:

Level 1 – Quoted prices are available in active markets for identical investments as of the reporting date.

Level 2 – Pricing inputs, including broker quotes, are generally those other than exchange quoted prices in active markets, which are either directly or indirectly observable as of the reporting date, and fair value is determined through the use of models or other valuation methodologies.

Level 3 – Pricing inputs are unobservable for the investment and include situations where there is little, if any, market activity for the investment. The inputs into the determination of fair value require significant management judgment, estimation, or other unobservable inputs.

Following is a description of the valuation methodologies used for assets and liabilities measured at fair value on a recurring basis.

Cash: Valued at face value. (Level 1)

Cash equivalents, certificates of deposit, U.S. government obligations and corporate bonds: Valued utilizing benchmark yields, reported trades or broker dealer quotes. (Level 2)

Equity securities, mutual and exchange traded funds: Valued utilizing quoted prices available in active markets for identical investments as of the reporting date. (Level 1)

Split-interest trusts future payments: Valued using life expectancy and discount factors obtained from external sources including the Internal Revenue Service. (Level 2)

Life insurance policies: Valued based on policy's cash surrender value. Cash surrender values are determined using unobservable inputs. (Level 3)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Cont.)

Annuities payable: Valued using the reasonably commensurate value factors for single life annuities provided by the California Department of Insurance. (Level 2)

Beneficial interest in perpetual trust: Valued based on the assets held by the trust utilizing quoted prices available in active markets for identical investments as of the reporting date. These assets consist of cash and cash equivalents, bonds, mutual funds, and equity securities. The Institute does not have the ability to control or direct the assets held by the trust and the interest in the trust is nonredeemable. (Level 3)

Property and Equipment

Property and equipment are stated at cost or, if acquired by gift, at the fair market value at the date of donation. Expenditures for building improvements and major renewals in excess of $500 that extend the useful lives of property and equipment are capitalized. Expenditures for maintenance and repairs are charged to operations as incurred. Depreciation is computed using the straight-line method over the estimated useful lives as follows:

	Years
Specialized equipment	2
Buildings and improvements	15-40
Furniture and equipment	4-10

Functional Expenses

Direct expenses are charged to programs or supporting services in general categories based on specific identification. Overhead costs are allocated to programs or supporting services based on the relative ratio of square footage charged to each respective category.

Tax Exempt Status

The Institute is an exempt organization under Section 501(c)(3) of the Internal Revenue Code (IRC) and Section 23701(d) of the California Revenue and Taxation Code, and is considered a public charity.

Uncertain Tax Positions

The Institute's IRS Form 990 is subject to review and examination by Federal and state authorities. The Institute is not aware of any activities that would jeopardize its tax-exempt status. The Institute is not aware of any activities that are subject to tax on unrelated business income, excise or other taxes.

Use of Estimates

Financial statements prepared in accordance with GAAP require management to make estimates and assumptions that affect certain reported amounts and disclosures. Actual results could differ from those estimates.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Cont.)

Reclassifications

Certain items in the 2016 financial statements were reclassified in order to conform to the 2017 presentation.

Subsequent Events

Management has evaluated subsequent events through August 24, 2018, the date that the financial statements were available to be issued.

2. BEQUESTS AND PLEDGES RECEIVABLE

Unconditional promises to give are included in the financial statements as bequests and pledges receivable and contributions revenue of the appropriate net asset category. Future receipt of bequests and pledges receivable are expected to be collected each respective year as follows:

	Pledges	Bequests	Total
2018	$ 1,018,200	$ -	$ 1,018,200
2019	1,013,925	-	1,013,925
2020	4,083	-	4,083
2021	1,000	-	1,000
2022	-	221,000	221,000
Thereafter	-	88,000	88,000
Less present value discount	(56,690)	(15,826)	(72,516)
	$ 1,980,518	$ 293,174	$ 2,273,692

3. INVESTMENTS

As of December 31, 2017 and 2016, unrestricted, temporarily restricted and permanently restricted investments consist of the following:

December 31, 2017	Cost	Fair Value	Excess (Deficit) of Fair Value Over Cost
Cash and cash equivalents	$ 713,178	$ 716,003	$ 2,825
U.S. equity securities, mutual & exchange-traded funds	2,918,184	4,739,091	1,820,907
U.S. government obligations	97,135	103,104	5,969
U.S. corporate bonds	2,657,106	2,651,674	(5,432)
	$ 6,385,603	$ 8,209,872	$ 1,824,269

3. INVESTMENTS (Cont.)

December 31, 2016	Cost	Fair Value	Excess (Deficit) of Fair Value Over Cost
Cash and cash equivalents	$ 897,039	$ 899,473	$ 2,434
U.S. equity securities, mutual & exchange-traded funds	2,212,056	3,719,938	1,507,882
U.S. government obligations	92,683	98,741	6,058
U.S. corporate bonds	2,229,883	2,122,528	(107,355)
	$ 5,431,661	$ 6,840,680	$ 1,409,019

Investment income as of December 31, 2017 and 2016 consists of the following:

	2017	2016
Interest and dividends	$ 183,106	$ 164,623
Change in cash surrender value of life insurance	2,489	2,645
Net realized gain	235,774	137,999
Net change in unrealized gain	415,250	109,092
	836,619	414,359
Less: Investment fees	(21,506)	(20,137)
Total investment income, net	$ 815,113	$ 394,222

4. FAIR VALUE MEASUREMENTS

The following sets forth by level, within the fair value hierarchy, the Institute's assets and liabilities at fair value as of December 31, 2017 and 2016:

December 31, 2017	Fair Value (Level 1)	Fair Value (Level 2)	Fair Value (Level 3)
Assets			
Investments			
Cash and cash equivalents	$ 34,796	$ 681,207	$ -
U.S. equity securities, mutual & exchange-traded funds	4,739,090	-	-
U.S. government obligations	-	103,104	-
U.S. corporate bonds	-	2,651,675	-
	4,773,886	3,435,986	-

4. FAIR VALUE MEASUREMENTS (Cont.)

Other Assets			
Cash – operating	884,516	-	-
Split interest trusts:			
Cash and cash equivalents	102,209	8,250	-
U.S. corporate bonds	-	193,487	-
Equities and mutual funds	1,426,724	-	-
Beneficial interest in perpetual trust	-	-	1,718,546
Life insurance policies	-	-	112,801
	2,413,449	201,737	1,831,347
Total Assets	$ 7,187,335	$ 3,637,723	$ 1,831,347
Liabilities			
Split interest trusts – trustee	$ -	$ 30,296	$ -
Split interest trusts – non-trustee	-	1,070,089	-
Annuities payable	-	71,420	-
Total Liabilities	$ -	$ 1,171,805	$ -

December 31, 2016	Fair Value (Level 1)	Fair Value (Level 2)	Fair Value (Level 3)
Assets			
Investments			
Cash and cash equivalents	$ 194,595	$ 704,878	$ -
U.S. equity securities, mutual & exchange-traded funds	3,719,938	-	-
U.S. government obligations	-	98,741	-
U.S. corporate bonds	-	2,122,528	-
	3,914,533	2,926,147	-
Other Assets			
Cash – operating	361,144	-	-
Split interest trusts:			
Cash and cash equivalents	16,250	18,904	-
U.S. corporate bonds	-	45,997	-
Equities and mutual funds	584,124	-	-
Beneficial interest in perpetual trust	-	-	1,578,816
Life insurance policies	-	-	110,176
	961,518	64,901	1,688,992
Total Assets	$ 4,876,051	$ 2,991,048	$ 1,688,992

4. FAIR VALUE MEASUREMENTS (Cont.)

Liabilities			
Split interest trusts – trustee	$ -	$ 39,076	$ -
Split interest trusts – non-trustee	-	314,912	-
Annuities payable	-	74,669	-
Total Liabilities	$ -	$ 428,657	$ -

Level 3 Activity

The table below sets forth a summary of changes in the fair value of the Institute's level 3 assets for the year ended December 31, 2017.

	Cash Surrender Value of Life Insurance
Balance, beginning of year	$ 110,176
Realized gain	136
Increase in cash surrender value	2,489
Balance, end of year	$ 112,801

	Beneficial Interest in Perpetual Trust
Balance, beginning of year	$ 1,578,816
Unrealized gain	220,051
Distributions	(80,321)
Balance, end of year	$ 1,718,546

The table below sets forth a summary of changes in the fair value of the Institute's level 3 assets for the years ended December 31, 2016.

	Cash Surrender Value of Life Insurance
Balance, beginning of year	$ 107,667
Realized loss	(136)
Increase in cash surrender value	2,645
Balance, end of year	$ 110,176

	Beneficial Interest in Perpetual Trust
Balance, beginning of year	$ 1,577,369
Unrealized gain	83,117
Distributions	(81,670)
Balance, end of year	$ 1,578,816

5. SPLIT INTEREST TRUST AGREEMENTS

The Institute has a remainder interest in several charitable trusts which have been established by donors to provide income, generally for life, to designated beneficiaries. The remainder of the trust assets at maturity will be distributed to the Institute and other remainder beneficiaries for the purposes designated in the trust agreements. Each year, beneficiaries receive trust income or a percentage of the trust's fair market value. The trusts are separate legal entities created under the provisions of Section 664 of the IRC.

If the Institute is the trustee, the fair market value of the trust is recorded in the Institute's statement of financial position and a corresponding liability is recorded for the net present value of the required payments as specified in the agreement. A contribution is recorded for the difference between the two amounts in the year received. At December 31, 2017, the fair market value of the trusts was $136,891 with a corresponding liability of $30,296. At December 31, 2016, the fair market value of these trusts was $137,782 with a corresponding liability of $39,076.

If the Institute is not the trustee, the interest in the trust is recorded as the difference between the fair market value of the assets of the trust and the present value of required payments. At December 31, 2017, the net interest of the trusts was $523,690, which includes the fair market value of $1,593,779 and the corresponding liability of $1,070,089. At December 31, 2016, the net interest of these trusts was $212,580, which includes the fair market value of $527,492 and the corresponding liability of $314,912.

Any change in subsequent years in the fair market value of the trust assets or the required payment liability is recorded in the statement of activities as a change in the value of charitable trusts.

Trust assets and liabilities are stated at fair value. (Notes 1 and 4)

6. BENEFICIAL INTEREST IN PERPETUAL TRUST

The Institute is the beneficiary of an interest in a perpetual trust. The Institute is the sole recipient of the investment income from the trust. The income will be 5% to 8% of the average of the previous three years' fair market value of trust assets at December 31, paid at the trustee's discretion either annually or quarterly. The payments are restricted for research and education. The estimated fair value of the interest in the perpetual trust based on the fair market value of assets held in the trust was $1,718,546 and $1,578,816 at December 31, 2017 and 2016, respectively.

7. LIFE INSURANCE

The Institute is the beneficiary of life insurance policies with total death benefits of $144,841 and a cash surrender value of $112,801 and $110,176 as of December 31, 2017 and 2016, respectively. The increase of cash surrender value of $2,489 and $2,645 for the years ended December 31, 2017 and 2016, respectively, have been recorded in investment income in the accompanying statement of activity.

8. PROPERTY AND EQUIPMENT

Property and equipment at December 31, 2017 and 2016 are summarized by major classifications as follows:

	2017	2016
Land	$ 351,758	$ 351,758
Buildings and improvements	3,648,613	3,612,744
Furniture and equipment	1,544,620	1,485,724
Artwork	6,647	6,647
Specialized equipment	-	18,585
	5,551,638	5,475,458
	(3,882,702)	(3,753,217)
	$ 1,668,936	$ 1,722,241

Depreciation expense for the years ended December 31, 2017 and 2016 was $148,070 and $153,250, respectively.

9. ENDOWMENT FUNDS

Endowment funds and related income restrictions are as follows at December 31,

		2017	
Income Restriction	Unrestricted	Temporarily Restricted	Permanently Restricted
None	$ -	$ 72,917	$ 500,000
Education and research	-	292,402	4,138,600
Internship	-	27,706	272,500
	$ -	$ 393,025	$ 4,911,100

		2016	
Income Restriction	Unrestricted	Temporarily Restricted	Permanently Restricted
None	$ -	$ 65,394	$ 660,636
Education and research	-	220,332	4,113,957
Internship	-	45,900	282,500
	$ -	$ 331,626	$ 5,057,093

9. ENDOWMENT FUNDS (Cont.)

The Board of Trustees of the Institute has interpreted the Uniform Prudent Management of Institutional Funds Act (UPMIFA) as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the Institute classifies as permanently restricted net assets the original value of gifts donated to the permanent endowment. The unrealized gains and endowment investment income on funds not restricted by the donor are classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the organization in a manner consistent with the standard of prudence prescribed by UPMIFA. In accordance with UPMIFA, the organization considered the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

(1) The duration and preservation of the fund
(2) The purposes of the Institute and the donor-restricted endowment fund
(3) General economic conditions
(4) The possible effect of inflation and deflation
(5) The expected total return from income and the appreciation of investments
(6) Other resources of the Institute
(7) The investment policies of the Institute

Endowment net asset composition by type of fund as of December 31, 2017:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Donor-restricted - endowment funds	$ -	$ 393,025	$ 4,911,100	$ 5,231,208

Endowment net asset composition by type of fund as of December 31, 2016:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Donor-restricted - endowment funds	$ -	$ 331,626	$ 5,057,093	$ 5,388,719

9. ENDOWMENT FUNDS (Cont.)

Changes in endowment net assets for the year ended December 31, 2017:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets Beginning of year	$ -	$ 331,626	$ 5,057,093	$ 5,388,719
Investment return:				
Investment income and distributions from perpetual trust	-	153,016	-	153,016
Net gain/(loss) (realized and unrealized)	-	363,009	139,643	502,652
Total investment return	-	516,025	139,643	655,668
Contributions	-	-	-	-
Donor and Board releases from restrictions (Note 12)	-	(170,513)	(285,636)	(456,149)
Appropriation of endowment assets for expenditure	-	(284,113)	-	(284,113)
Endowment net assets End of year	$ -	$ 393,025	$ 4,911,100	$ 5,231,208

9. ENDOWMENT FUNDS (Cont.)

Changes in endowment net assets for the year ended December 31, 2016:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets Beginning of year	$ -	$ 545,183	$ 5,055,765	$ 5,600,948
Investment return:				
Investment income and distributions from perpetual trust	-	172,373	-	90,703
Net gain/(loss) (realized and unrealized)	-	132,932	1,328	134,260
Total investment return	-	305,305	1,328	224,963
Contributions	-	-	-	-
Appropriation of endowment assets for expenditure	-	(518,862)	-	(437,192)
Endowment net assets End of year	$ -	$ 331,626	$ 5,057,093	$ 5,388,719

Funds with Deficiencies

From time to time, the fair value of assets associated with individual donor restricted endowment funds may fall below the level that the donor or UPMIFA requires the Institute to retain as a fund of perpetual duration. There were no deficiencies of this nature as of December 31, 2017 or 2016.

Return Objectives and Risk Parameters

The Institute has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of the endowment assets. Under this policy, as approved by the Board of Trustees, the endowment assets are invested approximately 60% in equities and 40% in fixed income securities. The equity investments are either exchange traded funds or index mutual funds. The fixed income investments are intermediate term and include U.S. Government obligations as well as U.S. corporations rated not less than 'A' by recognized rating agencies. The Institute expects its endowment funds, over time, to provide an average rate of return of approximately 6% percent annually. Actual returns in any given year may vary from this amount.

9. ENDOWMENT FUNDS (Cont.)

Strategies Employed for Achieving Objectives

To satisfy its long-term rate-of-return objectives, the Institute 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).

Spending Policy and How the Investment Objectives Relate to Spending Policy

The Institute has a policy of appropriating for distribution each year a prudent portion of earnings from endowment assets. In establishing this policy, the Institute considered the long-term expected return on its endowment. Accordingly, over the long term, the Institute expects its spending policy to allow the Institute to conduct diabetes research. This is consistent with the Institute's objective to maintain the purchasing power of the endowment assets held in perpetuity as well as to provide additional real growth through new gifts. During the years ended December 31, 2017 and 2016 the Institute appropriated income earned from certain endowment funds that had accumulated for the past eight years. The income was used to fund research and operations.

10. BOARD DESIGNATED NET ASSETS

The Board has designated unrestricted net assets to be expended for the following purposes at December 31:

	2017	2016
Board designated		
Operating reserve	$ 2,659,712	$ 2,085,330

The 2017 increase in board designated net assets was primarily due to the release from restrictions totaling $456,149 (Note 12).

11. TEMPORARILY RESTRICTED NET ASSETS

Temporarily restricted net assets are available for the following purposes at December 31:

	2017	2016
Portion of income from endowment funds subject to a time restriction under UPMIFA	$ 72,917	$ 65,336
Portion of income from endowment funds subject to a time restriction & a purpose restriction under UPMIFA- research, education & internship	1,159,171	266,232
Operations – unrestricted upon collection of bequests & other receivables	2,273,692	1,656,090
Research, education & internship activities	1,084,423	426,023
Present value of remainder interests in trusts	630,285	311,287
Equipment purchases	12,937	12,937
	$ 5,233,425	$ 2,737,885

12. PERMANENTLY RESTRICTED NET ASSETS

Certain net assets are permanently restricted, with income thereon to be expended for the following purposes at December 31:

Donor	Income Restriction	2017	2016
Various	Unrestricted	$ -	$ 660,636
Burtness	Unrestricted	500,000	-
Burtness	Diabetes research	-	100,000
Burtness	Internship	-	25,000
Kroc	Education	50,000	50,000
Demott	Internship	10,000	10,000
Parsons	Internship	20,000	20,000
Close	Internship	20,000	20,000
Barker	Internship	222,500	222,500
McOmie	General research	2,370,054	2,370,141
Turner perpetual interest	General research & education	1,718,546	1,578,816
		$ 4,911,100	$ 5,057,093

12. PERMANENTLY RESTRICTED NET ASSETS (Cont.)

In 2017 the Burtness family granted permission to the Institute to release $285,636 of permanently restricted endowment principal of Burtness family contributions to Board designated net assets. In addition the Board and the Burtness family agreed to release the prior earnings not yet appropriated for expenditure on these funds in the amount of $170,513 to Board designated net assets (Note 9).

13. EMPLOYEE BENEFITS

The Institute maintains a defined contribution retirement plan for eligible employees with at least one year of employment. The plan is a qualified retirement plan under IRC Section 401(a). Contributions to the plan by the Institute are discretionary. Contributions to the plan for the years ended December 31, 2017 and 2016 were $71,605 and $74,788, respectively.

The Institute also offers a salary reduction plan as described in Section 403(b) of the IRC. Employees may contribute 100% of their salaries, subject to IRC limits of $18,000 employee deferral, $6,000 additional catch up if over the age of 50. Employees are eligible to participate as of their hire date.

The Institute pays all administrative costs of the above plans.

14. CUSTOMER AND CREDIT RISK CONCENTRATIONS

Financial instruments that potentially subject the Institute to credit risk consist principally of cash, cash held for investment, and accounts receivable.

The Institute maintains bank accounts at three financial institutions. Deposits at each institution are insured by the Federal Deposit Insurance Corporation up to $250,000. Cash balances held in brokerage accounts are insured by the Securities Investor Protection Corporation (SIPC) up to $250,000 per institution. The Institute's uninsured cash balances totaled approximately $839,400 at December 31, 2017.

One funding agency accounted for 23% of the outstanding balance in accounts receivable as of December 31, 2017 and 48% as of December 31, 2016.