AMERICAN DIABETES ASSOCIATION

Consolidated Financial Statements
and Consolidating Schedules

December 31, 2018

(With Independent Auditors' Report Thereon)

KPMG LLP
1676 International Drive
McLean, VA 22102

Independent Auditors' Report

The Board of Directors
American Diabetes Association:

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of American Diabetes Association and its subsidiaries, which comprise the consolidated balance sheets as of December 31, 2018, 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, 2018 and the results of their operations and their cash flows for the year then ended in accordance with U.S. generally accepted accounting principles.

KPMG

Emphasis of Matter

As discussed in Note 3(m) to the consolidated financial statements, in 2018 the American Diabetes Association and its subsidiaries adopted new accounting guidance, Accounting Standards Update (ASU) 2016-14, *Presentation of Financial Statements of Not-for-Profit Entities*. Our opinion is not modified with respect to this matter.

Report on Summarized Comparative Information

We have previously audited the American Diabetes Association and its subsidiaries' 2017 consolidated financial statements, and we expressed an unmodified audit opinion on those audited consolidated financial statements in our report dated May 29, 2018. In our opinion, the summarized comparative information presented herein as of and for the year ended December 31, 2017 is consistent, in all material respects, with the audited consolidated financial statements from which it has been derived before the adjustments to adopt ASU 2016-14. As part of our audit of the 2018 consolidated financial statements, we also audited the adjustments described in Note 3(m) that were applied to adopt ASU 2016-14 retrospectively in the 2017 consolidated financial statements. In our opinion, such adjustments are appropriate and have been properly applied.

Other Matter

Our audit was conducted for the purpose of forming opinions on the consolidated financial statements as a whole. The supplementary information included in schedules 1 and 2 is presented for purposes of additional analysis and are not a required part of the basic 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 statement 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 relation to the consolidated financial statements as a whole.

KPMG LLP

McLean, Virginia
May 28, 2019

AMERICAN DIABETES ASSOCIATION

Consolidated Balance Sheet

December 31, 2018
(with comparative information as of December 31, 2017)

(In thousands of dollars)

Assets		**2018**	**2017**
Cash and cash equivalents	$	10,720	9,472
Investments (notes 5 and 6)		50,213	52,945
Accounts receivable, net (notes 7 and 18)		9,768	10,128
Inventory and supplies, net		2,476	2,296
Prepaid expenses and other assets		2,985	3,377
Contributions receivable, net (note 8)		44,111	31,722
Fixed assets, net (note 9)		13,823	16,095
Interest in perpetual trusts (note 6)		9,687	10,431
Total assets	$	143,783	136,466
Liabilities and Net Assets			
Accounts payable and accrued liabilities (notes 15 and 17)	$	24,383	25,682
Research grants payable		23,511	26,898
Deferred revenues		9,792	10,463
Total liabilities		57,686	63,043
Net assets (note 10):			
Without donor restrictions		(6,773)	(12,831)
With donor restrictions		92,870	86,254
Total net assets		86,097	73,423
Total liabilities and net assets	$	143,783	136,466

See accompanying notes to consolidated financial statements.

AMERICAN DIABETES ASSOCIATION

Consolidated Statement of Activities

Year ended December 31, 2018
(with summarized information for the year ended December 31, 2017)

(In thousands of dollars)

	Without donor restrictions	With donor restrictions	2018 Total	2017 Total
Revenue:				
Contributions and grants:				
Donations	$ 30,996	36,431	67,427	54,713
Special events	21,631	1,989	23,620	30,435
Less costs of direct benefits to donors	(3,938)	—	(3,938)	(4,985)
Bequests	18,845	14,681	33,526	23,275
Federated and nonfederated organizations	4,309	132	4,441	5,287
Total contributions and grants	71,843	53,233	125,076	108,725
Fees from exchange transactions:				
Subscriptions and other income from periodicals	12,665	—	12,665	13,259
Sales of materials	2,743	—	2,743	2,991
Program service fees	16,256	—	16,256	16,980
Investment income (note 5)	1,373	(737)	636	5,329
Miscellaneous revenues	3,891	—	3,891	2,956
Total fees from exchange transactions	36,928	(737)	36,191	41,515
Net assets released from restrictions	45,880	(45,880)	—	—
Total revenue	154,651	6,616	161,267	150,240
Expenses (note 13):				
Program activities:				
Research	37,853	—	37,853	49,098
Information	45,015	—	45,015	48,973
Advocacy and public awareness	25,200	—	25,200	31,055
Total program activities	108,068	—	108,068	129,126
Supporting services:				
Management and general	9,043	—	9,043	10,710
Fundraising	31,482	—	31,482	35,779
Total supporting services	40,525	—	40,525	46,489
Total expenses	148,593	—	148,593	175,615
Change in net assets	6,058	6,616	12,674	(25,375)
Net assets, beginning of year	(12,831)	86,254	73,423	98,798
Net assets, end of year	$ (6,773)	92,870	86,097	73,423

See accompanying notes to consolidated financial statements.

AMERICAN DIABETES ASSOCIATION

Consolidated Statement of Functional Expenses

Year ended December 31, 2018
(with summarized information for the year ended December 31, 2017)

(In thousands of dollars)

	Program activities				Supporting services				
	Research	**Information**	**Advocacy and public awareness**	**Total**	**Management and general**	**Fundraising**	**Total**	**2018 Total**	**2017 Total**
Grants	$ 26,288	149	57	26,494	—	—	—	26,494	36,656
Employee costs	3,147	17,922	13,264	34,333	5,363	12,703	18,066	52,399	60,276
Professional fees	1,608	6,546	2,839	10,993	1,066	3,522	4,588	15,581	17,838
Supplies	44	2,705	218	2,967	38	183	221	3,188	3,928
Telecommunications	91	503	378	972	129	360	489	1,461	1,746
Postage and shipping	213	1,523	1,078	2,814	65	3,330	3,395	6,209	7,475
Occupancy cost	441	4,820	1,765	7,026	610	1,689	2,299	9,325	9,987
Equipment rental and maintenance	47	407	277	731	73	258	331	1,062	1,315
Printing and publications	1,409	4,825	2,120	8,354	205	5,986	6,191	14,545	15,887
Travel	104	988	601	1,693	39	511	550	2,243	2,416
Conferences and meetings	3,833	1,144	469	5,446	7	108	115	5,561	6,295
Data processing	143	714	208	1,065	—	691	691	1,756	1,789
Depreciation and amortization	233	1,323	1,011	2,567	350	973	1,323	3,890	4,110
Miscellaneous	252	1,446	915	2,613	1,098	1,168	2,266	4,879	5,897
Total expenses	$ 37,853	45,015	25,200	108,068	9,043	31,482	40,525	148,593	175,615
Costs of direct benefits to donors								3,938	4,985
Total expenses and costs of direct benefits to donors								$ 152,531	180,600

See accompanying notes to consolidated financial statements.

AMERICAN DIABETES ASSOCIATION

Consolidated Statement of Cash Flows

Year ended December 31, 2018
(with comparative information for the year ended December 31, 2017)

(In thousands of dollars)

		2018	2017
Cash flows from operating activities:			
Change in net assets	$	12,674	(25,375)
Adjustments to reconcile change in net assets to net cash provided by (used in) operating activities:			
Depreciation and amortization		3,890	4,110
Net unrealized and realized loss (gain) on investments		2,593	(1,596)
Loss on disposal of assets		4	97
Provisions for doubtful receivables and obsolete inventory		977	2,648
Adjustments for changes in operating assets and liabilities:			
(Increase) decrease in accounts receivable		(140)	285
Increase in inventory and supplies		(333)	(189)
Decrease in prepaid expenses and other assets		392	1,603
(Increase) decrease in contributions receivable		(12,713)	7,684
(Decrease) in accounts payable and accrued liabilities		(1,299)	(3,478)
(Decrease) increase in research grants payable		(3,387)	7,910
Decrease in deferred revenues		(671)	(532)
Net cash provided by (used in) operating activities		1,987	(6,833)
Cash flows from investing activities:			
Purchases of investments		(38,160)	(44,338)
Sales or maturities of investments		39,043	43,539
Proceeds from sale of fixed assets		9	5
Purchase of fixed assets		(1,631)	(1,523)
Net cash used in investing activities		(739)	(2,317)
Net increase (decrease) in cash and cash equivalents		1,248	(9,150)
Cash and cash equivalents, beginning of year		9,472	18,622
Cash and cash equivalents, end of year	$	10,720	9,472

See accompanying notes to consolidated financial statements.

(1) Consolidation and Organization

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

The American Diabetes Association and the RF are generally 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. PTHC is generally exempt from income taxes under Section 501(c)(2) of the Code. These entities are subject to taxation on any net unrelated business income and 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, 2018, 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.

The Tax Cuts and Jobs Act (the Tax Act) was signed into law on December 22, 2017. The Tax Act 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 has determined that the new law will not have a significant impact on the Association’s 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.

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(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.

The net assets and revenues, gains, and losses of the Association are classified based on the existence or absence of donor-imposed restrictions. Accordingly, net assets of the Association are classified and reported as follows:

Without donor restrictions – Net assets that are not subject to donor-imposed stipulations.

With donor restrictions – Net assets with donor restrictions carry specific donor-imposed stipulations that will be met either by actions of the Association and/or the passage of time. Other net assets with donor restrictions include net assets with stipulations that require the corpus of the gifts to be retained permanently with only the income to be used to support operations or another specified purpose.

(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) 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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(e) 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 with donor restrictions, otherwise such donations are reported as contributions without donor restrictions.

(f) 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 contributions with donor restrictions 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, net assets with donor restrictions are reclassified to net assets without donor restrictions and are reported in the consolidated statement of activities as net assets released from restrictions.

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 1.4% to 3.0%. 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.

(g) 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.

The Association's share of split-interest agreements is included in investments, contributions receivable, or interest in perpetual trusts. Assets of approximately $19,660,000 and $21,742,000 are reported on the consolidated balance sheets as of December 31, 2018 and 2017, respectively. When

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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 2018 and 2017 was 3.0% and 2.7%, respectively.

Amounts payable to beneficiaries, gift annuities payable, and pooled income fund liabilities of approximately $1,061,000 and $911,000 are reported as accrued liabilities or deferred revenues on the consolidated balance sheets as of December 31, 2018 and 2017, respectively.

(h) 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.

(i) 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.

(j) 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.

(k) Functional Allocation of Expenses

Expenses have been summarized on a functional basis in the consolidated statement of activities. Expenses that are specifically associated with a programmatic activity or supporting service are allocated to that activity. Employee costs are allocated based on employee time attributed to each programmatic activity or supporting service. Costs associated with the development and distribution of mail pieces that include a call to action along with fundraising component, as described further in note 13, are allocated based on the proportion of space used for each purpose. Overhead costs are allocated based on a weighted average of employee costs attributed to each programmatic activity or supporting service.

(l) Comparative Financial Statements

The consolidated statements of activities and functional expenses include certain summarized comparative information for the year ended December 31, 2017. 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, 2017, from which the summarized information was derived.

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(m) Recent Accounting Pronouncements

Not-for-Profit Financial Statement Presentation

In August 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update No. 2016-14 (ASU 2016-14), *Presentation of Financial Statements of Not-for-Profit Entities*. This guidance is intended to improve the net asset classification requirements and the information presented in the financial statements and notes about a not-for-profit entity's liquidity, financial performance, and cash flows. Main provisions of this guidance include: presentation of two classes of net assets versus the previously required three; recognition of capital gifts for construction as a net asset without donor restrictions when the associated long-lived asset is placed in service; and recognition of underwater endowment funds as a reduction in net assets with donor restrictions. The guidance also requires enhanced disclosures for board designated amounts, composition of net assets without donor restrictions, liquidity, and the presentation of expenses by both their natural and functional classification.

The Association adopted the provisions of ASU 2016-14 in 2018 and has applied the provisions retrospectively as required by the standard. A presentation of net assets as previously reported as of December 31, 2017 follows:

		Presentation under ASU 2016-14		
	As previously presented	Without donor restrictions	With donor restrictions	Total
Net assets:				
Unrestricted	$ (12,831)	(12,831)	—	(12,831)
Temporarily restricted	71,286	—	71,286	71,286
Permanently restricted	14,968	—	14,968	14,968
Total net assets	$ 73,423	(12,831)	86,254	73,423
Net assets as restated in accordance with ASU 2016-14		$ (12,831)	86,254	73,423

(4) Financial Assets and Liquidity Reserves

The Association funds its operations through contributions and grants and through fees from exchange transactions. The Association maintains a policy of structuring its financial assets to be available as its general expenditures, liabilities, and other obligations come due. Cash required to meet operating needs is invested in short term accounts.

The following is a reconciliation of the Association's financial assets as of December 31, 2018 to financial assets available to fund the Association's general expenditures for the following fiscal year. General expenditures include all programmatic and supporting operating expenditures.

Cash and cash equivalents	$	10,720
Investments		50,213
Accounts receivable, net		9,768
Contributions receivable, net		44,111
Total financial assets at December 31, 2018		114,812
Less financial assets unavailable for general expenditure within one year:		
Perpetual and term endowments		(22,635)
Accounts receivable due after one year, net		(7,083)
Contributions receivable due after one year, net		(15,011)
Donor restricted net assets that are not expected to be spent within one year		(19,806)
Financial assets available to meet cash needs for general expenditures within one year	$	50,277

(5) Investments

Investments as of December 31, 2018 and 2017, consist of the following (in thousands):

		2018	2017
U.S. government securities	$	14,686	16,175
Real estate		12,818	12,818
Fixed-income bonds		6,873	7,421
Fixed-income mutual funds		4,759	4,854
Corporate equities		4,662	5,142
Equity mutual funds		3,903	4,315
Money market funds		2,512	2,220
Total investments	$	50,213	52,945

Investments as of December 31, 2018 and 2017, include gift annuity investments of approximately $2,661,000 and $2,931,000, respectively, and the fair value of gift annuity obligations under those agreements was approximately $1,061,000 and $911,000, 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, 2018 and 2017, includes (in thousands):

		2018	2017
Property rental income, net	$	1,536	1,977
Net realized and unrealized (losses) gains		(2,593)	1,596
Interest and dividends		1,931	1,989
Investment fees		(238)	(233)
Total investment income, net	$	636	5,329

(6) 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 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, 2018 (in thousands):

	Total	Level 1	Level 2	Level 3
Financial assets:				
Investments:				
Fixed-income bonds	$ 6,873	—	6,873	—
U.S. government securities	14,686	—	14,686	—
Fixed-income mutual funds	4,759	4,759	—	—
Equity mutual funds	3,903	3,903	—	—
Money market funds	2,512	2,512	—	—
Corporate equities	4,662	4,662	—	—
Interest in perpetual trusts	9,687	—	—	9,687
Funds held in remainder trusts	7,312	—	—	7,312
Financial liabilities:				
Split-interest obligations	$ 1,061	—	1,061	—

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, 2017 (in thousands):

	Total	Level 1	Level 2	Level 3
Financial assets:				
Investments:				
Fixed-income bonds	$ 7,421	—	7,421	—
U.S. government securities	16,175	—	16,175	—
Fixed-income mutual funds	4,854	4,854	—	—
Equity mutual funds	4,315	4,315	—	—
Money market funds	2,220	2,220	—	—
Corporate equities	5,142	5,142	—	—
Interest in perpetual trusts	10,431	—	—	10,431
Funds held in remainder trusts	8,380	—	—	8,380
Financial liabilities:				
Split-interest obligations	$ 911	—	911	—

Changes in perpetual trusts and funds held in remainder trusts for the years ended December 31, 2018 and 2017, are as follows (in thousands):

		Perpetual trusts	Funds held in remainder trusts
Balance, December 31, 2016	$	9,806	10,871
New trusts		—	501
Investment gains		988	1,093
Distributions		(363)	(4,085)
Balance, December 31, 2017		10,431	8,380
New trusts		—	290
Investment losses		(744)	(780)
Distributions		—	(578)
Balance, December 31, 2018	$	9,687	7,312

(7) 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 $1,603,000 and $991,000 as of December 31, 2018 and 2017, respectively. Of the allowance amount, $808,000 and $696,000 as of December 31, 2018 and 2017, respectively, relate to the land rental (note 18).

(8) Contributions Receivable

Contributions receivable consist of the following amounts due as of December 31, 2018 and 2017 (in thousands):

		2018	2017
Within one year	$	32,243	23,882
In one to five years		7,706	2,291
Greater than five years		400	—
Total contributions receivable		40,349	26,173
Less:			
Allowance for doubtful accounts		(3,143)	(2,753)
Present value discount		(407)	(78)
Subtotal		36,799	23,342
Funds held in remainder trusts		7,312	8,380
Contributions receivable, net	$	44,111	31,722

(9) Fixed Assets

Fixed assets consist of the following as of December 31, 2017 and 2016 (in thousands):

		2018	2017
Land	$	4	4
Leasehold improvements		6,328	6,352
Software		21,327	20,728
Furniture, fixtures, and equipment		20,074	19,209
Total fixed assets		47,733	46,293
Less accumulated depreciation and amortization		(33,910)	(30,198)
Fixed assets, net	$	13,823	16,095

(10) Net Assets

As of December 31, 2018 and 2017, net assets consisted of the following:

		2018			2017		
		Without donor restrictions	With donor restrictions	Total	Without donor restrictions	With donor restrictions	Total
Permanent endowments	$	—	4,502	4,502	—	4,537	4,537
Perpetual trusts held by third parties		—	9,687	9,687	—	10,431	10,431
Total net assets restricted in perpetuity		—	14,189	14,189	—	14,968	14,968
Term endowments		—	18,133	18,133	—	18,362	18,362
Total net assets subject to spending rules		—	32,322	32,322	—	33,330	33,330
Net assets with donor restrictions available for:							
Research		—	31,878	31,878	—	32,330	32,330
Information		—	14,835	14,835	—	4,242	4,242
Advocacy		—	1,475	1,475	—	2,370	2,370
Sponsorship for fundraising activities		—	1,659	1,659	—	2,529	2,529
Future periods (otherwise not restricted)		—	10,701	10,701	—	11,453	11,453
Undesignated		(6,773)	—	(6,773)	(12,831)	—	(12,831)
Total net assets	$	(6,773)	92,870	86,097	(12,831)	86,254	73,423

(11) Endowment

The Association's endowment consists of 49 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 and the term endowment funds are reported as net assets with donor restrictions 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. During these periods, the Association does not spend income derived from underwater endowment funds but rather uses that income to replenish the corpus.

The following provides information about donor-restricted endowment funds that are below the historic dollar value of the fund as of December 31:

		2018	2017
Fair value of endowment funds that are below historic dollar value	$	9,817	—
Original endowment gift		9,903	—
Amount of deficiency	$	(86)	—

Changes in endowment net assets for the years ended December 31, 2018 and 2017, are as follows (in thousands):

		Net assets without donor restrictions	Net assets with donor restrictions	Total
Endowment net assets, December 31, 2016	$	—	22,534	22,534
Investment return:				
Investment income		2,052	334	2,386
Net appreciation		—	171	171
Contributions		—	182	182
Appropriation for expenditure		(2,052)	(322)	(2,374)
Endowment net assets, December 31, 2017		—	22,899	22,899
Investment return:				
Investment income		1,536	398	1,934
Net depreciation		—	(484)	(484)
Contributions		—	5	5
Appropriation for expenditure		(1,536)	(183)	(1,719)
Endowment net assets, December 31, 2018	$	—	22,635	22,635

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., medical services provided in conjunction with the Association's program activities, primarily camps held for children with diabetes, and corporate communication services. Contributed services for occupancy are recorded in occupancy expenses. The Association recognized approximately $3,241,000 and $2,696,000, in donated services provided in conjunction with the Association's activities during the years ended December 31, 2018 and 2017, 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 $2,198,000 and $2,638,000 for the years ended December 31, 2018 and 2017, 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, 2018 and 2017, were allocated as follows (in thousands):

		2018	2017
Advocacy and public awareness	$	4,844	5,680
Management and general		306	925
Fundraising		13,477	14,516
Total joint costs	$	18,627	21,121

(Continued)

(14) Pension Plan

The Association has defined-contribution pension plans that cover most salaried employees who have reached the age of 21 and completed one year of service. Pension expense for the years ended December 31, 2018 and 2017, was approximately $1,451,000 and $1,421,000, 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 $8,807,000 and $9,629,000 in 2018 and 2017, respectively.

The liability as of December 31, 2018 and 2017, was approximately $375,000 and $572,000, respectively, and is included in accounts payable and accrued liabilities in the consolidated balance sheets. Benefit expense under this plan was approximately $4,652,000 and $6,057,000 for the years ended December 31, 2018 and 2017, respectively. The benefit expense includes claims paid and changes to the reserve for future claims.

(16) Line of Credit

The Association had a $10,000,000 unsecured line of credit with a bank at interest rates of the London Interbank Offered Rate (LIBOR) plus 2.15% points through July 31, 2018. There was no outstanding balance on the line of credit as of December 31, 2017.

On November 18, 2018, the PTHC obtained a new revolving line of credit with a bank. The line of credit bears interest at the rate of LIBOR plus 2.0%, is secured by real property of PTHC and is guaranteed by the Association. The line of credit expires on November 28, 2019. The Association expects to renew the line of credit each year. There was no outstanding balance as of December 31, 2018. Interest and fees for the years ended December 31, 2018 and 2017 were approximately $15,000 and $38,000, respectively.

The line of credit is available for working capital and requires that the Association maintain compliance with certain financial covenants. The Association was in compliance with these covenants as of December 31, 2018.

(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, 2018, the future minimum lease payments under operating leases with noncancelable lease terms in excess of one year were (in thousands):

Year ending December 31:		
2019	$	6,341
2020		5,053
2021		4,699
2022		4,174
2023		3,656
2024 and thereafter		25,088
Total minimum lease payments	$	49,011

Rent expense totaled approximately $5,545,000 and $6,238,000 for the years ended December 31, 2018 and 2017, respectively.

(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, 2018, the future minimum lease payments due to the Association under these leases were (in thousands):

Year ending December 31:		
2019	$	1,634
2020		1,643
2021		1,240
2022		1,225
2023		1,268
2024 and thereafter		39,444
Total minimum lease receipts	$	46,454

The accumulated difference between the rental income recognized and the straight-line value of the leases was approximately $7,871,000 and $7,775,000 as of December 31, 2018 and 2017, 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 $808,000 and $696,000 as of December 31, 2018 and 2017, respectively.

(19) Subsequent Events

For the year ended December 31, 2018, the Association has evaluated subsequent events through May 28, 2019, the date the consolidated financial statements were available to be issued, and determined that no items required disclosure.

Schedule 1

AMERICAN DIABETES ASSOCIATION

Consolidating Schedule – Balance Sheet

December 31, 2018

(In thousands of dollars)

Assets		American Diabetes Association	Research Foundation	Property Title Holding Corp	Intercompany Eliminations	Consolidated Association
Cash and cash equivalents	$	10,600	120	—	—	10,720
Investments		50,213	—	12,818	(12,818)	50,213
Intercompany receivables		6,480	50,215	—	(56,695)	—
Accounts receivable, net		2,530	—	7,238	—	9,768
Inventory and supplies, net		2,476	—	—	—	2,476
Prepaid expenses and other assets		2,985	—	—	—	2,985
Contributions receivable, net		43,752	359	—	—	44,111
Fixed assets, net		13,823	—	—	—	13,823
Interest in perpetual trusts		9,608	79	—	—	9,687
Total assets	$	142,467	50,773	20,056	(69,513)	143,783
Liabilities and Net Assets						
Accounts payable and accrued liabilities	$	24,294	—	89	—	24,383
Research grants payable		—	23,511	—	—	23,511
Intercompany payables		50,215	—	6,480	(56,695)	—
Deferred revenues		9,123	—	669	—	9,792
Total liabilities		83,632	23,511	7,238	(56,695)	57,686
Net assets:						
Without donor restrictions		(6,773)	—	—	—	(6,773)
With donor restrictions		65,608	27,262	12,818	(12,818)	92,870
Total net assets		58,835	27,262	12,818	(12,818)	86,097
Total liabilities and net assets	$	142,467	50,773	20,056	(69,513)	143,783

See accompanying independent auditors' report.

Schedule 2

AMERICAN DIABETES ASSOCIATION

Consolidating Schedule – Statement of Activities

Year ended December 31, 2018

(In thousands of dollars)

	American Diabetes Association	Research Foundation	Property Title Holding Corp	Intercompany Eliminations	Consolidated Association
Revenue:					
Contributions and grants:					
Donations	$ 64,912	2,515	—	—	67,427
Special events, net	19,682	—	—	—	19,682
Bequests	31,745	1,781	—	—	33,526
Federated and nonfederated organizations	4,335	106	—	—	4,441
Total contributions and grants	120,674	4,402	—	—	125,076
Fees from exchange transactions:					
Subscriptions and periodicals	12,665	—	—	—	12,665
Sale of materials	2,743	—	—	—	2,743
Program service fees	16,256	—	—	—	16,256
Investment income (loss)	(898)	(2)	1,536	—	636
Miscellaneous revenues	3,695	—	196	—	3,891
Total fees from exchange transactions	34,461	(2)	1,732	—	36,191
Intercompany revenues	2,424	12,910	—	(15,334)	—
Total revenue	157,559	17,310	1,732	(15,334)	161,267
Expenses:					
Program activities	80,959	27,109	—	—	108,068
Management and general	9,043	—	—	—	9,043
Fundraising	31,482	—	—	—	31,482
Intercompany expenses	12,910	692	1,732	(15,334)	—
Total expenses	134,394	27,801	1,732	(15,334)	148,593
Change in net assets	23,165	(10,491)	—	—	12,674
Net assets, beginning of year	35,670	37,753	12,818	(12,818)	73,423
Net assets, end of year	$ 58,835	27,262	12,818	(12,818)	86,097

See accompanying independent auditors' report.