

**AMERICAN ACADEMY OF FAMILY  
PHYSICIANS FOUNDATION AND SUBSIDIARY  
YEARS ENDED DECEMBER 31, 2012 AND 2011**



**HOUSE PARK DOBRATZ & WIEBLER, P.C.**  
CERTIFIED PUBLIC ACCOUNTANTS

**AMERICAN ACADEMY OF FAMILY  
PHYSICIANS FOUNDATION AND SUBSIDIARY**

YEARS ENDED DECEMBER 31, 2012 AND 2011

CONTENTS

	Page
Independent Auditors' Report	1
Consolidated Financial Statements:	
Statements of Financial Position	2
Statements of Activities and Changes in Net Assets	3
Statements of Cash Flows	4
Notes to Consolidated Financial Statements	5-21
Independent Auditors' Report on Supplemental Information	22
Consolidating Statement of Financial Position	23
Consolidating Statement of Activities	24
Consolidating Statement of Cash Flows	25



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**INDEPENDENT AUDITORS' REPORT**

To the Board of Trustees of  
American Academy of Family Physicians Foundation and Subsidiary  
Leawood, Kansas

**Report on the Financial Statements**

We have audited the accompanying consolidated financial statements of American Academy of Family Physicians Foundation and Subsidiary (a nonprofit organization), which comprise the statements of financial position as of December 31, 2012 and 2011, and the related statements of activities, functional expenses, and cash flows for the years then ended, and the related notes to the financial statements. The prior year summarized comparative information in the consolidated statement of activities has been derived from the Organization's 2011 financial statements. We did not audit the financial statements of AAFP Insurance Services, Inc., a wholly-owned subsidiary, which statements reflect total assets of \$4,730,143 and \$4,830,986 as of December 31, 2012 and 2011, respectively, and total revenues of \$3,655,838 and \$3,514,842, respectively, for the years then ended. Those statements were audited by other auditors whose report has been furnished to us, and our opinion, insofar as it relates to the amounts included for AAFP Insurance Services, Inc., is based solely on the report of the other auditors.

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

Management is responsible for the preparation and fair presentation of these financial statements in accordance with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

**Auditors' Responsibility**

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with U.S. generally accepted auditing standards. 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 presentation of the financial statements.

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

**Opinion**

In our opinion, based on our audits and the report of other auditors, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of American Academy of Family Physicians Foundation and Subsidiary as of December 31, 2012 and 2011, and the changes in their consolidated net assets and cash flows for the years then ended in accordance with U.S. generally accepted accounting principles.

*House Park Dobratz & Wiebler, P.C.*

Kansas City, Missouri  
May 19, 2013

**AMERICAN ACADEMY OF FAMILY  
PHYSICIANS FOUNDATION AND SUBSIDIARY**

**CONSOLIDATED STATEMENTS OF FINANCIAL POSITION**

DECEMBER 31, 2012 AND 2011

**ASSETS**

	<u>2012</u>	<u>2011</u>
Cash and cash equivalents (Note 4)	\$ 12,895,225	\$ 12,909,997
Accounts receivable (Note 10)	847,252	850,601
Beneficial interest in trust assets (Note 3)	36,321	34,377
Prepaid expenses	149,368	162,772
Investments at fair value (Notes 2, 3 and 4)	12,003,054	10,754,996
Deferred income taxes (Note 7)	6,834	--
Office equipment, furniture and fixtures, net of accumulated depreciation of \$721,416 and \$672,867 as of December 31, 2012 and 2011, respectively	<u>90,816</u>	<u>132,133</u>
	<u>\$ 26,028,870</u>	<u>\$ 24,844,876</u>

**LIABILITIES AND NET ASSETS**

<b>Liabilities:</b>		
Accounts payable (Note 10)	\$ 4,956,458	\$ 4,549,233
Deferred revenue and advances (Note 11)	5,222,911	5,915,705
Deferred income taxes (Note 7)	--	5,564
Liabilities under split-interest agreements (Note 3)	56,986	57,642
Federal and state income taxes payable (Note 7)	28,177	25,331
Grant awards payable	<u>380,434</u>	<u>321,927</u>
Total liabilities	<u>10,644,966</u>	<u>10,875,402</u>
<b>Commitments (Notes 8 and 12)</b>		
<b>Net assets:</b>		
Unrestricted:		
Undesignated	3,498,668	3,097,154
Equity in office equipment, furniture and fixtures	24,696	39,843
Board-designated (Note 4)	<u>9,293,758</u>	<u>8,402,801</u>
Total unrestricted	12,817,122	11,539,798
Temporarily restricted (Note 4)	1,035,077	1,028,631
Permanently restricted (Note 4)	<u>1,531,705</u>	<u>1,401,045</u>
Total net assets	<u>15,383,904</u>	<u>13,969,474</u>
	<u>\$ 26,028,870</u>	<u>\$ 24,844,876</u>

See notes to consolidated financial statements.

**AMERICAN ACADEMY OF FAMILY  
PHYSICIANS FOUNDATION AND SUBSIDIARY**

**CONSOLIDATED STATEMENTS OF ACTIVITIES AND  
CHANGES IN NET ASSETS**

YEAR ENDED DECEMBER 31, 2012  
(With comparative totals for the year ended December 31, 2011)

	2012		
	<u>American Academy of Family Physicians Foundation</u>		
	<u>Unrestricted</u>	<u>Temporarily restricted</u>	<u>Permanently restricted</u>
Revenues and support:			
Insurance revenues	--	--	--
Individual donations (Note 10)	\$ 448,439	\$ 211,558	\$ 32,950
Corporate and chapter support	1,154,700	--	35,000
Grants	49,656	3,605,944	--
Special events, net of direct expenses of \$38,040 and \$23,622 in 2012 and 2011, respectively	42,089	11,616	--
Investment income (loss) (Notes 2 and 3)	1,064,567	44,521	62,710
Other	--	--	--
Net assets released from restrictions, satisfaction of donor stipulations (Note 4)	<u>3,867,193</u>	<u>( 3,867,193)</u>	<u>          </u>
Total revenues and support	<u>6,626,644</u>	<u>6,446</u>	<u>130,660</u>
Expenses:			
Board, general staff and administration	504,207	--	--
Family Medicine Philanthropic Consortium	109,915	--	--
Center for the History of Family Medicine	200,288	--	--
Grant awards and administration	1,216,796	--	--
Family Medicine Cares	168,147	--	--
Individual development	624,984	--	--
Professional and corporate affairs	211,065	--	--
Communications and public relations	--	--	--
Programs, other	1,371,396	--	--
Peers for Progress (Note 11)	1,990,471	--	--
Income taxes (Note 7)	<u>--</u>	<u>--</u>	<u>--</u>
Total expenses (Note 6)	<u>6,397,269</u>	<u>--</u>	<u>--</u>
Change in net assets	229,375	6,446	130,660
Equity in income of subsidiary	1,047,949	--	--
Transfers	--	--	--
Net assets, beginning of year	<u>11,539,798</u>	<u>1,028,631</u>	<u>1,401,045</u>
Net assets, end of year	<u>\$ 12,817,122</u>	<u>\$ 1,035,077</u>	<u>\$ 1,531,705</u>

<u>2012</u>		<u>2011</u>	
<u>AAFP</u> <u>Foundation</u> <u>total</u>	<u>AAFP</u> <u>Insurance</u> <u>Services, Inc.</u>	<u>Consolidated</u> <u>totals</u>	<u>Consolidated</u> <u>totals</u>
--	\$ 3,655,324	\$ 3,655,324	\$ 3,494,191
\$ 692,947	--	692,947	626,717
1,189,700	--	1,189,700	1,328,840
3,655,600	--	3,655,600	3,420,279
53,705	--	53,705	25,833
1,171,798	--	1,171,798	( 148,585)
--	514	514	20,651
--	--	--	--
<u>6,763,750</u>	<u>3,655,838</u>	<u>10,419,588</u>	<u>8,767,926</u>
504,207	1,770,237	2,274,444	2,139,448
109,915	--	109,915	107,368
200,288	--	200,288	179,889
1,216,796	--	1,216,796	1,248,578
168,147	--	168,147	30,062
624,984	174,499	799,483	880,475
211,065	8,255	219,320	190,343
--	17,849	17,849	38,682
1,371,396	--	1,371,396	911,077
1,990,471	--	1,990,471	2,049,597
--	637,049	637,049	622,072
<u>6,397,269</u>	<u>2,607,889</u>	<u>9,005,158</u>	<u>8,397,591</u>
366,481	1,047,949	1,414,430	370,335
1,047,949	( 1,047,949)	--	--
--	--	--	--
<u>13,969,474</u>	<u>--</u>	<u>13,969,474</u>	<u>13,599,139</u>
<u>\$ 15,383,904</u>	<u>\$ --</u>	<u>\$ 15,383,904</u>	<u>\$ 13,969,474</u>

See notes to consolidated financial statements.

**AMERICAN ACADEMY OF FAMILY  
PHYSICIANS FOUNDATION AND SUBSIDIARY**

**CONSOLIDATED STATEMENTS OF CASH FLOWS**

YEARS ENDED DECEMBER 31, 2012 AND 2011

	<u>2012</u>	<u>2011</u>
Reconciliation of change in net assets to net cash provided by operating activities:		
Cash flows from operating activities:		
Change in net assets/net income	\$ 1,414,430	\$ 370,335
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation	61,588	56,186
Realized gains	( 269,315)	( 82,300)
Unrealized (gains) losses	( 673,182)	396,863
Change in value of split-interest agreements	( 9,428)	4,001
Change in operating assets and liabilities:		
Accounts receivable	3,349	77,992
Prepaid expenses	13,404	( 92,325)
Accounts payable	407,225	( 1,043,976)
Deferred revenue and advances	( 692,794)	3,715,791
Deferred income taxes	( 12,398)	( 1,328)
Federal and state income taxes payable	2,846	29,557
Grant awards payable	<u>58,507</u>	<u>( 45,015)</u>
Net cash provided by operating activities	<u>304,232</u>	<u>3,385,781</u>
Cash flows from investing activities:		
Purchase of office equipment, furniture and fixtures	( 20,271)	( 44,083)
Purchase of investments	<u>( 298,733)</u>	<u>( 370,689)</u>
Net cash used by investing activities	<u>( 319,004)</u>	<u>( 414,772)</u>
Increase (decrease) in cash and cash equivalents	( 14,772)	2,971,009
Cash and cash equivalents, beginning of year	<u>12,909,997</u>	<u>9,938,988</u>
Cash and cash equivalents, end of year	<u>\$ 12,895,225</u>	<u>\$ 12,909,997</u>
<i>Supplemental disclosures of cash flow information:</i>		
Amounts paid for federal and state income taxes (Note 7)	<u>\$ 646,601</u>	<u>\$ 595,831</u>

See notes to consolidated financial statements.

**AMERICAN ACADEMY OF FAMILY  
PHYSICIANS FOUNDATION AND SUBSIDIARY**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**YEARS ENDED DECEMBER 31, 2012 AND 2011**

**1. Organization and summary of significant accounting policies:**

*Organization and principles of consolidation:*

The American Academy of Family Physicians Foundation (the Foundation) is a not-for-profit organization whose primary activity is serving as a fiscal intermediary for programs that serve to promote and benefit family medicine throughout the United States. The Foundation encourages philanthropy, awards research grants, offers education programs and maintains a center for the history of family medicine. The Foundation's donors and members are located primarily throughout the United States of America.

AAFP Insurance Services, Inc. (Insurance Services) is a wholly-owned, for-profit subsidiary of the American Academy of Family Physicians Foundation. Insurance Services administers and sells various types of insurance plans (life, medical, disability, accidental death, etc.) to members of the American Academy of Family Physicians (the Academy), the sole contract holder of such plans. Insurance Services maintains a relationship with one insurance company that services a majority of these plans and is the source for a significant portion of revenues from insurance plans. Insurance Services' insured are located primarily throughout the United States of America.

The consolidated financial statements include the financial position, operations, cash flows and changes in net assets of the Foundation and Insurance Services (collectively referred to as the Organization). Inter-entity transactions and balances have been eliminated for financial statement purposes.

The consolidated statement of activities includes certain prior year summarized comparative information in total, but not by net asset class. Such information does not include sufficient detail to constitute a presentation in conformity with U.S. generally accepted accounting principles (GAAP). Accordingly, such information should be read in conjunction with the Organization's financial statements for the year ended December 31, 2011, from which the summarized information is derived.

*Accounts receivable:*

Accounts receivable consists primarily of Foundation donations collected by the Academy and commissions due from an insurance carrier. Neither the Foundation nor Insurance Services requires collateral for the accounts. Balances become past due according to the terms of various agreements with the chapters, organizations who handle the initial processing and insurance carriers. Balances that are still outstanding after management has used reasonable collection efforts are charged to expense when that determination is made. Management believes that all accounts receivable are collectible; therefore, no allowance for uncollectible accounts has been established.

*Advertising:*

Insurance Services expenses advertising and other promotional costs as they are incurred. These types of expenses for mailing campaigns, newsletters and similar activities totaled \$160,043 for 2012 and \$223,093 for 2011.



**AMERICAN ACADEMY OF FAMILY  
PHYSICIANS FOUNDATION AND SUBSIDIARY**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

YEARS ENDED DECEMBER 31, 2012 AND 2011

**1. Organization and summary of significant accounting policies (continued):**

*Basis of presentation:*

The accompanying financial statements have been prepared on the accrual basis of accounting. All financial transactions have been recorded in and reported by the following net asset groups:

Unrestricted net assets consist of funds free of any donor-imposed restrictions and are classified into undesignated funds and Board-designated funds. The Board-designated funds represent a portion of unrestricted donations received, which are set aside by the Board for the future general operation and administration of the Foundation.

Temporarily restricted net assets are those whose use by the Foundation has been limited by donors to a specific time period or purpose.

Permanently restricted net assets are those contributions whose use by the Foundation is limited by donor-imposed stipulations that the corpus be held in perpetuity. The earnings from these net assets are available for use for temporarily restricted purposes or are added to the corpus as specified by the donor.

*Cash equivalents:*

For purposes of the consolidated statements of cash flows, cash equivalents consist primarily of money market accounts and are carried at cost which approximates fair value.

*Contributions:*

Contributions received by the Foundation are recorded as unrestricted, temporarily restricted, or permanently restricted support depending on the existence and/or nature of any donor restrictions. When a restriction expires, temporarily restricted net assets are reclassified to unrestricted net assets. Contributions to certain programs are considered unrestricted support when the restrictions are met in the same reporting year.

*Fair value of financial instruments:*

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

The framework for measuring fair value provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The fair value hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are described below:

**AMERICAN ACADEMY OF FAMILY  
PHYSICIANS FOUNDATION AND SUBSIDIARY**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)**

**YEARS ENDED DECEMBER 31, 2012 AND 2011**

**1. Organization and summary of significant accounting policies (continued):**

*Fair value of financial instruments (continued):*

Level 1 – Quoted prices for identical instruments in active markets.

Level 2 – Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in inactive markets; or derived from inputs that are observable. Also included in Level 2 are investments measured using net asset value (NAV) per share, or its equivalent, that may be redeemed at that NAV at or near the reporting date.

Level 3 – Significant unobservable inputs that are significant to the fair value of the assets or liabilities

The carrying amount of financial instruments including cash and cash equivalents, accounts receivable, prepaid expenses, accounts payable, deferred revenue, income taxes payable and grants payable approximated fair values as of December 31, 2012 and 2011 due to their short-term nature. The fair value of investments is disclosed in Note 2.

Investments are presented at fair value as determined by methodologies relevant to each asset class with any related gain or loss reported in the statement of activities. Marketable securities are held by a custodian and are stated at fair value based on quoted market prices. Alternative investments, including hedge funds and commodity funds, are valued using net asset values provided by external investment managers as a practical expedient in determining fair value. Because such investments are not readily marketable, the estimated value is subject to uncertainty and, therefore, may differ materially from the value that would have been used had a ready market for such investments existed.

The Foundation holds units in a pooled investment fund administered by the Academy. The pooled investment fund investments include money market funds and equity and fixed income funds. The Foundation reflects the investments in the pooled investment funds at the Academy at NAV (Level 2) as a practical expedient to fair value, because these investments have a readily determined value and transact frequently. The underlying holdings in these funds are valued by the respective managers or custodians using quoted market prices for publicly traded securities and fair value for other investments, using methodologies relevant to each asset class. The valuations are routinely evaluated by management, and management believes such values are reasonable.

**AMERICAN ACADEMY OF FAMILY  
PHYSICIANS FOUNDATION AND SUBSIDIARY**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

YEARS ENDED DECEMBER 31, 2012 AND 2011

**1. Organization and summary of significant accounting policies (continued):**

*Investments and concentrations of credit risk:*

Financial instruments which potentially subject the Organization to significant concentrations of credit risk consist principally of cash, accounts receivable and investments. The Organization maintains its bank accounts at two institutions where accounts were fully insured by the Federal Deposit Insurance Corporation through December 31, 2012, and insured up to \$250,000 thereafter. As of December 31, 2012, cash and cash equivalents includes \$6,219,802 invested by the Foundation in a mutual fund which holds certificates of deposit and fixed income securities, and are not covered by FDIC insurance.

Investment securities, in general, are exposed to various risks, such as interest rate, credit, and overall market volatility. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect the amounts reported as net assets in the consolidated statements of financial position.

Certain assets are pooled for investment purposes. Related investment income, net of investment expenses, and net realized and unrealized gains and losses are allocated to each component fund based on a ratio of the individual weighted average fund balance to total weighted average fund balance.

*Income tax status:*

The Foundation is an organization as described in Section 501(c)(3) of the Internal Revenue Code (IRC), and has received a determination letter from the Internal Revenue Service (IRS) that it is exempt from federal income tax on its related exempt activities under IRC 501(a). The Foundation's current accounting policy is to provide liabilities for uncertain income tax provisions when a liability is probable and estimable. The Foundation has no uncertain income tax positions for the years ended December 31, 2012 and 2011. The Foundation is no longer subject to audits by the IRS for years prior to 2009. Management is not aware of any violation of its tax status as an organization exempt from income taxes.

Insurance Services is a for-profit entity. Income taxes are provided for the tax effects of Insurance Services transactions reported in the financial statements and consist of taxes currently due plus deferred taxes. Deferred taxes are recognized for differences between the basis of assets or liabilities for financial statement and income tax purposes and are measured using the enacted tax rates and laws anticipated to be in effect when the differences are expected to reverse.

The differences relate to depreciable assets (use of accelerated depreciation methods) and accrued expenses (timing differences on deductibility). The deferred tax assets or liabilities represent the future tax return consequences of those differences, which will either be deductible or taxable when the assets or liabilities are recovered or settled.

**AMERICAN ACADEMY OF FAMILY  
PHYSICIANS FOUNDATION AND SUBSIDIARY**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)**

**YEARS ENDED DECEMBER 31, 2012 AND 2011**

**1. Organization and summary of significant accounting policies (continued):**

*Income tax status (continued):*

Insurance Services has adopted the provisions of ASC 740-10 *Accounting for Uncertain Income Tax Positions* as it might apply to Insurance Services' financial transactions. Insurance Services' policy is to record a liability for any tax position that is beneficial to Insurance Services, including any related interest and penalties, when it is more likely than not the position taken by management with respect to the transaction or class of transactions will be overturned by a taxing authority upon examination. Management believes there are no such positions as of December 31, 2012 and, accordingly, no liability has been accrued. However, Insurance Services' federal income tax returns for 2009, 2010 and 2011 are subject to examination by the IRS, generally for three years after they are filed.

*Office equipment, furniture and fixtures:*

Office equipment, furniture and fixtures are stated at cost if purchased or at fair value if donated. Depreciation is charged to operations using the straight-line method over the estimated useful lives of the assets (three to ten years).

*Revenue recognition:*

Insurance Services' revenues are based upon broker and service agreements between Insurance Services and the insurance companies that provide coverage. Commissions and administrative allowances are accrued on premiums collected in the period earned.

*Use of estimates:*

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, and the reported amounts of revenues and expenses. Actual results could differ from those estimates.

*Reclassification of prior year amounts:*

Certain amounts previously reported in the prior year financial statements have been reclassified to conform to the current year's presentation.

*Subsequent events:*

Subsequent events have been evaluated through May 19, 2013, which is the date the financial statements were available to be issued.

**AMERICAN ACADEMY OF FAMILY  
PHYSICIANS FOUNDATION AND SUBSIDIARY**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

YEARS ENDED DECEMBER 31, 2012 AND 2011

**2. Investments:**

Investments of the Foundation are reported at fair value and consist of the following:

	<u>2012</u>	<u>2011</u>
Common and preferred stock	\$ 6,191,288	\$ 5,639,017
Corporate bonds	1,888,455	1,409,400
Equity funds	656,565	698,734
Gold fund	493,353	462,810
Treasury and federal agency obligations	1,152,177	1,110,481
Investment in pooled funds at the Academy	921,434	798,593
Hedge funds	48,588	85,125
Certificate of deposit	--	200,000
Cash and equivalents	<u>651,194</u>	<u>350,836</u>
	<u>\$ 12,003,054</u>	<u>\$ 10,754,996</u>

Assets held as investments for planned giving programs totaled \$134,678 and \$127,941 at December 31, 2012 and 2011, respectively. These amounts are included in investments and consist almost exclusively of equities and fixed income funds.

Investment income (loss) from the Foundation investments is summarized as follows:

	<u>2012</u>	<u>2011</u>
Interest and dividends	\$ 291,780	\$ 238,083
Investment fees and expenses	( 71,907)	( 68,104)
Realized gains	269,315	82,300
Unrealized gains (losses)	673,182	( 396,863)
Change in value of split-interest agreements (Note 3)	<u>9,428</u>	<u>( 4,001)</u>
	<u>\$ 1,171,798</u>	<u>(\$ 148,585)</u>

**AMERICAN ACADEMY OF FAMILY  
PHYSICIANS FOUNDATION AND SUBSIDIARY**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

YEARS ENDED DECEMBER 31, 2012 AND 2011

**2. Investments (continued):**

The following is a summary of the inputs used in valuing the Foundation's investments carried at fair value:

	December 31 <u>2012</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
Common and preferred stock	\$ 6,191,288	\$ 6,191,288	--	--
Corporate bonds	1,888,455	--	\$ 1,888,455	--
Equity funds	656,565	656,565	--	--
Gold fund	493,353	493,353	--	--
Treasury and federal agency obligations	1,152,177	--	1,152,177	--
Investment in pooled funds at the Academy	921,434	--	921,434	--
Hedge funds	48,588	--	--	\$ 48,588
Cash and equivalents	<u>651,194</u>	<u>651,194</u>	<u>--</u>	<u>--</u>
	<u>\$ 12,003,054</u>	<u>\$ 7,994,200</u>	<u>\$ 3,962,066</u>	<u>\$ 48,588</u>
	December 31 <u>2011</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
Common and preferred stock	\$ 5,639,017	\$ 5,639,017	--	--
Corporate bonds	1,409,400	36,285	\$ 1,373,115	--
Equity funds	698,734	698,734	--	--
Gold fund	462,810	462,810	--	--
Treasury and federal agency obligations	1,110,481	--	1,110,481	--
Investment in pooled funds at the Academy	798,593	--	798,593	--
Hedge funds	85,125	--	--	\$ 85,125
Certificate of deposit	200,000	200,000	--	--
Cash and equivalents	<u>350,836</u>	<u>350,836</u>	<u>--</u>	<u>--</u>
	<u>\$ 10,754,996</u>	<u>\$ 7,387,682</u>	<u>\$ 3,282,189</u>	<u>\$ 85,125</u>

**AMERICAN ACADEMY OF FAMILY  
PHYSICIANS FOUNDATION AND SUBSIDIARY**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

YEARS ENDED DECEMBER 31, 2012 AND 2011

**2. Investments (continued):**

Units in pooled investment funds at the Academy are reported at net asset value as a practical expedient to estimate the fair value of the Foundation's interest therein. Classification of these funds as Level 2 is based on the Foundation's ability to redeem its interest at or near the date of the statement of financial position. The hedge fund is in the process of liquidation with expected payouts through 2015.

The classification of investments in the fair value hierarchy is not necessarily an indication of the risks, liquidity, or degree of difficulty in estimating the fair value of each investment's underlying assets and liabilities.

The following is a reconciliation of investments in which significant unobservable inputs (Level 3) were used in determining fair value:

	<u>Hedge fund</u>
December 31, 2010	\$ 162,149
Interest income	333
Realized losses	( 18,602)
Unrealized gains	17,605
Transfers to Level 1	( 76,360)
December 31, 2011	85,125
Dividend income	259
Realized losses	( 13,578)
Unrealized gains	6,755
Transfers to Level 1	( 29,973)
December 31, 2012	<u>\$ 48,588</u>

Transfers between levels are recorded at the end of each fiscal year. Transfers from Level 3 to Level 1 in 2012 and 2011 represented a portion of the proceeds from redemption of hedge funds.

**AMERICAN ACADEMY OF FAMILY  
PHYSICIANS FOUNDATION AND SUBSIDIARY**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

YEARS ENDED DECEMBER 31, 2012 AND 2011

**3. Split-interest agreements:**

*Charitable Remainder Trusts:*

The Foundation is the named beneficiary of two Charitable Remainder Unitrusts (CRUTs). These split interest agreements provide for a lifetime benefit to be paid to the donor or other designated beneficiary. Upon the death of the beneficiary(ies), the remaining trust assets are distributed to charitable remainder beneficiaries as provided in the trust document. The Foundation is the trustee and sole remainder beneficiary of one of the CRUTs. The assets held in this trust totaled \$49,750 as of December 31, 2012 and are included in investments. Based on the value of the assets and the age of the beneficiaries, the Foundation has recorded a liability of \$34,297 at December 31, 2012, equal to the present value of the estimated future obligations based on mortality rates derived from ordinary life annuity tables. The increase in the net value of the CRUT of \$1,081 is included in "investment income" in the statement of activities for 2012.

The other CRUT names the Foundation as beneficiary of the remainder interest but the Foundation is not the trustee. Therefore, the present value of the estimated remainder interest attributable to the Foundation of \$36,321 is recorded as "beneficial interest in trust assets" as of December 31, 2012. The increase in this receivable of \$1,944 is included in "investment income" in the statement of activities for 2012.

*Pooled income fund:*

Donors contribute assets to an investment pool and are assigned a specific number of units based on the proportion of the fair value of their contribution to the total fair value of the pooled income fund on the date of the donor's entry to the pooled fund. The contributed assets are recorded at fair value. A contribution is recorded at the fair value of the assets discounted for the estimated time period until the donor's death. The difference between the fair value of the assets received and the revenue recognized is recorded as deferred revenue, representing the amount of the discount for future interest. Until a donor's death, the donor or donor's designated beneficiary is paid the actual ordinary income earned on the donor's units. Upon the donor's death, the fair value of the units is released to the Foundation or other designated charitable beneficiary for unrestricted use. No additional pooled income fund contributions were received in 2012 or 2011.

The fair value of the pooled income fund assets of \$85,018 is included in investments in the accompanying consolidated statements of financial position as of December 31, 2012. Periodic income on the pooled income fund and payments to the donors are reflected as increases and decreases in the liability to the donors, \$841 for 2012, which is included in "liabilities under split-interest agreements." The present value of the future interest is calculated using discount rates ranging from 5.75% to 8.75% and applicable life expectancy tables. The estimated future liability of the pooled income fund contributions of \$21,848 is recognized as deferred revenue and is included in "liabilities under split-interest agreements". The increase in the net value of the pooled income fund of \$6,402 is included in "investment income" in the statement of activities for 2012.



**AMERICAN ACADEMY OF FAMILY  
PHYSICIANS FOUNDATION AND SUBSIDIARY**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

YEARS ENDED DECEMBER 31, 2012 AND 2011

**4. Net assets:**

Certain net assets have been designated or appropriated by the Board as follows:

	<u>2012</u>	<u>2011</u>
General endowment	\$ 8,377,730	\$ 7,522,609
Archives endowment	816,335	730,039
Family Medicine Philanthropic Consortium	99,693	130,215
Family Medicine Cares	<u>--</u>	<u>19,938</u>
	<u>\$ 9,293,758</u>	<u>\$ 8,402,801</u>

Temporarily restricted net assets consist of cash and investments and are held for the following purposes at December 31:

	<u>2012</u>	<u>2011</u>
Resident Repayment Program	\$ 483,941	\$ 483,941
Pass-through grants	104,407	92,166
Stern Lectureship Fund	87,901	79,560
Immunization program	28,516	75,655
Teacher Development Awards	4,921	5,808
Pooled income fund	62,330	55,928
CRT planned gifts	51,772	48,747
Visiting Professorship Program	--	13,026
International fund	38,171	51,275
Nutrition Grant	33,368	36,237
Health Literacy fund	3,128	3,469
Disaster relief fund	27,124	25,819
Family Medicine Cares	69,603	35,501
Research Skills Seminar	--	6,342
Fellowship awards	7,125	8,560
Sundry	<u>32,770</u>	<u>6,597</u>
	<u>\$ 1,035,077</u>	<u>\$ 1,028,631</u>

**AMERICAN ACADEMY OF FAMILY  
PHYSICIANS FOUNDATION AND SUBSIDIARY**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

YEARS ENDED DECEMBER 31, 2012 AND 2011

**4. Net assets (continued):**

Net assets released from temporary restrictions due to satisfaction of donor restrictions are as follows:

	<u>2012</u>	<u>2011</u>
Peers for Progress	\$ 2,092,956	\$ 2,125,686
Highlight on Diabetes	322,304	143,023
Pass-through grants	460,114	636,431
Time to Talk Cardio	--	125,000
Immunization program	222,139	289,483
Visiting Professorship Program	13,025	95,990
Teacher Development Awards	50,887	63,615
Research Skills Seminar	6,342	1,261
International fund	37,588	64,564
Nutrition Grant	2,869	5,814
Cities for Life	614,508	16,397
Behavior Economics Roundtable	--	48,000
Fellowship awards	1,935	1,000
Health Literacy fund	341	500
Disaster relief	18,971	50,550
Family Medicine Cares	22,433	--
Sundry	<u>781</u>	<u>8,504</u>
	<u>\$ 3,867,193</u>	<u>\$ 3,675,818</u>

The Foundation's endowment funds include permanently restricted net assets consisting of six individual funds established for a variety of purposes and funds designated by the Board of Trustees. The Foundation's policy requires the preservation of the fair value as of the gift date of donor-restricted endowment funds absent explicit donor stipulations to the contrary. Based on its interpretation of state law regarding management of endowment funds, the Foundation classifies as permanently restricted net assets the original value of the gifts to the permanent endowment, the fair value of any subsequent gifts to the endowment and any accumulation required to be made by donor stipulation. Amounts in excess of the stated value of permanently restricted funds are classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Foundation.

The Foundation has investment and expenditure policies that consider the purpose of the donor-restricted fund, general economic conditions, and expected investment returns. From time to time, the fair value of net assets associated with individual donor-restricted endowment funds may fall below the level the donor required the Foundation to retain as a fund of perpetual duration. In accordance with GAAP, deficiencies of this nature would be appropriated from unrestricted funds. As of December 31, 2012 and 2011, these deficiencies totaled \$0 and \$56,944, respectively.

**AMERICAN ACADEMY OF FAMILY  
PHYSICIANS FOUNDATION AND SUBSIDIARY**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

YEARS ENDED DECEMBER 31, 2012 AND 2011

**4. Net assets (continued):**

Endowment net assets composition by type of fund as of December 31, 2012 and 2011 is as follows:

	<u>Unrestricted</u>	<u>Temporarily restricted</u>	<u>Permanently restricted</u>	<u>Total</u>
December 31, 2012:				
Donor-restricted endowment funds	--	\$ 27,953	\$ 1,531,705	\$ 1,559,658
Board-designated endowment funds	<u>\$ 9,194,064</u>	<u>--</u>	<u>--</u>	<u>9,194,064</u>
	<u>\$ 9,194,064</u>	<u>\$ 27,953</u>	<u>\$ 1,531,705</u>	<u>\$ 10,753,722</u>
December 31, 2011:				
Donor-restricted endowment funds	(\$ 56,944)	\$ 1,801	\$ 1,401,045	\$ 1,345,902
Board-designated endowment funds	<u>8,252,648</u>	<u>--</u>	<u>--</u>	<u>8,252,648</u>
	<u>\$ 8,195,704</u>	<u>\$ 1,801</u>	<u>\$ 1,401,045</u>	<u>\$ 9,598,550</u>

Donor-restricted endowment funds consist of cash and investments and are held for the following purposes at December 31:

	<u>2012</u>	<u>2011</u>
Archives endowment	\$ 851,276	\$ 723,687
Lopez endowments	179,071	162,066
Graham endowment	296,597	260,925
McCord endowment	99,148	90,063
Panther endowment	32,802	29,719
Ostergaard endowment	<u>100,764</u>	<u>79,442</u>
	<u>\$ 1,559,658</u>	<u>\$ 1,345,902</u>

**AMERICAN ACADEMY OF FAMILY  
PHYSICIANS FOUNDATION AND SUBSIDIARY**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

YEARS ENDED DECEMBER 31, 2012 AND 2011

**4. Net assets (continued):**

Changes in endowment net assets for the years ended December 31, 2012 and 2011, are as follows:

	<u>Unrestricted</u>	<u>Temporarily restricted</u>	<u>Permanently restricted</u>	<u>Total</u>
Endowment net assets, December 31, 2010	\$8,299,874	\$ 5,550	\$ 1,340,859	\$ 9,646,283
Contributions	19,384	--	60,186	79,570
Net investment income	145,048	4,276	--	149,324
Net realized and unrealized losses	( 283,602)	( 7,425)	--	( 291,027)
Program expenses	( 600)	--	--	( 600)
Transfers in (from AAFP)	<u>15,000</u>	<u>--</u>	<u>--</u>	<u>15,000</u>
Endowment net assets, December 31, 2011	8,195,704	1,801	1,401,045	9,598,550
Contributions	65,350	--	67,950	133,300
Net investment income	170,829	6,049	13,780	190,658
Net realized and unrealized gains	747,181	20,703	48,930	816,814
Program expenses	( 600)	--	--	( 600)
Transfers in (from AAFP)	<u>15,000</u>	<u>--</u>	<u>--</u>	<u>15,000</u>
Endowment net assets, December 31, 2012	<u>\$9,194,064</u>	<u>\$ 27,953</u>	<u>\$ 1,531,705</u>	<u>\$ 10,753,722</u>

**5. Employee benefit plans:**

Insurance Services administers a non-contributory, defined contribution retirement plan (the Defined Contribution Plan) for its employees. All employees who have attained the age of 21 and completed 1,000 hours of service during a 12-month period are eligible. The right to discontinue the Defined Contribution Plan has been reserved by Insurance Services, and in such event the trust fund must be used for the exclusive benefit of participants. Insurance Services' annual contribution to the Defined Contribution Plan is seven percent (7%) of each participant's annual salary. Additionally, Insurance Services has a 401(k) plan, under which Insurance Services matches employee contributions up to an additional four percent (4%) of compensation. Insurance Services contributed \$78,303 and \$80,675 to the plans for 2012 and 2011, respectively.

**AMERICAN ACADEMY OF FAMILY  
PHYSICIANS FOUNDATION AND SUBSIDIARY**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

YEARS ENDED DECEMBER 31, 2012 AND 2011

**6. Functional allocation of expenses:**

The costs of providing various program and supporting activities of the Foundation have been reported on a natural basis in the statement of activities. The costs of these activities on a functional basis, including allocation of certain costs, are summarized below.

	<u>2012</u>	<u>2011</u>
Program services	\$ 5,109,618	\$ 4,629,965
Supporting services:		
Administration	504,207	433,281
Fundraising	783,444	763,140
	<u>1,287,651</u>	<u>1,196,421</u>
	<u>\$ 6,397,269</u>	<u>\$ 5,826,386</u>

**7. Income taxes:**

Insurance Services' current federal and state income tax liability and deferred tax asset (liability) follow:

	<u>2012</u>	<u>2011</u>
Current tax liability	\$ 28,177	\$ 25,331
Deferred tax asset	\$ 30,953	\$ 28,232
Deferred tax liability	( 24,119)	( 33,796)
Deferred tax asset (liability), net	<u>\$ 6,834</u>	<u>(\$ 5,564)</u>

The provisions for income taxes consist of the following components:

Current expense	\$ 649,447	\$ 623,400
Deferred benefit	( 12,398)	( 1,328)
	<u>\$ 637,049</u>	<u>\$ 622,072</u>

Insurance Services' provision for income taxes differs from applying the statutory U.S. federal income tax rate to income before income taxes primarily due to provisions for state income taxes and deducting certain expenses for financial statement purposes but not for federal income tax purposes.

**AMERICAN ACADEMY OF FAMILY  
PHYSICIANS FOUNDATION AND SUBSIDIARY**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)**

**YEARS ENDED DECEMBER 31, 2012 AND 2011**

**8. Leases:**

Insurance Services leases space from the Academy. The current lease expires in September 2014. Future minimum lease payments are as follows:

<u>Year ending December 31,</u>	<u>Amount</u>
2013	\$ 84,342
2014	<u>56,228</u>
	<u>\$ 140,570</u>

Total rent expense for the office operating lease was \$84,342 for the years ended December 31, 2012 and 2011, respectively.

**9. Major customer and sole stockholder:**

The Academy, as the contract holder, controls certain plans administered by Insurance Services. The Board of Directors of the Academy constitutes the membership of Insurance Services' sole stockholder, the American Academy of Family Physicians Foundation. Insurance Services administers Academy-sponsored life insurance plans and, pursuant to a royalty agreement related thereto, incurred costs to the Academy of \$56,418 and \$56,030 for the years ended December 31, 2012 and 2011, respectively.

**10. Related-party transactions:**

Foundation accounts receivable include revenues and other support from the Academy of \$88,774 and \$56,251 at December 31, 2012 and 2011, respectively. Accounts payable includes \$836,307 and \$351,632 at December 31, 2012 and 2011, respectively, due to the Academy by the Foundation for services and other items. In addition, \$4,034 and \$10,831 were due to the Academy from Insurance Services at December 31, 2012 and 2011, respectively, as reimbursements for certain common administrative costs.

Insurance Services reimbursed the Academy for common administrative costs (postage, internet, telephone) and marketing expenses in the amount of \$85,137 and \$100,324 for 2012 and 2011, respectively.

**AMERICAN ACADEMY OF FAMILY  
PHYSICIANS FOUNDATION AND SUBSIDIARY**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)**

**YEARS ENDED DECEMBER 31, 2012 AND 2011**

**10. Related-party transactions (continued):**

The following amounts were provided to the Foundation as support from, or pass-through donations collected by, the Academy for the years ended December 31:

	<u>2012</u>	<u>2011</u>
Dues check-off (pass-through donation)	\$ 190,071	\$ 274,265
Contributions directed through AAFP	55,510	
Center for the History of Family Medicine support	15,000	15,000
Other	<u>68,557</u>	<u>39,740</u>
	<u>\$ 329,138</u>	<u>\$ 329,005</u>

Effective January 1, 2011, the administrative services contract with the Academy changed so that all of the expenses incurred through the Academy are now considered direct expenses. The Foundation pays the direct expenses and an overhead rate of 22.2% on those expenses. During 2012 and 2011 the Foundation incurred \$1,723,092 and \$1,721,067, respectively, of expenses and overhead for personnel, travel, postage, supplies, design, printing, rent and other program expenses. The Foundation also recorded \$1,419,640 in 2012 and \$1,178,536 in 2011 for grants and related costs to the Academy.

**11. Conditional promises:**

In May 2007, The Foundation entered into an agreement with Eli Lilly and Company Foundation, Inc. (Lilly) whereby Lilly agreed to a grant of \$15 million to the Foundation to support the development of the "Peers for Progress" program (PFP). PFP is designed to help the diabetes community establish a new model of peer education for people with diabetes. The program is rooted in peer-to-peer interactions in order to sustain individual behavior changes that will improve health as well as quality of life. PFP is designed to demonstrate the value of peer support, extend the evidence base for such interventions, help establish peer support as an accepted, core component of diabetes care, and promote peer support programs and networks around the world.

In December 2010, the Foundation entered into a grant agreement with Bristol-Myers Squibb Foundation, Inc. that provides for a grant of up to \$5,239,876, in three annual payments, in support of a demonstration project to be led by the PFP management team. The grant expires December 31, 2013.

These grants are cancellable by the grantors at any time with or without cause with unexpended or uncommitted advances to be refunded. The Foundation retains a 5% fee for administering the grants. Through December 31, 2012, the Foundation had received \$20,239,876 under these grant agreements, and \$15,163,135 in expenses had been incurred. The balance of \$5,076,741 is included in deferred revenue at December 31, 2012.

**AMERICAN ACADEMY OF FAMILY  
PHYSICIANS FOUNDATION AND SUBSIDIARY**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)**

**YEARS ENDED DECEMBER 31, 2012 AND 2011**

**12. Commitments:**

On June 4, 2012, Insurance Services entered into a two-year employment contract with its president, effective July 1, 2012, and renewable automatically on a two-year basis subject to cancellation by either party under specified conditions. This contract provides for a base compensation including a fixed salary along with incentive compensation based on dividends paid.