

**American Academy of Family Physicians
Foundation and Subsidiary**

Independent Auditor's Report and Consolidated Financial Statements

December 31, 2017 and 2016



**American Academy of Family Physicians
Foundation and Subsidiary
December 31, 2017 and 2016**

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Independent Auditor's Report

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

We have audited the accompanying consolidated financial statements of American Academy of Family Physicians Foundation and Subsidiary, which comprise the consolidated statement of financial position as of December 31, 2017, and the related consolidated statements of activities 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 accounting principles generally accepted in the United States of America; this includes the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these 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 auditor's 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.

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Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of American Academy of Family Physicians Foundation and Subsidiary as of December 31, 2017, and the changes in their net assets and their cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Report on Summarized Consolidated Comparative Information

We have previously audited the December 31, 2016 consolidated financial statements, and we expressed an unmodified audit opinion on those audited consolidated financial statements in our report dated May 21, 2017. In our opinion, the summarized consolidated comparative information presented herein as of and for the year ended December 31, 2016 is consistent, in all material respects, with the consolidated audited financial statements from which it has been derived.

BKD, LLP

Kansas City, Missouri
May 21, 2018

**American Academy of Family Physicians
Foundation and Subsidiary
Consolidated Statement of Financial Position
December 31, 2017
(with Comparative Totals for 2016)**

Assets	2017			Consolidated Total	Comparative Totals for 2016
	Foundation	Insurance Services	Eliminations		
Cash and cash equivalents	\$ 328,290	\$ 1,012,236	\$ -	\$ 1,340,526	\$ 1,475,098
Cash and cash equivalents - premium account	-	3,124,158	-	3,124,158	3,212,854
Accounts receivable	146,393	609,777	-	756,170	893,430
Prepaid expenses	45,722	16,310	-	62,032	91,932
Investments at fair value	16,837,328	-	-	16,837,328	15,245,323
Investment in subsidiary	1,497,655	-	(1,497,655)	-	-
Contributions receivable	84,021	-	-	84,021	30,000
Beneficial interest in trust assets	59,376	-	-	59,376	54,593
Income tax receivable	-	152,725	-	152,725	-
Deferred tax asset	-	7,300	-	7,300	34,900
Office equipment, furniture and fixtures, net of accumulated depreciation; 2017 - \$822,251, 2016 - \$790,978	62,806	27,682	-	90,488	114,704
	<u>\$ 19,061,591</u>	<u>\$ 4,950,188</u>	<u>\$ (1,497,655)</u>	<u>\$ 22,514,124</u>	<u>\$ 21,152,834</u>
Liabilities and Net Assets					
Liabilities					
Accounts payable and accrued expenses	\$ 700,560	\$ 318,595	\$ -	\$ 1,019,155	\$ 926,911
Premiums payable	-	3,126,838	-	3,126,838	3,213,087
Grant awards payable	251,327	-	-	251,327	319,436
Deferred revenue and advances	50,849	-	-	50,849	105,206
Liabilities under split-interest agreements	204,991	-	-	204,991	197,847
Deferred tax liability	-	7,100	-	7,100	12,000
Federal and state income taxes payable	-	-	-	-	19,135
Total liabilities	<u>1,207,727</u>	<u>3,452,533</u>	<u>-</u>	<u>4,660,260</u>	<u>4,793,622</u>
Net Assets					
Unrestricted					
Undesignated	3,005,631	1,497,655	(1,497,655)	3,005,631	2,821,016
Board designated	10,670,512	-	-	10,670,512	10,060,303
Total unrestricted	<u>13,676,143</u>	<u>1,497,655</u>	<u>(1,497,655)</u>	<u>13,676,143</u>	<u>12,881,319</u>
Temporarily restricted	1,982,251	-	-	1,982,251	1,590,480
Permanently restricted	2,195,470	-	-	2,195,470	1,887,413
Total net assets	<u>17,853,864</u>	<u>1,497,655</u>	<u>(1,497,655)</u>	<u>17,853,864</u>	<u>16,359,212</u>
Total liabilities and net assets	<u>\$ 19,061,591</u>	<u>\$ 4,950,188</u>	<u>\$ (1,497,655)</u>	<u>\$ 22,514,124</u>	<u>\$ 21,152,834</u>

**American Academy of Family Physicians
Foundation and Subsidiary
Consolidated Statement of Activities
Year Ended December 31, 2017
(with Comparative Totals for 2016)**

	2017			Consolidated Total	Comparative Totals for 2016
	Foundation	Insurance Services	Eliminations		
Unrestricted Net Assets					
Revenues, Gains and Other Support					
Grant revenue	\$ 6,590	\$ -	\$ -	\$ 6,590	\$ 56,480
Corporate and chapter support	1,008,747	-	-	1,008,747	876,667
Individual contributions	448,163	-	-	448,163	505,764
Special events, net of direct expenses of \$34,027 in 2017 and \$39,268 in 2016	41,171	-	-	41,171	53,527
Investment return	1,734,231	-	-	1,734,231	695,610
Insurance agreement revenues	-	3,776,328	-	3,776,328	3,922,265
Net assets released from restrictions	946,234	-	-	946,234	905,663
Total revenues, gains and other support	<u>4,185,136</u>	<u>3,776,328</u>	<u>-</u>	<u>7,961,464</u>	<u>7,015,976</u>
Expenses and Losses					
Insurance services	-	2,878,773	-	2,878,773	2,821,965
Board, general, staff and administration	499,555	-	-	499,555	487,159
Family Medicine Philanthropic Consortium	80,586	-	-	80,586	91,048
Center for the History of Family Medicine	247,584	-	-	247,584	254,609
Family Medicine Cares	327,465	-	-	327,465	334,354
Family Medicine Leads	373,951	-	-	373,951	388,684
Grant awards and administration	544,963	-	-	544,963	432,667
Individual development	606,785	-	-	606,785	759,204
Professional and corporate affairs	201,275	-	-	201,275	183,510
Programs, other	1,405,703	-	-	1,405,703	1,527,889
Total expenses and losses	<u>4,287,867</u>	<u>2,878,773</u>	<u>-</u>	<u>7,166,640</u>	<u>7,281,089</u>
Change in unrestricted net assets	<u>(102,731)</u>	<u>897,555</u>	<u>-</u>	<u>794,824</u>	<u>(265,113)</u>
Temporarily Restricted Net Assets					
Grant revenues	588,829	-	-	588,829	652,777
Corporate and chapter support	11,000	-	-	11,000	5,000
Individual contributions	325,617	-	-	325,617	209,354
Special events	84	-	-	84	1,545
Investment return	412,475	-	-	412,475	156,706
Net assets released from restrictions	(946,234)	-	-	(946,234)	(905,663)
Change in temporarily restricted net assets	<u>391,771</u>	<u>-</u>	<u>-</u>	<u>391,771</u>	<u>119,719</u>
Permanently Restricted Net Assets					
Corporate and chapter support	37,500	-	-	37,500	36,000
Individual contributions	210,163	-	-	210,163	64,633
Investment return	60,394	-	-	60,394	14,794
Change in permanently restricted net assets	<u>308,057</u>	<u>-</u>	<u>-</u>	<u>308,057</u>	<u>115,427</u>
Increase (Decrease) in Net Assets Before					
Earnings of Subsidiary and Dividends Paid	597,097	897,555	-	1,494,652	(29,967)
Earnings of Subsidiary	897,555	-	(897,555)	-	-
Dividends Paid	-	(1,001,000)	1,001,000	-	-
Increase (Decrease) in Net Assets	1,494,652	(103,445)	103,445	1,494,652	(29,967)
Net Assets, Beginning of Year	16,359,212	1,601,100	(1,601,100)	16,359,212	16,389,179
Net Assets, End of Year	<u>\$ 17,853,864</u>	<u>\$ 1,497,655</u>	<u>\$ (1,497,655)</u>	<u>\$ 17,853,864</u>	<u>\$ 16,359,212</u>

**American Academy of Family Physicians
Foundation and Subsidiary
Consolidated Statement of Cash Flows
Year Ended December 31, 2017
(with Comparative Totals for 2016)**

	2017			Consolidated Total	Comparative Totals for 2016
	Foundation	Insurance Services	Eliminations		
Operating Activities					
Change in net assets	\$ 1,494,652	\$ 897,555	\$ (897,555)	\$ 1,494,652	\$ (29,967)
Items not requiring (providing) operating cash flows					
Depreciation	18,842	12,431	-	31,273	26,379
Net realized and unrealized gains on investments	(1,890,538)	-	-	(1,890,538)	(635,980)
Gain on split-interest agreements	(31,156)	-	-	(31,156)	(10,597)
Contributions of investment securities	(132,547)	-	-	(132,547)	(180,638)
Contributions and investment income received restricted for long-term investment	(248,235)	-	-	(248,235)	(101,554)
Change in investment in subsidiary	103,445	-	(103,445)	-	-
Deferred income taxes	-	22,700	-	22,700	1,600
Change in					
Accounts receivable	69,073	68,187	-	137,260	(127,379)
Prepaid expenses	11,391	34,400	-	45,791	31,065
Contributions receivable	(54,021)	-	-	(54,021)	(30,000)
Accounts payable and accrued expenses	(94,078)	186,322	-	92,244	(91,782)
Premiums payable	-	(86,249)	-	(86,249)	8,189
Grant awards payable	(68,109)	-	-	(68,109)	(109,188)
Deferred revenue and advances	(54,357)	-	-	(54,357)	(96,232)
Federal and state income taxes payable	-	(171,860)	-	(171,860)	5,907
Net cash provided by (used in) operating activities	<u>(875,638)</u>	<u>963,486</u>	<u>(1,001,000)</u>	<u>(913,152)</u>	<u>(1,340,177)</u>
Investing Activities					
Purchase of office equipment, furniture and fixtures	-	(7,057)	-	(7,057)	(109,418)
Purchase of investments	(3,871,555)	-	-	(3,871,555)	(6,245,960)
Sales and maturities of investments	4,329,008	-	-	4,329,008	6,626,272
Net cash provided by (used in) investing activities	<u>457,453</u>	<u>(7,057)</u>	<u>-</u>	<u>450,396</u>	<u>270,894</u>
Financing Activities					
Proceeds from contributions and investment income restricted for long-term investment	248,235	-	-	248,235	101,554
Proceeds from annuities	-	-	-	-	176,800
Payments on annuities	(8,747)	-	-	(8,747)	(3,979)
Cash dividends paid	-	(1,001,000)	1,001,000	-	-
Net cash provided by (used in) financing activities	<u>239,488</u>	<u>(1,001,000)</u>	<u>1,001,000</u>	<u>239,488</u>	<u>274,375</u>
Decrease in Cash and Cash Equivalents	<u>(178,697)</u>	<u>(44,571)</u>	<u>-</u>	<u>(223,268)</u>	<u>(794,908)</u>
Cash and Cash Equivalents, Beginning of Year	<u>506,987</u>	<u>4,180,965</u>	<u>-</u>	<u>4,687,952</u>	<u>5,482,860</u>
Cash and Cash Equivalents, End of Year	<u>\$ 328,290</u>	<u>\$ 4,136,394</u>	<u>\$ -</u>	<u>\$ 4,464,684</u>	<u>\$ 4,687,952</u>
Reconciliation of Cash and Cash Equivalents to the Statement of Financial Position					
Cash and cash equivalents	\$ 328,290	\$ 1,012,236	\$ -	\$ 1,340,526	\$ 1,475,098
Cash and cash equivalents - premium account	-	3,124,158	-	3,124,158	3,212,854
	<u>\$ 328,290</u>	<u>\$ 4,136,394</u>	<u>\$ -</u>	<u>\$ 4,464,684</u>	<u>\$ 4,687,952</u>
Supplemental Cash Flows Information					
Income taxes paid	\$ -	\$ 710,360	\$ -	\$ 710,360	\$ 683,493

**American Academy of Family Physicians
Foundation and Subsidiary
Notes to Consolidated Financial Statements
December 31, 2017 and 2016**

Note 1: Nature of Operations and Summary of Significant Accounting Policies

Nature of Operations

The American Academy of Family Physicians Foundation (the Foundation) is a not-for-profit organization whose mission and principal activity is to serve as a fiscal intermediary for programs that serve to promote and benefit family medicine throughout the United States of America. 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 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), which is the sole contract holder of such plans. Insurance Services maintains a relationship with one insurance company that services a majority of these plans and through agreements provides the source for a significant portion of revenues from insurance plans.

Principles of Consolidation

The consolidated financial statements include the accounts of the Foundation and its wholly-owned subsidiary, Insurance Services (hereinafter collectively known as the Organization). All significant intercompany accounts and transactions have been eliminated in consolidation.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues, expenses, gains, losses and other changes in net assets during the reporting period. Actual results could differ from those estimates.

Cash and Cash Equivalents

The Organization considers all liquid investments with original maturities of three months or less to be cash equivalents. At December 31, 2017 and 2016, cash and cash equivalents consisted primarily of deposit accounts and a money market account with a financial institution.

At December 31, 2017, the Organization's deposit accounts exceeded federally insured limits by approximately \$3,988,000.

The premium account is a restricted cash account that holds premiums collected on behalf of Insurance Services.

**American Academy of Family Physicians
Foundation and Subsidiary
Notes to Consolidated Financial Statements
December 31, 2017 and 2016**

Investments and Investment Return

Investments in equity securities having a readily determinable fair value and in all debt securities are carried at fair value. Investment return includes dividend, interest and other investment income, realized and unrealized gains and losses on investments carried at fair value and realized gains and losses on other investments.

The pooled investment funds are valued at net asset value which estimates fair value. Investment earnings are allocated monthly on a pro rata basis representative of the Foundation's overall percentage of the ownership in the fund.

Investment return that is initially restricted by donor stipulation and for which the restriction will be satisfied in the same year is recorded as temporarily restricted and then released from restriction. Other investment return is reflected in the statement of activities as unrestricted, temporarily restricted or permanently restricted based upon the existence and nature of any donor or legally imposed restrictions.

The Foundation maintains pooled investment accounts for its endowments. Investment income and realized and unrealized gains and losses from securities in the pooled investment accounts are allocated monthly to the individual endowments based on the relationship of the fair value of the interest of each endowment to the total fair value of the pooled investments accounts, as adjusted for additions to or deductions from those accounts.

Investment securities are exposed to various risks such as interest rate, market and credit. 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 change could materially affect the amounts reported in the accompanying consolidated statement of financial position.

Accounts Receivable

Foundation accounts receivable consist primarily of Foundation donations collected by the Academy, and donations or grants receivable from third parties. Balances become past due according to the terms of various agreements with third parties and organizations who handle the initial processing. 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 at December 31, 2017 and 2016; therefore, no allowance for uncollectible accounts has been established.

Insurance Services accounts receivable consist primarily of commissions due from one insurance carrier. Insurance Services holds the funds of these accounts receivable and, accordingly, believes that no allowance for doubtful accounts is needed for the years ended December 31, 2017 and 2016. The insurance carrier and the insured are located throughout the United States of America.

**American Academy of Family Physicians
Foundation and Subsidiary
Notes to Consolidated Financial Statements
December 31, 2017 and 2016**

Property and Equipment

Property and equipment are stated at cost less accumulated depreciation. Depreciation is charged to expense using the straight-line method over the estimated useful life of each asset. The estimated useful lives of the assets range from three years to fifteen years.

Temporarily and Permanently Restricted Net Assets

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 have been restricted by donors to be maintained by the Foundation in perpetuity.

Contributions

Gifts of cash and other assets received without donor stipulations are reported as unrestricted revenue and net assets. Gifts received with a donor stipulation that limits their use are reported as temporarily or permanently restricted revenue and net assets. When a donor stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of activities as net assets released from restrictions. Gifts and investment income that are originally restricted by the donor, and for which the restriction is met in the same time period, are recorded as temporarily restricted and then released from restriction.

Conditional gifts depend on the occurrence of a specified future and uncertain event to bind the potential donor and are recognized as assets and revenue when the conditions are substantially met and the gift becomes unconditional.

There were no individually significant contributions in 2017 and 2016.

Grant Awards Payable

Grant awards payable include amounts due to outside organizations from grants the Foundation has awarded.

Grant Revenue and Deferred Revenue

Support funded by grants is recognized as the Foundation performs the contracted services or incurs outlays eligible for reimbursement under the grant agreements. Grant activities and outlays are subject to audit and acceptance by the granting agency and, as a result of such audit, adjustments could be required.

**American Academy of Family Physicians
Foundation and Subsidiary
Notes to Consolidated Financial Statements
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Insurance Revenues

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.

Approximately 95 percent and 97 percent of revenues from insurance agreements were generated from one insurance carrier during the years ended December 31, 2017 and 2016, respectively.

Income Taxes

The Foundation is exempt from income taxes under Section 501 of the Internal Revenue Code and a similar provision of state law. However, the Foundation is subject to federal income tax on any unrelated business taxable income.

The Organization files tax returns in the U.S. federal jurisdiction.

Insurance Services is a for-profit entity. Income taxes are provided for the tax effects of transactions reported in the consolidated financial statements and consist of taxes currently due and 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 that will be in effect when the differences are expected to reverse.

The differences relate to depreciable assets (use of different depreciation methods and lives for financial statements and income tax purposes) and certain accrued expenses (expensed for financial statement purposes but not deductible for income tax purposes until paid). The deferred tax asset and liability 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. Valuation allowances are provided for deferred tax assets based on management's projection of the sufficiency of future taxable income to realize the assets.

Income tax accounting guidance (ASC Topic 740, *Income Taxes*) requires that the Organization record a liability for uncertain tax positions when it is more likely than not that a tax position would not be sustained if examined by the taxing authority. Insurance Services continually evaluates expiring statutes of limitations, audits, proposed settlements, changes in tax law and new authoritative rulings.

Advertising

Insurance Services expenses advertising and other promotional costs as they are incurred. These types of expenses for mailing campaigns, newsletters and similar activities were approximately \$454,000 and \$543,000 for the years ended December 31, 2017 and 2016, respectively.

**American Academy of Family Physicians
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Subsequent Events

Subsequent events have been evaluated through May 21, 2018, which is the date the consolidated financial statements were available to be issued.

Note 2: Investments and Investment Return

Investments at December 31 consisted of the following:

	2017	2016
Money markets accounts	\$ 422,835	\$ 408,339
Common and preferred stock	6,532,696	6,365,906
Equity mutual funds	4,386,243	2,891,949
Fixed income mutual funds	1,264,911	1,053,552
Corporate bonds	1,679,838	1,638,452
Treasury and federal agency obligations	1,094,193	1,623,054
Pooled investment funds	1,454,405	1,255,080
Hedge fund	2,207	8,991
	<u>\$ 16,837,328</u>	<u>\$ 15,245,323</u>

Total investment return is comprised of the following:

	2017	2016
Interest and dividend income	\$ 370,262	\$ 303,165
Realized gains	791,607	196,827
Unrealized gains	1,098,931	439,153
Investment fees and expenses	(84,856)	(82,632)
Change in value of split-interest agreements	31,156	10,597
	<u>\$ 2,207,100</u>	<u>\$ 867,110</u>

**American Academy of Family Physicians
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Notes to Consolidated Financial Statements
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Note 3: Split-Interest Agreements

Charitable Remainder Trusts

The Foundation is the beneficiary of two charitable remainder unitrusts. The trusts provide for a lifetime benefit to be paid to the donor or other designated beneficiary. Upon the death of the beneficiaries, the remaining trust assets are distributed in accordance with the trust document.

The Foundation is the trustee and sole remainder beneficiary of one of the trusts. The fair values of the trust assets were \$48,726 and \$46,046 as of December 31, 2017 and 2016, respectively, and are included in investments in the Foundation's consolidated statement of financial position. The Foundation has recorded a liability at December 31, 2017 and 2016, of \$29,026 and \$28,387, respectively, which represents the present value of the future obligations to make distributions to the designated beneficiaries.

The second trust is administered by an outside party. Therefore, the estimated value of the expected future cash flows of \$59,376 and \$54,593, which represents the fair value of the trust assets at December 31, 2017 and 2016, respectively, is recorded as "beneficial interest in trust assets" on the consolidated statement of financial position.

Pooled Income Fund

The Foundation manages a pooled income fund in which donors who contribute to the fund 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. Until the donor's death, the donor or the donor's designated beneficiary is paid the actual ordinary income earned on the donor's units. Upon the donor's death, the value of the assigned units reverts to the Foundation.

The Foundation recognizes its remainder interest in the assets received as temporarily restricted contribution revenue in the period in which the assets are received from the donor. The contributed assets are recognized at fair value when received. The difference between the fair value of the assets when received and the revenue recognized is recorded as deferred revenue, representing the amount of discount for future interest.

The fair value of the pooled income fund assets was \$114,446 and \$101,534 as of December 31, 2017 and 2016, respectively, and is included in "investments" in the consolidated statement of financial position. The present value of the estimated future payments is calculated using a discount rate ranging from 5.75 percent to 8.75 percent and applicable life expectancy tables. The estimated future liability of the pooled income fund was \$32,252 and \$34,237 as of December 31, 2017 and 2016, respectively, and is included in "liabilities under split-interest agreements" in the consolidated statement of financial position.

**American Academy of Family Physicians
Foundation and Subsidiary
Notes to Consolidated Financial Statements
December 31, 2017 and 2016**

Charitable Gift Annuity

The Foundation has been the recipient of a gift annuity which requires future payments to the donor or their named beneficiaries. The assets received from the donor are recorded at fair value. The Foundation has recorded a liability at December 31, 2017 and 2016 of \$143,713 and \$135,223, respectively, which represents the present value of the future annuity obligations. The liability had been determined using a discount rate of 1.8 percent and a rate of return of 4.4 percent. Contribution revenue recognized under the agreement was \$0 and \$176,800 for the years ended December 31, 2017 and 2016, respectively.

Note 4: Net Assets

Board-Designated Net Assets

Certain net assets have been designated by the Board for the following purposes:

	2017	2016
General endowment	\$ 9,208,754	\$ 8,783,600
Center for the History of Family Medicine endowment	1,301,887	1,116,692
Panther endowment	40,370	36,008
Total board-designated endowments	<u>10,551,011</u>	<u>9,936,300</u>
Family Medicine Philanthropic Consortium	104,134	108,637
Research committee mentorships	<u>15,367</u>	<u>15,366</u>
	<u><u>\$ 10,670,512</u></u>	<u><u>\$ 10,060,303</u></u>

**American Academy of Family Physicians
Foundation and Subsidiary**
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Temporarily Restricted Net Assets

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

	<u>2017</u>	<u>2016</u>
Resident Service Award	\$ 496,691	\$ 461,059
Center for the History of Family Medicine	702,398	485,567
Family Medicine Cares	84,138	55,180
Family Medicine Leads	109,113	82,709
Stern Lectureship	122,638	108,141
Special projects	88,199	100,796
Charitable remainder trusts	77,022	61,958
Pooled income fund	82,194	67,297
Disaster relief fund	47,540	57,366
Ruth Ostergaard Children's Fund	34,898	21,416
Immunization program	7,216	7,216
Other	<u>130,204</u>	<u>81,775</u>
	<u>\$ 1,982,251</u>	<u>\$ 1,590,480</u>

**American Academy of Family Physicians
Foundation and Subsidiary
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Permanently Restricted Net Assets

Permanently restricted net assets at December 31 are restricted to:

	2017	2016
Investment in perpetuity, the income of which is expendable to support		
Family Medicine Leads Scholarships (McCord endowment)	\$ 140,432	\$ 123,938
Ruth Ostergaard Children’s Fund	103,913	102,813
Robert Graham Center	434,282	407,823
Family Medicine Leads (Lopez endowment)	87,985	87,985
Research (Lopez Pollina endowment)	135,066	117,569
Fellowship in the History of Family Medicine (Panther endowment)	22,226	20,726
Family Medicine Residents and Students (Walters endowment)	54,854	52,674
Family Medicine Cares International (Smith endowment)	100,467	-
Lectureship on Ethics, Professionalism, and Family Medicine Values (Feldman endowment)	50,000	-
Family Medicine Leads Emerging Leader Institute (Hughes Melton endowment)	25,000	-
Family Medicine Leads Emerging Leader Institute (Smith endowment)	25,000	-
Investment in perpetuity, the income of which is expendable upon board approval to support		
Center for the History of Family Medicine	1,001,401	960,237
Charitable remainder trusts	14,844	13,648
	<u>\$ 2,195,470</u>	<u>\$ 1,887,413</u>

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Net Assets Released from Restrictions

Net assets were released from donor restrictions by incurring expenses satisfying the restricted purposes or by occurrence of other events by donors.

	<u>2017</u>	<u>2016</u>
Special projects	\$ 276,860	\$ 522,653
Family Medicine Cares	72,931	101,480
Family Medicine Leads	105,300	97,000
Immunization program	174,204	129,965
Disaster relief	135,813	1,589
Highlight on Diabetes	140,272	6,533
Resident Service Award	33,000	33,000
Stern Lectureship	1,500	1,500
Ruth Ostergaard Children's Fund	5,000	6,200
Other	1,354	5,743
	<u>\$ 946,234</u>	<u>\$ 905,663</u>

Note 5: Endowment

The Foundation's endowment consists of twelve individual funds established for a variety of purposes. The endowment includes both donor-restricted endowment funds and funds designated by the governing body to function as endowments (board-designated endowment funds). As required by accounting principles generally accepted in the United States of America (GAAP), net assets associated with endowment funds, including board-designated endowment funds, are classified and reported based on the existence or absence of donor-imposed restrictions.

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The Foundation's governing body has interpreted the State of Kansas *Prudent Management of Institutional Funds Act* (KPMIFA) as requiring preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the Foundation classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of donor-restricted endowment funds is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Foundation in a manner consistent with the standard of prudence prescribed by KPMIFA. In accordance with KPMIFA, the Foundation considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

1. Duration and preservation of the fund
2. Purposes of the Foundation and the fund
3. General economic conditions
4. Possible effect of inflation and deflation
5. Expected total return from investment income and appreciation or depreciation of investments
6. Other resources of the Foundation
7. Investment policies of the Foundation

The composition of net assets by type of endowment fund at December 31, 2017 and 2016, was:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
December 31, 2017				
Donor-restricted	\$ -	\$ 834,376	\$ 2,180,626	\$ 3,015,002
Board-designated	10,551,011	-	-	10,551,011
	<u>\$ 10,551,011</u>	<u>\$ 834,376</u>	<u>\$ 2,180,626</u>	<u>\$ 13,566,013</u>
Total endowment funds	<u>\$ 10,551,011</u>	<u>\$ 834,376</u>	<u>\$ 2,180,626</u>	<u>\$ 13,566,013</u>
December 31, 2016				
Donor-restricted	\$ -	\$ 550,093	\$ 1,873,765	\$ 2,423,858
Board-designated	9,936,300	-	-	9,936,300
	<u>\$ 9,936,300</u>	<u>\$ 550,093</u>	<u>\$ 1,873,765</u>	<u>\$ 12,360,158</u>
Total endowment funds	<u>\$ 9,936,300</u>	<u>\$ 550,093</u>	<u>\$ 1,873,765</u>	<u>\$ 12,360,158</u>

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Changes in endowment net assets for the years ended December 31, 2017 and 2016 were:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets, January 1, 2016	\$ 10,177,045	\$ 448,091	\$ 1,758,727	\$ 12,383,863
Investment return				
Investment income	141,895	28,979	1,045	171,919
Net appreciation	439,761	84,823	13,484	538,068
Total investment return	<u>581,656</u>	<u>113,802</u>	<u>14,529</u>	<u>709,987</u>
Contributions	590	-	100,509	101,099
Appropriation of endowment assets for expenditures	(367,325)	(11,800)	-	(379,125)
Other transfers	<u>(455,666)</u>	<u>-</u>	<u>-</u>	<u>(455,666)</u>
Endowment net assets, December 31, 2016	<u>9,936,300</u>	<u>550,093</u>	<u>1,873,765</u>	<u>12,360,158</u>
Investment return				
Investment income	200,382	45,199	568	246,149
Net appreciation	1,276,195	252,784	58,626	1,587,605
Total investment return	<u>1,476,577</u>	<u>297,983</u>	<u>59,194</u>	<u>1,833,754</u>
Contributions	2,615	-	247,667	250,282
Appropriation of endowment assets for expenditures	(401,000)	(13,700)	-	(414,700)
Other transfers	<u>(463,481)</u>	<u>-</u>	<u>-</u>	<u>(463,481)</u>
Endowment net assets, December 31, 2017	<u>\$ 10,551,011</u>	<u>\$ 834,376</u>	<u>\$ 2,180,626</u>	<u>\$ 13,566,013</u>

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Amounts of donor-restricted endowment funds classified as permanently and temporarily restricted net assets at December 31 consisted of:

	2017	2016
Permanently restricted net assets		
Portion of perpetual endowment funds required to be retained permanently by explicit donor stipulation or KPMIFA	\$ 2,180,626	\$ 1,873,765
Temporarily restricted net assets		
Portion of perpetual endowment funds subject to a time restriction under KPMIFA with purpose restrictions	\$ 834,376	\$ 550,093

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level the Foundation is required to retain as a fund of perpetual duration pursuant to donor stipulation or KPMIFA. In accordance with GAAP, deficiencies of this nature are reported in unrestricted net assets. There were no deficiencies of this nature at December 31, 2017 and 2016.

The Foundation has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs and other items supported by its endowment while seeking to maintain the purchasing power of the endowment. Endowment assets include those assets of donor-restricted endowment funds the Foundation must hold in perpetuity or for donor-specified periods, as well as those of board-designated endowment funds. Under the Foundation's policies, endowment assets are invested in a manner that is intended to grow the principal of the funds while assuming a tolerable level of investment risk. The Foundation expects its endowment funds to provide an average rate of return of approximately 7.5 percent annually over time. Actual returns in any given year may vary from this amount.

To satisfy its long-term rate of return objectives, the Foundation relies on a total return strategy in which investment returns are achieved through both current yield (investment income such as dividends and interest) and capital appreciation (both realized and unrealized). The Foundation targets a diversified asset allocation that places a greater emphasis on equity-based investments to achieve its long-term return objectives within prudent risk constraints.

When specified, the Foundation follows the donor's stipulations in the endowment agreement regarding the appropriation of endowment earnings. For board-designated funds, earnings are being reinvested until determined expendable by the board. For donor funds, earnings are being reinvested until the endowment reaches a point that the earnings would support the intended purpose of the endowment in perpetuity.

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Note 6: Conditional Grants

In May 2007, the Foundation entered into an agreement with Eli Lilly and Company Foundation, Inc. (Lilly) whereby Lilly agreed to grant \$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.

This grant is cancellable by the grantor at any time with or without cause with unexpended or uncommitted advances to be refunded. The Foundation retains a 5 percent fee for administering the grant. Through December 31, 2017, the Foundation had received \$15,000,000 under this grant agreement and \$15,000,000 in expenses had been incurred. The balance of \$0 and \$67,747 is included in deferred revenue at December 31, 2017 and 2016, respectively.

Note 7: Related-Party Transactions

The Organization and the Academy are related parties that are not financially interrelated organizations.

The Academy provides certain services to the Foundation under an administrative services agreement. The administrative services agreement includes services such as day-to-day executive, administrative, legal, accounting, clerical and other services in connection with the operations of the Foundation. The Foundation reimburses the Academy for direct costs under the agreement. In addition, the Foundation pays the Academy an additional service fee equal to 22.2 percent of the aggregate allocated amount of the actual salaries, fringe benefits and payroll taxes and a flat fee of \$25,000 per year. Fees paid under the administrative services agreement were \$1,745,354 and \$1,925,198 for 2017 and 2016, respectively. The Foundation also paid \$467,495 in 2017 and \$479,059 in 2016 for grants and related costs to the Academy.

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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:

	2017	2016
Dues check-off (pass through donations)	\$ 189,325	\$ 204,068
Contributions directed through the Academy	68,674	52,043
Contributions from the Academy to the Foundation	5,379	-
Center for the History of Family Medicine support	15,000	15,000
Other	53,550	69,295
	\$ 331,928	\$ 340,406

Foundation accounts receivable included revenues and other support from the Academy of \$48,946 and \$52,900 at December 31, 2017 and 2016, respectively. Accounts payable include \$650,594 and \$716,226 at December 31, 2017 and 2016, respectively, due to the Academy by the Foundation for services and other items.

Insurance Services remitted reimbursements to the Academy for common administrative costs (postage, internet and telephone) and marketing expenses in the amount of \$188,203 and \$160,453 in 2017 and 2016, respectively. The amount due to the Academy was \$0 and \$22,354 as of December 31, 2017 and 2016, respectively, for these common administrative and marketing expenses.

The Academy, as the contract holder, controls certain plans administered by Insurance Services. Insurance Services administers Academy-sponsored life insurance plans and, pursuant to a royalty agreement relating thereto, incurred costs to the Academy of \$71,914 and \$75,742 for the years ended December 31, 2017 and 2016, respectively.

Note 8: Operating Leases

Insurance Services entered into a noncancellable operating lease for office space with the Academy, which expires in 2019. This lease requires Insurance Services to pay additional rent, to be determined annually, for related operating expenses, taxes and other rent provisions. Rental payments include minimum rentals, plus a fixed monthly fee for certain utilities.

Future minimum lease payments at December 31, 2017 were:

2018	\$ 78,880
2019	53,312
	\$ 132,192

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Rent expense under this operating lease was \$77,248 and \$75,616, respectively, for the years ended December 31, 2017 and 2016, respectively.

Note 9: Income Taxes

The provision for federal and state income taxes consists of the following components for the years ended December 31:

	<u>2017</u>	<u>2016</u>
Current expense	\$ 538,500	\$ 689,400
Deferred benefit (expense)	<u>22,700</u>	<u>1,600</u>
Total income tax expense	<u>\$ 561,200</u>	<u>\$ 691,000</u>

A reconciliation of income tax expense at the statutory rate to the Company's actual income tax expense is shown below:

	<u>2017</u>	<u>2016</u>
Computed at the statutory rate (34%)	\$ 495,977	\$ 609,042
Increase (decrease) resulting from		
Nondeductible meals and entertainment	654	502
State income taxes - net of federal tax benefit	66,519	81,651
Other	<u>(1,950)</u>	<u>(195)</u>
Actual tax provision	<u>\$ 561,200</u>	<u>\$ 691,000</u>

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The tax effects of temporary differences related to deferred taxes shown on the consolidated statement of financial position were:

	<u>2017</u>	<u>2016</u>
Deferred tax assets		
Accrued vacation	\$ 7,300	\$ 34,900
Deferred tax liability		
Book/tax difference on fixed assets	<u>(7,100)</u>	<u>(12,000)</u>
Net deferred tax asset	<u>\$ 200</u>	<u>\$ 22,900</u>

The above net deferred tax asset is presented on the consolidated statement of financial position as follows:

	<u>2017</u>	<u>2016</u>
Deferred tax asset	\$ 7,300	\$ 34,900
Deferred tax liability	<u>(7,100)</u>	<u>(12,000)</u>
Net deferred tax asset	<u>\$ 200</u>	<u>\$ 22,900</u>

On December 22, 2017, the United States enacted tax reform legislation through the *Tax Cuts and Jobs Act*, which significantly changes the existing U.S. tax laws, including a reduction in the corporate tax rate from 34 percent to 21 percent, as well as other changes. As a result of enactment of the legislation, the Company remeasured certain deferred tax assets and liabilities for the year ended December 31, 2017 and will utilize this new rate effective January 1, 2018.

Note 10: Commitments

On April 4, 2017, Insurance Services entered into an agreement with the President of Insurance Services effective July 1, 2017. The agreement stated the President will continue to serve as President of Insurance Services and continue to be compensated pursuant to the terms of his last Employment Contract, effective July 1, 2016. In addition, the President will receive two weeks of vacation and the Company will pay to the President all accrued and unused vacation, which totaled approximately \$80,000 as of December 31, 2017. The President resigned his position as President of Insurance Services effective December 31, 2017. Insurance Services, in recognition of the President's outstanding years of service to Insurance Services, elected to pay the President a severance of approximately \$196,000, which is accrued as of December 31, 2017, in the accounts payable and accrued liability line item on the accompanying consolidated statements of financial position.

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Note 11: Profit Sharing Plan and 401(k) Plan

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 for the Defined Contribution Plan is seven percent (7 percent) of each participant's annual salary. Additionally, Insurance Services has a 401(k) plan and Insurance Services matches employee contributions up to an additional four percent (4 percent) of compensation. Insurance Services contributed \$89,334 and \$84,813 to the plans in 2017 and 2016, respectively.

Retirement benefits for the Foundation are provided under the administrative services agreement with the Academy.

Note 12: Functional Expenses

The costs of supporting activities have been allocated to the various programs in the consolidated statement of activities. Expenses summarized on a functional basis are shown below. Certain costs have been allocated among the program, administration and fundraising categories based on time expended, usage and other methods.

	<u>2017</u>	<u>2016</u>
Foundation		
Program services	\$ 2,999,091	\$ 3,044,298
Administration	480,714	472,109
Fundraising	808,062	942,717
Insurance Services	<u>2,878,773</u>	<u>2,821,965</u>
	<u>\$ 7,166,640</u>	<u>\$ 7,281,089</u>

Note 13: Disclosures About Fair Value of Assets and Liabilities

Fair value is 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. Fair value measurements must maximize the use of observable inputs and minimize the use of unobservable inputs. There is a hierarchy of three levels of inputs that may be used to measure fair value:

Level 1 Quoted prices in active markets for identical assets or liabilities

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- Level 2** Observable inputs other than Level 1 prices, 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
- Level 3** Unobservable inputs supported by little or no market activity and are significant to the fair value of the assets or liabilities

Recurring Measurements

The following tables present the fair value measurements of assets recognized in the accompanying consolidated statement of financial position measured at fair value on a recurring basis and the level within the fair value hierarchy in which the fair value measurements fall at December 31, 2017 and 2016:

	Fair Value Measurements Using			
	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
December 31, 2017				
Investments				
Money markets accounts	\$ 422,835	\$ 422,835	\$ -	\$ -
Common and preferred stock	6,532,696	6,532,696	-	-
Equity mutual funds	4,386,243	4,386,243	-	-
Fixed income mutual funds	1,264,911	1,264,911	-	-
Corporate bonds	1,679,838	-	1,679,838	-
Treasury and federal agency obligations	1,094,193	-	1,094,193	-
Pooled investment funds	1,454,405	-	1,454,405	-
Hedge fund	2,207	-	-	2,207
Beneficial interest in trust assets	59,376	-	59,376	-
	<u>\$ 16,896,704</u>	<u>\$ 12,606,685</u>	<u>\$ 4,287,812</u>	<u>\$ 2,207</u>

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	Fair Value	Fair Value Measurements Using		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
December 31, 2016				
Investments				
Money markets accounts	\$ 408,339	\$ 408,339	\$ -	\$ -
Common and preferred stock	6,365,906	6,365,906	-	-
Equity mutual funds	2,891,949	2,891,949	-	-
Fixed income mutual funds	1,053,552	1,053,552	-	-
Corporate bonds	1,638,452	-	1,638,452	-
Treasury and federal agency obligations	1,623,054	-	1,623,054	-
Pooled investment funds	1,255,080	-	1,255,080	-
Hedge fund	8,991	-	-	8,991
Beneficial interest in trust assets	54,593	-	54,593	-
	<u>\$ 15,299,916</u>	<u>\$ 10,719,746</u>	<u>\$ 4,571,179</u>	<u>\$ 8,991</u>

Following is a description of the valuation methodologies and inputs used for assets and measured at fair value on a recurring basis and recognized in the accompanying consolidated statement of financial position, as well as the general classification of such assets and liabilities pursuant to the valuation hierarchy. There have been no significant changes in the valuation techniques during the year ended December 31, 2017.

Investments

Where quoted market prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. If quoted market prices are not available, then fair values are estimated by using quoted prices of securities with similar characteristics or independent asset pricing services and pricing models, the inputs of which are market-based or independently sourced market parameters, including, but not limited to, yield curves, interest rates, volatilities, prepayments, defaults, cumulative loss projections and cash flows. Such securities are classified in Level 2 of the valuation hierarchy. In certain cases where Level 1 or Level 2 inputs are not available, securities are classified within Level 3 of the hierarchy.

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The value of certain investments, classified as pooled investments and hedge fund, is determined using net asset value (or its equivalent) as a practical expedient. The pooled investment fund invests primarily in publicly traded mutual funds and a limited partnership. Investment income and realized and unrealized gains and losses from securities in the pooled investment fund are allocated monthly to the fund partners based on the relationship of the fair value of the interest of each partner's account to the total fair value of the pooled investment fund, as adjusted for additions to or deductions from those accounts. The Foundation has the ability to redeem the pooled investments at any time and has, therefore, categorized these investments as Level 2. The underlying investments of the hedge fund include a portfolio of alternative investments funds. The hedge fund is currently in liquidation with expected payouts through 2018. As the hedge fund is invested in alternative investment funds without observable inputs, the Foundation has categorized the investment as Level 3.

Fair value determinations for Level 3 measurements of securities are the responsibility of management. Management challenges the reasonableness of the assumptions used and reviews the methodology to ensure the estimated fair value complies with accounting standards generally accepted in the United States.

Beneficial Interest in Trust Assets

Fair value is estimated at the present value of the future distributions expected to be received over the term of the agreement. Due to the nature of the valuation inputs, the interest is classified within Level 2 of the hierarchy.