

# **Cystic Fibrosis Foundation**

**Consolidated Financial Statements**

**For the years ended December 31, 2017 and**

**December 31, 2016**



KPMG LLP  
Suite 12000  
1801 K Street, NW  
Washington, DC 20006

## Independent Auditors' Report

The Board of Trustees  
Cystic Fibrosis Foundation:

We have audited the accompanying consolidated financial statements of the Cystic Fibrosis Foundation, which comprise the consolidated statements of financial position as of December 31, 2017 and 2016, and the related consolidated statements of activities, functional expenses, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

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

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

### *Auditors' Responsibility*

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

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

### *Opinion*

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Cystic Fibrosis Foundation as of December 31, 2017 and 2016, and the changes in their net assets, and their cash flows for the years then ended in accordance with U.S. generally accepted accounting principles.

**KPMG LLP**

Washington, DC  
May 2, 2018

**Cystic Fibrosis Foundation**  
**Consolidated Statements of Financial Position**  
**As of December 31, 2017 and December 31, 2016**

|  | 2017                    | 2016                    |
|--|-------------------------|-------------------------|
| <b>Assets</b>                          |                         |                         |
| Cash and cash equivalents              | \$ 138,231,954          | \$ 101,987,992          |
| Investments                            | 4,239,695,576           | 3,795,790,436           |
| Receivables, net                       | 12,137,402              | 15,658,290              |
| Other assets                           | 5,403,261               | 11,401,161              |
| Fixed assets, net                      | 11,959,914              | 7,069,182               |
| Total assets                           | <u>\$ 4,407,428,107</u> | <u>\$ 3,931,907,061</u> |
| <b>Liabilities and Net Assets</b>      |                         |                         |
| Accounts payable and other liabilities | 36,422,049              | 27,044,203              |
| Awards payable                         | 176,819,993             | 172,707,680             |
| Total liabilities                      | <u>213,242,042</u>      | <u>199,751,883</u>      |
| Unrestricted net assets:               |                         |                         |
| Undesignated net assets                | 881,431,067             | 420,457,947             |
| Board-designated net assets            | 3,300,000,000           | 3,300,000,000           |
| Total unrestricted net assets          | <u>4,181,431,067</u>    | <u>3,720,457,947</u>    |
| Temporarily restricted net assets      | 8,657,764               | 7,954,458               |
| Permanently restricted net assets      | 4,097,234               | 3,742,773               |
| Total net assets                       | <u>4,194,186,065</u>    | <u>3,732,155,178</u>    |
| Total liabilities and net assets       | <u>\$ 4,407,428,107</u> | <u>\$ 3,931,907,061</u> |

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

**Cystic Fibrosis Foundation**  
**Consolidated Statement of Activities**  
**For the year ended December 31, 2017**

|   | <u>Unrestricted</u> | <u>Temporarily<br/>Restricted</u> | <u>Permanently<br/>Restricted</u> | <u>Total</u>     |
|---|---------------------|-----------------------------------|-----------------------------------|------------------|
| <b>Revenue</b>  |                     |                                   |                                   |                  |
| Support received from the public  |                     |                                   |                                   |                  |
| Special event revenue   | \$ 93,931,027       | \$ 4,820,692                      | \$ -                              | \$ 98,751,719    |
| Direct benefit expenses   | (14,630,047)        | -                                 | -                                 | (14,630,047)     |
| Net special event revenue   | 79,300,980          | 4,820,692                         | -                                 | 84,121,672       |
| General contributions   | 20,912,188          | 5,690,571                         | -                                 | 26,602,759       |
| Total support received from the public                                      | 100,213,168         | 10,511,263                        | -                                 | 110,724,431      |
| Other   | 23,611,370          | 1,345,936                         | -                                 | 24,957,306       |
| Use of amounts restricted by donors for<br>specified purpose or time        | 11,253,893          | (11,153,893)                      | (100,000)                         | -                |
| Total revenue   | 135,078,431         | 703,306                           | (100,000)                         | 135,681,737      |
| <b>Expenses</b>   |                     |                                   |                                   |                  |
| Program services  |                     |                                   |                                   |                  |
| Medical programs  | 213,999,714         | -                                 | -                                 | 213,999,714      |
| Public and professional information and<br>education                        | 16,900,416          | -                                 | -                                 | 16,900,416       |
| Community services  | 17,822,831          | -                                 | -                                 | 17,822,831       |
| Total program services  | 248,722,961         | -                                 | -                                 | 248,722,961      |
| Supporting services   |                     |                                   |                                   |                  |
| Management and general  | 15,968,460          | -                                 | -                                 | 15,968,460       |
| Fundraising   | 24,702,883          | -                                 | -                                 | 24,702,883       |
| Total supporting services   | 40,671,343          | -                                 | -                                 | 40,671,343       |
| Total expenses  | 289,394,304         | -                                 | -                                 | 289,394,304      |
| Provision for lease commitment  | (4,358,356)         | -                                 | -                                 | (4,358,356)      |
| (Decrease) increase in net assets from<br>operations                        | (158,674,229)       | 703,306                           | (100,000)                         | (158,070,923)    |
| <b>Other changes in net assets</b>  |                     |                                   |                                   |                  |
| Net nonoperating investment income  | 606,502,224         | -                                 | 454,461                           | 606,956,685      |
| Proceeds from sale of remainder of<br>member interest in specialty pharmacy | 13,145,125          | -                                 | -                                 | 13,145,125       |
| Increase in net assets  | 460,973,120         | 703,306                           | 354,461                           | 462,030,887      |
| Net assets, beginning of year   | 3,720,457,947       | 7,954,458                         | 3,742,773                         | 3,732,155,178    |
| Net assets, end of year   | \$ 4,181,431,067    | \$ 8,657,764                      | \$ 4,097,234                      | \$ 4,194,186,065 |

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

**Cystic Fibrosis Foundation**  
**Consolidated Statement of Activities**  
**For the year ended December 31, 2016**

|  | <u>Unrestricted</u> | <u>Temporarily<br/>Restricted</u> | <u>Permanently<br/>Restricted</u> | <u>Total</u>     |
|--|---------------------|-----------------------------------|-----------------------------------|------------------|
| <b>Revenue</b>   |                     |                                   |                                   |                  |
| Support received from the public                                     |                     |                                   |                                   |                  |
| Special event revenue  | \$ 95,198,407       | \$ 4,904,692                      | \$ -                              | \$ 100,103,099   |
| Direct benefit expenses  | (13,839,765)        | -                                 | -                                 | (13,839,765)     |
| Net special event revenue  | 81,358,642          | 4,904,692                         | -                                 | 86,263,334       |
| General contributions  | 25,830,249          | 5,150,599                         | -                                 | 30,980,848       |
| Total support received from the public                               | 107,188,891         | 10,055,291                        | -                                 | 117,244,182      |
| Royalty revenue  | 52,695,149          | -                                 | -                                 | 52,695,149       |
| Other  | 11,972,106          | 4,761                             | -                                 | 11,976,867       |
| Use of amounts restricted by donors for<br>specified purpose or time | 13,360,897          | (13,360,897)                      | -                                 | -                |
| Total revenue  | 185,217,043         | (3,300,845)                       | -                                 | 181,916,198      |
| <b>Expenses</b>  |                     |                                   |                                   |                  |
| Program services   |                     |                                   |                                   |                  |
| Medical programs   | 277,291,061         | -                                 | -                                 | 277,291,061      |
| Public and professional information<br>education                     | 14,539,590          | -                                 | -                                 | 14,539,590       |
| Community services   | 15,317,469          | -                                 | -                                 | 15,317,469       |
| Total program services   | 307,148,120         | -                                 | -                                 | 307,148,120      |
| Supporting services  |                     |                                   |                                   |                  |
| Management and general   | 13,912,941          | -                                 | -                                 | 13,912,941       |
| Fundraising  | 22,784,588          | -                                 | -                                 | 22,784,588       |
| Total supporting services  | 36,697,529          | -                                 | -                                 | 36,697,529       |
| Total expenses   | 343,845,649         | -                                 | -                                 | 343,845,649      |
| Decrease in net assets from operations                               | (158,628,606)       | (3,300,845)                       | -                                 | (161,929,451)    |
| <b>Other changes in net assets</b>                                   |                     |                                   |                                   |                  |
| Net nonoperating investment income                                   | 214,594,404         | -                                 | 65,697                            | 214,660,101      |
| Increase (decrease) in net assets                                    | 55,965,798          | (3,300,845)                       | 65,697                            | 52,730,650       |
| Net assets, beginning of year  | 3,664,492,149       | 11,255,303                        | 3,677,076                         | 3,679,424,528    |
| Net assets, end of year  | \$ 3,720,457,947    | \$ 7,954,458                      | \$ 3,742,773                      | \$ 3,732,155,178 |

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

**Cystic Fibrosis Foundation**  
**Consolidated Statements of Cash Flows**  
**For the years ended December 31, 2017 and December 31, 2016**

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|  | 2017                  | 2016                  |
|--|-----------------------|-----------------------|
| <b>Cash flows from operating activities</b>  |                       |                       |
| Increase in net assets   | \$ 462,030,887        | \$ 52,730,650         |
| Adjustments to reconcile increase in net assets<br>to net cash used in operating activities: |                       |                       |
| Net realized and unrealized gains on investments   | (562,100,833)         | (168,025,253)         |
| Decrease in discount on pledges  | (48,013)              | (163,382)             |
| Depreciation   | 3,009,824             | 2,171,334             |
| Loss on disposal of fixed assets   | 10,828                | 39,691                |
| Disposal of assets at former headquarters  | 119,646               | -                     |
| Provision for (recoveries of) losses on accounts receivable                                  | 11,592                | (3,049)               |
| Gain on sale of pharmacy   | (13,145,125)          | -                     |
| Decrease in receivables  | 3,557,309             | 34,980,351            |
| Increase in other assets   | (981,143)             | (2,593,154)           |
| Increase in accounts payable and accrued expenses  | 9,377,846             | 2,454,255             |
| Increase in awards payable   | 4,112,313             | 45,837,286            |
| Net cash used in operating activities  | <u>(94,044,869)</u>   | <u>(32,571,271)</u>   |
| <b>Cash flows from investing activities</b>  |                       |                       |
| Purchases of fixed assets  | (8,031,030)           | (4,730,053)           |
| Maturities/sales of investments  | 1,174,435,480         | 922,681,822           |
| Purchases of investments   | (1,056,239,787)       | (1,064,475,015)       |
| Proceeds from sale of remainder of member interest in specialty pharmacy                     | 20,124,168            | -                     |
| Net cash provided by (used in) investing activities  | <u>130,288,831</u>    | <u>(146,523,246)</u>  |
| Net increase (decrease) in cash and cash equivalents   | 36,243,962            | (179,094,517)         |
| Cash and cash equivalents, beginning of year   | <u>101,987,992</u>    | <u>281,082,509</u>    |
| Cash and cash equivalents, end of year   | <u>\$ 138,231,954</u> | <u>\$ 101,987,992</u> |

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

**Cystic Fibrosis Foundation**  
**Consolidated Statement of Functional Expenses**  
**For the year ended December 31, 2017**

| Nature of Costs of Services   | Program Services |   |                    | Supporting Services    |               | Total          |
|---|------------------|---|--------------------|------------------------|---------------|----------------|
|   | Medical Programs | Public and Professional Information and Education | Community Services | Management and General | Fundraising   |                |
| Therapeutics Development Program awards   | \$ 85,214,357    | \$ -  | \$ -               | \$ -                   | \$ -          | \$ 85,214,357  |
| Research grants   | 20,085,565       | -   | -                  | -                      | -             | 20,085,565     |
| Clinical research grants  | 21,571,664       | -   | -                  | -                      | -             | 21,571,664     |
| Center and adult care grants  | 33,994,693       | -   | -                  | -                      | -             | 33,994,693     |
| Clinical and research fellowship grants   | 4,837,947        | -   | -                  | -                      | -             | 4,837,947      |
| Quality improvement training program  | 4,382,168        | -   | -                  | -                      | -             | 4,382,168      |
| Patient assistance and other program grants   | -                | -   | 1,935,395          | -                      | -             | 1,935,395      |
| Salaries  | 19,167,212       | 9,483,692   | 8,176,979          | 9,608,093              | 13,943,478    | 60,379,454     |
| Employee benefits and payroll taxes   | 4,919,441        | 2,419,720   | 2,031,781          | 2,445,351              | 3,329,241     | 15,145,534     |
| Publications and printing   | 533,563          | 460,377   | 309,417            | 112,955                | 893,556       | 2,309,868      |
| Occupancy and insurance   | 2,978,966        | 845,116   | 703,612            | 931,709                | 1,462,423     | 6,921,826      |
| Postage and shipping  | 120,193          | 347,767   | 121,429            | 97,103                 | 986,649       | 1,673,141      |
| Travel and conferences  | 5,277,184        | 611,348   | 647,943            | 375,941                | 1,015,381     | 7,927,797      |
| Data processing   | 3,695,052        | 1,271,657   | 844,947            | 776,950                | 1,322,045     | 7,910,651      |
| Lab and other supplies  | 1,544,532        | 193,449   | 190,038            | 191,604                | 373,673       | 2,493,296      |
| Fees for legal hotline and other community services   | -                | -   | 1,744,625          | -                      | -             | 1,744,625      |
| Professional fees and medical honoraria   | 3,483,181        | 516,420   | 493,165            | 670,355                | 221,786       | 5,384,907      |
| Depreciation  | 1,505,820        | 409,483   | 321,019            | 277,915                | 495,587       | 3,009,824      |
| Other   | 688,176          | 341,387   | 302,481            | 480,484                | 659,064       | 2,471,592      |
| Total functional expenses before investment expenses and costs of direct benefits to donors | 213,999,714      | 16,900,416  | 17,822,831         | 15,968,460             | 24,702,883    | 289,394,304    |
| Investment expenses   | -                | -   | -                  | 12,822,543             | -             | 12,822,543     |
| Costs of direct benefits to donors  | -                | -   | -                  | -                      | -             | 14,630,047     |
| Total functional expenses after investment expenses and costs of direct benefits to donors  | \$ 213,999,714   | \$ 16,900,416                                     | \$ 17,822,831      | \$ 28,791,003          | \$ 24,702,883 | \$ 316,846,894 |

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

**Cystic Fibrosis Foundation**  
**Consolidated Statement of Functional Expenses**  
**For the year ended December 31, 2016**

| Nature of Costs of Services   | Program Services      |   |                      | Supporting Services    |                      | Total                 |
|---|-----------------------|---|----------------------|------------------------|----------------------|-----------------------|
|   | Medical Programs      | Public and Professional Information and Education | Community Services   | Management and General | Fundraising          |                       |
| Therapeutics Development Program awards   | \$ 157,764,535        | \$ -  | \$ -                 | \$ -                   | \$ -                 | \$ 157,764,535        |
| Research grants   | 17,809,839            | -   | -                    | -                      | -                    | 17,809,839            |
| Clinical research grants  | 18,996,738            | -   | -                    | -                      | -                    | 18,996,738            |
| Center and adult care grants  | 34,387,281            | -   | -                    | -                      | -                    | 34,387,281            |
| Clinical and research fellowship grants   | 3,883,778             | -   | -                    | -                      | -                    | 3,883,778             |
| Quality improvement training program  | 3,763,507             | -   | -                    | -                      | -                    | 3,763,507             |
| Patient assistance and other program grants   | -                     | -   | 1,877,416            | -                      | -                    | 1,877,416             |
| Salaries  | 16,700,637            | 7,690,000   | 6,777,256            | 8,270,305              | 12,953,561           | 52,391,759            |
| Employee benefits and payroll taxes   | 3,824,569             | 2,063,442   | 1,664,325            | 2,128,889              | 3,186,976            | 12,868,201            |
| Publications and printing   | 438,029               | 501,962   | 247,506              | 134,551                | 998,125              | 2,320,173             |
| Occupancy and insurance   | 3,224,078             | 620,642   | 583,466              | 686,551                | 1,264,448            | 6,379,185             |
| Postage and shipping  | 185,099               | 218,969   | 128,090              | 104,637                | 788,201              | 1,424,996             |
| Travel and conferences  | 5,246,790             | 492,462   | 533,693              | 350,119                | 861,316              | 7,484,380             |
| Data processing   | 4,074,742             | 1,437,507   | 1,051,997            | 731,239                | 1,409,296            | 8,704,781             |
| Lab and other supplies  | 1,416,518             | 173,990   | 174,874              | 164,288                | 393,952              | 2,323,622             |
| Fees for legal hotline and other community services   | -                     | -   | 1,415,375            | -                      | -                    | 1,415,375             |
| Professional fees and medical honoraria   | 3,746,161             | 845,826   | 486,529              | 791,702                | 220,055              | 6,090,273             |
| Depreciation  | 1,217,256             | 255,764   | 179,706              | 183,085                | 335,523              | 2,171,334             |
| Other   | 611,504               | 239,026   | 197,236              | 367,575                | 373,135              | 1,788,476             |
| Total functional expenses before investment expenses and costs of direct benefits to donors | 277,291,061           | 14,539,590  | 15,317,469           | 13,912,941             | 22,784,588           | 343,845,649           |
| Investment expenses   | -                     | -   | -                    | 9,644,576              | -                    | 9,644,576             |
| Costs of direct benefits to donors  | -                     | -   | -                    | -                      | -                    | 13,839,765            |
| Total functional expenses after investment expenses and costs of direct benefits to donors  | <u>\$ 277,291,061</u> | <u>\$ 14,539,590</u>                              | <u>\$ 15,317,469</u> | <u>\$ 23,557,517</u>   | <u>\$ 22,784,588</u> | <u>\$ 367,329,990</u> |

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

# **Cystic Fibrosis Foundation**

## **Notes to Consolidated Financial Statements**

### **December 31, 2017 and 2016**

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#### **1. Organization**

The accompanying consolidated financial statements include the operations of the Cystic Fibrosis Foundation, including all of its field offices (the “Foundation”) and Cystic Fibrosis Foundation Therapeutics, Inc. (“CFFT”). CFFT, an affiliate of the Foundation, operates the Therapeutics Development Program, which supports activities related to cystic fibrosis (CF) drug discovery through the many stages of drug development and clinical evaluation. The mission of the Foundation and CFFT is to cure CF and to provide all people with the disease the opportunity to lead full, productive lives by funding research and drug development, promoting individualized treatment, and ensuring access to high quality, specialized care. The Board of Trustees authorized management of the Foundation to transfer the activities of CFFT to the Foundation in 2018.

#### **2. Summary of significant accounting policies**

##### **Basis of accounting**

The accompanying consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America applicable to voluntary health and welfare organizations. All inter-entity balances at year-end and transactions during the year have been eliminated in the consolidated financial statements. The consolidated financial statements are presented on the accrual basis. The expenses reported in the consolidated statement of activities are classified by function.

##### **Use of estimates**

The preparation of consolidated 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 dates of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Significant items subject to such estimates and assumptions include the allowance for doubtful accounts, investment fair value measurements and functional expense allocations. Actual results could differ materially, in the near term, from the amounts reported.

##### **Measure of operations**

The Foundation includes in its measure of operations all support received from the public, income on investments designated for operations, royalty revenue, other revenue and all costs of program and supporting services. The measure of operations excludes interest and dividends and realized and unrealized gains and losses on nonoperating investments. Nonoperating investments are amounts identified for investment over the intermediate to long term.

##### **Revenue recognition**

Support received directly or indirectly from the public is recorded as revenue when received or when the donor has made an unconditional promise to give. Conditional promises to give are not recognized until the conditions on which they depend are substantially met. Contributions of assets other than cash, including gifts-in-kind, are recorded at their estimated fair value at the date of the gift.

Contributions received are recorded as unrestricted, temporarily restricted, or permanently restricted support, depending on the existence or nature of any donor restrictions. All donor-restricted support,

# **Cystic Fibrosis Foundation**

## **Notes to Consolidated Financial Statements**

### **December 31, 2017 and 2016**

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including related investment income and realized and unrealized gains and losses, is reported as an increase in temporarily or permanently restricted net assets, depending on the nature of the restriction. When a restriction expires (that is, when a stipulated time restriction ends or purpose restriction is accomplished), temporarily restricted net assets are reclassified to unrestricted net assets and reported in the consolidated statement of activities as net assets released from restrictions.

CFF and CFFT retain legal and beneficial rights to intellectual property developed under certain scientific grants and drug discovery agreements. Revenues received under these agreements are recorded when earned. In addition, at times CFFT may sell its intangible rights under certain agreements in exchange for a lump sum. Amounts received under these agreements are recorded when rights are forfeited and proceeds are receivable. In November 2014, CFFT entered into an agreement to sell its intangible rights to future revenues under a drug discovery agreement. In October 2016, CFFT entered into an amendment to the 2014 agreement and recognized an additional \$51,400,000 in royalty revenue related to the sale. The net proceeds from these transactions are classified in operating activities on the consolidated statements of cash flows.

#### **Grants, contracts and awards**

The Foundation and CFFT generally award medical/scientific grants and contracts for periods of three years or less. Grants are awarded contingent upon renewal criteria at the beginning of each award period. Awards are expensed at the time that the Foundation or CFFT unconditionally commits to fund the grant or, for those contracts recorded as exchange transactions, when the contract expense has been incurred.

#### **Cash and cash equivalents**

Cash and cash equivalents represent demand deposits, money market funds and money market mutual funds. Cash equivalents consist of highly liquid investments with original maturities of three months or less and present an insignificant risk of change in value. The Foundation's investments in money market mutual funds are classified as Level 2 as defined in note 3 because they consist of funds that seek to maintain a stable net asset value (NAV) of \$1 per share. These funds are marketed to institutional investors directly or through financial intermediaries. Quoted prices in active markets are not available; however, the published NAV is a reasonable estimation of fair value because redemptions are priced at NAV and are generally available to the Foundation within one business day.

The Foundation had outstanding commitments to purchase \$35,000,000 of investments as of December 31, 2017. The cash associated with these commitments is classified as cash and cash equivalents within the fair value hierarchy, as described in Note 3, as of December 31, 2017 and the purchases were completed in January 2018.

#### **Investments**

Investment assets are stated at fair value in the consolidated financial statements. Where applicable, investments are stated at net asset value (NAV) as a practical expedient to fair value. Investment income is reported when earned. The change in unrealized appreciation or depreciation of investments is reflected in the consolidated statement of activities. Realized gains and losses on sales of investments are computed on an average cost basis and are recorded on the trade date of the transaction.

**Cystic Fibrosis Foundation**  
**Notes to Consolidated Financial Statements**  
**December 31, 2017 and 2016**

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**Other assets**

As of December 31, 2016, other assets included a 20% membership interest in specialty pharmacy, prepaid expenses and deposits. The membership interest in specialty pharmacy at December 31, 2016 was \$6,979,043. In February 2017, the Foundation sold its interest for \$20,124,168, net of \$734,949 in transaction costs, and recognized a net gain on the sale of \$13,145,125 in 2017.

**Fixed assets**

Fixed assets consisting of furniture, fixtures, equipment, software and leasehold improvements are recorded at cost and are depreciated over their estimated useful lives, ranging from three to ten years, on a straight-line basis. The cost and related accumulated depreciation of furniture, fixtures, equipment, software and leasehold improvements are removed from the accounts upon sale or disposition and any resulting gain or loss is reflected in the consolidated statement of activities.

**Functional expenses**

The costs of various Foundation activities have been accounted for on a functional basis in the consolidated statement of activities. Accordingly, certain costs have been allocated among the various activities.

**Net assets**

The Foundation's net assets have been grouped into the following classes:

*Unrestricted - Undesignated Net Assets* – Undesignated net assets generally result from revenues derived from receiving unrestricted contributions, investment income and royalty revenue, less Board-designated net assets and expenses incurred in providing program services, raising contributions, and performing administrative functions.

*Unrestricted - Board-Designated Net Assets* – The Foundation's Board of Trustees has designated \$3,300,000,000 as of December 31, 2017 and 2016 to be spent in support of the mission of the Foundation over the long term.

*Temporarily Restricted Net Assets* – Temporarily restricted net assets generally result from contributions and other inflows of assets whose use by the organization is limited by donor-imposed stipulations that either expire by passage of time or can be fulfilled and removed by actions of the Foundation or CFFT pursuant to those stipulations. Temporarily restricted net assets were restricted as summarized below as of December 31, 2017 and 2016.

|                                     | <b>2017</b>         | <b>2016</b>         |
|-------------------------------------|---------------------|---------------------|
| Time restricted                     | \$ 4,048,759        | \$ 2,963,661        |
| Medical research and other purposes | 4,609,005           | 4,990,797           |
|                                     | <u>\$ 8,657,764</u> | <u>\$ 7,954,458</u> |

*Permanently Restricted Net Assets* – The Foundation's permanently restricted net assets consist of the beneficial interest in seven donor-restricted funds that must be maintained in perpetuity. Net assets associated with perpetual trusts are classified

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and reported based on the existence or absence of donor-imposed restrictions. The Foundation has a policy of appropriating for operations each year the income received from the perpetual trusts.

Unrealized and realized gains and losses and dividends and interest may be included in any of these net asset classifications depending on donor restrictions.

#### **Income Taxes**

The Foundation and CFFT are not-for-profit voluntary health organizations exempt from Federal income taxes under Section 501(c)(3) of the Internal Revenue Code (the Code) and from state taxes and have been classified as organizations that are not private foundations under Section 509(a) of the Code. The Foundation does not have any unrelated business income tax liability as of December 31, 2017 and 2016. Contributions to the Foundation qualify for the charitable contributions deduction to the extent provided by Section 170 of the Code.

The Foundation is not aware of any tax position taken that requires disclosure based on current facts and circumstances. The Foundation annually reviews its tax positions and has determined that there are no material uncertain tax positions that require recognition or disclosure in the financial statements.

The Tax Cuts and Jobs Act (the Tax Act) was signed into law on December 22, 2017. The Tax Act includes several changes relevant to tax-exempt organizations, primarily related to unrelated business income, net operating losses, certain new excise taxes, and changes affecting the deductibility of certain expenses. Management has determined that the new law will not have a significant impact on the Foundation's financial statements.

### **3. Fair value measurements**

Authoritative guidance on fair value measurements requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The guidance describes three levels of inputs that may be used to measure fair value: Level 1 - Quoted prices in active markets for identical assets or liabilities. Level 2 - Observable inputs other than Level 1 prices, such as quoted prices for similar assets. Level 3 - Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets.

The following processes were used to determine the fair value of each class of financial instruments listed below:

- (a) Investment balances reported for amounts classified as Level 1 are derived from quoted market prices on public exchanges or, for funds similar to mutual funds, at published NAV.
- (b) Values reported for government and corporate bonds classified as Level 2 represent the portfolio managers' good faith estimate as to what a buyer in the marketplace would pay for these securities in a current sale. The Foundation believes these estimates are reflective of fair value. In deriving these estimates, the portfolio managers utilize pricing models and applications that incorporate available market information and, because many fixed income securities do not trade on a daily basis, apply available information through processes such as

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benchmark curves, benchmarking of like securities, sector groupings, and matrix pricing. These investments can be redeemed daily without restriction.

- (c) The fair value of the Foundation's interest in perpetual trusts is estimated using the fair value of the assets in the trusts, as that amount approximates the fair value of the Foundation's beneficial interests in the trusts. There is no active market for these trusts and they are therefore classified as Level 3.

The letter references in the following fair value tables refer to the above descriptions. Financial instruments measured at fair value on a recurring basis are summarized below as of December 31:

| Description                                 | 2017                    | Quoted Prices in<br>Active Markets for<br>Identical Assets<br>(Level 1) (a) | Significant Other<br>Observable Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) | Investments<br>measured at net<br>asset value <sup>1</sup> |
|---|-------------------------|---|---|--|--|
| Cash equivalents                            | \$ 106,697,533          | \$ -  | \$ 106,697,533                                      | \$ -   | \$ -   |
| Investments                                 |                         |   |   |  |  |
| Corporate debt securities                   | 237,600                 | -   | -   | 237,600  | -  |
| Corporate and other bond mutual funds       | 215,180,323             | 215,180,323   | -   | -  | -  |
| Short duration bond mutual funds            | 363,090,053             | 363,090,053   | -   | -  | -  |
| U.S. equity mutual funds                    | 107,665,055             | 107,665,055   | -   | -  | -  |
| International developed equity mutual funds | 348,688,286             | 348,688,286   | -   | -  | -  |
| Emerging markets equity mutual funds        | 91,395,062              | 91,395,062  | -   | -  | -  |
| Global equity mutual funds                  | 126,025,054             | 126,025,054   | -   | -  | -  |
| Other global equity securities              | 583,214,000             | 582,194,273   | 269,990   | 749,737  | -  |
| Global multi-asset strategy mutual funds    | 82,234,540              | 82,234,540  | -   | -  | -  |
| Fixed income index commingled funds         | 130,952,699             | 130,952,699   | -   | -  | -  |
| Public equity commingled funds              | 1,494,197,079           | 571,306,712   | -   | -  | 922,890,367  |
| Other public equity based strategies        | 99,856,362              | -   | -   | -  | 99,856,362   |
| Hedged strategies                           | 436,127,209             | -   | -   | -  | 436,127,209  |
| Private equity and other illiquid funds     | 152,546,327             | -   | -   | -  | 152,546,327  |
| Perpetual trusts                            | 4,097,234               | -   | -   | 4,097,234 (c)                                      | -  |
| Other                                       | 4,188,693               | 4,188,693   | -   | -  | -  |
| Total investments                           | 4,239,695,576           | 2,622,920,750   | 269,990   | 5,084,571  | 1,611,420,265  |
|   | <u>\$ 4,346,393,109</u> | <u>\$ 2,622,920,750</u>   | <u>\$ 106,967,523</u>                               | <u>\$ 5,084,571</u>                                | <u>\$ 1,611,420,265</u>                                    |

<sup>1</sup> Investments that are measured at fair value using the net asset value per share (or its equivalent) practical expedient have not been categorized in the fair value hierarchy. The fair value amounts presented in this table are intended to permit reconciliation of the fair value hierarchy to the amounts presented in the statement of financial position.

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| Description                                 | 2016                    | Quoted Prices in<br>Active Markets for<br>Identical Assets<br>(Level 1) (a) | Significant Other<br>Observable Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) | Investments<br>measured at net<br>asset value <sup>1</sup> |
|---|-------------------------|---|---|--|--|
| Cash equivalents                            | \$ 36,602,978           | \$ -  | \$ 36,602,978                                       | \$ -   | \$ -   |
| Investments                                 |                         |   |   |  |  |
| Corporate debt securities                   | 4,006,451               | -   | 4,006,451 (b)                                       | -  | -  |
| Corporate and other bond mutual funds       | 208,557,386             | 208,557,386   | -   | -  | -  |
| Short duration bond mutual funds            | 650,152,922             | 650,152,922   | -   | -  | -  |
| U.S. equity mutual funds                    | 88,088,210              | 88,088,210  | -   | -  | -  |
| International developed equity mutual funds | 165,092,107             | 165,092,107   | -   | -  | -  |
| Emerging markets equity mutual funds        | 42,636,380              | 42,636,380  | -   | -  | -  |
| Global equity mutual funds                  | 103,546,884             | 103,546,884   | -   | -  | -  |
| Other global equity securities              | 519,187,233             | 518,491,765   | 645,450   | 50,018   | -  |
| Global multi-asset strategy mutual funds    | 249,456,513             | 249,456,513   | -   | -  | -  |
| Exchange traded equity funds                | 232,277,464             | 232,277,464   | -   | -  | -  |
| Fixed income index commingled funds         | 124,856,726             | 124,856,726   | -   | -  | -  |
| Public equity commingled funds              | 1,023,485,288           | 259,617,236   | -   | -  | 763,868,052  |
| Other public equity based strategies        | 58,752,003              | -   | -   | -  | 58,752,003   |
| Hedged strategies                           | 241,362,101             | -   | -   | -  | 241,362,101  |
| Private equity and other illiquid funds     | 77,105,665              | -   | -   | -  | 77,105,665   |
| Perpetual trusts                            | 3,742,773               | -   | -   | 3,742,773 (c)                                      | -  |
| Other                                       | 3,484,330               | 3,484,330   | -   | -  | -  |
| Total investments                           | <u>3,795,790,436</u>    | <u>2,646,257,923</u>  | <u>4,651,901</u>                                    | <u>3,792,791</u>                                   | <u>1,141,087,821</u>                                       |
|   | <u>\$ 3,832,393,414</u> | <u>\$ 2,646,257,923</u>   | <u>\$ 41,254,879</u>                                | <u>\$ 3,792,791</u>                                | <u>\$ 1,141,087,821</u>                                    |

<sup>1</sup> Investments that are measured at fair value using the net asset value per share (or its equivalent) practical expedient have not been categorized in the fair value hierarchy. The fair value amounts presented in this table are intended to permit reconciliation of the fair value hierarchy to the amounts presented in the statement of financial position.

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The table below presents reconciliation information for financial instruments measured at fair value on a recurring basis using significant unobservable inputs (Level 3) during 2017 and 2016.

|  | <b>Perpetual<br/>Trusts</b> | <b>Global equity<br/>securities</b> | <b>Corporate debt<br/>securities</b> | <b>2017</b>         |
|--|-----------------------------|-------------------------------------|--------------------------------------|---------------------|
| Level 3 investments, beginning of year | \$ 3,742,773                | \$ 50,018                           | \$ -                                 | \$ 3,792,791        |
| Total gains or losses                  |                             |                                     |                                      |                     |
| Net realized gains                     | 166,859                     | -                                   | -                                    | 166,859             |
| Net unrealized gains                   | 385,795                     | -                                   | -                                    | 385,795             |
| Purchases/additions                    | 151,394                     | 699,719                             | 237,600                              | 1,088,713           |
| Sales/distributions                    | (349,587)                   | -                                   | -                                    | (349,587)           |
| Level 3 investments, end of year       | <u>\$ 4,097,234</u>         | <u>\$ 749,737</u>                   | <u>\$ 237,600</u>                    | <u>\$ 5,084,571</u> |
|  | <b>Perpetual<br/>Trusts</b> | <b>Global equity<br/>securities</b> | <b>Asset-backed<br/>securities</b>   | <b>2016</b>         |
| Level 3 investments, beginning of year | \$ 3,677,076                | \$ -                                | \$ 1,021,071                         | \$ 4,698,147        |
| Total gains or losses                  |                             |                                     |                                      |                     |
| Net realized (losses)                  | (30,570)                    | -                                   | (1,739)                              | (32,309)            |
| Net unrealized gains                   | 205,548                     | -                                   | -                                    | 205,548             |
| Purchases/additions                    | 94,976                      | 50,018                              | -                                    | 144,994             |
| Sales/distributions                    | (204,257)                   | -                                   | (1,019,332)                          | (1,223,589)         |
| Level 3 investments, end of year       | <u>\$ 3,742,773</u>         | <u>\$ 50,018</u>                    | <u>\$ -</u>                          | <u>\$ 3,792,791</u> |

The amount of net unrealized gains relating to Level 3 assets still held at December 31, 2017 and 2016 is approximately \$764,536 and \$410,370, respectively. Unrealized and realized gains and losses of Level 3 investments are classified as nonoperating investment income on the consolidated statement of activities.

The following table summarizes the nature of the Foundation's investments in funds valued based on net asset value as a practical expedient for fair value as of December 31, 2017 and 2016:

| <b>Description</b>                          | <b>Fair value</b>       |                         | <b>2017 unfunded<br/>commitments</b> | <b>Redemption frequency</b> |
|---|-------------------------|-------------------------|--------------------------------------|-----------------------------|
|   | <b>2017</b>             | <b>2016</b>             |                                      |                             |
| Public equity commingled funds (a)          | \$ 922,890,367          | \$ 763,868,052          | \$ -                                 | Monthly to quarterly        |
| Other public equity based strategies (a)    | 99,856,362              | 58,752,003              | -                                    | Monthly                     |
| Hedged strategies (b)                       | 436,127,209             | 241,362,101             | -                                    | Monthly to semi-annual      |
| Private equity and other illiquid funds (c) | 152,546,327             | 77,105,665              | 308,739,318                          | Illiquid                    |
|   | <u>\$ 1,611,420,265</u> | <u>\$ 1,141,087,821</u> | <u>\$ 308,739,318</u>                |                             |

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- (a) The Foundation maintains the ability to redeem these investments at the net asset values (NAV) reported by the investee managers and therefore uses these amounts to derive the reported investment values. Approximately \$204,846,000 of investments in this category are subject to a lock-up period expiring in one year or less and approximately \$63,168,000 of investments in this category are subject to a lock-up period expiring in three years.
- (b) Approximately \$54,504,000 of investments in this category once redeemed are payable at a maximum of 1/6 of the investment every June 30 and December 31.
- (c) The fair values of the investments in this category have been estimated using the NAV of the Foundation's ownership interest in partners' capital. Investments in this class cannot be redeemed. Instead, distributions are made from operating proceeds on a periodic basis. It is estimated that the underlying assets of these various funds will be liquidated over the next five to ten years.

The investment income is as follows for the years ended December 31:

|                        | <b>2017</b>           | <b>2016</b>           |
|------------------------|-----------------------|-----------------------|
| Interest and dividends | \$ 58,068,867         | \$ 56,600,061         |
| Net unrealized gains   | 483,673,911           | 159,852,206           |
| Net realized gains     | 78,306,929            | 8,034,583             |
| Investment expenses    | <u>(12,822,543)</u>   | <u>(9,644,576)</u>    |
|                        | <u>\$ 607,227,163</u> | <u>\$ 214,842,274</u> |

Operating cash equivalents and investments amounted to \$54,234,433 and \$3,485,282 as of December 31, 2017 and 2016, respectively. Nonoperating cash equivalents and investments amounted to \$4,292,158,676 and \$3,828,908,132 as of December 31, 2017 and 2016, respectively. The investment income during the years ended December 31, 2017 and 2016 is reflected on the consolidated statement of activities as follows:

|   | <b>2017</b>           | <b>2016</b>           |
|---|-----------------------|-----------------------|
| Investment income - operating (included in other) | \$ 270,478            | \$ 182,173            |
| Net nonoperating investment income                | <u>606,956,685</u>    | <u>214,660,101</u>    |
|   | <u>\$ 607,227,163</u> | <u>\$ 214,842,274</u> |

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**4. Receivables**

Receivables consist of the following at December 31, 2017 and 2016:

|  | <b>2017</b>          | <b>2016</b>          |
|--|----------------------|----------------------|
| Special events and other contributions                       | \$ 2,630,787         | \$ 2,278,994         |
| Pledges receivable   | 9,354,759            | 9,851,347            |
| Accrued interest on investments                              | 924,232              | 2,986,634            |
| Other receivable   | 1,065,641            | 2,661,664            |
|  | <u>13,975,419</u>    | <u>17,778,639</u>    |
| Discount on pledges receivable (at rates ranging from 1%-2%) | (1,235,823)          | (1,283,836)          |
| Allowance for doubtful accounts                              | (602,194)            | (836,513)            |
|  | <u>\$ 12,137,402</u> | <u>\$ 15,658,290</u> |

The pledges receivable as of December 31, 2017 and 2016 are payable in the following periods:

|                   | <b>2017</b>         | <b>2016</b>         |
|-------------------|---------------------|---------------------|
| Within one year   | \$ 2,866,401        | \$ 3,362,377        |
| One to five years | 4,903,125           | 4,717,959           |
| After five years  | 1,585,233           | 1,771,011           |
|                   | <u>\$ 9,354,759</u> | <u>\$ 9,851,347</u> |

As of December 31, 2017, and 2016, pledges receivable amounting to approximately \$2,784,000 and \$3,743,000, respectively, were due from members of the Board of Trustees or related organizations.

**5. Fixed assets**

Fixed assets at December 31, 2017 and 2016 consisted of the following:

|                          | <b>2017</b>          | <b>2016</b>         |
|--------------------------|----------------------|---------------------|
| Equipment and software   | \$ 14,499,977        | \$ 11,958,075       |
| Furniture and fixtures   | 921,412              | 675,729             |
| Leasehold improvements   | 5,663,396            | 1,719,584           |
|                          | <u>21,084,785</u>    | <u>14,353,388</u>   |
| Accumulated depreciation | (9,124,871)          | (7,284,206)         |
|                          | <u>\$ 11,959,914</u> | <u>\$ 7,069,182</u> |

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**6. Awards payable and commitments**

Changes in awards payable during the years ended December 31, 2017 and 2016 are summarized as follows:

|                                   | <b>2017</b>           | <b>2016</b>           |
|-----------------------------------|-----------------------|-----------------------|
| Awards payable, beginning of year | \$ 172,707,680        | \$ 126,870,394        |
| Awards expensed                   | 169,343,719           | 235,404,840           |
| Awards disbursed                  | <u>(165,231,406)</u>  | <u>(189,567,554)</u>  |
| Awards payable, end of year       | <u>\$ 176,819,993</u> | <u>\$ 172,707,680</u> |

As of December 31, 2017, the Foundation and CFFT have additional medical scientific grant commitments of approximately \$59,292,000 which extend through December 31, 2022. These subsequent year awards are contingent upon renewal criteria, and therefore the costs and liabilities are not reflected in the consolidated financial statements.

Certain agreements provide for future contracted drug discovery and development research payments amounting to approximately \$149,262,000. These costs will be expensed when the services are provided.

Volunteers from the medical and scientific community were included among affiliate Board members in 2017 and 2016. These volunteers provided valuable leadership and assistance to these Boards, but do not participate in decisions regarding awards to institutions with which they are affiliated. Awards to institutions affiliated with these volunteers totalled \$712,187 and \$551,569 for the years ended December 31, 2017 and 2016, respectively.

**7. Accounts payable and other liabilities**

Accounts payable at December 31, 2017 and 2016 consist of the following:

|  | <b>2017</b>          | <b>2016</b>          |
|--|----------------------|----------------------|
| Accounts payable and accrued expenses      | \$ 24,995,422        | \$ 21,816,859        |
| Former office lease liability (see Note 8) | 4,463,202            | -                    |
| Refundable advances for special events     | 3,298,678            | 3,493,288            |
| Deferred licensing and other revenue       | 2,615,679            | 864,983              |
| Other liabilities                          | <u>1,049,068</u>     | <u>869,073</u>       |
|  | <u>\$ 36,422,049</u> | <u>\$ 27,044,203</u> |

**8. Lease commitments**

In June 2017, the Foundation entered into a lease agreement for new office space in Maryland. The Foundation secured a favorable long-term rental rate for this space, which better meets the present and future needs of the Foundation. In 2017, the Foundation recognized a one-time charge of approximately \$4,358,356 to recognize the net future liability and exit costs (including costs to

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prepare the space for rental), associated with former office space. The liability (see Note 7) is calculated as the net present value of future cash outlays under the existing lease and the net present expected receipts from sublease arrangements. The Foundation remains obligated to pay rental costs and abide by terms of the original lease, which expires in April 2023. The Foundation has entered into sublease agreements for substantially all of the original office space.

The Foundation is obligated under various operating leases for office space as of December 31, 2017. The approximate future minimum commitments for each calendar year, subject to escalation, are as follows:

|                                  |                      |
|----------------------------------|----------------------|
| 2018                             | \$ 5,116,000         |
| 2019                             | 6,276,000            |
| 2020                             | 5,996,000            |
| 2021                             | 5,853,000            |
| 2022                             | 5,646,000            |
| Thereafter                       | <u>14,063,000</u>    |
| Total minimum payments required* | <u>\$ 42,950,000</u> |

\*The minimum payments required includes the future minimum commitments for the former office space as described above.

The Foundation has entered into lease agreements with tenants to occupy its former headquarters space. As of December 31, 2017 the approximate future minimum sublease rental payments to be received for each calendar year, subject to escalation, are as follows:

|                                 |                     |
|---------------------------------|---------------------|
| 2018                            | \$ 208,000          |
| 2019                            | 835,000             |
| 2020                            | 1,015,000           |
| 2021                            | 1,051,000           |
| 2022                            | 1,088,000           |
| Thereafter                      | <u>369,000</u>      |
| Total minimum sublease payments | <u>\$ 4,566,000</u> |

Rental costs for the years ended December 31, 2017 and 2016 were approximately \$6,072,000 and \$5,506,000, respectively.

**9. Retirement plan**

Under the provisions of the Foundation's 401(k) retirement plan, employees who defer wages are eligible for an employer match, which vests immediately. In addition, eligible employees receive a non-matching employer contribution that vests after employees complete three years of service, as defined in the plan. The Foundation and CFFT made contributions in accordance with the provisions of the plan amounting to approximately \$4,381,000 and \$3,074,000, respectively, for the years ended December 31, 2017 and 2016.

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**10. Allocation of joint costs**

The Foundation conducted direct mail activities in the years ended December 31, 2017 and 2016 that included requests for contributions as well as program components. The costs of conducting those activities included a total of approximately \$2,288,000 and \$1,984,000 of joint costs during the years ended December 31, 2017 and 2016, respectively. These costs were not specifically attributable to particular components of the activities. Of those costs, \$1,706,000 and \$1,611,000 was allocated to fundraising expense and \$582,000 and \$373,000 was allocated to public and professional information and education program services for the years ended December 31, 2017 and 2016, respectively.

**11. Subsequent events**

The Foundation has performed an evaluation of subsequent events through May 2, 2018, which is the date the financial statements were available to be issued, noting no events which affect the financial statements or require additional disclosure.