



STEADMAN PHILIPPON RESEARCH INSTITUTE

**Consolidated Financial Statements
and
Independent Auditors' Report
December 31, 2015 and 2014**

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AUDIT | TAX | CONSULTING

STEADMAN PHILIPPON RESEARCH INSTITUTE

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INDEPENDENT AUDITORS' REPORT

To the Board of Directors
Steadman Philippon Research Institute and Subsidiary
Vail, Colorado

We have audited the accompanying consolidated financial statements of Steadman Philippon Research Institute and Subsidiary, which are comprised of the consolidated statements of financial position as of December 31, 2015 and 2014, 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 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.

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 auditors consider 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.

To the Board of Directors
Steadman Philippon Research Institute and Subsidiary
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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 Steadman Philippon Research Institute and Subsidiary as of December 31, 2015 and 2014, and the changes in their net assets and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

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August 11, 2016
Denver, Colorado

STEADMAN PHILIPPON RESEARCH INSTITUTE

Consolidated Statements of Financial Position

	December 31,	
	2015	2014
Assets		
Current assets		
Cash and cash equivalents	\$ 97,838	\$ 508,981
Accounts receivable	33,360	19,413
Accounts receivable, related party	50,434	-
Contributions receivable, current portion	1,095,000	125,000
Prepaid expenses and other assets	127,093	185,961
Investments	2,149,642	5,038,396
Inventory	-	37,548
Total current assets	3,553,367	5,915,299
Contributions receivable, less current portion	8,162,022	70,377
Property and equipment, net	365,343	1,399,555
Investments, other	227,050	227,050
Deferred tax asset	2,651	36,880
Total assets	\$ 12,310,433	\$ 7,649,161
Liabilities and Net Assets		
Current liabilities		
Accounts payable	\$ 130,238	\$ 171,139
Accounts payable, related parties	-	149,888
Accrued expenses	121,847	159,208
Line-of-credit	1,425,800	628,800
Total liabilities	1,677,885	1,109,035
Commitments		
Net assets		
Unrestricted	1,135,289	5,804,306
Temporarily restricted	9,497,259	735,820
Total net assets	10,632,548	6,540,126
Total liabilities and net assets	\$ 12,310,433	\$ 7,649,161

See notes to consolidated financial statements.

STEADMAN PHILIPPON RESEARCH INSTITUTE

Consolidated Statements of Activities

	For the Years Ended					
	December 31, 2015			December 31, 2014		
	Unrestricted	Temporarily Restricted	Total	Unrestricted	Temporarily Restricted	Total
Revenues, gains, and other support						
Contributions	\$ 1,271,764	\$ 334,422	\$ 1,606,186	\$ 905,504	\$ 496,349	\$ 1,401,853
Fundraising events	-	-	-	966,663	-	966,663
Grants and corporate partners	1,269,599	9,728,728	10,998,327	1,114,998	810,822	1,925,820
MRI income	723,000	-	723,000	723,000	-	723,000
Other income	1,740	-	1,740	4,123	-	4,123
In-kind contributions	297,955	-	297,955	30,799	-	30,799
	<u>3,564,058</u>	<u>10,063,150</u>	<u>13,627,208</u>	<u>3,745,087</u>	<u>1,307,171</u>	<u>5,052,258</u>
Net assets released from restrictions	1,301,711	(1,301,711)	-	1,012,009	(1,012,009)	-
Total revenues, gains, and other support	<u>4,865,769</u>	<u>8,761,439</u>	<u>13,627,208</u>	<u>4,757,096</u>	<u>295,162</u>	<u>5,052,258</u>
Operating expenses						
BioMedical engineering	1,565,132	-	1,565,132	1,309,259	-	1,309,259
Center for regenerative sports medicine	1,610,875	-	1,610,875	288,060	-	288,060
Surgical skills laboratory	922,302	-	922,302	953,547	-	953,547
Center for outcomes-based orthopaedic research	774,737	-	774,737	756,565	-	756,565
Education department	558,624	-	558,624	522,845	-	522,845
Department of technology and multimedia communications	257,054	-	257,054	313,785	-	313,785
Imaging research	551,116	-	551,116	562,028	-	562,028
General and administrative	1,278,769	-	1,278,769	451,224	-	451,224
Development	1,697,430	-	1,697,430	924,165	-	924,165
Total operating expenses	<u>9,216,039</u>	<u>-</u>	<u>9,216,039</u>	<u>6,081,478</u>	<u>-</u>	<u>6,081,478</u>
Other expenses						
Investment loss	(237,368)	-	(237,368)	(147,547)	-	(147,547)
Interest expense	(40,235)	-	(40,235)	(16,966)	-	(16,966)
Total other expenses	<u>(277,603)</u>	<u>-</u>	<u>(277,603)</u>	<u>(164,513)</u>	<u>-</u>	<u>(164,513)</u>
Rescinded pledge	-	-	-	(90,000)	-	(90,000)
Provision for income tax (expense) benefit	(41,144)	-	(41,144)	9,490	-	9,490
Change in net assets	(4,669,017)	8,761,439	4,092,422	(1,569,405)	295,162	(1,274,243)
Net assets at beginning of year	<u>5,804,306</u>	<u>735,820</u>	<u>6,540,126</u>	<u>7,373,711</u>	<u>440,658</u>	<u>7,814,369</u>
Net assets at end of year	<u>\$ 1,135,289</u>	<u>\$ 9,497,259</u>	<u>\$ 10,632,548</u>	<u>\$ 5,804,306</u>	<u>\$ 735,820</u>	<u>\$ 6,540,126</u>

See notes to consolidated financial statements.

STEADMAN PHILIPPON RESEARCH INSTITUTE

**Consolidated Statement of Functional Expenses
For the Year Ended December 31, 2015**

	Program Services							Support Services		Total	
	BioMedical Engineering	Center for Regenerative Sports Medicine	Surgical Skills Laboratory	Center for Outcomes-Based Orthopaedic Research	Education Department	Department of Technology and Multimedia Communications	Imaging Research	Total Program Services	General and Administrative		Development
Salaries and benefits	\$ 424,553	\$ 477,003	\$ 73,955	\$ 650,008	\$ 378,145	\$ 196,250	\$ 190,732	\$ 2,390,646	\$ 1,115,888	\$ 279,125	\$ 3,785,659
Consulting and contract labor	11,193	417,560	150	1,400	2,540	1,075	77,212	511,130	1,520	441,875	954,525
Supplies (office, computer, lab)	670,346	132,878	223,438	18,644	734	4,437	3,963	1,054,440	6,852	5,345	1,066,637
Events and fundraising	-	-	-	-	-	-	-	-	-	111,760	111,760
Printing	9,843	592	265	3,471	896	544	545	16,156	1,225	93,437	110,818
Maintenance and supplies	13,095	8,326	17,613	4,816	10,448	4,598	4,272	63,168	7,356	12,097	82,621
Rent and leases	54,570	147,291	28,322	40,587	5,306	5,193	7,638	288,907	(917)	19,557	307,547
Telephone and utilities	69,485	12,485	34,660	8,649	6,113	7,154	8,672	147,218	13,377	3,955	164,550
Travel	11,264	158,803	68	13,068	30,236	705	11,914	226,058	22,771	733	249,562
Legal and accounting	17,317	106,927	1,211	13,697	24,747	2,984	6,236	173,119	30,573	14,307	217,999
Fellows	-	-	-	-	22,908	-	925	23,833	-	-	23,833
Education meetings/lectures	-	-	-	-	41,731	-	-	41,731	-	-	41,731
Direct mail/planned giving	-	-	-	-	-	-	-	-	-	120,965	120,965
Meals and entertainment	6,576	13,364	1,072	3,647	16,651	1,019	3,197	45,526	17,760	7,357	70,643
Gifts	1,077	314	180	1,946	1,257	359	359	5,492	1,236	10,133	16,861
Postage	856	1,473	507	1,770	1,163	201	(577)	5,393	237	3,436	9,066
Insurance	1,131	140	166	1,530	658	451	373	4,449	27,202	308	31,959
Fees, dues, and subscriptions	2,395	3,950	-	2,053	14,607	735	925	24,665	2,372	357	27,394
Bank/credit card fees	-	-	-	-	-	-	500	500	175	6,670	7,345
Meetings (Board and SAC)	-	54,801	-	-	-	-	-	54,801	29,326	-	84,127
Scientific summit	-	68,071	-	-	-	-	-	68,071	-	-	68,071
Research grant	-	30	-	-	-	-	-	30	-	-	30
Advertising	2,000	-	-	273	90	-	-	2,363	-	564,718	567,081
	<u>1,295,701</u>	<u>1,604,008</u>	<u>381,607</u>	<u>765,559</u>	<u>558,230</u>	<u>225,705</u>	<u>316,886</u>	<u>5,147,696</u>	<u>1,276,953</u>	<u>1,696,135</u>	<u>8,120,784</u>
Depreciation and amortization	<u>269,431</u>	<u>6,867</u>	<u>540,695</u>	<u>9,178</u>	<u>394</u>	<u>31,349</u>	<u>234,230</u>	<u>1,092,144</u>	<u>1,816</u>	<u>1,295</u>	<u>1,095,255</u>
Total	\$ <u>1,565,132</u>	\$ <u>1,610,875</u>	\$ <u>922,302</u>	\$ <u>774,737</u>	\$ <u>558,624</u>	\$ <u>257,054</u>	\$ <u>551,116</u>	\$ <u>6,239,840</u>	\$ <u>1,278,769</u>	\$ <u>1,697,430</u>	\$ <u>9,216,039</u>

See notes to consolidated financial statements.

STEADMAN PHILIPPON RESEARCH INSTITUTE

**Consolidated Statement of Functional Expenses
For the Year Ended December 31, 2014**

	Program Services							Support Services			
	BioMedical Engineering	Center for Regenerative Sports Medicine	Surgical Skills Laboratory	Center for Outcomes-Based Orthopaedic Research	Education Department	Department of Technology and Multimedia Communications	Imaging Research	Total Program Services	General and Administrative	Development	Total
Salaries and benefits	\$ 538,822	\$ 155,280	\$ 92,909	\$ 624,885	\$ 369,212	\$ 189,611	\$ 170,371	\$ 2,141,090	\$ 374,804	\$ 219,303	\$ 2,735,197
Consulting and contract labor	25,624	6,360	1,110	9,470	1,680	44,608	98,685	187,537	12,547	5,940	206,024
Supplies (office, computer, lab)	262,147	653	238,438	20,254	1,761	4,352	2,688	530,293	2,438	985	533,716
Events and fundraising	-	-	-	-	-	-	-	-	-	377,217	377,217
Printing	12,747	136	233	5,795	737	370	204	20,222	562	57,404	78,188
Maintenance and supplies	28,657	7,010	14,559	8,307	3,809	2,316	1,084	65,742	4,978	3,171	73,891
Rent and leases	53,040	5,121	26,973	33,403	5,723	25,024	7,381	156,665	4,226	2,921	163,812
Telephone and utilities	73,166	8,421	37,159	9,315	6,371	8,694	8,940	152,066	14,804	2,570	169,440
Travel	21,443	42,811	-	13,724	15,263	1,830	9,648	104,719	575	526	105,820
Legal and accounting	11,864	1,043	1,043	15,828	17,116	3,628	4,939	55,461	8,176	2,783	66,420
Fellows	-	-	-	-	36,963	-	2,136	39,099	-	-	39,099
Education meetings/lectures	-	2,500	-	-	33,304	-	-	35,804	-	-	35,804
Direct mail/planned giving	-	-	-	-	-	-	-	-	-	132,069	132,069
Meals and entertainment	6,578	2,277	-	657	4,792	182	1,253	15,739	1,703	150	17,592
Gifts	-	838	-	72	-	-	150	1,060	85	343	1,488
Postage	1,901	232	249	2,547	1,218	531	258	6,936	759	6,521	14,216
Insurance	1,166	159	159	1,642	742	424	159	4,451	20,065	371	24,887
Fees, dues, and subscriptions	2,619	2,543	-	723	20,616	429	4,825	31,755	1,022	375	33,152
Bank/credit card fees	56	-	-	-	-	-	173	229	1,795	9,441	11,465
Meetings (Board and SAC)	-	51,635	-	-	-	-	-	51,635	673	-	52,308
Advertising	1,590	-	-	-	90	1,118	2,940	5,738	-	100,662	106,400
	<u>1,041,420</u>	<u>287,019</u>	<u>412,832</u>	<u>746,622</u>	<u>519,397</u>	<u>283,117</u>	<u>315,834</u>	<u>3,606,241</u>	<u>449,212</u>	<u>922,752</u>	<u>4,978,205</u>
Depreciation and amortization	<u>267,839</u>	<u>1,041</u>	<u>540,715</u>	<u>9,943</u>	<u>3,448</u>	<u>30,668</u>	<u>246,194</u>	<u>1,099,848</u>	<u>2,012</u>	<u>1,413</u>	<u>1,103,273</u>
Total	\$ <u>1,309,259</u>	\$ <u>288,060</u>	\$ <u>953,547</u>	\$ <u>756,565</u>	\$ <u>522,845</u>	\$ <u>313,785</u>	\$ <u>562,028</u>	\$ <u>4,706,089</u>	\$ <u>451,224</u>	\$ <u>924,165</u>	\$ <u>6,081,478</u>

See notes to consolidated financial statements.

STEADMAN PHILIPPON RESEARCH INSTITUTE

Consolidated Statements of Cash Flows

	For the Years Ended December 31,	
	2015	2014
Cash flows from operating activities		
Change in net assets	\$ 4,092,422	\$ (1,274,243)
Adjustments to reconcile change in net assets to net cash used in operating activities		
Depreciation and amortization expense	1,095,255	1,103,273
Net loss on investments	229,587	128,586
Rescinded pledge	-	90,000
Donated stock	(330,698)	(43,644)
Deferred taxes	34,229	(21,995)
Changes in assets and liabilities		
Accounts receivable	(64,381)	4,959
Contributions receivable	(9,061,645)	(56,156)
Prepaid expenses and other assets	58,868	(158,772)
Inventory	37,548	107,256
Accounts payable	(190,789)	163,341
Accrued expenses	(37,361)	(83,160)
	(8,229,387)	1,233,688
Net cash used in operating activities	(4,136,965)	(40,555)
Cash flows from investing activities		
Proceeds from sale of investments	2,989,865	52,235
Purchases of property and equipment	(61,043)	(27,948)
Net cash provided by investing activities	2,928,822	24,287
Cash flows from financing activities		
Payments on capital leases	-	(100,790)
Net borrowings on line-of-credit	797,000	365,300
Net cash provided by financing activities	797,000	264,510
Net (decrease) increase in cash and cash equivalents	(411,143)	248,242
Cash and cash equivalents at beginning of year	508,981	260,739
Cash and cash equivalents at end of year	\$ 97,838	\$ 508,981

Supplemental disclosure of cash flow information:

Cash paid for interest was \$40,235 and \$16,966 for the years ended December 31, 2015 and 2014, respectively.

See notes to consolidated financial statements.

STEADMAN PHILIPPON RESEARCH INSTITUTE

Notes to Consolidated Financial Statements

Note 1 - Organization and Summary of Significant Accounting Policies

Organization

The Steadman Philippon Research Institute ("SPRI"), a non-profit organization, was founded in 1988 and incorporated in the state of Colorado on February 22, 1999. SPRI is located in Vail, Colorado, and is dedicated to keeping people of all ages physically active through orthopaedic research and education in the areas of arthritis, healing, rehabilitation, and injury prevention. SPRI's primary sources of support are public donations, grants, special events, and corporate partners.

SPRI has agreements with several corporations that sponsor SPRI's research. This research is for the general use of and publication by SPRI. These agreements are recorded as income in the year the research is performed and payment is received.

SPRI created the SPRI Leasing Corporation ("Subsidiary"), a wholly owned subsidiary, in order to hold the assets, liabilities, revenues, and expenses derived from SPRI's MRI scanner.

Principles of Consolidation

The reporting entity referred to as Steadman Philippon Research Institute and Subsidiary (collectively, the "Institute") includes the accounts of SPRI and SPRI Leasing Corporation. All intercompany accounts and transactions have been eliminated in consolidation.

Basis of Presentation

The Institute reports information regarding its financial position and activities according to three classes of net assets: unrestricted net assets, temporarily restricted net assets, and permanently restricted net assets.

Unrestricted amounts are those currently available at the discretion of the Board of Directors ("Board") for use in the Institute's operations, fundraising, and certain programs.

Temporarily restricted amounts are monies restricted by donors specifically for certain purposes or programs; these monies are available for use by the Institute for the restricted purpose.

Permanently restricted amounts are assets that must be maintained permanently by the Institute as required by the donor, but the Institute is permitted to use or expend part or all of any income derived from those assets. As of December 31, 2015 and 2014, the Institute did not have any permanently restricted amounts.

Cash and Cash Equivalents

The Institute considers all highly liquid investments with a maturity of three months or less when purchased to be cash equivalents, unless held for reinvestment as part of the investment portfolio or otherwise encumbered.

STEADMAN PHILIPPON RESEARCH INSTITUTE

Notes to Consolidated Financial Statements

Note 1 - Organization and Summary of Significant Accounting Policies (continued)

Accounts and Contributions Receivable

Accounts and contributions receivable represent amounts due from individuals and organizations in support of the Institute's programs. Management considers all amounts collectible; therefore, no allowance has been recorded as of December 31, 2015 and 2014.

Unconditional gifts expected to be collected within one year are reported at their net realizable value. Unconditional gifts expected to be collected in future years are reported at the present value of estimated future cash flows. The resulting discount is amortized using the effective interest method and is reported as contribution revenue.

Investments

The Institute reports investments in equity securities with readily determinable fair values and all investments in debt securities at their fair values with unrealized gains and losses included in the consolidated statements of activities.

The Institute holds alternative investments, which are not readily marketable and are carried at fair value as provided by the investment managers. The Institute reviews and evaluates the value provided by the investment managers and agrees with the valuation methods and assumptions used in determining the fair value of the alternative investments. Those estimated fair values may differ significantly from the values that would have been used had a ready market for these securities existed.

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. Investment return is reflected in the consolidated statements of activities as unrestricted, temporarily restricted, or permanently restricted based upon the existence and nature of any donor or legally imposed restrictions.

Inventory

Inventory is stated at the lower of cost (first-in, first-out method) or market. Inventory consists of donated medical supplies of medical implants used for medical research.

Property and Equipment

Leasehold improvements and equipment purchased by the Institute are recorded at cost. Donated fixed assets are capitalized at fair value at the date of donation. Depreciation is provided on the straight-line method based upon the estimated useful lives of the assets, which range from three to seven years. Leasehold improvements are amortized over the shorter of the lease term plus renewal options or the estimated useful lives of the improvements.

STEADMAN PHILIPPON RESEARCH INSTITUTE

Notes to Consolidated Financial Statements

Note 1 - Organization and Summary of Significant Accounting Policies (continued)

Other Investment

The Institute holds contributed real estate, which was recorded at estimated fair value at the date of donation. The investment is assessed for impairment if events and circumstances warrant such a review. No such impairment was recognized during 2015 or 2014.

Contributions

Gifts of cash and other assets received without donor stipulations are reported as unrestricted support. Gifts received with a donor stipulation that limits their use are reported as temporarily or permanently restricted support. When a donor-stipulated time restriction ends or a purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the consolidated statements of activities as net assets released from restrictions.

Gifts of land, buildings, equipment, and other long-lived assets are reported as unrestricted support unless explicit donor stipulations specify how such assets must be used, in which case the gifts are reported as temporarily or permanently restricted support. Absent explicit donor stipulations for the time that long-lived assets must be held, expirations of restrictions resulting in reclassification of temporarily restricted net assets as unrestricted net assets are reported when the long-lived assets are placed in service.

Revenue Recognition

MRI and other income are recognized at the time the services are provided.

Functional Expenses

Expenses incurred directly for a program service are charged to such program. Allocations of certain overhead costs are also allocated to programs on a pro rata basis of total space occupied by each service or by headcount.

Rescinded Pledge

During the year ended December 31, 2014, a donor notified the Institute that they were rescinding the remaining \$90,000 of a pledge made in 2010. The Institute did not have any rescinded pledges during the year ended December 31, 2015.

Income Taxes

SPRI is exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code ("IRC"). SPRI is not a private foundation within the meaning of Section 509(a) of the IRC.

The Subsidiary is a for-profit corporation that is required to file a corporate income tax return for its operations and recognizes deferred tax assets and liabilities based upon differences between its basis of assets for tax and financial reporting purposes.

STEADMAN PHILIPPON RESEARCH INSTITUTE

Notes to Consolidated Financial Statements

Note 1 - Organization and Summary of Significant Accounting Policies (continued)

Income Taxes (continued)

The Institute applies a more-likely-than-not measurement methodology to reflect the financial statement impact of uncertain tax positions taken or expected to be taken in a tax return. After evaluating the tax positions taken, none are considered to be uncertain; therefore, no amounts have been recognized as of December 31, 2015 and 2014. If incurred, interest and penalties associated with tax positions are recorded in the period assessed as general and administrative expense. No interest or penalties have been assessed for the years ended December 31, 2015 or 2014.

Use of Estimates

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

Subsequent Events

The Institute has evaluated all subsequent events through the auditors' report date, which is the date the consolidated financial statements were available for issuance.

Note 2 - Fair Value Measurements and Investments

The Institute values its financial assets and liabilities based on 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. In order to increase consistency and comparability in fair value measurements, the following fair value hierarchy prioritizes observable inputs used to measure fair value into three broad levels, which are described below:

- Level 1: Quoted prices in active markets for identical assets or liabilities that are accessible at the measurement date. The fair value hierarchy gives the highest priority to Level 1 inputs.
- Level 2: Other than quoted prices that are observable for the asset or liability, either directly or indirectly.
- Level 3: Unobservable inputs where little or no market data is available, which requires the reporting entity to develop its own assumptions.

In determining fair value, the Institute utilizes valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs to the extent possible, as well as considers counterparty credit risk in its assessment of fair value. These classifications (Levels 1, 2, and 3) are intended to reflect the observability of inputs used in the valuation of investments and are not necessarily an indication of risk or liquidity.

STEADMAN PHILIPPON RESEARCH INSTITUTE

Notes to Consolidated Financial Statements

Note 2 - Fair Value Measurements and Investments (continued)

Following is a description of the valuation methodologies used for assets measured at fair value:

Common stock and mutual funds: Valued at the closing price reported on the active market on which the individual securities are traded.

Limited partnerships: Valued based on the net asset value per share of the fund.

There have been no changes to valuation methodologies during the years ended December 31, 2015 and 2014.

Financial assets carried at fair value as of December 31, 2015 are classified in the table below in one of the three categories described above.

<u>Description</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Equity mutual funds	\$ 234,982	\$ -	\$ -	\$ 234,982
Limited partnerships	-	<u>1,826,950</u>	-	<u>1,826,950</u>
Total	<u>\$ 234,982</u>	<u>\$ 1,826,950</u>	<u>\$ -</u>	<u>\$ 2,061,932</u>

Financial assets carried at fair value as of December 31, 2014 are classified in the table below in one of the three categories described above.

<u>Description</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Common stock	\$ 24,697	\$ -	\$ -	\$ 24,697
Equity mutual funds	758,011	-	-	758,011
Limited partnerships	-	<u>3,562,712</u>	-	<u>3,562,712</u>
Total	<u>\$ 782,708</u>	<u>\$ 3,562,712</u>	<u>\$ -</u>	<u>\$ 4,345,420</u>

Included in investments on the consolidated statements of financial position are money market funds in the amount of \$87,710 and \$692,976 at December 31, 2015 and 2014, respectively, which are not subject to fair value classification.

Investments in certain entities that calculate net asset value per share are as follows:

<u>Fund Description</u>	<u>December 31, 2015 Fair Value</u>	<u>December 31, 2014 Fair Value</u>	<u>Unfunded Commitments</u>	<u>Redemption Frequency</u>	<u>Redemption Notice Period</u>
Absolute Return Funds	\$ 1,826,950	\$ 3,562,712	None	Quarterly to Annually	45 to 90 Days

STEADMAN PHILIPPON RESEARCH INSTITUTE

Notes to Consolidated Financial Statements

Note 2 - Fair Value Measurements and Investments (continued)

The Absolute Return Funds employ a strategy to achieve consistent positive, absolute returns with low volatility primarily by seeking to exploit pricing inefficiencies in equity and debt securities and by using a traditional hedge fund approach. The fair value of the investments has been calculated using the net asset value per share of the investments.

Investment return consists of the following:

	For the Years Ended December 31,	
	2015	2014
Net realized and unrealized losses	\$ (229,587)	\$ (128,586)
Fees	(7,781)	(18,981)
Dividends and interest - reinvested	-	20
Total return on investments	<u>\$ (237,368)</u>	<u>\$ (147,547)</u>

Note 3 - Contributions

Contributions receivable consist of the following:

	December 31,	
	2015	2014
Due in less than one year	\$ 1,095,000	\$ 125,000
Due in one to five years	5,110,000	75,000
Due in over five years	<u>4,000,000</u>	<u>-</u>
	10,205,000	200,000
Less unamortized discount	<u>(947,978)</u>	<u>(4,623)</u>
	<u>\$ 9,257,022</u>	<u>\$ 195,377</u>

The discount rate used was 2.27% and 3.25% for 2015 and 2014, respectively.

In December 2015, the Institute entered into an agreement that guaranteed a minimum contribution of \$1,000,000 per year from 2016 through 2025. The contribution has been recorded as a contribution receivable and is included as a temporarily restricted net asset. In addition, there are certain conditional requirements in the agreement that allow the Institute to receive up to \$4,300,000 per year.

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Notes to Consolidated Financial Statements

Note 4 - Property and Equipment

The Institute's property and equipment consist of the following:

	December 31,	
	2015	2014
Equipment	\$ 423,492	\$ 538,388
Furniture and fixtures	142,019	142,019
Leasehold improvements	2,153,948	2,107,558
Machines and video equipment	897,143	1,151,086
Medical equipment	<u>4,301,646</u>	<u>4,301,646</u>
	7,918,248	8,240,697
Less accumulated depreciation and amortization	<u>(7,552,905)</u>	<u>(6,841,142)</u>
	<u>\$ 365,343</u>	<u>\$ 1,399,555</u>

Note 5 - Line-of-Credit

The Institute has an unsecured line-of-credit with a bank available up to \$1,500,000, which bears interest at the prime rate plus 0.50% with a floor of 3.75% (4.00% at December 31, 2015) and matures in March 2018. As of December 31, 2015 and 2014, the outstanding balance was \$1,425,800 and \$628,800, respectively.

Note 6 - Retirement Plan

The Institute has a defined contribution retirement plan (the "Plan") under IRC Section 401(k). Employees are eligible to participate in the Plan after one year of service. The Institute's contributions to the Plan are determined annually. The Institute contributed \$36,352 and \$32,957 to the Plan in fiscal years 2015 and 2014, respectively.

STEADMAN PHILIPPON RESEARCH INSTITUTE

Notes to Consolidated Financial Statements

Note 7 - Temporarily Restricted Net Assets

The temporarily restricted net assets that have been restricted by the donors to be used only for specified purposes and/or are time restricted until payments on contributions receivable are received are as follows:

	<u>December 31,</u>	
	<u>2015</u>	<u>2014</u>
Assets available for		
BioMedical engineering	\$ 240,237	\$ 480,228
Administration	-	60,215
	<u>240,237</u>	<u>540,443</u>
Assets available in future periods		
Education	50,000	50,000
Center for outcomes-based orthopaedic research	72,664	120,377
BioMedical engineering	76,301	-
Time restricted only	<u>9,058,057</u>	<u>25,000</u>
Total contributions receivable	<u>9,257,022</u>	<u>195,377</u>
	<u>\$ 9,497,259</u>	<u>\$ 735,820</u>

Note 8 - Related Party Transactions

During 2015 and 2014, the Institute received approximately \$688,000 and \$1,135,000, respectively, in contributions from related parties, including various Board members, employees, and medical staff at The Steadman Clinic (the "Clinic").

A contribution receivable in the amount of \$10 million and the Institute's lease commitment are with an organization whose CEO is a Board member of the Institute. In addition, the Institute received contributions from this organization during the years ended December 31, 2015 and 2014 for approximately \$365,000 and \$345,000, respectively.

In addition, the Institute received \$723,000 from the Clinic during both 2015 and 2014, as a corporate sponsor and for the use of certain equipment. The balance due from (to) the Clinic totaled \$50,434 and \$(149,888) as of December 31, 2015 and 2014, respectively.

See Note 10 for additional related party transactions.

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Notes to Consolidated Financial Statements

Note 9 - Income Taxes

Income tax (expense) benefit has been computed at the statutory rates applicable during the period. The components of taxes on income are approximately as follows:

	For the Years Ended December 31,	
	2015	2014
Current		
Federal	\$ (5,224)	\$ (12,000)
State	(1,691)	(1,000)
	(6,915)	(13,000)
Deferred		
Federal	(34,930)	20,000
State	701	2,000
	(34,229)	22,000
	\$ (41,144)	\$ 9,000

The Institute's deferred tax assets are a result of the difference in the tax and book basis of depreciable assets and net operating losses.

Note 10 - Commitments

Operating Leases

The Institute leases facilities under a non-cancelable operating lease with a related party expiring in February 2016, which calls for both base rent payments and operating expenses. During the year, a new lease was signed that begins in 2017 and ends in 2026. The Institute also leases other facilities under non-cancelable operating leases with non-related parties, expiring between April and October 2016. Rent under these leases for the years ended December 31, 2015 and 2014 was \$456,784 and \$321,064, respectively. Of these amounts, \$245,940 and \$182,508 for the years ended December 31, 2015 and 2014, respectively, were with a related party.

Future minimum lease payments under these leases are approximately as follows:

<u>Year Ending December 31,</u>	
2016	\$ 85,000
2017	272,000
2018	272,000
2019	272,000
2020	272,000
Thereafter	1,587,000
	\$ 2,760,000

STEADMAN PHILIPPON RESEARCH INSTITUTE

Notes to Consolidated Financial Statements

Note 10 - Commitments (continued)

Research Collaboration

In 2015, the Institute signed an agreement in which \$7,500,000 was committed to a research collaboration over a period of five years to pay for laboratory space, staff support, researchers' salaries, equipment, and other related expenses incurred by the research collaboration.