

CONSOLIDATED FINANCIAL STATEMENTS  
AND REPORTS ON FEDERAL AWARD PROGRAMS

Texas Biomedical Research Institute  
Years Ended December 31, 2018 and 2017  
With Reports of Independent Auditors

Ernst & Young LLP



Texas Biomedical Research Institute  
Consolidated Financial Statements  
and Reports on Federal Award Programs  
Years Ended December 31, 2018 and 2017

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## Report of Independent Auditors

Management and Trustees  
Texas Biomedical Research Institute

### **Report on the Financial Statements**

We have audited the accompanying consolidated financial statements of Texas Biomedical Research Institute, which comprise the consolidated statements of financial position as of December 31, 2018 and 2017, and the related consolidated statements of activities, 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 conformity 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 of material misstatement, whether due to fraud or error.

### ***Auditor's Responsibility***

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement.

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

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

***Opinion***

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Texas Biomedical Research Institute as of December 31, 2018 and 2017, and the changes in its net assets and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

***Other Reporting Required by Government Auditing Standards***

In accordance with *Government Auditing Standards*, we also have issued our report dated June 5, 2019, on our consideration of Texas Biomedical Research Institute's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of Texas Biomedical Research Institute's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Texas Biomedical Research Institute's internal control over financial reporting and compliance.

*Ernst + Young LLP*

June 5, 2019

Texas Biomedical Research Institute

Consolidated Statements of Financial Position

	December 31	
	2018	2017
<b>Assets</b>		
Cash and cash equivalents	\$ —	\$ 817,384
Accounts receivable	9,508,603	5,975,169
Prepaid expenses and supplies	102,714	242,607
Assets limited as to use:		
Cash ( <i>Note 2</i> )	2,567,258	2,409,065
Investments ( <i>Note 3</i> )	102,488,599	119,397,804
Investment – Evestra, Inc.	2,821,861	2,821,861
Funds held in trust by others ( <i>Note 4</i> )	2,436,840	2,575,529
Land, buildings and equipment, net ( <i>Note 7</i> )	67,750,413	66,627,380
Total assets	<u>\$ 187,676,288</u>	<u>\$ 200,866,799</u>
<b>Liabilities and net assets</b>		
Liabilities:		
Accounts payable	\$ 5,424,849	\$ 4,113,350
Accrued wages, vacation and other liabilities	2,721,285	2,894,529
Unearned revenue	1,569,838	2,091,184
Notes payable ( <i>Note 9</i> )	29,500,000	15,058,239
Total liabilities	<u>39,215,972</u>	<u>24,157,302</u>
Net assets:		
Net assets without donor restrictions	90,971,555	115,929,384
Net assets with donor restrictions	57,488,761	60,780,113
Total net assets	<u>148,460,316</u>	<u>176,709,497</u>
Total liabilities and net assets	<u>\$ 187,676,288</u>	<u>\$ 200,866,799</u>

*See accompanying notes.*

Texas Biomedical Research Institute

Consolidated Statements of Activities

	2018 Without Donor Restrictions	2018 With Donor Restrictions	2018
<b>Operating revenues</b>			
Grants and contracts	\$ 39,023,421	\$ –	\$ 39,023,421
Contributions	2,419,292	4,182,648	6,601,940
Insurance proceeds	–	–	–
Endowment income allocation for operations	6,484,107	2,620,293	9,104,400
Other revenue	166,614	–	166,614
Total operating revenues	<u>48,093,434</u>	<u>6,802,941</u>	<u>54,896,375</u>
Net assets released from restrictions	4,687,660	(4,687,660)	–
Total revenues, gains and other support	<u>52,781,094</u>	<u>2,115,281</u>	<u>54,896,375</u>
<b>Operating expenses</b>			
Salaries and benefits	32,623,895	–	32,623,895
Supplies	9,812,729	–	9,812,729
Depreciation	7,178,222	–	7,178,222
Services and professional fees	5,835,859	–	5,835,859
Subcontracts	4,617,331	–	4,617,331
Utilities	2,091,914	–	2,091,914
Interest expense	887,436	–	887,436
Subscriptions	549,344	–	549,344
Travel	485,577	–	485,577
Insurance	411,947	–	411,947
Shipping	324,733	–	324,733
Other expenses	1,207,015	–	1,207,015
Total operating expenses	<u>66,026,002</u>	<u>–</u>	<u>66,026,002</u>
Net (decrease) increase from operations	<u>(13,244,908)</u>	<u>2,115,281</u>	<u>(11,129,627)</u>
<b>Nonoperating revenues, gains and losses</b>			
Endowment income allocation for operations	(6,484,107)	(2,620,293)	(9,104,400)
Investment (loss) gain	(6,301,770)	(2,786,340)	(9,088,110)
Royalty income	1,157,198	–	1,157,198
Loss on disposal of assets	(84,242)	–	(84,242)
Total nonoperating revenues, gains and losses	<u>(11,712,921)</u>	<u>(5,406,633)</u>	<u>(17,119,554)</u>
Change in net assets	<u>(24,957,829)</u>	<u>(3,291,352)</u>	<u>(28,249,181)</u>
Beginning net assets	<u>115,929,384</u>	<u>60,780,113</u>	<u>176,709,497</u>
Ending net assets	<u>\$ 90,971,555</u>	<u>\$ 57,488,761</u>	<u>\$ 148,460,316</u>

See accompanying notes.

Texas Biomedical Research Institute

Consolidated Statements of Activities (continued)

<b>2017</b>	<b>2017</b>	<b>2017</b>
<b>Without Donor</b>	<b>With Donor</b>	
<b>Restrictions</b>	<b>Restrictions</b>	<b>2017</b>
\$ 36,909,753	\$ —	\$ 36,909,753
2,640,143	1,840,360	4,480,503
200,000	—	200,000
6,256,529	2,871,871	9,128,400
185,280	—	185,280
46,191,705	4,712,231	50,903,936
4,515,606	(4,515,606)	—
50,707,311	196,625	50,903,936
31,868,366	—	31,868,366
7,295,681	—	7,295,681
7,288,845	—	7,288,845
6,531,132	—	6,531,132
3,746,903	—	3,746,903
2,551,930	—	2,551,930
243,525	—	243,525
526,452	—	526,452
459,100	—	459,100
586,838	—	586,838
288,424	—	288,424
1,562,372	—	1,562,372
62,949,568	—	62,949,568
(12,242,257)	196,625	(12,045,632)
(6,256,529)	(2,871,871)	(9,128,400)
13,082,210	6,108,382	19,190,592
1,030,778	—	1,030,778
(33,694)	—	(33,694)
7,822,765	3,236,511	11,059,276
(4,419,492)	3,433,136	(986,356)
120,348,876	57,346,977	177,695,853
\$ 115,929,384	\$ 60,780,113	\$ 176,709,497

Texas Biomedical Research Institute

Consolidated Statements of Cash Flows

	<b>Year Ended December 31</b>	
	<b>2018</b>	<b>2017</b>
<b>Operating activities</b>		
Decrease in net assets	\$ (28,249,181)	\$ (986,356)
Adjustments to reconcile decrease in net assets to net cash used in operating activities:		
Depreciation	7,178,222	7,288,845
Loss on disposal of assets, net	84,242	33,694
Net investment (gain) loss	8,869,513	(19,415,355)
Contributions revenue with donor restrictions	(4,182,647)	(1,840,360)
Changes in operating assets and liabilities:		
Accounts receivable	(3,533,433)	(395,017)
Prepaid expenses and supplies	139,893	(84,068)
Accounts payable and accrued expenses	1,138,254	(558,888)
Unearned revenue	(521,346)	610,168
Net cash used in operating activities	(19,076,483)	(15,347,337)
<b>Investing activities</b>		
Purchases of plant and equipment	(8,451,197)	(7,744,803)
Sale of plant and equipment	65,700	1,505
Purchases of investments	(22,736,059)	(23,150,000)
Sale of investments	30,775,751	33,913,700
Net cash (used in) provided by investing activities	(345,805)	3,020,402
<b>Financing activities</b>		
Proceeds from notes payable	14,441,761	11,287,380
Payments on notes payable	-	(281,917)
Proceeds from contributions with donor restrictions	4,321,336	1,586,897
Net cash provided by financing activities	18,763,097	12,592,360
Increase (decrease) in cash, cash equivalents and restricted cash	(659,191)	265,425
Cash, cash equivalents and restricted cash at beginning of year	3,226,449	2,961,024
Cash, cash equivalents and restricted cash at end of year	\$ 2,567,258	\$ 3,226,449
<b>Supplemental disclosure of cash flow information</b>		
Interest paid	\$ 887,436	\$ 243,525

*See accompanying notes.*

# Texas Biomedical Research Institute

## Notes to Consolidated Financial Statements

December 31, 2018

### 1. Significant Accounting Policies

#### Nature of Operations

The creation of Texas Biomedical Research Institute (Texas Biomed) was by trust indenture dated December 16, 1941, and restated November 1, 1993, appointing trustees and specifying the scientific, educational, and charitable purposes of Texas Biomed. Texas Biomed conducts scientific research and educational programs to improve the health of the global community. The main revenue sources for these activities include federal and commercial grants and contracts.

#### Principles of Consolidation

For the years ended December 31, 2018 and 2017, the accompanying consolidated financial statements include the accounts of Texas Biomed and the Tom Slick Memorial Trust for Texas Biomed, which is controlled by the Board of Trustees of Texas Biomed.

The Tom Slick Memorial Trust is held in the Texas Biomed endowment fund. Each month, in accordance with Texas Biomed's board-adopted spending policy, the Tom Slick Memorial Trust contributes a percentage of its earnings to Texas Biomed to be used for operations. The contribution was 8% in 2018 and 2017. As of December 31, 2018 and 2017, all intercompany accounts and transactions have been eliminated in consolidation.

#### Basis of Presentation

The accompanying consolidated financial statements of Texas Biomed are presented on the accrual basis, in accordance with U.S. generally accepted accounting principles (U.S. GAAP). Texas Biomed is required to report information regarding its consolidated financial position and activities according to two classes of net assets. As such, the accompanying consolidated financial statements reflect net assets grouped into these two classes, described as follows:

- *Net assets without donor restrictions* – Net assets that are not subject to donor-imposed restrictions and may be designated for specific purposes by action of the Board of Trustees
- *Net assets with donor restrictions* – Net assets whose use by Texas Biomed is subject to donor-imposed restrictions

# Texas Biomedical Research Institute

## Notes to Consolidated Financial Statements (continued)

### 1. Significant Accounting Policies (continued)

#### Recent Accounting Pronouncements

In 2018, Texas Biomed adopted Financial Accounting Standards Board (FASB) Accounting Standards Update (ASU) 2016-18, *Statement of Cash Flows (Topic 230), Restricted Cash*. ASU 2016-18 was issued in November 2016. This ASU requires that a statement of cash flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. Therefore, amounts generally described as restricted cash and restricted cash equivalents are now included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown on the statement of cash flows.

Texas Biomed also adopted FASB ASU 2016-15, *Statement of Cash Flows (Topic 230), Classification of Certain Cash Receipts and Cash Payments* in 2018. ASU 2016-15 was issued in August 2016. This ASU provides guidance on the classification of eight specific cash flow issues on the statement of cash flows.

In 2019, Texas Biomed will adopt FASB ASU No. 2014-09: *Revenue from Contracts with Customers (Topic 606)*. ASU 2014-09 was issued in May 2014 and replaces previous revenue recognition guidance. It establishes a new control-based revenue recognition model, changes the basis for deciding when revenue is recognized over time or at a point in time, provides new and more detailed guidance on specific topics, and expands and improves disclosures about revenue.

In 2020, Texas Biomed will adopt FASB ASU No. 2016-02: *Leases (Topic 842)*. ASU 2016-02 was issued in February 2016. This ASU requires a lessee to recognize right-of-use assets and related lease liabilities on the balance sheet for all arrangements with terms longer than 12 months. The pattern of expense recognition in the income statement depends on a lease's classification. In addition, the new ASU aligns certain of the underlying principles of the new lessor model with those in ASU 2014-09, the new revenue recognition standard.

# Texas Biomedical Research Institute

## Notes to Consolidated Financial Statements (continued)

### **1. Significant Accounting Policies (continued)**

#### **Reclassifications**

In order to distinguish between operating and nonoperating activity, certain line items on the consolidated statements of activities have been reclassified. Investment gains and losses, royalty income, and loss on disposal of assets have been categorized as nonoperating.

#### **Use of Estimates**

The preparation of consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results could differ from those estimates.

#### **Cash and Cash Equivalents**

Cash and cash equivalents include non-interest-bearing and interest-bearing demand deposits, as well as a money market sweep account, all of which have maturities of less than 90 days.

Restricted cash includes cash and cash equivalents that are separately maintained by management based on donor restrictions or other needs.

#### **Assets Limited as to Use and Investments**

Assets limited as to use primarily include assets designated by the donor or set aside by the Board of Trustees for capital expenditures and research, scientific recruitment, and endowment funds.

The investment objectives for Texas Biomed's endowment funds are to preserve the principal value of the endowment funds in both absolute and real terms, and to maximize over the long term the total rate of return (cash income plus market appreciation) earned by the endowment funds, without assuming an unreasonable degree of risk. Accordingly, the Board of Trustees has adopted a spending formula for determining the maximum that can be expended annually, which is 4% of the trailing 12-quarter rolling average value of the endowment funds computed annually. For 2017 and 2018, the Board temporarily increased the spending formula to 8% of the trailing 12-quarter rolling average.

## Texas Biomedical Research Institute

### Notes to Consolidated Financial Statements (continued)

#### **1. Significant Accounting Policies (continued)**

Net appreciation on endowment funds whose income is unrestricted as to use should be reported as net assets without donor restrictions unless such net appreciation has been restricted by the donor or by law. In those cases, where a donor has placed specific restrictions on the use of endowment income, any related net appreciation is also subject to the same restriction and is reported as a part of net assets with donor restrictions until such time as the restriction has been met.

Endowment funds are invested primarily in funds made up of U.S. equities, global equities, U.S. fixed-income securities, global fixed-income securities, alternative investments, emerging markets equities, cash, and cash equivalents. The vehicles for these investments include mutual funds and investments in limited partnerships and trusts. The basis for the investments is the aggregate fair market value. A portion of the endowment funds are invested in 11 limited partnerships and 2 trusts. The limited partnerships and trusts are recorded at fair value, based on the net asset value of the units held by Texas Biomed.

Realized gains and losses on investments are recognized in the period in which they occur. Investment income or loss (including realized and unrealized gains and losses on investments, interest, and dividends) is included in net assets without donor restrictions unless the income or loss is restricted by donor or law. Market appreciation or decreases on donor restricted gifts are classified on the accompanying consolidated financial statements as either net assets with or without donor restrictions, as stipulated by the donor.

#### **Donor-Restricted Gifts**

Unconditional promises to give cash and other assets are reported at fair value at the date the promise is received, and that amount is then treated as the basis of the asset. The gifts are reported as restricted support if they are received with donor stipulations that limit the use of the donated assets.

When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, net assets with donor restrictions are reclassified as net assets without donor restrictions and reported on the statements of changes in net assets as net assets released from program restrictions.

## Texas Biomedical Research Institute

### Notes to Consolidated Financial Statements (continued)

#### 1. Significant Accounting Policies (continued)

##### Net Assets With Donor Restrictions

Net assets with donor restrictions are those whose use by Texas Biomed has been limited by donors to a specific time period or purpose or those net assets that have been restricted by donors to be maintained by Texas Biomed in perpetuity. Income from the donor restricted net assets that can be used for current operations, subject to donor restrictions on use, is reflected as an increase to net assets without donor restrictions. This accounting policy was also used for the Tom Slick Memorial Trust consistent with the terms of the documents establishing that trust, with income from the donor restricted corpus being recorded as income without donor restrictions.

Net assets with donor restrictions are restricted for the following purposes:

	<b>December 31</b>	
	<b>2018</b>	<b>2017</b>
Subject to expenditure for specified purpose:		
Research	\$ 5,261,770	\$ 5,293,521
Facility Renovation/Construction	2,285,721	–
Subject to spending policy and appropriation:		
Endowments (including amounts above original gift amount), which, once appropriated, is expendable to support:		
Research	15,629,411	21,036,044
Scientific and educational purposes	10,929,047	10,929,047
Not subject to appropriation or expenditure:		
Endowments held in perpetuity	23,382,812	23,521,501
Total net assets with donor restrictions	\$ 57,488,761	\$ 60,780,113

##### Land, Buildings and Equipment

Land, buildings and equipment are carried at cost or at estimated fair value on dates contributed. Texas Biomed provides for depreciation and amortization of property, plant and equipment at amounts calculated to amortize the cost of the assets over their estimated useful lives, using the straight-line method. The estimated useful lives are as follows:

Buildings and improvements	30 years
Fixtures and equipment	5 years

## Texas Biomedical Research Institute

### Notes to Consolidated Financial Statements (continued)

#### **1. Significant Accounting Policies (continued)**

Expenditures for maintenance and repairs are charged to costs or expenses; renewals and betterments are capitalized. Land, buildings and equipment acquired by federal funds are made available for use in other similar federally sponsored projects or programs as workload permits. The land, buildings and equipment acquired with federal funds are subject to use and disposition conditions, including possible repayments to the federal government if assets are disposed. The amount of total land, buildings and equipment acquired with federal funds, less accumulated depreciation, is \$9,839,312 and \$11,254,042 as of December 31, 2018 and 2017, respectively.

Gifts of long-lived assets, such as land, buildings or equipment, are reported as unrestricted support unless explicit donor stipulations specify how the donated assets must be used. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as donor restricted support.

#### **Retirement Plan**

Texas Biomed's qualified defined contribution retirement plan is available to all active full-time employees and those who work a minimum of 1,000 hours, immediately upon employment. Contributions to the plan consist of employer contributions ranging from 7% to 9% of such employee's base salary up to the maximum amount allowed under Section 401(a)(17) of the Internal Revenue Code (the Code) based on years of service. Employees are fully vested after the completion of three years of service.

The plan is carried with the Teachers Insurance and Annuity Association and College Retirement Equities Fund and is a defined contribution (money-purchase) plan. Payments for employer contributions to the plan were allocated to the various grants, contracts, and departments of Texas Biomed in the amount of \$1,960,256 and \$1,950,436 in 2018 and 2017, respectively.

## Texas Biomedical Research Institute

### Notes to Consolidated Financial Statements (continued)

#### **1. Significant Accounting Policies (continued)**

##### **Income Taxes**

Texas Biomed is exempt from federal income taxes under Section 501(a) of the Code, as an organization described under Section 501(c)(3) of the Code. This exemption does not apply to unrelated business income, as defined by Section 512(a)(1) of the Code, which is subject to federal income tax. Texas Biomed has no tax liability resulting from such unrelated business income in 2018 or 2017. U.S. GAAP require management to evaluate uncertain tax positions taken by Texas Biomed. The financial statement effects of a tax position are recognized when the position is more likely than not, based on its technical merits, to be sustained upon examination by the Internal Revenue Service (the IRS). Management has analyzed the tax positions taken by Texas Biomed and has concluded that, as of December 31, 2018, there are no uncertain positions taken or expected to be taken. Texas Biomed has recognized no interest or penalties related to uncertain tax positions. Texas Biomed is subject to routine audits by taxing jurisdictions; however, there are currently no audits for any tax periods in progress.

The Tax Cuts and Jobs Act (the Act) was enacted on December 22, 2017. The Act reduces the U.S. federal corporate tax rate from 35% to 21%. For tax-exempt entities, the Act also requires organizations to categorize certain fringe benefit expenses as a source of unrelated business income, pay an excise tax on remuneration above certain thresholds that is paid to certain executives by the organization, and report income or loss from unrelated business activities on an activity-by-activity basis, among other provisions. Certain regulatory guidance provides for a measurement period of up to one year during which the accounting for the tax effects of the Act may be completed. Texas Biomed will continue to evaluate the impact of the Act and may record adjustments as additional information and guidance is released by the IRS on provisions of the Act that impact tax-exempt organizations.

## Texas Biomedical Research Institute

### Notes to Consolidated Financial Statements (continued)

#### 2. Cash, Cash Equivalents and Restricted Cash

The following table provides a reconciliation of cash, cash equivalents, and restricted cash reported within the statement of consolidated financial position that sum to the total of the same such amounts shown in the consolidated statement of cash flows:

	<b>December 31</b>	
	<b>2018</b>	<b>2017</b>
Cash and cash equivalents	\$ —	\$ 817,384
Restricted cash	<b>2,567,258</b>	2,409,065
	<b>\$ 2,567,258</b>	\$ 3,226,449

Amounts included in restricted cash represent contributions required to be set aside for specific use as stipulated by the donors.

#### 3. Investments

Investments in securities with determinable fair value are stated at fair value. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (see Note 4). The composition of these securities is set forth as follows:

	<b>December 31</b>	
	<b>2018</b>	<b>2017</b>
Mutual funds	<b>\$ 50,810,374</b>	\$ 56,962,073
Limited partnerships and trusts	<b>51,678,225</b>	62,435,731
	<b>\$ 102,488,599</b>	\$ 119,397,804

Investments traded on a national securities exchange are valued at the last reported sales price on the last business day of the year. If no sale was reported on that date, they are valued at the last reported bid price.

Limited partnerships and trusts are valued at the net asset values of units held at year end. Purchases and sales of securities are recorded as of the trade date at cost. Realized gains and losses on sales of securities are determined on the basis of average costs. Interest income is recognized on the accrual basis. Dividend income is recognized on the ex-dividend date.

Texas Biomedical Research Institute

Notes to Consolidated Financial Statements (continued)

**3. Investments (continued)**

The holdings in the limited partnerships and trusts are primarily composed of publicly traded securities with readily determinable market values. The risks associated with these investments are numerous and include non-regulation risk, managerial risk, minimal liquidity, and limited transparency. Investment income earned by Texas Biomed and its allocation among net asset classifications are as follows:

	<b>December 31</b>	
	<b>2018</b>	<b>2017</b>
Dividends and interest earned on investments	<b>\$ 1,541,290</b>	\$ 1,674,216
Net realized gain on investments reported at fair value	<b>1,018,023</b>	1,254,228
Net unrealized (loss) gain on investments reported at fair value	<b>(11,126,702)</b>	16,758,132
Investment expenses netted against income	<b>(520,721)</b>	(495,984)
Total investment income	<b><u>\$ (9,088,110)</u></b>	<u>\$ 19,190,592</u>
	<b>December 31</b>	
	<b>2018</b>	<b>2017</b>
Net asset classification of investment income:		
Without donor restrictions	<b>\$ (6,301,771)</b>	\$ 13,082,210
With donor restrictions	<b>(2,786,339)</b>	6,108,382
Total investment income	<b><u>\$ (9,088,110)</u></b>	<u>\$ 19,190,592</u>

Investments in oil and gas mineral interests are considered other investments and the investments are measured at the lower of cost or fair value. As of December 31, 2018 and 2017, Texas Biomed's investments in oil and gas mineral interests are \$0. For the years ended December 31, 2018 and 2017, royalty income from oil and gas mineral interests are \$1,157,198 and \$1,030,778, respectively.

## Texas Biomedical Research Institute

### Notes to Consolidated Financial Statements (continued)

#### 3. Investments (continued)

In 2008, Texas Biomed helped create a new for-profit pharmaceutical development corporation named Evestra, Inc. (Evestra). Texas Biomed transferred to Evestra certain equipment, supplies, intellectual property, and a National Institutes of Health contract for steroid manufacturing. Additionally, the former staff of Texas Biomed's Organic Chemistry Department became employees of Evestra. As of December 31, 2018 and 2017, Texas Biomed owns 36% and 37%, respectively, of Evestra's common stock and has two of four voting representatives on Evestra's board; therefore, it is accounted for as an equity investment. As of December 31, 2018 and 2017, Texas Biomed's investment in Evestra is \$2,821,861. No income has been received from Evestra for the years ended December 31, 2018 and 2017.

#### 4. Funds Held in Trust by Others

Texas Biomed's interest in funds held in trust by others is included in net assets for the years ended December 31, 2018 and 2017. These funds are neither in the possession nor under the control of Texas Biomed. Texas Biomed is an income beneficiary of perpetual trusts held by third parties where the trustee has no discretion regarding the income beneficiaries' participation in the trust. Texas Biomed's proportionate share of the fair value of the trust, which approximates the net present value of the estimated future cash flows receivable by Texas Biomed, is reported as an asset and as permanently restricted contribution revenue at the formation of the trust. Annual income distributions from the trusts are recognized as investment income in the appropriate net asset class according to the restrictions of the trust. Changes in Texas Biomed's proportionate share of the fair value of the trust is reported as gains or losses on funds held in trust by others in net assets with donor restrictions.

	<b>December 31</b>	
	<b>2018</b>	<b>2017</b>
Ruth Chapman Cowles and Andrew G. Cowles Memorial Trust:		
Texas Biomed has a 10% interest in the income generated from this perpetual trust. The income from the trust is to be used primarily for postdoctoral fellowships	<b>\$ 2,436,840</b>	\$ 2,575,529
Unrealized gain (loss) in Texas Biomed's 10% interest	<b>(138,689)</b>	478,669

## Texas Biomedical Research Institute

### Notes to Consolidated Financial Statements (continued)

#### 5. Fair Value Measurements

Accounting Standards Codification (ASC) 820, *Fair Value Measurements and Disclosures*, establishes a framework for measuring fair value. The fair value hierarchy is based on inputs to valuation techniques that are used to measure fair value, which are either observable or unobservable. Observable inputs reflect assumptions that market participants would use in pricing an asset or liability based on market data obtained from independent sources, while unobservable inputs reflect a reporting entity's pricing based upon management's own market assumptions. The fair value hierarchy under ASC 820 consists of the following three levels:

- Level 1 – Unadjusted quoted prices in active markets for identical assets and liabilities that are accessible to the reporting entity at the measurement date.
- Level 2 – Inputs other than quoted prices in active markets for identical assets and liabilities that are observable either directly or indirectly for substantially the full term of the asset or liability. Level 2 inputs include the following:
  - Quoted prices for similar assets and liabilities in active markets
  - Quoted prices for identical or similar assets or liabilities in markets that are not active
  - Observable inputs other than quoted prices that are used in the valuation of the asset or liabilities (e.g., interest rate and yield curve quotes at commonly quoted intervals)
  - Inputs that are derived principally from or corroborated by observable market data
- Level 3 – Unobservable inputs for the asset or liability (i.e., supported by little or no market activity). Level 3 inputs include management's own judgment about the assumptions market participants would use in pricing the asset or liability, including assumptions about risk.

A financial instrument's categorization within the valuation hierarchy is based on the lowest level of input that is significant to the fair value measurement. The following tables present the financial instruments carried at fair value as of December 31, 2018 and 2017, by caption on the consolidated balance sheets and by level in the ASC 820 fair value hierarchy. None of Texas Biomed's holdings are concentrated in one specific industry or investment type.

Texas Biomedical Research Institute

Notes to Consolidated Financial Statements (continued)

**5. Fair Value Measurements (continued)**

	Fair Value Measurement at December 31, 2018, Using:			
	December 31, 2018	Quoted Prices in Active Markets for Identical Assets Level 1	Significant Other Observable Inputs Level 2	Significant Unobservable Inputs Level 3
Investments:				
Mutual funds:				
U.S. equities	\$ 26,533,599	\$ 26,533,599	\$ -	\$ -
International equities	10,740,487	10,740,487	-	-
U.S. fixed-income securities	9,576,466	9,576,466	-	-
Emerging markets	3,959,822	3,959,822	-	-
Total mutual funds	<u>50,810,374</u>	<u>\$ 50,810,374</u>	<u>\$ -</u>	<u>\$ -</u>
Investments measured at net asset value:				
Limited partnerships and trusts:				
U.S. equities	12,858,477			
International equities	18,720,757			
Global fixed-income securities	2,078,544			
Hedge funds	<u>18,020,447</u>			
Total measured at net asset value	<u>51,678,225</u>			
Total investments at fair value	<u>\$ 102,488,599</u>			
Funds held in trust by others	<u>\$ 2,436,840</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 2,436,840</u>

Texas Biomedical Research Institute

Notes to Consolidated Financial Statements (continued)

5. Fair Value Measurements (continued)

	Fair Value Measurement at December 31, 2017, Using:			
	December 31, 2017	Quoted Prices in Active Markets for Identical Assets Level 1	Significant Other Observable Inputs Level 2	Significant Unobservable Inputs Level 3
Investments:				
Mutual funds:				
U.S. equities	\$ 32,424,363	\$ 32,424,363	\$ –	\$ –
International equities	11,831,831	11,831,831	–	–
U.S. fixed-income securities	7,590,026	7,590,026	–	–
Emerging markets	5,115,853	5,115,853	–	–
Total mutual funds	56,962,073	\$ 56,962,073	\$ –	\$ –
Investments measured at net asset value:				
Limited partnerships and trusts:				
U.S. equities	16,789,322			
International equities	24,732,111			
Global fixed-income securities	1,679,352			
Hedge funds	19,234,946			
Total measured at net asset value	62,435,731			
Total investments at fair value	\$ 119,397,804			
Funds held in trust by others	\$ 2,575,529	\$ –	\$ –	\$ 2,575,529

The valuation methodologies used for instruments measured at fair value as presented in the table above are as follows:

Investments that are valued at quoted prices available in an active market and interest-bearing cash are classified within Level 1 of the valuation hierarchy.

The fair values of investments in limited partnerships and trusts are measured at the entities' net asset value per share. The table on the following page includes additional disclosures required by ASC 820 for the fair value measurements of investments in certain entities that calculate fair value based on net asset value per share.

Texas Biomedical Research Institute

Notes to Consolidated Financial Statements (continued)

**5. Fair Value Measurements (continued)**

	Fair Value	Unfunded Commitments	Redemption Frequency	Redemption Notice Period
<b>December 31, 2018</b>				
U.S. equities <sup>(a)</sup>	\$ 12,858,477	\$ –	Daily-quarterly	10-30 days
International equities <sup>(b)</sup>	18,720,757	–	Monthly	10 days
Global fixed-income securities <sup>(c)</sup>	2,078,544	–	Daily-monthly	10 days
Hedge funds <sup>(d)</sup>	18,020,447	–	Monthly-annually	30-90 days
	<u>\$ 51,678,225</u>	<u>\$ –</u>		
<b>December 31, 2017</b>				
U.S. equities <sup>(a)</sup>	\$ 16,789,322	\$ –	Quarterly	30 days
International equities <sup>(b)</sup>	24,732,110	–	Monthly	10 days
Global fixed-income securities <sup>(c)</sup>	1,679,352	–	Daily-monthly	10 days
Hedge funds <sup>(d)</sup>	19,234,946	–	Monthly-annually	30-90 days
	<u>\$ 62,435,730</u>	<u>\$ –</u>		

<sup>(a)</sup> U.S. equities include investments in a limited partnership that invests in publicly traded securities in the United States. Management of the partnership has the ability to manage the investment portfolio. Their strategy is to invest in a broad spectrum of stocks covering growth and value stocks and a range of industries. This includes seeking long-term capital appreciation and investing in out-of-favor companies at attractive valuations.

<sup>(b)</sup> International equities include investments in a trust and a limited partnership that invest in international securities outside the United States. Management of the trust and partnership manage their respective investment portfolios. They focus on maximizing intrinsic value in the form of earnings, assets and dividends provided by their companies and aggregated within their portfolio by implementing a strong price discipline and by quality appraisals which seeks to identify strong companies.

<sup>(c)</sup> Global fixed-income securities include investments in a trust and limited partnership that invest in fixed-income securities, such as corporate and government bonds. Management of the trust and partnership manage their respective investment portfolios. Their strategy is to seek global bond investments offering high yield and attractive fundamentals, maintaining primary focus on sovereign debt with a goal of unlocking potential benefits of mean-reversion tendencies in interest rates and currency valuations.

<sup>(d)</sup> Hedge funds include investments in limited partnerships that invest in securities and financial instruments of issuers. Management of the partnerships practice a conservative but flexible form of event-driven investing that favors safer, more predictable transactions while accepting lower expected returns.

## Texas Biomedical Research Institute

### Notes to Consolidated Financial Statements (continued)

#### 5. Fair Value Measurements (continued)

Funds held in trust of others were classified as Level 3, because Texas Biomed must rely on the trustee's measurement of fair value of the investments held by the trust. Texas Biomed takes necessary steps to obtain a comfort level with valuation procedures used by the trustee.

#### Level 3 Reconciliation

The changes in assets measured at fair value for which Texas Biomed has used Level 3 inputs to determine fair value are as follows:

	<b>Funds Held in Trust by Others</b>
Balance, December 31, 2016	\$ 2,096,860
Unrealized gain included in the consolidated statement of changes in net assets	<u>478,669</u>
Balance, December 31, 2017	2,575,529
Unrealized gain included in the consolidated statement of changes in net assets	<u>(138,689)</u>
Balance, December 31, 2018	<u><u>\$ 2,436,840</u></u>

#### 6. Contributions Receivable

As of December 31, 2018 and 2017, Texas Biomed has received unconditional promises to give totaling \$2,342,993 and \$57,272, respectively. Contributions receivable are included in accounts receivable in the consolidated statement of financial position. Unconditional promises to give include both with and without donor restrictions for capital construction, research, faculty recruitment, or endowments. The amounts are recorded at the present value of estimated future cash flows.

The contributions receivable balance at December 31, 2018 reflects a \$2,285,721 unconditional promise to give for the renovation of Texas Biomed's property at 934 Patterson Avenue in Alamo Heights, Texas. This property is leased to The Argyle Club (The Argyle), a nonprofit organization operated as a social welfare organization. Membership in The Argyle requires initial and annual contributions to Texas Biomed. Texas Biomed leases the property (a building, its contents, surrounding land, and a parking lot) to The Argyle for a monthly rental fee of \$6,000.

Texas Biomedical Research Institute

Notes to Consolidated Financial Statements (continued)

**6. Contributions Receivable (continued)**

The Argyle is a related party to Texas Biomed as Texas Biomed has representation (but not control) on The Argyle's board.

Contributions receivable are due as follows:

	<b>December 31</b>	
	<b>2018</b>	<b>2017</b>
Promises to give:		
Less than one year	\$ 2,327,721	\$ 42,000
One to five years	17,500	17,500
	<u>2,345,221</u>	<u>59,500</u>
Less amount to reduce to present value	2,228	2,228
Contributions receivable	<u>\$ 2,342,993</u>	<u>\$ 57,272</u>

Texas Biomed records no allowance for uncollectible contributions based on the history of actual collections from donors making the promises to give. Texas Biomed expects all remaining promises to give will be received as pledged.

**7. Land, Buildings and Equipment**

At December 31, 2018 and 2017, land, buildings and equipment, less total accumulated depreciation were as follows:

	<b>December 31,</b>	
	<b>2018</b>	<b>2017</b>
Argyle, buildings and improvements	\$ 9,485,981	\$ 9,471,062
Land	359,959	359,959
Buildings and improvements	114,561,256	112,916,394
Fixtures and equipment	35,615,758	35,857,695
Construction in progress	6,013,277	1,122,508
Less: Accumulated depreciation	(98,285,818)	(93,100,238)
Net land, buildings and equipment	<u>\$ 67,750,413</u>	<u>\$ 66,627,380</u>

Land, buildings, and equipment not used in the research operations of Texas Biomed are identified separately and valued at cost. Currently, this is limited to property leased to The Argyle and is included in the table above as Argyle, buildings and improvements.

## Texas Biomedical Research Institute

### Notes to Consolidated Financial Statements (continued)

#### 8. Endowment Funds and Funds Functioning as Endowments

Texas Biomed holds donor-restricted and Board-designated endowment funds established primarily to fund specified activities for and within Texas Biomed and the research community as a whole. As required by U.S. GAAP, net assets associated with endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions.

The Uniform Prudent Management of Institutional Funds Act provides statutory guidelines for management, investment, and expenditure of endowment funds held by charitable organizations, which apply in the absence of explicit donor stipulations. The intent of Texas Biomed is to preserve the historic dollar value of original permanently restricted gifts.

Texas Biomed classifies the historic value of donor-restricted gifts to be held in perpetuity as net assets with donor restrictions. The remaining accumulated earnings of the donor-restricted endowment funds are also classified as net assets with donor restrictions until those amounts are appropriated for expenditure. Board-designated endowment funds are reported in net assets without donor restrictions.

Activity of endowments and funds functioning as endowments for the years ended December 31, 2018 and 2017, is as follows:

	Net Assets Without Donor Restrictions	Net Assets With Donor Restrictions	Total
Endowment net assets at December 31, 2016	\$ 61,079,042	\$ 51,771,412	\$ 112,850,454
Contributions	114,789	–	114,789
Investment income	910,482	441,271	1,351,753
Net unrealized/realized gain on investments	12,164,347	5,667,111	17,831,458
Gain on funds held in trust by others	–	478,669	478,669
Net assets released from program restrictions	–	(2,871,871)	(2,871,871)
Appropriation of endowment assets for expenditure	(6,256,529)	–	(6,256,529)
Endowment net assets at December 31, 2017	68,012,131	55,486,592	123,498,723
Contributions	<b>130,630</b>	–	<b>130,630</b>
Investment income	<b>807,783</b>	<b>389,363</b>	<b>1,197,146</b>
Net unrealized/realized loss on investments	<b>(7,127,748)</b>	<b>(3,175,702)</b>	<b>(10,303,450)</b>
Loss on funds held in trust by others	–	<b>(138,689)</b>	<b>(138,689)</b>
Net assets released from program restrictions	–	<b>(2,620,293)</b>	<b>(2,620,293)</b>
Appropriation of endowment assets for expenditure	<b>(6,484,108)</b>	–	<b>(6,484,108)</b>
Transfer	–	–	–
Endowment net assets at December 31, 2018	<b>\$ 55,338,688</b>	<b>\$ 49,941,271</b>	<b>\$ 105,279,959</b>

## Texas Biomedical Research Institute

### Notes to Consolidated Financial Statements (continued)

#### 8. Endowment Funds and Funds Functioning as Endowments (continued)

Texas Biomed has adopted investment and spending policies for endowment assets reflecting a disciplined, consistent management philosophy that accommodates reasonable and probable events. Preservation of capital and return on investment are of primary importance.

The primary investment objective is to preserve financial assets generated through donor gifts, so that the proceeds may be distributed for the purposes intended by the donors and to the benefit of Texas Biomed, at a level of risk deemed acceptable by the Board of Trustees.

To satisfy its long-term rate-of-return objectives, Texas Biomed relies on an investment policy outlined by its Investment Committee, which includes a desired mix of international and U.S. bonds, stocks, alternative investments, and cash and cash equivalents. Texas Biomed, at the direction of its Investment Committee, rebalances the portfolio periodically to maintain the desired distribution of assets within each asset class.

A reconciliation of endowment net assets to investments is as follows:

	<b>Net Assets Without Donor Restrictions</b>	<b>Net Assets With Donor Restrictions</b>	<b>Total</b>
Endowment net assets at December 31, 2018	\$ 55,338,688	\$ 49,941,271	\$ 105,279,959
Investment fees not withheld from investments	1,556,476	-	1,556,476
Funds held in trust by others	-	(2,436,840)	(2,436,840)
Funds in liquidity account held as cash equivalents			(1,910,996)
Investments at December 31, 2018			<u>\$ 102,488,599</u>
Endowment net assets at December 31, 2017	\$ 68,012,131	\$ 55,486,592	\$ 123,498,723
Investment fees not withheld from investments	1,319,789	-	1,319,789
Funds held in trust by others	-	(2,575,529)	(2,575,529)
Funds in liquidity account held as cash equivalents			(2,845,179)
Investments at December 31, 2017			<u>\$ 119,397,804</u>

Texas Biomed has adopted spending policies allowing endowment funds to be utilized only in accordance with the purposes established by the donor or Board of Trustees designation. In addition, it is Texas Biomed's policy not to spend or appropriate underwater endowment funds. An underwater endowment fund is one with a fair market value lower than the value of the gift that originally created that fund.

Texas Biomed has no underwater endowment funds as of December 31, 2018 and December 31, 2017.

## Texas Biomedical Research Institute

### Notes to Consolidated Financial Statements (continued)

#### 9. Notes Payable

Borrowed funds are shown in the consolidated statement of financial position as notes payable.

Interest expense is reported in the consolidated statement of activities under other expenses. Interest expense totaled \$887,436 and \$243,525 for the years ended December 31, 2018 and 2017, respectively.

#### Line of Credit

On June 6, 2017, Texas Biomed entered into a new unsecured promissory note for a \$3,000,000 one-year line of credit with a financial institution available through June 5, 2018. On June 14, 2018, the note was extended to June 13, 2019. The line of credit may be extended each year.

The interest rate was variable based on changes in London Interbank Offered Rate (LIBOR) for three months as quoted in the most recently published issue of *The Wall Street Journal*. The amount outstanding was \$3,000,000 as of December 31, 2018 and 2017.

On August 25, 2017, Texas Biomed entered into an agreement for a \$15,000,000 secured revolving line of credit with a financial institution available through August 25, 2020. On April 4, 2018, Texas Biomed and the financial institution amended the agreement to increase the secured revolving line of credit to \$20,000,000. On July 31, 2018, Texas Biomed and the financial institution further amended the agreement to increase the secured revolving line of credit to \$40,000,000. These amendments were made to consolidate outstanding balances on other loan agreements and to allow for spending in accordance with Texas Biomed's strategic plan. The amount outstanding was \$26,500,000 and \$12,058,239 as of December 31, 2018 and 2017, respectively. The interest rate is variable based on changes in the LIBOR for one month as quoted in the most recently published issue of *The Wall Street Journal* plus 1.50% per annum. As of December 31, 2018 and 2017, all interest due on the line of credit was paid by Texas Biomed. Unrestricted securities are pledged as collateral on the line of credit.

#### 10. Functional Expenses

Texas Biomed incurs expenses in three functional categories – research programs, fundraising, and general and administrative. The research programs function includes costs incurred for external research programs. The costs incurred in the efforts of gathering contributions are included in the fundraising function. The costs remaining after allocation to these two functions are categorized as general and administrative.

Texas Biomedical Research Institute

Notes to Consolidated Financial Statements (continued)

**10. Functional Expenses (continued)**

The following table shows the allocation of expenses from the functional categories to the natural expense classifications.

**For the year ended December 31, 2018**

Allocation	Research	Supporting Activities			Total Expenses
	Program Activities	General & Admin	Fund-Raising	Supporting Subtotal	
Salaries and benefits	\$ 13,404,017	\$ 18,657,237	\$ 562,641	\$ 19,219,878	\$ 32,623,895
Supplies	5,648,637	4,158,622	5,470	4,164,092	9,812,729
Depreciation	233,801	6,944,421	–	6,944,421	7,178,222
Services and professional fees	1,682,998	3,712,907	439,954	4,152,861	5,835,859
Subcontracts	4,513,926	103,405	–	103,405	4,617,331
Utilities	–	2,091,914	–	2,091,914	2,091,914
Interest expense	–	887,436	–	887,436	887,436
Subscriptions	–	549,244	100	549,344	549,344
Travel	89,284	388,826	7,467	396,293	485,577
Insurance	–	411,947	–	411,947	411,947
Shipping	190,905	133,515	313	133,828	324,733
Other expenses	40,834	1,107,308	58,873	1,166,181	1,207,015
	<u>\$ 25,804,402</u>	<u>\$ 39,146,782</u>	<u>\$ 1,074,818</u>	<u>\$ 40,221,600</u>	<u>\$ 66,026,002</u>

Texas Biomedical Research Institute

Notes to Consolidated Financial Statements (continued)

**10. Functional Expenses (continued)**

**For the year ended December 31, 2017**

Allocation	Research	Supporting Activities			Total Expenses
	Program Activities	General & Admin	Fund-Raising	Supporting Subtotal	
Salaries and benefits	\$ 13,675,421	\$ 17,654,472	\$ 538,473	\$ 18,192,945	\$ 31,868,366
Supplies	4,501,247	2,793,676	758	2,794,434	7,295,681
Depreciation	211,228	7,077,617	–	7,077,617	7,288,845
Services and professional fees	976,439	5,328,037	226,656	5,554,693	6,531,132
Subcontracts	3,673,886	73,017	–	73,017	3,746,903
Utilities	–	2,551,930	–	2,551,930	2,551,930
Interest expense	–	243,525	–	243,525	243,525
Subscriptions	–	526,342	110	526,452	526,452
Travel	95,536	354,659	8,905	363,564	459,100
Insurance	–	586,838	–	586,838	586,838
Shipping	156,462	131,145	817	131,962	288,424
Other expenses	70,866	1,428,992	62,514	1,491,506	1,562,372
	<u>\$ 23,361,085</u>	<u>\$ 38,750,250</u>	<u>\$ 838,233</u>	<u>\$ 39,588,483</u>	<u>\$ 62,949,568</u>

**11. Liquidity Management**

The following reflects Texas Biomed’s financial assets as of the balance sheet date, reduced by amounts not available for general use because of contractual or donor-imposed restrictions within one year of the balance sheet date. Amounts not available include amounts set aside for long-term investing in the endowment that could be drawn upon if the governing board approves that action; however, amounts already appropriated from the donor-restricted endowment for general expenditure within one year of the balance sheet have not been subtracted as unavailable.

## Texas Biomedical Research Institute

### Notes to Consolidated Financial Statements (continued)

#### 11. Liquidity Management (continued)

	<b>December 31</b>	
	<b>2018</b>	<b>2017</b>
Financial assets	<b>\$ 119,925,875</b>	\$ 134,239,419
Less those unavailable for general expenditures within one year, due to:		
Contractual or donor-imposed restrictions	<b>(57,488,762)</b>	(60,780,113)
Collateral requirement on outstanding debt	<b>(31,176,471)</b>	(14,186,163)
Financial assets available to meet cash needs for general expenditures within one year	<b><u>\$ 31,260,642</u></b>	<b><u>\$ 59,273,143</u></b>

Texas Biomed is substantially supported by contributions with donor restrictions. Because a donor's restriction requires resources to be used in a particular manner or in a future period, Texas Biomed must maintain sufficient resources to meet those responsibilities to its donors. Thus, financial assets may not be available for general expenditure within one year. As part of Texas Biomed's liquidity management, it has a policy to structure its financial assets to be available as its general expenditures, liabilities, and other obligations come due. In the event of an unanticipated liquidity need, Texas Biomed could also draw upon the line of credit (as further discussed in Note 8).

#### 12. Contingencies

Texas Biomed is involved in various claims and legal actions arising in the ordinary course of business. In the opinion of management, the ultimate disposition of these matters will not have a material adverse effect on Texas Biomed's consolidated financial position.

#### 13. Subsequent Events

Texas Biomed has evaluated subsequent events through June 5, 2019, the date the accompanying consolidated financial statements were available to be issued.

# Reports on Federal Award Programs



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## Report of Independent Auditors on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

Management and Trustees  
Texas Biomedical Research Institute

We have audited, in accordance with auditing standards generally accepted in the United States and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of Texas Biomedical Research Institute, which comprise the consolidated statement of financial position as of December 31, 2018, and the related consolidated statements of activities, and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated June 5, 2019.

### **Internal Control Over Financial Reporting**

In planning and performing our audit of the financial statements, we considered Texas Biomedical Research Institute's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Texas Biomedical Research Institute's internal control. Accordingly, we do not express an opinion on the effectiveness of Texas Biomedical Research Institute's internal control.

*A deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. *A material weakness* is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. *A significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

## **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether Texas Biomedical Research Institute's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

## **Purpose of this Report**

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

*Ernst + Young LLP*

June 5, 2019



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## Report of Independent Auditors on Compliance for the Major Federal Program; Report on Internal Control Over Compliance and Report on Schedule of Expenditures of Federal Awards Required by the Uniform Guidance

Management and Trustees  
Texas Biomedical Research Institute

### **Report on Compliance for the Major Federal Program**

We have audited Texas Biomedical Research Institute's compliance with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) *Compliance Supplement* that could have a direct and material effect on Texas Biomedical Research Institute's major federal program for the year ended December 31, 2018. Texas Biomedical Research Institute's major federal program is identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

#### ***Management's Responsibility***

Management is responsible for compliance with the requirements of federal statutes, regulations and the terms and conditions of its federal awards applicable to its federal programs.

#### ***Auditor's Responsibility***

Our responsibility is to express an opinion on compliance for Texas Biomedical Research Institute's major federal program based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States and the audit requirements of Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Those standards and the Uniform Guidance require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about Texas Biomedical Research Institute's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for the major federal program. However, our audit does not provide a legal determination of Texas Biomedical Research Institute's compliance.

### ***Opinion on the Major Federal Program***

In our opinion, Texas Biomedical Research Institute complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on its major federal program for the year ended December 31, 2018.

### ***Other Matters***

The results of our auditing procedures disclosed instances of noncompliance which are required to be reported in accordance with the Uniform Guidance, and which are described in the accompanying schedule of findings and questioned costs as item 2018-001, Research and Development Cluster – Allowable Costs/Cost Principles. Our opinion on the major federal program is not modified with respect to these matters.

Texas Biomedical Research Institute’s response to the noncompliance finding identified in our audit is described in the accompanying schedule of findings and questioned costs. Texas Biomedical Research Institute’s response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

### **Report on Internal Control Over Compliance**

Management of Texas Biomedical Research Institute is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered Texas Biomedical Research Institute’s internal control over compliance with the types of requirements that could have a direct and material effect on the major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for the major federal program and to test and report on internal control over compliance in accordance with the Uniform Guidance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of Texas Biomedical Research Institute’s internal control over compliance.

*A deficiency in internal control over compliance* exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. *A material weakness in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. *A significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that have not been identified. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, we did identify a deficiency in internal control over compliance, as described in the accompanying schedule of findings and questioned costs as item 2018-001, Research and Development Cluster – Allowable Costs/Cost Principles, that we consider to be a significant deficiency.

Texas Biomedical Research Institute’s response to the internal control over compliance finding identified in our audit is described in the accompanying schedule of findings and questioned costs. Texas Biomedical Research Institute’s response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of the Uniform Guidance. Accordingly, this report is not suitable for any other purpose.

### **Report on Schedule of Expenditures of Federal Awards Required by the Uniform Guidance**

We have audited the consolidated financial statements of Texas Biomedical Research Institute as of and for the year ended December 31, 2018, and have issued our report thereon dated June 5, 2019, which contained an unmodified opinion on those consolidated financial statements. Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by the Uniform Guidance and is not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States. In our opinion, the schedule of expenditures of federal awards is fairly stated, in all material respects, in relation to the consolidated financial statements as a whole.

*Ernst + Young LLP*

August 16, 2019

Texas Biomedical Research Institute  
Schedule of Expenditures of Federal Awards  
Year Ended December 31, 2018

Cluster/Federal Agency/Major Subdivision/Federal Grantor	CFDA Name/Project Name	CFDA #	Pass-Through Entity (PTE)	PTE Subaward #	Federal Expenditures			Amounts
					Direct	Pass-Through	Total	Provided to Subrecipients
<b>Research and Development</b>								
<b>U.S. Department of Defense</b>								
Advanced Research Projects Agency	Research and Technology Development	12.910	The General Hospital Corporation	227668	\$ -	\$ 112,905	\$ 112,905	\$ -
	<i>Subtotal Research and Technology Development</i>				-	112,905	112,905	-
<b>TOTAL - Advanced Research Projects Agency</b>					-	<b>112,905</b>	<b>112,905</b>	-
<b>Chemical, Biological, Radiological &amp; Nuclear Defense</b>								
Information Analysis Center								
Defense Technical Information Center	Challenge Phase for Profectus BioSciences Trivalent Pan-Filovirus Vaccine	12.RD	Battelle	512256	-	(9,789)	(9,789)	-
	<i>Subtotal</i>				-	(9,789)	(9,789)	-
<b>TOTAL - Chemical, Biological, Radiological &amp; Nuclear Defense Information Analysis Center</b>					-	<b>(9,789)</b>	<b>(9,789)</b>	-
<b>Office of the Secretary of Defense</b>								
Department of Defense	In vitro and in vivo Characterization of Filoviruses through the Exploration of Various Vaccine Candidates	12.RD			2,146	-	2,146	-
	A Novel Strategy for Treating Peripheral Nerve Injury	12.RD	The President and Fellows of Harvard College	164608-5110301	-	32,291	32,291	-
	<i>Subtotal</i>				2,146	32,291	34,437	-
<b>TOTAL - Office of the Secretary of Defense</b>					<b>2,146</b>	<b>32,291</b>	<b>34,437</b>	-
<b>U.S. Army Medical Command</b>								
U.S. Army Medical Research Acquisition Activity	Military Medical Research and Development	12.420	UTHSCSA	159421/155536	-	69,984	69,984	-
	<i>Subtotal Military Medical Research and Development</i>				-	69,984	69,984	-
<b>TOTAL - U.S. Army Medical Command</b>					-	<b>69,984</b>	<b>69,984</b>	-
<b>TOTAL U.S. Department of Defense</b>					<b>2,146</b>	<b>205,391</b>	<b>207,537</b>	-

Texas Biomedical Research Institute  
Schedule of Expenditures of Federal Awards (continued)  
Year Ended December 31, 2018

Cluster/Federal Agency/Major Subdivision/Federal Grantor	CFDA Name/Project Name	CFDA #	Pass-Through Entity (PTE)	PTE Subaward #	Federal Expenditures			Amounts
					Direct	Pass-Through	Total	Provided to Subrecipients
<b>Research and Development (continued)</b>								
<b>US Department of Health and Human Services</b>								
<b>Food and Drug Administration</b>								
Food and Drug Administration	Bordetella-Free Weanling Baboons	93.RD			\$ (1,652)	\$ -	\$ (1,652)	\$ -
	Bordetella-Free Weanling Baboons	93.RD			179,085	-	179,085	-
	Pertussis Vaccine Study in Baboons-R	93.RD			132,563	-	132,563	-
	Purchase of 20 Baboons (10 males and and 10 females); all laboratory work; and transport to Maryland	93.RD	Board of Regents of the University of Oklahoma		-	25,246	25,246	-
	<i>Subtotal</i>				<u>309,996</u>	<u>25,246</u>	<u>335,242</u>	<u>-</u>
<b>TOTAL - Food and Drug Administration</b>								
<b>Office of the Secretary</b>								
Office of the Assistant Secretary for Preparedness and Response	Biomedical Advanced Research and Development Authority (BARDA), Biodefense Medical Countermeasure Development	93.360	IIT Research Institute	144-0-2378-001-RL	-	5,187	5,187	-
		93.360	Battelle	587402	-	1,500,989	1,500,989	-
		93.360	Battelle	703470	-	1,047,890	1,047,890	-
		93.360	Battelle	703661	-	976,638	976,638	-
		93.360	Battelle	722369	-	932,821	932,821	-
	<i>Subtotal Biomedical Advanced Research and Development Authority (BARDA), Biodefense Medical Countermeasure Development</i>				<u>-</u>	<u>4,463,525</u>	<u>4,463,525</u>	<u>-</u>
<b>TOTAL - Office of the Secretary</b>								
<b>National Institutes of Health</b>								
National Institute of Environmental Health Sciences	Environmental Health	93.113	The Trustees of Columbia University in the City of New York	3(GG013113-01)	-	66,851	66,851	-
	<i>Subtotal Environmental Health</i>				<u>-</u>	<u>66,851</u>	<u>66,851</u>	<u>-</u>
National Institute of Dental and Craniofacial Research	Oral Diseases and Disorders Research	93.121			567,519	-	567,519	46,945
	<i>Subtotal Oral Diseases and Disorders Research</i>				<u>567,519</u>	<u>-</u>	<u>567,519</u>	<u>46,945</u>
National Human Genome Research Institute	Human Genome Research	93.172			(587)	-	(587)	-
	<i>Subtotal Human Genome Research</i>				<u>(587)</u>	<u>-</u>	<u>(587)</u>	<u>-</u>
National Institute of Mental Health	Mental Health Research Grants	93.242			282,277	-	282,277	22,470
	<i>Subtotal Mental Health Research Grants</i>				<u>282,277</u>	<u>-</u>	<u>282,277</u>	<u>22,470</u>
National Institute on Minority Health and Health Disparities	Minority Health and Health Disparities Research	93.307	University of North Carolina	5109072	-	460,390	460,390	-
	<i>Subtotal Minority Health and Health Disparities Research</i>				<u>-</u>	<u>460,390</u>	<u>460,390</u>	<u>-</u>

Texas Biomedical Research Institute  
Schedule of Expenditures of Federal Awards (continued)  
Year Ended December 31, 2018

Cluster/Federal Agency/Major Subdivision/Federal Grantor	CFDA Name/Project Name	CFDA #	Pass-Through Entity (PTE)	PTE Subaward #	Federal Expenditures			Amounts
					Direct	Pass-Through	Total	Provided to Subrecipients
<b>Research and Development (continued)</b>								
<b>US Department of Health and Human Services (continued)</b>								
<b>National Institutes of Health (continued)</b>								
NIH Office of the Director	Research Infrastructure Programs	93.351			\$ 7,251,573	\$ -	\$ 7,251,573	\$ 268,540
		93.351			2,261,167	-	2,261,167	-
		93.351			571,619	-	571,619	263,705
	<i>Subtotal Research Infrastructure Programs</i>				10,084,359	-	10,084,359	532,245
National Heart, Lung, and Blood Institute	Cardiovascular Diseases Research	93.837	University of Alabama at Birmingham	000509019-001	-	3,642	3,642	-
		93.837	The Regents of the University of California, San Diego	104297239	-	125,058	125,058	-
		93.837			487,908	-	487,908	-
		93.837			114,774	-	114,774	-
	<i>Subtotal Cardiovascular Diseases Research</i>				602,682	128,700	731,382	-
National Institute of Diabetes and Digestive and Kidney Diseases	Diabetes, Digestive, and Kidney Diseases Extramural Research	93.847			607,414	-	607,414	544,480
		93.847			263,510	-	263,510	18,059
		93.847			55,172	-	55,172	-
	<i>Subtotal Diabetes, Digestive, and Kidney Diseases Extramural Research</i>				926,096	-	926,096	562,539
National Institute of Neurological Disorders and Stroke	Extramural Research Programs in the Neurosciences and Neurological Disorders	93.853	Trinity University	26-1342523-TXBIO	-	3,055	3,055	-
	<i>Subtotal Extramural Research Programs in the Neurosciences and Neurological Disorders</i>				-	3,055	3,055	-
National Institute of Allergy and Infectious Diseases	Allergy and Infectious Diseases Research	93.855	Battelle	403732	-	52,634	52,634	-
		93.855	Battelle	521876	-	743,026	743,026	-
		93.855	The Regents of the University of CA, Santa Cruz	A00-2044-S002-S0183838	-	15,777	15,777	-
		93.855	University of Louisville Research Foundation, Inc.	ULRF 12-0393-02	-	69,149	69,149	-
		93.855	UTHSCSA	158423/158421	-	112,443	112,443	-
		93.855	Purdue University	4102-68572	-	120,871	120,871	-
		93.855	The Scripps Research Institute	5-53116	-	55,628	55,628	-
		93.855	The Scripps Research Institute	5-53585	-	51,385	51,385	-
		93.855	The Washington University	WU-17-31-Mod 1	-	279,255	279,255	-
		93.855	The Washington University	WU-17-48-Mod 1	-	307,741	307,741	-
		93.855	Board of Regents of University of Georgia	SP00012813-03	-	14,474	14,474	-

Texas Biomedical Research Institute  
Schedule of Expenditures of Federal Awards (continued)  
Year Ended December 31, 2018

Cluster/Federal Agency/Major Subdivision/Federal Grantor	CFDA Name/Project Name	CFDA #	Pass-Through Entity (PTE)	PTE Subaward #	Federal Expenditures			Amounts Provided to Subrecipients
					Direct	Pass-Through	Total	
<b>Research and Development (continued)</b>								
<b>US Department of Health and Human Services (continued)</b>								
<b>National Institutes of Health (continued)</b>								
National Institute of Allergy and Infectious Diseases (continued)								
		93.855	Board of Regents of University of Georgia	SP00012813-02	\$ -	\$ 37,272	\$ 37,272	\$ -
		93.855	Stellenbosch University, Faculty of Med.&HS	S004089	-	2,156	2,156	-
		93.855	University of Notre Dame	203189TBRI	-	267,269	267,269	-
		93.855	University of Notre Dame	203482TBRI	-	242,417	242,417	-
		93.855	The UTHSCA at Houston	0012911A	-	1,138,639	1,138,639	-
		93.855	University of Maryland	PUR01-0000039445	-	145,496	145,496	-
		93.855	University of Maryland Baltimore	PUR01-0000040522	-	95,276	95,276	-
		93.855	University of Iowa	S00205-01	-	4,867	4,867	-
		93.855			781,232	-	781,232	-
		93.855			512,200	-	512,200	-
		93.855			319,331	-	319,331	-
		93.855			437,375	-	437,375	-
		93.855			658,154	-	658,154	63,042
		93.855			746	-	746	-
		93.855			84,625	-	84,625	-
		93.855			969,089	-	969,089	364,974
		93.855			499,442	-	499,442	209,343
		93.855			2,915,789	-	2,915,789	1,073,241
		93.855			488,093	-	488,093	30,000
		93.855			208,634	-	208,634	-
		93.855			105,847	-	105,847	-
	<i>Subtotal Allergy and Infectious Diseases Research</i>				<u>7,980,557</u>	<u>3,755,775</u>	<u>11,736,332</u>	<u>1,740,600</u>

Texas Biomedical Research Institute  
Schedule of Expenditures of Federal Awards (continued)  
Year Ended December 31, 2018

Cluster/Federal Agency/Major Subdivision/Federal Grantor	CFDA Name/Project Name	CFDA #	Pass-Through Entity (PTE)	PTE Subaward #	Federal Expenditures			Amounts	
					Direct	Pass-Through	Total	Provided to Subrecipients	
<b>Research and Development (continued)</b>									
<b>US Department of Health and Human Services (continued)</b>									
<b>National Institutes of Health (continued)</b>									
National Institute of Allergy and Infectious Diseases (continued)	Targeting Therapeutics Development to Relieve Bottlenecks: Optimizing Lead Therapeutic Compounds against Infectious Pathogens	93.HHSN272201500015C	Southwest Research Institute	H99067CP	\$ -	\$ 363,118	\$ 363,118	\$ -	
	<i>Subtotal Targeting Therapeutics Development to Relieve Bottlenecks: Optimizing Lead Therapeutic Compounds against Infectious Pathogens</i>					-	363,118	363,118	-
Eunice Kennedy Shriver National Institute of Child Health and Human Development	Child Health and Human Development Extramural Research	93.865	The Board of Trustees University of Illinois	15966	-	8,201	8,201	-	
		93.865	University of Wyoming	1002696-TBRI-Year3	-	17,969	17,969	-	
		93.865	University of Wyoming	1002696-TBRI-Year4	-	187,776	187,776	-	
	<i>Subtotal Child Health and Human Development Extramural Research</i>					-	213,946	-	
National Institute on Aging	Aging Research	93.866			1,838,018	-	1,838,018	366,885	
	<i>Subtotal Aging Research</i>					1,838,018	-	1,838,018	366,885
<b>TOTAL - National Institutes of Health</b>					<b>22,280,921</b>	<b>4,991,835</b>	<b>27,272,756</b>	<b>3,271,684</b>	
<b>TOTAL - U.S. Department of Health and Human Services</b>					<b>22,590,917</b>	<b>9,480,606</b>	<b>32,071,523</b>	<b>3,271,684</b>	
<b>TOTAL - RESEARCH AND DEVELOPMENT CLUSTER</b>					<b>22,593,063</b>	<b>9,685,997</b>	<b>32,279,060</b>	<b>3,271,684</b>	
<b>TOTAL - EXPENDITURES OF FEDERAL AWARDS</b>					<b>\$ 22,593,063</b>	<b>\$ 9,685,997</b>	<b>\$ 32,279,060</b>	<b>\$ 3,271,684</b>	

See accompanying notes to schedule of expenditures of federal awards.

# Texas Biomedical Research Institute

## Notes to Schedule of Expenditures of Federal Awards

December 31, 2018

### 1. Basis of Presentation

The accompanying schedule of expenditures of federal awards (the Schedule) includes the federal grant activity of Texas Biomedical Research Institute (Texas Biomed) under programs of the federal government for the year ended December 31, 2018. The information in this Schedule is presented in accordance with the Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the consolidated financial statements.

### 2. Summary of Significant Accounting Policies

Expenditures reported on the Schedule are reported on the accrual basis of accounting. Such expenditures are recognized following the cost principles contained in the Uniform Guidance or OMB Circular A-122, *Cost Principles for Non-Profit Organizations*. Negative amounts shown on the Schedule represent adjustments or credits made in the normal course of business to amounts reported as expenditures in prior years. Texas Biomed has elected not to use the 10% de minimis indirect cost rate allowed under the Uniform Guidance.

### 3. Reconciliation to Financial Statements

Texas Biomed recognizes revenues from grants and contracts at the time eligible direct and indirect costs are incurred under terms of the awards and recognized as expenditures. Revenue recognized from expenditure of federal awards is reconciled to Texas Biomed's consolidated statement of activities as follows:

Revenues reported in Texas Biomed's consolidated financial statements:	
Grants and contracts	\$ 39,023,421
Less amounts not subject to Uniform Guidance	6,030,680
Less subrecipient accruals	713,681
Total federal award expenditures	<u>\$ 32,279,060</u>

Texas Biomedical Research Institute

Schedule of Findings and Questioned Costs

Year Ended December 31, 2018

**Section I – Summary of Auditor’s Results**

**Financial Statements**

Type of report the auditor issued on whether the financial statements audited were prepared in accordance with GAAP (unmodified, qualified, adverse or disclaimer):

Unmodified

Internal control over financial reporting:

Material weakness(es) identified?

\_\_\_ yes      X no

Significant deficiency(ies) identified?

\_\_\_ yes      X none reported

Noncompliance material to financial statements noted?

\_\_\_ yes      X no

**Federal Awards**

Internal control over major federal programs:

Material weakness(es) identified?

\_\_\_ yes      X no

Significant deficiency(ies) identified?

X yes      \_\_\_ none reported

Type of auditor’s report issued on compliance for major federal programs (unmodified, qualified, adverse or disclaimer):

Unmodified

Any audit findings disclosed that are required to be reported in accordance with 2 CFR 200.516(a)?

X yes      \_\_\_ no

**Identification of major federal programs**

**CFDA number(s)**

**Name of federal program or cluster**

12.910, 12.RD, 12.420, 93.RD, 93.360, 93.113, 93.121, 93.172, 93.242, 93.307, , 93.351, 93.837, 93.847, 93.853, 93.855, 93.HHSN272201500015C, 93.865, 93.866

Research and Development Cluster

Dollar threshold used to distinguish between Type A and Type B programs:

\$ 968,372

Auditee qualified as low-risk auditee?

X yes      \_\_\_ no

Texas Biomedical Research Institute

Schedule of Findings and Questioned Costs (continued)

**Section II – Financial Statement Findings**

No findings were noted.

**Section III – Federal Award Findings and Questioned Costs**

**Finding 2018-001 – Allowable Costs/Cost Principles**

Information on the federal program:

U.S. Department of Defense  
U.S. Department of Health and Human Services – National Institutes of Health  
Research and Development Cluster

Criteria or specific requirement (including statutory, regulatory or other citation)

In accordance with 2 CFR Section 200.430 – Compensation Personal Services:

(a) General. Compensation for personal services includes all remuneration, paid currently or accrued, for services of employees rendered during the period of performance under the Federal award including, but not necessarily limited to wages and salaries. Compensation for personal services may also include fringe benefits which are addressed in §200.431 Compensation—fringe benefits. Costs of compensation are allowable to the extent that they satisfy the specific requirements of this part, and that the total compensation for individual employees:

- (1) Is reasonable for the services rendered and conforms to the established written policy of the non-Federal entity consistently applied to both Federal and non-Federal activities;
- (2) Follows an appointment made in accordance with a non-Federal entity’s laws and/or rules or written policies and meets the requirements of Federal statute, where applicable; and
- (3) Is determined and supported as provided in paragraph (i) of this section, Standards for Documentation of Personnel Expenses, when applicable.

Texas Biomedical Research Institute

Schedule of Findings and Questioned Costs (continued)

**Section III – Federal Award Findings and Questioned Costs (continued)**

Criteria or specific requirement (including statutory, regulatory or other citation) (continued)

(i) Standards for Documentation of Personnel Expenses (1) Charges to Federal awards for salaries and wages must be based on records that accurately reflect the work performed. These records must:

(i) Be supported by a system of internal control which provides reasonable assurance that the charges are accurate, allowable, and properly allocated;

(ii) Be incorporated into the official records of the non-Federal entity;

(iii) Reasonably reflect the total activity for which the employee is compensated by the non-Federal entity, not exceeding 100% of compensated activities;

(iv) Encompass both federally assisted and all other activities compensated by the non-Federal entity on an integrated basis, but may include the use of subsidiary records as defined in the non-Federal entity's written policy;

(v) Comply with the established accounting policies and practices of the non-Federal entity; and

(vii) Support the distribution of the employee's salary or wages among specific activities or cost objectives if the employee works on more than one Federal award; a Federal award and non-Federal award; an indirect cost activity and a direct cost activity; two or more indirect activities which are allocated using different allocation bases; or an unallowable activity and a direct or indirect cost activity.

(viii) Budget estimates (i.e., estimates determined before the services are performed) alone do not qualify as support for charges to Federal awards, but may be used for interim accounting purposes, provided that:

(A) The system for establishing the estimates produces reasonable approximations of the activity actually performed;

Texas Biomedical Research Institute

Schedule of Findings and Questioned Costs (continued)

**Section III – Federal Award Findings and Questioned Costs (continued)**

Criteria or specific requirement (including statutory, regulatory or other citation) (continued)

(B) Significant changes in the corresponding work activity (as defined by the non-Federal entity's written policies) are identified and entered into the records in a timely manner. Short term (such as one or two months) fluctuation between workload categories need not be considered as long as the distribution of salaries and wages is reasonable over the longer term; and

(C) The non-Federal entity's system of internal controls includes processes to review after-the-fact interim charges made to a Federal award based on budget estimates. All necessary adjustments must be made such that the final amount charged to the Federal award is accurate, allowable, and properly allocated.

(ix) Because practices vary as to the activity constituting a full workload, records may reflect categories of activities expressed as a percentage distribution of total activities.

(2) For records which meet the standards required in paragraph (i)(1) of this section, the non-Federal entity will not be required to provide additional support or documentation for the work performed, other than that referenced in paragraph (i)(3) of this section.

Condition:

Texas Biomedical Research Institute (Texas Biomed) did not meet the Standards for Documentation of Personnel Expenses according to 2 CFR 200.430, since Texas Biomed's records were not adequately supported by a system of internal control which provided reasonable assurance that the charges were accurate, allowable, and properly allocated during the year. Texas Biomed indicated that internal controls over personnel expenses include semi-annual effort certifications of actual hours worked. We determined this internal control to be ineffective during the year based on the following:

Texas Biomedical Research Institute

Schedule of Findings and Questioned Costs (continued)

**Section III – Federal Award Findings and Questioned Costs (continued)**

Condition:  
(continued)

- Semi-annual effort certifications were not completed timely. For the period from January 1, 2018 through June 30, 2018, certifications were not completed until April 2019, during the audit. For the period from July 1, 2018 through December 31, 2018, certifications were not completed until April 2019. According to Texas Biomed’s written effort reporting procedures, the deadline for certification of all reports is no later than the end of the third month following the end of the reporting period (September and March, respectively, for each reporting period).

Questioned costs:

\$0

Context:

We selected 25 Research and Development cluster payroll expenditures for testing. Our selections totaled \$22,182 out of a population totaling \$7.3 million of salaries and fringe benefits. As in prior years, we obtained written procedures which indicated internal controls included semi-annual certification of personnel costs and requested the certifications. Texas Biomed indicated during the audit in March and April 2019 that the semi-annual certifications were in process but not completed. Once the certifications were completed in March and April 2019, Texas Biomed provided them for our review. Upon review of the certifications, we noted that the certifications agreed to the amounts charged to the Federal awards within immaterial differences for all of our 25 selections. In addition to our 25 selections, we obtained semi-annual certifications for all other employees charged to Federal awards to determine they had been completed. As a result of our testing, we consider the personnel costs for our 25 selections to be allowable costs for the Federal awards; however, as noted above, we have identified deficiencies in internal control over compliance and noncompliance with 2 CFR 200.430 based upon the above criteria.

Texas Biomedical Research Institute

Schedule of Findings and Questioned Costs (continued)

**Section III – Federal Award Findings and Questioned Costs (continued)**

Effect

Texas Biomed did not perform timely semi-annual certifications of personnel costs in accordance with its written procedures and internal controls. This could delay necessary adjustments from being made to ensure the final amounts charged to the Federal award are accurate, allowable, and properly allocated based on actual hours worked.

Cause

Effective internal controls were not in place to ensure timely completion of semi-annual certifications of personnel costs.

Identification as a repeat finding, if applicable

N/A

Recommendation

Texas Biomed should ensure that semi-annual effort certifications are completed timely, within three months of the end of certification period, in accordance with written procedures.

Views of responsible officials and planned corrective actions:

Texas Biomed agrees with the finding and we have updated our procedures to ensure timely certifications of effort.

Responsible Officials: Bruce Edwards, Chief Financial Officer and Eva Zepeda, Director of Finance

Implementation Date: July 25, 2019

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## Summary Schedule of Prior Audit Findings

Year Ended December 31, 2018

### **Finding 2017-001 – Period of Performance**

Status: This finding has been corrected.

There were no uncorrected findings in 2016.

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Corrective Action Plan

Finding 2018-001 – Allowable Costs/Cost Principles

In accordance with 2 CFR Section 200.430 – Compensation Personal Services:

(a) General. Compensation for personal services includes all remuneration, paid currently or accrued, for services of employees rendered during the period of performance under the Federal award, including but not necessarily limited to wages and salaries. Compensation for personal services may also include fringe benefits which are addressed in §200.431 Compensation—fringe benefits. Costs of compensation are allowable to the extent that they satisfy the specific requirements of this part, and that the total compensation for individual employees:

(1) Is reasonable for the services rendered and conforms to the established written policy of the non-Federal entity consistently applied to both Federal and non-Federal activities;

(2) Follows an appointment made in accordance with a non-Federal entity's laws and/or rules or written policies and meets the requirements of Federal statute, where applicable; and

(3) Is determined and supported as provided in paragraph (i) of this section, Standards for Documentation of Personnel Expenses, when applicable.

(i) Standards for Documentation of Personnel Expenses (1) Charges to Federal awards for salaries and wages must be based on records that accurately reflect the work performed. These records must:

(i) Be supported by a system of internal control which provides reasonable assurance that the charges are accurate, allowable, and properly allocated;

(ii) Be incorporated into the official records of the non-Federal entity;

(iii) Reasonably reflect the total activity for which the employee is compensated by the non-Federal entity, not exceeding 100% of compensated activities (for IHE, this per the IHE's definition of IBS);

(iv) Encompass both federally assisted and all other activities compensated by the non-Federal entity on an integrated basis, but may include the use of subsidiary records as defined in the non-Federal entity's written policy;

(v) Comply with the established accounting policies and practices of the non-Federal entity (See paragraph (h)(1)(ii) above for treatment of incidental work for IHEs.); and

(vii) Support the distribution of the employee's salary or wages among specific activities or cost objectives if the employee works on more than one Federal award; a Federal award and non-Federal award; an indirect cost activity and a direct cost activity; two or more indirect activities which are allocated using different allocation bases; or an unallowable activity and a direct or indirect cost activity.

(viii) Budget estimates (i.e., estimates determined before the services are performed) alone do not qualify as support for charges to Federal awards, but may be used for interim accounting purposes, provided that:

(A) The system for establishing the estimates produces reasonable approximations of the activity actually performed;

(B) Significant changes in the corresponding work activity (as defined by the non-Federal entity's written policies) are identified and entered into the records in a timely manner. Short term (such as one or two months) fluctuation between workload categories need not be considered as long as the distribution of salaries and wages is reasonable over the longer term; and

(C) The non-Federal entity's system of internal controls includes processes to review after-the-fact interim charges made to a Federal awards based on budget estimates. All necessary adjustment must be made such that the final amount charged to the Federal award is accurate, allowable, and properly allocated.

(ix) Because practices vary as to the activity constituting a full workload (for IHEs, IBS), records may reflect categories of activities expressed as a percentage distribution of total activities.

(x) It is recognized that teaching, research, service, and administration are often inextricably intermingled in an academic setting. When recording salaries and wages charged to Federal awards for IHEs, a precise assessment of factors that contribute to costs is therefore not always feasible, nor is it expected.

(2) For records which meet the standards required in paragraph (i)(1) of this section, the non-Federal entity will not be required to provide additional support or documentation for the work performed, other than that referenced in paragraph (i)(3) of this section.

Condition Reported by EY:

Texas Biomedical Research Institute (Texas Biomed) did not meet the Standards for Documentation of Personnel Expenses according to 2 cfr 200.430, since Texas Biomed's records were not adequately supported by a system of internal control which provided reasonable assurance that the charges were accurate, allowable, and properly allocated during the year. Texas Biomed indicated that internal controls over personnel expenses include semi-annual effort certifications of actual hours worked. We determined this internal control to be ineffective during the year based on the following:

Semi-annual effort certifications were not completed timely. For the period from January 1, 2018 through June 30, 2018, certifications were not completed until April 2019, during the audit. For the period from July 1, 2018 through December 31, 2018 certifications were not completed until April 2019. According to Texas Biomed's written effort reporting procedures, the deadline for certification of all reports is no later than the end of the third month following the end of the reporting period (September and March respectively for each reporting period).

Corrective Action:

Texas Biomed has approved an Effort Certification Policy (SPA-03) enforced by Sponsored Programs Administration. Per policy, Sponsored Programs Administration will be responsible for distributing Effort Reports no less than twice a year to all required Certifiers. Certifiers must review and approve or communicate necessary modifications within 14 days of receipt; modified Effort Reports must be reviewed and approved within 14 days of receipt. Certifiers' approval within 14 days serves as confirmation of accurate, allowable and properly allocated personnel expenses for each reporting period.

Responsible Parties: Bruce Edwards, Chief Financial Officer  
Eva Zepeda, Director of Finance  
Eduardo Meza, Director of Sponsored Programs Administration

Completion Date: July 25, 2019