

**TEXAS HEART INSTITUTE
AND SUBSIDIARY**

Consolidated Financial Statements and
Independent Auditor's Reports

Years Ended December 31, 2017 and 2016

TEXAS HEART INSTITUTE AND SUBSIDIARY
YEARS ENDED DECEMBER 31, 2017 AND 2016

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INDEPENDENT AUDITOR'S REPORT

To the Board of Trustees
Texas Heart Institute and Subsidiary

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of Texas Heart Institute and Subsidiary (the "Institute"), a Texas nonprofit organization, which comprise the consolidated statements of financial position as of December 31, 2017 and 2016, and the related consolidated statements of activities and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America 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 financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Institute as of December 31, 2017 and 2016, and the changes in its net assets and cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated August 3, 2018, on our consideration of the 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 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 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 the Institute's internal control over financial reporting and compliance.



Houston, Texas
August 3, 2018

TEXAS HEART INSTITUTE AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF FINANCIAL POSITION
DECEMBER 31, 2017 AND 2016

ASSETS	<u>2017</u>	<u>2016</u>
CURRENT ASSETS		
Cash and cash equivalents	\$ 6,711,571	\$ 9,160,497
Receivables:		
Pledges	4,215,372	4,367,551
Grants and contracts	2,909,025	5,704,047
Other receivables	20,224	1,711
Total receivables	<u>7,144,621</u>	<u>10,073,309</u>
Property held for sale	-	500,000
Other assets	<u>261,708</u>	<u>287,516</u>
Total current assets	<u>14,117,900</u>	<u>20,021,322</u>
NONCURRENT ASSETS		
Cash and cash equivalents restricted for endowment	986,969	917,786
Long-term pledges receivable, net	4,797,295	6,963,965
Long-term investments, includes \$26,231,999 and \$21,883,794 for 2017 and 2016, respectively, subject to donor restriction	78,994,407	67,441,604
Property and equipment, net	<u>26,831,467</u>	<u>28,498,015</u>
Total long-term assets	<u>111,610,138</u>	<u>103,821,370</u>
TOTAL ASSETS	<u>\$ 125,728,038</u>	<u>\$ 123,842,692</u>
LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES		
Accounts payable and accrued liabilities	\$ 1,467,428	\$ 1,377,212
Payables to St. Luke's Health System	617,428	2,779,217
Deferred revenues	1,865,918	2,383,007
Other current liabilities	<u>229,907</u>	<u>1,308,267</u>
Total current liabilities	4,180,681	7,847,703
LONG-TERM LIABILITIES		
Pension obligations	294,587	769,660
Capital lease liabilities	-	74,831
Total long-term liabilities	<u>294,587</u>	<u>844,491</u>
Total Liabilities	<u>4,475,268</u>	<u>8,692,194</u>
NET ASSETS		
Unrestricted	65,665,532	73,018,416
Temporarily restricted	37,476,224	25,533,529
Permanently restricted	<u>18,111,014</u>	<u>16,598,553</u>
Total Net Assets	<u>121,252,770</u>	<u>115,150,498</u>
TOTAL LIABILITIES AND NET ASSETS	<u>\$ 125,728,038</u>	<u>\$ 123,842,692</u>

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

TEXAS HEART INSTITUTE AND SUBSIDIARY

CONSOLIDATED STATEMENT OF ACTIVITIES

YEAR ENDED DECEMBER 31, 2017

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
REVENUES				
Net revenue from operations	\$ 1,532,627	\$ -	\$ -	\$ 1,532,627
Grants and contracts	6,537,600	-	-	6,537,600
Contributions from affiliates	12,381,462	-	-	12,381,462
Philanthropy	3,260,947	3,431,627	991,638	7,684,212
Investment income, net	8,410,916	3,279,805	520,823	12,211,544
Net assets released from restrictions:				
Satisfaction of program restrictions	(5,231,263)	5,231,263	-	-
TOTAL REVENUES	26,892,289	11,942,695	1,512,461	40,347,445
EXPENSES				
Personnel	20,879,151	-	-	20,879,151
Supplies	2,735,025	-	-	2,735,025
Professional costs	1,656,263	-	-	1,656,263
Purchased services	2,873,083	-	-	2,873,083
Facilities expense	4,268,098	-	-	4,268,098
Interest expense	6,253	-	-	6,253
Depreciation	2,302,373	-	-	2,302,373
TOTAL EXPENSES	34,720,246	-	-	34,720,246
ADJUSTMENT TO UNFUNDED PENSION LOSSES	475,073	-	-	475,073
CHANGE IN NET ASSETS	(7,352,884)	11,942,695	1,512,461	6,102,272
NET ASSETS, BEGINNING OF YEAR	73,018,416	25,533,529	16,598,553	115,150,498
NET ASSETS, END OF YEAR	<u>\$ 65,665,532</u>	<u>\$ 37,476,224</u>	<u>\$ 18,111,014</u>	<u>\$ 121,252,770</u>

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

TEXAS HEART INSTITUTE AND SUBSIDIARY

CONSOLIDATED STATEMENT OF ACTIVITIES

YEAR ENDED DECEMBER 31, 2016

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
REVENUES				
Net revenue from operations	\$ 1,331,613	\$ -	\$ -	\$ 1,331,613
Grants and contracts	7,968,106	-	-	7,968,106
Contributions from affiliates	12,128,251	-	-	12,128,251
Philanthropy	5,857,818	8,735,092	62,954	14,655,864
Investment income, net	2,852,682	1,232,616	142,339	4,227,637
Net assets released from restrictions:				
Satisfaction of program restrictions	2,774,476	(2,774,476)	-	-
TOTAL REVENUES	32,912,946	7,193,232	205,293	40,311,471
EXPENSES				
Personnel	20,520,455	-	-	20,520,455
Supplies	3,387,744	-	-	3,387,744
Professional costs	1,807,959	-	-	1,807,959
Purchased services	2,445,841	-	-	2,445,841
Facilities expense	4,752,993	-	-	4,752,993
Interest expense	16,284	-	-	16,284
Depreciation	2,965,682	-	-	2,965,682
TOTAL EXPENSES	35,896,958	-	-	35,896,958
ADJUSTMENT TO UNFUNDED PENSION LOSSES	25,119	-	-	25,119
CHANGE IN NET ASSETS	(2,958,893)	7,193,232	205,293	4,439,632
NET ASSETS, BEGINNING OF YEAR	75,977,309	18,340,297	16,393,260	110,710,866
NET ASSETS, END OF YEAR	<u>\$ 73,018,416</u>	<u>\$ 25,533,529</u>	<u>\$ 16,598,553</u>	<u>\$ 115,150,498</u>

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

TEXAS HEART INSTITUTE AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CASH FLOWS

YEARS ENDED DECEMBER 31, 2017 AND 2016

CASH FLOWS FROM OPERATING ACTIVITIES	<u>2017</u>	<u>2016</u>
Change in net assets	\$ 6,102,272	\$ 4,439,632
Adjustments to reconcile changes in net assets to net cash provided by operating activities:		
Amortization of unearned interest income	(6,253)	(6,253)
Contributions restricted for endowment	(5,001)	(50,503)
Depreciation and amortization	2,302,373	2,965,682
Net unrealized and realized investment (gains)/losses	(10,190,327)	(2,384,653)
Adjustment to unfunded pension losses	(475,073)	25,119
Interest payments under capital lease	-	(10,031)
Changes in operating assets and liabilities:		
Receivables	5,095,358	(4,863,670)
Other assets	525,808	(110,982)
Accounts payable and accrued liabilities	90,216	(801,899)
Deferred revenues	(517,089)	345,194
Payables to St. Luke's Episcopal Hospital	(2,161,789)	2,287,243
Pension obligations	-	(27,426)
Other liabilities	(196,408)	(30,028)
Total adjustments	<u>(5,538,185)</u>	<u>(2,662,207)</u>
Net cash provided by operating activities	<u>564,087</u>	<u>1,777,425</u>
 CASH FLOWS FROM INVESTING ACTIVITIES		
Additions to property and equipment	(635,824)	(314,650)
Purchase of investments	(41,055,867)	(1,461,321)
Proceeds from sales of investments	39,699,643	1,217,774
Net cash used in investing activities	<u>(1,992,048)</u>	<u>(558,197)</u>
 CASH FLOWS FROM FINANCING ACTIVITIES		
Contributions restricted for endowment	5,001	50,503
Change in cash restricted for endowment	(69,183)	(682,138)
Short-term debt payment for preferred stock	(859,750)	(1,000,000)
Payments on capital lease obligations	(97,033)	(411,298)
Net cash used in financing activities	<u>(1,020,965)</u>	<u>(2,042,933)</u>

Continued

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

TEXAS HEART INSTITUTE AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS, CONT'D
YEARS ENDED DECEMBER 31, 2017 AND 2016

Net decrease in cash and cash equivalents	(2,448,926)	(823,705)
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	<u>9,160,497</u>	<u>9,984,202</u>
CASH AND CASH EQUIVALENTS, END OF YEAR	<u>\$ 6,711,571</u>	<u>\$ 9,160,497</u>
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION		
Interest paid	<u>\$ 6,253</u>	<u>\$ 6,253</u>

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

TEXAS HEART INSTITUTE AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 2017 AND 2016

1. Nature of Activities and Summary of Significant Accounting Policies

Organization and Business

The accompanying consolidated financial statements include the accounts of Texas Heart Institute (“THI”), THI Foundation and its affiliate, Cardiopulmonary Perfusion Associates (“CPPA”), (collectively, the “Institute”).

THI is a Texas nonprofit organization founded by Dr. Denton A. Cooley in 1962 organized to reduce the devastating toll of cardiovascular disease through innovative programs in research, education, and improved patient care. Basic and clinical research is performed in all specialties of cardiovascular disease, including: cardiology, cardiovascular surgery, anesthesiology, pathology, and cardiothoracic transplantation. Education involves the training of medical residents and fellows in cardiovascular specialties as well as continuing education for medical doctors and educational information for the public.

THI Foundation’s mission is to help provide for the future financial needs of the Institute by encouraging financial support from individuals, organizations and foundations.

CPPA is a wholly-owned Texas nonprofit corporation. CPPA trains and grants post baccalaureate certificates of completion to approximately 20 students annually in the field of cardiopulmonary perfusion technology.

Basis of Accounting

The accompanying financial statements have been prepared using the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP).

Financial Statement Presentation

The Institute’s financial statements are presented in accordance with Financial Accounting Standards Board’s (FASB) Accounting Standards Codification (ASC) Topic 958-205, *Not-for-Profit Entities-Presentation of Financial Statements*. Under FASB ASC Topic 958-205, the Institute is required to report information regarding its financial position and activities according to three classes of net assets: unrestricted net assets, temporarily restricted net assets, and permanently restricted net assets. Accordingly, net assets of the Institute and changes therein are classified and reported as follows:

- Unrestricted net assets:
 1. *Net revenue from operations* which represents patient care and tuition revenue.

TEXAS HEART INSTITUTE AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

YEARS ENDED DECEMBER 31, 2017 AND 2016

2. *Grants and contracts* which represent the Institute's fulfillment of the requirements of certain government and private grants and contracts. From time to time, the Institute is awarded with federal grants and contracts through CHI St. Luke's Health-Baylor St. Luke's Medical Center ("SLMC") or the University of Texas System. The Institute records awarded grants and contracts at the award date as deferred revenues and increases unrestricted net assets when the requirements of grants and contracts are met.
 3. *Contributions from affiliates* which represent contributions (monetary and non-monetary) from SLMC.
 4. *Investment income* which represents income earned from endowment and temporarily restricted funds unless the donor has specified a restriction on the investment income.
 5. *Philanthropy* which consists of gifts and contributions from individual donors.
- Temporarily restricted net assets – These are financial resources for which donor-imposed restrictions have not been met and pledges receivable for which the ultimate purpose of the proceeds is not permanently restricted. As of December 31, 2017 and 2016, the Institute had temporarily restricted net assets of \$37,476,224 and \$25,533,529, respectively.
 - Permanently restricted net assets – These are endowment funds and pledges to establish endowment funds whose corpus is permanently restricted from expenditures. As of December 31, 2017 and 2016, the Institute had permanently restricted net assets of \$18,111,014 and \$16,598,553, respectively.

Additionally, the Institute is required under FASB ASC Topic 958-205 to present statements of activities and cash flows.

Revenue Recognition

Revenues from contributions, donations and other sources are recognized as unrestricted, temporarily restricted, or permanently restricted revenues when received or unconditionally promised by a third party. Conditional promises to give cash or other assets are not recognized until received. Interest income is recognized when earned based on passage of time.

TEXAS HEART INSTITUTE AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 2017 AND 2016

Contributions and Promises to Give

Contributions received are recorded as unrestricted, temporarily restricted, or permanently restricted support depending on the existence and/or nature of any donor restrictions. Contributions that are restricted by the donor are reported as increases in unrestricted net assets if the restrictions expire (that is, when a stipulated time restriction ends or purpose restriction is accomplished) in the reporting period in which the revenue is recognized.

All other donor-restricted contributions are reported as increases in temporarily restricted or permanently restricted net assets, depending on the nature of the restrictions. When a restriction expires, temporarily restricted net assets are reclassified to unrestricted net assets upon satisfaction of the time or purpose restrictions and reported in the statement of activities as net assets released from restrictions. When both restricted and unrestricted resources are available for use, it is the Institute's policy to use restricted resources first, then unrestricted resources as they are needed.

Contributed Services and Facilities

A number of unpaid volunteers have made significant contributions of their time and services to the Institute. The value of these contributions is not reflected in the accompanying consolidated financial statements since it is not susceptible to objective measurement or valuation.

Cash and Cash Equivalents

The Institute considers all highly liquid investments with a maturity of three months or less when purchased to be cash equivalents. For purposes of the statements of cash flows, cash and cash equivalents exclude restricted cash and cash equivalents.

Cash equivalents, consisting primarily of overnight investments, included in cash and cash equivalents at December 31, 2017 and 2016, amounted to \$1,169,017 and \$1,008,090, respectively.

Investments

Investments are measured at fair value in the consolidated statements of financial position. Investment income or loss (including realized and unrealized gains and losses on investments, interest, and dividends) is included in the change in unrestricted net assets unless the investment income is restricted by donor.

TEXAS HEART INSTITUTE AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 2017 AND 2016

Income Taxes

The Institute is exempt from federal income tax under Section 501(c)(3) of the Internal Revenue Code, except on net income derived from unrelated business activities.

At December 31, 2017 and 2016, the Institute has determined that no income taxes are due for its activities. Accordingly, no provision for income taxes has been recorded in the accompanying consolidated financial statements.

The Institute follows the guidance issued by the FASB in accounting for uncertainty in income taxes. This guidance clarifies the accounting for income taxes by prescribing the minimum recognition threshold an income tax position is required to meet before being recognized in the financial statements and applies to all income tax positions. Each income tax position is assessed using a two-step process. A determination is first made as to whether it is more likely than not that the income tax position will be sustained, based upon technical merits, upon examination by the taxing authorities. If the income tax position is expected to meet the more likely than not criteria, the benefit recorded in the financial statements equals the largest amount that is greater than 50% likely to be realized upon its ultimate settlement. The Institute did not recognize any uncertain tax positions upon adoption of the guidance and had no uncertain tax positions as of December 31, 2017 and 2016, respectively.

The income tax position taken by the Institute, for any years open under the various statutes of limitations, is that the Institute continues to be exempt from income taxes by virtue of being a nonprofit organization. Management believes this tax position meets the more-likely-than-not threshold and, accordingly, the tax benefit of this income tax position (no income tax liability) has been recognized for the years ended December 31, 2017 and 2016.

As part of the adoption of this guidance, the Institute records income tax related interest and penalties, if applicable, as a component of the provision for income tax expense. However, there were no amounts recognized relating to interest and penalties in the statement of activities for the years ended December 31, 2017 and 2016. The Federal income tax returns of the Institute for years 2014 through 2016 are still subject to examination by the Internal Revenue Service, generally for three years after they were filed.

Property and Equipment

Property and equipment is recorded at cost if purchased or at the fair market value at the date of gift if donated. Such donations are recorded as unrestricted support unless the donor has restricted the donated asset to a specific purpose. Assets donated with explicit restrictions regarding their use and contributions of cash that must be used to acquire or

TEXAS HEART INSTITUTE AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 2017 AND 2016

maintain property and equipment are recorded as restricted contributions. At December 31, 2017 and 2016, the Institute did not have any assets with donor-imposed restrictions.

The Institute follows the policy of capitalizing all expenditures for property and equipment in excess of \$5,000. Depreciation is recorded using the straight-line method based upon the estimated useful lives of the related assets, which range from 5 years for equipment to 40 years for the building. Maintenance and repairs are charged to operations when incurred. Major improvements and renewals are capitalized.

Impairment of Long-lived Assets

The Institute reviews the recoverability of its long-lived assets, such as property and equipment, when events or changes in circumstances occur that indicate the carrying value of the asset or asset group may not be recoverable. The assessment of possible impairment is based on the Institute's ability to recover the carrying value of the asset or asset group from the expected future cash flows. If these cash flows are less than the carrying value of such asset, an impairment loss is recognized for the difference between estimated fair value and carrying value. The Institute recognized no impairment loss during the years ended December 31, 2017 and 2016 related to its long-lived assets.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

New Accounting Pronouncements

In February 2016, the FASB issued Accounting Standards Update (ASU) 2016-02 – *Leases (Topic 842)*, which supersedes existing guidance on leases and amends and supersedes a number of other paragraphs throughout the FASB ASC. This update will be effective for the Institute's 2020 annual consolidated financial statements. Management has not determined the impact that adoption of this guidance will have on its consolidated financial statements.

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In August 2016, the FASB issued ASU 2016-14 – *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities*, which will eliminate the distinction between resources with permanent restrictions and those with temporary restrictions from the face of financial statements as well as improve the information presented in the financial statements and notes about a not-for-profit entity’s liquidity, financial performance, and cash flows. This update will be effective for the Institute’s 2018 annual consolidated financial statements. Management has not determined the impact that adoption of this guidance will have on its consolidated financial statements.

In August 2016, the FASB issued ASU 2016-15 – *Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments*, which clarified guidance on certain cash flow classification issues. This update will be effective for the Institute’s 2019 annual consolidated financial statements. Management has not determined the impact that adoption of this guidance will have on its consolidated financial statements.

In November 2016, the FASB issued ASU 2016-18 – *Statement of Cash Flows (Topic 230): Restricted Cash*, which requires amounts generally described as restricted cash and restricted cash equivalents be 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. This update will be effective for the Institute’s 2019 annual consolidated financial statements. Management has not determined the impact that adoption of this guidance will have on its consolidated financial statements.

In July 2017, the FASB issued ASI 2017-07, *Compensation - Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost*. The amendments in this update apply to all employers, including not-for-profit entities, that offer to their employees defined benefit pension plans, other postretirement benefit plans, and other types of benefit accounted for under Topic 715. The amendments in this update require that an employer report the service cost component in the same line item or items as other compensation costs arising from services rendered by the pertinent employees during the period. The other components of net benefit cost as defined in paragraphs 715-30-35-4 and 715-60-35-9 are required to be presented in the income statement separately from the service cost component and outside a subtotal of income from operations, if one is presented. If a separate line item or items are used to present the other components of net benefit cost, that line item or items must be appropriately described. If a separate line item or items are not used, the line item or items used in the income statement to present the other components of net benefit costs must be disclosed. This update will be effective for the Institute’s 2019 annual consolidated financial statements. Management has not determined the impact that adoption of this guidance will have on its consolidated financial statements.

TEXAS HEART INSTITUTE AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 2017 AND 2016

2. Pledges Receivable

The following table sets forth the components of pledges receivable included in the accompanying consolidated statement of financial position as of December 31, 2017:

	December 31, 2017			Total
	Pledges receivable due within one year	Pledges receivable due in one to five years	Pledges receivable due after five years	
Unrestricted pledges	\$ 1,723,001	\$ 1,705,000	\$ -	\$ 3,428,001
Temporary restricted pledges	2,092,371	2,269,822	-	4,362,193
Permanently restricted pledges	400,000	1,000,000	-	1,400,000
Less: discount on pledges receivable	-	(177,527)	-	(177,527)
Pledges receivable, net	<u>\$4,215,372</u>	<u>\$4,797,295</u>	<u>\$ -</u>	<u>\$ 9,012,667</u>

The following table sets forth the components of pledges receivable included in the accompanying consolidated statement of financial position as of December 31, 2016:

	December 31, 2016			Total
	Pledges receivable due within one year	Pledges receivable due in one to five years	Pledges receivable due after five years	
Unrestricted pledges	\$ 2,556,523	\$ 3,375,000	\$ 80,000	\$ 6,011,523
Temporary restricted pledges	1,611,028	3,437,134	-	5,048,162
Permanently restricted pledges	200,000	400,000	-	600,000
Less: discount on pledges receivable	-	(319,502)	(8,667)	(328,169)
Net pledges receivable	<u>\$4,367,551</u>	<u>\$6,892,632</u>	<u>\$ 71,333</u>	<u>\$11,331,516</u>

Pledges receivable with due dates extending beyond one year are discounted using T-bill rates for similar investments. The applicable rates for outstanding pledges receivable range from 0.8% - 1.8% and 0.4% - 2.0%, respectively, at December 31, 2017 and 2016.

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3. Property Held for Sale

In October 2014, a donor donated land valued at \$500,000 to the Institute in satisfaction of his pledge. The land was listed for sale as of December 31, 2016. The donor agreed to bear all costs and taxes associated with the land until the sale is completed. The land was sold during the current year for \$500,000, net of all charges.

4. Investments

Investments purchased with an original maturity of one year or more or otherwise not expected to be utilized within one year are considered to be long-term investments. Long-term investments consist of the following:

	December 31, 2017	December 31, 2016
United States treasury securities	\$ 1,988,730	\$ 3,672,218
Corporate debt securities	8,871,267	10,199,337
Equity securities	63,935,612	53,570,049
Hedge funds	3,836,986	-
Tangible assets	361,812	-
	<u>\$ 78,994,407</u>	<u>\$ 67,441,604</u>

Investment returns excluding earnings on cash and cash equivalents consist of the following:

	December 31, 2017	December 31, 2016
Interest and dividends	\$ 2,326,082	\$ 2,099,288
Net unrealized gains on investments	10,094,179	2,291,456
Net realized gains on sales of investments	96,148	93,197
	<u>\$ 12,516,409</u>	<u>\$ 4,483,941</u>

Investment revenues are reported net of related investment expenses in the consolidated statement of activities. The amount of expenses netted with revenues was \$333,342 and \$294,265 for the years ended December 31, 2017 and 2016, respectively.

TEXAS HEART INSTITUTE AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 2017 AND 2016

5. Fair Value Measurements

U.S. GAAP establishes a fair value hierarchy which classifies fair value measurements from level 1 through level 3 based upon the inputs used to measure fair value, as follows:

Level 1 — Quoted prices (unadjusted) are available in active markets for identical assets or liabilities as of the reporting date. Active markets are those in which transactions for the asset or liability occur in sufficient frequency and volume to provide pricing information on an ongoing basis.

Level 2 — Pricing inputs include quoted prices for similar assets and liabilities in active markets, and inputs other than quoted prices that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument.

Level 3 — Pricing inputs include significant inputs that are generally less observable or from unobservable sources. These inputs may be used with internally developed methodologies that result in management’s best estimate of fair value.

The following tables present the Institute’s investments that were accounted for at fair value on a recurring basis as of December 31, 2017 and 2016, by level within the fair value hierarchy. Investments are classified in their entirety based on the lowest level of input that is significant to the fair value measurement. The Institute’s assessment of significance for a particular input to the fair value measurement requires judgment, and may affect the valuation of fair value assets and liabilities within the fair value hierarchy levels.

	Fair Value at December 31, 2017			
	Level 1	Level 2	Level 3	Total
Cash and cash equivalents	\$ 986,969	\$ -	\$ -	\$ 986,969
Equities	63,393,669	-	5,070,994	68,464,663
Corporate and government bonds	7,246,022	3,283,722	-	10,529,744
	<u>\$ 71,626,660</u>	<u>\$ 3,283,722</u>	<u>\$ 5,070,994</u>	<u>\$ 79,981,376</u>
	Fair Value at December 31, 2016			
	Level 1	Level 2	Level 3	Total
Cash and cash equivalents	\$ 917,786	\$ -	\$ -	\$ 917,786
Equities	48,570,049	-	5,000,000	53,570,049
Corporate and government bonds	13,871,555	-	-	13,871,555
	<u>\$ 63,359,390</u>	<u>\$ -</u>	<u>\$ 5,000,000</u>	<u>\$ 68,359,390</u>

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Recurring Level 3 measurements consists of the Institute's \$5 million private equity investment in the preferred stock of Miromatrix Medical, Inc. (see Note 12) purchased in May 2014. The fair value of this investment is measured using a cost approach considering the selling price of the preferred stock, which was valued at \$7.50 per share as of December 31, 2017.

Management determines the fair value measurements valuation policies and procedures, including those for Level 3 recurring and nonrecurring measurements. At least annually, management determines if the current valuation techniques used in Level 3 fair value measurements are still appropriate, and evaluates and adjusts the unobservable inputs used in the Level 3 fair value measurements based on current market conditions and third-party information.

The table below presents information about recurring Level 3 fair value measurements that use significant unobservable inputs:

	Level 3 Fair Value Measurements
Balance as of January 1, 2017	\$ 5,000,000
Purchase of private equity investment	-
Balance as of December 31, 2017	\$ 5,000,000

Gains and losses (realized and unrealized) included in unrestricted net assets are reported in investment income for the years ended December 31, 2017 and 2016 as follows:

	Investment Income, net	
	2017	2016
Total net gains included in unrestricted net assets for the year	\$ 96,148	\$ 25,084
Net change in unrealized gains relating to assets held at year end	\$ 6,331,756	\$ 1,694,451

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6. Property and Equipment

Property and equipment consists of the following:

	December 31,	
	2017	2016
The Denton A. Cooley Building	\$ 46,155,436	\$ 46,155,436
Leasehold improvements	425,096	425,095
Furniture, fixtures and equipment	15,878,578	13,880,504
Artwork & valuables	89,840	89,840
Software	351,877	351,878
Equipment under capital lease	291,078	2,083,307
Total costs of assets placed in service	63,191,905	62,986,060
Less: Accumulated depreciation and amortization	(36,360,438)	(34,488,045)
Property & equipment, net	<u>\$ 26,831,467</u>	<u>\$ 28,498,015</u>

Depreciation and amortization expense for the years ended December 31, 2017 and 2016 was \$2,302,373 and \$2,965,682, respectively.

7. Relationship with Catholic Health Initiatives/CHI St. Luke’s Health Baylor St. Luke’s Medical Center

The Institute entered into a Definitive Agreement, effective as of December 23, 2013, with Catholic Health Initiatives (“CHI”), a Colorado nonprofit corporation. CHI is a Catholic health care system dedicated to transforming health care delivery and building healthier communities and is the sole corporate member of St. Luke’s Health System Corporation, a Texas nonprofit corporation (“SLHS”), which comprises an expansive healthcare network throughout the Houston-Baytown-Huntsville, Texas area that includes SLMC. The purpose of this agreement was to collaborate for the purpose of furthering the development and success of the Institute’s mission to reduce the devastating toll of cardiovascular disease through innovative programs in research, education, and improved patient care, and CHI’s commitment to improving the health of the people in communities it serves. The agreement governs the contributions of financial support by CHI to the Institute. The Institute records support from CHI as contributions from affiliate.

Upon the finalization of the affiliation agreement with CHI, the Institute received a \$50 million conditional promise from a third-party donor to be deployed by CHI for the support and benefit of the Institute. Payment is contingent upon the Institute remaining affiliated with SLHS over the initial term of the affiliation agreement.

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The Institute and SLMC jointly own the Denton A. Cooley Building, an approximately 310,000-square-foot cardiovascular center opened in 2002. The Institute currently occupies approximately 43% of the building, including the space leased to the University of Texas System (see Note 11).

Support from SLMC for cash contributions and donated services are as follows:

	<u>Year Ended December 31,</u>	
	<u>2017</u>	<u>2016</u>
Cash contributions	<u>\$ 12,381,462</u>	<u>\$ 12,128,251</u>
	<u>\$ 12,381,462</u>	<u>\$ 12,128,251</u>

SLMC pays facility operations expenses on behalf of the Institute and the Institute reimburses SLMC quarterly for expenses paid on its behalf. As of December 31, 2017 and 2016, \$617,428 and \$2,779,217, respectively, were outstanding and due to SLMC for expenses paid on behalf of the Institute.

The Institute incurred expenses of \$47,000 for the years ended December 31, 2017 and 2016 for donor development and database management services provided by the CHI National Foundation based on an agreement effective September 1, 2014 through September 1, 2017.

The Institute leases space from SLMC for the purposes of furthering its mission. The lease agreement is effective January 1, 2014 through December 31, 2018. Rent expense for the years ended December 31, 2017 and 2016 amounted to \$890,330 and \$816,136, respectively.

8. Endowments

FASB ASC Topic 958-205, *Endowments of Not-for-Profit Organizations: Net Asset Classification of Funds Subject to an Enacted Version of the Uniform Prudent Management of Institutional Funds Act, and Enhanced Disclosures for All Endowment Funds*, provides guidance on the net asset classification of donor-restricted endowment funds for not-for-profit organizations that are subject to Uniform Prudent Management of Investment Funds Act (“UPMIFA”), a version of which was enacted by the State of Texas on September 1, 2007; and improves disclosures about an organization’s endowment funds (both donor restricted funds and funds functioning as an endowment), regardless of whether it is subject to UPMIFA. The Institute adopted this guidance beginning the year ended December 31, 2008.

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In addition, FASB ASC Topic 958-205 addresses how UPMIFA’s elimination of the historic dollar value threshold — the amount below which a not-for-profit could not spend under regulations prior to the adoption of UPMIFA — affects net asset classification. FASB ASC Topic 958-205 also requires an organization to classify a portion of a donor-restricted endowment fund (other than a term endowment) as permanently restricted net assets. That portion is equal to the amount of the fund that: (1) must be retained permanently, in accordance with explicit donor stipulations, or (2) that, in the absence of such stipulations, the not-for-profit’s governing board determines must be retained permanently under the relevant law.

The Institute has determined that the majority of the Institute’s permanently restricted net assets meet the definition of endowment funds under UPMIFA. The Institute’s endowments consist of funds established for a variety of purposes.

Balances of the funds included in permanently restricted net assets were as follows:

	December 31,	
	2017	2016
Endowment funds:		
Use of income is unrestricted	\$ 3,557,036	\$ 2,587,353
Use of income is restricted for:		
Stem Cell Research	5,597,387	5,597,387
Annual Cardio Symposium	229,650	229,650
Artificial Heart Research and Development	3,656,987	3,635,021
Cardiovascular surgical research with a focus on children	2,000,000	2,000,000
Cardiology Research	494,591	494,591
Increasing Huffington Endowment	2,575,363	2,054,551
	14,553,978	14,011,200
Total endowment funds	\$ 18,111,014	\$ 16,598,553

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 Institute’s Board has interpreted UPMIFA as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the Institute classifies as permanently restricted net assets the original value of gifts donated to the permanent endowment, the original value of subsequent gifts to the permanent endowment,

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and accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Institute in a manner consistent with the standard of prudence prescribed by UPMIFA. In accordance with UPMIFA, the Institute considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds: the duration and preservation of the fund, the purposes of the Institute and the donor-restricted endowment fund, general economic conditions, the possible effect of inflation and deflation, the expected total return from income and the appreciation of investments, other resources of the Institute, and the investment policies of the Institute.

Endowment Net Asset Composition by Type of Fund as of December 31, 2017:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Donor-restricted endowment funds	\$ -	\$ -	\$ 18,111,014	\$ 18,111,014
	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 18,111,014</u>	<u>\$ 18,111,014</u>
Changes in Endowment Net Assets for the year ended December 31, 2017:				
Endowment net assets, January 1, 2017	\$ -	\$ -	\$ 16,598,553	\$ 16,598,553
Investment return:				
Investment income	306,616	751,720	39,148	1,097,484
Net realized and unrealized appreciation	-	3,280,748	481,675	3,762,423
Total investment return	<u>306,616</u>	<u>4,032,468</u>	<u>520,823</u>	<u>4,859,907</u>
Contributions	-	-	991,638	991,638
Appropriation of endowment assets for expenditures	<u>(306,616)</u>	<u>(4,032,468)</u>	<u>-</u>	<u>(4,339,084)</u>
Endowment net assets, December 31, 2017	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 18,111,014</u>	<u>\$ 18,111,014</u>

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Endowment Net Asset Composition by Type of Fund as of December 31, 2016:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Donor-restricted endowment funds	\$ -	\$ -	\$ 16,598,553	\$ 16,598,553
	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 16,598,553</u>	<u>\$ 16,598,553</u>
Changes in Endowment Net Assets for the year ended December 31, 2016:				
Endowment net assets, January 1, 2016	\$ -	\$ -	\$ 16,393,260	\$ 16,393,260
Investment return:				
Investment income	258,484	740,015	37,935	1,036,434
Net realized and unrealized appreciation	-	492,601	104,404	597,005
Total investment return	<u>258,484</u>	<u>1,232,616</u>	<u>142,339</u>	<u>1,633,439</u>
Contributions	-	-	62,954	62,954
Appropriation of endowment assets for expenditures	<u>(258,484)</u>	<u>(1,232,616)</u>	<u>-</u>	<u>(1,491,100)</u>
Endowment net assets, December 31, 2016	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 16,598,553</u>	<u>\$ 16,598,553</u>

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level that the donor or UPMIFA requires the Institute to retain as a fund of perpetual duration. Such shortfalls are recorded as decreases in unrestricted net assets. There were no deficiencies of this nature reported in unrestricted net assets as of December 31, 2017 and 2016.

The Institute has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowments while seeking to maintain the purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the Institute must hold in perpetuity or for a donor-specified period.

To satisfy its long term objective, the Institute targets a diversified asset allocation that places a greater emphasis on equity-based investments to achieve its long-term objectives within prudent risk constraints.

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9. Pension Plan

The Institute's retirement plan (the "Plan") is a noncontributory cash balance defined benefit pension plan covering substantially all employees of the Institute. The Institute makes annual contributions to the Plan to meet the minimum funding requirements of the Employee Retirement Income Security Act of 1974.

The Plan obtained its latest determination letter on October 13, 2011, in which the Internal Revenue Service (IRS) stated that the Plan and related trust, as then designed, were in compliance with the applicable requirements of the Internal Revenue Code (the Code) and, therefore, exempt from taxation. Effective September 30, 2012, the Plan was amended to freeze the grandfathered benefit accrual formula. However, Plan management believes that the Plan and related trust are currently designed and being operated in compliance with the applicable requirements of the Code.

The assets of the Plan are not segregated for plan valuation or payment of benefits, and should not be construed as being segregated among the subsidiaries. The accounting and valuation for the Plan are determined by prescribed accounting and actuarial methods that consider a number of assumptions and estimates. The selection of appropriate assumptions and estimates is significant due to the long time period over which benefits will be considered. The most sensitive assumptions in using actuarial methods to value the Institute's pension obligations and determine the related expense amounts are discount rates, expected long-term investment returns on plan assets and future salary increases. Additionally, other assumptions made with respect to retirement ages, mortality and employee turnover affect the valuations. Actual results and future changes in these assumptions could result in future costs significantly different than those recorded in the results of operations.

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The following table sets forth the Plan's funded status, factors assumed, and amounts as of the measurement dates of December 31, 2017 and 2016. These amounts materially agree with the amounts recognized in the accompanying consolidated financial statements as follows:

	December 31,	
	2017	2016
Changes in projected benefit obligation:		
Projected benefit obligation, beginning of year	\$ 11,845,944	\$ 11,299,150
Service cost	55,000	67,000
Interest cost on projected benefit obligation	434,385	451,483
Actuarial loss/(gain)	734,215	560,656
Benefits paid from Plan assets	(271,505)	(477,060)
Administrative expenses paid	(58,431)	(55,285)
Plan amendments	-	-
Plan curtailments	-	-
Plan settlements	(1,572,006)	-
Projected benefit obligation, at end of year	11,167,602	11,845,944
Changes in Plan assets:		
Fair value of Plan assets, beginning	11,076,284	10,527,183
Actual return on Plan assets	1,548,673	931,446
Employer contributions	150,000	150,000
Benefits paid	(271,505)	(477,060)
Administrative expenses paid	(58,431)	(55,285)
Plan settlements	(1,572,006)	-
Fair value of Plan assets at end of year	10,873,015	11,076,284
Unfunded status	\$ 294,587	\$ 769,660
Amounts recognized in the consolidated statement financial position:		
Pension obligation	(294,587)	(769,660)
Cumulative adjustments to unrestricted net assets	(3,001,880)	(3,693,225)
Amounts recognized in the consolidated statement of activities:		
Pension costs included in personnel expenses	366,272	172,812

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The accumulated benefit obligation was \$11,167,602 and \$11,845,944 at December 31, 2017 and 2016, respectively.

	December 31,	
	2017	2016
Service cost	\$ 55,000	\$ 67,000
Interest cost on projected benefit obligation	434,385	451,483
Expected return on Plan assets	(611,857)	(617,565)
Amortization of prior service cost	-	-
Recognized net actuarial loss	67,728	271,894
Curtailment gain	-	-
Settlement loss	421,016	-
Net periodic pension cost	<u>\$ 366,272</u>	<u>\$ 172,812</u>

The estimated net loss that will be amortized from net assets into net periodic benefit cost over the next fiscal year will be based on the average expected future service of Plan participants. There is no estimated prior service credit that will be amortized from net assets into net periodic benefit cost over the next fiscal year.

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Other changes in Plan assets and benefit obligations recognized as changes in unrestricted net assets:

	December 31,	
	2017	2016
Net (loss) gain	\$ (202,601)	\$ 246,775
Prior service cost	-	-
Amortization of prior service cost	-	-
Amortization of net actuarial loss	(488,744)	(271,894)
	\$ (691,345)	\$ (25,119)

Weighted-average assumptions used to determine benefit obligations for the Plan measurement date:

Discount rate	3.62%	4.13%
Rate of compensation return	N/A	N/A

Weighted-average assumptions used to determine net periodic benefit cost for the Plan measurement date:

Discount rate	4.13%	4.41%
Expected return on Plan assets	6.25%	6.50%
Rate of compensation return	N/A	N/A

The Plan's expected return on assets is derived from a review of the Plan's asset allocation strategy, anticipated long-term performance of individual asset classes, risks and correlations of asset classes, and general economic conditions of the investment marketplace.

The assets of the Plan by weighted-average asset allocation categories are as set forth in the following table:

Asset category:		
Mutual funds	12%	21%
Common collective trusts	88%	79%
Total	100.00%	100.00%

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The Plan's general investment objective is to achieve attractive long-term total return from income and growth of capital over a full market cycle, with a low-to-moderate level of risk, through investments in a well-diversified portfolio of equity, fixed income, and short-term liquid securities.

Effective October 1, 2008, the Plan adopted the FASB standard on fair value measurements and disclosures for its financial assets and liabilities carried at fair value on a recurring basis in the financial statements. As defined by this standard, 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 (exit price). The transaction is based on a hypothetical transaction in the principal or most advantageous market considered from the perspective of the market participant that holds the asset or owes the liability.

The Plan utilizes market data or assumptions that market participants who are independent, knowledgeable, and willing and able to transact would use in pricing the asset or liability, including assumptions about risk and the risks inherent in the inputs to the valuation technique. These inputs can be readily observable, market corroborated, or generally unobservable. The Plan attempts to utilize valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs. The Plan is able to classify fair value balances based on the observability of those inputs. The FASB standard on fair value measurement and disclosure establishes a formal fair value hierarchy based on the inputs used to measure fair value. The hierarchy gives the highest priority to level 1 measurements and the lowest priority to level 3 measurements, and accordingly, level 1 measurement should be used whenever possible. The three levels are defined as follows:

- Level 1 - Valuations utilizing quoted, unadjusted prices for identical assets or liabilities in active markets that the Plan has the ability to access. This is the most reliable evidence of fair value and does not require a significant degree of judgment.
- Level 2 - Valuations utilizing quoted prices in markets that are not considered to be active or financial instruments for which all significant inputs are observable, either directly or indirectly for substantially the full term of the asset or liability.
- Level 3 - Valuations utilizing significant, unobservable inputs. This provides the least objective evidence of fair value and requires a significant degree of judgment. Inputs may be used with internally developed methodologies and should reflect an entity's assumptions using the best information available about the assumptions that market participants would use in pricing an asset or liability.

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Following are the valuation methodologies used for investments measured at fair value as presented in the table below. There have been no changes in the methodologies used at December 31, 2017 and 2016.

Mutual Funds: Valued at the closing price reported on the active market in which the individual securities are traded.

Common/collective trusts: Valued using net asset value (NAV), as determined by the issuer, based on the fair value of the underlying assets.

The following fair value hierarchy table presents information about the Plan's investments measured at fair value on a recurring basis:

	Assets at Fair Value as of December 31, 2017			
	Level 1	Level 2	Level 3	Total
Mutual funds:				
Income funds	\$ 642,545	\$ -	\$ -	\$ 642,545
International funds	438,595	-	-	438,595
Commodity funds	181,315	-	-	181,315
Common collective trusts:				
International trusts	-	1,689,556	-	1,689,556
Index trusts	-	2,877,385	-	2,877,385
Growth trusts	-	377,131	-	377,131
Bond trusts	-	4,664,186	-	4,664,186
Total investments measured at fair value	<u>\$ 1,262,455</u>	<u>\$ 9,608,258</u>	<u>\$ -</u>	<u>\$ 10,870,713</u>

	Assets at Fair Value as of December 31, 2016			
	Level 1	Level 2	Level 3	Total
Mutual funds:				
Income funds	\$ 1,431,196	\$ -	\$ -	\$ 1,431,196
International funds	529,972	-	-	529,972
Commodity funds	331,065	-	-	331,065
Common collective trusts:				
International trusts	-	3,032,164	-	3,032,164
Index trusts	-	3,696,274	-	3,696,274
Growth trusts	-	642,408	-	642,408
Bond trusts	-	1,413,205	-	1,413,205
Total investments measured at fair value	<u>\$ 2,292,233</u>	<u>\$ 8,784,051</u>	<u>\$ -</u>	<u>\$ 11,076,284</u>

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Investments in Certain Entities that Calculate NAV Per Share

Under the amended guidance of FASB ASU No. 2009-12, *Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)* (ASU 2009-12), entities are permitted, as a practical expedient, to estimate the fair value of investments within its scope using the NAV per share of the investment as of the reporting entities' measurement dates. The amended guidance also requires additional disclosures to better enable users of the financial statements to understand the nature and risks of the reporting entity's investments that fall under these rules.

In accordance with FASB ASU 2009-12, the Plan expanded its disclosure to include the category, fair value, redemption frequency, and redemption notice period for those assets whose fair value is estimated using the NAV per share or its equivalent for which the fair value is not readily determinable as of December 31, 2017 and 2016. For the Plan, such assets include investments in common collective trust.

The following tables for December 31, 2017 and 2016, sets forth a summary of the Plan's investments with a reported NAV:

	Fair Values Estimated Using NAV per Share					
	2017	2016	Unfunded Commitments	Redemption Frequency	Other Redemption Restrictions	Redemption Notice Period
Common/collective trusts						
International trusts ¹	\$ 1,689,556	\$ 3,032,164	None	Daily	None	No
Index trusts ²	2,877,385	3,696,274	None	Daily	None	No
Bond trusts ³	377,131	642,408	None	Daily	None	No
Growth trusts ⁴	4,664,186	1,413,205	None	Daily	None	No
	<u>\$ 9,608,258</u>	<u>\$ 8,784,051</u>				

¹ Represents pooled funds invested primarily to provide investment results that exceed the overall performance of Morgan Stanley Europe, Australasia, and Far East (MSCI EAFE) Index with net dividends.

² Represents pooled funds invested in the mid cap segment of the U.S. equity market and selective weighting of the issues in the S&P 500 Index with security and sector guidelines to ensure similar risk characteristics as the underlying S&P 500.

³ Represents pooled funds invested primarily to provide investment results that approximate the overall performance of the Barclay's Capital Aggregate Bond Index. This fund may hold units of participation in any fixed income collective fund established and maintained by the Trustee or any of its affiliates.

⁴ Represents pooled funds invested primarily in high-grade money market instruments with short maturities and investments with diversified exposure representative of the small cap segment of the U.S. equity market.

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The Institute expects to contribute \$150,000 to the Plan in 2017.

The following benefit payments, which reflect expected future service, as appropriate, are expected to be paid as follows:

Year Ending December 31,	Amount
2018	1,358,661
2019	938,024
2020	878,514
2021	798,220
2022 - 2026	3,411,355
	\$ 7,384,774

Defined Contribution Plan

The Institute offers a tax-deferred savings plan (the “TSA Plan”), designed in conformity with Section 403(b) of the Internal Revenue Code, covering substantially all of its employees. The TSA Plan provides for elective contributions by employees up to the maximum limit allowed by the federal tax regulations in the United States of America. Under the term of the TSA Plan, the Institute matches 50% of employees’ contributions for amounts contributed by employees up to a maximum of 3% of employees’ wages. Employees are fully vested in their own contributions and become 100% vested in the employer’s matching contributions after completing three years of service. Vested service is based on 1,000 hours or more of paid service during each year. During the years ended December 31, 2017 and 2016, the Institute recognized expenses related to the TSA Plan of \$436,477 and \$400,627, respectively.

10. Functional Classification of Expenses

The Institute and its wholly-owned subsidiaries perform research and educational activities related to the treatment of cardiovascular diseases and provide patient services. The following table sets forth the significant components of the Institute’s expenditures by major classification:

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	Year Ended December 31,	
	2017	2016
Research	\$ 17,032,751	\$ 18,678,689
Education	3,069,285	2,465,381
Patient services	396,414	306,951
Program expenditures	<u>20,498,450</u>	<u>21,451,021</u>
Fund-raising expenditures	<u>1,404,595</u>	<u>1,086,922</u>
General facility and maintenance costs, building depreciation and SLMC's support service	6,570,471	7,816,302
Other general and administrative	<u>6,246,730</u>	<u>5,542,713</u>
General and administrative expenditures	<u>12,817,201</u>	<u>13,359,015</u>
Total expenditures	<u>\$ 34,720,246</u>	<u>\$ 35,896,958</u>

11. Capital Lease Transactions with University of Texas System

In October 2002, the Institute and the University of Texas System ("UTS") entered into a lease transaction whereby the Institute leased the shell of the 9th floor of the Denton A. Cooley Building to UTS for an initial term of ten years through August 2012. UTS indicated its intention not to renew after the initial term in August 2012.

In January 2013, the Institute exercised its purchase option per the Sublease Agreement dated October 5, 2012 to acquire the tenant's equipment in the 9th floor space of the Denton Cooley Building from UTS for use in its research activities at the cost of \$6 million. The sum of \$2 million was agreed to be paid during year 2013 and \$1 million each year from years 2014 through 2017. As of December 31, 2017 and 2016, the sum of \$0 and \$1 million, respectively, was outstanding. The outstanding balance is included in other liabilities in the consolidated statements of financial position.

12. Miromatrix Medical Inc. Preferred Stock

During 2013, the Institute entered into a Subscription and Letter of Investment Intent ("Subscription Agreement") dated October 8, 2013 with Miromatrix Medical Inc. ("Miromatrix") for the offer to purchase 666,667 shares of preferred stock "Series B" at a purchase price of \$7.50 per share for a total of \$5 million. The Institute paid \$1 million upon execution of the Subscription Agreement and also executed a note payable agreement for the

TEXAS HEART INSTITUTE AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 2017 AND 2016

payment of the \$4 million balance. The Institute paid the balance in full in March 2014 and was issued 666,667 shares of preferred stock of Miromatrix at a per share price of \$7.50 in May 2014. At December 31, 2017 and 2016, the preferred stock is valued at cost, which the Institute has estimated to be the fair value of the investment.

Pursuant to a Sub-License agreement effective October 1, 2013, by and between Miromatrix and the Institute, both parties agreed to sub-license certain patents and patent applications as described in the agreement. In line with the Sub-License agreement, Miromatrix shall pay to the Institute a royalty of 5% of the net sales price from commercial sales of products by Miromatrix or its affiliates, while the Institute shall pay to Miromatrix, a royalty of 10% of the net sales price from commercial sales of products by the Institute or its affiliates or sub-licensees.

13. Related Party Transactions

A trustee of the Institute is a partner in a law firm that provides legal services to the Institute. Fees paid by the Institute to this firm totaled \$442,591 and \$357,432 for the years ended December 31, 2017 and 2016, respectively.

Certain members of the board of trustees of the Institute made total cash contributions of \$0 and \$45,100 in support of the Institute in 2017 and 2016, respectively.

14. Commitments and Contingencies

Litigation

From time to time, the Institute is a defendant in legal proceedings related to its operations. In the best judgment of the Institute's management, and after consultation with its legal counsel, the outcome of any present legal proceedings will not have a material adverse effect on the accompanying financial statements.

Government Grants

Costs charged to the federal government under cost-reimbursement grants and contracts are subject to government audit. Therefore, all such costs are subject to adjustment. Management believes that adjustments, if any, would not have a significant effect on the Institute's financial statements.

TEXAS HEART INSTITUTE AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 2017 AND 2016

Lease Obligations

The Institute leases space under non-cancelable operating and capital lease agreements that expire at different times through November 2019. Approximate future minimum annual rental payments under the noncancelable operating and capital lease agreements are as follows:

Year Ending December 31,	Operating	Capital
2018	1,171,752	74,832
2019	230,855	-
Total minimum lease payments	\$ 1,402,607	\$ 74,832
	Less amounts representing interest	(1,050)
	Present value of net minimum lease payments	\$ 73,782

The current portion of the capital lease obligation is included in the other current liabilities in the consolidated statements of financial position. Office rent expense for the years ended December 31, 2017 and 2016 amounted to \$945,748 and \$902,755, respectively. Office equipment rent expense for the years ended December 31, 2017 and 2016 amounted to \$278,709 and \$216,162, respectively.

Employment Agreement

The Institute entered into an agreement for a Collaborative Center for Cell and Organ Biotechnology effective March 1, 2012 with University of Houston (UH) to expand the activities of the Regenerative Medicine Research Laboratories (RMRL) with the goal of researching, developing, and commercializing innovative technologies for improved detection, treatment, and prevention of cardiovascular and other diseases.

In addition, the Institute engaged the services of a research professional to lead its RMRL. In accordance with the employment agreement effective March 1, 2012 through December 31, 2016, the Institute paid an annual base salary of not less than \$450,000 during each of the first and second contract years, and not less than \$500,000 during each of the third, fourth and fifth contract years. These amounts include the annual amount of \$100,000 the Institute received from UH pursuant to the agreement for professional services, and any renegotiated compensation that the Institute may have received pursuant to the agreement for professional services. Of the \$8 million of support associated with the research activities, the Institute was committed to paying not less than \$1 million per year in years 2013 through 2016. The Institute paid a total salaries of \$498,704 to the research professional for the year 2017, and both parties are currently negotiating an amendment to the agreement.

TEXAS HEART INSTITUTE AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
YEARS ENDED DECEMBER 31, 2017 AND 2016

Future Funding

The Institute's ability to continue its activities at current levels is dependent on achieving adequate levels of external research funding and philanthropy.

15. Concentrations

The Institute is subject to geographic and donor concentrations. Because of the nature of its non-profit purpose, its contributors are located primarily in the Houston metropolitan area. In addition, due to the Institute's purpose, it relies heavily on contributions from donors and its affiliates within the medical fields.

Approximately 31% and 30% of the Institute's revenue, excluding non-cash support, at December 31, 2017 and 2016, respectively, was derived from cash contributions received as a result of the relationship with CHI and SLMC as described at Note 7.

Financial instruments that potentially subject the Institute to credit risk consist of cash and cash equivalents, investments and pledges receivable. The Institute's cash and cash equivalents are held by major financial institutions.

The Federal Deposit Insurance Corporation (FDIC) insures all of a depositor's accounts up to \$250,000 per bank. At December 31, 2017, the Institute had a total of \$2,901,607 in various banks, of which \$2,401,607 exceeded the FDIC insured amounts, and was not otherwise insured. At December 31, 2016, the Institute had a total of \$2,252,011 in various banks, of which \$1,752,011 exceeded the FDIC insured amounts, and was not otherwise insured.

The Institute's investments are kept by accredited global investment firms. Pledges receivable are from many different donors and organizations. The Institute reviews the collectability of pledges receivable periodically.

16. Subsequent Events

The Institute has evaluated subsequent events through August 3, 2018; the date consolidated financial statements were available to be issued. No changes were made, or necessary to be made, to the consolidated financial statements, as a result of this evaluation.

**Report in Accordance with
*Government Auditing Standards***



**INDEPENDENT AUDITOR’S REPORT 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***

To the Board of Trustees of
Texas Heart Institute

We have audited, in accordance with the auditing standards generally accepted in the United States of America 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 Heart Institute (the “Institute”), which comprise the consolidated statements of financial position as of December 31, 2017 and 2016, and the related consolidated statements of activities and cash flows for the years then ended, and the related notes to the consolidated financial statements, and have issued our report thereon dated August 3, 2018.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the 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 the Institute’s internal control. Accordingly, we do not express an opinion on the effectiveness of the 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 a 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 and therefore, material weaknesses or significant deficiencies may exist that were not identified. We did not identify any deficiencies in internal control over financial reporting.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Institute's consolidated financial statements are free from 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 Institute'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 Institute's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.



Houston, Texas
August 3, 2018

TEXAS HEART INSTITUTE

**SCHEDULE OF CURRENT YEAR AUDIT FINDING
YEAR ENDED DECEMBER 31, 2017**

FINDINGS - CONSOLIDATED FINANCIAL STATEMENT AUDIT

This section identifies the significant deficiencies, material weaknesses, and instances of fraud, illegal acts, violations of provisions of contracts and grant agreements, and abuse related to the financial statements for which *Government Auditing Standards* require reporting under 2 CFR Section 200.515(d)(2).

No findings were noted.

TEXAS HEART INSTITUTE

SCHEDULE OF PRIOR YEAR AUDIT FINDING YEAR ENDED DECEMBER 31, 2017

Finding No. 2016–001: Material Weakness in Internal Control Over Financial Reporting

Condition:

During the current year audit, we identified several significant misstatements in the general ledger resulting from the following:

- Prior year audit and client proposed adjusting entries were not posted in the general ledger.
- Reconciliation of accounts payable, payroll and benefits accruals, and philanthropy receivables general ledger accounts were not completed in a timely manner.
- Bank reconciliations were not completed in a timely manner.

Recommendations:

We recommend the Institute establish timely monthly and year-end general ledger closing and review processes, including reconciliation of accrual and cash accounts and recognition of adjusting entries resulting from the annual audit. In addition, we recommend the Institute hire a management-level employee in the accounting department to segregate certain accounting process including the processing of cash disbursements and receipts, reconciliation of accounts, and recording of journal entries.

Current Status:

Resolved.

TEXAS HEART INSTITUTE
(A Texas Nonprofit Organization)

Single Audit Report

Year Ended December 31, 2017

TEXAS HEART INSTITUTE
(A Texas Nonprofit Organization)

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**INDEPENDENT AUDITOR’S REPORT ON COMPLIANCE FOR
EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER
COMPLIANCE REQUIRED BY THE UNIFORM GUIDANCE, AND ON THE
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS ISSUED IN A
SINGLE AUDIT**

To the Board of Trustees of
Texas Heart Institute

Report on Compliance for Each Major Federal Program

We have audited Texas Heart Institute’s (the “Institute”) 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 each of the Institute’s major federal programs for the year ended December 31, 2017. The Institute’s major federal programs are 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 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 each of the Institute’s major federal programs 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 of America; 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 the 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 each major federal program. However, our audit does not provide a legal determination of the Institute’s compliance.

Opinion on Each Major Federal Program

In our opinion, the Institute complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended December 31, 2017.

Report on Internal Control Over Compliance

Management of the 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 the Institute's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each 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 the 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 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. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Report on the Schedule of Expenditures of Federal Awards

We have audited the consolidated financial statements of the Institute as of and for the year ended December 31, 2017, and have issued our report thereon dated August 3, 2018, which contained an unmodified opinion on those consolidated financial statements. Our audits were 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 of America. 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.

The purpose of our 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.



Houston, Texas
August 3, 2018

TEXAS HEART INSTITUTE

(A Texas Nonprofit Organization)

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS YEAR ENDED DECEMBER 31, 2017

Program Title	Federal CFDA #	Contract #	Federal Expenditures
Research and Development Cluster:			
National Aeronautics and Space Administration:			
Direct Agency Funded Programs:			
Space Operations	43.007	NNX14AB55G	\$ 13,245
Total National Aeronautics and Space Administration			<u>13,245</u>
U.S. Department of Health and Human Services			
Direct Agency Funded Programs:			
National Institute of Health: National Heart, Lung and Blood Institute:			
Cardiovascular Diseases Research	93.837	4UM1HL087365-10	735,076
Cardiovascular Diseases Research	93.837	3UM1HL0837365-10S1	87,386
Cardiovascular Diseases Research	93.837	1R01HL127717-01A1	719,406
Total Direct Agency Funded Programs			<u>1,541,868</u>
Passed-Through Programs:			
Passed-through University of Texas Health Science Center at Houston:			
Cardiovascular Diseases Research	93.837	001624F	64,779
Cardiovascular Diseases Research	93.837	0011624J	203,416
Passed-through 7 Hills Pharma, LLC:			
Cardiovascular Diseases Research	93.837	1R1R41HL129612-01A1	103,559
Cancer Treatment Research	93.395	1R41CA203456-01A1	21,491
Passed-through Icahn School of Medicine at Mount Sinai:			
Cardiovascular Diseases Research	93.837	02555-3108-4609	110,194
Total Passed-Through Programs			<u>503,439</u>
Total U.S. Department of Health and Human Services			<u>2,045,307</u>
Total Research and Development Cluster			<u>2,058,552</u>
Total Federal Awards			<u>\$ 2,058,552</u>

TEXAS HEART INSTITUTE

(A Texas Nonprofit Organization)

NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS YEAR ENDED DECEMBER 31, 2017

1. BASIS OF PRESENTATION

The accompanying Schedule of Expenditures of Federal Awards (the “Schedule”) includes federal grant activities of the Texas Heart Institute (the “Institute”) under programs of the federal government for the year ended December 31, 2017. The information in the Schedule is presented in accordance with the 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). Because the Schedule presents only a selected portion of the operations of the Institute, it is not intended to and does not present the financial position, changes in net assets, or cash flows of the Institute.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Expenditures reported on the Schedule are presented on the accrual basis of accounting. Such expenditures are recognized following the cost principles contained in Subpart E of the Uniform Guidance, wherein certain types of expenditures are not allowable or are limited as to reimbursement.

3. RELATIONSHIP TO FINANCIAL REPORT SUBMITTED TO GRANTOR AGENCIES

Amounts reflected in the financial reports submitted to grantor agencies and the Schedule may differ due to the following reasons:

- The Institute’s fiscal year end may differ from the programs’ year ends.
- Accruals recognized in the Schedule, because of year-end procedures, may not be reported in the programs’ financial reports until the next program reporting period.
- Capitalized property and equipment purchases and the resulting depreciation and amortization charges recognized in the Institute’s financial statements are reported as expenditures in the programs’ financial reports submitted to grantor agencies.

4. INDIRECT COST RATE

The Institute has not elected to use the 10% de minimis indirect cost rate allowed under the Uniform Guidance.

TEXAS HEART INSTITUTE

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NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS YEAR ENDED DECEMBER 31, 2017

5. RECONCILIATION TO CONSOLIDATED FINANCIAL STATEMENTS:

The following reconciles federal award expenditures, as included in the Schedule, to the expenditures reported in the consolidated financial statements of the Institute for the year ended December 31, 2017:

	<u>Amount</u>
Grants and contracts revenue per the Consolidated Statement of Activities	\$ 6,537,600
Adjustments:	
Less: Non-federal grants and contracts revenue	<u>(4,479,048)</u>
Total expenditures per the Schedule of Expenditures of Federal Awards	<u>\$ 2,058,552</u>

6. CONTINGENCIES

Federal grants received by the Institute are subject to reviews and audits by grantor agencies that could result in the discovery of unallowable activities and costs. Also, the ability of the Institute to collect any related grants receivable at December 31, 2017 may be impaired. Consequently, any of the funding sources may, at its discretion, request reimbursement for expenses or return of funds, or both, as a result of noncompliance by the Institute with the terms of the grant agreements. In the opinion of management, such disallowances, if any, would not be significant in relation to the Institute's grant activities.

FINDINGS AND QUESTIONED COSTS

TEXAS HEART INSTITUTE

(A Texas Nonprofit Organization)

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS
YEAR ENDED DECEMBER 31, 2017**

PART I: SUMMARY OF AUDITOR’S RESULTS

Financial Statements:

- 1. Type of auditor’s report issued: Unmodified
- 2. Internal control over financial reporting:
 - a) Material weakness identified? No
 - b) Significant deficiency identified that is not considered to be a material weakness? No
- 3. Noncompliance material to financial statements noted? No

Federal and State Awards:

- 1. Internal control over major programs:
 - a) Material weakness identified? No
 - b) Significant deficiency identified that is not considered to be a material weakness? No
- 2. Type of auditor’s report issued on compliance for major programs: Unmodified
- 3. Any audit findings disclosed that are required to be reported in accordance with the Uniform Guidance? No
- 4. Identification of major programs:

<u>Federal - CFDA Number</u>	<u>Name of Federal Program or Cluster</u>
------------------------------	---

Research & Development Cluster:	
43.007	Space Operations
93.395	Cancer Treatment Research
93.837	Cardiovascular Diseases Research

- 5. Dollar threshold used to distinguish between type A programs and type B programs: \$750,000

TEXAS HEART INSTITUTE

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**SCHEDULE OF FINDINGS AND QUESTIONED COSTS
YEAR ENDED DECEMBER 31, 2017**

6. Auditee qualified as low-risk auditee under
2 CFR section 200.520? No

PART II: FINDINGS - FINANCIAL STATEMENT AUDIT

This section identifies the significant deficiencies, material weaknesses, and instances of fraud, illegal acts, violations of provisions of contracts and grant agreements, and abuse related to the financial statements for which *Government Auditing Standards* require reporting under 2 CFR Section 200.515(d)(2).

No findings were noted.

**PART III: FINDINGS AND QUESTIONED COSTS - MAJOR FEDERAL
AWARD PROGRAMS**

This section identifies the significant deficiencies, material weaknesses, and material instances of noncompliance, including questioned costs, as well as any abuse findings involving federal awards that are material to a major program.

No findings were noted.

TEXAS HEART INSTITUTE

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SCHEDULE OF PRIOR YEAR FINDINGS AND QUESTIONED COSTS YEAR ENDED DECEMBER 31, 2017

Finding No. 2016-001: **Noncompliance and Significant Deficiency in Internal Control Over Major Programs**

**U.S. Department of Health and Human Services
National Aeronautics and Space Administration**

Research and Development Cluster [43.007, 93.395, 93.837]

Condition: During the course of our audit procedures, we noted that the Institute does not have written procedures in place for procurement, cash management, and allowability of costs.

Recommendations: We recommend the Institute adopt and implement written policies for cash management, allowability of costs, and procurement for the fiscal year ended December 31, 2017.

Current Status: Resolved.