REPORT OF INDEPENDENT AUDITORS AND
FINANCIAL STATEMENTS

THE SALK INSTITUTE FOR BIOLOGICAL STUDIES

June 30, 2018 and 2017

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MOSSADAMS

Report of Independent Auditors

The Board of Trustees
The Salk Institute for Biological Studies

Report on the Financial Statements

We have audited the accompanying financial statements of The Salk Institute for Biological Studies (the "Institute"), which comprise the statements of financial position as of June 30, 2018 and 2017, and the related 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 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 financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the 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 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 financial statements referred to above present fairly, in all material respects, the financial position of The Salk Institute for Biological Studies as of June 30, 2018 and 2017, and the changes in net assets and cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Moss Adams LLP

San Diego, California
September 28, 2018

The Salk Institute for Biological Studies
Statements of Financial Position
(In Thousands)

	June 30, 2018	June 30, 2017
ASSETS		
Cash and cash equivalents	$ 20,159	$ 9,626
Receivables and other assets, net	17,933	13,495
Contributions receivable, net	13,504	34,143
Funds held by trustees	11,649	11,994
Investments	385,666	353,691
Property, net	72,407	77,650
Total assets	$ 521,318	$ 500,599
LIABILITIES AND NET ASSETS		
Liabilities		
Accounts payable and accrued expenses	$ 20,565	$ 21,255
Unexpended advances	25,803	24,536
Retirement obligations	5,968	6,504
Debt	65,553	63,237
Total liabilities	117,889	115,532
Commitments and Contingencies (Note 10)		
Net Assets		
Unrestricted	86,082	88,141
Temporarily restricted	125,960	110,130
Permanently restricted	191,387	186,796
Total net assets	403,429	385,067
Total liabilities and net assets	$ 521,318	$ 500,599

See accompanying notes.

The Salk Institute for Biological Studies
Statement of Activities
(In Thousands)

	Year Ended June 30, 2018			
	Unrestricted	Temporarily Restricted	Permanently Restricted	2018 Total
REVENUES, GAINS, AND OTHER SUPPORT				
Grants	$ 84,799	$ -	$ -	$ 84,799
Contributions	4,670	22,622	4,591	31,883
Other	3,730	-	-	3,730
Investment return designated for current operations	6,507	8,934	-	15,441
Net assets released from restrictions	21,639	(21,639)	-	-
Total revenues, gains, and other support	121,345	9,917	4,591	135,853
EXPENSES				
Research	103,836	-	-	103,836
Management and general	16,906	-	-	16,906
Fundraising	5,223	-	-	5,223
Total expenses	125,965	-	-	125,965
EXCESS (DEFICIENCY) OF REVENUES, GAINS, AND OTHER SUPPORT OVER EXPENSES	(4,620)	9,917	4,591	9,888
INVESTMENT GAIN IN EXCESS OF AMOUNT DESIGNATED FOR CURRENT OPERATIONS UNDER SPENDING POLICY	4,580	5,913	-	10,493
COSTS OF DEFEASANCE OF DEBT	(2,541)	-	-	(2,541)
POST-RETIREMENT BENEFIT CHANGES OTHER THAN NET PERIODIC BENEFIT COST	522	-	-	522
CHANGE IN NET ASSETS	(2,059)	15,830	4,591	18,362
NET ASSETS				
Beginning of year	88,141	110,130	186,796	385,067
End of year	$ 86,082	$ 125,960	$ 191,387	$ 403,429

See accompanying notes.

(In Thousands)

	Year Ended June 30, 2017			
	Unrestricted	Temporarily Restricted	Permanently Restricted	2017 Total
REVENUES, GAINS, AND OTHER SUPPORT				
Grants	$ 77,542	$ -	$ -	$ 77,542
Contributions	3,585	25,170	9,893	38,648
Other	3,462	-	-	3,462
Investment return designated for current operations	6,201	8,080	-	14,281
Net assets released from restrictions	25,569	(25,569)	-	-
Total revenues, gains, and other support	116,359	7,681	9,893	133,933
EXPENSES				
Research	100,730	-	-	100,730
Management and general	14,307	-	-	14,307
Fundraising	4,636	-	-	4,636
Total expenses	119,673	-	-	119,673
EXCESS (DEFICIENCY) OF REVENUES, GAINS, AND OTHER SUPPORT OVER EXPENSES	(3,314)	7,681	9,893	14,260
INVESTMENT GAIN IN EXCESS OF AMOUNT DESIGNATED FOR CURRENT OPERATIONS UNDER SPENDING POLICY	10,597	11,674	-	22,271
POST-RETIREMENT BENEFIT CHANGES OTHER THAN NET PERIODIC BENEFIT COST	556	-	-	556
CHANGE IN NET ASSETS	7,839	19,355	9,893	37,087
NET ASSETS				
Beginning of year	80,302	90,775	176,903	347,980
End of year	$ 88,141	$ 110,130	$ 186,796	$ 385,067

The Salk Institute for Biological Studies
Statements of Cash Flows
(In Thousands)

	Years Ended June 30, 2018	Years Ended June 30, 2017
OPERATING ACTIVITIES		
Change in net assets	$ 18,362	$ 37,087
Adjustments to reconcile change in net assets to net cash provided by (used in) operating activities:		
Depreciation and amortization	10,477	10,205
Contributions restricted for investment in perpetuity	(2,042)	(1,784)
Net gain on investments and funds held by trustees	(26,981)	(36,266)
Changes in assets and liabilities:		
Receivables and other assets	(4,438)	(1,131)
Contributions receivable	(3,985)	(6,619)
Accounts payable and accrued expenses	(690)	1,583
Unexpended advances	1,267	(1,395)
Retirement obligations	(536)	(513)
Net cash (used in) provided by operating activities	(8,566)	1,167
INVESTING ACTIVITIES		
Purchases of property	(5,197)	(15,131)
Purchases of investments	(172,355)	(206,733)
Proceeds from sales of investments	166,553	204,568
Net cash used in investing activities	(10,999)	(17,296)
FINANCING ACTIVITIES		
Proceeds from contributions restricted for:		
Investment in perpetuity	26,041	6,625
Investment in plant	625	-
Debt proceeds	37,520	8,214
Repayment of debt through defeasance	(33,738)	-
Loan issue costs	(479)	-
Principal payments on debt	(1,024)	(828)
Additions to funds held by trustees	(1,908)	(2,447)
Proceeds from sale of funds held by trustees	3,061	2,234
Net cash provided by financing activities	30,098	13,798
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	10,533	(2,331)
CASH AND CASH EQUIVALENTS		
Beginning of year	9,626	11,957
End of year	$ 20,159	$ 9,626

SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION

	2018	2017
Cash payments for interest	$ 2,513	$ 2,598

See accompanying notes.

Note 1 – Nature of the Institute

The Salk Institute for Biological Studies, San Diego, California (the "Institute") conducts basic biomedical research funded primarily with grants and contributions from agencies of the United States government, foundations, and the general public.

The Institute is a California not-for-profit public benefit corporation exempt from income taxes under Section 501(c)(3) of the Internal Revenue Code and Section 23701(d) of the California Revenue and Taxation Code. Income determined to be unrelated business income is taxable.

Note 2 – Significant Accounting Policies

General – The financial statements have been prepared on the accrual basis of accounting and in accordance with accounting principles generally accepted in the United States of America ("GAAP"). Net assets and activities are presented as unrestricted, temporarily restricted, and permanently restricted based on related donor restrictions or lack of such restrictions. Unrestricted net assets represent expendable funds available for operations, which are not otherwise limited by donor restrictions. Temporarily restricted net assets consist of contributed funds whose use is limited by donor-imposed restrictions that either expire by passage of time or can be fulfilled and removed by actions of the Institute pursuant to the stipulations. Permanently restricted net assets are subject to irrevocable donor restrictions requiring the assets be maintained in perpetuity, usually for the purpose of generating investment income to fund research and other activities.

The costs of providing program services and other activities are summarized on a functional basis in the statements of activities and, accordingly, certain costs have been allocated among the activities benefited.

Revenue Recognition:

Grants – Grant revenue is recognized as unrestricted revenue when the related research costs are incurred, up to the maximum grant amount. Unspent grant funds received in advance of the related expenditures are reported as unexpended advances. Reimbursement for indirect expenses on certain research grants is based on specified rates applied to allowable direct expenses.

Contributions – Contributions are recorded as revenue at fair value when unconditionally pledged or when received, whichever is earlier. Contributions subject to donor-imposed restrictions for use in a future period or for a specific purpose are reported as either temporarily or permanently restricted, depending on the nature of the donor's restriction. When a donor restriction expires or is fulfilled, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statements of activities as net assets released from restrictions.

Note 2 – Significant Accounting Policies (continued)

Contributions (continued) – Contributions of equipment or other long-lived assets are recognized when pledged or received, whichever is earlier, and recorded at the fair value of the contributed asset at the time of donation. If donors stipulate how long the assets must be used, the contributions are recorded as restricted support. In the absence of such stipulations, contributions of property and equipment are recorded as unrestricted support.

Cash and cash equivalents – Cash and cash equivalents are defined as cash on hand and in banks, plus highly liquid investments, which fund the daily operating activities of the Institute and have a maturity, at the date of purchase, of three months or less. Cash and cash equivalents held within the investment portfolio as part of the Institute's investment strategy are included in investments on the statements of financial position.

Receivables and other assets – Receivables and other assets include amounts billed and unbilled on grants and other agreements through June 30. An allowance for estimated uncollectible accounts is recorded based on past experience and an analysis of current receivable balances. Accounts are written off against the allowance when deemed uncollectible. Management has determined that an allowance of $94 and $39 is necessary at June 30, 2018 and 2017, respectively.

Also included in receivables and other assets is the Institute's beneficial interest in split-interest agreements which provide for the payment of distributions to the donor or other designated beneficiaries over the split-interest agreement's term (usually the beneficiary's lifetime). At the end of a split-interest agreement's term, the remaining assets are available for use by the Institute for the purpose specified by the donor. The portion of the assets attributable to the fair value of the future benefits to be received by the Institute is recorded on the statement of activities as temporarily or permanently restricted contribution revenue in the year the split-interest agreement is established. The fair value of the Institute's beneficial interest in split-interest agreements totaled $1,735 and $2,121 at June 30, 2018 and 2017, respectively.

Contributions receivable – Contributions receivable consists of unconditional promises to give. Unconditional promises to give that are expected to be collected in future years are recorded at fair value when the promise is made, based on a discounted cash flow model. The discounts on these amounts are computed using risk-free rates established at the time those promises are received. The discount rates for the contributions receivable range from 0.625 percent to 2.75 percent as of June 30, 2018. Amortization of the discounts is included in contributions. Conditional promises to give are not recorded as revenue until the conditions are substantially met. An allowance for estimated uncollectible contributions receivable is recorded based on management's judgment and analysis of the creditworthiness of the donors, past collection experience, and other relevant factors. Accounts are written off against the allowance when deemed uncollectible. Management has determined that an allowance for uncollectible contributions receivable of $1,603 is necessary as of June 30, 2018 and 2017.

Note 2 – Significant Accounting Policies (continued)

Investments – Investments in marketable securities are carried at their fair values based on quoted prices in an active market. Alternative investments for which quoted market prices are not available are valued at fair value by third-party fund managers or the general partners of the related investment partnerships, based on factors deemed relevant by the third-party fund managers or the general partners including, but not limited to, market conditions, purchase price, estimated liquidation value, restrictions on transfer, and meaningful third-party transactions in the private market. The Institute's Finance Department, under the supervision of the Chief Financial Officer, determines the investment fair value measurement policies and procedures in consultation with the Institute's independent professional investment manager. These policies and procedures are reassessed at least annually to determine if the current valuation techniques are still appropriate. At that time, the unobservable inputs used in the fair value measurements are evaluated and adjusted, as necessary, based on current market conditions and other third-party information. The Institute reviews and evaluates the values provided by third-party fund managers and general partners and agrees with the valuation methods and assumptions used in determining the fair value of alternative investments. For these investments, the Institute uses the net asset value ("NAV") provided by the investment fund managers to evaluate the fair value of the investments (see Notes 4 and 9). The NAV may be adjusted based on liquidity factors or other information about the investments that management considers significant to the valuation of the investments.

Realized and unrealized gains and losses are included in investment return in the change in net assets on the accompanying statements of activities.

Funds held by trustees – At June 30, 2017, funds held by trustees include $1,377 required to be held in a separate account under the Certificates of Participation agreement and revenue bonds which were refinanced in April of 2018 (Note 6) and are comprised of cash and cash equivalents. In addition, funds held by trustees include $11,649 and $10,617 at June 30, 2018 and 2017, respectively, held primarily in mutual funds in a rabbi trust to pay the benefits provided by the Institute's retiree health plan (Note 8). Funds held by trustees held in fixed income, global equity, and large cap equity mutual funds are carried at their fair value based on quoted prices in an active market.

Property – Property, including land, buildings, and equipment, is carried at cost. The Institute capitalizes acquisitions of property of $5 or more. Depreciation and amortization are recorded using the straight-line method over estimated useful lives of the assets ranging from 3 to 50 years.

Impairment of long-lived assets – The Institute evaluates long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying value of an asset may not be recoverable. If the estimated future cash flows (undiscounted and without interest charges) from the use of an asset are less than the carrying value, a write-down will be recorded to reduce the related asset to its estimated fair value. To date, no such write-downs have occurred.

Note 2 – Significant Accounting Policies (continued)

Endowments – The Institute's endowment consists of 108 individual funds established for a variety of purposes. The endowment includes both donor-restricted endowment funds and funds designated by the Board of Trustees (the "Board") to function as endowments. Net assets associated with endowment funds, including funds designated by the Board to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions.

The Institute classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of 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 California's enacted version of the Uniform Prudent Management of Institutional Funds Act of 2006 ("UPMIFA"). In accordance with UPMIFA, the Institute considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

1) The duration and preservation of the fund;
2) The purposes of the Institute and the donor-restricted endowment fund;
3) General economic conditions;
4) The possible effect of inflation and deflation;
5) The expected total return from income and the appreciation of investments;
6) Other resources of the Institute; and
7) The investment policies of the Institute.

The Institute has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs and activities supported by its endowment while seeking to maintain the purchasing power of the endowment assets. The Institute's spending and investment policies work together to achieve this objective. The investment policy establishes an achievable return objective through diversification of asset classes. The current long-term return objective is a total return, over rolling ten-year periods, which exceeds biomedical inflation by an average of 5 percent per year. Actual returns in any given year may vary from this amount.

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

Note 2 – Significant Accounting Policies (continued)

The Institute has a policy of appropriating for distribution each year a percentage of its endowment funds' average fair value over the prior 12 quarters. The percentage distribution is determined annually by the Board in the budget approval process and was 5 percent for each of the years ended June 30, 2018 and 2017. In establishing this policy, the Institute considered the long-term expected return on its endowment. Accordingly, over the long term, the Institute expects the current spending policy to allow its endowment to grow at an average of the biomedical inflation rate annually. This is consistent with the Institute's objective to maintain the purchasing power of the endowment assets held in perpetuity or for a specified term with the goal of meeting current and future cash flow requirements, as well as to provide additional real growth through new gifts.

Use of estimates – The preparation of financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Risks and uncertainties – The Institute invests in various types of securities which are exposed to various risks such as interest rate, market, currency, and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near-term and such changes could materially affect the amounts reported in the statement of financial position.

Reclassifications – Certain reclassifications have been made to the 2017 amounts in order to conform to the presentation for the year ended June 30, 2018, with no impact to net assets.

Subsequent events – Subsequent events are events or transactions that occur after the statement of financial position date but before the financial statements are issued. The Institute recognizes in the financial statements the effects of all significant subsequent events that provide additional evidence about conditions that existed at the date of the statement of financial position, including the estimates inherent in the process of preparing the financial statements. The Institute's financial statements do not recognize subsequent events that provide evidence about conditions that did not exist at the date of the statement of financial position but arose after the statement of financial position date and before the financial statements are available to be issued.

The Institute has evaluated subsequent events through September 28, 2018, which is the date the financial statements were available to be issued.

(In Thousands)

Note 2 – Significant Accounting Policies (continued)

Recently issued accounting standard – In August 2016, the Financial Accounting Standards Board issued Accounting Standards Update 2016-14, *Not-for-Profit Entities (Topic 958): Presentation of Financial Statement for Not-for-Profit Entities*. This guidance revises the not-for-profit reporting model and requires expenses to be disclosed by both functional and natural classification, reduces the net asset classifications to two (with and without donor restrictions), and requires new disclosures on liquidity. The guidance is effective for fiscal years beginning after December 15, 2017. Management is currently evaluating the impact this will have on the Institute's future financial statements.

Note 3 – Contributions Receivable

Contributions receivable are summarized as follows at June 30:

	2018	2017
Contributions receivable to be paid in:		
Less than one year	$ 6,084	$ 29,088
One to five years	9,651	7,025
	15,735	36,113
Less:		
Unamortized discount	(628)	(367)
Reserve for uncollectible pledges	(1,603)	(1,603)
Total contributions receivable, net	$ 13,504	$ 34,143

At June 30, 2018 and 2017, net contributions receivable of $8,784 and $7,743, respectively, are from members of the Board.

Note 4 – Investments

The Institute's portfolio is managed by an independent professional investment manager subject to direction and oversight by a committee of the Board. The manager is authorized to invest in alternative investments to increase portfolio diversification and return and reduce volatility. Included in investment returns are investment advisory fees of $1,836 and $1,634 for the years ended June 30, 2018 and 2017, respectively.

Investments include endowment funds and general funds of the Institute. The Board has designated a portion of the Institute's cumulative investment return on general funds to be used for support of current operations. Under the Institute's spending policy, the Board determines annually a percentage of the average of the fair value of the Institute's general fund investment balances for the previous 12 quarters for appropriation to support current operations. The spending rate was 5 percent in 2018 and 2017.

(In Thousands)

Note 4 – Investments (continued)

Investments are summarized as follows at June 30:

	2018	2017
Marketable securities:		
Cash and cash equivalents	$ 10,745	$ 16,523
U.S. Treasury securities	58,975	29,954
Equity securities	35,092	31,457
Mutual funds:		
Emerging markets	10,958	14,753
Long/short equity	-	43,214
Fixed income	-	15,184
Total marketable securities	115,770	151,085
Alternative investments:		
Global equity funds	128,133	80,307
Fixed income funds	32,885	34,708
Emerging markets funds	22,045	18,949
Global multi-strategy funds	17,366	-
Long only equity funds	16,742	13,969
Private equity funds	16,731	7,091
Distressed securities funds	16,067	34,674
Long/short equity funds	12,212	11,553
Real assets funds	7,715	1,355
Total alternative investments	269,896	202,606
Total investments	$ 385,666	$ 353,691

Note 4 – Investments (continued)

Alternative investments – Alternative investments are generally less liquid than the Institute's other investments and invest primarily in the following:

Global equity funds – shares of companies listed on stock exchanges worldwide.

Fixed income funds – investment-grade debt and fixed income securities, fixed- and floating-rate debt securities, and debt obligations of governments or government-related issuers worldwide.

Emerging markets funds – financial markets of developing countries.

Global multi-strategy funds – performing debt, distressed debt, hedge/arbitrage positions, merger arbitrage, equity-oriented positions, basis trading, portfolio volatility protection positions, commodities, and real estate.

Long only equity funds – long only investments in publicly traded equity securities in the healthcare sector.

Private equity funds – pooled investment vehicles purchased from existing owners and not from the issuers of such investments and in the communications, media, technology, consumer, healthcare services, biotech, and financial sectors.

Distressed securities funds – distressed debt and mortgage investments, distressed securities, undervalued securities, private investments, debt and equity securities of companies involved in or affected by the real estate and mortgage crisis, and fixed income securities, including commercial bank loan debt.

Long/short equity funds – global investments in equities, commodities, and currencies on both the long and short side.

Real assets funds – investments in global agriculture and timber, North American oil and gas, and a broad range of real estate in the U.S., Europe, and Asia.

The fair values of the alternative investments have been estimated using the NAV of the Institute's ownership interest in the funds or the Institute's share of partners' capital.

(In Thousands)

Note 4 – Investments (continued)

The nature and risks of the alternative investments as of June 30, 2018, are summarized as follows:

	Fair Value	Unfunded Commitments	Redemption Frequency (if eligible)	Redemption Notice Period	Additional Redemption Terms and Restrictions (if any)
Global equity funds	$ 128,133	$ -	weekly, bi-monthly, monthly, quarterly	3-90 days	Generally, subject to the suspension of redemption rights if in the best interest of the fund. Redemptions subject to minimum withdrawal amounts, redemption fees, early redemption penalties, anti-dilution levies, up to a 5-year rolling lock up, and/or up to a 25% fund level gate.
Fixed income funds:					
Active	19,968	-	daily	2 days	Subject to the suspension of redemption rights if in the best interest of the fund and a 25% fund level gate.
Non-redeemable	12,917	5,447	n/a	n/a	Not eligible for redemption. Remaining lives of the funds 8 to 14 years.
Emerging markets funds	22,045	-	quarterly	45-90 days	Generally, subject to the suspension of redemption rights if in the best interest of the fund. $4,478 in a fund for which redemptions are subject to a 12-month lock-up period and a 20% master fund level gate.
Global multi-strategy funds	17,366	21,150	biannually, quarterly	60 days	Generally, subject to the suspension of redemption rights if in the best interest of the fund. Redemptions subject to a 2-year lock up for each contribution, 50% of the account balance, a 10% fund level gate, and/or a 25% investor level gate per quarter.
Long only equity funds	16,742	-	quarterly	45 days	Subject to the suspension of redemption rights if in the best interest of the fund and a 25% fund level gate. Eligible for redemption after November 1, 2018.
Private equity funds:					
Active	16,049	29,180	n/a	n/a	Not eligible for redemption. Remaining lives of the funds 9 to 27 years.
Liquidating	682	1,223	n/a	n/a	Not eligible for redemption.
Distressed securities funds:					
Active	7,899	-	biannually, annually, biennially	60-180 days	Generally, subject to the suspension of redemption rights if in the best interest of the fund. Full redemption of the investments may occur over a period of up to three years.
Non-redeemable	5,923	6,658	n/a	n/a	Not eligible for redemption. Remaining lives of funds 1 to 7 years.
Liquidating	2,245	-	n/a	n/a	Distributions may extend through February 1, 2024.
Long/short equity funds:					
Active	12,086	-	quarterly	3 months	Generally, subject to the suspension of redemption rights if in the best interest of the fund.
Liquidating	126	-	n/a	n/a	Not eligible for redemption.
Real assets funds	7,715	28,375	n/a	n/a	Not eligible for redemption. $2,423 in a fund for which there is no limit on the remaining life. $5,292 in funds with remaining lives of 7 to 18 years.
	$ 269,896	$ 92,033			

(In Thousands)

Note 4 – Investments (continued)

The composition of investment return includes the following for the years ended June 30, 2018 and 2017:

	2018			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Interest and dividends	$ 534	$ 509	$ -	$ 1,043
Net gain	10,553	14,338	-	24,891
Investment return	11,087	14,847	-	25,934
Investment return designated for current operations	6,507	8,934	-	15,441
Investment gain in excess of amounts designated for current operations	$ 4,580	$ 5,913	$ -	$ 10,493

	2017			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Interest and dividends	$ 1,090	$ 1,231	$ -	$ 2,321
Net gain	15,708	18,523	-	34,231
Investment return	16,798	19,754	-	36,552
Investment return designated for current operations	6,201	8,080	-	14,281
Investment gain in excess of amounts designated for current operations	$ 10,597	$ 11,674	$ -	$ 22,271

(In Thousands)

Note 5 – Property

Property is summarized as follows at June 30:

	2018	2017
Land	$ 1,154	$ 1,154
Buildings and improvements	161,111	160,325
Laboratory equipment	68,866	67,197
Other equipment	15,073	13,852
Construction in progress	546	284
	246,750	242,812
Less accumulated depreciation and amortization	(174,343)	(165,162)
Total property, net	$ 72,407	$ 77,650

Included in total expenses is depreciation expense of $10,440 and $10,165 for the years ended June 30, 2018 and 2017, respectively.

(In Thousands)

Note 6 – Debt

The Institute issued debt to fund the construction, renovation, and equipping of various facilities on its campus. The outstanding debt at June 30 is comprised of the following:

Debt Issue	Purpose	Terms	Total Debt Issue	Outstanding Balance 2018	Outstanding Balance 2017
2010 Certificates of Participation through the County of San Diego	Construction and renovation, including the renewal and expansion of the central plant and electrical distribution infrastructure; refinance 2000 Certificates of Participation issued for construction of a new research facility.	$8,595 in serial certificates due from July 1, 2011 through July 1, 2025, at interest rates from 3.00 percent to 5.00 percent; $7,320 in 5.25 percent term certificates due on July 1, 2030; and $21,530 in 5.125 percent term certificates due on July 1, 2040.	$ 37,445	$ -	$ 34,795
2014 tax-exempt direct placement loan through the California Statewide Communities Development Authority ("2014 Loan")	Renovation, restoration, improvement, and equipping of the Institute's campus facilities; refinance the 2005 bonds that had been issued to refinance the 1994 bonds that funded the construction of the research buildings expansion project.	Funds to be drawn monthly as needed for loan purposes through December 31, 2017; repayment at level debt service with the 2018 taxable direct placement loan, with final maturity on July 1, 2044; 3.4 percent fixed interest rate.	31,190	30,066	29,420
2018 taxable direct placement loan ("2018 Loan")	Refinance 2010 Certificates of Participation	Final maturity on July 1, 2040; 3.75 percent fixed interest rate.	36,360	36,360	-
	Subtotal			66,426	64,215
	Unamortized discount			-	(181)
	Unamortized costs of issuance			(873)	(797)
	Total debt			$ 65,553	$ 63,237

Issuance costs related to the Institute's debt are being amortized over the lives of the respective debt instruments. Amortization expense related to the issuance costs was $32 for the years ended June 30, 2018 and 2017.

The future annual principal payments under the 2014 Loan and the 2018 Loan are as follows:

Years ending June 30,	
2019	$ 1,533
2020	1,582
2021	1,647
2022	1,707
2023	1,770
Thereafter	58,187
Total	$ 66,426

(In Thousands)

Note 6 – Debt (continued)

The Institute's debt is collateralized by all of the revenue of the Institute and further secured by a deed of trust on the Institute's main campus. Interest expense related to the Institute's debt was $2,654 and $2,348 for the years ended June 30, 2018 and 2017, respectively. Under the terms of the Institute's debt, the Institute is subject to compliance with certain covenants, including restrictions on additional indebtedness.

Note 7 – Net Assets

Net assets at June 30 are summarized as follows:

	2018	2017
Unrestricted	$ 86,082	$ 88,141
Temporarily Restricted		
Research	116,882	103,351
Appreciation on unrestricted use endowments	9,078	6,779
Total temporarily restricted	125,960	110,130
Permanently Restricted		
Research	132,154	127,849
Unrestricted use	59,233	58,947
Total permanently restricted	191,387	186,796
Total net assets	$ 403,429	$ 385,067

Net assets were released from restrictions by satisfying donor restrictions for the following purposes during the years ended June 30:

	2018	2017
Temporarily Restricted		
Research	$ 19,941	$ 23,262
Unrestricted use	1,698	2,307
Total releases from restriction	$ 21,639	$ 25,569

(In Thousands)

Note 7 – Net Assets (continued)

The net asset composition of the Institute's donor-restricted and board-designated endowments is as follows at June 30:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
2018				
Donor-restricted	$ -	$ 44,582	$ 191,387	$ 235,969
Board-designated	4,087	-	-	4,087
Total endowment net assets	$ 4,087	$ 44,582	$ 191,387	$ 240,056
2017				
Donor-restricted	$ -	$ 38,251	$ 186,796	$ 225,047
Board-designated	3,878	-	-	3,878
Total endowment net assets	$ 3,878	$ 38,251	$ 186,796	$ 228,925

The changes in endowment net assets for the years ended June 30, 2018 and 2017, are as follows:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets at July 1, 2016	$ 3,759	$ 25,257	$ 176,903	$ 205,919
Investment return:				
Interest and dividends	24	1,231	-	1,255
Net gains (losses)	(24)	19,234	-	19,210
Total investment return	-	20,465	-	20,465
Contributions	200	-	9,893	10,093
Amounts appropriated for expenditure	(81)	(7,471)	-	(7,552)
Endowment net assets at June 30, 2017	3,878	38,251	186,796	228,925
Investment return:				
Interest and dividends	10	509	-	519
Net gains	267	14,295	-	14,562
Total investment return	277	14,804	-	15,081
Contributions	-	-	4,591	4,591
Amounts appropriated for expenditure	(68)	(8,473)	-	(8,541)
Endowment net assets at June 30, 2018	$ 4,087	$ 44,582	$ 191,387	$ 240,056

(In Thousands)

Note 7 – Net Assets (continued)

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. In accordance with GAAP, deficiencies of this nature are reported in unrestricted net assets. There were no deficiencies as of June 30, 2018 or 2017.

Note 8 – Employee Benefit Plans

Retirement Plan – The Institute has an employee retirement plan (the "Retirement Plan") for certain of its employees. The Retirement Plan is a defined-contribution plan under which the Institute contributes a percentage of the participant's annual compensation. The Institute's contributions are made in accordance with Section 403(b) of the Internal Revenue Code. Total contributions expense related to the Retirement Plan was $3,673 and $3,565 for the years ended June 30, 2018 and 2017, respectively.

Retiree Health Benefits Plan – The Institute sponsors a defined-benefit plan (the "Health Benefits Plan") that provides for retirees' health and related benefits. Employees hired prior to June 30, 1993, may become eligible for these post-retirement benefits upon attainment of age 60 with 10 years of service. The Health Benefits Plan includes cost-sharing features such as deductibles, coinsurance, and contributions, which can be adjusted annually, and the Institute's policy is to pay these benefits through a rabbi trust. The Institute uses a June 30 measurement date for the Health Benefits Plan.

The changes in the accumulated post-retirement benefit obligation at June 30 for the Health Benefits Plan are as follows:

	2018	2017
Benefit obligation, beginning of year	$ 6,504	$ 7,017
Service cost	27	27
Interest cost	218	232
Actuarial gain	(574)	(556)
Benefits paid	(207)	(216)
Benefit obligation, end of year	$ 5,968	$ 6,504
Funded status of plan, end of year	$ (5,968)	$ (6,504)
Rabbi trust investments, end of year	$ 11,649	$ 10,617

(In Thousands)

Note 8 – Employee Benefit Plans (continued)

For the years ended June 30, the components of the net periodic post-retirement benefit cost are:

	2018	2017
Service cost	$ 27	$ 27
Interest cost	218	232
Amortization of net gain	(52)	-
Net periodic post-retirement benefit cost	$ 193	$ 259

The deferred actuarial gains are not reflected in net periodic post-retirement benefit cost and are included in unrestricted net assets at June 30. The changes in the deferred actuarial gains are as follows:

	2018	2017
Balance, beginning of year	$ 1,097	$ 541
Actuarial gain	574	556
Amortization	(52)	-
Balance, end of year	$ 1,619	$ 1,097

The net actuarial gains included in unrestricted net assets at June 30, 2018, that are expected to be recognized in net periodic post-retirement benefit cost during the fiscal year ended June 30, 2019, are $66.

The benefits expected to be paid from the Health Benefits Plan in each of the next five years and in the aggregate for the following five years are as follows:

Years ending June 30,	
2019	$ 408
2020	403
2021	402
2022	400
2023	385
2024-2028	1,812
Total	$ 3,810

(In Thousands)

Note 8 – Employee Benefit Plans (continued)

Contributions to the Health Benefits Plan are expected to equal benefit payments. For the years ended June 30, 2018 and 2017, employer contributions were $207 and $216, respectively, and participant contributions were $180 and $174, respectively.

The Health Benefits Plan's weighted-average assumptions used to determine net periodic post-retirement benefit cost for the years ended June 30 were as follows:

	2018	2017
Discount rate	3.65%	3.40%
Rate of compensation increase	5.00%	5.00%

The amounts reported are affected by the healthcare trend assumptions. The assumed healthcare cost trend rate used in measuring the accumulated benefit obligation was 6.75 percent and 6.25 percent for 2018 and 2017, respectively, and is assumed to decrease gradually to 4.00 percent in 2073 and remain at that level thereafter. If the healthcare cost trend assumptions were increased by 1 percent, the accumulated post-retirement benefit obligation at June 30, 2018 and 2017, would be increased by approximately $32 and $42, respectively. The effect of this change would increase the aggregate of the service and interest cost components of the net periodic post-retirement benefit cost by approximately $1 and $5 for the years ended June 30, 2018 and 2017, respectively. If the healthcare cost trend assumptions were decreased by 1 percent, the accumulated post-retirement benefit obligation as of June 30, 2018 and 2017, would be decreased by approximately $30 and $39, respectively. The effect of this change would reduce the aggregate of the service and interest cost components of the net periodic post-retirement benefit cost by approximately $1 and $4 for the years ended June 30, 2018 and 2017, respectively.

Self-Insured Health Plan – The Institute self-insures hospitalization and medical coverage under two of the health plans offered to its employees. The Institute limits its losses through the use of a stop-loss policy with a deductible of $150 per covered participant and a maximum liability of 125 percent of the estimated aggregate claims.

Note 9 – Fair Value of Financial Instruments

Authoritative guidance defines fair value as the exchange price that would be received for an asset or paid to transfer a liability in an orderly transaction between market participants on the measurement date and establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The guidance describes three levels of inputs that may be used to measure fair value:

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

Level 2 – Inputs, other than quoted prices, that are observable for the asset or liability, directly or indirectly, including inputs in markets that are not considered to be active; and

Level 3 – Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

Transfers between levels are recognized as of the beginning of the reporting period in which the transfer occurs.

The carrying values of cash and cash equivalents, receivables, and accounts payable approximate their fair values due to the relatively short period of time between origination of the instruments and their expected realization. These assets and liabilities are considered by the Institute to be Level 1 measurements in the fair value hierarchy.

(In Thousands)

Note 9 – Fair Value of Financial Instruments (continued)

The following table presents information about each major category of the Institute's financial assets measured at fair value on a recurring basis at June 30, 2018:

	Fair Value Measurement at June 30, 2018			
	Level 1	Level 2	Level 3	Total
Marketable securities:				
Cash and equivalents	$ 10,932	$ -	$ -	$ 10,932
U.S. Treasury securities	58,975	-	-	58,975
Equity securities:				
Information technology	10,969	-	-	10,969
Consumer products	9,526	-	-	9,526
Industrial	6,726	-	-	6,726
Financial	6,415	-	-	6,415
Other	1,456	-	-	1,456
Total equity securities	35,092	-	-	35,092
Mutual funds:				
Emerging markets	10,958	-	-	10,958
Large cap equity	7,403	-	-	7,403
Global equity	2,052	-	-	2,052
Fixed income	2,007	-	-	2,007
Total mutual funds	22,420	-	-	22,420
Total marketable securities	127,419	-	-	127,419
Beneficial interest in split-interest agreements	-	-	1,735	1,735
	$ 127,419	$ -	$ 1,735	129,154
Investments measured at net asset value:				
Alternative investments:				
Global equity funds				128,133
Fixed income funds				32,885
Emerging markets funds				22,045
Global multi-strategy funds				17,366
Long only equity funds				16,742
Private equity funds				16,731
Distressed securities funds				16,067
Long/short equity funds				12,212
Real assets funds				7,715
Total investments measured at net asset value				269,896
				$ 399,050

(In Thousands)

Note 9 – Fair Value of Financial Instruments (continued)

The following table presents information about each major category of the Institute's financial assets measured at fair value on a recurring basis at June 30, 2017:

	Fair Value Measurement at June 30, 2017			
	Level 1	Level 2	Level 3	Total
Marketable securities:				
Cash and equivalents	$ 18,098	$ -	$ -	$ 18,098
U.S. Treasury securities	29,954	-	-	29,954
Equity securities:				
Information technology	9,272	-	-	9,272
Financial	5,603	-	-	5,603
Industrial	5,498	-	-	5,498
Other	4,463	-	-	4,463
Consumer products	3,201	-	-	3,201
Materials	1,081	-	-	1,081
Healthcare	997	-	-	997
Energy and utilities	778	-	-	778
Telecommunications	564	-	-	564
Total equity securities	31,457	-	-	31,457
Mutual funds:				
Long only equity	43,214	-	-	43,214
Fixed income	17,202	-	-	17,202
Emerging markets	14,753	-	-	14,753
Large cap equity	6,475	-	-	6,475
Global equity	1,926	-	-	1,926
Total mutual funds	83,570	-	-	83,570
Total marketable securities	163,079	-	-	163,079
Beneficial interest in split-interest agreements	-	-	2,121	2,121
	$ 163,079	$ -	$ 2,121	165,200
Investments measured at net asset value:				
Alternative investments:				
Global equity funds				80,307
Fixed income funds				34,708
Distressed securities funds				34,674
Emerging markets funds				18,949
Long only equity funds				13,969
Long/short equity funds				11,553
Private equity funds				7,091
Real estate funds				1,355
Total investments measured at net asset value				202,606
				$ 367,806

(In Thousands)

Note 9 – Fair Value of Financial Instruments (continued)

The decrease in the fair value of the Institute's Level 3 classified assets, the beneficial interest in split-interest agreements, was $386 and $202 for the years ended June 30, 2018 and 2017, respectively. The change in the value of the beneficial interest in split-interest agreements is included in contributions on the statements of activities.

The following table presents information about significant unobservable inputs for Level 3 assets and liabilities:

Asset/Liability	Fair Value as of June 30, 2018	Valuation Technique	Unobservable Input(s)	Rate (Wtd. Avg.)
Beneficial interest in split-interest agreements	$ 1,735	Discounted cash flow	Discount rate Mortality tables	3.4% (3.4%)

Increases (decreases) in the discount rate or life expectancy based on mortality tables would result in decreases (increases) in the fair value of the beneficial interest in split-interest agreements. An increase (decrease) in the fair value of the assets in the related trust or the increase in the Institute's percentage ownership will increase (reduce) the fair value of the Institute's beneficial interest in the split-interest agreement.

In determining the reasonableness of the methodology used to determine the fair value of the beneficial interest in split-interest agreements, the Finance Department evaluates a variety of factors including a review of existing agreements, economic conditions, and industry and market developments at least annually. Certain unobservable inputs are assessed through review of contract terms (e.g., duration or payout data), while others are substantiated utilizing available market data (e.g., discount rates and mortality tables).

(In Thousands)

Note 10 – Commitments and Contingencies

Commitments – At June 30, 2018, contractual commitments on purchases pending or in process are $4,175.

Leases – The Institute has entered into operating leases for building space and equipment that expire through June 2025. Rent expense totaled $652 and $677 for the years ended June 30, 2018 and 2017, respectively. Future minimum rental payments required under non-cancelable operating leases that have remaining lease terms in excess of one year as of June 30, 2018, are as follows:

Years ending June 30,	
2019	$ 670
2020	690
2021	336
2022	105
2023	56
Thereafter	117
	$ 1,974

Line of credit – The Institute has an unsecured line of credit loan agreement with a bank providing up to $5,000 for general working capital purposes. The agreement expires on February 10, 2019, and provides for monthly interest at the prime rate (5.00 percent on June 30, 2018) on the outstanding balance. At June 30, 2018, the Institute had no balance outstanding on the line of credit.

Grants – The Institute has grants with various organizations and government agencies which are subject to audit. Management believes that any liability which may result from these audits would not be material.

Income taxes – The Institute has no unrecognized tax benefits as of June 30, 2018 and 2017.

Legal – The Institute is party to certain legal actions in the ordinary course of business.

A liability is recorded when it is probable that a loss has been incurred and the amount can be reasonably estimated. If a loss is reasonably possible and the loss or range of loss can be estimated, the possible loss is disclosed in the accompanying notes to the financial statements. No such loss contingencies were accrued for the years ended June 30, 2018 and 2017.

Although the ultimate outcome of the legal actions is not determinable at this time, management, after taking into consideration advice of legal counsel, believes that the resolution of these pending matters cannot be reasonably estimated or will not result in a material charge against net assets.

Note 10 – Commitments and Contingencies (continued)

Guarantees and indemnities – From time to time, the Institute enters into certain types of contracts that contingently require the Institute to indemnify parties against third-party claims. These contracts primarily relate to: (i) certain technology transfer/license agreements under which the Institute may be required to indemnify licensees; and (ii) certain agreements with the Institute's officers, directors, and employees, under which the Institute may be required to indemnify such persons for liabilities arising out of their employment relationship. The terms of such obligations vary by contract and, in most instances, a specific or maximum dollar amount is not explicitly stated therein. Generally, amounts under those contracts cannot be reasonably estimated until a specific claim is asserted. Consequently, no liabilities have been recorded for these obligations in the Institute's statements of financial position at June 30, 2018 and 2017.

Note 11 – Concentrations of Credit Risk

Cash in bank deposit accounts and the investment portfolio exceeds federally-insured deposit limits. No losses have been experienced related to cash in such accounts.

The Institute receives funds under various research grants from federal and non-federal agencies. Funding from the National Institutes of Health represents approximately 61 percent and 52 percent of total grant revenue for the years ended June 30, 2018 and 2017, respectively.