



Report of Independent Auditors and
Financial Statements with
Federal Awards Supplementary Information

**Palo Alto Veterans Institute for
Research**

September 30, 2016

MOSS ADAMS LLP

Certified Public Accountants | Business Consultants

CONTENTS

	PAGE
REPORT OF INDEPENDENT AUDITORS	1
FINANCIAL STATEMENTS	
Statement of financial position	3
Statement of activities	4
Statement of functional expenses	5
Statement of cash flows	6
Notes to financial statements	7
SUPPLEMENTARY INFORMATION	
Schedule of expenditures of federal awards	12
Notes to schedule of expenditures of federal awards.....	14
REPORT OF INDEPENDENT AUDITORS ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH <i>GOVERNMENT AUDITING STANDARDS</i>.....	15
REPORT OF INDEPENDENT AUDITORS ON COMPLIANCE FOR THE MAJOR FEDERAL PROGRAM AND REPORT ON INTERNAL CONTROL OVER COMPLIANCE REQUIRED BY THE UNIFORM GUIDANCE	17
SCHEDULE OF FINDINGS AND QUESTIONED COSTS.....	19

REPORT OF INDEPENDENT AUDITORS

To the Board of Directors
Palo Alto Veterans Institute for Research

Report on the Financial Statements

We have audited the accompanying financial statements of Palo Alto Veterans Institute for Research (the "Organization"), which comprise the statement of financial position as of September 30, 2016, and the related statements of activities, functional expenses, and cash flows for the year 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 audit. We conducted our audit 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 financial statements are free of 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 Organization'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 Organization'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 Palo Alto Veterans Institute for Research as of September 30, 2016, and the changes in its net assets and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Other Matters

Supplementary Information

Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The *Schedule of Expenditures of Federal Awards*, as required by Title 2 U.S. Code of Federal Regulations (CFR) Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* is presented for purposes of additional analysis and is not a required part of the 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 financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated, in all material respects, in relation to the financial statements as a whole.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated March 2, 2017, on our consideration of the Organization'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 Organization's internal control over financial reporting and compliance.

A handwritten signature in cursive script that reads "Moss Adams LLP".

San Francisco, California
March 2, 2017

FINANCIAL STATEMENTS

PALO ALTO VETERANS INSTITUTE FOR RESEARCH
STATEMENT OF FINANCIAL POSITION
As of September 30, 2016

	<u>2016</u>
ASSETS	
CURRENT ASSETS	
Cash and cash equivalents	\$ 2,485,164
Certificates of deposit	3,110,459
Accounts receivable	3,902,244
Prepaid expenses	315,443
	<u>9,813,310</u>
Total current assets	<u>9,813,310</u>
EQUIPMENT, net	<u>1,132,233</u>
Total assets	<u>\$ 10,945,543</u>
LIABILITIES AND NET ASSETS	
CURRENT LIABILITIES	
Accounts payable	\$ 533,722
Payroll payable	600,012
Accrued vacation	747,265
Other accrued liabilities	536,449
Deferred revenue	758,474
	<u>3,175,922</u>
Total current liabilities	<u>3,175,922</u>
NET ASSETS	
Unrestricted	
Board-designated	1,360,000
Undesignated	5,451,348
	<u>6,811,348</u>
Total unrestricted	<u>6,811,348</u>
Temporarily restricted	958,273
	<u>7,769,621</u>
Total net assets	<u>7,769,621</u>
Total liabilities and net assets	<u>\$ 10,945,543</u>

See accompanying notes.

PALO ALTO VETERANS INSTITUTE FOR RESEARCH
STATEMENT OF ACTIVITIES
For the Year Ended September 30, 2016

	2016		
	Unrestricted	Temporarily Restricted	Total
REVENUE AND OTHER SUPPORT			
Federal award revenue	\$ 20,071,402	\$ -	\$ 20,071,402
Other program revenue	6,720,246	1,419,037	8,139,283
Interest income	18,705	1,336	20,041
Unrealized loss on certificates of deposit	(868)	-	(868)
Loss on equipment transfer	(16,496)	-	(16,496)
Other income	5,743	-	5,743
Total revenue	<u>26,798,732</u>	<u>1,420,373</u>	<u>28,219,105</u>
NET ASSETS RELEASED FROM RESTRICTIONS			
Satisfaction of program restrictions	1,449,213	(1,449,213)	-
Total revenue and other support	<u>28,247,945</u>	<u>(28,840)</u>	<u>28,219,105</u>
EXPENSES			
Program expenses	20,552,581	-	20,552,581
Management and general expenses	6,333,558	-	6,333,558
Total expenses	<u>26,886,139</u>	<u>-</u>	<u>26,886,139</u>
Change in net assets	1,361,806	(28,840)	1,332,966
NET ASSETS , at beginning of year	<u>5,449,542</u>	<u>987,113</u>	<u>6,436,655</u>
NET ASSETS , at end of year	<u><u>\$ 6,811,348</u></u>	<u><u>\$ 958,273</u></u>	<u><u>\$ 7,769,621</u></u>

See accompanying notes.

PALO ALTO VETERANS INSTITUTE FOR RESEARCH
STATEMENT OF FUNCTIONAL EXPENSES
For the Year Ended September 30, 2016

	<u>Program</u>	<u>Management and General</u>	<u>Total</u>
Personnel costs	\$ 13,770,129	\$ 3,720,303	\$ 17,490,432
Supplies	3,216,585	372,320	3,588,905
Subawards	1,752,243	-	1,752,243
Outside services	1,063,761	490,002	1,553,763
Depreciation	43,268	380,808	424,076
Computer maintenance & supplies	87,275	327,770	415,045
Maintenance and repairs	44,527	286,216	330,743
Travel	94,923	208,410	303,333
Comparative medicine	240,801	1,678	242,479
Professional fees	6,051	144,431	150,482
Subject payments	124,133	5,409	129,542
Small equipment	52,856	33,981	86,837
Printing and publication	20,683	62,906	83,589
Meetings and conferences	12,657	69,650	82,307
Office supplies	11,614	61,659	73,273
Postage and delivery	23,311	28,189	51,500
Insurance	-	43,955	43,955
Dues and subscriptions	2,773	35,067	37,840
Telecommunications	265	18,404	18,669
Miscellaneous expense	(27,203)	39,045	11,842
VA Services	9,054	-	9,054
Subject recruitment	2,490	-	2,490
Books	385	2,008	2,393
Bank charges and fees	-	1,347	1,347
	<u>\$ 20,552,581</u>	<u>\$ 6,333,558</u>	<u>\$ 26,886,139</u>

See accompanying notes.

PALO ALTO VETERANS INSTITUTE FOR RESEARCH
STATEMENT OF CASH FLOWS
For the Year Ended September 30, 2016

	2016
CASH FLOWS FROM OPERATING ACTIVITIES	
Change in net assets	\$ 1,332,966
Adjustments to reconcile change in net assets to net cash from operating activities:	
Depreciation	424,076
Unrealized loss on certificates of deposit	868
Loss on disposal of furniture and equipment	16,496
Change in operating assets:	
Accounts receivable	(863,945)
Prepaid expenses	(96,775)
Change in operating liabilities:	
Accounts payable	(189,970)
Payroll payable	(4,043)
Accrued vacation	28,135
Other accrued liabilities	244,794
Deferred revenue	(434,797)
Total adjustments	(875,161)
Net cash from operating activities	457,805
CASH FLOWS USED IN INVESTING ACTIVITIES	
Purchases of equipment	(504,176)
Purchases of certificate of deposits	(3,982,682)
Proceeds from sales of certificates of deposit	3,375,000
Net cash used in investing activities	(1,111,858)
Net change in cash and cash equivalents	(654,053)
CASH AND CASH EQUIVALENTS, beginning of year	3,139,217
CASH AND CASH EQUIVALENTS, end of year	\$ 2,485,164

See accompanying notes.

**PALO ALTO VETERANS INSTITUTE FOR RESEARCH
NOTES TO FINANCIAL STATEMENTS**

NOTE 1 – GENERAL DESCRIPTION OF ACTIVITIES AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Palo Alto Veterans Institute for Research (the “Organization”), formerly known as Palo Alto Institute for Research and Education (PAIRE), Inc., was incorporated in the State of California on November 30, 1988, and is an independent 501(c)(3) tax exempt corporation. The Organization is located at the VA Palo Alto Health Care System facility (VAPAHCS) in Palo Alto, California. In 2006, the Organization entered into an agreement with Stanford University that delineated under what circumstances PAVIR will administer Federal awards for research conducted in VAPAHCS space. The Organization is the second largest of 80 active VA affiliated not for profits in the United States. The mission of the Organization is to advance Veteran and public health through innovative research.

Program revenues are primarily derived from conducting investigative projects sponsored by public and private funding sources. The Organization receives government grants and contracts as well as awards from private corporations and philanthropic foundations to pursue health research goals.

The Organization works with a large community of uniquely talented medical researchers across a broad spectrum of research areas. The range of research activities is broad and includes special emphasis on major diseases categories, all of which are prevalent in the VA’s patient population. These are:

- Cardiovascular medicine
- Mental health – including Traumatic Brain Injury (“TBI”) and Post Traumatic Stress Disorder (“PTSD”)
- Infectious diseases
- Pain management

In addition, the Organization is particularly interested in chronic inflammatory disease, and stem cell/regenerative medicine. A deeper understanding of chronic inflammatory disease, genetic, and other factors influencing veterans’ health can provide significant insight into the understanding of an individual’s health status.

Basis of presentation – The accompanying financial statements have been prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America (“GAAP”).

Use of estimates – The preparation of the financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amount of revenues and expenses during the reporting period. Actual results could differ from those estimates. The Organization utilizes estimates in its functional expenses, calculation of depreciation expense, and determination of certificates of deposit values.

Net asset classifications – Net assets, revenues, gains, and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, net assets of the Organization and changes therein are classified and reported as follows:

Unrestricted net assets – Include those assets over which the Board of Directors has discretionary control in carrying out the operations of the Organization.

Temporarily restricted net assets – Net assets subject to donor-imposed restrictions that will be met either by actions of the Organization and/or the passage of time. When donor-stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of activities as net assets released from restrictions.

Permanently restricted net assets – Net assets that are subject to donor-imposed restrictions that specify assets donated be invested to provide a permanent source of income. There were no permanently restricted net assets as of September 30, 2016.

**PALO ALTO VETERANS INSTITUTE FOR RESEARCH
NOTES TO FINANCIAL STATEMENTS**

Revenue recognition – The Organization administers several different types of research agreements, including those that are reciprocal and nonreciprocal (charitable) in nature. Grant revenue is recognized when earned, generally in proportion to the expense incurred. Reciprocal agreements are typically on a per-subject payment schedule or milestones. Advance payments from sponsors are classified as deferred revenue and recognized as revenue upon expenditure of allowable costs or completion of the various stages of the studies.

Nonreciprocal revenues or contributions are reported as increases in restricted net assets if they are given with a donor-imposed restriction. Expiration of donor-imposed restrictions (i.e., the donor-stipulated purpose has been satisfied) is reported as satisfaction of program restrictions. The Organization reports donations as unrestricted revenue when the donor does not restrict its use as well as when the donor's restrictions are met in the same reporting period.

Other program revenue includes both grants and contracts from public and private sources. Revenue is recognized as unrestricted or temporarily restricted as specified by the donor, either when received, when costs are incurred or when milestones are reached based on the individual grant or contract provisions.

Cash and cash equivalents – The Organization considers short-term, highly liquid investments to be cash equivalents provided that they are both readily convertible to cash and had an original maturity of three months or less when purchased.

Certificates of deposit – Certificates of deposits are carried at fair value. The Organization has both the ability and the intent to hold them to maturity. Fair value is determined by discounting the related cash flows based on current yields of similar instruments with comparable durations considering the credit-worthiness of the issuer.

Accounts receivable – Accounts receivable are stated at the amount management expects to collect from outstanding balances after reserves for discounts, bad debts, and allowances, taking into account past experience, contracts, history and other organizations' ability to meet their obligations. Balances that are still outstanding after management has used reasonable collection efforts are written off through a charge to expense and a reduction of accounts receivable. Management has deemed all accounts receivable fully collectible.

Equipment – Equipment is stated at cost. Depreciation is computed using the straight-line method with half-year convention over the assets' estimated useful lives ranging from three to seven years. The Organization has adopted a capitalization policy of capitalizing equipment purchases of \$5,000 or more.

Fair value of financial instruments – Unless otherwise indicated, the fair values of all reported assets and liabilities, which represent financial instruments, approximate their carrying values.

Accrued vacation – Accrued vacation represents vacation earned but not taken. The maximum vacation time that can be accrued is 240 hours. The accrued vacation balance as of September 30, 2016, was \$747,265.

Deferred revenue – The Organization receives advances for services to be performed in the future. The amounts are recorded as deferred revenue when received and are recognized as revenue when the services are provided.

Functional expenses allocation – All costs are charged directly to the appropriate functional expense category. There were no fundraising activities for the year ended September 30, 2016.

Income taxes – Palo Alto Veterans Institute for Research is a nonprofit corporation exempt from federal income tax under Internal Revenue Code section 501(c)(3) and state income tax under California Revenue and Taxation Code section 23701d. The Organization qualifies for the charitable contribution deduction under IRC section 170(b)(1)(A)(iii) and has been classified as an Organization that is not a private foundation under section 509(a)(1). As of September 30, 2016, the Organization had no unrecognized tax benefits or uncertain tax positions requiring accrual. Therefore, no provision for income taxes has been provided in the financial statements.

**PALO ALTO VETERANS INSTITUTE FOR RESEARCH
NOTES TO FINANCIAL STATEMENTS**

NOTE 2 - EQUIPMENT

Equipment is comprised of the following as of September 30, 2016:

Administrative assets	\$	711,665
Medical research assets		2,282,250
Less accumulated depreciation		<u>(1,861,682)</u>
Equipment, net	\$	<u>1,132,233</u>

NOTE 3 - TEMPORARILY RESTRICTED NET ASSETS

Temporarily restricted net assets as of September 30, 2016, are available for the following purposes:

Research restricted donations	\$	943,122
Educational activities		<u>15,151</u>
Total	\$	<u>958,273</u>

Net assets were released from donor restrictions during the year ended September 30, 2016, by incurring expenses to satisfy the purpose of the restriction, by the passage of time, or by the occurrence of other specific events as shown in the table below:

Research restricted donations	\$	1,439,213
Educational activities		<u>10,000</u>
Total	\$	<u>1,449,213</u>

NOTE 4 - RETIREMENT PLAN

The Organization's retirement plan (under Internal Revenue Code section 401(k)) is a defined contribution retirement plan which includes a company-match contribution and a profit-sharing contribution. Effective March 1, 2014, regular full-time, part-time and temporary employees are eligible to participate in the plan. Eligible employees may elect to defer a percentage of their salary into the plan. Effective August 1, 2014, the name of the plan was changed from PAIRE Retirement Plan to Palo Alto Veterans Institute for Research (PAVIR) Retirement Plan. Effective October 1, 2014, the plan year changed from a fiscal year to a calendar year plan. Effective January 1, 2015, a Safe Harbor plan was implemented and the company match for 401(k) deferrals increased to 6% from 5%, and the company profit sharing contribution decreased to 3% from 5%. Postdoctorate fellows were excluded from the Plan.

Contributions made to the plan by the Organization were \$647,876 for the year ended September 30, 2016. Plan assets are not reflected in the accompanying financial statements.

NOTE 5 - RELATED PARTY TRANSACTIONS

In 1988 Congress passed Public Law 100-322 (now codified at section 7361-66 of title 38, United States Code) that allowed Department of Veterans Affairs (VA) medical centers to establish nonprofit research corporations (NPCs), forming a unique partnership that dramatically broadened VA's ability to benefit from private and non-VA public support for research conducted at VA medical centers.

Accordingly, the Organization provides a flexible funding mechanism for the conduct of approved research and education at the VAPAHCS facility. Furthermore, as stipulated by statute, the persons holding the positions of Director, Chief of Staff, Associate Chief of Staff for Research and Development and Associate Chief of Staff for Education of VAPAHCS are permanent board members of the Organization. The majority of the Organization's board of directors are employed or affiliated with the VA.

The Organization reimburses the VA for various services. Expenses incurred for services received from the VA were \$9,657 for the fiscal year.

Additionally, the Organization charges the VA for some personnel costs via the Intergovernmental Personnel Act ("IPA") of 1970. Costs expended include salaries and wages, as well as payroll taxes and other benefit costs. Reimbursements for these costs were \$2,338,494 for the year ended September 30, 2016. These costs were included in personnel costs on the statement of functional expenses. At September 30, 2016, the VA was indebted to the Organization in the amount of \$980,223 which is included in the accounts receivable balance at September 30, 2016. In addition, the VA provides office space and utilities to the Organization at no cost. This is not recorded as an in-kind donation as management has deemed it insignificant to the financial statements.

NOTE 6 - CONCENTRATIONS

Major funding – During the year ended September 30, 2016, the Organization received approximately 58% of its revenue from the U.S. Department of Health & Human Services National Institutes of Health. The Organization has long-term agreements with the federal agency and does not anticipate a decrease in funding from these sources.

As of September 30, 2016, the Organization had receivables from the U.S. Department of Health and Human Services National Institutes of Health of \$1,109,427, or 28% of total accounts receivable; Stanford University of \$ 624,296, or 16% of total accounts receivable; and the VA of \$980,223, or 25% of total accounts receivable.

Major vendor – The Organization incurred expenses from one vendor for the year ended September 30, 2016, of \$2,899,711 or 14% of program expenses.

NOTE 7 - COMMITMENTS AND CONTINGENCIES

The Organization has received federal grants for specific purposes that are subject to review and audit by the federal government. Although such audits could result in expenditure disallowances under grant terms, management believes the Organization is in substantial compliance with current laws and regulations and that any potential liability arising from compliance issues will not be material to the Organization's financial position and changes in net assets as of and for the year ended September 30, 2016.

Board designated funds – The Organization's Board has designated \$1,360,000 of unrestricted net assets, which could be spent with board approval.

NOTE 8 - FAIR VALUE MEASUREMENT

Fair value is defined as 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. The fair value hierarchy requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The standard describes three levels of inputs that may be used to measure fair value:

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

Level 2 – Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities

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

Where quoted market prices are available in an active market, investments are classified within Level 1 of the valuation hierarchy. If quoted market prices are not available, then fair values are estimated by using pricing models, quoted prices of investments with similar characteristics or discounted cash flows. Level 2 investments include certificates of deposit. In certain cases where Level 1 or Level 2 inputs are not available, investments are classified within Level 3 of the hierarchy.

PALO ALTO VETERANS INSTITUTE FOR RESEARCH
NOTES TO FINANCIAL STATEMENTS

The following table presents the fair value measurements of assets recognized in the accompanying statement of financial position measured at fair value on a recurring basis and the level within the fair value hierarchy in which the fair value measurements fall at September 30, 2016:

<u>Description</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Certificates of deposit	\$ -	\$ 3,110,459	\$ -	\$ 3,110,459

NOTE 9 – SUBSEQUENT EVENTS

Subsequent events are events or transactions that occur after the statement of financial position date but before financial statements are issued. The Organization recognizes in the financial statements the effects of all 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 Organization’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 financial statements are available to be issued.

The Organization has evaluated subsequent events through March 2, 2017, which is the date the financial statements are available to be issued.

SUPPLEMENTARY INFORMATION



**PALO ALTO VETERANS INSTITUTE FOR RESEARCH
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
For the Year Ended September 30, 2016**

Federal Grantor/Pass-Through Grantor/Program or Cluster Title	Federal CFDA Number (*)	Pass-Through Entity Identifying Number	Passed Through to Subrecipients	Federal Expenditures
<i>Research and Development Cluster</i>				
U.S. Department of Defense:				
Military Medical Research and Development	12.420		61,843	2,352,948
Subtotal direct programs			61,843	2,352,948
Pass-through programs from:				
Fibralign Corporation - Military Medical Research and Development	*	W81XWH-16-C-0009	-	13,461
Fibralign Corporation - Military Medical Research and Development	*	W81XWH-15-C-0038	-	3,146
General Dynamics Information Technology - Military Medical Research and Development	*	W91YTZ-13-C-0015	-	809,841
Tampa Veterans Research and Education Foundation - Military Medical Research and Development	*	W91YTZ-13-C-0015	-	52,356
University of California, San Diego - Military Medical Research and Development	12.420	W81XWH-14-1-0562	-	17,159
K-PAX Pharmaceuticals - Military Medical Research and Development	12.420	W81XWH-14-1-0607	-	130,091
University of Virginia - Military Medical Research and Development	12.420	W81XWH-15-2-0012	-	180,270
University of Colorado - Military Medical Research and Development	12.420	W81XWH-13-1-0408	-	8,745
University of California, San Diego - Military Medical Research and Development	12.420	W81 XWH-13-2-009	-	3,974
Subtotal pass-through programs			-	1,219,043
Total U.S. Department of Defense			61,843	3,571,991
National Aeronautics and Space Administration				
Pass-through programs from:				
University of California, San Francisco - Engineering Grants	47.041	NNX14AC94G	-	109,045
Total National Science Foundation			-	109,045
U.S. Department of Health and Human Services:				
Oral Diseases and Disorders Research	93.121		142,079	397,404
Research and Training in Complementary and Integrative Health	93.213		-	331,548
National Center on Sleep Disorders Research	93.233		-	47,497
Mental Health Research Grants	93.242		562,870	1,391,364
Drug Abuse and Addiction Research Programs	93.279		14,876	76,326
Minority Health and Health Disparities Research	93.307		109,134	385,525
Trans-NIH Research Support	93.310		323,929	2,559,363
Cancer Cause and Prevention Research	93.393		99,970	124,715
Cancer Biology Research	93.396		-	301,788
Cardiovascular Diseases Research	93.837		28,366	1,109,962
Lung Diseases Research	93.838		22,050	371,392
Blood Diseases and Resources Research	93.839		-	13,329
Arthritis, Musculoskeletal and Skin Diseases Research	93.846		-	351,474
Diabetes, Digestive, and Kidney Diseases Extramural Research	93.847		-	39,083
Extramural Research Programs in the Neurosciences and Neurological Disorders	93.853		8,655	616,151
Allergy and Infectious Diseases Research	93.855		113,882	2,484,482
Biomedical Research and Research Training	93.859		22,810	669,823
Aging Research	93.866		158,218	2,072,362
Subtotal direct programs			1,606,839	13,343,588

(*) CFDA numbers that are not available were intentionally left blank

PALO ALTO INSTITUTE FOR RESEARCH AND EDUCATION
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
For the Year Ended September 30, 2016

Federal Grantor/Pass-Through Grantor/Program or Cluster Title	Federal CFDA Number (*)	Pass-Through Entity Identifying Number	Passed Through to Subrecipients	Federal Expenditures
Pass-through programs from:				
Brandeis University - Research and Training in Complementary and Alternative Medicine	93.213	R01 AT008404	-	56,381
University of Michigan - Mental Health Research Grants	93.242	R01 MH096699	-	36,576
Fred Hutchinson Cancer Research Center - Drug Abuse and Addiction Research Programs	93.279	R34 DA040119	-	35,269
Stanford University - Discovery and Applied Research for Technological Innovations	93.286	R21 EB020235	-	56,053
University of Michigan - Nursing Research	93.361	R01 NR012011	-	27,542
Stanford University - Cardiovascular Diseases Research	93.837	various	-	352,761
University of Colorado, Denver - Lung Diseases Research	93.838	P01 HL014985	-	180,434
Stanford University - Lung Diseases Research	93.838	P01 HL108797	-	236,194
Stanford University - Arthritis, Musculoskeletal and Skin Diseases Research	93.846	UM2AR067678	-	108,207
Brigham & Women's - Arthritis, Musculoskeletal and Skin Diseases Research	93.846	R01 AR049880	-	12,541
Stanford University - Diabetes, Digestive, and Kidney Diseases Extramural Research	93.847	various	-	167,451
UCSF - Diabetes, Digestive, and Kidney Diseases Extramural Research	93.847	R01 DK080123	-	(447)
NCIRE - Diabetes, Digestive, and Kidney Diseases Extramural Research	93.847	R01 DK069406	-	142,457
Brigham & Women's - Extramural Research Programs in the Neurosciences & Neurological Disorders	93.853	R01 NS030843	-	38,333
Mayo Clinic - Extramural Research Programs in the Neurosciences & Neurological Disorders	93.853	U01 NS080168	-	3,750
Stanford University - Allergy and Infectious Diseases Research	93.855	various	-	413,212
John Hopkins University - Allergy and Infectious Diseases Research	93.855	R01 AI117032	-	218,185
Emory University - Allergy and Infectious Diseases Research	93.855	U19 AI057266	-	242,646
Mayo Clinic - Allergy & Infectious Diseases Research	93.855	U01 AI089859	-	2,454
University of Pennsylvania - Allergy & Infectious Diseases Research	93.855	various	-	135,552
Washington University in St. Louis - Child Health and Human Development Extramural Research	93.865	various	-	192,460
University of Maryland, Baltimore - Aging Research	93.866	R01 AG037120	-	68,907
Stanford University - Aging Research	93.866	various	-	278,152
Subtotal pass-through programs			-	3,005,070
Total U.S. Department of Health and Human Services			1,606,839	16,348,658
Total Research and Development Cluster and Expenditures of Federal Awards			1,668,682	20,029,694

(*) CFDA numbers that are not available were intentionally left blank

PALO ALTO VETERANS INSTITUTE FOR RESEARCH
NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
For the Year Ended September 30, 2016

NOTE 1 – BASIS OF PRESENTATION

The accompanying Schedule of Expenditures of Federal Awards (the "Schedule") includes the federal grant activity of Palo Alto Veterans Institute for Research (the "Organization"), under programs of the federal government for the year ended September 30, 2016. The information in this 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 Organization, it is not intended to and does not present the financial position, changes in net assets, or cash flows of the Organization.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Expenditures reported on the Schedule are reported on the accrual basis of accounting. Such expenditures are recognized following, as applicable, either the cost principles in OMB Circular A-122, *Cost Principles for Non-Profit Organizations*, or the cost principles contained in Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards*, wherein certain types of expenditures are not allowable or are limited as to reimbursement. Pass-through entity identifying numbers are presented where available. Negative amounts shown on the Schedule represent adjustments or credits made in the normal course of business to amounts reported as expenditures in prior years. The Organization elected not to use the ten percent de minimis indirect cost rate allowed under the Uniform Guidance.

NOTE 3 – SUBRECIPIENTS

Certain funds are passed through to subrecipient organizations by the Organization. Expenditures incurred by the subrecipients, and reimbursed by the Organization, are included in the Schedule of Expenditures of Federal Awards. The Organization is also the subrecipient of federal funds, which are reported as expenditures and listed separately as federal pass through funds.

REPORT OF INDEPENDENT AUDITORS ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

To the Board of Directors
Palo Alto Veterans Institute for Research

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 Palo Alto Veterans Institute for Research (the "Organization"), which comprise the statement of financial position as of September 30, 2016, and the related statements of activities, functional expenses, and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated March 2, 2017.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Organization'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 Organization's internal control. Accordingly, we do not express an opinion on the effectiveness of the Organization'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 Organization's financial statements will not be prevented, or detected and corrected, on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

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

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Organization's 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 entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Organization's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Mass Adams LLP

San Francisco, California
March 2, 2017

**REPORT OF INDEPENDENT AUDITORS ON COMPLIANCE FOR THE MAJOR
FEDERAL PROGRAM AND REPORT ON INTERNAL CONTROL OVER COMPLIANCE
REQUIRED BY THE UNIFORM GUIDANCE**

To the Board of Directors
Palo Alto Veterans Institute for Research

Report on Compliance for the Major Federal Program

We have audited Palo Alto Veterans Institute for Research's (the "Organization") compliance with the types of compliance requirements described in the *OMB Compliance Supplement* that could have a direct and material effect on the Organization's major federal program for the year ended September 30, 2016. The Organization's major federal program is identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

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

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for the Organization's major federal program based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States 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 Organization's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

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

Opinion on the Major Federal Program

In our opinion, the Organization complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on its major federal program for the year ended September 30, 2016.

Report on Internal Control over Compliance

Management of the Organization 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, we considered the Organization's internal control over compliance with the types of requirements that could have a direct and material effect on the major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for the major federal program and to test and report on internal control over compliance in accordance with the Uniform Guidance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Organization'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.

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

A handwritten signature in cursive script that reads "Moss Adams LLP".

San Francisco, California
March 2, 2017

**PALO ALTO VETERANS INSTITUTE FOR RESEARCH
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
For the Year Ended September 30, 2016**

Section I - Summary of Auditor's Results

Financial Statements

Type of report the auditor issued on whether the financial statements audited were prepared in accordance with GAAP:

Unmodified

Internal control over financial reporting:

- Material weakness(es) identified? Yes No
- Significant deficiency(ies) identified? Yes None reported
- Noncompliance material to financial statements noted? Yes No

Federal Awards

Internal control over federal major programs:

- Material weakness(es) identified? Yes No
- Significant deficiency(ies) identified? Yes None reported

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

Yes No

Identification of major federal programs and type of auditor's report issued on compliance for major federal programs:

<i>CFDA Numbers</i>	<i>Name of Federal Program or Cluster</i>	<i>Type of Auditor's Report Issued on Compliance for the Major Federal Program</i>
Various	Research and Development Cluster	<i>Unmodified</i>

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

\$750,000

Auditee qualified as low-risk auditee?

Yes No

Section II - Financial Statement Findings

None noted

Section III - Federal Award Findings and Questioned Costs

None noted