American Academy of Dermatology, Inc. and American Academy of Dermatology Association, Inc.

Combined Financial Report
with Additional Information
December 31, 2018

American Academy of Dermatology, Inc. and American Academy of Dermatology Association, Inc.

Contents

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Independent Auditor's Report

To the Board of Directors
American Academy of Dermatology, Inc.
and American Academy of
Dermatology Association, Inc.

We have audited the accompanying combined financial statements of American Academy of Dermatology, Inc. and American Academy of Dermatology Association, Inc. (collectively, the "Academy"), which comprise the combined statement of financial position as of December 31, 2018 and the related combined statements of activities and changes in net assets, functional expenses, and cash flows for the year then ended, and the related notes to the combined financial statements.

Management's Responsibility for the Combined Financial Statements

Management is responsible for the preparation and fair presentation of these combined 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 combined 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 combined financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the combined financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the combined financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the combined 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 combined 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 combined 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 combined financial statements referred to above present fairly, in all material respects, the financial position of American Academy of Dermatology, Inc. and American Academy of Dermatology Association, Inc. as of December 31, 2018 and the changes in their net assets, functional expenses and their cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

To the Board of Directors
American Academy of Dermatology, Inc.
and American Academy of
Dermatology Association, Inc.

Emphasis of Matter

As described in Note 2 to the combined financial statements, the Academy adopted the provisions of Accounting Standards Update (ASU) No. 2016-14, *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities*, as of December 31, 2018. Our opinion is not modified with respect to this matter.

Plante & Moran, PLLC

May 22, 2019

Combined Statement of Financial Position

		December 31, 2018
Assets		
Cash	$	5,592,807
Investments (Note 3)		69,031,983
Receivables - Net of allowances:		
Trade receivables		3,144,414
Pledges receivable		2,011,715
Inventory - Net		163,212
Prepaid expenses and other assets		2,231,774
Property and equipment - Net (Note 5)		7,394,540
Total assets	**$**	**89,570,445**
Liabilities and Net Assets		
Liabilities		
Accounts payable and other	$	1,508,139
Accrued retirement costs		963,253
Accrued salaries		1,386,070
Accrued vacation leave		637,010
Deferred revenue - Annual national meeting		11,487,162
Deferred revenue - Subscriptions and other		5,436,048
Deferred revenue - Membership dues		7,332,321
Loan commitment (Note 6)		4,090,909
Total liabilities		32,840,912
Net Assets (Note 7)		
Net assets without donor restrictions		45,660,467
Net assets with donor restrictions		11,069,066
Total net assets		56,729,533
Total liabilities and net assets	**$**	**89,570,445**

See notes to combined financial statements.

American Academy of Dermatology, Inc. and American Academy of Dermatology Association, Inc.

Combined Statement of Activities and Changes in Net Assets

Year Ended December 31, 2018

	Without Donor Restrictions	With Donor Restrictions	Total
Revenue, Gains, and Other Support			
Membership dues	$ 10,678,195	$ -	$ 10,678,195
Meetings	20,518,594	-	20,518,594
JAAD and other royalties	7,206,212	-	7,206,212
Educational product sales	3,034,271	-	3,034,271
Other	239,837	-	239,837
Grants and contributions	665,230	6,807,312	7,472,542
Investment loss - Net	(2,082,836)	(271,976)	(2,354,812)
Net assets released from restrictions	6,307,085	(6,307,085)	-
Total revenue, gains, and other support	46,566,588	228,251	46,794,839
Expenses			
Program services:			
Educational	17,590,697	-	17,590,697
Communications	4,984,462	-	4,984,462
Government affairs and research	9,873,380	-	9,873,380
Constituent relations	2,039,567	-	2,039,567
Total program services	34,488,106	-	34,488,106
Member services and administration	13,532,704	-	13,532,704
Fundraising	1,403,058	-	1,403,058
Total expenses	49,423,868	-	49,423,868
(Decrease) Increase in Net Assets	(2,857,280)	228,251	(2,629,029)
Net Assets - Beginning of year	48,517,747	10,840,815	59,358,562
Net Assets - End of year	**$ 45,660,467**	**$ 11,069,066**	**$ 56,729,533**

Combined Statement of Functional Expenses

Year Ended December 31, 2018

	Program Services					Support Services		
	Educational	Communications	Government Affairs and Research	Constituent Relations	Total	Member Services and Administration	Fundraising	Total
Grants and other assistance	$ 1,156,817	$ -	$ 104,315	$ 157,500	$ 1,418,632	$ 82,000	$ -	$ 1,500,632
Salaries and wages	5,513,137	2,066,554	5,002,489	591,182	13,173,362	6,955,235	432,269	20,560,866
Employee benefits	1,570,785	561,446	1,281,113	154,545	3,567,889	1,684,968	109,755	5,362,612
Professional services	1,075,667	842,939	526,122	209,122	2,653,850	271,744	44,498	2,970,092
Legal fees	-	1,700	22,968	-	24,668	316,766	-	341,434
Accounting fees	-	-	-	-	-	100,335	-	100,335
Advertising and promotion	231,674	430,859	98,321	3,957	764,811	44,442	7,261	816,514
Office expenses	877,497	450,613	168,339	21,917	1,518,366	460,787	84,209	2,063,362
Information technology	399,063	159,392	619,730	42,731	1,220,916	503,792	32,086	1,756,794
Occupancy	386,064	151,615	317,094	41,350	896,123	1,005,286	27,566	1,928,975
Travel	994,684	113,916	901,287	623,143	2,633,030	593,661	298,203	3,524,894
Conferences, conventions, and meetings	4,403,875	41,230	205,794	121,807	4,772,706	165,333	339,839	5,277,878
Interest	38,929	15,288	31,925	4,169	90,311	44,516	2,780	137,607
Insurance	170,640	-	23,530	-	194,170	136,733	-	330,903
Training and development	44,692	14,189	211,940	13,932	284,753	652,414	515	937,682
Depreciation and amortization	330,232	129,688	270,816	35,370	766,106	377,625	23,580	1,167,311
Bad debt expense	-	-	-	-	-	7,741	-	7,741
UBIT expense	102,625	-	-	-	102,625	(60,375)	-	42,250
Other	17,544	5,033	87,597	18,842	129,016	189,701	497	319,214
Cost of goods sold	276,772	-	-	-	276,772	-	-	276,772
Total functional expenses	**$ 17,590,697**	**$ 4,984,462**	**$ 9,873,380**	**$ 2,039,567**	**$ 34,488,106**	**$ 13,532,704**	**$ 1,403,058**	**$ 49,423,868**

See notes to combined financial statements.

Combined Statement of Cash Flows

Year Ended December 31, 2018

Cash Flows from Operating Activities	
Decrease in net assets	$ (2,629,029)
Adjustments to reconcile decrease in net assets to net cash from operating activities:	
Depreciation and amortization	1,167,311
Loss on disposal of property and equipment	2,402
Net realized and unrealized loss on investments	4,036,353
Changes in operating assets and liabilities that provided (used) cash:	
Trade receivables	1,929,856
Inventories	52,578
Pledges receivable	497,450
Prepaid expenses and other assets	(279,922)
Accounts payable and other	(38,316)
Accrued liabilities	183,247
Deferred revenue	1,850,659
Net cash provided by operating activities	6,772,589
Cash Flows from Investing Activities	
Purchases of property and equipment	(4,154,690)
Proceeds from disposition of property and equipment	598
Purchases of investments	(34,025,397)
Proceeds from sales and maturities of investments	31,409,522
Net cash used in investing activities	(6,769,967)
Cash Flows Used in Financing Activities - Payments on long-term debt	(409,091)
Net Decrease in Cash	(406,469)
Cash - Beginning of year	5,999,276
Cash - End of year	**$ 5,592,807**
Supplemental Cash Flow Information - Cash paid for interest	$ 133,334

See notes to combined financial statements.

Note 1 - Nature of Business

The American Academy of Dermatology, Inc. (AAD) was incorporated in 1938 as a nonprofit corporation under the laws of the State of Minnesota to promote the highest possible standards of clinical practice, education, and research in dermatology.

The American Academy of Dermatology Association, Inc. (AADA) was incorporated in 2000 as a nonprofit corporation under the laws of the State of Minnesota to promote educational and professional association interests, including, but not limited to, the promotion of the field of dermatology. AADA is not a subsidiary of the Academy; rather, it maintains accounts that are under common management. Interorganizational transactions have been eliminated for combined presentation purposes.

For combined financial statement purposes, the combined entity of AAD and AADA is collectively referred to as the "Academy."

Note 2 - Significant Accounting Policies

Cash

Cash balances are maintained at a financial institution, which at times may exceed federally insured limits. The Academy has not experienced any losses in such accounts and believes it is not exposed to any significant credit risk on cash.

Investments

Investments are recorded at fair value in the combined statement of financial position and are composed of money market funds, corporate stock, corporate bonds, international bonds, mutual funds, governmental and agency bonds, mortgage and asset-backed bonds, municipal bonds, and education bonds. Gains and losses are reported as increases or decreases in net assets and are reflected as changes in net assets with donor restrictions and net assets without donor restrictions, as appropriate.

The Academy's marketable securities are exposed to various risks, such as interest rate, credit, and overall market volatility. Due to these risk factors, it is reasonably possible that changes in the value of marketable securities will occur in the near term and could materially affect the amounts reported in the combined financial statements. The Academy places its cash and marketable securities with high quality institutions and, accordingly, limits its credit exposure.

Trade Receivables

Trade receivables are derived primarily from registration and exhibits for the annual meeting, royalties due from the DermSource affinity programs, and advertising from the Academy's periodical, *Dermatology World*. An allowance for doubtful accounts is established based on a specific assessment of all invoices that remain unpaid following normal customer payment periods. The allowance for doubtful accounts was $12,000 at December 31, 2018. All amounts deemed to be uncollectible are charged against the allowance for doubtful accounts in the period that determination is made.

Pledges Receivable

Pledges receivable are composed primarily of corporate grants, which support academy activities. Contributions expected to be received over more than one year are recorded by the Academy as pledges receivable at fair value, as measured by the present value of future cash flows. Pledges receivable at December 31, 2018 are expected to be collected within one year. The Academy has not recorded a provision for doubtful pledges since it is the opinion of management that those receivables are collectible in full.

Note 2 - Significant Accounting Policies (Continued)

Inventory

Inventory is valued at average cost. The inventory consists primarily of educational finished good items, such as pamphlets and CD-ROMs. Inventory is stated net of an allowance for obsolete inventory of $85,173 at December 31, 2018.

Property and Equipment

Property and equipment are recorded at cost. Assets are depreciated over their estimated useful lives using the straight-line method. Leasehold improvements are amortized over the shorter of their estimated useful lives or terms of the leases. Costs of maintenance and repairs are charged to expense when incurred.

Classification of Net Assets

Net assets of the Academy are classified as net assets with donor restrictions and net assets without donor restrictions depending on the presence and characteristics of donor-imposed restrictions limiting the Academy's ability to use or dispose of contributed assets or the economic benefits embodied in those assets.

Net Assets without Donor Restrictions

Net assets that are not subject to donor-imposed restrictions or for which the donor-imposed restrictions have expired or been fulfilled. Net assets in this category may be expended for any purpose in performing the primary objectives of the Academy.

Net Assets with Donor Restrictions

Net assets subject to stipulations imposed by donors and grantors. Some donor restrictions are temporary in nature; those restrictions will be met by actions of the Academy or by the passage of time. Other donor restrictions are perpetual in nature, whereby the donor has stipulated the funds be maintained in perpetuity.

Earnings, gains, and losses on donor-restricted net assets are classified as net assets without donor restrictions unless specifically restricted by the donor or by applicable state law.

Revenue

The Academy derives its revenue primarily from membership dues, meetings, *Journal of the American Academy of Dermatology* (JAAD) and other royalties, grants and contributions, and educational product sales. Meetings represent amounts earned for exhibit booth space sales and registration fees for admission and educational seminars. JAAD and other royalties represent amounts earned from the publisher for rights to reproduce, sell, and distribute publications and materials.

Revenue is recognized in the year in which it is earned. Membership dues revenue is recognized over the respective membership periods. Meetings revenue is recognized when the events take place. Educational product sales revenue is recognized when products are shipped. Grant and contribution revenue is recognized when pledged. Deferred revenue represents cash received for registration fees and deposits for meetings and expositions to be held in future periods, membership dues relating to future periods, and advances on royalties.

Note 2 - Significant Accounting Policies (Continued)

Functional Allocation of Expenses

The costs of providing the program and support services have been reported on a natural basis in the combined statement of activities and changes in net assets and on a functional basis in the combined statement of functional expenses. Costs are charged to program services and support services on an actual basis when available. In addition, certain costs have been allocated among the programs and support services functions based on various allocation methods and estimates. Allocations for technology and occupancy are based on each function's personnel headcount as a percentage of the total personnel headcount. Although the methods of allocation used are considered appropriate, other methods could be used that would produce different amounts.

Income Taxes

AAD is a not-for-profit corporation and is exempt from tax under the provisions of Internal Revenue Code Section 501(c)(3). AADA is a not-for-profit corporation and is exempt from tax under the provisions of Internal Revenue Code Section 501(c)(6). Accounting principles generally accepted in the United States of America require management to evaluate tax positions taken by the Academy and recognize a tax liability if the Academy has taken an uncertain position that more likely than not would not be sustained upon examination by the IRS or other applicable taxing authorities.

Use of Estimates

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

Adoption of New Accounting Pronouncement

As of December 31, 2018, the Academy adopted the Financial Accounting Standards Board (FASB) Accounting Standards Update (ASU) No. 2016-14, *Not-for-Profit Entities*. This standard requires net assets to be classified in two categories, net assets without donor restrictions and net assets with donor restrictions, rather than the three previous classifications. This standard also requires changes in the way certain information is aggregated and reported by the Academy, including disclosures of quantitative and qualitative information about the liquidity and availability of resources and the presentation of expenses by both functional and natural classification. The standard also clarifies the definition of management and general and prohibits certain expenses from being allocated out of management and general. As a result of the adoption of this standard, net assets of $8,497,700 previously reported as temporarily restricted net assets and net assets of $2,343,115 previously reported as permanently restricted net assets have been combined into net assets with donor restrictions.

Subsequent Events

The combined financial statements and related disclosures include evaluation of events up through and including May 22, 2019, which is the date the combined financial statements were available to be issued.

Note 2 - Significant Accounting Policies (Continued)

Upcoming Accounting Pronouncements

In May 2014, the FASB issued ASU No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*, which will supersede the current revenue recognition requirements in Topic 605, *Revenue Recognition*. The ASU is based on the principle that revenue is recognized to depict the transfer of goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The ASU also requires additional disclosure about the nature, amount, timing, and uncertainty of revenue and cash flows arising from customer contracts, including significant judgments and changes in judgments and assets recognized from costs incurred to obtain or fulfill a contract. The new guidance will be effective for the Academy's year ending December 31, 2019. The ASU permits application of the new revenue recognition guidance using one of two retrospective application methods: retrospectively to each period presented (full retrospective method) or retrospectively with the cumulative effect of initially applying the recognized at the date of initial application (the cumulative catch-up transition method). The Academy will most likely adopt the cumulative catch-up method if the implementation of the standard does not result in a significant adjustment. The Academy's primary revenue streams are not expected to be significantly impacted by the ASU.

In February 2016, the FASB issued ASU No. 2016-02, *Leases*, which will supersede the current lease requirements in ASC 840. The ASU requires lessees to recognize a right-of-use asset and related lease liability for all leases, with a limited exception for short-term leases. Leases will be classified as either finance or operating, with the classification affecting the pattern of expense recognition in the statement of operations. Currently, leases are classified as either capital or operating, with only capital leases recognized on the statement of net position. The reporting of lease-related expenses in the statements of operations and cash flows will be generally consistent with the current guidance. The new lease guidance will be effective for the Academy's year ending December 31, 2019 and will be applied using a modified retrospective transition method to the beginning of the earliest period presented. The new lease standard is expected to have a significant effect on the Academy’s financial statements as a result of the Academy's operating leases, as disclosed in Note 8, that will be reported on the combined statement of financial position at adoption. Upon adoption, the Academy will recognize a lease liability and corresponding right-to-use asset based on the present value of the minimum lease payments. The effects on the results of operations are not expected to be significant, as recognition and measurement of expenses and cash flows for leases will be substantially the same under the new standard.

In June 2018, the FASB issued ASU No. 2018-08, *Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made*, which provides enhanced guidance to assist entities in (1) evaluating whether transactions should be accounted for as contributions (nonreciprocal transactions) or as exchange (reciprocal transactions) and (2) determining whether a contribution is conditional. The accounting guidance will result in more governmental contracts being accounted for as contributions and may delay revenue recognition for certain grants and contributions that no longer meet the definition of unconditional. The new guidance will be effective for the Academy’s year ending December 31, 2019 and will be applied on a modified prospective basis. The Academy does not expect the standard to have a significant impact on the timing of revenue recognition for government grants and contracts but has not yet determined the impact on the timing of recognition of foundation and individual grants and contributions.

Note 3 - Investments

The cost and related fair values for investments are as follows as of December 31, 2018:

	Cost	Fair Value
AAD:		
Without donor restrictions:		
Money market funds	$ 4,083,730	$ 4,083,730
Corporate stock	1,185,857	1,087,656
Corporate bonds	1,485,278	1,413,934
International bonds	222,805	219,233
Mutual funds	44,571,559	45,028,188
Government and agency bonds	219,163	214,076
Mortgage and asset-backed bonds	396,697	384,877
Total	52,165,089	52,431,694
With donor restrictions:		
Money market funds	69,057	69,057
Corporate bonds	113,296	110,241
International bonds	22,191	22,030
Mutual funds	4,455,917	4,211,296
Government and agency bonds	9,860	9,855
Mortgage and asset-backed bonds	39,155	37,973
Total	4,709,476	4,460,452
Total - AAD	56,874,565	56,892,146
AADA - Without donor restrictions:		
Money market funds	482,455	482,455
Corporate stock	1,191,648	1,095,943
Corporate bonds	3,320,280	3,194,293
International bonds	911,566	897,250
Mutual funds	4,226,230	3,986,881
Government and agency bonds	1,346,524	1,338,569
Mortgage and asset-backed bonds	1,175,759	1,144,446
Total - AADA	12,654,462	12,139,837
Total - Academy	$ 69,529,027	$ 69,031,983

Note 3 - Investments (Continued)

The components of investment income (loss) relating to investments and cash for the year ended December 31, 2018 are as follows:

AAD:	
Without donor restrictions:	
Interest and dividends	$ 1,315,005
Net realized and unrealized losses	(2,731,640)
Investment expense	(125,121)
Total	(1,541,756)
With donor restrictions:	
Interest and dividends	130,433
Net realized and unrealized losses	(388,508)
Investment expense	(13,901)
Total	(271,976)
Total - AAD	(1,813,732)
AADA - Without donor restrictions:	
Interest and dividends	439,081
Net realized and unrealized losses	(916,205)
Investment expense	(63,956)
Total	(541,080)
Total - Academy	$ (2,354,812)

Note 4 - Fair Value Measurements

Accounting standards require certain assets and liabilities be reported at fair value in the financial statements and provide a framework for establishing that fair value. The framework for determining fair value is based on a hierarchy that prioritizes the inputs and valuation techniques used to measure fair value.

The following table presents information about the Academy's assets measured at fair value on a recurring basis at December 31, 2018 and the valuation techniques used by the Academy to determine those fair values.

Fair values determined by Level 1 inputs use quoted prices in active markets for identical assets that the Academy has the ability to access.

Fair values determined by Level 2 inputs use other inputs that are observable, either directly or indirectly. These Level 2 inputs include quoted prices for similar assets in active markets and other inputs, such as interest rates and yield curves, that are observable at commonly quoted intervals.

Level 3 inputs are unobservable inputs, including inputs that are available in situations where there is little, if any, market activity for the related asset or liability. These Level 3 fair value measurements are based primarily on management's own estimates using pricing models, discounted cash flow methodologies, or similar techniques taking into account the characteristics of the asset. The Academy currently does not utilize any Level 3 inputs.

In instances whereby inputs used to measure fair value fall into different levels in the above fair value hierarchy, fair value measurements in their entirety are categorized based on the lowest level input that is significant to the valuation. The Academy's assessment of the significance of particular inputs to these fair value measurements requires judgment and considers factors specific to each asset or liability.

Note 4 - Fair Value Measurements (Continued)

	Assets Measured at Fair Value on a Recurring Basis at December 31, 2018			
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
AAD				
Assets - Investments:				
Fixed income - Mutual funds:				
Short term	$ 9,113,693	$ -	$ -	$ 9,113,693
Intermediate term	23,831,034	-	-	23,831,034
International	605,793	-	-	605,793
Equity - Mutual funds:				
Small cap	1,519,074	-	-	1,519,074
Mid cap	1,869,591	-	-	1,869,591
Large cap	6,675,429	-	-	6,675,429
International	6,712,526	-	-	6,712,526
International bonds:				
Short-term bond funds	191,834	-	-	191,834
Intermediate term	-	49,430	-	49,430
Corporate bonds:				
Short term	-	251,451	-	251,451
Intermediate term	-	1,118,381	-	1,118,381
Long term	-	154,343	-	154,343
Government and agency bonds:				
Short term	-	9,855	-	9,855
Intermediate term	-	214,076	-	214,076
Mortgage and asset-backed bonds:				
Short term	-	5,240	-	5,240
Intermediate term	-	69,342	-	69,342
Long term	-	348,267	-	348,267
Total AAD	50,518,974	2,220,385	-	52,739,359
AADA				
Assets - Investments:				
Fixed income - Mutual funds:				
Short term	49,781	-	-	49,781
Intermediate term	1,259,499	-	-	1,259,499
International	446,398	-	-	446,398
Equity - Mutual funds:				
Small cap	348,230	-	-	348,230
Mid cap	338,957	-	-	338,957
Large cap	1,287,956	-	-	1,287,956
International	1,352,003	-	-	1,352,003
International bonds:				
Short term	637,287	-	-	637,287
Intermediate term	-	259,964	-	259,964
Corporate bonds:				
Short term	-	870,542	-	870,542
Intermediate term	-	2,054,232	-	2,054,232
Long term	-	269,519	-	269,519
Government and agency bonds:				
Short term	-	922,970	-	922,970
Intermediate term	-	415,599	-	415,599
Mortgage and asset-backed bonds:				
Short term	-	126,984	-	126,984
Intermediate term	-	476,287	-	476,287
Long term	-	541,174	-	541,174
Total AADA	5,720,111	5,937,271	-	11,657,382
Total assets	$ 56,239,085	$ 8,157,656	$ -	$ 64,396,741

Not included in the above tables are $4,152,787 in money market accounts as of December 31, 2018 for AAD and $482,455 in money market accounts for AADA.

Level 1 Inputs

Fair values of fixed-income mutual funds, equity mutual funds, and international short-term bond funds were based on quoted market prices.

Note 4 - Fair Value Measurements (Continued)

Level 2 Inputs

Estimated fair values of international intermediate bonds, corporate bonds, government and agency bonds, mortgage and asset-backed bonds, municipal bonds, and education bonds were based on similar investments that are traded on a secondary market.

The Academy's policy is to recognize transfers in and transfers out of Level 1, 2, and 3 fair value classifications as of the actual date of the event of change in circumstances that caused the transfer. During the year ended December 31, 2018, there were no such transfers.

Note 5 - Property and Equipment

Property and equipment are summarized as follows at December 31, 2018:

	AAD	AADA	Combined Total	Depreciable Life - Years
Leasehold improvements	$ 5,403,668	$ 717,852	$ 6,121,520	10
Data processing equipment and system development costs	2,251,077	-	2,251,077	3-8
Furniture and equipment	1,640,196	338,771	1,978,967	5-10
Total cost	9,294,941	1,056,623	10,351,564	
Less accumulated depreciation	2,054,498	902,526	2,957,024	
Net property and equipment	$ 7,240,443	$ 154,097	$ 7,394,540	

Depreciation and amortization expense for 2018 was $1,167,311.

Note 6 - Loan Commitment

Long-term debt at December 31, 2018 is $4,090,909 and consists of a mortgage loan payable with quarterly installments of $102,273, including interest at 3.14 percent through December 31, 2028. The note is collateralized by substantially all of the Academy's assets.

The balance of the debt matures as follows:

Years Ending	Amount
2019	$ 409,091
2020	409,091
2021	409,091
2022	409,091
2023	409,091
Thereafter	2,045,454
Total	$ 4,090,909

Interest expense for 2018 was $137,607.

Note 7 - Net Assets

Net assets without donor restrictions consist of the following as of December 31, 2018:

	AAD	AADA	Total
General Operating Fund	$ 3,452,860	$ 325,588	$ 3,778,448
Area of Greatest Need	137,732	-	137,732
Sulzberger Endowment Fund	367,396	-	367,396
Reserve Income Fund (includes PPE/Tech Fund)	10,786,696	6,971,938	17,758,634
Strategic Reserve Fund	5,210,833	-	5,210,833
Excellence in Dermatology Endowment Fund	11,746,459	-	11,746,459
Camp Discovery Endowment Fund	6,626,410	-	6,626,410
Disaster Fund	34,555	-	34,555
Total	$ 38,362,941	$ 7,297,526	$ 45,660,467

Net assets with donor restrictions as of December 31, 2018 are available for the following purposes:

	AAD	AADA	Total
Subject to expenditures for a specified purpose:			
SKINnovations	$ 190,868	$ -	$ 190,868
Everett C. Fox Fund	893,687	-	893,687
Lila Gruber Endowment Fund - Unappropriated earnings	349,760	-	349,760
Awards for Young Investigators	142,025	-	142,025
World Congress of Dermatology Endowment Fund - Unappropriated earnings	1,497,045	-	1,497,045
Program for Innovative Continuing Medical Education in Dermatology Endowment Fund - Unappropriated earnings	947,411	-	947,411
Camp Discovery Fund	55,331	-	55,331
Lebwohl Camp Scholarship Fund	549,616	-	549,616
Phillip Frost Award	90,000	-	90,000
Annual Meeting*	2,966,750	-	2,966,750
Summer Academy Meeting*	101,250	-	101,250
Access Derm	310,273	-	310,273
Clarence Livingood Award	10,000	-	10,000
D.E.R.M. Program*	400,000	-	400,000
DataDerm Audit	350,000	-	350,000
Derm Pamphlets	55,000	-	55,000
Dermatological Patient Care	188,480	-	188,480
Improving Quality of Life for Patients	199,716	-	199,716
Leadership Programs*	56,500	-	56,500
Quality Innovation Center	50,000	-	50,000
Practice Management Center	-	242,879	242,879
Psoriasis Resource Center	29,170	-	29,170
Skin Care Disease Outreach*	79,201	-	79,201
SPOT ME (Melanoma Exposed)	476,586	-	476,586
Resident Access to Educ Contributions	3,771	-	3,771
Take a Hike*	119,271	-	119,271
Education/Research AYI Contributions	1,000	-	1,000
Shade Structure Contributions	267,440	-	267,440
SPOT Contributions*	67,904	-	67,904
Area of Greatest Need Contributions*	378,132	-	378,132
Total	$ 10,826,187	$ 242,879	$ 11,069,066

*Amounts included in these restrictions are also included in the pledges receivable balance on the combined statement of financial position, and, therefore, are restricted for time and purpose.

Note 8 - Operating Leases

The Academy has the following leases for office space:

Washington, D.C.

In 2009, the Academy entered into an 11-year lease for office space located at 1445 New York Avenue NW in Washington, D.C. with a lease term through November 2020. The monthly rent expense under the lease is $58,850 for the year ended December 31, 2018.

Rosemont, Illinois

The agreement to lease back the Schaumburg facility ended March 12, 2018. In October 2017, the Academy entered into an 11-year lease for its new headquarters located at 9500 West Bryn Mawr Avenue in Rosemont, Illinois with a lease term through May 2029. The first rent payment is due February 1, 2019 in the amount of $62,189.

As part of the Rosemont lease agreement, the landlord provided the Academy with the following:

- Rent abatement of 10 months (April 2018-January 2019). The Academy recognizes rent expense over the term of the lease using the straight-line method.
- Reimbursement for the cost of certain leasehold improvements totaling $2,528,999. The Academy deferred the reimbursement amount as lease incentive and will recognize the reimbursements as reductions in rent expense over the life of the lease.

In addition, the Academy leases various equipment under operating leases with various expiration dates until 2022.

The following is a schedule of future minimum rental payments under operating leases:

Years Ending December 31	Offices	Equipment	Total
2019	$ 1,406,991	$ 133,951	$ 1,540,942
2020	1,444,502	130,707	1,575,209
2021	804,121	107,011	911,132
2022	826,234	19,882	846,116
2023	848,955	-	848,955
Thereafter	5,020,413	-	5,020,413
Total	$ 10,351,216	$ 391,551	$ 10,742,767

Total rent expense under all operating leases was $913,585 for the year ended December 31, 2018.

Note 9 - Employee Benefit Plans

Defined Contribution Plan

The Academy sponsors a defined contribution pension plan (401(a)) for all eligible employees. Employer contributions to the plan were $826,403 for the year ended December 31, 2018.

The Academy also sponsors a deferred salary plan with employer matching contributions (403(b)) for all eligible employees. Employer matching contributions to the plan totaled $965,500 for the year ended December 31, 2018.

Note 9 - Employee Benefit Plans (Continued)

Deferred Compensation Plans

The Academy has a 457(b) deferred compensation plan. According to the 457(b) plan, the participants are eligible to make salary reduction contributions.

Effective January 1, 2017, the Academy adopted a 457(f) deferred compensation plan. The amount is maintained on the Academy's books in a designated account, will remain the sole property of the Academy, and is available to satisfy the claims of all general creditors of the Academy. The executive director shall have a fully vested, nonforfeitable interest in her deferred compensation if she (1) continues her employment with the Academy until December 31, 2021, (2) dies, (3) is involuntarily terminated due to disability, or (4) is terminated from employment for reasons other than cause. Pursuant to the amended and restated employment agreement dated June 3, 2016, the executive director will receive a lump-sum distribution from her 457(f) plan account in an amount equal to her accrued balance through December 31, 2021. With respect to the 457(f) plan, the Academy recorded contributions of $22,064 for the year ended December 31, 2018, which are included in accrued retirement costs on the combined statement of financial position.

On an annual basis, the Academy will make a contribution equal to 7 percent of the executive director's annual base salary to her 457(b) and 457(f) plans, whereby the contribution will first go to the 457(b) plan until the IRS maximum amount is reached and the remaining balance will be contributed to the 457(f) plan.

Effective April 5, 2019, the executive director resigned from the Academy and has, under the terms of the 457(f) plan, forfeited her accrued balance of approximately $39,000 as of that date.

Note 10 - Donor-restricted and Board-designated Endowments

The Academy's endowment includes both donor-restricted endowment funds and funds designated by the board of trustees to function as endowments. Net assets associated with endowment funds, including funds designated by the board of trustees to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions.

Interpretation of Relevant Law

The Academy is subject to the State Prudent Management of Institutional Funds Act (SPMIFA) and, thus, classifies amounts in its donor-restricted endowment funds as net assets with donor restrictions because those net assets are time restricted until the board of trustees appropriates such amounts for expenditures. Most of those net assets also are subject to purpose restrictions that must be met before reclassifying those net assets to net assets without donor restrictions. The board of trustees of the Academy had interpreted SPMIFA as not requiring the maintenance of purchasing power of the original gift amount contributed to an endowment fund, unless a donor stipulates the contrary. As a result of this interpretation, when reviewing its donor-restricted endowment funds, the Academy considers a fund to be underwater if the fair value of the fund is less than the sum of (a) the original value of initial and subsequent gift amounts donated to the fund and (b) any accumulations to the fund that are required to be maintained in perpetuity in accordance with the direction of the applicable donor gift instrument. The Academy has interpreted SPMIFA to permit spending from underwater funds in accordance with the prudent measures required under the law. Additionally, in accordance with SPMIFA, the Academy considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

- The duration and preservation of the fund
- The purpose of the Academy and the donor-restricted endowment fund

Note 10 - Donor-restricted and Board-designated Endowments (Continued)

- General economic conditions
- The possible effect of inflation and deflation
- The expected total return from income and the appreciation of investments
- Other resources of the Academy
- The investment policies of the Academy

	Endowment Net Asset Composition by Type of Fund as of December 31, 2018		
	Without Donor Restrictions	With Donor Restrictions	Total
Board-designated endowment funds	$ 18,740,265	$ -	$ 18,740,265
Donor-restricted endowment fundsAssets - Investments:	-	2,936,239	2,936,239
Total	$ 18,740,265	$ 2,936,239	$ 21,676,504

	Changes in Endowment Net Assets for the Fiscal Year Ended December 31, 2018		
	Without Donor Restrictions	With Donor Restrictions	Total
Endowment net assets - Beginning of year	$ 19,866,345	$ 3,184,667	$ 23,051,012
Investment return:			
Investment income	512,778	85,032	597,810
Net depreciation (realized and unrealized)	(1,634,858)	(274,200)	(1,909,058)
Total investment return	(1,122,080)	(189,168)	(1,311,248)
Contributions	-	33,009	33,009
Appropriation of endowment assets for expenditure	(5,000)	(92,269)	(97,269)
Other changes - Transfers to create board-designated endowment funds	1,000	-	1,000
Endowment net assets - End of year	$ 18,740,265	$ 2,936,239	$ 21,676,504

Underwater Endowment Funds

As of December 31, 2018, there were no funds with deficiencies.

Note 10 - Donor-restricted and Board-designated Endowments (Continued)

Return Objectives and Risk Parameters

The Academy has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the Academy must hold in perpetuity or for a donor-specified period, as well as board-designated funds. Under this policy, as approved by the board of directors, the endowment assets are invested in a manner that is intended to produce results that exceed the price and yield results of the respective benchmarks for the different asset classes provided for in the Academy's investment policy. The asset classes include cash, fixed income, equities, stocks, large-cap stocks and options, mid-cap stocks and options, small-cap stocks and options, and foreign stocks and options. The Academy expects its endowment funds, over time, to provide an average rate of return equal to or greater than benchmarks associated with each of its three investment policies. Actual returns in any given year may vary from this amount; the investment committee reviews actual returns versus benchmarks for all funds.

Strategies Employed for Achieving Objectives

To satisfy its long-term rate-of-return objectives, the Academy 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 Academy targets a diversified asset allocation that places a greater emphasis on prudent risk constraints, balancing equity-based investments with fixed-income investments to achieve its long-term return objectives.

Spending Policy and How the Investment Objectives Relate to Spending Policy

During the budgeting process, the Academy has a policy of reviewing each endowment fund's budgeted expenditures and compares these expenditures to the endowment fund's investment returns for the current year. In establishing this policy, the Academy considered the long-term expected rate of return on its endowment. Accordingly, over the long term, the Academy expects the current spending policy to be below the current market investment returns for its endowment. This is consistent with the Academy’s objective to maintain the purchasing power of the endowment assets held in perpetuity or for a specified term, as well as to provide additional real growth through new gifts and investment return.

Note 11 - Journal of the American Academy of Dermatology

The Academy has a copyright license agreement with a publisher for reproduction, sale, and distribution of *Journal of the American Academy of Dermatology*. On December 20, 2016, the Academy entered into a new agreement that began on January 1, 2018 and will expire on December 31, 2022.

Note 12 - Liquidity

The following reflects the Academy's financial assets as of December 31, 2018, reduced by amounts not available for general use because of contractual or donor-imposed restrictions within one year of the statement of financial position date.

Note 12 - Liquidity (Continued)

Cash and investments	$ 74,624,792
Accounts and interest receivable	5,132,946
Financial assets - At year end	79,757,738
Less those unavailable for general expenditures within one year due to - Contractual or donor-imposed restrictions:	
Assets restricted by program	15,197,725
Restricted by donor with time or purpose restrictions	6,443,324
Rosemont facility loan	4,090,909
Financial assets available to meet cash needs for general expenditures within one year	$ 54,025,780

The Academy is partially supported by restricted contributions. Because a donor's restriction requires resources to be used in a particular manner or in a future period, the Academy must maintain sufficient resources to meet those responsibilities to its donors. Thus, financial assets may not be available for general expenditure within one year. As part of the Academy's liquidity management, it structures its financial assets to be available as its general expenditures, liabilities, and other obligations come due. In addition, the Academy invests cash in excess of daily requirements in short-term investments.

Additional Information

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Independent Auditor's Report on Additional Information

To the Board of Directors
American Academy of Dermatology, Inc.
and American Academy of
Dermatology Association, Inc.

We have audited the combined financial statements of American Academy of Dermatology, Inc. and American Academy of Dermatology Association, Inc. as of and for the years ended December 31, 2018 and have issued our report thereon dated May 22, 2019, which contained an unmodified opinion on those combined financial statements. Our audits were performed for the purpose of forming an opinion on the 2018 combined financial statements as a whole. The combining information is presented for the purpose of additional analysis rather than to present the financial position, changes in net assets, and cash flows of the individual companies and is not a required part of the combined 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 combined financial statements. The information has been subjected to the auditing procedures applied in the audit of the 2018 combined financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the combined financial statements or to the combined 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 combined financial statements as a whole.

Plante & Moran, PLLC

May 22, 2019

Combining Statement of Financial Position

December 31, 2018

	AAD	AADA	Eliminating Entries	Total
Assets				
Cash	$ 4,836,482	$ 756,325	$ -	$ 5,592,807
Investments	56,892,145	12,139,838	-	69,031,983
Receivables - Net of allowances:				
Trade receivables	2,873,609	270,805	-	3,144,414
Pledges receivable	2,011,715	-	-	2,011,715
Due from related organizations	7,945,631	4,169,986	(12,115,617)	-
Inventory - Net	163,212	-	-	163,212
Prepaid expenses and other assets	1,862,820	368,954	-	2,231,774
Property and equipment - Net	7,240,443	154,097	-	7,394,540
Total assets	**$ 83,826,057**	**$ 17,860,005**	**$ (12,115,617)**	**$ 89,570,445**
Liabilities and Net Assets				
Liabilities				
Accounts payable and other	$ 1,446,024	$ 62,115	$ -	$ 1,508,139
Accrued retirement costs	963,253	-	-	963,253
Accrued salaries	1,386,070	-	-	1,386,070
Accrued vacation leave	637,010	-	-	637,010
Deferred revenue - Annual national meeting	11,487,162	-	-	11,487,162
Deferred revenue - Subscriptions and other	5,045,766	390,282	-	5,436,048
Due to related organizations	9,580,735	2,534,882	(12,115,617)	-
Deferred revenue - Membership dues	-	7,332,321	-	7,332,321
Loan commitment	4,090,909	-	-	4,090,909
Total liabilities	34,636,929	10,319,600	(12,115,617)	32,840,912
Net Assets				
Net assets without donor restrictions	38,362,941	7,297,526	-	45,660,467
Net assets with donor restrictions	10,826,187	242,879	-	11,069,066
Total net assets	49,189,128	7,540,405	-	56,729,533
Total liabilities and net assets	**$ 83,826,057**	**$ 17,860,005**	**$ (12,115,617)**	**$ 89,570,445**

Combining Statement of Activities

Year Ended December 31, 2018

	AAD	AADA	Eliminating Entries	Total
Changes in Net Assets without Donor Restrictions				
Revenue, gains, and other support:				
Membership dues	$ -	$ 10,678,195	$ -	$ 10,678,195
Meetings	20,425,876	92,718	-	20,518,594
JAAD and other royalties	6,098,863	1,107,349	-	7,206,212
Educational product sales	2,586,485	447,786	-	3,034,271
Other	123,978	115,859	-	239,837
Grants and contributions	617,266	47,964	-	665,230
Investment loss	(1,541,756)	(541,080)	-	(2,082,836)
Net assets released from restrictions	6,149,966	157,119	-	6,307,085
Total revenue, gains, other support, and net assets released from restrictions	34,460,678	12,105,910	-	46,566,588
Expenses:				
Program services:				
Educational	16,353,976	1,236,721	-	17,590,697
Communications	3,834,756	1,149,706	-	4,984,462
Government affairs and research	3,767,445	6,105,935	-	9,873,380
Constituent relations	1,563,615	475,952	-	2,039,567
Member services and administration	9,101,826	4,430,878	-	13,532,704
Fundraising	1,328,067	74,991	-	1,403,058
Total expenses	35,949,685	13,474,183	-	49,423,868
Decrease in Net Assets without Donor Restrictions	(1,489,007)	(1,368,273)	-	(2,857,280)
Changes in Net Assets with Donor Restrictions				
Grants and contributions	6,657,312	150,000	-	6,807,312
Investment loss	(271,976)	-	-	(271,976)
Net assets released from restrictions	(6,149,966)	(157,119)	-	(6,307,085)
Increase (Decrease) in Net Assets with Donor Restrictions	235,370	(7,119)	-	228,251
Decrease in Net Assets	**$ (1,253,637)**	**$ (1,375,392)**	**$ -**	**$ (2,629,029)**