

LUPUS RESEARCH ALLIANCE, INC. AND SUBSIDIARY

CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2019 AND 2018



LUTZ AND GARR

CERTIFIED PUBLIC ACCOUNTANTS, LLP

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INDEPENDENT AUDITORS' REPORT

To the Board of Directors of
Lupus Research Alliance, Inc.

We have audited the accompanying consolidated financial statements of Lupus Research Alliance, Inc. (a nonprofit corporation) and Subsidiary, which comprise the consolidated statements of financial position as of December 31, 2019 and 2018, and the related consolidated statements of activities, functional expenses and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in 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 consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement.

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

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Lupus Research Alliance, Inc. and Subsidiary as of December 31, 2019 and 2018, and the changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Lotz + Carr, LLP

New York, New York
September 11, 2020

LUPUS RESEARCH ALLIANCE, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

DECEMBER 31, 2019 AND 2018

	<u>2019</u>	<u>2018</u>
Assets		
Cash and cash equivalents (Notes 2b and 5)	\$ 4,598,465	\$ 5,206,980
Investments (Notes 2c, 2d and 6)	62,118,380	53,584,534
Unconditional promises to give (Notes 2e and 8)	2,579,649	4,778,785
Accounts receivable	373,770	157,680
Prepaid expenses and other current assets	162,892	168,860
Land and building held for resale (Note 11)	493,500	-
Property and equipment, at cost, net of accumulated depreciation (Notes 2f and 9)	494,479	573,771
Security deposit	610,583	609,345
	<u>610,583</u>	<u>609,345</u>
Total Assets	<u><u>\$71,431,718</u></u>	<u><u>\$65,079,955</u></u>
Liabilities and Net Assets		
Liabilities		
Accounts payable and other current liabilities	\$ 438,885	\$ 465,895
Research grants payable (Notes 2i and 10)	25,422,502	22,572,203
Deferred rent liability (Note 2j)	800,130	780,561
Total Liabilities	<u>26,661,517</u>	<u>23,818,659</u>
Commitments (Notes 12, 13 and 15)		
Net Assets		
Without donor restrictions (Note 4a)	39,293,680	36,803,806
With donor restrictions (Note 4b)	5,476,521	4,457,490
Total Net Assets	<u>44,770,201</u>	<u>41,261,296</u>
Total Liabilities and Net Assets	<u><u>\$71,431,718</u></u>	<u><u>\$65,079,955</u></u>

See notes to consolidated financial statements.

LUPUS RESEARCH ALLIANCE, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF ACTIVITIES

YEARS ENDED DECEMBER 31, 2019 AND 2018

	2019			2018		
	Without Donor Restrictions	With Donor Restrictions	Total	Without Donor Restrictions	With Donor Restrictions	Total
Changes in Net Assets						
Revenue and Other Support						
Contributions (Notes 1 and 2e)	\$ 7,279,254	\$ 4,645,830	\$11,925,084	\$ 8,341,106	\$ 720,748	\$ 9,061,854
Pledge reduction	-	(100,000)	(100,000)	-	-	-
Special events income	4,509,497	-	4,509,497	5,270,865	-	5,270,865
Less: Expenses directly benefiting contributors	(486,194)	-	(486,194)	(500,138)	-	(500,138)
Walkathon income	1,361,711	-	1,361,711	1,603,816	-	1,603,816
Less: Expenses directly benefiting contributors	(29,976)	-	(29,976)	(39,862)	-	(39,862)
Donated land and property held for resale (Note 11)	493,500	-	493,500	-	-	-
LuCIN consulting revenue (Note 2h)	1,236,449	-	1,236,449	1,334,475	-	1,334,475
Net investment income (loss) for operations (Note 6)	1,467,354	-	1,467,354	(401,511)	-	(401,511)
Board designated endowment spending policy withdrawals (Notes 4a and 7)	2,713,456	-	2,713,456	2,683,279	-	2,683,279
	<u>18,545,051</u>	<u>4,545,830</u>	<u>23,090,881</u>	<u>18,292,030</u>	<u>720,748</u>	<u>19,012,778</u>
Net assets released from restrictions						
Satisfaction of program restrictions	3,526,799	(3,526,799)	-	5,645,511	(5,645,511)	-
	<u>22,071,850</u>	<u>1,019,031</u>	<u>23,090,881</u>	<u>23,937,541</u>	<u>(4,924,763)</u>	<u>19,012,778</u>
Expenses						
Program Services						
Research	11,771,155	-	11,771,155	9,608,831	-	9,608,831
Scientific programs	8,746,496	-	8,746,496	7,064,789	-	7,064,789
Public policy	846,235	-	846,235	788,377	-	788,377
Total Program Services	<u>21,363,886</u>	<u>-</u>	<u>21,363,886</u>	<u>17,461,997</u>	<u>-</u>	<u>17,461,997</u>
Supporting Services						
Administration	2,129,277	-	2,129,277	1,973,754	-	1,973,754
Fundraising	3,029,588	-	3,029,588	3,179,907	-	3,179,907
Total Supporting Services	<u>5,158,865</u>	<u>-</u>	<u>5,158,865</u>	<u>5,153,661</u>	<u>-</u>	<u>5,153,661</u>
Total Expenses	<u>26,522,751</u>	<u>-</u>	<u>26,522,751</u>	<u>22,615,658</u>	<u>-</u>	<u>22,615,658</u>
Increase (Decrease) in Net Assets Before Items Below	(4,450,901)	1,019,031	(3,431,870)	1,321,883	(4,924,763)	(3,602,880)
Non-Operating Activities						
Net investment income (loss) (Note 6)	8,404,231	-	8,404,231	(2,936,193)	-	(2,936,193)
Board designated endowment spending policy withdrawals (Notes 4a and 7)	(2,713,456)	-	(2,713,456)	(2,683,279)	-	(2,683,279)
Grants cancelled (Note 10)	1,250,000	-	1,250,000	-	-	-
Increase (decrease) in net assets	2,489,874	1,019,031	3,508,905	(4,297,589)	(4,924,763)	(9,222,352)
Net assets, beginning of year	<u>36,803,806</u>	<u>4,457,490</u>	<u>41,261,296</u>	<u>41,101,395</u>	<u>9,382,253</u>	<u>50,483,648</u>
Net Assets, End of Year	<u>\$39,293,680</u>	<u>\$ 5,476,521</u>	<u>\$44,770,201</u>	<u>\$36,803,806</u>	<u>\$ 4,457,490</u>	<u>\$41,261,296</u>

See notes to consolidated financial statements.

LUPUS RESEARCH ALLIANCE, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENT OF FUNCTIONAL EXPENSES

YEAR ENDED DECEMBER 31, 2019 WITH COMPARATIVE TOTALS FOR 2018

	2019							2018	
	Program Services				Supporting Services			Total Expenses	Total Expenses
	Research	Scientific Programs	Public Policy	Total	Administration	Fundraising	Total		
Salaries	\$ 359,061	\$1,084,035	\$315,373	\$ 1,758,469	\$ 900,005	\$ 1,286,467	\$2,186,472	\$ 3,944,941	\$ 3,761,875
Payroll taxes and fringe benefits	111,770	337,442	98,170	547,382	280,155	400,457	680,612	1,227,994	1,126,126
Total Personnel Expenses	470,831	1,421,477	413,543	2,305,851	1,180,160	1,686,924	2,867,084	5,172,935	4,888,001
Peer reviewed research awards	10,872,939	-	-	10,872,939	-	-	-	10,872,939	8,646,136
LuCIN Grants	-	4,465,282	-	4,465,282	-	-	-	4,465,282	2,520,000
Clinical studies	-	512,086	-	512,086	-	-	-	512,086	845,312
Lupus emergency grant	-	-	1,828	1,828	-	-	-	1,828	-
Professional fees and contract services	123,000	806,270	104,186	1,033,456	161,572	229,591	391,163	1,424,619	1,483,462
Occupancy	88,276	384,033	77,535	549,844	221,269	316,282	537,551	1,087,395	1,073,165
Printing and publications	20,111	27,762	900	48,773	27,194	153,809	181,003	229,776	227,785
Staff and volunteer travel	26,490	224,709	41,447	292,646	47,496	100,305	147,801	440,447	456,787
Meetings and conferences	40,771	568,088	142,363	751,222	62,651	15,858	78,509	829,731	992,443
Walkathon promotional events and location expenses	-	-	-	-	-	216,339	216,339	216,339	245,802
Postage, shipping and delivery	1,121	17,455	853	19,429	11,151	63,003	74,154	93,583	83,454
Management information systems	72,489	149,699	33,645	255,833	198,927	59,810	258,737	514,570	412,265
Supplies	156	15,176	322	15,654	43,637	1,913	45,550	61,204	76,295
Data processing and accounting services	26,507	490	334	27,331	84,325	60,594	144,919	172,250	158,848
Branding and design	750	32,555	2,575	35,880	14,933	20,025	34,958	70,838	121,770
Telephone	4,264	19,728	3,693	27,685	10,487	16,191	26,678	54,363	88,930
Insurance	4,082	31,350	3,586	39,018	10,233	14,626	24,859	63,877	59,554
Licenses	975	2,943	856	4,774	2,444	3,493	5,937	10,711	13,346
Equipment lease	2,726	8,230	2,394	13,350	6,833	9,766	16,599	29,949	35,813
Professional development	-	-	-	-	4,755	692	5,447	5,447	9,617
Dues and subscriptions and other expenses	-	11,864	2,415	14,279	1,941	4,237	6,178	20,457	12,080
Total expenses before depreciation	11,755,488	8,699,197	832,475	21,287,160	2,090,008	2,973,458	5,063,466	26,350,626	22,450,865
Depreciation	15,667	47,299	13,760	76,726	39,269	56,130	95,399	172,125	164,793
Total Expenses, 2019	<u>\$11,771,155</u>	<u>\$8,746,496</u>	<u>\$846,235</u>	<u>\$21,363,886</u>	<u>\$ 2,129,277</u>	<u>\$ 3,029,588</u>	<u>\$5,158,865</u>	<u>\$26,522,751</u>	
Total Expenses, 2018	<u>\$ 9,608,831</u>	<u>\$7,064,789</u>	<u>\$788,377</u>	<u>\$17,461,997</u>	<u>\$ 1,973,754</u>	<u>\$ 3,179,907</u>	<u>\$5,153,661</u>		<u>\$22,615,658</u>

See notes to consolidated financial statements.

LUPUS RESEARCH ALLIANCE, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENT OF FUNCTIONAL EXPENSES
YEAR ENDED DECEMBER 31, 2018

	Program Services			Supporting Services			Total Expenses	
	Research	Scientific Programs	Public Policy	Total	Administration	Fundraising		Total
Salaries	\$ 378,189	\$1,045,433	\$283,168	\$ 1,706,790	\$ 808,913	\$ 1,246,172	\$2,055,085	\$ 3,761,875
Payroll taxes and fringe benefits	113,212	312,952	84,767	510,931	242,151	373,044	615,195	1,126,126
Total Personnel Expenses	491,401	1,358,385	367,935	2,217,721	1,051,064	1,619,216	2,670,280	4,888,001
Peer reviewed research awards	8,646,136	-	-	8,646,136	-	-	-	8,646,136
LuCIN Grants	-	2,520,000	-	2,520,000	-	-	-	2,520,000
Clinical studies	-	845,312	-	845,312	-	-	-	845,312
Professional fees and contract services	128,139	631,224	99,718	859,081	208,602	415,779	624,381	1,483,462
Occupancy	95,972	383,817	71,859	551,648	205,278	316,239	521,517	1,073,165
Printing and publications	27,743	23,492	2,459	53,694	52,387	121,704	174,091	227,785
Staff and volunteer travel	22,738	208,007	50,200	280,945	45,385	130,457	175,842	456,787
Meetings and conferences	66,768	722,874	133,755	923,397	49,730	19,316	69,046	992,443
Walkathon promotional events and location expenses	-	-	-	-	-	245,802	245,802	245,802
Postage, shipping and delivery	1,382	16,016	1,991	19,389	15,738	48,327	64,065	83,454
Management information systems	63,211	124,354	28,942	216,507	113,080	82,678	195,758	412,265
Supplies	871	32,252	951	34,074	32,760	9,461	42,221	76,295
Data processing and accounting services	25,183	-	407	25,590	87,024	46,234	133,258	158,848
Branding and design	8,750	55,701	1,841	66,292	34,701	20,777	55,478	121,770
Telephone	4,438	56,210	3,545	64,193	9,224	15,513	24,737	88,930
Insurance	4,565	26,763	3,418	34,746	9,765	15,043	24,808	59,554
Licenses	1,342	3,709	1,005	6,056	2,869	4,421	7,290	13,346
Equipment lease	3,600	9,952	2,696	16,248	7,702	11,863	19,565	35,813
Professional development	-	-	1,000	1,000	6,597	2,020	8,617	9,617
Dues and subscriptions and other expenses	25	925	4,250	5,200	6,413	467	6,880	12,080
Total expenses before depreciation	9,592,264	7,018,993	775,972	17,387,229	1,938,319	3,125,317	5,063,636	22,450,865
Depreciation	16,567	45,796	12,405	74,768	35,435	54,590	90,025	164,793
Total Expenses	\$9,608,831	\$7,064,789	\$788,377	\$17,461,997	\$ 1,973,754	\$ 3,179,907	\$5,153,661	\$22,615,658

See notes to consolidated financial statements.

LUPUS RESEARCH ALLIANCE, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CASH FLOWS

YEARS ENDED DECEMBER 31, 2019 AND 2018

	<u>2019</u>	<u>2018</u>
Cash Flows From Operating Activities		
Increase (decrease) in net assets	\$3,508,905	\$(9,222,352)
Adjustments to reconcile change in net assets to net cash used by operating activities:		
Depreciation	172,125	164,793
Realized gain on sale of investments	(702,675)	(960,183)
Unrealized (gain) loss on investments	(7,845,756)	5,510,895
Donated property held for resale	(493,500)	-
(Increase) decrease in:		
Unconditional promises to give	2,199,136	6,298,741
Accounts receivable	(216,090)	(157,680)
Prepaid expenses and other current assets	5,968	28,767
Security deposit	(1,238)	-
Increase (decrease) in:		
Accounts payable and other current liabilities	(27,010)	(38,036)
Research grants payable	2,850,299	(2,736,252)
Deferred rent	19,569	70,621
Net Cash Used By Operating Activities	<u>(530,267)</u>	<u>(1,040,686)</u>
Cash Flows From Investing Activities		
Acquisition of property and equipment	(92,833)	(56,700)
Purchase of investments	(9,507,895)	(9,813,629)
Proceeds from sale of investments	9,522,480	11,329,110
Net Cash Provided (Used) By Investing Activities	<u>(78,248)</u>	<u>1,458,781</u>
Net increase (decrease) in cash and cash equivalents	(608,515)	418,095
Cash and cash equivalents, beginning of year	<u>5,206,980</u>	<u>4,788,885</u>
Cash and Cash Equivalents, End of Year	<u><u>\$4,598,465</u></u>	<u><u>\$ 5,206,980</u></u>

See notes to consolidated financial statements.

LUPUS RESEARCH ALLIANCE, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2019 AND 2018

Note 1 - Organization

Lupus Research Alliance, Inc. (the "Alliance") is a national voluntary 501(c)(3) health organization based in New York City. The Alliance is a Delaware nonprofit corporation. The mission of the Alliance is to find better treatments and ultimately prevent and cure systemic lupus erythematosus (SLE or lupus), a debilitating autoimmune disease, by supporting medical research. Lupus is a chronic autoimmune disease that causes inflammation and tissue damage to any organ system in the body. The health effects of lupus include heart attacks, strokes, seizures, organ failure, and possible death. More information can be found at lupusresearch.org. Since its founding, the Alliance has committed approximately \$203 million to fund lupus research projects. All supporting services are funded by contributions from the Board of Directors. One hundred percent (100%) of all other donations to the Alliance are available to support lupus research programs.

On January 5, 2018, Lupus Therapeutics, LLC (the "LLC"), a single member limited liability company, was formed with the Alliance as its sole member. The LLC was formed to conduct clinical trial studies.

During the year ended December 31, 2019, the Alliance received approximately 34% of its contributions from one corporation and one trust and during the year ended December 31, 2018, approximately 18% of its contributions from one trust.

Note 2 - Summary of Significant Accounting Policies

a - Principles of Consolidation

The consolidated financial statements include the accounts of the Alliance and its subsidiary, LLC. All significant intercompany transactions and accounts have been eliminated in consolidation.

b - Cash and Cash Equivalents

For purposes of the statement of cash flows, the Alliance considers all short-term investments to be cash equivalents, except for those short-term investments managed by the Alliance's investment managers as part of their long-term investment strategies.

At December 31, 2019 and 2018, included in cash and cash equivalents is approximately \$874,000 and \$1,121,000, respectively, being held in interest-bearing accounts.

LUPUS RESEARCH ALLIANCE, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2019 AND 2018

Note 2 - Summary of Significant Accounting Policies (continued)

c - Investments

The Alliance reflects investments at fair value in the statement of financial position. Investment income including unrealized gains and losses on investments are reflected in the statement of activities as increases and decreases in net assets without donor restrictions unless their use is restricted by explicit donor stipulations or by law.

Alternative investments, which do not have readily determinable fair values, are reported based upon the underlying net asset value per share or its equivalent as a practical expedient. Net asset value per share is estimated at fair value by the fund manager or general partner in a manner consistent with accounting principles generally accepted in the United States for investment companies. The Alliance reviews and evaluates the values provided by the fund managers and general partners and agrees with the valuation methods and assumptions used in determining the net asset values of these investments. These estimated fair values may differ significantly from the values that would have been used had a ready market for these investments existed.

d - Fair Value Measurements

Fair value is an estimate of the exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants (i.e., the exit price at the measurement date). Fair value measurements are not adjusted for transaction costs. Fair value hierarchy prioritizes inputs to valuation techniques used to measure fair value into three levels.

Unadjusted quoted prices in active markets for identical assets and liabilities are referred to as Level 1 inputs. Inputs other than quoted market prices that are observable, either directly or indirectly and reasonably available are referred to as Level 2 inputs. Observable inputs reflect the assumptions market participants would use in pricing the asset or liability and are developed based on market data obtained from sources independent of the Alliance. Unobservable inputs reflect the assumptions that the Alliance develops based on available information about what market participants would use in valuing the asset or liability and are referred to as Level 3 inputs.

An asset or liability's level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Availability of observable inputs can vary and is affected by a variety of factors.

LUPUS RESEARCH ALLIANCE, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2019 AND 2018

Note 2 - Summary of Significant Accounting Policies (continued)

e - Unconditional Promises to Give and Contributions

Contributions are recognized when the donor makes a promise to give to the Alliance, that is, in substance, unconditional. Contributions that are restricted by the donor are reported as increases in net assets without donor restrictions if the restrictions expire in the fiscal year in which the contributions are recognized. All other donor-restricted contributions are reported as increases in net assets with donor restrictions depending on the nature of the restrictions. When a restriction expires, net assets with donor restrictions are reclassified to net assets without donor restrictions. The Alliance uses the allowance method to determine uncollectible promises to give. Such allowance, when necessary, is based on prior years' experience and management's analysis of specific promises made.

The contribution of donated property held for resale (Note 11) was recorded at fair value (less the estimated costs to sell the property) on the date that the Alliance assumed legal ownership of the property.

f - Property and Equipment

Property, equipment, and leasehold improvements are recorded at cost. Depreciation is provided on a straight-line basis over the estimated useful lives of the related assets.

g - Financial Statement Presentation

The financial statements of the have been prepared in accordance with U.S. generally accepting accounting principles, which require the Alliance to report information regarding its financial position and activities according to the following net asset classifications:

Net Assets Without Donor Restrictions

Net assets that are not subject to donor-imposed restrictions and may be expended for any purpose in performing the primary objectives of the Alliance. These net assets may be used at the discretion of the Alliance's management and the Board of Directors.

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 Alliance or the passage of time. Other donor restrictions are perpetual in nature, whereby the donor has stipulated the funds be maintained in perpetuity.

LUPUS RESEARCH ALLIANCE, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2019 AND 2018

Note 2 - Summary of Significant Accounting Policies (continued)

h - Revenue Recognition

Revenue from consulting is recognized when the services take place.

i - Grants Awarded

Unconditional grants awarded are recognized as expenses at fair value in the period the award is made.

j - Deferred Rent Liability

The Alliance records rent expense associated with its office leases on a straight-line basis over the life of the leases (Note 12a). The difference between the straight-line amount and the amount actually paid during the year is recorded as a liability and an expense in the accompanying financial statements.

k - Functional Allocation of Expenses

The cost of providing the various programs and supporting services has been summarized on a functional basis in the statement of activities. The Alliance's primary programming areas are categorized as Research, Scientific Programs and Public Policy. Accordingly, certain costs have been allocated among the programs and the supporting services benefited. Expenses are allocated directly to programs, where applicable, on a reasonable and consistent basis. A substantial portion of the Alliance's expenses are directly related to program activities. Certain other expenses are attributable to more than one program or supporting function and require allocation. The expenses that are allocated include salaries, payroll taxes and benefits, which are allocated on the basis of estimates of employee time and effort, while occupancy, telephone, insurance, licenses, equipment lease, and depreciation are allocated on overall salary percentages.

l - Estimates

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

m - Tax Status

Lupus Research Alliance, Inc. is a not-for-profit corporation that is exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code and has been designated as an organization which is not a private foundation.

LUPUS RESEARCH ALLIANCE, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2019 AND 2018

Note 2 - Summary of Significant Accounting Policies (continued)

n - Subsequent Events

The Alliance has evaluated subsequent events through September 11, 2020, the date that the financial statements are considered available to be issued.

o - Recent Accounting Pronouncement

In February 2016, the FASB issued ASU 2016-02, "*Leases (Topic 842)*". The core principles of ASU 2016-02 change the way organizations will account for their leases by recognizing lease assets and related liabilities on the statement of financial position for all leases with terms longer than 12 months and disclosing key information about leasing arrangements. ASU 2016-02 is effective for fiscal years beginning after December 15, 2021. The Alliance is currently evaluating the impact of ASU 2016-02 on its financial statements.

Note 3 - Information Regarding Liquidity and Availability

The Alliance operates with a balanced budget for each fiscal year based on the revenue expected to be available to fund anticipated expenses. A substantial portion of annual revenue is comprised of contribution revenue raised during the current year. The Alliance considers general expenditures to consist of all expenses related to its ongoing program activities, and the expenses related to administrative and fundraising activities undertaken to support those services.

The Alliance regularly monitors liquidity to meet its operating needs and other commitments and obligations, while seeking to maximize the investment of its available funds. Management prepares regular cash flow projections to determine liquidity needs and has a policy to maintain liquid financial assets on an ongoing basis sufficient to cover ninety days of general expenditures.

LUPUS RESEARCH ALLIANCE, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2019 AND 2018

Note 3 - Information Regarding Liquidity and Availability

The Alliance's financial assets as of December 31, 2019 and 2018 that are available within one year to meet cash needs for general expenditures are summarized as follows:

	<u>2019</u>	<u>2018</u>
Financial Assets at Year End:		
Cash and cash equivalents	\$ 4,598,465	\$ 5,206,980
Investments	62,118,380	53,584,534
Unconditional promises to give	2,579,649	4,778,785
Accounts receivable	<u>373,770</u>	<u>157,680</u>
Total Financial Assets	69,670,264	63,727,979
Less: Amounts not Available to be Used within One Year:		
Net assets with donor restrictions, subject to expenditure for specific purposes or passage of time	(5,476,521)	(4,457,490)
Plus: Net assets with donor restrictions expected to be met within one year	2,745,159	3,330,859
Net assets restricted by Board, subject to spending policy and appropriation	(51,813,700)	(46,122,925)
Plus: Amount appropriated in the budget for use within one year	<u>2,835,293</u>	<u>2,735,923</u>
Financial Assets Available to Meet General Expenditures within One Year	<u>\$17,960,495</u>	<u>\$19,214,346</u>

In addition to these financial assets available within one year at December 31, 2019, the Alliance has board designated endowment funds not appropriated for use within one year of approximately \$48,912,000, which are invested for long-term appreciation and current income. However, these funds could be made available at any time to meet cash needs for general expenditures at the discretion of the Board.

LUPUS RESEARCH ALLIANCE, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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Note 4 - Net Assets

a - Net Assets Without Donor Restrictions

Net assets without donor restrictions at December 31, 2019 and 2018 consist of the following:

	<u>2019</u>	<u>2018</u>
Board designated endowment	\$51,813,700	\$46,122,925
Accumulated net spending	<u>(12,520,020)</u>	<u>(9,319,119)</u>
Total Net Assets Without Donor Restrictions	<u>\$39,293,680</u>	<u>\$36,803,806</u>

The Board of Directors established a board designated endowment for lupus research (Note 7). Investment return, net of spending policy withdrawals, are added to the board designated endowment.

The accumulated net spending represents the net spending on research and operations since inception.

b - Net Assets With Donor Restrictions

Net assets with donor restrictions at December 31, 2019 and 2018 are restricted for the following future programs and periods:

	<u>2019</u>	<u>2018</u>
Future periods	\$ 892,035	\$3,360,654
Grants	3,288,518	584,206
Rally for Lupus	749,245	-
Walk sponsorship	200,000	-
Patient advocacy fund	196,723	197,630
Conferences	150,000	90,000
Lupus Index	<u>-</u>	<u>225,000</u>
Total Net Assets With Donor Restrictions	<u>\$5,476,521</u>	<u>\$4,457,490</u>

LUPUS RESEARCH ALLIANCE, INC. AND SUBSIDIARY
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Note 5 - Concentration of Credit Risk

The Alliance maintains its cash balances in a number of financial institutions. The balances are insured by the Federal Deposit Insurance Corporation up to \$250,000 at December 31, 2019. At times throughout the year, the balances may exceed these limits.

Note 6 - Investments

Investments consist of the following at December 31, 2019 and 2018.

	2019		2018	
	Cost	Fair Value	Cost	Fair Value
Common Stock:				
Domestic	\$20,202,895	\$38,246,436	\$19,755,472	\$32,211,309
Foreign	2,523,802	3,022,847	2,378,514	2,360,236
Mutual Funds:				
Domestic equities	2,856,617	3,647,916	2,241,439	2,390,744
Foreign equities	1,825,559	2,150,135	2,119,154	2,168,933
Domestic fixed income	4,218,638	4,244,223	3,658,321	3,630,677
Foreign fixed income	910,000	882,732	910,000	835,317
Real assets	2,677,828	3,101,050	2,738,368	2,531,867
Fixed Income:				
Corporate bonds	2,733,816	2,769,395	2,601,586	2,473,409
Government obligations	2,230,192	2,256,464	1,943,545	1,879,089
Mortgage backed securities	316,121	312,368	248,008	240,203
Cash and short-term investments	1,086,083	1,086,083	1,347,785	1,347,785
Alternative Investments:				
Capital appreciation	398,731	398,731	800,000	905,615
Long/short - absolute return	-	-	550,000	609,350
	<u>\$41,980,282</u>	<u>\$62,118,380</u>	<u>\$41,292,192</u>	<u>\$53,584,534</u>

At December 31, 2019 and 2018, approximately 42% and 43%, respectively, of total investments was invested in one Fortune 500 company.

LUPUS RESEARCH ALLIANCE, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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Note 6 - Investments (continued)

The following summarizes the fair value of the investments that are measured on a recurring basis at December 31, 2019 and 2018.

	<u>2019</u>		<u>2018</u>	
	<u>Total</u>	<u>Level 1</u>	<u>Total</u>	<u>Level 1</u>
Common stock:				
Domestic	\$38,246,436	\$38,246,436	\$32,211,309	\$32,211,309
Foreign	3,022,847	3,022,847	2,360,236	2,360,236
Mutual Funds:				
Domestic equities	3,647,916	3,647,916	2,390,744	2,390,744
Foreign equities	2,150,135	2,150,135	2,168,933	2,168,933
Domestic fixed income	4,244,223	4,244,223	3,630,677	3,630,677
Foreign fixed income	882,732	882,732	835,317	835,317
Real assets	3,101,050	3,101,050	2,531,867	2,531,867
Fixed income:				
Corporate bonds	2,769,395	2,769,395	2,473,409	2,473,409
Government obligations	2,256,464	2,256,464	1,879,089	1,879,089
Mortgage backed securities	312,368	312,368	240,203	240,203
Cash and short-term investments	<u>1,086,083</u>	<u>1,086,083</u>	<u>1,347,785</u>	<u>1,347,785</u>
Total Assets in Fair Value Hierarchy	61,719,649	<u>\$61,719,649</u>	52,069,569	<u>\$52,069,569</u>
Investments measured at net asset value	<u>398,731</u>		<u>1,514,965</u>	
	<u>\$62,118,380</u>		<u>\$53,584,534</u>	

Net investment income for the years ended December 31, 2019 and 2018 is summarized as follows:

	<u>2019</u>		
	<u>Without Donor Restrictions</u>		
	<u>Operating</u>	<u>Board Designated Endowment</u>	<u>Total</u>
Interest and dividends	\$ 250,948	\$1,194,998	\$1,445,946
Realized gain on sale of investments	110,140	592,535	702,675
Unrealized gain on investments	<u>1,123,364</u>	<u>6,722,392</u>	<u>7,845,756</u>
	1,484,452	8,509,925	9,994,377
Less: Investment fees	<u>(17,098)</u>	<u>(105,694)</u>	<u>(122,792)</u>
Net Investment Income	<u>\$1,467,354</u>	<u>\$8,404,231</u>	<u>\$9,871,585</u>

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Note 6 - Investments (continued)

	2018		
	Without Donor Restrictions		
	Operating	Board Designated Endowment	Total
Interest and dividends	\$ 197,625	\$ 1,138,678	\$ 1,336,303
Realized gain on sale of investments	114,939	845,244	960,183
Unrealized loss on investments	<u>(698,504)</u>	<u>(4,812,391)</u>	<u>(5,510,895)</u>
	(385,940)	(2,828,469)	(3,214,409)
Less: Investment fees	<u>(15,571)</u>	<u>(107,724)</u>	<u>(123,295)</u>
Net Investment Loss	<u><u>\$(401,511)</u></u>	<u><u>\$(2,936,193)</u></u>	<u><u>\$(3,337,704)</u></u>

The alternative investments included in the Alliance's investment portfolio at December 31, 2019 and 2018 are redeemable based on the following terms and conditions:

	2019	2018
Monthly with 45 days' notice	\$ -	\$ 609,350
Quarterly with 100 days' notice	-	905,615
At the end of ten years' term	<u>398,731</u>	<u>-</u>
	<u><u>\$398,731</u></u>	<u><u>\$1,514,965</u></u>

The following are descriptions of the investment strategies of the alternative investments:

Long/Short - Absolute Return

Invests in long/short equity, fixed income and currencies focused on various global regions and sectors including emerging markets.

Capital Appreciation

Invests in long/short equity, event driven/distressed credit, asset-backed securities, global macro, relative value and portfolios of controlling private equity investments in companies in the United States and Canada.

LUPUS RESEARCH ALLIANCE, INC. AND SUBSIDIARY
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Note 7 - Endowment Funds

The Alliance's endowment consists of a board designated endowment which was established to fund research projects and consists solely of funds designated by the Board of Directors to function as an endowment. As required by generally accepted accounting principles, net assets associated with endowment funds, including funds designated by the Board of Directors to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions.

Changes in the Alliance's board designated endowment funds for the years ended December 31, 2019 and 2018 are summarized as follows:

	<u>2019</u>	<u>2018</u>
Endowment funds, beginning of year	\$46,122,925	\$51,742,397
Investment Return:		
Interest and dividends	1,194,998	1,138,678
Net realized and unrealized gains (losses)	7,314,927	(3,967,147)
Investment fees	<u>(105,694)</u>	<u>(107,724)</u>
Total Investment Return (Loss)	<u>8,404,231</u>	<u>(2,936,193)</u>
Spending policy withdrawals	<u>(2,713,456)</u>	<u>(2,683,279)</u>
Endowment Funds, End of Year	<u>\$51,813,700</u>	<u>\$46,122,925</u>

The Board of Directors has established a spending policy of up to 5% per year of the three-year moving average of the market value of the portfolio to support research projects. Additional funds may be used for special research projects at the Board's discretion.

The Alliance has adopted an investment policy. To satisfy long-term rate-of-return objectives, the investment policy relies on a total return strategy in which investment returns are achieved through asset appreciation (realized and unrealized) and current yield (interest and dividends). The policy targets a diversified asset allocation that places a greater emphasis on equity-based investments to achieve its long-term return objectives. The asset allocation includes equities, mutual funds, cash, real estate investment trusts, short-term investments and alternative investments.

LUPUS RESEARCH ALLIANCE, INC. AND SUBSIDIARY
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Note 8 - Unconditional Promises to Give

Unconditional promises to give at December 31, 2019 and 2018 are due as follows:

	2019		
	Without Donor Restrictions	With Donor Restrictions	Total
Due in less than one year	\$267,525	\$ 814,045	\$1,081,570
Due in one to six years	-	1,605,227	1,605,227
	<u>267,525</u>	<u>2,419,272</u>	<u>2,686,797</u>
Less: Discount to present value	-	(107,148)	(107,148)
	<u>\$267,525</u>	<u>\$2,312,124</u>	<u>\$2,579,649</u>
	2018		
	Without Donor Restrictions	With Donor Restrictions	Total
Due in less than one year	\$896,425	\$3,070,000	\$3,966,425
Due in one to five years	-	855,000	855,000
	<u>896,425</u>	<u>3,925,000</u>	<u>4,821,425</u>
Less: Discount to present value	-	(42,640)	(42,640)
	<u>\$896,425</u>	<u>\$3,882,360</u>	<u>\$4,778,785</u>

Uncollectible promises are expected to be insignificant. Unconditional promises to give due after one year are discounted to net present value using the discount rate of 3%.

At December 31, 2019, approximately 33% of unconditional promises to give were from three donors. At December 31, 2018, approximately 53% of unconditional promises to give were from two donors.

LUPUS RESEARCH ALLIANCE, INC. AND SUBSIDIARY
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Note 9 - Property and Equipment

Property and equipment at December 31, 2019 and 2018 consist of the following:

	<u>Life</u>	<u>2019</u>	<u>2018</u>
Furniture, fixtures and equipment	3-5 years	\$ 336,526	\$ 336,526
Computer equipment	3-5 years	336,160	245,527
Leasehold improvements	Life of lease	<u>424,912</u>	<u>422,712</u>
		1,097,598	1,004,765
Less: Accumulated depreciation		<u>(603,119)</u>	<u>(430,994)</u>
		<u>\$ 494,479</u>	<u>\$ 573,771</u>

Note 10 - Grants Payable

Grants payable at December 31, 2019 and 2018 are due as follows:

	<u>2019</u>	<u>2018</u>
Due within one year	\$20,053,085	\$16,127,533
Due within one to three years	<u>5,693,689</u>	<u>6,781,751</u>
	25,746,774	22,909,284
Less: Discount to present value	<u>(324,272)</u>	<u>(337,081)</u>
	<u>\$25,422,502</u>	<u>\$22,572,203</u>

Research grants payable for periods due after one year are discounted to net present value using a discount rate of 3%.

During 2019, two grants totaling \$1,250,000 that were awarded in prior years were cancelled by the Alliance due to the grantees' breach of their grant agreements.

LUPUS RESEARCH ALLIANCE, INC. AND SUBSIDIARY
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DECEMBER 31, 2019 AND 2018

Note 11 - Land and Building Held for Resale

In December 2019, the Alliance received a donation of land and building (the "Property"). The Property was recorded at fair value less estimated costs to sell the property. The property was sold on July 31, 2020.

Note 12 - Commitments

a - The Alliance leases office space in New York, NY for its main office and in Arlington, VA, Chicago, IL and Los Angeles, CA for its branch offices. The leases provide for minimum annual payments as follows:

<u>Year Ending December 31,</u>	
2020	\$ 990,513
2021	1,009,313
2022	1,055,204
2023	990,410
2024	1,012,694
Thereafter, through April 30, 2027	2,449,792

Rent expense for the years ended December 31, 2019 and 2018 was \$1,077,918 and \$1,064,266, respectively.

b - The Alliance has commitments of approximately \$291,000 for consulting services through December 31, 2021.

Note 13 - Employee Benefit Plan - Defined Contribution Plan

The Alliance maintains a defined contribution retirement plan (the "Plan"). The Alliance contributes up to 4% of each employee's eligible compensation and at the Alliance's discretion, makes an additional contribution between 4% and 7% the employee's eligible compensation depending on years of service. The contributions are subject to limitations as stated in relevant provisions of the Internal Revenue Code. Total contributions to the plan for the years ended December 31, 2019 and 2018 was \$297,330 and \$284,103, respectively.

LUPUS RESEARCH ALLIANCE, INC. AND SUBSIDIARY
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Note 14 - Joint Costs

The Alliance achieves certain educational goals for its science program during its walkathon promotional events by providing informational discussions and materials regarding lupus research. The cost of conducting those joint activities included joint costs that are not directly attributable to either the program component or the fundraising component of the activities. Those joint costs were allocated as follows:

	<u>2019</u>	<u>2018</u>
Fundraising	\$216,339	\$245,802
Scientific programs	<u>54,084</u>	<u>61,450</u>
Total	<u>\$270,423</u>	<u>\$307,252</u>

Note 15 - Subsequent Events

In March 2020, the United States declared the global pandemic novel coronavirus COVID-19 outbreak a national emergency. As a result, the Alliance has suspended some of its program activities at the direction of state and local governmental authorities. While management is currently evaluating the potential impact that the resulting economic uncertainties may have on the Alliance, it believes that its current financial assets are sufficient to support the Alliance's operations on an ongoing basis.

In April 2020, the Alliance received a \$698,800 Paycheck Protection Program loan having an interest rate of 1% and a maturity of 2 years. The loan and any accrued interest can be forgiven in its entirety if the loan proceeds are applied towards applicable payroll and occupancy costs, as defined by the Coronavirus Aid, Relief and Economic Security Act. The Alliance expects the entire loan and all accrued interest will be forgiven.