



**GEORGIA TECH RESEARCH
CORPORATION**

FINANCIAL STATEMENTS

As of and for the Year Ended June 30, 2017

And Report of Independent Auditor

GEORGIA TECH RESEARCH CORPORATION

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Report of Independent Auditor

To the Board of Trustees
Georgia Tech Research Corporation
Atlanta, Georgia

Report on the Financial Statements

We have audited the accompanying financial statements of the business-type activities and the component unit of the Georgia Tech Research Corporation (“GTRC”), a component unit of the state of Georgia, as of and for the year ended June 30, 2017, which collectively comprise GTRC’s basic financial statements as listed in the table of contents, 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 from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor’s judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to GTRC’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 GTRC’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 opinions.

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the net position of the business-type activities and the component unit of GTRC as of June 30, 2017, and the respective changes in net position and cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

OTHER MATTERS

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that management's discussion and analysis on pages 3 through 6 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated September 12, 2017, on our consideration of GTRC'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 the internal control over financial reporting or on compliance. The report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering GTRC's internal control over financial reporting and compliance.

Cherry Bekaert LLP

Atlanta, Georgia
September 12, 2017

GEORGIA TECH RESEARCH CORPORATION

MANAGEMENT'S DISCUSSION AND ANALYSIS

JUNE 30, 2017

Introduction

The Georgia Tech Research Corporation ("GTRC") is a state-chartered, not-for-profit corporation serving the Georgia Institute of Technology ("GIT"), a unit of the University System of the state of Georgia, as an approved cooperative organization. The Georgia Tech Applied Research Corporation ("GTARC") is a state-chartered, not-for-profit corporation serving GIT as an approved cooperative organization.

GTRC and GTARC are organized and operate primarily for the purpose of soliciting grants and contracts, accepting grants or entering into contracts for research or services to be performed by or in conjunction with GIT or to be performed using GIT's facilities, and for related objectives. GTRC serves the business segments of GIT, which perform research in accordance with guidance released by the Office of Management and Budget ("OMB"). Awards adhere to Uniform Administrative Requirements, Cost Principles, and Audit Requirements contained in Title 2 of the Code of Federal Regulations (CFR). With respect to subsequent incremental funding provided on awards which were received preceding the changes to OMB guidance, GTRC administers the research in accordance with instruction provided by the individual awarding Federal agencies.

Description of the Financial Statements

The statements of net position; revenues, expenses and changes in net position; and cash flows are designed to provide information which will assist in understanding the financial condition and performance of GTRC. The net position is an indicator of GTRC's financial health. Over time, increases or decreases in net position are another measure of the changes in GTRC's financial condition when considered with other non-financial facts.

The statement of net position presents the assets, liabilities, and net position of GTRC.

The statement of revenues, expenses, and changes in net position presents the revenues earned and the expenses incurred during the year. Activities are reported as either operating or nonoperating. The financial reporting model classifies investment earnings and changes in the fair value of investments as nonoperating revenues. As a result, the financial statements may show operating losses that are then offset by nonoperating revenues from a total financial perspective.

The statement of cash flows presents information in the form of cash inflows and outflows summarized by operating, capital and related financing activities, and investing activities.

GEORGIA TECH RESEARCH CORPORATION
MANAGEMENT'S DISCUSSION AND ANALYSIS

JUNE 30, 2017

Financial Highlights

The condensed statements of net position at June 30, 2017 and 2016 are shown below:

	<u>2017</u>	<u>2016</u>
Assets		
Current assets	\$ 124,145,329	\$ 117,731,045
Capital assets, (net)	1,152,763	1,384,930
Noncurrent assets	<u>4,466,600</u>	<u>5,334,994</u>
Total Assets	<u>129,764,692</u>	<u>124,450,969</u>
Liabilities		
Current liabilities	91,198,582	88,575,304
Noncurrent liabilities	<u>4,425,181</u>	<u>5,088,535</u>
Total Liabilities	<u>95,623,763</u>	<u>93,663,839</u>
Net Position		
Invested in capital assets	1,152,763	1,384,931
Unrestricted	<u>32,988,166</u>	<u>29,402,199</u>
Total Net Position	<u>\$ 34,140,929</u>	<u>\$ 30,787,130</u>

Current assets increased by \$6,414,283, or approximately 5.4% from fiscal 2016, due primarily to an increase in cash levels.

Noncurrent assets consist primarily of a note receivable and an investment in direct financing lease. Noncurrent assets decreased by \$868,393, or approximately 16.3% from fiscal 2016, primarily due to a pay down of principal related to the investment in the direct financing lease.

Capital assets decreased by \$232,168, or approximately 16.8% from fiscal 2016, due primarily to current year additions being less than current year depreciation expense.

Current liabilities increased by \$2,623,277, or approximately 3.0% from fiscal 2016, due to an increase in accounts payable for direct research costs owed to GIT, and higher advance payments on research contracts.

Net position represents the difference between total assets and liabilities. There was an increase in net position of \$3,353,799, or approximately 10.9% from fiscal 2016, which was attributable to GTRC generating net income for the year and not being in a loss position.

GEORGIA TECH RESEARCH CORPORATION

MANAGEMENT'S DISCUSSION AND ANALYSIS

JUNE 30, 2017

Financial Highlights (continued)

The condensed statements of revenues, expenses, and changes in net position for the years ended June 30, 2017 and 2016 are shown below:

	June 30,	
	2017	2016
Operating revenues	\$ 309,472,343	\$ 306,851,938
Operating expenses	(306,810,396)	(305,998,169)
Income from operations	2,661,947	853,769
Nonoperating revenues, net	691,852	254,077
Increase in net position	3,353,799	1,107,846
Net position, beginning of year	30,787,130	29,679,284
Net position, end of year	\$ 34,140,929	\$ 30,787,130

Operating revenues consist primarily of research contracts, licensing fees, royalty revenues and lease income. During fiscal 2017, operating revenues increased by \$2,620,405, or approximately 0.9%, primarily due to increase research project revenues.

Operating expenses increased by \$812,227, or approximately 0.3%, which is primarily proportional to the increase in operating revenues but also reflects an increase in general and administrative expenses.

Nonoperating revenues increased by \$437,775, or approximately 172.3%, due to a gain recognized on the disposition of certain assets and an increase in interest income.

Economic Outlook

GIT, through GTRC and GTARC received more than \$690 million in sponsored research awards in fiscal year 2017. Research awards grew in the academic units of GIT. GTRC received over \$313 million in new research funding while GTARC received approximately \$377 million. Overall, new funding for GIT research decreased approximately 3.9% over new funding received in 2016.

GIT is working with a diverse set of public and private sponsors to support growth in research with continued emphasis on engagement with private industry. The development of Research Neighborhoods aligned with the Institute's strategic research themes provides opportunities for educational engagement for students as well as research collaboration. Significant progress in that regard was made in 2017 for manufacturing and new initiatives are underway and will continue in 2017 in life sciences. The numbers of master agreements and contracts executed by GTRC and GTARC with private industry has remained steady as has total funding and average award size. In 2017, the Office of Industry Engagement will work with the Vice Presidents for Research, Corporate Relations, and faculty to focus on building and maintaining research relationships with strategic research sponsors. Certain areas of research continue to promise opportunities for funding for innovative research. These include cyber security; data analytics and data sciences which will occupy new facilities in 2019: and manufacturing including cell based manufacturing. Work with traditional Department of Defense sponsors continues to be an area of strength and focus.

GEORGIA TECH RESEARCH CORPORATION

MANAGEMENT'S DISCUSSION AND ANALYSIS

JUNE 30, 2017

Economic Outlook (continued)

GIT is attentive to the extremely competitive environment and uncertain prospects for growth in federal funding in many areas of basic research although funding for 2018 and awards already made should sustain GIT research expenditures through fiscal year 2018. GIT is attentive to proposed limits on reimbursement of Facilities and Administrative Costs that arise from time to time. The federal government has emphasized the importance of public-private research collaboration which makes the emphasis on relationships with industry sponsors an important part of supporting research at GIT. The Offices of Industry Engagement and Corporate Relations will continue to work with the Vice President for Research to develop major public-private projects aligned with GIT's strategic research themes. Overall new awards for research reflect growth, which although not uniform in all sectors, is very strong in some.

Requests for Information

This financial report is designed to provide a general overview of Georgia Tech Research Corporation's finances for all those with an interest in the corporation's finances. Questions concerning any of the information provided in this report or requests for additional financial information, including the separately issued financial statements for Georgia Tech Applied Research Corporation, should be addressed to the Office of the Controller, Georgia Tech Research Corporation, 505 Tenth Street, N.W., Atlanta, Georgia, 30332-0415.

GEORGIA TECH RESEARCH CORPORATION
STATEMENT OF NET POSITION

JUNE 30, 2017

	Georgia Tech Research Corporation	Component Unit Georgia Tech Applied Research Corporation	Total Business-Type Activities
ASSETS			
Current Assets:			
Cash	\$ 71,315,489	\$ 27,048,787	\$ 98,364,276
Accounts receivable:			
Research contracts - billed	19,185,469	37,089,873	56,275,342
Research contracts - unbilled	31,319,781	31,496,597	62,816,378
Other receivables	1,132,785	85,331	1,218,116
Less - allowance for doubtful accounts	(250,217)	(1,509,098)	(1,759,315)
Accounts receivable, net	51,387,818	67,162,703	118,550,521
Due from component unit	1,042,902	-	1,042,902
Net investment in direct financing lease - current portion	327,503	-	327,503
Prepaid expenses	71,617	-	71,617
Total Current Assets	124,145,329	94,211,490	218,356,819
Noncurrent Assets:			
Investments	128	-	128
Net investment in direct financing lease - long-term portion	4,466,472	-	4,466,472
Other assets	-	3	3
Capital assets, net	1,152,763	70,313	1,223,076
Total Noncurrent Assets	5,619,363	70,316	5,689,679
Total Assets	129,764,692	94,281,806	224,046,498
LIABILITIES			
Current Liabilities:			
Accounts payable:			
Georgia Institute of Technology	43,425,030	39,266,818	82,691,848
Due to component unit	-	1,042,902	1,042,902
Obligation under leases - current portion	368,794	-	368,794
Unearned research contract revenue	47,404,758	1,994,513	49,399,271
Total Current Liabilities	91,198,582	42,304,233	133,502,815
Noncurrent Liabilities:			
Obligation under leases - long-term portion	4,425,181	-	4,425,181
Funds held on behalf of others	-	29,998,329	29,998,329
Total Noncurrent Liabilities	4,425,181	29,998,329	34,423,510
Total Liabilities	95,623,763	72,302,562	167,926,325
NET POSITION			
Invested in capital assets	1,152,763	70,313	1,223,076
Unrestricted	32,988,166	21,908,931	54,897,097
Total Net Position	\$ 34,140,929	\$ 21,979,244	\$ 56,120,173

See accompanying notes to financial statements.

GEORGIA TECH RESEARCH CORPORATION
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION

YEAR ENDED JUNE 30, 2017

	Georgia Tech Research Corporation	Component Unit Georgia Tech Applied Research Corporation	Total Business-Type Activities
Operating Revenues:			
Research contracts	\$ 297,647,035	\$ 384,367,400	\$ 682,014,435
Licenses and royalties	1,760,594	53,023	1,813,617
Lease income	10,064,714	9,900	10,074,614
Total Operating Revenues	309,472,343	384,430,323	693,902,666
Operating Expenses:			
Research subcontracted to Georgia Institute of Technology	280,951,833	379,373,261	660,325,094
Depreciation	337,705	3,160	340,865
Administrative and general expenses	6,678,957	4,233,707	10,912,664
Licenses and royalties expenses	2,845,684	-	2,845,684
Lease expenses	10,064,714	9,900	10,074,614
Payments to or on behalf of Georgia Institute of Technology	5,931,503	315,397	6,246,900
Total Operating Expenses	306,810,396	383,935,425	690,745,821
Income from operations	2,661,947	494,898	3,156,845
Nonoperating Revenues:			
Interest income	321,150	101,039	422,189
Net gain on disposition of investments	370,702	-	370,702
Total Nonoperating Revenues	691,852	101,039	792,891
Increase in net position	3,353,799	595,937	3,949,736
Net position, beginning of year	30,787,130	21,383,307	52,170,437
Net position, end of year	\$ 34,140,929	\$ 21,979,244	\$ 56,120,173

See accompanying notes to financial statements.

GEORGIA TECH RESEARCH CORPORATION
STATEMENT OF CASH FLOWS

YEAR ENDED JUNE 30, 2017

		<u>Component Unit</u>	
		<u>Georgia Tech</u>	
	<u>Georgia Tech</u>	<u>Applied</u>	<u>Total</u>
	<u>Research</u>	<u>Research</u>	<u>Business-Type</u>
	<u>Corporation</u>	<u>Corporation</u>	<u>Activities</u>
Cash flows from operating activities:			
Receipts from grantors	\$ 286,838,056	\$ 385,991,282	\$ 672,829,338
Receipts of license fees and royalties	1,760,593	53,023	1,813,616
Receipts from leases	10,064,714	9,900	10,074,614
Payments to or on behalf of Georgia Institute of Technology	(5,931,503)	(315,397)	(6,246,900)
Payments for research contract costs	(279,296,961)	(383,321,590)	(662,618,551)
Payments for licenses and royalties	(2,845,684)	-	(2,845,684)
Payments for leases	(10,064,714)	(9,900)	(10,074,614)
Payments to suppliers	(6,034,829)	(4,700,137)	(10,734,966)
Net cash used in operating activities	<u>(5,510,328)</u>	<u>(2,292,819)</u>	<u>(7,803,147)</u>
Cash flows from capital and related financing activities			
Purchases of capital assets	(105,538)	-	(105,538)
Net cash used in financing activities	<u>(105,538)</u>	<u>-</u>	<u>(105,538)</u>
Cash flows from investing activities:			
Net gain on disposition of investments	370,702	-	370,702
Interest income	321,150	101,039	422,189
Net cash provided by investing activities	<u>691,852</u>	<u>101,039</u>	<u>792,891</u>
Net decrease in cash	(4,924,014)	(2,191,780)	(7,115,794)
Cash, beginning of year	76,239,503	29,240,567	105,480,070
Cash, end of year	<u>\$ 71,315,489</u>	<u>\$ 27,048,787</u>	<u>\$ 98,364,276</u>
Reconciliation of operating income to net cash used in operating activities:			
Operating income	\$ 2,661,947	\$ 494,898	\$ 3,156,845
Adjustments to reconcile operating income to net cash used in operating activities:			
Depreciation	337,705	3,160	340,865
Changes in assets and liabilities:			
Other assets	-	682	682
Prepaid expenses	(22,975)	-	(22,975)
Accounts receivable	(11,752,573)	2,194,863	(9,557,710)
Direct financing lease	838,537	-	838,537
Due to/from component unit	467,106	(467,106)	-
Accounts payable to Georgia Institute of Technology	1,654,872	(7,060,494)	(5,405,622)
Obligations under leases	(638,535)	-	(638,535)
Funds held on behalf of others	-	3,112,165	3,112,165
Unearned research contract revenue	943,588	(570,987)	372,601
Net cash used in operating activities	<u>\$ (5,510,328)</u>	<u>\$ (2,292,819)</u>	<u>\$ (7,803,147)</u>

See accompanying notes to financial statements.

GEORGIA TECH RESEARCH CORPORATION

NOTES TO THE FINANCIAL STATEMENTS

JUNE 30, 2017

Note 1—Description of organization

The Georgia Tech Research Corporation (“GTRC”) was chartered on April 13, 1937, as the Industrial Development Council, a state-chartered, not-for-profit corporation serving the Georgia Institute of Technology (“GIT”), a unit of the University System of the state of Georgia, as an approved cooperative organization. GTRC was established for the purpose of engaging in sponsored research for scientific, literary, and educational purposes or related objectives. On February 9, 1946, the corporate charter was amended and included a provision to change the name from the Industrial Development Council to the Georgia Tech Research Institute (“GTRI”). On April 6, 1984, GTRI amended its corporate charter to change the name to the Georgia Tech Research Corporation.

GTRC serves as the contracting entity for GIT, which performs research in accordance with guidance released by the Office of Management and Budget (“OMB”). Awards adhere to Uniform Administrative Requirements, Cost Principles, and Audit Requirements contained in Title 2 of the Code of Federal Regulations (“CFR”). With respect to subsequent incremental funding provided on awards which were received preceding the changes to OMB guidance, GTRC administers the research in accordance with instruction provided by the individual awarding Federal agencies.

On July 1, 1998, the Georgia Tech Applied Research Corporation (“GTARC”) was established. GTARC was organized as the contracting entity for units of GIT performing research in accordance with guidance released by the OMB and Federal Acquisition Regulations (“FAR”) 31.2. Awards adhere to guidance contained in Title 2 of the CFR and FAR 31.2. With respect to subsequent incremental funding provided on awards which were received preceding the changes to OMB guidance, GTARC administers the research in accordance with instruction provided by the individual awarding federal agencies.

GTRC and GTARC (hereinafter collectively referred to as “GTRC”), enter into contracts and grant agreements with various organizations, including federal agencies, and subcontract with GIT to provide services in connection with these agreements. Since 1946, GTRC has served as a “university-connected research foundation.” As part of the relationship, payments occur between GIT and GTRC for certain sponsored project expenditures and research administration.

In a Memorandum of Understanding (“MOU”) dated April 1, 1953, the Board of Regents of the University System of Georgia authorized GTRC (then GTRI) to serve as the official grantee for all contracts and grants for the conduct of sponsored research at GIT. The MOU also assigned all intellectual property developed through the performance of contracts subcontracted to GIT to GTRC. GTRC is the administrative organization for discoveries, innovations, inventions, patents, and copyrights and is responsible for intellectual property management including patenting and licensing. Currently, pursuant to the Cooperative Organization Guiding Principles Memoranda of Understanding and the Board of Regents Policy 1905, payments occur between GIT and GTRC and GTARC for certain sponsored project expenditures and research administration. GTRC and GTARC hold in trust for GIT any balances, after the payment of necessary operating costs, for the promotion of research at GIT and for the benefit of research at GIT. Intellectual property created in the course of research and other activities at GIT is assigned to GTRC in accordance with the GIT Intellectual Property Policy.

In accordance with accounting principles generally accepted in the United States of America (“GAAP”) applicable to governments, GTRC and GTARC are considered part of the same reporting entity due to the nature and significance of the relationship between the two corporations. Accordingly, the financial statements for GTARC are presented in the financial statements of GTRC as a discretely presented component unit. In addition, the accompanying financial statements present a total column which represents the entity-wide financial statements of GTRC. Separately issued financial statements for Georgia Tech Applied Research Corporation can be obtained by contacting the Office of the Controller, Georgia Tech Applied Research Corporation, 505 Tenth Street N.W., Atlanta, Georgia, 30332-0415.

GEORGIA TECH RESEARCH CORPORATION

NOTES TO THE FINANCIAL STATEMENTS

JUNE 30, 2017

Note 2—Summary of significant accounting policies

GTRC's financial statements have been prepared in accordance with GAAP as prescribed by the Governmental Accounting Standards Board ("GASB"). The financial statements of GTRC have been prepared on the accrual basis of accounting and are presented in conformity with GAAP.

The following is a summary of certain significant accounting policies followed in the preparation of the financial statements:

Reporting Entity – In accordance with the criteria in Statement of Governmental Accounting Standards ("SGAS") No. 61, *The Financial Reporting Entity*, GTRC and GTARC are legally separate, tax exempt component units of the state of Georgia (the "State"). Although GIT is not fiscally accountable for GTRC and GTARC, it has been determined that the nature and significance of the relationship between GIT, GTRC and GTARC is such that exclusion of GTARC and GTRC from GIT's departmental financial statements would render those statements misleading.

Revenues – Substantially all of GTRC's revenues are derived from grants and cost reimbursement contracts which provide for the recovery of direct and indirect costs. GTRC recognizes revenue associated with direct and indirect costs as the related costs are incurred for approved research activities. The recovery of indirect costs is generally recorded at fixed rates negotiated with the sponsoring agency. License and royalty revenues are recorded when earned.

GTRC and GTARC classify revenue generated from their normal operational cycles as operating income. Revenue streams such as research contracts, licenses and royalties, and lease income are examples of what are considered to be operating revenues. Revenues that are not generated during the normal operating cycle such as interest income and unrealized gains and losses on investments are classified as nonoperating revenues.

Unbilled Accounts Receivable and Unearned Research Contract Revenue – Unbilled accounts receivable represent costs incurred and charged to projects in excess of amounts invoiced on those projects. Unearned research contract revenue represents amounts invoiced on various projects in excess of costs incurred and charged to those projects.

Funds Held on Behalf of Others – Sponsored research projects have fees charged to sponsors in accordance with FAR 31.2. These fees are held on behalf of GIT and can be invoiced to GTARC by the appropriate department of GIT.

Overhead Revenue – GTRC receives reimbursement from sponsoring agencies for indirect costs incurred. GTRC retains a portion of the indirect costs which is used for operating expenses, and the remainder is granted back to GIT for the benefit of research at GIT. The overhead revenue is reported as revenue from research contracts in the accompanying financial statements.

Cash – At June 30, 2017, the bank balance was \$72,243,748 and \$27,224,207, and the book balance was \$71,315,489 and \$27,048,787 for GTRC and GTARC, respectively. Cash balances usually exceed federally insured amounts. GTRC mitigates this risk by depositing and investing cash with major financial institutions. GTRC has not experienced any loss in such accounts and believes it is not exposed to any significant credit risk on cash. At June 30, 2017, the bank balances were collateralized by a pool of pledged securities administered under the direction of the Georgia Office of Treasury and Fiscal Services.

GEORGIA TECH RESEARCH CORPORATION
NOTES TO THE FINANCIAL STATEMENTS

JUNE 30, 2017

Note 2—Summary of significant accounting policies (continued)

Investments – GTRC’s investments consist entirely of equity securities which are acquired as partial consideration for licenses. These equity securities are held exclusively in GTRC’s name and are not subject to GTRC’s investments policy. These equity securities usually do not have readily determinable fair values and are recorded at their fair value at acquisition, which is generally zero or an insignificant amount. Any subsequent disposition of these equity securities is recorded as a gain or loss on sale of investments in nonoperating revenues on the statement of revenues, expenses, and changes in net position.

Major Clients and Concentration of Credit Risk – During the fiscal year ended June 30, 2017, GTRC and GTARC derived approximately 74.5% and 95.2%, respectively, of their revenue from contracts with the U.S. government. At June 30, 2017, GTRC and GTARC had billed research contracts accounts receivable from the U.S. government of 21.1% and 81.4%, respectively. Management does not believe these receivables represent significant credit risk at June 30, 2017.

Federal Income Taxes – GTRC is exempt from income taxes as provided by Section 501(c)(3) of the Internal Revenue Code.

Allowance for Doubtful Accounts – The allowance for doubtful accounts is determined by evaluating the prior experience, nature of the contract, and credit rating of the sponsor for each contract with an outstanding balance greater than 180 days. Generally, all account balances greater than 180 days are reserved.

Changes in the allowance for doubtful accounts for the year ended June 30, 2017 were as follows:

	Georgia Tech Research Corporation	Component Unit Georgia Tech Applied Research Corporation
Beginning balance	\$ 1,082,495	\$ 1,882,609
Recoveries	16,336	-
Write-offs	(848,614)	(373,511)
Ending balance	<u>\$ 250,217</u>	<u>\$ 1,509,098</u>

Capital Assets – Capital assets are recorded at cost. GTRC has established a threshold of \$5,000 for capitalizing equipment. All capitalized assets purchased under the terms of equipment and facilities grants are donated to GIT when fully depreciated. Depreciation is provided for in amounts sufficient to relate the cost of depreciable assets to operations over their estimated service lives which range from three to ten years. The straight-line method of depreciation is followed for all capital assets.

Grants to Georgia Institute of Technology – Pursuant to an agreement between GTRC and the Board of Regents of the University System of Georgia, dated April 1, 1953, the GTRC Board of Trustees will issue grants from time to time as it sees fit for the promotion of research at GIT. These grants will be funded from the balances held in trust for GIT which are reflected in the unrestricted net position of GTRC.

GEORGIA TECH RESEARCH CORPORATION

NOTES TO THE FINANCIAL STATEMENTS

JUNE 30, 2017

Note 2—Summary of significant accounting policies (continued)

Net Position – GTRC’s net position is classified as follows: *Invested in capital assets* represents GTRC’s total investment in capital assets, net of related depreciation and *unrestricted net position* represents resources derived primarily from research contracts, licensing and royalties, and lease income. These resources can be used for the ongoing operations of GTRC. However, in accordance with the April 1, 1953 Memorandum of Understanding between GTRC and the Board of Regents of the University System of Georgia, all balances held after the payment of necessary operating costs are to be held in trust for GIT for the promotion of research at GIT. These balances will be returned to GIT in the form of grants which are made at the discretion of the Board of Trustees of GTRC.

Research Administration – During the year ended June 30, 2017, GTRC and GTARC incurred research administration costs totaling \$6,678,957 and \$4,233,707, respectively, for services provided by GIT, which are listed as administrative and general expenses in the statement of revenues, expenses, and changes in net position.

Use of Estimates in Preparation of Financial Statements – The preparation of financial statements in conformity with GAAP 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 financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

New Accounting Pronouncements – During the year ended June 30, 2017 GTRC adopted SGAS No. 80, *Blending Requirements For Certain Component Units – An Amendment of GASB Statement No. 14*, which clarifies the financial statement presentation requirements for certain component units. This statement amends the blending requirements for the financial statement presentation of component units of all state and local governments. The additional criterion requires blending of a component unit incorporated as a not-for-profit corporation in which the primary government is the sole corporate member. The adoption of this statement had no effect on GTRC’s financial statements.

In June 2017, GASB issued SGAS No. 87, *Leases*, which improves the accounting and financial reporting for leases by governments. This statement requires recognition of certain lease assets and liabilities for leases that previously were classified as operating leases and recognized as inflows of resources or outflows of resources based on the payment provisions of the contract. It also requires a lessee to recognize a lease liability and an intangible right-to-use lease asset, and a lessor is required to recognize a lease receivable and a deferred inflow of resources, thereby enhancing the relevance and consistency of information about governments’ leasing activities. GTRC is currently evaluating the impact implementing SGAS No. 87 will have on its financial statements.

GEORGIA TECH RESEARCH CORPORATION
NOTES TO THE FINANCIAL STATEMENTS

JUNE 30, 2017

Note 3—Capital assets

Following are changes in GTRC's capital assets for the year ended June 30, 2017:

	Balance June 30, 2016	Additions	Disposals	Transfers	Balance June 30, 2017
Capital assets not being depreciated:					
Construction in progress	\$ -	\$ 105,538	\$ -	\$ (82,681)	\$ 22,857
Historical treasures and works of art	240,735	-	-	-	240,735
Total capital assets not being depreciated	240,735	105,538	-	(82,681)	263,592
Capital assets being depreciated:					
Building improvements	812,586	-	-	56,832	869,418
Computer software	1,257,673	-	-	-	1,257,673
Furniture and equipment	1,046,046	-	-	25,849	1,071,895
Total capital assets being depreciated	3,116,305	-	-	82,681	3,198,986
Less accumulated depreciation for:					
Building improvements	(309,347)	(81,577)	-	-	(390,924)
Computer software	(950,653)	(129,158)	-	-	(1,079,811)
Furniture and equipment	(712,110)	(126,970)	-	-	(839,080)
Total accumulated depreciation	(1,972,110)	(337,705)	-	-	(2,309,815)
Total capital assets, net	\$ 1,384,930	\$ (232,167)	\$ -	\$ -	\$ 1,152,763

During the year ended June 30, 2017, GTARC capital assets had related depreciation expense of \$3,160, with a resulting net book value of \$70,313.

Note 4—Net investment in direct financing lease

On April 15, 2015, GTRC entered into a Master Lease Agreement (“Master Lease”) with Banc of America Leasing & Capital, LLC (“BOA”), covering the acquisition and lease of certain research equipment (see Note 5). On June 17, 2015, GTRC and GIT entered into a State of Georgia Standard Agency Agreement (the “Agreement”) whereby GIT leased the research equipment acquired under the Master Lease from GTRC. Per the terms of the Agreement, GIT will pay consideration to GTRC in an amount equal to the consideration due under the Master Lease. The Agreement between GTRC and GIT has a term of 119 months beginning on June 25, 2015 with quarterly payments until April 15, 2025; at which time the research equipment will be conveyed to GIT. Therefore, GIT has recorded the research equipment as a capital asset on its books and conversely, GTRC has recorded the asset as a net investment in direct financing lease on the statement of net position.

GEORGIA TECH RESEARCH CORPORATION
NOTES TO THE FINANCIAL STATEMENTS

JUNE 30, 2017

Note 4—Net investment in direct financing lease (continued)

Future minimum net amounts receivable under direct financing lease at June 30, 2017 are as follows:

<u>Years Ending June 30,</u>	
2018	\$ 727,400
2019	727,400
2020	727,400
2021	727,400
2022-2025	<u>2,744,970</u>
Gross investment in direct financing lease	5,654,570
Less unearned interest income	<u>(860,595)</u>
Net investment in direct financing lease	<u>\$ 4,793,975</u>

Note 5—Lease commitments

Operating Leases

Research Facilities – GTRC is committed to an operating lease with the University Financing Foundation, Inc., a Georgia nonprofit corporation, for the Centennial Research Building. The lease carries successive two-year terms that are automatically renewed at prevailing market rates in effect at the time of the renewal. GTRC may cancel the lease provided notice is given during July of any lease year to be effective as of June 30 of the then-current lease year. The term of this lease expires June 30, 2029. As of June 30, 2017, future minimum lease payments through the term of the lease total \$18,125,280.

Institute for BioEngineering and BioSciences Complex – The Institute for BioEngineering and BioSciences Complex (the “Complex”) was developed by Georgia Tech Facilities, Inc. (“GTFI”), formerly Georgia Tech Foundation Facilities, Inc., and funded by the issuance of 30-year, fixed rate, Series B bonds through the Fulton County Development Authority. On December 1, 1997, GTRC agreed to guarantee these bonds by entering into an agreement to lease the Complex from GTFI. On April 1, 2008, the Series 1997B Bonds were refunded by the issuance of \$19,900,000 Development Authority of Fulton County Series 2008B Revenue Bonds. In connection with the refunding, GTRC guaranteed the 2008B Revenue Bonds and entered into an Amended and Restated Facility Lease Agreement with GTFI. The term of this lease expires September 1, 2027, or when the Revenue Bonds are redeemed. GTRC is obligated to pay rent in an amount equal to the principal, premium (if any), and interest on the Series 2008B Revenue Bonds when due and upon any redemption or acceleration thereunder. As of June 30, 2017, future minimum lease payments through the term of the lease total \$14,792,784.

Cobb County Research Campus – In May 2010, The Development Authority of Cobb County issued Revenue Bonds in an aggregate principal amount of \$18,975,000 for the TUFF Cobb Research Campus – Georgia Tech Research Corporation Project. The proceeds of the bonds were loaned to TUFF Cobb Research LLC (“TUFF”), a Georgia limited liability company, the sole member of which is The University Financing Foundation, Inc. Simultaneous with the issuance of the Series 2010 bonds, TUFF issued \$12,575,000 Series 2010A Taxable Revenue Bonds. The aggregate amount of the two bond issues was \$31,550,000. According to the Offering Memorandums, TUFF used the proceeds from the 2010 bond issue primarily for capital improvements to the Cobb Research Campus, and the proceeds from the 2010A bond issue primarily for general corporate purposes.

GEORGIA TECH RESEARCH CORPORATION
NOTES TO THE FINANCIAL STATEMENTS

JUNE 30, 2017

Note 5—Lease commitments (continued)

The Cobb Research Campus is a six-building, 160,000 square foot Research Park located on approximately 53.2 acres in Cobb County, Georgia. GTRC leases the property from TUFF. GTRC subleases the property to the Board of Regents of the University System of Georgia for the benefit of GIT. The lease is a general obligation of GTRC. The end of the lease term is October 31, 2036, the maturity date of the bonds. The sublease is an annually renewable lease agreement. The timing and amount of rental payments under the sublease total approximately \$54,144,016, adequate to meet the debt service and debt service reserve fund requirement related to the 2010 and 2010A bonds of approximately \$53,620,668. As of June 30, 2017, future minimum lease payments through the term of the lease total \$40,145,280.

GTRC also has a number of other lease agreements that are subleased to GIT with lease terms expiring from 2018-2021. As of June 30, 2017, future minimum lease payments through the term of these leases total \$20,856,726.

The facilities GTRC leases in connection with the above lease agreements are subleased to GIT. The subleases carry successive one-year terms that are renewable annually. The timing and amount of rental payments under the subleases are substantially the same as those under their corresponding lease agreements between GTRC and the third-party lessors. GTRC expects to receive revenues sufficient to offset its obligations under the lease agreements through annual renewal of the subleases by GIT.

Future minimum operating lease payments at June 30, 2017 are as follows:

<u>Years Ending June 30,</u>	<u>Commitments</u>	<u>Sub Rental Receipts</u>	<u>Net Rental Commitment</u>
2018	\$ 10,825,768	\$ 10,825,768	\$ -
2019	10,560,769	-	10,560,769
2020	9,337,926	-	9,337,926
2021	8,353,181	-	8,353,181
2022	6,625,813	-	6,625,813
2023-2027	25,572,750	-	25,572,750
2028-2032	13,645,783	-	13,645,783
2033-2037	8,998,080	-	8,998,080
	<u>\$ 93,920,070</u>	<u>\$ 10,825,768</u>	<u>\$ 83,094,302</u>

Net rent expense for the year ended June 30, 2017 was as follows:

Minimum rentals	\$ 10,064,714
Less - Sublease rentals - Georgia Institute of Technology	<u>(10,064,714)</u>
Net rent expense	<u>\$ -</u>

GEORGIA TECH RESEARCH CORPORATION

NOTES TO THE FINANCIAL STATEMENTS

JUNE 30, 2017

Note 5—Lease commitments (continued)

Direct Financing Lease

BOA Master Lease Agreement – On April 15, 2015, GTRC entered into a Master Lease with BOA, covering the acquisition and lease of certain research equipment in an amount not to exceed \$5,800,000. BOA entered into an Acquisition Fund and Account Control Agreement with Deutsche Bank National Trust Company, as the Acquisition Fund Custodian, to provide the Acquisition Funding for the Master Lease. The Master Lease requires that the cost of the equipment be deposited into an Acquisition Fund for the purpose of fully funding the Master Lease, and the Acquisition Fund Custodian provides for a mechanism for the application of such amounts to the purchase of and payment for the equipment. GTRC will arrange for, supervise and provide for, or cause to be supervised and provided for, the acquisition of the equipment, with monies available in the Acquisition Fund. The Master Lease expires on April 15, 2025.

Future minimum direct financing lease payments at June 30, 2017 are as follows:

<u>Years Ending June 30,</u>	
2018	\$ 727,400
2019	727,400
2020	727,400
2021	727,400
2022-2025	<u>2,744,970</u>
Total minimum lease payments	5,654,570
Less: amount representing interest	<u>(860,595)</u>
	<u>\$ 4,793,975</u>

Note 6—Contingencies

Federal and state funded research projects are subject to special audits. Such audits could result in some allocated costs being disallowed or indirect cost rates adjusted. No provision has been made for any liabilities that may arise from such audits since the amounts, if any, cannot be determined at this time.

A lawsuit was filed on August 9, 2013, styled Transcardiac Therapeutics, Inc. vs. Ajit Yoganathan, Ph.D., Jorge H. Jimenez, Ph.D., Vinod H. Thourani, M.D., Emory University, Georgia Tech Research Corporation, and Georgia Tech Foundation, Inc. Attorneys for GTRC filed an answer to the Complaint denying the allegations in the Complaint and asserting a counterclaim. Discovery in the case is in process and no trial date has been set. Although GTRC cannot predict the outcome of the lawsuit, GTRC believes the claims are meritless and intends to vigorously defend the lawsuit.