

Starlight Children's Foundation

Financial Statements

December 31, 2017



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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Starlight Children's Foundation
Culver City, California

We have audited the accompanying financial statements of Starlight Children's Foundation (a California nonprofit corporation) (the "Foundation"), which comprise the statement of financial position as of December 31, 2017, and the related statements of activities, functional expenses, and cash flows for the year then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America (the "U.S."); 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 U.S. 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 the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Starlight Children's Foundation as of December 31, 2017, and the changes in its net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the U.S.

Change in Accounting Principle

As described in Note 2 to the financial statements, the Organization has elected early adoption of the Financial Accounting Standards Board Accounting Standards Update ("ASU") 2016-14, *Presentation of Financial Statements for Not-for-Profit Entities*. Our opinion is not modified with respect to that matter.

A handwritten signature in black ink that reads "Armanino LLP". The signature is written in a cursive, flowing style.

Armanino^{LLP}
Los Angeles, California

May 10, 2018

Starlight Children's Foundation
Statement of Financial Position
December 31, 2017

ASSETS

Cash and cash equivalents	\$ 725,768
Investments	7,032,908
Contributions and pledges receivable	491,020
Inventory	162,086
Prepaid and other assets	584,727
Property and equipment, net	<u>47,876</u>
Total assets	<u><u>\$ 9,044,385</u></u>

LIABILITIES AND NET ASSETS

Liabilities	
Accounts payable and accrued liabilities	\$ 580,095
Deferred revenue	1,250,000
Deferred rent	<u>53,853</u>
Total liabilities	<u><u>1,883,948</u></u>
Commitments (Notes 8 and 10)	
Net assets	
Without donor restrictions	
Undesignated	4,268,908
Board-designated reserve	<u>2,000,000</u>
Total without donor restrictions	6,268,908
With donor restrictions	<u>891,529</u>
Total net assets	<u><u>7,160,437</u></u>
Total liabilities and net assets	<u><u>\$ 9,044,385</u></u>

The accompanying notes are an integral part of these financial statements.

Starlight Children's Foundation
Statement of Activities
For the Year Ended December 31, 2017

	<u>Without Donor Restrictions</u>	<u>With Donor Restrictions</u>	<u>Total</u>
Revenues, gains and other support			
Contributed goods, services, and use of facilities	\$ 3,114,724	\$ -	\$ 3,114,724
Contributions	4,916,581	3,177,057	8,093,638
Revenue from related parties	60,581	-	60,581
Proceeds from fundraising events, net of direct benefit to donors of \$5,455	53,545	-	53,545
Investment income	39,288	-	39,288
Miscellaneous	64,840	-	64,840
Net assets released from restriction	<u>2,678,610</u>	<u>(2,678,610)</u>	<u>-</u>
	<u>10,928,169</u>	<u>498,447</u>	<u>11,426,616</u>
Functional expenses			
Program services	8,358,203	-	8,358,203
Management and general	824,699	-	824,699
Fundraising	<u>816,465</u>	<u>-</u>	<u>816,465</u>
Total functional expenses	<u>9,999,367</u>	<u>-</u>	<u>9,999,367</u>
Change in net assets	928,802	498,447	1,427,249
Net assets, beginning of year	<u>5,340,106</u>	<u>393,082</u>	<u>5,733,188</u>
Net assets, end of year	<u>\$ 6,268,908</u>	<u>\$ 891,529</u>	<u>\$ 7,160,437</u>

The accompanying notes are an integral part of these financial statements.

Starlight Children's Foundation
Statement of Functional Expenses
For the Year Ended December 31, 2017

	Starlight Fun Centers	Starlight Sites	Starlight Special Deliveries	Starlight Wish Lists	Starlight Gowns	Starlight Virtual Reality	Star Visits	Dream Halloween	Program General	Total program services	Management and General	Fundraising	Total
Advertising	\$ 46	\$ 4	\$ 63	\$ 30	\$ 189	\$ 257	\$ 92	\$ 26	\$ -	\$ 707	\$ 2,668	\$ 2,177	\$ 5,552
Bank charges	-	-	-	-	-	-	-	-	-	-	556	-	556
Depreciation	1,717	136	2,371	1,103	7,060	4,664	3,430	961	-	21,442	11,183	6,603	39,228
Donated professional services	2,262	179	3,124	1,453	72,461	155,572	4,519	6,077	77,438	323,085	14,732	54,552	392,369
Donated materials and supplies	-	-	2,142,088	150	298,752	-	-	117,909	-	2,558,899	-	-	2,558,899
Donated use of facilities	6,013	477	8,305	3,864	24,730	16,338	12,016	3,366	-	75,109	39,172	23,129	137,410
Equipment for program use	825,729	-	-	177,330	1,829,092	906	-	-	50,182	2,883,239	-	-	2,883,239
Equipment rental and repair	31,360	11	192	89	573	378	278	1,654	-	34,535	908	536	35,979
Facilities rent and parking	6,705	532	9,261	4,308	27,576	18,218	13,399	3,754	-	83,753	43,680	25,791	153,224
Fees	-	-	-	-	-	-	-	-	-	-	1,850	39,372	41,222
Insurance	1,520	121	2,100	977	6,253	4,131	3,038	851	-	18,991	9,905	5,848	34,744
IT Services	3,920	311	5,433	64,493	16,224	10,649	7,832	2,299	1,080	112,241	43,012	31,504	186,757
Membership dues	15	1	20	9	60	1,164	29	8	96	1,402	95	56	1,553
Miscellaneous	430	33	574	267	2,172	7,405	1,968	881	(146)	13,584	8,148	21,871	43,603
Postage, shipping, and delivery	104,227	134	146,158	2,747	89,921	1,310	442	306	10,168	355,413	695	508	356,616
Printing and publications	845	207	803	374	13,604	3,834	1,178	6,469	244	27,558	3,855	2,835	34,248
Professional services	9,998	2,281	8,951	4,164	168,459	152,488	19,237	200,081	-	565,659	80,941	264,729	911,329
Regulatory and other renewal fees	140	11	194	90	852	381	280	503	-	2,451	1,069	6,800	10,320
Renovation expense - Starlight Sites	-	200,000	-	-	-	-	-	-	-	200,000	-	-	200,000
Salaries and employee benefits	76,018	643	106,947	44,739	345,504	218,573	139,256	50,050	-	981,730	539,815	296,341	1,817,886
Supplies	120	35	165	77	542	926	1,316	647	-	3,828	783	481	5,092
Telephone	1,067	85	1,473	685	4,387	2,898	2,132	597	-	13,324	6,949	4,103	24,376
Travel and automobile	4,531	3,560	1,378	245	13,882	34,352	8,698	6,450	8,157	81,253	14,683	29,229	125,165
	<u>\$ 1,076,663</u>	<u>\$ 208,761</u>	<u>\$ 2,439,600</u>	<u>\$ 307,194</u>	<u>\$ 2,922,293</u>	<u>\$ 634,444</u>	<u>\$ 219,140</u>	<u>\$ 402,889</u>	<u>\$ 147,219</u>	<u>\$ 8,358,203</u>	<u>\$ 824,699</u>	<u>\$ 816,465</u>	<u>\$ 9,999,367</u>

The accompanying notes are an integral part of these financial statements.

Starlight Children's Foundation
Statement of Cash Flows
For the Year Ended December 31, 2017

Cash flows from operating activities	
Change in net assets	\$ 1,427,249
Adjustments to reconcile change in net assets to net cash provided by operating activities	
Donated inventory	(20,595)
Depreciation and amortization	39,228
Deferred rent	53,853
Warranty reserve	(25,000)
Changes in operating assets and liabilities	
Contributions and pledges receivable	(470,907)
Inventory	(102,391)
Prepaid and other assets	288,493
Accounts payable and accrued liabilities	97,082
Deferred revenue	<u>(1,030,000)</u>
Net cash provided by operating activities	<u>257,012</u>
Cash flows from investing activities	
Investment income reinvested	(39,288)
Purchases of investments	(25,043,733)
Proceeds from sales of investments	22,049,000
Purchases of property and equipment	<u>(24,690)</u>
Net cash used in investing activities	<u>(3,058,711)</u>
Net decrease in cash and cash equivalents	(2,801,699)
Cash and cash equivalents, beginning of year	<u>3,527,467</u>
Cash and cash equivalents, end of year	<u>\$ 725,768</u>

The accompanying notes are an integral part of these financial statements.

Starlight Children's Foundation
Notes to Financial Statements
December 31, 2017

1. ORGANIZATION

Founded in 1982, Starlight Children's Foundation raises funds and awareness to improve the lives of children with serious illnesses and their families through the provision of Starlight program services with over 700 hospital partners within the United States.

During 2017, in addition to its established programs, Starlight launched a new program, Starlight Gowns, which provides fun and comfortable gowns to hospitalized children. In its first year, over 141,000 gowns were provided to hospital partners across the United States. Another new initiative, Starlight's virtual reality program, which will transport hospitalized kids to anywhere in the world, was in development as of December 31, 2017. These new programs are intended to provide comfort, joy, entertainment, distraction and inspiration to hospitalized kids throughout the U.S.

Starlight Children's Foundation also provides ongoing programs throughout the United Kingdom, Canada, and Australia through international affiliates ("International Affiliates"). Affiliate Agreements entered into between each International Affiliate and Starlight provide for common purposes and policy direction.

The accompanying financial statements were prepared to present the financial information of Starlight Children's Foundation (referred to herein as the "Foundation") in the United States. The Foundation has agreements with International Affiliates in Australia, UK, and Canada. These affiliates operate independently, and the Foundation does not exercise control, nor does it have economic interests in the Affiliates. Therefore, the financial results of the Affiliates are not consolidated into the accompanying financial statements, based on Accounting Standards Codification (ASC) 958-810-25, *Consolidation*.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Change in Accounting Principle

The Foundation has elected early adoption of the Financial Accounting Standards Board Accounting Standards Update ("ASU") 2016-14, *Presentation of Financial Statements for Not-for-Profit Entities*. The standard requires that (1) net assets be classified and presented in two categories: net assets without donor restrictions and net assets with donor restrictions and (2) additional disclosures concerning the liquidity of the Organization, among other requirements.

Basis of presentation

The accompanying financial statements have been prepared on the accrual basis of accounting in accordance with U.S. generally accepted accounting principles.

Net Assets

The Foundation's net assets and changes therein are classified and reported as follows:

Starlight Children's Foundation
Notes to Financial Statements
December 31, 2017

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Net Assets (continued)

- *Without Donor Restrictions* - Net assets available for use in general operations and not subject to donor (or certain grantor) restrictions. The governing board has designated, from net assets without donor restrictions, net assets for an operating reserve.
- *With donor restrictions* - Net assets subject to donor- (or certain grantor-) imposed restrictions. Some donor-imposed restrictions are temporary in nature, such as those that will be met by the passage of time or other events specified by the donor. Other donor-imposed restrictions are perpetual in nature, where the donor stipulates that resources be maintained in perpetuity. Donor-imposed restrictions are released when a restriction expires, that is, when the stipulated time has elapsed, when the stipulated purpose for which the resource was restricted has been fulfilled, or both.

Cash and cash equivalents

The Foundation considers all highly liquid debt instruments purchased with original maturities of three months or less to be cash and cash equivalents. The carrying value of cash and cash equivalents at December 31, 2017 approximates its fair value. The Foundation had no cash equivalents as of December 31, 2017.

The Foundation maintains its cash, cash equivalents, and investments in bank deposit accounts and other investment accounts, which, at times, may exceed federally insured limits. The Foundation has not experienced any losses in such accounts.

Investments

The Foundation maintains investments in short-term U.S. Government Treasury bills. The term of the bills is 90 days.

Contributions and pledges receivable

Contributions, including pledges, representing unconditional promises to give are recorded at estimated fair value, and recognized as revenue in the period received. The Foundation reports unconditional contributions as restricted support if they are received with donor stipulations that limit the use of the donated assets. Total pledges receivable are expected to be collected in their entirety within one year.

The Foundation had three donors which made up 38% of total contributions for the year ended December 31, 2017.

Starlight Children's Foundation
Notes to Financial Statements
December 31, 2017

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Inventory

Inventory is comprised of materials that will be placed in hospital partner facilities for the use of hospitalized children. Inventory includes video game players, monitors, and other electronics that make up the Starlight Fun Center units. Other inventory includes Starlight Comfort Kit backpacks and other materials collected for distribution through the Foundation's programs. Purchased inventory is stated at cost. Donated inventory is recorded at estimated fair value at the time of donation. The Foundation reviews the carrying value of its inventory for possible impairment whenever events or changes in circumstances indicate that the fair value may have declined since it was originally acquired. An impairment loss is recognized when the fair value of the inventory is lower than the carrying amount, in which case a write-down is recorded to reduce the related asset to its estimated fair value. No impairment losses were recognized during the year ended December 31, 2017 for donated materials and supplies.

Prepaid and other assets

Prepaid and other assets primarily include a prepayment to Nintendo of America of \$437,772 as advance payment for the production and maintenance of Starlight fun centers which are placed in hospital partner facilities for hospitalized kids.

Property and equipment

Property and equipment having a useful life of more than one year are recorded at cost if purchased. Donated assets are capitalized at the estimated fair value at the date of receipt and restrictions are released once the asset has been placed into service. Depreciation is computed on the straight-line basis over the estimated useful lives of the related assets. Maintenance and repair costs are charged to expenses as incurred. Property and equipment are capitalized if the cost of an asset is greater than or equal to \$5,000. The estimated useful lives of property and equipment are as follows:

Software and computers	5 years
Furniture and fixtures	7 years

Leasehold improvements are amortized on the straight-line basis over the term of the lease or the estimated useful life, whichever is shorter.

Long-lived assets

The Foundation reviews the carrying values of its long-lived assets for possible impairment whenever events or changes in circumstances indicate that the book value of the assets may not be recoverable. An impairment loss is recognized when the sum of the undiscounted future cash flows is less than the carrying amount of the asset, in which case a write-down is recorded to reduce the related assets to its estimated fair value. No impairment losses were recognized during the year ended December 31, 2017.

Starlight Children's Foundation
Notes to Financial Statements
December 31, 2017

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Deferred revenue

Deferred revenue consists of funding that has been received as of December 31, 2017 under agreements which require the Foundation to develop specific program plans and secure the approval of donors prior to utilization of funds. The conditions are anticipated to be met during 2018.

Contributed goods, services, and use of facilities

Contributions of donated noncash assets are recorded at fair value in the period received. Contributions of donated services that create or enhance nonfinancial assets or that require specialized skills, are provided by individuals possessing those skills, and would typically need to be purchased if not provided by donation, are recorded at fair value in the period received. Contributed goods generally consist of materials for distribution to hospital partner facilities. For the year ended December 31, 2017, the Foundation received \$3,114,724 of contributed goods, services, and use of facilities.

Fair value of financial instruments

Fair value determination - The fair value of the Foundation's financial instruments as of December 31, 2017 represents management's best estimates of the amounts that would be received to sell those assets in an orderly transaction between market participants at that date. Those fair value measurements maximize the use of observable inputs. However, in situations where there are little, if any, observable inputs, management's own judgments about the assumptions of market participants were used in pricing the asset. Although the Foundation uses its best judgment in determining the fair value of financial instruments, there are inherent limitations in any methodology. Therefore, the values presented herein are not necessarily indicative of the amount the Foundation could realize in a current transaction. Future confirming events could affect the estimates of fair value and could be material to the financial statements. These events could also affect the amount realized upon liquidation of the financial instruments.

Fair value hierarchy - The Foundation's fair value hierarchy prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets (Level 1 measurements) and the lowest priority measurements involving significant unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are as follows:

- Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets that the Foundation has the ability to access at the measurement date.
- Level 2 inputs are inputs other than quoted prices included within Level 1 that are observable for the asset, either directly or indirectly, such as quoted prices for similar assets or liabilities, quoted prices in markets that are not active, or other observable inputs that can be corroborated by observable market data.

Starlight Children's Foundation
Notes to Financial Statements
December 31, 2017

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Fair value hierarchy (continued)

- Level 3 inputs are unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the asset.

The level in the fair value hierarchy within which a fair value measurement in its entirety falls is based on the lowest-level input that is significant to the fair value measurement in its entirety.

Due to the short-term nature of cash equivalents, receivables, other assets, accounts payable, and accrued liabilities, fair value approximates carrying value.

Income taxes

The Foundation is exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Service Code and corresponding California provisions. However, the Foundation remains subject to income taxes on any net income that is derived from a trade or business, regularly carried on and not in furtherance of the purpose for which it was granted exemption. No income tax provision has been recorded as the net income, if any, from any unrelated trade or business, in the opinion of management, is not material to the financial statements taken as a whole.

ASC Topic 740, *Income Taxes* (ASC 740), prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return, and provides guidance on derecognition, classification, interest and penalties, disclosure, and transition. Management believes that there are no such uncertain tax positions for the Foundation at December 31, 2017.

The Foundation's federal income tax and informational returns for tax years ended December 31, 2013 and subsequent remain open to examination by the Internal Revenue Service. The returns for California, the Foundation's only state tax jurisdiction, remain open to examination by the California Franchise Board for tax years ended December 31, 2014 and subsequent.

Use of estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, revenues and expenses as of the date and for the period presented. Actual results could differ from those estimates.

Functional allocation of expenses

The costs of providing the Foundation's programs and other activities have been presented in the statement of functional expenses. Indirect or shared costs are allocated among program and support services by a method that best measures the relative degree of benefit.

Starlight Children's Foundation
Notes to Financial Statements
December 31, 2017

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Subsequent events

The Foundation has evaluated events through May 10, 2018, the date the financial statements were available to be issued, and determined that no matters required disclosure.

3. INVESTMENTS

The following table sets forth by level, within the fair value hierarchy, the Foundation's assets at fair value as of December 31, 2017:

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Fair Value</u>
U.S. Treasury bills	\$ 7,032,908	\$ -	\$ -	\$ 7,032,908

4. PROPERTY AND EQUIPMENT

Property and equipment consists of the following:

Software and computers	\$ 673,598
Furniture and fixtures	31,824
Leasehold improvements	13,670
Total	719,092
Accumulated depreciation and amortization	(671,216)
Property and equipment net	\$ 47,876

Depreciation expense was \$39,228 for the year ended December 31, 2017.

5. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

Accounts payable and accrued liabilities consist of the following:

Accounts payable	\$ 224,766
Accrued payroll	21,243
Accrued paid time off	78,404
Accrued warranty reserve - Starlight Fun Center units	200,000
Other accrued liabilities	55,682
Total accounts payable and accrued liabilities	\$ 580,095

The \$200,000 warranty reserve relates to Starlight Fun Center units purchased from Nintendo of America. The Foundation is required to repair Starlight Fun Center units donated to healthcare facilities for 3 years after the units are distributed to the respective facilities.

Starlight Children's Foundation
Notes to Financial Statements
December 31, 2017

6. CONTRIBUTED GOODS, SERVICES, AND USE OF FACILITIES

Contributed goods, services, and use of facilities consist of the following:

Donated professional services	\$ 392,369
Donated materials and supplies	2,584,945
Donated use of facilities	<u>137,410</u>
Total	<u><u>\$ 3,114,724</u></u>

7. TEMPORARILY RESTRICTED NET ASSETS

Temporarily restricted net assets comprise the following:

Purpose restricted	\$ 845,509
Time-restricted	<u>46,020</u>
	<u><u>\$ 891,529</u></u>

In addition to the \$46,020 shown above, there are an additional \$445,000 of time-restricted net assets that are also purpose restricted. The total of these amounts, \$491,020, are shown as contributions and pledges receivable in the accompanying statement of financial position.

8. DEFINED CONTRIBUTION PENSION PLAN

The Foundation maintains a 403(b) defined contribution pension plan to which employees may contribute. The Foundation matches all contributions up to a maximum of 3% of annual salary. In 2017, the Foundation made \$29,315 in matching contributions for the year ended December 31, 2017.

9. RELATED PARTY TRANSACTIONS

The accounts of the Foundation's International Affiliates in the United Kingdom, Australia and Canada are not included in the accompanying 2017 financial statements. During 2017, the Foundation provided Starlight Fun Center units to its Canadian affiliate. During the fiscal year 2017, the Foundation received revenue for Starlight Fun Center units from the Canadian affiliate totaling \$60,581. There were no receivables from and payables to International Affiliates at December 31, 2017.

Starlight Children's Foundation
Notes to Financial Statements
December 31, 2017

10. COMMITMENTS

The Foundation leases certain facilities and equipment under long-term operating lease agreements that expire through November 2022. Future minimum lease payments for leases that have a remaining noncancelable term in excess of one year as follows:

		\$	
2018			134,676
2019			202,096
2020			207,792
2021			213,658
2022			<u>200,489</u>
Total noncancelable lease commitments			<u>\$ 958,711</u>

Facilities rent expenses were \$128,968 and equipment rent expenses were \$4,758 during the year ended December 31, 2017.

11. LIQUIDITY AND AVAILABILITY

Financial assets available for general expenditure, that is, without donor or other restrictions limiting their use, within one year of the balance sheet date, comprise the following:

Cash and cash equivalents		\$	725,768
Investments			7,032,908
Contributions and pledges receivable			<u>491,020</u>
			8,249,696
Board-designated reserve			<u>(2,000,000)</u>
		<u>\$</u>	<u>6,249,696</u>

As part of Starlight's liquidity management plan, cash in excess of daily requirements is invested in treasury securities.

Over the past few years, Starlight has accumulated substantial cash which is reflected in net assets. A key component of the current cash balance is prepaid donations for use in the new virtual reality program in 2018 of \$2.05 million. Starlight intends to use Funds in excess of what is needed for the virtual reality program and to ensure financial stability in increased discretionary spending on placement of Starlight fun centers and Starlight gowns and other Starlight programs.

The Board-designated reserve of \$2,000,000 was created to ensure ongoing operations in the event of unforeseen shortfalls and represents approximately five and one-half months of operating expenses. It is subject to expenditure only upon the approval of the Board of Directors. These funds are held in short-term investment accounts.