



Riverside Research Institute and Subsidiary

Consolidated Financial Statements and
Supplementary Information

November 30, 2018 and 2017

Riverside Research Institute and Subsidiary

Table of Contents

November 30, 2018 and 2017

	<u>Page</u>
Independent Auditors' Report	1
Financial Statements	
Consolidated Statements of Financial Position	3
Consolidated Statements of Activities and Changes in Net Assets, Retained Earnings (Deficit) and Noncontrolling Interest	4
Consolidated Statements of Cash Flows	5
Notes to Consolidated Financial Statements	6
Supplementary Information	
Consolidating Statement of Financial Position	21
Consolidating Statement of Activities and Changes in Net Assets, Retained Earnings and Noncontrolling Interest	22

Independent Auditors' Report

To the Board of Trustees of
Riverside Research Institute and Subsidiary

We have audited the accompanying consolidated financial statements of Riverside Research Institute and Subsidiary, which comprise the consolidated statements of financial position as of November 30, 2018 and 2017, and the related consolidated statements of activities and changes in net assets, retained earnings (deficit) and noncontrolling interest, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Consolidated 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 audits to obtain reasonable assurance about whether the consolidated financial statements are free from 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 entities' 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 entities' 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 financial position of Riverside Research Institute and Subsidiary as of November 30, 2018 and 2017, and the changes in their net assets, retained earnings (deficit) and noncontrolling interest and their cash flows for the years then ended, in accordance with accounting principles generally accepted in the United States of America.

Report on Consolidating Information

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The consolidating information presented on pages 21 and 22 is presented for the purposes of additional analysis of the consolidated financial statements rather than to present the financial position, changes in net assets, retained earnings and noncontrolling interest, and cash flows of the individual organizations, and is not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The consolidating information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the consolidating information is fairly stated, in all material respects, in relation to the consolidated financial statements as a whole.

Baker Tilly Virchow Krause, LLP

New York, New York
April 1, 2019

Riverside Research Institute and Subsidiary

Consolidated Statements of Financial Position

(In Thousands)

November 30, 2018 and 2017

	<u>2018</u>	<u>2017</u>
Assets		
Current Assets		
Cash	\$ 11,173	\$ 11,159
Investments	28,050	24,202
Accounts receivable, net	18,113	15,154
Prepaid expenses and other current assets	<u>1,084</u>	<u>1,244</u>
Total current assets	58,420	51,759
Assets whose use is limited	-	318
Property and equipment, net	16,016	16,004
Deferred tax assets	47	51
Interest rate swap	143	-
Other assets	<u>394</u>	<u>322</u>
Total assets	<u><u>\$ 75,020</u></u>	<u><u>\$ 68,454</u></u>
Liabilities and Net Assets, Retained Earnings (Deficit) and Noncontrolling Interest		
Current Liabilities		
Bond payable, current portion	\$ 345	\$ 335
Accounts payable and accrued expenses	12,343	9,596
Deferred revenue	520	926
Deferred rent, current portion	<u>287</u>	<u>92</u>
Total current liabilities	13,495	10,949
Bond payable, net of current portion	7,573	7,919
Deferred rent, net of current portion	1,210	1,506
Deferred compensation	137	81
Long-term incentive plan	635	406
Interest rate swap	<u>-</u>	<u>3</u>
Total liabilities	<u>23,050</u>	<u>20,864</u>
Net Assets and Retained Earnings (Deficit)		
Unrestricted	51,664	48,064
Retained earnings (deficit)	<u>242</u>	<u>(374)</u>
Total net assets and retained earnings (deficit)	<u>51,906</u>	<u>47,690</u>
Noncontrolling Interest		
	<u>64</u>	<u>(100)</u>
Total liabilities and net assets, retained earnings (deficit) and noncontrolling interest	<u><u>\$ 75,020</u></u>	<u><u>\$ 68,454</u></u>

See notes to consolidated financial statements

Riverside Research Institute and Subsidiary

Consolidated Statements of Activities and Changes in Net Assets, Retained Earnings (Deficit)
and Noncontrolling Interest
(In Thousands)

Years Ended November 30, 2018 and 2017

	2018	2017
Operating Revenue		
Contracts revenue	\$ 107,508	\$ 96,323
Grants revenue	1,308	1,953
Total operating revenue	<u>108,816</u>	<u>98,276</u>
Operating Expenses		
Direct labor	59,901	53,564
Subcontractors and other direct costs	14,668	15,415
Indirect costs	<u>29,551</u>	<u>26,176</u>
Total operating expenses	<u>104,120</u>	<u>95,155</u>
Changes in net assets and retained earnings (deficit) from operations before growth and outreach expense	4,696	3,121
Growth and outreach expense	<u>-</u>	<u>(2,201)</u>
Changes in net assets and retained earnings (deficit) from operations	<u>4,696</u>	<u>920</u>
Nonoperating Activities		
Interest income	46	20
Interest and fee expense	(240)	(313)
Investment income, net of fees	(55)	3,144
Unrealized gain on interest rate swap	146	112
Other income	<u>29</u>	<u>20</u>
Total nonoperating activities	<u>(74)</u>	<u>2,983</u>
Increase in net assets and retained earnings (deficit) before provision for (benefit from) income taxes	4,622	3,903
Provision for (benefit from) income taxes	<u>242</u>	<u>(1)</u>
Increase in net assets and retained earnings (deficit)	<u>4,380</u>	<u>3,904</u>
Net Assets and Retained Deficit, Beginning	47,690	43,737
Changes in net assets and retained earnings (deficit) attributable to: Riverside Research Institute	<u>4,216</u>	<u>3,953</u>
Net Assets and Retained Earnings (Deficit), Ending	<u><u>\$ 51,906</u></u>	<u><u>\$ 47,690</u></u>
Noncontrolling Interest, Beginning	\$ (100)	\$ (51)
Changes in retained earnings (deficit) attributable to: Noncontrolling interest	<u>164</u>	<u>(49)</u>
Noncontrolling Interest, Ending	<u><u>\$ 64</u></u>	<u><u>\$ (100)</u></u>

See notes to consolidated financial statements

Riverside Research Institute and Subsidiary

Consolidated Statements of Cash Flows
Riverside Research Institute and Subsidiary
Years Ended November 30, 2018 and 2017

	<u>2018</u>	<u>2017</u>
Cash Flows from Operating Activities		
Increase in net assets and retained earnings (deficit)	\$ 4,380	\$ 3,904
Adjustments to reconcile increase in net assets and retained earnings (deficit) to net cash flows from operating activities:		
Depreciation and amortization	1,859	2,363
Interest expense, debt issuance costs	23	23
Unrealized gain on interest rate swap	(146)	(112)
Loss on disposal of fixed assets	891	108
Net realized and unrealized losses (gains) on investments	759	(2,640)
Decrease in allowance for doubtful accounts	(118)	(22)
(Decrease) increase in deferred rent	(101)	58
Decrease in assets whose use is limited	318	3,727
Decrease in deferred tax assets	4	-
Increase in accounts receivable	(2,841)	(650)
Decrease (increase) in prepaid expenses and other current assets	160	(690)
Decrease (increase) in other assets	(72)	4
Increase in accounts payable and accrued expenses	2,747	1,802
Decrease in deferred revenue	(406)	(123)
Increase in deferred compensation	56	52
Increase in long-term incentive plan	229	261
Net cash flows from operating activities	<u>7,742</u>	<u>8,065</u>
Cash Flows from Investing Activities		
Purchases of investments	(4,607)	(2,263)
Capital expenditures	<u>(2,762)</u>	<u>(827)</u>
Net cash flows from investing activities	<u>(7,369)</u>	<u>(3,090)</u>
Cash Flows from Financing Activities		
Principal payments made on notes payable	-	(2,469)
Principal payments made on bond payable	<u>(359)</u>	<u>(349)</u>
Net cash flows from financing activities	<u>(359)</u>	<u>(2,818)</u>
Net change in cash	14	2,157
Cash, Beginning	<u>11,159</u>	<u>9,002</u>
Cash, Ending	<u><u>\$ 11,173</u></u>	<u><u>\$ 11,159</u></u>
Supplemental Disclosures of Cash Flow Information		
Cash paid during the year for interest	<u>\$ 240</u>	<u>\$ 313</u>
Cash paid during the year for income taxes	<u><u>\$ 204</u></u>	<u><u>\$ -</u></u>

See notes to consolidated financial statements

Riverside Research Institute and Subsidiary

Notes to Consolidated Financial Statements

(Dollars In Thousands)

November 30, 2018 and 2017

1. Organizations

Riverside Research Institute ("RRI") is a not-for-profit organization engaged in scientific and systems engineering research and program support services, primarily for the Department of Defense and other United States government agencies.

Applied Research Solutions, Inc. ("ARS") is a for-profit subsidiary of RRI, providing similar services as RRI as a qualified small business concern.

2. Summary of Significant Accounting Policies

The significant accounting policies followed by Riverside Research Institute and Subsidiary (together, the "Organization") in preparing the accompanying consolidated financial statements are as follows:

Presentation of Consolidated Financial Statements

The accompanying consolidated financial statements and notes to the consolidated financial statements are presented in thousands, except for the number of shares in Note 13.

Principles of Consolidation

The accompanying consolidated financial statements include the accounts of RRI and ARS. All intercompany account balances and transactions have been eliminated in consolidation. The non-controlling interest is the portion of the equity and earnings from the minority shareholders of ARS.

Basis of Accounting

The accompanying consolidated financial statements have been prepared on the accrual basis of accounting.

Net Asset Classification

The Organization is required to classify its net assets into three categories, which are unrestricted, temporarily restricted and permanently restricted.

Unrestricted net assets are reflective of revenues and expenses associated with the principal operating activities of the Organization and are not subject to donor-imposed stipulations. The Organization does not have any temporarily restricted or permanently restricted net assets as of November 30, 2018 and 2017.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America ("U.S. 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 consolidated financial statements, and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

Riverside Research Institute and Subsidiary

Notes to Consolidated Financial Statements

(Dollars In Thousands)

November 30, 2018 and 2017

Cash

Cash includes currency on hand and demand deposits with financial institutions. Interest bearing deposits with financial institutions are insured by the Federal Deposit Insurance Corporation ("FDIC") up to \$250 as of November 30, 2018 and 2017. Non-interest bearing deposits with financial institutions are insured by the FDIC up to the total account balance as of November 30, 2018 and 2017. The Organization maintains its cash in bank deposit accounts which at times may exceed the federally insured limits. The Organization has not experienced any losses in such accounts and management believes the Organization is not exposed to any significant credit risk.

Investments

Investments consist primarily of mutual funds that invest in stocks and bonds. Investments are reported at fair value based on quoted market prices in the consolidated statements of financial position. These investments are held in the custody of a major financial institution. Dividends and realized and unrealized gains and losses are reported as investment income from non-operating activities in the consolidated statements of activities and changes in net assets, retained earnings (deficit) and noncontrolling interest.

The financial markets' volatility may significantly impact the subsequent valuation of the Organization's investments. Accordingly, the valuation of investments may not necessarily be indicative of amounts that could be realized in a current market exchange.

Accounts Receivable

Billed accounts receivable represent amounts due under various contracts from the U.S. Government and commercial entities for services rendered or reimbursable direct and indirect costs incurred but unpaid as of each year-end. Unbilled accounts receivable represent costs and fees incurred for which the Organization had the right to bill and collect under the respective contracts, but were not billed to the customers prior to year end. Amounts unbilled as of November 30, 2018 and 2017, were subsequently billed.

Billed, net of allowance and unbilled accounts receivable as of November 30, 2018 and 2017, are as follows:

	<u>2018</u>	<u>2017</u>
Billed accounts receivable	\$ 16,788	\$ 13,468
Unbilled accounts receivable	<u>1,325</u>	<u>1,686</u>
Total accounts receivable	<u>\$ 18,113</u>	<u>\$ 15,154</u>

Management performs an analysis of accounts receivable to determine if any allowance for doubtful accounts is required. Factors considered in this analysis include aging of receivables and credit worthiness of the customers. Management arrives at an estimate of a reserve for any amounts not probable of collection at year end. As of November 30, 2018 and 2017, the allowance for doubtful accounts was \$10 and \$128, respectively.

Prepaid Expenses and Other Current Assets

Prepaid expenses and other current assets primarily consist of prepayments for insurance and other services.

Riverside Research Institute and Subsidiary

Notes to Consolidated Financial Statements

(Dollars In Thousands)

November 30, 2018 and 2017

Property and Equipment

The Organization capitalizes expenditures for property and equipment in excess of \$5 with estimated useful lives greater than one year. Property and equipment are recorded at cost and depreciated using the straight-line method over the estimated useful lives of the individual assets. Leasehold improvements are amortized using the straight-line method over the lesser of the estimated useful lives of the assets or the lease term. The Organization evaluates the remaining useful lives and recoverability of such assets on a continual basis.

The estimated useful lives of the assets are as follows:

Building	39 years
Building improvements	15 years
Furniture and fixtures	5 years
Computers and equipment	3 years
Leasehold improvements	2-10 years

Impairment of Long-Lived Assets

The Organization evaluates all long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying value of such assets may not be fully recoverable. Recoverability is evaluated by comparing the undiscounted future net cash flows resulting from the use of the asset and its eventual disposition to the carrying value of an asset. When the undiscounted future cash flows are less than the carrying value, impairment is deemed present. Management has concluded that no impairment to the Organization's long-lived assets was present as of November 30, 2018 and 2017.

Income Taxes

Income taxes are provided for the tax effect of transactions reported in the consolidated financial statements and consist of taxes currently due plus the change in deferred taxes. The Organization accounts for taxes using the liability method, whereby deferred tax assets and liabilities are recognized based on the future tax return consequences attributable to differences between the financial reporting and income tax basis of assets and liabilities. Valuation allowances are established, when necessary, to reduce deferred tax assets to the amount expected to be realized. Deferred income taxes are recorded using currently enacted income tax rates applicable in the period in which the deferred tax asset or liability is expected to be realized or settled. As changes in tax laws are enacted, deferred income taxes are adjusted through the provision for income taxes in the year of change.

The Internal Revenue Service has determined that RRI is exempt from federal income tax under Section 501(c)(3) of the Internal Revenue Code ("IRC"). RRI is also exempt from state income taxes. ARS is a C corporation for income tax purposes and therefore is subject to federal and state income taxation.

The Organization recognizes the tax benefit for uncertain tax positions when it is more likely than not the position will be sustained upon examination based on the technical merits of the position. The benefit is measured as the largest benefit that is more likely than not to be realized upon ultimate settlement. The Organization has not identified any material uncertain tax positions. The Organization is not currently under audit by any taxing jurisdiction.

Other Assets

Other assets consist of security deposits for the Organization's operating leases.

Riverside Research Institute and Subsidiary

Notes to Consolidated Financial Statements

(Dollars In Thousands)

November 30, 2018 and 2017

Debt Issuance Costs

Debt issuance costs, net of amortized interest expense, are reported as a direct deduction from the face amount of the related bond payable. Interest expense is computed using the straight-line method which approximates the interest method.

Deferred Revenue

The Organization bills its customers based on predetermined invoicing arrangements. When billed amounts are in excess of revenue recognized in accordance with the Organization's revenue recognition policies, a liability is recorded and classified as deferred revenue.

Deferred Compensation Agreement

The Organization maintains a deferred compensation agreement with an officer and accounts for this agreement in accordance with the terms of the underlying agreement. The Organization estimates the cost of future benefits and accrues the present value of those costs in a systematic and rational manner over the period in which the individual renders service and becomes eligible for the benefits. To the extent the terms of the agreement attribute all or a portion of the expected future benefits to an individual year of the individual's services, the cost of the benefits is recognized in that year.

Deferred Rent

Several of the Organization's operating leases contain predetermined rent escalations payable during the respective terms of the leases. For these leases, rent expense is recognized on a straight-line basis over the lease terms. The difference between the expense recognized and amounts payable under the leases during the year is recorded as deferred rent.

Revenue Recognition

Contracts revenue - The Organization generates revenue from services provided under both short-term and multi-year contracts. A majority of the Organization's contracts are priced based upon fixed-price arrangements, but also may be priced as reimbursable cost plus a fixed or award fee, or time and material as incurred. The Organization recognizes revenue when persuasive evidence of an arrangement exists, services have been rendered or goods delivered, the contract price is fixed and determinable, and collection of contractual fees is reasonably assured.

Under fixed-price contracts, the Organization is paid a predetermined fixed amount for a specified scope of work and generally has full responsibility for the costs associated with the contracts and the resulting profit or loss. Revenue on fixed-price contracts is recognized under the proportional performance method based on service delivery patterns over the period of contract performance, unless evidence suggests that revenue is earned or the obligations are fulfilled in a different pattern. Revenue from cost reimbursable contracts is measured and recognized as direct costs are incurred, including an allocation of allowable indirect costs, plus a proportional amount of the fixed fee. Revenue from time and materials contracts is measured and recognized based upon direct labor hours incurred, extended at contractual billing rates, plus any incurred and allowable other direct costs. Costs for all service contracts are expensed as incurred.

If the Organization's estimates indicate that a contract loss will occur, a loss provision is recorded in the period in which the loss is identified. Contract losses are determined to be the amount by which the estimated direct and certain indirect costs of the contract exceed the estimated total revenue that will be generated by the contract. Provisions for contract losses were not material to the consolidated financial statements as of November 30, 2018 or 2017.

Riverside Research Institute and Subsidiary

Notes to Consolidated Financial Statements

(Dollars In Thousands)

November 30, 2018 and 2017

Federal government contractors must also comply with applicable government procurement statutes and regulations and may be subject to potential contract termination, suspension and debarment from contracting with the government, or other remedies if they fail to comply with such regulations. Management believes the Organization has complied with all applicable procurement statutes and regulations. The Organization may provide reserves against amounts billed, collected, and recognized as revenues if and when a loss from such disputes is considered probable.

Grants Revenue

Grants revenue is recognized when the Organization incurs expenditures in compliance with restrictions designated in the grant documents.

Intergovernmental Personnel Act Mobility Program

The Organization participates in the Intergovernmental Personnel Act Mobility Program ("IPA"). Receipts under the IPA program, which are primarily based on payroll and fringe benefit costs of each IPA employee, are recorded net of costs, as the Organization is not the primary obligor for the services provided. The receipts under the IPA program for the years ended November 30, 2018 and 2017 were approximately \$146 and \$506, respectively.

Growth and Outreach Program

In accordance with RRI's not-for-profit status, during 2014, RRI began a program called Growth and Outreach as a vehicle for the Organization to reinvest earnings to further its mission to advance scientific research in the public interest and to extend its presence in the communities in which it operates. In the 2017 consolidated statement of activities and changes in net assets, retained earnings (deficit) and noncontrolling interest, RRI separated the Growth and Outreach expenses from normal operations. In the 2018 consolidated statement of activities and changes in net assets, retained earnings (deficit) and noncontrolling interest, RRI included the Growth and Outreach expenses as indirect costs instead of presenting them separately.

Recent Accounting Pronouncements

During May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2014-09, *Revenue from Contracts with Customers (Topic 606)*. The core principle of ASU 2014-09 requires recognition of revenue to depict the transfer of goods or services to customers at an amount that reflects the consideration for what an organization expects it will receive in association with this exchange. ASU 2014-09 is effective for the Organization for fiscal years beginning after December 15, 2018, with early adoption permitted. Management is currently evaluating the impact of ASU 2014-09 on the Organization's consolidated financial statements.

During 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 lease liabilities on the statement of financial position and disclosing key information about leasing arrangements. ASU 2016-02 is effective for the Organization for fiscal years beginning after December 15, 2019, with early adoption permitted. Management is currently evaluating the impact of ASU 2016-02 on the Organization's consolidated financial statements.

During August 2016, the FASB issued ASU 2016-14, *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities*. The new guidance is intended to improve and simplify the current net asset classification requirements and information presented in financial statements and notes that is useful in assessing a not-for-profit's liquidity, financial performance and cash flows. ASU 2016-14 is effective for fiscal years beginning after December 15, 2017, with early adoption permitted. ASU 2016-14 is to be applied retroactively with transition provisions. Management is currently evaluating the impact of ASU 2016-14 on the Organization's consolidated financial statements.

Riverside Research Institute and Subsidiary

Notes to Consolidated Financial Statements

(Dollars In Thousands)

November 30, 2018 and 2017

During November 2016, the FASB issued ASU 2016-18, *Statement of Cash Flows (Topic 230): Restricted Cash*. The amendments in this update require that a statement of cash flows explain the change during the period in the total of cash, cash equivalents and amounts generally described as restricted cash or restricted cash equivalents. Amounts generally described as restricted cash and restricted cash equivalents should be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period amounts shown on the statement of cash flows. ASU 2016-18 is effective for the Organization for fiscal years beginning after December 15, 2018, with early adoption permitted. ASU 2016-18 is to be applied retroactively with transition provisions. Management is currently evaluating the impact of ASU 2016-18 on the Organization's consolidated financial statements.

During June 2018, the FASB issued ASU 2018-08, *Not-for-Profit Entities (Topic 958): Clarifying the Scope and Accounting Guidance for Contributions Received and Contributions Made*. The amendments in this ASU should assist entities in (1) evaluating whether transactions should be accounted for as contributions (nonreciprocal transactions) or as exchange (reciprocal) transactions subject to other guidance and (2) determining whether a contribution is conditional. ASU 2018-08 is effective for the Organization for fiscal years beginning after December 15, 2018. Management is currently evaluating the impact of ASU 2018-08 on the Organization's consolidated financial statements.

Evaluation of Subsequent Events

The Organization has evaluated events and transactions for potential recognition or disclosure in the consolidated financial statements from the date of the consolidated statements of financial position through April 1, 2019, the date the consolidated financial statements were available for issuance.

3. Investments

Investments are summarized as follows as of November 30, 2018 and 2017:

	2018	
	Cost	Fair Value
Mutual funds:		
Short term bonds	\$ 9,488	\$ 9,036
Intermediate term bonds	2,318	2,255
Large blend	5,809	10,684
Foreign large blend	5,789	6,075
Total investments	\$ 23,404	\$ 28,050
	2017	
	Cost	Fair Value
Mutual funds:		
Short term bonds	\$ 7,653	\$ 7,570
Intermediate term bonds	1,896	1,883
Large blend	4,560	9,064
Foreign large blend	4,658	5,685
Total investments	\$ 18,767	\$ 24,202

Riverside Research Institute and Subsidiary

Notes to Consolidated Financial Statements

(Dollars In Thousands)

November 30, 2018 and 2017

The following schedule summarizes the net investment return reflected within the consolidated statements of activities and changes in net assets, retained earnings (deficit) and noncontrolling interest for the years ended November 30, 2018 and 2017:

	2018	2017
Interest and dividends	\$ 735	\$ 529
Realized gains	30	28
Unrealized (losses) gains	(789)	2,615
Investment fees	(31)	(28)
Investment income, net of fees	<u>\$ (55)</u>	<u>\$ 3,144</u>

4. Fair Value Measurements

The Organization measures fair value, the price that would be received from selling an asset or paid to transfer a liability (i.e., the "exit price") in an orderly transaction between market participants at the measurement date, in accordance with the Fair Value Measurement topic of the Accounting Standards Codification ("ASC").

In determining fair value, the Organization uses various valuation approaches. The Fair Value Measurement topic of the ASC establishes a hierarchy for inputs used in measuring fair value that maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that the most observable inputs be used when available.

The hierarchy is broken down into three levels based on the observability of inputs as follows:

Level 1 - inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets.

Level 2 - inputs to the valuation methodology include:

- quoted prices for similar assets or liabilities in active markets;
- quoted prices for identical or similar assets or liabilities in inactive markets;
- inputs other than quoted prices that are observable for the asset or liability;
- inputs that are derived principally from and corroborated by observable market data by correlation or other means.

If the asset or liability has a specified (contractual) term, the Level 2 input must be observable for substantially the full term of the asset or liability.

Level 3 - inputs to the valuation methodology are unobservable and significant to the fair value measurement.

The availability of observable inputs can vary from instrument to instrument and is affected by a wide variety of factors, including, for example, the type of instrument, whether the instrument is new and not yet established in the marketplace, the liquidity of markets, and other characteristics particular to the transaction. To the extent that valuation is based on models or inputs that are less observable or unobservable in the market, the determination of fair value requires more judgment. The valuation levels are not necessarily an indication of the risk or liquidity associated with the underlying assets and liabilities.

Riverside Research Institute and Subsidiary

Notes to Consolidated Financial Statements

(Dollars In Thousands)

November 30, 2018 and 2017

The following is a description of the valuation methodologies used for the assets and a liability measured at fair value. There have been no changes in the methodologies used at November 30, 2018 and 2017:

Mutual funds - Valued at the daily closing price as reported by the fund. The mutual funds are open-end mutual funds that are registered with the Securities and Exchange Commission. These funds are required to publish their daily net asset value ("NAV") and to transact at that price.

Interest rate swap - The Organization utilizes a mid-market level market valuation that is modeled on Bloomberg based on the terms set forth in the Swap Confirmation Agreement. The model uses the percentage of the London Interbank Offered Rate ("LIBOR") to forecast future cash flows over the remaining life of the swap.

The following tables present the fair value hierarchy for assets of the Organization measured at fair value as of November 30, 2018 and 2017:

2018				
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Other Unobservable Inputs (Level 3)	Total
Assets, mutual funds				
Short term bonds	\$ 9,036	\$ -	\$ -	\$ 9,036
Intermediate term bonds	2,255	-	-	2,255
Large blend	10,684	-	-	10,684
Foreign large blend	6,075	-	-	6,075
Total investments	<u>\$ 28,050</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 28,050</u>
Assets,				
Interest rate swap	<u>\$ -</u>	<u>\$ 143</u>	<u>\$ -</u>	<u>\$ 143</u>
2017				
Assets, mutual funds				
Short term bonds	\$ 7,570	\$ -	\$ -	\$ 7,570
Intermediate term bonds	1,883	-	-	1,883
Large blend	9,064	-	-	9,064
Foreign large blend	5,685	-	-	5,685
Total investments	<u>\$ 24,202</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 24,202</u>
Liability,				
Interest rate swap	<u>\$ -</u>	<u>\$ 3</u>	<u>\$ -</u>	<u>\$ 3</u>

Riverside Research Institute and Subsidiary

Notes to Consolidated Financial Statements

(Dollars In Thousands)

November 30, 2018 and 2017

5. Assets Whose Use is Limited

ARS satisfied their promissory note payable and outstanding line of credit balances during the year ended November 30, 2017 (see Note 7 for further details).

Under the terms of the Greene County Port Authority Economic Development Revenue Bond Series 2015 agreement, the bond proceeds are restricted for capital expenditures for the Dayton, Ohio facility. The bond proceeds not yet spent for their intended purpose amounted to \$0 and \$318 as of November 30, 2018 and 2017, respectively, and are classified as assets whose use is limited on the consolidated statements of financial position.

6. Property and Equipment

Property and equipment consists of the following as of November 30, 2018 and 2017:

	2018	2017
Land	\$ 698	\$ 698
Building and building improvements	13,445	13,363
Furniture and fixtures	4,567	4,572
Computers and equipment	1,125	2,358
Leasehold improvements	3,245	3,219
Construction-in-progress	2,216	261
	25,296	24,471
Less accumulated depreciation and amortization	(9,280)	(8,467)
Property and equipment, net	\$ 16,016	\$ 16,004

Depreciation and amortization expense charged to operations was approximately \$1,859 and \$2,363 for the years ended November 30, 2018 and 2017, respectively.

7. Notes Payable

During the year ended November 30, 2016, RRI obtained a line of credit facility with a commercial bank with a maximum limit of \$25,000. The line of credit was scheduled to expire on March 22, 2017 and was extended to May 31, 2019. The line employs a borrowing base to calculate line balances in excess of \$3,000. The line has an interest rate of LIBOR plus 170 basis points (LIBOR was 2.18 percent and 1.24 percent at November 30, 2018 and 2017, respectively). The line of credit is collateralized by all of the assets of RRI and a guaranty by ARS. The line was not utilized during the year ended November 30, 2018 and there were no balances as of November 30, 2018 and 2017, respectively.

ARS had a line of credit facility available with a commercial bank with a maximum limit of \$1,000. On February 14, 2017, the line of credit was paid in full and terminated, utilizing the proceeds from the preferred stock transaction between RRI and ARS as discussed in Note 13.

On June 25, 2017, ARS obtained a new \$1,000 line of credit from a commercial bank, which was set to expire on June 1, 2018 and was extended to May 29, 2019. The line bears interest at LIBOR plus 200 basis points (2.0 percent). The line of credit is guaranteed by RRI. As of November 30, 2018, the entire balance of the line of credit was fully available.

Riverside Research Institute and Subsidiary

Notes to Consolidated Financial Statements

(Dollars In Thousands)

November 30, 2018 and 2017

Interest expense was approximately \$0 and \$1 for the years ended November 30, 2018 and 2017, respectively.

On June 27, 2014, ARS entered into a promissory note agreement with a commercial bank in the original amount of \$3,000. The note was guaranteed by RRI. On January 23, 2017, ARS utilized the proceeds of the preferred stock transaction (as discussed in Note 13) with RRI to pay off the outstanding balance of approximately \$1,968, plus early payoff fees of approximately \$57.

Interest expense was approximately \$0 and \$8 for the years ended November 30, 2018 and 2017, respectively.

In accordance with the line of credit agreement, RRI and ARS are subject to certain financial covenants which require the Organization to maintain (on a consolidated basis) a funded debt ratio less than 65 percent of unrestricted net assets; at all times have a minimum unrestricted cash and investments of \$7,000; and a fixed coverage ratio of 1.20 to 1.00 at the end of each fiscal quarter. The Organization was in compliance with these covenants as of November 30, 2018.

8. Bond Payable

On December 15, 2015, RRI entered into a tax-exempt bond financing agreement with the Greene County Port Authority and a banking institution as trustee, purchaser and fiscal agent. RRI received \$9,000 in proceeds from the issuance of the Greene County Port Authority Economic Development Revenue Bond Series 2015. The bond principal is payable over a 20-year amortization term with a maturity date of December 24, 2035. Bond interest is payable monthly at a floating rate of 70 percent of the 30-day LIBOR plus 1.4 percent. At December 22, 2022 and annually thereafter, the banking institution may, at its option, tender the bond to RRI which will then have the option to pursue a refinancing transaction or otherwise obtain funds to pay the tender price.

The following is a schedule of future maturities of the bond payable for the years ending November 30:

Years ending November 30:	
2019	\$ 369
2020	380
2021	390
2022	401
2023	411
Thereafter	<u>6,061</u>
	8,012
Less net debt issuance costs	<u>(94)</u>
Total	<u>\$ 7,918</u>

Interest expense was approximately \$204 and \$182 for the years ended November 30, 2018 and 2017, respectively.

On December 23, 2015, RRI entered into an interest rate swap agreement with the same banking institution. The effect of the agreement is to fix the interest rate of the bond at 2.85 percent through December 22, 2022. For the years ended November 30, 2018 and 2017, RRI recognized unrealized gains of \$146 and \$112, respectively, which was as a result of fluctuations in the fair value of the interest rate swap.

Riverside Research Institute and Subsidiary

Notes to Consolidated Financial Statements

(Dollars In Thousands)

November 30, 2018 and 2017

In accordance with the tax-exempt bond financing agreement, RRI is subject to certain financial covenants which require RRI, on the last day of each fiscal quarter, to maintain (i) consolidated liquid assets consisting of cash and marketable securities of at least \$7,000; (ii) a ratio of funded debt to unrestricted net assets of not more than 0.65 to 1.00; and (iii) a consolidated fixed charge ratio of not less than 1.20:1.00. RRI was in compliance with these financial covenants as of November 30, 2018.

In addition, the bond proceeds are restricted for capital expenditures for the Dayton, Ohio facility. The bond proceeds not yet spent for their intended purpose amounted to \$0 and \$318 as of November 30, 2018 and 2017, respectively, and are classified as assets whose use is limited on the consolidated statements of financial position.

9. Accounts Payable and Accrued Expenses

Accounts payable and accrued expenses consist of the following as of November 30, 2018 and 2017

	2018	2017
Accrued salaries, bonus, and related payroll taxes	\$ 3,800	\$ 2,754
Other accrued expenses	3,443	960
Accrued PTO payable	3,092	2,719
Accounts payable	1,855	2,938
Accrued pension payable	153	225
Total accounts payable and accrued expenses	<u>\$ 12,343</u>	<u>\$ 9,596</u>

10. Deferred Compensation

During the year ended November 30, 2016, RRI entered into a deferred compensation agreement with an officer. In accordance with the agreement, RRI established a deferred compensation reserve account for the individual and provides a fixed monthly credit plus a quarterly compounded interest accrual based on the current prime rate, to the reserve account. To be eligible for the benefit, the agreement requires continuing employment until a specified time, and the account balance is then distributed based on an established vesting schedule, over a four-year period. Compensation expense, including interest accrual, related to the deferred compensation agreements was approximately \$55 and \$52 for the years ended November 30, 2018 and 2017, respectively.

11. Long-Term Incentive Plan

RRI has adopted a Long-Term Incentive Plan ("LTIP") for key employees and other eligible management employees which are based upon each employee agreement/contract and may include retention/sign-on bonuses. The LTIP incorporates a bonus compensation system based on performance measures that are aligned with RRI's strategic and operating goals, and was designed to promote the success of RRI. The LTIP award period is designed around a three-year period, and may be established by the Board at the beginning of each fiscal year. Amounts contributed to the LTIP and recorded as LTIP expense for the years ended November 30, 2018 and 2017 were approximately \$364 and \$355, respectively. As of November 30, 2018 and 2017, liabilities related to the LTIP were \$635 and \$406, respectively.

Riverside Research Institute and Subsidiary

Notes to Consolidated Financial Statements

(Dollars In Thousands)

November 30, 2018 and 2017

12. Commitments

The Organization is obligated for laboratory and office space under operating leases expiring on various dates through September 2024.

The following are the approximate minimum aggregate rental commitments under the lease obligations for the years ending November 30:

Years ending November 30:	
2019	\$ 2,248
2020	2,201
2021	2,008
2022	1,877
2023	1,403
	<hr/>
Total	<u>\$ 9,737</u>

Rent expense for the years ended November 30, 2018 and 2017 was approximately \$2,162 and \$2,203, respectively.

13. Stock

During 2012, the Organization reactivated its subsidiary, ARS and, with approval of the Board of Trustees of RRI, ARS granted restricted stock in ARS to two of its employees. A summary of ARS' restricted stock activity and related information for the year ended November 30, 2012 is as follows:

	<u>Shares</u>	<u>Weighted Average Grant Date Fair Value</u>
Restricted Stock Awards		
Outstanding at beginning of year	2,000	\$ -
Granted	-	-
Forfeited	-	-
	<hr/>	<hr/>
Outstanding at end of year	2,000	\$ -

The restricted stock vests 25 percent per year for four years commencing with the first anniversary date of the grant as long as the employee remains employed by ARS. As of November 30, 2018 and 2017, the two employees were 100 percent vested in the restricted stock.

All holders of common stock of ARS are restricted from selling or transferring their shares without the consent of RRI with the exception of transfers to a permitted transferee as defined by the shareholders' agreement. Except with regard to restrictions on selling, assigning, transferring, pledging, hypothecating, encumbering, or otherwise disposing of the restricted shares, the shareholders have all rights of a shareholder of ARS, including the right to receive dividends and vote.

If the employment of any holders of common stock of ARS is terminated at any time, RRI has the right to purchase any vested shares from the terminated shareholder within 90 days of the termination. The purchase price of vested shares is defined in the shareholders' agreement and is based on a trailing twelve months of earnings before interest, taxes, depreciation and amortization ("EBITDA") and a varying multiple which is also defined in the shareholders' agreement.

Riverside Research Institute and Subsidiary

Notes to Consolidated Financial Statements

(Dollars In Thousands)

November 30, 2018 and 2017

At the grant date, the value of the shares was insignificant as ARS had no assets or revenue and projections of future free cash flows were uncertain. As a result, the Organization has not recognized stock compensation expense related to the restricted stock agreements and no value was given to the stock that was transferred to the noncontrolling shareholders.

As of November 30, 2018 and 2017, ARS had 10,000 shares authorized, and 9,500 shares issued and outstanding. As of November 30, 2018 and 2017, two of ARS's employees each held 1,000 shares of common stock, while RRI held the remaining 7,500 shares issued and outstanding. As a result, approximately 21 percent of ARS's net equity position is reflected as a noncontrolling interest in the consolidated financial statements.

On December 12, 2016, RRI entered into a subscription agreement with ARS to purchase 250 shares of preferred stock, no par value per share, of ARS at a purchase price of \$10 per share. ARS utilized the proceeds from this preferred stock transaction to pay off in full the amounts outstanding on its line of credit and note payable during the year ended November 30, 2017.

The preferred stock does not entitle RRI any additional voting rights. In the event of any liquidation, dissolution or winding up of ARS, whether voluntary or involuntary, RRI as the "holder of each share of the preferred stock shall be entitled, prior to the common stock holders, to be paid out of the assets of ARS available for distribution" in amount equal to \$10 per share, plus all accrued and unpaid dividends (whether or not declared).

The preferred stock shall be redeemable, in whole or in part, at the discretion of ARS, at a price per share of \$10 per share, plus all accrued and unpaid dividends (with certain limits and restrictions). The preferred stock may not be reissued, however it may be issued in one or more series, from time to time within three (3) years from the date of first issuance of the shares.

As the holder of the preferred stock, RRI, is entitled to receive cumulative cash dividends at a rate of \$.6 per annum per share, payable quarterly on the first day of January, April, July and October each year. All accrued and accumulated dividends on the preferred stock shall be paid prior and in preference to any dividend on any common stock and any other class of securities. For the years ended November 30, 2018 and 2017, accumulated cash dividends ("dividends expense") amounted to \$150 and \$113, respectively. All payments and balances were eliminated on the consolidated financial statements.

14. Employee Benefit Plans

RRI maintains a tax sheltered retirement income (IRC 403(b)) plan (the "Plan") covering substantially all of its eligible employees. The Plan enables participants to make pretax salary contributions, within limits, through elective salary deferrals. RRI does not contribute to this plan.

RRI also maintains a defined-contribution plan covering all full-time employees of RRI who have at least one year of service and are at least age twenty-one years of age. RRI makes a contribution each year equal to a percentage of all participants' compensation. The contribution is dependent upon each employee's years of service. Participants are not permitted to contribute to this plan. Amounts contributed to this plan and recorded as pension expense for the years ended November 30, 2018 and 2017 were approximately \$2,930 and \$2,204, respectively.

ARS sponsors a 401(k) savings plan (the "Plan"). All ARS employees are eligible to participate after meeting certain age and service requirements as defined in the Plan document. ARS may make discretionary contributions to the Plan. Vesting of ARS contributions is graduated based on years of service. Contributions to the Plan were \$278 and \$171 for the years ended November 30, 2018 and 2017, respectively.

Riverside Research Institute and Subsidiary

Notes to Consolidated Financial Statements

(Dollars In Thousands)

November 30, 2018 and 2017

15. Income Taxes

The ARS provision for (benefit from) income taxes consists of the following for the years ended November 30, 2018 and 2017:

	<u>2018</u>	<u>2017</u>
Current		
Federal	\$ 226	\$ -
State	11	-
	<u>237</u>	<u>-</u>
Deferred		
Federal	5	(1)
State	-	-
	<u>5</u>	<u>(1)</u>
Total provision for (benefit from) income taxes	<u>\$ 242</u>	<u>\$ (1)</u>

Deferred tax assets consist of the following as of November 30, 2018 and 2017:

	<u>2018</u>	<u>2017</u>
Net operating loss carryforward	\$ -	\$ 15
Accrued vacation	47	36
Deferred tax assets, net	<u>\$ 47</u>	<u>\$ 51</u>

Deferred tax assets are provided for those items for which the reporting period for income tax purposes is different than the reporting period for financial statement purposes.

16. Contingency

The majority of the Organization's revenues are generated from prime contracts or subcontracts for which the U.S. government is the ultimate customer. Changes in federal government budgetary priorities, domestic and international economic conditions, and political circumstances, among other factors, could impact the status of the Organization's current contracts and the Organization's ability to win new or follow-on contract awards. In the event of unilateral early termination by the customer or expiration without renewal, the loss of one or more of the Organization's significant contracts could have a material and adverse impact on the Organization's future financial results. As of November 30, 2018, the Organization's contracts expire from 2019 to 2023.

Customer Concentrations

For the year ended November 30, 2018, the Organization generated revenues under prime or subcontracts with two customers that collectively approximated 49 percent of total revenues: 25 percent from Customer A and 24 percent from Customer B. For the year ended November 30, 2017, the Organization generated revenues under prime or subcontracts with two customers that collectively approximated 48 percent of total revenues: 25 percent from Customer A and 23 percent from Customer B.

Riverside Research Institute and Subsidiary

Notes to Consolidated Financial Statements

(Dollars In Thousands)

November 30, 2018 and 2017

Litigation

The Organization is subject to lawsuits and claims with respect to matters arising in the normal course of business. In the opinion of management, the ultimate liabilities, if any, resulting from these lawsuits or claims, will not materially affect the consolidated financial position or results of operations of the Organization.

17. Functional Expenses

RRI's operating expenses grouped by functional classification for the years ended November 30, 2018 and 2017 are as follows:

	2018	2017
Program expenses	\$ 85,713	\$ 82,607
General and administrative expenses	7,524	6,794
Total expenses	<u>\$ 93,237</u>	<u>\$ 89,401</u>

Riverside Research Institute and Subsidiary

Consolidating Statement of Financial Position

(In Thousands)

November 30, 2018

	Riverside Research Institute	Applied Research Solutions	Eliminations	Consolidated
Assets				
Current Assets				
Cash	\$ 9,777	\$ 1,396	\$ -	\$ 11,173
Investments	30,742	-	(2,692)	28,050
Accounts receivable, net	15,735	2,475	(97)	18,113
Prepaid expenses and other current assets	980	104	-	1,084
Total current assets	57,234	3,975	(2,789)	58,420
Property and equipment, net	16,016	-	-	16,016
Deferred tax assets	-	47	-	47
Interest rate swap	143	-	-	143
Other assets	384	10	-	394
Total assets	<u>\$ 73,777</u>	<u>\$ 4,032</u>	<u>\$ (2,789)</u>	<u>\$ 75,020</u>
Liabilities and Net Assets, Retained Earnings and Noncontrolling Interest				
Current Liabilities				
Bond payable, current portion	\$ 345	\$ -	\$ -	\$ 345
Accounts payable and accrued expenses	11,412	1,028	(97)	12,343
Deferred revenue	520	-	-	520
Deferred rent, current portion	281	6	-	287
Total current liabilities	12,558	1,034	(97)	13,495
Bond payable, net of current portion	7,573	-	-	7,573
Redeemable preferred stock	-	2,500	(2,500)	-
Deferred rent, net of current portion	1,210	-	-	1,210
Deferred compensation	137	-	-	137
Long-term incentive plan	635	-	-	635
Total liabilities	22,113	3,534	(2,597)	23,050
Net Assets and Retained Earnings				
Unrestricted net assets	51,664	-	-	51,664
Additional paid-in capital	-	192	(192)	-
Retained earnings	-	306	(64)	242
Total net assets and retained earnings	51,664	498	(256)	51,906
Noncontrolling Interest				
	-	-	64	64
Total liabilities and net assets, retained earnings and noncontrolling interest	<u>\$ 73,777</u>	<u>\$ 4,032</u>	<u>\$ (2,789)</u>	<u>\$ 75,020</u>

Riverside Research Institute and Subsidiary

 Consolidating Statement of Activities and Changes in Net Assets, Retained Earnings and Noncontrolling Interest
 (In Thousands)

Year Ended November 30, 2018

	Riverside Research Institute	Applied Research Solutions	Eliminations	Consolidated
Operating Revenue				
Contracts revenue	\$ 95,224	\$ 13,018	\$ (734)	\$ 107,508
Grants revenue	1,308	-	-	1,308
Total operating revenue	96,532	13,018	(734)	108,816
Operating Expenses				
Direct labor	51,263	8,638	-	59,901
Subcontractors and other direct costs	13,793	1,609	(734)	14,668
Indirect costs	27,941	1,610	-	29,551
Total operating expenses	92,997	11,857	(734)	104,120
Changes in net assets and retained earnings from operations	3,535	1,161	-	4,696
Nonoperating Activities				
Interest income	35	11	-	46
Interest and fee expense	(240)	-	-	(240)
Dividends expense	-	(150)	150	-
Investment income, net of fees	95	-	(150)	(55)
Unrealized gain on interest rate swap	146	-	-	146
Other income	29	-	-	29
Total nonoperating activities	65	(139)	-	(74)
Increase in net assets and retained earnings before provision for income taxes	3,600	1,022	-	4,622
Provision for income taxes	-	242	-	242
Increase in net assets and retained earnings	3,600	780	-	4,380
Changes in net assets and retained earnings (deficit) attributable to:				
Riverside Research Institute	3,600	616	-	4,216
Noncontrolling interest	-	164	(164)	-
Net Assets and Retained Deficit, Beginning	48,064	(282)	(92)	47,690
Net Assets and Retained Earnings, Ending	<u>\$ 51,664</u>	<u>\$ 498</u>	<u>\$ (256)</u>	<u>\$ 51,906</u>
Noncontrolling Interest, Beginning	\$ -	\$ -	\$ (100)	\$ (100)
Changes in retained earnings (deficit) attributable to:				
Noncontrolling interest	-	-	164	164
Noncontrolling Interest, Ending	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 64</u>	<u>\$ 64</u>



Riverside Research Institute

Federal Awards

November 30, 2018

Riverside Research Institute

Table of Contents
November 30, 2018

	<u>Page</u>
Independent Auditors' Report on Consolidated Financial Statements	1
Independent Auditors' Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <i>Government Auditing Standards</i>	3
Independent Auditors' Report on Compliance for Each Major Federal Program; Report on Internal Control Over Compliance Required by the Uniform Guidance; and Report on Schedule of Expenditures of Federal Awards Required by the Uniform Guidance	5
Schedule of Expenditures of Federal Awards	7
Notes to Schedule of Expenditures of Federal Awards	8
Schedule of Findings and Questioned Costs	9

Independent Auditors' Report on Consolidated Financial Statements

To the Board of Trustees of
Riverside Research Institute

Report on the Consolidated Financial Statements

We have audited the accompanying consolidated financial statements of Riverside Research Institute and Subsidiary, which comprise the consolidated statements of financial position as of November 30, 2018 and 2017, and the related consolidated statements of activities and changes in net assets, retained earnings (deficit) and noncontrolling interest, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Consolidated 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 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 audits to obtain reasonable assurance about whether the consolidated financial statements are free from 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 entities' 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 entities' 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 Riverside Research Institute and Subsidiary as of November 30, 2018 and 2017, and the change in their net assets, retained earnings (deficit) and noncontrolling interest and their cash flows for the years then ended, in accordance with accounting principles generally accepted in the United States of America.

Report on Consolidating Information

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The consolidating information presented on pages 21 and 22 of the consolidated financial statements is presented for the purposes of additional analysis of the consolidated financial statements rather than to present the financial position, changes in net assets, retained earnings and noncontrolling interest, and cash flows of the individual organizations, and is not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The consolidating information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the consolidating information is fairly stated, in all material respects, in relation to the consolidated financial statements as a whole.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated April 1, 2019, on our consideration of Riverside Research Institute's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Riverside Research Institute's internal control over financial reporting and compliance.



New York, New York
April 1, 2019

**Independent Auditors' Report on Internal Control
Over Financial Reporting and on Compliance
and Other Matters Based on an Audit of
Financial Statements Performed in Accordance
with *Government Auditing Standards***

To the Board of Trustees of
Riverside Research Institute

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the consolidated financial statements of Riverside Research Institute and Subsidiary (the "Organization"), which comprise the statement of financial position as of November 30, 2018, and the related statements of activities and changes in net assets, retained earnings (deficit) and noncontrolling interest and cash flows for the year then ended, and the related notes to the consolidated financial statements, and have issued our report thereon dated April 1, 2019.

Internal Control Over Financial Reporting

In planning and performing our audit of the consolidated financial statements, we considered the Organization's internal control over financial reporting ("internal control") to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the consolidated financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Organization's internal control. Accordingly, we do not express an opinion on the effectiveness of the Organization's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's consolidated financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

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

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Organization's consolidated financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of consolidated financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the Organization's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Organization's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Baker Tilly Virchow Krause, LLP

New York, New York
April 1, 2019

**Independent Auditors' Report on Compliance
for Each Major Federal Program; Report on
Internal Control Over Compliance Required by
the Uniform Guidance; and Report on
Schedule of Expenditures of Federal Awards
Required by the Uniform Guidance**

To the Board of Trustees of
Riverside Research Institute

Report on Compliance for the Major Federal Program

We have audited Riverside Research Institute's (the "Organization") compliance with the types of compliance requirements described in the OMB Compliance Supplement that could have a direct and material effect on the Organization's major federal program for the year ended November 30, 2018. The Organization's major federal program is identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to its federal program.

Auditors' Responsibility

Our responsibility is to express an opinion on compliance for the Organization's major federal program based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States; and the audit requirements of Title 2 U.S. Code of Federal Regulations ("CFR") Part 200, Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards ("Uniform Guidance"). Those standards and the Uniform Guidance require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Organization's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

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

Opinion on the Major Federal Program

In our opinion, the Organization complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on its major federal program for the year ended November 30, 2018.

Report on Internal Control Over Compliance

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

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A material weakness in internal control over compliance is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. A significant deficiency in internal control over compliance is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

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

Purpose of this Report

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

Report on Schedule of Expenditures of Federal Awards Required by the Uniform Guidance

We have audited the consolidated financial statements of Riverside Research Institute and Subsidiary as of and for the year ended November 30, 2018, and have issued our report thereon dated April 1, 2019, which contained an unmodified opinion on those consolidated financial statements. Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by the Uniform Guidance and is not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the schedule of expenditures of federal awards is fairly stated in all material respects in relation to the consolidated financial statements as a whole.



New York, New York
August 7, 2019

Riverside Research Institute

Schedule of Expenditures of Federal Awards
Year Ended November 30, 2018

Federal Grantor/Pass-Through Grantor/Program Title	Federal CFDA Number	Direct or Pass-through Agency Identification	Federal Expenditures	Subrecipient Awards
Research and Development Cluster:				
United States Department of Health and Human Services - National Institutes of Health:				
Direct Awards:				
Discovery and Applied Research for Technological Innovations to Improve Human Health	93.286	1R01EB022950-01	\$ 549,971	\$ 384,520
Discovery and Applied Research for Technological Innovations to Improve Human Health	93.286	1R03EB026233-01	29,102	-
Cancer Detection and Diagnosis Research	93.394	1R01CA192407-01A1	592,652	145,178
Cancer Detection and Diagnosis Research	93.394	1R21CA212744-01	89,479	-
Vision Research	93.867	GG008110	39,430	-
Vision Research	93.867	2(GG013362-01)	29,464	-
Total United States Department of Health and Human Services			<u>1,330,098</u>	<u>529,698</u>
United States Department of Defense:				
Direct Awards:				
STARS IV	N/A	****-14-C-4128	1,199,870	-
Direct Awards from United States Department of Defense Major Subdivisions:				
Department of the Air Force:				
TENS-Scanner Accreditation Support	N/A	12.3678RRREDE	125,180	-
DRAGON/ECP Phase 3	N/A	4102999681	1,457,247	-
DRAGON/ECP Phase 3B	N/A	4103812421	131,694	-
Total United States Department of Defense			<u>2,913,991</u>	<u>-</u>
Total Research and Development Cluster			<u>4,244,089</u>	<u>529,698</u>
Total Expenditures of Federal Awards			<u>\$ 4,244,089</u>	<u>\$ 529,698</u>

1. Basis of Presentation

The accompanying schedule of expenditures of federal awards (the "schedule") includes the federal awards activity of Riverside Research Institute (the "Organization") under programs of the federal government for the year ended November 30, 2018. The information in the schedule is presented in accordance with the requirements of Title 2 U.S. Code of Federal Regulations ("CFR") Part 200, *Uniform Administrative Requirements and Audit Requirements for Federal Awards* ("Uniform Guidance"). The Organization is exempt from the Subpart E - Cost Principles of Part 200 in accordance with Appendix VIII of the Uniform Guidance. Because the schedule presents only a selected portion of the operations of the Organization, it is not intended to and does not present the financial position, changes in net assets, retained earnings (deficit) and noncontrolling interest or cash flows of the Organization.

2. Summary of Significant Accounting Policies

Expenditures reported on the schedule are reported on the accrual basis of accounting. Such expenditures are recognized following the Federal Acquisition Regulation, wherein certain types of expenditures are not allowable or are limited as to reimbursement. Negative amounts (when applicable) shown on the schedule represent adjustments or credits made in the normal course of business to amounts reported as expenditures in prior years. Pass-through entity identifying numbers are presented where available.

3. Indirect Cost Rate

Management of the Organization has not elected to use the 10 percent de minimis indirect cost rate.

4. Classified Contract

A contract was identified as classified national security information and could not be tested with respect to both Reporting requirements and Special Tests and Provisions requirements. The contract has been included on the accompanying schedule of expenditures of federal awards at the request of the Defense Contract Audit Agency.

Riverside Research Institute

Schedule of Findings and Questioned Costs
November 30, 2018

Section I - Summary of Auditors' Results

Consolidated Financial Statements

Type of auditors' report issued: Unmodified

Internal control over financial reporting:

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

Noncompliance material to financial statements noted? _____ Yes x No

Federal Awards

Internal control over major programs:

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

Type of auditors' report issued on compliance for major programs: Unmodified

Any audit findings disclosed that are required to be reported in accordance with 2 CFR 200.516(a)? _____ Yes x No

Identification of Major Program:

CFDA Number(s)	Name of Federal Program or Cluster
Various	Research and Development Cluster

Dollar threshold used to distinguish between Type A and Type B programs: \$750,000

Auditee qualified as low-risk auditee? _____ yes X no

Section II - Financial Statement Findings

None.

Section III - Federal Award Findings and Questioned Costs

None.