# THE AMERICAN RED CROSS

Consolidated Financial Statements

June 30, 2006

(With Independent Auditors' Report Thereon)

**KPMG LLP**
2001 M Street, NW
Washington, DC 20036

## Independent Auditors' Report

The Board of Governors
The American Red Cross:

We have audited the accompanying consolidated statement of financial position of the American Red Cross as of June 30, 2006, and the related consolidated statements of activities, functional expenses, and cash flows for the year then ended. These consolidated financial statements are the responsibility of management of the American Red Cross. Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We did not audit the financial statements of certain chapters, which statements reflect total assets constituting 11 percent and total revenues and gains constituting 23 percent of the related consolidated totals. Those statements were audited by other auditors whose reports have been furnished to us, and our opinion, insofar as it relates to amounts included for such chapters, is based solely on the reports of the other auditors. The prior year summarized comparative information has been derived from the American Red Cross' 2005 consolidated financial statements and, in our report dated September 30, 2005, we expressed an unqualified opinion on those consolidated financial statements.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the American Red Cross' internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, based on our audit and the reports of the other auditors, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the American Red Cross as of June 30, 2006, and the changes in its net assets and its cash flows for the year then ended in conformity with U.S. generally accepted accounting principles.

KPMG LLP

January 5, 2007

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member firm of KPMG International, a Swiss cooperative.

**DEPARTMENT OF THE ARMY**
**U.S. ARMY AUDIT AGENCY**
**OFFICE OF THE AUDITOR GENERAL**
**3101 PARK CENTER DRIVE**
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A-2007-0050-FFM 19 March 2007

Independent Auditor's Report

This report presents the results of our review of the independent certified public accountant's audit of the American Red Cross consolidated financial statements for the fiscal year ended 30 June 2006. In the auditor's opinion, the American Red Cross statements are presented, in all material respects, in accordance with accounting principles generally accepted in the United States.

The Act of Congress that incorporated the American Red Cross, as implemented by DOD Directive 1330.5 and AR 930-5, requires U.S. Army Audit Agency to perform an annual audit of the consolidated financial statements of the American Red Cross. The American Red Cross contracted with the certified public accounting firm of KPMG LLP as the principal auditor to perform the financial audit of its 2006 consolidated financial statements. To fulfill our audit responsibilities, avoid duplication and unnecessary expense, and make the most efficient use of our resources, we reviewed the principal auditor's work and reports.

The American Red Cross is the instrument chosen by an Act of Congress, approved January 5, 1905, to help carry out obligations the United States assumed under certain international treaties known as the Geneva or Red Cross Conventions. Its congressional charter imposes on the American Red Cross the duties to act as the medium of voluntary relief and communications between the American people and the Armed Forces, and to carry on a system of national and international relief to prevent and mitigate suffering caused by disasters.

We conducted our review of the principal auditor's work in accordance with generally accepted government auditing standards issued by the Comptroller General of the United States. To determine the reasonableness of the principal auditor's work and the extent to which we could rely on it, we:

- Reviewed the principal auditor's approach and planning of the audit.
- Evaluated the qualifications and independence of the audit staff.
- Reviewed the consolidated financial statements and principal auditor's report to evaluate compliance with generally accepted accounting principles.

- Reviewed and tested the principal auditor's working papers to determine (i) the nature, timing, and extent of audit work performed; (ii) the extent of audit quality control methods the auditor used; (iii) whether a study and evaluation was conducted of the entity's internal accounting controls; and (iv) whether the evidence in the working papers supported the principal auditor's opinion on the consolidated financial statements.

In the opinion of KMPG LLP, the American Red Cross consolidated financial statements present fairly, in all material respects, its financial position as of June 30, 2006 and the related statement of activities, functional expenses, the changes in its net assets, and its cash flow for the year ended, in conformity with accounting principles generally accepted in the United States. Also, KPMG LLP's report to the American Red Cross on internal controls did disclose a material weakness in the design and operation of controls related to financial assistance. However, this material weakness did not have a material effect on the financial statements.

We found nothing during our review to indicate that KPMG LLP's opinion on the American Red Cross 2006 consolidated financial statements is inappropriate or cannot be relied on.

During the course of its audit, KPMG LLP also identified several matters that, although not material to the financial statements, were communicated to the American Red Cross for consideration in a separate management letter.

We believe the consolidated financial statements, together with the KPMG LLP opinion and our review of that work, provide Congress with a dependable basis for evaluating the financial position of the American Red Cross. This report presents the American Red Cross consolidated financial statements and the auditor's opinion thereon.

We are sending copies of this report to the American Red Cross Board of Governors.

PATRICK J. FITZGERALD, CPA
The Auditor General

**THE AMERICAN RED CROSS**

Consolidated Statement of Financial Position

June 30, 2006
(with comparative information as of June 30, 2005)
(In thousands)

| **Assets** | | **2006** | | **2005** |
|---|---|---|---|---|
| Current assets: | | | | |
| Cash and cash equivalents | $ | 427,573 | $ | 292,559 |
| Investments (Notes 7, 8, and 13) | | 1,104,975 | | 741,504 |
| Trade receivables, including grants, net of allowance for doubtful accounts of $2,674 in 2006 and $9,836 in 2005 | | 133,748 | | 251,806 |
| Contributions receivable (Note 2) | | 97,121 | | 102,555 |
| Inventories, net of allowance for obsolescence of $618 in 2006 and $549 in 2005 | | 121,831 | | 152,060 |
| Other current assets | | 17,608 | | 17,252 |
| Total current assets | | 1,902,856 | | 1,557,736 |
| Investments (Notes 7, 8, and 13) | | 1,333,560 | | 1,217,875 |
| Contributions receivable (Note 2) | | 23,211 | | 22,712 |
| Pension intangible asset (Note 9) | | - | | 10,555 |
| Land, buildings, and other property, net (Note 3) | | 1,165,790 | | 1,098,840 |
| Other assets (Note 8) | | 87,579 | | 59,604 |
| Total assets | | 4,512,996 | | 3,967,322 |
| **Liabilities and Net Assets** | | | | |
| Current liabilities: | | | | |
| Accounts payable and accrued expenses | | 416,299 | | 385,203 |
| Current portion of debt (Note 4) | | 42,127 | | 86,697 |
| Postretirement benefits (Note 9) | | 31,302 | | 27,095 |
| Other current liabilities (Note 8) | | 24,960 | | 20,451 |
| Total current liabilities | | 514,688 | | 519,446 |
| Debt (Note 4) | | 389,023 | | 340,695 |
| Pension and postretirement benefits (Note 9) | | 306,448 | | 361,815 |
| Other liabilities (Note 8) | | 117,274 | | 99,245 |
| Total liabilities | | 1,327,433 | | 1,321,201 |
| Net assets (Note 6): | | | | |
| Unrestricted net assets | | 1,596,067 | | 1,319,460 |
| Temporarily restricted net assets | | 1,095,221 | | 856,594 |
| Permanently restricted net assets | | 494,275 | | 470,067 |
| Total net assets | | 3,185,563 | | 2,646,121 |
| Commitments and contingencies (Notes 4, 5, 12, 13 and 14) | | | | |
| Total liabilities and net assets | $ | 4,512,996 | $ | 3,967,322 |

See accompanying notes to the consolidated financial statements.

**THE AMERICAN RED CROSS**

Consolidated Statement of Activities

Year ended June 30, 2006
(with summarized information for the year ended June 30, 2005)
(In thousands)

| | Unrestricted | Temporarily Restricted | Permanently Restricted | Totals 2006 | Totals 2005 |
|---|---|---|---|---|---|
| Operating revenues and gains: | | | | | |
| Contributions: | | | | | |
| Corporate, foundation and individual giving | $ 258,002 | $ 2,387,042 | $ - | $ 2,645,044 | $ 976,674 |
| United Way and other federated | 60,025 | 102,275 | - | 162,300 | 158,990 |
| Legacies and bequests | 59,666 | 9,609 | 23,412 | 92,687 | 118,235 |
| Services and materials | 25,126 | 213,215 | - | 238,341 | 67,594 |
| Grants | 33,520 | 40,932 | - | 74,452 | 55,766 |
| Products and services: | | | | | |
| Biomedical | 2,165,172 | - | - | 2,165,172 | 2,137,209 |
| Program materials | 141,300 | 387 | - | 141,687 | 149,432 |
| Contracts, including federal government | 311,435 | - | - | 311,435 | 83,307 |
| Investment income (Note 7) | 108,570 | 1,409 | - | 109,979 | 68,615 |
| Other revenues | 67,528 | - | - | 67,528 | 103,435 |
| Net assets released from restrictions | 2,517,098 | (2,517,098) | - | - | - |
| Total operating revenues and gains | 5,747,442 | 237,771 | 23,412 | 6,008,625 | 3,919,257 |
| Operating expenses: | | | | | |
| Program services: | | | | | |
| Armed Forces Emergency Services | 54,096 | - | - | 54,096 | 58,646 |
| Biomedical services (Notes 12 and 13) | 2,103,572 | - | - | 2,103,572 | 2,161,078 |
| Community services | 133,467 | - | - | 133,467 | 128,548 |
| Domestic disaster services | 2,630,766 | - | - | 2,630,766 | 411,187 |
| Health and safety services | 224,594 | - | - | 224,594 | 220,385 |
| International relief and development services | 154,283 | - | - | 154,283 | 157,132 |
| Total program services | 5,300,778 | - | - | 5,300,778 | 3,136,976 |
| Supporting services: | | | | | |
| Fund raising (Note 10) | 140,082 | - | - | 140,082 | 118,568 |
| Management and general | 187,249 | - | - | 187,249 | 172,325 |
| Total supporting services | 327,331 | - | - | 327,331 | 290,893 |
| Total operating expenses | 5,628,109 | - | - | 5,628,109 | 3,427,869 |
| Change in net assets from operations | 119,333 | 237,771 | 23,412 | 380,516 | 491,388 |
| Nonoperating gains (Notes 4 and 7) | 62,804 | 856 | 796 | 64,456 | 48,222 |
| Additional minimum pension liability (Note 9) | 94,470 | - | - | 94,470 | (94,470) |
| Change in net assets | 276,607 | 238,627 | 24,208 | 539,442 | 445,140 |
| Net assets, beginning of year | 1,319,460 | 856,594 | 470,067 | 2,646,121 | 2,200,981 |
| Net assets, end of year | $ 1,596,067 | $ 1,095,221 | $ 494,275 | $ 3,185,563 | $ 2,646,121 |

See accompanying notes to the consolidated financial statements.

**THE AMERICAN RED CROSS**

Statement of Functional Expenses

Year ended June 30, 2006
(with summarized information for the year ended June 30, 2005)
(In thousands)

| | Program Services | | | | | | |
|---|---|---|---|---|---|---|---|
| | Armed Forces Emergency Services | Biomedical Services | Community Services | Domestic Disaster Services | Health and Safety Services | Int'l Relief & Development Services | Total Program Services |
| Salaries and wages | $ 29,618 | $ 856,075 | $ 54,146 | $ 96,679 | $ 101,259 | $ 15,161 | $ 1,152,938 |
| Employee benefits | 8,895 | 259,663 | 15,993 | 28,837 | 28,808 | 4,783 | 346,979 |
| Subtotal | 38,513 | 1,115,738 | 70,139 | 125,516 | 130,067 | 19,944 | 1,499,917 |
| Travel and maintenance | 1,063 | 31,074 | 3,031 | 108,732 | 3,829 | 2,992 | 150,721 |
| Equipment maintenance and rental | 953 | 72,720 | 5,678 | 57,057 | 4,769 | 1,213 | 142,390 |
| Supplies and materials | 1,492 | 449,347 | 17,791 | 49,284 | 41,000 | 1,286 | 560,200 |
| Contractual services | 7,521 | 386,307 | 19,005 | 176,475 | 33,654 | 8,212 | 631,174 |
| Financial and material assistance | 2,941 | 717 | 12,340 | 2,101,941 | 3,039 | 120,022 | 2,241,000 |
| Depreciation and amortization | 1,613 | 47,669 | 5,483 | 11,761 | 8,236 | 614 | 75,376 |
| Total expenses | $ 54,096 | $ 2,103,572 | $ 133,467 | $ 2,630,766 | $ 224,594 | $ 154,283 | $ 5,300,778 |

| | Supporting Services | | | Total Expenses | |
|---|---|---|---|---|---|
| | Fund Raising | Management and General | Total Supporting Services | 2006 | 2005 |
| Salaries and wages | $ 47,473 | $ 83,984 | $ 131,457 | $ 1,284,395 | $ 1,285,965 |
| Employee benefits | 13,853 | 25,978 | 39,831 | 386,810 | 374,082 |
| Subtotal | 61,326 | 109,962 | 171,288 | 1,671,205 | 1,660,047 |
| Travel and maintenance | 2,614 | 5,098 | 7,712 | 158,433 | 74,248 |
| Equipment maintenance and rental | 1,523 | 5,009 | 6,532 | 148,922 | 95,359 |
| Supplies and materials | 21,512 | 3,971 | 25,483 | 585,683 | 517,207 |
| Contractual services | 49,277 | 46,543 | 95,820 | 726,994 | 659,822 |
| Financial and material assistance | 1,248 | 1,399 | 2,647 | 2,243,647 | 322,984 |
| Depreciation and amortization | 2,582 | 15,267 | 17,849 | 93,225 | 98,202 |
| Total expenses | $ 140,082 | $ 187,249 | $ 327,331 | $ 5,628,109 | $ 3,427,869 |

See accompanying notes to the consolidated financial statements.

**THE AMERICAN RED CROSS**

Consolidated Statement of Cash Flows

Year ended June 30, 2006
(with comparative information for the year ended June 30, 2005)
(In thousands)

| | 2006 | 2005 |
|---|---|---|
| Cash flows from operating activities: | | |
| Change in net assets | $ 539,442 | $ 445,140 |
| Adjustments to reconcile change in net assets to net cash provided by operating activities: | | |
| Depreciation and amortization | 93,225 | 98,202 |
| Provision for doubtful accounts receivable | (3,307) | 3,341 |
| Provision for obsolete inventory | (73) | 41 |
| Net gain on sales of property | (53,738) | (76,572) |
| Net investment and derivative gains | (82,776) | (56,323) |
| Additional minimum pension liability | (94,470) | 94,470 |
| Permanently restricted contributions | (23,412) | (40,216) |
| Changes in operating assets and liabilities: | | |
| Receivables | 126,300 | (15,140) |
| Inventories | 30,302 | 17,253 |
| Other assets | (28,331) | (2,560) |
| Pension intangible asset | 10,555 | (10,555) |
| Accounts payable and accrued expenses | 31,096 | 19,949 |
| Other liabilities | 24,030 | (4,362) |
| Pension and postretirement benefits | 43,310 | 54,675 |
| Net cash provided by operating activities | 612,153 | 527,343 |
| Cash flows from investing activities: | | |
| Purchases of property | (172,167) | (206,616) |
| Proceeds from sales of property | 66,068 | 89,013 |
| Purchases of investments | (743,001) | (1,016,903) |
| Proceeds from sales of investments | 347,847 | 525,735 |
| Net cash used in investing activities | (501,253) | (608,771) |
| Cash flows from financing activities: | | |
| Permanently restricted contributions | 20,694 | 36,658 |
| Proceeds from borrowings | 441,640 | 14,049 |
| Repayments of debt | (438,220) | (30,924) |
| Net cash provided by financing activities | 24,114 | 19,783 |
| Net increase (decrease) in cash and cash equivalents | 135,014 | (61,645) |
| Cash and cash equivalents, beginning of year | 292,559 | 354,204 |
| Cash and cash equivalents, end of year | $ 427,573 | $ 292,559 |
| Supplemental disclosures of cash flow information: | | |
| Cash paid during the year for interest | $ 21,729 | $ 17,629 |
| Noncash investing and financing transactions: | | |
| Acquisition of equipment under capital lease agreements | 338 | 947 |
| Donated stock and beneficial interest in perpetual trust | 17,628 | 9,001 |

See accompanying notes to the consolidated financial statements.

## (1) Summary of Significant Accounting Policies

**Organization and Basis of Presentation:** The American Red Cross (the Organization) was established by an Act of the United States Congress on January 5, 1905 for the primary purposes of furnishing volunteer aid to the sick and wounded of the Armed Forces in time of war and to carry on a system of national and international relief in time of peace to mitigate the suffering caused by fire, famine, floods and other great natural calamities. The mission of the Organization has expanded since that time to help people prevent, prepare for, and respond to emergencies.

The accompanying consolidated financial statements present the consolidated financial position and changes in net assets and cash flows of the Organization. The Organization has national and international programs that are conducted by its headquarters, biomedical services, and chartered local chapters. Also included in the consolidated financial statements are the net assets and operations of Boardman Indemnity Ltd., a 100 percent-owned captive insurance subsidiary. All significant intra-organizational accounts and transactions have been eliminated.

Program activities include armed forces emergency services, biomedical services, community services, disaster services, health and safety services, and international services. Biomedical services includes activities associated with the collection, processing, testing, and distribution of whole blood and components at 35 local blood services region operations, five national testing laboratories, a biomedical research facility, and related national support functions.

Net assets, revenues, gains, and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, the net assets of the Organization and changes therein are classified and reported as follows:

> *Unrestricted net assets* – Net assets that are not subject to any donor-imposed stipulations.
>
> *Temporarily restricted net assets* – Net assets subject to donor-imposed restrictions on their use that may be met either by actions of the Organization or the passage of time.
>
> *Permanently restricted net assets* – Net assets subject to donor-imposed or other legal restrictions requiring that the principal be maintained permanently by the Organization. Generally, the donors permit the Organization to use all or part of the income earned for either general or donor-specified purposes.

The consolidated financial statements are presented with certain prior year summarized comparative information. Such information does not include sufficient detail to constitute a presentation in conformity with generally accepted accounting principles. Accordingly, such information should be read in conjunction with the Organization's consolidated financial statements for the year ended June 30, 2005, from which the summarized information was derived.

**Use of Estimates:** The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities in the financial statements. Estimates and assumptions may also affect disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses. Actual results could differ from management's estimates.

**Cash Equivalents:** The Organization considers all highly liquid investments purchased with an average maturity of three months or less to be cash equivalents. Cash equivalents consisted of money market mutual funds and overnight investments of approximately $250 million and $154 million as of June 30, 2006 and 2005, respectively.

**Investments:** Investments are reported at fair value. The separately managed endowment fund accumulates realized gains and losses on security transactions which are available to meet current expenses to the extent approved by the Board of Governors. Amounts annually available for expenditure are based on the Board of Governors' approved spending rate used under the total-return method.

Investment income classified as operating revenue consists of interest and dividend income on investments and any gains approved for use in operations. All other realized and unrealized gains or losses are classified as nonoperating activity and are available to support operations in future years and to offset potential market declines.

Investments classified as current are available for operations in the next fiscal year.

**Derivative Financial Instruments:** The Organization makes limited use of derivative financial instruments for the purpose of managing interest rate risk. Derivative financial instruments are recorded at their fair value.

**Fair Values of Financial Instruments:** Various methods and assumptions were used to estimate the fair value of each class of financial instruments. Cash and cash equivalents are valued at their carrying amount due to their short maturities. Investments are reported at fair value based on quoted market prices or, in the case of alternative investments, at estimated values provided by the fund managers or general partners based on quoted market prices, if available, or other valuation methods. Management reviews and evaluates the values provided by the fund manager and general partners and agrees with the valuation methods and assumptions used in determining the fair value of the alternative investments. Debt is valued at rates currently available to the Organization for issuances with similar terms and remaining maturities. Interest rate swap agreements are valued at the net present value of future cash flows attributable to the difference between the contractual variable and fixed rates in those agreements.



(Continued)

The estimated fair value of the Organization's noncurrent debt was as follows at June 30, 2006 and 2005 (in thousands):

| | **2006** | | **2005** | |
|---|---|---|---|---|
| | **Carrying Amount** | **Fair Value** | **Carrying Amount** | **Fair Value** |
| Noncurrent debt | $ 389,023 | $ 391,444 | $ 340,695 | $ 348,664 |

The carrying value of all other financial instruments approximates fair value.

**Endowment Fund:** The Organization has maintained a national endowment fund since 1905. Since 1910, as stated in the bylaws of the Organization, and because of public declarations as to their intended use, gifts to the American Red Cross national headquarters under wills, trusts, and similar instruments which do not direct some other use of such funds are recorded as permanently restricted endowment funds to be kept and invested as such in perpetuity. Based upon the manner in which the Organization has solicited and continues to solicit such gifts, it has been determined by independent legal counsel that such gifts must be placed in the endowment fund and, accordingly, reported as permanently restricted net assets.

The Organization makes distributions from the endowment fund for current operations using the total return method. Under the total return method, fund distributions consist of net investment income and may, under certain conditions, include a portion of the cumulative realized gains. The Board of Governors approves the endowment fund spending rate, calculated as a percentage of the three-year calendar moving average fair value of the endowment fund at the beginning of each fiscal year.

A spending rate of 5.5 percent was applied to the endowment fund, and resulted in total distributions related to the endowment fund of approximately $27 million in each year for the years ended June 30, 2006 and 2005. Approximately $13 million and $17 million represented utilization of accumulated realized gains for the years ended June 30, 2006 and 2005, respectively.

**Inventories:** Inventories of supplies purchased for use in program and supporting services are carried at the lower of first-in, first-out cost or market. Whole blood and its components are valued at the lower of average cost or market.

**Land, Buildings, and Other Property:** Purchases of land, buildings, and other property having a unit cost per established guidelines and a useful life of three or more years are capitalized at cost. Donated assets are capitalized at the estimated fair value at date of receipt. Interest expense incurred during a period of construction, less related interest income earned on proceeds of tax-exempt borrowings, is capitalized. Property under capital leases is amortized over the lease term. Any gain or loss on the sale of land, buildings and other property is reported as other revenues on the consolidated statement of activities.

Application development costs incurred to develop internal-use software are capitalized and amortized over the expected useful life of the software application. Activities that are considered application development include design of software configuration and interfaces, coding, installation of hardware, and testing. All other expenses incurred to develop internal-use software are expensed as incurred.

Depreciation is computed using the straight-line method over the estimated useful lives of the assets as follows:

| Class of property | Useful life in years |
|---|---|
| Buildings | 45 |
| Building improvements | 10 |
| Equipment and software | 3-15 |

**Property and Casualty Insurance:** The Organization maintains various insurance policies under which it assumes a portion of each insured loss. Assumed losses are retained by the Organization through its wholly owned insurance subsidiary, Boardman Indemnity Ltd. (Boardman). The Organization also purchases insurance to supplement the coverage by Boardman. The liabilities for outstanding losses and incurred but not reported claims have been determined based on actuarial studies and are reported as other liabilities in the consolidated statement of financial position, and were approximately $90 million and $79 million at June 30, 2006 and 2005, respectively.

**Revenue Recognition:** Contributions, which include unconditional promises to give (pledges), are recognized as revenues in the period received or promised. Conditional contributions are recorded when the conditions have been met. Contributions are considered to be unrestricted unless specifically restricted by the donor.

The Organization reports contributions in the temporarily or permanently restricted net asset class if they are received with donor stipulations as to their use. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are released and reclassified to unrestricted net assets in the consolidated statement of activities. Donor-restricted contributions are initially reported in the temporarily restricted net asset class, even if it is anticipated such restrictions will be met in the current reporting period.

Products and services revenue, which arises principally from sales of whole blood and components and health and safety course fees, is generally recognized upon delivery of the product or services to the customer.

Revenues from federal agencies are generally reported as unrestricted contract revenue as qualifying expenses are incurred under the agreement.

Gains and losses on investments and other assets and liabilities are reported as increases or decreases in unrestricted net assets unless their use is restricted by explicit donor stipulation or by law.

**Contributed Services and Materials:** Contributed services are reported at fair value in the financial statements for voluntary donations of services when those services (1) create or enhance non-financial assets or (2) require specialized skills provided by individuals possessing those skills and are services which would be typically purchased if not provided by donation. The Organization recorded contributed services revenue, and related expense, for the years ended June 30, 2006 and 2005 of approximately $142 million and $24 million, respectively, mostly in support of the disaster services program.

Donated materials are recorded at their fair value at the date of the gift. The Organization does not imply time restrictions for gifts of long-lived assets. As a result, in the absence of donor-imposed restrictions, gifts of long-lived assets are reported as unrestricted revenue.

**Research and Development Costs:** Since 1956, the Organization has engaged in blood research to further enhance the safety of the blood supply. For the years ended June 30, 2006 and 2005, research and development expenses incurred by Biomedical Services were approximately $11 million and $19 million, respectively.

**Income Taxes:** The American Red Cross is a not-for-profit organization incorporated by the U.S. Congress through the issuance of a federal charter. The Organization is exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code, except on net income derived from unrelated business activities.

**Accounts Receivable Securitization:** The Organization has an accounts receivable securitization program whereby the Organization sells receivables in securitization transactions and retains a subordinated interest and servicing rights to those receivables. The Organization accounts for the program under FASB Statement No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishment of Liabilities." The gain or loss on sales of receivables is determined at the date of transfer based upon the relative fair value of the assets sold and the interests retained. The Organization estimates fair value based on the present value of future expected cash flows using management's best estimates of the key assumptions, including collection period and discount rates. See Note 10.

**Reclassifications:** Certain 2005 balances have been reclassified to conform to the 2006 presentation.

## (2) Contributions Receivable

The Organization anticipates collection of outstanding contributions receivable as follows at June 30, 2006 and 2005 (in thousands):

| | 2006 | 2005 |
|---|---|---|
| Amount receivable within one year | $ 98,962 | $ 105,308 |
| Amount receivable in 1 to 5 years | 23,211 | 22,712 |
| Total contributions receivable before allowance for uncollectible amounts | 122,173 | 128,020 |
| Less allowance for uncollectible amounts | (1,841) | (2,753) |
| Contributions receivable, net | 120,332 | 125,267 |
| Less current portion | (97,121) | (102,555) |
| Contributions receivable, net, noncurrent | $ 23,211 | $ 22,712 |

Amounts presented above have been discounted to present value using rates averaging approximately 3 percent. The Organization had commitments from donors for conditional contributions approximating $3 million and $4 million at June 30, 2006 and 2005, respectively. These pledges will be accrued in future periods as the conditions are met.

## (3) Land, Buildings, and Other Property

The cost and accumulated depreciation of land, buildings, and other property were as follows at June 30, 2006 and 2005 (in thousands):

| | 2006 | 2005 |
|---|---|---|
| Land | $ 102,646 | $ 100,868 |
| Buildings and improvements | 1,008,861 | 958,543 |
| Equipment and software | 727,168 | 699,133 |
| Buildings and equipment under capital lease | 27,250 | 28,110 |
| Total cost of assets placed in service | 1,865,925 | 1,786,654 |
| Less accumulated depreciation and amortization | (881,668) | (829,848) |
| Construction-in-progress | 181,533 | 142,034 |
| Land, buildings, and other property, net | $ 1,165,790 | $ 1,098,840 |

## (4) Debt

Debt consists of the following at June 30, 2006 and 2005 (in thousands):

| | 2006 | 2005 |
|---|---|---|
| Borrowings on lines of credit, due in 2007, bearing interest at various rates averaging 4.15% in 2006 and 2.4% in 2005 | $ 20,000 | $ 80,000 |
| Various notes, mortgages and bonds payable, bearing interest at rates ranging from 2.2% to 7.8% due 2007 through 2031, repayment terms generally require monthly payments of interest and annual principal reductions, and are generally backed only by the full faith and credit of the American Red Cross | 405,996 | 340,769 |
| Total bonds and notes payable | 425,996 | 420,769 |
| Obligations under capital leases (Note 5) | 5,154 | 6,623 |
| Total debt | 431,150 | 427,392 |
| Less current portion | (42,127) | (86,697) |
| Debt, noncurrent portion | $ 389,023 | $ 340,695 |

Certain bonds are subject to redemption prior to maturity at the option of the Organization. Additionally, registered owners of these bonds may demand repurchase of the bonds by the bond agent or the depository for an amount equal to the principal price plus accrued interest. Letters of credit or standby credit facilities have been established with multiple banks in the aggregate amount of $238 million and $221 million as of June 30, 2006 and 2005, respectively, to provide liquidity in the event other funding is not available to repurchase these bonds. The depository and bond agent have the authority to use standby credit facilities for the repurchase of certain bonds.



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Scheduled maturities and sinking fund requirements of the debt and credit agreements as of June 30, 2006 are as follows (in thousands):

| **Years ending June 30:** | | |
|---|---|---|
| 2007 | $ | 42,127 |
| 2008 | | 15,615 |
| 2009 | | 22,597 |
| 2010 | | 17,917 |
| 2011 | | 18,293 |
| Thereafter | | 314,601 |
| Total | $ | 431,150 |

Interest expense was approximately $21 million and $17 million for the years ended June 30, 2006 and 2005, respectively, which is included in contractual services on the statement of functional expenses.

**Bank Lines of Credit:** The Organization maintained numerous committed and uncommitted lines of credit with various banks for its working capital requirements. As of June 30, 2006 and 2005, $20 million and $80 million respectively had been borrowed under lines of credit to support operations. The Organization had unused lines of credit outstanding of approximately $180 million at June 30, 2006.

**Interest Rate Swap Agreements:** Interest rate swap agreements are used by the Organization to mitigate the risk of changes in interest rates associated with variable interest rate indebtedness. Under such arrangements, a portion of variable rate indebtedness is converted to fixed rates based on a notional principal amount. The Organization held variable rate debt of approximately $268 million and $279 million at June 30, 2006 and 2005, respectively. At June 30, 2006, the aggregate notional principal amount under the interest rate swap agreements, which mature in 2008, totaled $47 million. At June 30, 2006, the estimated fair value of the interest rate swap agreements was a liability of approximately $1 million.

The Organization applies the provisions of FASB Statement No. 133, *Accounting for Derivative Instruments and Hedging Activities*. This standard requires certain derivative financial instruments to be recorded at fair value. The interest rate swap agreements described above are derivative instruments that are required to be recorded at fair value. The change in fair value on these interest rate swap agreements for the years ended June 30, 2006 and June 30, 2005 was a gain of approximately $1 million each year, and is included as a nonoperating gain in the consolidated statement of activities.

**Letters of Credit:** The Organization had unused letters of credit outstanding of approximately $62 million at June 30, 2006.

## (5) Leases

The Organization leases certain buildings and equipment for use in its operations. The following summarizes, as of June 30, 2006, minimum future rental payments under capital and noncancelable operating leases for the fiscal years ending June 30 (in thousands):

| | Operating | Capital |
|---|---|---|
| 2007 | $ 30,955 | 2,231 |
| 2008 | 23,258 | 1,302 |
| 2009 | 18,101 | 1,019 |
| 2010 | 13,180 | 689 |
| 2011 | 9,323 | 454 |
| Thereafter | 21,177 | 15 |
| Total minimum lease payments | $ 115,994 | 5,710 |
| Less amounts representing interest | | (556) |
| Present value of net minimum lease payments (Note 4) | | $ 5,154 |

Total rent expense was approximately $84 million and $67 million for the years ended June 30, 2006 and 2005, respectively, and is included in contractual services on the statement of functional expenses.

## (6) Net Assets

Unrestricted net assets consisted of the following at June 30, 2006 and 2005 (in thousands):

| | 2006 | 2005 |
|---|---|---|
| Designated for the following purposes: | | |
| Biomedical services | $ 416,395 | $ 355,340 |
| Endowment inflation adjustment reserve | 113,200 | 95,500 |
| Endowment distribution reserve | 48,800 | 38,400 |
| Funds functioning as endowment | 273,286 | 262,384 |
| Fund for retiree health care premium subsidies | 107,585 | 104,811 |
| Replacement and improvement of buildings and equipment | 135,279 | 148,622 |
| Contingencies and other purposes | 206,539 | 112,817 |
| Undesignated | 294,983 | 201,586 |
| Total unrestricted net assets | $ 1,596,067 | $ 1,319,460 |

At June 30, 2006 and 2005, respectively, $162 million and $134 million of cumulative net realized gains on endowed investments were reported as unrestricted net assets. Of these amounts, as of June 30, 2006 and 2005, respectively, approximately $113 million and $96 million have been designated by the Board of Governors as an inflation adjustment reserve to protect donor corpus. This reserve increases each year at a rate equal to 100 percent of the increase in the Consumer Price Index applied against the book value of the original donor corpus. The remaining $49 million and $38 million as of June 30, 2006 and 2005, respectively, were designated as a distribution reserve to provide funds for operations in those years when net interest and dividends are less than the approved distribution rate.

Temporarily restricted net assets are available for the following purposes or periods at June 30, 2006 and 2005 (in thousands):

| | 2006 | 2005 |
|---|---|---|
| Disaster services | $ 208,169 | $ 84,905 |
| Hurricanes Katrina, Rita & Wilma Disaster Relief | 243,721 | — |
| Liberty disaster relief - September 11 response | 46,462 | 117,812 |
| Biomedical services | 8,127 | 9,678 |
| Health and safety services | 3,189 | 5,065 |
| International services | 37,138 | 31,183 |
| Tsunami relief and recovery | 385,491 | 445,826 |
| Community services | 12,427 | 11,008 |
| Buildings and equipment | 20,999 | 20,768 |
| Other specific purposes | 39,772 | 28,310 |
| For periods after June 30, 2006 and 2005, respectively | 89,726 | 102,039 |
| Total temporarily restricted net assets | $ 1,095,221 | $ 856,594 |

As a result of Hurricanes Katrina, Rita and Wilma, that hit the gulf coast in August and September 2005, the Organization received donations of approximately $2.6 billion during Fiscal Year 2006. The Organization has provided approximately $2.4 billion in immediate assistance for the relief and recovery efforts for these hurricanes. The remaining net asset balance of approximately $244 million will be devoted primarily to long-term recovery needs of the local communities in the wake of these storms.

Due to the hundreds of thousands of people potentially eligible for assistance as a result of these hurricanes, the multiple sources for accessing assistance, and evolving assistance guidelines, there were risks of both potential overpayments to eligible beneficiaries and assistance to ineligible beneficiaries. The Organization established procedures to mitigate the instances of fraud and to detect instances that occurred. In addition, the Organization established an internal task force to conduct investigations and ensure cooperation with law enforcement officials in an ongoing effort to identify and take action against identified fraudulent claims. This task force has implemented procedures for responding to requests from investigators in a timely manner and is actively reviewing case files for suspicious claims. Wherever feasible, the Organization has and will continue to seek restitution through civil or criminal processes. The Organization's practice is to restore recovered amounts to the funds designated for these hurricanes to benefit other eligible individuals.



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As a result of the terrorist attacks of September 11, 2001, the Organization received donations of over $1 billion. A separate fund, the Liberty Disaster Relief Fund, was set up to receive the donations and to pay for the immediate and long-term needs of those directly affected by the attacks. To date, the Organization has spent approximately $1 billion to assist victims of the tragedies. The remaining net asset balance of approximately $46 million will be devoted primarily to providing long-term services to those directly affected in the form of counseling, health care services and other assistance.

On December 26, 2004, a 9.0 magnitude earthquake hit off the coast of Indonesia causing a large tsunami and unprecedented damage to over 13 countries. As a result of the generous support of the American public, the Organization has received over $575 million of donations for the Tsunami Relief Fund. The Organization has provided approximately $189 million in immediate assistance for the Tsunami relief and recovery efforts. The remaining net asset balance of approximately $385 million will be used for long-term tsunami relief and recovery efforts primarily in the form of community health services and disease control, disaster preparedness, and community restoration and rebuilding.

Permanently restricted net assets consist primarily of endowed contributions, the income from which is available principally to fund general operations.

## (7) Investments

The following schedule summarizes the composition of investment income for the years ended June 30, 2006 and 2005 (in thousands):

| | 2006 | | | |
|---|---|---|---|---|
| | Unrestricted | Temporarily restricted | Permanently restricted | Total |
| Dividends and interest | $ 87,949 | $ 1,107 | $ — | $ 89,056 |
| Net operating investment gains | 20,621 | 302 | — | 20,923 |
| Investment income available for operations | 108,570 | 1,409 | — | 109,979 |
| Net nonoperating investment gains | 59,607 | 856 | 796 | 61,259 |
| Total return on investments | $ 168,177 | $ 2,265 | $ 796 | $ 171,238 |



(Continued)

| | 2005 | | | |
|---|---|---|---|---|
| | Unrestricted | Temporarily restricted | Permanently restricted | Total |
| Dividends and interest | $ 62,273 | $ 592 | $ — | $ 62,865 |
| Net operating investment gains | 5,266 | 484 | — | 5,750 |
| Investment income available for operations | 67,539 | 1,076 | — | 68,615 |
| Net nonoperating investment gains | 48,120 | 567 | 796 | 49,483 |
| Total return on investments | $ 115,659 | $ 1,643 | $ 796 | $ 118,098 |

The fair value of investments was as follows at June 30, 2006 and 2005 (in thousands):

| | 2006 | 2005 |
|---|---|---|
| U.S. Government securities | $ 317,806 | $ 319,857 |
| Corporate bonds and notes | 151,845 | 169,056 |
| Common and preferred stocks | 525,277 | 535,508 |
| Mortgage and asset backed securities | 121,029 | 121,817 |
| Marketable and nonmarketable alternative funds | 82,939 | 64,994 |
| Partnership funds | 145,244 | 118,600 |
| Money market and other | 1,094,395 | 629,547 |
| Total investments at fair value | 2,438,535 | 1,959,379 |
| Less current portion | (1,104,975) | (741,504) |
| Investments, noncurrent portion | $ 1,333,560 | $ 1,217,875 |

## (8) Split Interest Agreements

The Organization is the beneficiary of split interest agreements in the form of charitable gift annuities, perpetual trusts held by third parties, charitable remainder trusts and pooled income funds. Assets of split interest agreements of $157 million and $149 million are included in investments and other assets on the consolidated statement of financial position at June 30, 2006 and 2005, respectively. The value of split interest agreements is measured as the Organization's share of fair value of the assets. Liabilities associated with these agreements are $23 million, of which $5 million is included with other current liabilities and $18 million is included with other noncurrent liabilities on the consolidated statement of financial position.

## (9) Benefit Plans

**Pension and Postretirement Plans:** Employees of the American Red Cross, including participating local chapters, are covered by the Retirement System of the American National Red Cross (the Plan) after one year of employment.

For funding purposes under the Plan, normal pension costs are determined by the projected unit credit method and are funded currently. The Plan provides a pension funded entirely by the employer. Voluntary contributions may be made by active members to fund an additional, optional annuity benefit. Defined benefits are based on years of service and the employee's final average compensation, which is calculated using the highest consecutive 48 months of the last 120 months of service before retirement.

The Organization's funding policy was to set the employer contribution rate at a percentage of covered payroll that is intended to fund toward a target range of not less than 105 percent and no more than 115 percent of the projected unit credit accrued liability through June 30, 2005. Effective July 1, 2005, the target range is 115 percent to 120 percent of accrued liabilities. To the extent that the current funding is more or less than the target's upper bound, the difference is amortized over ten years in calculating the contribution rate. During fiscal years 2006 and 2005, the Organization contributed 4.25 percent and 4.5 percent, respectively, of covered payroll to the Retirement System.

The Organization has investment guidelines for Plan assets. The overall objective of the guidelines is to ensure the Plan assets provide capital growth over an extended period of time, while also considering market risks and ensuring that the portfolio income and liquidity are appropriate to meet the Plan benefit payments and other expenses. The Plan investments are required to be diversified by asset class and within each asset class, in order to ensure that no single investment will have a disproportionate impact on the total portfolio. The Plan asset allocation is reviewed each year with current market assumptions to ensure the asset mix will achieve the long-term goals of the Plan. The Plan assets were invested in the following categories at June 30, 2006 and 2005:

| | Pension Assets | |
|---|---|---|
| | **2006** | **2005** |
| Cash and short-term investments | 3% | 2% |
| Domestic equity | 41% | 42% |
| International equity | 24% | 23% |
| Fixed income deflation hedge | 15% | 17% |
| Inflation hedge | 8% | 9% |
| Marketable and nonmarketable alternative funds | 9% | 7% |
| | 100% | 100% |

The Plan assets were within authorized asset allocation ranges at June 30, 2006 and 2005.

The Organization also provides medical and dental benefits to eligible retirees and their eligible dependents. Generally, retirees and the Organization each pay a portion of the premium costs. The medical and dental plans pay a stated percentage of expenses reduced by deductibles and other coverages. The Organization has the right to modify cost-sharing provisions at any time. In addition, life insurance benefits of $5,000 are provided with no contributions required from the retirees.

The American Red Cross postretirement benefit plans are unfunded. However, as discussed in Note 6, the Board of Governors has designated $108 million of unrestricted net assets to fund a portion of premiums for retirees' postretirement medical benefits.

The following table presents the changes in benefit obligations, changes in Plan assets, and the composition of accrued benefit costs in the consolidated statements of financial position for the years ended June 30, 2006 and 2005 (in thousands):

| | Pension benefits | | Postretirement benefits | |
|---|---|---|---|---|
| | **2006** | **2005** | **2006** | **2005** |
| **Changes in benefit obligations** | | | | |
| Benefit obligations at beginning of year | $ 1,811,549 | $ 1,418,029 | $ 241,268 | $ 185,060 |
| Service cost | 55,060 | 72,105 | 16,785 | 14,326 |
| Interest cost | 96,762 | 91,874 | 12,499 | 11,380 |
| Plan participants' contributions | 20 | 6,854 | — | — |
| Plan amendment | — | — | — | (26,201) |
| Actuarial (gain) loss | (225,762) | 265,403 | (49,268) | 63,152 |
| Benefits paid | (49,167) | (42,716) | (6,848) | (6,449) |
| Benefit obligations at end of year | $ 1,688,462 | $ 1,811,549 | $ 214,436 | $ 241,268 |
| **Changes in plan assets** | | | | |
| Fair value of plan assets at beginning of year | $ 1,374,385 | $ 1,230,276 | $ — | $ — |
| Actual return on plan assets | 159,134 | 132,169 | — | — |
| Employer contributions | 45,404 | 47,802 | — | — |
| Plan participants' contributions | 20 | 6,854 | — | — |
| Benefits paid | (49,167) | (42,716) | — | — |
| Fair value of plan assets at end of year | $ 1,529,776 | $ 1,374,385 | $ — | $ — |
| **Accrued benefit costs** | | | | |
| Funded status | $ (158,686) | $ (437,164) | $ (214,436) | $ (241,268) |
| Unrecognized net actuarial loss | 21,351 | 327,157 | 20,136 | 72,638 |
| Unrecognized prior service cost | 8,472 | 10,555 | (14,587) | (15,803) |
| Additional minimum liability | — | (105,025) | — | — |
| **Accrued benefit costs** | $ (128,863) | $ (204,477) | $ (208,887) | $ (184,433) |



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The provisions of FASB Statement No. 87, Employers' Accounting for Pensions, require recognition of an additional minimum liability, if the accrued benefit costs for a pension plan are less than the excess of the accumulated benefit obligation over plan assets.

At June 30, 2005, the accumulated benefit obligation exceeded the fair value of plan assets by approximately $204 million, which resulted in a minimum pension liability adjustment of approximately $94 million. This adjustment was recorded as a non-operating loss on the consolidated statement of activities. At June 30, 2006, the value of Plan assets was sufficient such that no additional minimum liability was required, and the effects of the prior year adjustment were reversed, resulting in a minimum pension liability adjustment of approximately $94 million, recorded as a non-operating gain on the consolidated statement of activities.

The accumulated benefit obligation for the pension plan was approximately $1.5 billion and $1.6 billion as of June 30, 2006 and 2005, respectively.

Significant assumptions used in accounting for the plans as of June 30, 2006 and 2005 were:

| | Pension Benefits | | Postretirement Benefits | |
|---|---|---|---|---|
| | **2006** | **2005** | **2006** | **2005** |
| Discount rate | 6.25% | 5.25% | 6.25% | 5.25% |
| Expected return on plan assets | 7.50% | 7.50% | | |
| Rate of compensation increase | 5.00% | 5.00% | | |

The expected rate of return assumption on Plan assets was determined by considering current economic and market conditions and by reviewing asset class allocations, historical return analysis and forward looking capital market expectations. Asset class allocations were established by considering each class' risk premium commensurate for the level of risk, duration that matches the Plan's liabilities, and incremental diversification benefits. Historical returns and forward looking capital market expectations were gathered from, and compared among the Plan's investment managers, and a sampling of the consultant community.

For measurement purposes, a 9.5 percent annual rate of increase in the per capita cost of covered health care benefits was assumed for fiscal year 2006. The rate was assumed to decrease gradually to 6.3 percent for 2010 and remain at that level thereafter.

The components of net periodic benefit cost for the years ended June 30, 2006 and 2005 were (in thousands):

| | Pension benefits | | Postretirement benefits | |
|---|---|---|---|---|
| | **2006** | **2005** | **2006** | **2005** |
| Service cost | $ 55,060 | $ 72,105 | $ 16,785 | $ 14,326 |
| Interest cost | 96,762 | 91,874 | 12,499 | 11,380 |
| Expected return on plan assets | (99,075) | (95,087) | — | — |
| Amortization of prior service cost | 2,083 | 2,083 | (1,216) | 1,690 |
| Recognition of actuarial loss | 19,985 | — | 3,234 | — |
| Net periodic benefit cost | $ 74,815 | $ 70,975 | $ 31,302 | $ 27,396 |

Assumed health care cost trend rates have a significant effect on the amounts reported for the health care plans. A one-percentage point change in assumed health care cost trend rates would have the following effects (in thousands):

| | **Point increase** | **Point decrease** |
|---|---|---|
| Effect on total of service and interest cost components | $ 588 | $ (459) |
| Effect on postretirement benefit obligation | 2,120 | (1,711) |

The Organization expects to contribute approximately $50 million to its pension plan and $6 million to its postretirement benefit plan during the year ended June 30, 2007.

The following benefit payments, which reflect expected future service, as appropriate, are expected to be paid, as of June 30, 2006 (in thousands):

| | **Pension Benefits** | **Postretirement Benefits** |
|---|---|---|
| 2007 | $ 55,019 | $ 6,021 |
| 2008 | 62,264 | 6,324 |
| 2009 | 70,078 | 6,665 |
| 2010 | 78,134 | 7,078 |
| 2011 | 86,703 | 7,531 |
| 2012 - 2016 | 568,545 | 56,491 |
| | $ 920,743 | $ 90,110 |

**American Red Cross Savings Plan – 401(k) Plan:** The Organization participates in the American Red Cross Savings Plan (the Savings Plan), a defined contribution plan. Employees of the Organization hired prior to July 1, 2005, including participating chapters, were eligible to participate upon hire and are vested 100 percent in all contributions to the Savings Plan. Participants hired on or after July 1, 2005 are immediately vested in their own contributions, but will not vest in the American Red Cross' matching contributions for a period of three years. Prior to July 1, 2005, the Organization matched 50 cents for every dollar up to the first 4 percent of annual compensation contributed by the participant. Effective July 1, 2005, the Organization will match 100 percent of every dollar up to the first 4 percent of annual compensation contributed. For the 2005 and 2004 calendar years, contribution limits were based on a maximum annual compensation of $210,000 and $205,000, respectively. There are eleven investment options that an employee can choose from as well as a self-managed brokerage account. The Organization contributed approximately $27 million and $13 million to the Savings Plan for fiscal years 2006 and 2005, respectively.

## (10) Receivables Securitization Program

In August 2005, the Organization initiated a $100 million program to sell (securitize), on a revolving basis, certain biomedical hospital accounts receivable, while retaining a subordinated interest in a portion of the receivables. The eligible receivables are sold without legal recourse to a third party conduit through a wholly owned bankruptcy-remote special purpose entity that is consolidated for financial reporting purposes. The Organization continues servicing the sold receivables and charges the third party conduit a monthly servicing fee at market rates (1 %); accordingly no servicing asset or liability has been recorded.

The program qualifies for sale treatment under SFAS 140. As of June 30, 2006, the outstanding balance of securitized accounts receivable held by the third party conduit was approximately $109 million of which the Organization's subordinated retained interest was approximately $12 million. Accordingly, $97 million of accounts receivable balances, net of applicable allowances, were removed from the consolidated statement of financial position as of June 30, 2006. Expenses associated with the program totaled approximately $3 million in Fiscal Year 2006, and are recorded in contractual services on the statement of functional expenses.

The Organization measures the fair value of the receivable to determine the fair value of its retained interest. No present value calculation is done since the life of the receivable is usually less than 30 days.

## (11) Joint Costs

For the year ended June 30, 2006, the Organization incurred joint costs of approximately $4.6 million for informational materials and activities that included fund raising appeals. Of those costs, $2.4 million was allocated to fund raising, $0.7 million to disaster services, $0.7 million to health and safety services, and $0.8 million to other services.

## (12) Commitments and Contingencies

**Litigation:** The Organization is a defendant in a number of lawsuits incidental to its operations. In the opinion of management, the outcome of such lawsuits will not have a materially adverse effect on the Organization's financial position or its activities.

**Consent Decree:** In April 2003, the American Red Cross signed an amended consent decree (the Decree) with the United States Food and Drug Administration (FDA) affecting Biomedical Services and its blood services regional operations. The Decree requires compliance with specific standards on how the Organization will manage and monitor its Biomedical Services' operations and formalized management of compliance related issues and provides timelines for their resolution. The Decree subjects the Organization to potential monetary penalties if it fails to meet the compliance standards. The compliance penalty provisions cover two general areas: (1) penalties for violations of the law, including FDA regulation; and (2) penalties for the release of unsuitable blood products. Potential penalty amounts are limited to one percent of gross annual revenues generated by Biomedical Services for products and services in the first year (April 15, 2003 through April 14, 2004) of the Decree. The limit is increased to two percent in the second year, three percent in the third year, and four percent starting in the fourth year and annually thereafter. It is the opinion of management that the financial statements adequately provide for potential penalties resulting from the Consent Decree.

**Government Grants:** Costs charged to the federal government under cost-reimbursement grants and contracts are subject to government audit. Therefore, all such costs are subject to adjustment. Management believes that adjustments, if any, would not have a significant effect on the financial statements.

## (13) Risks and Uncertainties

The Organization's invested assets consist of common stocks, fixed income securities and other investment securities. Investment securities are exposed to various risks, such as interest rate, market and credit. Due to the level of uncertainty related to changes in interest rates, market volatility and credit risks, it is at least reasonably possible that changes in these risks could materially affect the fair value of investments reported in the statement of financial position as of June 30, 2006. However, the diversification of the Organization's invested assets among these various asset classes should mitigate the impact of any dramatic change on any one asset class.

## (14) Subsequent Event

In October 2006, the Organization entered into an agreement to sell the land and building of one of its headquarters buildings located in Falls Church, Virginia. The sales price was approximately $44 million and the net book value of the land and building was approximately $29 million as of the date of the sale, resulting in a gain of approximately $15 million. The Organization is also required to repay bonds associated with the purchase of the building within 90 days of the disposition of the building. The total outstanding balance of these bonds was approximately $24 million as of June 30, 2006.