

MOZILLA FOUNDATION
AND SUBSIDIARY

DECEMBER 31, 2018 AND 2017

INDEPENDENT AUDITORS' REPORT

AND

CONSOLIDATED FINANCIAL STATEMENTS

Mozilla Foundation and Subsidiary

Independent Auditors' Report and Consolidated Financial Statements

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A Century Strong

Independent Auditors' Report

THE BOARD OF DIRECTORS
MOZILLA FOUNDATION AND SUBSIDIARY
Mountain View, California

Report on the Consolidated Financial Statements

We have audited the accompanying consolidated financial statements of **MOZILLA FOUNDATION AND SUBSIDIARY (Mozilla)** which comprise the consolidated statement of financial position as of December 31, 2018 and 2017, and the related consolidated statements of activities and change in net assets, and cash flows for the years then ended, the statement of functional expenses for the year ended December 31, 2018, and the related notes to the consolidated financial statements (collectively, the financial statements).

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

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

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Mozilla Foundation and Subsidiary as of December 31, 2018 and 2017 and the change in their net assets and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Effect of Adopting New Accounting Standard

As described in Note 2u, Mozilla adopted the Financial Accounting Standards Board Accounting Standards Update (ASU) 2016-14, Not-For-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities. Accordingly, the accounting change has been retrospectively applied to all periods presented with the exception of the omission of certain information as permitted by the ASU. Our opinion is not modified with respect to that matter.

Hood & Strong LLP

San Jose, California
September 26, 2019

Mozilla Foundation and Subsidiary

Consolidated Statement of Financial Position (In thousands)

| <i>December 31,</i> | 2018 | 2017 |
|-----------------------------------|------------|------------|
| Assets | | |
| Cash and cash equivalents | \$ 113,133 | \$ 49,743 |
| Receivables | 60,937 | 56,628 |
| Prepaid expenses and other assets | 18,187 | 9,041 |
| Investments | 368,806 | 414,171 |
| Prepaid income taxes | 12,242 | 25,819 |
| Deferred taxes | 10,205 | 6,501 |
| Property and equipment, net | 14,391 | 16,682 |
| Goodwill, net | 23,415 | 26,017 |
| Intangible assets, net | 1,427 | 2,667 |
| Total assets | \$ 622,743 | \$ 607,269 |
| Liabilities and Net Assets | | |
| Liabilities: | | |
| Accounts payable | \$ 20,118 | \$ 30,457 |
| Accrued liabilities | 75,063 | 55,219 |
| Deferred revenue | 616 | 430 |
| Unrecognized tax positions | 3,409 | 6,991 |
| Total liabilities | 99,206 | 93,097 |
| Net Assets: | | |
| Without donor restrictions | 516,767 | 510,243 |
| With donor restrictions | 6,770 | 3,929 |
| Total net assets | 523,537 | 514,172 |
| Total liabilities and net assets | \$ 622,743 | \$ 607,269 |

See accompanying notes to financial statements.

Mozilla Foundation and Subsidiary

Consolidated Statement of Activities and Change in Net Assets (In thousands)

| <i>Years Ended December 31,</i> | 2018 | 2017 |
|--|-------------------|-------------------|
| Net Assets Without Donor Restrictions: | | |
| Revenues and other support: | | |
| Royalties | \$ 429,695 | \$ 539,168 |
| Subscription and advertising revenue | 5,377 | 2,653 |
| Interest and dividend income | 7,905 | 4,919 |
| Net realized and unrealized (loss) gain on investments, net | (1,688) | 819 |
| Contributions | 6,335 | 6,438 |
| Other | 864 | 553 |
| Foreign currency exchange (loss) gain | (2,402) | 2,409 |
| Loss on sale of assets | (42) | (43) |
| Net assets released from restrictions | 4,816 | 5,363 |
| Total revenue and support | 450,860 | 562,279 |
| Expenses: | | |
| Program: | | |
| Software development | 277,767 | 259,549 |
| Other program services | 33,484 | 20,713 |
| Management and general: | | |
| Branding and marketing | 52,805 | 65,928 |
| General and administrative | 86,045 | 74,473 |
| Fundraising: | | |
| Fundraising and development | 1,270 | 1,124 |
| Total expenses | 451,371 | 421,787 |
| Change in Net Assets Without Donor Restrictions before Provision for Income Taxes | (511) | 140,492 |
| Provision for income tax expense (benefit) | (7,035) | 50,588 |
| Change in Net Assets Without Donor Restrictions | 6,524 | 89,904 |
| Change in Net Assets With Donor Restrictions: | | |
| Contributions | 7,657 | 3,495 |
| Net assets released from restriction | (4,816) | (5,363) |
| Change in Net Assets With Donor Restrictions | 2,841 | (1,868) |
| Change in Net Assets | 9,365 | 88,036 |
| Net Assets - beginning of year | 514,172 | 426,136 |
| Net Assets - end of year | \$ 523,537 | \$ 514,172 |

See accompanying notes to financial statements.

Mozilla Foundation and Subsidiary

Consolidated Statement of Functional Expenses (In thousands)

Year Ended December 31, 2018

| | Program | Management and General | Fundraising | Total |
|---|------------|---------------------------|-------------|------------|
| Salaries and benefits | \$ 202,087 | \$ 82,423 | \$ 1,061 | \$ 285,571 |
| Information technology | 24,864 | 7,681 | 18 | 32,563 |
| Consultants | 23,672 | 7,359 | | 31,031 |
| Advertising and promotion | 230 | 21,860 | 143 | 22,233 |
| Conferences, conventions, and meetings | 13,411 | 6,344 | | 19,755 |
| Occupancy | 8,318 | 2,577 | | 10,895 |
| Grants and donations | 8,702 | 730 | | 9,432 |
| Legal | 4,929 | 1,779 | | 6,708 |
| Dues and subscriptions | 3,070 | 2,700 | | 5,770 |
| Travel | 3,912 | 1,466 | 40 | 5,418 |
| Office expenses | 4,167 | 1,722 | 4 | 5,893 |
| Accounting | | 1,611 | | 1,611 |
| Insurance | 254 | 91 | | 345 |
| Depreciation | 12,090 | 23 | | 12,113 |
| Other expenses | 1,545 | 484 | 4 | 2,033 |
| Expenses before income tax provision (benefit) | 311,251 | 138,850 | 1,270 | 451,371 |
| Provision for income tax expense (benefit) | (5,359) | (1,676) | | (7,035) |
| Total expenses | \$ 305,892 | \$ 137,174 | \$ 1,270 | \$ 444,336 |

See accompanying notes to financial statements.

Mozilla Foundation and Subsidiary

Consolidated Statement of Cash Flows (In thousands)

| <i>Years Ended December 31,</i> | 2018 | 2017 |
|--|-------------|-----------|
| Cash Flows from Operating Activities: | | |
| Change in net assets | \$ 9,365 | \$ 88,036 |
| Adjustments to reconcile change in net assets to net cash provided by operations: | | |
| Depreciation and amortization | 12,113 | 9,035 |
| Net realized and unrealized (gain) loss on investments | 1,688 | (819) |
| Foreign currency exchange loss (gain) | 2,402 | (2,409) |
| Unrecognized tax positions | (414) | 407 |
| Deferred income taxes | (4,119) | (4,722) |
| Loss on sale of assets | 42 | 43 |
| Changes in assets and liabilities: | | |
| Receivables | (4,362) | (3,424) |
| Prepaid expenses and other assets | (9,307) | 8,082 |
| Prepaid income taxes | 10,403 | (13,609) |
| Accounts payable, accrued expenses and deferred revenue | 10,471 | 20,802 |
| Net cash provided by operating activities | 28,282 | 101,422 |
| Cash Flows from Investing Activities: | | |
| Purchases of property and equipment | (6,385) | (9,674) |
| Purchases of investments | (290,453) | (315,245) |
| Proceeds from sale of investments | 333,946 | 231,083 |
| Acquisitions, net of cash acquired | | (29,262) |
| Net cash provided (used) by investing activities | 37,108 | (123,098) |
| Effect of Exchange Rate Changes on Cash | (2,000) | 2,355 |
| Net Change in Cash and Cash Equivalents | 63,390 | (19,321) |
| Cash and Cash Equivalents - beginning of year | 49,743 | 69,064 |
| Cash and Cash Equivalents - end of year | \$ 113,133 | \$ 49,743 |
| Supplemental Disclosure: | | |
| Cash paid for taxes, net of refunds | \$ (14,543) | \$ 83,115 |

See accompanying notes to financial statements.

Mozilla Foundation and Subsidiary

Notes to Consolidated Financial Statements

Note 1 - Nature of the Organization:

Established in July 2003, the Mozilla Foundation (the Foundation) is a California not-for-profit corporation that exists to improve and protect the internet as a public resource by working with thousands of volunteers to 1) keep the internet a universal open platform and 2) promote continued innovation on the internet. The Foundation supports the development of open source, standards compliant, free internet applications useable free of charge to hundreds of millions of users. It also a) develops foundational technologies that can be used to build the values of openness and interoperability into the internet; and b) fuels the movement for an open internet through educational work that connects open internet leaders with each other and mobilizes grassroots activities around the world.

The Foundation has a wholly-owned for-profit subsidiary, Mozilla Corporation (the Corporation). The Corporation serves the non-profit, public benefit goals of its parent and the vast Mozilla community. It provides internet based open source software and services (Mozilla Products) which are made available to hundreds of millions of users worldwide to fulfill Mozilla's worldwide mission to make the internet and the web open and accessible to all. The Corporation has wholly-owned subsidiaries operating in the United States, Canada, Europe, China and several other international branches to further its worldwide mission.

Note 2 - Summary of Significant Accounting Policies:

a. Basis of Accounting

The financial statements have been prepared on the accrual basis of accounting which recognizes revenue and support when earned and expenses when incurred and, accordingly, reflect all significant receivables, payables, and other liabilities in accordance with accounting principles generally accepted in the United States of America.

b. Principles of Consolidation

The consolidated financial statements include the accounts of the Foundation and its wholly-owned subsidiary, the Corporation (collectively "Mozilla"). All significant intercompany accounts and transactions have been eliminated.

c. Basis of Presentation

Net assets, revenues, expenses, gains and losses are classified based on the existence or absence of donor imposed restrictions.

Mozilla Foundation and Subsidiary

Notes to Consolidated Financial Statements

Net Assets Without Donor Restrictions – The portion of net assets that are not subject to time or donor-imposed restrictions and may be expended for any purpose in achieving the primary objective of the Foundation.

Net Assets With Donor Restrictions – represent contributions that are limited in use by Mozilla in accordance with donor imposed stipulations. These stipulations may expire with time or may be satisfied and removed by the actions of Mozilla according to the terms of the contribution. Net assets with donor restrictions also include net assets to be retained in perpetuity of which Mozilla has none as of December 31, 2018 and 2017.

d. Cash and Cash Equivalents

For purposes of the statement of cash flows, Mozilla considers its operating checking and sweep accounts to be cash and cash equivalents.

e. Receivables

Receivables consist primarily of amounts due from contracts with multiple search engine and information providers, and grantors. Receivables are carried at original invoice amount or accrued based on contractual agreements with each search provider or grantor. An allowance for uncollectible receivables is considered depending upon prior history and management's assessment of collectability. For 2018 and 2017, management considers all amounts to be fully collectible. Therefore, no allowance has been established.

Mozilla has \$1,298,000 and \$1,684,000 in grants receivable at December 31, 2018 and 2017, respectively.

f. Investments

Investments, which consist of money market funds, marketable debt securities, mutual funds, government issued securities, commercial paper and hedge funds, are stated at fair value. The fair value of money market funds is based on quoted market prices for identical assets in active markets. The fair value of marketable debt, government issued securities and commercial paper is based upon models that maximize the use of observable inputs for similar assets. The fair value of mutual funds is based on their quoted prices for identical assets in active or inactive markets. The fair value of hedge funds has been estimated using the net asset value (NAV) per share or ownership interest of the investment. Changes in fair value are recognized on a current basis in the statement of activities and change in net assets.

g. Fair Value of Financial Instruments

The carrying value of financial instruments not otherwise disclosed herein, approximates fair value due to the short-term nature of these financial instruments.

Mozilla Foundation and Subsidiary

Notes to Consolidated Financial Statements

Mozilla carries certain assets and liabilities at fair value. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. In addition, certain investments are reported using the NAV per share method practical expedient which allows NAV per share to represent fair value for reporting purposes when the criteria for using this method are met.

Mozilla classifies its financial assets and liabilities according to three levels, and maximizes the use of observable inputs and minimizes the use of unobservable inputs when measuring fair value.

Level 1: Quoted market prices (unadjusted) in active markets for identical assets or liabilities that the entity has the ability to access at the measurement date.

Level 2: Observable inputs other than quoted prices included within Level 1 for the asset or liability.

Level 3: Unobservable inputs for the asset or liability that are not corroborated by market data.

In determining the appropriate levels, Mozilla performed an analysis of the assets and liabilities. Any assets and liabilities for which the fair value measurement is based on significant unobservable inputs are classified as Level 3.

h. Property and Equipment

Property and equipment are stated at cost less accumulated depreciation and amortization. Depreciation is calculated over the estimated useful lives of the related assets, generally one to seven years, using the straight-line method. Leasehold improvements are amortized over the useful life or the term of the lease, whichever is shorter.

Mozilla recognizes asset retirement obligations (AROs) in the period in which it has an existing legal obligation associated with the retirement of a tangible long-lived asset, and the amount of the liability can be reasonably estimated. The ARO is recognized at fair value when the liability is incurred with a corresponding increase in the carrying amount of the related long-lived asset. Mozilla depreciates the tangible asset over its estimated useful life. The liability is adjusted in subsequent periods through accretion expense, if any, which represents the increase in the present value of the liability due to the passage of time. Such depreciation and accretion expenses are included in depreciation expense.

Mozilla Foundation and Subsidiary

Notes to Consolidated Financial Statements

Mozilla's AROs are primarily the result of requirements under facility lease agreements which generally have "return to original condition" clauses which would require Mozilla to remove or restore items such as demising walls and office buildouts, among others.

The significant assumptions used in estimating the aggregate ARO are the timing of removals, the probability of a requirement to perform, estimated cost and associated expected inflation rates that are consistent with historical rates and credit-adjusted risk-free rates that approximate Mozilla's incremental borrowing rate.

During 2018, there was \$3,220,000 of liabilities incurred with no liabilities assumed or settled, and no accretion expense for the ARO at December 31, 2018 of \$3,220,000.

i. Goodwill and Intangible Assets

Goodwill represents the excess of the cost of net assets acquired over the fair value of identifiable net assets at the date of acquisition. Intangible assets consist of acquired user base, trade names and trademarks, and developed technology.

Effective January 1, 2018 Mozilla adopted the private company alternative accounting policy for goodwill. Goodwill is amortized over a 10-year estimated useful life and impairment is assessed at the reporting unit level. Mozilla performs an impairment test only when there is a triggering event by comparing the fair value of the reporting unit to its carrying value.

j. Long-Lived Assets

Mozilla evaluates its long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future undiscounted net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the fair value of the assets. Assets to be disposed of are reported at the lower of the carrying amount or fair value less costs to sell.

k. Recognition of Revenue

Mozilla's primary source of revenue is royalty income from contracts with various search engine and information providers. Revenue from these contracts is determined by the search and information providers based upon end user activity or as contractually agreed to. Mozilla records revenue on the accrual basis of accounting based upon the amounts received.

Mozilla Foundation and Subsidiary

Notes to Consolidated Financial Statements

Other sources of revenue include advertising for content providers and monthly and annual subscriptions, which are recognized when the services are performed. Deferred revenue is recorded for the amount billed for which the service period has not yet occurred.

l. Contributions

Contributions are recorded at fair value when the donor makes an unconditional promise to give. Contributions collected by third parties are recorded as revenue when received by the third party. When donor restrictions expire, that is, when a stipulated time restriction ends or a purpose restriction is fulfilled, net assets with donor restrictions are reclassified to net assets without donor restriction and reported in the consolidated statement of activities and change in net assets as net assets released from restrictions.

Conditional promises are not recognized until they become unconditional, that is when the conditions on which they depend are substantially met. Mozilla received \$13,992,000 and \$9,933,000 in contributions during the years ending December 31, 2018 and 2017, respectively, and has \$2,441,000 and \$100,000 in conditional promises at December 31, 2018 and 2017, respectively.

m. Software Development Costs

Mozilla develops open source web-based solutions which are available free of charge to users. In addition, due to the open source nature of the development, there is generally no passage of time between achievement of technological feasibility and the availability for general release. Therefore, Mozilla expenses the cost of software development as incurred.

n. Advertising Costs

Mozilla expenses advertising costs as incurred. Amounts paid in advance of services provided are recorded as a prepaid expense. Advertising expense for the year ended December 31, 2018 and 2017 amounted to \$17,991,000 and \$30,670,000, respectively.

o. Grants

Grants are recorded when approved and all significant conditions are met.

p. Income Taxes

The Foundation qualifies as a public benefit charitable organization exempt from income taxes on related income under Section 501(c)(3) of the Internal Revenue Code and applicable sections of the California Revenue and Taxation Code. The Foundation provides for tax, if any, on unrelated business income.

Mozilla Foundation and Subsidiary

Notes to Consolidated Financial Statements

The Corporation is a C corporation. Income taxes are accounted for using an asset and liability approach, which requires the recognition of deferred tax liabilities and assets for the expected future tax consequences of temporary differences between the financial statement and tax basis of assets and liabilities at the applicable enacted tax rates. Differences relate primarily to state taxes, property and equipment, prepaid and accrued expenses. Valuation allowances are established, when necessary, to reduce deferred tax assets to amounts that are more likely than not to be realized.

In accordance with the accounting standard on accounting for uncertainty in income taxes, no portion of an uncertain tax position will be recognized if the position has less than a 50% likelihood of being sustained upon audit by the relevant taxing authority. Also, interest expense, if any, is recognized on the full amount of deferred benefits for uncertain tax positions.

q. Foreign Currency Translation

The financial statements of the foreign subsidiaries, which have defined their functional currency as their local currency, translate their balance sheet accounts at the exchange rate existing at the balance sheet date, and translate their income statement items at the average exchange rate for the year. The resulting translation adjustments are included in foreign currency exchange gain (loss) in the consolidated statement of activities and change in net assets.

r. Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions. Actual results could differ from those estimates.

s. Functional Expenses

The costs of providing various programs and activities have been summarized on a functional basis in the statement of activities and changes in net assets. Expenses such as salaries and benefits and facilities are allocated among program, management and general, and fundraising based on time estimates determined by Mozilla's management. Office supplies and other indirect costs are allocated based on time and effort. All other costs are allocated directly to the functions they benefit.

t. Reclassification

Certain accounts in the 2017 financial statements have been reclassified for comparative purposes to conform with the presentation in the 2018 financial statements. These reclassifications had no effect on net assets or change in net assets.

Mozilla Foundation and Subsidiary

Notes to Consolidated Financial Statements

u. Recent Accounting Pronouncements

Pronouncements Adopted:

In August 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2016-14, *Not-for-Profit Entities (Topic 958) Presentation of Financial Statements of Not-for-Profit Entities*, which changes presentation and disclosure requirements for nonprofit entities to provide more relevant information about their resources (and the changes in those resources) to donors, grantors, creditors, and other users. These include qualitative and quantitative requirements in the following areas: net asset classes, expenses, and liquidity. Mozilla adopted the ASU as of January 1, 2018. Accordingly, the accounting change has been retrospectively applied to all periods presented, with the exception of the omission of prior year functional expense and liquidity and availability of resource information as permitted by the ASU.

Pronouncements Effective in the Future:

The FASB issued authoritative guidance, *Revenue from Contracts with Customers (Topic 606)*. These amendments provide that revenue should be recognized to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. This guidance is effective for fiscal years beginning after December 15, 2018. The impact of adopting this guidance on subsequent periods has not yet been determined.

In June 2018, the FASB issued *ASU 2018-08, Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made (Topic 958)*. The ASU clarifies and improves current guidance about whether a transfer of assets, or the reduction, settlement, or cancellation of liabilities, is a contribution or an exchange transaction. It provides criteria for determining whether the resource provider is receiving commensurate value in return for the resources transferred which, depending on the outcome, determines whether the organization follows contribution guidance or exchange transaction guidance in the revenue recognition and other applicable standards. The ASU does not apply to transfers of assets from governments to businesses. The amendments in the update related to contributions received are effective for fiscal years beginning after December 15, 2018, while the amendments related to contributions made are effective one year later. Mozilla is currently evaluating the impact of this pronouncement on its financial statements.

The FASB issued *ASU 2016-02—Leases (Topic 842)*. Under the ASU, a lessee will be required to recognize right-to-use assets and liabilities on their balance sheet for all leases with lease terms of more than twelve months. The ASU is effective for fiscal years beginning after December 15, 2019. Early application will be permitted for all organizations. Mozilla has started to implement this ASU as of December 31, 2018.

Mozilla Foundation and Subsidiary

Notes to Consolidated Financial Statements

v. Subsequent Events

Mozilla evaluated subsequent events from December 31, 2018 through September 26, 2019, the date these financial statements were available to be issued. Except as disclosed in the following paragraph, there were no material subsequent events that required additional disclosure in these financial statements.

The Corporation entered into a minority investment transaction with Cliqz GmbH (Cliqz) in August 2016 to further explore and promote privacy-focused search innovation by Cliqz. As a result of this transaction, the Corporation maintained a 10% share of Cliqz with a total investment of EUR 1,610,000 (\$1,800,000), which includes an initial purchase price of EUR 10,026 and two subsequent investments. In July 2019, the Corporation sold the Cliqz shares back to Cliqz at the nominal fee for which the shares were initially purchased by the Corporation, and the Corporation is no longer a shareholder in Cliqz.

Note 3 - Availability of Financial Assets and Liquidity:

Mozilla's financial assets available within one year of December 31, 2018 for general expenditures are as follows:

| | |
|---|----------------|
| Financial assets at year-end: | |
| Cash and cash equivalents | \$ 113,133,000 |
| Receivables | 60,937,000 |
| Investments | 368,806,000 |
| <hr/> | |
| Total financial assets | 542,876,000 |
| Less amounts not available to be used within one year: | |
| Long-term contributions and notes receivable | (12,500,000) |
| Investments not convertible to cash within 12 months | (352,173,000) |
| Other assets | (1,000,000) |
| Net assets with donor restrictions | (6,770,000) |
| Add net assets with purpose restrictions to be met in less than a year | 6,693,000 |
| <hr/> | |
| Total amounts not available to be used within one year | (365,750,000) |
| <hr/> | |
| Financial assets available to meet general expenditures over the next twelve months | \$ 177,126,000 |
| <hr/> | |

Mozilla Foundation and Subsidiary

Notes to Consolidated Financial Statements

Mozilla has certain donor-restricted assets limited to use which are available for general expenditure within one year in the normal course of operations. Accordingly, these assets have been included in the quantitative information above for financial assets to meet general expenditures within one year. Donor restricted assets that are not available for general expenditure within the next year, are more fully described in Note 9.

As part of the Mozilla's liquidity management plan, cash in excess of daily requirements is invested in a managed portfolio of fixed income and equity securities.

Note 4 - Acquisition:

On February 24, 2017, Mozilla acquired 100% of the outstanding stock of Read It Later, Inc., known as Pocket, (RIL) for a total purchase price of \$25 million in cash, and \$5 million in deferred payments. The results of RIL are included in Mozilla's consolidated financial statements since the date of acquisition.

RIL is headquartered in California and provides a platform that helps people save interesting articles, videos and more from the web for later enjoyment. Once saved, the list of content is visible on any device — phone, tablet or computer — via its mobile and web applications. RIL's save-for-later service has been integrated into the Firefox web browser to provide Firefox users a better user experience. The goodwill arising from the acquisition will create growth opportunities and expected synergies and enhancements with Firefox integration. None of the goodwill recognized is expected to be deductible for income tax purposes.

Assets acquired, and liabilities assumed at the date of acquisition consisted of:

| | | |
|---------------------------------------|----|-----------|
| Cash | \$ | 187,000 |
| Accounts receivable | | 315,000 |
| Restricted cash | | 374,000 |
| Other assets | | 9,000 |
| Intangible assets | | 3,700,000 |
| <hr/> | | |
| Total assets acquired | \$ | 4,585,000 |
| <hr/> | | |
| Accounts payable and accrued expenses | \$ | 130,000 |
| Deferred revenue | | 608,000 |
| Other accrued expenses | | 40,000 |
| <hr/> | | |
| Total liabilities assumed | \$ | 778,000 |
| <hr/> | | |

Mozilla Foundation and Subsidiary

Notes to Consolidated Financial Statements

| | |
|---------------------|---------------|
| Net assets acquired | \$ 3,807,000 |
| Goodwill | 26,017,000 |
| <hr/> | |
| Purchase price | \$ 29,824,000 |

Note 5 - Investments and Fair Value Measurements:

The tables below present investments measured at fair value on a recurring basis by level within the valuation hierarchy at December 31:

| 2018 | <u>Total</u> | <u>Level 1</u> | <u>Level 2</u> | <u>Level 3</u> |
|--|----------------|----------------------|-----------------------|----------------|
| Money market funds | \$ 8,901,000 | \$ 8,901,000 | | |
| Commercial paper | 19,830,000 | | \$ 19,830,000 | |
| Mutual funds | | | | |
| Domestic | 14,170,000 | 11,875,000 | 2,295,000 | |
| ETF: Minerals | 433,000 | 433,000 | | |
| Municipal bonds | 2,379,000 | | 2,379,000 | |
| U.S. agency funds | 39,263,000 | | 39,263,000 | |
| Asset-backed securities | 57,596,000 | | 57,596,000 | |
| Corporate debentures/bonds: | | | | |
| Industrial | 151,789,000 | | 151,789,000 | |
| Financial | 72,739,000 | | 72,739,000 | |
| <hr/> | | | | |
| Total assets measured at fair value | 367,100,000 | <u>\$ 21,209,000</u> | <u>\$ 345,891,000</u> | |
| | | | | |
| Hedge fund investments measured at net asset value as a practical expedient | 1,706,000 | | | |
| <hr/> | | | | |
| Total | \$ 368,806,000 | | | |

Mozilla Foundation and Subsidiary

Notes to Consolidated Financial Statements

| 2017 | <u>Total</u> | <u>Level 1</u> | <u>Level 2</u> | <u>Level 3</u> |
|--|-----------------------|----------------|----------------|----------------|
| Money market funds | \$ 9,341,000 | \$ 9,341,000 | | |
| Commercial paper | 13,291,000 | | \$ 13,291,000 | |
| Mutual funds | | | | |
| Domestic | 14,095,000 | 9,506,000 | 4,589,000 | |
| ETF: Minerals | 442,000 | 442,000 | | |
| Municipal bonds | 1,786,000 | | 1,786,000 | |
| U.S. agency funds | 107,079,000 | | 107,079,000 | |
| Asset-backed securities | 49,333,000 | | 49,333,000 | |
| Corporate debentures/bonds: | | | | |
| Industrial | 182,827,000 | | 182,827,000 | |
| Financial | 31,922,000 | | 31,922,000 | |
| Total assets measured at fair value | 410,116,000 | \$ 19,289,000 | \$ 390,827,000 | |
| Hedge fund investments measured at net asset value as a practical expedient | 4,055,000 | | | |
| Total | \$ 414,171,000 | | | |

An investment's categorization within the valuation hierarchy is based on the lowest level of input that is significant to the fair value measurement. There has been no change in the methodology used for December 31, 2018 and 2017.

The method described above may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while Mozilla believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

Mozilla Foundation and Subsidiary

Notes to Consolidated Financial Statements

The following table provides information for investments using NAV to determine fair value as of December 31:

| 2018 | No. of Funds | Fair Value | Redemption Frequency | Redemption Notice Period (days) |
|-----------------------|--------------|---------------------|----------------------|---------------------------------|
| Global macro fund (a) | 1 | \$ 1,286,000 | Quarterly | 90 |
| Feeder fund (d) | 1 | 420,000 | None | N/A |
| Total | | \$ 1,706,000 | | |

| 2017 | No. of Funds | Fair Value | Redemption Frequency | Redemption Notice Period (days) |
|-------------------------|--------------|---------------------|----------------------|---------------------------------|
| Global macro fund (a) | 1 | \$ 1,139,000 | Quarterly | 90 |
| Event driven fund (b) | 1 | 1,738,000 | Monthly | 30 |
| Long and short fund (c) | 1 | 838,000 | Monthly | 60 |
| Feeder fund (d) | 1 | 340,000 | None | N/A |
| Total | | \$ 4,055,000 | | |

There were \$257,000 and \$300,000 in unfunded commitments as of December 31, 2018 and December 31, 2017, respectively.

- (a) This fund invests in an affiliated Master Fund LP, whose investment strategy is comprised of global investment strategies and a number of long and short strategies that may have directional risk.
- (b) This fund invests in an affiliated Master Fund LP, whose investment strategy is to achieve positive returns from capital appreciation and income generation.
- (c) This fund invests in affiliated Master Fund LP, whose objectives are to maximize risk adjusted, absolute returns over the course of various market cycles through a portfolio consisting of long and short equity investments and whose investment strategy combines elements of long and short equities and corporate credit relative value trading.
- (d) This fund invests in an affiliated Master Fund LP, whose objective is to invest on a leveraged basis, in whole or in part, in collateralized and unsecured commercial loans and debt securities of corporations, partnerships, companies or other securities.

Mozilla Foundation and Subsidiary

Notes to Consolidated Financial Statements

Note 6 - Property and Equipment:

Property and equipment as of December 31, are as follows:

| | 2018 | 2017 | Useful Life (Years) |
|--------------------------------|---------------|---------------|------------------------|
| Computer equipment | \$ 21,753,000 | \$ 20,059,000 | 3 |
| Furniture and office equipment | 12,321,000 | 11,944,000 | 3 - 7 |
| Leasehold improvements | 30,870,000 | 28,181,000 | 3 - 5 |
| Software | 305,000 | 223,000 | 1 - 3 |
| | 65,249,000 | 60,407,000 | |
| Less accumulated depreciation | (50,858,000) | (43,725,000) | |
| Net property and equipment | \$ 14,391,000 | \$ 16,682,000 | |

Depreciation and amortization expense, excluding amortization on intangibles and goodwill totaled \$8,271,000 and \$8,002,000 for the years ended December 31, 2018 and 2017, respectively.

Note 7 - Goodwill:

Goodwill is amortized over an estimated useful life of 10 years. Amortization expense for the for the year ended December 31, 2018 was \$2,602,000. Goodwill is as follows as of December 31:

| | 2018 | 2017 | Estimated Useful Life (Years) |
|--------------------------------|---------------|---------------|-------------------------------------|
| Goodwill | \$ 26,017,000 | \$ 26,017,000 | 10 |
| Less: Accumulated amortization | (2,602,000) | | |
| Total goodwill, net | \$ 23,415,000 | \$ 26,017,000 | |

Mozilla Foundation and Subsidiary

Notes to Consolidated Financial Statements

Mozilla adopted the private company alternative accounting policy for goodwill effective January 1, 2018 to reduce the complexity and costs of the original goodwill accounting method. Since the carrying amount of goodwill was recorded at fair value as of December 31, 2017, and given the recent nature of the transaction giving rise to the goodwill, management determined to apply the alternate guidance on a prospective basis. The results of which are reflected in these financial statements.

Note 8 - Intangible Assets:

Intangible assets are amortized over their estimated useful lives on a straight-line basis. No residual value is estimated for the intangible assets.

The components of intangible assets are as follows as of December 31:

| | 2018 | 2017 | Estimated Useful Life (Years) |
|------------------------------|--------------|--------------|-------------------------------|
| User base | \$ 1,500,000 | \$ 1,500,000 | 2 |
| Trade names and trademark | 1,200,000 | 1,200,000 | 5 |
| Developed technology | 1,000,000 | 1,000,000 | 4 |
| | 3,700,000 | 3,700,000 | |
| Accumulated amortization | (2,273,000) | (1,033,000) | |
| Total intangible assets, net | \$ 1,427,000 | \$ 2,667,000 | |

Amortization expense for the year ended December 31, 2018 was \$1,240,000 and for the period from February 24, 2017 through December 31, 2017 was \$1,033,000. Estimated aggregate amortization expense is as follows:

| | |
|-------|--------------|
| 2019 | \$ 615,000 |
| 2020 | 490,000 |
| 2021 | 282,000 |
| 2022 | 40,000 |
| Total | \$ 1,427,000 |

Mozilla Foundation and Subsidiary

Notes to Consolidated Financial Statements

Note 9 - Net Assets With Donor Restrictions:

Net assets with donor restrictions consist of the following at December 31, 2018:

| | 2018 | 2017 |
|--|---------------------|---------------------|
| Leadership Development: Ford-Mozilla Open Web Program | \$ 1,090,000 | \$ 1,012,000 |
| Leadership Development: Mozilla MITI/OIE Fellowships | 814,000 | |
| Leadership Development: Mozilla Science Fellowships | 1,021,000 | 1,213,000 |
| Leadership Development: Hive | | 174,000 |
| Community: Coral Software Project | 32,000 | 203,000 |
| Leadership Development: Responsible Computer Science Challenge | 1,287,000 | |
| Thunderbird | 1,805,000 | 1,077,000 |
| Other | 721,000 | 250,000 |
| | <u>\$ 6,770,000</u> | <u>\$ 3,929,000</u> |

Net assets were released from donor restrictions during the year ended December 31, 2018 and 2017 by incurring expenses satisfying the purpose of the restriction, by the passage of time, or by the occurrence of other specific events as follows:

| | 2018 | 2017 |
|--|---------------------|---------------------|
| Leadership Development: Hive | \$ 174,000 | \$ 1,165,000 |
| Leadership Development: Ford- Mozilla MITI/OIE Fellowships | 361,000 | |
| Leadership Development: Ford-Mozilla Open Web Program | 1,422,000 | 1,399,000 |
| Leadership Development: Mozilla Science Fellowships | 1,181,000 | 950,000 |
| Leadership Development: Knight-Mozilla OpenNews | | 106,000 |
| Community: Coral Software Project | 846,000 | 1,227,000 |
| Leadership Development: Responsible Computer Science Challenge | 73,000 | |
| Thunderbird | 477,000 | 183,000 |
| Agenda-setting: Digital Skills Observatory | | 137,000 |
| Other | 282,000 | 196,000 |
| | <u>\$ 4,816,000</u> | <u>\$ 5,363,000</u> |

Mozilla Foundation and Subsidiary

Notes to Consolidated Financial Statements

Note 10 - Income Taxes:

Mozilla's income tax provision (benefit) consists of the following:

| | 2018 | | | |
|------------------------------|-----------------------|-----------------------|---------------------|-----------------------|
| | Federal | State | Foreign | Total |
| Current provision (benefit) | | | | |
| Foundation | \$ 54,000 | | | \$ 54,000 |
| Corporation | (4,298,000) | \$ 48,000 | \$ 1,087,000 | (3,163,000) |
| Deferred provision (benefit) | | | | |
| Corporation | (2,701,000) | (1,301,000) | 76,000 | (3,926,000) |
| Total | \$ (6,945,000) | \$ (1,253,000) | \$ 1,163,000 | \$ (7,035,000) |

| | 2017 | | | |
|------------------------------|----------------------|-------------------|---------------------|----------------------|
| | Federal | State | Foreign | Total |
| Current provision (benefit) | | | | |
| Foundation | \$ (60,000) | | | \$ (60,000) |
| Corporation | 49,809,000 | \$ 1,080,000 | \$ 3,408,000 | 54,297,000 |
| Deferred provision (benefit) | | | | |
| Corporation | (3,329,000) | (126,000) | (194,000) | (3,649,000) |
| Total | \$ 46,420,000 | \$ 954,000 | \$ 3,214,000 | \$ 50,588,000 |

The provision for income taxes differs from taxes calculated at the federal statutory rate primarily due to the activity related to Mozilla's unrecognized tax positions, nondeductible expenses, research and development credits, accrued expenses and other reserves, and state income taxes net of federal tax benefit.

On December 22, 2017, the Tax Cuts and Jobs Act (the Tax Act) was signed into law, enacting a broad range of changes to the U.S. Internal Revenue Code. The Tax Act makes broad and complex changes to the U.S. tax code, including, but not limited to, (1) reducing the U.S. federal corporate tax rate from 35 percent to 21 percent; (2) requiring companies to pay a one-time transition tax on certain unrepatriated earnings of foreign subsidiaries; (3) generally eliminating U.S. federal income taxes on dividends from foreign subsidiaries; (4) requiring a current inclusion in U.S. federal taxable income of certain earnings of controlled foreign corporations; and (5) creating the base erosion anti-abuse tax (BEAT), a new minimum tax. The Tax Act also imposes significant limitations on the deductibility of interest, executive compensation and future net operating losses. The Tax Act allows for the expensing of certain capital expenditures.

Mozilla Foundation and Subsidiary

Notes to Consolidated Financial Statements

As part of the transition to the new territorial tax system, the Tax Act imposes a one-time tax on deemed repatriation of historical earnings of foreign subsidiaries. For the period ended December 31, 2017, Mozilla recorded a provisional tax expense of \$1,782,000 based on Mozilla's interpretation and understanding of the Tax Act at the time. During the twelve months ended December 31, 2018, Mozilla completed the accounting for tax effects of all income tax effects of the Tax Act and based on management's analysis, there were immaterial changes from provisional amounts previously recorded for the year ended December 31, 2017. These revisions will be treated in accordance with the measurement period guidance outlined in Staff Accounting Bulletin No. 118.

Deferred taxes are reflected in the statement of financial position as follows:

| | 2018 | 2017 |
|-------------------|---------------|--------------|
| Total assets | \$ 11,756,000 | \$ 7,518,000 |
| Total liabilities | (1,551,000) | (1,017,000) |
| | <hr/> | <hr/> |
| | \$ 10,205,000 | \$ 6,501,000 |

As of December 31, 2018, Mozilla had net operating loss carryforwards for federal and state income tax purposes of approximately \$27.7 million and \$20.2 million, respectively. Federal and state net operating losses incurred before tax year 2018 begin to expire in years beginning in 2032 and 2032, respectively. Federal net operating losses incurred during 2018 and future years will be carried forward indefinitely.

As of December 31, 2018, Mozilla had tax credit carryforwards for state income tax purposes of approximately \$13.7 million. The state credits do not expire.

Mozilla has not provided for U.S. deferred taxes on its undistributed earnings for non-U.S. subsidiaries because these earnings are intended to be permanently invested in operations outside the United States.

Mozilla Foundation and Subsidiary

Notes to Consolidated Financial Statements

The activity related to Mozilla's unrecognized tax positions is set forth below:

| | Foundation | Corporation | Total |
|---|------------|--------------|--------------|
| Balance at December 31, 2016 | | \$ 6,584,000 | \$ 6,584,000 |
| Increases related to current tax positions | | 1,484,000 | 1,484,000 |
| Increases related to prior year tax positions | | 545,000 | 545,000 |
| Lapse of time restrictions | | (1,622,000) | (1,622,000) |
| Balance at December 31, 2017 | | 6,991,000 | 6,991,000 |
| Decreases related to current tax positions | | (1,004,000) | (1,004,000) |
| Increases related to prior year tax positions | | 1,174,000 | 1,174,000 |
| Lapse of time restrictions | | (1,259,000) | (1,259,000) |
| Balance at December 31, 2018 | | \$ 5,902,000 | \$ 5,902,000 |

Mozilla also accrued potential penalties and interest of \$128,000 and \$73,000 related to these unrecognized tax benefits during 2018 and 2017, respectively, and in total, has recorded a liability for potential penalties and interest of \$372,000 and \$260,000, as of December 31, 2018 and 2017, respectively. Mozilla recognizes interest and penalties related to unrecognized tax benefits within the income tax expense line in the accompanying statement of activities and change in net assets. Accrued interest and penalties are included within the unrecognized tax positions line in the statement of financial position. Mozilla does not expect its unrecognized tax benefits to change significantly over the next 12 months.

Mozilla files U.S., state, and foreign income tax returns in jurisdictions with varying statutes of limitations. Mozilla is generally no longer subject to income tax examination by the U.S. Federal and state taxing authorities for the tax years ending before 2015 and 2014, respectively. In foreign jurisdictions, the 2012 through 2018 tax years generally remain subject to examination by their respective taxing authorities.

Mozilla Foundation and Subsidiary

Notes to Consolidated Financial Statements

Note 11 - Employee Benefit Plans:

The Foundation and the Corporation sponsor defined contribution plans covering substantially all employees in the United States and Canada. The Foundation and the Corporation contribute an amount equal to 3% of the employee's qualified salary plus an additional discretionary 4% of their qualified salary. Contributions to the plans totaled \$8,090,000 and \$7,213,000 for 2018 and 2017, respectively.

For certain other foreign locations, Mozilla contributes employee benefits due in accordance with local labor regulations. Contributions totaled \$2,361,000 and \$2,386,000 for 2018 and 2017, respectively.

The Corporation maintains a Long-Term Incentive Plan whereby a Board committee annually approves the participants and amount. Expenses of approximately \$21,819,000 and \$14,288,000 were recorded in 2018 and 2017, respectively.

Note 12 - Concentrations of Risk:

Mozilla has entered into contracts with search engine providers for royalties which expire through November 2020.

Approximately 91% and 93% of Mozilla's royalty revenues were derived from these contracts for 2018 and 2017, respectively, with receivables from these contracts representing approximately 75% and 79% of the December 31, 2018 and 2017 outstanding receivables, respectively.

Mozilla has defined its financial instruments which are potentially subject to credit risk as cash and cash equivalents and investments. At December 31, 2018 and 2017, essentially all of the cash and cash equivalents accounts are in excess of the federally insured limits. In addition, investments in general are exposed to various risks, such as interest rate, credit and overall market volatility. To address these risks, Mozilla maintains an investment policy that sets out performance criteria, investment, and asset allocation guidelines, and actively manages the investments to these policies.

Mozilla Foundation and Subsidiary

Notes to Consolidated Financial Statements

At December 31, 2018 and 2017, the financial statements include the following amounts of assets, liabilities and foreign currency transaction gains and losses relating to subsidiaries and branches outside the United States of America:

| | 2018 | 2017 |
|---|---------------|---------------|
| Assets: | | |
| Europe | \$ 17,342,000 | \$ 15,029,000 |
| Asia | 19,282,000 | 17,660,000 |
| North America | 1,638,000 | 1,644,000 |
| Australia and Oceanic | 150,000 | 168,000 |
| | <hr/> | <hr/> |
| | \$ 38,412,000 | \$ 34,501,000 |
| Liabilities: | | |
| Europe | \$ 1,535,000 | \$ 5,821,000 |
| Asia | 939,000 | 1,807,000 |
| North America | 8,544,000 | 8,588,000 |
| Australia and Oceanic | 754,000 | 638,000 |
| | <hr/> | <hr/> |
| | \$ 11,772,000 | \$ 16,854,000 |
| Foreign currency transaction gain (loss), net | \$ (134,000) | \$ 166,000 |

Note 13 - Commitments:

Included in cash at December 31, 2018 and 2017 is approximately \$1,000,000 of collateral pledged for lease agreements.

Mozilla leases office space under leases, which expire through August 2023. Some leases have options to renew and certain leases are guaranteed by letters of credit. Rent expense for 2018 and 2017 totaled \$10,869,000 and \$9,758,000, respectively. Future minimum lease commitments are as follows and include all base rent and operating expenses.

| | |
|--------------------------|---------------|
| 2019 | \$ 9,843,000 |
| 2020 | 10,663,000 |
| 2021 | 7,629,000 |
| 2022 | 4,844,000 |
| 2023 | 2,972,000 |
| | <hr/> |
| Total scheduled payments | \$ 35,951,000 |

Mozilla Foundation and Subsidiary

Notes to Consolidated Financial Statements

Mozilla is currently involved in litigation matters arising in the normal course of its operations. This includes Yahoo Holdings Inc. v. Mozilla Corporation, scheduled for trial in California State Court on September 29, 2019. Mozilla will vigorously defend itself in the pending actions and management does not anticipate any adverse material financial impact resulting from such matters. No accrual has been made in these financial statements.

Note 14 - Related Party Transactions:

The Corporation pays the Foundation two percent (2%) of its annual net revenues related to the use of the trademarks less approved expenses of the current year in license fees per a license agreement. The Corporation incurred \$8,500,000 and \$10,796,000 in license fees to the Foundation in 2018 and 2017, respectively.

During 2018, the Corporation also paid a one-time additional flat fee of \$4.5 million to the Foundation based on a one-time supplemental agreement between the parties.

The Corporation provides basic administrative services, IT support and legal services under a service agreement between the Corporation and the Foundation.

As noted in Note 2b, all significant intercompany transactions have been eliminated in the preparation of these consolidated financial statements.