

Michigan Humane Society

Financial Report
September 30, 2013

Michigan Humane Society

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Independent Auditor's Report

To the Board of Directors
Michigan Humane Society

We have audited the accompanying financial statements of Michigan Humane Society (the "Organization"), which comprise the balance sheet as of September 30, 2013 and 2012 and the related statements of activities and changes in net assets, functional expenses, and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our 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 from material misstatement.

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Michigan Humane Society as of September 30, 2013 and 2012 and the changes in its net assets and its cash flows for the years then ended, in accordance with accounting principles generally accepted in the United States of America.

Plante & Moran, PLLC

January 27, 2014

Michigan Humane Society

Balance Sheet

	September 30, 2013	September 30, 2012
Assets		
Cash and cash equivalents	\$ 1,469,224	\$ 1,717,913
Accounts receivable:		
Operational accounts receivable	34,608	29,143
Legacies and bequests receivable	1,168,164	941,206
Investment-related and other accounts receivable	97,202	150,927
Capital campaign receivable (Note 3)	984,401	-
Investments (Note 4)	10,915,790	11,354,436
Inventory	378,661	313,441
Prepaid expenses and other	147,785	177,229
Interest in trusts	1,081,000	1,074,000
Property and equipment - Net (Note 5)	8,325,308	7,992,679
	<u>\$ 24,602,143</u>	<u>\$ 23,750,974</u>
Total assets		
Liabilities and Net Assets		
Liabilities		
Accounts payable	\$ 688,821	\$ 834,798
Annuities payable	60,273	-
Accrued salaries, wages, and employee benefits payable	613,387	661,962
	<u>1,362,481</u>	<u>1,496,760</u>
Total liabilities		
Net Assets		
Unrestricted	19,128,827	18,930,444
Temporarily restricted (Note 6)	3,923,335	3,136,270
Permanently restricted	187,500	187,500
	<u>23,239,662</u>	<u>22,254,214</u>
Total net assets		
	<u>\$ 24,602,143</u>	<u>\$ 23,750,974</u>
Total liabilities and net assets		

Michigan Humane Society

Statement of Activities and Changes in Net Assets

	Year Ended	
	September 30, 2013	September 30, 2012
Changes in Unrestricted Net Assets		
Revenue and support:		
Contributions	\$ 5,329,705	\$ 5,083,973
Legacies and bequests	1,742,648	1,716,130
Adoption center and charitable veterinary hospital - Net (Note 2)	5,982,903	5,953,641
Retail	16,736	21,687
Special event revenue:		
Gross revenue	1,405,494	1,168,234
Direct benefit to donor costs	(61,616)	(50,672)
Investment gain (Note 4)	1,375,050	1,551,409
Gain on disposal of property and equipment	300	500
Total revenue and support	15,791,220	15,444,902
Net assets released from restrictions	1,409,662	1,543,266
Total unrestricted revenue, support, and net assets released from restrictions	17,200,882	16,988,168
Expenses:		
Program services	14,161,300	13,745,438
Support services:		
Management and general	660,633	630,486
Fundraising	2,180,566	2,426,698
Total expenses	17,002,499	16,802,622
Increase in Unrestricted Net Assets	198,383	185,546
Changes in Temporarily Restricted Net Assets		
Contributions	1,091,563	222,646
Legacies and bequests	1,098,164	846,206
Change in value of split interest agreements	7,000	(22,000)
Net assets released from restrictions	(1,409,662)	(1,543,266)
Increase (Decrease) in Temporarily Restricted Net Assets	787,065	(496,414)
Increase (Decrease) in Net Assets	985,448	(310,868)
Net Assets - Beginning of year	22,254,214	22,565,082
Net Assets - End of year	\$ 23,239,662	\$ 22,254,214

Michigan Humane Society

Statement of Functional Expenses Year Ended September 30, 2013

	Program Services	Support Services		Total
		Management and General	Fundraising	
Salaries	\$ 7,404,260	\$ 272,366	\$ 455,994	\$ 8,132,620
Employee benefits	1,006,053	59,275	33,587	1,098,915
Payroll taxes	666,326	44,632	37,789	748,747
Total salaries and salary-related expenses	9,076,639	376,273	527,370	9,980,282
Animal care expenses	1,880,269	-	56	1,880,325
Facility expense	255,413	706	240	256,359
Insurance	56,453	1,157	2,588	60,198
Vehicle expense	189,358	19,056	8,965	217,379
Rental expense	130,872	49,474	44,272	224,618
Repairs and maintenance - Building	159,631	82	74	159,787
Utilities	350,228	2,632	2,333	355,193
Telephone and connectivity	117,766	16,539	9,482	143,787
Fundraising and special event costs	240,514	-	882,055	1,122,569
Public relations and marketing	318,689	6,814	6,749	332,252
Postage	32,670	3,092	295,672	331,434
Printing	33,669	112	23,766	57,547
Professional fees	180,380	54,880	178,605	413,865
Office supplies and expenses	160,925	15,853	16,622	193,400
Meeting expense	22,837	11,950	3,031	37,818
Employee expenses	57,962	4,942	10,300	73,204
Cost of sales	5,902	-	8,229	14,131
Investment and banking fees	83,821	59,881	118,745	262,447
IT licenses and support	166,757	17,074	33,670	217,501
Support of collaborative efforts	12,659	300	-	12,959
Depreciation	591,065	8,180	5,973	605,218
Other	36,821	11,636	1,769	50,226
Total expenses before direct benefit to donor costs	14,161,300	660,633	2,180,566	17,002,499
Direct benefit to donor	-	-	-	61,616
Total expenses including direct benefit to donor costs	\$ 14,161,300	\$ 660,633	\$ 2,180,566	\$ 17,064,115

Michigan Humane Society

Statement of Functional Expenses Year Ended September 30, 2012

	Program Services	Support Services		Total
		Management and General	Fundraising	
Salaries	\$ 7,153,328	\$ 222,482	\$ 424,261	\$ 7,800,071
Employee benefits	920,169	41,726	33,299	995,194
Payroll taxes	627,367	41,487	34,203	703,057
Total salaries and salary-related expenses	8,700,864	305,695	491,763	9,498,322
Animal care expenses	1,800,309	-	-	1,800,309
Facility expense	270,476	664	-	271,140
Insurance	53,030	1,138	2,203	56,371
Vehicle expense	210,859	22,182	7,014	240,055
Rental expense	129,805	49,074	37,333	216,212
Repairs and maintenance - Building	160,760	238	632	161,630
Utilities	319,856	2,669	2,365	324,890
Telephone and connectivity	67,576	12,343	4,300	84,219
Fundraising and special events	171,106	-	1,160,827	1,331,933
Public relations and marketing	554,832	9,039	8,926	572,797
Postage	32,781	3,248	348,626	384,655
Printing	32,199	129	14,269	46,597
Professional fees	125,881	56,593	168,880	351,354
Office supplies and expenses	174,488	14,069	17,123	205,680
Meeting expense	20,613	17,211	3,050	40,874
Employee expenses	79,498	17,043	6,719	103,260
Investment and banking fees	78,303	64,216	108,503	251,022
IT license and support	124,517	20,913	33,807	179,237
Support of collaborative efforts	14,840	-	-	14,840
Interest expense	58,092	-	-	58,092
Change in fair value of interest rate swap	(36,559)	-	-	(36,559)
Depreciation	553,306	14,697	7,858	575,861
Other expenses	48,006	19,325	2,500	69,831
Total expenses before direct benefit to donor costs	13,745,438	630,486	2,426,698	16,802,622
Direct benefit to donor	-	-	-	50,672
Total expenses including direct benefit to donor costs	\$ 13,745,438	\$ 630,486	\$ 2,426,698	\$ 16,853,294

Michigan Humane Society

Statement of Cash Flows

	Year Ended	
	September 30, 2013	September 30, 2012
Cash Flows from Operating Activities		
Increase (decrease) in net assets	\$ 985,448	\$ (310,868)
Adjustments to reconcile increase (decrease) in net assets to net cash from operating activities:		
Depreciation	605,218	575,861
Gain on disposal of property and equipment	(300)	(500)
Amortization discount on pledges receivable	68,776	-
Net realized and unrealized gains on investments	(999,718)	(1,123,143)
Donated investments	(144,206)	(224,406)
Donated property lease receivable	-	(72,000)
Change in value of interest rate swap	-	(36,559)
Change in value of interest in trusts	(7,000)	22,000
Contributions restricted for building improvements	(1,105,183)	(55,024)
Contributions restricted for future operations - Requests receivable	(1,098,164)	(846,206)
Changes in operating assets and liabilities which (used) provided cash:		
Operational accounts receivable	(5,465)	2,038
Other accounts receivable	53,225	54,074
Legacies and bequests receivable	871,206	1,489,213
Inventory	(65,220)	75,159
Prepaid expenses and other	29,444	(35,780)
Accounts payable	(85,704)	149,272
Accrued salaries, wages, and employee benefits payable	(48,575)	183,107
Net cash used in operating activities	(946,218)	(153,762)
Cash Flows from Investing Activities		
Purchase of property and equipment	(937,847)	(590,197)
Proceeds from disposition of property and equipment	300	500
Purchases of investments	(2,266,683)	(924,583)
Proceeds from sales and maturities of investments	3,849,253	4,414,235
Net cash provided by investing activities	645,023	2,899,955
Cash Flows from Financing Activities		
Payments on debt	-	(2,840,827)
Payment to terminate interest rate swap	-	(25,515)
Proceeds from capital campaign contributions	38,780	4,298
Proceeds from contributions restricted for building improvements	13,726	55,024
Net cash provided by (used in) financing activities	52,506	(2,807,020)
Net Decrease in Cash and Cash Equivalents	(248,689)	(60,827)
Cash and Cash Equivalents - Beginning of year	1,717,913	1,778,740
Cash and Cash Equivalents - End of year	<u>\$ 1,469,224</u>	<u>\$ 1,717,913</u>
Supplemental Disclosure of Cash Flow Information - Cash paid for interest	<u>\$ -</u>	<u>\$ 58,092</u>

Note I - Nature of Organization and Significant Accounting Policies

Nature of Organization - Michigan Humane Society (the "Organization") is a not-for-profit corporation dedicated to ending companion animal homelessness, providing the highest quality service and compassion to the animals entrusted to its care, and being a leader in promoting humane values. The Organization operates three adoption centers, three charitable veterinary hospitals, emergency animal rescue services, a cruelty investigation division, and an education division. In addition, the Organization facilitates companion animal adoption at multiple offsite locations and special events. Southeastern Michigan is the primary service area for the Organization's operations.

Significant accounting policies are as follows:

Cash Equivalents - The Organization considers all highly liquid investments purchased with a maturity of three months or less to be cash equivalents except for certain money market mutual funds that are included in the Organization's investment portfolio. The balances in the Organization's deposit accounts may, from time to time, exceed the amounts covered by FDIC insurance.

Accounts Receivable - Accounts receivable consist of operational accounts receivable, capital campaign pledges receivable, legacies and bequests receivable, and investment-related and other accounts receivable.

Operational accounts receivable are stated at invoice amounts from services provided. An allowance for doubtful accounts is established based on a specific assessment of all invoices that remain unpaid following normal payment periods. In addition, a general valuation allowance is established for other accounts receivable based on historical loss experience. All amounts deemed uncollectible are charged against the allowance for doubtful accounts in the period that determination is made. All operational accounts receivable are considered fully collectible as of September 30, 2013 and 2012.

Capital campaign pledges receivable are stated at the gross promise to give, less amortized discounts and allowances for uncollectible pledges. The Organization calculates the amortized discounts at 3.00 percent of the pledges receivable balance at year end. The unamortized discount on capital campaign pledges receivable is \$68,776 and \$0 as of September 30, 2013 and 2012, respectively. The allowance on capital campaign pledges receivable is \$21,493 and \$0 as of September 30, 2013 and 2012, respectively.

The legacies and bequests receivable consist of wills and bequests for which the donor and all other life beneficiaries are deceased and are therefore irrevocable. Payment on these receivables is expected in the next year. The legacies and bequests receivable are deemed fully collectible as of September 30, 2013 and 2012.

Note 1 - Nature of Organization and Significant Accounting Policies (Continued)

The investment-related and other accounts receivable consists primarily of interest and dividend income receivable and donated rent receivable related to a below market lease agreement. The Organization has recorded a receivable for the fair market value of the lease over the remaining lease term.

Investments - Investments in debt and equity securities are recorded at fair value as described in Note 10.

Risks and Uncertainties - The Organization invests in various investment securities. Investment securities are exposed to various risks such as interest rate, market, and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect the amounts reported in the balance sheet.

Inventory - Inventory, which consists of medical supplies and retail items, is stated at the lower of cost or market, by use of the first-in, first-out (FIFO) method of valuation.

Interest in Trusts - Interest in trusts consists of funds which are held in trusts of which the Organization is a beneficiary. The corpus of the trusts is expected to be paid to the Organization through 2020.

Property and Equipment - Property and equipment are recorded at cost when purchased or at fair value at the date of donation and are being depreciated on a straight-line basis over their estimated useful lives, which range from 2 to 40 years depending on the type of asset. Costs of maintenance and repairs are charged to expense when incurred.

The Organization reports gifts of property, plant, and equipment as unrestricted support unless explicit donor stipulations specify how the donated assets must be used. Gifts of property, plant, and equipment with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire property, plant, and equipment are reported as restricted support. Absent explicit donor stipulations about how long the property, plant, and equipment must be maintained, the Organization reports expirations of donor restrictions over time based on an estimate of the useful lives of the donated or acquired property, plant, and equipment.

Contributions - Contributions of cash and other assets, including unconditional promises to give in the future, are reported as revenue when received, measured at fair value. Donor promises to give in the future are recorded at the present value of estimated future cash flows.

Note I - Nature of Organization and Significant Accounting Policies (Continued)

Contributions without donor-imposed restrictions and contributions with donor-imposed time or purpose restrictions that are met in the same period as the gift are both reported as unrestricted support. Other restricted gifts are reported as restricted support and temporarily or permanently restricted net assets.

The Organization receives donations of various goods and services. For the years ended September 30, 2013 and 2012, in-kind donations of \$141,030 and \$272,664, respectively, met the criteria for recording in accordance with generally accepted accounting principles and have been recorded in the statement of activities and changes in net assets. The Organization also receives significant volunteer services that are not recordable in accordance with generally accepted accounting principles.

Classification of Net Assets - Net assets of the Organization are classified as unrestricted, temporarily restricted, or permanently restricted depending on the presence and characteristics of donor-imposed restrictions limiting the Organization's ability to use or dispose of contributed assets or the economic benefits embodied in those assets.

Donor-imposed restrictions that expire with the passage of time or that can be removed by meeting certain requirements result in temporarily restricted net assets. Permanently restricted net assets result from donor-imposed restrictions that limit the use of net assets in perpetuity. Earnings, gains, and losses on permanently restricted net assets are available to support the general charitable purpose of the Organization. In accordance with generally accepted accounting principles, these earnings and gains are classified as temporarily restricted until they are appropriated for expenditure.

Board-designated Net Assets - Unrestricted board-designated net assets are investments and other assets set aside by the board for capital projects, sterilization, and as a general reserve fund. These designations are based on board actions, which can be altered or revoked at a future time by the board. As of September 30, 2013 and 2012, the board had designated net assets of \$10,276,398 and \$10,095,900, respectively.

Permanently Restricted Net Assets - The Organization has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the Organization must hold in perpetuity or for a donor-specified period. Under this policy, as approved by the board of directors, the endowment assets are invested in a manner that is intended to produce results that exceed the price and yield results of their equity and bond holdings, while assuming a moderate level of investment risk. The Organization expects its endowment funds, over time, to provide a rate of return equivalent to those of its general investment portfolio. Actual returns in any given year may vary from this amount.

Note I - Nature of Organization and Significant Accounting Policies (Continued)

To satisfy its long-term rate of return objectives, the Organization relies on a total return strategy in which investment returns are achieved through current yield (interest and dividends). The Organization targets a diversified asset allocation in order to achieve its long-term return objectives within prudent risk constraints.

Functional Allocation of Expenses - The costs of providing program and support services have been reported on a functional basis in the statement of activities and changes in net assets. Indirect costs have been allocated between the various programs and support services based on estimates, as determined by management. Although the methods of allocation used are considered reasonable, other methods could be used that would produce different amounts.

Use of Estimates - The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue, expenses, and other changes in net assets during the reporting period. Actual results could differ from those estimates.

Federal Income Taxes - The Organization is exempt from income tax under provisions of Internal Revenue Code Section 501(c)(3). Accounting principles generally accepted in the United States of America require management to evaluate tax positions taken by the Organization and recognize a tax liability if the Organization has taken an uncertain position that more likely than not would not be sustained upon examination by the IRS or other applicable taxing authorities. Management has analyzed the tax positions taken by the Organization and has concluded that as of September 30, 2013 and 2012, there are no uncertain positions taken or expected to be taken that would require recognition of a liability or disclosure in the financial statements. The Organization is subject to routine audits by taxing jurisdictions; however, there are currently no audits for any tax periods in progress. Management believes it is no longer subject to income tax examinations for years prior to 2010.

Reclassification - Certain expenses on the 2012 statement of functional expenses were reclassified to other line items to conform to the line items in the 2013 statement of functional expenses.

Subsequent Events - The financial statements and related disclosures include evaluation of events up through and including January 27, 2014, which is the date the financial statements were available to be issued.

Michigan Humane Society

Notes to Financial Statements September 30, 2013 and 2012

Note 2 - Adoption Center and Charitable Veterinary Hospital Revenue

Adoption center and charitable veterinary hospital revenue for the years ended September 30, 2013 and 2012 is reported net of discounts as follows:

	<u>2013</u>	<u>2012</u>
Adoption center and charitable veterinary hospital revenue - Gross	\$ 7,697,137	\$ 7,602,117
Clinic discounts and other	<u>(1,714,234)</u>	<u>(1,648,476)</u>
Net revenue	<u>\$ 5,982,903</u>	<u>\$ 5,953,641</u>

Clinic discounts represent services provided for free or at reduced fees, including sterilizations performed for free or below cost, treatment and care provided to animals during their stay at the Organization, treatment of animals post-adoption, treatment of animals from cruelty situations, and services provided to clients with limited financial capability at reduced prices.

Note 3 - Contributions Receivable

Included in contributions receivable are unconditional promises to give generated from a capital campaign that began during 2013. They are included as follows:

	<u>2013</u>	<u>2012</u>
Gross promises to give before unamortized discount	\$ 1,074,670	\$ -
Less unamortized discount, using 3 percent discount rate	(68,776)	-
Less allowance for doubtful accounts	<u>(21,493)</u>	<u>-</u>
Net contributions receivable	<u>\$ 984,401</u>	<u>\$ -</u>
Amounts due in:		
Less than one year	\$ 397,116	\$ -
One to five years	<u>677,554</u>	<u>-</u>
Total	<u>\$ 1,074,670</u>	<u>\$ -</u>

The Organization receives contributions from related parties such as board members and management. For the years ending September 30, 2013 and 2012, such contributions were approximately \$1,100,000 and \$94,000, respectively. The entire receivable balance above is due from these related parties.

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Notes to Financial Statements September 30, 2013 and 2012

Note 4 - Investments

Investments consisted of the following at September 30, 2013 and 2012:

	<u>2013</u>	<u>2012</u>
Money market funds	\$ 232,574	\$ 649,735
Corporate debt securities	3,634,636	5,719,453
Common stock	6,492,368	4,393,765
Mutual funds	307,798	258,486
Preferred stock	248,414	332,997
Total	<u>\$ 10,915,790</u>	<u>\$ 11,354,436</u>

Interest and dividend income totaled \$375,332 and \$428,266 in 2013 and 2012, respectively. Net realized and unrealized gains on investments totaled \$999,718 and \$1,123,143 in 2013 and 2012, respectively.

Note 5 - Property and Equipment

The cost of property and equipment is summarized as follows:

	<u>2013</u>	<u>2012</u>
Land	\$ 848,268	\$ 848,268
Land improvements	476,313	473,394
Buildings	7,066,643	7,066,643
Building improvements	2,338,290	2,191,713
Medical and other equipment	3,816,460	3,704,748
Transportation equipment - Cost	764,521	712,325
Furniture and fixtures - Cost	437,731	437,731
Computer equipment and software - Cost	296,117	282,984
Leasehold improvements	86,133	56,851
Construction in progress	887,575	305,547
Total cost	17,018,051	16,080,204
Accumulated depreciation	<u>(8,692,743)</u>	<u>(8,087,525)</u>
Net carrying amount	<u>\$ 8,325,308</u>	<u>\$ 7,992,679</u>

Depreciation expense totaled \$605,218 and \$575,861 in 2013 and 2012, respectively.

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Notes to Financial Statements September 30, 2013 and 2012

Note 6 - Temporarily Restricted Net Assets

Temporarily restricted net assets at September 30, 2013 and 2012 are restricted for the following:

	<u>2013</u>	<u>2012</u>
Time-restricted contributions	\$ 2,249,165	\$ 2,015,206
Construction of new facilities	1,362,095	742,048
Building and equipment improvements	168,413	180,902
Program activity	125,959	160,980
Life insurance policy cash surrender value	<u>17,703</u>	<u>37,134</u>
Total temporarily restricted net assets	<u>\$ 3,923,335</u>	<u>\$ 3,136,270</u>

Note 7 - Operating Leases

The Organization has operating lease agreements for office space and equipment. Total rent expense under these leases was \$258,884 and \$249,659 for the years ended September 30, 2013 and 2012, respectively. Future commitments under these operating leases are as follows:

2014	\$ 225,279
2015	218,808
2016	184,787
2017	21,598
2018	<u>11,088</u>
Total	<u>\$ 661,560</u>

Note 8 - Employee Benefit Plan

The Organization has a 403(b) retirement plan (the "Plan"). Under the Plan, employees can elect to defer a portion of their compensation. The Organization made matching contributions of \$151,213 and \$118,616 to the Plan for the years ended September 30, 2013 and 2012, respectively.

Note 9 - Allocation of Joint Costs

The Organization's newsletter and certain event activities include requests for contributions, as well as education and retail components. Total joint costs for these activities were \$568,605 and \$774,545 for the years ended September 30, 2013 and 2012, respectively. These costs are not specifically attributable to fundraising or education activities and were allocated as follows:

	2013	2012
Fundraising	\$ 255,449	\$ 337,674
Education	313,156	436,871
Total	<u>\$ 568,605</u>	<u>\$ 774,545</u>

Note 10 - Fair Value Measurements

Accounting standards require certain assets and liabilities be reported at fair value in the financial statements and provide a framework for establishing that fair value. The framework for determining fair value is based on a hierarchy that prioritizes the inputs and valuation techniques used to measure fair value.

The following tables present information about the Organization's assets and liabilities measured at fair value on a recurring basis at September 30, 2013 and 2012 and the valuation techniques used by the Organization to determine those fair values.

Fair values determined by Level 1 inputs use quoted prices in active markets for identical assets that the Organization has the ability to access.

Fair values determined by Level 2 inputs use other inputs that are observable, either directly or indirectly. These Level 2 inputs include quoted prices for similar assets in active markets and other inputs such as interest rates and yield curves that are observable at commonly quoted intervals.

Level 3 inputs are unobservable inputs, including inputs that are available in situations where there is little, if any, market activity for the related asset. These Level 3 fair value measurements are based primarily on management's own estimates using pricing models, discounted cash flow methodologies, or similar techniques taking into account the characteristics of the asset.

In instances whereby inputs used to measure fair value fall into different levels in the above fair value hierarchy, fair value measurements in their entirety are categorized based on the lowest level input that is significant to the valuation. The Organization's assessment of the significance of particular inputs to these fair value measurements requires judgment and considers factors specific to each asset.

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Notes to Financial Statements September 30, 2013 and 2012

Note 10 - Fair Value Measurements (Continued)

Assets and Liabilities Measured at Fair Value on a Recurring Basis at September 30, 2013

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance at September 30, 2013
Assets				
Investments:				
Money market funds	\$ 232,574	\$ -	\$ -	\$ 232,574
Mutual funds	307,798	-	-	307,798
Common stock:				
Communications	363,237	-	-	363,237
Consumer cyclical	602,725	-	-	602,725
Consumer noncyclical	140,441	-	-	140,441
Energy	1,617,075	-	-	1,617,075
Financial	1,048,480	-	-	1,048,480
Industrial	991,515	-	-	991,515
Technology	205,784	-	-	205,784
Utilities	1,267,749	-	-	1,267,749
Healthcare	255,362	-	-	255,362
Preferred stock	-	248,414	-	248,414
Corporate debt:				
A credit rating	-	427,468	-	427,468
Baa credit rating	-	1,758,008	-	1,758,008
Ba credit rating	-	573,677	-	573,677
B credit rating	-	734,775	-	734,775
Not rated	-	140,708	-	140,708
Total investments	7,032,740	3,883,050	-	10,915,790
Interest in trusts	-	-	1,081,000	1,081,000
Total assets	\$ 7,032,740	\$ 3,883,050	\$ 1,081,000	\$ 11,996,790
Liabilities - Charitable gift annuity	\$ -	\$ -	\$ 60,273	\$ 60,273

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Notes to Financial Statements September 30, 2013 and 2012

Note 10 - Fair Value Measurements (Continued)

Assets Measured at Fair Value on a Recurring Basis at September 30, 2012

Assets	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance at September 30, 2012
Cash equivalents - Sweep account - Money market funds	\$ 919,791	\$ -	\$ -	\$ 919,791
Investments:				
Money market funds	649,735	-	-	649,735
Mutual funds	258,486	-	-	258,486
Common stock:				
Basic materials	164,650	-	-	164,650
Communications	431,909	-	-	431,909
Consumer cyclical	428,225	-	-	428,225
Consumer noncyclical	234,990	-	-	234,990
Energy	740,183	-	-	740,183
Financial	699,081	-	-	699,081
Industrial	323,279	-	-	323,279
Technology	335,893	-	-	335,893
Utilities	1,035,555	-	-	1,035,555
Preferred stock	-	332,997	-	332,997
Corporate debt:				
A credit rating	-	749,285	-	749,285
Baa credit rating	-	3,012,455	-	3,012,455
Ba credit rating	-	956,061	-	956,061
B credit rating	-	864,151	-	864,151
Not rated	-	137,501	-	137,501
Total investments	5,301,986	6,052,450	-	11,354,436
Interest in trusts	-	-	1,074,000	1,074,000
Total assets	<u>\$ 6,221,777</u>	<u>\$ 6,052,450</u>	<u>\$ 1,074,000</u>	<u>\$ 13,348,227</u>

Preferred stock and debt securities, which include U.S. agency notes, convertible bonds, and corporate bonds, are valued using quoted market prices and other market data for the same or comparable instruments and transactions in establishing the prices, discounted cash flow models, and other pricing models. These models are primarily industry-standard models that consider various assumptions, including time value and yield curve as well as other relevant economic measures.

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Notes to Financial Statements September 30, 2013 and 2012

Note 10 - Fair Value Measurements (Continued)

The following table summarizes the valuation methods and inputs used to determine fair value at September 30, 2013 for assets and liabilities measured at fair value on a recurring basis using unobservable inputs (Level 3 inputs).

	Fair Value at September 30, 2013	Valuation Technique	Significant Unobservable Inputs Used	Range
Assets - Interest in trusts	\$ 1,081,000	Discounted cash flow	Growth rate Life expectancies of beneficiaries	3% 22-24 years
Liabilities - Charitable gift annuity	60,273	Discounted cash flow	Growth rate Life expectancies of beneficiaries	2% 3-7 years
	-			

The Organization has processes in place to select the appropriate valuation technique and unobservable inputs to perform Level 3 fair value measurements. These processes include reviewing the life expectancy of the income beneficiary of the trusts, the term of the trusts, the expected growth and distribution rates, and the Organization's relative share of assets held in the trusts.

Changes in Level 3 assets and liabilities measured at fair value on a recurring basis for the years ended September 30, 2013 and 2012 (dollars in thousands) are as follows:

	Interest in Trusts	Charitable Gift Annuity
Balance at October 1, 2012	\$ 1,074,000	\$ -
Issuances	-	61,790
Change in beneficial interest in trusts recognized in gains	7,000	-
Distributions	-	(1,517)
Balance at September 30, 2013	<u>\$ 1,081,000</u>	<u>\$ 60,273</u>
		Interest in Trusts
Balance at October 1, 2011		\$ 1,096,000
Change in beneficial interest in trusts recognized in gains		(22,000)
Balance at September 30, 2012		<u>\$ 1,074,000</u>

Note 10 - Fair Value Measurements (Continued)

Both observable and unobservable inputs may be used to determine the fair value of positions classified as Level 3 assets. As a result, the unrealized gains and losses for these assets presented in the tables above may include changes in fair value that were attributable to both observable and unobservable inputs.

Of the Level 3 assets still held by the Organization at September 30, 2013, the unrealized gain (loss) for the years ended September 30, 2013 and 2012 was \$7,000 and (\$22,000), respectively, which is recognized in the statement of activities and changes in net assets.