Michigan Humane Society

Financial Report
September 30, 2011

Contents

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Independent Auditor's Report

To the Board of Directors
Michigan Humane Society

We have audited the accompanying balance sheet of the Michigan Humane Society (the "Organization") as of September 30, 2011 and the related statements of activities and changes in net assets, functional expenses, and cash flows for the nine months then ended. These financial statements are the responsibility of the Organization's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the 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 examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes 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, the financial statements referred to above present fairly, in all material respects, the financial position of the Michigan Humane Society at September 30, 2011 and the changes in its net assets and its cash flows for the nine months then ended, in conformity with accounting principles generally accepted in the United States of America.

Plante & Moran, PLLC

January 19, 2012

Michigan Humane Society

Balance Sheet
September 30, 2011

Assets		
Cash and cash equivalents	$	1,778,740
Accounts receivable:		
Operational accounts receivable		31,181
Legacies and bequests receivable		1,584,213
Investment-related and other accounts receivable		137,299
Investments (Note 3)		13,496,539
Inventory		388,600
Prepaid expenses and other		141,449
Interest in trusts		1,096,000
Property and equipment - Net (Note 4)		7,978,343
Total assets	**$**	**26,632,364**
Liabilities and Net Assets		
Liabilities		
Accounts payable	$	685,526
Note payable (Note 5)		2,840,827
Interest rate swap (Note 5)		62,074
Accrued salaries, wages, and employee benefits payable		478,855
Total liabilities		4,067,282
Net Assets		
Unrestricted		18,744,898
Temporarily restricted (Note 6)		3,632,684
Permanently restricted		187,500
Total net assets		22,565,082
Total liabilities and net assets	**$**	**26,632,364**

Michigan Humane Society

Statement of Activities and Changes in Net Assets
Nine Months Ended September 30, 2011

Changes in Unrestricted Net Assets	
Revenue and support:	
Contributions	$ 2,903,395
Legacies and bequests	709,141
Adoption center and charitable veterinary hospital - Net (Note 2)	4,681,051
Retail	5,103
Special event:	
Gross revenue	1,065,974
Direct benefit to donor costs	(55,624)
Investment loss (Note 3)	(186,174)
Gain on disposal of property and equipment	8,475
Total revenue and support	9,131,341
Net assets released from restrictions	878,092
Total unrestricted revenue, support, and net assets released from restrictions	10,009,433
Expenses:	
Program services	9,202,028
Support services:	
Management and general	457,650
Fundraising	1,406,065
Total expenses	11,065,743
Decrease in Unrestricted Net Assets	(1,056,310)
Changes in Temporarily Restricted Net Assets	
Contributions	37,604
Legacies and bequests	1,294,213
Change in value of interest in trusts	54,000
Net assets released from restrictions	(878,092)
Increase in Temporarily Restricted Net Assets	507,725
Decrease in Net Assets	(548,585)
Net Assets - Beginning of period	23,113,667
Net Assets - End of period	**$ 22,565,082**

See Notes to Financial Statements.

Michigan Humane Society

Statement of Functional Expenses
Nine Months Ended September 30, 2011

	Program Services	Support Services: Management and General	Support Services: Fundraising	Total
Salaries	$ 5,096,313	$ 153,732	$ 344,780	$ 5,594,825
Employee benefits	552,205	24,706	18,914	595,825
Payroll taxes	418,481	32,022	25,202	475,705
Total salaries and related expenses	6,066,999	210,460	388,896	6,666,355
Animal care expense	1,163,706	-	-	1,163,706
Facilities expense	166,712	433	59	167,204
Printing	13,441	26	368,182	381,649
Special events and related costs	100,588	-	162,470	263,058
Public relations and advertising	59,027	7,170	6,940	73,137
Postage	18,062	3,376	191,590	213,028
Telephone	68,268	9,366	3,803	81,437
Office supplies and expenses	72,538	9,008	11,829	93,375
Employee expenses	74,092	7,626	12,353	94,071
Professional fees	99,026	56,931	100,893	256,850
Heat, light, and water	251,722	1,881	1,665	255,268
Insurance	54,683	1,028	1,779	57,490
Rental expense	103,995	43,637	34,386	182,018
Repairs and maintenance - Building	200,500	11,920	6,822	219,242
Vehicle expenses	120,549	15,805	6,828	143,182
Cost of sales	1,778	-	-	1,778
Investment and banking fees	65,628	47,014	77,938	190,580
Meeting expenses	11,693	17,101	3,317	32,111
Software maintenance fees	8,268	2,282	15,117	25,667
Support of collaborative efforts	10,000	-	-	10,000
Interest expense	150,017	-	-	150,017
Change in fair value of interest rate swap (Note 5)	(113,140)	-	-	(113,140)
Depreciation	395,393	575	6,372	402,340
Other expenses	38,483	12,011	4,826	55,320
Total expenses before direct benefit to donor costs	9,202,028	457,650	1,406,065	11,065,743
Direct benefit to donor costs	-	-	-	55,624
Total expenses including direct benefit to donor costs	**$ 9,202,028**	**$ 457,650**	**$ 1,406,065**	**$ 11,121,367**

Statement of Cash Flows
Nine Months Ended September 30, 2011

Cash Flows from Operating Activities	
Decrease in net assets	$ (548,585)
Adjustments to reconcile decrease in net assets to net cash from operating activities:	
Depreciation	402,340
Donated transportation equipment	1,894
Gain on disposal of property and equipment	(8,475)
Amortization discount on pledges receivable	(143)
Bad debt expense	35,718
Net realized and unrealized losses on investments	573,514
Donated investments	(1,100)
Change in value of interest rate swap	(113,140)
Change in value of interest in trusts	(54,000)
Contributions restricted for construction of facilities	(34,885)
Contributions restricted for future operations - Bequests receivable	(1,276,932)
Changes in operating assets and liabilities which (used) provided cash:	
Operational accounts receivable	(8,167)
Other accounts receivable	24,231
Legacies and bequests receivable	386,000
Inventory	(127,570)
Prepaid expenses and other	6,095
Interest in trusts	315,000
Accounts payable	29,295
Accrued salaries, wages, and employee benefits payable	197,403
Net cash used in operating activities	(201,507)
Cash Flows from Investing Activities	
Purchase of property and equipment	(436,492)
Proceeds from disposition of property and equipment	8,475
Purchases of investments	(4,775,706)
Proceeds from sales and maturities of investments	4,501,019
Net cash used in investing activities	(702,704)
Cash Flows from Financing Activities	
Payments on debt	(182,142)
Proceeds from capital campaign contributions	3,311
Proceeds from contributions restricted for construction of facilities	17,604
Net cash used in financing activities	(161,227)
Net Decrease in Cash and Cash Equivalents	(1,065,438)
Cash and Cash Equivalents - Beginning of period	2,844,178
Cash and Cash Equivalents - End of period	**$ 1,778,740**
Supplemental Disclosure of Cash Flow Information - Cash paid for interest	**$ 150,290**

See Notes to Financial Statements.

Note 1 - Nature of Organization and Significant Accounting Policies

Nature of Organization - The 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.

Effective January 1, 2011, the Organization changed its fiscal year end from December 31 to September 30. Therefore, the accompanying statement of activities and changes in net assets, statement of functional expenses, and statement of cash flows present the activities, changes in net assets, expenses, and cash flows for the nine-month period ended September 30, 2011.

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, and legacies and bequests 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 at September 30, 2011.

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 percent of the pledges receivable balance at period end. The unamortized discount on capital campaign pledges receivable was $143 as of September 30, 2011. All capital campaign pledges receivable are considered fully collectible at September 30, 2011 and are expected to be collected within one year.

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, 2011.

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

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. 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.

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.

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

The Organization receives donations of various goods and services. For the nine-month period ended September 30, 2011, in-kind donations of $86,333 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. Significant additional in-kind donations have not been reflected in the statement of activities and changes in net assets since they either do not meet the criteria for recording in accordance with generally accepted accounting principles or an appropriate fair market value was not readily determinable.

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 restricted net assets 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 to repay future debt obligations related to the Berman Center for Animal Care construction and to serve as a reserve fund. Investment income of the fund is used to fund annual operations. The principal of the fund may be used to fund operations with board approval. These designations are based on board actions, which can be altered or revoked at a future time by the board. As of September 30, 2011, the board had designated net assets of $7,265,677.

Permanently Restricted Net Assets - Permanently restricted net assets are restricted to investment in perpetuity. The income earned by these assets is available to support the general charitable purpose of the Organization and was recorded using unrestricted gains.

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

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.

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.

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

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, 2011, 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 2008.

Subsequent Events - The financial statements and related disclosures include evaluation of events up through and including January 19, 2012, which is the date the financial statements were available to be issued.

Note 2 - Adoption Center and Charitable Veterinary Hospital Revenue

Adoption center and charitable veterinary hospital revenue for the nine months ended September 30, 2011 is reported net of discounts as follows:

Adoption center and charitable veterinary hospital revenue - Gross	$ 5,790,334
Clinic discounts and other	(1,109,283)
Net revenue	$ 4,681,051

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 - Investments

Investments consisted of the following at September 30, 2011:

Money market funds	$ 1,775,631
U.S. agency notes	224,993
Convertible debt securities	831,031
Corporate debt securities	6,071,119
Common stock	4,249,453
Mutual funds	25,908
Preferred stock	318,404
Total	$ 13,496,539

Interest and dividend income totaled $387,340 in 2011. Net realized and unrealized losses on investments totaled $573,514 in 2011.

Note 4 - Property and Equipment

The cost of property and equipment is summarized as follows:

Land	$ 848,268
Land improvements	465,068
Buildings	7,066,643
Building improvements	2,075,414
Medical and other equipment	3,588,906
Transportation equipment	689,221
Furniture and fixtures	425,998
Computer equipment and software	226,509
Leasehold improvements	35,859
Construction in progress	88,662
Total cost	15,510,548
Accumulated depreciation	(7,532,205)
Net carrying amount	$ 7,978,343

Depreciation expense totaled $402,340 in 2011.

Note 5 - Note Payable

During 2005, the Organization entered into a loan of $4,160,000 that matures on December 1, 2011. The loan is payable in monthly installments of $37,159, including principal and interest. The loan is collateralized by certain assets of the Organization.

Note 5 - Note Payable (Continued)

During 2004, the Organization entered into an interest rate swap agreement that became effective in 2005 and essentially fixed the interest rate at 6.9 percent. The variable rate under the swap is based on the one-month LIBOR plus 1.40 percent. The effective variable rate was 1.62 percent as of September 30, 2011. The interest rate swap is recognized in the accompanying balance sheet at fair value. Changes in the fair value of the interest rate swap are reported on the statements of activities and changes in net assets and functional expenses. The Organization recognized a gain of $113,140 for the nine months ended September 30, 2011 related to the change in value of the swap agreement. The Organization has recorded an interest rate swap liability of $62,074 based on a total notional amount of $2,840,827 as of September 30, 2011.

Subsequent to period end, the note payable was repaid in full and the related swap agreement was terminated by the Organization.

Note 6 - Temporarily Restricted Net Assets

Temporarily restricted net assets at September 30, 2011 are restricted for the following:

Time-restricted contributions	$ 2,482,932
Life insurance policy cash surrender value	52,422
Construction of new facilities	961,344
Program activity	135,986
Total temporarily restricted net assets	$ 3,632,684

Note 7 - Operating Leases

The Organization has operating lease agreements for office space and equipment. Total rent expense under these leases was $166,232 for the nine months ended September 30, 2011. Future commitments under these operating leases are as follows:

2012	$ 241,074
2013	100,309
2014	23,261
2015	3,443
Total	$ 368,087

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 $68,074 to the Plan for the nine months ended September 30, 2011.

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 $156,358 for the nine months ended September 30, 2011. These costs are not specifically attributable to fundraising or education activities and were allocated as follows:

Fundraising	$	70,969
Education		85,389
Total	$	156,358

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 table presents information about the Organization's assets and liabilities measured at fair value on a recurring basis at September 30, 2011 and the valuation techniques used by the Organization to determine those fair values.

In general, fair values determined by Level 1 inputs use quoted prices in active markets for identical assets or liabilities 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 and liabilities 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 where 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 or liability.

Note 10 - Fair Value Measurements (Continued)

The Organization's policy is to recognize transfers between levels of the fair value hierarchy as of the actual date of the event of change in circumstances that caused the transfer. There were no significant transfers between levels of the fair value hierarchy during 2011.

Assets and Liabilities Measured at Fair Value on a Recurring Basis at September 30, 2011

	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, 2011
Assets				
Cash equivalents -				
Sweep account	$ 649,843	$ -	$ -	$ 649,843
Investments:				
Money market funds	1,775,631	-	-	1,775,631
U.S. agency notes	-	224,993	-	224,993
Mutual funds	25,908	-	-	25,908
Common stock:				
Basic materials	832,961	-	-	832,961
Communications	359,115	-	-	359,115
Consumer cyclical	248,370	-	-	248,370
Consumer non-cyclical	150,010	-	-	150,010
Energy	365,237	-	-	365,237
Financial	141,141	-	-	141,141
Health care	137,159	-	-	137,159
Industrial	492,264	-	-	492,264
Services	350,184	-	-	350,184
Technology	555,916	-	-	555,916
Utilities	617,096	-	-	617,096
Preferred stock	-	318,404	-	318,404
Corporate debt:				
Aa credit rating	-	74,135	-	74,135
A credit rating	-	944,374	-	944,374
Baa credit rating	-	2,566,379	-	2,566,379
Ba credit rating	-	1,344,783	-	1,344,783
B credit rating	-	821,236	-	821,236
Not rated	-	320,212	-	320,212
Convertible debt:				
Baa credit rating	-	125,156	-	125,156
Not rated	-	705,875	-	705,875
Total investments	6,050,992	7,445,547	-	13,496,539
Interest in trusts	-	-	1,096,000	1,096,000
Total assets	$ 6,700,835	$ 7,445,547	$ 1,096,000	$ 15,242,382
Liabilities - Interest rate swap	$ -	$ 62,074	$ -	$ 62,074

Note 10 - Fair Value Measurements (Continued)

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.

The fair value of the interest rate swap agreement is based on the present value of the expected future cash flows from the agreement. Inputs to the valuation include LIBOR forward interest rate curves and a discount rate commensurate with current market rates and other risks.

Changes in Level 3 assets measured at fair value on a recurring basis for the nine-month period ended September 30, 2011 were as follows:

	Interest in Trusts
Balance at December 31, 2010	$ 1,357,000
Change in beneficial interest in trusts recognized in income	54,000
Distributions	(315,000)
Balance at September 30, 2011	$ 1,096,000

Interest in trusts categorized as Level 3 assets consists of charitable remainder trusts and other trusts in which the Organization is the remainder beneficiary. The Organization estimates the fair value of these interests based on the present value of expected future cash flows using management's best estimate of key assumptions, including the market value of the assets held in the trusts, the expected payments to the income beneficiaries, and a discount rate commensurate with the current market and other risks involved. The discount rate used to measure the present value of future cash flows for these trusts was 3 percent at September 30, 2011.

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