

**SANTA BARBARA HUMANE SOCIETY
FOR THE PREVENTION OF
CRUELTY TO ANIMALS
FINANCIAL STATEMENTS
DECEMBER 31, 2018**

SANTA BARBARA HUMANE SOCIETY FOR THE PREVENTION OF CRUELTY TO ANIMALS

December 31, 2018

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CERTIFIED PUBLIC ACCOUNTANTS AND CONSULTANTS

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INDEPENDENT AUDITOR'S REPORT

Board of Directors

Santa Barbara Humane Society for the Prevention of Cruelty to Animals

Santa Barbara, California

We have audited the accompanying financial statements of the Santa Barbara Humane Society for the Prevention of Cruelty to Animals (a nonprofit organization), which comprise the statement of financial position as of December 31, 2018, and the related statements of activities and changes in net assets, functional expenses, and cash flows for the year 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 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 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 Santa Barbara Humane Society for the Prevention of Cruelty to Animals as of December 31, 2018, and the change in its net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Report on Summarized Comparative Information

We have previously audited the Santa Barbara Humane Society for the Prevention of Cruelty to Animals 2017 financial statements, and we expressed an unmodified audit opinion on those statements in our report dated July 10, 2018. In our opinion, the summarized comparative information presented herein as of and for the year ended December 31, 2017 is consistent, in all material respects, with the audited financial statements from which it has been derived.

McGowan Guntermann

Santa Barbara, California

October 14, 2019

SANTA BARBARA HUMANE SOCIETY FOR THE PREVENTION OF CRUELTY TO ANIMALS

STATEMENT OF FINANCIAL POSITION
December 31, 2018
(With Comparative Totals As Of December 31, 2017)

	ASSETS			(Memo)
	<u>Without Donor Restrictions</u>	<u>With Donor Restrictions</u>	<u>2018 Total</u>	<u>2017 Total</u>
Current Assets				
Cash and cash equivalents	\$ 2,130,759	\$ -	\$ 2,130,759	\$ 193,212
Accounts receivable	7,964	-	7,964	815
Investment income receivable	-	30,077	30,077	43,496
Pledges and bequests receivable, current portion	-	3,390,396	3,390,396	1,061,091
Prepaid expenses	60,169	-	60,169	42,640
Total Current Assets	<u>2,198,892</u>	<u>3,420,473</u>	<u>5,619,365</u>	<u>1,341,254</u>
Other Assets				
Investments	11,103,073	18,711,272	29,814,345	29,540,541
Perpetual interest trust	-	204,995	204,995	234,483
Pledges and bequests receivable, net of current portion	-	48,125	48,125	58,625
Other assets	419,010	-	419,010	386,127
Property and equipment, net	1,212,378	-	1,212,378	1,237,007
Total Other Assets	<u>12,734,461</u>	<u>18,964,392</u>	<u>31,698,853</u>	<u>31,456,783</u>
Total Assets	<u>\$ 14,933,353</u>	<u>\$ 22,384,865</u>	<u>\$ 37,318,218</u>	<u>\$ 32,798,037</u>
LIABILITIES AND NET ASSETS				
Current Liabilities				
Accounts payable	\$ 109,396	\$ -	\$ 109,396	\$ 87,653
Accrued expenses	146,179	-	146,179	103,144
Total Current Liabilities	<u>255,575</u>	<u>-</u>	<u>255,575</u>	<u>190,797</u>
Net Assets				
Without donor restrictions	14,677,778	-	14,677,778	11,497,821
With donor restrictions	-	22,384,865	22,384,865	21,109,419
Total Net Assets	<u>14,677,778</u>	<u>22,384,865</u>	<u>37,062,643</u>	<u>32,607,240</u>
Total Liabilities and Net Assets	<u>\$ 14,933,353</u>	<u>\$ 22,384,865</u>	<u>\$ 37,318,218</u>	<u>\$ 32,798,037</u>

The accompanying notes are an integral part of these financial statements.

SANTA BARBARA HUMANE SOCIETY FOR THE PREVENTION OF CRUELTY TO ANIMALS

STATEMENT OF ACTIVITIES AND CHANGES IN NET ASSETS

For the Year Ended December 31, 2018

(With Comparative Totals For the Year Ended December 31, 2017)

	Without Dono Restrictions	With Donor Restrictions	2018 Total	(Memo) 2017 Total
Support, Revenue, and Other Income				
Support				
Contributions, bequests, and grants	\$ 495,779	\$ 7,123,966	\$ 7,619,745	\$ 654,502
Membership	59,019	-	59,019	72,570
Other support	16,449	-	16,449	10,571
Total Support	<u>571,247</u>	<u>7,123,966</u>	<u>7,695,213</u>	<u>737,643</u>
Revenue				
Veterinary clinic	237,188	-	237,188	239,044
Boarding fees	123,422	-	123,422	135,874
Crematory	89,665	-	89,665	96,356
Other service revenue	61,595	-	61,595	37,983
Total Revenue	<u>511,870</u>	<u>-</u>	<u>511,870</u>	<u>509,257</u>
Other Income				
Royalty income	51,771	-	51,771	50,393
Change in value of perpetual interest trust	-	(29,488)	(29,488)	13,591
Interest and dividends	295,376	598,393	893,769	835,845
Gain on sale of assets	-	-	-	-
Realized gain (loss) on investments	(32,108)	(25,133)	(57,241)	630,282
Unrealized gain (loss) on investments	(684,006)	(1,370,806)	(2,054,812)	1,789,520
Unrealized gain (loss) on other assets	32,883	-	32,883	97,627
Net assets released from restrictions	5,021,486	(5,021,486)	-	-
Total Other Income	<u>4,685,402</u>	<u>(5,848,520)</u>	<u>(1,163,118)</u>	<u>3,417,258</u>
Total Support, Revenue, and Other Income	<u>5,768,519</u>	<u>1,275,446</u>	<u>7,043,965</u>	<u>4,664,158</u>
Expenses				
Program Services				
Shelter and kennel	1,054,558	-	1,054,558	996,894
Veterinary clinic	634,263	-	634,263	544,570
Education	110,764	-	110,764	152,319
Crematory	41,722	-	41,722	42,803
Total Program Services	<u>1,841,307</u>	<u>-</u>	<u>1,841,307</u>	<u>1,736,586</u>
Supporting Services				
General	525,253	-	525,253	299,625
Fundraising	222,002	-	222,002	99,156
Total Supporting Services	<u>747,255</u>	<u>-</u>	<u>747,255</u>	<u>398,781</u>
Total Expenses	<u>2,588,562</u>	<u>-</u>	<u>2,588,562</u>	<u>2,135,367</u>
Changes in Net Assets	3,179,957	1,275,446	4,455,403	2,528,791
Net Assets, Beginning of the Year	<u>11,497,821</u>	<u>21,109,419</u>	<u>32,607,240</u>	<u>30,078,449</u>
Net Assets, End of the Year	<u>\$ 14,677,778</u>	<u>\$ 22,384,865</u>	<u>\$ 37,062,643</u>	<u>\$ 32,607,240</u>

The accompanying notes are an integral part of these financial statements.

SANTA BARBARA HUMANE SOCIETY FOR THE PREVENTION OF CRUELTY TO ANIMALS

STATEMENT OF FUNCTIONAL EXPENSES

For the Year Ended December 31, 2018

(With Comparative Totals For the Year Ended December 31, 2017)

Expenses	Program Services					Supporting Services			2018	(Memo) 2017
	Shelter	Clinic	Education	Crematory	Total Program	Management	Fundraising	Total Supporting	Total	Total
Salaries	\$ 627,383	\$ 229,234	\$ 61,355	\$ -	\$ 917,972	\$ 241,420	\$ 99,376	\$ 340,796	\$ 1,258,768	\$ 1,088,111
Benefits	129,603	50,017	9,542	-	189,162	62,848	17,956	80,804	269,966	268,078
Payroll taxes	47,887	17,511	5,440	-	70,838	24,728	6,184	30,912	101,750	95,461
Clinical professional	19,964	78,443	6,564	-	104,971	-	-	-	104,971	60,576
Supplies	56,261	12,681	1,620	14,639	85,201	21,160	2,588	23,748	108,949	71,122
Legal and professional	19,355	14,800	1,669	3,339	39,163	127,463	27,511	154,974	194,137	74,419
Medications	-	121,155	-	-	121,155	-	-	-	121,155	82,252
Utilities	39,628	11,298	7,511	10,443	68,880	8,107	1,250	9,357	78,237	75,123
Depreciation	19,935	23,258	9,968	6,645	59,806	6,645	-	6,645	66,451	65,171
Insurance	11,878	13,858	1,980	3,959	31,675	3,960	3,959	7,919	39,594	36,709
Animal food	31,685	944	-	-	32,629	-	-	-	32,629	20,363
Auto, travel, and meetings	16,739	1,229	3,733	-	21,701	10,002	106	10,108	31,809	20,804
Repairs and maintenance	19,106	2,822	-	96	22,024	11,555	-	11,555	33,579	77,612
Printing and postage	1,189	153	-	-	1,342	2,912	20,043	22,955	24,297	27,312
Outside spay and neuter	-	32,000	-	-	32,000	-	-	-	32,000	32,600
Items purchased for resale	3,948	14,220	-	-	18,168	-	-	-	18,168	6,340
Bank fees	4,260	4,584	706	1,413	10,963	1,413	1,413	2,826	13,789	11,189
Direct program	-	-	-	-	-	-	-	-	-	4,903
Advertising	-	-	-	-	-	-	38,700	38,700	38,700	1,010
Property and other taxes	2,272	2,651	379	1,188	6,490	905	758	1,663	8,153	8,527
Dues and perscriptions	-	2,294	-	-	2,294	965	966	1,931	4,225	3,360
Uniform and laundry	3,465	1,111	297	-	4,873	1,170	481	1,651	6,524	1,663
Membership	-	-	-	-	-	-	711	711	711	2,662
2018 Total Expenses	\$ 1,054,558	\$ 634,263	\$ 110,764	\$ 41,722	\$ 1,841,307	\$ 525,253	\$ 222,002	\$ 747,255	\$ 2,588,562	
2017 Total Expenses (Memo)	\$ 996,894	\$ 544,570	\$ 152,319	\$ 42,803	\$ 1,736,586	\$ 299,625	\$ 99,156	\$ 398,781		\$ 2,135,367

The accompanying notes are an integral part of these financial statements.

SANTA BARBARA HUMANE SOCIETY FOR THE PREVENTION OF CRUELTY TO ANIMALS

STATEMENT OF CASH FLOWS

For the Year Ended December 31, 2018

(With Comparative Totals For the Year Ended December 31, 2017)

	2018	(Memo) 2017
Cash Flow from Operating Activities		
Change in net assets	\$ 4,455,403	\$ 2,528,791
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation	66,451	65,171
Unrealized (gain) loss on investments	2,054,812	(1,789,520)
Realized (gain) loss on investments	57,241	(630,282)
Decrease in accounts, pledges, and bequests receivable	(2,325,955)	8,191
Decrease in investment income receivable	13,419	3,067
Decrease (increase) in prepaid expenses	(17,529)	(20,988)
(Decrease) increase in value of perpetual interest trust	29,488	(13,591)
Increase in value of other assets	(32,883)	(97,627)
Increase (decrease) in accounts payable and accrued expenses	64,778	(15,564)
Net Cash Provided by Operating Activities	<u>4,365,225</u>	<u>37,648</u>
Cash Flow from Investing Activities		
Purchase of property and equipment	(41,822)	(43,787)
Proceeds from sale of securities	1,897,914	4,981,796
Purchase of securities	(4,283,770)	(4,943,601)
Net Cash Used by Investing Activities	<u>(2,427,678)</u>	<u>(5,592)</u>
Increase in Cash and Cash Equivalents	1,937,547	32,056
Cash at Beginning of the Year	<u>193,212</u>	<u>161,156</u>
Cash at End of the Year	<u>\$ 2,130,759</u>	<u>\$ 193,212</u>

The accompanying notes are an integral part of these financial statements.

SANTA BARBARA HUMANE SOCIETY FOR THE PREVENTION OF CRUELTY TO ANIMALS

NOTES TO FINANCIAL STATEMENTS

Note 1 - ORGANIZATION AND ACTIVITIES

Organization

The Santa Barbara Humane Society for the Prevention of Cruelty to Animals (the Society), a California nonprofit corporation, was founded in 1887 and is dedicated to the welfare of all animals in Santa Barbara, California and the surrounding area. Its services include shelter care of animals, adoption services, spay and neuter clinical services, euthanasia services, investigation services and education. Based on total expenses, the shelter and kennel activity constitutes the major activity of the Society. These activities are funded primarily by public support and investment income.

Note 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Accounting

The financial statements of the Organization have been prepared on the accrual basis of accounting following accounting principles generally accepted in the United States of America (GAAP). The significant accounting policies are described below to enhance the usefulness of the financial statements to the reader.

New Accounting Pronouncements

The December 31, 2018 financial statements reflect adoption of Financial Accounting Standards Board (FASB) Accounting Standards Update (ASU) No. 2014-15, Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern. ASU 2014-15 defines management's responsibility to evaluate whether there is a substantial doubt about an organization's ability to continue as a going concern and to provide related footnote disclosures. The Organization adopted this ASU and concluded there was not substantial doubt of its continued operations.

During 2018, the Organization adopted Financial Accounting Standards Board (FASB) Accounting Standards Update (ASU) No. 2016-14, Not-for-Profit Entities (Topic 958): Presentation of Financial Statements for Not-for-Profit Entities. This guidance is intended to improve the net asset classification requirements and the information presented in the financial statements and notes about a not-for-profit entity's liquidity, financial performance, and cash flows. Main provisions of this guidance include: presentation of two classes of net assets versus the previously required three; recognition of capital gifts for construction as a net asset without donor restrictions when the associated long-lived asset is placed in service; recognition of underwater endowment funds as a reduction in net assets with donor restrictions; and reporting investment income net of external and direct internal investment expenses. The guidance also enhances disclosures for board designated amounts, compositions of net assets with donor restrictions and how the restrictions affect the use of resources, qualitative and quantitative information about the liquidity and availability of financial assets to meet general expenditures within one year of the balance sheet (statement of financial position) date, and expenses by both their natural and functional classification, including methods used to allocate costs among program and support functions and underwater endowments.

SANTA BARBARA HUMANE SOCIETY FOR THE PREVENTION OF CRUELTY TO ANIMALS

NOTES TO FINANCIAL STATEMENTS

Note 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

New Accounting Pronouncements (continued)

Due to the adoption of ASU 2016-14 as of December 31, 2018, net assets have been reclassified as of December 31, 2017 as follows:

Net Asset Classification 12/31/17	ASU 2016-14 Classifications		Total Net Assets
	Without Donor Restrictions	With Donor Restrictions	
Unrestricted	\$ 11,497,821	\$ -	\$ 11,497,821
Temporarily Restricted	-	8,302,936	8,302,936
Permanently Restricted	-	<u>12,806,483</u>	<u>12,806,483</u>
Net Assets as previously presented	11,497,821	21,109,419	32,607,240
Net assets as reported after adoption of ASU 2016-14	<u>\$ 11,497,821</u>	<u>\$ 21,109,419</u>	<u>\$ 32,607,240</u>

Description of Net Assets

The Organization reports information regarding its financial position and activities in two classes of net assets - with donor restrictions and without donor restrictions - based on the existence or absence of donor-imposed restrictions.

Without Donor Restrictions

Net assets without donor restrictions represent net assets that are not subject to donor-imposed time or use restrictions. Net assets without donor restrictions include board designated funds.

With Donor Restrictions

Net assets with donor restrictions represent net assets that are subject to donor-imposed time or use restrictions. Net assets with donor restrictions generally include contributions and bequests receivable and planned gifts. Earnings on net assets with donor restrictions are reported as an increase in net assets with donor restrictions. Earnings on donor restricted endowment funds that have not yet been appropriated are also classified as net assets with donor restrictions. When a restriction expires, net assets with donor restrictions are reclassified to net assets without donor restrictions and reported in the Statement of Activities as “Net assets released from restrictions.” Net assets with donor restrictions include perpetual income trusts for which the related income is reported as contributions without donor restrictions when received on the Statement of Activities. The change in value of the underlying assets is recorded as an unrealized gain or loss in net assets with donor restrictions on the Statement of Activities. Net assets with donor restrictions also consist of those donor-restricted endowments held by the Organization as defined under the Uniform Prudent Management of Institutional Funds Act (UPMIFA).

SANTA BARBARA HUMANE SOCIETY FOR THE PREVENTION OF CRUELTY TO ANIMALS

NOTES TO FINANCIAL STATEMENTS

Note 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Cash and Cash Equivalents

The Society classifies unrestricted short-term, highly liquid investments having original maturities of three months or less as cash equivalents.

Investments

Investments in marketable securities with readily determinable fair values and all investments in marketable debt securities are valued at their fair values in the statement of financial position. Unrealized gains and losses are included in the change in net assets. Donated securities are recorded at their estimated value at date of receipt.

Property and Equipment

Property and equipment in excess of \$1,000 are capitalized at cost. The Society's investment in equipment and leasehold improvements is stated at cost, or fair market value if donated. Depreciation is calculated using the straight-line method over an estimated useful life of three to forty years.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Significant estimates used in the preparation of these financial statements include: allocation of certain expenses by function, fair market value of other assets, and depreciable lives of property and equipment.

Contributions and Bequests

Contributions received are recorded at their fair value on the date of donation. Contributions receivable are recognized as revenue when committed and as assets, decreases of liabilities, or expenses depending on the form of the benefits received. Conditional promises to give are recognized when the conditions on which they depend are substantially met.

The Society accrues bequests when all the events required for the transfer of the assets from the estate of the donor to the Society have occurred and/or the court has issued an order to transfer the assets.

Donated Services

Some individuals and organizations have donated time to the Society, to further its programs and objectives. Volunteers contributed approximately 4,487 hours to the Society in 2018. As this volunteer service does not meet the recognition requirements of generally accepted accounting principles, no amount has been recorded in these financial statements for these services.

SANTA BARBARA HUMANE SOCIETY FOR THE PREVENTION OF CRUELTY TO ANIMALS

NOTES TO FINANCIAL STATEMENTS

Note 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Functional Expenses

The Society allocates its expenses on a functional basis among its various projects and support services. Expenses that can be identified with a specific project and support service are allocated directly according to their expenditure classification. Other expenses that are common to several functions are allocated by various statistical bases.

Income Taxes

The Society is a California nonprofit public benefit corporation, which is exempt from income taxes under Internal Revenue Code Section number 501(c)(3) and State of California Revenue and Taxation Code Section 23701(d). The Society is not currently involved in any activity that is subject to unrelated business income tax; therefore, no provision for income taxes is required. The Society qualifies for the charitable contribution deduction under Section 170(b)(1)(A) and has been classified as an organization that is not a private foundation under Section 509(a)(1).

The Society evaluates uncertain tax positions, whereby the effect of the uncertainty would be recorded if the outcome was considered probable and reasonably estimable. As of December 31, 2018, the Society had no uncertain tax positions requiring accrual. The Society files tax returns in U.S. federal and California jurisdictions. The Society is no longer subject to U.S. federal and state tax examinations by tax authorities for the years ending before 2015 and 2014, respectively.

Subsequent Events

The Society has evaluated subsequent events through October 14, 2019, the date which the financial statements were available to be issued.

Note 3 - PLEDGES AND BEQUESTS RECEIVABLE

Pledges and bequests receivable are included in the financial statements as temporarily restricted net assets. The Society is also income beneficiary of a charitable lead annuity trust, and residual beneficiary of a charitable remainder trust, which are included in the amounts reported as pledges and bequests receivable. A discount factor of 2% is applied to amounts receivable in more than one year. These amounts are considered fully collectible and therefore no allowance for uncollectible receivables has been recorded. At December 31, 2018, contributions and bequests receivable are expected to be realized in the following periods:

In one year or less	\$ 3,390,396
In more than one year	<u>48,125</u>
Pledges and bequests receivable, net	<u>\$ 3,438,521</u>

SANTA BARBARA HUMANE SOCIETY FOR THE PREVENTION OF CRUELTY TO ANIMALS

NOTES TO FINANCIAL STATEMENTS

Note 4 - PROPERTY AND EQUIPMENT

Property and equipment consists of the following as of December 31, 2018:

Land	\$ 117,917
Land improvements	306,501
Buildings and improvements	2,541,657
Furniture and office equipment	230,985
Shelter equipment	224,221
Vehicles	<u>175,056</u>
Total Property and Equipment	3,596,337
Less: Accumulated depreciation	<u>(2,383,959)</u>
Property and equipment, net	<u>\$ 1,212,378</u>

Note 5 - INVESTMENTS

Investments are presented in the financial statements at fair market value. Fair value is defined as the amount that would be exchanged for an asset or to transfer a liability between market participants in an orderly transaction at the balance sheet date. Realized and unrealized gains and losses on investments are reflected in the Statement of Activities. At December 31, 2018, investments consisted of the following:

	<u>Cost Basis</u>	<u>Market Value</u>	<u>Unrealized Gains</u>
Money market funds	\$ 1,712,041	\$ 1,712,041	\$ -
Equities and index funds	13,721,112	14,443,078	721,966
Bonds and fixed income	<u>13,604,148</u>	<u>13,659,226</u>	<u>55,078</u>
Total	<u>\$ 29,037,301</u>	<u>\$ 29,814,345</u>	<u>\$ 777,044</u>

The following summarizes the net change in unrealized gain on investments:

	<u>Cost Basis</u>	<u>Market Value</u>	<u>Unrealized Gains</u>
Balance at end of the year	\$ 29,037,301	\$ 29,814,345	\$ 777,044
Balance at beginning of the year	\$ 26,708,685	\$ 29,540,541	2,831,856
Unrealized loss			<u>\$ (2,054,812)</u>

The following summarizes the investment return included in the statement of activities for the year ended December 31, 2018:

Interest and dividend income	\$ 893,769
Realized loss on value of securities	(57,241)
Unrealized loss on value of securities	<u>(2,054,812)</u>
Total Investment Return	<u>\$ (1,218,284)</u>

SANTA BARBARA HUMANE SOCIETY FOR THE PREVENTION OF CRUELTY TO ANIMALS

NOTES TO FINANCIAL STATEMENTS

Note 6 - INTEREST IN TRUSTS

Perpetual Income Trust Interest

The Society is named as an income beneficiary of a perpetual trust, the corpus of which is not controlled by the Society. Under these arrangements, the Society has the irrevocable right to receive income earned on the underlying assets held in perpetuity. Income received from the trust is for support of general operations. Since the Society is a beneficiary of this stream of income in perpetuity, the Society's share of the fair market value of the trusts' investments is recorded as an asset, with a fair market value of \$204,995 at December 31, 2018. Any change in subsequent fair market value of the Society's share of the investments is recorded in the Statement of Activities as a change in value of perpetual interest in trust. For the year ended December 31, 2018, the Society received \$9,503 in distributions from the trust.

Discretionary Income Trust Interest

The Society is named as an income beneficiary of a discretionary trust, the corpus of which is not controlled by the Society. Under these arrangements, the Society has the right to receive income earned on the underlying assets, subject to the discretion of the trustee. Income received from the trust is for support of general operations. Because the trustee retains discretion over distributions of income, the assets are not recorded on the Society's financial statements. For the year ended December 31, 2018, the Society received \$7,150 in distributions from the trust.

Community Foundation Endowment Trust Interest

The Society is the beneficiary of four endowments held by Santa Barbara Foundation. Because the Santa Barbara Foundation has been granted variance power, the endowment assets are not recorded on the Society's financial statements. The income from these endowments is used to support general operations. The Society is entitled to the income produced by the endowment in accordance with the Santa Barbara Foundation's spending policy, but has no control or access to the principal. For the year ended December 31, 2018, the Society received \$72,448 in distributions from these endowment trusts.

Note 7 - OTHER ASSETS

Other assets of the Society totaling \$419,010 for the year ended December 31, 2018, includes oil and gas rights and undeveloped land.

Oil and gas rights are a 50% undivided interest in 130 properties located in Oklahoma, Missouri and Louisiana with an estimated fair value of \$376,000 as of December 31, 2018.

Undeveloped land consists of a 1/8th interest in land in Fresno, California with an estimated fair value of \$3,500, and undeveloped land located in Hornbrook, California with an estimate fair value of \$40,000 as of December 31, 2018.

NOTES TO FINANCIAL STATEMENTS

Note 8 - FAIR VALUE MEASUREMENT

Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 820, Fair Value Measurement and Disclosures, provides the framework for measuring and disclosing the fair value of assets and liabilities. Accounting principles define fair value as the price that would be received by the Society to sell an asset or be paid by the Society to transfer a liability (an exit price) in an orderly transaction between market participants on the measurement date. A fair value hierarchy has been established that prioritizes valuation inputs into three broad levels to ensure consistency and comparability. The valuation hierarchy gives the highest priority to quoted prices in active markets (Level 1) and the lowest priority to unobservable inputs (Level 3) described as follows:

The standard describes three levels of inputs that may be used to measure fair value:

Level 1: Quoted prices in active markets for identical assets or liabilities

Level 2: Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in active markets that are not active; discounted cash flows; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities

Level 3: Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities; including estimates by management and information valuation methods

The following is a description of the valuation methodologies used for instruments measured at fair value on a recurring basis and recognized in the accompanying Statement of Financial Position, as well as the general classification of such instruments pursuant to the valuation hierarchy.

Where quoted market prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. If quoted market prices are not available, then Level 2 fair values are estimated by using pricing models quoted prices of securities with similar characteristics or discounted cash flows. The asset's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement.

Fair market valuation of Level 3 securities is based on estimates of management, information valuation methods used within a particular industry, or other market factors to determine if the carrying value of these investments should be adjusted. Because of the inherent uncertainty of valuations, however, the estimated values may differ from the values that would have been used had a ready market existed, and the differences could be material.

SANTA BARBARA HUMANE SOCIETY FOR THE PREVENTION OF CRUELTY TO ANIMALS

NOTES TO FINANCIAL STATEMENTS

Note 8 - FAIR VALUE MEASUREMENT (continued)

The following table presents assets and liabilities recognized in the accompanying Statement of Financial Position measured at fair value on a recurring basis and the level in which the fair value measurements fall at December 31, 2018:

<u>Description</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Investments				
Money market funds	\$ 1,712,041	\$ -	\$ -	\$ 1,712,041
Equities and index funds	14,443,078	-	-	14,443,078
Bonds and fixed income	<u>13,659,226</u>	<u>-</u>	<u>-</u>	<u>13,659,226</u>
Total Investments	<u>29,814,345</u>	<u>-</u>	<u>-</u>	<u>29,814,345</u>
Perpetual interest trust	204,995	-	-	204,995
Oil and gas rights	-	-	375,510	375,510
Undeveloped land	<u>-</u>	<u>-</u>	<u>43,500</u>	<u>43,500</u>
Total assets measured at fair value	<u>\$ 30,019,340</u>	<u>\$ -</u>	<u>\$ 419,010</u>	<u>\$ 30,438,350</u>

The following is a description of the general classification of investments pursuant to the valuation hierarchy:

Money market funds – include held for investment purposes includes money market funds and cash equivalent assets, and is valued at face value.

Equities and index funds – include a variety of publically traded stocks and exchange traded index funds from various industries. They are valued utilizing quoted market prices available in active markets for identical investments at the reporting date.

Bonds and fixed income –include fixed income mutual funds and corporate bonds to provide a hedge against deflation, provide a stable return, and to minimize the overall volatility. They are valued utilizing quoted market prices available in active markets for identical investments at the reporting date.

The following table provides a reconciliation of assets measured at fair value using significant unobservable inputs (Level 3) during 2018:

<u>Description</u>	<u>Beginning Balance</u>	<u>Net Gain</u>	<u>Purchases</u>	<u>Settlements</u>	<u>Ending Balance</u>
Oil and gas rights	\$ 343,000	\$ 32,510	\$ -	\$ -	\$ 375,510
Undeveloped land	<u>43,500</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>43,500</u>
Total	<u>\$ 386,500</u>	<u>\$ 32,510</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 419,010</u>

SANTA BARBARA HUMANE SOCIETY FOR THE PREVENTION OF CRUELTY TO ANIMALS

NOTES TO FINANCIAL STATEMENTS

Note 9 - CONCENTRATIONS AND RISKS

Concentrations of Pledges and Bequests Receivable

As of December 31, 2018, approximately 40% of the pledges and bequests receivable were due from a single estate.

Credit Risk

The Society maintains cash balances at several banks insured by the Federal Deposit Insurance Corporation (FDIC) up to \$250,000. At times, balances may exceed federally insured limits. At December 31, 2018, uninsured cash and cash equivalent balances totaled approximately \$1,900,000. The Society maintains a majority of cash balances in money market funds. Such balances may not be fully insured.

Market Risk

The Society holds its investments in a diversified portfolio. Nevertheless, these investments are exposed to various risks, such as interest rate, credit and overall market volatility. Due to the level of risk associated with certain investment securities, it is reasonably possible that changes in the values of investment securities will occur in the near term and that such change could materially affect the amounts reported in the consolidated financial statements.

Note 10 - NET ASSETS RELEASED FROM RESTRICTIONS

Net assets were released from donor restrictions by the passage of time or by satisfying the restricted purposes specified by donors. For the year ended December 31, 2018, net assets released from restriction totaled \$5,021,486.

Note 11 - ENDOWMENT FUNDS

Interpretation of Relevant Law

The Board of Directors of the Society has interpreted the California-adopted Uniform Prudent Management of Institutional Funds Act (UPMIFA) as requiring a long-term investment strategy designed to preserve the fair value of the original gift, as of the gift date. As a result of this interpretation, the Society has classified, at the explicit direction of the donor, as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the donor at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment funds that are not classified in permanently restricted net assets are classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Society in a manner consistent with the standard for prudence prescribed by UPMIFA.

NOTES TO FINANCIAL STATEMENTS

Note 11 - ENDOWMENT FUNDS (continued)

Interpretation of Relevant Law (continued)

In accordance with California UPMIFA, the Society considers the following factors in making a determination to appropriate or invest donor restricted endowment funds:

- (1) The duration and preservation of the fund.
- (2) The purposes of the Society and the donor-restricted endowment fund.
- (3) General economic conditions.
- (4) The possible effect of inflation and deflation.
- (5) The expected total return from income and the appreciation of investments.
- (6) Other resources of the Society.
- (7) The investment policies of the Society.

Endowment Investment and Spending Policies

The Society 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 long-term purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the organization must hold in perpetuity for donor-specified periods and purposes. The endowment assets are invested in a manner that is intended to produce results that provide a reasonable balance between the quest for growth and the need to protect principal. The investment policy calls for a diversified portfolio utilizing various asset classes with a goal of reducing portfolio volatility and risk.

The Society's endowment is invested in a diversified portfolio of equities, index funds, and fixed income. The portfolio employs both passive index funds and actively managed funds. The portfolio's objective is to achieve a total return equivalent to or greater than the Society's financial requirements over the long-term time horizon. Long-term investment strategies are used to manage risk with the goal to grow charitable dollars over time.

The Society uses a total investment return methodology for determining its spending policy each year. The portfolio's total returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The Board of Directors calculates the amount of money annually distributed from the Society's various discretionary funds and other endowed funds for general operations. The percentage is based upon the decision of the Board and is reviewed annually in light of changing market assumptions, investment returns and the rate of inflation. For the year ended December 31, 2018, the overall spending policy was approximately 4% of the fair market value of investments, while the spending policy related specifically to permanently restricted endowments was 7%.

Endowment net assets with donor restrictions totaled \$18,018,751, consisting of total original gift endowment contributions of \$12,572,000 and accumulated earnings of \$5,446,751 as of December 31, 2018.

SANTA BARBARA HUMANE SOCIETY FOR THE PREVENTION OF CRUELTY TO ANIMALS

NOTES TO FINANCIAL STATEMENTS

Note 12 - EMPLOYEE BENEFIT PLANS

Pension Plan

The Society maintains a defined contribution pension plan for full-time employees. Upon employment, employees are eligible for participation in the pension plan. No elective employee deferrals are allowed under the Plan. Employees are eligible for employer contributions if they are 21 years of age or greater, have completed one year of employment, and 1,000 hours of work. For eligible employees, the Society makes an annual contribution of 5% of the employees' gross wages. Participants are fully vested after six years. Net contributions to the plan by the Society totaled \$61,817 for the year ended December 31, 2018.

Tax Deferred Annuity

The Society has available to its employees a tax deferred investment plan. All full-time employees are eligible to participate. The Society does not contribute to this plan.

Deferred Compensation

The Society has in place a deferred compensation plan whereby employees can elect to receive salary upon separation from service. At December 31, 2018, there were no active participants in this plan.

Note 13 - LIQUIDITY

Financial assets available to meet cash needs for general expenditure for the following year are comprised of current assets and investments, adjusted for amounts unavailable due to illiquidity, endowments and other funds spending policy appropriations beyond one year, and current liabilities payable to vendors, financial institutions, and nonprofit organizations.

Financial assets available to meet cash needs for general expenditures within one year as of December 31, 2018:

Current assets	
Cash and cash equivalents available within one year	\$2,130,759
Pledges receivable, current portion	3,390,396
Accounts receivable	38,041
Other current assets	<u>60,169</u>
Total current assets	<u>5,619,365</u>
Investments	29,814,345
Less, investments unavailable for general expenditures within one year:	<u>(17,138,711)</u>
Total Investments	<u>12,675,634</u>
Current Liabilities	<u>(255,575)</u>
Financial assets available to meet cash needs for general expenditures within one year as of December 31, 2018	<u>\$12,420,059</u>

SANTA BARBARA HUMANE SOCIETY FOR THE PREVENTION OF CRUELTY TO ANIMALS

NOTES TO FINANCIAL STATEMENTS

Note 14 – NET ASSETS

Net Assets Without Donor Restrictions

As of December 31, 2018, net assets without donor restrictions consist of the following:

Operating net assets	\$ 13,046,390
Property and equipment, net	1,212,378
Other assets	<u>419,010</u>
Total Net Assets Without Donor Restrictions	<u>\$ 14,677,778</u>

Net Assets With Donor Restrictions

As of December 31, 2018, net assets with donor restrictions consist of the following:

Pledges, bequests, and interest receivable	\$ 3,468,598
Donor-restricted endowments	12,572,000
Unappropriated earnings on endowments	5,446,751
Receivables	692,521
Perpetual interest trust	<u>204,995</u>
Total Net Assets With Donor Restrictions	<u>\$ 22,384,865</u>

Note 15 - RECLASSIFICATIONS

Certain amounts from the December 31, 2017 financial statements have been reclassified to conform with the current year's presentation.

Note 16 - SUBSEQUENT EVENTS

Subsequent to the year ended December 31, 2018, the Board designated \$10,000,000 of net assets without restrictions towards the Capital Improvements.