

**Animal Assistance Foundation
Report to the Finance Committee
Regarding the July 31, 2014 Audit**

A. Review of Financial Statements

- The financial statements are presented on the income tax basis of accounting because of the partnership investments which result in timing differences between income received and income reported on the K-1s. For tax purposes, the income is recognized in the year in which the K-1 is received.
- Investments are shown at cost; fair market value is disclosed in note 2 to the financial statements.
- At fair market value, total assets increased from \$27,668,355 at July 31, 2013 to \$29,275,088 at July 31, 2014.
- Net investment income on a cash basis was \$810,690 in 2013 and \$746,291 in 2014. In addition to the cash basis investment income, the Foundation had an additional unrealized gain of \$2,241,669 in 2014.
- The Foundation received contributions of \$54,873 in 2014 from the Dorothy L. Broncucia Living Trust.
- Under the income tax basis of accounting, grants are expensed when paid. There were no future grant commitments outstanding at July 31, 2014.
- Partnership income and expense related to certain investments (Grosvenor & Clarion) are recorded in the financial statements from the information received on the K-1's for the year ended December 31, 2013. Investment income related to GAM and Babson is recognized only upon the receipt of distributions or redemptions. GAM was liquidated in 2014.

B. Internal Control Recommendations – None in the current year. Prior year recommendation regarding receipt and review of all cancelled checks by the Executive Director was fully implemented.

C. Communication with Those Charged with Governance (attached)

D. Tax Return

- Excise tax expense at a rate of 1% was \$7,093. A carry-over of \$683 will be applied to estimated excise tax in 2015. The Foundation should make estimated payments in 2015 totaling \$6,410.
- Legislation has been introduced in Congress to establish a permanent excise tax rate of 1%.
- See attached “Tax Information for Officers”.

**Animal Assistance Foundation
Report to the Finance Committee, Continued**

E. Other Items

- Reminder that audit work on alternative investments is very limited. Existence is verified based on confirmations and the cumulative contributions to the partnerships; we did not audit the market value of these investments (Clarion, Grosvenor, Babson).
- Tax reporting for alternative investments can be complex and failure to file the proper documents can result in severe penalties.

Summary of filing requirements

If you invest in:	Look for:	Possibly file:
Domestic partnership	UBTI, Transfers to Foreign Corporations, Transfers to Foreign Partnerships	Form 990-T, CO 112, Other State Returns, Form 926, Form 8865
Foreign Corporation	Transfers over \$100,000; Ownership of 10% or more	Form 926, Form 5471
Foreign Partnerships	Transfers over \$100,000; Ownership of 10% or more	Form 8865
Foreign bank account or mutual fund	Actively traded accounts, signature authority	FBAR

- Reminder of the provisions of the Pension Protection Act of 2006 regarding payments to Type III supporting organizations. These payments are not qualifying distributions for purposes of the minimum distribution requirement.
- Subsequent events update.

F. Final Details

- Approval of financial statements

G. Executive Session with Auditors

Animal Assistance Foundation

Financial Statements

July 31, 2014 and 2013

(With Independent Auditor's Report Thereon)

Independent Auditor's Report

Board of Directors Animal Assistance Foundation:

We have audited the accompanying financial statements of Animal Assistance Foundation which comprise the statements of assets, liabilities and net assets-income tax basis as of July 31, 2014 and 2013, and the related statements of revenue and support, expenses, and other changes in net assets-income tax basis 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 the basis of accounting Animal Assistance Foundation uses for income tax purposes; this includes determining that the income tax basis of accounting is an acceptable basis for the preparation of the financial statements in the circumstances. Management is also responsible for 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 of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to 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.

**Board of Directors
Animal Assistance Foundation:**

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the assets, liabilities, and net assets of Animal Assistance Foundation as of July 31, 2014 and 2013, and its revenue and support, expenses, and other changes in net assets for the years then ended in accordance with the basis of accounting Animal Assistance Foundation uses for income tax purposes as described in Note 1.

Basis of Accounting

We draw attention to Note 1 to the financial statements, which describes the basis of accounting. The financial statements are prepared on the basis of accounting Animal Assistance Foundation uses for income tax purposes, which is a basis of accounting other than accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to that matter.

November 6, 2014

Animal Assistance Foundation
Statements of Assets, Liabilities and Net Assets - Income Tax Basis
July 31, 2014 and 2013

	<u>2014</u>	<u>2013</u>
Assets:		
Cash and cash equivalents	\$ 19,865	25,494
Prepays and other assets	-	1,314
Investments at cost, fair market value of \$29,253,122 and \$27,639,446 at July 31, 2014 and 2013, respectively (note 2)	21,245,751	21,873,744
Deposit	<u>2,101</u>	<u>2,101</u>
Total assets	<u>\$ 21,267,717</u>	<u>21,902,653</u>
Liabilities and Net Assets:		
Liabilities	\$ 3,393	-
Net assets - unrestricted	<u>21,264,324</u>	<u>21,902,653</u>
Commitments (notes 3 and 4)		
Total liabilities and net assets	<u>\$ 21,267,717</u>	<u>21,902,653</u>

See accompanying notes to financial statements.

Animal Assistance Foundation
Statements of Revenue and Support, Expenses,
And Other Changes in Net Assets - Income Tax Basis
Years ended July 31, 2014 and 2013

	2014	2013
Revenue and Support:		
Contributions	\$ 54,873	11,750
Interest and dividend income	462,928	432,671
Realized gain on investments	379,310	435,792
Investment expenses	(95,947)	(57,773)
Total revenue and support	801,164	822,440
 Expenses:		
Grants paid	1,039,840	769,422
Operating and administrative expenses	388,205	460,388
Excise taxes paid	11,448	815
Total expenses	1,439,493	1,230,625
 Change in net assets	 (638,329)	 (408,185)
Net assets at beginning of year	21,902,653	22,310,838
Net assets at end of year	\$ 21,264,324	21,902,653

See accompanying notes to financial statements.

Animal Assistance Foundation

Notes to Financial Statements

July 31, 2014 and 2013

(1) Summary of Significant Accounting Policies

(a) General

The Animal Assistance Foundation (the Foundation) is a not-for-profit charitable foundation whose mission is to support and enhance the five freedoms for companion animals in the state of Colorado through impactful and innovative grant making. The Foundation's vision is a statewide community where all companion animals are free from hunger and thirst; free from discomfort; free from pain, injury and disease; free to express normal behavior; and free from fear and distress – the five freedoms. The Foundation has the following areas of interest:

- *Population Control:* Population control for companion animals has been a priority since the Foundation began in 1976. During the decade of the 1970's, hundreds of thousands of animals were euthanized every year because of the pet overpopulation crisis. Today this number has been reduced to under 25,000 annually. The Foundation continues with the priority to support pet sterilization surgeries.
- *Operational Optimization:* Optimizing animal shelters provides better managed animal shelters at a lower cost which results in saving more lives, increasing awareness for responsible ownership, and raises Colorado's capacity for being one of the foremost states in the nation where animals live well with people. To accomplish this, funding is allocated to traditional, open enrollment animal shelters, as well as other shelters and rescues where collaboration is evident. Programs with growing placement and adoption rates are the priority.
- *Permanent Homes:* The ultimate goal is to find permanent homes for homeless animals and the Foundation wants to encourage adoptions, improve the adoptability of animals through behavior and health and by reducing owner relinquishments to keep animals with their owners.
- *Cruelty Prevention and Intervention:* Stopping all forms of cruelty towards animals is an emerging and broad initiative potentially open to innovations leading to better treatment programs for offenders. Programs aimed at alleviating animal suffering as a result of abuse receive consideration for funding.
- *Innovation:* Innovation is the final priority. The Foundation seeks to learn about and support innovations enhancing the well-being of cats, dogs, and horses. The Foundation encourages new ideas from partners and potential partners which would expand the quality of life for animals.

Animal Assistance Foundation

Notes to Financial Statements

(1) Summary of Significant Accounting Policies, Continued

(b) Basis of Presentation

The financial statements of the Foundation have been prepared on the basis of accounting used for income tax reporting purposes. Under the income tax basis, revenue is recorded when the Foundation receives interest and dividends, sells investments or receives a Form K-1 on certain investments. Expenses are recorded when payments are made, except for those items which are capitalized under the Foundation's capitalization policy (see note 1(f)).

(c) Cash and Cash Equivalents

The Foundation considers all unrestricted highly liquid investments with an original maturity of three months or less, and which are not held as part of an investment portfolio or on behalf of others, to be cash equivalents.

(d) Concentrations of Credit Risk

Financial instruments which potentially subject the Foundation to concentrations of credit risk consist of investments in debt and equity securities and limited partnerships. Investments are made by investment managers engaged by the Foundation and are monitored by management and the Board of Directors. Though the market value of investments is subject to fluctuations on a year to year basis, the Foundation believes that the investment policy is prudent for the long-term welfare of the Foundation.

(e) Investments

Investments are stated at cost. Investment income consists of the Foundation's distributive share of any interest, dividends, capital gains and capital losses, generated from the Foundation's investments. Distributive shares of income or loss from "pass-through" entities such as partnerships are recorded as income in the year such items are recognized by the entity and are reported as adjustments to the initial cost basis of the investment. Distributions of cash or other property received from "pass-through" entities are generally recorded as adjustments to the Foundation's investment cost basis.

Gains and losses attributable to the Foundation's investments are realized and reported upon a sale or disposition of the investment. The Foundation uses an average cost basis for its investments in determining realized gains or losses.

(f) Property and Equipment

Property and equipment is stated at cost, if purchased, or at fair value if received by donation. The Foundation capitalizes all expenditures for property and equipment in excess of \$5,000 with an estimated useful life in excess of one year. Depreciation is computed using the straight-line method over the estimated useful lives of the assets ranging from 3 to 5 years. At July 31, 2014, assets with a cost basis of \$26,048 are fully depreciated.

Animal Assistance Foundation

Notes to Financial Statements

(1) Summary of Significant Accounting Policies, Continued

(g) Use of Estimates

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, the disclosure of contingent assets and liabilities, and the reported revenue and expenses. Actual results could differ from those estimates.

(h) Functional Allocation of Expenses

The costs of providing various programs and related supporting services have been summarized on a functional basis in the accompanying financial statements. Accordingly, certain costs have been allocated among the appropriate programs and supporting services benefited.

(i) Income Tax Status

The Foundation has been classified as a private foundation as defined in Section 509(a) of the Internal Revenue Code (the Code) and is exempt from federal income tax under section 501(c)(3) of the Code. Income from certain activities not directly related to the Foundation's tax-exempt purpose is subject to taxation as unrelated business taxable income. There was no unrelated business taxable income in 2014 or 2013.

Management is required to evaluate tax positions taken by the Foundation and to recognize a tax liability if the Foundation has taken an uncertain position that more likely than not would not be sustained upon examination by taxing authorities. Management believes it has appropriate support for any tax positions taken and that none would require recognition of a liability or disclosure in the financial statements. Management believes the Foundation is no longer subject to income tax examinations for years prior to July 31, 2011.

(j) Excise Taxes

Private foundations are subject to an excise tax on net investment income, which includes realized gains on the sale of assets. The tax is equal to 2% of net investment income, but can be reduced to 1% if qualifying expenditures exceed certain minimum amounts. Excise tax expense for 2014 and 2013 was \$7,093 and \$7,773, respectively.

The Code requires certain minimum distributions to be made in accordance with a specified formula. During 2015, the Foundation is required to make minimum qualifying distributions of \$1,276,890.

Animal Assistance Foundation

Notes to Financial Statements

(1) Summary of Significant Accounting Policies, Continued

(k) Subsequent Events

Management is required to evaluate, through the date the financial statements are issued or available to be issued, events or transactions that may require recognition or disclosure in the financial statements, and to disclose the date through which subsequent events were evaluated. The Foundation's financial statements were available to be issued on November 6, 2014 and this is the date through which subsequent events were evaluated.

(2) Investments

The Foundation's investment assets, which include private and publicly held investments, are dedicated to providing the financial resources needed to meet the Foundation's grant making and other charitable objectives. The Foundation's investments are managed by independent professional investment management firms and are held in various investment structures such as mutual funds and limited partnerships.

Marketable and private alternative investments are exposed to various risks that may cause the value of the Foundation's investment assets to fluctuate from period to period and result in a material change to that valuation. Investments in equity securities fluctuate in value in response to many factors such as the activities and financial condition of individual companies, business and industry market conditions, and the general economic environment. The value of bond investments and other fixed income securities fluctuate in response to changing interest rates, credit worthiness of issuers and overall economic policies that impact market conditions.

Some investment managers retained by the Foundation are permitted to use various investment strategies and techniques that are designed to achieve higher investment returns with lower volatility and low correlations to major market indices and other asset classes. Strategies and techniques, such as the use of leverage, futures and forward contracts, option agreements, and other derivative instruments create special risks and could increase the impact of adverse security price movements on the Foundation's investment portfolio.

Animal Assistance Foundation

Notes to Financial Statements

(2) Investments, Continued

The following is a summary of the cost and unaudited market value of investments at July 31, 2014:

	<u>Cost</u>	<u>Market (Unaudited)</u>
Cash and cash equivalents	\$ 22,408	22,408
Bond mutual funds:		
Total return	2,651,027	2,702,061
Short term	1,028,132	1,029,615
Bank credit	958,970	953,634
Equity mutual funds:		
Domestic	7,170,449	10,824,777
International	4,095,917	6,054,978
Emerging markets	506,379	703,724
Limited partnerships:		
Real estate	2,215,676	2,763,026
Multi-strategy hedge fund of funds	1,596,793	3,158,340
Floating rate income fund	<u>1,000,000</u>	<u>1,040,559</u>
Total investments	\$ <u>21,245,751</u>	<u>29,253,122</u>

The following is a summary of the cost and unaudited market value of investments at July 31, 2013:

	<u>Cost</u>	<u>Market (Unaudited)</u>
Cash and cash equivalents	\$ 87,012	87,012
Bond mutual funds:		
Total return	2,583,878	2,610,260
Short term	1,017,981	1,012,222
Equity mutual funds:		
Domestic	7,872,985	10,490,539
International	4,005,872	5,346,489
Emerging markets	492,239	609,276
Limited partnerships:		
Real estate	2,279,644	2,594,963
Multi-strategy hedge fund of funds	1,571,030	2,920,403
Macro-strategy hedge fund of funds	963,103	968,282
Floating rate income fund	<u>1,000,000</u>	<u>1,000,000</u>
Total investments	\$ <u>21,873,744</u>	<u>27,639,446</u>

In addition to the cash basis investment income, the Foundation had additional unrealized gains of \$2,241,669 and \$3,289,209 in 2014 and 2013, respectively.

Animal Assistance Foundation

Notes to Financial Statements

(3) Employee Benefit Plans

All regular, full-time employees of the Foundation are eligible to participate in the Foundation's 401(k) plan upon completion of one year of service. Under the plan, each participating employee has the option to contribute amounts, on a pre-tax basis, up to the maximum allowable by the Internal Revenue Code. The Foundation matches an amount equal to 100% of employee contributions, not to exceed 4% of the employee's salary. In addition, the Foundation may make additional contributions at the discretion of the Board. Contributions to the plan were \$5,570 and \$3,309 in 2014 and 2013, respectively.

(4) Lease Commitments

The Foundation has a non-cancelable operating lease for office space that expires May 31, 2018, and office equipment leases that expire at various terms through 2016. Future minimum lease payments are as follows for the years ending July 31:

2015	\$ 28,766
2016	28,700
2017	24,798
2018	<u>20,560</u>
	\$ <u>102,824</u>

Rent expense was \$24,311 and \$16,809 in 2014 and 2013, respectively.

Animal Assistance Foundation
Communication with Those Charged with Governance
Regarding the July 31, 2014 Audit

AREA	COMMENT
Our Responsibility Under U.S. Generally Accepted Auditing Standards (GAAS)	Audit performed in accordance with GAAS. The objective of an audit is reasonable, but not absolute, assurance about whether the financials are free of material misstatement. Our audit does not relieve you or management of your responsibilities.
Other Information in Documents Containing Audited Financials	None.
Planned Scope and Timing of Audit	The audit was performed according to the planned scope and timing previously communicated to you in our engagement letter dated May 9, 2014.
Significant Audit Findings	<ol style="list-style-type: none"> 1. Management has the responsibility for selection and use of appropriate accounting policies. The significant policies used are listed in Note 1 to the financial statements. The Foundation's most significant policy is the use of income tax basis accounting. 2. No new accounting policies were adopted in the current year. 3. We noted no accounting transactions were entered into in 2014 with an absence of authoritative accounting guidance or consensus. 4. There were no significant transactions recognized in a different period than when the transaction occurred. 5. Accounting estimates include the disclosed fair value of the alternative investments. 6. Financial statement disclosures are neutral, consistent and clear.
Difficulties Encountered in Performing the Audit	We encountered no difficulties in dealing with management in performing and completing our audit.
Corrected and Uncorrected Misstatements	There were no audit adjustments or uncorrected misstatements.
Disagreements with Management	No disagreements arose with management during the course of our audit on financial accounting, reporting or auditing matters.

Animal Assistance Foundation
Communication with Those Charged with Governance, Continued

AREA	COMMENT
Management Representations	We requested certain representations from management that are included in their representation letter dated November 6, 2014.
Management Consultations with Other Independent Accountants	We are not aware of any consultations by management with other accountants about accounting and auditing matters.
Other Audit Findings or Issues	There were no discussions of the application of certain accounting principles prior to our retention as auditor.

This report is intended solely for the information and use of the board of directors and management and is not intended to be and should not be used by anyone other than these specified parties.

November 6, 2014

ANIMAL ASSISTANCE FOUNDATION
Tax Information for Officers
July 31, 2014
by Kunding, Corder & Engle, P.C.

A. Basic IRS Distribution Requirements

- 1 Must distribute, for charitable purposes, 5% of fair market value of investments each year.
 - a. Foundations have 12 months after the end of the year to make the required distribution
 - b. "Charitable distributions" include certain general and administrative expenses
 - c. The required distribution is reduced by taxes on investment income
 - d. Fair market value is calculated based on a monthly average during the year, less an IRS allowance of 1.5% for "cash held for charitable purposes".

- 2 The actual calculation of 2014 undistributed income, which is required to be paid in 2015, is:

2014 Average monthly fair value of assets	\$ 28,892,163
Less 1.5% IRS allowance for "cash held"	(433,382)
Net value of assets	\$ 28,458,781
Minimum payout requirement (5% of above)	\$ 1,422,939
Reduced by 2014 excise tax	(7,093)
Required distribution by July 31, 2015	\$ 1,415,846

- 3 The minimum distribution is:

Required distribution by July 31, 2015 (see above)	\$ 1,415,846
Amount distributed as of July 31, 2014 (per tax return)	(138,956)
Adjusted minimum required distribution	1,276,890
Add recommended reserve (note 1)	50,000
Less estimated charitable, non-grant expenses for 2015	(350,000)
Calculated recommended minimum payments to charities in 2015	\$ 976,890

Note 1: A "permanent reserve" is recommended to provide some leeway in the event of IRS disputes regarding stock valuation or allocation of expenses, and because of the severity of the penalties for "failure to distribute" the required minimum amounts.

B. Taxes on Investment Income

- 1 Must pay taxes equal to 2% of net investment income
 - a. Investment income is calculated on a cash basis and includes the results of realized gains and losses on sales of securities
 - b. Investment income is reduced by investment expenses, including a portion of general and administrative expenses
 - c. Tax can be reduced to 1% if a foundation distributes an amount greater than the 5-year average percentage distribution

- 2 The actual calculations for 2015 are:

Average monthly fair value of assets	\$ 28,458,781
Average 5-year distribution % (from 2014 tax return)	4.65%
	<u>1,322,394</u>
Add back the 1% excise tax saved (which must be paid to charities)	7,093
Distribution required to use 1% rate in 2014	<u><u>1,329,487</u></u>
Actual qualifying distributions in 2014 (per tax return)	<u><u>1,391,015</u></u>

Therefore, the 1% rate was used in 2014.

C. Estimated 2015 Payments to Charities to Achieve 1% Rate:

Total required qualifying distribution (attached)	\$ 1,356,397
Less administrative expenses (2015 estimate)	(350,000)
Add reserve	10,000
Payments to charities to achieve 1% rate	<u><u>\$ 1,016,397</u></u>

D. Conclusion

The estimate above to achieve the 1% tax rate for the year ending July 31, 2015 is slightly more than the recommended minimum distribution on page 1. However, if grant payments in 2015 are comparable to 2014, a 1% tax rate is possible.

ANIMAL ASSISTANCE FOUNDATION
Calculation of 2% vs 1%
2015 Fiscal Year--Estimate made November 2014

Base Year	Adjusted Qualifying Distributions	Net Value of Noncharitable Use Assets	Payout Ratio
2014	1,383,922	28,450,707	0.0486427982
2013	1,189,466	25,935,291	0.0458628361
2012	1,077,964	24,163,638	0.0446109977
2011	1,104,583	24,893,504	0.0443723391
2010	1,165,394	23,415,341	0.0497705329
Total			<u>0.2332595040</u>
Average 5 Year Payout %			0.0466519008
Net Value of Noncharitable Use Assets (See note 1)			<u>28,860,500</u>
Net Value Times Average 5-Year Payout %			1,346,397
Add back 1% of Net Investment Income (estimated)			10,000
Total Required Qualifying Distributions			<u>1,356,397</u>

Note 1: Based on the 7/31/14 FMV of cash and investments - ~\$29,300,000, less a cash reserve of 1.5%

This is a tentative estimate and will change as a result of changes in market value, payments of expenses, and actual excise taxes.