

Financial Statements and Independent Auditors' Report

Arthritis Foundation, South Central Region, Inc.

Year ended December 31, 2012

(With Summarized Financial Information for the
Year Ended December 31, 2011)



Independent Auditors' Report

Board of Directors
Arthritis Foundation, South Central Region, Inc.

We have audited the accompanying financial statements of the Arthritis Foundation, South Central Region, Inc., (a nonprofit organization), which comprise the statement of financial position as of December 31, 2012, and the related statements of activities, 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 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.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Arthritis Foundation, South Central Region, Inc. as of December 31, 2012, and the changes in its net assets and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Report on Summarized Comparative Information

We have previously audited the Arthritis Foundation, South Central Region, Inc.'s 2011 financial statements, and we expressed an unmodified audit opinion on those audited financial statements in our report dated April 9, 2012. In our opinion, the summarized comparative information presented herein as of and for the year ended December 31, 2011 is consistent, in all material respects, with the audited financial statements from which it has been derived.

Metcalf Dewis

Atlanta, Georgia
March 22, 2013

ARTHRITIS FOUNDATION, SOUTH CENTRAL REGION, INC.

Statement of Financial Position

December 31, 2012 with Summarized Financial Information as of December 31, 2011

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Totals</u>	
				2012	2011
<u>Assets</u>					
Cash and cash equivalents	\$ 616,731	\$ 46,891	\$ -	\$ 663,622	\$ 848,205
Investments	1,001,842	2,586,031	1,837,079	5,424,952	5,367,509
Due from National Office	69,713	-	-	69,713	116,011
Contributions and bequests receivable, net	32,019	72,467	-	104,486	201,820
Prepaid expenses and other assets	52,012	-	-	52,012	31,985
Charitable remainder trusts	-	288,643	-	288,643	21,148
Beneficial interests in assets held by others	-	-	107,094	107,094	46,213
Property and equipment, net	<u>12,672</u>	<u>-</u>	<u>-</u>	<u>12,672</u>	<u>18,755</u>
Total assets	<u>\$ 1,784,989</u>	<u>\$ 2,994,032</u>	<u>\$ 1,944,173</u>	<u>\$ 6,723,194</u>	<u>\$ 6,651,646</u>
<u>Liabilities and Net Assets</u>					
Accounts payable	\$ 59,388	\$ -	\$ -	\$ 59,388	\$ 47,677
Accrued expenses and other liabilities	77,642	-	-	77,642	55,174
Research awards and grants payable	-	-	-	-	15,000
Due to National Office	<u>93,586</u>	<u>-</u>	<u>-</u>	<u>93,586</u>	<u>108,882</u>
Total liabilities	230,616	-	-	230,616	226,733
Net assets	<u>1,554,373</u>	<u>2,994,032</u>	<u>1,944,173</u>	<u>6,492,578</u>	<u>6,424,913</u>
Total liabilities and net assets	<u>\$ 1,784,989</u>	<u>\$ 2,994,032</u>	<u>\$ 1,944,173</u>	<u>\$ 6,723,194</u>	<u>\$ 6,651,646</u>

The accompanying notes are an integral part of this statement.

ARTHRITIS FOUNDATION, SOUTH CENTRAL REGION, INC.

Statement of Activities

Year Ended December 31, 2012 with Summarized Financial Information for the Year Ended December 31, 2011

	Unrestricted	Temporarily Restricted	Permanently Restricted	Totals	
				2012	2011
<u>Operating Activities</u>					
Personal major gifts	\$ 42,943	\$ 35,000	\$ -	\$ 77,943	\$ 135,000
Personal annual gifts	62,789	4,379	-	67,168	117,743
Commerce and industry gifts	260,089	120,390	-	380,479	299,060
Foundations	38,190	174,600	-	212,790	185,668
Memorials	12,984	50	-	13,034	7,805
Other gifts	5,191	-	-	5,191	13,099
Thrift shop	36,000	-	-	36,000	36,000
Membership/direct response marketing	742,508	-	-	742,508	738,315
Total contributions	1,200,694	334,419	-	1,535,113	1,532,690
Special events - gross income	2,115,276	-	-	2,115,276	2,101,941
Less direct donor benefit costs	(495,694)	-	-	(495,694)	(548,111)
Bequests/planned giving	233,407	282,869	62,449	578,725	224,474
Total direct public support	3,053,683	617,288	62,449	3,733,420	3,310,994
Federated campaigns	92,113	900	-	93,013	93,917
United Way	187,166	-	-	187,166	262,145
Total indirect public support	279,279	900	-	280,179	356,062
Total public support	3,332,962	618,188	62,449	4,013,599	3,667,056
Sales and service fees	22,509	-	-	22,509	18,473
Investment return appropriated for current operations	36,056	-	-	36,056	32,626
Miscellaneous income	3,836	6,131	-	9,967	11,192
Total other revenue	62,401	6,131	-	68,532	62,291
Losses on uncollectible pledges	-	(23,798)	-	(23,798)	-
Net assets released from restrictions	538,848	(538,848)	-	-	-
Total revenues, gains, losses and public support	3,934,211	61,673	62,449	4,058,333	3,729,347
<u>Expenses</u>					
Program	3,402,007	-	-	3,402,007	3,478,491
Fundraising	697,003	-	-	697,003	565,781
Management and general	363,736	-	-	363,736	376,053
Total program and supporting services expenses	4,462,746	-	-	4,462,746	4,420,325
Change in net assets from operating activities	(528,535)	61,673	62,449	(404,413)	(690,978)
<u>Non-operating Activities</u>					
Investment return over (under) amounts appropriated for current operations	53,109	419,336	-	472,445	(22,839)
Unrealized (loss) gain on beneficial interests in assets held by others	-	-	(1,568)	(1,568)	6,199
Unrealized gain on charitable remainder trusts	-	1,201	-	1,201	-
Contribution received in acquisition of the New Mexico and El Paso Offices	-	-	-	-	2,578,313
Change in net assets from non-operating activities	53,109	420,537	(1,568)	472,078	2,561,673
Change in net assets	(475,426)	482,210	60,881	67,665	1,870,695
Net assets, beginning of year	2,029,799	2,511,822	1,883,292	6,424,913	4,554,218
Net assets, end of year	<u>\$ 1,554,373</u>	<u>\$ 2,994,032</u>	<u>\$ 1,944,173</u>	<u>\$ 6,492,578</u>	<u>\$ 6,424,913</u>

The accompanying notes are an integral part of this statement.

ARTHRITIS FOUNDATION, SOUTH CENTRAL REGION, INC.

Statement of Functional Expenses

Year Ended December 31, 2012 with Summarized Financial Information for the Year Ended December 31, 2011

<u>Expenses</u>	PROGRAM SERVICES					SUPPORTING SERVICES			Totals	
	Research	Public Health Education	Professional Education and Training	Patient and Community Services	Total Program Services	Fundraising	Management and General	Total Supporting Services	2012	2011
Peer reviewed research awards	\$ 30,348	\$ -	\$ -	\$ -	\$ 30,348	\$ -	\$ -	\$ -	\$ 30,348	\$ 280,000
Salaries	-	597,360	48,435	581,215	1,227,010	242,173	145,304	387,477	1,614,487	1,539,982
Payroll taxes	-	50,451	4,091	49,088	103,630	20,453	12,272	32,725	136,355	128,337
Employee benefits	-	63,860	5,178	62,134	131,172	25,889	15,533	41,422	172,594	236,107
Technology fees	-	44,391	3,599	43,191	91,181	17,996	10,798	28,794	119,975	108,151
Data processing and accounting services	-	-	-	-	-	2,550	-	2,550	2,550	3,098
Professional fees and contract services	-	80,190	6,165	81,444	167,799	32,149	18,496	50,645	218,444	225,920
Professional services - contributed	-	-	-	-	-	-	-	-	-	1,508
Supplies	-	8,879	619	23,999	33,497	6,724	1,858	8,582	42,079	47,823
Printing, publications, and artwork	-	9,527	193	4,937	14,657	17,845	580	18,425	33,082	42,541
Materials expenses	-	1,919	154	11,936	14,009	790	462	1,252	15,261	13,418
Membership/direct response marketing	-	206,851	-	-	206,851	72,677	-	72,677	279,528	243,398
Arthritis Today cost recovery	-	78,920	-	-	78,920	-	-	-	78,920	86,508
Postage, shipping, and delivery	-	5,330	383	6,005	11,718	7,247	1,147	8,394	20,112	22,845
Telephone	-	17,919	1,360	16,538	35,817	9,677	4,081	13,758	49,575	53,349
Occupancy	-	71,531	5,800	69,598	146,929	28,999	17,400	46,399	193,328	170,911
Taxes and licenses	-	172	14	168	354	70	42	112	466	592
Insurance	-	9,721	788	10,285	20,794	3,941	2,365	6,306	27,100	13,321
Staff travel	-	17,553	1,057	22,032	40,642	25,194	3,147	28,341	68,983	64,162
Volunteer travel	-	4,274	242	9,450	13,966	1,404	726	2,130	16,096	15,910
Meetings and conferences	-	8,564	480	102,453	111,497	12,277	1,440	13,717	125,214	97,087
Equipment lease and maintenance	-	14,003	1,135	13,624	28,762	5,697	3,406	9,103	37,865	34,128
Membership dues and subscriptions	-	3,209	260	3,123	6,592	1,500	781	2,281	8,873	9,518
Advertising	-	188	-	1,049	1,237	1,563	-	1,563	2,800	5,378
Miscellaneous	-	15,110	1,278	14,817	31,205	39,510	3,675	43,185	74,390	55,645
Depreciation	-	2,252	182	2,190	4,624	912	547	1,459	6,083	3,582
Uncollectible receivables	-	555	45	540	1,140	225	135	360	1,500	-
Total operating expenses	30,348	1,312,729	81,458	1,129,816	2,554,351	577,462	244,195	821,657	3,376,008	3,503,219
Share expense	217,348	456,430	10,867	163,011	847,656	119,541	119,541	239,082	1,086,738	917,106
Total expenses	\$ 247,696	\$ 1,769,159	\$ 92,325	\$ 1,292,827	\$ 3,402,007	\$ 697,003	\$ 363,736	\$ 1,060,739	\$ 4,462,746	\$ 4,420,325

The accompanying notes are an integral part of this statement.

ARTHRITIS FOUNDATION, SOUTH CENTRAL REGION, INC.

Statement of Cash Flows

For the Year Ended December 31, 2012 with

Summarized Information for the Year Ended December 31, 2011

	2012	2011
Cash flows from operating activities		
Change in net assets	\$ 67,665	\$ 1,870,695
Adjustments to reconcile change in net assets to net cash (used in) provided by operating activities:		
Depreciation	6,083	3,582
Net unrealized losses (gains) on beneficial interests in assets held by others	1,568	(6,199)
Net realized and unrealized (gains) losses on investments	(388,936)	64,952
Net unrealized gains on charitable remainder trusts	(1,201)	-
Contribution of charitable remainder trust	(266,294)	-
Contribution of beneficial interest in assets held by others	(62,449)	-
Contribution restricted for permanent investment	-	(1,072,500)
Change in assets and liabilities:		
Due from National Office	46,298	10,995
Contributions receivable	97,334	(67,193)
Prepaid expenses and other assets	(20,027)	4,159
Accounts payable	11,711	47,677
Accrued expenses and other liabilities	22,468	(86,933)
Research awards and grants payable	(15,000)	(370,000)
Due to National Office	(15,296)	(109,523)
Net cash (used in) provided by operating activities	(516,076)	289,712
Cash flows from investing activities		
Proceeds from sale of property and equipment	-	338
Purchase of investments	(2,377,639)	(2,688,315)
Proceeds from sale of investments	2,709,132	54,806
Net cash provided by (used in) investing activities	331,493	(2,633,171)
Cash flows from financing activities		
Contribution restricted for permanent investment	-	1,072,500
Net decrease in cash and cash equivalents	(184,583)	(1,270,959)
Cash and cash equivalents at beginning of year	848,205	2,119,164
Cash and cash equivalents at end of year	\$ 663,622	\$ 848,205
<u>Supplemental Schedule:</u>		
Contribution of charitable remainder trust	\$ 266,294	\$ -
Contribution of beneficial interest in assets held by others	62,449	-
Fair value of assets acquired as part of contribution received in acquisition of New Mexico and El Paso Offices	\$ -	\$ 2,578,313

The accompanying notes are an integral part of this statement.

ARTHRITIS FOUNDATION, SOUTH CENTRAL REGION, INC.

Notes To Financial Statements

December 31, 2012 with Summarized Information for the Year Ended December 31, 2011

NOTE 1 – DESCRIPTION OF ORGANIZATION

Arthritis Foundation, South Central Region, Inc. (the “Region”) is a not-for-profit voluntary health agency serving the states of Texas, Oklahoma and New Mexico by charter of the Arthritis Foundation, Inc. The Region seeks to improve lives through leadership in the prevention, control and cure of arthritis and arthritis-related diseases. Major funding sources are from direct public contributions and bequests. The Region provides public health education and community service programs along with supporting arthritis-related research and influencing public policy regarding research funding and access to care.

On October 11, 2011, the South Central Region acquired the assets and net assets of two former Greater Southwest Chapter offices located in El Paso and New Mexico. No consideration was paid by the Region as a result of this acquisition. Assets acquired included cash of \$145,335 and investments with a fair value of \$2,432,978. No liabilities were assumed.

Since the operations of the Region, including the El Paso and New Mexico offices, were expected to be predominately supported by contributions and returns on investments, the Region recognized the acquisition-date amounts of the identifiable assets acquired on the statement of activities as “*Contribution received in acquisition of the New Mexico and El Paso Offices.*”

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A summary of the significant accounting policies consistently applied in the preparation of the accompanying financial statements follows.

Accrual Basis of Accounting - The financial statements of the Region have been prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America (“GAAP”).

Basis of Presentation - The Region classifies its net assets and revenues, expenses, gains and losses based on the existence or absence of donor-imposed restrictions. Accordingly, net assets of the Region and changes therein are classified and reported as follows:

Unrestricted net assets - Net assets that are not subject to donor-imposed stipulations.

Temporarily restricted net assets - Net assets subject to donor-imposed stipulations that may or will be met either by actions of the Region and/or the passage of time.

Permanently restricted net assets - Net assets subject to donor-imposed stipulations that the Region maintains them permanently. Generally, the donors of these assets permit the Region to use all or part of the income earned on related investments for general or specific purposes.

ARTHRITIS FOUNDATION, SOUTH CENTRAL REGION, INC.

Notes To Financial Statements

December 31, 2012 with Summarized Information for the Year Ended December 31, 2011

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Revenues are reported as increases in unrestricted net assets unless the use of the related assets is limited by donor-imposed restrictions. Expenses are reported as decreases in unrestricted net assets. Gains and losses on investments and other assets or liabilities are reported as increases or decreases in unrestricted net assets unless their use is restricted by explicit donor stipulation or by law. Expirations of temporary restrictions on net assets (i.e., the donor-stipulated purpose has been fulfilled and/or the stipulated time period has elapsed) are reported as reclassifications between the applicable classes of net assets.

Operating results in the statement of activities reflect all transactions increasing and decreasing net assets except those that the Region defines as non-operating. Non-operating includes all investment returns in excess of the Region's spending policy, unrealized gains and losses from operating accounts, unrealized gains and losses on beneficial interests in assets held by others and changes in valuation of split interest agreements. For 2011, non-operating also included the contribution received in donation of the New Mexico and El Paso offices.

Income Taxes - The Region is exempt from federal income tax under Section 501(c)(3) of the United States Internal Revenue Code (the "Code"), except to the extent it has unrelated business income. In addition, the Region has been determined by the Internal Revenue Service not to be a private foundation within the meaning of Section 509(a) of the Code. For the years ended December 31, 2012 and 2011, the Region had no net unrelated business income. Accordingly, no provision for income tax has been provided in the accompanying financial statements.

Accounting standards requires the evaluation of tax positions taken or expected to be taken in the course of preparing the Region's annual tax return to determine whether the tax positions are more likely than not of being sustained by the applicable tax authority. Tax positions not deemed to meet the more likely than not threshold would be recorded as a tax benefit or expense in the current year. A reconciliation is not provided herein, as the beginning and ending amounts of unrecognized benefits are zero, with no interim additions, reductions, or settlements. The Region is relying on its tax-exempt status and its adherence to all applicable laws and regulations to preserve that status. However, the conclusions regarding accounting for uncertainty in income taxes will be subject to review and may be adjusted at a later date based on factors including, but not limited to, ongoing analysis of tax laws, regulations, and interpretations thereof.

The Region recognizes interest and penalties, if any, related to uncertain tax positions as income tax expense. Informational returns filed are generally subject to examination for three years after the later of the due date or date of filing. As a result, the Region is no longer subject to income tax examinations by tax authorities for years prior to 2009.

Fair Value of Financial Instruments - The estimated fair value amounts for specific groups of financial instruments are presented within the notes applicable to such items. Prepaid expenses and other assets, accounts payable and accrued expenses and other liabilities are stated at cost, which approximates fair value, due to their short term maturity.

ARTHRITIS FOUNDATION, SOUTH CENTRAL REGION, INC.

Notes To Financial Statements

December 31, 2012 with Summarized Information for the Year Ended December 31, 2011

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

The fair value of investments and funds held in trust by others is disclosed in other notes and is based upon quoted market values or values provided by external investment managers which were reviewed by management and the board.

Cash and Cash Equivalents - Cash and cash equivalents include cash on hand and all highly-liquid investments with original maturities at the date of purchase of three months or less excluding (i) cash and cash equivalents in the investment portfolio and (ii) donor-restricted cash. Because of the short maturity of these financial instruments, the carrying value approximates the fair value. The Region places its cash and cash equivalents with high credit quality financial institutions located in the United States. At times, these balances may exceed federally insured limits. The Region has not experienced any losses on such accounts and believes it is not exposed to any significant credit risk on cash and cash equivalents.

Investments - Investments in marketable securities with readily determinable fair values are stated at fair value. The cost assigned to investments received by gift is the fair value at the date the gift is received. Purchases and sales of securities are reflected on a trade-date basis. Gains and losses on sales of securities are based on cost (cost of securities if purchased or the fair market value at the date of gift if received by donation). Dividend and interest income is recorded on the accrual basis. In accordance with the policy of stating investments at fair value, the net change in unrealized appreciation or depreciation for the year is reflected in the statement of activities.

The Region's investments are exposed to a variety of uncertainties, including interest rate, market and credit risks. Due to the level of risk associated with certain investments, it is possible that changes in the values of these instruments could occur in the near term. Such changes could materially affect the amounts reported in the financial statements of the Region.

Beneficial Interests in Assets Held by Others - The Region is the beneficiary of various trusts created by donors, the assets of which are not in the possession of the Region. The Region has legally enforceable rights or claims to such assets including the right to income there from. Under the perpetual trust arrangement the Region has recorded the asset and recognized permanently restricted contribution revenue at the fair value of its beneficial interests in the trust assets. Distributions received on the trust assets are recorded as unrestricted revenue in the statement of activities unless otherwise restricted by the donor. Subsequent changes in fair value of the beneficial interests in the trust assets are recorded as net unrealized gains or losses on beneficial interests in assets held by others in the permanently restricted net asset class.

Property and Equipment - Property and equipment are recorded at cost. Donated assets are capitalized at the estimated fair market value at date of receipt. Depreciation is provided on the straight-line method over the estimated useful lives of the assets. The cost of maintenance and repairs is expensed when incurred; significant renewals and betterments are capitalized. The Region's policy is to capitalize property and equipment acquisitions in excess of \$5,000.

ARTHRITIS FOUNDATION, SOUTH CENTRAL REGION, INC.

Notes To Financial Statements

December 31, 2012 with Summarized Information for the Year Ended December 31, 2011

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Contributed Goods and Services - Contributed goods and services are reflected as both contribution revenue and expenses if they meet the criteria defined in accordance with GAAP, “Accounting for Contributions”, in the accompanying statement of activities at their estimated fair value at date of receipt. The contributions of services are recognized if the services received (a) create or enhance nonfinancial assets or (b) require specialized skills that are provided by individuals possessing those skills and would typically need to be purchased if not provided. Generally, such services include advertising and donated media costs.

In addition, the Region receives services from a large number of volunteers who give significant amounts of their time to the Region's programs, fundraising campaigns and management. No amounts have been reflected for these types of donated services, as they do not meet the criteria for recognition.

Contributions and Bequests Receivable - Contributions, including unconditional promises to give, are recorded at the date of gift. Bequests are recorded as revenue at the time an unassailable right to the gift has been established and the proceeds are measurable in amount. The Region records unconditional promises to give, expected to be collected within one year, at net realizable value. Those expected to be collected in more than one year are recorded at the present value of their estimated future cash flows. The discounts on those amounts are computed on the date of the gift using risk-adjusted interest rates applicable to the years in which the promises are expected to be received. Accretion of discounts is recognized as contribution revenue using the effective interest rate.

An allowance for doubtful contributions and bequests receivable is recorded when deemed necessary based upon historical trends, current market risk assessments and specific donor considerations. Receivables are written off when management believes they will not be collected. Accounts receivable are considered past due after 30 days.

Conditional promises to give are recognized when the conditions stipulated by the donor are substantially met. A conditional promise to give is considered unconditional if the possibility that the condition will not be met is remote.

Special Events - The Region conducts special fundraising events including annual walks, runs, dinners, galas, and golf tournaments. Participation and registration fees, along with contributions received from participants and other donors in support of the event, are included as event revenue. The cost to the Region for the direct benefit that the participant receives at such events is presented as a separate component of direct public support revenue on the statement of activities. All other costs related to the event are recorded as fundraising expense.

Awards and Grants - Awards and grants are recorded as expense in the year for which the grants are designated. The terms of research awards and grants are from one to three years with continuation of the grant conditional upon completion of certain performance requirements.

ARTHRITIS FOUNDATION, SOUTH CENTRAL REGION, INC.

Notes To Financial Statements

December 31, 2012 with Summarized Information for the Year Ended December 31, 2011

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Functional Allocation - The cost of providing the Region's various programs and supporting services have been summarized on a functional basis. Accordingly, certain costs have been allocated among the programs and supporting services benefited.

Use of Estimates - Management of the Region has made a number of estimates and assumptions relating to the reporting of assets and liabilities and the disclosure of contingent assets and liabilities to prepare the financial statements in conformity with GAAP. Actual results could differ from these estimates.

Reclassifications - Certain reclassifications have been made to 2011 balances to conform to the 2012 presentation. These reclassifications were considered insignificant and did not change 2011 net assets as previously recorded.

NOTE 3 – RELATED PARTY TRANSACTIONS

The Region is required to share 27 percent, 35 percent or 45 percent of certain public support and bequests per their agreement with the National Office. This share expense totaled \$1,086,738 and \$917,106 for the years ended December 31, 2012 and 2011, respectively. The Region is also allocated a portion of certain contributions received by the National Office, which for the years ended December 31, 2012 and 2011 was \$950,511 and \$915,744, respectively. The Region reimburses the National Office for a portion of costs associated with *Arthritis Today*, the organization's magazine, its direct mail program, computer system support, financial services and educational and promotional materials which totaled approximately \$496,778 and \$452,946 in 2012 and 2011, respectively.

Amounts due to and from the National Office at year end arise as a result of transactions occurring between the two entities. To clearly identify amounts to be received from and to be paid to the National Office, the Region presents these amounts separately as receivables and payables on the statement of financial position. At December 31, 2012 and 2011, the National Office receivable totaled \$69,713 and \$116,011, respectively, and the payable totaled \$93,586 and \$108,882, respectively.

ARTHRITIS FOUNDATION, SOUTH CENTRAL REGION, INC.

Notes To Financial Statements

December 31, 2012 with Summarized Information for the Year Ended December 31, 2011

NOTE 4 – INVESTMENTS

Investments at December 31, 2012 and 2011 were as follows:

	<u>2012</u>	<u>2011</u>
Marketable securities:		
Domestic equity mutual funds		
Energy	\$ 89,789	\$ 28,531
Technology	-	1,935,648
Real estate	94,824	46,573
Other	2,230,210	403,687
Fixed income mutual funds	2,171,759	969,516
Mortgage backed securities	-	50,934
Corporate bonds	-	49,908
International equity mutual funds	-	10,506
Common stocks	5,046	1,195
Open end mutual funds - real estate	10,041	-
REITs	<u>1,299</u>	<u>-</u>
 Total marketable securities	 <u>4,602,968</u>	 <u>3,496,498</u>
 Money market funds	 581,463	 1,531,288
Certificates of deposit	<u>240,521</u>	<u>339,723</u>
 Total investments	 <u>\$ 5,424,952</u>	 <u>\$ 5,367,509</u>

ARTHRITIS FOUNDATION, SOUTH CENTRAL REGION, INC.

Notes To Financial Statements

December 31, 2012 with Summarized Information for the Year Ended December 31, 2011

NOTE 4 – INVESTMENTS - Continued

The following summarizes the Region’s total investment return, net of investment management fees of \$19,991 and \$8,911 for the years ended December 31, 2012 and 2011, respectively, and the classification in the statement of activities.

	December 31, 2012		
	Unrestricted	Temporarily Restricted	Total
Dividend and interest income	\$ 36,056	\$ 83,509	\$ 119,565
Net realized gains	19,459	125,754	145,213
Net unrealized gains	<u>33,650</u>	<u>210,073</u>	<u>243,723</u>
	89,165	419,336	508,501
Less investment return designated for operations	<u>36,056</u>	-	<u>36,056</u>
Investment return over amount designated for operations	<u>\$ 53,109</u>	<u>\$ 419,336</u>	<u>\$ 472,445</u>
	December 31, 2011		
	Unrestricted	Temporarily Restricted	Total
Dividend and interest income	\$ 32,626	\$ 48,312	\$ 80,938
Net realized gains	562	8,093	8,655
Net unrealized losses	<u>(13,231)</u>	<u>(66,575)</u>	<u>(79,806)</u>
	19,957	(10,170)	9,787
Less investment return designated for operations	<u>32,626</u>	-	<u>32,626</u>
Investment return under amount designated for operations	<u>\$ (12,669)</u>	<u>\$ (10,170)</u>	<u>\$ (22,839)</u>

ARTHRITIS FOUNDATION, SOUTH CENTRAL REGION, INC.

Notes To Financial Statements

December 31, 2012 with Summarized Information for the Year Ended December 31, 2011

NOTE 5 – FAIR VALUE MEASUREMENTS

GAAP emphasizes that fair value is a market-based measurement, not an entity-specific measurement. Therefore, a fair value measurement should be determined based on the assumptions that market participants would use in pricing the asset or liability.

As a basis for considering market participant assumptions in fair value measurements, GAAP establishes a three-tier hierarchy to distinguish between various types of inputs used in determining the value of the Organization's financial instruments. The inputs are summarized in three levels as outlined below:

Level 1 Inputs - Quoted prices (unadjusted) in active markets for identical assets and liabilities. Valuations of these instruments do not require a high degree of judgment since the valuations are based on readily available quoted prices in active markets.

Level 2 Inputs - Quoted prices for similar assets or liabilities in active markets; quoted prices for identical or similar assets or liabilities that are not active; and inputs other than quoted prices that are observable, such as models or other valuation methodologies. Valuations in this category are inherently less reliable than quoted market prices due to the degree of subjectivity involved in determining appropriate methodologies and the applicable underlying assumptions.

Level 3 Inputs - Unobservable inputs for the valuation of the asset or liability. Level 3 assets include investments for which there is little, if any, market activity. These inputs require significant management judgment or estimation. These financial instruments have inputs that cannot be validated by readily determinable market data and generally involve considerable judgment by management.

In certain cases, the inputs used to measure fair value may fall into different hierarchy levels. In such cases, for disclosure purposes, the level in the hierarchy within which the fair value measurement in its entirety falls is determined based on the lowest level input that is significant to the fair value measurement. The Region's assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment and considers factors specific to the financial instrument.

Valuation Techniques and Significant Inputs

During 2012, Level II investments consist of open end real estate mutual funds and real estate investment trusts that are valued based on market prices for similar and actively traded investments.

Level III includes the Region's interests in assets held by others. The fair value is based on the value of the Region's portion of the underlying investments in the trusts using valuation methods that are appropriate for those investments as determined by the trustee.

Quantitative information related to valuation inputs is not available since the value of the trusts that was provided by the trustees was used without adjustment. On an annual basis, Region management evaluates the return received from the trusts against the value of its portion of the trusts for reasonableness as compared with current market returns. Management believes that the sensitivity in the fair value measurement of the beneficial interests is related to market fluctuations, as the investments held in the trusts are primarily marketable securities.

ARTHRITIS FOUNDATION, SOUTH CENTRAL REGION, INC.

Notes To Financial Statements

December 31, 2012 with Summarized Information for the Year Ended December 31, 2011

NOTE 5 – FAIR VALUE MEASUREMENTS - Continued

The following tables summarize the valuation of the Region's marketable securities and funds held by others by the above hierarchy levels as of December 31, 2012 and 2011:

	December 31, 2012			
	Level I	Level II	Level III	Total
Common stocks	\$ 5,046	\$ -	\$ -	\$ 5,046
Domestic equity mutual funds				
Energy	89,789	-	-	89,789
Real estate	94,824	-	-	94,824
Other	2,230,210	-	-	2,230,210
Fixed income mutual funds	2,171,759	-	-	2,171,759
Open end mutual funds - real estate	-	10,041	-	10,041
REITs	-	1,299	-	1,299
Total marketable securities	4,591,628	11,340	-	4,602,968
Beneficial interests in assets held by others	-	-	107,094	107,094
Total	<u>\$ 4,591,628</u>	<u>\$ 11,340</u>	<u>\$ 107,094</u>	<u>\$ 4,710,062</u>
	December 31, 2011			
	Level I	Level II	Level III	Total
Corporate notes and bonds	\$ -	\$ 49,908	\$ -	\$ 49,908
Common stocks	1,195	-	-	1,195
International equity mutual funds	10,506	-	-	10,506
Domestic equity mutual funds				
Energy	28,531	-	-	28,531
Technology	1,935,648	-	-	1,935,648
Real estate	46,573	-	-	46,573
Other	403,687	-	-	403,687
Fixed income mutual funds	969,516	-	-	969,516
Mortgage backed securities	50,934	-	-	50,934
Total marketable securities	3,446,590	49,908	-	3,496,498
Beneficial interests in assets held by others	-	-	46,213	46,213
Total	<u>\$ 3,446,590</u>	<u>\$ 49,908</u>	<u>\$ 46,213</u>	<u>\$ 3,542,711</u>

During 2012 and 2011, there were no significant transfers between levels.

ARTHRITIS FOUNDATION, SOUTH CENTRAL REGION, INC.

Notes To Financial Statements

December 31, 2012 with Summarized Information for the Year Ended December 31, 2011

NOTE 5 – FAIR VALUE MEASUREMENTS - Continued

The following table summarizes the Region’s level III reconciliation for the beneficial interests in assets held by others for the years ended December 31, 2012 and 2011.

	<u>2012</u>	<u>2011</u>
Beginning balance	\$ 46,213	\$ 40,014
Contribution of beneficial interest in assets held by others	62,449	-
Net unrealized (loss) gain	<u>(1,568)</u>	<u>6,199</u>
Ending balance	<u>\$107,094</u>	<u>\$ 46,213</u>

NOTE 6 – ENDOWMENTS

The Region's endowment consists of seven donor restricted endowment funds established throughout the South Central Region for the purposes of funding research and supporting operations.

Region management understands Texas’ adoption of the Uniform Prudent Management of Institutional Funds Act (“UPMIFA”) as requiring the preservation of the fair value of the original gift as of the gift date of the donor restricted endowment funds absent explicit donor stipulations to the contrary. The Region classifies 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 applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of donor-restricted endowment fund in excess of the original fair value that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure in a manner consistent with the standard of prudence prescribed by UPMIFA.

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

1. The duration and preservation of the fund
2. The purpose of the Region and the donor-restricted endowment fund
3. General economic conditions
4. The possible effects of inflation and deflation
5. The expected total return from income and the appreciation of investments
6. Other resources of the Region
7. The investment policy of the Region

ARTHRITIS FOUNDATION, SOUTH CENTRAL REGION, INC.

Notes To Financial Statements

December 31, 2012 with Summarized Information for the Year Ended December 31, 2011

NOTE 6 – ENDOWMENTS - Continued

If the market value of any fund classified as permanently restricted at year-end is below the amount determined to be permanently restricted the deficit which cannot be funded from temporarily restricted unspent earnings of the fund are reported as a reduction in unrestricted net assets. There were no such deficiencies noted for the years ended December 31, 2012 and 2011.

The primary long-term financial objective for the Region's endowments is to preserve the real (inflation-adjusted) purchasing power of endowment assets and income after accounting for endowment spending, inflation and costs of portfolio management. Performance of the overall endowment against this objective is measured over rolling periods of one, three and five years. The endowments shall be managed to optimize the long run total rate of return on invested assets, assuming a prudent level of risk. The goal for this rate of return is one that funds the Region's existing spending policy and allows sufficient reinvestment to grow the endowment principal at a rate that exceeds inflation (as measured by the Consumer Price index). Over the short-term, the return for each element of the endowment portfolio should match or exceed each of the returns for the broader capital markets in which assets are invested.

As the earnings on each of the Region's endowments were donor designated for a specific purpose, earnings from the endowment are appropriated for expenditure as needed to fund each of these restricted programs. Spending in a given year will reduce the unit value of each endowment element by the amount used for the restricted purpose designated by the donor of each specific endowment. In no case will funds designated as True Endowment be reduced below their initial unit value. Growth of the unit values over time should allow for spending of principal without drawing from the original corpus of a particular gift.

The endowment is divided into three broad asset classes: equity fund, fixed income fund and cash or near-cash fund. The purpose of dividing the endowment fund in this way is to ensure that the optimal long-term return is achieved given the Region's risk preference.

The purpose of diversification is to provide reasonable assurance that no single security or class of securities will have a disproportionate impact on the total endowment and to reduce the overall risk and volatility of the entire portfolio. The total endowment will be monitored on a continual basis for consistency of investment philosophy, return relative to objectives and asset allocation with respect to target percentages.

ARTHRITIS FOUNDATION, SOUTH CENTRAL REGION, INC.

Notes To Financial Statements

December 31, 2012 with Summarized Information for the Year Ended December 31, 2011

NOTE 6 – ENDOWMENTS - Continued

Endowment net assets are restricted by donors for investment or specific purposes and are reflected by type of fund as of December 31, 2012 and 2011 as follows:

	<u>2012</u>	<u>2011</u>
Temporarily restricted	\$ 795,813	\$ 537,052
Permanently restricted	<u>1,837,079</u>	<u>1,832,079</u>
Total	<u>\$ 2,632,892</u>	<u>\$ 2,369,131</u>

The change in endowment net assets for the years ended December 31, 2012 and 2011 is as follows:

	<u>December 31, 2012</u>		
	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Endowment net assets, beginning of the year	\$ 537,052	\$ 1,837,079	\$ 2,374,131
Investment return:			
Investment income	50,711	-	50,711
Net appreciation	<u>219,836</u>	<u>-</u>	<u>219,836</u>
Total investment return	270,547	-	270,547
Appropriation of endowment assets for current operations	<u>(11,786)</u>	<u>-</u>	<u>(11,786)</u>
Endowment net assets, end of the year	<u>\$ 795,813</u>	<u>\$ 1,837,079</u>	<u>\$ 2,632,892</u>
	<u>December 31, 2011</u>		
	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Endowment net assets, beginning of the year	\$ 459,933	\$ 650,386	\$ 1,110,319
Contribution from acquisition	99,190	1,072,500	1,171,690
Other contributions	-	114,193	114,193
Investment return:			
Investment income	6,146	-	6,146
Net depreciation	<u>(19,606)</u>	<u>-</u>	<u>(19,606)</u>
Total investment return	(13,460)	-	(13,460)
Appropriation of endowment assets for current operations	<u>(8,611)</u>	<u>-</u>	<u>(8,611)</u>
Endowment net assets, end of the year	<u>\$ 537,052</u>	<u>\$ 1,837,079</u>	<u>\$ 2,374,131</u>

ARTHRITIS FOUNDATION, SOUTH CENTRAL REGION, INC.

Notes To Financial Statements

December 31, 2012 with Summarized Information for the Year Ended December 31, 2011

NOTE 7 – CONTRIBUTIONS RECEIVABLE

The Region had the following contributions receivable at December 31, 2012 and 2011:

	<u>2012</u>	<u>2011</u>
Amount due in:		
Less than one year	\$ 55,509	\$ 124,335
One to five years	<u>62,780</u>	<u>100,555</u>
Gross contributions receivable	118,289	224,890
Allowance for doubtful accounts	(12,941)	(21,598)
Unamortized present value discount	<u>(862)</u>	<u>(1,472)</u>
Net contributions receivable	<u>\$ 104,486</u>	<u>\$ 201,820</u>

Contributions receivable are net of unamortized present value discount calculated at the date of donation using rates between one and three percent.

NOTE 8 – BENEFICIAL INTERESTS IN ASSETS HELD BY OTHERS

At December 31, 2012 and 2011, the Region had \$107,094 and \$46,213, respectively, in funds held by others. These assets are reported on the statement of financial position and are valued at fair value. All net realized and unrealized gains are reported on the statement of activities as permanently restricted income, as appreciation in such funds is not available for expenditure by the Region.

NOTE 9 – CHARITABLE REMAINDER TRUSTS

The Region is a beneficiary under several charitable remainder trusts. Under these agreements, the Region will receive the assets of the trusts upon their expirations. Until that time, the life income beneficiary receives some portion of the income. The assets of this trust are held by an outside trustee and are valued at fair value. The Region records an interest in the net assets held in the trust measured at the present value of the distributions expected to be received using discount rates and actuarial assumptions which consider the donor's life expectancy and the rates typically earned on those investments. In the current year, the Region recorded an interest of \$266,294 in the net assets held in a trust based on the Region's percentage ownership of the trust. Net realized and unrealized gains in this interest are reported on the statement of activities as temporarily restricted income. Discount rates for these trusts range from one to two percent.

ARTHRITIS FOUNDATION, SOUTH CENTRAL REGION, INC.

Notes To Financial Statements

December 31, 2012 with Summarized Information for the Year Ended December 31, 2011

NOTE 10 – PROPERTY AND EQUIPMENT

Property and equipment consisted of the following at December 31, 2012 and 2011:

	<u>2012</u>	<u>2011</u>
Leasehold improvements (useful life 3-10 years)	\$ 22,476	\$ 22,476
Furniture and other equipment (useful life 3-5 years)	77,552	77,552
Accumulated depreciation	<u>(87,356)</u>	<u>(81,273)</u>
Net property and equipment	<u>\$ 12,672</u>	<u>\$ 18,755</u>

Depreciation expense was \$6,083 and \$3,582 for the year ended December 31, 2012 and 2011, respectively.

NOTE 11 – ACCRUED EXPENSES AND OTHER LIABILITIES

Accrued expenses and other liabilities consisted of the following at December 31, 2012 and 2011:

	<u>2012</u>	<u>2011</u>
Vacation	\$ 59,567	36,263
Other	<u>18,075</u>	<u>18,911</u>
Total accrued expenses and other liabilities	<u>\$ 77,642</u>	<u>\$ 55,174</u>

NOTE 12 – JOINT COSTS

In 2012 and 2011, the Region incurred joint costs in services provided by the National Office such as the direct mail program and other activities. Informational materials distributed in these programs included both public health education components and fundraising appeals which have been functionally allocated on the statement of activities using percentages provided by the National Office. Joint costs for the years ended December 31, 2012 and 2011 were as follows:

	<u>2012</u>	<u>2011</u>
Public health education	\$ 206,851	\$ 170,379
Fundraising	<u>72,677</u>	<u>73,019</u>
	<u>\$ 279,528</u>	<u>\$ 243,398</u>

ARTHRITIS FOUNDATION, SOUTH CENTRAL REGION, INC.

Notes To Financial Statements

December 31, 2012 with Summarized Information for the Year Ended December 31, 2011

NOTE 13 – NET ASSETS

Temporarily restricted net assets at December 31, 2012 and 2011 were available for the following purposes:

	<u>2012</u>	<u>2011</u>
Specific programs conducted by the Region	\$ 1,877,298	\$ 1,665,438
Research	875,457	679,425
Use in future periods	<u>241,277</u>	<u>166,959</u>
	<u>\$ 2,994,032</u>	<u>\$ 2,511,822</u>

Permanently restricted net assets consisted of the following at December 31, 2012 and 2011 and represent endowed gifts to be held in perpetuity with the investment income to be used for:

	<u>2012</u>	<u>2011</u>
Research and specific projects	\$ 1,837,079	\$ 1,837,079
Beneficial interest in assets held by others	<u>107,094</u>	<u>46,213</u>
	<u>\$ 1,944,173</u>	<u>\$ 1,883,292</u>

Temporarily restricted net assets released from donor and time restrictions consisted of the following in the years ended December 31, 2012 and 2011:

	<u>2012</u>	<u>2011</u>
Specific programs conducted by the Region	\$ 271,289	\$ 188,100
Scholarships, training and projects	-	2,500
Research	87,572	399,324
Time releases	<u>179,987</u>	<u>144,152</u>
	<u>\$ 538,848</u>	<u>\$ 734,076</u>

ARTHRITIS FOUNDATION, SOUTH CENTRAL REGION, INC.

Notes To Financial Statements

December 31, 2012 with Summarized Information for the Year Ended December 31, 2011

NOTE 14 – OPERATING LEASES

Rental expense for Region office space was \$193,328 and \$170,911 for the year ended December 31, 2012 and 2011, respectively. Lease agreements having an original term of more than one year expire on various dates through 2016.

Future minimum annual lease payments as of December 31, 2012 are as follows:

<u>For the years ending December 31,</u>	
2013	\$ 177,238
2014	156,592
2015	66,154
2016	<u>32,658</u>
Total future minimum lease payments	<u>\$ 432,642</u>

NOTE 15 – EMPLOYEE BENEFIT PLAN

The Region sponsors a defined contribution retirement plan (the “Plan”) covering substantially all of the employees of the Region. Prior to December 31, 2011, the Region contributed eight to 15 percent of each eligible employee’s compensation as specified in the Plan agreement. Effective January 1, 2012, the Plan was amended, and in accordance with the amended plan, the Region made contributions totaling two percent of each eligible employee’s compensation for the year ended December 31, 2012. Total contributions to the plan for the years ended December 31, 2012 and 2011 were \$19,945 and \$87,662, respectively.

NOTE 16 – SUBSEQUENT EVENTS

The Region has evaluated subsequent events for potential recognition and /or disclosure in the December 31, 2012 financial statements through March 22, 2013, the date that the financial statements were available to be issued.