

Michigan State Bar Foundation Report on Financial Statements

Years Ended September 30, 2006 and 2005

Independent Auditors' Report

Board of Trustees
Michigan State Bar Foundation
Lansing, Michigan

We have audited the accompanying statements of financial position of Michigan State Bar Foundation as of September 30, 2006 and 2005 and the related statements of activities and cash flows for the years then ended. These financial statements are the responsibility of the Foundation's management. 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 includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Michigan State Bar Foundation as of September 30, 2006 and 2005, and the changes in its net assets and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

Maner, Costerisan & Ellis, P.C.
Certified Public Accountants
Lansing, Michigan
December 4, 2006

MICHIGAN STATE BAR FOUNDATION STATEMENTS OF FINANCIAL POSITION

September 30, 2006 and 2005

ASSETS	2006	2005
CURRENT ASSETS:		
Cash and cash equivalents	\$ 2,318,105	\$ 735,255
Marketable debt and equity securities	3,271,642	2,846,501
Accounts receivable—IOLTA	409,666	164,469
Accounts receivable	57,325	25,836
Unconditional promises to give	155,003	134,013
Accrued interest receivable	26,352	16,105
Prepaid expenses	4,608	4,488
TOTAL CURRENT ASSETS	6,242,701	3,926,667
UNCONDITIONAL PROMISES TO GIVE, less current portion	266,583	229,614
LONG-TERM INVESTMENTS	1,045,523	1,011,742
EQUIPMENT, net	13,531	14,583
TOTAL ASSETS	\$ 7,568,338	\$ 5,182,606
LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES:		
Accounts payable:		
General	\$ 32,944	\$ 5,075
State Bar	12,887	27,627
Grants payable	869,370	715,602
IOLTA payable	564,023	172,867
TOTAL CURRENT LIABILITIES	1,479,224	921,171
NET ASSETS:		
Unrestricted	895,942	1,302,728
Unrestricted, board designated	500,000	
TOTAL UNRESTRICTED	1,395,942	
Temporarily restricted	3,647,649	1,946,965
Permanently restricted	1,045,523	1,011,742
TOTAL NET ASSETS	6,089,114	4,261,435
TOTAL LIABILITIES AND NET ASSETS	\$ 7,568,338	\$ 5,182,606

See notes to financial statements.

Notes to Financial Statements

NOTE 1—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of Michigan State Bar Foundation have been prepared on the accrual basis and the AICPA Industry Audit Guide of Not-for-Profit Organizations. The significant accounting policies followed are described below to enhance the usefulness of the financial statements to the reader.

Financial Statement Presentation—The Foundation is required to report information regarding its financial position and activities according to three classes of net assets: unrestricted net assets, temporarily restricted net assets, and permanently restricted net assets and are explained as follows.

- Unrestricted net assets represent the portion of expendable funds available for support of Foundation operations and unrestricted contributions. Currently, the board has designated \$500,000 for future uses.

- Temporarily restricted net assets consist of contributions or earnings, which have been restricted by the donor. Unexpended amounts are included in temporarily restricted net assets. These resources originate from IOLTA activities, the Access to Justice Campaign, gifts, grants, bequests, contracts, emergency appeals, and investment income earned on IOLTA investments. IOLTA revenue is directly affected by changes in interest rates.

Michigan State Bar Foundation Statements of Activities

Years Ended September 30, 2006 and 2005

	2006				2005			
	Unrestricted	Temporarily restricted	Permanently restricted	Total	Unrestricted	Temporarily restricted	Permanently restricted	Total
REVENUE AND OTHER SUPPORT:								
Contributions—IOLTA—net (See Note 7)	\$	\$3,142,054	\$	\$3,142,054	\$	\$1,304,903	\$	\$1,304,903
Fellows memberships		43,384		43,384		74,268		74,268
Access to Justice contributions		844,072	33,781	877,853		552,145	126,753	678,898
Filing fees reimbursement	74,778			74,778	72,986			72,986
Regular memberships	925			925	875			875
Interest	43,750	161,037		204,787	30,004	110,500		140,504
Contributions	29,597	800		30,397	1,000			1,000
Memorials	200	200		200	100			100
Realized gain (loss) on investments	34,542	(21,837)		12,705	41,653	2,271		43,924
Net assets released from restrictions	2,523,107	(2,523,107)			2,346,841	(2,346,841)		
TOTAL REVENUE AND OTHER SUPPORT	2,706,899	1,646,403	33,781	4,387,083	2,493,459	(302,754)	126,753	2,317,458
EXPENSES:								
Program services:								
IOLTA Grants	1,402,085			1,402,085	1,068,557			1,068,557
Fellows program	20,351			20,351	23,230			23,230
Filing fees	105,653			105,653	95,270			95,270
IOLTA Program	438,166			438,166	383,444			383,444
Cohn endowment program	8,500			8,500				
Access to Justice Program	617,506			617,506	659,435			659,435
Other programs	5,000			5,000				
TOTAL PROGRAM SERVICES	2,597,261			2,597,261	2,229,936			2,229,936
Management and general	26,904			26,904	22,936			22,936
TOTAL EXPENSES	2,624,165			2,624,165	2,252,872			2,252,872
Change in net assets before unrealized gain (loss) on current marketable equity securities	82,734	1,646,403	33,781	1,762,918	240,587	(302,754)	126,753	64,586
UNREALIZED GAIN ON CURRENT MARKETABLE EQUITY SECURITIES	10,480	54,281		64,761	98,319	53,043		151,362
CHANGE IN NET ASSETS	93,214	1,700,684	33,781	1,827,679	338,906	(249,711)	126,753	215,948
NET ASSETS, beginning of year	1,302,728	1,946,965	1,011,742	4,261,435	963,822	2,196,676	884,989	4,045,487
NET ASSETS, end of year	\$1,395,942	\$3,647,649	\$1,045,523	\$6,089,114	\$1,302,728	\$1,946,965	\$1,011,742	\$4,261,435

See notes to financial statements.

Notes to Financial Statements (continued)

- Permanently restricted net assets are gift instruments requiring the principal be maintained intact in perpetuity and only the income be used for purposes specified by the donor.

Functional Expenses—Expenses are classified on a functional basis as program services and management and general.

The following is a definition of the Foundation's significant program services:

- IOLTA Program—Grants and related expenses regarding improvements in the administration of justice and civil legal services to the poor.
- Fellows Program—A membership program that generates revenue for the Foundation's public service activities.
- Filing fees—Funds expended to provide grants for civil legal services to the poor.
- Access to Justice Program—Grants and related expenses regarding civil legal services to the poor.
- Cohn Endowment Program—Grants from endowment earnings have typically supported law related education.

- Other Programs—Miscellaneous programs administered by the Foundation.

Cash and cash equivalents consist of cash accounts and money market funds.

Investments—Investments in equity securities and debt securities with readily determinable fair values are reported at fair value with gains and losses included in the statement of activities. Amounts on deposit for investment purposes are not considered cash equivalents for cash flows purposes. Losses on investments of permanently restricted assets in excess of original principal reduce unrestricted net assets. Subsequent related gains are recorded as increases in unrestricted net assets until the gain offsets the amount of losses previously recorded as decreases in net assets.

Accounts Receivable—Accounts receivable are stated at the amount management expects to collect from outstanding balances. Management provides for probable uncollectible amounts through a provision for bad debt expense and an adjustment to a valuation allowance based on its assessment of the current status of individual accounts. Balances that are still

MICHIGAN STATE BAR FOUNDATION
STATEMENTS OF CASH FLOWS

Years Ended September 30, 2006 and 2005

	2006	2005
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS:		
Cash flows from operating activities:		
Change in net assets	\$ 1,827,679	\$ 215,948
Adjustments to reconcile change in net assets to net cash provided (used) by operating activities:		
Depreciation	6,724	8,802
Realized (gain) loss on sale of marketable equity securities	(12,705)	(43,924)
Unrealized (gain) loss on marketable equity securities	(64,761)	(151,362)
Permanently restricted contributions	(33,781)	(126,753)
Accounts receivable	(276,686)	(41,532)
Unconditional promise to give	(57,959)	37,742
Accrued interest receivable	(10,247)	2,136
Prepaid expenses	(120)	(641)
Accounts payable and IOLTA payable	404,285	83,782
Grants payable	153,768	120,520
Total adjustments	<u>108,518</u>	<u>(111,230)</u>
Net cash provided by operating activities	1,936,197	104,718
Cash flows from investing activities:		
Purchase of investments	(1,689,821)	(1,485,669)
Sale of investments	1,308,365	1,288,052
Purchase of property and equipment	(5,672)	(1,530)
Net cash used by investing activities	<u>(387,128)</u>	<u>(199,147)</u>
Cash flows from financing activities:		
Donations of permanently restricted funds	<u>33,781</u>	<u>126,753</u>
NET INCREASE IN CASH AND CASH EQUIVALENTS	1,582,850	32,324
CASH AND CASH EQUIVALENTS:		
Beginning of year	735,255	702,931
End of year	<u>\$2,318,105</u>	<u>\$735,255</u>

See notes to financial statements.

Notes to Financial Statements (continued)

outstanding after management has used reasonable collection efforts are written off through a charge to the valuation allowance and a credit to accounts receivable. See Note 4 for changes in the valuation allowance.

Contributions—Contributions received are recorded as unrestricted, temporarily restricted, or permanently restricted support, depending on the existence or nature of any donor restrictions.

Support that is restricted by the donor is reported as an increase in unrestricted net assets if the restriction expires in the reporting period in which the support is recognized. All other donor-restricted support is reported as an increase in temporarily or permanently restricted net assets, depending on the nature of the restriction. When a restriction expires (that is, when a stipulated time restriction ends or purpose restriction is accomplished), temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of activities as net assets released from restrictions.

Promises to Give—Unconditional promises to give are recognized as revenue in the period the promise is received and as assets, decreases of liabilities, or expenses depending on the form of the benefits received. Promises to give are recorded at net realizable value if they are expected to be collected in one year and at fair value if they are expected to be collected in more than one year. Long-term unconditional promises to give are initially recorded as temporarily restricted assets.

Prepaid expenses consist primarily of advance payments for insurance and maintenance agreements.

Equipment is stated at cost. Depreciation is computed over the estimated useful lives of the assets on the straight-line method and the Foundation's capitalization policy is \$1,000.

Contract services for personnel consist of reimbursement to other entities for services provided to the Foundation. These personnel are covered under the benefit plans of their respective entities.

Reclassifications—Certain prior year amounts have been reclassified to conform to the current year format for comparative purposes.

NOTE 2—ORGANIZATION, RISKS, AND UNCERTAINTIES

The Michigan State Bar Foundation was formed on September 30, 1947, as a nonprofit corporation under U.S. Internal Revenue Code Section 501(c)(3). Created in recognition of the legal profession's responsibilities to the public, the Foundation provides financial assistance to educational, research, and public service projects that promote advancements in the administration of justice, further a better understanding of our legal system and improve relations among the legal profession, the courts and the public, and further the delivery of legal services to the poor. No provision for income taxes is required due to the Foundation's tax-exempt status.

Credit Risk—The Foundation is required to disclose significant concentrations of credit risk regardless of the degree of such risk. Financial instruments, which potentially subject the Foundation to concentrations of credit risk, consist principally of cash and investments, promises to give, and accounts receivable.

The Foundation places its cash and investments with high credit quality financial institutions. Although such investments and cash balances exceeded the federally insured limits at certain times during the year and at year-end they are, in the opinion of management, subject to minimal risk.

The process of preparing financial statements in conformity with accounting principles generally accepted in the United States of America requires the use of estimates and assumptions regarding certain types of assets, liabilities, revenues, and expenditures. Such estimates primarily relate to unsettled transactions and events as of the date of the financial statements. Accordingly, upon settlement, actual results may differ from estimated amounts.

NOTE 3—INVESTMENTS

The fair values of investments are estimated based on quoted market prices for those of similar investments. Investments consist of traded securities on the New York Stock Exchange and U.S. Governmental Securities.

	Cost	Market	Unrealized gain (loss)
Investments:			
September 30, 2006:			
Government and corporate debt securities	\$2,524,499	\$2,470,370	\$(54,129)
Equities	<u>1,244,095</u>	<u>1,846,795</u>	<u>602,700</u>
Total	<u>\$3,768,594</u>	<u>\$4,317,165</u>	<u>\$548,571</u>
September 30, 2005:			
Government and corporate debt securities	\$2,255,122	\$2,176,824	\$(78,298)
Equities	<u>1,119,312</u>	<u>1,681,419</u>	<u>562,107</u>
Total	<u>\$3,374,434</u>	<u>\$3,858,243</u>	<u>\$483,809</u>

Investments are presented as follows:

	2006	2005
Marketable debt and equity securities	\$3,271,642	\$2,846,501
Long-term investments	<u>1,045,523</u>	<u>1,011,742</u>
	<u>\$4,317,165</u>	<u>\$3,858,243</u>

NOTE 4—UNCONDITIONAL PROMISES TO GIVE

	2006			
	Access to Justice	Fellows program	Total	2005
Gross amounts due in:				
Less than one year	\$118,862	\$63,300	\$182,162	\$145,381
One to five years	117,088	181,600	298,688	255,264
More than five years	<u>33,200</u>	<u>33,200</u>	<u>33,200</u>	<u>36,150</u>
Total	<u>\$235,950</u>	<u>\$278,100</u>	<u>\$514,050</u>	<u>\$436,795</u>

NOTE 4—UNCONDITIONAL PROMISES TO GIVE (continued)

Current portion—net	\$99,901	\$55,102	\$155,003	\$134,013
Long-term portion—net	<u>109,755</u>	<u>156,828</u>	<u>266,583</u>	<u>229,614</u>
	\$209,656	\$211,930	\$421,586	\$363,627

The discount rate used was 5% and 4% for 2006 and 2005, respectively.

The above amounts are net of an allowance for uncollectible amounts of \$28,221 and \$30,771 at September 30, 2006 and 2005, respectively.

NOTE 5—EQUIPMENT AND DEPRECIATION

Equipment at September 30 consists of the following:

	2006	2005
Computers and equipment	\$55,954	\$50,283
Office furniture	<u>12,040</u>	<u>12,040</u>
	67,994	62,323
Less accumulated depreciation	<u>54,463</u>	<u>47,740</u>
Equipment—net	\$13,531	\$14,583
Depreciation expense	\$ 6,724	\$ 8,802

NOTE 6—NET ASSETS RELEASED FROM RESTRICTIONS

Net assets were released from donor restrictions by incurring expenses or satisfying the restricted purposes.

Purpose and time restrictions accomplished and other items:

	2006	2005
IOLTA—grants	\$1,402,085	\$1,068,557
IOLTA expenses	<u>438,166</u>	<u>383,444</u>
Fellows memberships	56,850	64,250
Cohn Endowment	8,500	
Access to Justice Program grants and expenses	<u>617,506</u>	<u>659,435</u>
Release of assets due to time restrictions and other		<u>171,155</u>
	\$2,523,107	\$2,346,841

Temporarily restricted net assets at year-end consist of the following:

	2006	2005
IOLTA program	\$2,841,561	\$1,433,913
Fellows memberships to be collected	<u>211,930</u>	<u>225,396</u>
Franck program	60,216	55,998
Cohn Endowment and memorial programs	2,096	6,444
Access to Justice Program time and purpose restrictions	<u>529,396</u>	<u>223,564</u>
Special programs	<u>2,450</u>	<u>1,650</u>
	\$3,647,649	\$1,946,965

Permanently restricted net assets at year-end consist of the following:

	2006	2005
Access to Justice Program	\$ 995,523	\$ 961,742
Cohn Endowment	<u>50,000</u>	<u>50,000</u>
	\$ 1,045,523	\$1,011,742

NOTE 7—ENDOWMENT AND RESTRICTED ACTIVITIES

Cohn Endowment Program—The principal of the Irwin I. Cohn Endowment Fund shall be kept intact under all circumstances. Any income or capital gains generated from the principal may be used.

Access to Justice—Program to increase resources for civil legal services for low-income persons. The principal can be permanently restricted by option of the donor. Temporarily restricted contributions and income are restricted for the purpose of the program.

Franck Program—(Michael Franck Fund for Professional Responsibility) The income and principal are restricted to the furtherance of professional responsibility.

IOLTA Program (Interest on Lawyer's Trust Accounts)—The Michigan Supreme Court issued Administrative Order 1990-2 that the Board of Trustees of the Michigan State Bar Foundation would administer the IOLTA Program established pursuant to amendment of Rule 1.15 of the Michigan Rules of Professional Conduct (MRPC). Administrative Order 1997-9, effective No-

ember 14, 1997, modified Order 1990-2. The Michigan Supreme Court also adopted amendments to MRPC 1.15, effective October 18, 2005.

After administrative expenses, the IOLTA funds are to be distributed by the Foundation in accordance with administrative orders issued by the Michigan Supreme Court. Under the current order, IOLTA funds distributed to the Michigan Supreme Court for Gender and Racial/Ethnic issues and to the Michigan Supreme Court Historical Society are reported in an agency capacity.

The following is a summary of the IOLTA activity for the years ended September 30:

	2006	2005
IOLTA funds (accrual basis)	\$3,626,870	\$1,468,642
Less allocation for Gender and Racial/Ethnic Issues and Supreme Court Historical Society	<u>(484,816)</u>	<u>(163,739)</u>
IOLTA revenue—net of funds received in an agency capacity	\$3,142,054	\$1,304,903

Calculation of funds received in an agency capacity:

	2006	2005
IOLTA funds (accrual basis)	\$3,626,870	\$1,468,642
Administrative expenses and investment activity	<u>(475,514)</u>	<u>(407,079)</u>
IOLTA funds—net	\$3,151,356	\$1,061,563

	2006		
	Gender and Racial/Ethnic Issues	Supreme Court Historical Society	Total IOLTA Payable
IOLTA funds—net	\$3,151,356	\$3,151,356	\$3,151,356
Allocation per administrative order	<u>10%</u>	<u>5%</u>	<u>15%</u>
	315,136	157,568	472,704
Allocation of accumulated funds at beginning of year	118,676	54,191	72,867
Interest earned	<u>9,266</u>	<u>2,846</u>	<u>12,112</u>
Total funds available	443,078	214,605	657,683
Payments made	<u>(39,469)</u>	<u>(54,191)</u>	<u>(93,660)</u>
IOLTA payable, end of year	\$403,609	\$160,414	\$564,023

	2005		
	Gender and Racial/Ethnic Issues	Supreme Court Historical Society	Total IOLTA Payable
IOLTA funds—net	\$1,061,563	\$1,061,563	\$1,061,563
Allocation per administrative order	<u>10%</u>	<u>5%</u>	<u>15%</u>
	106,156	53,078	159,234
Allocation of accumulated funds at beginning of year	57,855	36,683	94,538
Interest earned	<u>3,210</u>	<u>1,112</u>	<u>4,322</u>
Total funds available	167,221	90,873	258,094
Payments made	<u>(48,545)</u>	<u>(36,682)</u>	<u>(85,227)</u>
IOLTA payable, end of year	\$118,676	\$54,191	\$172,867

NOTE 8—LEASED FACILITIES

Facilities are leased under agreements running through September 30, 2010. Rental expense for the year ended September 30, 2006 and 2005 was approximately \$31,744 and \$31,099, respectively. Minimum future rental amounts are calculated on the base monthly rent amount. The rent payment is adjusted annually by the Consumer Price Index. The maximum annual increase per adjustment is 10%.

Minimum future rentals under this lease are as follows:

Year ending September 30,	
2007	\$ 31,744
2008	31,744
2009	31,744
2010	<u>31,744</u>
Total	\$126,976