

Consolidated Financial Statements

Animal Humane Society and Subsidiaries

Golden Valley, Minnesota

For the Year Ended June 30, 2018
(With Comparative Totals for the Year Ended June 30, 2017)

Animal Humane Society and Subsidiaries
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June 30, 2018
(With Comparative Totals as of June 30, 2017)

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INDEPENDENT AUDITOR'S REPORT

Board of Directors
Animal Humane Society and Subsidiaries
Golden Valley, Minnesota

We have audited the accompanying consolidated financial statements of Animal Humane Society and Subsidiaries, which comprise the consolidated statement of financial position as of June 30, 2018, and the related consolidated 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 Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of the consolidated 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 consolidated 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 consolidated 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 consolidated financial statements are free of material misstatement.

An audit includes performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including assessment of the risks of material misstatement of the consolidated 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 consolidated 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 consolidated financial statements.

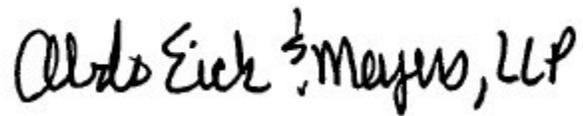
We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Animal Humane Society and Subsidiaries as of June 30, 2018, and the changes in its net assets and cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Report on Summarized Comparative Information

We have previously audited Animal Humane Society and Subsidiaries' June 30, 2017 consolidated financial statements, and we expressed an unmodified audit opinion on those audited consolidated financial statements in our report dated October 4, 2017. In our opinion, the summarized comparative information presented herein as of and for the year ended June 30, 2017, is consistent, in all material respects, with the audited consolidated financial statements from which it has been derived.

A handwritten signature in black ink that reads "Aldo Eick & Meyers, LLP". The signature is written in a cursive, flowing style.

ABDO, EICK & MEYERS, LLP
Minneapolis, Minnesota
October 19, 2018

CONSOLIDATED FINANCIAL STATEMENTS

Animal Humane Society and Subsidiaries
Consolidated Statement of Financial Position
June 30, 2018
(With Comparative Totals as of June 30, 2017)

	2018	2017
Assets		
Current Assets		
Cash and cash equivalents	\$ 2,908,508	\$ 2,045,861
Accounts receivable	83,251	190,001
Pledges receivable, short-term	10,000	10,000
Inventory	219,905	280,794
Prepaid expenses and other current assets	193,361	416,353
Total Current Assets	3,415,025	2,943,009
Investments	7,766,952	7,070,392
Property and Equipment		
Land	5,836,754	1,021,127
Buildings and leasehold improvements	25,545,060	22,157,333
Equipment and vehicles	1,519,223	1,601,849
Construction in process	453,252	145,241
Office equipment and furnishings	828,321	655,656
Total Property and Equipment, Cost	34,182,610	25,581,206
Accumulated Depreciation	(12,867,379)	(12,138,792)
Total Property and Equipment, Net	21,315,231	13,442,414
Noncurrent Assets		
Pledges receivable, long-term, net	28,765	18,319
Amounts held in trust	603,066	599,484
Unemployment funds held by others	65,602	77,881
Cash surrender value of life insurance	42,763	42,732
Total Noncurrent Assets	740,196	738,416
Total Assets	\$ 33,237,404	\$ 24,194,231

See Independent Auditor's Report and Notes to the Consolidated Financial Statements.

Animal Humane Society and Subsidiaries
Consolidated Statement of Financial Position (Continued)
June 30, 2018
(With Comparative Totals as of June 30, 2017)

	2018	2017
Liabilities and Net Assets		
Current Liabilities		
Accounts payable	\$ 231,877	\$ 171,635
Notes payable, current portion	-	154,095
Deferred revenue, current portion	241,536	213,922
Accrued liabilities	260,108	199,782
Accrued payroll expenses	967,230	843,944
Adoption credit vouchers	208,402	165,581
Total Current Liabilities	1,909,153	1,748,959
Noncurrent Liabilities		
Notes payable, long-term, net of deferred financing costs of \$102,842 and \$24,481, in 2018 and 2017, respectively	11,147,158	3,313,161
Gift annuities payable	119,832	133,020
Deferred revenue, long-term	183,518	223,558
Total Noncurrent Liabilities	11,450,508	3,669,739
Total Liabilities	13,359,661	5,418,698
Net Assets		
Unrestricted		
Program expansion and operating reserve	9,279,441	8,924,100
AHS property and equipment	12,386,348	11,554,705
Now Boarding equity (accumulated deficit)	(5,792,436)	(5,336,757)
Total Unrestricted	15,873,353	15,142,048
Temporarily restricted	891,202	1,147,008
Permanently restricted	3,113,188	2,486,477
Total Net Assets	19,877,743	18,775,533
Total Liabilities and Net Assets	\$ 33,237,404	\$ 24,194,231

See Independent Auditor's Report and Notes to the Consolidated Financial Statements.

Animal Humane Society and Subsidiaries
Consolidated Statement of Activities
For the Year Ended June 30, 2018
(With Comparative Totals for the Year Ended June 30, 2017)

	2018			2017
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Support and Revenue				
Support				
Contributions	\$ 7,250,560	\$ 7,120	\$ 620,990	\$ 7,878,670
In-kind contributions	317,385	-	-	317,385
Bequests	4,547,033	-	-	4,547,033
Total Support	<u>12,114,978</u>	<u>7,120</u>	<u>620,990</u>	<u>12,743,088</u>
Revenue				
Adoption fees	4,664,278	-	-	4,664,278
Other program revenue	2,737,073	-	-	2,737,073
Boarding fees	458,742	-	-	458,742
Merchandise sales				
Merchandise revenue	1,235,018	-	-	1,235,018
Cost of good sold	(522,719)	-	-	(522,719)
Special events				
Revenue	1,521,995	-	-	1,521,995
Expenses	(599,390)	-	-	(599,390)
Interest and dividend income	166,836	-	-	166,836
Investment gains	253,298	-	-	253,298
Other revenue	40,395	-	-	40,395
Total Revenue	<u>9,955,526</u>	<u>-</u>	<u>-</u>	<u>9,955,526</u>
Net Assets Released From Restrictions	<u>266,443</u>	<u>(266,443)</u>	<u>-</u>	<u>-</u>
Total Support and Revenue	<u>\$ 22,336,947</u>	<u>\$ (259,323)</u>	<u>\$ 620,990</u>	<u>\$ 22,698,614</u>
				<u>10,822,276</u>

See Independent Auditor's Report and Notes to the Consolidated Financial Statements.

Animal Humane Society and Subsidiaries
Consolidated Statement of Activities (Continued)
For the Year Ended June 30, 2018
(With Comparative Totals for the Year Ended June 30, 2017)

	2018			2017	
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total	Total
Expenses					
Program Services					
Adoption and surrender	\$ 12,323,003	\$ -	\$ -	\$ 12,323,003	\$ 11,732,994
Animal rescue and outreach	3,113,161	-	-	3,113,161	2,973,646
Pet services	1,051,655	-	-	1,051,655	1,035,702
Total Program Services	<u>16,487,819</u>	<u>-</u>	<u>-</u>	<u>16,487,819</u>	<u>15,742,342</u>
Supporting Services					
General and administrative	1,028,110	-	-	1,028,110	1,070,034
Capital Campaign	315,967	-	-	315,967	-
Fundraising	3,390,441	-	-	3,390,441	3,022,851
Total Supporting Services	<u>4,734,518</u>	<u>-</u>	<u>-</u>	<u>4,734,518</u>	<u>4,092,885</u>
Total Expenses	<u>21,222,337</u>	<u>-</u>	<u>-</u>	<u>21,222,337</u>	<u>19,835,227</u>
Change In Net Assets From Operations	<u>1,114,610</u>	<u>(259,323)</u>	<u>620,990</u>	<u>1,476,277</u>	<u>660,608</u>
Other Changes - Increase (Decrease)					
Change in value of trusts and insurance policies	-	3,517	5,721	9,238	27,781
Now Boarding, Inc.:					
Revenue	1,916,999	-	-	1,916,999	1,879,181
Expenses	(2,299,830)	-	-	(2,299,830)	(2,183,766)
Kasota Holdings, LLC:					
Revenue	291,425	-	-	291,425	-
Expenses	(291,319)	-	-	(291,319)	-
Provision for income taxes	(580)	-	-	(580)	(600)
Total Other Changes	<u>(383,305)</u>	<u>3,517</u>	<u>5,721</u>	<u>(374,067)</u>	<u>(277,404)</u>
Change In Net Assets	731,305	(255,806)	626,711	1,102,210	383,204
Net Assets, Beginning of the Year	<u>15,142,048</u>	<u>1,147,008</u>	<u>2,486,477</u>	<u>18,775,533</u>	<u>18,392,329</u>
Net Assets, End of the Year	<u>\$ 15,873,353</u>	<u>\$ 891,202</u>	<u>\$ 3,113,188</u>	<u>\$ 19,877,743</u>	<u>\$ 18,775,533</u>

See Independent Auditor's Report and Notes to the Consolidated Financial Statements.

Animal Humane Society and Subsidiaries
Consolidated Statement of Functional Expenses
For the Year Ended June 30, 2018
(With Comparative Totals for the Year Ended June 30, 2017)

	2018								2017	
	Program Services				Supporting Services				Total Expenses	
	Adoption & Surrender	Animal Rescue and Outreach	Pet Services	Total Program	General & Administrative	Capital Campaign	Fundraising	Total Support		
Personnel Expenses										
Salaries	\$ 7,271,028	\$ 1,944,808	\$ 723,229	\$ 9,939,065	\$ 579,316	\$ 46,158	\$ 1,535,914	\$ 2,161,388	\$ 12,100,453	\$ 11,204,577
Payroll taxes	575,800	153,371	57,213	786,384	48,248	3,322	119,751	171,321	957,705	876,936
Employee benefits	737,908	195,299	66,316	999,523	50,640	14,763	146,805	212,208	1,211,731	1,164,303
Staff expenses	118,249	27,112	11,104	156,465	31,757	6,289	33,584	71,630	228,095	250,717
Total Personnel Expenses	8,702,985	2,320,590	857,862	11,881,437	709,961	70,532	1,836,054	2,616,547	14,497,984	13,496,533
Expenses										
Advertising	-	-	-	-	-	29,875	263,413	293,288	293,288	250,341
General program supplies	1,064,429	311,163	15,623	1,391,215	976	1,061	28,091	30,128	1,421,343	1,622,806
Insurance	59,822	15,345	5,377	80,544	4,105	1,197	11,901	17,203	97,747	96,402
Office supplies	112,586	11,284	9,111	132,981	6,026	3,152	7,145	16,323	149,304	138,458
Other outside services	627,440	211,604	30,767	869,811	39,000	189,923	668,691	897,614	1,767,425	1,528,434
Postage	8,726	4,932	285	13,943	34,988	196	222,747	257,931	271,874	256,684
Printing	44,339	31,829	6,361	82,529	62,826	268	125,013	188,107	270,636	238,394
Professional fees	6,910	-	-	6,910	65,097	860	11,166	77,123	84,033	102,841
Repairs and maintenance	356,462	85,453	23,622	465,537	7,247	926	9,209	17,382	482,919	335,899
Telephone	56,687	10,322	5,320	72,329	3,206	242	8,041	11,489	83,818	128,390
Travel	56,795	17,138	4,926	78,859	55,332	315	7,464	63,111	141,970	98,001
Utilities	376,635	22,762	27,728	427,125	8,710	1,087	10,812	20,609	447,734	427,472
Miscellaneous expense	140,663	20,147	3,041	163,851	10,896	13,916	156,664	181,476	345,327	316,646
Total Expenses Before Depreciation	11,614,479	3,062,569	990,023	15,667,071	1,008,370	313,550	3,366,411	4,688,331	20,355,402	19,037,301
Depreciation	708,524	50,592	61,632	820,748	19,740	2,417	24,030	46,187	866,935	797,926
Total Expenses	\$ 12,323,003	\$ 3,113,161	\$ 1,051,655	\$ 16,487,819	\$ 1,028,110	\$ 315,967	\$ 3,390,441	\$ 4,734,518	\$ 21,222,337	\$ 19,835,227

See Independent Auditor's Report and Notes to the Consolidated Financial Statements.

Animal Humane Society and Subsidiaries
Consolidated Statement of Cash Flows
For the Year Ended June 30, 2018
(With Comparative Totals for the Year Ended June 30, 2017)

	2018	2017
Cash Flows from Operating Activities		
Change in net assets	\$ 1,102,210	\$ 383,204
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation expense	1,185,857	1,090,173
Deferred financing cost interest	29,894	3,865
Net realized and unrealized investment gain	(256,724)	(576,376)
Contributions to endowment fund	(620,990)	(29,484)
Loss on disposal of assets	971	5,662
Change in assets and liabilities:		
Accounts receivable	106,750	3,700
Pledges receivable	(10,446)	9,764
Inventory	60,889	13,253
Prepaid expenses and other current assets	222,992	(191,135)
Amounts held in trusts	(3,582)	(22,445)
Unemployment funds held by others	12,279	7,734
Cash surrender value of life insurance	(31)	(1,738)
Accounts payable	60,242	(85,940)
Accrued liabilities	60,326	43,660
Accrued payroll expenses	123,286	61,008
Deferred revenue	(12,426)	(24,258)
Gift certificates	42,821	24,026
Net Cash Provided by Operating Activities	2,104,318	714,673
Cash Flows from Investing Activities		
Purchases of property and equipment	(1,759,645)	(395,230)
Proceeds from sales of investments	76,750	1,155,000
Purchases of investments	(516,586)	(278,292)
Net Cash Provided by (Used for) Investing Activities	(2,199,481)	481,478
Cash Flows from Financing Activities		
Proceeds from issuance of notes payable	417,133	-
Principal payments on notes payable	(67,125)	(146,111)
Endowment fund contributions	620,990	29,484
Receipts for gift annuities	3,784	-
Payments on gift annuities	(16,972)	(10,975)
Net Cash Provided by (Used for) Financing Activities	957,810	(127,602)
Change in Cash and Cash Equivalents	862,647	1,068,549
Cash and Cash Equivalents at Beginning of Year	2,045,861	977,312
Cash and Cash Equivalents at End of Year	\$ 2,908,508	\$ 2,045,861
Supplemental Disclosure of Cash Flow Information		
Cash paid during the year for:		
Interest	\$ 243,571	\$ 144,506
Income tax	\$ 95,895	\$ 19,698
Supplemental Disclosure of Noncash Investing and Financing Activities		
Disposals of depreciated equipment	\$ 458,241	\$ 100,621
Property and equipment purchased through financing	\$ 7,300,000	\$ -

See Independent Auditor's Report and Notes to the Consolidated Financial Statements.

Animal Humane Society and Subsidiaries
Notes to the Consolidated Financial Statements
June 30, 2018
(With Comparative Totals as of June 30, 2017)

Note 1: Summary of Significant Accounting Policies

A. Organization and Purpose

Animal Humane Society and Subsidiaries (AHS) has been providing services since 1878 and was incorporated as a nonprofit charitable organization in 1891. AHS's mission is to engage the hearts, hands and minds of the community to help animals. Our vision is to compassionately and responsibly create a more humane world for animals. Three core values guide AHS as an organization: be good to animals, partner with people, and lead responsibly with compassion. These values guide AHS decisions in working with people and animals in the community. AHS is primarily supported through donations, adoption and other service fees, and sales of pet care supplies.

AHS has locations in Golden Valley, Coon Rapids, Saint Paul, and Woodbury, Minnesota. AHS maintains three wholly owned subsidiaries: Now Boarding, Inc., Kindest Cut, P.C., and Kasota Holdings, LLC. Now Boarding, Inc. is a for-profit subsidiary that operates a premier pet boarding and daycare facility located near Minneapolis-St. Paul International Airport in Minneapolis. Now Boarding, Inc. plays a key role in helping AHS fulfill its mission of providing quality animal care and in spreading awareness of AHS to a market segment that otherwise might not be familiar with the work of AHS. Kindest Cut, P.C. is a non-profit subsidiary that provides high-quality, low-cost neuter and spay services for pets of people in need, military personnel and veterans, feral cat caretakers, and nonprofit rescue organizations. Kasota Holdings, LLC is a non-profit single-member limited liability company that maintains rental units in St. Paul, Minnesota. AHS is the single-member owner of Kasota Holdings, LLC.

In fiscal year 2018, AHS continued its multi-year work to advance benefits to animals in progressive ways. AHS continues to identify and expand medical and behavioral treatments that improve an animal's eligibility for placement. Although many animals can be placed in our adoption programs as soon as they are vaccinated and sterilized, others require specialized care to overcome health and behavior issues. AHS provides extensive medical treatment, surgery, behavior modification, and foster care to those with special challenges, ensuring that even the most difficult-to-place animals have a chance at adoption.

AHS also began testing a new model for housing dogs in a newly constructed habitat prototype in our Golden Valley adoption center. Dogs are social animals, and housing them in solitary kennels in environments that are flooded with sensory information - like the sounds and smells of other dogs - can contribute to stress and anxiety. AHS's vision is to build group housing where dogs can exhibit a full range of natural behaviors, including socialization and play. The prototype will also offer dogs and potential adopters the chance to interact in a more comfortable environment. What AHS learns from this innovative space could change the way dogs are housed in animal shelters in the future.

Animal Humane Society and Subsidiaries provides an extensive variety of services:

Adoption and Surrender - AHS helps thousands of dogs, cats, and critters in need find loving homes each year - and no animal is ever turned away. AHS takes in every animal surrendered regardless of its health, age, breed, or behavior. This commitment to open admission guarantees shelter and care to thousands of animals that would otherwise have no safe refuge.

The success of Animal Humane Society's shelter program is reflected in three key measures: the total number of animals admitted for rehoming, the percentage of animals with live placements (placement rate), and the average length of stay in shelter. AHS continues to achieve strong results across all three metrics.

In the year ended June 30, 2018:

- 23,634 companion animals came into AHS facilities.
- 22,296 of those animals - more than 95.2% - were placed in homes, reunited with owners, or released to other organizations.
- Average length of stay for animals in shelter was 10.1 days.

Placements included 19,486 animals adopted, 889 animals reunited with owners, 796 cats returned to field, and 1,125 animals transferred to partner organizations.

Animal Humane Society and Subsidiaries
Notes to the Consolidated Financial Statements
June 30, 2018
(With Comparative Totals as of June 30, 2017)

Note 1: Summary of Significant Accounting Policies (Continued)

Robust medical and behavioral programs contribute to this continued success:

- 13,446 animals received spay/neuter surgeries prior to adoption and 11,198 more were sterilized for pet owners and other rescue groups through Kindest Cut P.C.
- AHS veterinarians diagnosed and treated 29,511 conditions.
- AHS Behavior Modification and Rehabilitation programs readied 1,129 cats and dogs for placement.

Community Engagement - AHS works with individuals and organizations across Minnesota to create a more humane world for animals. In the year ended June 30, 2018, those efforts included:

- Outreach to under-engaged communities, including education programs and free or low-cost services that empower low-income pet owners and improve the lives of pets. These programs served more than 7,755 families in Frogtown and East St. Paul. As a result, 1,633 animals received free spay/neuter surgeries and 1,296 pets were served at free wellness clinics.
- Education programs that foster humane values and compassion for animals, including day camps, a youth club, and other activities for kids and families. AHS educational programs served 9,281 people, including 2,028 students through educational programs in schools and 1,236 in summer camps.
- A Community Cats program focused on reducing euthanasia and providing alternative solutions for feral and free-roaming cats through return-to-field and trap-neuter-return programs. This program served 1,187 cats.
- A partnership with the Wildlife Rehabilitation Center of Minnesota that provided emergency care for 141 injured and orphaned wild animals.
- A robust volunteer program that enlists nearly 2,300 active volunteers in providing animal enrichment, foster care, shelter support, and other assistance. Volunteers contributed 147,735 hours to AHS and provided foster care for 2,477 animals prior to adoption.

Pet Services - AHS's offers programs to serve all stages of an animal's life, including:

- Our Kindest Cut P.C. clinics performed 11,198 spay/neuter surgeries and provided 3,953 wellness exams and procedures, all at reduced costs for people in need.
- More than 100 family-friendly pet training classes each week, along with one-on-one training and socialization sessions, therapy animal courses, play groups, and rabbit agility classes. 1,414 pets attended classes through AHS's Training School.
- A free Pet Helpline (952-HELP-PET) that handled 153,696 incoming calls, providing caring, compassionate advice and resources to help with everything from solving behavior problems to finding pet-friendly housing.
- Peace of mind pet boarding at Animal House in Golden Valley, which served 1,101 families and 3,638 pets.
- Compassionate end-of-life services, including owner-requested euthanasia for 2,295 pets and a weekly pet loss support group.
- Online resources for pet owners, including a lost and found pet bulletin board and behavior resource library at animalhumanesociety.org.

Rescue - Providing aid to animals in critical situations is core to AHS's work. AHS's humane agents respond to reports of possible animal cruelty or neglect throughout Minnesota. They receive reports about animals that are lacking proper food, water and shelter. They also participate in larger, more complex cases involving cruelty, with on-site investigations and seizures aiding law enforcement agencies that seek AHS assistance.

During the year ended June 30, 2018, our Humane Investigations unit received 1,494 requests for assistance and opened 545 formal cases. Follow-up investigation of these cases took AHS Agents into 67 counties across the state of Minnesota. Those investigations impacted the lives of 5,753 animals.

AHS took in 9,148 animals from 84 other animal welfare organizations throughout Minnesota and other states, finding homes for animals that would otherwise face euthanasia in overcrowded facilities.

Animal Humane Society and Subsidiaries
Notes to the Consolidated Financial Statements
June 30, 2018
(With Comparative Totals as of June 30, 2017)

Note 1: Summary of Significant Accounting Policies (Continued)

B. Principles of Consolidation

The consolidated financial statements include the accounts of AHS and its wholly owned subsidiaries, Now Boarding, Inc., Kindest Cut, P.C., and Kasota Holdings, LLC. All material inter-organization transactions have been eliminated.

C. Basis of Presentation

The accompanying financial statements have been prepared on the accrual basis of accounting in accordance with generally accepted accounting principles. Revenues are recorded when earned and expenses are recorded when a liability is incurred. Contributions received are recorded as an increase in unrestricted, temporarily restricted, or permanently restricted support depending on the existence or nature of any donor restrictions. Accordingly, net assets of the Organization and related changes are classified and reported as follows:

Unrestricted Net Assets - Those resources subject to the Board of Directors' discretionary control.

Temporarily Restricted Net Assets - Those resources subject to donor imposed restrictions which will be satisfied by actions of the Organization or passage of time. Donor restricted contributions whose restrictions are met in the same reporting period are reported as unrestricted support.

Permanently Restricted Net Assets - Those resources subject to a donor-imposed restriction that they be maintained permanently by the Organization.

The financial statements include certain prior-year summarized comparative information in total but not by net asset class. Such information does not include sufficient detail to constitute a presentation in accordance with generally accepted accounting principles. Accordingly, such information should be read in conjunction with the organization's financial statements for the year ended June 30, 2017, from which the summarized information was derived.

D. Cash and Cash Equivalents

Cash and cash equivalents include all monies in banks and highly liquid investments with maturity dates of less than three months. The carrying value of cash and cash equivalents approximates fair value because of the short maturities of those financial instruments.

Money market funds included with long-term investments are not considered cash equivalents because of their long-term designation by the board of directors.

E. Investments

Investments are generally recorded at fair value based upon quoted market prices, when available, or estimates of fair value. Investment income or loss and unrealized gains or losses are included in the statement of activities as increases or decreases in unrestricted net assets unless the income or loss is restricted by the donor or law.

F. Accounts Receivable

Accounts receivable are reported at the amount the Organization expects to collect on balances outstanding at period end. The Organization monitors outstanding balances and periodically writes off amounts that management determines to be uncollectible. The Organization has concluded that losses from uncollectible accounts at period end will not be significant. Therefore, no allowance has been made for uncollectible accounts. Generally, interest is not charged on past-due accounts.

Animal Humane Society and Subsidiaries
Notes to the Consolidated Financial Statements
June 30, 2018
(With Comparative Totals as of June 30, 2017)

Note 1: Summary of Significant Accounting Policies (Continued)

G. Inventories

Inventories, consisting primarily of pet care supplies, are stated at lower of cost or net realizable value, with cost determined on a first-in, first-out (FIFO) basis.

H. Pledges Receivable

Pledges are recorded at the amount management expects to collect from outstanding balances. Management expects all the pledges to be received; there is no allowance for uncollectible amounts as of June 30, 2018 and 2017. Pledges are recorded after being discounted to anticipated net present value of future cash flows. Conditional promises to give are not included as support until the conditions are substantially met. There were no conditional promises to give as of June 30, 2018 and 2017.

I. Property and Equipment

Property and equipment are carried at cost or, if donated, at the approximate fair value at the date of donation. Depreciation is computed on the straight-line method over the estimated useful lives of the assets (3 to 55 years). Generally, AHS, Now Boarding, Inc., and Kasota Holdings, LLC acquisitions of property and equipment of \$1,000 or more are capitalized, except certain IT equipment under \$1,000 that is capitalized.

J. Gift Annuities Payable

Under gift annuity contracts, AHS receives irrevocable title to contributed assets and agrees to make fixed period payments to the donor(s) for life or a specified period of time. Contributed assets are recorded at fair value at the date of receipt, and a liability is established for the present value of future annuity payments. To calculate the present value of the charitable gift annuities, the life expectancy tables in effect in the year of donation (published by the National Center of Health Statistics) and discount rates ranging from 1.4% to 9.4% were used. The excess of contributed assets over the annuity liability is recorded as unrestricted revenue. Any actuarial gain or loss resulting from the computation of the liability for the present value of future annuity payments is recorded as an unrestricted change in the value of split-interest agreements. Upon the donor's death, the remaining liability is recognized as revenue.

K. Revenue Recognition and Deferred Revenue

Contributions received are recorded as unrestricted, temporarily restricted, or permanently restricted support depending on the existence and nature of any restrictions. Contributions, including unconditional promises to give, are recognized in the period received. Program fees, merchandise sales and investment income is recognized when it is earned. Fees received for program and other services that have not yet been provided are classified as deferred revenue.

L. In-kind Contributions

The Organization reports gifts of non-cash assets as unrestricted support unless explicit donor stipulations specify how the donated assets must be used. Gifts of long-lived assets with explicit restrictions that specify how the assets are to be used and gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted support. Donated marketable securities and other noncash donations are recorded as contributions at their estimated fair market values at the date of donation.

M. Donated Services

The Organization has a large and dedicated team of volunteers that perform a variety of tasks that assist the Organization with specific programs and supporting services. These services are not recognized in the financial statements since the criteria for recording the services were not met.

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Notes to the Consolidated Financial Statements
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Note 1: Summary of Significant Accounting Policies (Continued)

N. Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

O. Allocation of Functional Expenses

Salaries and related expenses are allocated based on job descriptions and management estimates. Expenses, other than salaries and related payroll expenses, that are not directly identifiable by program or support service, are allocated based on management estimates.

P. Tax Status

AHS and Kindest Cut, P.C. are exempt from income taxes under Section 501(c)(3) of the Internal Revenue Code and Minnesota Statute 290.05. Kasota Holdings, LLC is a Minnesota limited liability company solely owned by AHS. These entities are considered public charities, as a result contributions received may be deductible by the donor for tax purposes.

Now Boarding, Inc. is a for-profit corporation that files its own corporate federal and Minnesota income tax returns.

Q. Deferred Financing Costs

Finance fees related to obtaining financing are deferred and amortized to interest expense over the term of the related debt using the straight-line method. Notes payable has been presented net of these deferred financing costs.

R. Advertising Costs

The Organization uses advertising to promote its programs among the audiences it serves. Advertising costs are expensed as incurred. Advertising expense for the years ending June 30, 2018 and 2017 was \$293,288 and \$250,341, respectively.

S. Subsequent Events

Subsequent events were evaluated through October 19, 2018, which is the date the financial statements were available to be issued. Subsequent events were identified and disclosed in Note 11 and Note 15.

T. Prior Period Information

The financial statements include certain prior year summarized comparative information in total. Such information does not include sufficient detail to constitute a presentation in conformity with accounting principles generally accepted in the United States. Accordingly, such information should be read in conjunction with the Organization's financial statements for the year ended June 30, 2017, from which the summarized information was derived.

Animal Humane Society and Subsidiaries
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Note 2: Unemployment Fund

AHS has elected to opt out of participation in the Minnesota Unemployment Insurance Program. AHS is self-insured for unemployment claims through Unemployment Services Trust (UST). Payments to UST are accumulated and used to pay future claims. An expense is recorded as claims are paid by UST. AHS believes there is no significant liability for claims incurred during the fiscal year ending June 30, 2018.

Note 3: Pledges Receivable

The balance of pledges receivable are due as follows for the years ended June 30, 2018 and 2017:

	2018	2017
Less than One Year	\$ 10,000	\$ 10,000
One to Five Years	30,000	20,000
Total Pledges Receivable	40,000	30,000
Less Discount to Present Value at 4%	(1,235)	(1,681)
Net Pledges Receivable	\$ 38,765	\$ 28,319

Note 4: Amounts Held In Trust

Amounts held in trust consisted of the following for the years ended June 30, 2018 and 2017:

	2018	2017
Charitable Remainder Trusts	\$ 564,823	\$ 555,586
Charitable Lead Annuity Trust	38,243	43,898
Total Amounts Held in Trust	\$ 603,066	\$ 599,484

Charitable Remainder Trusts - AHS is a beneficiary of a charitable remainder trust in which it receives one-seventh of the income from assets held by a trustee in perpetuity. Net realized and unrealized gains (losses) related to AHS's beneficial interest in this trust are reported as changes in permanently restricted net assets based on donor stipulations. AHS is the beneficiary of a second charitable remainder trust in which it receives 20% of the annual income from assets held by a trustee.

Charitable Lead Annuity Trust - AHS is one of six beneficiaries of a charitable lead annuity trust. Under terms of the split-interest agreement, AHS is to receive \$8,290 annually for its unrestricted use for eighteen years, with a final payment of \$4,717 in July 2023. At that time, the trust is to terminate and remaining trust assets are to be distributed to others. A discount rate of 6% has been used to calculate the present value of the expected future benefits.

Under FASB ASC 958, *Not-for-Profit Entities*, the Organization periodically remeasures its rights under these split-interest agreements using current market conditions for estimating present value calculations. The estimation of the net present value is subjective and requires significant judgment. Due to uncertainties inherent in the estimation process, it is possible that future events in either the near or long term could materially affect the amounts reported on the statement of financial position.

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Note 5: Fair Value Measurements

Fair value measurement accounting literature establishes a fair value hierarchy based on the priority of the inputs to the valuation methodologies used to measure fair value. The fair value hierarchy gives the highest priority to quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). If the inputs used to measure the financial instruments fall within different levels of hierarchy, the categorization is based on the lowest level input that is significant to the fair value measurement of the instrument. Investments recorded in the Statement of Financial Position are categorized based on the inputs to valuation techniques as follows:

Level 1 - Inputs to the valuation methodology are unadjusted quoted prices for identical assets in an active market that the Organization has the ability to access.

Level 2 - Inputs to the valuation methodology include:

- Quoted prices for similar assets or liabilities in active markets
- Quoted prices for identical or similar assets or liabilities in inactive markets
- Inputs other than quoted prices that are observable for the asset or liability
- Inputs that are derived principally from or corroborated by observable market data by correlation or other means

Level 3 - Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

Following is a description of the valuation methodologies used for assets measured at fair value. See Note 4 for methodology for amounts held in trust. There have been no changes in the methodologies used at June 30, 2018 and 2017.

Mutual Funds: Valued at the daily closing price as reported by the fund. Mutual funds held by the Organization are open-end mutual funds that are registered with the Securities and Exchange Commission. These funds are required to publish their daily net asset value (NAV) and to transact at that price. The mutual funds held by the Organization are deemed to be actively traded.

Stocks and Fixed Income Bonds: Valued at the daily closing price of the underlying stocks and bonds. The stocks and bond funds held by the Organization are deemed to be actively traded.

Amounts Held in Trust: Valued at the present value of expected receipts for the duration of the trust where stated. Where the trust is perpetual, valuation is the Organization's proportionate share of the fair value of the trust investments as report by the trustee. Additional information on amounts held in trust can be found in Note 4.

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Note 5: Fair Value Measurements (Continued)

The Organization's investments reported at fair value in the accompanying statement of financial position consist of the following:

June 30, 2018	Fair Value	Level 1	Level 3
Investments:			
Equity mutual funds	\$ 3,979,370	\$ 3,979,370	\$ -
Fixed income funds and bonds	3,048,798	3,048,798	-
Stocks	738,784	738,784	-
Total Investments	\$ 7,766,952	\$ 7,766,952	\$ -
Amounts Held in Trust	\$ 603,066	\$ 564,823	\$ 38,243
June 30, 2017	Fair Value	Level 1	Level 3
Investments:			
Equity mutual funds	\$ 2,713,852	\$ 2,713,852	\$ -
Fixed income funds and bonds	3,084,852	3,084,852	-
Stocks	1,271,688	1,271,688	-
Total Investments	\$ 7,070,392	\$ 7,070,392	\$ -
Amounts Held in Trust	\$ 599,484	\$ 555,586	\$ 43,898

The following sets forth the summary of changes in the fair value of Level 3 assets as of the years ended:

Annuity trust balance June 30, 2016	\$ 49,234
Payment, net of discount	<u>(5,336)</u>
Annuity trust balance June 30, 2017	43,898
Payment, net of discount	<u>(5,655)</u>
Annuity trust balance June 30, 2018	<u>\$ 38,243</u>

Note 6: Income Taxes

Animal Humane Society files informational returns in the United States federal jurisdiction and in the Minnesota state jurisdiction. In addition, AHS files tax returns in relation to their unrelated business income. As a wholly-owned, non-profit subsidiary, Kindest Cut, P.C. files separate informational returns in the United States federal jurisdiction and in the Minnesota state jurisdiction. As a wholly-owned, for-profit subsidiary, Now Boarding, Inc. files separate income tax returns in the United States federal jurisdiction and in the state of Minnesota. Kasota Holding, LLC is a limited liability company that is wholly owned by AHS and is considered a disregarded entity. As such, Kasota Holding, LLC activity is reported on Animal Humane Society's Form 990. All returns for Animal Humane Society prior to fiscal year 2015 are closed. No returns of any entity are currently under examination in any tax jurisdiction.

As of June 30, 2018, there were no material amounts of income tax related accrued interest or penalties recognized in either the balance sheet or statement of activities for AHS, Kindest Cut P.C., Now Boarding, Inc. nor Kasota Holdings, LLC.

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Note 6: Income Taxes (Continued)

Income taxes are provided for the tax effects of unrelated business transactions for AHS and all activity of Now Boarding, Inc. reported in the consolidated financial statements and consist of taxes currently due plus deferred taxes. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to temporary differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases, measured by enacted tax rates for years in which taxes are expected to be paid or recovered. Deferred tax assets are recognized only to the extent that it is more likely than not that they will be realized based on available evidence.

The following income tax related assets were included in the financial statements as of June 30, 2018 and 2017:

	2018	2017
Long-term Deferred Tax Asset		
Start-up and organization costs	\$ 2,116	\$ 3,609
Depreciation	471,003	590,825
Accrued vacation	4,912	6,319
Gift certificate liability/deposits	13,665	17,788
NOL carryforwards	1,133,016	1,435,630
Total deferred tax asset	1,624,712	2,054,171
Valuation allowance	(1,624,712)	(2,054,171)
Net Deferred Tax Asset	\$ -	\$ -

Income tax expense (benefit) consisted of the following for the years ended June 30, 2018 and 2017:

	2018	2017
Current:		
Federal	\$ (16,750)	\$ (97,201)
State	(16,298)	(27,113)
Deferred:		
Federal	(52,631)	(54,564)
State	(16,773)	(17,389)
Total income tax expense (benefit)	(102,452)	(196,267)
Valuation allowance	102,452	196,267
Net Income Tax Expense (Benefit)	\$ -	\$ -

The net operating loss (NOL) carryforwards expire at varying times beginning in 2028 through 2037.

Note 7: Line of Credit

The Organization has a line of credit with a bank for \$750,000 that matures in December 2019 and is secured by real property of AHS. The credit line was not used during the year and there was no outstanding balance as of June 30, 2018 and 2017.

Note 8: Credit Risk

The Organization maintains cash balances with banks insured by the Federal Deposit Insurance Corporation (FDIC). These deposits may, from time to time, exceed the balances insured by the FDIC.

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Note 9: Notes Payable

The Organization has the following notes payable as of June 30, 2018 and 2017.

	2018	2017
Note payable to a bank, due in monthly installments of \$24,218 with interest at 3.99% during the first 5 years. For the rest of the term, the interest will be 3% over the daily average interest rate charged for five year fixed advances as published at the Federal Home Loan Bank of Des Moines. The note matures in October 2023.	\$ -	\$ 3,491,737
Note payable to Old National Bank entered into in March 2018 to replace the previous loan, with interest only payments at an interest rate of 4.79% until April 2020. Starting in April 2020, the note has a maximum outstanding balance schedule with approximate monthly installments of \$22,835 with interest at 4.79%. The note matures in March 2023.	3,500,000	-
Note payable to Old National Bank entered into in March 2018 for the purchase of the Kasota Holdings property, with interest only payments at an interest rate of 4.55% until April 2020. Starting in April 2020, the note has a maximum outstanding balance schedule with approximate monthly installments of \$49,546 with interest at 4.55%. The note matures in March 2023.	7,750,000	-
Deferred financing costs, net	(102,842)	(24,481)
Total	11,147,158	3,467,256
Less amounts due within one year	-	(154,095)
Long-term portion	\$ 11,147,158	\$ 3,313,161

Approximate scheduled future principal payments due under the agreements are as follows:

Year ended June 30,	Note Payable	Deferred Financing	Total
2019	\$ -	(21,651)	\$ (21,651)
2020	77,187	(21,651)	55,536
2021	351,970	(21,651)	330,319
2022	368,822	(21,651)	347,171
2023	10,452,021	(16,238)	10,435,783
Total	\$ 11,250,000	\$ (102,842)	\$ 11,147,158

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Note 10: Lease Income

AHS leases its property to various businesses. AHS acquired the leases upon purchase of Kasota Holdings, LLC and the leases will expire on various dates through October 31, 2020. The lease payments include monthly fees to cover payment of the real estate taxes and mortgage insurance premiums. The total net lease income for the year ended June 30, 2018 is as follows:

	2018
Rental Income	\$ 291,425
Less:	
Direct management fees	(20,455)
Property tax	(98,111)
Depreciation	(20,511)
Mortgage interest	(98,931)
Loan fee interest	(3,552)
	\$ 49,865

As of June 30, 2018, future minimum lease payments to be received over the remaining term of the leases are as follows:

Year Ended	Amount
2019	\$ 689,333
2020	693,364
2021	231,572
	\$ 1,614,269

Note 11: Leases

AHS leases land on which its Saint Paul facility is located for one dollar per year from the City of Saint Paul, Minnesota through 2018. As additional rent, the lease requires AHS to maintain liability insurance and pay any utilities, maintenance and real estate taxes on the leased property. AHS also leases land adjacent to its St. Paul facility from the City of Saint Paul. The lease period for this adjacent land is from January 1, 2016 through December 31, 2018, and lease payments are one dollar annually.

Now Boarding, Inc. entered into a land and building lease with the Metropolitan Airports Commission (MAC). The lease term is for 15 years, began at December 1, 2008 and expires on December 31, 2023. The lease term may be extended by five years if written agreement is reached with MAC no later than December 31, 2022. Now Boarding, Inc. is required to pay rent to MAC. Rent expense was based upon the greater of Building plus Ground Rent specified in the lease agreement or a sliding scale percentage of Annual Gross Sales. On October 5, 2018, Now Boarding, Inc. entered into an amended lease with an effective date of January 1, 2018. The amendment eliminates the sliding scale percentage rent and establishes Building Rent at \$3,122 per month with a 2.5 percent increase annually and Ground Rent at \$9,600 per month with the MAC having the authority to adjust the rate after July 1, 2021.

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Note 11: Leases (Continued)

Based on the amended lease, future minimum base rent payments as of June 30, 2018 are as follows:

<u>Year ended June 30,</u>	<u>Amount</u>
2019	\$ 153,134
2020	154,083
2021	155,055
2022	156,051
2023	157,072
Thereafter	<u>78,795</u>
Total	<u>\$ 854,190</u>

Note 12: Employee Benefit Plans

AHS sponsors a 401(k) plan for all employees meeting certain eligibility requirements regarding age and length of service. AHS may make discretionary matching contributions which are immediately vested. Employer contributions were \$220,469 and \$155,690 for the years ended June 30, 2018 and 2017, respectively.

Note 13: Restricted Net Assets

AHS had the following temporarily restricted net assets at June 30, 2018 and 2017:

	<u>2018</u>	<u>2017</u>
Pet therapy and humane education	\$ 200,000	\$ 250,000
Perpetual care fund	231,873	236,216
Charitable remainder trust	362,742	359,225
Community engagement	-	131,870
Affordable spay/neuter	-	67,455
Companions for the elderly	54,097	54,097
Charitable lead annuity trust	38,243	43,898
Animal care and other	<u>4,247</u>	<u>4,247</u>
Total Temporarily Restricted Net Assets	<u>\$ 891,202</u>	<u>\$ 1,147,008</u>

AHS had the following permanently restricted net assets at June 30, 2018 and 2017:

	<u>2018</u>	<u>2017</u>
Endowment fund	\$ 2,734,307	\$ 2,113,317
Charitable remainder trust	202,081	196,360
Building maintenance fund	166,800	166,800
Perpetual care fund	<u>10,000</u>	<u>10,000</u>
Total Permanently Restricted Net Assets	<u>\$ 3,113,188</u>	<u>\$ 2,486,477</u>

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Note 14: Permanently Restricted Funds

The Organization holds certain funds in permanently restricted net assets. These funds were received from donors with a permanent restriction designation. These investments are for the future support of staff, programs, building maintenance and other activities of the Organization as determined by the Organization's Board of Directors.

Interpretation of Relevant Law

The Board of Directors of the Organization has interpreted the Minnesota 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. As a result of this interpretation, the Organization 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 the applicable donor gift instrument.

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

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

Endowment Composition and Changes in Endowment Net Assets

The composition of endowment funds includes donor-restricted funds only, and the changes in endowment net assets are as follows:

Balance June 30, 2016	\$ 2,442,265
Contributions	29,484
Increase in trust value	14,728
Balance June 30, 2017	2,486,477
Contributions	620,990
Increase in trust value	5,721
Balance June 30, 2018	\$ 3,113,188

According to the donor restrictions, the portion of permanently restricted funds that is required to be retained permanently either by explicit donor stipulation or by UPMIFA is \$3,113,188 and \$2,486,477 at June 30, 2018 and 2017, respectively. All earnings and investment gains and losses are included in unrestricted activity.

Spending Policy and how the Investment Objectives Relate to Spending Policy

The Board of Directors has sole discretion as to the investment and reinvestment of the assets of endowment funds. The primary investment objective of these accounts is capital preservation.

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Note 15: Subsequent Event

On October 4, 2018, Kindest Cut, P.C. amended its articles of incorporation to formally change its name to Animal Humane Society Veterinary Centers, P.C.

Note 16: New Accounting Pronouncements

In May 2014, the FASB issued Accounting Standards Update (ASU) No. 2014-09, *Revenue from Contracts with Customers* (ASU 2014-09) as a new Topic, Accounting Standards Codification *Topic 606*. The amendments are intended to provide a more robust framework for addressing revenue issues, improve comparability of revenue recognition practices and improve disclosure requirements. In August 2015, the FASB issued ASU No. 2015-14, *Revenue from Contracts with Customers: Deferral of the Effective Date*, which deferred the effective date of ASU 2014-09 by one year. This ASU is effective for annual reporting periods beginning after December 15, 2018, and shall be applied using either a full retrospective or modified retrospective approach. Early adoption is permitted. The new guidance is effective for the Organization for the year ended June 30, 2020. The Organization is currently evaluating the impact on the results of operations, financial condition and cash flows and has not determined the impact on its consolidated financial statements at this time.

In August 2016, the FASB issued ASU No. 2016-14, *Presentation of Financial Statements of Not-For-Profit Entities*, which is intended to improve how a not-for-profit entity classifies its net assets, as well as the information it presents in its financial statements about liquidity and availability of resources, expenses and investment return, and cash flows. This ASU is effective for annual reporting periods beginning after December 15, 2017, and shall be applied retrospectively. Early adoption is permitted. The new guidance is effective for the Organization for the year ended June 30, 2019. The Organization is currently evaluating the impact on the results of operations, financial condition and cash flows, and has not determined the impact on its consolidated financial statements at this time.

In March 2016, the FASB issued ASU No. 2016-02, *Leases*, as a new topic, Accounting Standards Codification 842. The objective of ASU No. 2016-02 is to increase transparency and comparability among organizations by reorganizing lease assets and lease liabilities on the statement of financial position and disclosing key information about leasing arrangements. ASU No. 2016-02 is effective for annual reporting periods beginning after December 15, 2019, and shall be applied using either a full retrospective or modified retrospective approach. Early adoption is permitted. The new guidance is effective for the Organization for the year ended June 30, 2021. The Organization is currently evaluating the impact on the results of operations, financial condition and cash flows and has not determined the impact on its consolidated financial statements at this time.