

THE GLADNEY CENTER FOR ADOPTION

CONSOLIDATED FINANCIAL STATEMENTS

Year Ended August 31, 2005
(with Summarized Comparative Information
for the Year Ended August 31, 2004)



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REPORT OF INDEPENDENT AUDITORS

To the Board of Directors of
The Gladney Center for Adoption

We have audited the accompanying consolidated statements of financial position of The Gladney Center for Adoption, a not-for-profit organization, as of August 31, 2005 and 2004, and the related consolidated statements of activities and changes in net assets, functional expenses, and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Organization's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. These 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 examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated 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 consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of The Gladney Center for Adoption as of August 31, 2005 and 2004 and the consolidated results of its activities and changes in net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Whitley Penn

Fort Worth, Texas
November 3, 2005

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THE GLADNEY CENTER FOR ADOPTION
CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

	August 31,	
	2005	2004
Assets		
Cash	\$ 512,086	\$ 865,788
Accounts receivable	16,142	698
Contributions receivable, less allowance of uncollectible pledges of \$204,000 and \$225,000 and discounts of \$87,000 and \$142,000, respectively	2,112,130	2,990,448
Prepaid expenses	177,954	142,914
Investments	30,866,947	27,110,458
Property and equipment, net	16,275,248	16,702,639
Bond issuance cost	78,390	85,615
Other assets	87,812	90,798
	<u>\$ 50,126,709</u>	<u>\$ 47,989,358</u>
Total assets		
	<u>\$ 50,126,709</u>	<u>\$ 47,989,358</u>
 Liabilities and Net Assets		
Liabilities:		
Accounts payable and accrued expenses	\$ 970,182	\$ 993,977
Interest payable	675,206	849,626
Funds held on deposit for programs	100,707	131,915
Deferred revenue	212,375	48,100
Other liabilities	22,798	31,088
Bond payable	7,797,789	8,306,566
Total liabilities	<u>9,779,057</u>	<u>10,361,272</u>
 Commitments and contingencies	-	-
 Net assets:		
Unrestricted	20,866,147	19,341,626
Temporarily restricted	10,752,563	9,571,628
Permanently restricted	8,728,942	8,714,832
Total net assets	<u>40,347,652</u>	<u>37,628,086</u>
 Total liabilities and net assets	<u>\$ 50,126,709</u>	<u>\$ 47,989,358</u>

See accompanying notes to consolidated financial statements.

THE GLADNEY CENTER FOR ADOPTION

CONSOLIDATED STATEMENTS OF ACTIVITIES AND CHANGES IN NET ASSETS

Year Ended August 31, 2005 with Summarized Comparative Totals for 2004

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total August 31, 2005</u>	<u>Total August 31, 2004</u>
Revenues, Gains, and Other Support					
Domestic adoption program	\$ 4,027,429	\$ -	\$ -	\$ 4,027,429	\$ 3,806,280
International adoption program	1,712,156	-	-	1,712,156	1,405,528
Resident insurance settlements	60,980	-	-	60,980	52,808
Post adoption	15,881	-	-	15,881	22,165
Contributions	1,364,905	49,011	14,110	1,428,026	1,567,761
Fees	152,631	-	-	152,631	134,976
Special events, net	628,818	-	-	628,818	-
Investment gains	1,654,403	2,037,089	-	3,691,492	2,204,828
Other	2,445	-	-	2,445	1,576
Net assets released from restrictions	905,165	(905,165)	-	-	-
Total revenue, gains, and other support	10,524,813	1,180,935	14,110	11,719,858	9,195,922
Expenses					
Programs					
Domestic adoption program	2,795,806	-	-	2,795,806	2,559,272
International adoption program	1,571,872	-	-	1,571,872	1,348,004
Post adoption	333,426	-	-	333,426	307,971
Client services	1,491,112	-	-	1,491,112	1,520,215
Administration	1,641,129	-	-	1,641,129	1,826,914
Gladney Fund	1,166,947	-	-	1,166,947	1,275,366
Total expenses	9,000,292	-	-	9,000,292	8,837,742
Net increase in net assets	1,524,521	1,180,935	14,110	2,719,566	358,180
Net assets at beginning of year	19,341,626	9,571,628	8,714,832	37,628,086	37,269,906
Net assets at end of year	<u>\$20,866,147</u>	<u>\$10,752,563</u>	<u>\$8,728,942</u>	<u>\$40,347,652</u>	<u>\$37,628,086</u>

See accompanying notes to consolidated financial statements.

THE GLADNEY CENTER FOR ADOPTION
CONSOLIDATED STATEMENTS OF FUNCTIONAL EXPENSES

Year Ended August 31, 2005 with Summarized Comparative Totals for 2004

	Domestic Adoption Program	International Adoption Program	Post Adoption	Client Services	Administration	Gladney Fund	Total Functional Expenses August 31, 2005	Total Functional Expenses August 31, 2004
Salaries	\$ 1,197,855	\$ 626,536	\$ 145,275	\$ 294,958	\$ 874,180	\$ 569,898	\$ 3,708,702	\$ 3,239,187
Employee benefits	257,748	181,971	52,943	84,556	265,831	5,654	848,703	646,122
Medical services	171,356	494	-	195	253	-	172,298	194,622
Office expense	31,007	51,400	5,170	44,848	11,840	188,696	332,961	305,907
Utilities and groundkeeping	157,040	59,120	13,409	76,914	50,325	34,500	391,308	442,938
Leases and rentals	95,210	42,984	4,962	3,773	4,622	-	151,551	149,724
Insurance expense	144,469	76,428	44,292	64,369	46,311	97,226	473,095	488,485
Depreciation expense	229,381	42,433	24,198	134,553	113,618	-	544,183	559,361
Professional fees	273,140	58,804	35,277	18,973	35,041	133,531	554,766	542,256
Other expenses	230,389	384,689	7,473	14,659	39,701	130,825	807,736	1,465,411
Marketing expenses	8,211	47,013	427	753,314	30,129	6,617	845,711	853,715
Unrealized (gain) loss on interest rate swap	-	-	-	-	169,278	-	169,278	(49,986)
Total functional expenses	\$ 2,795,806	\$ 1,571,872	\$ 333,426	\$ 1,491,112	\$ 1,641,129	\$ 1,166,947	\$ 9,000,292	\$ 8,837,742

See accompanying notes to consolidated financial statements.

THE GLADNEY CENTER FOR ADOPTION
CONSOLIDATED STATEMENTS OF CASH FLOWS

	Year Ended August 31,	
	2005	2004
Operating Activities		
Net increase in net assets	\$ 2,719,566	\$ 358,180
Adjustments to reconcile net increase in net assets to net cash provided by operating activities:		
Net realized and unrealized appreciation on investments	(3,210,999)	(1,894,389)
Provision for uncollectible contributions receivable	(16,238)	207,866
Depreciation	542,416	559,361
Amortization	7,225	7,043
Unrealized (gain) loss on interest rate swap	(169,278)	49,986
Changes in operating assets and liabilities:		
Accounts receivable	(15,444)	262
Contributions receivable	894,556	1,125,630
Prepaid expenses	(35,040)	(43,964)
Other assets	2,986	12,103
Accounts payable and accrued expenses	(23,795)	(140,794)
Interest payable	(5,142)	(25,201)
Funds held on deposit for programs	(31,208)	18,248
Deferred revenue	164,275	18,685
Other liabilities	(8,290)	(8,290)
Net cash provided by operating activities	815,590	244,726
Investing Activities		
Proceeds from sales of investments	7,946,479	1,329,206
Purchases of investments	(8,491,969)	(1,331,539)
Purchases of property and equipment	(115,025)	(107,910)
Net cash used in investing activities	(660,515)	(110,243)
Financing Activity		
Payments on bond payable	(508,777)	(481,849)
Net decrease in cash	(353,702)	(347,366)
Cash at beginning of year	865,788	1,213,154
Cash at end of year	\$ 512,086	\$ 865,788
Supplemental Disclosure of Cash Flow Information		
Cash paid for interest	\$ 202,023	\$ 458,582

See accompanying notes to consolidated financial statements.

THE GLADNEY CENTER FOR ADOPTION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

August 31, 2005 and 2004

A. Nature of Business

The Gladney Center for Adoption (the "Center"), founded in 1887 in Fort Worth, Texas, is a licensed not-for-profit 501(c)(3) tax exempt social services agency whose staff and directors are committed to providing ethical, timely, and individualized adoption services.

The accompanying consolidated financial statements include the financial information of the Center, The Gladney Fund (the "Fund"), and certain trust entities that benefit the Center (collectively the "Organization"). The Fund is a distinct entity established as a 501(c)(3) non-profit corporation, with a fiscal year end of August 31. The Fund was organized to exclusively perform the fundraising activities for the Center. These activities include generating, receiving, and administering funds for the growth, operations, and improvements of the Center. The trust entities were established by the Center as distinct 501(c)(3) entities for maintenance of investments previously held by the Center.

The comprehensive programs focus on Gladney's commitment to:

- Enhance a child's potential by placement in a permanent family
- Find forever families for children from other countries
- Support young women experiencing crisis pregnancies
- Help to fulfill the dream of parenthood
- Fund humanitarian aid programs to assist orphaned, abandoned and vulnerable children
- Offer each client access to post adoption services
- Educate the public about adoption

Adoptive Parent Programs - Domestic

Agency Assisted

This flexible program unites prospective parents with the children of young women who contact the Center to make adoption plans. The agency obtains the best possible adoptive homes for children entrusted to its care through a diligent preparation and education process.

ABC

The ABC program represents the Center's commitment to finding permanent families for African American and biracial children. It is designed to help families who are prepared to love and provide an environment of acceptance and pride for the heritage of their child.

New Beginnings

Children who are more difficult to place due to their circumstances are given a fresh chance at bright futures through this highly specialized program. Children waiting in foster care are placed in permanent families, and infants who have special needs, such as non-correctable medical or congenital conditions, are placed with parents who can provide the necessary care and resources.

THE GLADNEY CENTER FOR ADOPTION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – *(continued)*

A. Nature of Business - continued

Adoptive Parent Programs – International

International Adoptions

Through this program, the Center provides loving homes for children who are living in foreign orphanages. International adoptions help people achieve their dreams of parenthood by adopting infants and children from around the world. International adoption opportunities are available in Eastern European, Latin American, and Asian countries.

B. Summary of Significant Accounting Policies

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

Basis of Accounting

The accounts are maintained and the consolidated financial statements have been prepared using the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America. All significant accounts and transactions between the Center, the Fund, and the trust entities have been eliminated in consolidation.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the year. Actual results could differ from these estimates. Significant estimates used by the Organization include the collectibility of contributions receivable and the resulting allowance for uncollectible pledges.

Cash

The Organization considers all certificates of deposit, commercial paper, and U.S. government securities with original maturities of three months or less, when purchased, to be cash. At August 31, 2005 and 2004, the Organization had no such investments. The Organization maintains deposits primarily in two financial institutions, which may at times exceed amounts covered by insurance provided by the U.S. Federal Deposit Insurance Corporation. There were no uninsured deposits at August 31, 2005 or 2004 and the Organization has not experienced any losses related to such uninsured amounts.

THE GLADNEY CENTER FOR ADOPTION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (continued)

B. Summary of Significant Accounting Policies - continued

Contributions Receivable

The Organization states contributions receivable 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 an allowance of uncollectible pledges based on its assessment of the current status of individual receivables. Balances still outstanding after management has used reasonable collection efforts are written off through a charge to the allowance of uncollectible pledges and a credit to the applicable contribution receivable.

The Organization records contributions receivable at their discounted present value, with the exception of contributions to be pledged upon the death of an individual.

Investments

The Organization follows the provisions of Statement of Financial Accounting Standards (“SFAS”) No. 124, *Accounting for Certain Investments Held by Not-for-Profit Organizations*. SFAS No. 124 requires investments with readily determinable fair values to be stated at their fair value with realized and unrealized gains and losses included in the statement of activities.

Property and Equipment

The Organization states significant expenditures for property and equipment at cost less accumulated depreciation. Improvements, which substantially enhance the utilization of or increase the useful life of the property and equipment, are capitalized at cost. Depreciation is recognized using the straight-line method over the expected useful lives of the assets. Expected useful lives range from three to 10 years. The cost of assets disposed of and the related accumulated depreciation are eliminated, and any resulting gain or loss is reflected in the accompanying consolidated statements of activities and changes in net assets in the period of disposal.

Bond Issuance Cost

The Organization amortizes bond issuance cost related to the bond payable over the life of the bond payable using the straight-line method. Amortization expense during 2005 and 2004 approximated \$7,000 per year.

Contributions

The Organization accounts for contributions in accordance with SFAS No. 116, *Accounting for Contributions Received and Contributions Made*. In accordance with SFAS No. 116, contributions received are recorded as unrestricted, temporarily restricted, or permanently restricted support depending on the existence and/or nature of any donor restrictions. Under SFAS No. 116, time-restricted contributions are required to be reported as temporarily restricted support and are then reclassified to unrestricted net assets upon expiration of the time restriction. All contributions are considered to be available for unrestricted use unless specifically restricted by the donor.

THE GLADNEY CENTER FOR ADOPTION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (continued)

B. Summary of Significant Accounting Policies - continued

Contributions – continued

Contributed assets are recorded at their fair value on the date of receipt. Necessary services contributed by persons with specialized skills are reported as unrestricted support at the fair value of those services during the period the service is provided. Services contributed by persons without specialized skills are not recorded due to the difficulty of objectively determining their value. The Organization recognizes unconditional promises to give as support in the period the promise is made and reports them as contributions in the accompanying consolidated statements of activities and changes in net assets

Comparative Prior Year Information

The consolidated statements of activities and changes in net assets, and functional expenses for the year ended August 31, 2004 include certain summarized financial information in total but not by net asset class or program category for purposes of comparison to 2005 information. Such information does not include sufficient detail to constitute a presentation in conformity with accounting principles generally accepted in the United States of America. Accordingly, such information should be read in conjunction with the Organization's financial statements for the year ended August 31, 2004, from which the summarized information was derived.

C. Contributions Receivable

As of August 31, 2005, contributions receivable, net of discounts, are expected to be collected as follows:

Due in one year	\$ 582,636
Due in two to five years	1,733,684
Total	<u>2,316,320</u>
Less allowance	<u>204,190</u>
Total contributions	<u>\$ 2,112,130</u>

D. Investments and Investment Gains

The composition of investments as of August 31, are reflected in the following table:

	<u>2005</u>	<u>2004</u>
Equity securities	\$ 19,373,322	\$ 14,872,019
Debt securities and other obligations	10,947,512	11,846,620
Money market funds	546,113	391,819
Total investments	<u>\$ 30,866,947</u>	<u>\$ 27,110,458</u>

THE GLADNEY CENTER FOR ADOPTION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (continued)

D. Investments and Investment Gains - continued

The components of investment gains for the years ended August 31, 2005 and 2004 are reflected in the following table:

	<u>2005</u>	<u>2004</u>
Dividends and interest	\$ 480,493	\$ 310,439
Realized gains	773,279	337,166
Unrealized gains	<u>2,437,720</u>	<u>1,557,223</u>
Net investment gain	<u>\$ 3,691,492</u>	<u>\$ 2,204,828</u>

E. Property and Equipment

The following is a summary of property and equipment at August 31,:

	<u>2005</u>	<u>2004</u>
Land	\$ 1,335,252	\$ 1,335,252
Building	15,276,676	15,276,676
Furniture and fixtures	2,048,074	1,965,248
Automobiles	<u>144,263</u>	<u>110,300</u>
Total property and equipment	18,804,265	18,687,476
Less accumulated depreciation	<u>2,529,017</u>	<u>1,984,837</u>
Property and equipment, net	<u>\$ 16,275,248</u>	<u>\$ 16,702,639</u>

F. Liability Under Split-Interest Agreements

The Organization has included in accounts payable and accrued expenses a discounted liability of approximately \$48,000 and \$62,000 as of August 31, 2005 and 2004, respectively, for amounts due to donor-specified beneficiaries. This discounted liability represents the remaining annual payments due through October 28, 2006. This liability arose under a split-interest agreement wherein the Fund received a cash gift of approximately \$300,000 during the fiscal year ended August 31, 1998.

G. Bond Payable

The Organization borrowed \$9,750,000 from a financial institution in August 2000, incurring \$114,153 of bond issuance costs. The note agreement requires the Organization to maintain certain financial covenants. At August 31, 2005, the Organization was in compliance with all such covenants.

THE GLADNEY CENTER FOR ADOPTION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (continued)

G. Bond Payable – continued

Terms of the agreement require principal and interest payments through the maturity date of June 1, 2016. The note bears interest at either 75% of the 30, 60 or 90-day LIBOR rate or 51% of the prime rate, whichever method is chosen at the discretion of the Organization (2.77% and 1.24% as of August 31, 2005 and 2004, respectively).

Effective May 14, 2001, the Organization entered into an interest rate swap agreement with an initial notional principal amount of \$9,750,000 and an expiration date of June 1, 2016. Pursuant to the agreement, the Organization pays a fixed rate of 4.54% and receives a floating interest rate for the duration of the swap agreement.

The note and the interest rate swap are collateralized by the contributions receivable for the Capital Campaign Project.

The minimum required principal loan payments over the next five years and thereafter, are as follows:

2005	\$ 537,000
2006	567,000
2007	599,000
2008	632,000
2009	668,000
Thereafter	<u>4,795,000</u>
Total	<u>\$ 7,798,000</u>

H. Temporarily Restricted Net Assets

Temporarily restricted net assets were available for the following purposes as of August 31,:

	2005	2004
Gladney Fund	\$ 10,545,165	\$ 9,364,230
Domestic programs	151,969	138,044
International programs	<u>65,429</u>	<u>69,354</u>
Total temporarily restricted net assets	<u>\$ 10,762,563</u>	<u>\$ 9,571,628</u>

THE GLADNEY CENTER FOR ADOPTION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (continued)

I. Permanently Restricted Net Assets

Permanently restricted net assets were restricted to investments in perpetuity, the income from which is expendable to support the following as of August 31,:

	2005	2004
International Adoption Program	\$ 105,338	\$ 104,180
Greer Garson Educational Opportunities	545,000	545,000
ABC Adoption Program	1,221,700	1,221,700
Transitional care	370,753	370,753
Campus and capital improvement	555,000	555,000
Post adoption	302,318	302,318
Career development	268,818	268,818
China endowment	10,250	-
Any activities of the Center	5,349,765	5,347,063
 Total permanently restricted net assets	 \$ 8,728,942	 \$ 8,714,832

J. Special Events

The Fund has 17 family associations located throughout the United States that sponsor fund raising special events. These groups of volunteers raised a total of approximately \$617,000 and \$615,000 with related expenses of approximately \$224,000 and \$264,000 for the years ended August 31, 2005 and 2004, respectively.

The Fund also conducts a bi-annual golf tournament, The Gladney Cup. This tournament raised a total of approximately \$1,049,000 and \$43,000 with related expenses of approximately \$817,000 and \$89,000 for the years ended August 31, 2005 and 2004 respectively.

K. Retirement Plan

The Organization maintains a 403(b) defined contribution retirement plan for the benefit of its full-time employees who have attained 21 years of age and two years of service. The Center matches 50% of the employee's pre-tax compensation deferral contributions to the plan until their sixth year of service, and, thereafter, matches 100% of the employee's contribution. The expense recognized by the Organization totaled approximately \$227,000 and \$210,000 for the years ended August 31, 2005 and 2004, respectively.

THE GLADNEY CENTER FOR ADOPTION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – *(continued)*

L. Federal Income Tax

The Organization is exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code. Therefore, no provision for income taxes is made in the accompanying consolidated financial statements.