

THE GLADNEY CENTER FOR ADOPTION

**CONSOLIDATED FINANCIAL STATEMENTS
AND SUPPLEMENTAL INFORMATION**

**Year Ended August 31, 2006
(with Summarized Comparative Information
for the Year Ended August 31, 2005)**



THE GLADNEY CENTER FOR ADOPTION

CONSOLIDATED FINANCIAL STATEMENTS AND SUPPLEMENTAL INFORMATION

Year Ended August 31, 2006 (with Summarized Comparative
Information for the Year Ended August 31, 2005)

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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, 2006 and 2005, 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. 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. The Organization is not required to have, nor were we engaged to perform, an audit of its internal controls over financial reporting. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Organization's internal control over financial reporting. Accordingly, we express no such opinion. An audit also 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 financial position of The Gladney Center for Adoption as of August 31, 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.

Our audits were conducted for the purpose of forming an opinion on the basic consolidated financial statements taken as a whole. The schedule of fund raising expenses to contributions received on page 15 is presented for purposes of additional analysis and is not a required part of the basic consolidated financial statements. Such information has been subjected to the auditing procedures applied in the audits of the basic consolidated financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic consolidated financial statements taken as a whole.

Whitley Penn LLP

Fort Worth, Texas
November 2, 2006

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THE GLADNEY CENTER FOR ADOPTION
CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

	August 31,	
	2006	2005
Assets		
Cash	\$ 473,358	\$ 512,086
Accounts receivable	1,499	16,142
Contributions receivable, less allowance for uncollectible pledges of \$254,000 and \$204,000 and discounts of \$65,000 and \$87,000, respectively	1,565,391	2,112,130
Prepaid expenses	214,721	177,954
Investments	31,473,700	30,866,947
Property and equipment, net	16,037,153	16,275,248
Bond issuance cost, net of accumulated amortization of \$42,988 and \$35,763 respectively	71,165	78,390
Other assets	90,760	87,812
Total assets	\$ 49,927,747	\$ 50,126,709
 Liabilities and Net Assets		
Liabilities:		
Accounts payable and accrued expenses	\$ 1,175,907	\$ 970,182
Interest payable	84,893	91,219
Interest rate swap liability	248,808	583,987
Funds held on deposit for programs	102,937	100,707
Deferred revenue	31,225	212,375
Other liabilities	14,507	22,798
Bond payable	7,260,580	7,797,789
Total liabilities	8,918,857	9,779,057
Commitments and contingencies	-	-
 Net assets:		
Unrestricted	17,920,438	17,551,879
Temporarily restricted	10,982,919	10,813,246
Permanently restricted	12,105,533	11,982,527
Total net assets	41,008,890	40,347,652
Total liabilities and net assets	\$ 49,927,747	\$ 50,126,709

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, 2006 with Summarized Comparative Totals for 2005

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total August 31, 2006</u>	<u>Total August 31, 2005</u>
Revenues, Gains, and Other Support					
Domestic adoption program	\$ 3,836,277	\$ -	\$ -	\$ 3,836,277	\$ 4,027,429
International adoption program	1,555,986	-	-	1,555,986	1,712,156
Resident insurance settlements	51,827	-	-	51,827	60,980
Post adoption	49,205	-	-	49,205	15,881
Contributions	1,628,463	221,464	123,006	1,972,933	1,428,026
Fees	137,645	-	-	137,645	95,593
Special events, net	408,023	-	-	408,023	628,818
Investment gains	816,459	992,954	-	1,809,413	3,619,171
Other	1,185	-	-	1,185	2,445
Net assets released from restrictions	1,044,745	(1,044,745)	-	-	-
Total revenue, gains, and other support	9,529,815	169,673	123,006	9,822,494	11,590,499
Expenses					
Programs					
Domestic adoption program	2,647,313	-	-	2,647,313	2,795,806
International adoption program	1,498,979	-	-	1,498,979	1,571,872
Family services	562,432	-	-	562,432	409,656
Client services	1,868,957	-	-	1,868,957	1,491,112
Administration	1,807,338	-	-	1,807,338	1,910,123
Fund raising	776,237	-	-	776,237	692,364
Total expenses	9,161,256	-	-	9,161,256	8,870,933
Net increase in net assets	368,559	169,673	123,006	661,238	2,719,566
Net assets at beginning of year	17,551,879	10,813,246	11,982,527	40,347,652	37,628,086
Net assets at end of year	<u>\$ 17,920,438</u>	<u>\$ 10,982,919</u>	<u>\$ 12,105,533</u>	<u>\$ 41,008,890</u>	<u>\$ 40,347,652</u>

See accompanying notes to consolidated financial statements.

THE GLADNEY CENTER FOR ADOPTION
CONSOLIDATED STATEMENTS OF FUNCTIONAL EXPENSES

Year Ended August 31, 2006 with Summarized Comparative Totals for 2005

	Domestic Adoption Program	International Adoption Program	Family Services	Client Services	Administration	Fund Raising	Total Functional Expenses August 31, 2006	Total Functional Expenses August 31, 2005
Salaries	\$ 1,113,732	\$ 552,120	\$ 283,507	\$ 343,355	\$ 1,130,082	\$246,192	\$ 3,668,988	\$ 3,708,702
Employee benefits	228,347	142,457	68,873	125,734	303,124	23,753	892,288	848,703
Medical services	137,206	4,200	-	-	166	-	141,572	172,298
Office expense	42,510	65,813	10,075	47,109	14,859	177,577	357,943	332,961
Utilities and groundkeeping	177,515	76,569	18,586	94,585	51,646	34,500	453,401	391,308
Leases and rentals	81,620	98,731	3,368	3,776	4,049	-	191,544	151,551
Insurance expense	120,070	62,370	36,708	55,337	37,863	52,729	365,077	473,095
Depreciation expense	234,827	41,906	23,593	138,205	113,701	-	552,232	544,183
Professional fees	284,251	70,115	39,709	35,583	50,737	65,739	546,134	482,445
Other expenses	220,659	332,037	49,422	42,289	413,973	169,944	1,228,324	750,698
Marketing expenses	6,576	52,661	28,591	982,984	22,317	5,803	1,098,932	845,711
Unrealized (gain) loss on interest rate swap	-	-	-	-	(335,179)	-	(335,179)	169,278
Total functional expenses	\$2,647,313	\$ 1,498,979	\$562,432	\$1,868,957	\$ 1,807,338	\$776,237	\$ 9,161,256	\$ 8,870,933

See accompanying notes to consolidated financial statements.

THE GLADNEY CENTER FOR ADOPTION
CONSOLIDATED STATEMENTS OF CASH FLOWS

	Year Ended August 31,	
	2006	2005
	<u> </u>	<u> </u>
Operating Activities		
Net increase in net assets	\$ 661,238	\$ 2,719,566
Adjustments to reconcile net increase in net assets to net cash provided by operating activities:		
Net realized and unrealized appreciation		
on investments	(1,233,400)	(3,210,999)
Provision for uncollectible contributions receivable	87,025	(16,238)
Depreciation and amortization	568,905	549,641
Unrealized gain on interest rate swap	(335,179)	(169,278)
Changes in operating assets and liabilities:		
Accounts receivable	14,643	(15,444)
Contributions receivable	459,714	894,556
Prepaid expenses	(36,767)	(35,040)
Other assets	(2,948)	2,986
Accounts payable and accrued expenses	205,725	(23,795)
Interest payable	(6,326)	(5,142)
Funds held on deposit for programs	2,230	(31,208)
Deferred revenue	(181,150)	164,275
Other liabilities	(8,291)	(8,290)
Net cash provided by operating activities	<u>195,419</u>	<u>815,590</u>
Investing Activities		
Proceeds from sales of investments	6,017,397	7,946,479
Purchases of investments	(5,390,750)	(8,491,969)
Purchases of property and equipment	(323,585)	(115,025)
Net cash provided by (used in) investing activities	<u>303,062</u>	<u>(660,515)</u>
Financing Activity		
Payments on bond payable	<u>(537,209)</u>	<u>(508,777)</u>
Net decrease in cash	(38,728)	(353,702)
Cash at beginning of year	<u>512,086</u>	<u>865,788</u>
Cash at end of year	<u>\$ 473,358</u>	<u>\$ 512,086</u>
Supplemental Disclosure of Cash Flow Information		
Cash paid for interest	<u>\$ 361,225</u>	<u>\$ 202,023</u>

See accompanying notes to consolidated financial statements.

THE GLADNEY CENTER FOR ADOPTION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

August 31, 2006 and 2005

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 and The Gladney Fund (the "Fund")(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 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 and training
- 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, African, 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.

Principles of Consolidation

The consolidated financial statements include the accounts of the Center and the Fund. All significant accounts and transactions between the Center and the Fund 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, 2006 and 2005, 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. 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 for 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 for 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 consolidated statement of activities and changes in net assets of the respective period.

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. Expenditures for normal maintenance and repairs are expensed as incurred. 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 the bond issuance cost related to the bond payable over the life of the bond payable using the straight-line method of accounting. Amortization expense during 2006 and 2005 approximated \$7,000 per year.

Contributions

The Organization accounts for contributions received 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 consolidated statement of activities and changes in net assets of the respective period.

Comparative Prior Year Information

The consolidated statements of activities and changes in net assets, and functional expenses for the year ended August 31, 2005 include certain summarized financial information in total but not by net asset class or program category for purposes of comparison to 2006 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, 2005, from which the summarized information was derived.

Reclassifications

Certain 2005 amounts have been reclassified to conform to the 2006 presentation.

C. Contributions Receivable

As of August 31, 2006, contributions receivable, net of discounts, are expected to be collected as follows:

Due in one year	\$ 310,155
Due in two to five years	1,508,856
Total	<u>1,819,011</u>
Less allowance for uncollectible pledges	<u>253,620</u>
Total contributions receivable	<u>\$ 1,565,391</u>

THE GLADNEY CENTER FOR ADOPTION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (continued)

D. Investments and Investment Gains

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

	<u>2006</u>	<u>2005</u>
Equity securities	\$ 19,681,251	\$ 19,373,322
Debt securities and other obligations	11,219,870	10,947,512
Money market funds	<u>572,579</u>	<u>546,113</u>
Total investments	<u>\$ 31,473,700</u>	<u>\$ 30,866,947</u>

The components of investment gains for the years ended August 31, 2006 and 2005 are reflected in the following table:

	<u>2006</u>	<u>2005</u>
Dividends and interest	\$ 682,616	\$ 480,493
Realized gains	733,659	773,279
Unrealized gains	<u>499,741</u>	<u>2,437,720</u>
Investment gains before investment fees	1,916,016	3,691,171
Less investment fees	<u>106,603</u>	<u>72,321</u>
Investment gains	<u>\$ 1,809,413</u>	<u>\$ 3,619,171</u>

E. Property and Equipment

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

	<u>2006</u>	<u>2005</u>
Land	\$ 1,335,252	\$ 1,335,252
Building	15,471,008	15,276,676
Furniture and fixtures	2,177,318	2,048,074
Automobiles	<u>144,263</u>	<u>144,263</u>
Total property and equipment	19,127,841	18,804,265
Less accumulated depreciation	<u>3,090,688</u>	<u>2,529,017</u>
Property and equipment, net	<u>\$ 16,037,153</u>	<u>\$ 16,275,248</u>

THE GLADNEY CENTER FOR ADOPTION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (continued)

F. Liability Under Split-Interest Agreements

The Organization has included in accounts payable and accrued expenses a discounted liability of approximately \$33,000 and \$48,000 as of August 31, 2006 and 2005, 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, 2006, the Organization was in compliance with all such covenants.

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 (4.05% and 2.77% as of August 31, 2006 and 2005, 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:

2006	\$ 567,000
2007	599,000
2008	633,000
2009	668,000
2010	705,000
Thereafter	<u>4,089,000</u>
Total	<u>\$ 7,261,000</u>

THE GLADNEY CENTER FOR ADOPTION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – (continued)

H. Temporarily Restricted Net Assets

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

	<u>2006</u>	<u>2005</u>
Gladney Fund	\$ 10,724,501	\$ 10,605,858
Domestic programs	182,042	141,959
International programs	76,376	65,429
	<u> </u>	<u> </u>
Total temporarily restricted net assets	<u>\$ 10,982,919</u>	<u>\$ 10,813,246</u>

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,:

	<u>2006</u>	<u>2005</u>
International Adoption Program	\$ 105,444	\$ 105,338
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
Family services	302,318	302,318
Career development	268,818	268,818
China Endowment	137,575	10,250
Sproesser Wynn Endowment	2,145,348	2,145,348
Edna Gladney Home Endowment	1,108,237	1,108,237
Any activities of the Center	5,345,340	5,349,765
	<u> </u>	<u> </u>
Total permanently restricted net assets	<u>\$ 12,105,533</u>	<u>\$ 11,982,527</u>

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 \$609,000 and \$617,000 with related expenses of approximately \$201,000 and \$224,000 for the years ended August 31, 2006 and 2005, respectively.

THE GLADNEY CENTER FOR ADOPTION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – *(continued)*

J. Special Events - continued

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

K. Donated Services

During 2006, CW33, a local television station in Dallas/Fort Worth, ran weekly profiles and promotions to increase the community's awareness of children needing forever homes. This service was donated to the Organization. The total value of the promotion was approximately \$370,000 for the year ended August 31, 2006 and was recorded as a contribution and expense in the accompanying consolidated statement of activities and changes in net assets.

L. 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 \$314,000 and \$227,000 for the years ended August 31, 2006 and 2005, respectively.

M. 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.

SUPPLEMENTAL INFORMATION

THE GLADNEY CENTER FOR ADOPTION

SCHEDULE OF FUND RAISING EXPENSES TO CONTRIBUTIONS RECEIVED

	August 31,	
	2006	2005
Fund raising expenses	<u>\$ 776,237</u>	<u>\$ 692,364</u>
Contributions per the statements of activities and changes in net assets	\$ 1,972,933	\$ 1,428,026
Cash pledge payments received on Commitment to Families Campaign and Building for Adoption Campaign	<u>503,269</u>	<u>949,000</u>
Total contributions received	<u>\$ 2,476,202</u>	<u>\$ 2,377,026</u>
Percentage of fund raising expenses to contributions received	<u>31%</u>	<u>29%</u>