

MAGDALENE, INC. AND SUBSIDIARY
CONSOLIDATED FINANCIAL STATEMENTS
AND INDEPENDENT AUDITOR'S REPORT

June 30, 2006

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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Magdalene, Inc. and Subsidiary

We have audited the accompanying consolidated statement of financial position of Magdalene, Inc. and Subsidiary (a nonprofit Organization) as of June 30, 2006 and the related consolidated statements of activities, functional expenses and cash flows for the year 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 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 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 our audit provides 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 Magdalene, Inc. and Subsidiary as of June 30, 2006, and the changes in their net assets and their cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As described in Note 10 to the consolidated financial statements, the Organization restated unrestricted, temporarily restricted, and permanently restricted net assets at June 30, 2005 to properly reflect the classification of net assets.

Frasier, Dean & Howard, PLLC

December 14, 2006

MAGDALENE, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENT OF FINANCIAL POSITION
June 30, 2006

Assets

Current assets:	
Cash and cash equivalents	\$ 64,648
Unconditional promises to give, current	161,446
Other current assets	<u>12,367</u>
Total current assets	238,461
Cash restricted for endowment	65,000
Unconditional promises to give	96,947
Property and equipment, net	<u>839,392</u>
Total assets	<u><u>\$ 1,239,800</u></u>

Liabilities and Net Assets

Current liabilities:	
Accounts payable and accrued expenses	\$ 7,309
Note payable	<u>61,867</u>
Total current liabilities	<u>69,176</u>
Net assets:	
Unrestricted	829,780
Temporarily restricted	275,844
Permanently restricted	<u>65,000</u>
Total net assets	<u>1,170,624</u>
Total liabilities and net assets	<u><u>\$ 1,239,800</u></u>

See accompanying notes to financial statements.

MAGDALENE, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENT OF ACTIVITIES
For the year ended June 30, 2006

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Revenue and other support:				
Contributions	\$ 459,511	\$ 203,906	\$ -	\$ 663,417
Thistle Farms product sales	114,177	-	-	114,177
Men's rehabilitation program	29,801	-	-	29,801
Other	7,286	-	-	7,286
Net assets released from restrictions	79,090	(69,090)	(10,000)	-
Total revenue and other support	689,865	134,816	(10,000)	814,681
Expenses:				
Program services:				
Women's sanctuary and rehabilitation	421,022	-	-	421,022
Men's rehabilitation	4,545	-	-	4,545
Thistle Farms	189,748	-	-	189,748
Total program services	615,315	-	-	615,315
Supporting services:				
Management and general	61,912	-	-	61,912
Fundraising	33,040	-	-	33,040
Total supporting services	94,952	-	-	94,952
Total expenses	710,267	-	-	710,267
Losses:				
Provision for loss on uncollectible contributions	-	67,466	-	67,466
Change in net assets	(20,402)	67,350	(10,000)	36,948
Net assets, beginning of year, as previously reported	900,977	82,699	150,000	1,133,676
Restatement (Note 10)	(50,795)	125,795	(75,000)	-
Net assets, beginning of year, as restated	850,182	208,494	75,000	1,133,676
Net assets, end of year	<u>\$ 829,780</u>	<u>\$ 275,844</u>	<u>\$ 65,000</u>	<u>\$ 1,170,624</u>

See accompanying notes to financial statements.

MAGDALENE, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENT OF FUNCTIONAL EXPENSES
For the year ended June 30, 2006

	Program Services				Supporting Services		
	Women's Sanctuary and Rehabilitation	Men's Rehabilitation	Thirde Parish	Total Program Services	Management and General	Fundraising	Total Supporting Services
Salaries	\$ 121,612	\$ -	\$ 75,169	\$ 196,781	\$ 23,419	\$ 21,780	\$ 45,199
Contract labor	41,867	-	-	41,867	-	-	-
Cost of sales - labor	-	-	41,427	41,427	-	-	-
Depreciation	40,304	-	-	40,304	-	-	-
Cost of sales - materials	-	-	30,448	30,448	-	-	-
Utilities	28,396	-	1,880	30,276	-	-	-
Payroll tax	11,945	-	11,389	23,334	2,306	2,139	4,445
Reimbursement - St. Augustine's	21,605	-	-	21,605	1,200	1,200	2,400
Transportation	21,881	-	-	21,881	-	-	-
Outreach ministry	17,606	-	1,555	19,161	1,099	-	1,099
Employee benefits	8,365	-	7,976	16,341	1,615	1,498	3,113
Insurance	13,833	-	-	13,833	-	-	-
Stipends	12,053	-	-	12,053	-	-	-
Repairs and maintenance	11,495	-	-	11,495	-	-	-
Food and household supplies	11,489	-	-	11,489	-	-	-
Legal and professional	-	-	-	-	11,389	-	11,389
Telephone	9,439	-	-	9,439	1,111	555	1,666
Building rent	10,200	-	-	10,200	-	-	-
Community Foundation	-	-	-	-	10,000	-	10,000
Medical	8,634	-	4,572	8,634	-	-	-
Other program expenses	3,004	-	-	3,004	-	-	-
Miscellaneous	-	-	-	-	7,075	-	7,075
Meals and events	5,456	-	840	6,296	-	-	-
Cost of sales - printing	-	-	5,673	5,673	-	-	-
Interest	5,552	-	-	5,552	-	-	-
Individual Development Account	5,215	-	-	5,215	-	-	-
Printing and supplies	-	-	508	508	2,238	2,238	4,476
Clothing and grooming	4,619	-	-	4,619	-	-	-
Therapy seminars	-	4,545	-	4,545	-	-	-
Property taxes	4,250	-	-	4,250	-	-	-
Advertising and promotion	-	-	4,114	4,114	-	-	-
Fundraising	-	-	-	-	-	3,237	3,237
Supplies	-	-	1,909	1,909	-	-	-
Credit card fees	-	-	1,700	1,700	-	-	-
Newsletter	786	-	-	786	460	393	853
Education	1,416	-	-	1,416	-	-	-
Travel	-	-	588	588	-	-	-
	\$ 421,022	\$ 4,545	\$ 189,748	\$ 615,315	\$ 61,912	\$ 33,040	\$ 94,952
							\$ 710,267

See accompanying notes to financial statements.

MAGDALENE, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENT OF CASH FLOWS
For the year ended June 30, 2006

Change in net assets	\$ 36,948
Adjustments to reconcile change in net assets to net cash provided by operating activities:	
Depreciation	40,304
Provision for loss on uncollectible contributions	67,466
Change in operating assets and liabilities:	
Unconditional promises to give	(117,365)
Other current assets	(8,774)
Accounts payable and accrued expenses	(144)
Net cash provided by operating activities	<u>18,435</u>
Cash flows from investing activities:	
Purchases of property and equipment	<u>(21,584)</u>
Net cash used by investing activities	<u>(21,584)</u>
Cash flows from financing activities:	
Transfer of permanently restricted endowment funds	10,000
Proceeds from note payable	18,000
Principal payments on note payable	<u>(56,133)</u>
Net cash used by financing activities	<u>(28,133)</u>
Net decrease in cash and cash equivalents	(31,282)
Cash and cash equivalents, beginning of year	<u>95,930</u>
Cash and cash equivalents, end of year	<u><u>\$ 64,648</u></u>
Supplemental schedule of cash flow information:	
Interest paid	<u><u>\$ 5,552</u></u>

See accompanying notes to financial statements.

MAGDALENE, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2006

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Organization

Magdalene, Inc. and Subsidiary is a nonprofit corporation, organized in the state of Tennessee in 1993. Its mission is to provide sanctuary, therapeutic and education programs for women with a history of prostitution who are motivated to seek a healthy lifestyle in a secure and compassionate environment.

The Organization operates from facilities located in Nashville, Tennessee and attracts its participants and its support primarily from the Middle Tennessee area. The Organization is supported primarily by contributions from the general public, by fees for rehabilitation services provided for the men who are arrested for first offense soliciting in conjunction with the local court system, and by fundraising events.

The following program services are provided by the Organization:

Women's sanctuary and rehabilitation – A two-year residential community that provides housing and education for women with a criminal history of addiction and prostitution.

Men's rehabilitation – A program that conducts therapy seminars to first time offenders of prostitution solicitation.

Thistle Farms – A program that requires all participants to assist in manufacturing and selling selected domestic home items, such as candles, skin and lip balms, bath salts, etc. under the brand name of Thistle Farms. The program assists the participants in acquiring and developing life skills needed to assimilate into the workplace at the completion of the program.

During the fiscal year ended June 30, 2005, the Organization established a wholly owned entity, Magdalene Homes, LLC, to construct residential housing for graduates of its program (see note 8).

Principles of Consolidation

The consolidated statements include the accounts and activities of Magdalene, Inc. and Magdalene Homes, LLC referred herein as the "Organization". All significant intercompany accounts and transactions have been eliminated in consolidation.

Basis of Presentation

The accompanying financial statements have been prepared on the accrual basis of accounting in accordance with U.S. generally accepted accounting principles. Net assets and revenues, expenses, gains and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, net assets of the Organization and changes therein are classified and reported as follows:

MAGDALENE, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2006

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

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

Temporarily restricted net assets – Net assets subject to donor-imposed stipulations that may or will be met, either by actions of the Organization and/or the passage of time. When a restriction expires, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of activities as net assets released from restrictions.

Permanently restricted net assets – Net assets subject to donor-imposed stipulations that they be maintained permanently by the Organization. Generally, the donors of these assets permit the Organization to use all or part of the income earned and any related investments for general or specific purposes.

Cash and Cash Equivalents

For purposes of the statement of cash flows, the Organization considers all cash and related short-term investments with original maturities of three months or less to be cash equivalents.

Unconditional Promises to Give

Contributions are recognized when the donor makes a promise to give to the Organization that is, in substance, unconditional. Contributions that are restricted by the donor are reported as increases in unrestricted net assets if the restrictions expire in the fiscal year in which the contributions are recognized. All other donor restrictions are reported as increases in temporarily or permanently restricted net assets depending on the nature of the restrictions. When a restriction expires, temporarily restricted net assets are reclassified to unrestricted net assets. The Organization uses the allowance method to determine uncollectible unconditional promises to give.

Property and Equipment

Property and equipment are recorded at cost or, if donated, at the estimated fair market value as of the date of donation. Depreciation is provided using the straight-line basis over the estimated useful lives of the respective assets. Expenditures for repairs and maintenance are charged to expense as incurred.

Income Taxes

Magdalene, Inc. is exempt from income tax under Section 501(c)(3) of the Internal Revenue Code and is not a private foundation. Therefore, no provision for federal income taxes is included in the accompanying financial statements.

MAGDALENE, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2006

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Functional Allocation of Expenses

The costs of providing program services and supporting services have been summarized on a functional basis in the statement of activities. Accordingly, certain costs have been allocated among the programs and supporting services benefited based upon management's estimate.

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 certain amounts and disclosures. Actual results could differ from those estimates.

Donated Goods and Services

Donated goods and services are recognized at the fair value of items received at the time of donation. Volunteer time is recognized to the extent such time is provided by individuals with specialized training and which would normally need to be purchased. The Organization also receives volunteer services from a number of individuals in carrying out its programs but not meeting the criteria for recognition in the financial statements.

Concentration of Credit Risk

The Organization maintains cash balances with banks and other financial institutions which at times may exceed federally insured limits. Credit risk is managed by maintaining all deposits in high quality financial institutions.

NOTE 2 – UNCONDITIONAL PROMISES TO GIVE

Unconditional promises to give consist of the following at June 30, 2006:

Capital campaign	\$ 16,000
It's a Gift campaign	99,475
Love Feast campaign	186,455
Other	<u>17,219</u>
Subtotal	319,149
Less: allowance for uncollectible contributions	(45,000)
Less: discount to net present value	<u>(15,756)</u>
Net unconditional promises to give	<u>\$ 258,393</u>

MAGDALENE, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2006

NOTE 2 – UNCONDITIONAL PROMISES TO GIVE (Continued)

Receivable in less than one year, net	\$ 161,446
Receivable in one to five years, net	<u>96,947</u>
	<u>\$ 258,393</u>

NOTE 3 – PROPERTY AND EQUIPMENT

Property and equipment at June 30, 2006, consists of the following:

Land and buildings	\$ 889,498
Furniture, fixtures and equipment	21,337
Vehicle	20,247
Leasehold improvements	<u>10,236</u>
	941,318
Less: accumulated depreciation	<u>(101,926)</u>
	<u>\$ 839,392</u>

NOTE 4 – NOTE PAYABLE

During fiscal year 2006, the Organization refinanced its existing loan agreement with a bank. Under the terms of the agreement, the Organization pays interest monthly at a fixed rate of 7.5%. Final principal payments are due in February 2007. Borrowings under this agreement are secured by a first deed of trust on certain property. Amounts outstanding under the loan totaled \$61,867 at June 30, 2006.

NOTE 5 – NET ASSETS

Temporarily restricted net assets consist of the following at June 30, 2006:

Unconditional promises to give due in future periods	\$ 258,393
Contributions restricted for dental care	2,451
Contributions restricted for Thistle Farms	<u>15,000</u>
	<u>\$ 275,844</u>

Permanently restricted net assets are restricted to investment in perpetuity, the income from which is expendable to support the operations of the Organization. Permanently restricted net assets totaled \$65,000 at June 30, 2006.

MAGDALENE, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2006

NOTE 6 – LEASES

In conjunction with its community outreach program, The Campus for Human Development (“the Campus”), leases two homes in Nashville to the Organization, which uses these houses to provide safe residences for women in the program. Both houses are leased annually for one dollar (\$1) per year with the Organization paying all utilities. Insurance and minor repairs are paid for by the Campus as part of the lease agreement. The leases are renewable at the discretion of the Campus. Management has estimated the fair market rental value of the combined annual leases to be \$10,200 which has been recorded as rent expense and as contribution revenue.

NOTE 7 – RELATED PARTIES

The Executive Director is an Episcopalian priest who is assigned to Saint Augustine’s Chapel (“the Chapel”) on the campus of Vanderbilt University in Nashville, Tennessee, and receives no compensation from the Organization.

The Organization operates its administrative facilities from the Chapel, which donates the use of these facilities without cost, other than direct reimbursable expenses, as part of its community outreach program. Expenses reimbursed to the Chapel for program and administrative assistance were \$24,005 for the year ended June 30, 2006.

The Treasurer maintains the internal bookkeeping records of the Organization and was paid \$4,434 for these services in the year ended June 30, 2006.

NOTE 8 – MAGDALENE HOMES, LLC

Magdalene Homes, LLC, was organized on April 1, 2004 as a Tennessee limited liability company and is owned 100% by Magdalene, Inc. As of June 30, 2006, Magdalene Homes, LLC had purchased two parcels of property in Nashville, Tennessee for the purpose of building residential homes for graduates of its program. No construction activity has commenced as of June 30, 2006.

NOTE 9 – COMMUNITY FOUNDATION OF MIDDLE TENNESSEE INVESTMENTS

The Community Foundation of Middle Tennessee, a separate nonprofit organization, maintains investments on behalf of the Organization. The Community Foundation has ultimate authority and control over the investments; accordingly, the net assets of the Organization do not include these investments.

The Organization does anticipate receiving periodic investment earnings on its pro-rata share of the Community Foundation’s assets. The balance of the endowment fund held for the benefit of the Organization totaled approximately \$40,000 at June 30, 2006.

MAGDALENE, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2006

NOTE 10 – RESTATEMENT

The Organization discovered an error in the classification in net assets at June 30, 2005. As a result, unrestricted net assets have been decreased by \$50,795, temporarily restricted net assets have been increased by \$125,795, and permanently restricted net assets have been decreased by \$75,000 at June 30, 2005. The restatement had no effect on total change in net assets for the year ended June 30, 2005.