MONROE HARDING, INC.

FINANCIAL STATEMENTS

December 31, 2012

MONROE HARDING, INC.

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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors of
Monroe Harding, Inc.
Nashville, Tennessee

Report on the Financial Statements

We have audited the accompanying financial statements of Monroe Harding, Inc. (a nonprofit organization), which comprise the statement of financial position as of December 31, 2012, and the related 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 Financial Statements

Management is responsible for the preparation and fair presentation of these 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 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 financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the 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 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 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 financial statements referred to above present fairly, in all material respects, the financial position of Monroe Harding, Inc. as of December 31, 2012, and the changes in its net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated May 16, 2013, on our consideration of Monroe Harding Inc.'s internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Monroe Harding, Inc.'s internal control over financial reporting and compliance.

Frasier, Dean & Howell, PLLC

May 16, 2013

MONROE HARDING, INC.
STATEMENT OF FINANCIAL POSITION
December 31, 2012

Assets

Cash and cash equivalents	$ 1,169,003
Accounts receivable	479,336
Prepaid expenses	27,591
Investments	4,652,397
Pooled investments	15,841
Beneficial interests in perpetual trusts	558,073
Land, buildings and equipment,	
net of accumulated depreciation of $1,211,868	1,004,494
Total assets	$ 7,906,735

Liabilities and Net Assets

Liabilities:	
Accounts payable	$ 277,530
Accrued expenses	131,196
Children's account	4,477
Total liabilities	413,203
Net assets:	
Unrestricted:	
Undesignated	1,882,159
Board designated endowment	4,528,490
Total unrestricted	6,410,649
Temporarily restricted	385,062
Permanently restricted	697,821
Total net assets	7,493,532
Total liabilities and net assets	$ 7,906,735

See accompanying notes to financial statements.

MONROE HARDING, INC.
STATEMENT OF ACTIVITIES
For the Year Ended December 31, 2012

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Public support and revenue:				
Public support:				
Governmental contracts and sub-contracts	$ 3,663,779	$ -	$ -	$ 3,663,779
Church and private gifts	396,656	303,066	139,748	839,470
Special events	146,266	-	-	146,266
Miscellaneous	41,466	-	-	41,466
Gifts in-kind	20,290	8,160	-	28,450
Net assets released from restriction	231,558	(217,664)	(13,894)	-
Total public support	4,500,015	93,562	125,854	4,719,431
Revenue:				
Gain on disposal of property and equipment	1,192,017	-	-	1,192,017
Net gain on investments	395,364	-	53,334	448,698
Interest and dividend income, net of fees	110,467	-	11,981	122,448
Total public support and revenue	6,197,863	93,562	191,169	6,482,594
Expenses:				
Program services:				
Cooperative living	1,316,966	-	-	1,316,966
Middle Tennessee Collaborative	1,734,541	-	-	1,734,541
Independent living	221,023	-	-	221,023
Foster care	567,217	-	-	567,217
Youth Connections	308,274	-	-	308,274
Total program services	4,148,021	-	-	4,148,021
Supporting services:				
General and administrative	571,575	-	-	571,575
Development	280,401	-	-	280,401
Total supporting services	851,976	-	-	851,976
Total expenses	4,999,997	-	-	4,999,997
Change in net assets	1,197,866	93,562	191,169	1,482,597
Net assets, beginning of year	5,212,783	291,500	506,652	6,010,935
Net assets at end of year	$ 6,410,649	$ 385,062	$ 697,821	$ 7,493,532

See accompanying notes to financial statements.

MONROE HARDING, INC.
STATEMENT OF CASH FLOWS
For the Year Ended December 31, 2012

Cash flows from operating activities:	
Change in net assets	$ 1,482,597
Adjustments to reconcile change in net assets to net cash used in operating activities:	
Depreciation	87,277
In-kind donation of investments	(9,899)
Change in beneficial interests in perpetual trusts	(51,421)
Change in pooled investments	(15,841)
Gain on disposal of property and equipment	(1,192,017)
Net gain on investments	(375,078)
Changes in operating assets and liabilities:	
Accounts receivable	(105,643)
Prepaid expenses	4,525
Accounts payable	81,306
Accrued expenses	(3,722)
Children's account	(14,271)
Net cash used in operating activities	(112,187)
Cash flows from investing activities:	
Purchases of property and equipment	(309,169)
Purchases of investments	(12,018,098)
Proceeds from disposal of property and equipment	1,198,953
Proceeds from sale of investments	11,660,043
Net cash provided by investing activities	531,729
Net increase in cash and cash equivalents	419,542
Cash and cash equivalents, beginning of year	749,461
Cash and cash equivalents, end of year	$ 1,169,003
Supplemental schedule of non-cash investing and financing activities:	
In-kind donation of investments	$ 9,899

See accompanying notes to financial statements.

MONROE HARDING, INC.
STATEMENT OF FUNCTIONAL EXPENSES
For the Year Ended December 31, 2012

	Program Services						Supporting Services			
	Cooperative Living	Middle Tennessee Collaborative	Independent Living	Foster Care	Youth Connections	Total	General and Administrative	Development	Total	Total Expenses
Salaries and wages	$ 746,971	$ 41,248	$ 109,206	$ 224,171	$ 136,281	$ 1,257,877	$ 334,116	$ 130,144	$ 464,260	$ 1,722,137
Collaborative partner expenses	-	1,675,445	-	-	-	1,675,445	-	-	-	1,675,445
Employee benefits	155,141	9,672	15,794	37,534	23,495	241,636	14,449	22,736	37,185	278,821
Foster care expenses	-	-	-	194,564	-	194,564	-	-	-	194,564
Payroll taxes	51,918	2,666	8,120	16,730	10,178	89,612	24,893	9,200	34,093	123,705
Rent	-	-	46,200	-	58,000	104,200	-	-	-	104,200
Maintenance	36,109	280	2,120	4,209	10,528	53,246	47,684	2,474	50,158	103,404
Food and kitchen supplies	56,799	-	8,383	87	1,046	66,315	6,821	6,877	13,698	80,013
Youth specific assistance	36,456	-	5,750	14,203	16,656	73,065	-	-	-	73,065
Insurance	34,060	1,195	5,606	13,235	6,764	60,860	8,246	2,316	10,562	71,422
Professional expenses	1,550	2,000	1,550	1,550	3,660	10,310	56,683	3,855	60,538	70,848
Training and education	31,707	458	3,962	3,893	10,565	50,585	9,294	4,358	13,652	64,237
Printing and promotion	1,023	14	18	158	54	1,267	3,838	58,628	62,466	63,733
Utilities	37,115	291	1,567	1,496	8,176	48,645	11,016	942	11,958	60,603
Telephone and internet	20,044	323	2,706	6,854	6,353	36,280	5,990	1,706	7,696	43,976
Office supplies	9,986	8	641	6,353	1,002	17,990	21,525	4,051	25,576	43,566
Travel and transportation	12,689	500	2,642	13,751	1,644	31,226	3,913	507	4,420	35,646
Contracted services	4,587	21	339	784	2,170	7,901	746	21,479	22,225	30,126
Recruitment	4,077	82	158	19,338	639	24,294	1,055	1,173	2,228	26,522
Recreational and special	5,483	175	1,244	3,510	1,340	11,752	12,162	1,108	13,270	25,022
Dorm supplies	10,820	-	1,015	-	-	11,835	-	-	-	11,835
Other	-	-	21	117	589	727	732	8,371	9,103	9,830
	1,256,535	1,734,378	217,042	562,537	299,140	4,069,632	563,163	279,925	843,088	4,912,720
Depreciation	60,431	163	3,981	4,680	9,134	78,389	8,412	476	8,888	87,277
Total expenses	$ 1,316,966	$ 1,734,541	$ 221,023	$ 567,217	$ 308,274	$ 4,148,021	$ 571,575	$ 280,401	$ 851,976	$ 4,999,997

See accompanying notes to financial statements.

MONROE HARDING, INC.
NOTES TO THE FINANCIAL STATEMENTS
December 31, 2012

NOTE 1 – NATURE OF OPERATIONS

Monroe Harding, Inc. (the “Organization”) is a not-for-profit organization that continues to change young people’s lives every day. Founded in 1893 as an orphanage, the Organization now serves children and youth who are in state’s custody. The Organization believes every child deserves the chance for a better life. The Organization’s programs include foster care, cooperative living, independent living, and a resource center for older youth. The Organization’s range of services includes education, vocational skills, relationship building, spiritual formation, health & wellness, and – most importantly – the guidance and support of a caring adult in a safe and stable home.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of the Organization are presented on the accrual basis. The significant accounting policies followed are described below:

Basis of Presentation

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:

> 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.
>
> Permanently restricted net assets – Net assets subject to donor-imposed stipulations that they be maintained permanently by the Organization.

All contributions are considered to be available for unrestricted use unless specifically restricted by the donor. Amounts received that are designated for future periods or restricted by the donor for specific purposes are reported as temporarily restricted or permanently restricted support that increases those net asset classes. However, if a restriction is fulfilled in the same time period in which the contribution is received, the Organization reports the support as unrestricted.

Cash Equivalents

For purposes of the statement of cash flows, the Organization considers all highly liquid investments with an original maturity of three months or less when purchased to be cash equivalents.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Contributions

The Organization reports gifts of cash and other assets as restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or the purpose of the restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of activities as net assets released from restriction.

The Organization reports gifts of land, buildings, and equipment 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. Absent explicit donor stipulations about how long those long-lived assets must be maintained, the Organization reports expirations of donor restrictions when the donated or acquired long-lived assets are placed in service.

Investments

All gains and losses on investments are reported in the statement of activities as increases or decreases in unrestricted net assets unless their use is temporarily or permanently restricted by explicit donor stipulations or by law.

Land, Buildings and Equipment

Land, buildings and equipment are stated at cost. The fair value of donated labor services associated with fixed assets is added to the cost of the asset. Repairs and maintenance are charged to expense as incurred. Depreciation is computed using the straight-line method over the estimated useful lives of the assets, which range from three to thirty-nine years.

Income Taxes

The Organization is exempt from federal income taxes under the provisions of Internal Revenue Code Section 501(c)(3). Accordingly, no provision for income taxes is included in the accompanying financial statements. The Organization follows Financial Accounting Standards Board Accounting Standards Codification ("FASB ASC") guidance that clarifies the accounting for uncertainty in income taxes recognized in an entity's financial statements. This guidance prescribes a minimum probability threshold that a tax position must meet before a financial statement benefit is recognized. The minimum threshold is defined as a tax position that is more likely than not to be sustained upon examination by the applicable taxing authority, including resolution of any related appeals or litigation processes, based on the technical merits of the position. The tax benefit to be recognized is measured as the largest amount of benefit that is greater than fifty percent likely of

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Income Taxes (Continued)

being realized upon ultimate settlement. The Organization has no tax penalties or interest reported in the accompanying financial statements. Tax years that remain open for examination include the years ended December 31, 2009 through December 31, 2012. The Organization had no uncertain tax positions at December 31, 2012.

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 financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Functional Allocation of Expenses

The costs of providing the various programs and other activities have been summarized on a functional basis in the statement of functional expenses. Accordingly, certain costs have been allocated among program and supporting services based on estimates made by management.

Fair Value Measurements

The Organization has adopted the provisions of the Fair Value Measurement topic of the FASB ASC. This guidance establishes a framework for measuring fair value for financial assets and liabilities. That framework provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets (level 1 measurements) and the lowest priority to unobservable inputs (level 3 measurements). The fair value of a financial instrument is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value is best determined based upon quoted market prices (level 1). However, in some instances, there are no quoted market prices for financial instruments. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques (level 3). Those techniques are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. In that regard, the derived fair value estimates cannot be substantiated by comparison to independent markets and, in many cases, could not be realized in immediate settlement of the instruments.

The three levels of the fair value hierarchy are described below:

Level 1 Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that the Organization has the ability to access.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Fair Value Measurements (Continued)

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.

If the asset or liability has a specified (contractual) term, the level 2 input must be observable for substantially the full term of the asset or liability.

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

Subsequent Events

Management has evaluated subsequent events through May 16, 2013, when these financial statements were available to be issued. The Organization is not aware of any significant events that occurred subsequent to the statement of financial position date but prior to the filing of this report that would have a material impact on the financial statements.

NOTE 3 – ACCOUNTS RECEIVABLE

Accounts receivable are due primarily from various government and private agencies and are expected to be received within one year. The carrying values of accounts receivable approximate their fair values due to the short maturities of these instruments. No allowance for uncollectible amounts was considered necessary at December 31, 2012.

NOTE 4 – INVESTMENTS

The following table sets forth by level, within the fair value hierarchy, the Organization's assets at fair value at December 31, 2012:

	Level 1	Level 2	Total
Equity funds	$ 1,568,724	$ 1,108,425	$ 2,677,149
Fixed income funds	509,039	638,239	1,147,278
Other investments	353,203	17,531	370,734
Cash and short term investments	307,236	-	307,236
Corporate bonds	150,000	-	150,000
Pooled accounts	-	15,841	15,841
Total	$ 2,888,202	$ 1,780,036	$ 4,668,238

NOTE 4 – INVESTMENTS (Continued)

The following schedule summarizes the net investment income in the statement of activities for 2012:

Dividend and interest income, net of fees of ($33,714)	$ 122,448
Net realized gains on investments	431,818
Net unrealized gains on investments	16,880
	$ 571,146

NOTE 5 – LAND, BUILDINGS AND EQUIPMENT

A summary of land, buildings and equipment as of December 31, 2012 is as follows:

Land	$ 17,409
Buildings and improvements	1,323,229
Automobiles	129,940
Land improvements	103,107
Furniture, fixtures, and appliances	300,682
Information/communication technology	110,690
Construction in progress	231,305
	2,216,362
Less accumulated depreciation	(1,211,868)
Property and equipment, net	$ 1,004,494

NOTE 6 – BENEFICIAL INTERESTS IN PERPETUAL TRUSTS

The Organization is the beneficiary of two perpetual trusts held by others. The Stanley Trust is held by Westminster Presbyterian Church of Nashville, Tennessee. Distributions from the Stanley Trust may be made annually up to 5.5% of the average annual value of the trust. Distributions may not reduce the value of trust to less than the original principal amount. At December 31, 2012, the trust had a fair market value of $79,201. The Plummer Trust is held by First Presbyterian Church of Clarksville, Tennessee. The Organization is a 25% beneficiary of the trust and receives periodic distributions from the trust. At December 31, 2012, the trust had a fair market value of $1,915,484, of which $478,872 was for the benefit of the Organization. The trusts' assets are invested in publicly traded mutual funds and are considered to be level 1 investments.

NOTE 7 – TEMPORARILY RESTRICTED NET ASSETS

Temporarily restricted net assets at December 31, 2012 consist of the following:

Capital improvements	$ 226,100
Youth education	51,688
Cooperative living program	41,250
Special projects	28,256
Foster care	18,458
Youth Connections program	17,693
Independent living program	1,617
	$ 385,062

Net assets of $217,664 were released from donor restrictions by satisfying the restricted purposes or by occurrence of other events specified by donors during the year ended December 31, 2012. The purpose restrictions accomplished were for program services and the acquisition of capital assets.

NOTE 8 – GIFTS IN-KIND

Gifts in-kind received by the Organization are recorded based on their estimated value on the date of receipt. During 2012, the Organization recorded donated materials and services with an estimated value of $28,450 and donated investments with a value of $9,899. No amounts have been reflected in the financial statements for donated labor by unskilled volunteers as no objective basis is available to measure the value of such services; however, a substantial number of volunteers have donated significant amounts of their time to the Organization's program services.

NOTE 9 – RETIREMENT PLAN

The Organization has a retirement plan in accordance with Internal Revenue Code Section 401. The plan is a defined contribution plan that covers full-time employees who have a minimum of one year of service with the Organization or another nonprofit organization. The Organization contributes a minimum amount equal to 4% of the participants' compensation. The Organization also contributes additional matching contributions up to 4% of the participants' compensation. Employer contributions are fully vested after four years of service with the Organization or any other nonprofit health or social service organization. Total pension expense incurred during the year ended December 31, 2012 was $68,422.

NOTE 10 – COMMITMENTS AND CONTINGENCIES

The Company has entered into noncancelable operating lease agreements for certain office equipment and office space. The Organization has also entered into leases for independent living units with required monthly rent payments totaling approximately $4,000. These leases are cancelable at the end of each annual renewal period. Rent expense for all leases for 2012 totaled $107,677.

The future minimum lease payments under noncancelable operating lease arrangements are as follows for the years ending December 31:

2013	$ 60,929
2014	23,452
2015	2,864
	$ 87,245

NOTE 11 – BOARD DESIGNATED FUNDS

The board of directors has designated funds for a board designated endowment. One of the common uses of board designated funds is for periodic distributions to cover operating expenses that cannot be met with available cash from operations. At December 31, 2012, the board designated balances were as follows:

Endowment	$ 4,528,490
Total board designated net assets:	$ 4,528,490

NOTE 12 – CONCENTRATION OF CREDIT RISK

The Organization maintains its cash and cash equivalents in financial institutions with balances which, at times, may exceed federally insured limits. The Organization has not experienced any losses in such accounts. Management believes it is not exposed to any significant concentration risk on cash and cash equivalents.

The Organization is the lead agency of the Middle Tennessee Collaborative (the "Collaborative). The Collaborative has several contracts with agencies of the State of Tennessee to provide residential and foster care services for youth. As the lead agency in the Collaborative, the Organization bills the state agencies for services provided by all of the member agencies and remits payments to the member agencies, less an agreed upon administration fee. During the year ended December 31, 2012, approximately $3,334,000 was recorded as revenue from state agency contracts for services provided by the Collaborative. This accounted for approximately 51% of total public support and revenue recognized by the Organization during 2012. At December 31, 2012, approximately $393,000 was receivable from the state agencies related to those contracts. During the year ended

NOTE 12 – CONCENTRATION OF CREDIT RISK (Continued)

December 31, 2012, the Organization recognized expenses totaling approximately $1,675,000 for the amounts earned by the other members of the Collaborative for their services. At December 31, 2012, approximately $187,000 was due to Collaborative members for these services.

NOTE 13 – ENDOWMENT AND PERMANENTLY RESTRICTED NET ASSETS

The Organization's endowment consists of individual funds established for a variety of purposes and includes both donor restricted endowment funds and funds designated by the board of directors to function as endowments. As required by generally accepted accounting principles, net assets associated with endowment funds, including funds designated by the board of directors to function as endowments, are classified and reported based upon the existence or absence of donor-imposed restrictions. Permanently restricted endowment funds are beneficial interests in perpetual trusts held by the Westminster Presbyterian Church of Nashville and First Presbyterian Church of Clarksville, Tennessee.

Interpretation of Relevant Law

The board of directors of the Organization has interpreted the State Prudent Management of Institutional Funds Act ("SPMIFA") 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 at the time the accumulation is added to the fund.

The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Organization in a manner consistent with the standard of prudence prescribed by SPMIFA. In accordance with SPMIFA, the Organization considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

- The duration and preservation of the fund
- The purposes of the Organization and the donor-restricted endowment fund
- General economic conditions
- The possible effect of inflation and deflation
- The expected total return from income and the appreciation of investments
- The investment policies of the Organization

NOTE 13 – ENDOWMENT AND PERMANENTLY RESTRICTED NET ASSETS (Continued)

Return Objectives and Risk Parameters

The Organization has adopted investment spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the Organization must hold in perpetuity or for donor-specified periods as well as board-designated funds. Under this policy, as approved by the board of directors, the endowment assets are invested in a manner that is intended to produce results that exceed the price and yield results of selected market and comparative indices while assuming a moderate level of investment risk. Actual returns will vary in any given year.

Strategies Employed for Achieving Investment Objectives

To satisfy its long-term rate-of-return objectives, the Organization relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The Organization targets a diversified asset allocation that places a greater emphasis on equity-based investments to achieve its long-term return objectives within prudent risk constraints.

Spending Policy and How the Investment Objectives Relate to Spending Policy

The Organization has a policy which provides for the board of directors to identify distribution amounts, as needed, to fund the Organization's programs. In establishing this policy, the Organization considered the long-term expected return on its endowment. This is consistent with the Organization's objective to maintain the purchasing power of the endowment assets held in perpetuity or for a specified term as well as to provide additional real growth through new gifts and investment return.

Endowment Net Asset Composition by Type of Fund as of December 31, 2012:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Donor-restricted endowment funds	$ -	$ -	$ 697,821	$ 697,821
Board-restricted endowment funds	4,528,490	-	-	4,528,490
Total funds	$ 4,528,490	$ -	$ 697,821	$ 5,226,311

NOTE 13 – ENDOWMENT AND PERMANENTLY RESTRICTED NET ASSETS (Continued)

Changes in Endowment Net Assets for the Year Ended December 31, 2012:

Endowment net assets, beginning of year	$ 3,909,365	$ -	$ 506,652	$ 4,416,017
Investment return:				
Investment income	108,101	-	11,981	120,082
Net appreciation (realized and unrealized)	375,078	-	53,334	428,412
Total investment return	483,179	-	65,315	548,494
Contributions	-	-	139,748	139,748
Board designated transfers to endowment	135,946	-	-	135,946
Appropriation of endowment assets for expenditure	-	-	(13,894)	(13,894)
Endowment net assets, end of year	$ 4,528,490	$ -	$ 697,821	$ 5,226,311

INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

To the Board of Directors of
Monroe Harding, Inc.

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to the financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of Monroe Harding, Inc. (a nonprofit organization), which comprise the statement of financial position as of December 31, 2012, and the related statements of activities, functional expenses, and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated May 16, 2013.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered Monroe Harding, Inc.'s internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Monroe Harding, Inc.'s internal control. Accordingly, we do not express an opinion on the effectiveness of the Organization's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified. We did identify a certain deficiency in internal control, described below, that we consider to be a significant deficiency.

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Financial Reporting

During the year ended December 31, 2012, the Organization utilized the year-end audit to adjust its internal accounting records in order to present them in accordance with generally accepted accounting principles. We have communicated all adjustments identified during our audit to management. Adjustments primarily related to properly recording and classifying investment activity, including activity in the beneficial interest in trusts. We suggest that management establish a year-end closing process that does not utilize the year-end audit to record adjustments to be in accordance with generally accepted accounting principles.

Management's Response:

The Director of Financial Services holds an MBA in accounting and has the assistance of the Treasurer and Chairman of the Finance Committee, a practicing CPA, in preparing reliable financial statements. The knowledge and background of these individuals should result in financial statements that are prepared in accordance with GAAP.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Monroe Harding, Inc.'s financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the Organization's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Organization's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

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May 16, 2013