

State Bar of Texas

Financial Statements

For the Year Ended May 31, 2014

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State Bar of Texas

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Independent Auditor's Report

To the Board of Directors
State Bar of Texas
Austin, Texas

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component unit, each major fund, and the aggregate remaining fund information of the State Bar of Texas (the "State Bar") as of and for the year ended May 31, 2014, and the related notes to the financial statements, which collectively comprise the State Bar's basic financial statements, as listed in the table of contents.

Management's Responsibility for the Financial Statements

State Bar's 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 opinions 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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of 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.

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

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, the aggregate discretely presented component unit, each major fund, and the aggregate remaining fund information of the State Bar as of May 31, 2014, and the respective changes in financial position and, where applicable, cash flows thereof, for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

Other Matters

Emphasis of Matter

As described in Note 1, the State Bar implemented Governmental Accounting Standards Board (“GASB”) Statement No. 65, *Items Previously Reported as Assets and Liabilities*. Our opinion is not modified with respect to these matters.

Required Supplemental Information

Accounting principles generally accepted in the United States of America require that the management’s discussion and analysis and Schedule of Revenues, Expenditures, and Changes in Fund Balance – Budget (GAAP Basis) and Actual – General Fund, as listed in the table of contents, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by GASB, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplemental information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management’s responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Supplemental Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the State Bar’s basic financial statements. The combining balance sheet – nonmajor governmental funds, combining statement of revenues, expenditures, and changes in fund balances – nonmajor governmental funds, and the combining statement of revenues, expenditures, and changes in fund balances – governmental funds, as listed in the table of contents, are presented for purposes of additional analysis and are not a required part of the basic financial statements.

The combining balance sheet – nonmajor governmental funds, combining statement of revenues, expenditures, and changes in fund balances – nonmajor governmental funds, and the combining statement of revenues, expenditures, and changes in fund balances – governmental funds are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the basic financial statements as a whole.

Padgett, Statemann + Co., L.L.P.

Austin, Texas
November 12, 2014

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State Bar of Texas

Management's Discussion and Analysis

May 31, 2014

The following is a discussion and analysis of the State Bar of Texas' (the "State Bar") financial performance for the fiscal year ended May 31, 2014. This section is a summary of the State Bar's financial activities based on currently known facts, decisions, or conditions. It is also based on both the government-wide and fund-based financial statements. The results of the current year are discussed in comparison to the prior year, with emphasis placed on the current year. This section is only an introduction and should be read in conjunction with the State Bar's financial statements, which immediately follow this section.

Financial Highlights

- The assets of the State Bar exceeded its liabilities at the close of the most recent fiscal year by \$38,190,511 (net position). This amount includes all State Bar-related assets, including the reserves, all capital assets, all assets related to the Texas Bar Book Fund, the Sections, and all special revenue funds and capital project funds. Of this amount, \$29,003,556 (unrestricted net position) may be used to meet the State Bar's ongoing obligations to creditors.
- The State Bar's total net position decreased by \$1,327,145 from the end of fiscal year 2013 to the end of fiscal year 2014.
- As of the close of the current fiscal year, the State Bar's governmental funds reported combined ending fund balances of \$28,604,347, a decrease of \$842,553 in comparison with the prior year. Of this amount, \$9,876,655 is available for spending at the State Bar's discretion (unassigned fund balance). The amount includes the General Fund, the Client Security Fund, the Special Revenue and Capital Projects Funds, and the Sections.
- At the end of the current fiscal year, the fund balance for the General Fund was \$14,644,753, or 38.1% of the total General Fund expenditures for the year ended May 31, 2014. Of this amount, \$4,330,913 is subject to the Board of Director's (the "Board") approval on how the funds may be used, and \$437,185 is nonspendable.

Overview of the Financial Statements

The State Bar's basic financial statements are comprised of the following components: (1) the government-wide financial statements, (2) the fund financial statements, (3) notes to the basic financial statements, and (4) the required supplementary information. Each one is described below.

Government-Wide Statements

The government-wide financial statements are designed to provide readers with a broad overview of the State Bar's finances, in a manner similar to a private-sector business. The statements include all assets and liabilities using the accrual basis of accounting. The government-wide financial statements are made up of the statement of net position and the statement of activities. The government-wide financial statements can be found on pages 20 through 22 of this report.

State Bar of Texas

Management's Discussion and Analysis – Continued

May 31, 2014

The **statement of net position** presents information on all the State Bar's assets and liabilities, with the difference between the two reported as net position. Over time, increases or decreases in net position may serve as a useful indicator of the financial position of the State Bar.

The **statement of activities** presents information showing how the State Bar's net position changed during the most recent fiscal year. The statement of activities is presented on the full accrual basis. This means that all changes in net position are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Therefore, revenues and expenses are reported in this statement for some items that will result in cash flows only in future fiscal periods (e.g., earned, but unused vacation leave). From the end of fiscal year 2013 to the end of fiscal year 2014, net position decreased by \$1,327,145.

Both government-wide financial statements distinguish functions of the State Bar that are principally supported by dues and intergovernmental revenues (government activities) from other functions that are intended to recover all or a significant portion of their costs through user fees and charges (business-type activities). The governmental activities of the State Bar include general government, public services, member services, and public protection. The business-type activities of the State Bar include the Texas Bar Book Fund.

Fund Financial Statements

A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The State Bar, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. The fund financial statements are made up of a balance sheet and a statement of revenues, expenditures, and changes in fund balances. The basic governmental fund financial statements can be found on pages 23 through 31 of this report. All of the funds of the State Bar can be divided into three categories: governmental funds, proprietary funds, and fiduciary funds.

The State Bar has three types of funds:

- *Governmental funds* – Governmental funds are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on near-term inflows and outflows of spendable resources, as well as on balances of spendable resources available at the end of the fiscal year. Such information may be useful in evaluating a government's near-term financing requirements.

Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near-term financing decision. Both the governmental fund balance sheet and the governmental fund statement of revenues, expenditures, and changes in fund balances provide a reconciliation to facilitate this comparison between governmental funds and governmental activities.

State Bar of Texas

Management's Discussion and Analysis – Continued

May 31, 2014

The State Bar maintains 11 individual governmental funds. Information is presented separately in the governmental fund balance sheet and in the governmental fund statement of revenues, expenditures, and changes in fund balances for the General Fund, the Client Security Fund, and Sections, all of which are considered to be major funds. Data from the other 8 governmental funds are combined into a single, aggregated presentation. These 8 funds are: Texas Board of Legal Specialization Fund, State Bar College, Annual Meeting, Texas Law Center, Technology Fund, Project Grants Fund, Hatton W. Sumners Grants Fund, and Law Focused Education. Individual fund data for each of these nonmajor governmental funds is provided in the form of combining statements elsewhere in the report.

- *Proprietary funds* – The Texas Bar Book Fund is the State Bar's one proprietary fund. It is an enterprise fund. An enterprise fund is used to report an entity's business-type activities in the government-wide financial statements. The basic proprietary fund financial statements can be found on pages 27 through 29 of this report.
- *Fiduciary funds* – Fiduciary funds are used to account for resources held for the benefit of parties outside the government. Fiduciary funds are not reflected in the government-wide financial statements because the resources of those funds are not available to support the State Bar's own programs. The accounting used for fiduciary funds is much like that used for proprietary funds. The only fiduciary fund the State Bar has is an agency fund used to hold moneys for donations received for access to justice. The basic fiduciary fund financial statement can be found on page 30 through 31 of this report.

In addition, the basic financial statements provide information regarding The State Bar's legally separate discretely presented component unit. Discretely presented component unit financial information is reported separately from the primary government.

Notes to the Financial Statements

The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the basic financial statements can be found on pages 33 through 49 of this report.

Required Supplemental Information

In addition to the basic financial statements and accompanying notes, this report also presents certain required supplementary information. The State Bar adopts an annual budget for its general fund. A budgetary comparison statement has been provided for the general fund to demonstrate compliance with this budget. Required supplemental information can be found on pages 52 through 54 of this report. Other supplemental information is provided on page 56 through 58.

Government-Wide Financial Analysis

Net Position

As noted earlier, net position may serve over time as a useful indicator of a government's financial position. In the case of the State Bar, assets exceeded liabilities by \$38,190,511 at the close of the most recent fiscal year.

State Bar of Texas

Management's Discussion and Analysis – Continued

May 31, 2014

The State Bar's net position invested in capital assets, net of accumulated depreciation (e.g., land, buildings, furniture, and equipment), less any related debt used to acquire those assets that is still outstanding reflects 24% of net position. The State Bar uses these capital assets to provide services to members; consequently, these assets are not available for future spending. Although the State Bar's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.

Table A-1
The State Bar's Net Position

| | 2014 | | | 2013 |
|-------------------------------------|------------------------------------|-------------------------------------|-----------------------------|-----------------------------|
| | Governmental Activities | Business-Type Activities | Total | Total |
| Current and other assets | \$ 45,212,621 | \$ 2,015,268 | \$ 47,227,889 | \$ 46,107,172 |
| Capital assets | <u>9,203,775</u> | <u>39,626</u> | <u>9,243,401</u> | <u>9,848,969</u> |
| Total assets | \$ <u>54,416,396</u> | \$ <u>2,054,894</u> | \$ <u>56,471,290</u> | \$ <u>55,956,141</u> |
| Total liabilities | \$ <u>18,136,641</u> | \$ <u>144,138</u> | \$ <u>18,280,779</u> | \$ <u>16,438,485</u> |
| Net position: | | | | |
| Net investment in capital assets | \$ 9,147,329 | \$ 39,626 | \$ 9,186,955 | \$ 9,639,170 |
| Unrestricted | <u>27,132,426</u> | <u>1,871,130</u> | <u>29,003,556</u> | <u>29,878,486</u> |
| Total net position | \$ <u>36,279,755</u> | \$ <u>1,910,756</u> | \$ <u>38,190,511</u> | \$ <u>39,517,656</u> |

State Bar of Texas

Management's Discussion and Analysis – Continued

May 31, 2014

Governmental Activities – Governmental activities decreased the State Bar's net position by \$1,365,701. Key elements of this increase are as follows:

Table A-2
Changes in the State Bar's Net Position

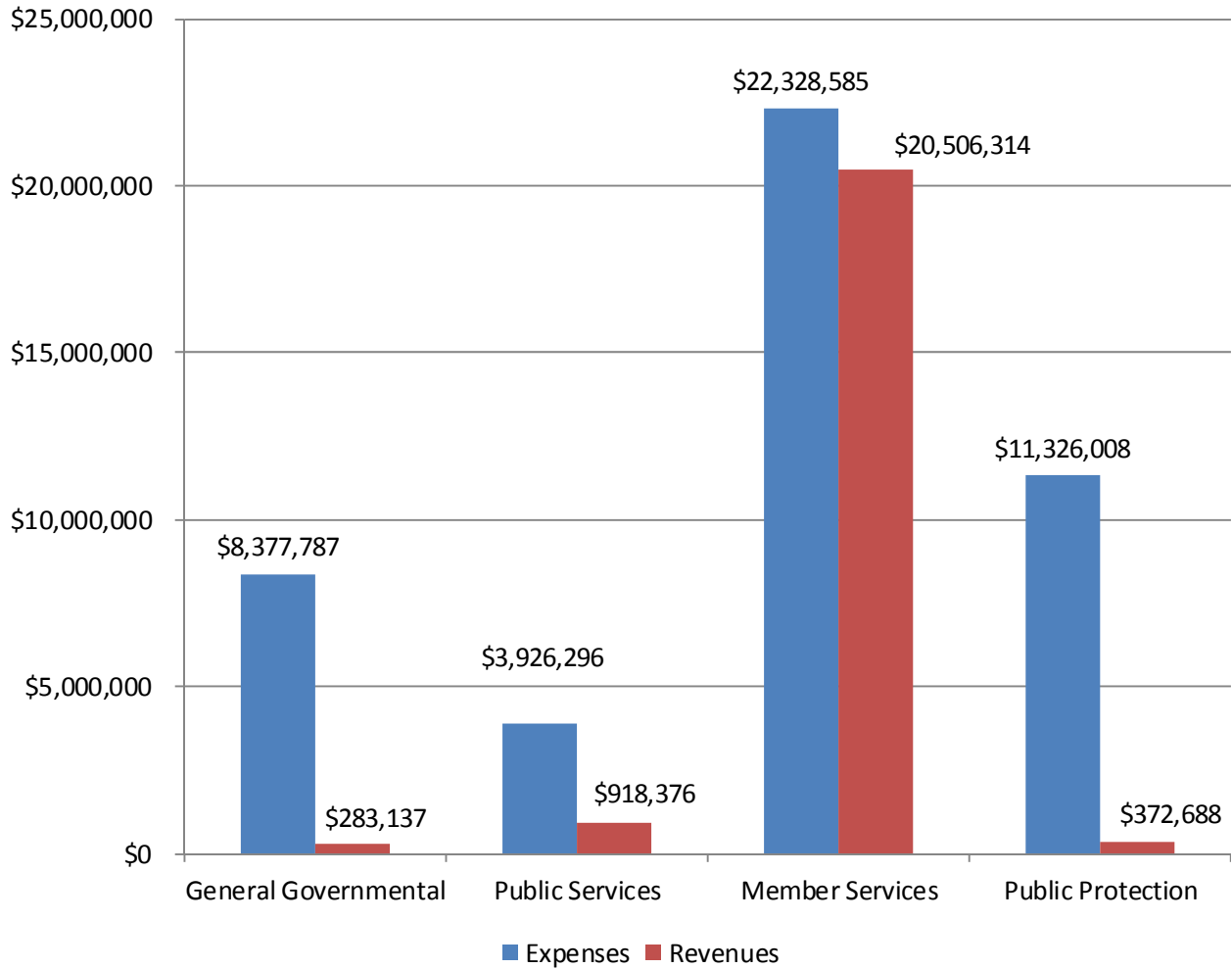
| | 2014 | | | 2013 Total |
|-------------------------------------|----------------------------|-----------------------------|----------------------|----------------------|
| | Governmental Activities | Business-Type Activities | Total | |
| Revenues | | | | |
| Program revenues: | | | | |
| Charges for services | \$ 20,556,408 | \$ 2,511,429 | \$ 23,067,837 | \$ 22,811,315 |
| Operating grants and contributions | 1,524,107 | - | 1,524,107 | 1,760,614 |
| General revenues: | | | | |
| Membership dues | 21,555,086 | - | 21,555,086 | 20,946,772 |
| Investment income | 115,787 | 389 | 116,176 | 101,452 |
| Royalty revenue | 489,925 | 977,853 | 1,467,778 | 878,740 |
| Other income | 351,662 | 4 | 351,666 | 829,959 |
| Total revenues | <u>44,592,975</u> | <u>3,489,675</u> | <u>48,082,650</u> | <u>47,328,852</u> |
| Expenses | | | | |
| General government | 8,377,787 | - | 8,377,787 | 7,721,083 |
| Public services | 3,926,296 | - | 3,926,296 | 3,513,383 |
| Member services | 22,328,585 | - | 22,328,585 | 21,332,716 |
| Public protection | 11,326,008 | - | 11,326,008 | 10,116,588 |
| Books | - | 3,451,119 | 3,451,119 | 2,912,184 |
| Total expenses | <u>45,958,676</u> | <u>3,451,119</u> | <u>49,409,795</u> | <u>45,595,954</u> |
| Increase (decrease) in net position | (1,365,701) | 38,556 | (1,327,145) | 1,732,898 |
| Net position at beginning of year | <u>37,645,456</u> | <u>1,872,200</u> | <u>39,517,656</u> | <u>37,784,758</u> |
| Net position at end of year | <u>\$ 36,279,755</u> | <u>\$ 1,910,756</u> | <u>\$ 38,190,511</u> | <u>\$ 39,517,656</u> |

State Bar of Texas

Management's Discussion and Analysis – Continued

May 31, 2014

Expense and Program Revenues – Governmental Activities

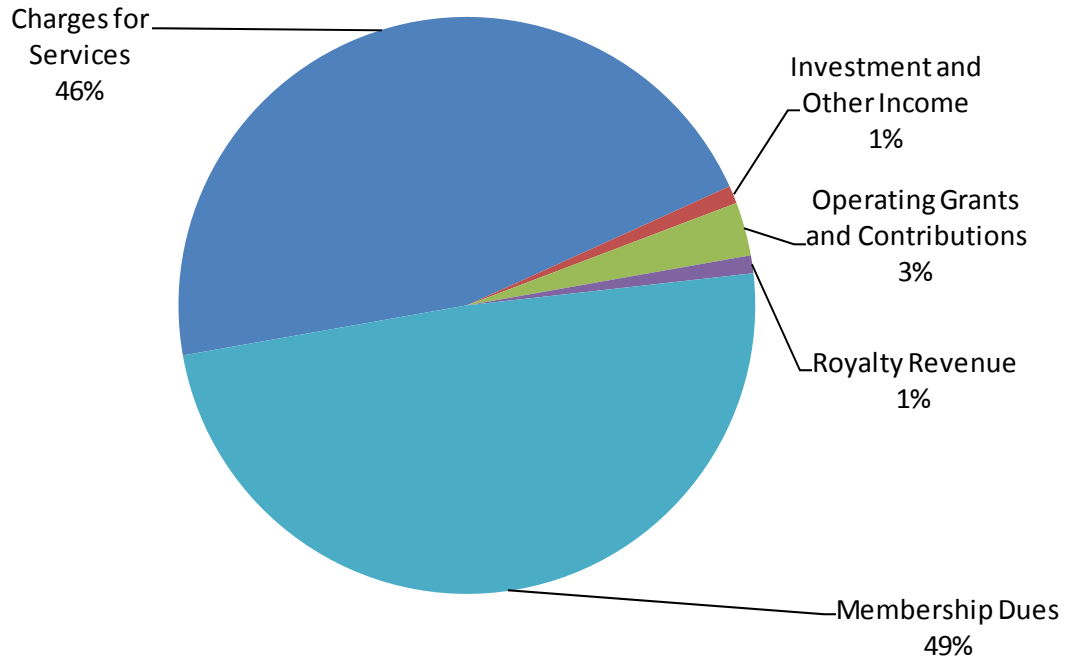


State Bar of Texas

Management's Discussion and Analysis – Continued

May 31, 2014

Revenues by Source – Governmental Activities



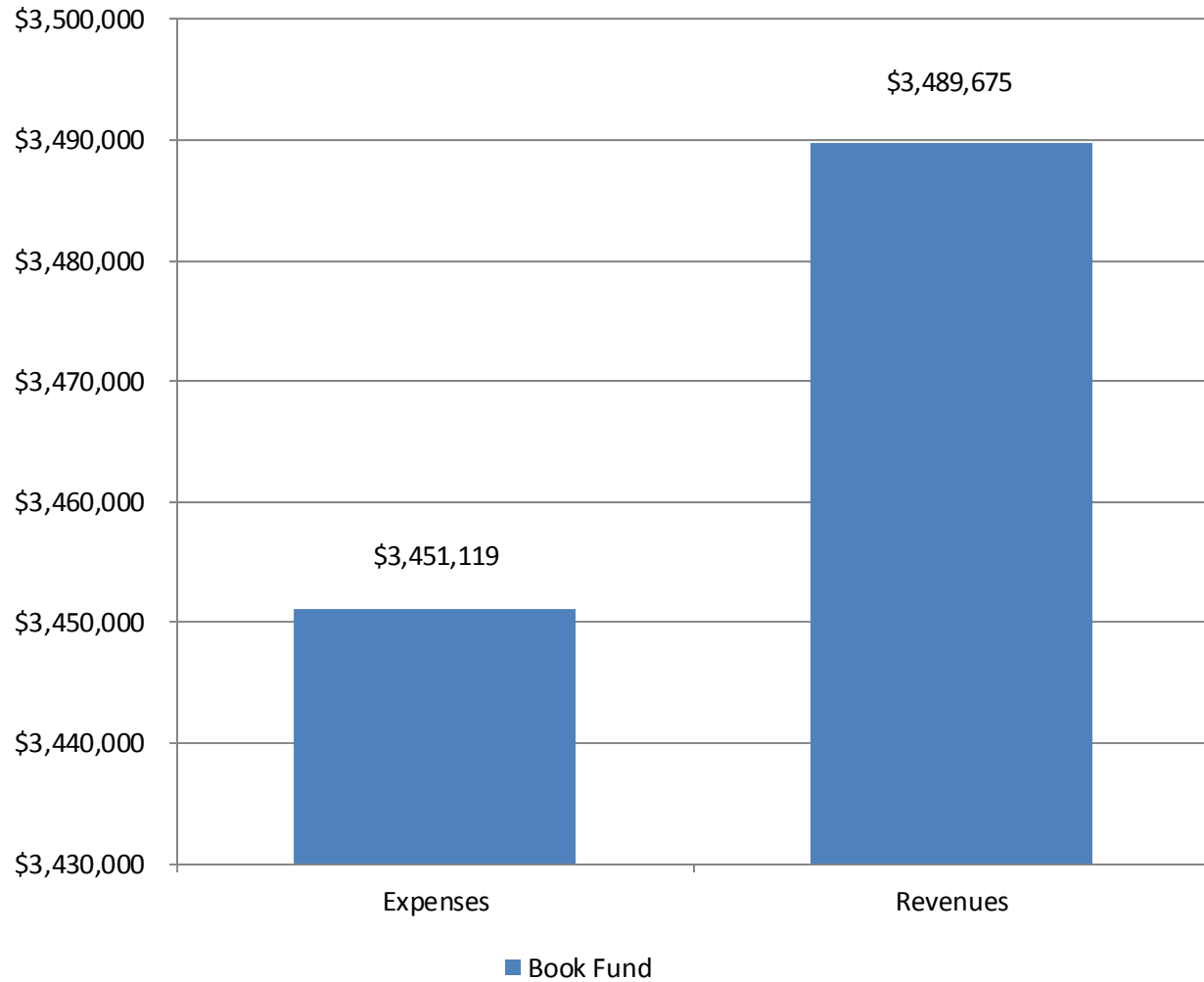
State Bar of Texas

Management's Discussion and Analysis – Continued

May 31, 2014

Business-Type Activities – Business-type activities increased the State Bar's net position by \$38,556. A breakdown of expenses and program revenues and revenues by source type follows:

Expenses and Program Revenues – Business-Type Activities

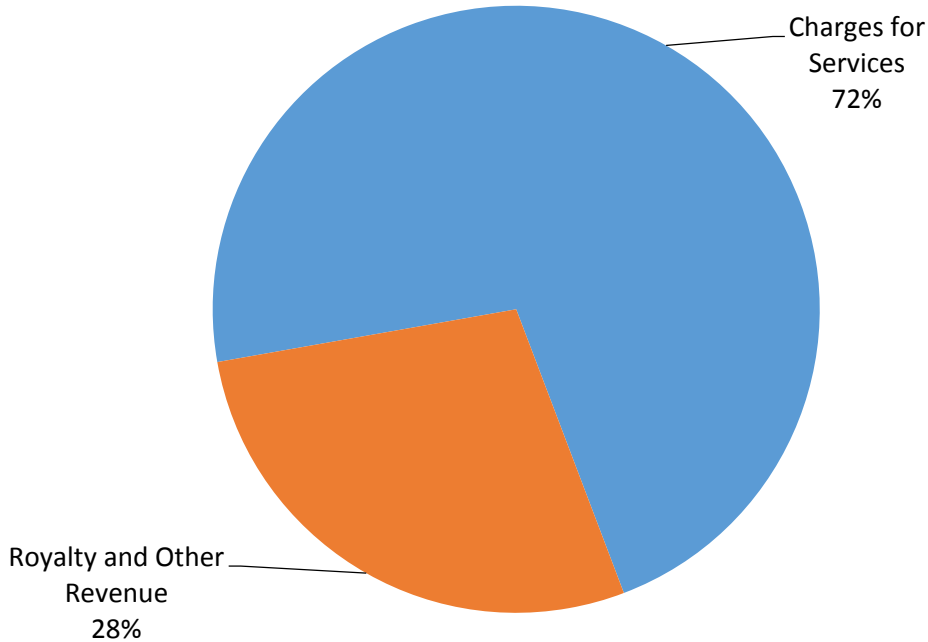


State Bar of Texas

Management's Discussion and Analysis – Continued

May 31, 2014

Revenues by Source – Business Activities



Financial Analysis of the Government's Funds

As noted earlier, the State Bar uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

Governmental Funds – The focus of the State Bar's governmental funds is to provide information on near-term inflows, outflows, and balances of spendable resources. Such information is useful in assessing the State Bar's financing requirements. In particular, undesignated fund balance may serve as a useful measure of a government's net resources available for spending at the end of the fiscal year.

At the end of the current fiscal year, the State Bar's governmental funds reported combined ending fund balances of \$28,604,347, a decrease of \$842,553 in comparison with the prior year. Of this amount, \$601,828 is nonspendable for prepaid expenditures and inventories, and \$18,125,864 is committed for specific uses by the Board of Directors.

The General Fund is the chief operating fund of the State Bar. At the end of the current fiscal year, the total fund balance of the General Fund was \$14,644,753, which is 67.4% unassigned. As a measure of the General Fund's liquidity, it may be useful to compare the unassigned fund balance to total fund expenditures. Unassigned fund balance represents 25.8% of total General Fund expenditures. During the current fiscal year, the fund balance of the State Bar's General Fund decreased by \$825,856.

State Bar of Texas

Management's Discussion and Analysis – Continued

May 31, 2014

Proprietary Funds – The State Bar's proprietary funds provide the same type of information found in the government-wide financial statements, but in more detail.

At the end of the current fiscal year, net position of the Texas Bar Book Fund totaled \$1,910,756. The total increase in net position was \$38,556. Other factors concerning the finances of this fund have already been addressed in the discussion of the State Bar's business-type activities.

General Fund Budgetary Highlights

The State Bar's actual revenue for the General Fund was \$500,805 below budgeted amounts. The most significant negative variances resulted from professional development revenue and membership revenue, which were offset by a positive variance from other income. The State Bar's actual expenditures for the General Fund were \$2,017,116 below budgeted amounts. The most significant positive variances resulted from professional development and board commitment expenditures.

Capital Asset Administration

Capital Assets – The State Bar's investment in capital assets for its governmental activities as of May 31, 2014, amounts to \$9,147,329 (net of accumulated depreciation and amortization). This investment in capital assets includes land, buildings, and furniture, equipment and other assets.

Table A-3
State Bar's Capital Assets – Net of Accumulated Depreciation

| | 2014 | | | 2013 Total |
|------------------------------------|----------------------------|-----------------------------|---------------------|---------------------|
| | Governmental Activities | Business-Type Activities | Total | |
| Land | \$ 154,074 | \$ - | \$ 154,074 | \$ 154,074 |
| Construction in progress | 10,500 | - | 10,500 | - |
| Building | 628,225 | - | 628,225 | 628,225 |
| Furniture, equipment, and other | 8,410,976 | 39,626 | 8,450,602 | 9,055,061 |
| Digital publication | - | - | - | 11,609 |
| | <u>\$ 9,203,775</u> | <u>\$ 39,626</u> | <u>\$ 9,243,401</u> | <u>\$ 9,848,969</u> |

Additional information on the State Bar's capital assets can be found in Note 4 on page 46 of this report.

Long-Term Liabilities – At the end of the current fiscal year, the State Bar had capital leases of \$56,446 and accrued compensated absences of \$1,539,493.

State Bar of Texas

Management's Discussion and Analysis – Continued

May 31, 2014

Table A-4
State Bar's Noncurrent Liabilities

| | 2014 | | | 2013 Total |
|---------------------------------|----------------------------|-----------------------------|-------------------|-------------------|
| | Governmental Activities | Business-Type Activities | Total | |
| Capital lease payable | \$ 56,446 | \$ - | \$ 56,446 | \$ 214,033 |
| Accrued compensated absences | <u>1,471,921</u> | <u>67,572</u> | <u>1,539,493</u> | <u>1,453,575</u> |
| | 1,528,367 | 67,572 | 1,595,939 | 1,667,608 |
| Less current portion | <u>(581,339)</u> | <u>(29,583)</u> | <u>(610,922)</u> | <u>(690,487)</u> |
| Total noncurrent liabilities | \$ <u>947,028</u> | \$ <u>37,989</u> | \$ <u>985,017</u> | \$ <u>977,121</u> |

Additional information on the State Bar's noncurrent liabilities can be found in Note 7 on page 48 of this report.

Economic Factors and Next Year's Budget

For the General Fund, estimated revenues for fiscal year 2015 are \$43,097,423 and estimated expenditures and other uses are \$39,091,664. If these estimates are realized, and the General Fund transfers \$4,005,759 to other funds as budgeted, the State Bar's budgetary General Fund fund balance is not expected to change.

Contacting the State Bar's Financial Management

This financial report is designed to provide a general overview of the State Bar's finances for all those with an interest in the government's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Chief Financial Officer, State Bar of Texas, and P.O. Box 12487, Austin, Texas 78711.

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Basic Financial Statements

State Bar of Texas
Statement of Net Position
May 31, 2014

| ASSETS | <u>Governmental Activities</u> | <u>Business-Type Activities</u> | <u>Total</u> |
|---|------------------------------------|-------------------------------------|----------------------|
| Assets | | | |
| Current assets: | | | |
| Cash and cash equivalents | \$ 19,881,178 | \$ - | \$ 19,881,178 |
| Investments | 22,816,027 | - | 22,816,027 |
| Receivables: | | | |
| Sales to members and others – net of allowance for uncollectible accounts of \$1,857 and \$84,964 | 35,282 | 957,664 | 992,946 |
| Interest receivable | 46,192 | - | 46,192 |
| Other accounts receivable | 2,169,192 | - | 2,169,192 |
| Internal balances | (337,078) | 337,078 | - |
| Inventories – lower of cost or market | 10,640 | 720,526 | 731,166 |
| Prepaid items | 591,188 | - | 591,188 |
| | <u>45,212,621</u> | <u>2,015,268</u> | <u>47,227,889</u> |
| Total current assets | | | |
| Noncurrent assets: | | | |
| Capital assets – net of accumulated depreciation/amortization: | | | |
| Land | 154,074 | - | 154,074 |
| Building | 628,225 | - | 628,225 |
| Furniture, equipment, and other | 8,410,976 | 39,626 | 8,450,602 |
| Construction in progress | 10,500 | - | 10,500 |
| | <u>9,203,775</u> | <u>39,626</u> | <u>9,243,401</u> |
| Total noncurrent assets | | | |
| | <u>9,203,775</u> | <u>39,626</u> | <u>9,243,401</u> |
| Total assets | \$ <u>54,416,396</u> | \$ <u>2,054,894</u> | \$ <u>56,471,290</u> |

| LIABILITIES AND NET POSITION | Governmental Activities | Business-Type Activities | Total |
|-------------------------------------|------------------------------------|-------------------------------------|----------------------|
| Liabilities | | | |
| Current liabilities: | | | |
| Accounts payable | \$ 1,531,656 | \$ - | \$ 1,531,656 |
| Accrued liabilities | 406,242 | 76,566 | 482,808 |
| Due to agency funds | 696,764 | - | 696,764 |
| Unearned revenue | 13,973,612 | - | 13,973,612 |
| Capital lease payable | 50,223 | - | 50,223 |
| Accrued compensated absences | <u>531,116</u> | <u>29,583</u> | <u>560,699</u> |
| Total current liabilities | <u>17,189,613</u> | <u>106,149</u> | <u>17,295,762</u> |
| Long-Term Liabilities | | | |
| Capital lease payable | 6,223 | - | 6,223 |
| Accrued compensated absences | <u>940,805</u> | <u>37,989</u> | <u>978,794</u> |
| Total noncurrent liabilities | <u>947,028</u> | <u>37,989</u> | <u>985,017</u> |
| Total liabilities | <u>\$ 18,136,641</u> | <u>\$ 144,138</u> | <u>\$ 18,280,779</u> |
| Net Position | | | |
| Net investment in capital assets | \$ 9,147,329 | \$ 39,626 | \$ 9,186,955 |
| Unrestricted | <u>27,132,426</u> | <u>1,871,130</u> | <u>29,003,556</u> |
| Total net position | <u>\$ 36,279,755</u> | <u>\$ 1,910,756</u> | <u>\$ 38,190,511</u> |

The accompanying notes are an integral part of this statement.

State Bar of Texas
Statement of Activities
Year Ended May 31, 2014

| Functions/Programs | Expenses | Program Revenues | | Net (Expenses) Revenues and Changes in Net Position | | |
|-------------------------------------|----------------------|----------------------|------------------------------------|---|--------------------------|----------------------|
| | | Charges for Services | Operating Grants and Contributions | Governmental Activities | Business-Type Activities | Total |
| Primary Government | | | | | | |
| Governmental activities: | | | | | | |
| General government | \$ 8,377,787 | \$ 276,161 | \$ 6,976 | \$ (8,094,650) | \$ - | \$ (8,094,650) |
| Public services | 3,926,296 | 524,443 | 393,933 | (3,007,920) | - | (3,007,920) |
| Member services | 22,328,585 | 19,383,116 | 1,123,198 | (1,822,271) | - | (1,822,271) |
| Public protection | <u>11,326,008</u> | <u>372,688</u> | <u>-</u> | <u>(10,953,320)</u> | <u>-</u> | <u>(10,953,320)</u> |
| Total governmental activities | <u>45,958,676</u> | <u>20,556,408</u> | <u>1,524,107</u> | <u>(23,878,161)</u> | <u>-</u> | <u>(23,878,161)</u> |
| Business-type activities: | | | | | | |
| Books | <u>3,451,119</u> | <u>2,511,429</u> | <u>-</u> | <u>-</u> | <u>(939,690)</u> | <u>(939,690)</u> |
| Total business-type activities | <u>3,451,119</u> | <u>2,511,429</u> | <u>-</u> | <u>-</u> | <u>(939,690)</u> | <u>(939,690)</u> |
| Total primary government activities | <u>\$ 49,409,795</u> | <u>\$ 23,067,837</u> | <u>\$ 1,524,107</u> | <u>(23,878,161)</u> | <u>(939,690)</u> | <u>(24,817,851)</u> |
| General revenues: | | | | | | |
| Membership dues | | | | 21,555,086 | - | 21,555,086 |
| Investment income | | | | 115,787 | 389 | 116,176 |
| Royalty revenue | | | | 489,925 | 977,853 | 1,467,778 |
| Other income | | | | 353,830 | 4 | 353,834 |
| Loss on disposal of capital assets | | | | <u>(2,168)</u> | <u>-</u> | <u>(2,168)</u> |
| Total general revenues | | | | <u>22,512,460</u> | <u>978,246</u> | <u>23,490,706</u> |
| Change in net position | | | | (1,365,701) | 38,556 | (1,327,145) |
| Net position at beginning of year | | | | <u>37,645,456</u> | <u>1,872,200</u> | <u>39,517,656</u> |
| Net position at end of year | | | | <u>\$ 36,279,755</u> | <u>\$ 1,910,756</u> | <u>\$ 38,190,511</u> |

The accompanying notes are an integral part of this statement.

State Bar of Texas

Balance Sheet – Governmental Funds

May 31, 2014

| ASSETS | General Fund | Client Security Fund | Sections | Nonmajor Governmental Funds | Total Governmental Funds |
|---|----------------------|----------------------------|---------------------|-----------------------------------|--------------------------------|
| Assets | | | | | |
| Current assets: | | | | | |
| Cash and cash equivalents | \$ 11,173,849 | \$ 582,040 | \$ 5,623,432 | \$ 2,501,857 | \$ 19,881,178 |
| Investments | 16,767,783 | 2,219,687 | 1,476,414 | 2,352,143 | 22,816,027 |
| Receivables: | | | | | |
| Sales to members and others – net of allowance for uncollectible accounts of \$1,857 | 35,282 | - | - | - | 35,282 |
| Interest receivable | 30,057 | 1,438 | - | 14,697 | 46,192 |
| Other accounts receivable | 1,962,770 | - | 146,097 | 60,325 | 2,169,192 |
| Due from other governmental funds | 413,592 | - | 1,180,830 | 1,102,144 | 2,696,566 |
| Inventories – at cost | 10,640 | - | - | - | 10,640 |
| Prepaid expenditures | 426,545 | - | 38,159 | 126,484 | 591,188 |
| Total assets | \$ 30,820,518 | \$ 2,803,165 | \$ 8,464,932 | \$ 6,157,650 | \$ 48,246,265 |
| LIABILITIES AND FUND BALANCE | | | | | |
| Liabilities | | | | | |
| Current liabilities: | | | | | |
| Accounts payable | \$ 1,126,779 | \$ - | \$ 404,877 | \$ - | \$ 1,531,656 |
| Accrued liabilities | 360,432 | - | 45,232 | 578 | 406,242 |
| Due to other governmental funds | 2,282,974 | 314,949 | - | 98,643 | 2,696,566 |
| Due to enterprise fund | 337,078 | - | - | - | 337,078 |
| Due to agency fund | 696,764 | - | - | - | 696,764 |
| Unearned revenue | 11,371,738 | - | 1,191,420 | 1,410,454 | 13,973,612 |
| Total liabilities | 16,175,765 | 314,949 | 1,641,529 | 1,509,675 | 19,641,918 |
| Fund Balances | | | | | |
| Nonspendable | 437,185 | - | 38,159 | 126,484 | 601,828 |
| Committed | 4,330,913 | 2,488,216 | 6,785,244 | 4,521,491 | 18,125,864 |
| Unassigned | 9,876,655 | - | - | - | 9,876,655 |
| Total fund balances | 14,644,753 | 2,488,216 | 6,823,403 | 4,647,975 | 28,604,347 |
| Total liabilities and fund balances | \$ 30,820,518 | \$ 2,803,165 | \$ 8,464,932 | \$ 6,157,650 | \$ 48,246,265 |

The accompanying notes are an integral part of this statement.

State Bar of Texas

Reconciliation of the Balance Sheet of Governmental Funds to the Statement of Net Position

May 31, 2014

| | |
|---|----------------------|
| Total fund balance – Governmental Funds balance sheet | \$ 28,604,347 |
| Amounts reported for governmental activities in the statement of net position are different because: | |
| Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the funds. | 9,203,775 |
| The following liabilities are not due and payable in the current period and, therefore, are not reported in the funds: | |
| Capital lease payable | (56,446) |
| Accrued compensated absences | <u>(1,471,921)</u> |
| Net position of governmental activities – statement of net position | <u>\$ 36,279,755</u> |

The accompanying notes are an integral part of this statement.

State Bar of Texas

Statement of Revenues, Expenditures, and Changes in Fund Balance – Governmental Funds

Year Ended May 31, 2014

| | <u>General Fund</u> | <u>Client Security Fund</u> | <u>Sections</u> | <u>Nonmajor Governmental Funds</u> | <u>Total Governmental Funds</u> |
|--|-------------------------|-------------------------------------|---------------------|--|---|
| Revenues | | | | | |
| Membership dues | \$ 19,432,743 | \$ - | \$ 2,122,343 | \$ - | \$ 21,555,086 |
| Accounting/management fees | 657,269 | - | - | - | 657,269 |
| Texas Bar Journal | 724,581 | - | - | - | 724,581 |
| MCLE fees | 2,850,550 | - | - | - | 2,850,550 |
| Professional development | 12,918,406 | - | - | - | 12,918,406 |
| Investment income | 78,259 | 11,448 | 17,328 | 8,752 | 115,787 |
| Grant revenue | - | - | - | 443,727 | 443,727 |
| Other income | 2,540,779 | 13,983 | 1,339,784 | 2,137,768 | 6,032,314 |
| Total revenues | <u>39,202,587</u> | <u>25,431</u> | <u>3,479,455</u> | <u>2,590,247</u> | <u>45,297,720</u> |
| Expenditures | | | | | |
| Executive | 2,050,804 | - | - | - | 2,050,804 |
| External affairs | 1,176,186 | - | - | - | 1,176,186 |
| Special services | - | - | 3,113,418 | 2,416,656 | 5,530,074 |
| Member and public service | 1,580,253 | - | - | - | 1,580,253 |
| Professional development | 9,950,880 | - | - | - | 9,950,880 |
| Legal and attorney services | 1,831,385 | - | - | - | 1,831,385 |
| Access to justice | 600,543 | - | - | - | 600,543 |
| Attorney compliance | 2,894,731 | - | - | - | 2,894,731 |
| Administration | 2,009,080 | - | - | 43,990 | 2,053,070 |
| Finance | 2,038,595 | - | - | - | 2,038,595 |
| Information technology | 1,577,024 | - | - | 884,804 | 2,461,828 |
| Communications | 2,287,829 | - | - | - | 2,287,829 |
| Public protection division | 9,474,118 | 1,346,419 | - | - | 10,820,537 |
| Expenditures related to board commitments | 873,948 | - | - | - | 873,948 |
| Total expenditures | <u>38,345,376</u> | <u>1,346,419</u> | <u>3,113,418</u> | <u>3,345,450</u> | <u>46,150,663</u> |
| Excess (deficiency) of revenues over (under) expenditures | <u>857,211</u> | <u>(1,320,988)</u> | <u>366,037</u> | <u>(755,203)</u> | <u>(852,943)</u> |
| Other Financing Sources (Uses) | | | | | |
| Proceeds from capital leases | - | - | - | 10,390 | 10,390 |
| Transfers in | - | 800,000 | - | 883,067 | 1,683,067 |
| Transfers out | (1,683,067) | - | - | - | (1,683,067) |
| Total other financing sources (uses) | <u>(1,683,067)</u> | <u>800,000</u> | <u>-</u> | <u>893,457</u> | <u>10,390</u> |
| Net change in fund balances | (825,856) | (520,988) | 366,037 | 138,254 | (842,553) |
| Fund balances at beginning of year | <u>15,470,609</u> | <u>3,009,204</u> | <u>6,457,366</u> | <u>4,509,721</u> | <u>29,446,900</u> |
| Fund balances at end of year | <u>\$ 14,644,753</u> | <u>\$ 2,488,216</u> | <u>\$ 6,823,403</u> | <u>\$ 4,647,975</u> | <u>\$ 28,604,347</u> |

The accompanying notes are an integral part of this statement.

State Bar of Texas

Reconciliation of the Statement of Revenues, Expenditures, and Changes in Fund Balance of Governmental Funds to the Statement of Activities

Year Ended May 31, 2014

| | |
|---|------------------------------|
| Net change in fund balance – total Governmental Funds | \$ (842,553) |
| Amounts reported for governmental activities in the statement of activities are different because: | |
| Governmental funds report capital outlays as expenditures. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives as depreciation expense. | |
| Capital outlay – exclusive of noncapitalized items | 379,224 |
| Depreciation expense | (975,241) |
| Loss on disposal of capital assets | (2,168) |
| Proceeds from capital leases provide current financial resources to governmental funds, but issuing debt increases noncurrent liabilities in the statement of net position. Repayment of capital leases is an expenditure in the governmental funds, but the repayment reduces noncurrent liabilities in the statement of net position. | |
| Proceeds from capital leases | (10,390) |
| Repayment of capital leases | 160,599 |
| Some expenses reported in the statement of activities do not require the use of current financial resources and, therefore, are not reported as expenditures in governmental funds. | |
| Change in compensated absences | <u>(75,172)</u> |
| Change in net position of governmental activities – statement of activities | \$ <u><u>(1,365,701)</u></u> |

The accompanying notes are an integral part of this statement.

State Bar of Texas

Statement of Net Position – Proprietary Fund

May 31, 2014

| | Business-Type Activities – Major Enterprise Fund |
|--|---|
| Assets | |
| Current assets: | |
| Accounts receivable – net of allowance for uncollectible accounts of \$84,964 | \$ 957,664 |
| Due from other funds | 337,078 |
| Inventories – at cost | <u>720,526</u> |
| Total current assets | 2,015,268 |
| Capital assets – furniture, equipment, digital publication, and other – net of accumulated depreciation and amortization of \$636,713 | <u>39,626</u> |
| Total assets | <u>\$ 2,054,894</u> |
| Liabilities | |
| Current liabilities: | |
| Accrued liabilities | \$ 76,566 |
| Accrued compensated absences | <u>29,583</u> |
| Total current liabilities | <u>106,149</u> |
| Long-Term Liabilities | |
| Accrued compensated absences | <u>37,989</u> |
| Total long-term liabilities | <u>37,989</u> |
| Total liabilities | <u>\$ 144,138</u> |
| Net Position | |
| Net Investment in capital assets | \$ 39,626 |
| Unrestricted | <u>1,871,130</u> |
| Total net position | <u>\$ 1,910,756</u> |

The accompanying notes are an integral part of this statement.

State Bar of Texas

Statement of Revenues, Expenses, and Changes in Net Position – Proprietary Fund

Year Ended May 31, 2014

| | Business-Type Activities – Major Enterprise Fund |
|-----------------------------------|---|
| Operating Revenues | |
| Charges for sales and services: | |
| Book sales | \$ 2,511,429 |
| Royalty revenue | 977,853 |
| Other income | 4 |
| | <hr/> |
| Total operating revenues | 3,489,286 |
| | <hr/> |
| Operating Expenses | |
| Costs of goods sold | 931,645 |
| Administrative | 2,512,091 |
| Depreciation | 7,383 |
| | <hr/> |
| Total operating expenses | 3,451,119 |
| | <hr/> |
| Operating income | 38,167 |
| | <hr/> |
| Nonoperating Revenues | |
| Investment income | 389 |
| | <hr/> |
| Total nonoperating revenues | 389 |
| | <hr/> |
| Change in net position | 38,556 |
| | <hr/> |
| Net position at beginning of year | 1,872,200 |
| | <hr/> |
| Net position at end of year | \$ 1,910,756 |
| | <hr/> <hr/> |

The accompanying notes are an integral part of this statement.

State Bar of Texas

Statement of Cash Flows – Proprietary Fund

Year Ended May 31, 2014

| | Business-Type Activities – Major Enterprise Fund |
|--|---|
| Cash Flows From Operating Activities | |
| Receipts from customers | \$ 2,016,004 |
| Receipts from royalties | 977,853 |
| Payments to suppliers for goods and services | (1,931,539) |
| Payments to employees | <u>(1,055,359)</u> |
| Net cash provided by operating activities | <u>6,959</u> |
| Cash Flows From Capital and Related Financing Activities | |
| Payments on capital leases | <u>(7,348)</u> |
| Net cash used in capital and related financing activities | <u>(7,348)</u> |
| Cash Flows From Investing Activities | |
| Interest received | <u>389</u> |
| Net cash provided by investing activities | <u>389</u> |
| Net change in cash and cash equivalents | - |
| Cash and cash equivalents at beginning of year | <u>-</u> |
| Cash and cash equivalents at end of year | <u>\$ -</u> |
| Reconciliation of Operating Income to Net Cash Provided by Operating Activities | |
| Operating income | \$ 38,167 |
| Depreciation expense | 7,383 |
| Bad debt expense | 60,635 |
| Adjustments to reconcile operating loss to net cash provided by operating activities: | |
| Increase in accounts receivable | (556,064) |
| Decrease in due from other funds | 499,474 |
| Increase in merchandise inventories | (102,420) |
| Increase in accrued liabilities | 49,038 |
| Increase in accrued compensated absences | <u>10,746</u> |
| Net cash provided by operating activities | <u>\$ 6,959</u> |

The accompanying notes are an integral part of this statement.

State Bar of Texas

Statement of Net Position – Fiduciary Funds

May 31, 2014

| | Agency Funds | Discrete Component Unit - State Bar of Texas Insurance Trust |
|---------------------------------------|-------------------------|---|
| Assets | | |
| Cash | \$ - | \$ 1,009,144 |
| Restricted cash | 38,173 | 948,777 |
| Accounts receivable | - | 52,372 |
| Prepaid expenses | - | 46,874 |
| Property and equipment – net | - | 37,009 |
| Due from general fund | <u>696,764</u> | <u>-</u> |
| Total assets | <u>\$ 734,937</u> | <u>\$ 2,094,176</u> |
| Liabilities | | |
| Accounts payable and accrued expenses | \$ - | \$ 492,226 |
| Unremitted premiums collected | - | 948,777 |
| Capital lease obligations | - | 61,410 |
| Due to other organizations | <u>734,937</u> | <u>-</u> |
| Total liabilities | <u>\$ 734,937</u> | <u>\$ 1,502,413</u> |
| Net Position | <u>\$ -</u> | <u>\$ 591,763</u> |

The accompanying notes are an integral part of this statement.

State Bar of Texas

Statement of Changes in Net Position – Fiduciary Funds

Year Ended May 31, 2014

| | Discrete Component Unit – State Bar of Texas Insurance Trust |
|--|---|
| Additions | |
| Contributions of subscribers (net of refunds and returns of \$139,670 and \$185,232, respectively) | \$ 23,974,171 |
| Less premiums to insurance carrier | <u>22,998,400</u> |
| | 975,771 |
| Commissions | 647,456 |
| Investment income | 363 |
| Other loss | <u>(1,273)</u> |
| Total additions | <u>1,622,317</u> |
| Deductions | |
| Accounting fees | 22,910 |
| Actuarial services | 147,551 |
| Compensation and related expenses | 1,248,509 |
| Depreciation and amortization | 74,016 |
| Insurance | 60,185 |
| Miscellaneous | 81,013 |
| Professional fees | 166,704 |
| Promotion | 92,578 |
| Printing, postage, and supplies | 12,677 |
| Rent | 151,406 |
| Telephone | 12,615 |
| Travel and meetings | <u>7,411</u> |
| Total deductions | <u>2,077,575</u> |
| Loss before income tax expense | (455,258) |
| Income tax expense | <u>4,478</u> |
| Change in net position | (459,736) |
| Net position at beginning of year | <u>1,051,499</u> |
| Net position at end of year | <u>\$ 591,763</u> |

The accompanying notes are an integral part of this statement.

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State Bar of Texas

Notes to the Financial Statements

May 31, 2014

1. Summary of Significant Accounting Policies

Reporting Entity

The State Bar of Texas' (the "State Bar") enabling legislation, Texas Rev. Civ. Stat. Ann. Art. 320a-1 (Vernon Supp. 1986), provides the authority for operations of the State Bar. In 1939, the State Bar was created by the State of Texas legislature. Located in the judicial branch of State government, its primary responsibility is to cooperate in the regulation of the practice of law in the State of Texas. The State Bar is an administrative branch or department of the Supreme Court of Texas. This report includes the funds and account groups required to account for those activities, organizations, and functions which are related to the State Bar and are controlled by the State Bar. The State Bar is included in the financial statements of the State of Texas as a component unit.

The State Bar is subject to the Texas Sunset Act (Chapter 325). Subsequent to May 31, 2003, the revised State Bar Act was approved (Texas Gov. Code Section 81.001 et. seq.), which recreated the State Bar until September 1, 2015 and thereafter, contingent upon the State of Texas legislature and the Supreme Court of Texas.

The State Bar's major activities or functions include the collection and monitoring of membership dues, discipline of attorneys, development and accreditation of professional development courses, publishing and printing of legal text for sale to members, preparation and distribution of the "Bar Journal," and providing access to a database of legal information for member use. These activities are included in the accompanying financial statements.

In the evaluation of how to define the State Bar for financial reporting purposes, management considered all potential component units. The decision to include a potential component unit in the reporting entity was made by applying the criteria set forth in Governmental Accounting Standards Board ("GASB") Statement No. 61, *The Financial Reporting Entity: Omnibus – an Amendment of GASB Statements No. 14 and No. 34*. The underlying concept of the financial reporting entity is improving guidance for including, presenting, and disclosing information about component units and equity interest transactions of a financial reporting entity.

The financial reporting entity consists of: (a) the primary government (in these financial statements the primary government is the State Bar), (b) component units, which are legally separate organizations for which the State Bar is financially accountable or the services rendered by the component unit are provided entirely or almost entirely to the State Bar (blended), and (c) component units, the nature and significance of their relationship with the State Bar is such that exclusion from the reporting entity's financial statements would be misleading or incomplete (discretely presented).

Using the criteria of GASB Statement No. 61 outlined below, potential component units were evaluated for inclusion in or exclusion from the reporting entity, whether the organizations were financially accountable or not, and were further evaluated for financial statement presentation. Based on their individual relationships with the State Bar, some component unit financial statements were blended as though they are part of the State Bar and discretely presented.

State Bar of Texas

Notes to the Financial Statements

May 31, 2014

The following criteria (as set forth in GASB Statement No. 61) were used in the evaluation of potential component units of the State Bar:

- 1) Legally separate
- 2) Financial accountability:
 - a) Appointment of a voting majority
 - b) Imposition of will
 - c) Financial benefit to or burden on the State Bar
 - d) Fiscal dependency with financial benefit to or burden on the State Bar
- 3) The relationship with the State Bar is such that exclusion would cause these financial statements to be misleading or incomplete
- 4) Service rendered by the potential component unit is provided entirely or almost entirely to the State Bar
- 5) The State Bar or its component units are entitled to or have the ability to access the majority of the resources received or held by the separate organization.

The criteria outlined above were excerpted from GASB Statement No. 39, *Determining Whether Certain Organizations are Component Units – an Amendment of GASB Statement No. 14*, and GASB Statement No. 61. For a more detailed explanation of the criteria established by the Statements, the reader is referred to the *Codification of Governmental Accounting and Financial Reporting Standards*, as of June 30, 2013, published by GASB, Section-2600. GASB Statement No. 39 further clarifies that a “not for profit” may not be financially accountable to the State Bar, but may be considered a component unit based on the nature and significance of its relations with the State Bar.

The State Bar appoints a majority of members to the Texas Bar Foundation’s (the “Foundation”) governing body; however, because the State Bar is not in a position to impose its will on or significantly influence the programs, projects, activities, or level of service performed by the Foundation, and because no financial burden or benefit exists between the State Bar and the Foundation, the Foundation is not considered a component unit of the State Bar. The State Bar also appoints a majority of members to the Texas Center For Legal Ethics’ (the “Center”) governing body; however, because the State Bar is not in a position to impose its will on or significantly influence the programs, projects, activities, or level of service performed by the Center, and because no financial burden or benefit exists between the State Bar and the Center, the Center is not considered a component unit of the State Bar. The State Bar also appoints a majority of members to the Texas Legal Protection Plan, Inc.’s (the “Plan”) governing body; however, because the State Bar is not in a position to impose its will on or significantly influence the programs, projects, activities, or level of service performed by the Plan, and because no financial burden or benefit exists between the State Bar and the Plan, the Plan is not considered a component unit of the State Bar.

Based upon the application of GASB Statement No. 61, the following is a brief overview of component units included in the reporting entity.

Blended Component Units

The College of the State Bar (the “College”) is an honor society designed to recognize attorneys who accumulate at least twice as many continuing legal education credit hours each year than the minimum required. The College was created in 1981 by order of the Texas Supreme Court. The College is governed

State Bar of Texas

Notes to the Financial Statements

May 31, 2014

by an 18-member board of directors, of which, 12 members are appointed by the State Bar's President, and 6 members are appointed by the State Bar's President based on nominations submitted by the College's board. The College is a Section 501(c)3 corporation and is self-funded through membership dues, investment income, and merchandise sales. The College is reported as a Special Revenue Fund.

Law Focused Education, Inc. was created in 1975 as a Section 501(c)3 corporation to plan, promote, and support law-related education programs aimed at preparing elementary, middle, and high school students for effective, responsible citizenship, and who are committed to liberty, justice, and the Rule of Law. Law Focused Education, Inc. is governed by a 16 member board of directors, all of which are appointed by the State Bar's President. Law Focused Education, Inc. is made up of two funds: Hatton W. Sumners Grants and Law Focused Education, both of which are reported as Special Revenue Funds. Contact the Finance Division of the State Bar to obtain financial statements of the blended component units.

Discretely Presented Component Unit

The discretely presented component unit is the State Bar of Texas Insurance Trust and Affiliate, which consists of The State Bar of Texas Insurance Trust (the "Trust") and the SBIT Insurance Agency, LLC (the "Agency"). The State Bar of Texas Insurance Trust and Affiliate is custodial in nature and is reported with the fiduciary fund financial statements. The Trust has a different fiscal year end from the State Bar with a fiscal year end of December 31, 2013.

Subsequent to December 31, 2013, the Trust's agreement was amended to reduce the number of the members of its board of trustees from seven to three, all of which are members of the State Bar's Board of Directors (the "Board"). Therefore, the Trust meets the criteria, as set forth in GASB statement No. 61, for inclusion in the reporting entity as a discretely presented component unit.

The Trust was formed in 1973 to provide group insurance benefits to members of the State Bar, including their employees, employees of the State Bar and the Trust, and families of all eligible participants. Premiums for the group policies are collected by the Trust and are remitted to the insurance companies, Aetna and Prudential Insurance Company of America ("Prudential"), who underwrite the State Bar of Texas Insurance Program. Aetna and Prudential are responsible for all claims.

The Agency was formed on January 11, 2005 as a general lines insurance agency. The Agency was formed to assist employees of the State Bar, the Trust, and the families of eligible participants in acquiring insurance from companies other than those currently provided by the Trust. The Trust owns 100% of the membership interest of the Agency and is, therefore, consolidated in its financial statements. All intercompany balances and transactions have been eliminated. Contact the Finance Division of the State Bar to obtain financial statements.

Government-Wide and Fund Financial Statements

The government-wide financial statements (i.e., the statement of net position and the statement of activities) report information on all of the nonfiduciary activities of the State Bar and are reported on a full accrual basis of accounting, using the economic resource measurement focus, which recognizes all long-term assets and receivables, as well as long-term debt and obligations. The effect of interfund

State Bar of Texas

Notes to the Financial Statements

May 31, 2014

activity has been removed from these statements. Governmental activities, which are supported by dues, fees, grants, and other revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segments are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function or segment. All capital asset depreciation is reported as a direct expense of the financial program that benefits from the use of the capital assets. Program revenues include (1) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment and (2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or segment. Membership dues and other items not properly included among program revenues are reported instead as general revenues.

Separate financial statements are provided for governmental funds, proprietary funds, and fiduciary funds, although the latter are excluded from the government-wide financial statements. Major individual governmental funds are reported as separate columns in the fund financial statements.

Measurement Focus, Basis of Accounting, and Financial Statement Presentation

The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting, as are the proprietary fund and fiduciary fund financial statements. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Internal activity between funds is eliminated in the government-wide financial statements.

Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. This measurement focus means that only current assets and current liabilities are included on the balance sheet. Operating statements of these funds present resources (i.e., revenues and other financing sources) and decreases (i.e., expenditures and other financing uses) in net current assets. Revenues earned are recognized as soon as they are both measurable and available.

In the governmental fund financial statements, revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the State Bar considers revenues to be available if they are collected within 60 days of the end of the current fiscal period. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, expenditures related to debt service, compensated absences, and claims and judgments are recorded only when payment is due.

The State Bar reports the following major governmental funds:

The General Fund is the State Bar's primary operating fund. It accounts for all financial resources of the general government, except those required to be accounted for in another fund.

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Notes to the Financial Statements

May 31, 2014

The Client Security Fund accounts for the payments associated with losses related to a lawyer's dishonest conduct or dishonest act against an individual. The Client Security Fund must maintain a corpus of \$2,000,000, in accordance with resolutions of the State Bar's Board. The fund did not meet the criteria for a major fund; however, management decided to include it as a major fund in the interest of the users of the financial statements.

The Sections are a special revenue fund. The Sections include all entities created by the State Bar's Board, which serve the individual members of the State Bar in certain legal specialization areas. The Sections' officers are elected by the members of the individual sections and are responsible for maintaining and administering their operations. Although the Sections collect a portion of their revenues and pay expenditures for administration and operations individually, the State Bar administers the collection of dues for the Sections. The State Bar believes it is unlikely that it will be required to use its assets to satisfy future claims of the Sections; however, the State Bar is liable for any claims should they occur.

The State Bar reports its Book Enterprise Fund, now known as "TexasBarBooks," as a major proprietary fund. The Book Fund accounts for the activities relating to the sales of books. Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues of the State Bar's Book Fund are charges for the sales of books. Operating expenses include the cost of sales and services, administrative expenses, depreciation on capital assets, and amortization on the intangible asset. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

Additionally, the State Bar reports the following nonmajor fund types:

The special revenue funds include: Texas Board of Legal Specialization Fund, State Bar College, Annual Meeting, Texas Law Center, Technology Fund, Project Grants Fund, Hatton W. Sumners Grants Fund, and Law Focused Education.

The special revenue funds function for the benefit of the members of the State Bar and the State Bar's Board administers and maintains all control over their operations. The State Bar is obligated to fund liabilities and deficits of the special revenue funds. Although expenses for administration and operations are paid by the special revenue funds individually, the State Bar controls the collection and disbursement of monies for the special revenue funds and executes all investment transactions.

The capital projects funds are used to account for the acquisition and construction of the State Bar's major capital facilities, and other capital expenditures, other than those financed by proprietary funds. The capital projects funds include the Technology Fund and the Texas Law Center Fund.

Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

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When both restricted and unrestricted resources are available for use, it is the State Bar's policy to use restricted resources first, then unrestricted resources as they are needed.

The agency fund (a fiduciary fund type) is custodial in nature and is used to account for reporting voluntary access to justice contributions and includes the Trust as a discretely presented component unit.

Cash and Cash Equivalents

The State Bar's cash and cash equivalents are considered to be demand deposits, petty cash, and money market accounts. Short-term highly liquid investments with an original maturity of three months or less are considered cash equivalents.

Investments

Investments [consisting primarily of government agency securities, United States Treasury securities, and certificates of deposit ("CDs")] are stated at fair value. Chapter 2256 of the Texas Governmental Code ("Public Funds Investment Act") authorizes the State Bar to invest in funds under a written investment policy. The State Bar's deposits and investments are invested pursuant to the investment policy, which is approved annually by the Board. The primary objectives of the State Bar's investment strategy, in order of priority, are preservation and safety of principal, liquidity, and return on investment.

The State Bar is authorized to invest in the following investment instruments provided that they meet the guidelines established in the State Bar's investment policy and the Public Funds Investment Act:

- United States Treasury securities
- United States federal agency securities
- CDs and share certificates
- Banker's acceptances
- Fully collateralized repurchase agreements
- Money market mutual funds
- Commercial paper

Stat Bar's investments are reported at fair value which are generally based on quoted market prices.

Merchandise Inventories

Merchandise inventories are valued at the lower of cost or market. Cost is determined for inventories on the first-in, first-out method. Merchandise inventories consist of books and other publications held for sale by the State Bar. Merchandise inventories reported in the General Fund are offset in the fund level financial statements by a fund balance reserve to indicate they do not represent "available spendable resources."

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Notes to the Financial Statements

May 31, 2014

Prepaid Items

Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid items in both the government-wide and fund financial statements. The cost of prepaid items is recorded as expenditures/expenses when consumed rather than when purchased.

Capital Assets

Capital assets, consisting of land, buildings, and furniture and equipment, are reported in the governmental activities and business-type activities columns of the government-wide financial statements. Capital assets are defined by the State Bar as assets with an initial cost of at least \$5,000. Capital assets are recorded at historical cost. Donated capital assets are recorded at estimated fair market value at the date of the donation. The costs of normal maintenance and repairs that do not add to the value of the assets or materially extend the assets' lives are not capitalized.

Capital assets of the State Bar are depreciated using the straight-line method over the following estimated useful lives:

| <u>Asset Description</u> | <u>Asset Life</u> |
|--------------------------|-------------------|
| Building | 30 years |
| Furniture and fixtures | 10-20 years |
| Computer equipment | 3-5 years |
| Software | 3-5 years |
| Other equipment | 5-10 years |

Intangible Asset

The intangible asset, consisting of a digital book publication, is reported in the business-type activities column of the government-wide financial statements and is considered to have a finite life. The finite-lived intangible asset is amortized over its estimated useful life, based on the digital publication's pattern of benefits. The finite-lived intangible asset is reviewed for impairments or obsolescence annually, or more frequently if events or changes in circumstances indicate that the carrying amount of the intangible asset may not be recoverable. If impaired, the intangible asset is written down to fair value based on discounted cash flows.

Income Taxes

The State Bar is operating as part of the judicial branch of the state government; therefore, it is not subject to federal or state income taxes.

Unearned Revenues

The State Bar collects certain dues, fees, and subscription revenue in advance for services to be rendered. These receipts are accounted for as unearned revenue, which will be earned and recognized in the subsequent fiscal year, as the services are rendered.

Interfund Receivables/Payables

Short-term advances between funds are accounted for in the appropriate interfund receivable and payable accounts. These balances will be repaid within the next year.

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May 31, 2014

Net Position

Net position represents the difference between assets and liabilities. Net position investment in capital assets consists of capital assets net of related capital leases. Net position is reported as restricted when there are external limitations imposed on its use by creditors, grantors, or laws or regulations of other governments. Unrestricted net position represents the remaining portion of net position.

Fund Balance

In accordance with GASB Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, the State Bar classifies the balances of governmental fund types as follows:

Nonspendable – The nonspendable fund balance category includes amounts that cannot be spent because they are not in spendable form, such as inventories and prepaid items, or amounts that are legally or contractually required to be maintained intact. The “not in spendable form” criterion includes items that are not expected to be converted to cash.

Restricted – Fund balance is reported as restricted when constraints placed on the use of resources are either externally imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments, or are imposed by law through constitutional provisions or enabling legislation. Legal enforceability means that the State Bar can be compelled by an external party, such as citizens, public interest groups, or the judiciary, to use resources created by enabling legislation only for the purposes specified by the legislation.

Committed – The committed fund balance classification includes amounts that can be used only for the specific purposes imposed by formal action (resolution) of the Board. Those committed amounts cannot be used for any other purpose unless the Board removes or changes the specified use by taking the same type of action (resolution) it employed to previously commit those amounts. In contrast to a fund balance that is restricted by enabling legislation, the committed fund balance classification may be redeployed for other purposes with appropriate due process. Constraints imposed on the use of committed amounts are imposed by the Board, separate from the authorization to raise the underlying revenue; therefore, compliance with these constraints is not considered to be legally enforceable. The committed fund balance also incorporates contractual obligations to the extent that existing resources in the fund have been specifically committed for use in satisfying those contractual requirements.

Assigned – Amounts in the assigned fund balance classification are intended to be used by the State Bar for specific purposes, but do not meet the criteria to be classified as restricted or committed. In Governmental Funds other than the General Fund, assigned fund balance represents the remaining amount that is not restricted or committed. In the General Fund, assigned amounts represent intended uses established by the Board or a State Bar official delegated by the Board or by resolution.

Unassigned – Unassigned fund balance is the residual classification for the General Fund and includes all spendable amounts not contained in the other classifications. In other Governmental Funds, the unassigned classification is used only to report a deficit balance resulting from overspending for specific purposes for which amounts had been restricted, committed, or assigned.

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May 31, 2014

When expenditures are incurred for purposes for which both restricted and unrestricted fund balance is available, the State Bar considers amounts to have been spent first out of restricted funds, then committed funds, then assigned funds, and finally unassigned funds, as needed, unless the Board or its delegated official has provided otherwise in its commitment or assignment actions.

The following table details fund balances between the various categories:

| | <u>General Fund</u> | <u>Client Security Fund</u> | <u>Sections</u> | <u>Nonmajor Governmental Funds</u> | <u>Total</u> |
|---|-------------------------|-------------------------------------|---------------------|--|----------------------|
| Fund balances: | | | | | |
| Nonspendable: | | | | | |
| Prepaid items | \$ 426,545 | \$ - | \$ 38,159 | \$ 126,484 | \$ 591,188 |
| Inventories | 10,640 | - | - | - | 10,640 |
| Committed to: | | | | | |
| Texas Law Center projects | 190,321 | - | - | 2,357,443 | 2,547,764 |
| Access to Justice student loan repayment program | 663,160 | - | - | - | 663,160 |
| Law related education – website | 40,769 | - | - | - | 40,769 |
| Texas Court Records Preservation Task Force | 201,917 | - | - | - | 201,917 |
| Presidential initiatives | 200,923 | - | - | - | 200,923 |
| Statewide Pro Bono Recruitment Campaign | 654,483 | - | - | - | 654,483 |
| Texas Bar Journal readership survey | 25,000 | - | - | - | 25,000 |
| Professionalism and ethics initiatives | 25,035 | - | - | - | 25,035 |
| Alternative Careers | 95,000 | - | - | - | 95,000 |
| Compensation Analysis | 30,000 | - | - | - | 30,000 |
| Client Security Fund expenditures | 1,204,305 | 2,488,216 | - | - | 3,692,521 |
| Sections expenditures | - | - | 6,785,244 | - | 6,785,244 |
| Information technology projects | 1,000,000 | - | - | 1,057,627 | 2,057,627 |
| Special revenue funds | - | - | - | 1,106,421 | 1,106,421 |
| Unassigned | <u>9,876,655</u> | <u>-</u> | <u>-</u> | <u>-</u> | <u>9,876,655</u> |
| Total fund balances | <u>\$ 14,644,753</u> | <u>\$ 2,488,216</u> | <u>\$ 6,823,403</u> | <u>\$ 4,647,975</u> | <u>\$ 28,604,347</u> |

At the September 2005 Board meeting, the Board adopted a financial policy to maintain a minimum level of unrestricted fund balance. The minimum level for this fiscal year is \$9,077,035 of the unassigned fund balance for fiscal year 2014. The target level is based on 2.7 months of budgeted operating expenditures.

Budgetary Information

The State Bar's budget is prepared annually by the Executive Director and is reviewed by the budget committee of the Board. The budget passes several stages of review, including a public hearing, adoption by the Board, and approval by the Supreme Court of Texas. The budget may be amended at any meeting of the Board, but the amendments made are subject to the approval of the Supreme Court of Texas. Variances from budgeted revenues and expenditures are analyzed by management, the finance committee, the executive committee, and the Board. Regulations do not prohibit the State Bar from having unfavorable variances.

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Notes to the Financial Statements

May 31, 2014

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. This will affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenditures/expenses during the reporting period. Actual results could differ from these estimates.

Compensated Absences

The State Bar allows employees to accumulate vacation leave with certain limitations. Accumulated vacation leave that is expected to be liquidated with expendable available financial resources in the event of termination is reported as an expenditure and a liability of the governmental funds that will pay the liability. Amounts of accumulated vacation leave that are not expected to be liquidated are reported in the governmental activities. Accumulated vacation leave of the Proprietary Funds is recorded as an expense and liability of those funds as the benefits accrue to employees. All full-time employees accumulate compensable leave in amounts ranging from 8 to 15 hours per month, depending on service, up to a maximum allowable accumulation ranging from 180 to 388 hours.

GASB Implementation

During the year, the State Bar adopted GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities*.

GASB Statement No. 65 properly establishes accounting and financial reporting standards that reclassify, as deferred outflows of resources, certain items that were previously reported as assets and liabilities and recognizes, as outflows of resources or inflows of resources, certain items that were previously reported as assets and liabilities. These determinations are based on the definitions of those elements in the Concepts Statement No. 4, *Elements of Financial Statements*.

The following GASB statements were reviewed and determined to be nonapplicable for the State Bar:

GASB Statement No. 66, *Technical Corrections – 2012 – an Amendment of GASB Statements No. 10 and No. 62* – This statement states that in the first period of adoption, changes made should be treated as an adjustment of prior periods, and financial statements presented for the periods affected should be restated. If restatement of financial statements for prior periods is not practical, the cumulative effect of adoption should be reported as a restatement of beginning net position (or fund balance or fund net position, as appropriate) for the earliest period restated (generally the current period). In the first period of adoption, the financial statements should disclose the nature of the restatement and its effect.

GASB Statement No. 67, *Financial Reporting for Pension Plans – an Amendment of GASB Statement No. 25* – This statement replaces requirements of GASB Statements No. 25, *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans*, and No. 50, *Pension Disclosures – an Amendment of GASB Statements No. 25 and No. 27*, related to pension plans administered through trusts or similar arrangements. This statement uses the existing framework for financial reports of defined benefit pension plans, including a statement of fiduciary net position and a statement of changes in fiduciary net position; enhances note disclosures and required supplementary information for both

State Bar of Texas

Notes to the Financial Statements

May 31, 2014

defined benefit and defined contribution pension plans; and requires the presentation of information about annual money-weighted rates of return in the notes and in 10-year required supplementary information schedules.

GASB Statement No. 69, *Government Combinations and Disposals of Government Operations* – This statement establishes accounting and financial reporting standards related to government combinations and disposals of government operations. The term “government combinations” includes a variety of transactions referred to as mergers, acquisitions, and transfers of operations.

GASB Statement No. 70, *Accounting and Financial Reporting for Nonexchange Financial Guarantees* – This statement requires a government that extends a nonexchange financial guarantee to recognize a liability when qualitative factors and historical data, if any, indicate that it is more likely than not that the government will be required to make a payment on the guarantee. This statement also requires a government that has issued an obligation guaranteed in a nonexchange transaction to report the obligation until legally released as an obligor and requires a government that is required to repay a guarantor for making a payment on a guaranteed obligation or legally assuming the guaranteed obligation to continue to recognize a liability until legally released as an obligor.

2. Deposits and Investments

As of May 31, 2014, the carrying amount of deposits was \$19,919,351, all of which is included in governmental funds and consists of \$7,910,180 of cash in banks and \$12,009,171 of cash equivalents in money market accounts. Additionally, the State Bar’s certificate of deposit purchases are covered by Federal Deposit Insurance Corporation insurance.

Deposit Custodial Credit Risk

In the case of deposits, the risk is that in the event of a bank failure, the State Bar’s deposits may not be returned to it. The State Bar has a deposit policy for custodial credit risk. As of May 31, 2014, the State Bar is not exposed to deposit custodial credit risk because it was collateralized with securities held by the Federal Reserve in the State Bar’s name in the amount of \$14,000,000. None of the State Bar’s funds are held in foreign currency.

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May 31, 2014

As of May 31, 2014, the State Bar had the following investments, all of which are included in governmental funds:

| <u>Description</u> | <u>Value</u> | <u>Rating</u> | <u>Organization</u> | <u>(In Days)</u> |
|---|----------------------|---------------|---------------------|------------------|
| United States government agency obligations | \$ 14,288,734 | AA+ | Standard & Poor's | 463 |
| Commercial paper | 7,495,954 | A-1+/A-1 | Standard & Poor's | 97 |
| Certificates of deposit | <u>1,031,339</u> | N/A | N/A | 422 |
| Total investments | \$ <u>22,816,027</u> | | | |

Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The State Bar's investment policy allows for various types of investments including: United States government agency obligations, United States Treasury securities, and money market funds investments. Investments in United States government agency obligations are not guaranteed by the United States government, but are government sponsored enterprises.

Custodial Credit Risk

In the case of investments, there is a risk that in the event of the failure of a counterparty, the State Bar will not be able to recover the value of its investment in the possession of an outside party. The State Bar had no exposed investment custodial credit risk at May 31, 2014.

Concentration of Credit Risk

Concentration of credit risk is the risk of loss attributable to the magnitude of investment in a single issuer. Information regarding investments in any one issuer that represents 5% or more of the State Bar's total investments must be disclosed under GASB Statement No. 40, excluding investments issued or explicitly guaranteed by the United States government.

As of May 31, 2014, the State Bar's investments consist of the following:

| <u>Issuer</u> | <u>Fair Value</u> | <u>Percentage</u> |
|---|----------------------|-------------------|
| Federal Home Loan Bank | \$ 2,000,116 | 9% |
| Federal Home Loan Mortgage Corp. | 8,717,433 | 37% |
| Commercial paper | 7,495,954 | 33% |
| Federal National Mortgage Association | 3,126,109 | 14% |
| Certificates of deposit | 1,031,339 | 5% |
| United States government agency obligations | <u>445,076</u> | <u>2%</u> |
| Total investments | \$ <u>22,816,027</u> | <u>100%</u> |

State Bar of Texas

Notes to the Financial Statements

May 31, 2014

Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. In accordance with its investments policy, the State Bar manages its exposure to declines in fair values by limiting the types of investment it allows and by limiting the average maturity to five years.

3. Interfund Receivables, Payables, and Transfers

During the course of operations, numerous transactions occur between individual funds for goods provided or services rendered. These receivables and payables are classified as “due from other funds” or “due to other funds.” The composition of interfund balances as of May 31, 2014 is as follows:

| <u>Receivable Fund</u> | <u>Payable Fund</u> | <u>Amount</u> |
|-----------------------------|-----------------------------|---------------------|
| General Fund | Nonmajor Governmental Funds | \$ 98,643 |
| General Fund | Client Security Fund | 314,949 |
| Nonmajor Governmental Funds | General Fund | 1,102,144 |
| Agency Fund | General Fund | 696,764 |
| Sections | General Fund | 1,180,830 |
| Enterprise Fund | General Fund | <u>337,078</u> |
| Total | | <u>\$ 3,730,408</u> |

During the year, the General Fund transferred \$800,000 to the Client Security Fund and \$883,067 to nonmajor governmental funds to supplement operations and to fund claims, technology projects, and future renovations to the Texas Law Center.

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Notes to the Financial Statements
 May 31, 2014

4. Changes in Capital Assets

Capital asset activity for the year ended May 31, 2014 was as follows:

| | <u>Balance at May 31, 2013</u> | <u>Increases</u> | <u>Decreases</u> | <u>Balance at May 31, 2014</u> |
|---|------------------------------------|---------------------|-------------------|------------------------------------|
| Governmental activities: | | | | |
| Capital assets not being depreciated: | | | | |
| Land | \$ 154,074 | \$ - | \$ - | \$ 154,074 |
| Construction in progress | <u>-</u> | <u>10,500</u> | <u>-</u> | <u>10,500</u> |
| Total capital assets not being depreciated | <u>154,074</u> | <u>10,500</u> | <u>-</u> | <u>164,574</u> |
| Capital assets being depreciated | | | | |
| Building | 6,282,249 | - | - | 6,282,249 |
| Furniture, equipment, and other | <u>15,537,838</u> | <u>368,724</u> | <u>(21,688)</u> | <u>15,884,874</u> |
| Total capital assets being depreciated | <u>21,820,087</u> | <u>368,724</u> | <u>(21,688)</u> | <u>22,167,123</u> |
| Less accumulated depreciation for: | | | | |
| Building | (5,654,024) | - | - | (5,654,024) |
| Furniture, equipment, and other | <u>(6,518,177)</u> | <u>(975,241)</u> | <u>19,520</u> | <u>(7,473,898)</u> |
| Total accumulated depreciation | <u>(12,172,201)</u> | <u>(975,241)</u> | <u>19,520</u> | <u>(13,127,922)</u> |
| Total capital assets being depreciated – net | <u>9,647,886</u> | <u>(606,517)</u> | <u>(2,168)</u> | <u>9,039,201</u> |
| Governmental activities capital assets – net | <u>\$ 9,801,960</u> | <u>\$ (596,017)</u> | <u>\$ (2,168)</u> | <u>\$ 9,203,775</u> |
| Business-type activities: | | | | |
| Digital publication | \$ 300,659 | \$ - | \$ - | \$ 300,659 |
| Furniture, equipment, and other | 375,680 | - | - | 375,680 |
| Accumulated depreciation | <u>(629,330)</u> | <u>(7,383)</u> | <u>-</u> | <u>(636,713)</u> |
| Business-type activities capital assets – net | <u>\$ 47,009</u> | <u>\$ (7,383)</u> | <u>\$ -</u> | <u>\$ 39,626</u> |

State Bar of Texas

Notes to the Financial Statements

May 31, 2014

Depreciation expense for the year ended May 31, 2014 for governmental activities totaled \$975,241 which was allocated in the following manner:

| <u>Functions/Programs</u> | |
|---------------------------|-------------------|
| General government | \$ 943,196 |
| Member services | 24,212 |
| Public protection | 4,857 |
| Public service | <u>2,976</u> |
| | <u>\$ 975,241</u> |

Depreciation expense for business-type activities totaled \$7,383 for the year ended May 31, 2014.

5. Capital Lease Obligations

During the fiscal year, the State Bar entered into a lease agreement as lessee for financing the acquisition of computer equipment valued at \$10,390. The equipment has a five-year estimated useful life. This year, \$769 was included in depreciation expense. This lease agreement qualifies as a capital lease for accounting purposes and, therefore, has been recorded at the present value of future minimum lease payments as of the inception date.

The State Bar is obligated under capital leases for certain equipment. The following is a schedule of future minimum lease payments under the capital leases, together with the net present value of all minimum lease payments as of May 31, 2014:

| | <u>Governmental Activities</u> |
|--|------------------------------------|
| 2015 | \$ 53,046 |
| 2016 | 2,285 |
| 2017 | 2,285 |
| 2018 | <u>2,285</u> |
| Total minimum lease payments | 59,901 |
| Less amounts representing interest | <u>3,455</u> |
| Due under capital lease obligations | 56,446 |
| Less current capital lease obligations | <u>50,223</u> |
| Long-term capital lease obligations | <u>\$ 6,223</u> |

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Notes to the Financial Statements

May 31, 2014

6. Operating Lease Obligations

At May 31, 2014, the State Bar was obligated under operating leases for the regional Chief Disciplinary Counsel Department's and the Texas Board of Legal Specialization's office space. Future minimum lease payments on these operating leases are as follows:

| | |
|---------------------|---------------------|
| Year ending May 31, | |
| 2015 | \$ 443,538 |
| 2016 | 384,808 |
| 2017 | 344,390 |
| 2018 | 339,806 |
| 2019 | 344,259 |
| Later years | <u>737,838</u> |
| | \$ <u>2,594,639</u> |

Rent expense incurred under all office space operating leases for the year ended May 31, 2014 totaled \$454,121.

7. Long-Term Liabilities

A summary of changes in long-term liabilities for the State Bar is shown below:

| | <u>Beginning Balance</u> | <u>Additions</u> | <u>Reductions</u> | <u>Ending Balance</u> | <u>Amount Due Within One Year</u> |
|-----------------------------------|------------------------------|-------------------|---------------------|---------------------------|---|
| Governmental activities: | | | | | |
| Capital lease obligations | \$ 206,655 | \$ 10,390 | \$ (160,599) | \$ 56,446 | \$ 50,223 |
| Accrued compensated absences | <u>1,396,749</u> | <u>495,398</u> | <u>(420,226)</u> | <u>1,471,921</u> | <u>531,116</u> |
| Total governmental activities | \$ <u>1,603,404</u> | \$ <u>505,788</u> | \$ <u>(580,825)</u> | \$ <u>1,528,367</u> | \$ <u>581,339</u> |
| Business-type activities: | | | | | |
| Capital lease obligations | \$ 7,348 | \$ | \$ (7,348) | \$ - | \$ - |
| Accrued compensated absences | <u>56,826</u> | <u>30,073</u> | <u>(19,327)</u> | <u>67,572</u> | <u>29,583</u> |
| Total business-type activities | \$ <u>64,174</u> | \$ <u>30,073</u> | \$ <u>(26,675)</u> | \$ <u>67,572</u> | \$ <u>29,583</u> |

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Notes to the Financial Statements

May 31, 2014

Retirement Plan

The State Bar contributes to the Employees Retirement System of Texas ("ERS"), a public employee retirement system. It is a single employer defined benefit pension plan, with all risks and costs being the liability of the State of Texas. ERS provides service retirement, death, and disability benefits to plan members and beneficiaries. ERS operates under the authority of provisions contained primarily in Texas Government Code, Title 8, Public Retirement Systems, Subtitle B, Employees Retirement System of Texas, which is subject to amendment by the Texas Legislature. The ERS' annual financial report and other required disclosure information are available by writing the Employees Retirement System of Texas, P.O. Box 13207, Austin, Texas, 78711-3207 or by calling (512) 476-6431.

Under provisions in state law, plan members are required to contribute 6.6% of their annual covered salary and the State Bar contributes an amount equal to 8.0% of the State Bar's covered payroll. The State Bar's contributions to ERS for the years ended May 31, 2014, 2013, and 2012, were \$1,335,953, \$1,080,506, and \$1,014,000, respectively. Beginning September 1, 2014 plan members are required to contribute 6.9% of their annual covered salary and the State Bar contributes an amount equal to 8.0% of the State Bar's covered payroll.

8. Risk Management

The State Bar is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The State Bar purchased commercial insurance to cover risks associated with potential claims in 2014. There were no significant reductions in coverage in the past fiscal year, and there were no settlements exceeding insurance coverage.

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Required Supplemental Information

State Bar of Texas

Statement of Revenues, Expenditures, and Changes in Fund Balance – Budget (GAAP Basis) and Actual – General Fund

Year Ended May 31, 2014

| | Budgeted Amounts – Original and Final | Actual | Variance Favorable (Unfavorable) |
|-------------------------------------|--|-------------------|--|
| Revenues | | | |
| Membership dues | \$ 19,663,656 | \$ 19,432,743 | \$ (230,913) |
| Accounting and management fees | 637,299 | 657,269 | 19,970 |
| Texas Bar Journal | 711,800 | 724,581 | 12,781 |
| MCLE fees | 2,793,000 | 2,850,550 | 57,550 |
| Professional development | 13,647,277 | 12,918,406 | (728,871) |
| Investment income | 80,000 | 78,259 | (1,741) |
| Other income | <u>2,170,360</u> | <u>2,540,779</u> | <u>370,419</u> |
| Total revenues | <u>39,703,392</u> | <u>39,202,587</u> | <u>(500,805)</u> |
| Expenditures | | | |
| Executive: | | | |
| Office of Executive Director | 524,269 | 485,221 | 39,048 |
| Office of Deputy Executive Director | 345,962 | 82,972 | 262,990 |
| Director of Special Projects | 155,841 | 156,818 | (977) |
| Deputy Director and Legal Counsel | 418,934 | 354,137 | 64,797 |
| Assistant Deputy Director | 129,859 | 142,757 | (12,898) |
| Officers and directors | <u>761,837</u> | <u>828,899</u> | <u>(67,062)</u> |
| Total executive | <u>2,336,702</u> | <u>2,050,804</u> | <u>285,898</u> |
| External Affairs: | | | |
| External Affairs Officer | 158,863 | 158,146 | 717 |
| Governmental relations | 316,876 | 283,495 | 33,381 |
| Sections | 268,180 | 273,421 | (5,241) |
| Local bars | 372,768 | 391,367 | (18,599) |
| Special events | <u>88,604</u> | <u>69,757</u> | <u>18,847</u> |
| Total external affairs | <u>1,205,291</u> | <u>1,176,186</u> | <u>29,105</u> |
| Member and public services: | | | |
| Member and Public Services Director | 153,320 | 149,957 | 3,363 |
| Center for Legal History | 144,624 | 138,179 | 6,445 |
| Law Related Education | 461,985 | 414,223 | 47,762 |
| Law Student Department | 20,266 | 18,876 | 1,390 |
| Texas Young Lawyers Association | <u>900,421</u> | <u>859,018</u> | <u>41,403</u> |
| Total member and public services | <u>1,680,616</u> | <u>1,580,253</u> | <u>100,363</u> |
| Professional development: | | | |
| Texas Bar CLE | 10,174,305 | 9,513,575 | 660,730 |
| Minority affairs | <u>378,179</u> | <u>437,305</u> | <u>(59,126)</u> |
| Total professional development | <u>10,552,484</u> | <u>9,950,880</u> | <u>601,604</u> |

State Bar of Texas

Statement of Revenues, Expenditures, and Changes in Fund Balance – Budget (GAAP Basis) and Actual – General Fund – Continued

Year Ended May 31, 2014

| | Budgeted Amounts – Original and Final | Actual | Variance Favorable (Unfavorable) |
|--|--|------------------|---|
| Legal and attorney services: | | | |
| Legal and Attorney Services Director | \$ 122,512 | \$ 213,797 | \$ (91,285) |
| Texas Lawyers Assistance Program | 329,175 | 316,094 | 13,081 |
| Legal Access Department | <u>1,321,704</u> | <u>1,301,494</u> | <u>20,210</u> |
| Total legal and attorney services | <u>1,773,391</u> | <u>1,831,385</u> | <u>(57,994)</u> |
| Access to Justice Commission | <u>710,265</u> | <u>600,543</u> | <u>109,722</u> |
| Total Access to Justice Commission | <u>710,265</u> | <u>600,543</u> | <u>109,722</u> |
| Attorney compliance: | | | |
| Office of Attorney Compliance Director | 153,626 | 149,582 | 4,044 |
| Advertising review | 222,846 | 151,057 | 71,789 |
| Client Attorney Assistance Program | 542,925 | 505,471 | 37,454 |
| Lawyer referral | 336,656 | 339,138 | (2,482) |
| Membership | 889,879 | 899,779 | (9,900) |
| MCLE | 634,475 | 630,386 | 4,089 |
| SBOT Volunteer Committees | <u>301,980</u> | <u>219,318</u> | <u>82,662</u> |
| Total attorney compliance | <u>3,082,387</u> | <u>2,894,731</u> | <u>187,656</u> |
| Administration: | | | |
| Office of Administration Director | 99,799 | 96,842 | 2,957 |
| Human resources | 407,651 | 400,872 | 6,779 |
| Training and tuition | 101,133 | 59,200 | 41,933 |
| Purchasing and facilities | 1,140,702 | 1,122,126 | 18,576 |
| Research and analysis | 115,257 | 91,843 | 23,414 |
| Professional liability insurance | - | 78,212 | (78,212) |
| Royalties | <u>-</u> | <u>159,985</u> | <u>(159,985)</u> |
| Total administration | <u>1,864,542</u> | <u>2,009,080</u> | <u>(144,538)</u> |
| Finance: | | | |
| Finance | 917,642 | 1,074,813 | (157,171) |
| Other administrative | <u>1,006,000</u> | <u>963,782</u> | <u>42,218</u> |
| Total finance | <u>1,923,642</u> | <u>2,038,595</u> | <u>(114,953)</u> |
| Information technology: | | | |
| Information technology | 1,239,314 | 1,229,536 | 9,778 |
| Customer service | <u>351,865</u> | <u>347,488</u> | <u>4,377</u> |
| Total information technology | <u>1,591,179</u> | <u>1,577,024</u> | <u>14,155</u> |

State Bar of Texas

Statement of Revenues, Expenditures, and Changes in Fund Balance – Budget (GAAP Basis) and Actual – General Fund – Continued

Year Ended May 31, 2014

| | Budgeted Amounts – Original and Final | Actual | Variance Favorable (Unfavorable) |
|---|--|----------------------|--|
| Communications: | | | |
| Office of Communications Director | \$ 271,508 | \$ 204,238 | \$ 67,270 |
| State Bar of Texas Leadership Academy | 94,000 | 93,442 | 558 |
| Texas Bar Journal | 1,393,748 | 1,435,834 | (42,086) |
| Public information | 198,114 | 202,336 | (4,222) |
| Web management | 434,367 | 351,979 | 82,388 |
| Total communications | <u>2,391,737</u> | <u>2,287,829</u> | <u>103,908</u> |
| Public protection: | | | |
| Chief Disciplinary Counsel | 8,653,643 | 8,776,178 | (122,535) |
| Grievance Oversight Committee | 48,800 | 36,047 | 12,753 |
| Unauthorized Practice of Law | 170,000 | 151,988 | 18,012 |
| Professional Ethics Commission | 11,080 | 7,877 | 3,203 |
| Board of Disciplinary Appeals | 524,566 | 502,028 | 22,538 |
| Total public protection | <u>9,408,089</u> | <u>9,474,118</u> | <u>(66,029)</u> |
| Expenditures related to Board commitments: | | | |
| Presidential initiatives | 200,000 | 138,988 | 61,012 |
| Statewide pro-bono campaign | 794,250 | 139,767 | 654,483 |
| Document preservation | 251,917 | 50,000 | 201,917 |
| Alternative careers | 115,000 | 115,000 | - |
| ATJ foundation student loan repayment program | 350,000 | 350,000 | - |
| LRE website update | 76,000 | 75,231 | 769 |
| TBJ survey | 25,000 | - | 25,000 |
| Ethics initiatives | 30,000 | 4,962 | 25,038 |
| Total expenditures related to board commitments | <u>1,842,167</u> | <u>873,948</u> | <u>968,219</u> |
| Total expenditures | <u>40,362,492</u> | <u>38,345,376</u> | <u>2,017,116</u> |
| Excess (deficiency) of revenues over (under) expenditures | <u>(659,100)</u> | <u>857,211</u> | <u>1,516,311</u> |
| Other Financing Sources (Uses) | | | |
| Transfers in (out) to: | | | |
| Technology Fund | (400,000) | (400,000) | - |
| Texas Law Center | (483,067) | (483,067) | - |
| Client Security Fund | (800,000) | (800,000) | - |
| Total other financing sources (uses) | <u>(1,683,067)</u> | <u>(1,683,067)</u> | <u>-</u> |
| Net change in fund balances | (2,342,167) | (825,856) | 1,516,311 |
| Fund balance at beginning of year | <u>15,470,609</u> | <u>15,470,609</u> | <u>-</u> |
| Fund balance at end of year | <u>\$ 13,128,442</u> | <u>\$ 14,644,753</u> | <u>\$ 1,516,311</u> |

Other Supplemental Information

State Bar of Texas

Combining Balance Sheet – Nonmajor Governmental Funds

May 31, 2014

| ASSETS | Texas Board of Legal Specialization Fund | State Bar College | Annual Meeting | Texas Law Center | Technology Fund | Project Grants Fund | Hatton W. Summers Grants Fund | Law Focused Education | Total Nonmajor Governmental Funds |
|-------------------------------------|---|-------------------------|-------------------|------------------------|---------------------|---------------------------|--|-----------------------------|--|
| Assets | | | | | | | | | |
| Current assets: | | | | | | | | | |
| Cash and cash equivalents | \$ 1,399,056 | \$ 342,930 | \$ 508,706 | \$ 3,578 | \$ - | \$ - | \$ 227,587 | \$ 20,000 | \$ 2,501,857 |
| Investments | - | - | - | 2,352,143 | - | - | - | - | 2,352,143 |
| Receivables: | | | | | | | | | |
| Interest receivable | - | - | - | 14,697 | - | - | - | - | 14,697 |
| Other accounts receivable | 60,325 | - | - | - | - | - | - | - | 60,325 |
| Due from other governmental funds | - | - | - | - | 1,057,627 | 44,517 | - | - | 1,102,144 |
| Prepaid expenditures | 8,493 | - | 117,991 | - | - | - | - | - | 126,484 |
| Total assets | <u>\$ 1,467,874</u> | <u>\$ 342,930</u> | <u>\$ 626,697</u> | <u>\$ 2,370,418</u> | <u>\$ 1,057,627</u> | <u>\$ 44,517</u> | <u>\$ 227,587</u> | <u>\$ 20,000</u> | <u>\$ 6,157,650</u> |
| LIABILITIES AND FUND BALANCE | | | | | | | | | |
| Liabilities | | | | | | | | | |
| Current liabilities: | | | | | | | | | |
| Accrued liabilities | \$ - | \$ 8 | \$ 570 | \$ - | \$ - | \$ - | \$ - | \$ - | \$ 578 |
| Due to other governmental funds | 67,253 | 9,691 | 4,480 | 12,975 | - | - | 1,744 | 2,500 | 98,643 |
| Unearned revenue | 620,521 | 139,545 | 362,528 | - | - | 44,517 | 225,843 | 17,500 | 1,410,454 |
| Total liabilities | <u>687,774</u> | <u>149,244</u> | <u>367,578</u> | <u>12,975</u> | <u>-</u> | <u>44,517</u> | <u>227,587</u> | <u>20,000</u> | <u>1,509,675</u> |
| Fund Balances | | | | | | | | | |
| Nonspendable | 8,493 | - | 117,991 | - | - | - | - | - | 126,484 |
| Committed | 771,607 | 193,686 | 141,128 | 2,357,443 | 1,057,627 | - | - | - | 4,521,491 |
| Total fund balances | <u>780,100</u> | <u>193,686</u> | <u>259,119</u> | <u>2,357,443</u> | <u>1,057,627</u> | <u>-</u> | <u>-</u> | <u>-</u> | <u>4,647,975</u> |
| Total liabilities and fund balances | <u>\$ 1,467,874</u> | <u>\$ 342,930</u> | <u>\$ 626,697</u> | <u>\$ 2,370,418</u> | <u>\$ 1,057,627</u> | <u>\$ 44,517</u> | <u>\$ 227,587</u> | <u>\$ 20,000</u> | <u>\$ 6,157,650</u> |

State Bar of Texas

Combining Statement of Revenues, Expenditures, and Changes in Fund Balances – Nonmajor Governmental Funds

Year Ended May 31, 2014

| | <u>Texas Board of Legal Specialization Fund</u> | <u>State Bar College</u> | <u>Annual Meeting</u> | <u>Texas Law Center</u> | <u>Technology Fund</u> | <u>Project Grants Fund</u> | <u>Hatton W. Summers Grants Fund</u> | <u>Law Focused Education</u> | <u>Total Nonmajor Governmental Funds</u> |
|--|---|----------------------------------|---------------------------|---------------------------------|----------------------------|------------------------------------|--|--------------------------------------|--|
| Revenues | | | | | | | | | |
| Investment income | \$ 1,006 | \$ 260 | \$ 287 | \$ 7,079 | \$ - | \$ - | \$ 120 | \$ - | \$ 8,752 |
| Grant revenue | - | - | - | - | - | 84,760 | 358,967 | - | 443,727 |
| Other income | 1,295,440 | 248,049 | 590,771 | - | - | - | - | 3,508 | 2,137,768 |
| Total revenues | <u>1,296,446</u> | <u>248,309</u> | <u>591,058</u> | <u>7,079</u> | <u>-</u> | <u>84,760</u> | <u>359,087</u> | <u>3,508</u> | <u>2,590,247</u> |
| Expenditures | | | | | | | | | |
| Special services | 1,154,156 | 215,487 | 599,658 | - | - | 84,760 | 359,087 | 3,508 | 2,416,656 |
| Administration | - | - | - | 43,990 | - | - | - | - | 43,990 |
| Information technology | - | - | - | - | 884,804 | - | - | - | 884,804 |
| Total expenditures | <u>1,154,156</u> | <u>215,487</u> | <u>599,658</u> | <u>43,990</u> | <u>884,804</u> | <u>84,760</u> | <u>359,087</u> | <u>3,508</u> | <u>3,345,450</u> |
| Excess (deficiency) of revenues over (under) expenditures | <u>142,290</u> | <u>32,822</u> | <u>(8,600)</u> | <u>(36,911)</u> | <u>(884,804)</u> | <u>-</u> | <u>-</u> | <u>-</u> | <u>(755,203)</u> |
| Other Financing Sources (Uses) | | | | | | | | | |
| Proceeds from capital leases | - | - | - | - | 10,390 | - | - | - | 10,390 |
| Transfers in | - | - | - | 483,067 | 400,000 | - | - | - | 883,067 |
| Total other financing sources (uses) | <u>-</u> | <u>-</u> | <u>-</u> | <u>483,067</u> | <u>410,390</u> | <u>-</u> | <u>-</u> | <u>-</u> | <u>893,457</u> |
| Net change in fund balances | 142,290 | 32,822 | (8,600) | 446,156 | (474,414) | - | - | - | 138,254 |
| Fund balances at beginning of year | <u>637,810</u> | <u>160,864</u> | <u>267,719</u> | <u>1,911,287</u> | <u>1,532,041</u> | <u>-</u> | <u>-</u> | <u>-</u> | <u>4,509,721</u> |
| Fund balances at end of year | <u>\$ 780,100</u> | <u>\$ 193,686</u> | <u>\$ 259,119</u> | <u>\$ 2,357,443</u> | <u>\$ 1,057,627</u> | <u>\$ -</u> | <u>\$ -</u> | <u>\$ -</u> | <u>\$ 4,647,975</u> |

State Bar of Texas

Combining Statement of Revenues, Expenditures, and Changes in Fund Balances – Governmental Funds

Year Ended May 31, 2014

| | General Fund | Client Security Fund | Sections | Nonmajor Governmental Funds | Total Governmental Funds |
|---|----------------------|----------------------------|---------------------|-----------------------------------|--------------------------------|
| Revenues | | | | | |
| Membership dues | \$ 19,432,743 | \$ - | \$ 2,122,343 | \$ - | \$ 21,555,086 |
| Accounting/management fees | 657,269 | - | - | - | 657,269 |
| Texas Bar journal | 724,581 | - | - | - | 724,581 |
| MCLE fees | 2,850,550 | - | - | - | 2,850,550 |
| Professional development | 12,918,406 | - | - | - | 12,918,406 |
| Investment income | 78,259 | 11,448 | 17,328 | 8,752 | 115,787 |
| Grant revenue | - | - | - | 443,727 | 443,727 |
| Other income | 2,540,779 | 13,983 | 1,339,784 | 2,137,768 | 6,032,314 |
| Total revenues | <u>39,202,587</u> | <u>25,431</u> | <u>3,479,455</u> | <u>2,590,247</u> | <u>45,297,720</u> |
| Expenditures | | | | | |
| Salaries | 16,468,404 | - | - | 512,738 | 16,981,142 |
| Benefits | 4,780,305 | - | - | 155,328 | 4,935,633 |
| Travel | 1,920,472 | - | 261,075 | 238,470 | 2,420,017 |
| Meetings and conferences | 4,014,259 | - | 1,355,842 | 521,098 | 5,891,199 |
| Professional services | 2,965,593 | - | 331,838 | 419,974 | 3,717,405 |
| Court fees | 82,621 | - | - | - | 82,621 |
| Publicity and advertising | 824,636 | - | 61,382 | 105,800 | 991,818 |
| Dues, subscriptions, and licenses | 727,983 | - | - | 27,398 | 755,381 |
| Education and training | 131,536 | - | 75,572 | 3,807 | 210,915 |
| Supplies, awards, gifts, and specialty items | 527,823 | - | 22,806 | 147,830 | 698,459 |
| Rentals – office, equipment, and storage | 975,853 | - | - | 99,287 | 1,075,140 |
| Maintenance and repairs | 575,036 | - | - | 328,399 | 903,435 |
| Utilities | 240,372 | - | - | - | 240,372 |
| Postage and freight | 810,893 | - | 14,087 | 30,901 | 855,881 |
| Telephone | 353,152 | - | 2,192 | 16,575 | 371,919 |
| Insurance | 381,734 | - | - | - | 381,734 |
| Claims and judgments | - | 1,346,419 | - | - | 1,346,419 |
| Administrative | 878,487 | - | 597,190 | 134,438 | 1,610,115 |
| Printing and copying | 1,655,223 | - | 391,434 | 71,326 | 2,117,983 |
| Capital outlay | 30,994 | - | - | 357,477 | 388,471 |
| Debt service: | | | | | |
| Principal | - | - | - | 160,596 | 160,596 |
| Interest | - | - | - | 14,008 | 14,008 |
| Total expenditures | <u>38,345,376</u> | <u>1,346,419</u> | <u>3,113,418</u> | <u>3,345,450</u> | <u>46,150,663</u> |
| Excess (deficiency) of revenues over (under) expenditures | <u>857,211</u> | <u>(1,320,988)</u> | <u>366,037</u> | <u>(755,203)</u> | <u>(852,943)</u> |
| Other Financing Sources (Uses) | | | | | |
| Proceeds from capital leases | - | - | - | 10,390 | 10,390 |
| Transfers in | - | 800,000 | - | 883,067 | 1,683,067 |
| Transfers out | (1,683,067) | - | - | - | (1,683,067) |
| Other financing sources (uses) | <u>(1,683,067)</u> | <u>800,000</u> | <u>-</u> | <u>893,457</u> | <u>10,390</u> |
| Net change in fund balances | (825,856) | (520,988) | 366,037 | 138,254 | (842,553) |
| Fund balance at beginning of year | <u>15,470,609</u> | <u>3,009,204</u> | <u>6,457,366</u> | <u>4,509,721</u> | <u>29,446,900</u> |
| Fund balance at end of year | <u>\$ 14,644,753</u> | <u>\$ 2,488,216</u> | <u>\$ 6,823,403</u> | <u>\$ 4,647,975</u> | <u>\$ 28,604,347</u> |