

**NATIONAL CUTTING
HORSE ASSOCIATION**

FINANCIAL STATEMENTS

**Years Ended December 31, 2013 and 2012
with Report of Independent Auditors**

**NATIONAL CUTTING
HORSE ASSOCIATION**

FINANCIAL STATEMENTS

Years Ended December 31, 2013 and 2012

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REPORT OF INDEPENDENT AUDITORS

To the Board of Directors of the
National Cutting Horse Association

We have audited the accompanying financial statements of the National Cutting Horse Association, a not-for-profit organization, which comprise the statements of financial position as of December 31, 2013 and 2012, and the related statements of activities and changes in net assets and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the National Cutting Horse Association as of December 31, 2013 and 2012, and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Whitley Penn LLP

Fort Worth, Texas
June 12, 2014

NATIONAL CUTTING HORSE ASSOCIATION

STATEMENTS OF FINANCIAL POSITION

	December 31,	2013	2012
Assets			
Cash and cash equivalents (Note C)	\$	2,278,357	\$ 643,158
Accounts receivable, net of allowance for doubtful accounts of \$16,522 and \$16,588, respectively		1,151,657	716,388
Accounts receivable - State of Texas incentives		1,954,775	4,301,380
Accrued interest receivable		46,313	52,067
Investments (Note D)		4,053,643	5,032,343
Inventories		4,266	5,666
Prepaid expenses and other assets		210,419	213,607
Property and equipment, net (Note E)		1,924,663	1,953,569
Collections (Note F)		-	-
Total assets		\$11,624,093	\$12,918,178
Liabilities and Net Assets			
Liabilities:			
Accounts payable	\$	1,328,065	\$ 1,170,525
Accounts payable - State of Texas incentives		-	361,959
Other accrued liabilities		95,058	119,381
Deferred revenue for future shows		477,520	965,739
Deferred revenue for stallion/ foal fees (Note M)		1,569,250	1,114,350
Deferred membership dues (Note G)		779,800	710,202
Deferred revenue, other		125,250	82,548
Youth scholarship awards (Note H)		790,420	670,733
Liability for pension obligation (Note L)		215,189	345,066
Total liabilities		5,380,552	5,540,503
Commitments and contingencies			
Net assets:			
Unrestricted:			
Undesignated		4,464,749	4,803,422
Board designated for youth funds (Note H)		272,083	352,693
Total unrestricted		4,736,832	5,156,115
Temporarily restricted - State of Texas incentives (Note I)		1,506,709	2,221,560
Total net assets		6,243,541	7,377,675
Total liabilities and net assets		\$11,624,093	\$12,918,178

See accompanying notes to financial statements.

NATIONAL CUTTING HORSE ASSOCIATION

STATEMENTS OF ACTIVITIES AND CHANGES IN NET ASSETS

	Year Ended December 31,	
	2013	2012
Unrestricted Net Assets		
Operating revenues and support:		
Show revenues and support:		
Entry fees	\$ 6,602,067	6,436,272
Show fees	4,133,310	3,766,486
Stall rentals and practice pen	1,512,474	1,406,990
Purse sponsors	15,551	319,268
Stallion subscription fees (Note M)	500,000	500,000
Booth exhibit rental	414,762	439,134
Tickets	533,825	429,040
Sponsorships	566,461	553,183
Affiliate income	290,319	246,300
Event facility allowances	370,865	382,527
Other show income (Note K)	19,325	17,395
Total show revenues and support	14,958,959	14,496,595
Department revenues and support:		
Advertising	1,575,705	1,594,887
Sponsorships	1,334,500	1,412,865
Affiliate income	1,215,707	1,142,316
Membership dues and fees	748,122	888,608
Horse sales	621,118	592,286
Fund-raising events (Note P)	111,186	131,832
Marketing promotions	213,024	195,366
Other department income (Note K)	310,206	378,827
Total department revenues and support	6,129,568	6,336,987
Net assets released from restrictions-		
State of Texas incentives (Note I)	3,564,636	3,124,231
Total unrestricted operating revenues and support	24,653,163	23,957,813
Operating expenses:		
Show expenses:		
Premiums, including sire awards, and NCHA Day	7,757,724	7,987,727
Premiums from State of Texas incentives	3,178,000	2,768,500
Cattle	2,096,172	1,941,147
Judges, contract labor and show staff, soundmen, security, and paramedics	896,276	808,955
Awards	1,053,936	975,348
Equipment and facilities rent	866,120	779,881
Coliseum preparation	327,388	351,153
Stall rentals and practice pen expenses	203,034	191,988
Advertising	89,998	124,034
Other show expenses (Note K)	484,481	423,659
Total show expenses	16,953,129	16,352,392

See accompanying notes to financial statements.

NATIONAL CUTTING HORSE ASSOCIATION

STATEMENTS OF ACTIVITIES AND CHANGES IN NET ASSETS - *continued*

	Year Ended December 31, 2013	2012
Operating expenses - continued:		
Department expenses:		
Salaries and benefits	\$ 2,226,073	\$ 2,069,774
Retirement expenses (Note L)	63,837	227,611
Affiliate Challenge and NCHA Weekend	78,342	77,938
Awards	364,951	377,402
Printing	402,429	454,190
Equipment and facilities rent	139,342	127,495
Monitor fees and expenses	140,317	152,046
Sponsor advertisements (non-cash)	611,431	611,567
Project, promotional, and public relations (Note N)	878,531	846,980
Advertising	370,642	261,422
Postage	198,644	226,307
Insurance	387,291	370,804
Payroll and ad valorem taxes	206,385	199,877
Professional fees (Note J)	597,002	739,165
Depreciation	146,946	153,716
Other department expenses (Note K)	1,027,583	1,021,914
Total department expenses	7,839,746	7,918,208
Total unrestricted operating expenses	24,792,875	24,270,600
Operating revenues net of operating expenses	(139,712)	(312,787)
Other unrestricted income:		
Interest and dividend income	156,155	191,770
Realized investment losses	(26,407)	(10,672)
Gains on disposals of property and equipment	200	-
Total other unrestricted income	129,948	181,098
Change in unrestricted net assets from operations	(9,764)	(131,689)
Other unrestricted non-operating activities:		
Unrealized losses in market value of investments	(91,338)	(50,713)
Pension Plan changes other than net periodic pension cost	28,651	236,393
Pension Plan settlement loss (Note L)	(163,435)	-
Executive director search expense (Note Q)	(89,539)	-
IT project (Note Q)	(93,858)	-
Employee severance expense (Note Q)	-	(186,795)
Litigation settlement expense (Note Q)	-	(92,707)
Total other unrestricted non-operating activities	(409,519)	(93,822)
Net decrease in unrestricted net assets	(419,283)	(225,511)
Temporarily Restricted Net Assets		
Restricted contributions-State of Texas incentives (Note I)	2,849,785	4,301,380
Net assets released from restrictions-State of Texas incentives (Note I)	(3,564,636)	(3,124,231)
Net increase (decrease) in temporarily restricted net assets	(714,851)	1,177,149
Net increase (decrease) in net assets	(1,134,134)	951,638
Net assets at beginning of year	7,377,675	6,426,037
Net assets at end of year	\$ 6,243,541	\$ 7,377,675

See accompanying notes to financial statements.

NATIONAL CUTTING HORSE ASSOCIATION

STATEMENTS OF CASH FLOWS

	Year Ended December 31,	2013	2012
Operating Activities			
Net increase (decrease) in net assets	\$ (1,134,134)	\$	951,638
Adjustments to reconcile net increase (decrease) in net assets to net cash used in operating activities:			
Depreciation	146,946		153,716
Provision for bad debts	12,032		11,976
Gains on disposals of property and equipment	(200)		-
Net realized and unrealized losses on investments	117,745		61,385
Restricted contributions - State of Texas incentives	(2,849,785)		(4,301,380)
Effect of defined benefit pension plan changes	(134,784)		(236,393)
Changes in operating assets and liabilities:			
Accounts receivable	(447,301)		115,027
Accounts receivable - State of Texas incentives	2,346,605		(2,884,360)
Accrued interest receivable	5,754		(4,801)
Inventories	1,400		(1,950)
Prepaid expenses and other assets	3,188		79,990
Accounts payable and other accrued liabilities	(228,742)		170,373
Deferred revenue for future shows	(488,219)		33,130
Deferred revenue for stallion/ foal fees	454,900		893,750
Deferred membership dues	69,598		2,452
Deferred revenue, other	42,702		(27,147)
Youth scholarship awards	119,687		99,831
Liability for pension obligation	4,907		(181,702)
Net cash used in operating activities	(1,957,701)		(5,064,465)
Investing Activities			
Proceeds from sales of investments	1,513,645		1,764,694
Purchases of investments	(652,690)		(2,469,045)
Purchases of property and equipment	(117,840)		(18,216)
Net cash provided by (used in) investing activities	743,115		(722,567)
Financing Activities			
Restricted contributions-State of Texas incentives	2,849,785		4,301,380
Net cash provided by financing activities	2,849,785		4,301,380
Net increase (decrease) in cash and cash equivalents	1,635,199		(1,485,652)
Cash and cash equivalents at beginning of year	643,158		2,128,810
Cash and cash equivalents at end of year	\$ 2,278,357		\$ 643,158

See accompanying notes to financial statements.

NATIONAL CUTTING HORSE ASSOCIATION

NOTES TO FINANCIAL STATEMENTS

December 31, 2013 and 2012

A. Nature of Activities

The National Cutting Horse Association (the "Association") is a non-profit organization incorporated under the laws of the State of Texas. The purpose of the Association is to encourage the development of, and public interest in, livestock and ranching through the promotion and sponsorship of public cutting horse contests, the public exhibition of cutting horses in conjunction with cattle and livestock, and the presentation and participation of cutting horse events in other general livestock exhibitions, shows and expositions. The Association also sets standards for cutting horse contests; standardizes the election and appointment of judges and directors or spokesmen for such contests, exhibitions and expositions; and, encourages the development and breeding of finer cutting horses. The business operations of the Association are managed based on the items and activities affecting the amounts of the change in unrestricted net assets from operations within the accompanying statements of activities and changes in net assets, along with actual investment earnings. The Association's corporate offices are located in Fort Worth, Texas.

B. Summary of Significant Accounting Policies

A summary of the significant accounting policies of the Association consistently applied in the preparation of the accompanying financial statements follows.

Basis of Accounting

The financial statements of the Association have been prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America ("GAAP").

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from these estimates.

Due to the high volume of business activity conducted in December of each year, the Association closes its books several months after the end of the year which minimizes the number of estimates required to prepare the accompanying annual financial statements.

NATIONAL CUTTING HORSE ASSOCIATION

NOTES TO FINANCIAL STATEMENTS (*continued*)

B. Summary of Significant Accounting Policies – continued

Financial Statement Presentation

The Association presents its financial statements in accordance with Financial Accounting Standards Board (“FASB”) Accounting Standards Codification (“ASC”) Topic No. 958-205, *Not-For-Profit Entities: Presentation of Financial Statements*. Under FASB ASC Topic No. 958-205, the Association is required to report information regarding its financial position and activities according to three classes of net assets: unrestricted net assets, temporarily restricted net assets, and permanently restricted net assets. The Association does not have any permanently restricted net assets.

Contributions

The Association accounts for contributions in accordance with FASB ASC Topic No. 958-605, *Not-For-Profit Entities: Revenue Recognition*, which requires contributions received to be recorded as unrestricted, temporarily restricted, or permanently restricted support depending on the existence and/or nature of any donor restrictions. Under FASB ASC Topic No. 958-605, time or purpose restricted contributions are required to be reported as temporarily restricted support and are then reclassified to unrestricted net assets upon expiration of the time or purpose restriction.

Cash and Cash Equivalents

The Association considers all highly-liquid investments with a maturity of three months or less when purchased to be cash equivalents. The Association maintains deposits primarily in two financial institutions, which may at times exceed amounts covered by insurance provided by the U.S. Federal Deposit Insurance Corporation (“FDIC”). The Association has not experienced any losses related to amounts in excess of FDIC limits.

Investments

The Association follows the provisions of FASB ASC Topic No. 958-320, *Not-for-Profit Entities: Investments—Debt and Equity Securities*, which requires investments with readily determinable fair values to be stated at fair value with realized and unrealized gains and losses included in the statements of activities and changes in net assets of the respective period.

The Association’s investment strategy is generally to hold investments to maturity. If a situation arises whereby there is a substantial gain in a security and there is an opportunity to reinvest the proceeds in a manner that will produce a similar yield, the Association may make the decision to sell the security and realize the gain.

The Association follows the provisions of FASB ASC Topic No. 820, *Fair Value Measurement*, which establishes a framework for measuring fair value. That framework provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy under FASB ASC Topic No. 820 are described below:

NATIONAL CUTTING HORSE ASSOCIATION

NOTES TO FINANCIAL STATEMENTS (*continued*)

B. Summary of Significant Accounting Policies – continued

Investments – continued

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

Level 2 Inputs to the valuation methodology include:

- Quoted prices for similar assets or liabilities in active markets;
- Quoted prices for identical or similar assets or liabilities in inactive markets;
- Inputs other than quoted prices that are observable for the assets or liabilities;
- Inputs that are derived principally from or corroborated by observable market data by correlation or other means.

If the assets or liabilities have a specified (contractual) term, the Level 2 input must be observable for substantially the full term of the assets or liabilities.

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

Accounts Receivable

Accounts receivable is comprised primarily of current amounts due under sponsorship agreements and advertising from the Association's magazine, *The Cutting Horse Chatter*, which are based on agreed-upon prices, as well as amounts due for the State of Texas incentives. The Association provides an allowance for doubtful collections, which is based upon a review of outstanding receivables, historical collection information, and existing economic conditions. Normal accounts receivable are due 30 days after the issuance of the invoice. Receivables past due more than 120 days are considered delinquent. Delinquent receivables are written off based on an individual credit evaluation and specific circumstances of the customer.

Inventories

Inventories consist primarily of DVDs and videotapes, and are valued at the lower of cost or market with cost determined using the first-in, first-out method.

Property and Equipment

Property and equipment have been recorded at acquisition cost. It is the Association's policy to capitalize property and equipment purchases over \$1,000. Lesser amounts are expensed. Maintenance, repairs, and minor replacements are charged to operations as incurred; major replacements and betterments are capitalized. The cost of assets retired and the related accumulated depreciation are removed from the accounts at the time of disposition, and any resulting gain or loss is reflected in the statements of activities and changes in net assets of the respective period.

NATIONAL CUTTING HORSE ASSOCIATION

NOTES TO FINANCIAL STATEMENTS *(continued)*

B. Summary of Significant Accounting Policies – continued

Property and Equipment – continued

Depreciation is computed using the straight-line method over the estimated useful lives of the assets, which are as follows:

Buildings and improvements	5 – 39 years
Automobiles and trailers	5 – 7 years
Office furniture and equipment	3 – 10 years

Donations of property and equipment are recorded as support at their estimated fair value at the time of receipt. Such donations are reported as unrestricted support unless the donor has restricted the asset to a specific purpose. Assets donated with explicit restrictions regarding their use and contributions of cash that must be used to acquire property and equipment are reported as restricted support. Absent donor stipulations regarding how long such donated assets must be maintained, the Association reports expirations of donor restrictions when the donated or acquired assets are placed in service as instructed by the donor. The Association reclassifies temporarily restricted net assets to unrestricted at such time.

Collections

The Association's collections are comprised of artifacts of historical significance or art objects, which have been acquired through various contributions from donors since the inception of the Association. The collections are not recognized as assets in the accompanying statements of financial position. Proceeds from the deaccessions or insurance recoveries are reflected as increases in the appropriate net asset classes.

Deferred Revenues and Deferred Membership Dues

Deferred revenue for membership dues and sponsorships represents money received in advance for future periods of activity. Deferred revenue for future shows represents entry fees received in the current period relating to future shows to be sponsored by the Association. The Association recognizes the deferred revenue upon completion of the respective show or in accordance with the terms of the sponsorship agreement. It is the Association's policy to amortize lifetime membership dues over twelve years.

Youth Scholarship Awards

The Association awards scholarships to youth participants at various cutting horse events throughout the year, which are required to be used for qualified educational expenses. The scholarships are charged to expense in the year in which the amount is awarded. The youth scholarship awards liability in the accompanying statements of financial position represents scholarships that have been awarded, but not yet disbursed to the educational institution.

NATIONAL CUTTING HORSE ASSOCIATION

NOTES TO FINANCIAL STATEMENTS (*continued*)

B. Summary of Significant Accounting Policies – continued

Advertising

Advertising costs are expensed as incurred and included as a separate line item in the accompanying statements of activities and changes in net assets.

Income Taxes

The Association is a non-profit organization as defined in Section 501(c)(5) of the Internal Revenue Code and, accordingly, does not provide for federal income taxes.

Advertising revenue generated from *The Cutting Horse Chatter* is considered unrelated business income and is reported as such for tax-reporting purposes. During 2013 and 2012, net taxable unrelated business income was not significant and therefore, no provision for income taxes was recorded in the accompanying financial statements. The Association has net operating loss carryforwards of approximately \$83,000 that were generated in years prior to 2013 as a result of unrelated business income and expense activity. Such loss carryforwards will expire in years 2014 through 2029, if not utilized.

FASB ASC Topic No. 740, *Income Taxes*, prescribes a comprehensive model for the financial statement recognition, measurement, presentation and disclosure of uncertain tax positions taken or expected to be taken in income tax returns. Management of the Association believes that it has not taken a tax position that, if challenged, would have a material effect on the financial statements. The Association files Forms 990 and 990-T in the federal jurisdiction within the United States. At December 31, 2013, the Association's tax returns related to the years ended December 31, 2010 through December 31, 2012 remain open to possible examination by tax authorities. No tax returns are currently under examination by any tax authorities. The Association has not incurred any penalties or interest under FASB ASC Topic No. 740.

Donated Services

Donated services are recognized as contributions if the services, (a) create or enhance non-financial assets, or (b) require specialized skills, and are performed by people with those skills, and would otherwise be purchased by the Association. The Association pays for most services requiring specialized skills. However, a number of individuals volunteer their time and perform a variety of tasks that assist the Association with specific program functions and various other activities that are not recognized as contributions in the accompanying financial statements, because the recognition criteria under GAAP was not met.

Reclassification

Certain prior year amounts have been reclassified to conform to the current year presentation.

NATIONAL CUTTING HORSE ASSOCIATION
NOTES TO FINANCIAL STATEMENTS (continued)

C. Cash and Cash Equivalents

At December 31, cash and cash equivalents consisted of the following:

	<u>2013</u>	<u>2012</u>
Cash	\$ 213,204	\$ 404,109
Cash equivalents	<u>2,065,153</u>	<u>239,049</u>
Total cash and cash equivalents	<u>\$ 2,278,357</u>	<u>\$ 643,158</u>

At December 31, 2013 and 2012, cash equivalents were held by the Association's third party investment advisor and were invested in short-term bond funds.

D. Investments

The cost and market value of investments held at December 31, are as follows:

	<u>2013</u>		<u>2012</u>	
	<u>Cost</u>	<u>Market Value</u>	<u>Cost</u>	<u>Market Value</u>
Certificates of deposit	\$ 3,827	\$ 3,827	\$ 3,826	\$ 3,826
Corporate bonds	3,103,750	3,031,472	4,387,775	4,382,716
Foreign bonds	396,662	392,889	-	-
Municipal bonds	<u>629,300</u>	<u>625,455</u>	<u>629,300</u>	<u>645,801</u>
Total investments	<u>\$ 4,133,539</u>	<u>\$ 4,053,643</u>	<u>\$ 5,020,901</u>	<u>\$ 5,032,343</u>

The market value of the Association's investments was based on Level 2 inputs, as defined by FASB ASC Topic No. 820, which represent quoted prices for identical or similar assets or liabilities in inactive markets.

During the years ended December 31, net investment income, including realized and unrealized gains and losses, consisted of the following:

	<u>2013</u>	<u>2012</u>
Interest and dividends	\$ 156,155	\$ 191,770
Net realized losses	(26,407)	(10,672)
Net unrealized losses	(91,338)	(50,713)
Investment management fees	<u>(26,590)</u>	<u>(30,372)</u>
Net investment income, including realized and unrealized gains and losses	<u>\$ 11,820</u>	<u>\$ 100,013</u>

NATIONAL CUTTING HORSE ASSOCIATION
NOTES TO FINANCIAL STATEMENTS (continued)

E. Property and Equipment

At December 31, property and equipment consisted of the following:

	<u>2013</u>	<u>2012</u>
Land	\$ 139,788	\$ 139,788
Buildings and improvements	2,292,749	2,292,749
Automobiles and trailers	48,488	71,011
Office furniture and equipment	866,433	867,713
Total property and equipment	<u>3,347,458</u>	<u>3,371,261</u>
Less accumulated depreciation	<u>1,422,795</u>	<u>1,417,692</u>
Property and equipment, net	<u><u>\$ 1,924,663</u></u>	<u><u>\$ 1,953,569</u></u>

F. Collections

The Association's collections are held for public exhibition, education, or research and the Association has a collections management policy which includes guidance on the preservation, care, and maintenance of the collections and procedures relating to the accession/deaccession of collection items.

No value is assigned to the collections in the accompanying financial statements. Proceeds from deaccessions or insurance recoveries for lost or destroyed collection items are recognized as increases in the appropriate net asset class and are designated for future collection acquisitions.

G. Deferred Membership Dues

The Association amortizes lifetime member dues over a twelve-year period. Non-pro dues, first-class postage dues, and trainer fee dues represent money received in advance for future periods of activity. Deferred membership dues, at December 31, were composed of the following:

	<u>2013</u>	<u>2012</u>
Membership dues	\$ 549,830	\$ 569,512
Non-pro dues	217,635	129,275
First-class postage dues	7,380	6,245
Trainer fee dues	4,955	5,170
Total deferred membership dues	<u><u>\$ 779,800</u></u>	<u><u>\$ 710,202</u></u>

NATIONAL CUTTING HORSE ASSOCIATION

NOTES TO FINANCIAL STATEMENTS (continued)

H. Unrestricted Net Assets – Board Designated for Youth Funds

As of December 31, 2013 and 2012, approximately \$272,000 and \$353,000 of net assets were designated by the Board of Directors of the Association for youth funds. Youth funds include excess revenues earned on youth activities that have been designated for future youth events. The liability for youth scholarship awards represents scholarships awarded that will be paid when the awardees enroll in college. If an awardee reaches age 26 and has not utilized the full amounts of the scholarship, the unused amounts are returned to the amount designated for youth funds.

I. Temporarily Restricted Net Assets – State of Texas Incentives

Based on approved applications, the State of Texas provides incentives to the City of Fort Worth for Association events held in the Fort Worth area. The City of Fort Worth, in turn, provides incentives to the Association that are restricted for the purpose of enhancing Association shows that qualify for the state incentives. Funds awarded for current Triple Crown events are restricted for use in qualifying shows. The temporarily restricted amounts were held in investments at December 31, 2013 and 2012. The following represents the incentives awarded by the State of Texas and how the incentives were used as approved by the Executive Committee for the years ended December 31:

	2013	2012
Beginning Balance at January 1,	\$ 2,221,560	\$ 1,044,411
Super Stakes:		
State of Texas incentive contribution	895,010	982,779
Net assets released from restrictions:		
Purse	(825,000)	(750,000)
Cattle allowance	(58,086)	(62,874)
Event marketing	(12,496)	(25,955)
Derby (Summer Spectacular):		
State of Texas incentive contribution	725,318	1,158,481
Net assets released from restrictions:		
Purse	(800,000)	(850,000)
Cattle allowance	(54,474)	(50,063)
Event marketing	(21,821)	(15,741)
Futurity:		
State of Texas incentive contribution	1,229,457	2,160,120
Net assets released from restrictions:		
Purse	(1,384,500)	(1,000,000)
Cattle allowance	(57,708)	(53,874)
World finals	(168,500)	(168,500)
Event marketing	(182,051)	(147,224)
Ending balance at December 31,	\$ 1,506,709	\$ 2,221,560

NATIONAL CUTTING HORSE ASSOCIATION

NOTES TO FINANCIAL STATEMENTS (continued)

J. Professional Fees

Professional fees, for the years ended December 31, were composed of the following:

	<u>2013</u>	<u>2012</u>
Actuarial services	\$ 62,710	\$ 46,571
Attorneys	261,781	424,446
Auditing, tax, and ballot counting services	57,564	48,071
Consulting - economic impact and review	52,010	54,900
Consulting – legislative	80,885	68,500
Consulting – marketing	28,877	67,562
Consulting – information technology	49,905	-
Consulting – other	3,270	29,115
Total professional fees	<u>\$ 597,002</u>	<u>\$ 739,165</u>

K. Other Income and Expenses

Other income and other expenses, for the years ended December 31, were composed of the following:

	<u>2013</u>	<u>2012</u>
Other show income:		
Show transfer fees	\$ 19,250	\$ 9,300
Scoreboard advertising	75	5,250
Convention tours	-	2,845
Total other show income	<u>\$ 19,325</u>	<u>\$ 17,395</u>
Other department income:		
Royalties and affinity programs	\$ 182,970	\$ 181,892
Judges - seminars and fees	18,605	44,860
Electronic advertising and NCHA blog	17,910	19,365
Donations and other miscellaneous income	27,285	63,927
Fines and protests	32,900	42,450
Convention registration	18,255	15,060
Horse records	12,281	11,273
Total other department income	<u>\$ 310,206</u>	<u>\$ 378,827</u>

NATIONAL CUTTING HORSE ASSOCIATION

NOTES TO FINANCIAL STATEMENTS (continued)

K. Other Income and Expenses – continued

	2013	2012
Other show expenses:		
Exhibit hall and show office supplies	\$ 160,361	\$ 131,734
Hospitality	27,653	24,004
Show postage, printing, and tickets	13,281	16,370
Show promotions	77,451	96,766
Show sponsor cost	24,460	7,713
Parties expenses	74,361	59,630
Veterinarian expenses and drug testing	106,914	87,442
	<u>\$ 484,481</u>	<u>\$ 423,659</u>
Other department expenses:		
Bad debts	\$ 12,032	\$ 11,976
Bank fees and charges	19,646	21,232
Committee expenses	66,827	79,650
Contract labor	212,136	186,437
Convention expenses	77,046	90,121
Credit card fees	173,913	166,057
Dues, fees, and subscriptions	27,910	21,631
Feature stories	21,727	15,905
Investment management fees	26,590	30,372
Miscellaneous expenses	2,782	14,018
Office supplies	52,191	49,446
Repairs and maintenance	17,249	9,817
Scholarships	87,816	81,574
Travel	115,379	134,065
Utilities	92,995	88,982
Vehicle allowance	21,344	20,631
	<u>\$ 1,027,583</u>	<u>\$ 1,021,914</u>

L. Benefit Plans

The Association sponsors a defined benefit pension plan (the “Pension Plan”) covering all of its full-time employees hired prior to October 31, 2003. Pension benefits are based upon years of service and average compensation. The Association’s funding policy is to make annual contributions sufficient to meet at least the minimum funding standards of the Employee Retirement Income Security Act of 1974. In 2003, the Association froze the Pension Plan. As a result, effective January 31, 2004, additional service and pay increases (other than employees with at least 10 years of service as of that date) are not recognized for benefit determination for the Pension Plan. No new entrants are allowed to join the Plan and generally, no new benefits are being earned.

NATIONAL CUTTING HORSE ASSOCIATION

NOTES TO FINANCIAL STATEMENTS (continued)

L. Benefit Plans – continued

During 2010, the Executive Committee approved a plan to truncate the Pension Plan over a five-year period beginning in 2010. During 2013, the Executive Committee approved a plan to begin terminating the Pension Plan with a target termination date in 2014. The Association made contributions to the Pension Plan of \$285,000 during 2013. During 2014, the Association expects to contribute approximately \$205,000 to the Pension Plan.

The Pension Plan’s funded status and other pertinent information related to the Pension Plan is set forth in the following table:

	<u>2013</u>	<u>2012</u>
Projected benefit obligation at December 31	\$ 2,306,413	\$ 2,364,305
Fair value of plan assets at December 31	<u>2,091,224</u>	<u>2,019,239</u>
Funded status	<u>\$ (215,189)</u>	<u>\$ (345,066)</u>
Prepaid benefit costs recognized in the statements of financial position	<u>\$ 895,148</u>	<u>\$ 793,922</u>
Accumulated benefit obligation (all vested)	<u>\$ 2,306,413</u>	<u>\$ 2,334,128</u>
Net periodic pension costs, including settlement loss	\$ 183,774	\$ 183,298
Employer contributions	285,000	365,000
Benefits paid	431,241	209,346
Weighted-average assumptions as of December 31:		
Discount rate	4.00%	4.00%
Expected return on plan assets	8.00%	8.00%
Rate of compensation increase	0.00%	4.00%

The overall expected long-term rate of return on assets assumption is based on historical returns for the Pension Plan and expected future long-term rate of returns based on the Pension Plan’s investment policy.

NATIONAL CUTTING HORSE ASSOCIATION

NOTES TO FINANCIAL STATEMENTS (continued)

L. Benefit Plans – continued

As discussed above, the Pension Plan is in the process of termination; therefore, benefits expected to be paid by the Pension Plan during 2014 total \$2,311,126. Additionally, as a result of the termination of the Pension Plan, a settlement loss of \$163,435 was recognized during 2013 in the accompanying statements of activities and changes in net assets.

The investment policy of the Pension Plan was to maximize long-term investment returns while assuring an acceptable level of risk. In order to satisfy this investment policy, the target weighted average ranges of percentages for each major category of the Pension Plan assets were 40-60% equity securities, 20-30% debt securities, and 10-20% cash and cash equivalents. Investment decisions are made with the understanding of how each asset class will promote optimal expected return and volatility characteristics of the portfolio given the obligations and time horizon of the Pension Plan's liabilities.

The Pension Plan's assets as of December 31, 2013, were invested 100% in cash and cash equivalents for liquidity purposes based on the termination of the Pension Plan. As of December 31, 2012, the Pension Plan's assets were invested 59% in equity securities, 4% in debt securities, 23% in mutual funds and 14% in cash and cash equivalents. At December 31, 2013 and 2012, the Pension Plan's investments were valued at fair value based on Level 1 inputs, as defined by FASB ASC Topic No. 820.

The Association also sponsors a defined contribution salary deferral plan (the "Deferred Plan") covering substantially all employees. Employees can make voluntary contributions. The Association matches 50% of employee contributions up to 3% of the employee's eligible compensation, as defined in the Deferred Plan documents. The Association at its discretion may also contribute an additional amount, as it deems necessary. During the years ended December 31, 2013 and 2012, the Association made matching contributions of approximately \$40,000 and \$39,000, respectively. The Association made no discretionary contributions to the Deferred Plan during 2013 and 2012.

Retirement expenses in the accompanying statements of activities and changes in net assets, for the years ended December 31, were comprised of the following:

	<u>2013</u>	<u>2012</u>
Pension Plan net periodic pension costs	\$ 20,339	\$ 183,298
Deferred Plan matching contributions	39,933	39,290
Pension Benefit Guaranty Corporation payments and fees	<u>3,565</u>	<u>5,023</u>
Total retirement expenses	<u>\$ 63,837</u>	<u>\$ 227,611</u>

NATIONAL CUTTING HORSE ASSOCIATION

NOTES TO FINANCIAL STATEMENTS (continued)

M. Stallion/ Foal Fees

In 2011, a new Stallion/ Foal fees incentive program replaced the previous Stallion Subscription program for the Super Stakes. Stallions are now required to subscribe the year before the breeding season, which is six years prior to the first Super Stakes that the resulting foals would be eligible to compete. The Stallion fee is \$2,500 (not including the \$100 insurance charge). The funds are held as deferred revenue and will be disbursed into the first show of eligibility for the resulting foals of each crop. Foals are also required to be nominated in the new program in order to compete in the Super Stakes. Foal nomination money is also held as deferred revenue and is also disbursed into the first year of eligibility for those foals at age 4. The foal nomination fee chart is below:

Foaling year (by deadline)	\$	200
Weanling year (by deadline)		1,250
2 year old (by deadline)		7,500
3 year old and up		10,000

During the interim three years between the close of the old program in 2011 and the initial foal disbursements in 2015, \$500,000 per year (for a total of \$1,500,000 over the three years) will be advanced to the Super Stakes from general fund to maintain added money in the show. Those funds will be reimbursed from the program to the general fund over a period of six years (\$250,000 per year), beginning in 2017 when the initial Stallion Fee funds are disbursed. No portion of the Foal Fee funds will be used to reimburse the general fund for any advances.

The following table shows the detail of the funds as of December 31, 2013 and 2012:

	<u>2013</u>	<u>2012</u>
Stallion fees collected for the 2017 Super Stakes	\$ 472,000	\$ 451,000
Stallion fees collected for the 2018 Super Stakes	463,000	430,000
Stallion fees collected for the 2019 Super Stakes	428,500	-
Total stallion fees collected	1,363,500	881,000
Advances to be repaid at each year-end	(1,000,000)	(500,000)
Net stallion fees	363,500	381,000
Foal fees collected for the 2015 Super Stakes	568,050	553,050
Foal fees collected for the 2016 Super Stakes	539,100	180,300
Foal fees collected for the 2017 Super Stakes	98,600	-
Total foal fees collected	1,205,750	733,350
Deferred revenue for stallion/ foal fees	<u>\$ 1,569,250</u>	<u>\$ 1,114,350</u>
Advances to the Super Stakes:		
Advance to the 2012 show	\$ 500,000	
Advance to the 2013 show	500,000	
To be advanced to the 2014 show	<u>500,000</u>	
Total advances to the Super Stakes	<u>\$ 1,500,000</u>	

NATIONAL CUTTING HORSE ASSOCIATION

NOTES TO FINANCIAL STATEMENTS (continued)

N. Project, Promotional and Public Relations

Project, promotional and public relations expense, for the years ended December 31, were composed of the following:

	<u>2013</u>	<u>2012</u>
Affiliate software	\$ 68,250	\$ 66,450
Bus tours	888	2,211
Celebrity cutting	994	3,616
Daily chatter	25,729	24,505
Cutting academy clinics	21,447	28,025
NCHA blog	20,610	23,071
Other projects	2,879	23,996
Promotions	82,690	103,840
Public relations	17,050	17,892
Sponsor cutting	17,150	10,793
Television – Futurity	130,077	40,000
Triple crown promotion	212,722	188,919
World series of cutting	265,917	296,943
Youth projects	12,128	16,719
	<u> </u>	<u> </u>
Total project, promotional and public relations expense	<u>\$ 878,531</u>	<u>\$ 846,980</u>

O. Concentrations

Entry fees, purse sponsorships, and other monies collected in advance of future shows are invested in money market accounts, certificates of deposit, and various fixed income securities, which consist of liquid assets in various financial institutions.

At December 31, 2013, approximately 63% of the Association's accounts receivable was comprised of outstanding amounts due from the State of Texas. Approximately 86% of the Association's accounts receivable at December 31, 2012 was comprised of outstanding amounts due from the State of Texas. All receivables are unsecured and are not pledged as collateral or limited in use.

P. Fund-Raising Events

The Association holds annual fund-raising events for the youth department and reports the revenue generated, net of any direct operating costs, as revenues in the accompanying statements of activities and changes in net assets which approximated \$111,000 and \$132,000 during 2013 and 2012, respectively. There were no direct costs relating to fund-raising events in 2013 or 2012.

NATIONAL CUTTING HORSE ASSOCIATION

NOTES TO FINANCIAL STATEMENTS (*continued*)

Q. Unrestricted Non-Operating Activities

During 2013, the Association incurred expenses relating to the search for the new executive director and an information technology project for developing in-house software which approximated \$90,000 and \$94,000, respectively. During 2012, the Association incurred expenses relating to employee severance and litigation settlement which approximated \$187,000 and \$93,000, respectively. These expenses have been recorded as unrestricted non-operating activities as these activities do not fall with the Association's normal operations as discussed in Note A.

R. Related Party Transactions

NCHA Charities Foundation (the "Foundation") was established to award scholarships and financial aid to eligible members of the Association. The purpose of this entity is separate from that of the Association, but it is also dependent in that only members of the Association may benefit from the Foundation. The Association disburses money specifically donated by its members to the Foundation. During 2013 and 2012, the Association disbursed approximately \$61,000 and \$51,000, respectively, to the Foundation. At December 31, 2013 and 2012, the Association had a receivable of approximately \$7,000 and \$8,000, respectively, due from the Foundation relating to reimbursement of costs. In addition, the Association's accounting department performs accounting functions for the Foundation at no cost.

The Association donated advertising in *The Cutting Horse Chatter* to the Foundation valued at approximately \$28,000 and \$23,000 for the years ended December 31, 2013 and 2012, respectively.

The Association receives a percentage of gross entry fees from national affiliates from their cutting horse contests. During the years ended December 31, 2013 and 2012, the Association received entry fees of approximately \$1,461,000 and \$1,339,000, respectively, from these affiliates.

Fees received from affiliates for use of the Association's show production software during 2013 and 2012 was approximately \$45,000 and \$50,000, respectively. Supplemental show software costs were reimbursed to affiliates meeting the requirements for partial reimbursement. During 2013 and 2012, show software costs of approximately \$68,000 and \$66,000, respectively, were reimbursed to affiliates.

S. Commitments and Contingencies

From time to time, the Association is involved in various lawsuits and claims arising in the normal course of business. In management's opinion, the ultimate outcome of these items will not have a material adverse effect on the Association's financial position or results of operations.

The Association guarantees all entry fees paid by contestants to show management (affiliates) representing cutting horse contests. During 2013 and 2012, the contestants must be members of the Association in good standing and the show must remit 8% of all entry fees to the Association. As of December 31, 2013 and 2012, approximately \$7,000 and \$5,000, respectively, was still receivable from the contestants. In the opinion of management, the amount of ultimate liability with respect to these entry fees will not materially affect the financial position or operations of the Association.

NATIONAL CUTTING HORSE ASSOCIATION

NOTES TO FINANCIAL STATEMENTS *(continued)*

S. Commitments and Contingencies – continued

The Association leases certain office equipment, with annual rental payments of approximately \$5,000, under a five-year, non-cancelable operating lease which matures in March 2018. Annual rental expense under this lease approximated \$5,000 for each of the years ended December 31, 2013 and 2012. Minimum annual lease payments approximate \$5,000 for 2014 through 2017 and \$1,000 for 2018.

The Association leases facilities from the City of Fort Worth under a five-year operating lease, which initially matured in May 2011, for the purpose of holding the Super Stakes, Summer Spectacular, World Championship Futurity, and World Finals events each year. On January 1 of each year beginning in 2008, one additional year will be automatically added to the end of the initial five-year term of this lease agreement unless written notice is given by either party prior to January 1. At December 31, 2013, the Association is obligated to continue under this lease until May 2016. The amount paid during 2013 and 2012 for the facilities rental under the lease was approximately \$385,000 and \$304,000, respectively. Minimum rentals, on an annual basis, are approximately \$304,000 for 2014 through 2016.

Prior to 2011, the Association entered into a three-year operating lease for the rental of facilities in Jackson, Mississippi for the annual Eastern National Championships event which matured in March of 2012. The Association entered into an extension agreement for the 2013 event. The amounts paid during 2013 and 2012 for the facilities rental was \$40,000 each year. As of December 31, 2013, this lease had not been renewed.

On June 27, 2006, the Association entered an agreement with the American Quarter Horse Association (the "AQHA"), a non-profit corporation, to undertake the development of software to capture data and create reports which will contain Association performance records, data and information incorporated with AQHA's pedigree records. Revenues from the sale of the reports and costs of software development will be shared equally by the two organizations. The agreement shall be in effect for a period of five years. The agreement limits the Association's share of costs of development to \$75,000 and such costs were incurred in 2006. The Association's share of revenue from the sale of reports will be retained by the AQHA until the revenues exceed the Association's share of costs incurred. No revenue from the sale of reports has been generated to date through December 31, 2013.

T. Subsequent Events

In preparing the accompanying financial statements, management has evaluated all subsequent events and transactions for potential recognition or disclosure through June 12, 2014, the date the financial statements were available for issuance.