

**NATIONAL CUTTING
HORSE ASSOCIATION**

FINANCIAL STATEMENTS

**Years Ended December 31, 2012 and 2011
with Report of Independent Auditors**

**NATIONAL CUTTING
HORSE ASSOCIATION**

FINANCIAL STATEMENTS

Years Ended December 31, 2012 and 2011

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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, 2012 and 2011, 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, 2012 and 2011, 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.

Emphasis of Matter

As discussed in Note C of the notes to the financial statements, in 2012 management discovered an error in the calculation of the State of Texas incentive contribution for 2008. Accordingly, the 2011 financial statements have been restated to correct for this error.

Whitley Penn LLP

Fort Worth, Texas
June 17, 2013

NATIONAL CUTTING HORSE ASSOCIATION

STATEMENTS OF FINANCIAL POSITION

	December 31,	2011
	2012	(As Restated)
Assets		
Cash and cash equivalents (Note D)	\$ 643,158	\$ 2,128,810
Accounts receivable, net of allowance for doubtful accounts of \$16,588 and \$18,239, respectively	716,388	843,391
Accounts receivable - State of Texas incentives	4,301,380	1,417,020
Accrued interest receivable	52,067	47,266
Investments (Note E)	5,032,343	4,389,377
Inventories	5,666	3,716
Prepaid expenses and other assets	213,607	293,597
Property and equipment, net (Note F)	1,953,569	2,089,069
Collections (Note G)	-	-
Total assets	<u>\$12,918,178</u>	<u>\$11,212,246</u>
Liabilities and Net Assets		
Liabilities:		
Accounts payable	\$ 1,170,525	\$ 979,845
Accounts payable - State of Texas incentives	361,959	361,959
Other accrued liabilities	119,381	139,688
Deferred revenue for future shows	2,080,089	1,153,209
Deferred membership dues (Note H)	710,202	707,750
Deferred revenue, other	82,548	109,695
Youth scholarship awards (Note I)	670,733	570,902
Liability for pension obligation (Note M)	345,066	763,161
Total liabilities	<u>5,540,503</u>	<u>4,786,209</u>
Commitments and contingencies		
Net assets:		
Unrestricted:		
Undesignated	4,803,422	5,020,956
Board designated for youth funds (Note I)	352,693	360,670
Total unrestricted	<u>5,156,115</u>	<u>5,381,626</u>
Temporarily restricted - State of Texas incentives (Note J)	2,221,560	1,044,411
Total net assets	<u>7,377,675</u>	<u>6,426,037</u>
Total liabilities and net assets	<u>\$12,918,178</u>	<u>\$11,212,246</u>

See accompanying notes to financial statements.

NATIONAL CUTTING HORSE ASSOCIATION

STATEMENTS OF ACTIVITIES AND CHANGES IN NET ASSETS

	Year Ended December 31,	2012	2011
Unrestricted Net Assets			
Operating revenues and support:			
Show revenues and support:			
Entry fees	\$ 6,436,272	6,245,859	
Show fees	3,766,486	3,590,918	
Stall rentals and practice pen	1,406,990	1,404,814	
Purse sponsors	319,268	379,653	
Stallion subscription fees	500,000	525,041	
Booth exhibit rental	439,134	432,982	
Tickets	429,040	442,966	
Sponsorships	553,183	531,413	
Affiliate income	246,300	253,244	
Event facility allowances	382,527	370,985	
Other show income (Note L)	17,395	13,450	
Total show revenues and support	14,496,595	14,191,325	
Department revenues and support:			
Advertising	1,594,887	1,719,621	
Sponsorships	1,412,865	1,468,678	
Affiliate income	1,142,316	940,943	
Membership dues and fees	888,608	791,530	
Horse sales	592,286	561,788	
Fund-raising events (Note O)	327,198	293,158	
Other department income (Note L)	378,827	426,015	
Total department revenues and support	6,336,987	6,201,733	
Net assets released from restrictions-			
State of Texas incentives (Note J)	3,124,231	1,821,942	
Total unrestricted operating revenues and support	23,957,813	22,215,000	
Operating expenses:			
Show expenses:			
Premiums, including sire awards, and NCHA Day	8,037,727	7,831,223	
Premiums from State of Texas incentives	2,718,500	1,463,417	
Cattle	1,941,147	1,878,920	
Judges, contract labor and show staff, soundmen, security, and paramedics	808,955	815,435	
Awards	975,348	798,249	
Equipment and facilities rent	779,881	716,686	
Coliseum preparation	351,153	351,326	
Stall rentals and practice pen expenses	191,988	219,893	
Advertising	124,034	109,152	
Other show expenses (Note L)	423,659	353,485	
Total show expenses	16,352,392	14,537,786	

See accompanying notes to financial statements.

NATIONAL CUTTING HORSE ASSOCIATION

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

	Year Ended December 31,	
	2012	2011
Operating expenses - continued:		
Department expenses:		
Salaries and benefits	\$ 2,069,774	\$ 1,979,198
Retirement expenses (Note M)	227,611	140,493
Affiliate Challenge and NCHA Weekend	77,938	735
Awards	377,402	371,523
Printing	454,190	441,265
Equipment and facilities rent	127,495	109,072
Monitor fees and expenses	152,046	155,169
Sponsor advertisements (non-cash)	611,567	663,924
Project, promotional, and public relations	846,980	957,638
Advertising	261,422	202,738
Postage	226,307	212,912
Insurance	370,804	373,367
Payroll and ad valorem taxes	199,877	194,386
Professional fees (Note K)	739,165	605,313
Depreciation	153,716	159,305
Other department expenses (Note L)	1,021,914	812,922
Total department expenses	7,918,208	7,379,960
Total unrestricted operating expenses	24,270,600	21,917,746
Operating revenues net of operating expenses	(312,787)	297,254
Other unrestricted income:		
Interest and dividend income	191,770	184,066
Realized investment gains (losses)	(10,672)	122,148
Gains on disposals of property and equipment	-	300
Total other unrestricted income	181,098	306,514
Change in unrestricted net assets from operations	(131,689)	603,768
Other unrestricted non-operating activities:		
Unrealized losses in market value of investments	(50,713)	(126,345)
Pension Plan changes other than net periodic pension cost	236,393	(266,633)
Employee severance expense	(186,795)	-
Litigation settlement expense	(92,707)	-
Total other unrestricted non-operating activities	(93,822)	(392,978)
Net increase (decrease) in unrestricted net assets	(225,511)	210,790
Temporarily Restricted Net Assets		
Restricted contributions-State of Texas incentives (Note J)	4,301,380	2,069,478
Net assets released from restrictions-State of Texas incentives (Note J)	(3,124,231)	(1,821,942)
Net increase in temporarily restricted net assets	1,177,149	247,536
Net increase in net assets	951,638	458,326
Net assets at beginning of year (As Restated)	6,426,037	5,967,711
Net assets at end of year	\$ 7,377,675	\$ 6,426,037

See accompanying notes to financial statements.

NATIONAL CUTTING HORSE ASSOCIATION

STATEMENTS OF CASH FLOWS

	Year Ended December 31,	2012	2011
Operating Activities			
Net increase in net assets	\$	951,638	\$ 458,326
Adjustments to reconcile net increase in net assets to net cash used in operating activities:			
Depreciation		153,716	159,305
Provision for bad debts		11,976	12,204
Gains on disposals of property and equipment		-	(300)
Net realized and unrealized losses on investments		61,385	4,197
Restricted contributions		(4,301,380)	(2,069,478)
Effect of defined benefit pension plan changes		(236,393)	266,633
Changes in operating assets and liabilities:			
Accounts receivable		115,027	(47,928)
Accounts receivable - State of Texas incentives		(2,884,360)	(759,720)
Accrued interest receivable		(4,801)	25,512
Inventories		(1,950)	3,662
Prepaid expenses and other assets		79,990	(122,383)
Accounts payable and other accrued liabilities		170,373	155,174
Deferred revenue for future shows		926,880	81,162
Deferred membership dues		2,452	85,824
Deferred revenue, other		(27,147)	18,403
Youth scholarship awards		99,831	46,377
Liability for pension obligation		(181,702)	(300,029)
Net cash used in operating activities		(5,064,465)	(1,983,059)
Investing Activities			
Proceeds from sales of investments		1,764,694	1,817,236
Purchases of investments		(2,469,045)	-
Proceeds from sales of property and equipment		-	300
Purchases of property and equipment		(18,216)	(45,596)
Net cash provided by (used in) investing activities		(722,567)	1,771,940
Financing Activities			
Restricted contributions-State of Texas incentives		4,301,380	2,069,478
Net cash provided by financing activities		4,301,380	2,069,478
Net increase (decrease) in cash and cash equivalents		(1,485,652)	1,858,359
Cash and cash equivalents at beginning of year		2,128,810	270,451
Cash and cash equivalents at end of year	\$	643,158	\$ 2,128,810

See accompanying notes to financial statements.

NATIONAL CUTTING HORSE ASSOCIATION

NOTES TO FINANCIAL STATEMENTS

December 31, 2012 and 2011

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.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States 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 and three year memberships over three 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 2012 and 2011, 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 \$86,000 that were generated in years prior to 2012 as a result of unrelated business income and expense activity. Such loss carryforwards will expire in years 2013 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, 2012, the Association's tax returns related to the years ended December 31, 2009 through December 31, 2011 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 accounting principles generally accepted in the United States of America were not met.

NATIONAL CUTTING HORSE ASSOCIATION

NOTES TO FINANCIAL STATEMENTS (continued)

C. Restatement

The accompanying statement of financial position at December 31, 2011 and statement of activities and changes in net assets for the year ended December 31, 2011 have been restated to reflect the correction of the State of Texas incentive contribution for 2008. In 2012, management discovered the economic impact study application submitted to the State of Texas in 2008 contained inaccurate information and therefore, the Association received additional funding of approximately \$362,000 to which it was not entitled. The Association will repay this amount in 2013; therefore, Accounts Payable - State of Texas incentives has been recorded in the accompanying statement of financial position. The effects of the restatement are summarized as follows on the statement of financial position as of December 31, 2011:

	As Previously Reported	Adjustment	Restated Balance
Accounts payable - State of Texas incentives	\$ -	\$ 361,959	\$ 361,959
Total liabilities	4,424,250	361,959	4,786,209
Temporarily restricted - State of Texas incentives	1,406,370	(361,959)	1,044,411
Total net assets	6,787,996	(361,959)	6,426,037

The effects of the restatement are summarized as follows on the statement of activities and changes in net assets for the year ended December 31, 2011:

	As Previously Reported	Adjustment	Restated Balance
Total net assets at beginning of year	\$ 6,329,670	\$ (361,959)	\$ 5,967,711
Total net assets at end of year	6,787,996	(361,959)	6,426,037

NATIONAL CUTTING HORSE ASSOCIATION
NOTES TO FINANCIAL STATEMENTS (continued)

D. Cash and Cash Equivalents

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

	<u>2012</u>	<u>2011</u>
Cash	\$ 404,109	\$ 653,744
Cash equivalents	239,049	1,475,066
Total cash and cash equivalents	<u>\$ 643,158</u>	<u>\$ 2,128,810</u>

At December 31, 2012 and 2011, cash equivalents were held by the Association's third party investment advisor.

E. Investments

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

	<u>2012</u>		<u>2011</u>	
	<u>Cost</u>	<u>Market Value</u>	<u>Cost</u>	<u>Market Value</u>
Certificates of deposit	\$ 3,826	\$ 3,826	\$ 3,820	\$ 3,820
Corporate bonds	4,387,775	4,382,716	3,177,463	3,212,739
Foreign bonds	-	-	514,160	517,270
Municipal bonds – tax exempt	-	-	317,295	334,374
Municipal bonds - taxable	629,300	645,801	314,484	321,174
Total investments	<u>\$ 5,020,901</u>	<u>\$ 5,032,343</u>	<u>\$ 4,327,222</u>	<u>\$ 4,389,377</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>2012</u>	<u>2011</u>
Interest and dividends	\$ 191,770	\$ 184,066
Net realized losses	(10,672)	122,148
Net unrealized losses	(50,713)	(126,345)
Investment management fees	(30,372)	(29,576)
Net investment income, including realized and unrealized gains and losses	<u>\$ 100,013</u>	<u>\$ 150,293</u>

NATIONAL CUTTING HORSE ASSOCIATION

NOTES TO FINANCIAL STATEMENTS (continued)

F. Property and Equipment

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

	<u>2012</u>	<u>2011</u>
Land	\$ 139,788	\$ 139,788
Buildings and improvements	2,292,749	2,292,749
Automobiles and trailers	71,011	71,011
Office furniture and equipment	867,713	974,147
Total property and equipment	<u>3,371,261</u>	<u>3,477,695</u>
Less accumulated depreciation	<u>1,417,692</u>	<u>1,388,626</u>
Property and equipment, net	<u>\$ 1,953,569</u>	<u>\$ 2,089,069</u>

G. 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.

H. Deferred Membership Dues

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

	<u>2012</u>	<u>2011</u>
Membership dues	\$ 569,512	\$ 631,619
Non-pro dues	129,275	61,464
First-class postage dues	6,245	8,201
Trainer fee dues	5,170	5,130
Supplement dues	-	1,336
Total deferred membership dues	<u>\$ 710,202</u>	<u>\$ 707,750</u>

NATIONAL CUTTING HORSE ASSOCIATION

NOTES TO FINANCIAL STATEMENTS (continued)

I. Unrestricted Net Assets – Board Designated for Youth Funds

As of December 31, 2012 and 2011, approximately \$353,000 and \$361,000 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.

J. 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 bettering Association shows that qualify for the state incentives. Funds awarded in excess of amounts used in current Triple Crown events are restricted for use in future qualifying shows. As discussed in Note C, the 2011 temporarily restricted net assets were restated. The temporarily restricted amounts were held in investments at December 31, 2012 and 2011. 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:

	2012	2011
Beginning Balance at January 1,	\$ 1,044,411	(As Restated) \$ 796,875
Super Stakes:		
State of Texas incentive contribution	982,779	208,716
Net assets released from restrictions:		
Purse	(750,000)	(480,917)
Cattle allowance	(62,874)	(55,678)
Event marketing	(25,955)	-
Derby (Summer Spectacular):		
State of Texas incentive contribution	1,158,481	443,742
Net assets released from restrictions:		
Purse	(850,000)	(482,500)
Cattle allowance	(50,063)	(51,240)
Event marketing	(15,741)	-
Futurity:		
State of Texas incentive contribution	2,160,120	1,417,020
Net assets released from restrictions:		
Purse	(1,000,000)	(500,000)
Cattle allowance	(53,874)	(55,145)
World finals	(168,500)	-
Event marketing	(147,224)	-
50 th Futurity promotion	-	(196,462)
Ending balance at December 31,	\$ 2,221,560	\$ 1,044,411

NATIONAL CUTTING HORSE ASSOCIATION

NOTES TO FINANCIAL STATEMENTS (continued)

K. Professional Fees

For the years ended December 31, professional fees were composed of the following:

	<u>2012</u>	<u>2011</u>
Actuarial services	\$ 46,571	\$ 28,141
Attorneys	424,446	379,255
Auditing, tax, and ballot counting services	48,071	53,239
Consulting - economic impact and review	54,900	23,250
Consulting – legislative	68,500	56,991
Consulting – marketing	67,562	61,401
Consulting – other	29,115	3,036
Total professional fees	<u>\$ 739,165</u>	<u>\$ 605,313</u>

L. Other Income and Expenses

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

	<u>2012</u>	<u>2011</u>
Other show income:		
Show transfer fees	\$ 9,300	\$ 9,700
Scoreboard advertising	5,250	3,750
Convention tours	2,845	-
Total other show income	<u>\$ 17,395</u>	<u>\$ 13,450</u>
Other department income:		
Royalties and affinity programs	\$ 181,892	\$ 222,603
Judges - seminars and fees	44,860	14,493
Electronic advertising and NCHA blog	19,365	48,845
Donations and other miscellaneous income	63,927	81,861
Fines and protests	42,450	26,942
Convention registration	15,060	18,995
Horse records	11,273	12,276
Total other department income	<u>\$ 378,827</u>	<u>\$ 426,015</u>

NATIONAL CUTTING HORSE ASSOCIATION

NOTES TO FINANCIAL STATEMENTS (continued)

L. Other Income and Expenses – continued

	<u>2012</u>	<u>2011</u>
Other show expenses:		
Exhibit hall and show office supplies	\$ 131,734	\$ 110,549
Hospitality	24,004	46,164
Show postage and printing	6,118	10,537
Show promotions	96,766	85,157
Show sponsor cost	7,713	11,460
Tickets and parties expenses	69,882	60,234
Veterinarian expenses and drug testing	87,442	29,384
	<u> </u>	<u> </u>
Total other show expenses	<u>\$ 423,659</u>	<u>\$ 353,485</u>
Other department expenses:		
Bad debts	\$ 11,976	\$ 12,204
Bank fees and charges	21,232	16,680
Committee expenses	79,650	76,955
Contract labor	186,437	94,454
Convention expenses	90,121	53,136
Credit card fees	166,057	133,013
Dues, fees, and subscriptions	21,631	22,120
Feature stories	15,905	17,455
Investment management fees	30,372	29,576
Miscellaneous expenses	14,018	38,430
Office supplies	49,446	47,709
Repairs and maintenance	9,817	8,636
Scholarships	81,574	78,038
Travel	134,065	69,635
Utilities	88,982	90,751
Vehicle allowance	20,631	24,130
	<u> </u>	<u> </u>
Total other department expenses	<u>\$ 1,021,914</u>	<u>\$ 812,922</u>

M. 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)

M. Benefit Plans – continued

During 2010, the Executive Committee approved a plan to truncate the Pension Plan over a five-year period beginning in 2010. The Association made contributions to the Pension Plan of \$365,000 during 2012, which included additional contributions pursuant to this plan of approximately \$47,500. During 2013, the Association expects to contribute approximately \$282,000 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:

	2012	2011
Projected benefit obligation at December 31	\$ 2,364,305	\$ 2,436,812
Fair value of plan assets at December 31	2,019,239	1,673,651
Funded status	\$ (345,066)	\$ (763,161)
Prepaid benefit costs recognized in the statements of financial position	\$ 793,922	\$ 612,220
Accumulated benefit obligation (all vested)	\$ 2,334,128	\$ 2,397,539
Net periodic pension costs	\$ 183,298	\$ 94,971
Employer contributions	365,000	395,000
Benefits paid	209,346	37,458
Weighted-average assumptions as of December 31:		
Discount rate	4.00%	5.00%
Expected return on plan assets	8.00%	8.00%
Rate of compensation increase	4.00%	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.

	2012
Amounts not recognized as components of net periodic pension cost in the statements of financial position:	
Unrecognized actuarial loss	\$ 1,138,988

It is anticipated that \$121,475 of the unrecognized actuarial loss will be recognized as a component of net periodic pension cost in 2013.

NATIONAL CUTTING HORSE ASSOCIATION

NOTES TO FINANCIAL STATEMENTS (continued)

M. Benefit Plans – continued

Benefits expected to be paid by the Pension Plan for the next five fiscal years and the aggregate for the five fiscal years thereafter are as follows:

2013	\$ 378,000
2014	95,000
2015	44,000
2016	111,000
2017	549,000
2018 to 2022	<u>554,000</u>
Total benefits expected to be paid	<u><u>\$ 1,731,000</u></u>

The investment policy of the Pension Plan is 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 are 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, 2012, were invested 59% in equity securities, 4% in debt securities, 23% in mutual funds and 14% in cash and cash equivalents. As of December 31, 2011, the Pension Plan's assets were invested 40% in equity securities, 8% in debt securities, 30% in mutual funds and 22% in cash and cash equivalents. At December 31, 2012 and 2011, 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, 2012 and 2011, the Association made matching contributions of approximately \$39,000 and \$40,000, respectively. The Association made no discretionary contributions to the Deferred Plan during 2012 and 2011.

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>2012</u>	<u>2011</u>
Pension Plan net periodic pension costs	\$ 183,298	\$ 94,971
Deferred Plan matching contributions	39,290	40,338
Pension Benefit Guaranty Corporation payments and fees	<u>5,023</u>	<u>5,184</u>
Total retirement expenses	<u><u>\$ 227,611</u></u>	<u><u>\$ 140,493</u></u>

NATIONAL CUTTING HORSE ASSOCIATION

NOTES TO FINANCIAL STATEMENTS (*continued*)

N. Concentrations of Credit Risk

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, 2012, approximately 86% of the Association's accounts receivable was comprised of outstanding amounts due from the State of Texas. Approximately 60% and 15% of the Association's accounts receivable at December 31, 2011, was comprised of outstanding amounts due from the State of Texas and Fort Worth Chamber of Commerce, respectively, which were subsequently collected in 2012. All receivables are unsecured and are not pledged as collateral or limited in use.

O. 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 \$327,000 and \$293,000 during 2012 and 2011, respectively. There were no direct costs relating to fund-raising events in 2012 or 2011.

P. 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 2012 and 2011, the Association disbursed approximately \$51,000 and \$133,000, respectively to the Foundation. The Association also had payable of approximately \$30,000 to the Foundation at December 31, 2011; however, there was no payable to the Foundation at December 31, 2012. At December 31, 2012, the Association had a receivable of approximately \$8,000 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 \$23,000 and \$11,000 for the years ended December 31, 2012 and 2011, respectively.

The Association receives a percentage of gross entry fees from national affiliates from their cutting horse contests. During the years ended December 31, 2012 and 2011, the Association received entry fees of approximately \$1,339,000 and \$1,148,000, respectively, from these affiliates.

NATIONAL CUTTING HORSE ASSOCIATION

NOTES TO FINANCIAL STATEMENTS *(continued)*

P. Related Party Transactions – continued

Fees received from affiliates for use of the Association's show production software during 2012 and 2011 was approximately \$50,000 and \$47,000, respectively. Supplemental show software costs were reimbursed to affiliates meeting the requirements for partial reimbursement. During 2012 and 2011, show software costs of approximately \$66,000 and \$71,000, respectively, were reimbursed to affiliates.

Q. 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. The contestants must be members of the Association in good standing and the show must remit 8% of all entry fees to the Association during 2012 and 2011. As of December 31, 2012 and 2011, approximately \$5,000 and \$3,000, 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.

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, 2012 and 2011. Minimum annual lease payments approximate \$5,000 for 2013 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 and World Championship Futurity 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, 2012, the Association is obligated to continue under this lease until May 2015. The amount paid during 2012 and 2011 for the facilities rental under the lease was approximately \$304,000 and \$310,000, respectively. Minimum rentals, on an annual basis, are approximately \$304,000 for 2013 through 2015.

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 amounts paid during 2012 and 2011 for the facilities rental was \$40,000 each year. As of December 31, 2012, this lease had not been renewed.

NATIONAL CUTTING HORSE ASSOCIATION

NOTES TO FINANCIAL STATEMENTS *(continued)*

Q. Commitments and Contingencies – continued

In 2010, the Association entered into a bartering arrangement with an event facility in Ogden, Utah, in which the Association was provided the use of facilities, stalls, services and equipment for the Western National Championship event with an estimated value of \$126,000 per year at no cost. In exchange, the Association provided the facility with sponsorship benefits at an official corporate partner level which includes advertisement in programs, annuals, posters, public announcements and wall signage. The value of the sponsorship recognition provided is to equal the value of the facilities provided to the Organization at no cost. This agreement was terminated in 2011, resulting in the Association paying \$30,000 to the facility during the year ended December 31, 2011.

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, 2012.

R. Subsequent Events

In preparing the accompanying financial statements, management has evaluated all subsequent events and transactions for potential recognition or disclosure through June 17, 2013, the date the financial statements were available for issuance.