

Mercy for Animals, Inc.

Financial Statements

December 31, 2016



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INDEPENDENT AUDITOR'S REPORT

Board of Directors
Mercy for Animals, Inc.
Los Angeles, California

We have audited the accompanying financial statements of Mercy for Animals, Inc., a nonprofit organization (the "Organization"), which comprise the statement of financial position as of December 31, 2016, and the related statements of activities, functional expenses, and cash flows for the year then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. 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 Mercy for Animals, Inc. as of December 31, 2016, and the changes in its net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

A handwritten signature in black ink that reads "Armanino LLP". The signature is written in a cursive, flowing style.

Armanino^{LLP}
San Francisco, California

January 10, 2018

Mercy for Animals, Inc.
Statement of Financial Position
December 31, 2016

ASSETS

Current assets	
Cash and cash equivalents	\$ 7,969,375
Accounts receivable	94,833
Pledges receivable	2,789,247
Investments	3,030,149
Inventory	44,782
Prepaid expenses	<u>22,336</u>
Total current assets	13,950,722
Property and equipment, net	<u>193,917</u>
Total assets	<u><u>\$ 14,144,639</u></u>

LIABILITIES AND NET ASSETS

Current liabilities	
Accounts payable	\$ 14,079
Accrued expenses	<u>145,106</u>
Total current liabilities	<u>159,185</u>
Net assets	
Unrestricted	11,097,832
Temporarily restricted	<u>2,887,622</u>
Total net assets	<u>13,985,454</u>
Total liabilities and net assets	<u><u>\$ 14,144,639</u></u>

The accompanying notes are an integral part of these financial statements.

Mercy for Animals, Inc.
Statement of Activities
For the Year Ended December 31, 2016

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Total</u>
Revenues			
Contributions	\$ 7,411,446	\$ 3,906,573	\$ 11,318,019
Sale of merchandise, net of cost of goods sold of \$114,238	48,018	-	48,018
Fundraising events, less event expense of \$169,297	1,369,399	-	1,369,399
Royalty revenue	57,500	-	57,500
Interest and dividend income	48,261	-	48,261
Unrealized losses on investments, net	(80,422)	-	(80,422)
Net assets released from restriction	<u>1,058,773</u>	<u>(1,058,773)</u>	<u>-</u>
Total revenues	<u>9,912,975</u>	<u>2,847,800</u>	<u>12,760,775</u>
Functional expenses			
Program services	5,045,478	-	5,045,478
Management and general	257,450	-	257,450
Fundraising	<u>1,320,430</u>	<u>-</u>	<u>1,320,430</u>
Total functional expenses	<u>6,623,358</u>	<u>-</u>	<u>6,623,358</u>
Change in net assets	<u>3,289,617</u>	<u>2,847,800</u>	<u>6,137,417</u>
Net assets, beginning of year, as previously reported	7,848,037	-	7,848,037
Reclassification	<u>(39,822)</u>	<u>39,822</u>	<u>-</u>
Net assets, beginning of year, as reclassified	<u>7,808,215</u>	<u>39,822</u>	<u>7,848,037</u>
Net assets, end of year	<u>\$ 11,097,832</u>	<u>\$ 2,887,622</u>	<u>\$ 13,985,454</u>

The accompanying notes are an integral part of these financial statements.

Mercy for Animals, Inc.
Statement of Functional Expenses
For the Year Ended December 31, 2016

	<u>Program Services</u>	<u>Management and General</u>	<u>Fundraising</u>	<u>Total</u>
Salaries, benefits and payroll taxes	\$ 2,191,043	\$ 129,199	\$ 635,698	\$ 2,955,940
Advertising	625,519	-	300	625,819
Contract labor	461,084	553	302,929	764,566
Contributions	568,660	-	-	568,660
Depreciation and amortization	42,009	2,454	12,482	56,945
Development	-	-	59,956	59,956
Insurance	46,068	69,911	6,852	122,831
Professional fees and dues	31,692	5,961	676	38,329
Office expenses	143,415	24,012	38,603	206,030
Supplies	158,054	350	22,516	180,920
Postage and shipping	177,137	-	-	177,137
Printing and copying	208,663	513	34,905	244,081
IT expenses	87,279	3,743	110,871	201,893
Telecommunications	25,952	5,063	6,083	37,098
Taxes	-	1,730	-	1,730
Travel	262,084	2,916	81,646	346,646
Organization expenses	16,819	11,045	6,913	34,777
	<u>\$ 5,045,478</u>	<u>\$ 257,450</u>	<u>\$ 1,320,430</u>	<u>\$ 6,623,358</u>

The accompanying notes are an integral part of these financial statements.

Mercy for Animals, Inc.
Statement of Cash Flows
For the Year Ended December 31, 2016

Cash flows from operating activities	
Change in net assets	\$ 6,137,417
Adjustments to reconcile change in net assets to net cash provided by operating activities	
Depreciation and amortization	56,945
Stock donation	(951,016)
Unrealized losses on investments, net	80,422
Changes in operating assets and liabilities	
Accounts receivable	(94,833)
Pledges receivable	(1,142,038)
Inventory	(12,237)
Prepaid expenses	14,838
Accounts payable	(14,270)
Accrued expenses	138,918
Deferred revenue	<u>(57,500)</u>
Net cash provided by operating activities	<u>4,156,646</u>
Cash flows from investing activities	
Purchase of property and equipment	(83,846)
Purchase of investments	<u>(532,840)</u>
Net cash used in investing activities	<u>(616,686)</u>
Net increase in cash	3,539,960
Cash, beginning of year	<u>4,429,415</u>
Cash, end of year	<u><u>\$ 7,969,375</u></u>

The accompanying notes are an integral part of these financial statements.

Mercy for Animals, Inc.
Notes to Financial Statements
December 31, 2016

1. NATURE OF OPERATIONS

Mercy for Animals, Inc. (the "Organization") is a 501(c)(3) nonprofit animal protection organization which works to prevent cruelty to farmed animals and promote compassionate food choices and policies through investigations, legal advocacy, corporate engagement, and education. Mercy for Animals, Inc. focuses on farmed animal advocacy and promoting cruelty-free food choices.

In order to spread the Organization's mission domestically and globally, the Organization assisted in the establishment of the following affiliated nonprofit organizations: The Good Food Institute, Inc., Mercy For Animals Canada, Mercy For Animals Brasil, Mercy For Animals Asia Limited, Mercy For Animals Latinoamerica, and Mercy For Animals India Foundation. Each affiliated organization has a separate Board of Directors and its own management team. The Organization has representation on certain Board of Directors of the affiliated organizations, but does not have control over any of the Board of Directors. Management of the Organization has evaluated the consolidation requirements and determined that the Organization is not required to consolidate any of the affiliated organizations.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of accounting

The Organization used the accrual basis of accounting, which recognizes income in the period earned and expenses when incurred.

Use of estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosure of contingent assets and liabilities, at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash and credit risks

Cash includes cash on hand, bank checking accounts, and savings accounts. While the Organization's cash, at times, may exceed federally insured limits, the Organization has not experienced any losses in such accounts. The Organization believes it is not exposed to any significant credit risk on these accounts.

Mercy for Animals, Inc.
Notes to Financial Statements
December 31, 2016

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Receivables

Accounts receivable are stated at the amount management expects to collect from outstanding balances. Pledges receivable represent unconditional promises to contribute specified amounts to the Organization in the future. Pledges to be received after fiscal year-end are recorded at the present value of their estimated future cash flows. The discount on these amounts is computed using risk adjusted market interest rates applicable to the years in which the promises are expected to be received. Amortization of the discount is recorded as additional contribution revenue in accordance with donor-imposed restrictions, if any, on the contributions.

An allowance for doubtful accounts is established based upon management's judgment including such factors as prior collection history, aging statistics of contributions, and the nature of the receivable. Account balances are charged off against the allowance for doubtful accounts after all means of collection have been exhausted and the potential for recovery is considered remote. Management believes that all of its receivables are collectible; accordingly, no allowance for doubtful accounts is recorded at December 31, 2016.

Fair value measurements

Generally accepted accounting principles establish a fair value hierarchy for inputs used in measuring fair value that maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that the most observable inputs be used when available. Observable inputs are those that market participants would use in pricing the asset or liability based on market data obtained from sources independent of the Organization. Unobservable inputs, if any, reflects the Organization's assumption about the inputs market participants would use in pricing the asset or liability developed based on the best information available in the circumstances. The fair value hierarchy is categorized into three levels based on the inputs as follows:

- *Level 1* - Valuations based on unadjusted quoted prices in active markets for identical assets or liabilities that the Organization has the ability to access at the measurement date. Since valuations are based on quoted prices that are readily and regularly available in an active market, valuation of these securities does not entail a significant degree of judgment.
- *Level 2* - Valuations based on significant inputs that are observable, either directly or indirectly or quoted prices in the markets that are not active, that is, markets in which there are few transactions, the prices are not current or price quotations vary substantially either over time or among market participants.
- *Level 3* - Valuations based on inputs that are unobservable and significant to the overall fair value measurement.

Mercy for Animals, Inc.
Notes to Financial Statements
December 31, 2016

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Property and equipment

Property and equipment are stated at cost and depreciated or amortized using the straight-line method over the estimated useful lives of 3-5 years or the lesser of the estimate useful life or lease term for leasehold improvements.

Net assets

The Organization reports information regarding its financial position and activities according to classes of net assets. Net assets and changes therein are classified as follows:

- *Unrestricted net assets* - Net assets not subject to donor-imposed stipulations. This category includes net assets designated by the board of trustees to require board approval prior to expenditure.
- *Temporarily restricted net assets* - Net assets subject to donor-imposed stipulations that will be met by actions of the Organization and/or the passage of time.
- *Permanently restricted net assets* - Net assets subject to donor-imposed stipulations that they be held in perpetuity by the Organization. Income from these funds is available to support specific activities of the Organization. There were no permanently restricted net assets at December 31, 2016.

Revenue recognition

Contributions, including unconditional promises to give, are recognized as revenue in the period received. Conditional promises to give are not recognized until they become unconditional; that is when the conditions on which they depend are substantially met. Contributions of assets other than cash are recorded at their estimated fair value. Grants represent contributions if resource providers do not receive direct commensurate value in exchange for the assets transferred. Contributions are recorded at their fair value as unrestricted support, temporarily restricted support, or permanently restricted support, depending on the absence or existence of donor imposed restrictions as applicable. When a restriction expires (that is, when a stipulated time restriction ends or purpose restriction is accomplished), temporarily restricted net assets are reclassified to unrestricted net assets and reported in the Statement of Activities as net assets released from restrictions.

Functional expenses

The costs of providing program services and supporting services have been summarized on a functional basis in the Statement of Activities and the Statement of Functional Expenses. Accordingly, certain costs are allocated among program services and supporting services based on estimates of employees' time incurred and on usage of resources.

Mercy for Animals, Inc.
Notes to Financial Statements
December 31, 2016

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Income tax status

The Organization is exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code and state income taxes under the related California code sections.

Subsequent events

Subsequent events have been evaluated through January 10, 2018, the date the financial statements were available to be issued. No subsequent events have occurred that would have a material impact on the presentation of the Organization's financial statements.

3. PLEDGES RECEIVABLE

Pledges receivable at December 31, 2016 amounted to \$2,789,247 and are due in less than one year.

4. PROPERTY AND EQUIPMENT

Property and equipment consist of the following:

Furniture and equipment	\$ 236,924
Leasehold improvements	134,284
Software	<u>5,600</u>
	376,808
Accumulated depreciation	<u>(182,891)</u>
	<u>\$ 193,917</u>

Depreciation and amortization expense for the year ended December 31, 2016 was \$56,945.

5. INVESTMENTS

Investments consist of the following:

Cash equivalents	\$ 2,787,999
Equity	217,298
Mutual funds	<u>24,852</u>
	<u>\$ 3,030,149</u>

Mercy for Animals, Inc.
Notes to Financial Statements
December 31, 2016

5. INVESTMENTS (continued)

The following table sets forth by level, within the fair value hierarchy, the Organization's assets at fair value as of December 31, 2016:

	Level 1	Level 2	Level 3	Total
Cash equivalents	\$ 2,787,999	\$ -	\$ -	\$ 2,787,999
Equity	217,298	-	-	217,298
Mutual funds	24,852	-	-	24,852
	\$ 3,030,149	\$ -	\$ -	\$ 3,030,149

6. TEMPORARILY RESTRICTED NET ASSETS

Temporarily restricted net assets consist of the following:

Broiler chicken	\$ 932,163
International cage free	844,575
Corporate cage free	521,722
Investigation	424,489
Legal advocacy	99,846
Mexico	40,000
Tapjoy	24,827
	\$ 2,887,622

Temporarily restricted net assets released from restriction during the year were as follows:

Corporate cage free	\$ 478,278
Investigation	209,779
International cage free	155,425
Broiler chicken	67,837
Tapjoy	50,173
Corporate outreach	30,000
Education	17,305
Legal advocacy	10,154
Other	39,822
	\$ 1,058,773

Mercy for Animals, Inc.
Notes to Financial Statements
December 31, 2016

7. OPERATING LEASE COMMITMENTS

The Organization leases space in the following three locations: Chicago, Illinois, New York, New York and West Hollywood, California. The Chicago and New York leases are on a month-to-month basis and require monthly payments of of \$570 and \$650, respectively. The West Hollywood lease extends through March 2018 and requires escalating monthly rent payments ranging from \$1,700 to \$4,194.

The scheduled minimum lease payments under the lease terms are as follows:

Year ending December 31,

2017	\$ 67,984
2018	<u>17,121</u>
	<u>\$ 85,105</u>

8. RELATED PARTY

The Organization paid for The Good Food Institute, Inc.'s ("GFI") expenses during 2016 with the understanding that GFI would reimburse the Organization for certain amounts. The Organization elected to not seek reimbursement for \$500,000 of expenses that the Organization paid for on behalf of GFI, which the Organization recognized as contribution expense. At December 31, 2016, the Organization had a receivable from GFI in amount of \$94,833.