

Audited Financial Statements

Midland Area Community Foundation

*Years ended December 31, 2010 and 2009
with Report of Independent Auditors*



Midland Area Community Foundation

Audited Financial Statements

Years ended December 31, 2010 and 2009

Contents

Financial Statements

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Report of Independent Auditors

Board of Directors
Midland Area Community Foundation
Midland, Michigan

We have audited the accompanying statement of financial position of Midland Area Community Foundation (Foundation) as of December 31, 2010 and the related statements of activities and cash flows for the year then ended. These financial statements are the responsibility of the Foundation's management. Our responsibility is to express an opinion on these financial statements based on our audit. The prior year summarized comparative information has been derived from the Foundation's 2009 financial statements and, in our report dated April 14, 2010, we expressed an unqualified opinion on those financial statements.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Midland Area Community Foundation as of December 31, 2010, and the changes in its net assets and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Andrews Hooper Pavlik PLC

Midland, Michigan
April 15, 2011

Midland Area Community Foundation

Statements of Financial Position

| | December 31 | |
|------------------------------------|----------------------|----------------------|
| | 2010 | 2009 |
| Assets | | |
| Cash and cash equivalents | \$ 6,498,624 | \$ 5,732,609 |
| Investments | 59,465,674 | 51,737,150 |
| Pledges receivable | 153,800 | 224,450 |
| Prepaid expenses and other | 5,201 | 5,320 |
| Parks and improvements | 668,647 | 668,647 |
| Office facility and equipment, net | 767,492 | 805,452 |
| Total assets | <u>\$ 67,559,438</u> | <u>\$ 59,173,628</u> |
| Liabilities and net assets | | |
| Current liabilities: | | |
| Accounts payable | \$ 20,887 | \$ 15,247 |
| Grants payable | 44,350 | 20,050 |
| Restricted organizational funds | 1,422,733 | 1,276,158 |
| Total current liabilities | <u>1,487,970</u> | <u>1,311,455</u> |
| Net assets: | | |
| Unrestricted | 63,925,406 | 55,825,223 |
| Temporarily restricted | 1,146,062 | 1,036,950 |
| Permanently restricted | 1,000,000 | 1,000,000 |
| Total net assets | <u>66,071,468</u> | <u>57,862,173</u> |
| Total liabilities and net assets | <u>\$ 67,559,438</u> | <u>\$ 59,173,628</u> |

See accompanying notes.

Midland Area Community Foundation

Statements of Activities

| | Year ended December 31, 2010 | | | Year ended | |
|---|------------------------------|--------------|--------------|--------------|--------------|
| | Temporarily Permanently | | | December 31, | |
| | Unrestricted | Restricted | Restricted | 2009 | |
| | | | Total | Comparative | |
| | | | | Totals | |
| Public support, revenue, and gains | | | | | |
| Contributions | \$ 3,433,344 | \$ 833 | \$ - | \$ 3,434,177 | \$ 2,486,909 |
| Investment income | 7,454,415 | 260,071 | - | 7,714,486 | 11,725,305 |
| Miscellaneous | 96,684 | - | - | 96,684 | 26,099 |
| Net assets released from restrictions | 151,792 | (151,792) | - | - | - |
| Total public support, revenue, and gains | 11,136,235 | 109,112 | - | 11,245,347 | 14,238,313 |
| Expenses | | | | | |
| Program services: | | | | | |
| Grant awards | 1,794,772 | - | - | 1,794,772 | 1,180,412 |
| Other program expenses | 757,814 | - | - | 757,814 | 929,276 |
| Support services: | | | | | |
| Management and general | 359,333 | - | - | 359,333 | 359,469 |
| Fundraising | 124,133 | - | - | 124,133 | 117,926 |
| Total expenses | 3,036,052 | - | - | 3,036,052 | 2,587,083 |
| Change in net assets | 8,100,183 | 109,112 | - | 8,209,295 | 11,651,230 |
| Net assets at beginning of year | 55,825,223 | 1,036,950 | 1,000,000 | 57,862,173 | 46,210,943 |
| Net assets at end of year | \$63,925,406 | \$ 1,146,062 | \$ 1,000,000 | \$66,071,468 | \$57,862,173 |

See accompanying notes.

Midland Area Community Foundation

Statements of Cash Flows

| | Year ended December 31 | |
|---|-------------------------------|---------------|
| | 2010 | 2009 |
| Operating activities | | |
| Change in net assets | \$ 8,209,295 | \$ 11,651,230 |
| Adjustments to reconcile change in net assets to net cash provided by operating activities: | | |
| Depreciation | 40,269 | 39,908 |
| Net appreciation in fair value of investments | (6,426,833) | (10,613,528) |
| Change in operating assets and liabilities: | | |
| Pledges receivable | 70,650 | 182,450 |
| Prepaid expenses and other | 119 | 13,975 |
| Accounts payable | 5,640 | (27,666) |
| Grants payable | 24,300 | (71,199) |
| Restricted organizational funds | 146,575 | 251,991 |
| Deferred revenue | - | (242,023) |
| Net cash provided by operating activities | 2,070,015 | 1,185,138 |
| Investing activities | | |
| Purchases of property and equipment | (2,309) | (2,997) |
| Proceeds from sale of investments | 2,541,030 | 4,893,454 |
| Purchases of investments | (3,842,721) | (6,751,006) |
| Net cash used in investing activities | (1,304,000) | (1,860,549) |
| Net increase (decrease) in cash and cash equivalents | 766,015 | (675,411) |
| Cash and cash equivalents at beginning of year | 5,732,609 | 6,408,020 |
| Cash and cash equivalents at end of year | \$ 6,498,624 | \$ 5,732,609 |

See accompanying notes.

Midland Area Community Foundation

Notes to Financial Statements

December 31, 2010

1. Nature of Organization, Risks and Uncertainties

Midland Area Community Foundation (Foundation) is organized as a not-for-profit community foundation for the purpose of promoting and enabling community-wide philanthropic giving to enrich and improve the lives of residents throughout the Michigan counties of Midland, Clare and Gladwin. In fulfilling this mission, the Foundation receives and administers gifts and bequests that are used to meet various needs.

The Foundation receives most of its contributions from numerous individuals, public and private foundations, and businesses located in Midland County. Contributions from a small number of large dollar amount donors may represent a material portion of total contribution revenue. The composition of large dollar amount donors changes each year. During the years ended December 31, 2010 and 2009, contributions from the Foundation's large dollar donors represented approximately 71% and 66%, respectively, of contribution revenue.

The Foundation is a not-for-profit organization exempt from income tax under Section 501(c)(3) of the Internal Revenue Code (Code). The Foundation has been classified as a publicly supported charitable organization under Section 509(a)(1) of the Code and contributions to it are tax deductible by donors within the limitations prescribed by the Code. Also, the Foundation is a Michigan certified community foundation; as such, certain contributions to the Foundation entitle the donor to a state tax credit in addition to the deduction allowed for federal income tax purposes.

2. Summary of Significant Accounting Policies

Basis of Accounting and Presentation

The Foundation reports 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. Net assets, including endowment funds, are classified and reported based on the existence or absence of donor imposed restrictions. The bylaws of the Foundation include a variance provision that allows the Board of Trustees of the Foundation to vary the use of substantially all contributions received.

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 certain reported amounts in the financial statements and accompanying notes. Actual results could differ from those estimates.

Midland Area Community Foundation

Notes to Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

Fair Value Measurements

Fair value is the exchange price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. In determining fair value, the Foundation uses various methods including market, income, and cost approaches. Based on these approaches, the Foundation often utilizes certain assumptions that market participants would use in pricing the asset or liability, including assumptions about risk and/or the risks inherent in the inputs to the valuation technique. These inputs can be readily observable, market corroborated, or generally unobservable inputs. The Foundation utilizes valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs. Based on the observability of the inputs used in the valuation techniques, the Foundation is required to provide the following information according to the fair value hierarchy. The fair value hierarchy ranks the quality and reliability of the information used to determine fair values. Financial assets and liabilities carried at fair value will be classified and disclosed in one of the following three categories:

- Level 1 – Valuations for assets and liabilities traded in active exchange markets, such as the New York Stock Exchange. Level 1 also includes U.S. Treasury and federal agency securities and federal agency mortgage-backed securities, which are traded by dealers or brokers in active markets. Valuations are obtained from readily available pricing sources for market transactions involving identical assets or liabilities.
- Level 2 – Valuations for assets and liabilities traded in less active dealer or broker markets. Valuations are obtained from third party pricing services for identical or similar assets or liabilities.
- Level 3 – Valuations for assets and liabilities that are derived from other valuation methodologies, including option pricing models, discounted cash flow models, and similar techniques, and not based on market exchange, dealer, or broker traded transactions. Level 3 valuations incorporate certain assumptions and projections in determining the fair value assigned to such assets or liabilities.

In determining the appropriate levels, the Foundation performs a detailed analysis of the assets and liabilities that are subject to the fair value standard. At each reporting period, all assets and liabilities for which the fair value measurement is based on significant unobservable inputs are classified as Level 3. The Foundation had no securities classified as level 3 at December 31, 2010 and 2009. Assets classified as level 3 at December 31, 2010 and 2009, included patent rights receivable. For the years ended December 31, 2010 and 2009, the application of valuation techniques applied to similar assets and liabilities has been consistent.

Midland Area Community Foundation

Notes to Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

Cash and Cash Equivalents

Cash and cash equivalents consist of cash deposits held in bank demand deposit accounts and money market funds. Bank demand deposits are held by high-credit-quality financial institutions. Although such cash balances exceeded the federally insured limits at certain times during the year, they are, in the opinion of management, subject to minimal risk. Money market funds are not federally insured. Management believes these funds are subject to minimal risk since a significant portion of securities held by money market funds consist of insured AAA rated bonds and United States Treasury bonds or notes.

Investments

The Foundation reports investments in marketable securities at their fair values in the statements of financial position. Unrealized gains and losses are included in investment income in the accompanying statements of activities.

The Foundation's investment portfolio consists of mutual funds including money market funds, bond funds, and equity funds. These mutual funds invest in and hold investment securities that are exposed to various risks such as interest rate, market, and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and such changes could materially affect the amounts reported in the statements of financial position.

Pledges Receivable

The Foundation reports unconditional pledges received as revenue in the period received. Pledges receivable are recorded at net realized value if expected to be collected in one year and at fair value if expected to be collected in more than one year. Fair value represents the present value of estimated future cash flows from unconditional promises to give discounted using an interest rate of 4.25 percent. Uncollectible promises to give are expected to be insignificant.

Parks and Improvements

Parks and improvements consist of the Overlook Park and related improvements recorded at estimated fair value at the date of donation plus any improvements.

Office Facility and Equipment and Depreciation

The office facility and equipment are stated at cost, if purchased, or at the estimated fair value at date of donation. Major improvements and renewals are capitalized while ordinary maintenance and repairs are expensed. Depreciation is computed on the straight-line method and is based on expected useful lives ranging from 3 to 40 years.

Midland Area Community Foundation

Notes to Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

Restricted Organizational Funds

Restricted organizational funds are recorded as liabilities and consist of amounts received from other not-for-profit organizations that specify the donor organization or a related organization as the beneficiary. Investment earnings or losses allocated to the funds and distributions paid to the beneficiary organization are recorded as increases and decreases, respectively, to the liability. Distributions from restricted organizational funds are subject to the current spending policies of the Foundation.

Net Asset Classifications

The Foundation classifies as permanently restricted net assets a) the original value of the gifts and grants to permanent endowments, b) the original value of subsequent gifts to the permanent endowments, and c) accumulations to the permanent endowments in accordance with the applicable donor or grantor gift instrument. The remaining portion of endowment fund investments that is not classified as permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure for the intended purpose or, when unrestricted, reported as unrestricted and designated by management for specific purposes.

Temporarily restricted net assets consist of pledges receivable because of the inherent time restrictions on the use of the funds and the remaining portion of donor restricted endowment funds that are not classified as permanently restricted. When a restriction expires, that is, when a stipulated time restriction ends or a purpose restriction is fulfilled, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statements of activity as net assets released from restrictions.

The Board of Directors, on advice of legal counsel, has determined that the majority of the Foundation's net assets do not meet the definition of an endowment under the Uniform Prudent Management of Institutional Funds Act (UPMIFA). The Foundation is governed subject to the Governing Documents for the Foundation and most contributions are subject to the terms of the Governing Documents and the related Fund or Gift Agreements. Certain contributions are received subject to other gift or grant instruments, or are subject to specific agreements with the Foundation, and may be recorded as permanently restricted, temporarily restricted, or unrestricted, depending on the specific terms of the agreements.

Midland Area Community Foundation

Notes to Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

Net Asset Classifications (continued)

Under the terms of the Governing Documents and the Fund or Gift Agreements, the Board of Directors has the ability to modify any restrictions or condition on the distribution of funds that becomes, in effect, unnecessary, incapable of fulfillment, or inconsistent with the charitable needs of the community of area service. The Board of Directors also has the ability to distribute so much of the corpus of any trust or separate gift, devise, bequest, or fund as the board in its sole discretion shall determine. As a result of the ability to distribute corpus, all contributions not classified as temporarily restricted or permanently restricted are classified as unrestricted net assets for financial statement purposes.

Contributions

Generally, contributions, including unconditional pledges to give, are recorded at fair value when received. Contributions of services, fixed assets, and other non-monetary contributions are recorded at the donor's estimated fair value. All current contributions are considered unrestricted.

Functional Classification of Expenses

The Foundation reports its expenses on the statement of activities in functional classifications based on direct identification, time studies and floor space. Each category is defined as follows:

Program Expenses

Program expenses include grant awards and other significant program expenses. Program expenses also include in-kind and other expenses incurred by such programs as the Santa House project, Riverdays event, Midland County Youth Action Council, Midland County Gang and Violence Prevention Partnership project, and Scholarships.

Management and General

Management and general expenses include those expenses associated with the management of the Foundation.

Fundraising Expenses

Fundraising expenses include those expenses associated with promoting and raising funds for the Foundation.

Midland Area Community Foundation

Notes to Financial Statements (continued)

2. Summary of Significant Accounting Policies (continued)

Grant Awards

Grants are recorded as expenses when approved by the Foundation's Board of Directors. Grant awards are presented on the financial statements net of grant refunds.

Comparative Financial Information

The statement of activities includes certain prior-year summarized comparative information in total but not by net asset class. Such information does not include sufficient detail to constitute a presentation in conformity with accounting principles generally accepted in the United States of America. Accordingly, such information should be read in conjunction with the Foundation's financial statements for the year ended December 31, 2009, from which the summarized information was derived.

Reclassification

Certain 2009 amounts have been reclassified to conform to the 2010 presentation. Such reclassifications had no effect on net assets or the change in net assets.

Subsequent Events

Subsequent events have been evaluated through April 15, 2011, which is the date the financial statements were available to be issued.

3. Investments

The following summarizes the cost basis and market value (carrying value) of investments.

| | December 31, 2010 | | December 31, 2009 | |
|---------------------------|--------------------------|---------------------|--------------------------|---------------------|
| | Cost | Market | Cost | Market |
| Fixed income mutual funds | \$12,769,118 | \$13,691,524 | \$10,838,169 | \$11,492,347 |
| Equity mutual funds | 34,641,364 | 43,299,918 | 34,093,250 | 36,781,849 |
| Hedge funds | 2,500,000 | 2,474,232 | 2,500,000 | 2,351,500 |
| Bank loan fund | - | - | 970,000 | 1,111,454 |
| | \$49,910,482 | \$59,465,674 | \$48,401,419 | \$51,737,150 |

Midland Area Community Foundation

Notes to Financial Statements (continued)

3. Investments (continued)

Investment income for the years ended December 31, consisted of the following:

| | <u>2010</u> | <u>2009</u> |
|---|---------------------|----------------------|
| Interest, dividends and distributions | \$ 1,468,681 | \$ 1,406,365 |
| Net appreciation in fair value | <u>6,426,833</u> | 10,613,528 |
| Net investment income | 7,895,514 | 12,019,893 |
| Less amounts allocated to restricted organizational funds | <u>181,028</u> | 294,588 |
| | <u>\$ 7,714,486</u> | <u>\$ 11,725,305</u> |

The Foundation paid bank trustee and investment management fees of \$4,267 and \$31,381, respectively, in 2010 and \$3,862 and \$31,430, respectively, in 2009.

4. Pledges Receivable

Pledges receivable at December 31, 2010 and 2009, consisted of unconditional promises to give and an assignment of patent rights. At December 31, 2010 and 2009, approximately 99% of pledges receivable were collectible from the assignment of patent rights. Pledges receivable are expected to be collected as follows:

| | <u>2010</u> | <u>2009</u> |
|------------------------------------|-------------------|-------------------|
| Receivable in less than one year | \$ 82,300 | \$ 82,300 |
| Receivable in one to five years | <u>80,000</u> | 160,000 |
| | 162,300 | 242,300 |
| Less discount to net present value | <u>8,500</u> | 17,850 |
| | <u>\$ 153,800</u> | <u>\$ 224,450</u> |

Patent Rights

During 2005, a contributor assigned patent rights to the Foundation, which expire in August 2012. The value of the patent rights, which is included in pledges receivable, is calculated based on the present value of the estimated amount of the semi-annual payments to be received discounted at 4.25%. At December 31, 2010, the estimated net present value is approximately \$151,500.

Midland Area Community Foundation

Notes to Financial Statements (continued)

5. Office Facility and Equipment

Office facility and equipment as of December 31, 2010 and 2009, consisted of the following:

| | <u>2010</u> | <u>2009</u> |
|------------------------------------|-------------------|-------------------|
| Land | \$ 65,000 | \$ 65,000 |
| Building and improvements | 688,868 | 688,868 |
| Office furniture and fixtures | 111,305 | 108,996 |
| Office equipment | 38,363 | 38,363 |
| Computer software | 32,845 | 32,845 |
| Total cost | <u>936,381</u> | <u>934,072</u> |
| Less accumulated depreciation | 168,889 | 128,620 |
| Office facility and equipment, net | <u>\$ 767,492</u> | <u>\$ 805,452</u> |

6. Endowments

Endowment Funds

The Foundation's endowment funds consist of approximately 325 individual funds established for a variety of reasons. The endowment funds consist of both donor restricted endowment funds and funds designated by the Board of Directors to function as endowments. Net assets associated with the endowment funds, including funds designated by the Board of Directors to function as endowments, are classified and reported based on the existence or absence of donor imposed restrictions.

Interpretation of Relevant Law

The Foundation has interpreted UPMIFA as requiring preservation of the fair value of the original gift, as of the gift date, of donor restricted endowment funds absent explicit donor stipulations to the contrary. The Foundation considers the following factors in making a determination to appropriate or accumulate donor restricted endowment funds and board designated endowment funds:

- (1) The duration and preservation of the fund.
- (2) The purposes of the Foundation and the donor restricted endowment fund.
- (3) General economic conditions.
- (4) The possible effect of inflation and deflation.
- (5) The expected total return from income and the appreciation or depreciation of investments.
- (6) Other resources of the Foundation.
- (7) The investment policies of the Foundation.

Midland Area Community Foundation

Notes to Financial Statements (continued)

6. Endowments (continued)

Endowment Funds and Changes Therein

The Foundation's endowment net asset composition as of December 31, 2010, was as follows:

| | Temporarily Permanently | | | |
|----------------------------------|-------------------------|-------------------|---------------------|----------------------|
| | Unrestricted | Restricted | Restricted | Total |
| Donor restricted endowment funds | \$ - | \$ 992,262 | \$ 1,000,000 | \$ 1,992,262 |
| Board designated endowment funds | 52,792,699 | - | - | 52,792,699 |
| | <u>\$ 52,792,699</u> | <u>\$ 992,262</u> | <u>\$ 1,000,000</u> | <u>\$ 54,784,961</u> |

Changes in board designated and donor restricted endowment funds during the year ended December 31, 2010, follows:

| | Temporarily Permanently | | | |
|---------------------------------|-------------------------|-------------------|---------------------|----------------------|
| | Unrestricted | Restricted | Restricted | Total |
| Balance, December 31, 2009 | \$ 46,008,303 | \$ 812,100 | \$ 1,000,000 | \$ 47,820,403 |
| Investment income: | | | | |
| Interest and dividends | 1,271,532 | 48,726 | - | 1,320,258 |
| Net appreciation of investments | 5,567,320 | 211,345 | - | 5,778,665 |
| Net investment return | 6,838,852 | 260,071 | - | 7,098,923 |
| Contributions | 2,745,843 | 833 | - | 2,746,676 |
| Grants appropriated | (1,738,696) | (36,744) | - | (1,775,440) |
| Fees and expenses | (1,061,603) | (43,998) | - | (1,105,601) |
| Balance, December 31, 2010 | <u>\$ 52,792,699</u> | <u>\$ 992,262</u> | <u>\$ 1,000,000</u> | <u>\$ 54,784,961</u> |

The Foundation's endowment net asset composition as of December 31, 2009, was as follows:

| | Temporarily Permanently | | | |
|----------------------------------|-------------------------|-------------------|---------------------|----------------------|
| | Unrestricted | Restricted | Restricted | Total |
| Donor restricted endowment funds | \$ - | \$ 812,100 | \$ 1,000,000 | \$ 1,812,100 |
| Board designated endowment funds | 46,008,303 | - | - | 46,008,303 |
| | <u>\$ 46,008,303</u> | <u>\$ 812,100</u> | <u>\$ 1,000,000</u> | <u>\$ 47,820,403</u> |

Midland Area Community Foundation

Notes to Financial Statements (continued)

6. Endowments (continued)

Changes in board designated and donor restricted endowment funds during the year ended December 31, 2009, follows:

| | | | | |
|---|---------------|------------|--------------|---------------|
| Balance, December 31, 2008 | \$ 35,682,200 | \$ - | \$ 1,000,000 | \$ 36,682,200 |
| Reclassification based on change in law | (470,867) | 470,867 | - | - |
| Investment income: | | | | |
| Interest and dividends | 1,171,830 | 48,580 | - | 1,220,410 |
| Net appreciation of investments | 8,843,818 | 366,638 | - | 9,210,456 |
| Net investment return | 10,015,648 | 415,218 | - | 10,430,866 |
| Contributions | 2,704,665 | 4,300 | - | 2,708,965 |
| Grants appropriated | (811,114) | (30,285) | - | (841,399) |
| Other program expenses | (889,880) | - | - | (889,880) |
| Fees and expenses | (222,349) | (48,000) | - | (270,349) |
| Balance, December 31, 2009 | \$ 46,008,303 | \$ 812,100 | \$ 1,000,000 | \$ 47,820,403 |

Funds with Deficiencies

From time to time, the fair value of investment assets associated with individual donor restricted endowment funds may fall below the level that the donor or UPMIFA requires the Foundation to retain as a fund of perpetual duration. In accordance with accounting principles generally accepted in the United States of America, deficiencies of this nature are reported in unrestricted net assets. The fair value of the Foundation's investment assets at December 31, 2010 and 2009, associated with the endowment portion of its funds exceeded the level required by the donor or UPMIFA to be retained as a fund of perpetual duration.

Return Objectives and Risk Parameters

The Foundation has adopted investment and spending policies for its investment portfolio that attempt to provide a predictable stream of funding to programs supported by the investment portfolio while seeking to maintain the purchasing power of the endowment investments. Endowment assets include those assets of donor restricted funds that the Foundation must hold in perpetuity or for a donor specified period and board designated funds. As approved by the Foundation's Investment Committee, the investments are invested in a manner that is intended to achieve a target rate of return that exceeds the consumer price index by at least 5.5% on a net-of-fees basis over a five-year rolling average. The portfolio is also expected to outperform a weighted benchmark index without exceeding a standard deviation of 1.2 times the weighted benchmark index on a total return basis over the full market cycle. The benchmark index is comprised of each asset class index weighted by its target allocation. Actual returns in any given year may vary from target amounts.

Midland Area Community Foundation

Notes to Financial Statements (continued)

6. Endowments (continued)

Strategies Employed for Achieving Objectives

The Foundation's investment portfolio is expected to endure into perpetuity. The Foundation invests a significant portion of assets in equity or equity-like securities to meet performance objectives. Management believes the long-term risk of not investing in growth securities outweighs the short-term volatility risk of such securities. As a result, fixed income securities will be used to lower the short-term volatility of the portfolio and to provide income stability, especially during periods of weak or negative equity markets. Cash is not viewed as a strategic asset of the portfolio, but instead is used to meet short-term liquidity needs. Other asset classes are included to provide diversification (e.g., international equities) and incremental return (e.g. small cap equities).

7. Spending Policy and How the Investment Objectives Relate to Spending Policy

The Foundation's spending policy annually calculates the amount of money available for distribution from the various endowed funds for grant making and administration. The current spending policy is to distribute 5.0% of the average fair value over the prior 20 quarters determined as of September 30, of the year preceding the planned distributions. Accordingly, over the long term, the Foundation expects current spending policy to allow its endowment assets to grow at an average rate of 3.0% annually. This is consistent with the Foundation's objectives to maintain the purchasing power of the endowment assets and to provide additional real growth through new gifts and investment return.

8. Fair Value

Investment Securities

Investment securities are recorded at fair value on a recurring basis. Fair value measurement is based on quoted market prices, if available. If quoted prices are not available, fair values are measured using independent pricing models or other model-based valuation techniques such as the present value of future cash flows, adjusted for the security's credit rating, prepayment assumptions and other factors such as credit loss and liquidity assumptions. Level 1 securities include those traded on an active exchange, such as the New York Stock Exchange, U.S. Treasury securities that are traded by dealers or brokers in active over-the-counter markets, publically traded mutual funds, and money market funds. Level 2 securities include mortgage-backed securities issued by government-sponsored entities, municipal bonds and corporate debt securities in active markets. The Foundation had no securities classified as level 3 at December 31, 2010 and 2009.

Midland Area Community Foundation

Notes to Financial Statements (continued)

8. Fair Value (continued)

Pledges Receivable

Pledges receivable, including patent rights, are recorded at fair value if expected to be collected in more than one year. Fair value represents the present value of estimated future cash flows. The fair value of the patent rights is calculated based on the present value of the estimated amount of the semi-annual payments to be received discounted at 4.25%.

Fair value measurements

Fair value measurements for money market funds reported as cash equivalents, the investment portfolio, and patent rights receivable, measured at fair value on a recurring basis, were as follows:

| | December 31, 2010 | | | |
|-----------------------|--------------------------|--|--|--|
| | Fair Value | Quoted Prices in Active Markets for Identical Assets/ Liabilities (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| Money market funds | \$ 1,323,433 | \$ 1,323,433 | \$ - | \$ - |
| Investment securities | 59,465,674 | 59,465,674 | - | - |
| Pledges receivable | 151,500 | - | - | 151,500 |
| | \$60,940,607 | \$ 60,789,107 | \$ - | \$ 151,500 |

| | December 31, 2009 | | | |
|-----------------------|--------------------------|--|--|--|
| | Fair Value | Quoted Prices in Active Markets for Identical Assets/ Liabilities (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| Money market funds | \$ 1,173,302 | \$ 1,173,302 | \$ - | \$ - |
| Investment securities | 51,737,150 | 51,737,150 | - | - |
| Pledges receivable | 222,150 | - | - | 222,150 |
| | \$53,132,602 | \$ 52,910,452 | \$ - | \$ 222,150 |