STATE BAR OF ARIZONA
AND THE CLIENT PROTECTION FUND
OF THE STATE BAR OF ARIZONA

CONSOLIDATED FINANCIAL STATEMENTS

Year Ended December 31, 2018

STATE BAR OF ARIZONA AND THE
CLIENT PROTECTION FUND OF THE STATE BAR OF ARIZONA

Year Ended December 31, 2018

CONTENTS

4722 North 24th Street, Suite 300 ■ Phoenix, AZ 85016
Main: 602.264.6835 ■ Fax: 602.265.7631 ■ www.mhmcpa.com

INDEPENDENT AUDITORS' REPORT

The Board of Governors and Trustees

STATE BAR OF ARIZONA AND
THE CLIENT PROTECTION FUND OF THE STATE BAR OF ARIZONA

Report on the Consolidated Financial Statements

We have audited the accompanying consolidated financial statements of ***State Bar of Arizona and the Client Protection Fund of the State Bar of Arizona*** (collectively referred to as "the Organization"), which comprise the consolidated statement of financial position as of December 31, 2018, and the related consolidated statements of activities, functional expenses and cash flows for the year then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated 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 consolidated 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 consolidated 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 consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated 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 consolidated 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 consolidated 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 consolidated financial statements referred to above present fairly, in all material respects, the financial position of ***State Bar of Arizona and the Client Protection Fund of the State Bar of Arizona*** as of December 31, 2018, and the changes in their net assets and cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Report on Supplementary Information

Our audit was performed for the purpose of forming an opinion on the consolidated financial statements as a whole. The consolidating statement of financial position and consolidating statement of activities are presented for the purpose of additional analysis of the consolidated financial statements, rather than to present the financial position, results of operation, and cash flows of the individual organizations, and is not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the consolidating information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

Emphasis of Matter

As discussed in Note 1 to the consolidated financial statements, ***State Bar of Arizona and the Client Protection Fund of the State Bar of Arizona*** adopted Financial Accounting Standards Update ("ASU") No. 2016-14, *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities*, in 2018. Our opinion is not modified with respect to this matter.

Mayer Hoffman McCann P.C.

May 3, 2019

STATE BAR OF ARIZONA AND THE
CLIENT PROTECTION FUND OF THE STATE BAR OF ARIZONA

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

December 31, 2018

ASSETS

CURRENT ASSETS	
Cash and cash equivalents	$ 6,308,554
Certificates of deposit	2,237,700
Accounts receivable, net	70,559
Inventories	84,818
Deferred rent - short term	12,480
Prepaid expenses and other assets	343,778
TOTAL CURRENT ASSETS	9,057,889
INVESTMENTS RESTRICTED FOR BENEFIT PLAN	376,760
OTHER ASSETS	93,017
DEFERRED RENT - LONG TERM	114,974
PROPERTY AND EQUIPMENT, net	10,758,100
TOTAL ASSETS	$ 20,400,740

LIABILITIES AND NET ASSETS

CURRENT LIABILITIES	
Accounts payable	$ 60,527
Property taxes payable	81,388
Accrued liabilities	1,447,610
Membership and Other Fees collected in advance	2,415,457
TOTAL CURRENT LIABILITIES	4,004,982
OTHER LIABILITIES	443,506
TOTAL LIABILITIES	4,448,488
NET ASSETS	
Net assets without donor restrictions	
Undesignated	9,328,302
Board designated	4,391,905
Statute designated	2,232,045
TOTAL NET ASSETS	15,952,252
TOTAL LIABILITES AND NET ASSETS	$ 20,400,740

See Notes to Consolidated Financial Statements

STATE BAR OF ARIZONA AND THE
CLIENT PROTECTION FUND OF THE STATE BAR OF ARIZONA

CONSOLIDATED STATEMENT OF ACTIVITIES

Year Ended December 31, 2018

SUPPORT AND REVENUE	
Membership Fees	
Active	$ 8,837,230
Inactive	1,144,245
Membership Fees penalties	428,950
Sections	318,330
Board of legal specializations	105,800
Admission on Motion	97,860
	10,932,415
PROGRAM SERVICE REVENUE	
Regulatory	
Judgement receipts	83,952
Professional services	58,508
Reinstatement fees	18,320
Trust account ethics program	6,600
Miscellaneous charges	20,610
	187,990
COMPLIANCE	
Board of legal specializations	51,525
Pro hac vice fees	419,636
Reinstatement Fees	10,100
Mandatory continuing legal education - late fees	420,039
Miscellaneous charges	300
	901,600
PROFESSIONAL DEVELOPMENT	
Continuing legal education	2,061,516
Convention	557,616
Publications	268,948
Advertising sales	819,891
Arizona attorney magazine	1,645
Sections meetings and conferences	203,151
Contributions and sponsorships	124,922
Membership benefits	70,308
Other miscellaneous	97,321
	4,205,318
ACCESS TO JUSTICE	
Lawyer referral services	19,050
CLIENT PROTECTION FUND	
Assessments	434,115
Restitution receipts	5,333
	439,448
OTHER REVENUE	
Rental Income	559,107
Interest and dividends	95,719
Loss on sale-disposal of assets	(12,582)
Other	5,976
TOTAL SUPPORT AND REVENUE	17,334,041
EXPENSES	
Program Services:	
Regulatory	6,031,574
Compliance	1,697,297
Professional Development	5,872,888
Access to Justice	595,168
Client Protection Fund	696,287
Total program services	14,893,214
Management and general	2,448,931
TOTAL EXPENSES	17,342,145
CHANGE IN NET ASSETS	(8,104)
NET ASSETS, BEGINNING OF YEAR	15,960,356
NET ASSETS, END OF YEAR	$ 15,952,252

See Notes to Consolidated Financial Statements

STATE BAR OF ARIZONA AND THE
CLIENT PROTECTION FUND OF THE STATE BAR OF ARIZONA

CONSOLIDATED STATEMENT OF FUNCTIONAL EXPENSES

Year Ended December 31, 2018

	Program Services							
	Regulatory	Compliance	Professional Development	Access to Justice	Client Protection Fund	Total Program Services	Management and General	Total
Salaries and wages	$ 3,193,930	$ 875,730	$ 2,025,980	$ 216,971	$ 101,741	$ 6,414,352	$ 1,164,891	$ 7,579,243
Employee benefits	518,684	157,925	356,088	37,864	15,791	1,086,352	242,616	1,328,968
Payroll taxes	239,261	66,394	152,158	16,708	7,792	482,313	83,616	565,929
Bank/credit card fees	110,136	52,001	171,699	12,077	-	345,913	269	346,182
Claims paid	-	-	-	-	547,907	547,907	-	547,907
Conferences, conventions and meetings	2,586	2,705	1,289,186	1,729	707	1,296,913	34,967	1,331,880
Contract labor	185,388	73,901	156,825	20,691	-	436,805	25,779	462,584
Contributions	60	22	5,092	104,137	-	109,311	-	109,311
Depreciation	269,063	106,640	217,721	30,159	-	623,583	193,802	817,385
Information technology	388,843	143,998	278,016	41,710	19	852,586	6,417	859,003
Legal fees	21,133	-	-	-	25	21,158	91,589	112,747
Member research tool	-	-	80,004	-	-	80,004	-	80,004
Occupancy	227,368	91,789	144,627	25,209	10,620	499,613	310,957	810,570
Office rxpense	132,020	81,766	502,469	20,219	2,626	739,100	10,046	749,146
Office of Presiding Disciplinary Judge	595,724	-	-	-	-	595,724	-	595,724
Professional services	38,020	13,146	250,226	53,527	896	355,815	76,989	432,804
Training and development	54,076	13,794	65,793	2,163	2,919	138,745	51,253	189,998
Other expenses	55,282	17,486	177,004	12,004	5,244	267,020	155,740	422,760
	$ 6,031,574	$ 1,697,297	$ 5,872,888	$ 595,168	$ 696,287	$ 14,893,214	$ 2,448,931	$ 17,342,145

See Notes to Consolidated Financial Statements

STATE BAR OF ARIZONA AND THE
CLIENT PROTECTION FUND OF THE STATE BAR OF ARIZONA

CONSOLIDATED STATEMENT OF CASH FLOWS

Year Ended December 31, 2018

CASH FLOWS FROM OPERATING ACTIVITIES	
Change in net assets	$ (8,104)
Adjustments to reconcile net assets to net cash from operating activities:	
Depreciation	817,385
Loss on sale-disposal of assets	12,582
Change in assets and liabilities	
Accounts receivable	(30,226)
Inventories	(2,095)
Prepaid expenses and other assets	112,605
Accounts payable	(349,598)
Property taxes payable	3,066
Accrued liabilities	35,882
Deferred rent	(47,255)
Membership and Other fees collected in advance	86,229
Other liabilities	(178,448)
Net cash from operating actitives	452,023
CASH FLOWS FOR INVESTING ACTIVITIES	
Purchases of property and equipment	(784,776)
Purchases of certificates of deposit	(2,397,820)
Redemptions of certificates of deposit	2,576,970
Net cash used in investing activities	(605,626)
NET CHANGE IN CASH AND CASH EQUIVALENTS	(153,603)
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	6,462,157
CASH AND CASH EQUIVALENTS, END OF YEAR	$ 6,308,554

(1) Principal business activity and significant accounting policies

Principal business activity - The State Bar of Arizona (SBA or State Bar) is an Arizona non-profit corporation formed in 1933 and operated under the supervision of the Arizona Supreme Court. SBA regulates approximately 18,750 active attorneys in Arizona and provides education and development programs for the legal profession and the public. The State Bar's mission states that it exists to serve and protect the public with respect to the provision of legal services and access to justice.

Regulatory - Pursuant to Rule 32 of the Supreme Court of Arizona, the State Bar of Arizona assists the Court with the regulation and discipline of persons engaged in the practice of law. The State Bar receives, screens, and investigates complaints against attorneys, which may be dismissed, require remedial action or lead to more formal proceedings resulting in various forms of discipline.

Compliance - Pursuant to Rule 32 of the Supreme Court of Arizona, the State Bar is charged with ensuring the competency of lawyers. Consistent with Rule 44, Legal Specialization, the State Bar administers a program through the Board of Legal Specialization in order to improve the quality of legal services. Additionally, in accordance with Rule 45, Mandatory Continuing Legal Education, the State Bar ensures active members complete required continuing legal education on an annual basis. The State Bar also assists in processing Pro Hac Vice Admissions under Rule 39 and processes In House Counsel registrations under Rule 38.

Professional Development - Pursuant to Rule 32 of the Supreme Court of Arizona, the State Bar is to conduct educational programs regarding substantive law, best practices, procedure and ethics and provide forums for discussion regarding the administration of justice and practice of law. The State Bar is also responsible for fostering ideals of integrity, learning, competence, and public service among attorneys and serve the professional needs of its members. The State Bar fosters professional development of attorneys through opportunities to serve on advisory groups, committees, sections, and task forces, and by providing continuing legal education, practice management assistance, legal resources and various other member services.

Access to Justice - Pursuant to Rule 32 of the Supreme Court of Arizona, the State Bar mission includes access to justice, which involves efforts to improve access to our legal system for all Arizonians. The Bar carries out this task through its Public Service Center by supporting various legal aid organizations, assisting with access to attorneys, working to educate the public about the legal process, and by supporting the Supreme Court's Access to Justice Commission.

Client Protection Fund - The Client Protection Fund of the State Bar of Arizona ("the CPF"): The CPF was established on January 7, 1961, by the Supreme Court of Arizona, pursuant to Arizona Revise Statutes Ct. 32(d)(8). The CPF is a trust that is an entity separate from the State Bar of Arizona but exists as part of the State Bar's business structure. Authority to revoke or amend the Declaration of Trust, which established the CPF, is delegated to the Board of Governors of the State Bar of Arizona. The Declaration of Trust was amended and restated in its entirety on December 13, 2013 and further amended on November 21, 2014 and September 29, 2017.

The purpose of the CPF is to promote the public confidence in the administration of justice and the integrity of the legal profession by reimbursing losses caused by the dishonest conduct of lawyers admitted and licensed to practice in Arizona, occurring in the course of the client-lawyer or fiduciary responsibility between the lawyer and the claimant.

(1) Principal business activity and significant accounting policies (continued)

Principles of consolidation - The consolidated financial statements include the accounts of State Bar of Arizona and the CPF because SBA has both control of and an economic interest in the CPF. All significant intercompany accounts and transactions have been eliminated in consolidation. Unless otherwise noted, these consolidated entities are hereinafter referred to as “the Organization”.

Basis of presentation - The Organization maintains its accounts in accordance with the principles and practices of fund accounting. Fund accounting classifies various resources in accordance with activities or objectives as specified, in accordance with regulations, restrictions, or limitations imposed by sources outside of the Organization, or in accordance with directions issued by the governing board.

Management's use of estimates - The preparation of consolidated financial statements in conformity with U.S. generally accepted accounting principles 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 consolidated financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash and cash equivalents - For purposes of the consolidated statement of cash flows, highly liquid investments with a maturity of three months or less at date of purchase are considered cash equivalents. No restricted cash balances existed at December 31, 2018.

The Organization maintains cash balances at various financial institutions. Deposits at each institution are insured in limited amounts by the Federal Deposit Insurance Corporation (FDIC) up to $250,000. The Organization has not experienced any loss in such accounts.

Accounts receivable - Accounts receivable consist of program service fees, all of which are due in less than one year and, accordingly, are presented as current assets in the accompanying consolidated financial statements. The Organization is exposed to certain credit risk. The Organization manages its risk by regularly reviewing its accounts and by providing appropriate allowances for uncollectible accounts. The Organization deems accounts over 90 days old to be past due. The Organization does not charge interest on late accounts. Accounts receivable are stated at the amount management expects to collect. Management provides for probable uncollectible amounts through a charge to revenue and a credit to the allowance for uncollectible accounts based on its assessment of the current status of individual balances. Balances that are still outstanding after management has used reasonable collection efforts are written off through a charge to the allowance for uncollectible accounts and a credit to accounts receivable.

Inventories - Inventories are measured at the lower of cost, determined on a first in, first out basis, or net realizable value. Net realizable value is the estimated selling price in the ordinary course of business, less reasonably predictable costs of completion, disposal, and transportation. As of December 31, 2018, inventories consisted of handbooks and textbooks for sale.

Investments - The Organization reports investments in equity securities that have readily determinable fair values, and all investments in debt securities, at fair value. The fair values of investments are based on quoted market prices. Investment income and gains and losses are recorded as increases or decreases in the statement of activities.

(1) Principal business activity and significant accounting policies (continued)

Property and equipment - Property and equipment additions $5,000 and above for building and improvements, $10,000 or above for tenant leasehold improvements, and $2,500 and above for all other additions, are recorded at cost, or if donated, at fair value on the date of donation. Depreciation is computed using the straight-line method over the estimated useful lives of the assets ranging from three to 40 years, or in the case of capitalized leased assets or leasehold improvements, the lesser of the useful life of the asset or the lease term. When assets are sold or otherwise disposed of, the cost and related depreciation are removed from the accounts, and any remaining gain or loss is included in the statement of activities. Costs of maintenance and repairs that do not improve or extend the useful lives of the respective assets are expensed currently.

The Organization reviews the carrying values of property and equipment for impairment whenever events or circumstances indicate that the carrying amount of an asset may not be recoverable. When considered impaired, an impairment loss is recognized to the extent carrying value exceeds the fair value of the asset. There were no indicators of asset impairment during the year ended December 31, 2018.

Membership and Other fees collected in advance - Membership fees are assessed in November for the following fiscal year. All such fees collected prior to the current year end are recorded as deferred revenue. Additionally, certain Continuing Learning Education (CLE) seminar registrations are opened in advance of the seminar. All such registration fees collected in advance are recorded as Membership and fees collected in advance. Deferred revenue is recognized as income in the year in which it is earned.

Net assets - Net assets, revenues, gains, and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, net assets and changes therein are classified and reported as follows:

Net Assets without Donor Restrictions - Net assets that are not subject to donor-imposed restrictions and may be expended for any purpose in performing the primary objectives of the Organization. These net assets may be used at the discretion of the Organization's management and board of governors.

Net Assets with Donor Restrictions - Net assets subject to stipulations imposed by donors, and grantors. Some donor restrictions are temporary in nature; those restrictions will be met by actions of the Organization or by the passage of time. Other donor restrictions are perpetual in nature, where by the donor has stipulated the funds be maintained in perpetuity. The Organization had no donor restricted net assets as of December 31, 2018.

Revenue recognition - The Organization's main source of revenues are membership fees, regulatory fees/assessments, compliance fees, revenue generated from professional development programs and events, and lawyer referral services. Membership fees are generally collected at the beginning of the membership year and recognized ratably over the year to which they pertain. Regulatory fees/assessments and compliance fees are recognized as paid. Revenue associated with professional development programs and events are recognized at the time the event occurs. Lawyer referral services are collected throughout the year as an annual fee which is recognized ratably over the year to which the fee pertains.

As of December 31, 2018 the CPF received a $20 annual assessment from each active and inactive member of the Organization. This is not part of the member's bar fees, but a separate assessment established by the Arizona Supreme Court. Assessments are recognized in the year for which they are assessed.

(1) Principal business activity and significant accounting policies (continued)

Contributions - Contributions received are recorded as net assets without donor restrictions or net assets with donor restrictions depending on the existence and/or nature of any donor-imposed restrictions. Contributions that are restricted by the donor are reported as an increase in net assets without donor restrictions if the restriction expires in the reporting period in which the contribution is recognized. All other donor restricted contributions are reported as an increase in net assets with donor restrictions, depending on the nature of restriction. When a restriction expires (that is, when a stipulated time restriction ends, or purpose restriction is accomplished), net assets with donor restrictions are reclassified to net assets without donor restrictions and reported in the statement of activities as net assets released from restrictions.

Donated materials and services - Donated materials and services are reflected as contributions in the accompanying consolidated financial statements at their estimated fair values as of the date of donation. Donated services are recognized as contributions if the services create or enhance nonfinancial assets, or require specialized skills performed by people with those skills, and would otherwise be purchased. The Organization utilizes and depends on the services of volunteers to perform a variety of tasks that assist the Organization with specific programs. The value of this contributed time is not reflected in these consolidated financial statements since the services did not require specialized skills and it was not susceptible to objective measurement.

Advertising and promotion costs - The Organization expenses advertising and promotion costs as incurred. Advertising and promotion expense for the year ended December 31, 2018 was $77,695.

Functional expense allocation - The costs of providing program and supporting services activities have been summarized on a functional basis in the consolidated statement of activities. The consolidated statement of functional expenses presents the natural classification detail of expense by function. Accordingly, certain departmental costs have been allocated among the programs and supporting services benefited by natural classification. Such allocations are determined by management on an equitable basis.

The departmental expenses that are allocated by natural classification include the following:

Expense	Method of Allocation
Occupancy	Square Footage
Information Technology	Full Time Equivalent
Office Support Services	Full Time Equivalent
Communications	Full Time Equivalent
Tucson support office	Full Time Equivalent

(1) Principal business activity and significant accounting policies (continued)

Income and certain excise taxes - SBA is organized as an Arizona non-profit corporation. The Internal Revenue Service has determined that SBA is exempt from federal income taxes under Section 501(a) of the Internal Revenue Code as an organization described in Section 501(c)(6). Management has determined the CPF is a grantor trust and as such it is disregarded entity treated as a division of SBA solely for income tax purposes. Accordingly, contributions to either organization do not qualify for the charitable contribution deduction under Section 170(b)(1)(A). The combined entity is annually required to file a Return of Organization Exempt from Income Tax (Form 990) with the IRS. In addition, the combined entity is generally subject to income tax on net income that is derived from business activities that are unrelated to their exempt purposes and it files an Exempt Organization Business Income Tax Return (IRS Form 990-T) and the Arizona equivalent (Form 99-T) to report its unrelated business taxable income.

SBA believes that it has appropriate support for any material income tax positions taken, and, as such, does not have any uncertain tax positions that are material to the consolidated the financial statements. SBA would recognize future accrued interest and penalties related to unrecognized tax benefits and liabilities in income tax expense if such interest and penalties are incurred. The Organization’s federal Form 990-T and Arizona Form 99-T are no longer subject to tax examination for years before 2015 and 2014, respectively.

Fair value measurements - The Organization’s significant financial instruments include investments, and deferred compensation plan assets. For these financial instruments, carrying values approximate fair value. FASB ASC 820-10, *Fair Value Measurement*, establishes a common definition for fair value to be applied to accounting principles generally accepted in the United States of America requiring the use of fair value, establishes a framework for measuring fair value, and expands disclosures about such fair value measurements. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction in the principal, or most advantageous, market at the measurement date under current market conditions regardless of whether that price is directly observable or estimated using another valuation technique. Inputs used to determine fair value refer broadly to the assumptions that market participants would use in pricing the asset including assumptions about risk. Inputs may be observable or unobservable. Observable inputs are inputs that reflect the assumptions market participants would use in pricing the asset or liability based on market data obtained from sources independent of the reporting entity. Unobservable inputs are inputs that reflect the reporting entity’s own assumptions about the assumptions market participants would use in pricing the asset or liability based on the best information available. A three-tier hierarchy categorizes the inputs as follows:

Level 1 **-** Quoted prices (unadjusted) in active markets for identical assets or liabilities that the Organization can access at the measurement date.

Level 2 **-** Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. These include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability, and market-corroborated inputs.

Level 3 **-** Unobservable inputs for the asset or liability. In these situations, the Organization develops inputs using the best information available in the circumstances.

In some cases, the inputs used to measure the fair value of an asset or a liability might be categorized within different levels of the fair value hierarchy. In those cases, the fair value measurement is categorized in its entirety in the same level of the fair value hierarchy as the lowest level input that is significant to the entire measurement.

(1) Principal business activity and significant accounting policies (continued)

Assessing the significance of a particular input to entire measurement requires judgment, taking into account factors specific to the asset or liability. The categorization of an asset within the hierarchy is based upon the pricing transparency of the asset and does not necessarily correspond to the Organization's assessment of the quality, risk or liquidity profile of the asset or liability.

All of the Organization's investment assets are classified within Level 1 because they are comprised of open-end mutual funds with readily determinable fair values based on daily redemption values.

Rental income - Commercial space is rented under long-term operating lease agreements and rent income related to commercial space is recorded on a straight-line basis. Rent income from tenants is recognized in the month in which it is earned rather than received. Any rent received prior to the month of occupancy is reported as prepaid rent. Tenant securities deposits are included in other long-term liabilities.

Recent accounting pronouncements - In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2014-09, Revenue from Contracts with Customers (Topic 606) that will supersede most current revenue recognition guidance, including industry-specific guidance. The core principle of the new guidance is that an entity will recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The standard provides a five-step analysis of transactions to determine when and how revenue is recognized. Other major provisions include the capitalization and amortization of certain contract costs, ensuring the time value of money is considered in the transaction price, and allowing estimates of variable consideration to be recognized before contingencies are resolved in certain circumstances. Additionally, the guidance requires disclosures related to the nature, amount, timing, and uncertainty of revenue that is recognized.

In August 2015, the FASB issued FASB ASU No. 2015-14, Revenue from Contracts with Customers (Topic 606), which changed the effective date of the provisions of FASB ASU No. 2014-09. As a result, the new effective dates for public business entities, certain not-for-profit entities, and certain employee benefit plans to apply the guidance in FASB ASU No. 2014-09 is for annual reporting periods beginning after December 15, 2017. All other entities should apply the guidance in FASB ASU No. 2014-09 to annual reporting periods beginning after December 15, 2018. Earlier application is permitted only as of annual reporting periods beginning after December 15, 2017. Transition to the new guidance may be done using either a full or modified retrospective method. The Organization is currently evaluating the effect the new guidance will have on the Organization's consolidated financial statements.

(1) Principal business activity and significant accounting policies (continued)

In February 2016, the Financial Accounting Standards Board issued Accounting Standards Update (ASU) 2016-02 to improve financial reporting about leasing transactions (Topic 842). The ASU affects all lease transactions. The Organization as a lessee is required to recognize a right-of-use asset and a lease liability, initially measured at present value of the lease payments, on the consolidated statement of financial position. For leases greater than twelve months, the Organization as a lessee must also recognize interest on the lease liability separately from amortization of the right-of-use asset in the consolidated statement of activities. Repayments of the principal portion of the lease liability must be classified within financing activities and payments of interest on the lease liability and variable lease payments within operating activities in the consolidated statement of cash flows. Leases for less than twelve months recognize a single lease cost on a straight-line basis. The amendments in this update are effective for years beginning after December 15, 2019. The Organization is currently evaluating the impact of adopting ASU 2016-02 and has not determined the effect to the consolidated financial statements. The standard requires a modified retrospective approach to implementation.

In August 2016, the Financial Accounting Standards Board issued Accounting Standards Update (ASU) 2016-14 to improve presentation of financial statements for not-for-profit entities. The ASU affects all not-for-profit entities. The main provisions of this Update that will impact the Organization include:

- Present on the face of the statement of financial position amounts for two classes of net assets at the end of the period, rather than for the previously required three classes. The not-for-profits will report amounts for net assets with donor restrictions and net assets without donor restrictions. They will also be required to present on the face of the statement of activities the amount of the change in each of the two classes of net assets rather than that of the currently required three classes.
- All not-for-profits will now be required to disclose an analysis of expenses by both functional and natural classifications.
- All not-for-profits will have to add disclosures regarding how they manage liquidity and information that communicates the availability of financial assets to meet cash needs for general expenditures.

The Organization has implemented ASU 2016-14 and has adjusted the presentation in these consolidated financial statements accordingly.

In accordance with the amendments of this ASU, the Organization elected to present expenses by function and nature as a separate statement of functional expenses. Disclosures around liquidity and availability of resources is included in Note 3.

Subsequent events - The Organization has evaluated subsequent events through May 3, 2019, which is the date the consolidated financial statements were available to be issued.

(2) Certificates of deposit

The CPF invests in the Certificate of Deposit Account Registry Service (“CDARS”). The CDARS program allows the Organization to purchase certificates of deposit, each within the applicable federal insurance limit, from participating U.S. banks. All certificates of deposit are recorded at amortized cost and are scheduled to mature in 2019.

(3) Liquidity and availability

Financial assets available for general expenditure, that is, without donor or other restrictions limiting their use, within one year of the balance sheet date are as follows:

Financial assets at year-end:	
Cash and cash equivalents	$ 6,308,554
Certificates of deposit	2,237,700
Accounts receivable, net	70,559
Total financial assets	8,616,813
Less:	
Board-designated funds	4,391,905
Statute designated funds	2,232,045
	6,623,950
Financial assets available to meet general expenditures Over the next twelve months	$ 1,992,863

As part of the Organization's liquidity management, it has a policy to structure its financial assets to be available as its general expenditures, liabilities, and other obligations come due. To help manage unanticipated liquidity needs, the Organization has a revolving line of credit of $4,000,000, which it could draw upon. Additionally, the Organization had Board-designated net assets without donor restrictions that, while the Organization does not intend to spend for these purposes, the amounts could be made available for current operations, if necessary.

(4) Fair value measurements and disclosures

The following table presents assets measured at fair value on a recurring basis at December 31, 2018.

		Fair Value Measurements At Report Date Using		
	Total	Quoted Prices In Active Markets for Identical Assets **Level 1**	Significant Other Observable Inputs **Level 2**	Significant Unobservable Inputs **Level 3**
Assets				
Equity securities for benefit plan	$ 376,760	$ 376,760	$ -	$ -

(5) Property and equipment

Property and equipment consisted of the following at December 31, 2018:

Land	$ 1,753,943
Land improvements	116,195
Buildings	7,739,696
Building improvements	4,937,840
Furniture and equipment	2,038,270
Computer hardware	939,007
Computer software	459,918
Total cost or donated value	17,984,869
Accumulated depreciation	(7,226,769)
Property and equipment, net	$ 10,758,100

(6) Line of credit

SBA has a $4,000,000 revolving line of credit with a financial institution which expires in August 2019. The line of credit bears interest at LIBOR + 1.50% (3.85% at December 31, 2018). This line of credit is collateralized by a first deed of trust, together with an assignment of rents and leases on real property and improvements. No interest expense was incurred during 2018. There were no amounts outstanding on the line of credit as of December 31, 2018.

(7) Net assets

Each of the Organization's 31 sections charges separate fees and may only spend out of their current year income or their cumulative surplus, if any. The remaining balances are designated by the Organization's Board of Governors for that specific section. The section carryover totaled $559,273 for the year ended December 31, 2018.

The Board of Directors adopted a cash reserve policy during the year ended December 31, 2017 and 2016. Under this new policy $3,832,632 as of December 31, 2018, has been designated and allocated between Membership Fees Reserve and Capital Projects Reserves.

Additionally, the net assets of the CPF are designated by Arizona State Statue to only be used for the purposes of the CPF as set forth in the trust agreement and per statute mandate.

(8) Leasing activities

The Organization leases office space to the Arizona Foundation for Legal Services & Education (the "Foundation") under an operating lease agreement. During 2017 the Foundation down-sized from 8,027 square feet to 4,962 square feet effective November 15, 2017. A new operating lease agreement was entered into during 2017 with a lease commencement date of February 1, 2018 ending on January 31, 2028 for the 4,962 square feet currently occupied. In addition to this lease agreement, the State Bar has a memorandum of understanding in which the State Bar donates 1% of membership fees collected to the Foundation. This donation is required to be utilized to implement pro bono legal service programs and promote pro bono involvement with legal services. For 2018, $55,000 of the contribution to the Foundation was utilized as a reduction of rent from the Foundation to the Organization. For years beginning 2019 and forward, the reduction of rent are expected to be $60,000 annually, to be adjusted based on the actual membership fees collected. Minimum future rental payments to be received under this lease including the above referenced in-kind reductions at December 31, 2018 are approximately as follows:

Years ending December 31,		
2019	$	94,278
2020		94,278
2021		94,278
2022		94,278
2023		96,552
Thereafter		395,099
Total minimum lease receipts	$	868,763

The Organization also leases office space to unrelated third parties. The lease terms call for monthly payments of approximately $27,000, maturing through January 2028. Minimum future rental payments to be received on these non-cancelable leases at December 31, 2018 are approximately as follows:

Years ending December 31,		
2019	$	323,233
2020		296,752
2021		248,107
2022		185,020
Thereafter		11,728
Total minimum lease receipts	$	1,064,840

(9) Leasing commitments

The Organization leases offsite storage and convention and meeting facilities with varying minimum annual payments under non-cancelable lease agreements. Lease expense under these agreements was $56,919 during the year ended December 31, 2018. Future minimum lease payments under operating leases are due as follows:

Years ending December 31,		
2019	$	47,795
2020		20,447
Total minimum lease payments	$	68,242

(10) Retirement plans

Defined contribution plan - SBA sponsors a defined contribution plan (the Plan) qualified under Section 401(k) of the Internal Revenue Code covering substantially all employees who meet specified age and years of service requirements. SBA may make discretionary contributions on behalf of participants. This plan was restated as of January 1, 2015. The entry date was changed from the January 1 and July 1 following when the employee had satisfied the eligibility requirements, to the first day of the month following the date the employee satisfies eligibility requirements. The plan now includes an automatic deferral feature and adopted a safe harbor plan. Under the safe harbor election SBA is required to make safe harbor matching contributions equal to 100% of the salary deferrals that do not exceed 1% of the employee's compensation plus 50% of the employee's salary deferrals between 1% and 6% of compensation. The safe harbor matching contribution is subject to a different vesting schedule from the employer discretionary non-elective contributions to the plan. The vesting schedule for the employer qualified safe harbor contributions is 0% for one year of service or less and 100% for two years of service or more.

Deferred compensation plan - The Organization sponsors a non-qualified deferred compensation plan (the Non-Qualified 457b Plan) for top management employees. This plan allows for deferral of employee salary, as well as discretionary contributions from SBA. Participant contributions are fully vested upon funding. Discretionary employer contributions are made in the first quarter of each fiscal year and fully vest on June 30 of the same year. As of December 31, 2018, all contributions to this plan are fully vested. This plan was restated as of January 1, 2015, and maintains all qualities and characteristics with the exception employees are divided between two tiers with only the top tier eligible to benefit from discretionary employer contributions, and that vesting is achieved over the employee's period of service. The liability related to the plan totaled approximately $376,760 at December 31, 2018, and is included in other liabilities on the consolidated statements of financial position.

Total expense related to these two retirement plans was $520,304 for the year ended December 31, 2018.

(11) Related parties

SBA appoints six of the 25 members of the Board of Directors for the Foundation. Transactions with the Foundation include the following for the year ended December 31:

In-kind expense - rent (see Note 8)	$	55,000
In-kind advertising revenue		5,110
Accounts payable		35,671
Rental income - straight line (see Note 8 – includes common area maintenance recovery)		157,363
Expenses (cash paid - 1% ProBono & Mock Trial)		60,021

(12) Contingencies

From time to time, the Organization may become involved in various legal proceedings. In the opinion of management, any liability resulting from such proceedings would not have a material adverse effect on the consolidated financial statements.

(13) Commitments

As of December 31, 2018, SBA had signed various contracts with convention locations for future years. These contracts include minimum revenue guarantees and are subject to a cancellation fee if terminated early. The following is a summary of approximate future minimum guaranteed payments under these contracts:
Years ending December 31,

2019	$ 663,851
2020	593,779
2021	9,355
Total minimum payments	$ 1,266,985

Subsequent to year end, the Organization entered into a contract for the 2021 convention location with an approximate future minimum guaranteed payment of $157,200.

SUPPLEMENTARY INFORMATION

STATE BAR OF ARIZONA AND THE
CLIENT PROTECTION FUND OF THE STATE BAR OF ARIZONA

SUPPLEMENTAL INFORMATION

CONSOLIDATING STATEMENT OF FINANCIAL POSITION

December 31, 2018

A S S E T S	**SBA**	**CPF**	**Eliminations**	**Total**
CURRENT ASSETS				
Cash and cash equivalents	$ 6,285,063	$ 23,491	$ -	$ 6,308,554
Certificates of deposit		2,237,700	-	2,237,700
Accounts receivable, net	102,575	86,790	(118,806)	70,559
Inventories	84,818	-	-	84,818
Deferred rent - short term	12,480	-	-	12,480
Prepaid expenses and other assets	343,778	-	-	343,778
TOTAL CURRENT ASSETS	6,828,714	2,347,981	(118,806)	9,057,889
INVESTMENTS RESTRICTED FOR BENEFIT PLAN	376,760	-	-	376,760
OTHER ASSETS	93,017	-	-	93,017
DEFERRED RENT - LONG TERM	114,974	-	-	114,974
PROPERTY AND EQUIPMENT, net	10,758,100	-	-	10,758,100
TOTAL ASSETS	$ 18,171,565	$ 2,347,981	$ (118,806)	$ 20,400,740
CURRENT LIABILITIES				
Accounts payable	$ 147,317	$ 32,016	$ (118,806)	$ 60,527
Property taxes payable	81,388	-	-	81,388
Accrued liabilities	1,447,610	-	-	1,447,610
Membership and Other fees collected in advance	2,331,537	83,920	-	2,415,457
TOTAL CURRENT LIABILITIES	4,007,852	115,936	(118,806)	4,004,982
LONG-TERM LIABILITIES				
Other liabilities	443,506	-	-	443,506
TOTAL LIABILITIES	4,451,358	115,936	(118,806)	4,448,488
NET ASSETS				
Net assets without donor restrictions				
Undesignated	9,328,302	-	-	9,328,302
Board designated	4,391,905	-	-	4,391,905
Statute designated	-	2,232,045	-	2,232,045
TOTAL NET ASSETS	13,720,207	2,232,045	-	15,952,252
TOTAL LIABILITIES AND NET ASSETS	$ 18,171,565	$ 2,347,981	$ (118,806)	$ 20,400,740

STATE BAR OF ARIZONA AND THE
CLIENT PROTECTION FUND OF THE STATE BAR OF ARIZONA

SUPPLEMENTAL INFORMATION

CONSOLIDATING STATEMENT OF ACTIVITIES

Year Ended December 31, 2018

	SBA	CPF	Eliminations	Total
SUPPORT AND REVENUE				
Membership fees				
Active	$ 8,837,230	$ -	$ -	$ 8,837,230
Inactive	1,144,245	-	-	1,144,245
Membership fees penalties	428,950	-	-	428,950
Sections	318,330	-	-	318,330
Board of legal specializations	105,800	-	-	105,800
Admission on Motion	97,860	-	-	97,860
	10,932,415	-	-	10,932,415
PROGRAM SERVICE REVENUE				
Regulatory				
Judgement receipts	83,952	-	-	83,952
Professional services	58,508	-	-	58,508
Reinstatement fees	18,320	-	-	18,320
Trust account ethics program	6,600	-	-	6,600
Miscellaneous charges	20,610	-	-	20,610
	187,990	-	-	187,990
COMPLIANCE				
Board of legal specializations	51,525	-	-	51,525
Legal Services	147,484	-	(147,484)	-
Pro hac vice fees	419,636	-	-	419,636
Reinstatement Fees	10,100	-	-	10,100
Mandatory continuing legal education - late fees	420,039	-	-	420,039
Miscellaneous charges	300	-	-	300
	1,049,084	-	(147,484)	901,600
PROFESSIONAL DEVELOPMENT				
Continuing legal education	2,061,516	-	-	2,061,516
Convention	557,616	-	-	557,616
Publications	268,948	-	-	268,948
Advertising sales	819,891	-	-	819,891
Arizona attorney magazine	1,645	-	-	1,645
Sections meetings and conferences	203,151	-	-	203,151
Contributions and sponsorships	124,922	-	-	124,922
Membership benefits	70,308	-	-	70,308
Other miscellaneous	97,321	-	-	97,321
	4,205,318	-	-	4,205,318
ACCESS TO JUSTICE				
Lawyer referral services	19,050	-	-	19,050
CLIENT PROTECTIONS FUND				
Assessments	-	434,115	-	434,115
Restitution receipts	-	5,333	-	5,333
	-	439,448	-	439,448
Rental Income	556,583	-	2,524	559,107
Interest and dividends	74,550	21,169	-	95,719
Loss on sale-disposal of assets	(12,582)	-	-	(12,582)
Other	5,976	-	-	5,976
TOTAL SUPPORT AND REVENUE	17,018,384	460,617	(144,960)	17,334,041
EXPENSES				
Program Services:				
Regulatory	6,031,574	-	-	6,031,574
Compliance	1,697,297	-	-	1,697,297
Professional Development	5,872,888	-	-	5,872,888
Access to Justice	595,168	-	-	595,168
Client Protection Fund	136,864	696,287	(136,864)	696,287
Total program services	14,333,791	696,287	(136,864)	14,893,214
Management and general	2,457,027	-	(8,096)	2,448,931
TOTAL EXPENSES	16,790,818	696,287	(144,960)	17,342,145
CHANGE IN NET ASSETS	227,566	(235,670)	-	(8,104)
NET ASSETS, BEGINNING OF YEAR	13,492,641	2,467,715	-	15,960,356
NET ASSETS, END OF YEAR	$ 13,720,207	$ 2,232,045	$ -	$ 15,952,252

See Independent Auditors' Report