



**AMERICAN COUNCIL ON EXERCISE**

**INDEPENDENT AUDITOR'S REPORTS**

**AND**

**FINANCIAL STATEMENTS**

**WITH ADDITIONAL INFORMATION**

**JUNE 30, 2006 AND 2005**

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## INDEPENDENT AUDITOR'S REPORT ON THE FINANCIAL STATEMENTS

Board of Directors  
American Council on Exercise

We have audited the accompanying statements of financial position of American Council on Exercise as of June 30, 2006 and 2005, and the related statements of activities and cash flows for the years then ended. These financial statements are the responsibility of American Council on Exercise's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free 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 audits provide 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 American Council on Exercise as of June 30, 2006 and 2005, and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

*Moss Adams LLP*

San Diego, California  
August 25, 2006

# AMERICAN COUNCIL ON EXERCISE

## STATEMENTS OF FINANCIAL POSITION JUNE 30, 2006 AND 2005

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	2006	2005
<b>ASSETS</b>		
<b>Current Assets</b>		
Cash and cash equivalents	\$ 2,148,737	\$ 2,692,221
Investments	593,538	960,151
Accounts receivable	17,410	26,059
Inventory	319,632	404,885
Deferred and prepaid expenses and other assets, current portion	<u>232,120</u>	<u>253,535</u>
Total current assets	3,311,437	4,336,851
<b>Fixed Assets</b>	4,220,893	4,398,040
<b>Deferred and Prepaid Expenses and Other Assets,</b> long-term portion	<u>211,171</u>	<u>111,111</u>
Total assets	<u>\$ 7,743,501</u>	<u>\$ 8,846,002</u>
<b>LIABILITIES AND NET ASSETS</b>		
<b>Current Liabilities</b>		
Accounts payable and accrued expenses	\$ 680,386	\$ 591,117
Note payable and capital lease, current portion	70,198	109,497
Deferred revenue	<u>355,340</u>	<u>439,308</u>
Total current liabilities	1,105,924	1,139,922
<b>Note Payable and Capital Lease, long-term portion</b>	<u>1,137,075</u>	<u>2,807,677</u>
Total liabilities	2,242,999	3,947,599
<b>Commitments and Contingency (Note 7)</b>		
<b>Unrestricted Net Assets</b>	<u>5,500,502</u>	<u>4,898,403</u>
Total liabilities and net assets	<u>\$ 7,743,501</u>	<u>\$ 8,846,002</u>

# AMERICAN COUNCIL ON EXERCISE

## STATEMENTS OF ACTIVITIES YEARS ENDED JUNE 30, 2006 AND 2005

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	2006	2005
<b>REVENUE AND SUPPORT</b>		
Educational materials and training manuals	\$ 3,640,487	\$ 3,699,358
Certification fees	2,143,040	2,028,715
Instructors renewal fees	1,412,487	1,418,294
Continuing education fees	1,259,863	998,247
Shipping and handling	330,250	283,984
Mailing lists rentals	121,296	125,942
Royalties	119,346	132,401
Interest and dividends	75,113	34,306
Membership fees	31,651	36,592
Other	3,815	3,491
Professional registry	2,475	2,825
Contributions	856	3,803
Donated equipment	-	154,117
Grants	-	7,900
Total revenue and support	<u>9,140,679</u>	<u>8,929,975</u>
<b>EXPENSES</b>		
Program	6,924,636	6,839,764
General and administrative	<u>1,677,564</u>	<u>1,665,764</u>
Total expenses	<u>8,602,200</u>	<u>8,505,528</u>
Excess of revenue over expenses	538,479	424,447
<b>NET INVESTMENT GAINS</b>	<u>63,620</u>	<u>64,792</u>
<b>INCREASE IN UNRESTRICTED NET ASSETS</b>	602,099	489,239
<b>UNRESTRICTED NET ASSETS</b>		
Beginning of year	<u>4,898,403</u>	<u>4,409,164</u>
End of year	<u>\$ 5,500,502</u>	<u>\$ 4,898,403</u>

# AMERICAN COUNCIL ON EXERCISE

## STATEMENTS OF CASH FLOWS YEARS ENDED JUNE 30, 2006 AND 2005

	2006	2005
<b>OPERATING ACTIVITIES</b>		
Change in net assets	\$ 602,099	\$ 489,239
Adjustments to reconcile change in net assets to net cash from operating activities:		
Depreciation and amortization	369,104	371,944
Loss on disposal of equipment	1,859	-
Realized and unrealized (gains) on investments	(63,620)	(64,792)
(Increase) decrease in operating assets		
Accounts receivable	8,649	11,769
Inventory	85,253	(103,033)
Deferred and prepaid expenses and other assets	(78,645)	(110,193)
Increase (decrease) in operating liabilities		
Accounts payable and accrued expenses	89,269	(73,732)
Deferred revenue	(83,968)	96,996
Net cash provided by operating activities	<u>930,000</u>	<u>618,198</u>
<b>INVESTING ACTIVITIES</b>		
Purchases of fixed assets	(193,816)	(211,469)
Proceeds from sales of investments	1,076,484	11,692
Purchases of investments	(646,251)	-
Net cash provided by (used in) investing activities	<u>236,417</u>	<u>(199,777)</u>
<b>FINANCING ACTIVITIES</b>		
Payments on note payable	(1,693,099)	(122,352)
Payments on capital lease	(16,802)	(14,920)
Net cash (used in) financing activities	<u>(1,709,901)</u>	<u>(137,272)</u>
<b>(DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS</b>	(543,484)	281,149
<b>CASH AND CASH EQUIVALENTS</b>		
Beginning of year	<u>2,692,221</u>	<u>2,411,072</u>
End of year	<u>\$ 2,148,737</u>	<u>\$ 2,692,221</u>
<b>SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION</b>		
Cash payments for interest	<u>\$ 126,238</u>	<u>\$ 114,827</u>

# AMERICAN COUNCIL ON EXERCISE

## NOTES TO FINANCIAL STATEMENTS

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### Note 1 – Nature of Organization and Significant Accounting Policies

American Council on Exercise (ACE), incorporated under the laws of the state of California in 1985, is a not-for-profit organization committed to enriching quality of life through safe and effective physical activity. ACE protects all segments of society against ineffective fitness products, programs, and trends through its on-going public education, outreach, and research. ACE further protects the public by setting certification and continuing education standards for fitness professionals.

**Income Tax Status** - ACE is exempt from income taxes under Section 501(c)(3) of the Internal Revenue Code and Section 23701(d) of the California Revenue and Taxation Code.

**Method of Accounting** - The financial statements of ACE are prepared on the accrual basis of accounting.

**Financial Statement Presentation** - ACE follows Financial Accounting Standards Board Statement (FASB) Statement No. 117, "Financial Statements of Non-Profit Organizations," for presentation of its financial statements which requires that net assets and revenue, gains, expenses and losses be classified as unrestricted, temporarily restricted, and permanently restricted as follows:

- Unrestricted net assets represent expendable funds available for operations that are not otherwise limited by donor restrictions.
- Temporarily restricted net assets consist of contributed funds, subject to specific donor-imposed restrictions, contingent upon a specific performance of a future event or a specific passage of time before ACE may spend the funds. At June 30, 2006 and 2005, ACE did not have any temporarily restricted net assets.
- Permanently restricted net assets are subject to irrevocable donor restrictions, requiring that the assets be maintained in perpetuity, usually for the purpose of generating investment income to fund current operations. At June 30, 2006 and 2005, ACE did not have any permanently restricted net assets.

### Revenue Recognition

**Revenue** - ACE derives revenue from the following:

- Publishing and selling various educational and training manuals for exercise professionals (recognized as manuals are sold)
- Fees charged for taking certification examinations (recognized as exams are administered)
- Certification renewal fees for exercise professionals (recognized as renewals are processed)
- Processing fees for continuing education quizzes (recognized as quizzes are processed)
- Shipping and handling of materials purchased (recognized as materials are shipped)
- Mailing list rentals (recognized when lists are rented)
- Royalties (recognized as earned)
- Memberships (recognized as memberships are renewed)

# AMERICAN COUNCIL ON EXERCISE

## NOTES TO FINANCIAL STATEMENTS

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### Note 1 – Nature of Organization and Significant Accounting Policies (Continued)

#### Revenue Recognition (Continued)

**Contributions** - Contributions are recognized as support when received or unconditionally pledged. Contributions subject to donor-imposed restrictions for use in a future period or for a specific purpose are reported as either temporarily or permanently restricted, depending on the nature of the donor's restriction. When a donor restriction expires, temporarily restricted net assets are reclassified to unrestricted net assets, and reported in the statement of activities as net assets released from restrictions. Donor-restricted contributions, whose restrictions are met in the same reporting period, are reported as unrestricted contributions.

**Donated Equipment** – Donated equipment is recorded at its estimated fair value at the date of contribution.

**Grants** - Revenue from grants is recognized to the extent of eligible costs incurred, up to the maximum grant amount.

**Cash and Cash Equivalents** - Cash and cash equivalents include highly liquid investments with an original maturity of three months or less.

**Investments** - Investments in marketable securities with readily determinable fair values and all investments in debt securities are reported at their fair value in the statements of financial position. Realized and unrealized gains and losses are included in the change in net assets in the statements of activities.

**Accounts Receivable** - Credit terms for payment of products and services purchased are extended to customers in the normal course of business and no collateral is required. The allowance for estimated uncollectible accounts is based on past experience and on analysis of current accounts receivable. Accounts deemed uncollectible are written-off in the year deemed uncollectible. For the years ended June 30, 2006 and 2005, management has determined that an allowance is not required.

**Inventory** - Inventory, which consists principally of training manuals and merchandise, is valued at lower-of-cost or market, using the first-in/first-out method (FIFO).

**Deferred Expenses** - Deferred expenses are costs associated with content development, pre-production, typesetting, artwork, design, promotion, and color separation of manuals. Accumulated costs are expensed over the estimated marketable life of the manuals.

**Fixed Assets** - ACE capitalizes fixed assets that cost greater than \$500. Furniture, equipment, computer software, website and database development, and leasehold improvements are recorded at cost and depreciated on the straight-line basis over the estimated useful lives of the assets, generally 3 to 5 years. The building was recorded at cost and is being depreciated over 30 years.

**Impairment of Long-lived Assets** - ACE evaluates long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying value of an asset may not be recoverable. If the estimated future cash flows (undiscounted and without interest charges) from the use of an asset is less than the carrying value, a write-down would be recorded to reduce the related asset to its estimated fair value. To date, no such write-downs have occurred.

# AMERICAN COUNCIL ON EXERCISE

## NOTES TO FINANCIAL STATEMENTS

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### Note 1 – Nature of Organization and Significant Accounting Policies (Continued)

**Deferred Revenue** – Deferred revenue represents fees received in advance for exams and training.

**Advertising** – Advertising costs are expensed as incurred.

**Shipping and Handling Costs** – Shipping and handling costs are expensed as incurred and are primarily included in program expenses.

**Functional Allocation of Expenses** - The costs of providing ACE's programs and other activities have been summarized on a functional basis in the statements of activities. Accordingly, certain costs have been allocated among the programs and supporting services benefited.

**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.

### Note 2 – Concentration of Credit Risk

Financial instruments which potentially subject ACE to credit risk consist primarily of cash and cash equivalents and investments.

**Cash and Cash Equivalents** - ACE maintains its cash and cash equivalents in bank accounts which exceed federally insured deposit limits. ACE has not experienced any losses in such accounts, and believes it is not exposed to any significant credit risk on its cash and cash equivalents.

**Investments** - Investments are exposed to various risks, such as interest rates, market, and credit risk. It is at least reasonably possible given the level of risk associated with investments that changes in the near term could materially affect the amounts reported in the financial statements.

### Note 3 - Investments

Investments, at fair value, are summarized as follows at June 30:

	<b>2006</b>	<b>2005</b>
Mutual funds	\$ 593,538	\$ 953,032
Common stock	-	7,119
	<u>\$ 593,538</u>	<u>\$ 960,151</u>

### Note 4 – Deferred and Prepaid Expenses and Other Assets

Deferred and prepaid expenses and other assets are summarized as follows at June 30:

Deferred expenses	\$ 326,429	\$ 211,844
Prepaid expenses	<u>116,862</u>	<u>152,802</u>
	443,291	364,646
Less current portion	<u>(232,120)</u>	<u>(253,535)</u>
	<u>\$ 211,171</u>	<u>\$ 111,111</u>

# AMERICAN COUNCIL ON EXERCISE

## NOTES TO FINANCIAL STATEMENTS

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### Note 5 – Fixed Assets

At June 30, fixed assets consist of:

	<b>2006</b>	<b>2005</b>
Land	\$ 1,286,883	\$ 1,286,883
Building	3,113,744	3,113,744
Equipment	877,755	810,872
Website and database development	583,898	498,962
Furniture (including \$79,963 of fixed assets acquired under capital lease in 2006 and 2005) (Note 6)	362,434	350,822
Computer software	350,063	322,465
Leasehold improvements	34,089	34,089
Vehicle	<u>8,475</u>	<u>8,475</u>
	6,617,341	6,426,312
Less accumulated depreciation (including accumulated amortization on fixed assets acquired under capital lease of \$71,967 and \$55,974 in 2006 and 2005, respectively)	<u>2,396,448</u>	<u>2,028,272</u>
	<u>\$ 4,220,893</u>	<u>\$ 4,398,040</u>

### Note 6 – Note Payable and Capital Lease

At June 30, note payable and capital lease consists of:

Note payable, bank, due in monthly principal and interest payments of \$10,250 at 6.51 percent, balloon payment of approximately \$891,000, due January 2012, secured by deed of trust on land and building	\$ 1,198,657	\$ 2,891,756
Capital lease payable, finance company, payable in monthly lease payments of \$1,450 at 3.4 percent through December 2006, secured by furniture	<u>8,616</u>	<u>25,418</u>
	1,207,273	2,917,174
Less current maturities	<u>(70,198)</u>	<u>(109,497)</u>
	<u>\$ 1,137,075</u>	<u>\$ 2,807,677</u>

# AMERICAN COUNCIL ON EXERCISE

## NOTES TO FINANCIAL STATEMENTS

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### Note 6 – Note Payable and Capital Lease (Continued)

Payments on the note payable and capital lease are due as follows:

	<u>Note Payable</u>	<u>Capital Lease</u>	<u>Total</u>
Years ending June 30,			
2007	\$ 61,497	\$ 8,701	\$ 70,198
2008	61,497	-	61,497
2009	61,497	-	61,497
2010	61,497	-	61,497
2011	61,497	-	61,497
Thereafter	<u>891,172</u>	<u>-</u>	<u>891,172</u>
Total	1,198,657	8,701	1,207,358
Less amount representing interest	<u>-</u>	<u>(85)</u>	<u>(85)</u>
Present value of future minimum lease payments and note payable	<u>\$ 1,198,657</u>	<u>\$ 8,616</u>	<u>\$ 1,207,273</u>

Total interest expense was approximately \$126,000 and \$115,000 for the years ended June 30, 2006 and 2005, respectively.

### Note 7 – Commitments and Contingency

**Operating Leases** – ACE has a month-to-month lease for an off-site storage facility. In addition, ACE has one operating lease for computers which expires in January 2007.

The minimum annual payments remaining under the operating leases is \$5,100 for the year ended June 30, 2007.

Rent expense for the years ended June 30, 2006 and 2005 was approximately \$36,000 and \$53,000, respectively.

**Line of Credit** – ACE has an unused line of credit with a bank with a maximum borrowing amount of \$500,000. The line matures on January 31, 2007 and bears interest at the bank's specified reference rate plus one percent. The line is secured by all of ACE's assets excluding land and building.

**Certification, Administration, and Development** - ACE has an agreement that expires in March 2007 with an organization that provides assistance in the development and administration of personal trainers, group fitness instructors, clinical exercise specialists, and life weight management consultant certification tests. Fees paid under this agreement for the years ended June 30, 2006 and 2005 were approximately \$594,000 and \$595,000, respectively.

# AMERICAN COUNCIL ON EXERCISE

## NOTES TO FINANCIAL STATEMENTS

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### **Note 7 – Commitments and Contingency (Continued)**

**Retirement Plan** – ACE has a 401(k) plan (Plan) which covers all full-time employees after one year of employment. Employees can defer up to 20 percent of their gross wages into the Plan. Employees also receive a 25 percent employer match for the first 8 percent of salary deferral, which vests evenly over 5 years. For the years ended June 30, 2006 and 2005, ACE contributed approximately \$24,000 and \$37,000 to the Plan, respectively.

**Trademark Matters** - ACE operates under a trademark and, at times, must defend its rights by filing for an administrative proceeding before the Trademark Trial and Appeals Board, a unit of the U.S. Patent and Trademark office.

### **Note 8 – June 30, 2005 Financial Information**

Certain amounts in the June 30, 2005 financial statements have been reclassified to conform to the June 30, 2006 presentation with no effect on total net assets.

**ADDITIONAL INFORMATION**

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## INDEPENDENT AUDITOR'S REPORT ON THE ADDITIONAL INFORMATION

Board of Directors  
American Council on Exercise

Our audit was made for the purpose of forming an opinion on the basic financial statements taken as a whole. The statement of functional expenses that follows on page 12 is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

*Moss Adams LLP*

San Diego, California  
August 25, 2006

# AMERICAN COUNCIL ON EXERCISE

## ADDITIONAL INFORMATION STATEMENT OF FUNCTIONAL EXPENSES

YEAR ENDED JUNE 30, 2006

(With Summarized Financial Information for Year Ended June 30, 2005)

	2006			2005 Total
	Program	General and Administrative	Total	
Salaries and wages	\$ 2,129,398	\$ 838,070	\$ 2,967,468	\$ 3,084,941
Educational materials and training materials	930,211	-	930,211	832,655
Postage, shipping and handling	593,594	3,918	597,512	631,192
Testing services	594,180	-	594,180	594,950
Marketing	530,549	27,236	557,785	325,663
Depreciation and amortization	242,388	126,716	369,104	371,944
Printing, photography, and production	318,937	-	318,937	311,999
Advertising and promotion	237,945	5,872	243,817	199,700
Meetings	140,119	96,178	236,297	199,521
Insurance	157,693	73,343	231,036	267,783
Payroll taxes	167,834	45,778	213,612	222,599
Travel	179,330	24,074	203,404	203,005
Merchant fees	173,054	-	173,054	175,349
Interest	88,367	37,871	126,238	114,827
Events and trade shows	119,831	-	119,831	126,427
Professional development and dues	57,658	49,507	107,165	62,416
Repairs, maintenance, and janitorial services	65,386	29,299	94,685	83,087
Legal and accounting	-	94,074	94,074	89,143
Recruitment	-	88,071	88,071	5,523
Utilities	36,240	15,531	51,771	54,367
Telephone	36,055	15,452	51,507	53,164
Fulfillment	47,843	-	47,843	48,785
Miscellaneous	6,026	31,083	37,109	31,223
Office and computer supplies	17,102	18,413	35,515	47,321
Entertainment	5,327	23,125	28,452	26,990
Computer leases	16,170	8,707	24,877	48,917
401(k) contribution	16,724	7,167	23,891	37,280
Copying and duplication	12,913	5,534	18,447	20,347
Building rent	-	8,761	8,761	1,333
Fitness equipment purchases	3,762	-	3,762	69,992
Property taxes	-	1,830	1,830	-
Temporary wages	-	1,266	1,266	6,880
Bad debt	-	688	688	2,089
Contributions of fitness equipment	-	-	-	154,117
	<u>\$ 6,924,636</u>	<u>\$ 1,677,564</u>	<u>\$ 8,602,200</u>	<u>\$ 8,505,528</u>
Total expenses for the year ended June 30, 2005	<u>\$ 6,839,764</u>	<u>\$ 1,665,764</u>	<u>\$ 8,505,528</u>	