

FINANCIAL STATEMENTS



CHESAPEAKE BAY FOUNDATION

Saving a National Treasure

**FOR THE YEAR ENDED JUNE 30, 2016
WITH SUMMARIZED FINANCIAL
INFORMATION FOR 2015**

CHESAPEAKE BAY FOUNDATION, INC.

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INDEPENDENT AUDITOR'S REPORT

To the Board of Trustees
Chesapeake Bay Foundation, Inc.
Annapolis, Maryland

We have audited the accompanying financial statements of the Chesapeake Bay Foundation, Inc. (the Foundation), which comprise the statement of financial position as of June 30, 2016, and the related statements of activities and change in net assets, functional expenses and cash flows for the year then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Foundation as of June 30, 2016, and the change in its net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

4550 MONTGOMERY AVENUE · SUITE 650 NORTH · BETHESDA, MARYLAND 20814
(301) 951-9090 · FAX (301) 951-3570 · WWW.GRFCPA.COM

Report on Summarized Comparative Information

We have previously audited the Foundation's 2015 financial statements, and we expressed an unmodified audit opinion on those audited financial statements in our report dated December 16, 2015. In our opinion, the summarized comparative information presented herein as of and for the year ended June 30, 2015, is consistent, in all material respects, with the audited financial statements from which it has been derived.

Other Matter

Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The Summary of Conservation and Scenic Easements on page 29, which is the responsibility of management, is presented for purposes of additional analysis and is not a required part of the financial statements. Such information has not been subjected to the auditing procedures applied in the audit of the financial statements, and, accordingly, we do not express an opinion or provide any assurance on it.

A handwritten signature in cursive script that reads "Gelman Rosenberg & Freedman".

December 14, 2016

CHESAPEAKE BAY FOUNDATION, INC.

STATEMENT OF FINANCIAL POSITION
AS OF JUNE 30, 2016
WITH SUMMARIZED FINANCIAL INFORMATION FOR 2015

ASSETS

	<u>2016</u>	<u>2015</u>
Cash and cash equivalents	\$ 4,966,040	\$ 10,450,712
Investments	57,231,749	55,313,607
Accounts receivable, less allowance for doubtful accounts of \$1,909 and \$4,014 for 2016 and 2015, respectively	843,584	1,494,899
Note receivable	87,013	88,732
Pledges receivable, net of allowance for doubtful accounts of \$123,774 and \$136,818 for 2016 and 2015, respectively	11,676,703	11,628,547
Prepaid, deposits and other assets	651,495	685,359
Deferred financing cost, net of accumulated amortization of \$49,049 and \$30,656 for 2016 and 2015, respectively	105,931	124,324
Property and equipment, net of accumulated depreciation and amortization of \$17,071,657 and \$15,907,313 for 2016 and 2015, respectively	<u>31,007,554</u>	<u>30,484,837</u>
TOTAL ASSETS	<u>\$106,570,069</u>	<u>\$110,271,017</u>

LIABILITIES AND NET ASSETS**LIABILITIES**

Loan payable	\$ 2,449,742	\$ 5,049,742
Bonds payable	4,854,120	5,379,056
Accounts payable and accrued expenses	1,740,573	1,705,662
Deferred income	863,126	515,244
Liability under split interest agreements	840,555	878,611
Interest rate swap obligation	<u>721,368</u>	<u>744,069</u>
Total liabilities	<u>11,469,484</u>	<u>14,272,384</u>

NET ASSETS

Unrestricted	31,759,859	31,088,547
Temporarily restricted	17,233,727	20,271,121
Permanently restricted	<u>46,106,999</u>	<u>44,638,965</u>
Total net assets	<u>95,100,585</u>	<u>95,998,633</u>
TOTAL LIABILITIES AND NET ASSETS	<u>\$106,570,069</u>	<u>\$110,271,017</u>

CHESAPEAKE BAY FOUNDATION, INC.

**STATEMENT OF ACTIVITIES AND CHANGE IN NET ASSETS
FOR THE YEAR ENDED JUNE 30, 2016
WITH SUMMARIZED FINANCIAL INFORMATION FOR 2015**

	2016			2015	
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total	Total
REVENUE					
Membership contributions	\$ 4,535,112	\$ -	\$ -	\$ 4,535,112	\$ 4,579,738
Grants and gifts	8,264,772	8,661,154	-	16,925,926	14,993,448
Education contracts and tuition	1,093,983	-	-	1,093,983	1,125,462
Investment distribution	590,111	2,178,284	-	2,768,395	2,689,224
Donated goods and services	1,191,947	-	-	1,191,947	1,070,141
Other	918,063	-	-	918,063	1,373,768
Net assets released from donor restrictions	<u>12,314,993</u>	<u>(12,314,993)</u>	<u>-</u>	<u>-</u>	<u>-</u>
Total revenue	<u>28,908,981</u>	<u>(1,475,555)</u>	<u>-</u>	<u>27,433,426</u>	<u>25,831,781</u>
EXPENSES					
Program Services:					
Environmental Education	6,334,976	-	-	6,334,976	6,191,494
Environmental Protection and Restoration	11,436,224	-	-	11,436,224	10,771,586
Strategic Communications	<u>3,288,085</u>	<u>-</u>	<u>-</u>	<u>3,288,085</u>	<u>3,031,303</u>
Total program services	<u>21,059,285</u>	<u>-</u>	<u>-</u>	<u>21,059,285</u>	<u>19,994,383</u>
Support Services:					
General and Administrative	2,172,742	-	-	2,172,742	2,280,081
Fundraising	<u>3,357,652</u>	<u>-</u>	<u>-</u>	<u>3,357,652</u>	<u>3,404,722</u>
Total support services	<u>5,530,394</u>	<u>-</u>	<u>-</u>	<u>5,530,394</u>	<u>5,684,803</u>
Total expenses	<u>26,589,679</u>	<u>-</u>	<u>-</u>	<u>26,589,679</u>	<u>25,679,186</u>
Change in net assets before capital (deductions) additions	<u>2,319,302</u>	<u>(1,475,555)</u>	<u>-</u>	<u>843,747</u>	<u>152,595</u>
CAPITAL (DEDUCTIONS) ADDITIONS					
Investment gain (loss) and distributions, net	(1,265,636)	(1,825,619)	39	(3,091,216)	(1,031,665)
Reclassification of net assets	(405,055)	263,780	141,275	-	-
Grants and gifts	-	-	1,326,720	1,326,720	11,000
Loss on sale of property and equipment	-	-	-	-	(540)
Unrealized gain on interest rate swap	<u>22,701</u>	<u>-</u>	<u>-</u>	<u>22,701</u>	<u>136,824</u>
Total capital (deductions) additions	<u>(1,647,990)</u>	<u>(1,561,839)</u>	<u>1,468,034</u>	<u>(1,741,795)</u>	<u>(884,381)</u>
Change in net assets	671,312	(3,037,394)	1,468,034	(898,048)	(731,786)
Net assets at beginning of year	<u>31,088,547</u>	<u>20,271,121</u>	<u>44,638,965</u>	<u>95,998,633</u>	<u>96,730,419</u>
NET ASSETS AT END OF YEAR	\$ <u>31,759,859</u>	\$ <u>17,233,727</u>	\$ <u>46,106,999</u>	\$ <u>95,100,585</u>	\$ <u>95,998,633</u>

CHESAPEAKE BAY FOUNDATION, INC.

STATEMENT OF FUNCTIONAL EXPENSES
FOR THE YEAR ENDED JUNE 30, 2016
WITH SUMMARIZED FINANCIAL INFORMATION FOR 2015

	2016			
	Program Services			
	Environmental Education	Environmental Protection and Restoration	Strategic Communications	Total Program Services
Salaries	\$ 2,461,692	\$ 4,181,665	\$ 1,060,718	\$ 7,704,075
Fringe benefits	956,932	1,605,498	417,102	2,979,532
Supplies	236,978	217,247	47,224	501,449
Restoration supplies	-	203,124	-	203,124
Telephone	50,796	75,268	15,711	141,775
Postage and shipping	109,282	204,561	124,519	438,362
Occupancy and utilities	427,201	922,601	122,079	1,471,881
Equipment rental, leasing, repairs and maintenance	280,542	162,289	31,722	474,553
Printing and publications	120,341	249,664	160,910	530,915
Dues and subscriptions	1,243	29,585	12,319	43,147
Travel	223,638	173,895	21,874	419,407
Meetings and seminars	134,256	110,528	26,062	270,846
Outside services	38,465	86,644	163,006	288,115
Professional fees	327,046	1,233,552	541,959	2,102,557
Restoration fees	-	247,625	-	247,625
Personnel recruitment	-	-	-	-
Miscellaneous	11,905	47,303	1,712	60,920
Mailing preparation	29,393	53,061	15,256	97,710
Insurance	159,482	127,972	14,321	301,775
List rentals	28,461	51,379	14,772	94,612
Depreciation and amortization - other	172,553	160,860	10,901	344,314
Subrecipients	-	528,845	-	528,845
Donated goods and services	<u>350,817</u>	<u>376,819</u>	<u>374,869</u>	<u>1,102,505</u>
Sub-total	6,121,023	11,049,985	3,177,036	20,348,044
Allocation of management and general	<u>213,953</u>	<u>386,239</u>	<u>111,049</u>	<u>711,241</u>
TOTAL	<u>\$ 6,334,976</u>	<u>\$ 11,436,224</u>	<u>\$ 3,288,085</u>	<u>\$ 21,059,285</u>

Support Services					2015
General and Administrative	Fundraising	Total Support Services	Total Expenses	Total Expenses	
\$ 1,717,588	\$ 1,143,699	\$ 2,861,287	\$ 10,565,362	\$ 10,029,301	
633,261	463,993	1,097,254	4,076,786	3,915,896	
55,184	36,621	91,805	593,254	988,037	
-	-	-	203,124	209,424	
12,911	10,837	23,748	165,523	162,565	
1,375	224,551	225,926	664,288	681,229	
243,508	77,462	320,970	1,792,851	1,806,851	
23,029	36,059	59,088	533,641	511,145	
1,350	255,666	257,016	787,931	797,607	
4,439	3,745	8,184	51,331	54,329	
33,299	22,140	55,439	474,846	439,630	
49,577	112,180	161,757	432,603	381,180	
12,178	189,516	201,694	489,809	535,856	
100,788	401,443	502,231	2,604,788	1,970,640	
-	-	-	247,625	331,199	
28,573	-	28,573	28,573	36,122	
41,280	14,625	55,905	116,825	78,010	
-	81,998	81,998	179,708	202,770	
35,353	22,874	58,227	360,002	344,657	
-	47,859	47,859	142,471	179,790	
3,689	9,543	13,232	357,546	393,327	
-	-	-	528,845	559,480	
-	<u>89,442</u>	<u>89,442</u>	<u>1,191,947</u>	<u>1,070,141</u>	
2,997,382	3,244,253	6,241,635	26,589,679	25,679,186	
<u>(824,640)</u>	<u>113,399</u>	<u>(711,241)</u>	<u>-</u>	<u>-</u>	
<u>\$ 2,172,742</u>	<u>\$ 3,357,652</u>	<u>\$ 5,530,394</u>	<u>\$ 26,589,679</u>	<u>\$ 25,679,186</u>	

CHESAPEAKE BAY FOUNDATION, INC.

**STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED JUNE 30, 2016
WITH SUMMARIZED FINANCIAL INFORMATION FOR 2015**

	<u>2016</u>	<u>2015</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Change in net assets	\$ (898,048)	\$ (731,786)
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation and amortization	1,209,626	1,109,924
Unrealized gain on interest rate swap	(22,701)	(136,823)
Loss on sale of property and equipment	-	540
Capital additions - permanently restricted contributions	(1,326,720)	(11,000)
Change in the discount of long-term pledges receivable	(828,134)	(319,756)
Change in allowance for doubtful accounts	(15,149)	(36,167)
Unrealized loss on investments	1,825,422	2,984,041
Realized gains on investments	(456,770)	(4,133,620)
Change in value of split interest agreements	11,790	(15,940)
(Increase) decrease in:		
Accounts receivable	653,420	37,203
Pledges receivable	793,022	3,400,960
Prepays, deposits and other assets	33,864	269,132
Increase (decrease) in:		
Accounts payable and accrued expenses	34,911	(1,524,431)
Deferred income	<u>347,882</u>	<u>96,683</u>
Net cash provided by operating activities	<u>1,362,415</u>	<u>988,960</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Net (purchases) sales of investments	(3,286,794)	2,045,907
Purchases of property and equipment	(1,713,950)	(4,816,195)
Proceeds from sale of property and equipment	-	2,500
Proceeds from note receivable	<u>1,719</u>	<u>1,886</u>
Net cash used by investing activities	<u>(4,999,025)</u>	<u>(2,765,902)</u>
CASH FLOWS FROM FINANCING ACTIVITIES		
Capital additions - permanently restricted contributions	1,326,720	11,000
Payments on bonds payable	(524,936)	(499,020)
Proceeds on loan payable	-	4,817,000
Payments on loan payable	(2,600,000)	(500,000)
Proceeds from split interest agreements	29,217	77,668
Payments made on split interest agreements	<u>(79,063)</u>	<u>(88,490)</u>
Net cash (used) provided by financing activities	<u>(1,848,062)</u>	<u>3,818,158</u>

CHESAPEAKE BAY FOUNDATION, INC.

STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED JUNE 30, 2016
WITH SUMMARIZED FINANCIAL INFORMATION FOR 2015

	<u>2016</u>	<u>2015</u>
Net (decrease) increase in cash and cash equivalents	\$ (5,484,672)	\$ 2,041,216
Cash and cash equivalents at beginning of year	<u>10,450,712</u>	<u>8,409,496</u>
CASH AND CASH EQUIVALENTS AT END OF YEAR	\$ <u>4,966,040</u>	\$ <u>10,450,712</u>

SUPPLEMENTAL INFORMATION

Interest Paid	<u>\$ 345,512</u>	<u>\$ 342,147</u>
Taxes Paid	<u>\$ 22,366</u>	<u>\$ -</u>

CHESAPEAKE BAY FOUNDATION, INC.

**NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2016**

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND GENERAL INFORMATION

Organization -

The Chesapeake Bay Foundation, Inc. (the Foundation) is a non-profit organization, incorporated in the State of Maryland in March 1966. Its principal sources of funds are contributions received directly from the public and grants received from individuals, foundations, governments, and corporations for environmental education, environmental protection, and land management and conservation programs relating to the Chesapeake Bay Region.

Basis of presentation -

The accompanying financial statements are presented on the accrual basis of accounting, and in accordance with FASB ASC 958, *Not-for-Profit Entities*.

The financial statements include 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 generally accepted accounting principles. Accordingly, such information should be read in conjunction with the Foundation's financial statements for the year ended June 30, 2015, from which the summarized information was derived.

Cash and cash equivalents -

The Foundation considers all cash and other highly liquid investments, including certificates of deposit with maturities of three months or less, and excluding cash and cash equivalents held by investment managers, to be cash equivalents.

At times during the year, the Foundation maintains a portion of its cash balances at financial institutions in excess of the Federal Deposit Insurance Corporation (FDIC) limits. Management believes the risk in these situations to be minimal.

Investments -

The Foundation invests in shares held in individual securities or investment funds which include bonds, stocks, investment trusts, money market funds held for investment purposes, and limited partnerships. Investment fund managers trade in various domestic and foreign financial markets, which carry a certain amount of risk of loss. Investments are stated at fair value based on quoted market prices at the reporting date, or in absence of such quoted market price, a reasonable estimate of fair value as approved by management. Unrealized and realized gains and losses are included in investment (loss) return and investment income in the Statement of Activities and Change in Net Assets.

The fair value of financial instruments is determined by reference to various market data and other valuation techniques as appropriate. Credit risk from financial instruments relates to the possibility that invested assets within a particular industry segment may experience loss due to market conditions. The Foundation has diversified its financial instruments to help ensure that no one industry segment represents a significant concentration of risk.

Although management uses its best judgment at estimating fair value of the underlying assets for its investments, there are inherent limitations in any valuation technique. Therefore, the value is not necessarily indicative of the amount that could be realized in a current transaction. Future events will also affect the estimates of fair value, and the effect of such events on the estimates of fair value could be material.

CHESAPEAKE BAY FOUNDATION, INC.

**NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2016**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND GENERAL INFORMATION
(Continued)**

Financial instruments with off-balance sheet risk -

In the course of trading activities entered into by the Foundation's various investment fund managers, certain financial instruments with off-balance sheet risk were acquired in order to structure the portfolio transactions to economically match the investment objectives of the funds and to hedge market risk. The exposure to credit risk associated with non-performance of any of these types of financial instruments is typically limited to the value of such investments reported as assets in the Statement of Financial Position.

Accounts and pledges receivable -

Accounts receivable are recorded at their net realizable value, which approximates fair value. Pledges receivable that are expected to be collected in future years are recorded at fair value, measured as the present value of their future cash flows. The discounts on these amounts are computed using risk-adjusted interest rates applicable to the years in which the promises are received. Amortization of the discounts is included in grants and gifts revenue. Conditional promises to give are not included as support until the conditions are substantially met. The allowance for doubtful accounts is determined based upon an annual review of account balances, including the age of the balance and the historical experience with the customer and donor.

Deferred financing costs -

Deferred financing costs represent loan issuance and bond issuance costs and other costs related to the construction of the Brock Environmental Center and the acquisition of the Bay Ridge Facility (Notes 8 and 9). Deferred financing costs are being amortized over the respective lives of the loan and bonds.

Property and equipment -

Property and equipment are stated at acquisition cost or fair market value at the date of donation, less accumulated depreciation. Property and equipment are depreciated on a straight-line basis over the estimated useful lives of the related assets, generally three to thirty years. The cost of maintenance and repairs is recorded as expenses are incurred. The Foundation has established \$5,000 as its threshold for capitalization.

Land is stated at acquisition cost, fair market value, or if fair market value is not available, at assessment value, at the date of donation. The land is used for educational, conservation, and operating purposes.

Impairment of long-lived assets -

Management reviews asset carrying amounts whenever events or circumstances indicate that such carrying amounts may not be recoverable. When considered impaired, the carrying amount of the assets is reduced, by a charge to Statement of Activities and Change in Net Assets, to its current fair value.

Split interest agreements -

A split interest agreement is a trust or other arrangements initiated by donors under which the Foundation receives benefits that are shared with either the donor or third party beneficiaries.

CHESAPEAKE BAY FOUNDATION, INC.

NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2016

1. **SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND GENERAL INFORMATION**
(Continued)

Split interest agreements (continued) -

The Foundation is the beneficiary of several split interest agreements. The Foundation's interest in these split interest agreements is reported as a contribution in the year received at its net present value. For the years ended June 30, 2016 and 2015, liabilities under split interest agreements totaled \$840,555 and \$878,611, respectively.

Net asset classification -

The net assets of the Foundation are reported in three self-balancing groups as follows:

- **Unrestricted net assets** include unrestricted revenue and contributions received without donor-imposed restrictions. These net assets are available for the operation of the Foundation and include both internally designated and undesignated resources.
- **Temporarily restricted net assets** include revenue and contributions subject to donor-imposed stipulations that will be met by the actions of the Foundation and/or the passage of time. When a restriction expires, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the Statement of Activities and Change in Net Assets as net assets released from restrictions.
- **Permanently restricted net assets** represent funds restricted by the donor to be maintained in-perpetuity by the Foundation.

Contributions and grants -

Contributions and grants are recorded as revenue in the year notification is received from the donor. Temporarily restricted contributions and grants are recognized as unrestricted support only to the extent of actual expenses incurred in compliance with the donor-imposed restrictions and satisfaction of time restrictions. Such contributions and grants received in excess of expenses incurred are shown as temporarily restricted net assets in the accompanying financial statements.

The Foundation receives funding under grants and contracts from the U.S. Government for direct and indirect program costs. This funding is subject to contractual restrictions, which must be met through incurring qualifying expenses for particular programs. Accordingly, such grants are considered exchange transactions and are recorded as unrestricted grant revenue to the extent that related expenses are incurred in compliance with the criteria stipulated in the grant agreements.

Grants and support receivable represents amounts due from funding organizations for reimbursable expenses incurred in accordance with the grant agreements. Grant funding received in advance of incurring the related expenses is recorded as a refundable advance.

Donated goods and services -

Contributions of goods or services are recognized when they are received if the goods or services either (a) create or enhance non-financial assets, or (b) require specialized skills, and are provided by individuals possessing those skills, and would typically need to be purchased if not donated. These amounts are shown as revenue and expenses on the Statement of Activities and Change in Net Assets.

CHESAPEAKE BAY FOUNDATION, INC.

NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2016

1. **SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND GENERAL INFORMATION**
(Continued)

Income taxes -

The Foundation is exempt from Federal income taxes under Section 501(c)(3) of the Internal Revenue Code. The Foundation is not a private foundation. The Foundation is required to report unrelated business income to the Internal Revenue Service and the appropriate state taxing authorities. The Foundation reports unrelated business income associated with its investments and is reporting the tax on a sale of debt financed investment property which occurred in the year ending June 30, 2012.

The Foundation has recorded income tax expense of \$22,366 and income tax recovery in the amount of \$(4,590) for the years ended June 30, 2016 and 2015, respectively, as follows:

	<u>2016</u>	<u>2015</u>
Other Unrelated Business Income Tax (Recovery) Included as an Addition/ (Reduction) to Miscellaneous Expenses in the Accompanying Statement of Functional Expenses	\$ <u>22,366</u>	\$ <u>(4,590)</u>

Federal and state income tax refunds of \$- and \$1,500 were outstanding and included in accounts payable in the Statement of Financial Position as of June 30, 2016 and 2015, respectively.

Uncertain tax positions -

For the years ended June 30, 2016 and 2015, the Foundation has documented its consideration of FASB ASC 740-10, *Income Taxes*, that provides guidance for reporting uncertainty in income taxes and has determined that no material uncertain tax positions qualify for either recognition or disclosure in the financial statements.

Use of estimates -

The preparation of the 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 at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Accordingly, actual results could differ from those estimates.

Fair value measurement -

The Foundation adopted the provisions of FASB ASC 820, *Fair Value Measurement*. FASB ASC 820 defines fair value, establishes a framework for measuring fair value, establishes a fair value hierarchy based on the quality of inputs (assumptions that market participants would use in pricing assets and liabilities, including assumptions about risk) used to measure fair value, and enhances disclosure requirements for fair value measurements. The Foundation accounts for a significant portion of its financial instruments at fair value or considers fair value in their measurement.

CHESAPEAKE BAY FOUNDATION, INC.

**NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2016**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND GENERAL INFORMATION
(Continued)**

Functional allocation of expenses -

The costs of providing the various programs and other activities have been summarized on a functional basis in the Statement of Activities and Change in Net Assets. Accordingly, certain costs have been allocated among the programs and support services benefited.

Joint costs -

For fiscal years 2016 and 2015, the Foundation incurred joint costs of \$2,194,443 and \$2,279,581, respectively, for educational materials, membership and support services. These costs were allocated as follows:

	2016	2015
Environmental Education	\$ 474,025	\$ 502,964
Environmental Protection and Restoration	855,734	875,027
Strategic Communications	246,036	246,247
Fundraising	618,648	655,343
TOTAL JOINT COSTS INCURRED	\$ 2,194,443	\$ 2,279,581

Reclassification -

Certain amounts in the prior year's financial statements have been reclassified to conform to the current year's presentation. These reclassifications had no effect on the previously reported changes in net assets.

2. INVESTMENTS

At June 30, 2016 and 2015, investments at readily determinable fair values, consisted of the following:

	2016	2015
Equity securities	\$ 16,574,704	\$ 20,721,597
International equity securities	3,399,425	3,726,419
Partnerships/Alternative investments	19,902,319	18,764,364
Corporate bonds and other agencies	10,920,144	2,613,649
Beneficial interest in perpetual trust	3,223,517	2,924,350
Sub-total investments	54,020,109	48,750,379
Cash and cash equivalents held by investment managers	3,211,640	6,563,228
TOTAL INVESTMENTS	\$ 57,231,749	\$ 55,313,607

Under the terms of certain agreements for several alternative investments, the Foundation is obligated to remit additional funding periodically as capital calls are exercised. As of June 30, 2016 and 2015, the Foundation has uncalled commitments of \$1,509,957 and \$560,771, respectively.

CHESAPEAKE BAY FOUNDATION, INC.

NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2016

2. INVESTMENTS (Continued)

Alternative investments are comprised of the following at June 30, 2016 and 2015:

Investment Type	Amount		Liquidity
	2016	2015	
Domestic/U.S. Limited Partnerships	\$ 1,912,775	\$ 1,239,782	None until dissolution or winding up of partnership.
Domestic/U.S. Limited Partnerships	1,857,864	1,874,300	100 days notice
Domestic/U.S. Alternative Trusts	3,639,123	3,190,917	Month end
Domestic/U.S. Limited Partnerships	12,492,557	12,428,420	Last day of each quarter.
Hedge Funds	<u>-</u>	<u>30,945</u>	Last day of each quarter.
ALTERNATIVE INVESTMENTS	<u>\$19,902,319</u>	<u>\$18,764,364</u>	

Included in the investment balance at June 30, 2016 and 2015 are investments related to certain split-interest agreements in the amounts of \$887,275 and \$970,538, respectively.

The investment portfolio includes \$37,413,618 and \$36,428,383 of permanently restricted endowment investments at June 30, 2016 and 2015, respectively (see Note 18).

The Foundation follows the Uniform Prudent Management Institutional Funds Act (UPMIFA). As such, endowment earnings not yet authorized for spending are shown as temporarily restricted net assets. If, in a given year, there are deficiencies in any endowment fund, unrestricted net assets will cover the deficiencies.

It is the policy of the Foundation to spend on operations 5% of a twelve quarter trailing average of the sum of accumulated investments, including endowment fund investments. This 5% amount is shown in the revenue section of the Statement of Activities and Change in Net Assets. Investment income that exceeds this target and all losses in a given year are considered non-operating items and are included in the capital additions (deductions) section of the Statement of Activities and Change in Net Assets, as "Investment (loss) return, net".

Investment return for the years ended June 30, 2016 and 2015 consisted of the following:

	<u>2016</u>	<u>2015</u>
Interest and dividends	\$ 1,045,831	\$ 507,980
Unrealized loss	(1,825,422)	(2,984,041)
Realized gains	<u>456,770</u>	<u>4,133,620</u>
Total investment (loss) return	(322,821)	1,657,559
Less: Investment distribution for operations	<u>(2,768,395)</u>	<u>(2,689,224)</u>
INVESTMENT GAIN (LOSS) AND DISTRIBUTIONS, NET	<u>\$ (3,091,216)</u>	<u>\$ (1,031,665)</u>

CHESAPEAKE BAY FOUNDATION, INC.

**NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2016**

3. ACCOUNTS RECEIVABLE

Accounts receivable are stated at their carrying value, which approximates fair value, and are due within one year. The allowance for doubtful accounts is determined based upon an annual review of account balances, including the age of the balance and the historical experience with the customer. Accounts receivable consisted of the following at June 30, 2016 and 2015, respectively:

	2016	2015
Federal and state receivables	\$ 762,694	\$ 537,279
Non-Federal and state receivables	82,799	961,634
Total accounts receivable	845,493	1,498,913
Less: Allowance for doubtful accounts	(1,909)	(4,014)
NET ACCOUNTS RECEIVABLE	\$ 843,584	\$ 1,494,899

4. NOTE RECEIVABLE

On July 20, 1998, the Foundation loaned \$135,000 to the Rappahannock Tribe, Inc. (the Tribe). The loan was collateralized by the Tribe's property. The note bears interest at a rate of 7.5% annually, with interest payable monthly. The note was due on July 1, 1999; however, the note has been extended every year and is now due July 1, 2017. Only monthly payments of interest are to be made by the Tribe until maturity. The amounts outstanding at June 30, 2016 and 2015 were \$87,013 and \$88,732, respectively.

5. PLEDGES RECEIVABLE

As of June 30, 2016 and 2015, contributors to the Foundation have made written promises to give totaling \$13,085,147 and \$13,878,169, respectively. Pledges due in more than one year have been recorded at the present value of the estimated cash flows, using a discount rate ranging from 2% to 7%. The allowance for doubtful accounts is determined based upon an annual review of account balances, including the age of the balance and the historical experience with the donor. Pledges are due as follows at June 30, 2016 and 2015:

	2016	2015
Less than one year	\$ 4,492,273	\$ 3,854,870
One to five years	3,133,954	4,713,723
Beyond five years	5,458,920	5,309,576
Total pledges	13,085,147	13,878,169
Less: Discount to net present value	(1,284,670)	(2,112,804)
Less: Allowance for doubtful accounts	(123,774)	(136,818)
NET PLEDGES RECEIVABLE	\$ 11,676,703	\$ 11,628,547

CHESAPEAKE BAY FOUNDATION, INC.

NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2016

6. PROPERTY AND EQUIPMENT

Property and equipment consisted of the following at June 30, 2016 and 2015:

	<u>2016</u>	<u>2015</u>
Land	\$ 11,747,533	\$ 11,734,840
Building and improvements	26,867,591	26,258,175
Furniture and equipment	3,693,575	3,463,806
Boats	4,003,386	4,003,386
Vehicles	590,720	617,609
Construction in progress	1,159,406	297,334
Art	<u>17,000</u>	<u>17,000</u>
Total property and equipment	48,079,211	46,392,150
Less: Accumulated depreciation and amortization	<u>(17,071,657)</u>	<u>(15,907,313)</u>
NET PROPERTY AND EQUIPMENT	<u>\$ 31,007,554</u>	<u>\$ 30,484,837</u>

The amount of property and equipment (at cost or fair market value at date of donation) that cannot be sold by the Foundation due to donor restrictions is \$8,155,524 at June 30, 2016 and 2015 (see Note 18).

Depreciation and amortization expense for the years ended June 30, 2016 and 2015 totaled \$1,209,626 and \$1,109,924, respectively. Of these amounts, \$852,080 and \$716,570 is included in occupancy expense, and \$357,546 and \$393,354 is included in depreciation and amortization expense in the accompanying Statement of Functional Expenses for the years ended June 30, 2016 and 2015, respectively.

7. LINE OF CREDIT

The Foundation had obtained an unsecured \$1,000,000 line of credit with Capital One, effective October 1, 2013 (the "Line of Credit"). The line of credit expired on January 29, 2016, at which time, the Foundation did not renew for an additional term. There was no outstanding balance on the line of credit for the year ended June 30, 2015.

8. LOAN PAYABLE

The Chesapeake Bay Foundation's Brock Environmental Center is a 10,200 square foot facility located at Pleasure House Point in Virginia Beach, Virginia. It sits on land once slated for heavy development that is now saved in perpetuity. The Brock Environmental Center provides a collaborative workspace for all of the Foundation's Virginia Beach program staff, the local Lynnhaven River NOW environmental group, a partner group of the Foundation, and the City of Virginia Beach Parks and Recreation.

The Brock Environmental Center is also a venue for expanded environmental education programs for decision makers, students, teachers and volunteers, serves as a lasting demonstration site for restoration projects, and provides meeting space for local nonprofit groups.

CHESAPEAKE BAY FOUNDATION, INC.

**NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2016**

8. LOAN PAYABLE (Continued)

The Brock Environmental Center is one of the most sustainable buildings in the world. The facility earned the U.S. Green Building Council's LEED Platinum Certification and expects to obtain the International Living Building Institute's Living Building Challenge Certification.

The construction of the Brock Environmental Center was completed on October 31, 2014, and staff began to move into the facility in mid-December 2014. Environmental programs, tours, and volunteer activities began in January 2015.

On October 1, 2013, the Foundation obtained a variable rate taxable loan in the amount of \$8,300,000 from Capital One in connection with the development of the Brock Environmental Center (the "Taxable Loan"). The Taxable Loan is unsecured, and is structured as a "draw down facility" and payments are interest only through maturity. The entire unpaid balance, together with all accrued and unpaid interest, shall be due and payable in full on the maturity date of October 1, 2020. The total amount of the loan outstanding as of June 30, 2016 and 2015 was \$2,449,742 and \$5,049,742, respectively.

Total interest of \$14,937 was capitalized and included in the buildings and improvements account for the year ending June 30, 2015. Additionally, financing costs totaling \$67,560, related to obtaining the Taxable Loan, were capitalized and are being amortized over the life of the Taxable Loan. At June 30, 2016 and 2015, accumulated amortization for the Taxable Loan financing costs totaled \$25,737 and \$16,086, respectively.

Additionally, the agreements for the loan payable and bonds payable (discussed in Note 9) contain various covenants, which among other things, require the Foundation to maintain certain financial ratios and submit various financial reports throughout their fiscal year.

Interest expense for the years ended June 30, 2016 and 2015 was \$69,714 and \$39,449, respectively, which is included in occupancy and utilities expense within the Statement of Functional Expenses.

9. BONDS PAYABLE

In December 2000, the Foundation moved into its U.S. Green Building Council LEED Platinum headquarters, a facility named the Philip Merrill Environmental Center (Merrill Center), which is widely recognized as one of the most environmentally innovative buildings in the world. The facility includes a two story, 30,000 square foot "green" office building and common meeting centers for internal and external groups. Since moving into the Merrill Center, much of the site has been and continues to be restored with native plants.

During fiscal year 2014, the "Variable Rate Economic Development Revenue Bonds, Series 1998" which were used to finance the acquisition, construction and equipping a portion of the Merrill Center, were refinanced with the related bond sinking fund extinguished and capitalized costs fully amortized. As described further below, no amount of the 1998 Bonds was outstanding as of June 30, 2014.

On October 1, 2013, the Maryland Economic Development Corporation (MEDCO) issued an Economic Development Refunding Revenue Bond, The Chesapeake Bay Foundation Project, 2013 Series (the "2013 Series Bonds") in the amount of \$6,195,000 for the benefit of the Foundation. Proceeds of the 2013 Series Bonds were used to refinance MEDCO's outstanding 1998 Series Bonds, noted above.

CHESAPEAKE BAY FOUNDATION, INC.

NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2016

9. BONDS PAYABLE (Continued)

The 2013 Series Bonds were purchased by Capital One Bank, N.A. ("Capital One"). Principal and interest on the 2013 Series Bonds are due monthly based on a mortgage style amortization structure. The final maturity date of the Series 2013 Bonds is October 1, 2023. Financing costs related to the issuance of the 2013 Series Bonds in the amount of \$87,420, were capitalized and are being amortized over the life of the bonds. At June 30, 2016 and 2015, accumulated amortization for the bond financing costs totaled \$23,312 and \$14,570, respectively.

To mitigate the effect of fluctuations in interest rates, the Foundation has hedged these bonds using the interest rate swap agreement described in Note 10. The bond agreements, among other provisions, require the Foundation to meet certain financial ratio tests. For the years ended June 30, 2016 and 2015, the Foundation was in compliance with all bond covenants.

As of June 30, 2016 and 2015, the outstanding principal of the bond payable totaled \$4,854,120 and \$5,379,056, respectively.

Principal payments are due as follows:

<u>Year Ending June 30,</u>	
2017	\$ 554,735
2018	585,406
2019	616,824
2020	652,423
2021	687,925
Thereafter	<u>1,756,807</u>
BONDS PAYABLE	<u>\$ 4,854,120</u>

The Foundation incurred interest expense on the bonds totaling \$275,798 and \$302,698 for the years ended June 30, 2016 and 2015, respectively, which is included in occupancy and utilities expense within the Statement of Functional Expenses.

10. INTEREST RATE SWAP

The bonds discussed in Note 9 include interest payments based on the Securities Industry and Financial Markets Association ("SIFMA") Index, formerly the Bond Market Association (BMA). As a means to reduce its exposure to volatility in the variable rate index, the Foundation entered into certain interest rate swap agreements. The intention of the swap agreement is to synthetically fix the interest rate on the bonds.

The Foundation had an interest rate swap agreement (the "Wells Fargo Swap"), which was terminated on September 27, 2013 in connection with the issuance of the 2013 Series Bonds. The market value of the Wells Fargo Swap, at the time of termination, was embedded in the new Swap provided by Capital One Bank, N.A. (the "Capital One Swap"). Under the Capital One Swap, the Foundation pays a fixed rate of 4.52% and receives a floating rate equal to 78% of 1-Month LIBOR. The Capital One Swap hedges 100% of the outstanding amount of the 2013 Series Bonds and provides the Foundation with a synthetic fixed rate cost of capital through the maturity of the 2013 Series Bonds on October 1, 2023.

CHESAPEAKE BAY FOUNDATION, INC.

**NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2016**

10. INTEREST RATE SWAP (Continued)

For the years ended June 30, 2016 and 2015, the outstanding notional amount of the Capital One Swap was \$4,854,120 and \$5,379,056, respectively. As of June 30, 2016 and 2015, the Capital One Swap had a negative fair value of \$721,368 and \$744,069, respectively, which is reflected as a liability in the financial statements.

The swaps expose the Foundation to basis risk should the actual rate on the Foundation's bonds exceed the LIBOR Index for the years ended June 30, 2016 and 2015). Since the Foundation's bonds are based upon the LIBOR Index, there is relatively little basis risk. Should the Foundation terminate the Capital One Swap prior to maturity, the Foundation will either receive or pay a termination payment. This payment is equal to the fair value of the Capital One Swap at the time it is terminated.

11. TEMPORARILY RESTRICTED NET ASSETS

Temporarily restricted net assets consisted of the following at June 30, 2016 and 2015:

	2016	2015
Program Restricted:		
Environmental Education	\$ 541,564	\$ 1,208,491
Environmental Protection and Restoration	6,881,215	9,171,735
Property and Equipment	868,921	645,646
Other	17,201	23,786
Total program restricted	8,308,901	11,049,658
Time Restricted	8,924,826	9,221,463
TEMPORARILY RESTRICTED NET ASSETS	\$ 17,233,727	\$ 20,271,121

The Foundation is the recipient of several charitable remainder unitrusts that are administered by third parties. Under the terms of these trusts, payments of income are made from the trusts to the donors or other specified parties over the terms of the trusts. Upon the termination of the trusts, the remaining net assets will be transferred to the Foundation for its unrestricted use.

Accumulated investment earnings from permanently restricted endowed funds included within temporarily restricted net assets as of June 30, 2016 and 2015 are as follows:

	2016	2015
With purpose restrictions	\$ 3,777,793	\$ 4,323,880
Time restriction	1,123,962	2,056,435
ACCUMULATED ENDOWMENT EARNINGS INCLUDED IN TEMPORARILY RESTRICTED NET ASSETS	\$ 4,901,755	\$ 6,380,315

CHESAPEAKE BAY FOUNDATION, INC.

**NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2016**

11. TEMPORARILY RESTRICTED NET ASSETS (Continued)

Temporarily restricted net assets released from donor restrictions by incurring expenses, which satisfied the restricted purposes specified by the donors or the passage of time are as follows:

	2016	2015
Donor Restrictions:		
Environmental Education	\$ 1,652,024	\$ 1,409,902
Environmental Protection and Restoration	8,114,673	6,432,807
Strategic Communications	-	90,000
Property and Equipment	265,655	190,564
Other	48,748	88,076
Total donor restrictions	10,081,100	8,211,349
Time Restricted	2,233,893	2,512,445
NET ASSETS RELEASED FROM RESTRICTIONS	\$ 12,314,993	\$ 10,723,794

12. LEASE COMMITMENT

The Foundation leases office space, equipment, and distribution facilities under noncancellable leases expiring at various dates.

Certain lease agreements call for escalation of rental payments based upon increases in operating costs of the lessor and increases in consumer price indices. Additionally, some of the leases include renewal options ranging from three months to three years.

The minimum rental payments under these noncancellable leases for future fiscal years are as follows:

<u>Year Ending June 30,</u>	
2017	\$ 341,771
2018	202,438
2019	137,113
2020	27,929
2021	2,753
	\$ 712,004

Rent expense for the years ended June 30, 2016 and 2015 totaled \$248,267 and \$281,173, respectively. Rent expense is included in occupancy and utilities in the Statement of Functional Expenses.

13. DEFINED CONTRIBUTION RETIREMENT BENEFIT PLAN

Retirement benefits are available for substantially all regular, full-time Foundation personnel, through direct payments by the Foundation to the Plan administrators. For these employees, the Foundation matches the employee's voluntary contribution up to four percent. For the years ended June 30, 2016 and 2015, the Foundation made contributions in the amounts of \$376,026 and \$383,982, respectively.

CHESAPEAKE BAY FOUNDATION, INC.

**NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2016**

14. RELATED PARTY

For the years ended June 30, 2016 and 2015, the Foundation received gross contributions and grants in the amounts of \$4,094,833 and \$2,832,775, respectively, from Trustees and Executive Management. Net amounts due under pledges receivable from related parties totaled \$2,663,790 and \$2,549,296 as of June 30, 2016 and 2015, respectively.

15. CONTINGENCIES

The Foundation receives grants from various agencies of the United States Government. For fiscal years through June 30, 2015, such grants were subject to audit under the provisions of OMB Circular A-133. Beginning for fiscal year ended June 30, 2016, such grants are subject to audit under the provisions of *Title 2 U.S. Code of Federal Regulations (CFR) Part 200 Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards*. The ultimate determination of amounts received under the United States Government grants is based upon the allowance of costs reported to and accepted by the United States Government as a result of the audits. Audits in accordance with the applicable provisions have been completed for all required fiscal years through 2016. Until such audits have been accepted by the United States Government, there exists a contingency to refund any amount received in excess of allowable costs. Management is of the opinion that no material liability will result from such audits.

Various lawsuits and other contingent liabilities arise in the ordinary course of the Foundation's activities. While the final outcome of these legal actions cannot be determined at this time, management is of the opinion that the ultimate liability, if any, from the final resolution of these matters will not have a material effect on the Foundation's financial statements. During the year ended June 30, 2015, the Foundation received a settlement in the amount of \$800,000 related to previous year's litigation, which is included in Other revenue in the Statement of Activities and Change in Net Assets.

16. DONATED GOODS, SERVICES AND PROPERTY

During the years ended June 30, 2016 and 2015, the Foundation was the beneficiary of donated goods and services, which allow the Foundation to provide greater resources toward various programs. To properly reflect total program expenses, donations totaling \$1,191,947 and \$1,070,141 have been included in revenue and expense for the years ended June 30, 2016 and 2015, respectively, which included \$1,049,500 and \$875,000 of in-kind public service announcements for the years ended June 30, 2016 and 2015, respectively.

17. FAIR VALUE MEASUREMENT

In accordance with FASB ASC 820, *Fair Value Measurement*, the Foundation has categorized its financial instruments, based on the priority of the inputs to the valuation technique, into a three-level fair value hierarchy. The fair value hierarchy gives the highest priority to quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). If the inputs used to measure the financial instruments fall within different levels of hierarchy, the categorization is based on the lowest level input that is significant to the fair value measurement of the instrument.

Investments recorded in the Statement of Financial Position are categorized based on the inputs to valuation techniques as follows:

Level 1. These are investments where values are based on unadjusted quoted prices for identical assets in an active market the Foundation has the ability to access.

CHESAPEAKE BAY FOUNDATION, INC.

**NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2016**

17. FAIR VALUE MEASUREMENT (Continued)

Level 2. These are investments where values are based on quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, or model-based valuation techniques that utilize inputs that are observable either directly or indirectly for substantially the full-term of the investments.

Level 3. These are investments where inputs to the valuation methodology are unobservable and significant to the fair value measurement.

Following is a description of the valuation methodology used for investments measured at fair value. There have been no changes in the methodologies or classifications used at June 30, 2016.

- *Equity/International Equity* - Valued at the closing price reported on the active market in which the individual securities are traded.
- *Partnerships/Alternative investments* - These instruments do not have a readily determinable fair value. The fair values used are generally determined by the general partner or management of the entity and are based on appraisals or other estimates that require varying degrees of judgment. Inputs used in determining fair value may include the cost and recent activity concerning the underlying investments in the funds or partnerships.
- *Corporate bonds and other agencies* - Fair value is based upon current yields available on comparable securities of issuers with similar ratings, the security's terms and conditions, and interest rate and credit risk.
- *Beneficial interest in perpetual trust* - Valued at the present value of discounted cash flows of the trust investment value into perpetuity.
- *Cash and cash equivalents held by investment managers* - Fair value is equal to the reported net asset value of the fund.
- *Interest rate swap obligations* - Fair value is derived from quotes from a dealer or broker, where available. Models used in valuing such agreements consider the contractual terms of and specific risks inherent in the instrument, and inputs used typically include yield curve, instrument volatility, prepayment rates and assumptions concerning nonperformance risk.

The tables below summarizes, by level within the fair value hierarchy, the Foundation's investments as of June 30, 2016:

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total June 30, 2016</u>
Asset Class:				
Equity securities	\$ 16,574,704	\$ -	\$ -	\$ 16,574,704
International equity securities	3,399,425	-	-	3,399,425
Partnerships/Alternative investments	-	-	19,902,319	19,902,319
Corporate bonds and other agencies	10,920,144	-	-	10,920,144
Beneficial interest in perpetual trust	-	3,223,517	-	3,223,517
Cash and cash equivalents held by investment managers	<u>3,211,640</u>	<u>-</u>	<u>-</u>	<u>3,211,640</u>
Total Investments	<u>\$ 34,105,913</u>	<u>\$ 3,223,517</u>	<u>\$ 19,902,319</u>	<u>\$ 57,231,749</u>
Liability:				
Interest Rate Swap Obligation	<u>\$ -</u>	<u>\$ 721,368</u>	<u>\$ -</u>	<u>\$ 721,368</u>

CHESAPEAKE BAY FOUNDATION, INC.

NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2016

17. FAIR VALUE MEASUREMENT (Continued)

The tables below summarizes, by level within the fair value hierarchy, the Foundation's investments as of June 30, 2015:

Asset Class:	Level 1	Level 2	Level 3	Total June 30, 2015
Equity securities	\$ 20,721,597	\$ -	\$ -	\$ 20,721,597
International equity securities	3,726,419	-	-	3,726,419
Partnerships/Alternative investments	-	-	18,764,364	18,764,364
Corporate bonds and other agencies	2,613,649	-	-	2,613,649
Beneficial interest in perpetual trust	-	2,924,350	-	2,924,350
Cash and cash equivalents held by investment managers	6,563,228	-	-	6,563,228
Total Investments	\$ 33,624,893	\$ 2,924,350	\$ 18,764,364	\$ 55,313,607
Liability:				
Interest Rate Swap Obligation	\$ -	\$ 744,069	\$ -	\$ 744,069

Level 3 Financial Assets

Following is the change in fair value of the Foundation's assets using significant unobservable inputs (Level 3) for the year ended June 30, 2016:

	Domestic/ U.S. Limited Partnership	Domestic/ U.S. Limited Partnership	Domestic/ U.S. Limited Partnership	Trusts	Hedge Funds	Total
Beginning balance	\$ 1,239,782	\$ 1,874,300	\$12,428,420	\$ 3,190,917	\$ 30,945	\$ 18,764,364
Unrealized (loss) gain	(322,396)	(216,436)	(144,211)	448,206	(15,246)	(250,083)
Realized gain	9,720	-	165,536	-	16,774	192,030
Earned income	264,965	(2,675)	38,725	(1,091)	(20)	299,904
Purchases (sales)	720,704	202,675	4,087	1,091	(32,453)	896,104
BALANCE AS OF JUNE 30, 2015	\$ 1,912,775	\$ 1,857,864	\$12,492,557	\$ 3,639,123	\$ -	\$ 19,902,319

Following is the change in fair value of the Foundation's assets using significant unobservable inputs (Level 3) for the year ended June 30, 2015 :

	Domestic/ U.S. Limited Partnership	Domestic/ U.S. Limited Partnership	Domestic/ U.S. Limited Partnership	Trusts	Hedge Funds	Total
Beginning balance	\$ 1,347,491	\$ 1,000,000	\$11,869,132	\$ -	\$ 2,493,721	\$ 16,710,344
Unrealized (loss) gain	(79,528)	74,300	(467,343)	-	(441,225)	(913,796)
Realized gain	221,255	-	942,586	-	426,594	1,590,435
Earned income	50,548	(10,134)	80,093	-	(633)	119,874
Purchases (sales)	(299,984)	810,134	3,952	3,190,917	(2,447,512)	1,257,507
BALANCE AS OF JUNE 30, 2015	\$ 1,239,782	\$ 1,874,300	\$12,428,420	\$ 3,190,917	\$ 30,945	\$ 18,764,364

CHESAPEAKE BAY FOUNDATION, INC.

**NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2016**

17. FAIR VALUE MEASUREMENT (Continued)

As of June 30, 2016, the Foundation's individual investment funds which exceed 5% of net assets are:

<u>Name of Investment</u>	<u>Type of Investment</u>	<u>Fair Value</u>	<u>Fair Value as a % of Net Assets</u>
Vanguard Ltd Term Tax Exp	Corporate bonds and other agencies	\$ 10,500,856	11%
DF Dent	Equity	\$ 7,919,707	8%
Acacia Partners	Partnerships/Alternative investments	\$ 6,566,058	7%
Multi-strategy Fund for Institutional Investors	Partnerships/Alternative investments	\$ 5,926,499	6%
T Rowe Price Equity Income Fund	Equity	\$ 5,222,772	5%

As of June 30, 2015, the Foundation's individual investment funds which exceed 5% of net assets are:

<u>Name of Investment</u>	<u>Type of Investment</u>	<u>Fair Value</u>	<u>Fair Value as a % of Net Assets</u>
DF Dent	Equity	\$ 8,011,795	8%
Acacia Partners	Partnerships/Alternative investments	\$ 6,655,295	7%
Restricted Short-Term Investments	Cash and cash equivalents	\$ 6,181,556	7%
Multi-strategy Fund for Institutional Investors	Partnerships/Alternative investments	\$ 5,773,125	6%
T Rowe Price Equity Income Fund	Equity	\$ 5,242,253	5%

18. ENDOWMENT

The Foundation's endowment consists of several individual funds established for a variety of purposes. Its endowment includes both donor-restricted endowment funds and funds designated by the Board of Trustees to function as an endowment. As required by GAAP, net assets associated with endowment funds, including funds designated by the Board of Trustees to function as endowments, are classified and reported based on existence or absence of donor imposed restrictions. The Board of Trustees has interpreted UPMIFA as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary.

As a result of this interpretation, the Foundation classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund.

The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the organization in a manner consistent with the standard of prudence prescribed by UPMIFA. (See Note 11, total endowments funds classified as temporarily restricted net assets.)

CHESAPEAKE BAY FOUNDATION, INC.

NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2016

18. ENDOWMENT (Continued)

In accordance with UPMIFA, the Foundation considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

- The duration and preservation of the fund;
- The purpose of the donor-restricted endowment fund;
- General economic conditions and the possible effect of inflation and deflation;
- The expected total return from income and the appreciation of investments; and
- The investment policies of the organization.

Permanently restricted net assets are invested in-perpetuity, the income of which is restricted to the following:

	<u>2016</u>	<u>2015</u>
Environmental Education	\$ 10,267,588	\$ 9,244,188
Environmental Protection and Restoration	13,514,767	13,074,325
Property and Equipment	8,155,524	8,155,524
General Operating	<u>14,169,120</u>	<u>14,164,928</u>
PERMANENTLY RESTRICTED NET ASSETS	<u>\$ 46,106,999</u>	<u>\$ 44,638,965</u>

Permanently restricted net assets consists of the following:

	<u>2016</u>	<u>2015</u>
Investments	\$ 37,413,618	\$ 36,428,383
Property and equipment	8,155,524	8,155,524
Pledge receivables, net of discount	537,857	51,858
Due from operations	<u>-</u>	<u>3,200</u>
PERMANENTLY RESTRICTED NET ASSETS	<u>\$ 46,106,999</u>	<u>\$ 44,638,965</u>

Endowment net asset composition by type of fund as of June 30, 2016:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Donor-Restricted Endowment Funds	\$ (1,209,333)	\$ 4,901,755	\$ 46,106,999	\$ 49,799,421
Board-Designated Endowment Funds	<u>840,190</u>	<u>-</u>	<u>-</u>	<u>840,190</u>
TOTAL FUNDS	<u>\$ (369,143)</u>	<u>\$ 4,901,755</u>	<u>\$ 46,106,999</u>	<u>\$ 50,639,611</u>

CHESAPEAKE BAY FOUNDATION, INC.

NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2016

18. ENDOWMENT (Continued)

Changes in endowment net assets for the year ended June 30, 2016:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Endowment net assets, beginning of year	\$ 217,327	\$ 6,380,315	\$ 44,638,965	\$ 51,236,607
Interest and dividends	15,266	917,237	26	932,529
Net appreciation (depreciation) of investments	<u>(22,092)</u>	<u>(1,033,361)</u>	<u>13</u>	<u>(1,055,440)</u>
Total investment return	<u>(6,826)</u>	<u>(116,124)</u>	<u>39</u>	<u>(122,911)</u>
Contributions	15,000	-	1,326,720	1,341,720
Appropriation of endowment assets for expenditure	(42,576)	(2,178,284)	-	(2,220,860)
Other changes:				
Transfer of net assets	<u>(552,068)</u>	<u>815,848</u>	<u>141,275</u>	<u>405,055</u>
ENDOWMENT NET ASSETS, END OF YEAR	<u>\$ (369,143)</u>	<u>\$ 4,901,755</u>	<u>\$ 46,106,999</u>	<u>\$ 50,639,611</u>

Endowment net asset composition by type of fund as of June 30, 2015:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Donor-Restricted Endowment Funds	\$ (657,265)	\$ 6,380,315	\$ 44,638,965	\$ 50,362,015
Board-Designated Endowment Funds	<u>874,592</u>	<u>-</u>	<u>-</u>	<u>874,592</u>
TOTAL FUNDS	<u>\$ 217,327</u>	<u>\$ 6,380,315</u>	<u>\$ 44,638,965</u>	<u>\$ 51,236,607</u>

Changes in endowment net assets for the year ended June 30, 2015:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Endowment net assets, beginning of year	\$ 373,914	\$ 7,013,342	\$ 44,627,835	\$ 52,015,091
Interest and dividends	5,023	445,945	9	450,977
Net appreciation of investments	<u>19,628</u>	<u>881,563</u>	<u>121</u>	<u>901,312</u>
Total investment return	<u>24,651</u>	<u>1,327,508</u>	<u>130</u>	<u>1,352,289</u>
Contributions	-	-	11,000	11,000
Appropriation of endowment assets for expenditure	(40,866)	(2,100,907)	-	(2,141,773)
Other changes:				
Transfer of net assets	<u>(140,372)</u>	<u>140,372</u>	<u>-</u>	<u>-</u>
ENDOWMENT NET ASSETS, END OF YEAR	<u>\$ 217,327</u>	<u>\$ 6,380,315</u>	<u>\$ 44,638,965</u>	<u>\$ 51,236,607</u>

CHESAPEAKE BAY FOUNDATION, INC.

**NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2016**

18. ENDOWMENT (Continued)

Funds with Deficiencies -

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level that the donor or UPMIFA requires the Foundation to retain into perpetuity. In accordance with GAAP, deficiencies of this nature that are reported in unrestricted net assets were \$1,209,333 and \$657,265 as of June 30, 2016 and 2015, respectively. These deficiencies resulted from unfavorable market fluctuations occurring after the investment of permanently restricted contributions and the appropriation for certain programs that were deemed prudent by the Board of Trustees.

Return Objectives and Risk Parameters -

The Foundation has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the Foundation must hold in-perpetuity or for a donor-specified period(s). Under this policy, as approved by the Board of Trustees, the endowment assets are invested in a manner that is intended to produce results that exceed a blended index of the Standard & Poor's 500 Index and the Barclays Aggregate Bond Index while assuming a moderate level of investment risk. The Foundation expects its endowment funds, over time, to provide an average rate of return of approximately 8% annually. Actual returns in any given year may vary from this amount.

Strategies Employed for Achieving Objectives -

To satisfy its long-term rate-of-return objectives, the Foundation relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The Foundation targets a diversified asset allocation that places a greater emphasis on equity-based and partnerships/alternative investments to achieve its long-term return objectives within prudent risk constraints.

Spending Policy and How the Investment Objectives Relate to Spending Policy -

The Foundation has a policy of appropriating for distribution each year 5% of a twelve quarter trailing average of the sum of accumulated investments for each fund. In establishing this policy, the Foundation considered the long-term expected return on its endowment. Accordingly, over the long-term, the Foundation expects the current spending policy to allow its endowment to grow. This is consistent with the Foundation's objective to maintain the purchasing power of the endowment assets held in-perpetuity or for a specified term as well as to provide additional real growth through new gifts and investment return.

19. SUBSEQUENT EVENTS

In preparing these financial statements, the Foundation has evaluated events and transactions for potential recognition or disclosure through December 14, 2016, the date the financial statements were issued.

SUPPLEMENTAL INFORMATION

CHESAPEAKE BAY FOUNDATION, INC.**SUMMARY OF CONSERVATION AND SCENIC EASEMENTS
FOR INFORMATION PURPOSES ONLY (UNAUDITED)
FOR THE YEAR ENDED JUNE 30, 2016**

The Chesapeake Bay Foundation, Inc. (the Foundation) holds conservation and scenic easements on various properties in the Chesapeake Bay region that are designed to prohibit the property owner, his successor, heirs, or assignees from developing or altering the property in any way inconsistent with the easement. The Foundation has responsibility for enforcing the specific provisions of each easement, which are primarily obtained by donation. The following is a description of easements held at June 30, 2016.

Maryland

- Approximately 45 acres along the Tavern Creek in Kent County, Maryland
- Approximately 70 acres along the Southeast Creek in Queen Anne's County, Maryland
- Approximately 209 acres along the Pocomoke River in Somerset County, Maryland

Virginia

- Approximately 1 acre along the Smarts Creek/Potomac River in Westmoreland County, Virginia
- Approximately 2 acres along the Pamunkey River in King William County, Virginia
- Approximately 20 acres along Middle River in Augusta County, Virginia
- Approximately 20 acres along Brush Creek in Frederick County, Virginia
- Approximately 32 acres along the Dragon Run in Middlesex County, Virginia
- Approximately 37 acres along the Jordan River in Rappahannock County, Virginia
- Approximately 39 acres along the Totuskey Creek in Richmond County, Virginia
- Approximately 72 acres near Piscataway Creek in King and Queen and Essex Counties, Virginia
- Approximately 72 acres along the Chesapeake Bay in Northumberland County, Virginia
- Approximately 94 acres along Barnes Creek in Northumberland County, Virginia
- Approximately 118 acres along Mountain Run in Orange County, Virginia
- Approximately 150 acres along Garden Creek and the Chesapeake Bay in Mathews County, Virginia