

**FINANCIAL STATEMENTS**

**CHESAPEAKE BAY FOUNDATION, INC.**

**FOR THE YEAR ENDED JUNE 30, 2009  
WITH SUMMARIZED FINANCIAL  
INFORMATION FOR 2008**

**CHESAPEAKE BAY FOUNDATION, INC.**

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**GELMAN, ROSENBERG & FREEDMAN**  
**CERTIFIED PUBLIC ACCOUNTANTS**

**INDEPENDENT AUDITORS' REPORT**

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

We have audited the accompanying statement of financial position of the Chesapeake Bay Foundation, Inc. (the Foundation) as of June 30, 2009, and the related statements of activities and change in net assets, functional expenses and cash flows for the year then ended. These financial statements are the responsibility of the Foundation's management. Our responsibility is to express an opinion on these financial statements based on our audit. The prior year summarized comparative information has been derived from the Foundation's financial statements for the year ended June 30, 2008 and, in our report dated November 17, 2008, we expressed an unqualified opinion on those statements.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Foundation as of June 30, 2009, and its change in net assets and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated November 18, 2009 on our consideration of the Foundation's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

*Gelman Rosenberg & Freedman*

November 18, 2009

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**CHESAPEAKE BAY FOUNDATION, INC.**  
**STATEMENT OF FINANCIAL POSITION**  
**AS OF JUNE 30, 2009**  
**WITH SUMMARIZED FINANCIAL INFORMATION FOR 2008**

**ASSETS**

|  | <u>2009</u>                 | <u>2008</u>                 |
|--|-----------------------------|-----------------------------|
| Cash and cash equivalents  | \$ 5,414,562                | \$ 3,873,122                |
| Investments (Notes 2 and 16)   | 38,796,358                  | 48,189,659                  |
| Cash held in bond sinking fund (Note 8)  | 292,244                     | 287,024                     |
| Accounts receivable, less allowance for doubtful accounts of<br>\$3,563 and \$5,671 for 2009 and 2008, respectively (Note 3)                             | 599,313                     | 374,707                     |
| Note receivable (Note 4)   | 103,000                     | 103,000                     |
| Pledges receivable, net of allowance for doubtful accounts of<br>\$132,165 and \$163,719 for 2009 and 2008, respectively<br>(Notes 5 and 9)              | 9,934,186                   | 12,744,067                  |
| Other assets   | 287,441                     | 255,421                     |
| Deferred financing cost, net of accumulated amortization of<br>\$56,910 and \$51,490 for 2009 and 2008, respectively<br>(Note 8)                         | 78,591                      | 84,011                      |
| Property and equipment, net of accumulated depreciation and<br>amortization of \$11,883,830 and \$11,084,571 for 2009 and<br>2008, respectively (Note 6) | <u>20,995,963</u>           | <u>21,678,787</u>           |
| <b>TOTAL ASSETS</b>  | <b><u>\$ 76,501,658</u></b> | <b><u>\$ 87,589,798</u></b> |

**LIABILITIES AND NET ASSETS**

**LIABILITIES**

|   |                   |                   |
|---|-------------------|-------------------|
| Note payable (Note 7)                           | \$ 685,125        | \$ 720,112        |
| Bonds payable (Note 8)                          | 7,795,000         | 8,155,000         |
| Accounts payable and accrued expenses           | 1,632,096         | 1,932,234         |
| Deferred income                                 | 187,950           | 111,505           |
| Liability under split interest agreements       | 927,178           | 1,077,443         |
| Interest rate swap obligation (Notes 10 and 16) | <u>721,761</u>    | <u>499,675</u>    |
| Total liabilities                               | <u>11,949,110</u> | <u>12,495,969</u> |

**NET ASSETS**

|  |                             |                             |
|--|-----------------------------|-----------------------------|
| Unrestricted                             | 16,338,669                  | 25,012,007                  |
| Temporarily restricted (Note 11)         | 9,572,616                   | 11,552,889                  |
| Permanently restricted (Notes 11 and 17) | <u>38,641,263</u>           | <u>38,528,933</u>           |
| Total net assets                         | <u>64,552,548</u>           | <u>75,093,829</u>           |
| <b>TOTAL LIABILITIES AND NET ASSETS</b>  | <b><u>\$ 76,501,658</u></b> | <b><u>\$ 87,589,798</u></b> |

## CHESAPEAKE BAY FOUNDATION, INC.

**STATEMENT OF ACTIVITIES AND CHANGE IN NET ASSETS  
FOR THE YEAR ENDED JUNE 30, 2009  
WITH SUMMARIZED FINANCIAL INFORMATION FOR 2008**

|   | <b>2009</b>                 |                                   |                                   | <b>2008</b>                 |                             |
|---|-----------------------------|-----------------------------------|-----------------------------------|-----------------------------|-----------------------------|
|   | <b>Unrestricted</b>         | <b>Temporarily<br/>Restricted</b> | <b>Permanently<br/>Restricted</b> | <b>Total</b>                | <b>Total</b>                |
| <b>REVENUE</b>  |                             |                                   |                                   |                             |                             |
| Membership contributions                                      | \$ 5,084,819                | \$ -                              | \$ -                              | \$ 5,084,819                | \$ 5,130,217                |
| Grants and gifts (Note 9)                                     | 8,622,605                   | 4,391,926                         | -                                 | 13,014,531                  | 11,341,562                  |
| Education contracts and tuition                               | 1,146,090                   | -                                 | -                                 | 1,146,090                   | 1,160,718                   |
| Investment income (Note 2)                                    | 1,399,074                   | 618,909                           | -                                 | 2,017,983                   | 2,435,992                   |
| Donated goods and services (Note 15)                          | 351,066                     | 15,998                            | -                                 | 367,064                     | 298,506                     |
| Other   | 727,321                     | -                                 | -                                 | 727,321                     | 645,093                     |
| Net assets released from donor<br>restrictions (Note 11)      | <u>8,504,696</u>            | <u>(8,504,696)</u>                | <u>-</u>                          | <u>-</u>                    | <u>-</u>                    |
| Total revenue   | <u>25,835,671</u>           | <u>(3,477,863)</u>                | <u>-</u>                          | <u>22,357,808</u>           | <u>21,012,088</u>           |
| <b>EXPENSES</b>   |                             |                                   |                                   |                             |                             |
| Program Services:   |                             |                                   |                                   |                             |                             |
| Environmental Education                                       | 6,075,301                   | -                                 | -                                 | 6,075,301                   | 6,323,551                   |
| Environmental Protection and<br>Restoration                   | 9,469,932                   | -                                 | -                                 | 9,469,932                   | 8,853,805                   |
| Communications  | <u>2,766,796</u>            | <u>-</u>                          | <u>-</u>                          | <u>2,766,796</u>            | <u>3,175,809</u>            |
| Total program services  | <u>18,312,029</u>           | <u>-</u>                          | <u>-</u>                          | <u>18,312,029</u>           | <u>18,353,165</u>           |
| Support Services:   |                             |                                   |                                   |                             |                             |
| General and Administrative                                    | 1,698,116                   | -                                 | -                                 | 1,698,116                   | 1,742,560                   |
| Fundraising   | <u>3,073,912</u>            | <u>-</u>                          | <u>-</u>                          | <u>3,073,912</u>            | <u>3,215,347</u>            |
| Total support services  | <u>4,772,028</u>            | <u>-</u>                          | <u>-</u>                          | <u>4,772,028</u>            | <u>4,957,907</u>            |
| Total expenses  | <u>23,084,057</u>           | <u>-</u>                          | <u>-</u>                          | <u>23,084,057</u>           | <u>23,311,072</u>           |
| Change in net assets before capital<br>additions (deductions) | <u>2,751,614</u>            | <u>(3,477,863)</u>                | <u>-</u>                          | <u>(726,249)</u>            | <u>(2,298,984)</u>          |
| <b>CAPITAL ADDITIONS (DEDUCTIONS)</b>                         |                             |                                   |                                   |                             |                             |
| Investment return, net (Note 2)                               | (6,661,203)                 | (3,060,259)                       | (41,822)                          | (9,763,284)                 | (5,093,893)                 |
| Reclassification of net assets (Note 17)                      | (4,557,849)                 | 4,557,849                         | -                                 | -                           | -                           |
| Grants and gifts (Note 9)                                     | -                           | -                                 | 154,152                           | 154,152                     | 433,147                     |
| Donated property (Note 15)                                    | 17,036                      | -                                 | -                                 | 17,036                      | 222,966                     |
| (Loss) gain on sale/transfer of property                      | (850)                       | -                                 | -                                 | (850)                       | 79,259                      |
| Unrealized loss on interest rate swap<br>(Note 10)            | <u>(222,086)</u>            | <u>-</u>                          | <u>-</u>                          | <u>(222,086)</u>            | <u>(308,902)</u>            |
| Total capital additions<br>(deductions)                       | <u>(11,424,952)</u>         | <u>1,497,590</u>                  | <u>112,330</u>                    | <u>(9,815,032)</u>          | <u>(4,667,423)</u>          |
| Change in net assets  | (8,673,338)                 | (1,980,273)                       | 112,330                           | (10,541,281)                | (6,966,407)                 |
| Net assets at beginning of year                               | <u>25,012,007</u>           | <u>11,552,889</u>                 | <u>38,528,933</u>                 | <u>75,093,829</u>           | <u>82,060,236</u>           |
| <b>NET ASSETS AT END OF YEAR</b>                              | <b><u>\$ 16,338,669</u></b> | <b><u>\$ 9,572,616</u></b>        | <b><u>\$ 38,641,263</u></b>       | <b><u>\$ 64,552,548</u></b> | <b><u>\$ 75,093,829</u></b> |

See accompanying notes to financial statements.

CHESAPEAKE BAY FOUNDATION, INC.

STATEMENT OF FUNCTIONAL EXPENSES  
FOR THE YEAR ENDED JUNE 30, 2009  
WITH SUMMARIZED FINANCIAL INFORMATION FOR 2008

2009

|   | Program Services           |  |                     | Total<br>Program<br>Services |
|---|----------------------------|--|---------------------|------------------------------|
|   | Environmental<br>Education | Environmental<br>Protection and<br>Restoration | Communications      |                              |
| Salaries  | \$ 2,375,140               | \$ 3,562,143                                   | \$ 926,452          | \$ 6,863,735                 |
| Fringe benefits (Note 13)                             | 842,836                    | 1,278,838                                      | 340,795             | 2,462,469                    |
| Supplies  | 204,627                    | 144,738  | 42,678              | 392,043                      |
| Restoration supplies                                  | -                          | 281,198  | -                   | 281,198                      |
| Telephone   | 48,206                     | 80,006   | 9,365               | 137,577                      |
| Postage and shipping                                  | 114,907                    | 200,015  | 149,165             | 464,087                      |
| Occupancy and utilities (Notes 10 and 12)             | 511,277                    | 632,383  | 133,686             | 1,277,346                    |
| Equipment rental, leasing, repairs and<br>maintenance | 149,239                    | 97,492   | 21,622              | 268,353                      |
| Printing and publications                             | 150,195                    | 266,087  | 354,469             | 770,751                      |
| Dues and subscriptions                                | 1,887                      | 38,854   | 12,905              | 53,646                       |
| Travel  | 235,980                    | 144,002  | 13,636              | 393,618                      |
| Meetings and seminars                                 | 44,543                     | 91,766   | 14,354              | 150,663                      |
| Outside services                                      | 17,114                     | 31,207   | 318,871             | 367,192                      |
| Boat charter  | 39,228                     | 1,783  | 500                 | 41,511                       |
| Professional fees                                     | 369,785                    | 1,291,909                                      | 193,682             | 1,855,376                    |
| Restoration fees                                      | -                          | 233,846  | -                   | 233,846                      |
| Personnel recruitment                                 | -                          | 1,323  | -                   | 1,323                        |
| Miscellaneous   | 12,013                     | 28,816   | 2,130               | 42,959                       |
| Mailing preparation                                   | 32,542                     | 50,564   | 14,777              | 97,883                       |
| Honorariums/stipends                                  | 550                        | 454  | 1,000               | 2,004                        |
| Insurance   | 181,725                    | 57,144   | 8,627               | 247,496                      |
| List rentals  | 42,730                     | 66,393   | 19,403              | 128,526                      |
| Depreciation and amortization - other                 | 223,381                    | 41,592   | 32,567              | 297,540                      |
| Subcontracts  | 203,380                    | 252,750  | -                   | 456,130                      |
| In-kind   | 2,212                      | 171,588  | 32,295              | 206,095                      |
| Sub-total   | 5,803,497                  | 9,046,891                                      | 2,642,979           | 17,493,367                   |
| Allocation of management and general                  | 271,804                    | 423,041  | 123,817             | 818,662                      |
| <b>TOTAL</b>  | <b>\$ 6,075,301</b>        | <b>\$ 9,469,932</b>                            | <b>\$ 2,766,796</b> | <b>\$ 18,312,029</b>         |

|                                       |                            |                                       |                             |                             | <b>2008</b> |
|---------------------------------------|----------------------------|---------------------------------------|-----------------------------|-----------------------------|-------------|
| <b>Support Services</b>               |                            |                                       |                             |                             |             |
| <b>General and<br/>Administrative</b> | <b>Fundraising</b>         | <b>Total<br/>Support<br/>Services</b> | <b>Total<br/>Expenses</b>   | <b>Total<br/>Expenses</b>   |             |
| \$ 1,289,188                          | \$ 1,119,561               | \$ 2,408,749                          | \$ 9,272,484                | \$ 9,258,092                |             |
| 471,572                               | 410,464                    | 882,036                               | 3,344,505                   | 3,278,406                   |             |
| 37,467                                | 56,110                     | 93,577                                | 485,620                     | 779,170                     |             |
| -                                     | -                          | -                                     | 281,198                     | 109,434                     |             |
| 7,520                                 | 11,281                     | 18,801                                | 156,378                     | 151,520                     |             |
| 4,091                                 | 193,868                    | 197,959                               | 662,046                     | 639,656                     |             |
| 244,146                               | 118,999                    | 363,145                               | 1,640,491                   | 1,667,938                   |             |
| 51,848                                | 34,108                     | 85,956                                | 354,309                     | 415,026                     |             |
| 6,122                                 | 234,748                    | 240,870                               | 1,011,621                   | 979,722                     |             |
| 2,637                                 | 3,811                      | 6,448                                 | 60,094                      | 74,704                      |             |
| 50,463                                | 42,367                     | 92,830                                | 486,448                     | 583,320                     |             |
| 42,359                                | 66,903                     | 109,262                               | 259,925                     | 325,367                     |             |
| 80,356                                | 66,725                     | 147,081                               | 514,273                     | 419,895                     |             |
| 50                                    | 125                        | 175                                   | 41,686                      | 42,435                      |             |
| 275,898                               | 214,299                    | 490,197                               | 2,345,573                   | 2,956,952                   |             |
| -                                     | -                          | -                                     | 233,846                     | 152,562                     |             |
| 9,212                                 | -                          | 9,212                                 | 10,535                      | 15,608                      |             |
| 43,927                                | 12,413                     | 56,340                                | 99,299                      | 149,724                     |             |
| -                                     | 63,955                     | 63,955                                | 161,838                     | 165,682                     |             |
| -                                     | -                          | -                                     | 2,004                       | 22,524                      |             |
| 20,766                                | 18,679                     | 39,445                                | 286,941                     | 273,509                     |             |
| -                                     | 99,580                     | 99,580                                | 228,106                     | 230,394                     |             |
| 16,518                                | 7,585                      | 24,103                                | 321,643                     | 296,201                     |             |
| -                                     | -                          | -                                     | 456,130                     | 24,725                      |             |
| <u>178</u>                            | <u>160,791</u>             | <u>160,969</u>                        | <u>367,064</u>              | <u>298,506</u>              |             |
| 2,654,318                             | 2,936,372                  | 5,590,690                             | 23,084,057                  | 23,311,072                  |             |
| <u>(956,202)</u>                      | <u>137,540</u>             | <u>(818,662)</u>                      | <u>-</u>                    | <u>-</u>                    |             |
| <b><u>\$ 1,698,116</u></b>            | <b><u>\$ 3,073,912</u></b> | <b><u>\$ 4,772,028</u></b>            | <b><u>\$ 23,084,057</u></b> | <b><u>\$ 23,311,072</u></b> |             |

See accompanying notes to financial statements.

## CHESAPEAKE BAY FOUNDATION, INC.

**STATEMENT OF CASH FLOWS  
FOR THE YEAR ENDED JUNE 30, 2009  
WITH SUMMARIZED FINANCIAL INFORMATION FOR 2008**

|   | <u>2009</u>      | <u>2008</u>        |
|---|------------------|--------------------|
| <b>CASH FLOWS FROM OPERATING ACTIVITIES</b>   |                  |                    |
| Change in net assets  | \$ (10,541,281)  | \$ (6,966,407)     |
| Adjustments to reconcile change in net assets to net cash provided by operating activities: |                  |                    |
| Depreciation and amortization   | 932,263          | 895,094            |
| Unrealized loss on interest rate swap   | 222,086          | 308,902            |
| Loss (gain) on sale/transfer of property  | 850              | (79,259)           |
| Donated property  | (17,036)         | (222,966)          |
| Capital additions - permanently restricted contributions                                    | (154,152)        | (433,147)          |
| Change in the discount of long-term pledges receivable                                      | (293,318)        | (1,064,136)        |
| Change in allowance for doubtful accounts   | (33,662)         | (35,276)           |
| Unrealized loss   | 4,691,093        | 4,692,076          |
| Realized loss   | 3,631,400        | 45,728             |
| (Increase) decrease in:   |                  |                    |
| Accounts receivable   | (222,498)        | 632,523            |
| Pledges receivable  | 3,134,753        | 3,934,896          |
| Other assets  | (32,020)         | 31,729             |
| Increase (decrease) in:   |                  |                    |
| Accounts payable and accrued expenses   | (300,138)        | (61,922)           |
| Deferred income   | 76,445           | 65,895             |
| Liability under split interest agreements   | <u>(150,265)</u> | <u>6,048</u>       |
| Net cash provided by operating activities   | <u>944,520</u>   | <u>1,749,778</u>   |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES</b>   |                  |                    |
| Net proceeds (purchases) of investments   | 1,070,808        | (715,587)          |
| Purchases of property   | (229,083)        | (654,894)          |
| Proceeds from sale of property  | <u>1,250</u>     | <u>88,000</u>      |
| Net cash provided (used) by investing activities  | <u>842,975</u>   | <u>(1,282,481)</u> |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES</b>   |                  |                    |
| Capital additions - permanently restricted contributions                                    | 154,152          | 433,147            |
| Increase in cash held for bond sinking fund   | (5,220)          | (8,210)            |
| Payments on bonds payable   | (360,000)        | (340,000)          |
| Payments on note payable  | <u>(34,987)</u>  | <u>(25,888)</u>    |
| Net cash provided (used) by financing activities  | <u>(246,055)</u> | <u>59,049</u>      |

See accompanying notes to financial statements.



CHESAPEAKE BAY FOUNDATION, INC.

STATEMENT OF CASH FLOWS  
FOR THE YEAR ENDED JUNE 30, 2009  
WITH SUMMARIZED FINANCIAL INFORMATION FOR 2008

|   | <u>2009</u>                | <u>2008</u>                |
|---|----------------------------|----------------------------|
| Net increase in cash and cash equivalents       | \$ 1,541,440               | \$ 526,346                 |
| Cash and cash equivalents at beginning of year  | <u>3,873,122</u>           | <u>3,346,776</u>           |
| <b>CASH AND CASH EQUIVALENTS AT END OF YEAR</b> | <b><u>\$ 5,414,562</u></b> | <b><u>\$ 3,873,122</u></b> |
| <br><b>SUPPLEMENTAL INFORMATION:</b>            |                            |                            |
| Interest Paid                                   | <u>\$ 353,044</u>          | <u>\$ 362,208</u>          |

**CHESAPEAKE BAY FOUNDATION, INC.**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2009**

**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 lands 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 Statement of Financial Accounting Standards No. 117, "Financial Statements of Not-for-Profit Organizations".

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, 2008, 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 nine months or less to be cash equivalents, excluding cash and cash equivalents held by investment managers in the amounts of \$7,351,925 and \$6,521,682, for the years ended June 30, 2009 and 2008, respectively.

At times during the year, the Foundation maintains 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, real estate investment trusts, money market funds held for investment purposes, limited partnerships, and a non-domestic professional fund. 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 on 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 relate 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, 2009

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.

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.

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 one of its investments. Accordingly, the Foundation has recorded income tax expense in the amount of \$39,693 for the year ended June 30, 2009. An unrelated business income tax in the amount of \$5,000 was recorded as a liability and included in the Statement of Financial Position as of June 30, 2009.

During fiscal year 2009, management elected to implement FASB Interpretation No. (FIN) 48, *Accounting for Uncertainty in Income Taxes*. As a result, the Foundation did not identify any uncertain tax positions that qualify for either recognition or disclosure in the financial statements.

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.

CHESAPEAKE BAY FOUNDATION, INC.

NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2009

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

Net asset classification (continued) -

- **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. 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. Contributions and grants received in excess of expenses incurred are shown as temporarily restricted net assets in the accompanying 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 measurements -

The Foundation adopted the provisions of Statement of Financial Accounting Standards (SFAS) No. 157, entitled *Fair Value Measurements*. SFAS No. 157 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.

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.

Reclassification -

Certain amounts in the prior year's financial statements have been reclassified to conform to the current year's presentation.

Deferred financing costs -

Deferred financing costs represent bond issuance costs and other costs related to the acquisition of the Bay Ridge Facility for use as the Foundation's Headquarters (Note 8). Deferred financing costs are being amortized over the life of the bonds.

**CHESAPEAKE BAY FOUNDATION, INC.**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2009**

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

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. 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, 2009 and 2008, liabilities under split interest agreements totaled \$927,178 and \$1,077,443, respectively.

Joint costs -

For fiscal years 2009 and 2008, the Foundation incurred joint costs of \$2,260,215 and \$2,222,874, respectively.

For the years ended June 30, 2009 and 2008, joint costs were comprised of the following

|  | <u>2009</u>                | <u>2008</u>                |
|--|----------------------------|----------------------------|
| Environmental Education                  | \$ 506,082                 | \$ 492,434                 |
| Environmental Protection and Restoration | 786,342                    | 683,568                    |
| Communications                           | 229,806                    | 243,882                    |
| Fundraising                              | 737,985                    | 721,953                    |
| General and Administrative               | <u>-</u>                   | <u>81,037</u>              |
| <b>TOTAL JOINT COSTS INCURRED</b>        | <b><u>\$ 2,260,215</u></b> | <b><u>\$ 2,222,874</u></b> |

**2. INVESTMENTS**

At June 30, 2009 and 2008, investments at readily determinable fair values consisted of the following:

|   | <u>2009</u>                 | <u>2008</u>                 |
|---|-----------------------------|-----------------------------|
| Equity securities                                     | 13,439,020                  | 21,511,698                  |
| Partnerships/Alternative investments                  | 11,247,954                  | 12,651,487                  |
| Corporate bonds and other agencies                    | 3,797,730                   | 4,387,932                   |
| Beneficial interest in perpetual trust                | 2,924,350                   | 2,924,350                   |
| U.S. Government obligations                           | <u>35,379</u>               | <u>192,510</u>              |
| Sub-total investments                                 | 31,444,433                  | 41,667,977                  |
| Cash and cash equivalents held by investment managers | <u>7,351,925</u>            | <u>6,521,682</u>            |
| <b>TOTAL INVESTMENTS</b>                              | <b><u>\$ 38,796,358</u></b> | <b><u>\$ 48,189,659</u></b> |

Under the terms of certain agreements for several alternative investments, the Foundation is obligated to remit additional funding periodically as capital calls are exercised.

**CHESAPEAKE BAY FOUNDATION, INC.**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2009**

**2. INVESTMENTS (Continued)**

As of June 30, 2009 and 2008, the Foundation has uncalled commitments of \$571,140 and \$744,088, respectively.

Alternative investments are comprised of the following at June 30, 2009:

| <u>Investment Type</u>              | <u>Amount</u>              | <u>Liquidity</u>                                     |
|-------------------------------------|----------------------------|--|
| Domestic/ U.S. Limited Partnerships | \$ 1,758,877               | None until dissolution or winding up of partnership. |
| Domestic/ U.S. Limited Partnerships | 1,878,180                  | No lock up.  |
| Domestic/ U.S. Limited Partnership  | 2,000,579                  | Last day of each quarter.                            |
| Offshore investment funds           | <u>5,610,318</u>           | Last day of each quarter.                            |
| <b>ALTERNATIVE INVESTMENTS</b>      | <b><u>\$11,247,954</u></b> |  |

Alternative investments are comprised of the following at June 30, 2008:

| <u>Investment Type</u>              | <u>Amount</u>              | <u>Liquidity</u>                                     |
|-------------------------------------|----------------------------|--|
| Domestic/ U.S. Limited Partnerships | \$ 1,801,532               | None until dissolution or winding up of partnership. |
| Domestic/ U.S. Limited Partnerships | 1,847,530                  | No lock up.  |
| Domestic/ U.S. Limited Partnership  | 2,490,900                  | Last day of each quarter.                            |
| Offshore investment funds           | <u>6,511,525</u>           | Last day of each quarter.                            |
| <b>ALTERNATIVE INVESTMENTS</b>      | <b><u>\$12,651,487</u></b> |  |

Included in the investment balance at June 30, 2009 and 2008 are investments related to certain split-interest agreements in the amounts of \$1,538,599 and \$1,851,175, respectively.

It is the policy of the Foundation to spend on operations 5% of a twelve quarter trailing average of the sum of accumulated investments. If investment earnings do not meet this 5% target in a given year, a transfer from Board Designated Funds will be made to the General Operating Fund. If, in a given year, investment earnings exceed this 5% target, a transfer will be made from the General Operating Fund to Board Designated Funds. All earnings that exceed this target and all losses in a given year are considered non-operating and are shown as capital additions (deductions) in the Statement of Activities and Change in Net Assets.

Investment return for the years ended June 30, 2009 and 2008 consisted of the following:

|   | <u>2009</u>                  | <u>2008</u>                  |
|---|------------------------------|------------------------------|
| Interest and dividends                      | \$ 577,192                   | \$ 2,079,903                 |
| Unrealized loss                             | (4,691,093)                  | (4,692,076)                  |
| Realized loss                               | <u>(3,631,400)</u>           | <u>(45,728)</u>              |
| Total investment return                     | (7,745,301)                  | (2,657,901)                  |
| Less: Investment income used for operations | <u>(2,017,983)</u>           | <u>(2,435,992)</u>           |
| <b>NET INVESTMENT RETURN</b>                | <b><u>\$ (9,763,284)</u></b> | <b><u>\$ (5,093,893)</u></b> |

**CHESAPEAKE BAY FOUNDATION, INC.**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2009**

**2. INVESTMENTS (Continued)**

Subsequent to June 30, 2009, the fair market value of the investment portfolio increased by the estimated amount of \$2,200,000.

**3. ACCOUNTS RECEIVABLE**

Accounts receivable are stated at their carrying value, which approximates fair value. 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, 2009 and 2008, respectively:

|                                       | <b>2009</b>       | <b>2008</b>       |
|---------------------------------------|-------------------|-------------------|
| Federal receivables                   | \$ 401,024        | \$ 227,309        |
| Non-Federal receivables               | 201,852           | 153,069           |
| Total accounts receivable             | 602,876           | 380,378           |
| Less: Allowance for doubtful accounts | (3,563)           | (5,671)           |
| <b>NET ACCOUNTS RECEIVABLE</b>        | <b>\$ 599,313</b> | <b>\$ 374,707</b> |

**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, on July 1, 1999, the note was extended every year and is now due July 1, 2010. Only monthly payments of interest are to be made by the Tribe until maturity. The amount outstanding at June 30, 2009 and 2008 was \$103,000.

**5. PLEDGES RECEIVABLE**

As of June 30, 2009 and 2008, contributors to the Foundation have made written promises to give totaling \$13,254,235 and \$16,388,989, 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 1.25% 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, 2009 and 2008:

|                                       | <b>2009</b>         | <b>2008</b>          |
|---------------------------------------|---------------------|----------------------|
| Less than one year                    | \$ 4,367,500        | \$ 4,565,803         |
| One to five years                     | 2,080,284           | 4,455,826            |
| Beyond five years                     | 6,806,452           | 7,367,360            |
| Total pledges                         | 13,254,236          | 16,388,989           |
| Less: Discount to net present value   | (3,187,885)         | (3,481,203)          |
| Less: Allowance for doubtful accounts | (132,165)           | (163,719)            |
| <b>NET PLEDGES RECEIVABLE</b>         | <b>\$ 9,934,186</b> | <b>\$ 12,744,067</b> |

**CHESAPEAKE BAY FOUNDATION, INC.**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2009**

**6. PROPERTY AND EQUIPMENT**

Property and equipment consisted of the following at June 30, 2009 and 2008:

|   | <b>2009</b>                     | <b>2008</b>                     |
|---|---------------------------------|---------------------------------|
| Land  | \$ 10,315,411                   | \$ 10,315,411                   |
| Building and improvements                       | 14,918,382                      | 14,767,081                      |
| Furniture and equipment                         | 3,530,877                       | 3,571,882                       |
| Boats   | 3,643,850                       | 3,602,985                       |
| Vehicles  | 454,273                         | 488,999                         |
| Art   | 17,000                          | 17,000                          |
| <br>Total property and equipment                | <br>32,879,793                  | <br>32,763,358                  |
| Less: Accumulated depreciation and amortization | (11,883,830)                    | (11,084,571)                    |
| <br><b>NET PROPERTY AND EQUIPMENT</b>           | <br><b><u>\$ 20,995,963</u></b> | <br><b><u>\$ 21,678,787</u></b> |

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 \$7,916,052 at June 30, 2009 and 2008.

**7. NOTE PAYABLE**

In January, 2007 the Foundation entered into a \$746,000 purchase money note payable to a trust. The annual interest rate is 5.62%. The maturity date is March 2022.

As of June 30, 2009 and 2008, respectively, the outstanding principal of the note payable was \$685,125 and \$720,112.

Principal payments are due as follows:

| <u>Year Ended June 30,</u> |  |                              |
|----------------------------|--|------------------------------|
| 2010                       |  | \$ 36,982                    |
| 2011                       |  | 39,091                       |
| 2012                       |  | 41,321                       |
| 2013                       |  | 43,677                       |
| 2014                       |  | 46,168                       |
| 2015 and Thereafter        |  | 477,886                      |
|                            |  | <br><b><u>\$ 685,125</u></b> |

**8. BONDS PAYABLE**

On July 6, 1998, the Foundation purchased a 33-acre parcel of land, the Bay Ridge Facility, located just outside the city of Annapolis, Maryland, for its central headquarters for approximately \$3.7 million. A \$4 million bridge loan from Wachovia Bank, N.A. (formerly known as First Union National Bank) was used to purchase the site. Also, U.S. Bank, N.A. completed the purchase of the corporate trust and institutional custody businesses of Wachovia Corporation (NYSE:WB) on December 30, 2005.



CHESAPEAKE BAY FOUNDATION, INC.

NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2009

8. BONDS PAYABLE (Continued)

On November 1, 1998, the Foundation issued variable rate bonds ("Variable Rate Economic Development Revenue Bonds, Series 1998") in the amount of \$10 million through the Maryland Economic Development Corporation. The proceeds of the bonds were used to repay the bridge loan with Wachovia Bank, N.A. and finance the acquisition, construction and equipping of a portion of the Bay Ridge Facility. In December 2000, The Foundation moved into its U.S. Green Building Council LEED Platinum headquarters, a facility called the Philip Merrill Environmental Center and widely recognized as one of the most environmentally innovative buildings in the world. The facilities include a two-story, 30,000 square foot "green" office building and common meeting centers for internal and external groups. Since moving to the Merrill Center, much of the site has been restored with native plants, and there are plans to continue native restoration.

Interest only payments were due on the bonds until November 2001, when mandatory sinking fund and interest payments were due monthly with the final payment due October 1, 2023. Financing costs in the amount of \$135,501 were capitalized and amortized over the life of the bonds. At June 30, 2009 and 2008, deferred financing costs, net of accumulated depreciation and amortization, totaled \$78,591 and \$84,011, respectively.

The bonds are secured by a letter of credit issued by Wachovia Bank in the amount of \$7,918,012, resetting on November 1, 2009. The letter of credit is secured by the Foundation's interest in the facility fund, the bond fund, and all funds that are under the control of Wachovia Bank. The bonds bear interest at variable rates that is determined weekly by Wachovia Capital Markets in order to place the bonds at 100% par with a final maturity date of November 1, 2023. 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 year ending June 30, 2009, the Foundation was not in compliance with the bond covenants. The Foundation received a waiver from the creditor. For the year ended June 30, 2008, the Foundation was in compliance with the bond covenants.

The Foundation has cash set aside in a bond sinking fund in the amounts of \$292,244 and \$287,024 for the years ending June 30, 2009 and 2008, respectively.

As of June 30, 2009 and 2008, respectively, the outstanding principal of the bond payable totaled \$7,795,000 and \$8,155,000.

Principal payments are due as follows:

| <u>Year Ended June 30,</u> |                            |
|----------------------------|----------------------------|
| 2010                       | \$ 375,000                 |
| 2011                       | 390,000                    |
| 2012                       | 410,000                    |
| 2013                       | 425,000                    |
| 2014                       | 445,000                    |
| 2015 and Thereafter        | <u>5,750,000</u>           |
| <b>BONDS PAYABLE</b>       | <b><u>\$ 7,795,000</u></b> |

**CHESAPEAKE BAY FOUNDATION, INC.**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2009**

**9. RELATED PARTY**

For the years ended June 30, 2009 and 2008, the Foundation received gross pledges in the amounts of \$280,550 and \$342,500, respectively, from its Trustees and their associated companies. Net amounts due under pledges receivable from the Foundation's Trustees and their associated companies totaled \$3,712,582 and \$6,821,441 as of June 30, 2009 and 2008, respectively.

**10. INTEREST RATE SWAP**

The bonds discussed in Note 8 include interest payments based on the Securities Industry and Financial Markets Association ("SIFMA") Index, formerly the Bond Market Association (BMA) Index. As a means to reduce its exposure to volatility in the variable rate index (SIFMA), the Foundation entered into the following interest rate swap agreements with Wachovia Bank, N.A. in connection with its Variable Rate Economic Development Revenue Bonds, Series 1998. The intention of the swap agreement is to synthetically fix the interest rate on the bonds.

On November 5, 1998, the Foundation entered into an interest-rate swap agreement to fix one-half of its outstanding variable rate bonds at a synthetic fixed rate of 5.00%. On January 6, 2004, one-quarter of the remaining variable rate bonds was synthetically fixed at a rate of 3.25%. On May 26, 2005, the Foundation cancelled all previous interest-rate swap agreements and fixed the outstanding notional of \$9,140,000 to a synthetic fixed rate of 4.33%. Interest on the swap is due monthly.

The Foundation incurred total interest expense on the bonds of \$353,044 and \$362,208 for the years ended June 30, 2009 and 2008, respectively, and is included in occupancy and utilities expense within the Statement of Functional Expenses.

The bonds and the related swap agreement mature on November 1, 2023 and the swap notional amount of \$9,140,000 will hedge 100% of the outstanding variable-rate bonds as of the effective date of the swap, June 1, 2005. Starting in fiscal year 2006, the combined notional value of the swap and the combined principal amount of the associated debt will decline. For the years ended June 30, 2009 and 2008, the outstanding notional amount was \$7,795,000 and \$8,155,000, respectively. Under the swap, the Foundation pays Wachovia Bank a fixed rate of 4.33% and receives a variable rate at SIFMA.

As of June 30, 2009 and 2008, the swap had a negative fair value of \$721,761 and \$499,675, respectively, which is reflected in the financial statements. The swap valuations were established by market quotations from Wachovia Bank representing estimates of the amounts that would be paid upon terminating the agreement.

As of June 30, 2009, the Foundation was not exposed to credit risk because the swap had a negative fair value. The Foundation is only exposed to credit risk if the swap has a positive fair value. The swap counterparty (Wachovia Bank) was rated Aa2 by Moody's Investors Service (Moody's), AA by Standard and Poor's (S&P) and AA- by Fitch Ratings (Fitch). In addition, since the swap agreement was executed to the maturity of the underlying bonds there is no rollover risk.

The SIFMA swap exposes the Foundation to basis risk should the actual rate on the Foundation's bonds exceed the SIFMA Index. Since the Foundation's bonds are based upon the SIFMA Index, there is relatively little basis risk. Should the Foundation terminate the swap prior to maturity, the Foundation will either receive or pay a termination payment. This payment is equal to the fair value of the swap at the time the swap is terminated.

**CHESAPEAKE BAY FOUNDATION, INC.**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2009**

**11. RESTRICTED NET ASSETS**

**Temporarily restricted net assets:**

Temporarily restricted net assets consisted of the following at June 30, 2009 and 2008:

|  | <u>2009</u>                | <u>2008</u>                 |
|--|----------------------------|-----------------------------|
| <b>Program Restricted:</b>               |                            |                             |
| Environmental Education                  | \$ 728,994                 | \$ 506,028                  |
| Environmental Protection and Restoration | 607,720                    | 1,626,838                   |
| Communications                           | 9,900                      | 9,717                       |
| Time restricted (death of donors)        | 2,701,962                  | 2,920,609                   |
| Property and equipment                   | 28,329                     | 515,579                     |
| Other                                    | <u>38,488</u>              | <u>38,776</u>               |
| Total program restricted                 | 4,115,393                  | 5,617,547                   |
| Time Restricted                          | <u>5,457,223</u>           | <u>5,935,342</u>            |
| <b>TEMPORARILY RESTRICTED NET ASSETS</b> | <b><u>\$ 9,572,616</u></b> | <b><u>\$ 11,552,889</u></b> |

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.

**Temporarily restricted net assets released from restrictions:**

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:

|  | <u>2009</u>                | <u>2008</u>                |
|--|----------------------------|----------------------------|
| <b>Donor Restrictions:</b>                   |                            |                            |
| Environmental Education                      | \$ 1,630,364               | \$ 738,195                 |
| Environmental Protection and Restoration     | 2,350,415                  | 1,934,283                  |
| Communications                               | 10,000                     | 5,000                      |
| Time restricted (death of donors)            | -                          | 51,342                     |
| Property and equipment                       | 298,887                    | 300,000                    |
| Other  | <u>56,874</u>              | <u>122,892</u>             |
| Total donor restrictions                     | 4,346,540                  | 3,151,712                  |
| Time Restricted                              | <u>4,158,156</u>           | <u>3,635,672</u>           |
| <b>NET ASSETS RELEASED FROM RESTRICTIONS</b> | <b><u>\$ 8,504,696</u></b> | <b><u>\$ 6,787,384</u></b> |

CHESAPEAKE BAY FOUNDATION, INC.

NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2009

11. RESTRICTED NET ASSETS (Continued)

Permanently restricted net assets:

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

|  | <u>2009</u>                 | <u>2008</u>                 |
|--|-----------------------------|-----------------------------|
| Environmental Education                  | \$ 8,036,397                | \$ 8,034,625                |
| Environmental Protection and Restoration | 8,574,325                   | 8,574,325                   |
| Property and equipment                   | 7,916,052                   | 7,916,052                   |
| General operating                        | <u>14,114,489</u>           | <u>14,003,931</u>           |
| <b>PERMANENTLY RESTRICTED NET ASSETS</b> | <b><u>\$ 38,641,263</u></b> | <b><u>\$ 38,528,933</u></b> |

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 Ended June 30,</u> |                          |
|----------------------------|--------------------------|
| 2010                       | \$ 185,403               |
| 2011                       | 90,882                   |
| 2012                       | 75,284                   |
| 2013                       | 64,843                   |
| 2014                       | <u>66,310</u>            |
| <b>LEASE COMMITMENT</b>    | <b><u>\$ 482,722</u></b> |

Rent expense for the years ended June 30, 2009 and 2008 totaled \$242,368 and \$244,447, respectively.

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, 2009 and 2008, the Foundation made contributions in the amounts of \$366,479 and \$353,715, respectively.

## CHESAPEAKE BAY FOUNDATION, INC.

### NOTES TO FINANCIAL STATEMENTS JUNE 30, 2009

#### 14. CONTINGENCY

The Foundation receives grants from various agencies of the United States Government. Such grants are subject to audit under the provisions of OMB Circular A-133. 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 provisions of OMB Circular A-133 have been completed for all required fiscal years through 2009. 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.

#### 15. DONATED GOODS, SERVICES, AND PROPERTY

During the years ended June 30, 2009 and 2008, the Foundation was the beneficiary of donated goods and services, which allow the Foundation to provide greater resources towards various programs. To properly reflect total program expenses, donations totaling \$367,064 and \$298,506 have been included in revenue and expense for the years ended June 30, 2009 and 2008, respectively. In addition, the Foundation was the beneficiary of donated property and equipment totaling \$17,036 and \$222,966 for the years ended June 30, 2009 and 2008, respectively. These assets were capitalized at their fair value and the income is recognized in the Statement of Activities and Change in Net Assets.

#### 16. FAIR VALUE MEASUREMENTS

In accordance with Statement of Financial Accounting Standards (SFAS) No. 157, 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 financial instruments where values are based on unadjusted quoted prices for identical assets or liabilities in an active market the Foundation has the ability to access.

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

**Level 3.** These are financial instruments where values are based on prices or valuation techniques that require inputs that are both unobservable and significant to the overall fair value measurement. These inputs reflect assumptions of management about assumptions market participants would use in pricing the financial instruments. These financial instruments include non-readily marketable securities that do not have an active market.

**CHESAPEAKE BAY FOUNDATION, INC.**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2009**

**16. FAIR VALUE MEASUREMENTS (Continued)**

Financial instruments recorded in the Statement of Financial Position are categorized based on the inputs to the valuation technique as follows for the year ended June 30, 2009:

|                                      | <u>Level 1</u>       | <u>Level 2</u>      | <u>Level 3</u>       | <u>Total<br/>June 30, 2009</u> |
|--------------------------------------|----------------------|---------------------|----------------------|--------------------------------|
| <b>Assets:</b>                       |                      |                     |                      |                                |
| <b>Investments</b>                   | \$ <u>24,142,905</u> | \$ <u>3,405,499</u> | \$ <u>11,247,954</u> | \$ <u>38,796,358</u>           |
| <b>Liability:</b>                    |                      |                     |                      |                                |
| <b>Interest Rate Swap Obligation</b> | \$ <u>-</u>          | \$ <u>721,761</u>   | \$ <u>-</u>          | \$ <u>721,761</u>              |

**Level 3 Financial Assets**

The change in fair value of the Foundation's assets using significant unobservable inputs (Level 3) for the year ended June 30, 2009:

|                                      | <u>Investments</u>   |
|--------------------------------------|----------------------|
| Beginning balance as of July 1, 2008 | \$ 12,651,487        |
| Unrealized and realized losses       | (1,386,325)          |
| Earned income                        | 46,721               |
| Purchases/Distributions              | <u>(63,929)</u>      |
| <b>BALANCE AS OF JUNE 30, 2009</b>   | \$ <u>11,247,954</u> |

**17. ENDOWMENT**

In August of 2008, the Financial Accounting Standards Board (FASB) issued FASB Staff Position No. 117-1, Endowments of Not-for-Profit Organizations: Net Asset Classification of Funds Subject to an Enacted Version of The Uniform Prudent Management of Institutional Funds Act, and Enhanced Disclosures for All Endowment Funds. The FASB Staff Position (FSP 117-1) provides guidance on the net asset classification of donor-restricted endowment funds for a non-for-profit organization that is subject to an enacted version of the Uniform Prudent Management of Institutional Funds Act of 2006. In 2009, Maryland signed into law the Uniform Prudent Management of Institutional Funds Act of 2007 (UPMIFA). The law became effective April 14, 2009. The Foundation implemented FSP-117-1 in 2009 and evaluated its endowment funds to ensure compliance with UPMIFA. As a result, the Foundation reclassified \$4,557,849 of unrestricted net assets to temporarily restricted net assets due to the change in law.

The Foundation's Board of Directors 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.

**CHESAPEAKE BAY FOUNDATION, INC.**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2009**

**17. 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 organization and 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
- Investment policies of the organization.

Endowment net asset composition by type of fund as of June 30, 2009:

|   | <b>Unrestricted</b>          | <b>Temporarily<br/>Restricted</b> | <b>Permanently<br/>Restricted</b> | <b>Total</b>                |
|---|------------------------------|-----------------------------------|-----------------------------------|-----------------------------|
| <b>Donor-Restricted Endowment<br/>Funds</b> | <b><u>\$ (3,698,919)</u></b> | <b><u>\$ 1,812,239</u></b>        | <b><u>\$ 38,641,263</u></b>       | <b><u>\$ 36,754,583</u></b> |

Changes in endowment net assets for the year ended June 30, 2009:

|  | <b>Unrestricted</b>          | <b>Temporarily<br/>Restricted</b> | <b>Permanently<br/>Restricted</b> | <b>Total</b>                |
|--|------------------------------|-----------------------------------|-----------------------------------|-----------------------------|
| Endowment net assets, beginning of year            | \$ 4,557,849                 | \$ -                              | \$ 38,528,933                     | \$ 43,086,782               |
| Net assets reclassification based on change of law | <u>(4,557,849)</u>           | <u>4,557,849</u>                  | <u>-</u>                          | <u>-</u>                    |
| Endowment net assets after reclassification        | <u>-</u>                     | <u>4,557,849</u>                  | <u>38,528,933</u>                 | <u>43,086,782</u>           |
| Interest and dividends                             | -                            | 386,438                           | -                                 | 386,438                     |
| Net depreciation of investments                    | <u>(3,698,919)</u>           | <u>(2,637,804)</u>                | <u>(41,822)</u>                   | <u>(6,378,545)</u>          |
| Total investment return                            | <u>(3,698,919)</u>           | <u>(2,251,366)</u>                | <u>(41,822)</u>                   | <u>(5,992,107)</u>          |
| Contributions                                      | -                            | -                                 | 154,152                           | 154,152                     |
| Appropriation of endowment assets for expenditure  | <u>-</u>                     | <u>(494,244)</u>                  | <u>-</u>                          | <u>(494,244)</u>            |
| <b>ENDOWMENT NET ASSETS, END OF YEAR</b>           | <b><u>\$ (3,698,919)</u></b> | <b><u>\$ 1,812,239</u></b>        | <b><u>\$ 38,641,263</u></b>       | <b><u>\$ 36,754,583</u></b> |

CHESAPEAKE BAY FOUNDATION, INC.

NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2009

17. ENDOWMENT (Continued)

Description of amounts classified as permanently restricted net assets and temporarily restricted net assets (Endowment only) as of June 30, 2009:

**Permanently Restricted Net Assets:**

(1) The portion of perpetual endowment funds that is required to be retained permanently either by explicit donor stipulation or UPMIFA **\$ 38,641,263**

**Temporarily Restricted Net Assets:**

The portion of perpetual endowment funds subject to a time restriction under UPMIFA:

With purpose restrictions \$ 1,667,029  
Without purpose restrictions 145,210

**Total Endowment Funds Classified as Temporarily Restricted Net Assets \$ 1,812,239**

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 the State of Maryland Prudent Management of Institutional Funds Act (SPMIFA) requires the Foundation to retain into perpetuity. In accordance with GAAP, deficiencies of this nature that are reported in unrestricted net assets were \$3,698,919 as of June 30, 2009. 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.



**CHESAPEAKE BAY FOUNDATION, INC.**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2009**

**17. ENDOWMENT (Continued)**

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.

**18. SUBSEQUENT EVENTS**

Subsequent to June 30, 2009, the Foundation received funding approval from the Pennsylvania Infrastructure Investment Authority under the Green Project Reserve program funded by a Federal grant totaling \$14,966,444 from the American Recovery and Reinvestment Act of 2009 (ARRA), pending final settlement.

In addition, the U.S. Environmental Protection Agency awarded \$1,300,000 in ARRA Funds to the Foundation to fund the Chesapeake Bay Marine Engine Repower Project.

In preparing these financial statements, the Foundation has evaluated events and transactions for potential recognition or disclosure through November 18, 2009, the date the financial statements were issued.



**GELMAN, ROSENBERG & FREEDMAN**  
**CERTIFIED PUBLIC ACCOUNTANTS**

**INDEPENDENT AUDITORS' REPORT ON  
SUPPLEMENTAL FINANCIAL INFORMATION**

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

Our report on our audit of the basic financial statements of the Chesapeake Bay Foundation, Inc. as of June 30, 2009 appears on page 2. The audit was made for the purpose of forming an opinion on the basic financial statements taken as a whole. The accompanying Summary of Conservation and Scenic Easements 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 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.

*Gelman Rosenberg & Freedman*

November 18, 2009

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MEMBER OF CPAMERICA INTERNATIONAL, AN AFFILIATE OF HORWATH INTERNATIONAL  
MEMBER OF THE AMERICAN INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS' PRIVATE COMPANIES PRACTICE SECTION

**CHESAPEAKE BAY FOUNDATION, INC.**

**SUMMARY OF CONSERVATION AND SCENIC EASEMENTS  
FOR INFORMATION PURPOSES ONLY (UNAUDITED)  
FOR THE YEAR ENDED JUNE 30, 2009**

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, 2009.

**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 850 acres along the Sassafras River in Cecil County, Maryland, known as Sheffield and Rose Hill Farms

**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 13 acres along the Craddock Creek in Accomack County, Virginia
- Approximately 20 acres along Back Creek in Accomack County, Virginia
- Approximately 20 acres along Brush Creek in Frederick County, Virginia
- Approximately 22 acres in Accomack County, Virginia
- Approximately 29 acres along Nandua Creek in Accomack 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 Hunting Creek in Accomack County, Virginia
- Approximately 40 acres along Pitts Creek in Accomack County, Virginia
- Approximately 41 acres along Occohannock Creek in Accomack County, Virginia
- Approximately 45 acres along the Totuskey Creek in Richmond County, Virginia
- Approximately 63 acres along the Chesapeake Bay in Northampton County, Virginia
- Approximately 68 acres at Lake Anna in Spotsylvania County, Virginia
- Approximately 72 acres in King & Queen County, Virginia
- Approximately 72 acres along the Chesapeake Bay in Northumberland County, Virginia
- Approximately 78 acres at Tacketts Mill in Stafford County, Virginia
- Approximately 90 acres along Bullbegger Creek in Accomack County, Virginia
- Approximately 92 acres in Stafford County, Virginia
- Approximately 94 acres along Barnes Creek in Northumberland County, Virginia
- Approximately 99 acres on unnamed tributary to Pitts Creek in Accomack County, Virginia
- Approximately 106 acres on Pungoteague Creek in Accomack County, Virginia
- Approximately 118 acres along Mountain Run in Orange County, Virginia
- Approximately 118 acres along Occohannock Creek in Northampton County, Virginia
- Approximately 128 acres along Tawes Creek in Accomack County, Virginia
- Approximately 130 acres along Corrotoman River in Lancaster County, Virginia
- Approximately 136 acres along Laton Swamp in Richmond County, Virginia
- Approximately 145 acres along Cherrystone Inlet in Northampton County, Virginia
- Approximately 150 acres along the Chesapeake Bay in Mathews County, Virginia
- Approximately 157 acres along the Middle River in Augusta County, Virginia
- Approximately 161 acres along Holdens Creek in Accomack County, Virginia
- Approximately 161 acres in Northampton County, Virginia
- Approximately 179 acres along Messongo Creek in Accomack County, Virginia

**CHESAPEAKE BAY FOUNDATION, INC.**

**SUMMARY OF CONSERVATION AND SCENIC EASEMENTS  
FOR INFORMATION PURPOSES ONLY (UNAUDITED)  
FOR THE YEAR ENDED JUNE 30, 2009**

**Virginia (Continued)**

- Approximately 210 acres along Nassawadox Creek in Northampton County, Virginia
- Approximately 241 acres along Holly Grove Cove in Northampton County, Virginia
- Approximately 256 acres in Stafford County, Virginia
- Approximately 345 acres along the Chesapeake Bay in Accomack County, Virginia
- Approximately 368 acres along Bullbegger Creek in Accomack County, Virginia
- Approximately 411 acres along Jacobus Creek in Northampton County, Virginia
- Approximately 601 acres in Accomack County, Virginia
- Approximately 1,431 acres along the Potomac River in King George County, Virginia