

# FINANCIAL STATEMENTS



**CHESAPEAKE BAY FOUNDATION**

*Saving a National Treasure*

**FOR THE YEAR ENDED JUNE 30, 2014  
WITH SUMMARIZED FINANCIAL  
INFORMATION FOR 2013**

**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, 2014, 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, 2014, 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.

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### **Report on Summarized Comparative Information**

We have previously audited the Foundation's 2013 financial statements, and we expressed an unmodified audit opinion on those audited financial statements in our report dated November 12, 2013. In our opinion, the summarized comparative information presented herein as of and for the year ended June 30, 2013, 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".

November 14, 2014

**CHESAPEAKE BAY FOUNDATION, INC.**  
**STATEMENT OF FINANCIAL POSITION**  
**AS OF JUNE 30, 2014**  
**WITH SUMMARIZED FINANCIAL INFORMATION FOR 2013**

**ASSETS**

	<u>2014</u>	<u>2013</u>
Cash and cash equivalents	\$ 8,409,496	\$ 7,213,502
Investments (Notes 2 and 17)	56,209,935	51,107,017
Cash held in bond sinking fund (Note 9)	-	324,916
Accounts receivable, less allowance for doubtful accounts of \$4,344 and \$5,224 for 2014 and 2013, respectively (Notes 3 and 14)	1,531,772	1,009,764
Note receivable (Note 4)	90,618	92,231
Pledges receivable, net of allowance for doubtful accounts of \$172,655 and \$195,494 for 2014 and 2013, respectively (Notes 5 and 14)	14,673,914	16,602,400
Prepaid, deposits and other assets	954,491	704,804
Deferred financing cost, net of accumulated amortization of \$10,332 and \$78,590 for 2014 and 2013, respectively (Notes 8 and 9)	144,648	56,911
Property and equipment, net of accumulated depreciation and amortization of \$14,821,429 and \$14,012,813 for 2014 and 2013, respectively (Note 6)	<u>26,761,282</u>	<u>21,979,466</u>
<b>TOTAL ASSETS</b>	<b><u>\$108,776,156</u></b>	<b><u>\$ 99,091,011</u></b>

**LIABILITIES AND NET ASSETS**

**LIABILITIES**

Loan payable (Note 8)	\$ 732,742	\$ -
Bonds payable (Note 9)	5,878,076	6,195,000
Accounts payable and accrued expenses	3,230,092	1,436,058
Deferred income	418,561	385,958
Liability under split interest agreements	905,373	922,492
Interest rate swap obligation (Notes 10 and 17)	880,893	938,039
Income taxes payable on sale of debt financed property	<u>-</u>	<u>1,043,062</u>
Total liabilities	<u>12,045,737</u>	<u>10,920,609</u>

**NET ASSETS**

Unrestricted	28,688,043	21,786,476
Temporarily restricted (Note 11)	23,414,541	21,913,329
Permanently restricted (Note 18)	<u>44,627,835</u>	<u>44,470,597</u>
Total net assets	<u>96,730,419</u>	<u>88,170,402</u>
<b>TOTAL LIABILITIES AND NET ASSETS</b>	<b><u>\$108,776,156</u></b>	<b><u>\$ 99,091,011</u></b>

## CHESAPEAKE BAY FOUNDATION, INC.

**STATEMENT OF ACTIVITIES AND CHANGE IN NET ASSETS  
FOR THE YEAR ENDED JUNE 30, 2014  
WITH SUMMARIZED FINANCIAL INFORMATION FOR 2013**

	2014			2013	
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total	Total
<b>REVENUE</b>					
Membership contributions	\$ 4,673,323	\$ -	\$ -	\$ 4,673,323	\$ 4,744,675
Grants and gifts (Notes 14 and 15)	9,846,369	10,388,836	-	20,235,205	20,816,788
Education contracts and tuition	1,204,874	-	-	1,204,874	1,032,141
Investment income (Note 2)	537,707	1,745,466	-	2,283,173	2,087,952
Donated goods and services (Note 16)	1,807,514	-	-	1,807,514	1,907,836
Other	476,601	-	-	476,601	418,062
Net assets released from donor restrictions (Note 11)	<u>13,482,754</u>	<u>(13,482,754)</u>	<u>-</u>	<u>-</u>	<u>-</u>
Total revenue	<u>32,029,142</u>	<u>(1,348,452)</u>	<u>-</u>	<u>30,680,690</u>	<u>31,007,454</u>
<b>EXPENSES</b>					
Program Services:					
Environmental Education	6,404,143	-	-	6,404,143	6,500,239
Environmental Protection and Restoration	11,602,781	-	-	11,602,781	10,952,200
Communications	<u>3,498,193</u>	<u>-</u>	<u>-</u>	<u>3,498,193</u>	<u>3,619,695</u>
Total program services	<u>21,505,117</u>	<u>-</u>	<u>-</u>	<u>21,505,117</u>	<u>21,072,134</u>
Support Services:					
General and Administrative	2,138,630	-	-	2,138,630	1,805,917
Fundraising	<u>3,394,420</u>	<u>-</u>	<u>-</u>	<u>3,394,420</u>	<u>2,933,351</u>
Total support services	<u>5,533,050</u>	<u>-</u>	<u>-</u>	<u>5,533,050</u>	<u>4,739,268</u>
Total expenses	<u>27,038,167</u>	<u>-</u>	<u>-</u>	<u>27,038,167</u>	<u>25,811,402</u>
Change in net assets before capital additions (deductions)	<u>4,990,975</u>	<u>(1,348,452)</u>	<u>-</u>	<u>3,642,523</u>	<u>5,196,052</u>
<b>CAPITAL ADDITIONS (DEDUCTIONS)</b>					
Investment return, net (Note 2)	1,763,149	2,849,664	138,895	4,751,708	3,998,685
Realized loss on sale of debt financed property (Note 2)	-	-	-	-	(108,886)
Income recovery on sale of debt financed property	11,472	-	-	11,472	31,711
Grants and gifts (Note 14)	-	-	18,343	18,343	575,055
Donated property (Note 16)	70,000	-	-	70,000	-
Gain (loss) on sale/transfer of property	8,825	-	-	8,825	(6,665)
Unrealized gain on interest rate swap (Note 10)	<u>57,146</u>	<u>-</u>	<u>-</u>	<u>57,146</u>	<u>338,455</u>
Total capital additions (deductions)	<u>1,910,592</u>	<u>2,849,664</u>	<u>157,238</u>	<u>4,917,494</u>	<u>4,828,355</u>
Change in net assets	6,901,567	1,501,212	157,238	8,560,017	10,024,407
Net assets at beginning of year	<u>21,786,476</u>	<u>21,913,329</u>	<u>44,470,597</u>	<u>88,170,402</u>	<u>78,145,995</u>
<b>NET ASSETS AT END OF YEAR</b>	<b>\$ <u>28,688,043</u></b>	<b>\$ <u>23,414,541</u></b>	<b>\$ <u>44,627,835</u></b>	<b>\$ <u>96,730,419</u></b>	<b>\$ <u>88,170,402</u></b>

CHESAPEAKE BAY FOUNDATION, INC.

STATEMENT OF FUNCTIONAL EXPENSES  
FOR THE YEAR ENDED JUNE 30, 2014  
WITH SUMMARIZED FINANCIAL INFORMATION FOR 2013

	2014			
	Program Services			
	Environmental	Environmental		Total
	Education	Protection and	Communications	Program
	Education	Restoration	Communications	Services
Salaries	\$ 2,496,843	\$ 3,906,655	\$ 1,102,392	\$ 7,505,890
Fringe benefits (Note 13)	961,252	1,497,774	431,110	2,890,136
Supplies	233,325	220,144	27,677	481,146
Restoration supplies	-	199,072	-	199,072
Telephone	56,359	80,711	19,192	156,262
Postage and shipping	133,737	251,626	124,403	509,766
Occupancy and utilities (Notes 6, 10 and 12)	497,438	630,403	113,268	1,241,109
Equipment rental, leasing, repairs and maintenance	132,451	116,194	21,569	270,214
Printing and publications	124,262	287,194	207,425	618,881
Dues and subscriptions	1,442	32,700	6,293	40,435
Travel	203,529	165,387	12,616	381,532
Meetings and seminars	85,230	84,318	10,782	180,330
Outside services	10,262	98,842	162,838	271,942
Boat charter	41,528	1,721	-	43,249
Professional fees	182,046	1,150,144	436,698	1,768,888
Restoration fees	-	509,815	-	509,815
Personnel recruitment	65	117	919	1,101
Miscellaneous	71	27,421	258	27,750
Mailing preparation	37,446	67,839	20,459	125,744
Honorariums/stipends	-	116	-	116
Insurance	144,448	104,707	11,461	260,616
List rentals	38,919	70,506	21,263	130,688
Depreciation and amortization - other (Note 6)	176,316	92,360	9,943	278,619
Subcontracts	-	941,515	-	941,515
Donated goods and services (Note 16)	<u>572,667</u>	<u>568,155</u>	<u>607,683</u>	<u>1,748,505</u>
Sub-total	6,129,636	11,105,436	3,348,249	20,583,321
Allocation of management and general	<u>274,507</u>	<u>497,345</u>	<u>149,944</u>	<u>921,796</u>
<b>TOTAL</b>	<b>\$ <u>6,404,143</u></b>	<b>\$ <u>11,602,781</u></b>	<b>\$ <u>3,498,193</u></b>	<b>\$ <u>21,505,117</u></b>

					2013
<u>Support Services</u>					
<u>General and Administrative</u>	<u>Fundraising</u>	<u>Total Support Services</u>	<u>Total Expenses</u>	<u>Total Expenses</u>	
\$ 1,706,387	\$ 1,335,474	\$ 3,041,861	\$ 10,547,751	\$ 9,882,181	
629,122	521,130	1,150,252	4,040,388	3,850,392	
98,707	45,922	144,629	625,775	649,315	
-	-	-	199,072	201,772	
15,137	12,924	28,061	184,323	223,921	
2,093	269,064	271,157	780,923	850,640	
138,125	100,898	239,023	1,480,132	1,564,896	
51,323	28,281	79,604	349,818	375,416	
3,122	280,415	283,537	902,418	914,477	
5,930	6,999	12,929	53,364	47,827	
27,769	18,097	45,866	427,398	424,100	
73,897	41,301	115,198	295,528	267,369	
45,174	45,621	90,795	362,737	251,014	
-	-	-	43,249	40,431	
275,553	284,321	559,874	2,328,762	1,818,316	
-	-	-	509,815	779,012	
11,409	163	11,572	12,673	18,238	
7,887	6,724	14,611	42,361	63,162	
-	104,079	104,079	229,823	253,452	
-	-	-	116	3,512	
20,716	18,383	39,099	299,715	296,058	
-	62,951	62,951	193,639	215,204	
92,037	8,702	100,739	379,358	317,614	
-	-	-	941,515	595,247	
<u>1,536</u>	<u>57,473</u>	<u>59,009</u>	<u>1,807,514</u>	<u>1,907,836</u>	
3,205,924	3,248,922	6,454,846	27,038,167	25,811,402	
<u>(1,067,294)</u>	<u>145,498</u>	<u>(921,796)</u>	<u>-</u>	<u>-</u>	
<b><u>\$ 2,138,630</u></b>	<b><u>\$ 3,394,420</u></b>	<b><u>\$ 5,533,050</u></b>	<b><u>\$ 27,038,167</u></b>	<b><u>\$ 25,811,402</u></b>	



## CHESAPEAKE BAY FOUNDATION, INC.

**STATEMENT OF CASH FLOWS**  
**FOR THE YEAR ENDED JUNE 30, 2014**  
**WITH SUMMARIZED FINANCIAL INFORMATION FOR 2013**

	<b>2014</b>	<b>2013</b>
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Change in net assets	\$ 8,560,017	\$ 10,024,407
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation and amortization	916,863	855,766
Unrealized gain on interest rate swap	(57,146)	(338,455)
(Gain) loss on sale of property and equipment	(8,825)	6,665
Donated property	(70,000)	-
Capital additions - permanently restricted contributions	(18,343)	(575,055)
Change in the discount of long-term pledges receivable	(328,782)	(202,151)
Change in allowance for doubtful accounts	(23,719)	18,817
Unrealized gain on investments	(3,468,858)	(1,423,048)
Realized gains on investments (including realized loss on sale of debt financed property)	(2,809,690)	(3,718,625)
Change in value of split interest agreements	47,113	11,177
(Increase) decrease in:		
Accounts receivable	(521,128)	421,690
Pledges receivable	2,280,107	(1,561,041)
Prepays, deposits and other assets	(249,687)	(242,238)
Increase (decrease) in:		
Accounts payable and accrued expenses	1,794,034	(75,857)
Deferred income	32,603	103,491
Income taxes payable on sale of debt financed property	<u>(1,043,062)</u>	<u>(42,672)</u>
Net cash provided by operating activities	<u>5,031,497</u>	<u>3,262,871</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Net proceeds from sale of investments	1,175,630	633,084
Purchases of property and equipment	(5,552,611)	(2,204,543)
Proceeds from sale of property and equipment	-	8,373
Proceeds from note receivable	1,613	10,669
Capitalized bond costs	<u>(154,980)</u>	<u>-</u>
Net cash used by investing activities	<u>(4,530,348)</u>	<u>(1,552,417)</u>
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Capital additions - permanently restricted contributions	18,343	575,055
Decrease in cash held for bond sinking fund	324,916	10,194
Extinguishments/retirement of bonds payable	(6,195,000)	-
Payments on bonds payable	(316,924)	(425,000)
Issuance of bond payable	6,195,000	-
Proceeds on loan payable	2,413,434	-
Payments on loan payable	(1,680,692)	-
Proceeds from split interest agreements	53,354	83,082
Payments made on split interest agreements	<u>(117,586)</u>	<u>(104,274)</u>
Net cash provided by financing activities	<u>694,845</u>	<u>139,057</u>

See accompanying notes to financial statements.

## CHESAPEAKE BAY FOUNDATION, INC.

STATEMENT OF CASH FLOWS  
FOR THE YEAR ENDED JUNE 30, 2014  
WITH SUMMARIZED FINANCIAL INFORMATION FOR 2013

	<u>2014</u>	<u>2013</u>
Net increase in cash and cash equivalents	\$ 1,195,994	\$ 1,849,511
Cash and cash equivalents at beginning of year	<u>7,213,502</u>	<u>5,363,991</u>
<b>CASH AND CASH EQUIVALENTS AT END OF YEAR</b>	<b><u>\$ 8,409,496</u></b>	<b><u>\$ 7,213,502</u></b>
 <b>SUPPLEMENTAL INFORMATION</b>		
Interest Paid	<u>\$ 311,545</u>	<u>\$ 370,239</u>
Taxes Paid	<u>\$ 1,047,968</u>	<u>\$ 17,000</u>

**CHESAPEAKE BAY FOUNDATION, INC.**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2014**

**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, 2013, 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, 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 in investment 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, 2014

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 bond issuance costs and other costs related to the acquisition of the Bay Ridge Facility, etc. for use as the Foundation's Headquarters (Note 9). Deferred financing costs are being amortized over the life of the 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.

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, 2014 and 2013, liabilities under split interest agreements totaled \$905,373 and \$922,492, 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.

CHESAPEAKE BAY FOUNDATION, INC.

NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2014

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

Net asset classification (continued) -

- **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.

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 nonfinancial 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 Statement of Activities and Change in Net Assets.

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 and is being reported for income tax purposes in the year ending June 30, 2013.

Accordingly, the Foundation has recorded income tax recovery in the amount of \$11,472 and \$24,243 for the years ended June 30, 2014 and 2013, respectively, as follows:

	<u>2014</u>	<u>2013</u>
Income recovery on sale of debt financed property	\$ 11,472	\$ 31,711
Other unrelated business income tax included in miscellaneous expenses in the accompanying Statement of Functional Expenses	<u>-</u>	<u>(7,468)</u>
<b>TOTAL INCOME TAX RECOVERY</b>	<b><u>\$ 11,472</u></b>	<b><u>\$ 24,243</u></b>

CHESAPEAKE BAY FOUNDATION, INC.

NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2014

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

Income taxes (continued) -

An unrelated business income tax of \$7,468 was recorded as a liability and included in accounts payable in the Statement of Financial Position as of June 30, 2013.

The taxes payable from the sale of the debt financed property is presented separately in the Statement of Financial Position and is \$0 at June 30, 2014 (this liability was estimated at \$1,043,062 at June 30, 2013).

Uncertain tax positions -

For the years ended June 30, 2014 and 2013, 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.

The Federal Form 990, *Return of Organization Exempt from Income Tax*, is subject to examination by the Internal Revenue Service, generally for three years after it is filed.

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.

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 2014 and 2013, the Foundation incurred joint costs of \$2,499,805 and \$2,625,128, respectively, for educational materials, membership and support services. These costs were allocated as follows:

	<u>2014</u>	<u>2013</u>
Environmental Education	\$ 523,164	\$ 580,059
Environmental Protection and Restoration	947,856	977,336
Communications	285,768	323,009
Fundraising	<u>743,017</u>	<u>744,724</u>
<b>TOTAL JOINT COSTS INCURRED</b>	<b><u>\$ 2,499,805</u></b>	<b><u>\$ 2,625,128</u></b>

CHESAPEAKE BAY FOUNDATION, INC.

NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2014

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

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, 2014 and 2013, investments at readily determinable fair values, consisted of the following:

	<u>2014</u>	<u>2013</u>
Equity securities	\$ 24,529,255	\$ 17,832,851
International equity securities	5,242,067	4,808,496
Partnerships/Alternative investments	16,710,344	16,527,973
Corporate bonds and other agencies	2,693,971	2,653,078
Beneficial interest in perpetual trust	2,924,350	2,924,350
U.S. Government obligations	<u>-</u>	<u>38,312</u>
Sub-total investments	52,099,987	44,785,060
Cash and cash equivalents held by investment managers	<u>4,109,948</u>	<u>6,321,957</u>
<b>TOTAL INVESTMENTS</b>	<b><u>\$ 56,209,935</u></b>	<b><u>\$ 51,107,017</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. As of June 30, 2014 and 2013, the Foundation has uncalled commitments of \$1,398,770 and \$571,162, respectively.

Alternative investments are comprised of the following at June 30, 2014 and 2013:

<u>Investment Type</u>	<u>Amount</u>		<u>Liquidity</u>
	<u>2014</u>	<u>2013</u>	
Domestic/U.S. Limited Partnerships	\$ 1,347,491	\$ 1,420,734	None until dissolution or winding up of partnership.
Domestic/U.S. Limited Partnerships	1,000,000	-	100 days notice
Domestic/U.S. Limited Partnerships	11,869,132	9,847,858	Last day of each quarter.
Hedge Funds	<u>2,493,721</u>	<u>5,259,381</u>	Last day of each quarter.
<b>ALTERNATIVE INVESTMENTS</b>	<b><u>\$16,710,344</u></b>	<b><u>\$16,527,973</u></b>	

Included in the investment balance at June 30, 2014 and 2013 are investments related to certain split-interest agreements in the amounts of \$1,112,186 and \$1,132,729, respectively.

The investment portfolio includes \$36,412,049 and \$35,699,000 of permanently restricted endowment investments at June 30, 2014 and 2013, respectively (see Note 18).

**CHESAPEAKE BAY FOUNDATION, INC.**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2014**

**2. INVESTMENTS (Continued)**

The Foundation follows the Uniform Prudent Management Of 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 return, net".

Investment return for the years ended June 30, 2014 and 2013 consisted of the following:

	<b>2014</b>	<b>2013</b>
Interest and dividends	\$ 756,333	\$ 836,078
Unrealized gain	3,468,858	1,423,048
Realized gains (including realized loss on sale of debt financed property in the amount of \$0 in 2014 and \$108,886 in 2013)	2,809,690	3,718,625
Total investment return	7,034,881	5,977,751
Less: Investment income used for operations	(2,283,173)	(2,087,952)
<b>NET INVESTMENT RETURN</b>	<b>\$ 4,751,708</b>	<b>\$ 3,889,799</b>

**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, 2014 and 2013, respectively:

	<b>2014</b>	<b>2013</b>
Federal and state receivables	\$ 1,371,289	\$ 888,419
Non-Federal and state receivables	164,827	126,569
Total accounts receivable	1,536,116	1,014,988
Less: Allowance for doubtful accounts	(4,344)	(5,224)
<b>NET ACCOUNTS RECEIVABLE</b>	<b>\$ 1,531,772</b>	<b>\$ 1,009,764</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, the note has been extended every year and is now due July 1, 2015. Only monthly payments of interest are to be made by the Tribe until maturity. The amounts outstanding at June 30, 2014 and 2013 were \$90,618 and \$92,231, respectively.



**CHESAPEAKE BAY FOUNDATION, INC.**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2014**

**5. PLEDGES RECEIVABLE**

As of June 30, 2014 and 2013, contributors to the Foundation have made written promises to give totaling \$17,279,129 and \$19,559,236, 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 3.1% 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, 2014 and 2013:

	<b>2014</b>	<b>2013</b>
Less than one year	\$ 4,597,553	\$ 5,800,498
One to five years	6,888,768	7,666,555
Beyond five years	5,792,808	6,092,183
Total pledges	17,279,129	19,559,236
Less: Discount to net present value	(2,432,560)	(2,761,342)
Less: Allowance for doubtful accounts	(172,655)	(195,494)
<b>NET PLEDGES RECEIVABLE</b>	<b>\$ 14,673,914</b>	<b>\$ 16,602,400</b>

**6. PROPERTY AND EQUIPMENT**

Property and equipment consisted of the following at June 30, 2014 and 2013:

	<b>2014</b>	<b>2013</b>
Land	\$ 11,645,983	\$ 11,645,983
Building and improvements	16,163,695	15,904,834
Furniture and equipment	3,041,420	3,046,020
Boats	3,984,795	3,777,750
Vehicles	614,995	570,282
Construction in progress	6,114,823	1,030,410
Art	17,000	17,000
Total property and equipment	41,582,711	35,992,279
Less: Accumulated depreciation and amortization	(14,821,429)	(14,012,813)
<b>NET PROPERTY AND EQUIPMENT</b>	<b>\$ 26,761,282</b>	<b>\$ 21,979,466</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 \$8,155,524 at June 30, 2014 and 2013 (see Note 18).

The construction in progress at year end consisted of costs associated with the construction of the Brock Environmental Center, located at Pleasure House Point in Virginia Beach, Virginia. The Chesapeake Bay Foundation's Brock Environmental Center will be a 10,200 square foot facility in Virginia Beach, Virginia. It sits on land once slated for heavy development that is now saved in perpetuity. Once opened, the Brock Center will provide a collaborative workspace for all of the Foundation's Virginia Beach program staff and for the local Lynnhaven RiverNow environmental group, a partner group of the Foundation's. The building also will provide a venue for expanded environmental education programs for students and volunteers, serve as a lasting demonstration site for restoration projects, and provide meeting space for local conservation groups. The facility is expected to be one of the most environmentally sound buildings in the world. The Foundation aims to qualify for the US Green Building Council's LEED Platinum Certification and International Living Building Institute's Living Building Challenge Certification.

**CHESAPEAKE BAY FOUNDATION, INC.**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2014**

**6. PROPERTY AND EQUIPMENT (Continued)**

The construction of the facility was completed on October 31, 2014, and staff will move into the facility mid-December 2014. Environmental programs, tours, and volunteer activities will begin January 2015.

Depreciation and amortization expense for the years ended June 30, 2014 and 2013 totaled \$916,863 and \$850,346, respectively. Of these amounts, \$537,505 and \$538,152 is included in occupancy expense, and \$379,358 and \$312,194 is included in depreciation and amortization expense in the accompanying Statement of Functional Expenses for the years ended June 30, 2014 and 2013, respectively.

**7. LINE OF CREDIT**

The Foundation obtained an unsecured \$1,000,000 line of credit with Capital One, effective October 1, 2013 (the "Line of Credit"). The Line of Credit is renewable annually, with the first expiration date occurring on October 1, 2014. Subsequent to year end, the Line of Credit was extended for an additional year through October 1, 2015. There was no outstanding balance on the line of credit for the year ended June 30, 2014.

**8. LOAN PAYABLE**

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 in the City of Virginia Beach, Virginia (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, 2014 was \$732,742.

Total interest of \$10,754 was capitalized and included in the work in process account for the period ending June 30, 2014. 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, 2014, accumulated amortization for the taxable loan financing costs totaled \$4,263.

**9. BONDS PAYABLE**

On July 6, 1998, the Foundation purchased a 30.261-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 Wells Fargo Bank, N.A. (formerly known as Wachovia Bank) was used to purchase the site.

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 (MEDCO). Wells Fargo Bank was Trustee for the bonds. (On December 30, 2005, U.S. Bank, N.A. completed the purchase of the corporate trust and institutional custody business of Wells Fargo Corporation and became the successor Trustee.) The proceeds of the bonds were used to repay the bridge loan with Wells Fargo Bank, N.A and finance the acquisition, construction and equipping of a portion of the Bay Ridge Facility.

**CHESAPEAKE BAY FOUNDATION, INC.**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2014**

**9. BONDS PAYABLE (Continued)**

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 is 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 into 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. Subsequent to that date, mandatory sinking fund and interest payments were due monthly with the final payment due on October 1, 2023. Financing costs in the amount of \$135,501 were capitalized and being amortized over the life of the bonds.

The 1998 Series Bonds were also secured by a letter of credit issued by Wells Fargo Bank in the amount of \$6,724,469 maturing on October 31, 2013. The letter of credit was secured by the Foundation's interest in cash held in Wells Fargo Bank accounts. The bonds carried interest at variable rates that were determined weekly by Wells Fargo Capital Markets (the "Remarketing Agent") 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 hedged these bonds using the interest rate swap agreement described in Note 10. As of June 30, 2013, the outstanding principal on the 1998 Bonds was \$6,195,000 and cash in the bond sinking fund was in the amount of \$324,916.

The bond agreements, among other provisions, required the Foundation to meet certain financial ratio tests. For the year ended June 30, 2013, the Foundation was in compliance with all bond covenants.

During fiscal year 2014, the 1998 Series Bonds 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. The 2013 Series Bonds were purchased by Capital One, 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, 2014, accumulated amortization for the bond financing costs totaled \$6,069.

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, 2014 and 2013, the Foundation was in compliance with all bond covenants.

As of June 30, 2014, the outstanding principal of the bond payable totaled \$5,878,076.

CHESAPEAKE BAY FOUNDATION, INC.

NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2014

9. BONDS PAYABLE (Continued)

Principal payments are due as follows:

Year Ending June 30,

2015	\$ 499,020
2016	524,936
2017	554,735
2018	585,406
2019	616,824
Thereafter	<u>3,097,155</u>
<b>BONDS PAYABLE</b>	<b><u>\$ 5,878,076</u></b>

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 the following interest rate swap agreements. 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 hedge 50% of its outstanding 1998 Series Bonds (the "Wells Fargo Swap"). Under the Wells Fargo Swap, the fixed rate paid by the Foundation was 5.00% and the variable rate received by the Foundation was the SIFMA Index. On January 6, 2004, the Wells Fargo Swap was amended to add an additional 25% of the then outstanding 1998 Series Bonds at a fixed rate of 3.25%. On May 26, 2005, the Wells Fargo Swap was further amended to fix 100% of the then outstanding 1998 Series Bonds at a fixed rate of 4.33%. For the year ended June 30, 2013, the outstanding notional amount on the Wells Fargo Swap was \$6,195,000. As of June 30, 2013, the swap had a negative fair value of \$938,039, which is reflected as a liability in the financial statements.

The Wells Fargo Swap 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. For the year ended June 30, 2014 the outstanding notional amount of the Capital One Swap was \$5,878,076.

As of June 30, 2014, the Capital One Swap had a negative fair value of \$880,893, which is reflected as a liability in the financial statements.

The Foundation incurred interest expense on the bonds totaling \$311,545 and \$370,239 for the years ended June 30, 2014 and 2013, respectively, which is included in occupancy and utilities expense within the Statement of Functional Expenses.

**CHESAPEAKE BAY FOUNDATION, INC.**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2014**

**10. INTEREST RATE SWAP (Continued)**

As of June 30, 2014 and 2013, the Foundation was not exposed to credit risk because the respective swaps had a negative fair value. The Foundation is only exposed to credit risk if the swap has a positive fair value. In addition, since the swap agreements were executed to the maturity of the underlying bonds, there is no rollover risk.

The swaps expose the Foundation to basis risk should the actual rate on the Foundation's bonds exceed the respective Index (LIBOR Index and SIFMA Index for the years ended June 30, 2014 and 2013, respectively). Since the Foundation's bonds are based upon the respective 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, 2014 and 2013:

	<b>2014</b>	<b>2013</b>
<b>Program Restricted:</b>		
Environmental Education	\$ 1,604,558	\$ 645,828
Environmental Protection and Restoration	11,367,043	11,506,998
Communications	90,000	264,490
Property and Equipment	186,461	1,932,756
Other	73,238	134,634
Total program restricted	13,321,300	14,484,706
<b>Time Restricted</b>	<b>10,093,241</b>	<b>7,428,623</b>
<b>TEMPORARILY RESTRICTED NET ASSETS</b>	<b>\$ 23,414,541</b>	<b>\$ 21,913,329</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.

Accumulated investment earnings from permanently restricted endowed funds included within temporarily restricted net assets as of June 30, 2014 and 2013 are as follows:

	<b>2014</b>	<b>2013</b>
With purpose restrictions	\$ 4,631,222	\$ 3,241,493
Time restriction	2,382,120	964,108
<b>ACCUMULATED ENDOWMENT EARNINGS INCLUDED IN TEMPORARILY RESTRICTED NET ASSETS</b>	<b>\$ 7,013,342</b>	<b>\$ 4,205,601</b>

**CHESAPEAKE BAY FOUNDATION, INC.**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2014**

**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:

	<b>2014</b>	<b>2013</b>
<b>Donor Restrictions:</b>		
Environmental Education	\$ 1,383,019	\$ 987,126
Environmental Protection and Restoration	7,642,688	4,575,550
Communications	180,000	113,500
Property and Equipment	2,142,701	2,049,035
Other	119,603	130,551
Total donor restrictions	11,468,011	7,855,762
<b>Time Restricted</b>	<b>2,014,743</b>	<b>2,069,440</b>
<b>NET ASSETS RELEASED FROM RESTRICTIONS</b>	<b>\$ 13,482,754</b>	<b>\$ 9,925,202</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 Ending June 30,</u>		
2015	\$	384,503
2016		285,521
2017		285,521
2018		171,237
2019		88,090
Thereafter		12,345
	<b>\$</b>	<b>1,227,217</b>

Rent expense for the years ended June 30, 2014 and 2013 totaled \$277,134 and \$256,380, 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, 2014 and 2013, the Foundation made contributions in the amounts of \$397,422 and \$383,471, respectively.

CHESAPEAKE BAY FOUNDATION, INC.

NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2014

**14. RELATED PARTY**

For the years ended June 30, 2014 and 2013, the Foundation received gross contributions and grants in the amounts of \$3,785,946 and \$9,708,625, respectively, from Trustees, Executive Management, and their associated companies. Net amounts due under pledges receivable from related parties totaled \$2,565,247 and \$3,061,717 as of June 30, 2014 and 2013, respectively. Net amounts due under accounts receivable from related parties totaled \$0 and \$47,991 as of June 30, 2014 and 2013, respectively.

**15. 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 2014. 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.

**16. DONATED GOODS, SERVICES AND PROPERTY**

During the years ended June 30, 2014 and 2013, 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 \$1,807,514 and \$1,907,836 have been included in revenue and expense for the years ended June 30, 2014 and 2013, respectively, which included \$1,477,600 of in-kind public service announcements for the years ended June 30, 2014 and 2013.

In addition, the Foundation was the beneficiary of donated property and equipment totaling \$70,000 and \$0 for the years ended June 30, 2014 and 2013, respectively. These assets were capitalized at their fair value and the income is recognized in the Statement of Activities and Change in Net Assets.

**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.

**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.

CHESAPEAKE BAY FOUNDATION, INC.

NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2014

17. FAIR VALUE MEASUREMENT (Continued)

**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 used at June 30, 2014.

- *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.
- *U.S. Government obligations* - Valued at the closing price reported on the active market in which the individual securities are traded.
- *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 summarize, by level within the fair value hierarchy, the Foundation's investments as of June 30, 2014:

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total June 30, 2014</u>
<b>Asset Class:</b>				
Equity securities	\$ 23,507,005	\$ 1,022,250	\$ -	\$ 24,529,255
International equity securities	5,242,067	-	-	5,242,067
Partnerships/Alternative investments	-	-	16,710,344	16,710,344
Corporate bonds and other agencies	2,693,971	-	-	2,693,971
Beneficial interest in perpetual trust	-	2,924,350	-	2,924,350
Cash and cash equivalents held by investment managers	<u>4,109,948</u>	<u>-</u>	<u>-</u>	<u>4,109,948</u>
<b>Total Investments</b>	<b><u>\$ 35,552,991</u></b>	<b><u>\$ 3,946,600</u></b>	<b><u>\$ 16,710,344</u></b>	<b><u>\$ 56,209,935</u></b>
<b>Liability:</b>				
Interest Rate Swap Obligation	<u>\$ -</u>	<u>\$ 880,893</u>	<u>\$ -</u>	<u>\$ 880,893</u>



**CHESAPEAKE BAY FOUNDATION, INC.**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2014**

**17. FAIR VALUE MEASUREMENT (Continued)**

The tables below summarize, by level within the fair value hierarchy, the Foundation's investments as of June 30, 2013:

<b>Asset Class:</b>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total June 30, 2013</u>
Equity securities	\$ 16,893,422	\$ 939,429	\$ -	\$ 17,832,851
International equity securities	4,808,496	-	-	4,808,496
Partnerships/Alternative investments	-	-	16,527,973	16,527,973
Corporate bonds and other agencies	2,653,078	-	-	2,653,078
Beneficial interest in perpetual trust	-	2,924,350	-	2,924,350
U.S. Government obligations	38,312	-	-	38,312
Cash and cash equivalents held by investment managers	<u>6,321,957</u>	<u>-</u>	<u>-</u>	<u>6,321,957</u>
<b>Total Investments</b>	<b><u>\$ 30,715,265</u></b>	<b><u>\$ 3,863,779</u></b>	<b><u>\$ 16,527,973</u></b>	<b><u>\$ 51,107,017</u></b>
<b>Liability:</b>				
Interest Rate Swap Obligation	<u>\$ -</u>	<u>\$ 938,039</u>	<u>\$ -</u>	<u>\$ 938,039</u>

**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, 2014:

	<u>Domestic/ U.S. Limited Partnership</u>	<u>Domestic/ U.S. Limited Partnership</u>	<u>Domestic/ U.S. Limited Partnership</u>	<u>Hedge Funds</u>	<u>Total</u>
Beginning balance	\$ 1,420,734	\$ -	\$ 9,847,858	\$ 5,259,381	\$ 16,527,973
Unrealized (loss) gain	(111,315)	-	1,867,984	(633,079)	1,123,590
Realized gain	341,859	-	114,549	576,346	1,032,754
Earned income	(186)	-	35,077	(1,006)	33,885
Purchases (sales)	<u>(303,601)</u>	<u>1,000,000</u>	<u>3,664</u>	<u>(2,707,921)</u>	<u>(2,007,858)</u>
<b>BALANCE AS OF JUNE 30, 2014</b>	<b><u>\$ 1,347,491</u></b>	<b><u>\$ 1,000,000</u></b>	<b><u>\$ 11,869,132</u></b>	<b><u>\$ 2,493,721</u></b>	<b><u>\$ 16,710,344</u></b>

Following is the change in fair value of the Foundation's assets using significant unobservable inputs (Level 3) for the year ended June 30, 2013 :

	<u>Domestic/ U.S. Limited Partnership</u>	<u>Domestic/ U.S. Limited Partnership</u>	<u>Domestic/ U.S. Limited Partnership</u>	<u>Hedge Funds</u>	<u>Total</u>
Beginning balance	\$ 1,993,494	\$ -	\$ 6,055,824	\$ 7,965,519	\$ 16,014,837
Unrealized (loss) gain	(581,015)	-	730,058	16,325	165,368
Realized gain	1,689,034	-	428,380	294,841	2,412,255
Earned income	55,498	-	(26,404)	998	30,092
Purchases (sales)	<u>(1,736,277)</u>	<u>-</u>	<u>2,660,000</u>	<u>(3,018,302)</u>	<u>(2,094,579)</u>
<b>BALANCE AS OF JUNE 30, 2013</b>	<b><u>\$ 1,420,734</u></b>	<b><u>\$ -</u></b>	<b><u>\$ 9,847,858</u></b>	<b><u>\$ 5,259,381</u></b>	<b><u>\$ 16,527,973</u></b>

**CHESAPEAKE BAY FOUNDATION, INC.**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2014**

**17. FAIR VALUE MEASUREMENT (Continued)**

The amount of total gains or losses included in net unrestricted net assets attributable to the change in unrealized gains or losses relating to assets still held at the reporting date was a gain of \$1,123,590 for the year ended June 30, 2014 and a loss of \$400,827 for the year ended June 30, 2013.

As of June 30, 2014, 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	\$ 7,194,545	7%
Acacia Partners	Partnerships/Alternative investments	\$ 6,112,772	6%
Davidson Kempner	Partnerships/Alternative investments	\$ 5,756,360	6%
T Rowe Price Equity Income Fund	Equity	\$ 5,353,927	6%
Cypress Asset Management	Equity	\$ 5,014,511	5%

As of June 30, 2013, 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>
PNC - Restricted Short Term Investments	Cash and cash equivalents held by investment managers	\$ 5,750,453	7%
Davidson Kempner	Partnerships/Alternative investments	\$ 5,235,738	6%
Acacia Partners	Partnerships/Alternative investments	\$ 4,952,120	6%
Stralem & Company	Equity	\$ 4,822,268	5%
T Rowe Price Equity Income Fund.	Equity	\$ 4,522,973	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.

CHESAPEAKE BAY FOUNDATION, INC.

NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2014

18. ENDOWMENT (Continued)

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.)

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>2014</u>	<u>2013</u>
Environmental Education	\$ 9,239,488	\$ 9,093,198
Environmental Protection and Restoration	13,074,325	13,071,290
Property and equipment	8,155,524	8,155,524
General operating	<u>14,158,498</u>	<u>14,150,585</u>
<b>PERMANENTLY RESTRICTED NET ASSETS</b>	<b><u>\$ 44,627,835</u></b>	<b><u>\$ 44,470,597</u></b>

Permanently restricted net assets consists of the following:

	<u>2014</u>	<u>2013</u>
Investments	\$ 36,412,049	\$ 35,699,000
Property and equipment	8,155,524	8,155,524
Pledge receivables, net of discount	<u>60,262</u>	<u>616,073</u>
<b>PERMANENTLY RESTRICTED NET ASSETS</b>	<b><u>\$ 44,627,835</u></b>	<b><u>\$ 44,470,597</u></b>

Endowment net asset composition by type of fund as of June 30, 2014:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Donor-Restricted Endowment Funds	\$ (516,893)	\$ 7,013,342	\$ 44,627,835	\$ 51,124,284
Board-Designated Endowment Funds	<u>890,807</u>	<u>-</u>	<u>-</u>	<u>890,807</u>
<b>TOTAL FUNDS</b>	<b><u>\$ 373,914</u></b>	<b><u>\$ 7,013,342</u></b>	<b><u>\$ 44,627,835</u></b>	<b><u>\$ 52,015,091</u></b>

CHESAPEAKE BAY FOUNDATION, INC.

NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2014

18. ENDOWMENT (Continued)

Changes in endowment net assets for the year ended June 30, 2014:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Endowment net assets, beginning of year	\$ (357,750)	\$ 4,205,601	\$ 44,470,597	\$ 48,318,448
Interest and dividends	12,315	654,373	14,628	681,316
Net appreciation of investments	<u>104,616</u>	<u>4,552,812</u>	<u>124,267</u>	<u>4,781,695</u>
Total investment return	<u>116,931</u>	<u>5,207,185</u>	<u>138,895</u>	<u>5,463,011</u>
Contributions	-	-	18,343	18,343
Appropriation of endowment assets for expenditure	(39,245)	(1,745,466)	-	(1,784,711)
Other changes:				
Transfer of net assets	<u>653,978</u>	<u>(653,978)</u>	<u>-</u>	<u>-</u>
<b>ENDOWMENT NET ASSETS, END OF YEAR</b>	<b><u>\$ 373,914</u></b>	<b><u>\$ 7,013,342</u></b>	<b><u>\$ 44,627,835</u></b>	<b><u>\$ 52,015,091</u></b>

Endowment net asset composition by type of fund as of June 30, 2013:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Donor-Restricted Endowment Funds	\$ (1,170,870)	\$ 4,205,601	\$ 44,470,597	\$ 47,505,328
Board-Designated Endowment Funds	<u>813,120</u>	<u>-</u>	<u>-</u>	<u>813,120</u>
<b>TOTAL FUNDS</b>	<b><u>\$ (357,750)</u></b>	<b><u>\$ 4,205,601</u></b>	<b><u>\$ 44,470,597</u></b>	<b><u>\$ 48,318,448</u></b>

Changes in endowment net assets for the year ended June 30, 2013:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Endowment net assets, beginning of year	\$ (1,707,871)	\$ 2,614,607	\$ 43,773,268	\$ 44,680,004
Interest and dividends	12,735	630,702	15,115	688,552
Net depreciation of investments	<u>90,293</u>	<u>3,805,197</u>	<u>107,159</u>	<u>4,002,649</u>
Total investment return	<u>103,028</u>	<u>4,435,899</u>	<u>122,274</u>	<u>4,661,201</u>
Contributions	-	-	575,055	575,055
Appropriation of endowment assets for expenditure	(37,623)	(1,560,189)	-	(1,597,812)
Other changes:				
Transfer of net assets	<u>1,284,716</u>	<u>(1,284,716)</u>	<u>-</u>	<u>-</u>
<b>ENDOWMENT NET ASSETS, END OF YEAR</b>	<b><u>\$ (357,750)</u></b>	<b><u>\$ 4,205,601</u></b>	<b><u>\$ 44,470,597</u></b>	<b><u>\$ 48,318,448</u></b>

**CHESAPEAKE BAY FOUNDATION, INC.**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2014**

**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 \$516,893 and \$1,170,870 as of June 30, 2014 and 2013, 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 November 14, 2014, 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, 2014**

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, 2014.

**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

**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