

**THE SAN JUAN PRESERVATION TRUST**  
**FINANCIAL STATEMENTS**  
**DECEMBER 31, 2012 and 2011**

# The San Juan Preservation Trust

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December 31, 2012 and 2011

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# Sanders & Sanders Sanders

CERTIFIED PUBLIC ACCOUNTANTS

*A Professional Service Corporation*

## Independent Auditors' Report

The Board of Trustees  
The San Juan Preservation Trust  
San Juan Islands, Washington

We have audited the accompanying financial statements of San Juan Preservation Trust, (a nonprofit organization) which comprise the statements of financial position as of December 31, 2012, and 2011, and the related statements of activities, cash flows and functional expenses for the years 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 controls relevant to the preparation and fair presentation of the 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 of 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 auditors' 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 auditors consider internal control relevant to the entities' 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 entities' 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 San Juan Preservation Trust, as of December 31, 2012, and 2011, and the changes in their net assets and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.



August 10, 2013

**The San Juan Preservation Trust**  
**Statements of Financial Position**  
**December 31, 2012 and 2011**

	<b>2012</b>	<b>2011</b>
<b>Assets</b>		
Cash and cash equivalents	\$ 1,090,422	\$ 737,490
Accrued investments income receivable	4	5,991
Inventory	5,683	3,334
Prepaid expenses	6,320	3,100
Unconditional promises to give:		
Unrestricted	7,244	4,036
Restricted to land acquisition	6,868	101,975
Allowance for doubtful accounts		(50,000)
Net unconditional promises to give	14,112	56,011
Long term investments	5,084,446	5,520,016
Long term investments - permanently restricted	1,024,827	467,590
Buildings, equipment and furnishings	655,966	248,013
Land and conservation easements	26,812,271	21,114,380
Total assets	\$ 34,694,051	\$ 28,155,925
<b>Liabilities and Net Assets</b>		
Accounts payable and accrued expenses	\$ 58,338	\$ 37,128
Note payable - land transaction	3,078,356	2,799,074
Total liabilities	3,136,694	2,836,202
Net assets		
Unrestricted		
Undesignated	804,249	774,880
Designated for land acquisition	1,133,441	1,023,380
Designated for land stewardship	632,310	607,421
Designated for endowment	537,208	473,514
Land holdings	24,343,197	18,514,303
	27,450,405	21,393,498
Temporarily restricted		
Restricted for land stewardship	977,011	968,815
Restricted for land acquisition	814,810	1,160,159
Restricted for special stewardship endowment	1,277,525	1,315,396
Restricted for specific programs	12,779	14,265
	3,082,125	3,458,635
Permanently restricted		
General endowment	468,590	467,590
Waldron endowment	556,237	
	1,024,827	467,590
Total net assets	31,557,357	25,319,723
Total liabilities and net assets	\$ 34,694,051	\$ 28,155,925

The accompanying notes are an integral part of these financial statements.

**The San Juan Preservation Trust  
Statements Of Activities  
For the Years Ended December 31, 2012 and 2011**

	2012			2011				
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
<b>Support and Revenue</b>								
Contributions	\$ 611,087	\$ 1,723,501	\$ 557,237	\$ 2,891,825	\$ 559,993	\$ 622,972	\$ 500	\$ 1,183,465
Bequests	5,000			5,000				
In-kind contributions	5,696			5,696	12,468			12,468
Land and easements	4,072,090			4,072,090	460,000			460,000
Fundraising events, net of expenses	10,966			10,966	11,561			11,561
Other income	268	20,000		20,268	703	10,000		10,703
Net investment return	466,899	239,564		706,463	131,931	(6,905)		125,026
Released from restriction	2,359,575	(2,359,575)		0	656,813	(656,813)		
	<u>7,531,581</u>	<u>(376,510)</u>	<u>557,237</u>	<u>7,712,308</u>	<u>1,833,469</u>	<u>(30,746)</u>	<u>500</u>	<u>1,803,223</u>
Total support and revenue								
<b>Expenses</b>								
Land preservation programs:								
Easements and acquisitions	660,239			660,239	200,151			200,151
External education	214,094			214,094	215,356			215,356
Stewardship	253,841			253,841	202,146			202,146
Supporting services								
Management and general	187,051			187,051	137,544			137,544
Fundraising	159,449			159,449	157,050			157,050
	<u>1,474,674</u>	<u>0</u>	<u>0</u>	<u>1,474,674</u>	<u>912,247</u>	<u>0</u>	<u>0</u>	<u>912,247</u>
Total expenses								
<b>Change in net assets</b>	6,056,907	(376,510)	557,237	6,237,634	921,222	(30,746)	500	890,976
Net assets at beginning of year	21,393,498	3,458,635	467,590	25,319,723	20,472,276	3,489,381	467,090	24,428,747
Net assets at end of year	<u>\$ 27,450,405</u>	<u>\$ 3,082,125</u>	<u>\$ 1,024,827</u>	<u>\$ 31,557,357</u>	<u>\$ 21,393,498</u>	<u>\$ 3,458,635</u>	<u>\$ 467,590</u>	<u>\$ 25,319,723</u>

The accompanying notes are an integral part of these financial statements.

**The San Juan Preservation Trust**  
**Statements of Cash Flows**  
**For the Years Ended December 31, 2012 and 2011**

	<u>2012</u>	<u>2011</u>
<b>Cash Flows From Operating Activities</b>		
Increase in net assets	\$ 6,237,634	\$ 890,976
Adjustment to reconcile change in net assets to net cash used by operating activities:		
Depreciation	20,028	15,762
Allowance for doubtful accounts	50,000	
Increase (Decrease)		
Accrued investment income receivable	5,988	3,271
Inventory	(2,349)	(1,431)
Prepaid expenses	(3,220)	(1,000)
Unconditional promises to give - unrestricted	(3,209)	(1,905)
Unconditional promises to give - restricted	(4,892)	21,125
Increase (decrease) in accrued expenses	21,211	(16,626)
Net realized and unrealized (gain) loss on investments	(553,022)	52,401
Net realized (gain) loss on dispositions of assets	132	(302)
Contributions of marketable securities	(749,486)	(204,569)
Contributions of land & buildings	(4,072,090)	(460,000)
Contributions restricted for land acquisition	(1,137,513)	(578,699)
Contributions restricted for permanent endowment	(557,237)	(500)
Net cash provided by operating activities	<u>(748,025)</u>	<u>(281,497)</u>
<b>Cash Flows From Investing Activities</b>		
Purchase of investments	(1,878,552)	(6,778,995)
Proceeds from sale and maturity of investments	3,059,392	7,037,499
Proceeds from sale of equipment	100	975
Acquisition of land and buildings	(1,063,201)	(83,721)
Acquisition of equipment	(10,814)	(7,586)
Net cash used by investing activities	<u>106,925</u>	<u>168,172</u>
<b>Cash Flows From Financing Activities</b>		
Contributions restricted for land acquisition	1,137,513	578,699
Payment on note payable	(700,718)	(502,082)
Contributions restricted for permanent endowment	557,237	500
Net cash provided by financing activities	<u>994,032</u>	<u>77,117</u>
<b>Cash and Cash Equivalents at Beginning of Year</b>	<u>737,490</u>	<u>773,698</u>
<b>Cash and Cash Equivalents at End of Year</b>	<u>\$ 1,090,422</u>	<u>\$ 737,490</u>

The accompanying notes are an integral part of these financial statements.

**The San Juan Preservation Trust  
Statement of Functional Expenses  
For the Year Ended December 31, 2012**

	Easements & Acquisitions	External Education	Land Stewardship	Management and General	Fundraising	Total
Staff salaries/Benefits	\$ 120,627	\$ 118,694	\$ 124,083	\$ 67,434	\$ 103,168	\$ 534,006
Easement acquisition	400,135					400,135
Contract Services	15,564	12,044	25,010	6,939	6,436	65,993
Interest	58,394					58,394
Bad debts				50,000		50,000
Payroll taxes	9,997	9,471	10,463	5,504	8,065	43,500
Legal	37,867		3,304		66	41,237
Rent/Utilities	8,208	10,153	5,738	10,153	4,987	39,239
Printing/Media/Identity	595	15,439	746	544	18,847	36,171
Meetings	595	22,148	2,443	4,617	2,806	32,609
Maintenance/Cleaning	993	242	29,203	1,542	211	32,191
Travel	2,787	3,031	15,963	1,543	2,093	25,417
Taxes & fees	443		13,517	2,888	3,730	20,578
Depreciation	1,464	1,768	13,868	1,464	1,464	20,028
Insurance	86	86	1,370	15,470	86	17,098
Accounting				13,034		13,034
Advertising/Outreach		11,865		27	461	12,353
Phone	1,258	1,148	4,085	1,947	2,029	10,467
Supplies	922	1,980	3,658	1,194	1,669	9,423
Postage	294	4,311	371	827	3,157	8,960
Subscriptions/Dues	10	1,714	19	1,924	174	3,841
	<u>\$ 660,239</u>	<u>\$ 214,094</u>	<u>\$ 253,841</u>	<u>\$ 187,051</u>	<u>\$ 159,449</u>	<u>\$ 1,474,674</u>

The accompanying notes are an integral part of these financial statements.

**The San Juan Preservation Trust  
Statement of Functional Expenses  
For the Year Ended December 31, 2011**

	Easements & Acquisitions	External Education	Land Stewardship	Management and General	Fundraising	Total
Staff salaries/Benefits	\$ 110,569	\$ 104,400	\$ 127,920	\$ 66,257	\$ 100,108	\$ 509,254
Contract services	3,285	32,635	9,564	4,238	7,608	57,330
Interest expense	50,273					50,273
Payroll taxes	9,932	8,891	11,339	5,860	8,671	44,693
Rent and utilities	8,315	10,168	5,459	10,246	5,003	39,191
Printing/Media/Identity	1,344	14,526	637	2,655	18,099	37,261
Meetings	218	27,214	1,426	4,639	2,480	35,977
Taxes /Fees			12,330	7,671	2,828	22,829
Deprecation	1,599	1,889	9,076	1,599	1,599	15,762
Travel	1,488	2,027	7,189	976	1,518	13,198
Legal	10,372		2,289	163	65	12,889
Accounting				12,068		12,068
Supplies	742	2,718	3,120	2,517	2,040	11,137
Phone	1,436	1,593	3,592	1,982	2,242	10,845
Bad debts				10,475		10,475
Postage	240	4,532	510	822	3,138	9,242
Insurance	257	257	4,609	2,103	256	7,482
Maintenance	81	38	3,086	1,472	135	4,812
Incentives/Gifts		3,360		14	1,100	4,474
Subscriptions/Dues		580		1,787	160	2,527
Advertising/Outreach		528				528
	<u>\$ 200,151</u>	<u>\$ 215,356</u>	<u>\$ 202,146</u>	<u>\$ 137,544</u>	<u>\$ 157,050</u>	<u>\$ 912,247</u>

The accompanying notes are an integral part of these financial statements.

**The San Juan Preservation Trust**  
**Notes to the Financial Statements**  
**For the Years Ended December 31, 2012 and 2011**

**The Organization**

The San Juan Preservation Trust (the Trust) is a not-for-profit corporation exempt from Federal income tax under Section 501(c)(3) of the Internal Revenue Code. It was established in 1979 to preserve and protect the natural values and scenic beauty of the San Juan Islands and environs by acting as custodian of land of special significance through acquisitions of conservation easements and land by gift or purchase.

**Note 1 – Summary of Significant Accounting Policies**

The financial statements of the San Juan Preservation Trust have been prepared on the accrual basis of accounting and accordingly reflect all significant receivables, payables, and other liabilities.

*a. Financial Statement Presentation.*

The Trust follows the recommendations of the Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) Topic 958 *Not-for-Profit Entities*, which requires reporting of information regarding its financial position and activities according to three classes of net assets: unrestricted net assets, temporarily restricted net assets and permanently restricted net assets.

*b. Restricted and Unrestricted Revenue.*

Contributions received are recorded as increases in unrestricted, temporarily restricted, or permanently restricted net assets, depending on the existence and or nature of any donor restrictions.

When the Trust receives resources donated for specific purposes, the resources are treated as temporarily restricted net assets. When a donor restriction ends, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of activities as net assets released from restrictions. When a donor places permanent restrictions on income producing assets, the resources are classified as permanently restricted net assets.

The Trust reports gifts of long-lived assets that arrive with a donor's explicit restrictions that specify how the assets are to be used, and gifts of cash or other assets that must be used to acquire long-lived assets, as restricted support. The Trust reports expirations of donor restrictions when the donated or acquired long-lived assets are placed in service. Other gifts of land, buildings and equipment are treated as unrestricted support if there are no explicit donor stipulations specifying how the donated assets must be used.

Absent explicit donor instructions investment earnings of temporarily restricted net assets are treated by the Trust as unrestricted income and may be combined with other unrestricted net assets.

*c. Designated Net Assets*

From time to time, the Trust designates a portion of its unrestricted net assets for special purposes. Since these designations are made by the Trustees and not by donors, the net assets are considered to be designated, but unrestricted.

*d. Gifts of Land and Conservation Easements*

The Trust records gifts of land at their estimated fair value as of the date of the gift. Fair value is based on appraised value, if available, or at assessed value for property taxation purposes. Conservation easements are not valued in the Trust's financial records as they carry no rights of affirmative use or access except for monitoring purposes, and constitute an obligation of the Trust to maintain and defend them.

*e. Purchases of Land and Conservation Easements*

The Trust records purchases of land at the lower of cost or fair value. Cost includes direct related costs, closing fees and taxes, legal fees, and survey and engineering costs. Purchased conservation easements, along with direct related costs of purchase, are treated as an expense in the Trust's financial records as they carry no rights of affirmative use or access except for monitoring purposes and constitute an obligation of the Trust to maintain and defend them.

*f. Promises to Give*

Unconditional promises to give are recognized as revenue in the period received. Unconditional promises to give that are expected to be collected within one year are recorded at net realizable value. Unconditional promises to give that are expected to be collected in future years are recorded at the present value of their estimated future cash flows. The discounts on those amounts are computed using risk-free interest rates applicable to the years in which the promises are received. Amortization of the discount over time is included in contribution revenue. Conditional promises to give are not recognized until the conditions on which they depend are substantially met.

*g. Cash and Cash Equivalents*

The Trust considers all unrestricted highly liquid investments with an initial maturity of three months or less to be cash equivalents.

*h. Inventories*

Inventories are stated at the lower of cost or market determined by the first-in, first-out method.

*i. Donated Property and Services*

The Trust records the value of materials donated by businesses and individuals in the regular course of business at their estimated fair value. The Trust follows the policy of the FASB and records donations of specialized services requiring specific expertise. Contributions of unspecialized labor are not recorded in the financial records. For example, unpaid volunteers make significant contributions of their time to the Trust. The value of this contributed time is not reflected in these statements since it is not susceptible to objective measurement or valuation.

*j. Concentration of Contributions*

The organization's fundraising efforts focus primarily on land owners and residents of the San Juan Islands. Economic conditions that impact the region can impact Trust contributions. Contributions are also sought from other individuals and organizations interested in the preservation of this geographic area.

*k. Investments*

Investments consist of marketable debt and equity securities, which are carried at their fair values in the statements of financial position. The Trust determines fair value for these investments in accordance with ASC Topic 820-10 *Fair Value Measurements*. Unrealized gains and losses are included in the change in net assets in the accompanying statement of activities. Donated investments are reflected as contributions at their market value at the date of receipt.

*l. Functional Allocation of Expenses*

The costs of providing the various programs and other activities have been summarized in accordance with their principal purpose in the statements of activities and in the statements of functional expenses. Expenses related to more than one purpose are allocated among the programs and support services benefited.

The Trust provided the following program services:

- Easements & Acquisitions - costs of acquiring land and easements.
- External Education - education of the public.
- Stewardship - oversight and protection of Trust land and conservation easements including restoration of natural habitat and annual monitoring of land status.

Supporting services are divided between Management and General and Fundraising expenditures. Periodically, fundraising includes major campaigns to raise funds for specific land acquisition projects.

*m. Estimates*

Management uses estimates and assumptions in preparing the financial statements. Those estimates and assumptions affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, and reported revenues and expenses. Actual results could differ from those estimates.

*n. Reclassifications*

Certain accounts in the prior year financial statements have been reclassified to conform to the presentation in the current year financial statements. The reclassifications have no impact on the previously reported change in net assets.

*o. Federal Income Tax*

The Trust's increases in net assets are exempt from federal income taxation under Internal Revenue Code Section 501(c)(3) as a public supported charity. In addition, the Trust qualifies for the charitable contribution deduction under Section 170(b)(1)(A) and has been classified as an organization other than a private foundation under Section 509(a)(2). The Trust's management believes that returns for years prior to 2009, are no longer subject to income tax examination.

*p. Investment Pool*

The Trust maintains a master investment account for its donor-restricted and board-designated endowment accounts. Realized and unrealized gains and losses from securities in the master investment account are allocated at least annually to the two segments of the master account based on the relationship of the market value of each endowment to the total market value of the master investment account, as adjusted for additions to or deductions from those accounts.

*q. Subsequent Events*

Management has evaluated subsequent events through August 10, 2013, the date the financial statements were available to be issued.

**Note 2 – Buildings, Equipment and Furnishings**

Buildings, equipment and furnishings at year end consist of the following components:

	<b><u>2012</u></b>		
	<u>Cost</u>	Accumulated <u>Depreciation</u>	<u>Net</u>
Stewardship buildings	\$ 621,500	\$ 12,219	\$ 609,281
Stewardship equipment	38,156	7,114	31,042
Office equipment & furnishings	<u>92,642</u>	<u>76,999</u>	<u>15,643</u>
Total	<u>\$ 752,298</u>	<u>\$ 96,332</u>	<u>\$ 655,966</u>
	<b><u>2011</u></b>		
	<u>Cost</u>	Accumulated <u>Depreciation</u>	<u>Net</u>
Stewardship buildings	\$ 204,100	\$ 5,103	\$ 198,997
Stewardship equipment	29,700	2,160	27,540
Office equipment & furnishings	<u>92,593</u>	<u>71,117</u>	<u>21,476</u>
Total	<u>\$ 326,393</u>	<u>\$ 78,380</u>	<u>\$ 248,013</u>

Stewardship buildings, equipment and furnishings include office equipment for Trust operations, plus assets acquired as part of land transactions. Depreciation is calculated using the straight-line method. Office equipment and furnishing, which includes software, are depreciated over three to seven years. Stewardship buildings are depreciated over forty years. Stewardship equipment for maintenance of managed lands is depreciated over seven years.

All acquisitions of equipment and furnishings in excess of \$200, and all expenditures for repairs, maintenance, renewals, and betterments that materially prolong the useful lives of assets are capitalized. Equipment and furnishings are carried at cost or, if donated, at the approximate fair value at the date of donation. Depreciation expenses totaled \$20,028 in 2012, and \$15,762 in 2011.

**Note 3 – Cash, Cash Equivalents and Investments**

Investments are held in mutual funds in equities and fixed income investments. Fair values for investments are determined by reference to quoted market prices. Cash and cash equivalents include deposits (including certificates of deposit) with institutions insured by the Federal government, as well as in cash management accounts that are not directly insured by the Federal government. Interest rates on cash and cash equivalents ranged from 0.0001% to 0.26% in 2012, and .03% to .06% in 2011.

A summary of cash, cash equivalents and investments at the end of years 2012 and 2011 follows:

	<b><u>2012</u></b>		
	<u>Cost</u>	<u>Market Value</u>	<u>Unrealized Gain (Loss)</u>
Mutual funds-Fixed income	\$ 2,207,679	\$ 2,240,084	\$ 32,405
Mutual funds-Equity securities	3,462,937	3,869,189	406,252
Cash and cash equivalents	<u>1,090,422</u>	<u>1,090,422</u>	<u>.</u>
Total	<u>\$ 6,761,038</u>	<u>\$ 7,199,695</u>	<u>\$ 438,657</u>
	<b><u>2011</u></b>		
	<u>Cost</u>	<u>Market Value</u>	<u>Unrealized Gain (Loss)</u>
Mutual funds-Fixed income	\$ 2,436,621	\$ 2,454,527	\$ 17,906
Mutual fund-Equity securities	3,553,021	3,533,079	(19,942)
Cash and cash equivalents	<u>737,490</u>	<u>737,490</u>	<u>.</u>
Total	<u>\$ 6,727,132</u>	<u>\$ 6,725,096</u>	<u>\$ (2,036)</u>

Investment gains and losses follow:

	<b><u>2012</u></b>	<b><u>2011</u></b>
Realized gains (losses)	\$ 112,328	\$ (50,364)
Unrealized gains (losses)	440,693	(2,036)
Investment fees (23,352)	(36,590)	
Interest and dividends:		
Unrestricted	5,411	15,337
Unrestricted designated by the Board	115,884	170,679
Temporarily restricted	<u>55,499</u>	<u>28,000</u>
Net investment return	<u>\$ 706,463</u>	<u>\$ 125,026</u>

The Trust's investment portfolio is managed by a professional investment firm. Monthly investment fees are paid based on portfolio market value. Investment fees paid or accrued totaled \$23,352 in 2012, and \$36,590 in 2011. Fees paid to mutual funds are deducted directly from investment earnings and have not been shown separately.

Financial instruments that potentially subject the Trust to concentrations of credit risk include temporary cash investments. The Trust places its temporary cash investments with financial and brokerage institutions. Temporary cash investment credit exposure is limited by investments in cash management funds that invest in a broad range of liquid investments. The Trust's temporary cash investments subject to credit risk held in

brokerage accounts totaled \$758,128 at year end 2012, and \$549,588 at year end 2011. The Trust also invests in bond mutual funds and individual bond issues. Credit risk is minimized by selecting a broad assortment of issuers.

The Trust maintains cash balances for operations or before transfer to brokerage institutions at a single bank. The balances are insured by the Federal Deposit Insurance Corporation up to \$250,000. The Trust had an uninsured balance of \$63,357 at December 31, 2012.

A portion of equity securities and fixed income investments are handled through investments in mutual funds some of which invest in international markets. Such investments may expose the Trust to financial risk through currency fluctuations and unforeseen international events.

#### **Note 4 – Fair Value Measurements**

The Trust has adopted the FASB ASC Topic 820-10 *Fair Value Measurements*, which defines fair value, establishes a framework for measuring fair value under generally accepted accounting principles and specifies disclosures concerning fair value measurements. Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability in an orderly transaction between market participants on the measurement date.

Topic 820-10 establishes a hierarchy of valuation inputs based on the extent to which the inputs are observable in the marketplace. Observable inputs reflect market data obtained from participants and unobservable inputs reflect the entity's own assumptions about how market participants would value an asset or liability based on the best information available. Valuation techniques used to measure fair value must maximize the use of observable inputs and minimize the use of unobservable inputs. The standard describes a fair value hierarchy based on three levels of inputs, of which the first two are considered observable and the last unobservable, that may be used to measure fair value.

The following describes the hierarchy of inputs, with decreasing levels of reliability, used to measure fair value and the primary valuation methodologies used by the Trust for financial instruments measured at fair value on a recurring basis.

- Level 1 – quoted prices in active markets for identical assets or liabilities.
- Level 2 – inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the same assets or liabilities.
- Level 3 – unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

The following table presents the Trust's financial instruments carried at fair value as of December 31, 2012, and 2011:

	<u>2012</u>	<u>2011</u>
Cash and cash equivalents	\$ 1,090,422	\$ 737,489
Fixed income mutual funds	2,240,084	2,472,727
Large-Cap mutual funds	2,713,003	2,120,602
Mid-cap equity mutual funds	313,662	140,748
Small cap equity mutual funds	90,039	138,677
Foreign equity mutual funds	<u>752,485</u>	<u>1,114,852</u>
	<u>\$ 7,199,695</u>	<u>\$ 6,725,095</u>

All valuations are considered to be Level 1 valuations and are provided by the Trust's investment advisory firm. Fair values reported may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the Trust believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different estimate of fair value at the reporting date.

#### **Note 5 – Non Cash Transactions and Cash Flow Information**

The following donations have been recorded in the financial records:

	<u>2012</u>	<u>2011</u>
Land	\$ 4,072,090	\$ 460,000
Marketable securities	749,486	204,569
Legal services	1,456	2,021
Professional services		7,367
Transportation	850	2,500
Outreach event supplies	3,390	580

The Trust acquired two parcels using seller financing of \$980,000 during the year ending December 31, 2012.

Cash expenditures for interest expense were \$40,057 in 2012, and \$50,227 in 2011. There were no payments for income taxes in either year.

#### **Note 6 – Promises to Give**

Payments on unconditional promises to give at December 31, 2012, and 2011, are expected to be received as follows:

	<u>2012</u>	<u>2011</u>
Receivable in less than one year	\$ 14,112	\$ 106,011
Less allowance for uncollectible promises	_____	(50,000)
Net unconditional promises to give	<u>\$ 14,112</u>	<u>\$ 56,011</u>

**Note 7 - Land and Conservations Easements**

At the end of 2012 a total of 15,056 acres are under protection after adjustment for the overlap between owned land and conservations easements. The Trust holds and protects 217 conservation easements, including two easements received in 2012 covering 248 acres, and two easements received in 2011 covering 87 acres. In 2012 a conservation easement covering 20 acres and over 2,400 feet of waterfront was purchased.

Other land activities during 2012 include a donation by The Nature Conservancy of approximately 480 acres on Waldron Island along with the transfer of an endowment for maintenance of the property. The Trust purchased 112 acres on Orcas Island to expand the Turtleback preserve property. The Turtleback transaction included a real estate financing contract with the sellers. The Trust acquired a San Juan Island agricultural property with a combination of a land donation, life estate and real estate financing contract. The 697 acre agricultural property was previously protected by a conservation easement. Death of the donor in 2012 terminated the life estate restriction.

During 2011, the Trust purchased a 39 acre San Juan Island wetlands and received donations of a San Juan Island 20 acre parcel and a shoreline parcel on Orcas. .

The Trust holds three donated land parcels that are encumbered by life estates. It is the intention of the Trust to sell these parcels when the encumbrances are lifted.

**Note 8 – Notes Payable**

The Trust borrowed \$3,400,000 from a private party to serve as bridge financing for the purchase of Vendovi Island, in 2010. Interest only payments are due annually at an interest rate of 1.53%. The loan is non-recourse and secured by the property with a Deed of Trust. Partial principal payments are due at the end of year 6 and year 7, with the remaining balance due in full at the end of year 8 (December 2018), or whenever the property is sold or transferred to an approved entity. In addition, the Trust is actively seeking contributions for repayments of the loan and is required to transfer those funds to the lender as received. These payments have eliminated the amount due in 2016 and reduced the amount due in 2017.

As part of the acquisition of the Turtleneck property on Orcas Island, a real estate contract with the sellers was negotiated with a face value of \$380,000. The loan is non-recourse and secured by the property with a Deed of Trust. Interest is accruing at 4% per annum with full payment required on the note by October 2014. The Trust will make principal payment as contributions restricted to that purpose become available.

As part of the acquisition of the Red Mill Farm property on San Juan Island, a real estate contract with a seller was negotiated with a face value of \$600,000. Payments of \$200,000 plus interest at 4% per annum are scheduled over three years beginning March, 2013.

Future scheduled payments by year are as follows:

2013	\$ 200,000
2014	580,000
2015	200,000
2017	698,356
2018	<u>1,400,000</u>
	<u>\$ 3,078,356</u>

### Note 9 – Operating Leases

The Trust rents office space in two locations. One office is rented on a month to month basis. The other office has a lease until March 2013. After the balance sheet date, the lease was renewed for one year to March 2014, with an option for an additional three year renewal. The new lease includes an option to cancel with 90 days' notice. Operating lease payments were \$25,200, in 2012, and 2011.

### Note 10 – Employee Benefit Plans

The Trust allows qualifying full-time employees to participate in a tax deferred SIMPLE IRA plan. Employees may make elective contributions to the plan up to the maximum amount allowed by the Internal Revenue Code. The Trust matches these contributions up to a maximum of 3% of gross salaries for participating employees. Plan expenses were \$13,697 in 2012, and \$11,175 in 2011.

The Trust allows qualifying full-time employees to participate in a group health insurance policy. Plan expenses totaled \$39,110 in 2012, and \$37,592 in 2011.

### Note 11 – Endowments

The Trust manages endowments that include both donor-restricted net assets and net assets designated by the Board of Trustees to function as endowments. Net assets associated with endowment funds, including amounts designated by the Board to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions.

#### Adoption of UPMIFA and reclassifications

The State of Washington enacted the Uniform Prudent Management of Institutional Funds Act (the Act), effective July 1, 2009, the provisions of which apply to endowments existing on or established after that date.

Under the Act, the Trust classifies as permanently restricted net assets the original value of gifts donated to the permanent endowment, and accumulations to the permanent endowment made in accordance with the direction of the donor. The remaining portion of the donor-restricted endowment that is not classified as permanently restricted is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Trust in accordance with the Act.

#### Endowment investment policies

Under the Trust's endowment policies, the Trust's investment firm maintains a portfolio diversified among equity and fixed rate investments and seeks to maximize investment

returns through both capital appreciation and current yield. Investment risk is measured in terms of total endowment funds. Investment assets and allocation between asset classes and strategies are managed to reduce levels of market or other risks.

#### Endowment spending policies-General Endowment

The Board has determined the need to grow the endowment funds outweighs the need for current expenditure. Accordingly, only investment fee expenditures have been charged to the endowments. Earnings have not been transferred for Trust use through December 31, 2012. All investment income through December 31, 2012 has been reinvested.

#### Endowment spending policies-Special Endowments

Trust spending policies have been adopted to balance the objective of maintaining the purchasing power of the endowments through investment return and providing current funds for the endowed projects.

#### Board-designated Endowment

In prior years, the Board of Trustees designated \$468,040 of unrestricted net assets as a general endowment fund to support the mission of the Trust. Since these amounts resulted from an internal designation and are not donor-restricted, the general board-designated fund is classified as unrestricted net assets. For investment purposes, these funds are pooled with the Trust's donor-designated general endowment portfolio.

#### Donor Restricted Endowments

The Trust maintains a donor restricted General Endowment, Waldron Endowment and Special Stewardship endowments:

Special Stewardship: In 2006, the Trust, together with the San Juan County Land Bank (the Land Bank) acquired a large parcel of land on Orcas Island known as "Turtleback Preserve". Under the arrangement, the Land Bank received title to the land and the Trust received a conservation easement. Under an agreement between the Trust and the Land Bank the Trust established a Special Stewardship quasi-endowment in the amount of \$1,000,000 to support the long term maintenance of the Preserve. The Trust made the final contribution of \$200,000 in 2011 to fully fund this Special Stewardship quasi-endowment. The principal and earnings of this endowment are available for distribution under the supervision of both the Trust and the Land Bank. The corpus and earnings of this quasi-endowment are classified as temporarily restricted. Earnings are reported net of investment fees which were \$3,895 in 2012, and \$5,552 in 2011.

In 2012, with Land Bank approval, \$16,000 was transferred to cover Turtleback general expenses and \$250,000 was transferred to complete the financing package for the Turtleneck land parcel, which is contiguous to the Turtleback Preserve.

General Endowment: The Trust's permanently restricted General Endowment corpus was established to provide a sustainable source of unrestricted revenue for general operations. For investment purposes the General Endowment is pooled with the Trust's Board designated endowment portfolio, and earnings are allocated annually. Earnings are reported net of investment fees of \$3,794 in 2012, and \$6,086 in 2011.

Waldron Endowment: In 2012 The Nature Conservancy (TNC) transferred \$556,237 for a permanently restricted endowment, the earnings of which are to be used to support the maintenance of 480 acres of land on Waldron Island. Expenditures in 2012 were \$1,342 for investment fees, and \$11,435 for Waldron expenses. The TNC requires status reporting on this endowment for a period of ten years.

Endowment composition by type:

	<b>2012</b>			
	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Net assets - beginning	\$ 473,514	\$ 1,315,396	\$ 467,590	\$ 2,256,500
Changes in investments:				
Contributions			557,237	557,237
Distributions		(277,435)		(277,435)
Investment income	13,664	70,820		84,484
Net appreciation (depreciation)	<u>50,030</u>	<u>168,743</u>	<u>          </u>	<u>218,773</u>
Net assets - ending	<u>\$ 537,208</u>	<u>\$ 1,277,524</u>	<u>\$ 1,024,827</u>	<u>\$ 2,839,559</u>

	<b>2011</b>			
	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Net assets - beginning	\$ 475,196	\$ 1,122,301	\$ 467,090	\$ 2,064,587
Changes in investments:				
Contributions		200,000	500	200,500
Investment income	(2,213)	(7,174)		(9,387)
Net appreciation (depreciation)	<u>531</u>	<u>269</u>	<u>          </u>	<u>800</u>
Net assets - ending	<u>\$ 473,514</u>	<u>\$ 1,315,396</u>	<u>\$ 467,590</u>	<u>\$ 2,256,500</u>

## **Note 12 – Restrictions on Net Assets**

Restrictions on net assets are classified as follows:

### Unrestricted Net Assets

Use of unrestricted net assets is at the discretion of the Trustees. From time to time, the Trustees designate unrestricted net assets for particular purposes. Earnings of temporarily restricted land stewardship net assets have been designated for future land stewardship needs, earnings of temporarily restricted land acquisition net assets have been designated for future land acquisition needs. Periodically the Trustees budget these designated earnings for current expenses and those amounts are removed from their Board designated categories and become undesignated unrestricted net assets.

### Temporarily Restricted Net Assets

Net assets restricted for land stewardship are resources donated to the Trust to cover expenses of the Trust for restoration of natural habitat on Trust lands and defense of the Trust's interest in land and easements. This supports the Trust's efforts to carry out the donor's intent in transferring conservation easements or outright gifts of land to the Trust.

Net assets restricted for land acquisition are resources donated to the Trust for the purchase of significant conservation land or easements. Some donations are further restricted as to island of interest or acquisition project of interest.

Net assets restricted for special stewardship endowment are resources establishing a quasi-endowment to provide earnings temporarily restricted to support the Turtleback Preserve.

Net assets restricted for specific programs are contributions restricted for various special projects.

*Permanently Restricted Net Assets*

General endowment contains assets donated to create a perpetual source of unrestricted income to the Trust.

Waldron endowment was established in 2012 to provide earnings temporarily restricted to stewardship maintenance of Waldron Island preserves.