



Financial Statements

Year ended June 30, 2011

with

Report of Independent Auditors

Report of Independent Auditors

To the Board of Directors of Baykeeper:

We have audited the accompanying statement of financial position of Baykeeper as of June 30, 2011 and 2010, and the related statements of activities and changes in net assets, functional expenses and cash flows for the years then ended. These financial statements are the responsibility of the management of Baykeeper. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Baykeeper as of June 30, 2011 and 2010, and the results of its operations and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Wilson Markle Stuckey Hardesty & Bott
March 9, 2012

Baykeeper
Statement of Financial Position
June 30, 2011 and 2010

	2011	As adjusted See Note 9 2010
Assets		
Cash and cash equivalents – Unrestricted	\$ 283,118	\$ 438,917
Cash and cash equivalents – Restricted	73,208	3,854
Investments	361,372	319,787
Grants and pledges receivable	6,815	25,300
Settlements receivable – Current	9,000	46,500
Settlements receivable – Long-term	32,000	41,000
Prepaid expenses – Litigation	468,355	132,582
Prepaid expenses – Other	11,823	18,909
Attorney-client trust accounts	227,782	195,291
Property and equipment, net	11,808	19,060
Deposits	9,858	9,858
 Total assets	 \$1,495,139	 \$1,251,058
 Liabilities and Net Assets		
Liabilities		
Accounts payable and accrued expenses	\$ 352,401	\$ 118,321
Reserve	73,208	3,854
Deferred revenue	248,044	231,870
Deferred rent	1,166	–
 Total liabilities	 674,819	 354,045
 Net assets		
Unrestricted		
Undesignated	375,129	421,226
Board-designated	359,566	310,712
 Total unrestricted	 734,695	 731,938
 Temporarily restricted	 85,625	 165,075
 Total net assets	 820,320	 897,013
 Total liabilities and net assets	 \$1,495,139	 \$1,251,058

See accompanying notes.

Baykeeper
Statement of Activates and Changes in Net Assets
Years ended June 30, 2011 and 2010

	Unrestricted	Temporarily restricted	2011 Totals	Unrestricted	Temporarily restricted	As adjusted See Note 9 2010 Totals
Support and revenue						
Contributions	\$ 279,548	\$200,750	\$ 480,298	\$ 754,529	\$ 55,000	\$ 809,529
In-kind services	1,096,418	-	1,096,418	884,635	-	884,635
Fee and cost recovery	526,670	-	526,670	304,284	-	304,284
Settlement monitoring	97	-	97	12,478	-	12,478
Investment, net	55,099	-	55,099	33,966	-	33,966
Other	28,977	-	28,977	3,653	-	3,653
Net assets reclassified	280,200	(280,200)	-	20,885	(20,885)	-
Total support and revenue	2,267,009	(79,450)	2,187,559	2,014,430	34,115	2,048,545
Expenses						
Program services	2,055,374	-	2,055,374	1,797,698	-	1,797,698
Management and general	70,008	-	70,008	69,432	-	69,432
Fundraising	138,870	-	138,870	74,294	-	74,294
Total expenses	2,264,252	-	2,264,252	1,941,424	-	1,941,424
Changes in net assets	2,757	(79,450)	(76,693)	73,006	34,115	107,121
Net assets, beginning of year	731,938	165,075	897,013	658,932	130,960	789,892
Net assets, end of year	\$ 734,695	\$ 85,625	\$ 820,320	\$ 731,938	\$165,075	\$ 897,013

See accompanying notes.

Baykeeper
Statement of Functional Expenses
Years ended June 30, 2011 and 2010

Expenses	Program services	Supporting services		2011 Totals
		Management and general	Fundraising	
Salaries	\$ 315,629	\$27,341	\$ 78,566	\$ 421,536
Payroll taxes	25,412	1,523	5,092	32,027
Employee benefits	53,181	4,683	12,979	70,843
Bay patrol	15,766	—	—	15,766
Conferences and meetings	14,162	520	80	14,762
Information technology	1,778	54	2,510	4,342
Insurance	4,874	292	1,335	6,501
Occupancy	44,871	2,689	8,992	56,552
Operating	14,941	6,048	7,275	28,264
Professional services				
Accounting	—	21,388	—	21,388
Legal – Environmental law enforcement	1,400,260	—	—	1,400,260
Scientific	133,988	—	374	134,362
Other	11,125	3,588	15,476	30,189
Publications and outreach	7,326	1,705	5,431	14,462
Travel	5,578	—	168	5,746
Depreciation	6,483	177	592	7,252
Total expenses	\$2,055,374	\$70,008	\$138,870	\$2,264,252

Expenses	Program services	Supporting services		2010 Totals
		Management and general	Fundraising	
Salaries	\$ 327,695	\$25,424	\$36,044	\$ 389,163
Payroll taxes	26,954	1,422	2,983	31,359
Employee benefits	57,687	3,044	6,384	67,115
Bay patrol	16,492	—	—	16,492
Conferences and meetings	—	610	—	610
Information technology	1,203	65	159	1,427
Insurance	3,244	2,867	359	6,470
Occupancy	48,598	2,564	5,378	56,540
Operating	57,132	6,801	13,804	77,737
Professional services				
Accounting	—	26,225	—	26,225
Legal – Environmental law enforcement	1,189,571	—	—	1,189,571
Scientific	45,391	—	—	45,391
Other	3,142	281	1,612	5,035
Publications and outreach	525	—	7,294	7,819
Travel	8,733	—	6	8,739
Depreciation	11,331	129	271	11,731
Total expenses	\$1,797,698	\$69,432	\$74,294	\$1,941,424

See accompanying notes.

Baykeeper
Statement of Cash Flows
Years ended June 30, 2011 and 2010

	2011	As adjusted See Note 9 2010
Cash flows from operating activities		
Change in net assets	(\$ 76,693)	\$107,121
Adjustments to reconcile change in net assets with cash flows provided by operating activities		
Realized (gains) losses and unrealized (appreciation) depreciation of investments	(49,211)	(26,895)
Contributions of investments	(1,702)	(10,732)
(Gains) from sales of property and equipment	(25,700)	(200)
Depreciation	7,252	11,731
Changes in assets and liabilities		
Grants and pledges receivable	18,485	4,500
Settlements receivable	46,500	(17,500)
Accounts receivable	-	107
Prepaid expenses – Litigation	(335,773)	(132,582)
Prepaid expenses – Other	7,086	3,877
Attorney-client trust accounts	(32,491)	(72,147)
Accounts payable and accrued expenses	234,080	88,424
Reserve	-	-
Deferred revenue	16,174	178,892
Deferred rent	1,166	-
	(190,827)	134,596
Net cash provided (used) by operating activities		
Cash flows from investing activities		
Purchases of investments	(1,334)	(1,076)
Proceeds from sale of investments	10,662	1,636
Purchases of property and equipment	-	(14,516)
Proceeds from sale of property and equipment	25,700	200
	35,028	(13,756)
Net cash provided (used) by investing activities		
Net change in cash and cash equivalents	(155,799)	120,840
Cash and cash equivalents, beginning of year	438,917	318,077
Cash and cash equivalents, end of year	\$283,118	\$438,917

See accompanying notes.

Baykeeper
Notes to Financial Statements
June 30, 2011

Note 1 – Summary of significant accounting policies

Basis of presentation

The mission of San Francisco Baykeeper (Baykeeper) is to protect and restore the water quality of the San Francisco Bay (Bay). For more than 20 years, Baykeeper has worked to address the greatest threats to the health of the Bay in order to protect local wildlife, the ecosystem and Bay Area communities.

The Bay is part of the largest estuarine system on the Pacific Coast of the Americas and one of the most ecologically productive water bodies in the world. Open water habitats, intertidal mudflats, rocky shores, salt ponds, marshes and shaded creek habitats all come together to form the iconic San Francisco Bay that defines the character and community of the Bay Area.

A diverse wildlife community has historically thrived in and around the Bay and can flourish again. The Bay provides a home for 130 fish species and nursery for ocean-going herring, sturgeon, salmon and Dungeness crab. Millions of migratory shorebirds using the Pacific Flyway depend on the Bay as a resting spot. Twenty-two threatened or endangered species, including the Snowy plover and the mission blue butterfly, are found in the watershed of the Bay. Hundreds of native rare or endemic plants grow in the wide variety of environmental conditions unique to the Bay and surrounding landscapes.

Seven million people, 1,300 industrial facilities, 100 cities, two major ports and massive oil refineries also surround the Bay. Every day, toxic pollution from the urban and industrial landscape flows into the Bay, threatening people and wildlife. Aging sewer infrastructures release millions of gallons of raw and undertreated sewage into local creeks and the Bay each winter and rain washes pollution from industrial sites, roadways and pesticide-laden landscapes directly into waterways with no treatment. Meanwhile, the bustling maritime economy of the Bay increases the risk of oil spills and other vessel pollution.

Clean water laws and regulations intended to protect the health of the Bay and its tributaries are not strong enough or enforced consistently. That is where Baykeeper enters. Using advocacy, science and legal action, Baykeeper strengthens clean water laws and regulations to rein in Bay pollution and enforces the Clean Water Act to hold polluters accountable.

Baykeeper
Notes to Financial Statements
June 30, 2011

Note 1 – Summary of significant accounting policies (continued)

As the sole nonprofit organization dedicated to protecting the Bay from pollution, Baykeeper has a tightly focused mission. The small, highly skilled staff of Baykeeper conducts research, water quality monitoring and on-the-water patrols to identify the sources of pollution most damaging to the Bay. The staff of Baykeeper evaluates where there is the greatest need and where it can target advocacy to have the greatest impact on reducing pollution in the Bay. The science and legal staff of Baykeeper work together to develop the most effective strategies for pollution clean-up. Baykeeper engages in advocacy and public education, pushes government agencies to do their job to safeguard and restore the Bay and—when necessary—brings strategic lawsuits under the Clean Water Act to compel polluters to stop contaminating the waters that belong to all.

Baykeeper incorporated as a nonprofit, public benefit corporation in California on January 23, 1987, as the San Francisco Bay-Delta Preservation Association, and became Baykeeper in May 1989, the fourth “Waterkeeper” organization in the country. Along with Robert F. Kennedy, Jr. and other leaders, Baykeeper helped found an international network of on-the-water clean water activists to protect local waterways; there are now 200 related groups around the world. Baykeeper holds the “Baykeeper” trademark and licenses its use by other organizations. To avoid confusion, Baykeeper operates primarily under the name San Francisco Baykeeper.

Basis of accounting

Baykeeper prepares its financial statements using the accrual basis of accounting. Baykeeper records revenues when earned and expenses when incurring the related obligations.

Fair value

Baykeeper uses a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. This hierarchy consists of three broad levels: Level 1 inputs consist of unadjusted quoted prices in active markets for identical assets and have the highest priority. Level 2 inputs consist of observable inputs other than quoted prices for identical assets. Level 3 inputs consist of unobservable inputs that reflect internal judgments and have the lowest priority. Baykeeper uses appropriate valuation techniques based on the available inputs to measure the fair value of its investments. When available, Baykeeper measures fair value using Level 1 inputs because they generally provide the most reliable evidence of fair value. Baykeeper only uses Level 3 inputs when Level 1 or Level 2 inputs are not available.

Baykeeper
Notes to Financial Statements
June 30, 2011

Note 1 – Summary of significant accounting policies (continued)

Baykeeper values contributions initially at fair value when promised. Baykeeper only revalues debt and marketable equity securities at least as often as it presents financial statements. For contributions valued initially at fair value but not revalued, Baykeeper treats the initial fair value as cost in subsequent financial statements.

The management of Baykeeper estimates that the aggregate net fair value of financial instruments recognized (including receivable, payables and accrued expenses) approximates their carrying value, as such financial instruments are short-term in nature or bear interest at current market rates.

Subsequent events

The management of Baykeeper has evaluated subsequent events through March 9, 2012, the date these financial statements were available for issuance.

Cash and cash equivalents

Cash and cash equivalents consist of amounts on hand and on deposit with a commercial bank, available within 90 days of demand. The carrying amount of cash approximates fair value due to its short-term nature.

Investments

Investments (Note 2) consist principally of units of pooled investment funds (PIFs) of community foundations, corporate marketable equity securities (stock) and registered investment company shares (mutual funds). Baykeeper records PIFs at their contract value. Contract value represents the amount Baykeeper would realize upon sale, transfer, exchange or liquidation of the investment when transacted with the investment custodians. Contract value of the units of the PIFs is the Baykeeper share of the fair value of the underlying investments, determined by the community foundations, net of certain custodial and administrative fees.

Baykeeper records stock and mutual funds at fair value that the registered investment company holding the investments provides and the management of Baykeeper evaluates. Baykeeper bases the fair value of stock and mutual funds on unadjusted quoted prices in active markets for identical assets, which is a Level 1 input.

Baykeeper records interest, dividends, gains, losses and changes in contract value (unrealized appreciation and depreciation) as net investment income, but not custodial and administrative fees.

Baykeeper
Notes to Financial Statements
June 30, 2011

Note 1 – Summary of significant accounting policies (continued)

The PIFs of the community foundations are subject to variance power under various agreements. The boards of trustees of the community foundations shall have the power to modify any restriction or condition on the distribution of funds for any specified charitable purposes or to a specified organization, if, in the sole judgment of the boards of trustees, such restriction or condition becomes, in effect, unnecessary, incapable of fulfillment or inconsistent with the needs of the community served by the community foundation.

Receivables

Receivables (Note 3) consist principally of amounts due from governmental and corporate entities related to compliance activities and from corporations, foundations and individuals as contributions, grants and pledges. Baykeeper initially records contribution receivables at fair value. Baykeeper estimates the initial fair value of contribution receivables as the estimated present value of expected future cash flows, taking into consideration the risk-free interest rate and expected collection timing and risk. These are Level 2 and Level 3 inputs, using an income approach. Baykeeper records a discount representing the difference between the future cash flows promised by the grantor or pledgor and the estimated present value of the expected future cash flows. Baykeeper accretes the discount, using the interest method and based on actual collections, to contribution support. As of June 30, 2011 and 2010, the management of Baykeeper estimated that any discount of grants and pledges receivable was not material to the financial position of Baykeeper.

Allowance for uncollectible receivable

Baykeeper uses the allowance method to estimate any uncollectible receivables. Under this method, Baykeeper reviews all receivables, and estimates, based on aging, debtor history and other information, an allowance. When Baykeeper exhausts all attempts to collect specific receivables or the debtor discharges the receivable in bankruptcy, Baykeeper writes off the receivable against the estimated allowance. As of June 30, 2011 and 2010, the management of Baykeeper estimated that any allowance for uncollectible receivables was not material to the financial position of Baykeeper.

Property and equipment

Property and equipment consist of furniture, office, computer, boat and laboratory equipment and leasehold improvements. Baykeeper records property and equipment at cost or initially at fair value for contributed items. Baykeeper bases the initial

Baykeeper
Notes to Financial Statements
June 30, 2011

Note 1 – Summary of significant accounting policies (continued)

fair value of contributed property and equipment on comparable sales of identical or similar items in markets available to Baykeeper, which is a Level 2 input, using a market approach. Baykeeper expenses property and equipment with a cost or fair value under \$500 and the costs of maintenance and repairs that do not improve or extend the lives of the property and equipment. Baykeeper computes depreciation using the straight-line method over the estimated useful lives of the property and equipment of five years or the shorter remaining lease term for leasehold improvements.

Attorney-Client Trust Accounts (ACTA)

Baykeeper contracts with various attorneys, under Attorney Retention and Co-Counseling or similar Agreements (Retainer), to assist Baykeeper to compel governmental agencies and corporations to comply with various laws and regulations that protect the health of the Bay and its habitats (Litigation). Generally, contracted Litigation attorneys work on a contingency fee basis; i.e., the contracted Litigation attorneys only receive legal fees based on successful Litigation resulting in a settlement or Court ruling that includes payments for legal fees.

When represented by outside counsel on a contingency fee basis, Baykeeper agrees to be responsible for expert, consultant and other Litigation costs that are necessary to carry out the Litigation. To pay for the costs for each case, Baykeeper sometimes provides assets to outside counsel to hold on behalf of Baykeeper in an Attorney Client Trust Account (ACTA), which California law regulates tightly to protect the assets. Outside attorneys that manage ACTAs must submit invoices to Baykeeper for review and approval before paying any Litigation costs from the ACTAs and must provide monthly accounting to Baykeeper of expert and consultant fees and costs paid from the ACTAs. Assets Baykeeper uses to fund ACTAs may include both unrestricted and restricted funds donated by other organizations.

Baykeeper may pursue Litigation internally, without contracting with outside counsel or establishing a Litigation ACTA. Under those circumstances, Baykeeper capitalizes all costs of Litigation, except staff salaries and indirect costs. Baykeeper expenses capitalized Litigation costs upon resolution of the case and records any related recovery as revenue.

Successful Litigation against governmental agencies and corporations (Defendant) under federal and state environmental laws usually results in Settlement Agree-

Baykeeper
Notes to Financial Statements
June 30, 2011

Note 1 – Summary of significant accounting policies (continued)

ments, Consent Decrees or similar arrangements (Settlement). Settlements generally require the Defendant to take corrective actions at their own expense; perform or contribute to an environmental mitigation project (not conducted by Baykeeper); and partially reimburse Baykeeper for the direct costs of bringing the Litigation, including legal fees (internal and external). Baykeeper records revenue for Settlement funds received that reimburse Baykeeper for the direct costs of bringing the Litigation.

In addition, Defendants generally agree to provide funds to enable Baykeeper to monitor compliance by the Defendant with the Settlement (Compliance). Compliance funds represent a negotiated estimate by Baykeeper and the Defendant of any remaining Litigation and Settlement costs and the future costs Baykeeper will incur to monitor Compliance.

Historically, Baykeeper contracted with outside attorneys to perform and manage Compliance monitoring activities. Accordingly, the contracted Litigation attorneys would establish a Compliance ACTA to receive and disburse the Compliance funds, with Baykeeper authorizing expenditures of Compliance ACTA funds when incurring the related expenses. During the year ended June 30, 2011, Baykeeper elected to manage Compliance monitoring activities and to pay for related costs using bank accounts it opened and controlled. Accordingly, attorneys holding Compliance ACTAs for Baykeeper transferred funds totaling \$131,458 to Baykeeper and Baykeeper opened separate accounts to accept and manage the funds. After June 30, 2011, Baykeeper elected to pay for Compliance monitoring activities using general operating funds and began closing its separate bank accounts and transferring unspent funds to its operating accounts.

Baykeeper defers the recognition of revenue from funds received for Compliance until Baykeeper incurs the related expense or the Compliance period expires. In addition, Baykeeper records the unexpended balances of Compliance ACTAs as assets.

Finally, Baykeeper reclassifies contributed legal services and related in-kind legal expenses to program service revenue and paid legal services when Settlement funds pay contracted Litigation attorneys' contingent legal fees.

Contributions and net assets

Baykeeper recognizes contributions at fair value when a donor makes an unconditional promise to provide support. Net assets include cumulative unrestricted, tempo-

Baykeeper
Notes to Financial Statements
June 30, 2011

Note 1 – Summary of significant accounting policies (continued)

rarily restricted and permanently restricted net assets, net of cumulative expenses. Unrestricted net assets consist of revenue and support not restricted to a particular purpose or time by the donor, net of expenses. Temporarily restricted net assets consist of support restricted by the donor to a particular purpose or time. Temporarily restricted net assets become unrestricted net assets when Baykeeper meets the donor purpose or time restriction. Permanently restricted net assets consist of support restricted by the donor for Baykeeper to hold permanently, allowing for use of only the revenue generated by investing the support. As of June 30, 2011 and 2010, Baykeeper held no permanently restricted net assets.

Contributed services

Attorneys, paralegals and others contribute substantial professional services to Baykeeper. Baykeeper determines the fair value of attorney fees by following judicial precedent to compare a proposed rate with the prevailing rate in the community for similar work performed by attorneys of comparable skill, experience and reputation, considering the novelty and complexity of the issues. In addition, Baykeeper uses the "Laffey Matrix" as a guide for calculating attorney rates. The D.C. Circuit Court approved the Laffey Matrix to provide objective guidance in assessing appropriate hourly rates depending on attorney experience. Baykeeper adjusts the Laffey Matrix by straight-lining annually the multi-year step increases and by the regional difference between attorney rates in the Washington, DC and San Francisco metropolitan areas. Finally, Baykeeper compares rates of other San Francisco attorneys who specialize in environmental litigation. The U.S. District Court for the Northern District of California, in *Baykeeper v. West Bay Sanitary District* 2011 U.S. Dist. LEXIS 138093, upheld this process and approved the rates of Baykeeper staff attorneys and outside counsel. Baykeeper records contributed professional services, including contingent fees, at fair value. This process involves principally Level 2 inputs, using a market approach. Baykeeper bases the fair value of non-legal professional services on the cost of similar services from comparable purchases, which is a Level 3 input, using a cost approach. Baykeeper only reports contributions in-kind of professional services when the professional services are of a professional or technical nature requiring expertise or education not available to Baykeeper and Baykeeper would have paid for the professional services if donors had not contributed them.

Volunteers contribute their time assisting Baykeeper in carrying out its activities. Although the value of volunteer contributions is substantial to the activities of Baykeeper, Baykeeper does not recognize their value herein because they do not meet the

Baykeeper
Notes to Financial Statements
June 30, 2011

Note 1 – Summary of significant accounting policies (continued)

criteria for recognition in accordance with accounting principles generally accepted in the United States of America (US-GAAP).

Allocation of functional expenses

Baykeeper summarized the costs of providing its program and supporting services on a functional basis. Accordingly, Baykeeper allocated certain indirect costs between program and support services based on annual estimates of time and usage.

Income taxes

In letters to Baykeeper, the Internal Revenue Service (IRS) and California Franchise Tax Board (FTB) stated that Baykeeper is exempt from federal income tax under Section 501(c)(3) of the Internal Revenue Code (IRC) and from California bank and corporation taxes under Section 23701(d) of the California Revenue and Taxation Code, respectively. In addition, Baykeeper qualifies for the charitable contribution deduction under IRC Section 170(b)(1)(A) and has been classified as a publicly supported organization as described in IRC Section 509(a)(1). Accordingly, donors are entitled to the maximum charitable contribution deduction allowed by law.

The management of Baykeeper believes that no activities of Baykeeper jeopardized its exemption from income taxes or its classification as a “public charity” or are subject to unrelated business income taxes. Accordingly, Baykeeper did not provide for income taxes.

The management of Baykeeper considers certain tax positions taken by Baykeeper. A tax position is a position taken in a previously filed tax return or a position the management of Baykeeper expects to take in a future tax return that figures in measuring current or deferred income tax assets and liabilities for interim or annual periods. A tax position can result in a permanent reduction in income taxes payable, a deferral of income taxes otherwise currently payable to future years or a change in the expected realizability of deferred tax assets. A tax position also encompasses, but is not limited to:

1. A decision not to file a tax return
2. An allocation or a shift of income between jurisdictions
3. The characterization of income or a decision to exclude reporting taxable income in a return

Baykeeper
Notes to Financial Statements
June 30, 2011

Note 1 – Summary of significant accounting policies (continued)

4. A decision to classify a transaction, entity or other position in a tax return as tax exempt
5. The status of an entity, including its status as a pass-through or tax-exempt entity.

Evaluating a tax position requires the management of Baykeeper to determine, for each tax position, whether it is more likely than not that, upon examination by taxing authorities, such authorities will uphold the tax position and, for each more-likely-than-not tax position, determine the highest benefit with a more than 50% likelihood of realization upon ultimate settlement. Accordingly, it is possible that tax positions taken on tax returns and related amounts recognized herein could vary.

Baykeeper files tax returns with the IRS and FTB. Baykeeper recognizes interest and penalties related to income taxes and tax positions with interest and income tax expense, respectively. As of and for the year ended June 30, 2011, interest and penalties related to income taxes and tax positions were not material. As of June 30, 2011, the management of Baykeeper believes that there are no tax positions of Baykeeper where it is reasonably possible that the total amount of unrecognized tax benefits will significantly increase or decrease within the period ending June 30, 2012. As of June 30, 2011, open tax periods subject to future examination by taxing authorities cover periods from July 1, 2007 through June 30, 2011.

The management of Baykeeper does not believe that differences between income taxes Baykeeper measures using the current “tax position” method and the methods Baykeeper used previously to be material to the financial position of Baykeeper, except for the additional disclosures.

Use of estimates

The preparation of financial statements in conformity with US-GAAP requires the management of Baykeeper to make estimates and assumptions that affect the amounts reported herein. Actual results could differ from those estimated.

Risks and concentrations

Investments are subject to credit and market risks. Credit risk is the probability that parties holding or supporting an investment will default or otherwise fail to perform. Market risk is the inherent change in the value of an investment due to changes in conditions.

Baykeeper
Notes to Financial Statements
June 30, 2011

Note 1 – Summary of significant accounting policies (continued)

Cash and cash equivalents held by the commercial bank exceeded federal deposit insurance limits at various times during the years ended June 30, 2011 and 2010.

During the year ended June 30, 2010, support received from one “cy pres” award totaled approximately 20% of total support and revenue reported.

During the year ended June 30, 2011, in-kind services received from one law firm totaled 49% of total support and revenue and 47% of total expenses.

During the year ended June 30, 2010, in-kind services received from two law firms totaled 50% of total support and revenue and 53% of total expenses.

Note 2 – Investments

As of June 30, 2011 and 2010, investments totaled as follows:

	<u>2011</u>	<u>2010</u>
Contract value		
PIFs	\$359,566	\$310,712
Fair value – Level 1		
Stock	1,777	–
Mutual funds	<u>29</u>	<u>9,075</u>
Total investments	<u>\$361,372</u>	<u>\$319,787</u>

During the years ended June 30, 2011 and 2010, net investment income totaled as follows:

	<u>2011</u>	<u>2010</u>
Dividends and interest	\$ 5,888	\$ 7,071
Unrealized appreciation (depreciation)	<u>49,211</u>	<u>26,895</u>
Net investment income	<u>\$55,099</u>	<u>\$33,966</u>

In addition, during the years ended June 30, 2011 and 2010, Baykeeper incurred custodial and administrative fees on its investments in PIFs, totaling \$2,421 and \$2,415, respectively, and included with operating expenses.

Baykeeper
Notes to Financial Statements
June 30, 2011

Note 3 – Receivables

As of June 30, 2011 and 2010, receivables totaled as follows:

	<u>2011</u>	<u>2010</u>
City of Burlingame	\$30,000	\$ 35,000
Cemex	–	12,500
Town of Hillsborough	5,000	7,500
San Francisco Foundation	–	20,000
County of San Mateo et. al.	6,000	7,500
Port of Stockton	–	25,000
Various individuals and others	<u>6,815</u>	<u>5,300</u>
 Total receivables	 <u>\$47,815</u>	 <u>\$112,800</u>

Note 4 – Property and equipment

As of June 30, 2011 and 2010, property and equipment totaled as follows:

	<u>2011</u>	<u>2010</u>
Furniture	\$ 5,830	\$ 5,830
Office equipment	24,064	24,064
Computer equipment	20,357	20,357
Boat and laboratory equipment	175,759	227,222
Leasehold improvements	<u>1,500</u>	<u>1,500</u>
 Property and equipment, at cost	 227,510	 278,973
Accumulated depreciation	<u>(215,702)</u>	<u>(259,913)</u>
 Property and equipment, net	 <u>\$ 11,808</u>	 <u>\$ 19,060</u>

During the year ended June 30, 2011, Baykeeper sold a fully depreciated boat and related equipment for \$25,700.

Baykeeper
Notes to Financial Statements
June 30, 2011

Note 5 – Temporarily restricted net assets

During the year ended June 30, 2011, temporarily restricted net assets reconciled as follows:

<u>Activity</u>	<u>Beginning</u>	<u>Additions</u>	<u>Releases</u>	<u>Ending</u>
Agricultural Pesticide and Mercury Programs	\$ 16,615	\$ –	(\$ 16,615)	\$ –
Boating operations	80,960	–	(80,960)	–
Municipality Accountability Project	–	115,000	(115,000)	–
Sacramento River Project	50,000	–	(–)	50,000
Time-restricted	<u>17,500</u>	<u>85,750</u>	<u>(67,625)</u>	<u>35,625</u>
Totals	<u>\$165,075</u>	<u>\$200,750</u>	<u>(\$280,200)</u>	<u>\$85,625</u>

During the year ended June 30, 2010, temporarily restricted net assets reconciled as follows:

<u>Activity</u>	<u>Beginning</u>	<u>Additions</u>	<u>Releases</u>	<u>Ending</u>
Agricultural Pesticide and Mercury Programs	\$ –	\$25,000	(\$ 8,385)	\$ 16,615
Boating operations	80,960	–	(–)	80,960
Sacramento River Project	50,000	–	(–)	50,000
Time-restricted	<u>–</u>	<u>30,000</u>	<u>(12,500)</u>	<u>17,500</u>
Totals	<u>\$130,960</u>	<u>\$55,000</u>	<u>(\$20,885)</u>	<u>\$165,075</u>

Note 6 – Endowment funds

Baykeeper follows Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 958-205, “Endowments of Not-for-Profit Organizations: Net Asset Classification of Funds Subject to an Enacted Version of the Uniform Prudent Management of Institutional Funds Act (UPMIFA) and Enhanced Disclosures for All Endowment Funds” and the related state of California version of the UPMIFA (CA-UPMIFA).

Baykeeper
Notes to Financial Statements
June 30, 2011

Note 6 – Endowment funds (continued)

Endowment funds subject to FASB ASC 958-205 include all the endowment funds described below. As of June 30, 2011 and 2010, no endowment funds are subject to the CA-UPMIFA.

The endowment funds of Baykeeper consist of two individual funds held by separate community foundations. The endowment funds of Baykeeper include only funds designated by the Board of Directors to function as endowments. As required by US-GAAP, Baykeeper classifies and records net assets associated with endowment funds, including funds designated by the Board of Directors to function as endowments, based on the existence or absence of donor-imposed restrictions.

The Board of Directors of Baykeeper has interpreted the CA-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. Because of this interpretation, Baykeeper classifies as permanently restricted net assets the original value of gifts donated to the permanent endowment, the original value of subsequent gifts to the permanent endowment and accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund that Baykeeper does not classify as permanently restricted net assets Baykeeper classifies as temporarily restricted net assets until the Board of Directors of Baykeeper appropriates those amounts for expenditure by Baykeeper in a manner consistent with the standard of prudence prescribed by CA-UPMIFA. In accordance with CA-UPMIFA, Baykeeper considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

1. The duration and preservation of the fund
2. The purposes of Baykeeper and the donor-restricted endowment fund
3. General economic conditions
4. The possible effect of inflation and deflation
5. The expected total return from income and the appreciation of investments
6. Other resources of Baykeeper
7. The investment policies of Baykeeper
8. The limitation under California state law of appropriations to seven percent of the fair value of the endowment funds.

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Notes to Financial Statements
June 30, 2011

Note 6 – Endowment funds (continued)

In addition, the endowment assets held by the community foundations are subject to the “Spending Rule” of the community foundations.

As of June 30, 2011, endowment funds totaled as follows:

	<u>Unrestricted</u>	Temporarily <u>restricted</u>	Permanently <u>restricted</u>	<u>Totals</u>
Board designated	<u>\$359,566</u>	<u>\$-</u>	<u>\$-</u>	<u>\$359,566</u>
Totals	<u>\$359,566</u>	<u>\$-</u>	<u>\$-</u>	<u>\$359,566</u>

During the year ended June 30, 2011, endowment funds reconciled as follows:

	<u>Unrestricted</u>	Temporarily <u>restricted</u>	Permanently <u>restricted</u>	<u>Totals</u>
Beginning of year	\$310,712	\$-	\$-	\$310,712
Contributions	-	-	-	-
Dividends and interest	3,731	-	-	3,731
Unrealized appreciation (depreciation)	47,544	-	-	47,544
Investment management and administrative fees	(2,421)	-	-	(2,421)
Appropriations for expenditure	-	-	-	-
Board designations (undesignations)	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
End of year	<u>\$359,566</u>	<u>\$-</u>	<u>\$-</u>	<u>\$359,566</u>

As of June 30, 2010, endowment funds totaled as follows:

	<u>Unrestricted</u>	Temporarily <u>restricted</u>	Permanently <u>restricted</u>	<u>Totals</u>
Board designated	<u>\$310,712</u>	<u>\$-</u>	<u>\$-</u>	<u>\$310,712</u>
Totals	<u>\$310,712</u>	<u>\$-</u>	<u>\$-</u>	<u>\$310,712</u>

Baykeeper
Notes to Financial Statements
June 30, 2011

Note 6 – Endowment funds (continued)

During the year ended June 30, 2010, endowment funds reconciled as follows:

	<u>Unrestricted</u>	Temporarily <u>restricted</u>	Permanently <u>restricted</u>	<u>Totals</u>
Beginning of year	\$282,720	\$–	\$–	\$282,720
Contributions	–	–	–	–
Dividends and interest	3,487	–	–	3,487
Unrealized appreciation (depreciation)	26,921	–	–	26,921
Investment management and administrative fees	(2,416)	–	–	(2,416)
Appropriations for expenditure	–	–	–	–
Board designations (undesignations)	<u>–</u>	<u>–</u>	<u>–</u>	<u>–</u>
End of year	<u>\$310,712</u>	<u>\$–</u>	<u>\$–</u>	<u>\$310,712</u>

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 CA-UPMIFA requires Baykeeper to retain as a fund of perpetual duration. In accordance with US-GAAP, Baykeeper records deficiencies of this nature in unrestricted net assets. Deficiencies may result from unfavorable market fluctuations that occur shortly after the investment of new permanently restricted contributions and continued appropriation for certain programs that the Board of Directors deems prudent. There were no such deficiencies as of June 30, 2011 or 2010.

Baykeeper 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 Baykeeper must hold in perpetuity or for donor-specified periods as well as board-designated funds.

Because Baykeeper invests all endowment assets with two community foundations, Baykeeper has adopted the investment policies of the two community foundations. Actual returns in any given year may vary from expected returns under the investment policies of the respective community foundations.

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Notes to Financial Statements
June 30, 2011

Note 6 – Endowment funds (continued)

Because Baykeeper invests all endowment assets with two community foundations, Baykeeper has adopted the spending policies of the two community foundations. This is consistent with the 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.

Unrestricted (board designated) endowment funds are subject to redesignation at any time, including redesignation as other than endowment funds.

Note 7 – Retirement plan

Baykeeper sponsors a defined contribution salary deferral plan under IRC section 401(k) for its eligible employees. Eligible employees may contribute up to 100% of their eligible salary to the plan, subject to limits imposed under the IRC. The plan allows, but does not require, Baykeeper to contribute. During the year ended June 30, 2011 and 2010, Baykeeper contributed to eligible employees, based on 10% of their eligible compensation, totaling \$21,645 and \$25,061, respectively.

Note 8 – Commitments and contingencies

Baykeeper leases office space under an operating lease that expires January 31, 2015. The lease contains an automatic fixed amount escalation clause and option to renew for three years. Future minimum office space lease payments, for each of the years ending June 30, total as follows:

2012	\$58,538
2013	61,246
2014	63,954
2015	38,228

During the years ended June 30, 2011 and 2010, office space rent expense totaled \$54,663 and \$55,500, respectively.

Baykeeper
Notes to Financial Statements
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Note 9 – Changes in accounting principles

During the year ended June 30, 2011, Baykeeper changed its method of accounting for certain Litigation costs other than legal services and applied the change retrospectively. Baykeeper elected to capitalize certain Litigation costs other than legal services rather than expense those costs when incurred. The management of Baykeeper believes that Litigation costs other than legal services are probable of recovery in Settlement or by court ruling and represent an asset of Baykeeper, which will result in future program service revenue. Accordingly, Baykeeper retrospectively adjusted certain amounts previously presented in its financial statements as of and for the year ended June 30, 2010, as follows:

<u>Financial statement component</u>	<u>Herein</u>	<u>Previously</u>	<u>Difference</u>
Asset: Prepaid litigation expenses	\$132,582	\$ –	\$132,582
Net Assets: Unrestricted, undesignated	421,226	288,644	132,582
Change in net assets: Unrestricted	73,006	(59,576)	132,582

The management of Baykeeper determined that retrospective application of this change in accounting principle was impracticable and/or immaterial before July 1, 2009, principally because Settlements received for Litigation costs other than legal services incurred before July 1, 2009 were likely received before June 30, 2010.

During the year ended June 30, 2011, Baykeeper changed its method of accounting for certain Litigation costs of contingent legal services reported as contributed services prior to Settlement and applied the change retrospectively. Baykeeper elected to reclassify contributed legal services as program service revenue and in-kind legal expenses as paid legal expenses upon Settlement when the Settlement covers some or all of the cost of related contingent legal services. The management of Baykeeper believes that this reclassification better reflects the efforts and costs of Litigation and recognizes that legal costs paid with Settlement funds are not contributed or in-kind. Accordingly, Baykeeper retrospectively adjusted certain amounts previously presented in its financial statements as of and for the year ended June 30, 2010, as follows:

<u>Financial statement component</u>	<u>Herein</u>	<u>Previously</u>	<u>Difference</u>
Support: In-kind services	\$884,635	\$1,189,571	(\$304,936)
Revenue: Fee and cost recovery	304,284	(652)	304,936

Baykeeper
Notes to Financial Statements
June 30, 2011

Note 9 – Changes in accounting principles (continued)

The management of Baykeeper determined that retrospective application of this change in accounting principle has no net asset affect. Accordingly, Baykeeper made no retrospective adjustment related to activity before July 1, 2009.