

**ALLIANCE FOR THE CHESAPEAKE
BAY, INC.**

FINANCIAL REPORT

DECEMBER 31, 2010

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INDEPENDENT AUDITOR'S REPORT

Board of Directors
Alliance for the Chesapeake Bay, Inc.
Annapolis, Maryland

We have audited the accompanying statement of financial position of Alliance for the Chesapeake Bay, Inc. (a nonprofit organization) as of December 31, 2010, and the related statements of activities and cash flows for the year then ended. These financial statements are the responsibility of Alliance for the Chesapeake Bay, Inc.'s management. Our responsibility is to express an opinion on these financial statements based on our audit.

Except as discussed in the following paragraph, 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 includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

Due to errors in the posting of payroll and related expenses to the job/grant cost system, an accurate schedule of expenditures of federal awards was not prepared by the Organization. Accordingly, it was not practicable for us to extend our audit of payroll and related expenses beyond the payroll transactions recorded in the schedule and general ledger. In relation to the errors in the posting of payroll and related expenses to the job/grant cost system, the Organization was unable to prepare an accurate accounts receivable and temporarily restricted net assets detail at December 31, 2010. This is due to payroll and related expenses affecting amounts owed by funding agencies to the Organization for reimbursements of such expenses and the determination of temporarily restricted net assets remaining at December 31, 2010.

In our opinion, except for the effects of such adjustments, as might have been determined to be necessary had the payroll transactions referred to in the preceding paragraph been susceptible to satisfactory audit tests, the financial statements referred to in the first paragraph present fairly, in all material respects, the financial position of the Organization as of December 31, 2010, and the changes in its net assets and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The accompanying financial statements have been prepared assuming that the Organization will continue as a going concern. As discussed in Note 13 to the financial statements, the Organization has suffered recurring reductions in unrestricted cash flows and has a net deficiency in unrestricted net assets that raise substantial doubt about its ability to continue as a going concern. Management's plans regarding these matters also are described in Note 13. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

In accordance with *Government Auditing Standards*, we have also issued our report dated September 29, 2011, on our consideration of Alliance for the Chesapeake Bay's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements. The schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations, and is not a required part of the basic financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the basic financial statements as a whole.

Anderson, Davis & Associates, CPA

Glen Burnie, Maryland
September 29, 2011

ALLIANCE FOR THE CHESAPEAKE BAY, INC.
STATEMENT OF FINANCIAL POSITION

December 31, 2010

ASSETS

Current assets	
Cash	\$ 90,115
Contributions receivable	10,000
Grants receivable	189,130
Total current assets	<u>289,245</u>
Equipment	
Office equipment	14,638
Less: accumulated depreciation	<u>(14,638)</u>
	<u>-</u>
Other assets	
Long-term contributions receivable	<u>20,000</u>
	<u>20,000</u>
Total assets	<u>\$ 309,245</u>

LIABILITIES AND NET ASSETS

Current liabilities	
Accounts payable	\$ 185,961
Accrued expenses	72,675
Loans payable	94,674
Total liabilities	<u>353,310</u>
Net assets	
Unrestricted	(358,086)
Temporarily restricted	314,021
	<u>(44,065)</u>
Total liabilities and net assets	<u>\$ 309,245</u>

The notes to the financial statements are an
integral part of these statements.

ALLIANCE FOR THE CHESAPEAKE BAY, INC.**STATEMENT OF ACTIVITIES**

For the year ended December 31, 2010

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Total</u>
Revenues and other support:			
Grants and contracts, government	\$ -	\$ 1,337,618	\$ 1,337,618
Grants and contracts, private	-	351,388	351,388
Public support	140,587	-	140,587
Taste of the Chesapeake	59,645	-	59,645
Interest income	486	-	486
Net assets released from restrictions (Note 9):			
Satisfaction of program restrictions	<u>1,834,662</u>	<u>(1,834,662)</u>	<u>-</u>
Total revenues and other support	<u>2,035,380</u>	<u>(145,656)</u>	<u>1,889,724</u>
Expenses and losses:			
Programs	1,524,812	-	1,524,812
Management and general	451,644	-	451,644
Fundraising	<u>100,090</u>	<u>-</u>	<u>100,090</u>
Total expenses and losses	<u>2,076,546</u>	<u>-</u>	<u>2,076,546</u>
Change in net assets	(41,166)	(145,656)	(186,822)
Net assets, beginning of year	(300,174)	459,677	159,503
Prior period adjustment (Note 12)	<u>(16,746)</u>	<u>-</u>	<u>(16,746)</u>
Restated net assets, beginning of year	<u>(316,920)</u>	<u>459,677</u>	<u>142,757</u>
Net assets, end of year	<u>\$ (358,086)</u>	<u>\$ 314,021</u>	<u>\$ (44,065)</u>

The notes to the financial statements are an integral part of these statements.

ALLIANCE FOR THE CHESAPEAKE BAY, INC.**STATEMENT OF CASH FLOWS**

For the year ended December 31, 2010

Cash flows from operating activities:	
Change in net assets	\$ (186,822)
Adjustments to reconcile change in net assets to net cash used in operating activities:	
Changes in assets and liabilities:	
Decrease (increase) in:	
Grants receivable	(50,773)
Contributions receivable	10,000
Decrease in:	
Accounts payable	(20,500)
Accrued expenses	(2,276)
Net cash used in operating activities	<u>(250,371)</u>
Cash flows from financing activities:	
Repayments of loan payable	(5,979)
Borrowings on loan payable	83,907
Net cash provided by financing activities	<u>77,928</u>
Net decrease in cash	(172,443)
Cash, beginning of year	<u>262,558</u>
Cash, end of year	<u>\$ 90,115</u>
Supplementary Information:	
Interest paid	<u>\$ 11,952</u>
Taxes paid	<u>\$ -</u>

The notes to the financial statements are an
integral part of these statements.

NOTES TO THE FINANCIAL STATEMENTS

Note 1. ORGANIZATION AND PURPOSE

Alliance for the Chesapeake Bay, Inc. (the Organization) was incorporated in Maryland in August 1973 and was formed to serve as a neutral forum where Bay-related issues may be analyzed and considered, for the purpose of providing its membership, responsible officials, and the public with a basis for making informed decisions concerning the management of the resources of the Chesapeake Bay. Alliance for the Chesapeake Bay, Inc. is a nonstock, nonprofit entity.

The Organization's mission statement states: "The Alliance for the Chesapeake Bay, Inc. is a regional nonprofit organization that builds and fosters partnerships to restore the Bay and its rivers. To this end, the Alliance:

- Develops methods and tools for restoration activities and trains citizens to use them.
- Mobilizes decision-makers, stakeholders, and other citizens to learn about Bay issues and participate in resolving them.
- Provides analysis, information, and evaluation of Bay policies, proposals, and institutions.

Founded in 1971, the Alliance for the Chesapeake Bay is funded by individuals, corporations, governments and foundations. The Alliance maintains offices in Annapolis, Maryland; Harrisburg, Pennsylvania; and Richmond, Virginia."

Note 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Significant accounting policies not disclosed elsewhere in the financial statements are as follows:

Basis of Accounting

The Organization maintains its financial records and prepares its financial statements on the accrual basis of accounting. Therefore, revenues and related assets are recognized when earned, and expenses and related liabilities are recognized when the obligations are incurred.

Basis of Presentation

Financial statement presentation follows the recommendations of the Financial Accounting Standards Board in its Accounting Standards Codification. Under these recommendations, the Organization is required to report 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.

NOTES TO THE FINANCIAL STATEMENTS

Note 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Unrestricted net assets – Net assets that are not subject to donor-imposed stipulations and consist of undesignated funds, which are resources available for the support of the Organization’s general operations, and designated funds, or resources designated by the Organization’s Board of Directors for a particular use.

Temporarily restricted net assets – Net assets whose use has been limited by donors to a specific time period and/or purpose. When the donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is met, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of activities as net assets released from restrictions.

Permanently restricted net assets – The principal amounts of gifts which are required by donors to be permanently retained.

The Organization has no permanently restricted net assets.

Cash

The Organization considers all highly liquid investments with a maturity of three months or less when purchased to be cash equivalents.

Income Taxes

The Organization is a nonprofit entity and is exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code. Therefore, contributions to the Organization are tax deductible under Section 170 of the Internal Revenue Code.

Donated Services and Goods

The Organization receives a substantial amount of volunteer service hours, for which it maintains records, but management has elected not to record such hours and related dollar amounts in the financial statements due to the difficulty in quantifying such amounts and not meeting U.S. generally accepted accounting principles criteria for recording. Donated items, such as food or other tangible property, are recorded at fair value when received.

Estimates

The preparation of financial statements in conformity with generally accepted accounting principles accepted in the United States of America requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

NOTES TO THE FINANCIAL STATEMENTS

Note 2. **SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

Grants Receivable

Grants receivable at December 31, 2010 consist mainly of grants and contracts earned, but not yet received. No allowance for uncollectible accounts has been recorded at December 31, 2010, due to any uncollectible amounts deemed to be immaterial.

Allocation of Expenses

The Organization records expenses, both direct and indirect, according to their functional classification as programs, management and general, or fundraising as determined by time recording methods and in accordance with appropriate grants or contracts.

Contributions, Grants, and Support

Contributions and grants received and unconditional promises to give are measured at their fair values and are reported as an increase in net assets. The Organization reports gifts of cash and other assets as restricted support if they are received with donor/grantor stipulations that limit the use of the donated assets, or if they are designated as support for future periods.

When a donor/grantor restriction expires, 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.

The Organization reports gifts of goods and equipment as unrestricted support unless explicit donor/grantor stipulations specify how the donated assets must be used. Gifts of long-lived assets with 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 are reported as restricted support. Absent explicit donor/grantor stipulations about how those long-lived assets must be maintained, the Organization reports expirations of donor/grantor restrictions when the donated or acquired long-lived assets are placed in service.

Subsequent Events

The Organization has evaluated events and transactions for potential recognition or disclosure through September 29, 2011, the date the financial statements were available to be issued.

Note 3. **PROPERTY AND EQUIPMENT**

Property and equipment is stated at cost. The Organization chooses to capitalize fixed asset additions of \$10,000 and greater. Depreciation is provided on the straight-line method over the estimated useful life of the asset. Office equipment is depreciated over a useful life of 5 years. In 2010, there was no depreciation expense recorded as all assets have been fully depreciated.

NOTES TO THE FINANCIAL STATEMENTS

Note 4. RETIREMENT PLAN

The Organization has a 403(b)(7) retirement plan whereby eligible employees can contribute to his or her own custodial account, through salary reduction, with certain limitations, as outlined in the Plan document. The Organization incurred no expense during 2010 related to the Plan.

Note 5. CONTRIBUTIONS RECEIVABLE

As of December 31, 2010, contributions receivable was \$30,000. Management deems this amount fully collectible and therefore has not established an allowance for uncollectible contributions. Contributions are due as follows:

Amounts Due In:	
Less Than One Year	\$ 10,000
One to Five Years	20,000
More Than Five Years	-
Total	<u>\$ 30,000</u>

Note 6. RENTAL COMMITMENTS

The Organization rented office space in Maryland for \$3,975 a month, with an annual increase of 4.5%. This lease expired in November 2010. In October 2010, the Organization entered into a lease agreement to rent office space in Annapolis, Maryland for \$4,883 a month, with an annual increase of 3%. The lease expires December 2015. The Organization rents office space in Pennsylvania for \$1,000 a month. The lease expired May 2010 and was renewed for 2 years with expiration in May 2012. The Organization rents office space in Virginia for \$1,578 a month, with an annual increase of 3.5%. The lease expired October 2010. During 2010, the Organization renewed this lease for an additional three years with lease payments at \$1,530 a month with no annual increase. Total rent expense on these leases for 2010 was \$73,674. Future minimum lease payments are as follows:

2011	\$ 89,991
2012	\$ 84,714
2013	\$ 80,525
2014	\$ 79,329
2015	\$ 65,950

Note 7. OPERATING LEASES

The Organization leases various office equipment for their three office locations, with these leases expiring on various dates through 2013. Total expense for these leases for 2010 was \$9,957. Future minimum lease payments are as follows:

2011	\$ 11,041
2012	\$ 8,853
2013	\$ 2,916

NOTES TO THE FINANCIAL STATEMENTS

Note 8. TEMPORARILY RESTRICTED NET ASSETS

Temporarily restricted net assets are available for the following purposes:

Various federal, state, and private agency programs	<u>\$ 314,021</u>
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Note 9. NET ASSETS RELEASED FROM RESTRICTIONS

Net assets were released from donor/grantor restrictions by incurring expenses satisfying the restricted purposes or by occurrence of other events specified by donors/grantors.

Purpose restrictions accomplished:

Various expenses related to performance of federal, state, and private agency programs	<u>\$ 1,834,662</u>
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Note 10. CONCENTRATION OF REVENUES

During the year ended December 31, 2010, the Organization recognized revenues from United States Environmental Protection Agency of approximately \$893,000 for program services performed. This represents 47% of all revenues recognized by the Organization as a whole in 2010.

Note 11. LOAN PAYABLE

The Organization has a line of credit agreement with a bank for an amount up to \$115,000. This line of credit is renewable each year by verbal agreement. At December 31, 2010, the unpaid balance on this line of credit was \$94,674. The line of credit is secured by all personal property of the Organization and is payable on demand. Interest is due monthly at prime plus one percent. The interest rate as of December 31, 2010 was 5.25%. Total interest expense for the year ended December 31, 2010 was \$11,952.

Note 12. PRIOR PERIOD ADJUSTMENT

Net assets at December 31, 2009 have been adjusted to reflect the addition of a line of credit payable of \$16,746. This was discovered during 2011 by management.

Note 13. GOING CONCERN

For the year ending December 31, 2010, the Organization has a cumulative unrestricted net asset deficit and lack of sufficient unrestricted cash. Currently, the Organization does not have any assets held for sale or immediate unrestricted donations that would provide unrestricted cash. The Organization renewed its line of credit available up to \$115,000. There is substantial doubt about the ability of the Organization to continue as a going concern.

NOTES TO THE FINANCIAL STATEMENTS

Note 13. **GOING CONCERN (continued)**

The possible effects of these conditions are discontinuance of operations, default on the bank line of credit, possible lack of repayment of advanced restricted monies and default on completing contracts in progress funded by federal and state agencies and private corporations and donors.

Management's Response and Plans:

The Alliance's Board of Directors and its management recognize the need to better control costs and increase unrestricted revenues. The Alliance has taken numerous steps to institute and monitor new procedures and tools that will ensure accurate and timely review of costs and revenues. In addition, we have new development and membership initiatives aimed at diversification of financial resources and a refocusing of strategic program direction. Our financial initiatives include the specific steps outlined below:

A new Executive Director has been hired. This Executive Director has outstanding management skills and a hands-on management style which will be imperative in gaining effective financial control. In addition, he has a long and successful track record in work directly aligned with the Alliance mission, is highly respected in the field, and has many strong relationships with contacts in the Chesapeake Bay restoration community which will be very valuable for the fundraising activities of the organization.

The Alliance has hired a new Finance Director who brings 15 years of solid hands-on experience in nonprofit financial management. The new Finance Director has a demonstrated track record in turning around a multi-million dollar nonprofit from a major negative unrestricted net asset balance to a major positive unrestricted net balance.

The Alliance has replaced its the antiquated ACCPAC accounting software with a comprehensive but user-friendly package, Peachtree Complete Accounting. This new software will improve accuracy and timeliness of financial reporting. Financial staff are trained and proficient in the use of this software and have transferred existing data into the new system.

The Board of Directors recognizes how essential it is to have a disciplined approach to rebuilding unrestricted net assets. Therefore, at the first 2011 meeting, the Board approved a net surplus operating budget, the intention for the difference to be purposefully identified as restoring net assets.

The new Executive Director and Finance Director have initiated weekly financial reviews of cash position, accounts payable, accounts receivable and other critical financial issues. Additionally, a standing monthly financial meeting has been established to review the income statement, balance sheet, unrestricted net assets and grant accounting, among other critical financial issues.

NOTES TO THE FINANCIAL STATEMENTS

Note 13. GOING CONCERN (continued)

Management's Response and Plans (continued):

The Alliance's Board elected a new member who is a CPA and professionally employed as CFO of a non-profit organization. She serves as Chair of the Board's Finance Committee. This brings knowledge and skills that will assist the Alliance Board, Executive Director, and Finance Director and ensure closer professional oversight of the organization's overall financial operations. This Board Member will participate in monthly financial meetings.

The Alliance's annual fundraising event occurred in September 2011. Sponsorship funding for this event is currently being received. A second major fundraising event is being planned for the Spring of 2012.

The Alliance Board's Development Committee and new Executive Director are in the process of completing a new development initiative. The Development Committee will be expanding outreach to the corporate community, foundations, and individuals for the purpose of obtaining critical unrestricted fund donations. The Organization has engaged a fund raising consultant who is helping to prepare for a major gift campaign – "Campaign for the Bay" which will be rolled out in 2011. In addition to seeking gifts from existing and new donors, a renewed membership campaign, and a Business for the Bay Program initiative are being designed for 2012 will expand and diversify the Alliance funding base.

The Alliance's line of credit through a bank in the amount of \$115,000 was renewed and this line will continue to help better manage cash flow and aged payables.

The Alliance has consolidated the Finance Department from three individuals to two, both with technical skills and personal commitment to the Alliance mission. The impact of this is an estimated \$54,000 per year savings.

The new Finance Director has implemented tighter and more timely grant reports to eliminate the possibility of overspending on individual grants. The Alliance Program Director has been assigned to assist the Finance Director in working with staff to ensure that grant files are accurate and up to date.

SUPPLEMENTARY INFORMATION

ALLIANCE FOR THE CHESAPEAKE BAY, INC.
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

For the year ended December 31, 2010

<i>Federal Direct Grantor/Pass-Through Grantor</i>	<i>Program or Cluster Title</i>
U.S. Environmental Protection Agency (EPA):	
Region III	Circuit Rider
Region III	Local Government Advisory Committee Coordination
Region III	Chesapeake Bay Program
Region III	Chesapeake Bay Program
Region III	Chesapeake Bay Program Support
Region III	Chesapeake Bay Program Support
DC Department of the Environment	ARRA - Riversmart Homes Grant
U.S. Department of Agriculture and :	
National Fish & Wildlife Foundation	Chesapeake Online Network
National Fish & Wildlife Foundation	Spatial Land Registry
National Fish & Wildlife Foundation	Cedar Run
National Fish & Wildlife Foundation	Chesapeake Network
National Fish & Wildlife Foundation	Reedy Creek Stewardship
National Fish & Wildlife Foundation	Urban Tree Canopy
National Fish & Wildlife Foundation	Fish Survey Interns
National Fish & Wildlife Foundation	Watershed Forum
National Fish & Wildlife Foundation	Greening of Virginia
Forestry Service	Year of the Forest Outreach
Forestry Service	Forestry for the Bay - Phase V
Forestry Service	Forestry for the Bay - Phase VI

Total Expenditures of Federal Awards

NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

Note 1. Basis of Presentation

The accompanying schedule of expenditures of federal awards (the Schedule) includes the federal grant activity of Alliance for the Chesapeake Bay, Inc. (the Organization) under programs of the federal government for the year ended December 31, 2010. The information in this schedule is presented in accordance with the requirements of *OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations*. Because the Schedule presents only a selected portion of the operations of the Organization, it is not intended to and does not present the statement of financial position, changes in net assets, or cash flows of the Organization.

Note 2. Summary of Significant Accounting Policies

A. Expenditures reported on the Schedule are reported on the accrual basis of accounting. Such expenditures are recognized following the cost principles contained in *OMB Circular A-122, Cost Principles of Non-Profit Organizations*, wherein certain types of expenditures are not allowable or are limited as to reimbursement.

B. Pass-through entity identifying numbers are presented where available.

<i>Federal CFDA Number</i>	<i>Pass-Through Entity Number/ Identifying Grant Number</i>	<i>Federal Expenditures</i>
66.466	CB97375801-0	\$ 89,634
66.466	CB97375701-0	129,468
66.466	CB97383601-0	25,278
66.466	CB97383602	27,252
66.466	CB97324705-0	33,683
66.466	CB97391901	344,615
66.466	09-08-MS4-WPD04	386,358
		<u>1,036,288</u>
10.678	2010-0912-002	9,000
10.678	2007-0081-012	15,243
10.678	2009-0054-026	32,221
10.678	2008-0901-001	44,301
10.678	2009-0055-020	51,988
10.678	2008-0059-0027	18,827
10.678	51410-A-J034	12,768
10.678	2010-0912-002	65,000
10.678	1544-PO-2	17,740
10.678	10-DG-11420004-328	415
10.678	06-DG-11244225-099	42,030
10.678	06-DG-099	55,289
		<u>364,822</u>
		<u>\$ 1,401,110</u>

The accompanying notes are an integral part of this schedule.



**REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE
AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED
IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS**

Board of Directors
Alliance for the Chesapeake Bay, Inc.
Annapolis, Maryland

We have audited the financial statements of Alliance for the Chesapeake Bay, Inc. as of and for the year ended December 31, 2010 and have issued our report thereon dated September 29, 2011. Our report on the financial statements includes an explanatory paragraph describing conditions, discussed in Note 13 to the financial statements that raise substantial doubt about the Organization's ability to continue as a going concern. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Alliance for the Chesapeake Bay, Inc.'s internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Alliance for the Chesapeake Bay, Inc.'s internal control over financial reporting. Accordingly, we do not express an opinion of the effectiveness of Alliance for the Chesapeake Bay, Inc.'s internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purposed described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses, and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as discussed in the accompanying schedule of findings and questioned costs, we identified certain deficiencies in internal control over financial reporting that we consider to be material weaknesses.

Internal Control Over Financial Reporting (continued)

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiencies, described as items 10-1, 08-1 and 07-1, in the accompanying schedule of findings and questioned costs to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Alliance for the Chesapeake Bay's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed an instance of noncompliance or other matters that are required to be reported under Government Auditing Standards and which are described in the accompanying schedule of findings and questioned costs as item 10-1

We noted certain matters that we reported to management of Alliance for the Chesapeake Bay, Inc. in a separate letter dated September 29, 2011.

Alliance for the Chesapeake Bay, Inc.'s response to the findings identified in our audit is described in the accompanying schedule of findings and questioned costs. We did not audit Alliance for the Chesapeake Bay, Inc.'s response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of the Finance Committee, Board of Directors, management and federal awarding agencies and pass-through entities and is not intended to be, and should not be used by anyone other than these specified parties.

Anderson, Davis & Associates, CPA

Glen Burnie, Maryland

September 29, 2011



**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE WITH REQUIREMENTS THAT
COULD HAVE A DIRECT AND MATERIAL EFFECT ON EACH MAJOR PROGRAM AND ON
INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH
OMB CIRCULAR A-133**

Board of Directors
Alliance for the Chesapeake Bay, Inc.
Annapolis, Maryland

Compliance

We have audited the compliance of Alliance for the Chesapeake Bay, Inc. with the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended December 31, 2010. Alliance for the Chesapeake Bay, Inc.'s major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of Alliance for the Chesapeake Bay, Inc.'s management. Our responsibility is to express an opinion on Alliance for the Chesapeake Bay, Inc.'s compliance based on our audit.

Except as discussed in the following paragraph, we conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about Alliance for the Chesapeake Bay, Inc.'s compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of Alliance for the Chesapeake Bay, Inc.'s compliance with those requirements.

As described in item 10-1 in the accompanying schedule of findings and questioned costs, we were unable to obtain sufficient documentation supporting the compliance of Alliance for the Chesapeake Bay, Inc. with the U.S. Environmental Protection Agency Region III funding regarding Activities Allowed or Unallowed, Allowable Costs/Cost Principles, Cash Management and Reporting. Nor were we able to satisfy ourselves as to Alliance for the Chesapeake Bay's compliance with those requirements by other auditing procedures.

In our opinion, except for the effects of such noncompliance, if any, as might have been determined had we been able to examine sufficient evidence regarding Alliance for the Chesapeake Bay's compliance with the requirements of U.S. Environmental Protection Agency Region III funding regarding Activities Allowed or Unallowed, Allowable Costs/Cost Principles and Cash Management,

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Compliance (continued)

Alliance for the Chesapeake Bay complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended December 31, 2010.

Internal Control Over Compliance

Management of Alliance for the Chesapeake Bay, Inc. is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered Alliance for the Chesapeake Bay, Inc.'s internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of Alliance for the Chesapeake Bay, Inc.'s internal control over compliance.

Our consideration of internal control over compliance was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be significant deficiencies or material weakness in internal control over compliance and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as discussed below, we identified certain deficiencies in internal control over compliance that we consider to be material weaknesses.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. *A significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance. *A material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. We consider the deficiencies in internal control over compliance, described as items 10-1, 08-1 and 07-1, in the accompanying schedule of findings and questioned costs to be material weaknesses.

Alliance for the Chesapeake Bay, Inc.'s response to the findings identified in our audit are described in the accompanying schedule of findings and questioned costs. We did not audit Alliance for the Chesapeake Bay, Inc.'s response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of the Finance Committee, Board of Directors, management and federal awarding agencies and pass-through entities and is not intended to be, and should not be, used by anyone other than these specified parties.

Anderson, Davis & Associates, CPA

Glen Burnie, Maryland
September 29, 2011

Alliance for the Chesapeake Bay, Inc.
Summary Schedule of Prior Audit Findings
Year Ended December 31, 2010

Finding 07-1 from fiscal year 2008: Temporarily restricted net assets were not reconciled to the restricted funds job/grant cost system. (Questioned costs - N/A)

Current Status: Financial statement finding 07-01 remains as a current year finding.

Finding 08-1 from fiscal year 2008: The Organization did not effectively implement internal control procedures to review payroll entries, input and allocations in the restricted funds job/grant cost system. (Questioned costs – N/A).

Current Status: Financial statement finding 08-01 remains as a current year finding.

Alliance for the Chesapeake Bay, Inc.
Schedule of Findings and Questioned Costs
 Year Ended December 31, 2010

Section I - Summary of Auditor's Results

Financial Statements

Type of auditor's report issued: Qualified

Internal control over financial reporting:

Material weaknesses identified? yes no

Significant deficiency identified not considered to be material weakness? yes none reported

Noncompliance material to financial statements noted? yes no

Federal Awards

Internal control over major programs:

Material weaknesses identified? yes no

Significant deficiency identified that is not considered to be material weakness? yes none reported

Type of auditor's report issued on compliance for major programs: Qualified

Any audit findings disclosed that are required to be reported in accordance with Circular A-133, Section 510(a)? yes no

Identification of major programs:

<u>CFDA Number</u>	<u>Name of Federal Program or Cluster</u>
66.466	U.S. Environmental Protection Agency, Region III and ARRA passed through from District of Columbia Department of the Environment

Dollar threshold used to distinguish between Type A and Type B Programs: \$300,000

Auditee qualified as low-risk auditee? yes no

Alliance for the Chesapeake Bay, Inc.
Schedule of Findings and Questioned Costs (continued)
Year Ended December 31, 2010

Section II - Financial Statement Findings

Finding 07-1 (Organization-wide):

Criteria - In order to maintain effective internal controls, there must be timely and accurate reconciliation of temporarily restricted net assets to the restricted funds job/grant cost system.

Condition –Temporarily restricted net assets were not reconciled to the restricted funds job/grant cost system.

Questioned costs - No dollar amount can be determined due to no specific instances of material noncompliance found.

Context - Even though this condition exists, no material quantifiable issues of noncompliance found.

Cause - The Organization is a small non-profit with a limited number of employees in the accounting function and thus, such employees have minimal time to perform account reconciliations after fulfilling and performing daily duties.

Effect - Discovery of errors or fraud could go undetected with the lack of timely and accurate reconciliation of temporarily restricted net assets to the restricted funds job/grant cost system and thus internal financial statements could be misstated.

Recommendation - The Organization should perform accurate and timely reconciliations of temporarily restricted net assets to the restricted funds job/grant cost system on an ongoing basis and at least monthly.

Management's Response – For 2011, the Alliance's new Finance Director has replaced the antiquated ACCPAC accounting software with a new and proven software package, Peachtree Complete Accounting. This new software will substantially improve accurate and timely financial reporting. This allows for timely reconciliation of temporarily restricted net assets and a timely and ongoing review of grant expenses. Weekly financial review is being conducted by the Finance Director and Executive Director starting September 2011.

Alliance for the Chesapeake Bay, Inc.
Schedule of Findings and Questioned Costs (continued)
Year Ended December 31, 2010

Section II - Financial Statement Findings

Finding 08-1 (Organization-wide):

Criteria – Internal grant control procedures to review payroll entries, input and allocations in the restricted funds job/grant cost system need to be implemented.

Condition – The Organization did not effectively implement internal control procedures to review payroll entries, input and allocations in the restricted funds job/grant cost system.

Questioned costs – Net immaterial dollar affect, thus no questioned costs reported.

Context - Even though this condition exists, no material quantifiable issues of noncompliance found.

Cause – There is a lack of adequate internal control procedures to review payroll entries, input and allocations in the restricted funds job/grant cost system.

Effect – Certain payroll entries, input and allocations were not recorded correctly in the restricted funds job/grant cost system.

Recommendation – Management should implement supervisory payroll review procedures.

Management's Response – During 2011, the Alliance has hired a new Finance Director who brings 15 years of solid hands-on experience in nonprofit financial management. The Finance Director has streamlined payroll processing and time allocation posting and has implemented payroll review procedures.

Finding 10-1 (Organization-wide):

Criteria – Payroll entries need to be recorded in the job/grant cost system to produce an accurate schedule of expenditures of federal awards and should be reconciled to the general ledger. Accounts receivable detail for reimbursement of payroll and related expenditures must be maintained and reconciled to the general ledger in order to properly record federal funds activity.

Condition – The Organization did not properly record payroll entries into the job/grant cost systems. Certain entries were double counted and some were not recorded during the fiscal year. Job/grant cost system and schedule of federal awards were not reconciled to the general ledger.

Questioned costs – Dollar effect not quantifiable, thus no questioned costs reported.

Context – This finding appears to be systematic as all payroll transactions are to be recorded in the job/grant cost system and submitted for reimbursement. Even though the condition exists, the issues of noncompliance are not quantifiable. During 2010, the prior Finance Director did not initially understand the posting process from the ACCPAC subledger to job/grant cost system. However, after the errors were noted at the beginning of the 2010 audit, the Organization’s new Finance Director reconstructed each pay period for 2010 by re-entering this information in the software. Management of the Organization believes payroll transactions were corrected and recorded in a complete and accurate manner as reflected in these financial statements.

Cause – There is a lack of adequate internal control procedures to review payroll entries, input and allocations in the restricted funds job/grant cost system. The job/grant cost system was not reconciled to the general ledger during the fiscal year 2010.

Effect – Certain payroll entries, input and allocations were not recorded correctly in the restricted funds job/grant cost system, thus an accurate schedule of federal awards could not be produced.

Recommendation – Management should implement supervisory payroll review procedures and reconcile job/grant cost system to general ledger at least monthly.

Management’s Response – In the new accounting software that was implemented in January 2011, job/grant reporting is integrated with the general ledger. The new Finance Director has implemented procedures to cross check each payroll allocation on a monthly basis. This will insure accuracy moving forward.

Section III - Federal Award Findings and Questioned Costs

Finding 07-1 (Organization-wide):

Summary identification of finding – Timely and accurate reconciliation of temporarily restricted net assets to the restricted funds job/grant cost system was not performed. (See Finding 07-1 in Section II of the Schedule of Findings and Questioned Costs.)

Finding 08-1 (Organization-wide):

Summary identification of finding – The Organization did not effectively implement internal control procedures to review payroll entries, input and allocations in the restricted funds job/grant cost system. (See Finding 08-1 in Section II of the Schedule of Findings and Questioned Costs.)

Finding 10-1 (Organization-wide):

Summary identification of finding – The Organization did not accurately record payroll transactions in the job/grant cost system and did not create an accurate schedule of federal awards or accounts receivable detail during 2010. The Organization did not reconcile the job/grant cost system or schedule of federal awards to the general ledger. (See Finding 10-1 in Section II of the Schedule of Findings and Questioned Costs.)



Organization: Alliance for the Chesapeake Bay
Audit Firm: Anderson, Davis & Associates CPA, PA
Audit Period: 1/1/2010 to 12/31/2010

Corrective Action Plan

A. Comments on Findings 07-1, 08-1 and 10-1

The Alliance agrees with the findings and recommendations of the auditor.

B. Actions Taken or Planned

Finding 07-1 - Summary identification of finding – Timely and accurate reconciliation of temporarily restricted net assets to the restricted funds job/grant cost system was not performed.

For 2011, the Alliance's new Finance Director has replaced the antiquated ACCPAC accounting software with a new and proven software package, Peachtree Complete Accounting. This new software will substantially improve accurate and timely financial reporting. This allows for timely reconciliation of temporarily restricted net assets and a timely and ongoing review of grant expenses. Weekly financial review is being conducted by the Finance Director and Executive Director starting September 2011.

Finding 08-1 - Summary identification of finding – The Organization did not effectively implement internal control procedures to review payroll entries, input and allocations in the restricted funds job/grant cost system.

During 2011, the Alliance has hired a new Finance Director who brings 15 years of solid hands-on experience in nonprofit financial management. The Finance Director has streamlined payroll processing and time allocation posting and has implemented payroll review procedures. All payrolls and payroll postings are being reviewed and signed off on during monthly financial meetings. Although payroll entries as of 12/31/2010 were not entered correctly the Alliance did manually review and correct all payroll entries during 2011. This situation resulted in the first place because the Alliance staff did not fully understand the posting process in the ACCPAC sub ledger to the job cost system.

Finding 10-1 - Summary identification of finding – The Organization did not accurately record payroll transactions in the job/grant cost system and did not create an accurate schedule of federal awards or accounts receivable detail during 2010. The Organization did not reconcile the job/grant cost system or schedule of federal awards to the general ledger.

In the new accounting software that was implemented in January 2011, job/grant reporting is integrated with the general ledger. The new Finance Director has implemented procedures to cross check each payroll allocation on a monthly basis. This will insure accuracy moving forward. Although payroll entries as of 12/31/2010 were not entered correctly the Alliance did manually review and correct all payroll entries during 2011. This situation resulted in the first place because the Alliance staff did not fully understand the posting process in the ACCPAC sub ledger to the job cost system.

Sincerely,



Al Todd
Executive Director

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