

U. S. ENDOWMENT
FOR FORESTRY AND
COMMUNITIES, INC. AND SUBSIDIARY

Consolidated Financial Statements

December 31, 2011 and 2010

(with Independent Auditors'
Report thereon)

**U. S. ENDOWMENT FOR FORESTRY
AND COMMUNITIES, INC. AND SUBSIDIARY**

December 31, 2011 and 2010
Table of Contents

	Page(s)
Independent Auditors' Report.....	1
Consolidated Statements of Financial Position.....	2
Consolidated Statements of Activities	3
Consolidated Statements of Cash Flows	4
Notes to the Consolidated Financial Statements.....	5 – 20
Consolidated Schedules of Functional Expenses.....	21
Independent Auditors' Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Consolidated Financial Statements Performed in Accordance with <i>Government Auditing Standards</i>	22
Independent Auditors' Report on Compliance with Requirements Applicable to Each Major Federal Program and Internal Control Over Compliance in Accordance with OMB Circular A-133.....	23 – 24
Schedule of Expenditures of Federal Awards.....	25
Schedule of Findings and Questioned Costs.....	26 – 29
Corrective Action Plan.....	30
Summary Schedule of Prior Audit Findings	31



DIXON HUGHES GOODMAN LLP
Certified Public Accountants and Advisors

Independent Auditors' Report

The Board of Directors
U.S. Endowment for Forestry and Communities, Inc. and Subsidiary
Greenville, South Carolina

We have audited the accompanying consolidated statements of financial position of U.S. Endowment for Forestry and Communities, Inc. (the "Endowment") and Community Wealth through Forestry, Inc. (the "Subsidiary") as of December 31, 2011 and 2010, and the related consolidated statements of activities and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Endowment's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of US Endowment for Forestry and Communities, Inc. and Subsidiary as of December 31, 2011 and 2010, and the changes in its net assets and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with Government Auditing Standards, we have also issued our report dated September 21, 2012 on our consideration of the Endowment's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be considered in assessing the results of our audit.

Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements taken as a whole. The Consolidated Schedules of Functional Expenses, as well as the accompanying Schedule of Expenditures of Federal Awards as required by the U.S. Office of Management and Budget Circular A-133, Audits of States, Local Governments and Non-Profit Organizations are presented for purposes of additional analysis and are not a required part of the consolidated 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 consolidated financial statements. The information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated 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 consolidated financial statements as a whole.

September 21, 2012

Dixon Hughes Goodman LLP

U. S. ENDOWMENT FOR FORESTRY AND COMMUNITIES, INC. AND SUBSIDIARY
Consolidated Statements of Financial Position
December 31, 2011 and 2010

	<u>2011</u>	<u>2010</u>
<u>Assets</u>		
Cash and cash equivalents	\$ 1,540,737	\$ 808,031
Grants receivable	342,954	602,651
Other receivables	35,327	11,451
Due from investment broker	2,000,000	2,743,662
Prepaid expenses	13,961	8,604
Notes receivable, net of allowance for doubtful accounts of approximately \$402,000 and \$345,000	2,214,250	645,500
Investments	173,738,902	188,297,117
Investment in North Star Jefferson, LLC	138,066	-
Property and equipment, net	<u>452,442</u>	<u>198,862</u>
 Total assets	 <u>\$ 180,476,639</u>	 <u>\$ 193,315,878</u>
<u>Liabilities and Net Assets</u>		
Accounts payable and other accruals	\$ 1,166,332	\$ 733,468
Deferred revenue	1,169,794	948,247
Notes payable	337,085	-
Total liabilities	<u>2,673,211</u>	<u>1,681,715</u>
Net assets:		
Unrestricted	(22,260,077)	(8,575,764)
Temporarily restricted	63,505	209,927
Permanently restricted	<u>200,000,000</u>	<u>200,000,000</u>
Total net assets	<u>177,803,428</u>	<u>191,634,163</u>
 Total liabilities and net assets	 <u>\$ 180,476,639</u>	 <u>\$ 193,315,878</u>

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

U. S. ENDOWMENT FOR FORESTRY AND COMMUNITIES, INC. AND SUBSIDIARY

Consolidated Statements of Activities

For the Years Ended December 31, 2011 and 2010

	<u>2011</u>	<u>2010</u>
Unrestricted support, revenues and gains (losses):		
Interest and dividend income, net of investment fees	\$ 2,749,485	\$ 2,415,347
Net realized and unrealized gains (losses) on investments	(13,284,804)	14,104,444
Equity interest in loss of North Star Jefferson, LLC	(90,002)	-
Federal support	2,806,286	1,841,466
Nonfederal support	209,960	154,047
Net assets released from restrictions	266,422	837,476
Total support, revenues and gains (losses)	<u>(7,342,653)</u>	<u>19,352,780</u>
Expenses:		
Program	5,902,905	6,092,326
Management and general	438,755	454,181
Total expenses	<u>6,341,660</u>	<u>6,546,507</u>
Increase (decrease) in unrestricted net assets	<u>(13,684,313)</u>	<u>12,806,273</u>
Temporarily restricted support and revenue:		
Nonfederal support	120,000	558,453
Releases from restriction	(266,422)	(837,476)
Decrease in temporarily restricted net assets	<u>(146,422)</u>	<u>(279,023)</u>
Total increase (decrease) in net assets	(13,830,735)	12,527,250
Net assets at beginning of year	<u>191,634,163</u>	<u>179,106,913</u>
Net assets at end of year	\$ <u><u>177,803,428</u></u>	\$ <u><u>191,634,163</u></u>

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

U. S. ENDOWMENT FOR FORESTRY AND COMMUNITIES, INC. AND SUBSIDIARY

Consolidated Statements of Cash Flows
For the Years Ended December 31, 2011 and 2010

	<u>2011</u>	<u>2010</u>
Cash flows from operating activities:		
Increase (decrease) in net assets	\$ (13,830,735)	\$ 12,527,250
Adjustments to reconcile increase (decrease) in net assets to net cash used in operating activities:		
Net realized and unrealized (gains) losses on investments	13,284,804	(14,104,444)
Equity interest in loss of North Star Jefferson, LLC	90,002	-
Depreciation	9,453	-
Loss on disposal of fixed asset	-	14,101
Net changes in operating assets and liabilities:		
Grants receivables	259,697	(387,728)
Other receivable	(23,876)	(11,451)
Notes receivable	(1,568,750)	(645,500)
Due from investment broker	743,662	(2,743,662)
Prepaid expenses	(5,357)	531
Accounts payable and other accruals	432,864	601,796
Deferred revenue	221,547	(34,283)
Net cash used in operating activities	<u>(386,689)</u>	<u>(4,783,390)</u>
Cash flows from investing activities:		
Sales of investments	143,488,255	104,222,380
Purchases of investments	(142,214,844)	(99,122,349)
Investment in North Star Jefferson, LLC	(228,068)	-
Purchases of property and equipment	<u>(263,033)</u>	<u>(198,862)</u>
Net cash provided by investing activities	<u>782,310</u>	<u>4,901,169</u>
Cash flows from financing activities:		
Proceeds from note payable	<u>337,085</u>	<u>-</u>
Net cash provided by financing activities	<u>337,085</u>	<u>-</u>
Net increase in cash	732,706	117,779
Cash and cash equivalents at beginning of year	<u>808,031</u>	<u>690,252</u>
Cash and cash equivalents at end of year	<u>\$ 1,540,737</u>	<u>\$ 808,031</u>

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

**U.S. ENDOWMENT FOR FORESTRY AND
COMMUNITIES, INC. AND SUBSIDIARY**

Notes to the Consolidated Financial Statements

December 31, 2011 and 2010

1. **Summary of Significant Accounting Policies**

Organization - The U.S. Endowment for Forestry and Communities, Inc. (the “Endowment”) is a not-for-profit organization incorporated and established in 2006 at the request of the governments of the United States and Canada in accordance with the terms of the Softwood Lumber Agreement (“SLA”) between the two countries. The Endowment is one of three entities designated to share in a one-time infusion of funds to support “meritorious initiatives” in the United States. It was endowed with \$200 million under the terms of the SLA. The Endowment has been chartered with two purposes: 1) educational and charitable causes in timber-reliant communities; and 2) educational and public-interest projects addressing forest management issues that affect timber-reliant communities, or the sustainability of forests as sources of building materials, wildlife habitat, bio-energy, recreation and other values.

During 2011, the Endowment formed a wholly owned subsidiary, Community Wealth Through Forestry, Inc (“CWF”). The purpose of CWF is to support sustainable green energy development that captures and distributes benefits to rural forest-reliant communities. CWF became operational in November 2011 and its activity has been consolidated in the financial statements for the year ended December 31, 2011.

Principles of Consolidation - The consolidated financial statements include the accounts of the Endowment and the Subsidiary. All material intercompany accounts and transactions have been eliminated in consolidation.

Use of Estimates - The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements. Estimates could also affect the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash and Cash Equivalents - For the purpose of the consolidated statements of cash flows, the Endowment considers unrestricted highly liquid investments with a remaining maturity of three months or less when purchased to be cash equivalents.

At times throughout the year, the Endowment may temporarily maintain cash balances at financial institutions in excess of FDIC insured limits. Management attempts to minimize this exposure by minimizing un-invested cash balances and monitoring the strength of the financial institutions with which it has accounts.

Grants Receivable - Grants receivable consist of unsecured balances due from grantor agencies for reimbursement of allowable grant expenditures and do not bear interest.

Notes Receivable - The Endowment's notes receivable are due primarily from for-profit organizations that are working on various projects related to the Endowment's purpose and are recorded at estimated net realizable value. Credit is extended to the for-profit organizations and collateral is not required. Notes are due between fiscal years of 2013 to 2017, and accrued interest is deferred for the first three years of the note and then due semi-annually. Interest rates on the notes vary from 3% to 8% per annum simple interest. Management reviews the receivables periodically and provides an allowance for uncollectible accounts at a level which, in management's judgment, is adequate to absorb potential losses inherent in uncollectible notes receivables.

Investments - The Endowment's investments are recorded at fair value.

The Endowment has estimated the fair value of certain investments in investment companies for which the investment does not have a readily determinable fair value using the investment's net asset value per share or its equivalent, such as partners' capital per share, without adjustment. The total fair value of these investments estimated based on the investment's net asset value per share is \$169,936,298 and \$187,625,974 at December 31, 2011 and 2010, respectively. Also included in investments are money market funds valued at \$3,802,604 and \$671,143 at December 31, 2011 and 2010.

Investments in common trust or commingled funds valued at \$120,871,119 and \$149,542,471 at December 31, 2011 and 2010, respectively, do not have quoted market prices. The fair value of such investments is based upon the net asset value of the respective funds, which are based upon the estimated fair values of the underlying investments. The fair values of the underlying investments are based upon quoted market prices, where applicable, or upon estimated fair values determined by the respective fund managers and are subject to review by the Endowment and independent annual financial statement audits.

The financial statements also include investments in hedge funds, venture capital funds, international and domestic private equity funds, distressed debt funds and real estate funds valued at \$49,065,179 and \$38,083,503 at December 31, 2011 and 2010, respectively. The fair values of these funds have been estimated by management at net asset value (or its equivalent) in the absence of readily determinable fair values. The recorded market price for such investments is estimated by the individual investment manager of the funds taking into account such factors as the financial condition of each investee, economic and market conditions affecting their operations, any changes in management, the length of time since the initial investment, recent arm's-length transactions involving the securities of the investee, the value of similar securities issued by companies in the same or similar businesses, and limited marketability of the portfolio. The fair value in such investments is subject to review by the Endowment and independent annual financial statement audits.

Investment securities are exposed to several risks, such as changes in interest rates, market fluctuations, and credit risks. Due to the risks associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and such changes could materially affect the amounts reported in the Endowment's consolidated financial statements.

Due from Investment Broker - Amounts due from broker consists of funds that were not settled as a result of investment sales at December 31; these funds were awaiting transfer to the Endowment's investment cash account.

Property and Equipment - Property and equipment are reported at cost, if purchased, or fair value at the date of donation. The Endowment's policy is to capitalize property and equipment with value greater than \$2,500. Depreciation is computed on a straight-line basis over the estimated useful life of the assets. Depreciation expense was \$9,453 and \$-0- for the years ended December 31, 2011 and 2010, respectively.

Deferred Revenue - Certain grants received by the Endowment and paid in advance are deferred until the sub-recipient of the grant submits a reimbursement request which includes documentation of actual expenditures incurred under the grant.

Net Assets - Net assets and revenues, expenses, gains, and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, net assets of the Endowment and changes therein are classified and reported as follows:

Unrestricted - Net assets that are not subject to donor-imposed restrictions. Unrestricted net assets may be designated for specific purposes by the Endowment or may otherwise be limited by contractual agreements with outside parties.

Temporarily Restricted - Net assets whose use by the Endowment is subject to donor-imposed stipulations that can be fulfilled by actions of the Endowment pursuant to those stipulations or that expire by the passage of time.

Permanently Restricted - Net assets subject to donor-imposed stipulations that they be maintained in perpetuity by the Endowment.

Restricted and Unrestricted Revenue and Support - Contributions received are recorded as unrestricted, temporarily restricted, or permanently restricted support, depending on the existence and/or nature of any donor restrictions.

Support that is restricted by the donor is reported as an increase in unrestricted net assets if the restriction expires in the reporting period in which the support is recognized. All other donor-restricted support is reported as an increase in temporarily or permanently restricted net assets, depending on the nature of the restriction. When a 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 Consolidated Statement of Activities as net assets released from restrictions.

In-Kind Contributions - The Endowment records in-kind contributions at their fair value at the date of the contribution.

Functional Expenses - The cost of providing various programs and supporting services has been reported on a functional basis in the statements of activities. Accordingly, certain costs

have been allocated to the program initiatives and supporting services based on estimates made by management.

Fair Value of Financial Instruments - The fair value of the financial instruments of the Endowment are set forth as follows:

Cash and cash equivalents, receivables, due from broker, prepaid expenses, accounts payable and other accruals - The carrying amounts approximate fair value due to the immediate or short-term maturity of these instruments.

Notes receivable - Notes receivable are recorded at carrying amount of approximately \$2,214,000 and \$645,000 for the years ended December 31, 2011 and 2010. The fair value of notes receivable is estimated to be approximately \$1,900,000 and \$540,000 for the years ended December 31, 2011 and 2010. The fair value was estimated using discounted cash flow analyses, using interest rates for corporate bonds with similar maturities for borrowers of similar credit quality.

Investments - Investments are carried at fair value as determined by quoted market prices or other available information (Note 3).

Income Taxes - The Endowment has obtained nonprofit status under Internal Revenue Code Section 501(c)(3), and as such, is exempt from income taxes except on unrelated business income. Accordingly, the accompanying financial statements do not reflect a provision or liability for Federal and state income taxes. The Endowment has determined that there are no material unrecognized tax benefits or obligations as of December 31, 2011. Fiscal years ending on or after December 31, 2008 remain subject to examination by Federal and state tax authorities.

Community Wealth through Forestry, Inc. is classified as a C Corporation under the Internal Revenue Code. CWF reported a net loss for the year ended December 31, 2011, therefore there was no tax expense. Accordingly, no provision has been made for federal or state income taxes.

Recently Issued Accounting Standards - The FASB recently issued amendments to ASC 820, *Fair Value Measurements*, which are effective for fiscal years beginning after December 15, 2011. The objective of the amendments under Accounting Standards Update (“ASU”) 2011-04 is to achieve common fair value measurement and disclosure requirements in U.S Generally Accepted Accounting Principles (“GAAP”) and International Financial Reporting Standards (“IFRS”). The amendments change the wording used to describe many of the requirements in U.S. GAAP for measuring fair value and for disclosing information about fair value measurements. Additionally, some of the amendments clarify the application of existing fair value measurement requirements, while others change a particular principle or requirement for measuring fair value or for disclosing information about fair value measurements. Upon adoption, the Endowment will be required to provide revised disclosures regarding fair value measurements and will need to re-assess its fair value measurements to ensure compliance with the provisions of the amendments.

Reclassifications – Certain reclassifications have been made to the 2010 consolidated financial statements to conform to the 2011 consolidated financial statement presentation.

2. **Investments**

The estimated fair values of investments at December 31 follows:

	<u>2011</u>	<u>2010</u>
Money market funds	\$ 3,802,604	\$ 671,143
Equity funds	73,614,230	99,166,346
Fixed income funds	30,992,760	36,414,478
Real asset funds	11,183,207	13,961,647
Natural resource stock index fund	5,080,922	-
Hedge funds	40,190,206	32,658,240
Real estate partnership	1,587,245	127,986
Private equity partnerships	3,020,395	2,141,951
Venture capital partnership	2,280,221	1,393,746
Distressed debt partnership	1,987,112	1,761,580
Total investments	<u>\$ 173,738,902</u>	<u>\$ 188,297,117</u>

Interest and dividend income is reported net of custodial and investment management fees approximating \$194,000 and \$192,000 for the years ended December 31, 2011 and 2010, respectively.

3. **Fair Value of Measurements**

The Financial Accounting Standards Board (“FASB”) issued a statement that defines fair value and establishes a framework for measuring fair value. That framework provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are described as follows:

Level 1 – Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that the Endowment has the ability to access.

Level 2 – Inputs to the valuation methodology include

- quoted prices for similar assets or liabilities in active markets;
- quoted prices for identical or similar assets or liabilities in inactive markets;
- inputs that are derived principally from or corroborated by observable market data by correlation or other means.

If the asset or liability has a specified (contractual) term, the Level 2 input must be observable for substantially the full term of the asset or liability.

Level 3 – Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

The following tables sets forth by level within the fair value hierarchy the Endowment's assets accounted for at fair value on a recurring basis as of December 31, 2011 and 2010. Assets are classified in their entirety based on the lowest level of input that is significant to the fair value measurement. The Endowment's assessment of the significance of a particular input to the fair value measurement requires judgment, and may affect the valuation of fair value assets and their placement within the fair value hierarchy levels.

	Fair value measurements at December 31, 2011 using:			
	Fair value at December 31, 2011	Quoted prices in active markets for identical assets and liabilities (Level 1 inputs)	Quoted prices for similar assets and liabilities (Level 2 inputs)	Significant unobservable inputs (Level 3 inputs)
<u>Assets measured at fair value:</u>				
Money market funds	\$ 3,802,604	\$ 3,802,604	\$ -	\$ -
Equity funds:				
Emerging markets	18,768,255	-	18,768,255	-
Multi-strategy	11,983,056	-	11,983,056	-
International	11,435,943	-	11,435,943	-
All-Cap	9,354,874	-	9,354,874	-
SSG equity	9,991,749	-	9,991,749	-
Core equity	12,080,353	-	12,080,353	-
Total equity funds	<u>73,614,230</u>	<u>-</u>	<u>73,614,230</u>	<u>-</u>
Fixed income funds:				
High quality bond	20,178,414	-	20,178,414	-
Real return bond	5,970,031	-	5,970,031	-
Global bond	4,844,315	-	4,844,315	-
Total fixed income funds	<u>30,992,760</u>	<u>-</u>	<u>30,992,760</u>	<u>-</u>
Real asset funds:				
Multi-strategy commodities	11,183,207	-	11,183,207	-
Natural resource stock index	5,080,922	-	5,080,922	-
Hedge funds:				
Global hedged	7,942,453	-	-	7,942,453
Relative value and event driven	21,054,894	-	-	21,054,894
Diversified	11,192,859	-	-	11,192,859
Total hedge funds	<u>40,190,206</u>	<u>-</u>	<u>-</u>	<u>40,190,206</u>
Realty investors partnership	1,587,245	-	-	1,587,245
Private equity partnerships	3,020,395	-	-	3,020,395
Venture capital partnership	2,280,221	-	-	2,280,221
Distressed equity partnership	1,987,112	-	-	1,987,112
Totals	<u>\$173,738,902</u>	<u>\$ 3,802,604</u>	<u>\$120,871,119</u>	<u>\$ 49,065,179</u>

	<u>Fair value measurements at December 31, 2010 using:</u>			
	<u>Fair value at December 31, 2010</u>	<u>Quoted prices in active markets for identical assets and liabilities (Level 1 inputs)</u>	<u>Quoted prices for similar assets and liabilities (Level 2 inputs)</u>	<u>Significant unobservable inputs (Level 3 inputs)</u>
<u>Assets measured at fair value:</u>				
Money market funds	\$ 671,143	\$ 671,143	\$ -	\$ -
Equity funds:				
Emerging markets	20,371,942	-	20,371,942	-
Multi-strategy	51,888,073	-	51,888,073	-
International	16,081,148	-	16,081,148	-
All-Cap	10,825,183	-	10,825,183	-
Total equity funds	<u>99,166,346</u>	<u>-</u>	<u>99,166,346</u>	<u>-</u>
Fixed income funds:				
High quality bond	28,000,000	-	28,000,000	-
Real return bond	4,974,197	-	4,974,197	-
Global bond	3,440,281	-	3,440,281	-
Total fixed income funds	<u>36,414,478</u>	<u>-</u>	<u>36,414,478</u>	<u>-</u>
Real asset funds:				
Multi-strategy commodities	13,961,647	-	13,961,647	-
Hedge funds:				
Global hedged	16,889,689	-	-	16,889,689
Relative value and event driven	12,877,347	-	-	12,877,347
Diversified	2,891,204	-	-	2,891,204
Total hedge funds	<u>32,658,240</u>	<u>-</u>	<u>-</u>	<u>32,658,240</u>
Realty investors partnership	127,986	-	-	127,986
Private equity partnerships	2,141,951	-	-	2,141,951
Venture capital partnership	1,393,746	-	-	1,393,746
Distressed equity partnership	1,761,580	-	-	1,761,580
Totals	<u>\$188,297,117</u>	<u>\$ 671,143</u>	<u>\$ 149,542,471</u>	<u>\$ 38,083,503</u>

The following table illustrates the activity of Level 3 assets measures at fair value on a recurring basis from December 31, 2010 to December 31, 2011:

	Fair Value Measurements Using Observable Inputs (Level 3)							Total
	Global Hedged	Relative Value and Event Driven	Diversified	Realty Investors Partnership	Private Equity Partnerships	Venture Capital Partnership	Distressed Debt Partnership	
Beginning balance, December 31, 2010	\$ 16,889,689	\$ 12,877,347	\$ 2,891,204	\$ 127,986	\$ 2,141,951	\$ 1,393,746	\$ 1,761,580	\$ 38,083,503
Total gains or losses included in changes in net assets:								
Unrealized gains (losses)	(1,130,409)	(1,787,036)	(468,913)	2,517,292	29,047	274,795	(24,133)	(589,357)
Realized gains (losses)	183,174	(535,417)	(229,431)	(1,058,033)	124,397	11,680	13,465	(1,490,165)
Purchases, issuances/subscriptions, and sales:								
Purchases	1,334,584	25,535,830	11,165,930	-	-	-	-	38,036,344
Issuances/subscriptions	-	-	-	-	725,000	622,500	236,200	1,583,700
Sales	<u>(9,334,585)</u>	<u>(15,035,830)</u>	<u>(2,165,931)</u>	<u>-</u>	<u>-</u>	<u>(22,500)</u>	<u>-</u>	<u>(26,558,846)</u>
Ending balance, December 31, 2011	<u>\$ 7,942,453</u>	<u>\$ 21,054,894</u>	<u>\$ 11,192,859</u>	<u>\$ 1,587,245</u>	<u>\$ 3,020,395</u>	<u>\$ 2,280,221</u>	<u>\$ 1,987,112</u>	<u>\$ 49,065,179</u>

**U.S. ENDOWMENT FOR FORESTRY
AND COMMUNITIES, INC. AND SUBSIDIARY**

Notes to Financial Statements, continued

The following table illustrates the activity of Level 3 assets measures at fair value on a recurring basis from December 31, 2009 to December 31, 2010:

	<u>Global Hedged</u>	<u>Relative Value and Event Driven</u>	<u>Diversified</u>	<u>Multi- strategy Global Hedged</u>	<u>Hedged Investors</u>	<u>Global Absolute</u>	<u>Absolute Return</u>	<u>Realty Investors Partnership</u>	<u>Private Equity Partnerships</u>	<u>Venture Capital Partnership</u>	<u>Distressed Debt Partnership</u>	<u>Total</u>
Beginning balance,												
December 31, 2009	\$ -	\$ -	\$ -	\$ 10,500,491	\$ 10,394,532	\$ 5,715,984	\$ 900,780	\$ 3,545,965	\$ 1,085,008	\$ 735,095	\$ 1,537,154	\$ 34,415,009
Total gains or losses included in changes in net assets:												
Unrealized gains												
(losses)	538,691	703,811	238,780	-	130,565	-	(147,064)	(3,164,150)	242,441	223,234	222,532	(1,011,160)
Realized gains												
(losses)	-	-	-	-	218,565	-	-	(253,829)	(45,498)	(59,583)	(7,106)	(147,451)
Purchases, issuances/subscriptions, and sales:												
Purchases	16,350,998	12,173,536	2,652,424	-	-	-	-	-	-	-	-	31,176,958
Issuances/subscriptions	-	-	-	-	-	-	-	-	860,000	495,000	9,000	1,364,000
Sales	-	-	-	(10,500,491)	(10,743,662)	(5,715,984)	(753,716)	-	-	-	-	(27,713,853)
Ending balance,												
December 31, 2010	<u>\$ 16,889,689</u>	<u>\$ 12,877,347</u>	<u>\$ 2,891,204</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 127,986</u>	<u>\$ 2,141,951</u>	<u>\$ 1,393,746</u>	<u>\$ 1,761,580</u>	<u>\$ 38,083,503</u>

Total net losses for level 3 assets for the periods above are included in net realized and unrealized gains (losses) on investments in the statement of activities. There were no transfers in or out of Level 3 for the years ended December 31, 2011 and 2010.

The Endowment has investments in various common and collective equity funds of \$73,614,230 and \$99,166,346 at December 31, 2011 and 2010. Interests in these funds are generally redeemable on a monthly basis with 5 to 30 business days notice and include various U.S domestic large, mid and small cap securities and international equity securities including equity securities of companies located in the less developed countries of the world.

The Endowment has investments in various common and collective fixed income funds of \$30,992,760 and \$36,414,478 at December 31, 2011 and 2010, respectively. Interests in these funds are generally redeemable on a monthly basis with 5 to 30 business days notice and include various fixed income investments in the sovereign bonds and other fixed income securities in the U.S and worldwide in an attempt to outperform both the broad U.S bond market and the broad worldwide bond market. These funds also invest in investment grade inflation-indexed securities, including U.S. Treasury inflation indexed securities and no-U.S. dollar denominated inflation-indexed securities.

The Endowment has an investment in a common and collective real asset fund of \$11,183,207 and \$13,961,647 at December 31, 2011 and 2010, respectively. Interests in this fund is generally redeemable on a monthly basis with 5 to 30 days business notice and include various assets across a broad spectrum of commodity-oriented asset categories pursuing a multi-strategy approach to investing in the commodities markets, which include futures, options on futures and forward contracts on exchange traded agricultural goods, metals, minerals, energy products and foreign currencies.

The Endowment has an investment in a common and collective natural resource fund of \$5,080,922 and \$-0- at December 31, 2011 and 2010, respectively. Interest in this fund is generally redeemable on a daily basis. The investment objective of the fund is to approximate the performance of the MSCI World Resource Industry: Paper & Forest Products, Metals & Mining, Oil & Gas, and Energy & Equipment.

The Endowment has investments in directional and relative value hedge funds of \$40,190,206 and \$32,658,240 at December 31, 2011 and 2010, respectively. The Endowment may redeem its interests in the funds on a quarterly (\$19,135,313 and \$19,780,893 at December 31, 2011 and 2010, respectively), or annual basis (\$21,054,893 and \$12,877,347 at December 31, 2011 and 2010, respectively) with generally 65-95 days notice. The funds pursue multiple strategies to diversify risks and reduce volatility while seeking to deliver positive returns regardless of the direction of the broader market.

The Endowment has an investment in a real estate fund of \$1,587,245 and \$127,986 at December 31, 2011 and 2010, respectively. The fund is generally ineligible for redemption except the Endowment may elect during September of each year to have the fund redeem up to 20% of the units owned for at least 5 years, provided the fund has not commenced a

general liquidation. September 2013 would be the first year the Endowment would be eligible to be issued any redemption. Redemptions are paid prior to the end of the subsequent calendar year and at the net asset value determined at the date of the redemption period. The Endowment committed total funds of \$16,000,000 and has no unfunded commitments to this fund as of December 31, 2011. The real estate fund generally invests in a variety of real estate assets in the U.S.

The Endowment has investments in international and domestic private equity partnerships of \$3,020,395 and \$2,141,951 at December 31, 2011 and 2010, respectively. The Endowment has committed a total of \$6,000,000 and has unfunded commitments of \$3,207,500 as of December 31, 2011. These funds are ineligible for redemption and the typical life of the partnerships is 12 years from the date of formation but can be extended under certain circumstances. These partnerships generally seek to generate higher returns over the long-term than those generally available on the foreign and domestic securities exchanges through investments in a diversified portfolio of international and domestic private capital funds.

The Endowment has an investment in a venture capital partnership of \$2,280,221 and \$1,393,746 at December 31, 2011 and 2010, respectively. The Endowment has committed a total of \$3,000,000 and has unfunded commitments of \$1,110,000 as of December 31, 2011. These funds are ineligible for redemption and the typical life of the partnership is 12 years from the date of formation but can be extended under certain circumstances. This partnership seeks to earn returns above those on publically traded stocks by investing in early stage, high growth private companies, principally in the information technology and life sciences/healthcare fields.

The Endowment has an investment in a distressed debt partnership of \$1,987,112 and \$1,761,580 at December 31, 2011 and 2010, respectively. The Endowment has committed a total of \$2,000,000 and has unfunded commitments of \$487,400 as of December 31, 2011. The Endowment may redeem certain portions of its investment on each December 31, provided the fund has not commenced a general liquidation; however, interests in the fund with respect to longer-term investments as defined by the offering memorandum, are not redeemable by the Endowment until the corresponding longer-term investments are realized. The partnership seeks to pursue an investment program comprised of performing restructured debt, stressed debt, distressed debt and mezzanine debt investments that seeks to provide a net internal rate of return in the mid teens.

4. **Investment in North Star Jefferson, LLC**

During 2011, CWF entered into an operating agreement with another company to form a limited liability company, North Star Jefferson, LLC. The purpose of the company is to develop, construct, finance and operate biomass fired renewable energy power plants. CWF has an approximate 31% ownership interest and the future allocation of profits and losses, if any, will be allocated in proportion to the value of the capital account balances of the members. Total capital contributions of \$228,068 were made for the year ended

December 31, 2011. CWF's portion of the net loss recognized by the limited partnership was \$(90,002) for the year ended December 31, 2011. CWF has committed to invest a total of \$1,500,000 in North Star Jefferson, LLC. In addition, included in notes receivable December 31, 2011 is \$1,500,000 due from North Star Jefferson, LLC.

5. Property and Equipment

Property and equipment at December 31, 2011 and 2010 consists of the following:

	<u>2011</u>	<u>2010</u>
Land	\$ 137,794	\$ 135,374
Building	324,101	-
Total property and equipment	<u>461,895</u>	<u>135,374</u>
Less: accumulated depreciation	(9,453)	-
Construction in progress	-	63,488
	<u>\$ 452,442</u>	<u>\$ 198,862</u>

6. Note Payable

Note payable to a bank with six interest only payments through October 2011; then thirty monthly payments of \$2,361 including principle and interest at prime minus .26%. The bank's prime rate at December 31, 2011 is 3.25%. The note matures in March 2014. The note is collateralized by the building.

	<u>\$ 337,085</u>
Total long-term debt	<u>\$ 337,085</u>

The aggregate annual maturities of long-term debt for the years subsequent to December 31, 2011 follow:

2012	\$ 18,506
2013	19,067
2014	<u>299,512</u>
	<u>\$ 337,085</u>

7. Employee Benefit Plan

The Endowment sponsors a Simplified Pension Plan whereby deposits in an amount equal to 11% of each full-time employee's gross pay is deposited into a self-directed individual retirement account. Employees are eligible to participate in the plan from the first day of employment and are fully vested in all funds deposited into their accounts. The

Endowment’s contribution totaled approximately \$76,000 and \$66,000 for the years ended December 31, 2011 and 2010, respectively.

8. Net Assets

Temporarily restricted net assets are restricted for the following purposes at December 31, 2011 and 2012:

	<u>2011</u>	<u>2010</u>
Advancing Forest Health through Biotechnology	\$ -	\$ 151,474
Hardwood check-off	45,488	28,453
Water from Forest Convening	18,017	30,000
	<u>\$ 63,505</u>	<u>\$ 209,927</u>

Permanently restricted net asset consists of a \$200,000,000 endowment received as a result of the SLA to be invested in perpetuity with the investments gains and investment earnings to be used for the Endowment’s set purpose as described in Note 1. As of December 31, 2011 as a result of recent market declines, the fair value of Endowment assets was less than the Endowment corpus by \$22,188,864, which has been absorbed by unrestricted net assets.

9. Endowment Funds

The Endowment was organized to support educational and charitable causes in timber-reliant communities and educational and public interest projects addressing forest management issues that affect timber-reliant communities, or the sustainability of forests as sources of building materials, wildlife habitat, bio-energy, recreation, and other values. The Endowment’s funds include donor-restricted endowment funds classified as permanently restricted.

The investment objectives of the donor-restricted endowment funds have been established in conjunction with a comprehensive review of the current and projected financial requirements. The investment objectives are:

- To achieve a favorable long term, real rate of return primarily through capital appreciation.
- To preserve principal through reasonable efforts, but preservation of principal shall not be imposed as a requirement on each individual investment.
- To produce current income, but only as a secondary consideration.
- To reduce risk by diversifying among markets, managers and time frames.

Interpretation of Relevant Law - The Board of Directors of the Endowment has interpreted the Uniform Prudent Management of Institutional Funds Act (“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. The Endowment follows the laws of UPMIFA in Delaware, the incorporation state, and South Carolina, the state in which the Endowment is headquartered. The Endowment has classified

as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the required accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets, if positive, until those amounts are appropriated for expenditure by the Endowment in a manner consistent with the standard of prudence prescribed by UPMIFA.

Donor-restricted endowment net asset composition by type of fund as of December 31, 2011 is as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Donor-restricted endowment funds	<u>\$ (22,188,864)</u>	<u>\$ -</u>	<u>\$ 200,000,000</u>	<u>\$ 177,811,136</u>

Changes in donor-restricted endowment net asset for the year ended December 31, 2011 are as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Endowment net assets, December 31, 2010	\$ (8,504,551)	\$ -	\$ 200,000,000	\$ 191,495,449
Investment return:				
Investment income, net	2,749,485	-	-	2,749,485
Net unrealized and realized investment gains	<u>(13,284,804)</u>	<u>-</u>	<u>-</u>	<u>(13,284,804)</u>
Total investment return	<u>(10,535,319)</u>	<u>-</u>	<u>-</u>	<u>(10,535,319)</u>
Appropriation of assets for expenditures	<u>(3,148,994)</u>	<u>-</u>	<u>-</u>	<u>(3,148,994)</u>
Endowment net assets, December 31, 2011	<u>\$ (22,188,864)</u>	<u>\$ -</u>	<u>\$ 200,000,000</u>	<u>\$ 177,811,136</u>

Donor-restricted endowment net asset composition by type of fund as of December 31, 2010 is as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Donor-restricted endowment funds	<u>\$ (8,504,551)</u>	<u>\$ -</u>	<u>\$ 200,000,000</u>	<u>\$ 191,495,449</u>

Changes in donor-restricted endowment net asset for the year ended December 31, 2010 are as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Endowment net assets, December 31, 2009	\$ (21,310,824)	\$ -	\$ 200,000,000	\$ 178,689,176
Investment return:				
Investment income, net	2,415,347	-	-	2,415,34
Net unrealized and realized investment gains	<u>14,104,444</u>	<u>-</u>	<u>-</u>	<u>14,104,444</u>
Total investment return	16,519,791	-	-	16,519,791
Appropriation of assets for expenditures	<u>(3,713,518)</u>	<u>-</u>	<u>-</u>	<u>(3,713,518)</u>
Endowment net assets, December 31, 2010	<u>\$ (8,504,551)</u>	<u>\$ -</u>	<u>\$ 200,000,000</u>	<u>\$ 191,495,449</u>

Funds with Deficiencies

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level that the donor or UPMIFA requires the Endowment to retain as a fund of perpetual duration. Deficiencies of this nature that are reported in unrestricted net assets were \$22,188,864 and \$8,504,551 as of December 31, 2011 and 2010, respectively. These deficiencies resulted from unfavorable market fluctuations.

Return Objectives and Risk Parameters

The Endowment has adopted investment and spending policies for endowment assets that are intended to provide an ongoing stream of funding of the Endowment's set mission. Endowment assets include those assets of donor-restricted funds that the Endowment must hold in perpetuity. Under this policy, as approved by the Board, the endowment assets are invested in a manner that is intended to produce a high level of total investment return consistent with a prudent level of portfolio risk.

Strategies Employed for Achieving Objectives

To satisfy its long-term rate-of-return objectives, the Endowment relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The Endowment targets a diversified asset allocation that places a greater emphasis on equity and fixed income-based investments to achieve its long-term return objectives within prudent risk constraints.

Spending Policy and How the Investment Objectives Relate to Spending Policy

The Endowment's Board of Directors seeks to address twin objectives of deploying resources to achieve its mission and operating as prudent fiduciaries. The Endowment's long-range target is to distribute grants of up to 5% of the investment corpus annually, with the understanding that the distributions plus inflation (at an assumed rate of 2.5%), modest real growth (1%), and the costs of non-programmatic operating expenses (0.375%) will not

exceed total return from investment over rolling 5-year periods. This target assumes an 8.875% average annual rate of return which is a rate within the range of historic market returns. Recognizing that, from time to time, the realities of unfavorable market fluctuations could cause the fair value of its assets to decline below the level that the Endowment is required to retain, in May 2008, the Board amended its policy to address the event of “underwater” conditions. The amended policy provided for the spending of not more than 2.5% of corpus in the event of a decline below the \$200 million corpus, and further called for the Board to revisit the policy in the face of “exceptional downturns”, defined as declines in the fair value of assets to below \$190 million. To offer some level of stability to its emerging mission / programmatic investment during a period of radical declines in the fair market value of its assets, the Board voted to spend an average of \$5 million per year over the three-year period from 2009 – 2011. The Board believed that this interim policy was prudent and supportive of both the Endowment’s mission and fiduciary obligations.

10. **Commitments**

The Endowment makes multi-year commitments to fund specific research and public interest projects with other nonprofit organizations and universities. Committed funds totaled approximately \$7,793,000 at December 31, 2011. These contracts are committed for varying dates through 2013.

11. **Subsequent Events**

During 2012, the CWF contributed additional capital of \$1,271,300 to North Star Jefferson, LLC.

The Endowment evaluated the effect subsequent events would have on the financial statements through September 21, 2012, which is the date the financial statements were available to be issued.

U.S. ENDOWMENT FOR FORESTRY AND COMMUNITIES, INC. AND SUBSIDIARY

Consolidated Schedules of Functional Expenses

For the Years Ended December 31, 2011 and 2010

	2011			2010		
	Programmatic	Management and General	Total	Programmatic	Management and General	Total
Grant expenditures	\$ 4,569,846	\$ -	\$ 4,569,846	\$ 4,739,616	\$ -	\$ 4,739,616
Program expenses	595,917	-	595,917	428,969	-	428,969
Compensation - officers	217,440	54,360	271,800	208,726	52,182	260,908
Compensation - non-officers	277,139	160,107	437,246	232,335	137,441	369,776
Compensation - interns	26,288	6,572	32,860	6,132	1,533	7,665
Employee benefits	119,011	51,492	170,503	89,673	53,118	142,791
Travel	17,989	33,277	51,266	32,680	36,455	69,135
Communications	12,150	5,257	17,407	8,695	5,150	13,845
Rent/utilities/supplies	-	29,329	29,329	-	74,903	74,903
Professional services	-	66,780	66,780	-	66,697	66,697
Insurance	-	16,194	16,194	-	11,268	11,268
Interest expense	-	5,086	5,086	-	-	-
Uncollectible accounts	67,125	-	67,125	345,500	-	345,500
Other	-	10,301	10,301	-	15,434	15,434
	\$ 5,902,905	\$ 438,755	\$ 6,341,660	\$ 6,092,326	\$ 454,181	\$ 6,546,507

See accompanying Independent Auditors' Report.



Independent Auditors' Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Consolidated Financial Statements Performed in Accordance with *Government Auditing Standards*

The Board of Directors
US Endowment for Forestry and Communities, Inc. and Subsidiary
Greenville, South Carolina

We have audited the consolidated financial statements of US Endowment for Forestry and Communities, Inc. and Subsidiary (the "Endowment") as of and for the year ended December 31, 2011, and have issued our report thereon dated September 21, 2012. 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

Management of the Endowment is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered the Endowment'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 the Endowment's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Endowment's internal control over financial reporting.

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 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.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in the internal control over financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be a material weakness, as defined above.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Endowment's consolidated financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, non-compliance 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 no instances of non-compliance or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of the Board of Directors, management and Federal awarding agencies and is not intended to be and should not be used by anyone other than these specified parties.

Dixon Hughes Goodman LLP

September 21, 2012



**Report On Compliance With Requirements Applicable
To Each Major Program and Internal Control
Over Compliance In Accordance With OMB Circular A-133**

The Board of Directors
US Endowment for Forestry and Communities, Inc. and Subsidiary
Greenville, South Carolina

Compliance

We have audited the compliance of US Endowment for Forestry and Communities, Inc. and Subsidiary (the “Endowment”) with the types of compliance requirements described in the *U. S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that could have a direct and material effect on each of its major Federal programs for the year ended December 31, 2011. The Endowment’s major Federal programs are identified in the summary of auditors’ results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to its major Federal programs is the responsibility of the Endowment’s management. Our responsibility is to express an opinion on the Endowment’s compliance based on our audit.

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, and *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 the Endowment’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 on the Endowment’s compliance with those requirements.

In our opinion, the Endowment 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, 2011. However, the results of our auditing procedures disclosed an instance of noncompliance with those requirements, which is required to be reported in accordance with OMB Circular A-133 and which is described in the accompanying schedule of findings and questions costs as Finding 2011-1.

Internal Control Over Compliance

Management of the Endowment is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to Federal programs. In planning and performing our audit, we considered the Endowment’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 the Endowment’s internal control over compliance.

The Board of Directors
US Endowment for Forestry and Communities, Inc. and Subsidiary
Page Two

A deficiency in internal control over compliance 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 non-compliance with a type of compliance requirement of a major program on a timely basis. A material weakness in internal control over compliance is a deficiency or a combination of deficiencies in internal control over compliance, such that there is a reasonable possibility that material non-compliance with a type of compliance requirement of a Federal program will not be prevented, or detected and corrected, on a timely basis.

Our consideration of the internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

The Endowment's response to the finding identified in our audit is described in the accompanying corrective action plan. We did not audit the Endowment's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of the Board of Directors, management, and Federal awarding agencies, and is not intended to be and should not be used by anyone other than these specific parties.

Dixon Hughes Goodman LLP

September 21, 2012

U.S. ENDOWMENT FOR FORESTRY AND COMMUNITIES, INC. AND SUBSIDIARY

Schedule of Expenditures of Federal Awards

Year Ended December 31, 2011

<u>Federal Grantor/Pass-Through Grantor/Program or Cluster Title</u>	<u>Federal CFDA Number</u>	<u>Federal Expenditures</u>
U. S. Department of Agriculture		
<u>Direct Program:</u>		
Forestry Research	10.652	\$ 912,110
Cooperative Forestry Assistance	10.664	949,353
Forestry Legacy Program	10.676	64,226
Forest Stewardship Program	10.678	45,483
Environmental Quality Incentives	10.912	531,188
Total U.S. Department of Agriculture		<u>2,502,360</u>
U. S. Department of the Interior Fish and Wildlife Service		
<u>Direct Program:</u>		
Service Training and Technical Assistance	15.649	<u>15,000</u>
Total expenditures of Federal awards		<u><u>\$ 2,517,360</u></u>

1. **Basis of Presentation**

The accompanying schedule of expenditures of Federal awards includes the Federal grant activity of U.S. Endowment for Forestry and Communities, Inc. and Subsidiary and is presented on the accrual basis of accounting.

2. **Subrecipients**

Of the Federal expenditures presented in this schedule, U.S. Endowment for Forestry and Communities, Inc. and Subsidiary provided Federal awards to subrecipients as follows:

<u>Program Title</u>	<u>Federal CFDA Number</u>	<u>Amount Provided to Subrecipients</u>
Forestry Research	10.652	\$ 748,041
Environmental Quality Incentives	10.912	\$ 531,188
Cooperative Forestry Assistance	10.664	\$ 52,565

U.S. ENDOWMENT FOR FORESTRY AND COMMUNITIES, INC. AND SUBSIDIARY
 Schedule of Findings and Questioned Costs
 For the Year Ended December 31, 2011

Section I—Summary of Auditors’ Results

Financial Statements

Type of auditors’ report issued: Unqualified

Internal control over financial reporting:

- Material weakness(es) identified? _____ Yes X No
- Significant deficiencies identified that are not considered to be material weaknesses? _____ Yes X None reported

Noncompliance material to financial statements noted? _____ Yes X No

Federal Awards

Internal control over major programs:

- Material weakness(es) identified? _____ Yes X No
- Significant deficiencies identified that are not considered to be material weaknesses? _____ Yes X None reported

Type of auditors’ report issued on compliance for major programs: Unqualified

Any audit findings disclosed that are required to be reported in accordance with section 510(a) of Circular A-133? X Yes _____ No

U.S. ENDOWMENT FOR FORESTRY AND COMMUNITIES, INC. AND SUBSIDIARY
Schedule of Findings and Questioned Costs (continued)
For the Year Ended December 31, 2011

Section I—Summary of Auditors' Results (continued)

Identification of major programs:

<u>CFDA Numbers</u>	<u>Name of Federal Program or Cluster</u>
10.652	Forestry Research
10.664	Cooperative Forestry Assistance
10.912	Environmental Quality Incentives

Dollar threshold used to distinguish
between type A and type B programs:

\$ 300,000

Auditee qualified as low-risk auditee?

Yes No

Section II— Consolidated Financial Statement Findings

There were none.

U.S. ENDOWMENT FOR FORESTRY AND COMMUNITIES, INC. AND SUBSIDIARY
Schedule of Findings and Questioned Costs (continued)
For the Year Ended December 31, 2011

Section III— Federal Award Findings and Questioned Costs

U.S. Department of Agriculture

Forestry Research and Environmental Quality Incentives
CFDA 10.652, 10.664, and 10.912

2011-1 Finding: Monitoring

Subrecipient Monitoring

Criteria: Subrecipients were not appropriately informed at the time of the subaward.

Condition: During test work, we noted that the Endowment provided grants to subrecipients without appropriately identifying the Federal award information (i.e., CFDA title and number, award name and number; if the award is research and development; and name of Federal awarding agency) and applicable compliance requirements.

Effect: The Endowment is not effectively identifying or executing controls over the subrecipient compliance requirements.

Cause: Lack of administrative oversight and internal control design.

Questioned Costs: None noted

Recommendation: We recommend that the Endowment revise grant agreements to appropriately identify the Federal award information to all subrecipients.

U.S. ENDOWMENT FOR FORESTRY AND COMMUNITIES, INC. AND SUBSIDIARY
Schedule of Findings and Questioned Costs (continued)
For the Year Ended December 31, 2011

Section III— Federal Award Findings and Questioned Costs

Management Response:

Grant agreements issued in the initial years of the Endowment's existence did not provide information, where applicable, as to percentage of federal funding included in awards or CFDA numbers associated with the funded programs. All subrecipients that received these grant agreements have been contacted and given the required information. Furthermore, this information and relevant compliance requirements have been included in all contracts issued since mid-2010. Contracts and award agreements are written by a program officer employing a template that prompts inclusion of this information, and are reviewed prior to issuance by a second program officer and by administrative personnel to insure that necessary information has been supplied to recipients of grants awarded. We believe that these procedures have been effective in ensuring that similar oversights have not been repeated and will not occur in the future.

U.S. ENDOWMENT FOR FORESTRY AND COMMUNITIES, INC. AND SUBSIDIARY
Corrective Action Plan
For the Year Ended December 31, 2011

Section II— Consolidated Financial Statement Findings

None reported.

Section III— Federal Award Findings and Questioned Costs

2011-1 Finding:	Monitoring
Contact Person:	Kim Free
Corrective Action:	Management has taken appropriate action to contact subrecipients with the information required by this compliance requirement.
Proposed Completion Date:	September 2012

U.S. ENDOWMENT FOR FORESTRY AND COMMUNITIES, INC. AND SUBSIDIARY
Summary Schedule of Prior Audit Findings
For the Year Ended December 31, 2011

Finding 2010-1:	Monitoring
Status:	Resolved - Management has taken appropriate action to contact subrecipients and provided them with the information required by this compliance requirement.

The year ended December 31, 2010 was the first year the Endowment was required to have a Single Audit, therefore, no findings reported for the year ended December 31, 2009.