

**RURAL ADVANCEMENT FOUNDATION
INTERNATIONAL – USA AND AFFILIATE**

Pittsboro, North Carolina

**CONSOLIDATED
AUDITED FINANCIAL STATEMENTS
FOR THE YEAR ENDED DECEMBER 31, 2011
(With Comparative Totals for the
Year Ended December 31, 2010)**

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INDEPENDENT AUDITOR'S REPORT

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Board of Directors
Rural Advancement Foundation International - USA
and Affiliate
Pittsboro, North Carolina

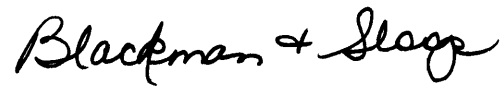
We have audited the accompanying consolidated statement of financial position of Rural Advancement Foundation International - USA, (a nonprofit organization), and its affiliate, Rural Advancement Institute, (a nonprofit organization), as of December 31, 2011, and the related consolidated statement of activities, changes in net assets, and cash flows for the year then ended. These consolidated financial statements are the responsibility of the Organization's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audit. The prior year summarized comparative information has been derived from the Organization's 2010 audited financial statements and, in our report dated March 17, 2011, we expressed an unqualified opinion on those financial statements.

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. 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.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Rural Advancement Foundation International - USA and its affiliate, Rural Advancement Institute, as of December 31, 2011, and the changes in their net assets and their cash flows for the year 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 May 2, 2012, on our consideration of Rural Advancement Foundation International - USA's and its affiliate, Rural Advancement Institute'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 consolidated financial statements of Rural Advancement Foundation International - USA and its affiliate, Rural Advancement Institute, as a whole. The schedule of functional expenses is presented for purposes of additional analysis and is not a required part of the financial statements. The accompanying schedule of state awards is presented for purposes of additional analysis as required by NC General Statute 143-6.2 *"Use of State Funds by Non-State Entities,"* and is also not a required part of the 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 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 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 consolidated financial statements taken as a whole.

A handwritten signature in black ink that reads "Blackman + Sloss". The signature is written in a cursive, flowing style.

Chapel Hill, North Carolina
May 2, 2012

**RURAL ADVANCEMENT FOUNDATION INTERNATIONAL - USA
AND AFFILIATE**

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

EXHIBIT A

December 31, 2011 and 2010

ASSETS

	2011	2010
CURRENT ASSETS:		
Cash and cash equivalents	\$ 403,219	\$ 595,788
Charitable gift annuity	10,083	12,938
Receivables:		
Grants	379,359	2,961,160
Contracts	28,890	10,498
Other	1,849	3,090
Unconditional promises to give	1,799	500
Prepaid expenses and deposits	9,987	11,529
	835,186	3,595,503
PROPERTY AND EQUIPMENT:		
Land	168,229	168,229
Building	908,720	908,720
Office equipment	40,572	41,770
Furniture and fixtures	10,911	10,911
	1,128,432	1,129,630
Less accumulated depreciation	(290,135)	(260,994)
	838,297	868,636
OTHER ASSETS:		
Other assets	9,146	-
	\$ 1,682,629	\$ 4,464,139

LIABILITIES AND NET ASSETS

CURRENT LIABILITIES:		
Accounts payable	\$ 36,349	\$ 109,130
Security deposits	830	2,330
Charitable gift annuity	1,071	1,071
Deferred compensation - current maturity	1,738	16,218
	39,988	128,749
OTHER LIABILITIES:		
Line of credit	150,000	-
Deferred compensation - net of current maturity	65,042	53,504
	215,042	53,504
TOTAL LIABILITIES	255,030	182,253
NET ASSETS:		
Unrestricted	746,667	1,198,015
Temporarily restricted	680,932	3,083,871
	1,427,599	4,281,886
TOTAL LIABILITIES AND NET ASSETS	\$ 1,682,629	\$ 4,464,139

The accompanying Notes to Financial Statements are an integral part of these statements.

**RURAL ADVANCEMENT FOUNDATION INTERNATIONAL - USA
AND AFFILIATE**

CONSOLIDATED STATEMENT OF ACTIVITIES

EXHIBIT B

**For the Year Ended December 31, 2011
(With Comparative Totals for the Year Ended December 31, 2010)**

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>2011 Totals</u>	<u>2010 Totals</u>
REVENUES AND PUBLIC SUPPORT:				
Private foundations and public funds	\$ 194,875	\$ 471,330	\$ 666,205	\$ 1,387,920
Service contracts and honoraria	231,589	-	231,589	238,291
Individual contributions	88,752	1,953	90,705	99,520
Corporate contributions	3,076	18,146	21,222	61,500
Rental income	22,125	-	22,125	26,396
In-kind contributions	88,939	-	88,939	23,926
Interest and dividends	2,479	57	2,536	4,504
Change in value of charitable gift annuity	(1,825)	-	(1,825)	2,492
Realized loss on donated stock	(366)	-	(366)	-
Registration fees	7,448	-	7,448	-
	<u>637,092</u>	<u>491,486</u>	<u>1,128,578</u>	<u>1,844,549</u>
Net assets released from restrictions	<u>2,894,425</u>	<u>(2,894,425)</u>	<u>-</u>	<u>-</u>
TOTAL REVENUES AND PUBLIC SUPPORT	<u>3,531,517</u>	<u>(2,402,939)</u>	<u>1,128,578</u>	<u>1,844,549</u>
EXPENSES:				
PROGRAM SERVICES:				
Just Foods	403,633	-	403,633	459,067
Tobacco Communities and Ag Enterprise Development	2,482,323	-	2,482,323	1,678,762
Contract Agriculture Reform	170,435	-	170,435	205,428
Farm Sustainability	578,080	-	578,080	337,557
TOTAL PROGRAM SERVICES	<u>3,634,471</u>	<u>-</u>	<u>3,634,471</u>	<u>2,680,814</u>
SUPPORTING SERVICES:				
General and administrative	166,513	-	166,513	145,394
Fundraising	181,881	-	181,881	148,739
TOTAL SUPPORTING SERVICES	<u>348,394</u>	<u>-</u>	<u>348,394</u>	<u>294,133</u>
TOTAL EXPENSES	<u>3,982,865</u>	<u>-</u>	<u>3,982,865</u>	<u>2,974,947</u>
CHANGES IN NET ASSETS	(451,348)	(2,402,939)	(2,854,287)	(1,130,398)
NET ASSETS - BEGINNING OF YEAR (AS RESTATED)	<u>1,198,015</u>	<u>3,083,871</u>	<u>4,281,886</u>	<u>5,412,284</u>
NET ASSETS - END OF YEAR	<u>\$ 746,667</u>	<u>\$ 680,932</u>	<u>\$ 1,427,599</u>	<u>\$ 4,281,886</u>

The accompanying Notes to Financial Statements are an integral part of these statements.

**RURAL ADVANCEMENT FOUNDATION INTERNATIONAL - USA
AND AFFILIATE**

CONSOLIDATED STATEMENT OF FUNCTIONAL EXPENSES

EXHIBIT C

For the Year Ended December 31, 2011

(With Comparative Totals for the Year Ended December 31, 2010)

	Program Services				Supporting Services			2011 Totals	2010 Totals
	Just Foods	Communities and Ag Enterprise Development	Contract Agriculture Reform	Farm Sustainability	General and Administrative	Fundraising			
Organizational contracts	\$ 960	\$ 1,983,041	\$ -	\$ 4,500	\$ -	\$ -	\$ -	\$ 1,988,501	\$ 1,206,998
Salaries	128,805	232,242	68,376	230,820	80,855	122,809	863,907	863,907	718,575
Consultants	164,463	124,429	44,639	213,269	875	3,559	551,234	551,234	391,991
Employee benefits	35,462	61,604	25,612	53,431	19,700	32,929	228,738	228,738	281,130
Travel	35,633	23,580	7,864	31,599	1,020	551	100,247	100,247	124,520
Meetings and conferences	19,108	9,031	7,120	12,551	3,439	1,760	53,009	53,009	26,832
Professional fees	3,779	13,101	2,279	4,083	22,136	2,639	48,017	48,017	61,373
Depreciation	4,059	4,059	4,059	4,059	13,685	-	29,921	29,921	29,905
Printing and copying	1,860	9,687	5,769	5,651	661	4,067	27,695	27,695	21,303
Communications	4,074	8,015	2,026	6,782	1,108	793	22,798	22,798	24,576
Occupancy	226	4,455	170	3,014	10,143	2,696	20,704	20,704	42,375
Equipment maintenance and repairs	1,439	2,433	1,423	3,317	4,613	1,077	14,302	14,302	14,480
Postage and shipping	426	2,177	425	946	427	6,289	10,690	10,690	10,231
Supplies	1,508	3,335	435	3,422	1,196	731	10,627	10,627	11,713
Memberships and subscriptions	1,747	715	228	646	1,209	1,981	6,526	6,526	3,968
Insurance	-	-	-	-	5,339	-	5,339	5,339	4,704
Miscellaneous	84	419	10	(10)	107	-	610	610	273
TOTAL EXPENSES	\$ 403,633	\$ 2,482,323	\$ 170,435	\$ 578,080	\$ 166,513	\$ 181,881	\$ 3,982,865	\$ 3,982,865	\$ 2,974,947

The accompanying Notes to Financial Statements are an integral part of these statements.

**RURAL ADVANCEMENT FOUNDATION INTERNATIONAL - USA
AND AFFILIATE**

CONSOLIDATED STATEMENTS OF CASH FLOWS

EXHIBIT D

For the Years Ended December 31, 2011 and 2010

	2011	2010
CASH FLOWS FROM OPERATING ACTIVITIES:		
Changes in net assets	\$ (2,854,287)	\$ (1,130,398)
Adjustments to reconcile changes in net assets to net cash used in operating activities:		
Change in fair value of charitable gift annuity	1,825	(2,492)
Realized loss on donated stock	366	-
Donated stock	(10,442)	-
Depreciation	29,921	29,905
Loss on disposal of assets	418	-
Increase (decrease) in cash arising from changes in assets and liabilities:		
Grants receivable	2,581,801	(340,461)
Contracts receivable	(18,392)	75,903
Other receivables	1,241	(1,063)
Unconditional promises to give	(1,299)	84,720
Prepaid expenses and deposits	1,542	(8,666)
Other assets	(9,146)	-
Accounts payable	(72,781)	26,968
Security deposits	(1,500)	(470)
Deferred compensation	(2,942)	(33,603)
NET CASH USED IN OPERATING ACTIVITIES	(353,675)	(1,299,657)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Net charitable gift annuity activity	1,030	885
Net proceeds from sale of donated stock	10,076	-
Purchase of property and equipment	-	(11,150)
NET CASH USED IN INVESTING ACTIVITIES	11,106	(10,265)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from line of credit	150,000	-
NET DECREASE IN CASH AND CASH EQUIVALENTS	(192,569)	(1,309,922)
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	595,788	1,905,710
CASH AND CASH EQUIVALENTS AT END OF YEAR	\$ 403,219	\$ 595,788
OTHER DISCLOSURES:		
In-kind donations	\$ 88,939	\$ 23,926

The accompanying Notes to Financial Statements are an integral part of these statements.

**RURAL ADVANCEMENT FOUNDATION INTERNATIONAL – USA
AND AFFILIATE**

NOTES TO FINANCIAL STATEMENTS

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NATURE OF ACTIVITIES

Rural Advancement Foundation International - USA (RAFI-USA) is a nonprofit organization promoting community, equity, and diversity in agriculture. Rural Advancement Institute (RAI), a supporting organization of RAFI-USA, was incorporated in 2002 to exclusively operate for the benefit of, to perform the functions of, or to carry out the purposes of RAFI-USA. Activities of the organizations are organized as follows:

Just Foods.

This program works to revitalize public plant and animal breeding to increase the availability of seeds and animals suitable for sustainable agriculture. It educates farmers and other citizens about agricultural biotechnology. The program encourages the development of meaningful standards for food labels and proper implementation of labeling and certification programs. It also promotes new and expanded production, marketing, and research opportunities for organic farmers.

Tobacco Communities and Agriculture Enterprise Development.

This program serves as a resource for farmers and communities seeking to survive changes in the farm economy. It documents the impacts and promotes the model of the Tobacco Communities Reinvestment Fund as a way for state and private agencies to support agricultural enterprise development.

Contract Agriculture Reform.

This program promotes fair and equitable contract arrangements between individual farmers and processors. The program provides educational materials and trainings for farmers and community groups about contract agriculture, supports policy and administrative action related to fair contract standards, and serves as a resource and reference for contract farmers in crisis.

Farm Sustainability.

This program assists farmers and communities in adapting to changes in agriculture with sustainable solutions. The program provides skilled, in-depth farm planning and financial counseling, assists farmers with access to federal agriculture programs, provides research and analysis of farm policy impacts on farms and rural communities, and advises independent marketing and conservation initiatives aimed at assisting small and mid-scale farmers. It also trains farmers, communities, and churches in disaster assistance and addressing community issues resulting from disasters and farm loss.

**RURAL ADVANCEMENT FOUNDATION INTERNATIONAL – USA
AND AFFILIATE**

NOTES TO FINANCIAL STATEMENTS

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SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Principles of Consolidation.

The consolidated financial statements include the accounts of RAFI-USA, and its affiliate, RAI, after elimination of all intercompany accounts and transactions (hereafter, the Organization). All activities of RAI were assumed by RAFI-USA effective January 1, 2011.

B. Basis of Accounting.

The Organization's financial statements are presented on the accrual basis of accounting in conformity with accounting principles generally accepted in the United States of America (U.S. GAAP), which require the use of certain estimates made by the Organization's management. Accordingly, revenues are recognized when earned, and expenses are recognized when the obligation is incurred.

The Organization reports gifts of cash and other assets as restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor 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. If the Organization receives and spends restricted monies within the same year, it is treated as unrestricted revenues.

C. Cash and Cash Equivalents.

Cash and cash equivalents consist of monies on deposit at financial institutions and other highly liquid investments with maturities of three months or less. At times, the Organization places deposits with high-quality financial institutions that may be in excess of federally insured amounts. The Organization has not experienced any financial loss related to such deposits.

D. Investments.

Investments in marketable securities are stated at their fair market value. Donated securities are recorded at their fair market value at the date of the gift.

**RURAL ADVANCEMENT FOUNDATION INTERNATIONAL – USA
AND AFFILIATE**

NOTES TO FINANCIAL STATEMENTS

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SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

E. Promises to Give.

Unconditional promises to give are recognized as support and assets in the period received. Conditional promises to give are recognized when the conditions upon which they depend are substantially met. The Organization provides an allowance for doubtful accounts equal to the estimated losses that are expected to be incurred in their collection. No allowance is deemed necessary at December 31, 2011 and 2010. The promises to give are expected to be collected within one year and are recorded at their net realizable value.

F. Grants and Contracts Receivable.

Grants and contracts receivable are carried at the estimated collectible amount. The Organization uses the reserve method to account for bad debts. An allowance is recorded based on management's estimates of the collectability of the grants and contracts receivable balances. No allowance is deemed necessary at December 31, 2011 and 2010. The receivables are expected to be collected within one year.

G. Property and Equipment.

Property and equipment are stated at cost for purchased assets and at market value on the date of the gift for donated assets. Property and equipment are capitalized if their life is expected to be greater than one year and if their cost exceeds \$1,000. Depreciation is calculated using the straight-line method over estimated lives of 3 to 5 years for office equipment, 5 to 7 years for furniture and fixtures, 7 years for building improvements, and 40 years for building.

The Organization reports gifts of land, buildings, and equipment as unrestricted support unless explicit donor 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 stipulations about how long those long-lived assets must be maintained, the Organization reports expirations of donor restrictions when the donated or acquired long-lived assets are placed in service.

**RURAL ADVANCEMENT FOUNDATION INTERNATIONAL – USA
AND AFFILIATE**

NOTES TO FINANCIAL STATEMENTS

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SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

H. Net Assets.

Unrestricted - Resources of the Organization that are not restricted by donors or grantors as to use or purpose. These resources include amounts generated from operations, undesignated gifts, and investments in property and equipment.

Temporarily Restricted - Resources that carry a donor-imposed restriction that permits the Organization to use or expend the donated assets as specified for which the restrictions are satisfied by the passage of time or by actions of the Organization.

Permanently Restricted - Resources that carry a donor-imposed restriction that stipulates that donated assets be maintained in perpetuity, but may permit the Organization to use or expend part or all of the income derived from the donated assets.

I. Fair Value of Financial Instruments.

U.S. GAAP requires the Organization to disclose estimated fair values for its financial instruments. The carrying amount of financial instruments approximates fair value because of the short maturities of the instruments held.

J. Marketing and Promotion Costs.

Marketing and promotion costs are expensed as incurred.

K. Income Taxes.

RAFI-USA is an exempt organization under Section 501(c)(3) of the Internal Revenue Code, and is classified as other than a private foundation.

RAI is an exempt organization under Section 501(c)(3) of the Internal Revenue Code, and is classified as other than a private foundation.

L. Estimates.

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Accordingly, actual results could differ from those estimates.

**RURAL ADVANCEMENT FOUNDATION INTERNATIONAL – USA
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NOTES TO FINANCIAL STATEMENTS

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CHARITABLE GIFT ANNUITY

In 2002, the Organization was named a recipient of a charitable gift annuity with a market value at the date of gift totaling approximately \$11,000. The trust agreement specifies that payments be made to another beneficiary over the life of that beneficiary. At the termination of the agreement, the remaining assets will pass to the donee organization. The fair market value of net assets held in the charitable gift annuity totaled \$10,083 and \$12,938, at December 31, 2011 and 2010, respectively. A corresponding liability was recorded for the payment of \$1,071 to the beneficiary at December 31, 2011 and 2010, utilizing present value techniques and a discount rate of 0% based on actuarial assumptions, including life expectancy.

FAIR VALUE OF ASSETS

U.S. GAAP defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. It also establishes a fair value hierarchy for inputs used in measuring fair value that maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that the most observable inputs be used when available. Observable inputs are those that market participants would use in pricing the asset or liability based on market data obtained from sources independent of the Organization. Unobservable inputs reflect the Organization's assumptions about the inputs market participants would use in pricing the asset or liability developed based on the best information available in the circumstances.

The fair value hierarchy is categorized into three levels based on the inputs as follows:

Level 1 – Valuations based on adjusted quoted prices in active markets for identical assets as of the reporting date.

Level 2 - Valuations based on inputs other than quoted prices included, which are either directly or indirectly observable as of the reporting date, are valued at prices for similar assets or liabilities in markets not active, or determined through the use of models or other valuation methodologies.

Level 3 - Pricing inputs are unobservable and include situations where there is little, if any, market activity for the asset. Fair value for these assets is determined using valuation methodologies that consider a range of factors, including but not limited to the price at which the asset was acquired, the nature of the asset, local market conditions, trading values on public exchanges for comparable securities, current and projected operating performance, and financing transactions subsequent to the acquisition of the asset. The inputs into the determination of fair value require significant management judgment. Due to the inherent uncertainty of these estimates, these values may differ materially from the values that would have been used had a ready market for these assets existed.

**RURAL ADVANCEMENT FOUNDATION INTERNATIONAL – USA
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NOTES TO FINANCIAL STATEMENTS

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FAIR VALUE OF ASSETS (CONTINUED)

The Organization's charitable gift annuity is classified as Level 1. No assets or liabilities were classified as Level 2 or 3.

There were no changes during the year ended December 31, 2011, to the Organization's valuation techniques used to measure asset values on a recurring basis.

The following tables summarize the assets of the Organization for which fair values are determined on a recurring basis at December 31, 2011 and 2010. As required by U.S. GAAP, assets are classified in their entirety based on the lowest level of input that is significant to the fair value measurement.

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
<u>December 31, 2011</u>				
Charitable gift annuity:				
Smallcap World Fund Class A:	<u>\$ 10,083</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 10,083</u>
	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
<u>December 31, 2010</u>				
Charitable gift annuity:				
Smallcap World Fund Class A:	<u>\$ 12,938</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 12,938</u>

CONTRACTS RECEIVABLE

Contracts receivable consists of the following at December 31, 2011 and 2010:

	<u>2011</u>	<u>2010</u>
Southern Risk Management Education Center	\$ 23,877	\$ -
North Carolina State University	4,513	4,998
Farmers Legal Action Group	500	2,500
Northeast Organic Dairy Producers Alliance	-	3,000
	<u>\$ 28,890</u>	<u>\$ 10,498</u>

**RURAL ADVANCEMENT FOUNDATION INTERNATIONAL – USA
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NOTES TO FINANCIAL STATEMENTS

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GRANTS RECEIVABLE

Grants receivable consists of the following at December 31, 2011 and 2010:

	2011	2010
The N.C. Tobacco Trust Fund Commission	\$ 277,784	\$ 2,258,128
Duke Endowment/United Conference of Methodists	25,000	-
Lawson Valentine Foundation	25,000	75,000
Branch Banking and Trust Company	20,000	20,000
The Rural Economic Development Center, Inc.	11,575	346,350
Tides Foundation	10,000	-
Mary Lynn Richardson Fund	10,000	20,000
The Golden LEAF Foundation	-	180,000
Z Smith Reynolds Foundation	-	60,000
First Citizens Bank	-	1,500
National Family Farm Coalition	-	182
	<u>\$ 379,359</u>	<u>\$ 2,961,160</u>

A grant receivable totaling \$127,785 and \$2,258,128 at December 31, 2011 and 2010, respectively, from The N.C. Tobacco Trust Fund Commission is included in grants receivable on the consolidated statement of financial position. Grant payments were received in advance for the first half of the grant period. During 2010 the advanced funding was fully expended, and grant payments began on the reimbursement basis. In accordance with the terms of the grant agreement, the receivable has been reduced by interest income of \$484 and \$3,140, earned for the years ended December 31, 2011 and 2010, respectively. The interest was earned on the initial advance payment of grant funds received in July 2008.

LINE OF CREDIT

The Organization has a \$150,000 line of credit with a financial institution secured by real estate. The interest rate is at prime with a minimum rate of 4.00% and a maximum rate of 8.00%. The rate at December 31, 2011 and 2010, was 4.00%. The outstanding balance at December 31, 2011, is \$150,000. There was no outstanding balance at December 31, 2010.

DEFERRED COMPENSATION

After seven years of service, and upon completion of each subsequent seven years of service, employees are entitled to a sabbatical leave of up to twelve weeks pay or twelve weeks paid time off. The Organization reserves the right to determine when the leave can be taken or paid.

**RURAL ADVANCEMENT FOUNDATION INTERNATIONAL – USA
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NOTES TO FINANCIAL STATEMENTS

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DEFERRED COMPENSATION (CONTINUED)

Sabbatical leave is classified as deferred compensation – current maturity and deferred compensation – net of current maturity in the consolidated statement of financial position based on the timing of the employees' estimated time off.

Employees with ten years of service receive a lump sum payment equal to 10% of their salary for future health insurance coverage and expenses upon retiring from service to the Organization. Health insurance assistance is classified as deferred compensation – current and deferred compensation – net of current maturity in the consolidated statement of financial position based on the timing of the employees' expected retirement.

Deferred compensation totaled \$66,780 and \$69,722, at December 31, 2011 and 2010, respectively.

DONATED SERVICES

The Organization recognizes donated services that create or enhance nonfinancial assets or that require specialized skills, and would typically need to be purchased if not provided by donation. The Organization recognized donated professional services totaling \$88,939 and \$23,926, during the years ended December 31, 2011 and 2010, respectively.

RETIREMENT PLAN

Effective January 1, 2009, the Organization implemented a 401(k) plan. The plan covers all employees at the time of hire. The Organization may contribute a matching contribution to each employee's plan as determined by the Board of Directors annually for employees who have reached 520 hours (13 weeks) of service. Contributions by the Organization for the years ended December 31, 2011 and 2010, totaled \$25,551 and \$23,313, respectively, and are included in accounts payable on the consolidated statement of financial position.

LEASE COMMITMENTS

The Organization leases a postage meter over a 36-month period, with quarterly payments of \$447, expiring in July 2012. The Organization leases a copier over a 60-month period, with monthly payments of \$471, expiring in June 2016. Total lease expense for the years ended December 31, 2011 and 2010, totaled \$6,935 and \$6,132, respectively.

**RURAL ADVANCEMENT FOUNDATION INTERNATIONAL – USA
AND AFFILIATE**

NOTES TO FINANCIAL STATEMENTS

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LEASE COMMITMENTS (CONTINUED)

Future minimum lease payments are as follows:

<u>Year ending December 31,</u>	
2012	\$ 6,546
2013	5,652
2014	5,652
2015	5,652
2016	<u>2,826</u>
Total minimum lease payments	<u>\$ 26,328</u>

In prior years, the Organization leased an office space in Washington, DC, with a one year term renewing each year. This space was subleased to a tenant with identical terms. The Organization cancelled this lease in March 2011. Net rental income and expense for the leasing arrangement for the years ended December 31, 2011 and 2010, totaled \$3,769 and \$9,391, respectively.

The Organization also leases office space and the conference center to tenants under operating leases with one year terms. Rental income for the years ended December 31, 2011 and 2010, totaled \$22,125 and \$26,396, respectively.

ALLOCATION OF EXPENSES

Expenses, not specifically identified by type, are allocated between program, general and administrative, and fundraising expenses using the following methods. Expenses associated with occupancy are allocated based upon the square footage used by the program, management, and administrative personnel. All other expenses are allocated based upon estimates made by the Organization's management. Functional expenses fluctuate annually based on the priorities of the Organization.

CONTINGENCIES

The Organization has received proceeds from state and private foundation grants. Periodic audits of these grants are possible, and certain costs may be questioned as not being appropriate under the grant agreements. Such audits could result in the refund of grant monies to the grantor agencies. Management believes that any required refunds are unlikely, and in any event would be immaterial. No provision has been made in the accompanying financial statements for the refund of grant monies due to questioned costs.

**RURAL ADVANCEMENT FOUNDATION INTERNATIONAL – USA
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TEMPORARILY RESTRICTED NET ASSETS

Temporarily restricted net assets are available for the following purposes at December 31, 2011 and 2010:

	<u>2011</u>	<u>2010</u>
Purpose Restricted:		
Tobacco Communities and Ag Enterprise Development	\$ 446,445	\$ 2,619,604
Just Foods	82,302	10,809
Contract Agriculture Reform	46,500	25,500
Farm Sustainability	44,663	297,458
General and administrative - board meetings	8,223	-
	<u>628,133</u>	<u>2,953,371</u>
Time Restricted:		
Unrestricted promises to give	1,799	500
Grants receivable	51,000	130,000
	<u>52,799</u>	<u>130,500</u>
Total temporarily restricted net assets	<u>\$ 680,932</u>	<u>\$ 3,083,871</u>

INCOME TAXES

In accordance with Financial Accounting Standards Board Accounting Standards Codification (“ASC”) 740-10 *Accounting for Income Taxes*, the Organization reflects in the financial statements the benefit of positions taken in a previously filed tax return or expected to be taken in a future tax return only when it is considered ‘more-likely-than-not’ that the position taken will be sustained by a taxing authority. The Organization evaluates its uncertain tax positions using provisions of ASC 450, *Contingencies*. Accordingly, a loss contingency is recognized when it is probable that a liability has been incurred as of the date of the financial statements and the amount of the loss can be reasonably estimated. The amount recognized is subject to estimate and management judgment with respect to the likely outcome of each uncertain tax position. The amount that is ultimately sustained for an individual uncertain tax position or for all uncertain tax positions in the aggregate could differ from the amount recognized.

**RURAL ADVANCEMENT FOUNDATION INTERNATIONAL – USA
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NOTES TO FINANCIAL STATEMENTS

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INCOME TAXES (CONTINUED)

If applicable, penalties and interest assessed by income taxing authorities are included in general and administrative expenses. Under the statute of limitations, the tax returns of the Organization for 2008 through 2011 are subject to examination by taxing authorities. Management evaluated tax positions for the 2008 through 2011 returns, and concluded that there are no uncertain tax positions and believes there is no income tax effect on the financial statements.

PRIOR YEAR INFORMATION

The statements of activities and changes in net assets, and functional expenses include certain prior-year summarized comparative information in total but not by net asset class and functional category, respectively. Such information does not include sufficient detail to constitute a presentation in conformity with accounting principles generally accepted in the United States of America. Accordingly, such information should be read in conjunction with the Organization's financial statements for the year ended December 31, 2010, from which the summarized information was derived.

RESTATEMENT

It was noted during 2011 that temporarily restricted funds had been misclassified in 2010 resulting in December 31, 2010, unrestricted net assets being overstated and temporarily restricted net assets being understated. Accordingly, an adjustment of \$15,500 has been made to decrease the December 31, 2010, unrestricted net assets with a corresponding increase in temporarily restricted net assets. Unrestricted and temporarily restricted net assets at December 31, 2010, were originally reported as \$1,213,515 and \$3,068,371, respectively. The restated balances are \$1,198,015 and \$3,083,871, respectively. The restatement had no effect on total net assets.

RECLASSIFICATION

Certain reclassifications to the 2010 presentation have been made to conform to the 2011 presentation. Such reclassifications had no effect on net assets.

SUBSEQUENT EVENTS

Management has evaluated subsequent events for recognition or disclosure through May 2, 2012, the date the financial statements were available to be issued. Management did not identify any events that occurred subsequent to year-end that require disclosure in the financial statements.

RURAL ADVANCEMENT FOUNDATION INTERNATIONAL - USA

SCHEDULE OF STATE AWARDS

For the Year Ended December 31, 2011

<u>State Grantor Program Title</u>	<u>Project Number</u>	<u>Receipts</u>	<u>Expenditures</u>
The North Carolina Tobacco Trust Fund Commission			
Tobacco Communities Reinvestment Project	2008 (OC)-C01-02	\$ 2,130,470	\$ 2,111,867
Tobacco Communities Reinvestment Project	2011-052-20	150,000	-
		2,280,470	2,111,867
The North Carolina Tobacco Trust Fund Commission			
The Golden LEAF Foundation			
The Crop Insurance Feasibility Project	N/A	5,000	-
The Crop Insurance R&D Institute Project	N/A	175,000	146,839
		180,000	146,839
The State of North Carolina			
Pass through from the North Carolina			
Rural Economic Development Center, Inc.			
Family Farm Innovation Fund Program	2011-010-50401-104	331,650	352,225
North Carolina Rural Economic Development Center, Inc.			
Crop Insurance for Strawberry Growers	2011-208-50401-102	24,000	30,000
		\$ 2,816,120	\$ 2,640,931
TOTAL STATE AWARDS		\$ 2,816,120	\$ 2,640,931

NOTES TO SCHEDULE OF STATE AWARDS

This schedule includes the state grant activity of Rural Advancement Foundation International - USA and its affiliate, Rural Advancement Institute, and is presented on the cash basis of accounting. Consequently, receipts are recognized when received rather than when earned, and expenditures are recognized when paid rather than when the obligations are incurred. The information is presented in accordance with the requirements of *Government Auditing Standards*.

BLACKMAN & SLOOP, CPAs, P.A.

Certified Public Accountants
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**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**

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Board of Directors
Rural Advancement Foundation International - USA
and Affiliate
Pittsboro, North Carolina

We have audited the financial statements of Rural Advancement Foundation International - USA and its affiliate, Rural Advancement Institute, as of and for the year ended December 31, 2011, and have issued our report thereon dated May 2, 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 Rural Advancement Foundation International - USA and its affiliate, Rural Advancement Institute, is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered Rural Advancement Foundation International - USA and its affiliate, Rural Advancement Institute'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 Rural Advancement Foundation International - USA and its affiliate, Rural Advancement Institute's, internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Organization'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 combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the Organization's financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of 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 the deficiencies in 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 material weaknesses, as defined above. However, we identified certain deficiencies in internal control over financial reporting described in the accompanying schedule of findings that we consider to be significant deficiencies in internal control over financial reporting (2011-01). 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.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Rural Advancement Foundation International - USA and its affiliate, Rural Advancement Institute'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 no instances 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.

Rural Advancement Foundation International - USA and its affiliate, Rural Advancement Institute's, response to the finding identified in our audit is described in the accompanying schedule of findings and responses. We did not audit Rural Advancement Foundation International - USA and its affiliate, Rural Advancement Institute's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of management, others within the entity, the Board of Directors, funding agencies, and the Office of State Auditor, and is not intended to be and should not be used by anyone other than these specified parties.

Blackman & Sloop

Chapel Hill, North Carolina
May 2, 2012

**RURAL ADVANCEMENT FOUNDATION INTERNATIONAL - USA
AND AFFILIATE**

SCHEDULE OF FINDINGS AND RESPONSES

Year Ended December 31, 2011

2011-01 Preparation of Financial Statements.

Condition and Criteria: As part of the audit, management requested us to prepare a draft of the financial statements, including the related notes to financial statements. Management reviewed, approved, and accepted responsibility for those financial statements prior to their issuance; however, management does not have access to tools to evaluate the completeness of financial statement disclosures.

Recommendation: We recommend the Organization continue to seek consultation for guidance on the proper treatment and disclosure of financial transactions and technical issues. In addition, we recommend the Organization continue to utilize the current disclosure checklist from the AICPA to ensure propriety and completeness of the footnotes.

Management Response: Management has consulted with an external accounting firm to prepare the Organization's draft financial statements for 2011 and accompanying footnotes. This is done to improve the efficiency of the process. Management will continue to consult regularly with the external accounting firm, and solicit their expertise and guidance on new and ongoing matters.

**RURAL ADVANCEMENT FOUNDATION INTERNATIONAL - USA
AND AFFILIATE**

SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS AND RESPONSES

Year Ended December 31, 2011

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2010-01 Preparation of Financial Statements.

Condition and Criteria: As part of the audit, management requested us to prepare a draft of the financial statements, including the related notes to financial statements. Management reviewed, approved, and accepted responsibility for those financial statements prior to their issuance; however, management does not have access to tools to evaluate the completeness of financial statement disclosures.

Recommendation: We recommend the Organization continue to seek consultation for guidance on the proper treatment and disclosure of financial transactions and technical issues. In addition, we recommend the Organization continue to utilize the current disclosure checklist from the AICPA be used to ensure propriety and completeness of the footnotes.

Management Response: Management has consulted with an external accounting firm to prepare the Organization's draft financial statements for 2010 and accompanying footnotes. This is done to improve the efficiency of the process. Management will continue to consult regularly with the external accounting firm and solicit their expertise and guidance on new and ongoing matters. Management will also review the current disclosure checklist from the AICPA to ensure the propriety and completeness of the footnotes.

Current Status: The Organization requested that the audit firm prepare a draft of the financial statements and related notes for 2010, and will do so again for 2011. The Organization consulted regularly with the audit firm throughout the year for its expertise and guidance on transactions and technical issues and new and ongoing matters.

**RURAL ADVANCEMENT FOUNDATION INTERNATIONAL - USA
AND AFFILIATE**

SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS AND RESPONSES

Year Ended December 31, 2011

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2010-02 Security Over Physical Assets.

Condition and Criteria: Various employees have copies of the same key which accesses their offices. For a period during the year, blank checks were kept in one of these offices in an unlocked drawer. There is not a separate key restricting access to blank checks which increases the risk for misappropriation of assets.

Recommendation: We recommend the blank checks be maintained in a locked drawer or file cabinet to reduce the risk of misappropriation of assets.

Management Response: Upon discussion with the auditors, management agreed that there needed to be controls in place over the physical access to the blank checks. In December 2010, the blank checks were moved to a locked file cabinet that is maintained in the Financial Officer's office. Access to the file cabinet is limited to three personnel: the Financial Officer, the Director of Administration, and the Executive Director. The Financial Officer's office is also locked overnight.

Current Status: Management implemented additional controls over the physical access to the blank checks in December 2010. These controls remained in effect for the full 2011 fiscal year.