

INDEPENDENT AUDITORS' REPORT

**Board of Directors
National Endowment for Democracy
Washington, D.C.**

We have audited the accompanying statements of financial position of the National Endowment for Democracy (the Endowment) as of September 30, 2007, and the related statements of activities and changes in net assets and cash flows for the year then ended. These financial statements are the responsibility of the Endowment's management. Our responsibility is to express an opinion on these financial statements based on our audit. The financial statements as of September 30, 2006 were audited by other auditors, whose report thereon dated January 5, 2007 expressed an unqualified opinion on those statements.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Endowment's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by the Endowment's 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 financial statements referred to above present fairly, in all material respects, the financial position of the National Endowment for Democracy as of September 30, 2007, 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.

Calibre CPA Group, PLLC

Washington, DC

January 10, 2008

STATEMENTS OF FINANCIAL POSITION AS OF SEPTEMBER 30, 2007 AND 2006

	<u>2007</u>	<u>2006</u>
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	\$ 1,033,693	\$ 1,983,264
Investments	680,746	611,909
Accounts receivable	-	780
Grants receivable	116,197,874	117,604,402
Prepaid and other assets	<u>35,545</u>	<u>18,977</u>
Total current assets	117,947,858	120,219,332
FURNITURE, EQUIPMENT AND LEASEHOLD IMPROVEMENTS, NET		
	<u>4,150,998</u>	<u>4,678,115</u>
TOTAL	<u>\$ 122,098,856</u>	<u>\$ 124,897,447</u>
LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES:		
Accounts payable and accrued liabilities	\$ 1,828,663	\$ 1,658,025
Grants payable	78,294,882	76,639,694
Deferred grant revenue—government agencies	36,169,284	40,653,561
Capital lease obligations - current portion	45,464	44,935
Deferred rent obligation - current portion	<u>300,218</u>	<u>300,218</u>
Total current liabilities	<u>116,638,511</u>	<u>119,296,433</u>
LEASE OBLIGATIONS, NON-CURRENT PORTION		
Capital leases	34,557	79,814
Deferred rent obligation	<u>2,967,982</u>	<u>3,025,360</u>
Total non-current liabilities	<u>3,002,539</u>	<u>3,105,174</u>
Total liabilities	<u>119,641,050</u>	<u>122,401,607</u>
NET ASSETS:		
Unrestricted	1,103,205	1,320,517
Temporarily restricted	<u>1,354,601</u>	<u>1,175,323</u>
Total net assets	<u>2,457,806</u>	<u>2,495,840</u>
TOTAL LIABILITIES AND NET ASSETS	<u>\$ 122,098,856</u>	<u>\$ 124,897,447</u>

See accompanying notes to financial statements.

STATEMENTS OF ACTIVITIES AND CHANGES IN NET ASSETS FOR THE YEARS ENDED SEPTEMBER 30, 2007 AND 2006

	2007			2006		
	Unrestricted	Temporarily Restricted	Total	Unrestricted	Temporarily Restricted	Total
SUPPORT AND REVENUE:						
Grant revenue—government agencies	\$106,408,363	\$ —	\$106,408,363	\$109,565,437	\$ —	\$109,565,437
Other grants and contributions	—	334,595	334,595	—	547,650	547,650
Other revenue, interest, and miscellaneous income	173,500	68,837	242,337	177,405	41,177	218,582
Total support and revenue	106,581,863	403,432	106,985,295	109,742,842	588,827	110,331,669
NET ASSETS RELEASED FROM RESTRICTIONS—						
Satisfaction of program restrictions	224,154	(224,154)	—	785,965	(785,965)	—
Total revenues	106,806,017	179,278	106,985,295	110,528,807	(197,138)	110,331,669
EXPENSES:						
Program services:						
Grant programs:						
Federal	90,476,556	—	90,476,556	93,999,784	—	93,999,784
Other activities—Non-Federal						
International Forum						
Management and support	8,074	—	8,074	8,325	—	8,325
<i>Journal of Democracy</i>	78,635	—	78,635	74,820	—	74,820
Research and conferences	18,775	—	18,775	32,600	—	32,600
World Movement for Democracy	2,208	—	2,208	732,039	—	732,039
NED events and development	124,538	—	124,538	145,576	—	145,576
Total other activities—Non-Federal	232,230	—	232,230	993,360	—	993,360
Other activities—Federal						
International Forum						
<i>Journal of Democracy</i>	324,820	—	324,820	290,071	—	290,071
Democracy Resource Center	357,963	—	357,963	300,865	—	300,865
Research and conferences	149,474	—	149,474	124,650	—	124,650
Management and support	352,706	—	352,706	442,259	—	442,259
Reagan/Fascell Fellowship Program	1,137,660	—	1,137,660	1,292,738	—	1,292,738
World Movement for Democracy	543,974	—	543,974	640,831	—	640,831
World Movement for Democracy—						
NDRI Program	—	—	—	43,437	—	43,437
World Movement for Democracy—						
Network Program	55,304	—	55,304	94,374	—	94,374
World Movement for Democracy—						
MEPI Program	71,497	—	71,497	—	—	—
World Movement for Democracy—						
Defending Civil Society	84,467	—	84,467	—	—	—
Center for International Media Assistance	489,504	—	489,504	—	—	—
Total other activities—Federal	3,567,369	—	3,567,369	3,229,225	—	3,229,225
Supporting services—Federal	12,747,174	—	12,747,174	11,206,788	—	11,206,788
Total other activities and supporting services	16,546,773	—	16,546,773	15,429,373	—	15,429,373
Total expenses	107,023,329	—	107,023,329	109,429,157	—	109,429,157
CHANGES IN NET ASSETS	(217,312)	179,278	(38,034)	1,099,650	(197,138)	902,512
NET ASSETS—Beginning of year	1,320,517	1,175,323	2,495,840	220,867	1,372,461	1,593,328
NET ASSETS—End of year	\$ 1,103,205	\$ 1,354,601	\$ 2,457,806	\$ 1,320,517	\$ 1,175,323	\$ 2,495,840

See accompanying notes to financial statements.

STATEMENTS OF CASH FLOWS FOR THE YEARS ENDED SEPTEMBER 30, 2007 AND 2006

	<u>2007</u>	<u>2006</u>
CASH FLOWS FROM OPERATING ACTIVITIES:		
Changes in net assets	\$ (38,034)	\$ 902,512
Adjustments to reconcile change in net assets to net cash (used in) provided by operating activities:		
Depreciation and amortization	664,463	245,886
Loss on disposal of furniture and equipment	-	7,233
Net appreciation in fair value of investments	(46,914)	(41,177)
Changes in assets and liabilities:		
Grants receivable	1,406,528	(184,283)
Accounts receivable	780	1,543
Prepaid expenses	(16,568)	106,903
Accounts payable and accrued liabilities	170,638	763,948
Grants payable	1,655,188	3,192,133
Deferred grant revenue—government agencies	(4,484,277)	(3,688,787)
Deferred rent obligation	(57,378)	323,402
	<u>(745,574)</u>	<u>1,629,313</u>
CASH FLOWS USED IN INVESTING ACTIVITIES:		
Purchases of furniture and equipment	(137,346)	(535,421)
Purchases of leasehold improvements	-	(1,123,430)
Purchases of investments	(21,923)	(570,732)
	<u>(159,269)</u>	<u>(2,229,583)</u>
CASH FLOWS USED IN FINANCING ACTIVITIES:		
Principal payments under capital lease obligations	(44,728)	(47,311)
	<u>(949,571)</u>	<u>(647,581)</u>
NET DECREASE IN CASH AND CASH EQUIVALENTS	(949,571)	(647,581)
CASH AND CASH EQUIVALENTS—Beginning of year	<u>1,983,264</u>	<u>2,630,845</u>
CASH AND CASH EQUIVALENTS—End of year	<u>\$ 1,033,693</u>	<u>\$ 1,983,264</u>
SUPPLEMENTAL DISCLOSURE OF NON-CASH INVESTING AND FINANCING ACTIVITIES:		
Acquisition of equipment under capital lease	<u>\$ -</u>	<u>\$ 54,746</u>
Deferred rent obligation—leasehold improvements	<u>\$ -</u>	<u>\$ 3,002,176</u>
CASH PAYMENTS FOR INTEREST	<u>\$ 9,524</u>	<u>\$ 10,367</u>

See accompanying notes to financial statements.

NOTES TO FINANCIAL STATEMENTS AS OF AND FOR THE YEARS ENDED SEPTEMBER 30, 2007 AND 2006

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization — The National Endowment for Democracy (the “Endowment”) is a private, not-for-profit organization headquartered in Washington, D.C. The Endowment was established coincident to a grant awarded by the United States Information Agency (“USIA”) as mandated by the National Endowment for Democracy Act (the “Act”) of the United States Congress. The purpose of the Endowment is to encourage free and democratic institutions throughout the world through activities that promote individual rights and freedoms. The Endowment awards grants to organizations with programs consistent with its objectives. On October 1, 1999, USIA and the U.S. Department of State (“USDOS”) consolidated. Accordingly, the Endowment receives funding for its annual Congressional Appropriation and other special federal funding from the USDOS.

Basis of Presentation — The accounts of the Endowment are maintained and the financial statements have been prepared on the accrual basis of accounting. The Endowment reports to the U.S. Government on the basis of obligations incurred and cash expenditures made.

Use of Estimates — The preparation of 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 financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash and Cash Equivalents — Cash and cash equivalents include cash on deposit, overnight repurchase agreements, and investments in money market accounts that are reported at cost and are readily convertible to known amounts of cash. Such instruments have maturities of three months or less from the date of purchase.

Investments — Investments are carried at fair value with any related gain or loss reported in the statements of activities and changes in net assets. The Endowment’s investments consist entirely of mutual funds.

Furniture, Equipment and Leasehold Improvements — Furniture, equipment and leasehold improvements are recorded at cost and are depreciated or amortized on the straight-line method over their estimated service lives or the term of the lease, as applicable, ranging from three to ten years.

Grants Receivable — Federal Appropriation and Special Funding — At the time a grant agreement is signed and awarded to the Endowment, a receivable and deferred revenue are recorded. When payments are received from the awarding agency, the receivable is reduced. The deferred revenue is recognized as revenue in accordance with the Endowment’s revenue recognition policy.

Revenue Recognition — Grants received from government agencies specify the periods in which monies are to be expended. Additionally, certain government grants restrict the use of funds for programs in specific countries. Revenues from government grants are recognized as earned in the year in which the Endowment obligates the funds for the intended purpose which is set forth in the grant agreement.

Agreements with the former USIA, USAID and USDOS provide for the subsequent audit of costs funded under the grant agreements. It is the policy of the Endowment to provide for cost disallowances based upon its experience in previous grant audits.

Deferred Grant Revenue — Government Agencies — Resources awarded in the form of federal grant agreements made to the Endowment in excess of obligations incurred are recorded as deferred grant revenue - federal appropriation and special funding.

Contributions — The Endowment 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 in the statement of activities as net assets released from restrictions. Income on these net assets is classified as temporarily restricted or unrestricted in accordance with the donor’s stipulation.

2. GRANTS RECEIVABLE

Grants receivable are from the U.S. Government and represent balances of Federal Reserve Letters of Credit and direct funding established by the former USIA, USAID and USDOS grant agreements. The Endowment collects U.S. Government funds by filing requests for direct funding and by presenting payment vouchers against letters of credit when it disburses cash for program grants and administrative costs.

3. FURNITURE, EQUIPMENT AND LEASEHOLD IMPROVEMENTS

Furniture, equipment and leasehold improvements less accumulated depreciation and amortization as of September 30, 2007 and 2006 is as follows:

	<u>2007</u>	<u>2006</u>
Furniture and equipment	\$ 781,075	\$ 745,859
Equipment under capital lease	222,311	222,311
Leasehold improvements	<u>4,125,605</u>	<u>4,125,605</u>
Total	5,128,991	5,093,775
Less accumulated depreciation and amortization	<u>(977,993)</u>	<u>(415,660)</u>
Furniture, equipment and leasehold improvements—net	<u>\$4,150,998</u>	<u>\$4,678,115</u>

4. GRANTS PAYABLE

Grants payable represent the undisbursed balances of funds obligated to the Endowment's grantees. Grantee organizations are entitled to collect grant funds as needed by presenting requests for funds to the Endowment. Such grants payable are generally disbursed within a 12-month period after the funds have been obligated to the Endowment's grantees.

5. DEFERRED GRANT REVENUE—GOVERNMENT AGENCIES

Changes in deferred grant revenue from agencies of the U.S. Government as of and for the years ended September 30, 2007 and 2006, are summarized in the following schedule:

	<u>2007</u>	<u>2006</u>
Deferred revenue, beginning of year	\$ 40,653,561	\$ 44,342,348
Grants awarded/amended	101,927,600	105,671,100
Grants obligated	(106,408,363)	(109,565,437)
Grants adjustments	<u>(3,514)</u>	<u>205,550</u>
Deferred revenue, end of the year	<u>\$ 36,169,284</u>	<u>\$ 40,653,561</u>