N-VIRO INTERNATIONAL CORP
Form 10-K
March 30, 2012

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

(Mark One)
[X] ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2011
or

[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from ____________ to ____________

Commission File Number: 0-21802

N-VIRO INTERNATIONAL CORPORATION
(Exact name of registrant as specified in its charter)

Delaware	34-1741211
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
2254 Centennial Road Toledo, Ohio	43617
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: (419) 535-6374

Securities registered pursuant to Section 12(b) of the Exchange Act: None

Securities registered pursuant to Section 12(g) of the Act: Common Stock, par value $.01 per share

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes [ ] No [X]

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Exchange Act. Yes [ ] No [X]

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for at least the past 90 days. Yes [X] No [ ]

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes [X] No [ ]

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. [ ]

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer	Accelerated filer
Non-accelerated filer	Smaller reporting company [X]

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).Yes [ ] No [X]

State the aggregate market value of the voting and non-voting common equity held by non-affiliates computed by reference to the price at which the common equity was last sold, or the average bid and asked price of such common equity, as of the last business day of the registrant's most recently completed second fiscal quarter: $11,519,000.

The number of shares of Common Stock of the registrant outstanding as of March 5, 2012 was 6,083,624.

DOCUMENTS INCORPORATED BY REFERENCE

None

INDEX

PART I

PART III

PART IV

PART I

Cautionary Statement with Respect to Forward-Looking Statements

This annual report on Form 10-K contains statements that are forward-looking. We caution that words used in this document such as “expects,” “anticipates,” “believes,” “may,” and “optimistic,” as well as similar words and expressions us herein, identify and refer to statements describing events that may or may not occur in the future. These forward-looking statements and the matters to which they refer are subject to considerable uncertainty that may cause actual results to be materially different from those described herein. There are numerous factors that could cause actual results to be different than those anticipated or predicted by us, including: (i) a deterioration in economic conditions in general; (ii) a decrease in demand for our products or services in particular; (iii) our loss of a key employee or employees; (iv) regulatory changes, including changes in environmental regulations, that may have an adverse affect on the demand for our products or services; (v) increases in our operating expenses resulting from increased costs of labor and/or consulting services; (vi) our inability to exploit existing or secure additional sources of revenues or capital to fund operations; (vii) a failure to collect upon or otherwise secure the benefits of existing contractual commitments with third parties, including our customers; and (viii) other factors and risks identified in this Form 10-K, including under the caption "Risk Factors." This list provides examples of factors that could affect the results described by forward-looking statements contained in this Form 10-K; however, this list is not exhaustive. Many other factors could impact our business and it is impossible to predict with any accuracy which factors could result in negative impacts. Although we believe that the forward-looking statements contained in this Form 10-K are reasonable, we cannot provide you with any guarantee that the anticipated results will not be adverse and that the anticipated results will be achieved. All forward-looking statements in this Form 10-K are expressly qualified in their entirety by the cautionary statements contained in this section and you are cautioned not to place undue reliance on the forward-looking statements contained in this Form 10-K. In addition to the risks listed above, other risks may arise in the future, and we disclaim any obligation to update information contained in any forward-looking statement.

Item 1. Business

General

We were incorporated in Delaware in April 1993, and became a public company in October 1993. We own and sometimes license various N-Viro processes and patented technologies to treat and recycle wastewater and other bio-organic wastes, utilizing certain alkaline and mineral by-products produced by the cement, lime, electrical generation and other industries. To date, the N-Viro Process has been commercially utilized for the recycling of wastewater sludge from municipal wastewater treatment facilities. All N-Viro products produced according to the N-Viro Process specifications, are "exceptional quality" sludge products under the 40 CFR Part 503 Sludge Regulations promulgated under the Clean Water Act of 1987 (the "Part 503 Regs").

Our current business strategy is to market our N-Viro FuelTM technology, which produces a renewable alternative fuel product out of certain bio-organic wastes. This N-Viro Fuel process has been acknowledged by the USEPA as a fuel product that can be used to produce alternative energy. In this business strategy, the primary focus is to identify allies, public and private, which will allow the opportunity for N-Viro to build, own and operate N-Viro Fuel facilities either on its own or in concert with others.

In 2011, we operated two biosolids processing facilities located in Toledo, Ohio and Volusia County, Florida. These two facilities each produce the N-Viro SoilTM agricultural product, and have provided us with working and development capital. In late 2011 we effectively ceased operations at the Toledo facility, and our goal is to continue to operate thethe Florida facility and aggressively market our N-Viro Fuel technology. These patented processes are best suited for current and future demands, satisfying both waste treatment needs as well as domestic and international directives for clean, renewable alternative fuel sources.

The N-Viro Process

The N-Viro Soil Process involves mixing wastewater residuals (sludge) with an alkaline admixture and then subjecting the mixture to a controlled period of storage, mechanical turning and accelerated drying. The N-Viro Process stabilizes and pasteurizes the wastewater residuals, reduces odors to acceptable levels, neutralizes or immobilizes various constituents and generates N-Viro Soil™, a product which has a granular appearance similar to soil and has multiple agricultural uses. N-Viro and its licensees have successfully marketed and distributed all N-Viro Soil product produced for beneficial reuse.

The alkaline products used in all N-Viro Processes consist of by-products from the cement or lime industry and certain fly ashes from coal-fired systems used in electric power generation. The particular admixture that is used usually depends upon economics and availability in local markets. We are a distributor of alkaline admixtures for others. We also work with established by-product marketers to identify and utilize available materials. We generally charge a mark-up over our cost for alkaline admixtures sold to third parties.

Our original N-Viro Process was enhanced in the 1990's with the addition of advanced mechanical drying known as the N-Viro BioDry process. BioDry had been successfully implemented in five plants operating in Canada.

N-Viro FuelTM

N-Viro Fuel™ is a relatively new and patented biomass alternative energy fuel process that produces a product that has physical and chemical characteristics similar to certain coals and is created from municipal biosolids, collectable animal manure, pulp and paper sludge and possibly other organic wastes. N-Viro Fuel is manufactured by blending the waste material(s) with one or more alkaline products, followed by thorough drying of the mixture using a thermal evaporative process. The resulting product can be easily blended with coal, waste coal, petroleum coke and/or other biomass-type fuels, and burned as a partial fuel substitute in combustion power plants. N-Viro Fuel has satisfied initial guidelines set forth by the U.S. Environmental Protection Agency (EPA) to qualify as an alternative energy source that may be utilized in commercial power generation subject to state permitting. The N-Viro Fuel technology, utilizing an alkaline/heat process to produce a fuel product, still satisfies all requirements of the USEPA 40 CFR part 503 regulations and is a safe product usable for agriculture as well as for energy production.

Our N-Viro Fuel technology can convert waste products presently being landfilled or land applied into safe, beneficial and renewable long-term energy solutions as part of a renewable-energy economy. Attaining and maintaining this status means that N-Viro Fuel technology is now a likely candidate to qualify for certain economic incentives that may be granted to alternative energy technologies, and a catalyst for obtaining permits more efficiently in each state. We plan to accelerate our development efforts as this designation is an important factor for our potential energy partners.

N-Viro Process Facilities

Our first N-Viro processing facility was located in Toledo, Ohio and was managed by us through a contract management agreement with the City of Toledo since our inception through November 2011. Revenue generated from and related to the Toledo operation accounted for about 17% of our total revenue in 2011. Under this contract, we processed Toledo's wastewater biosolids and sold the resulting N-Viro Soil product to the agricultural market throughout Northwest Ohio. The contract we operated under during most of 2011 had been extended several times, including 2004, 2009, and twice in 2010. The current extension scheduled to conclude in September 2011 was officially not renewed in October 2011, and we ceased taking Toledo's sludge in November 2011, at the end of our twenty-second year of operation.

Florida N-Viro, LP, a wholly-owned subsidiary we fully acquired effective January 1, 2007, has been in continuous operation since 1995 in Florida. The Florida facility is located in Volusia County and presently processes regional biosolids for multiple communities and maintains contracts with the City of Altamonte Springs, the City of Oviedo, the City of Palm Coast, the City of Port Orange, the Tohopekaliga Water Authority and Volusia County. Additionally, the company works with other regional biosolids management companies and has worked with other municipalities with short-term and interim agreements. In December 2011, we received notice from Seminole County they were terminating their agreement for wastewater residuals processing at our Florida facility, effective January 2012.

Florida N-Viro derives revenue from several sources. Each municipal customer compensates N-Viro for the processing of their waste materials. Florida N-Viro also receives revenue from utilizing the alkaline products produced by regional power utilities, including Cedar Bay Generating, thru a supply agreement with Headwaters Corporation and Jacksonville Electric Authority. We have also been successful in marketing our N-Viro Soil to local agricultural markets.

Our Volusia County facility operates under and is regulated by a permit issued by the Florida Department of Environmental Protection. We believe we have a satisfactory operating history and positive relationship with the regulatory agencies. We lease the processing facility from Volusia County and renewed our five year contract and lease agreement for the third time in 2010. Florida N-Viro represented 79% of our total revenue in 2011, and this percentage and total revenues have been escalating using N-Viro's regional processing model.

Sales and Marketing of N-Viro Process

We market our technologies principally through internal sales efforts. All domestic sales and marketing are controlled by management. The primary focus of our marketing efforts is towards the full commercialization of our N-Viro Fuel™ technologies.

The N-Viro Fuel market requires us to work within two different and unique regulatory segments. First, our N-Viro Fuel facilities must satisfy biosolids permit requirements for the 40 CFR Part 503 regulations. Second, the finished fuel product must comply with each individual power generator's emission permit requirements. To accomplish this requirement to satisfy air permitting in the power generation facilities, N-Viro has procured, permitted, constructed and has operated a mobile facility to produce N-Viro Fuel on a commercial full-scale basis. We will continue to use this facility to demonstrate the effectiveness of our process at discrete locations with the purpose of meeting the requirements necessary to ultimately permit, build, own and operate permanent N-Viro Fuel processing facilities. We can provide no assurance in our ability to negotiate long-term arrangements from the mobile facility's performance.

International Sales And Marketing

In certain countries outside the United States, we sell or license the N-Viro Process through agents. In their respective territories, the agents market licenses for the N-Viro Processes, serve as distributors of alkaline admixture, oversee quality control of the installed N-Viro facilities, enforce the terms of the license agreements with licensees and market N-Viro Soil. In general, the agents have paid one-time, up-front fees to us for the rights to market or use the N-Viro Process in their respective territories. Typically, the agreements with the agents provide for us to receive a portion of the up-front license fees, ongoing royalty fees paid by the licensees, a portion of the proceeds from the distribution and resale of alkaline admixture and the sale of N-Viro Soil. Agents have total responsibility and control over the marketing and contracts for N-Viro technology, subject only to license models or minimum agreements with us.

The following table sets forth our Agent and the territorial rights of that Agent:

Agent	Territory
CRM Technologies	Israel, Greece and Eastern Europe

Earnings Variation Due to Business Cycles and Seasonal Factors. Our operating results can experience quarterly or annual variations due to business cycles, seasonality and other factors. During the last fiscal quarter of 2011, approximately 98% of our revenue was from management-run operations, 2% from other domestic third party agreements and 0% from foreign agreements or research and development grants. Sales of the N-Viro technology are affected by general fluctuations in the business cycles in the United States and worldwide, instability of economic conditions and interest rates, as well as other factors.

Risks of Doing Business in Other Countries. We conduct a very small amount of business in markets outside the United States, and expect to continue to do so. In addition to the risk of currency fluctuations, the risks associated with conducting business outside the United States include: social, political and economic instability; slower payment of invoices; underdeveloped infrastructure; underdeveloped legal systems; and nationalization. We have not entered into any currency swap agreements which may reduce these risks. We may enter into such agreements in the future if it is deemed necessary to do so. We cannot predict the full impact of this economic instability, but it could have a material adverse effect on revenues and profits.

Research and Development

We continue to investigate methods to shorten drying time, improve the N-Viro Fuel process, substitute various other materials for use as alkaline admixtures and improve the quality and attractiveness of N-Viro Fuel to a variety of end-users. We see opportunities to improve the efficiency of our process through the utilization of alterative heat sources such as methane, waste heat solid fuel and gasification technologies, as viable alternatives to the use of natural gas for process drying.

In 2007 we performed a full scale test of the N-Viro Fuel product at the T.B. Simon Power Plant located on the campus of Michigan State University. The successful results of this first full test encouraged us to focus primarily on the development of the N-Viro Fuel technology. In September 2011, we performed a multiple day 10% N-Viro Fuel test with a Pennsylvania power producer, utilizing our mobile facility for the production of the test fuel. This test was successful as it demonstrated that N-Viro Fuel had no adverse effects on the boiler operation, no negative impacts on resulting ash and no exceedences in stack air emissions. This successful test is expected to be followed by a 20% test with full stack monitoring to allow for full permitting at that site for the use of N-Viro Fuel.

Patents and Proprietary Rights

We have several patents and licenses relating to the treatment and processing of biosolids. While there is no one single patent that is alone material to our business, we believe that our aggregate patents are important to our prospects for future success. However, we cannot be certain that future patent applications will successfully be issued as patents, or that any already issued patents will give us a competitive advantage. It is also possible that our patents could be successfully challenged or circumvented by competitors or other parties. In addition, we cannot assure that our treatment processes do not infringe on patents held by third-parties or their proprietary rights. We are aware of no such infringement, however.

We hold several patents relating to N-Viro Fuel. In the N-Viro Fuel process, waste products, which can include domestic sewage sludge, manures and other materials, are treated with mineral by-products, dried by a mechanical dryer, and converted into a renewable fuel that can be used as a substitute for coal in coal-fired boilers and kilns. We are actively marketing the N-Viro Fuel process in response to the national policy encouraging both alternative energy generation as well as attaining the highest and best reuse of waste materials.

Some early N-Viro patents were developed jointly with the former Medical College of Ohio, now under the name of the University of Toledo ("UT"). Because of the joint development of early N-Viro patents with UT, we agreed the licensing of these early patents would generate a royalty payable by us to UT. We also agreed with UT that claims to the traditional N-Viro Soil process was one-quarter of one percent (1/4%) of technical revenues until expiration of those patents. UT rights to BioBlend and certain other N-Viro technologies range from 2% to 4% of technical revenues derived from these newer technologies. Cumulative royalties paid to UT through December 31, 2011 were approximately $65,000, and no amount was expensed during any of the years 2008 through 2011. UT has no claim to the N-Viro Fuel technologies or process.

In addition, we make use of our trade secrets or "know-how" developed in the course of our experience in the marketing of our services. To the extent that we rely upon trade secrets, unpatented know-how and the development of improvements in establishing and maintaining a competitive advantage in the market for our services, we can provide no assurance that such proprietary technology will remain a trade secret or that others will not develop substantially equivalent or superior technologies to compete with our services.

Industry Overview

Under the Part 503 Regulations, landfills, surface disposal and incineration remain permissible sludge management alternatives. However, these conventional disposal options have become subject to more stringent regulatory standards. The vast majority of states have enacted site restrictions and/or other management practices governing the disposal of sludge in landfills or surface disposal. Amendments to the Clean Air Act governing incineration and disposal of residual ash also impose stricter air emission standards for incineration in general, and the Part 503 Regulations impose additional specific pollutant limits for sludge to be incinerated and for the resulting air emissions.

Surface disposal of sludge involves the placement of sludge on the land, often at a dedicated site for disposal purposes. The Part 503 Regulations subject surface disposal to increased regulation by requiring, among other things, run-off and leachate collection systems, methane monitoring systems and monitoring of, and limits on, pollutant levels. In addition, sludge placed in a surface disposal site are often required to meet certain standards with respect to pathogen levels relating to coliform or salmonella bacteria counts ("Class B" pathogen levels), levels of various pollutants, including metals, and elimination of attractiveness to pests, such as insects and rodents.

Land application for beneficial use involves the application of sludge or sludge-based products, for non-disposal purposes, including agricultural, silvicultural and horticultural uses and for land reclamation. Under the Part 503 Regulations, N-Viro Soil is a product that meets certain stringent standards. "Class A" pathogen levels”, levels of various pollutants, including metals, and elimination of attractiveness to pests, such as insects and rodents, are considered by the EPA to be "exceptional quality" products. The Class A pathogen levels are significantly more stringent than the Class B pathogen levels.

"Exceptional quality" products are treated by the USEPA as safe products, thereby exempting these products from many federal restrictions on their use. All N-Viro products that are produced according to N-Viro Process specifications meet the pollutant concentration limits and other standards set forth in the Part 503 Regulations, and therefore qualify as an "exceptional quality" product that exceeds the USEPA's standards for unrestricted use.

Competition

We are in direct and indirect competition with other businesses, including disposal and other wastewater sludge treatment businesses, some of which are larger and more firmly established and may have greater marketing and development budgets and capital resources than us. There can be no assurance that we will be able to maintain a competitive position in the sludge treatment industry.

We compete against companies in a highly competitive market and have fewer resources than many of those companies. Our business competes within and outside the United States principally on the basis of pricing, reliability of our services provided, product quality, specifications and technical support. Competitive pressures and other factors could cause us to lose market share or could result in decreases in prices, either of which could have a material adverse effect on our financial position and results of operation.

Environmental Regulation

Various environmental protection laws have been enacted and amended during recent decades in response to public concern over the environment. Our operations and those of our licensees are subject to these evolving laws and the implementing regulations. The primary United States environmental laws which we believe may be applicable to the N-Viro Process and the land application of N-Viro SoilTM include Resource Conservation and Recovery Act ("RCRA"), the Federal Water Pollution Control Act of 1972 ("Clean Water Act"), the Comprehensive Environmental Response, Compensation, and Liability Act, ("CERCLA") and the Pollution Prevention Act of 1990 ("PPA"). These laws regulate the management and disposal of wastes, control the discharge of pollutants into the water, provide for the investigation and remediation of contaminated land and groundwater resources and establish a pollution prevention program. In addition, various states have implemented environmental protection laws that are similar to the applicable federal laws. States also may require, among other things, permits to construct N-Viro facilities and to sell and/or use N-Viro SoilTM. There can be no assurance that any such permits will be issued.

The Part 503 Regulations. Historically, sludge management has involved either disposal, principally by landfilling, incineration, ocean dumping and surface disposal, or land application for beneficial use. Sewage sludge and the use and disposal thereof are regulated under the Clean Water Act. In 1993, the U.S. Environmental Protection Agency ("EPA") published the Part 503 Regulations under the Clean Water Act, implementing the EPA's "exceptional quality" program. These regulations establish sludge use and disposal standards applicable to public and privately-owned wastewater treatment plants in the United States, including publicly-owned treatment works, or POTWs. Under the Part 503 Regs, sludge products that meet certain stringent standards are considered to be "exceptional quality" ("Class A") products and are not subject to any federal restrictions on agricultural use or land application. N-Viro Soil™ is an "exceptional quality" product. Lower quality sludge products are subject to federal restrictions governing, among other items, the type and location of application, the volume of application and the cumulative application levels for certain pollutants. Agricultural application of these lower quality sludges in bulk amounts also requires an EPA permit. Agricultural and land applications of all sludge and sludge products, including N-Viro Soil™ and other "exceptional quality" products, are typically subject to state and local regulation and, in most cases, require a permit.

In order to ensure compliance with the Part 503 Regs, we review the results of regular testing of sludge required by the EPA to be conducted by wastewater treatment plants, and it tests N-Viro Soil™ produced at N-Viro facilities on a regular basis. In general, we do not license or permit the ongoing use of the N-Viro Process to treat any sludge that may not be processed into an "exceptional quality" sludge product. Although N-Viro Soil™ exceeds the current federal standards imposed by the EPA for unrestricted agricultural use and land application, state and local authorities are authorized under the Clean Water Act to impose more stringent requirements than those promulgated by the EPA. Most states require permits for land application of sludge and sludge based products and several states have regulations for certain pollutants that impose more stringent numerical concentration limits than the federal rules.

The Resource Conservation and Recovery Act. RCRA regulates all phases of hazardous waste generation, management and disposal. Waste is subject to regulation as a hazardous waste under RCRA if it is a solid waste specifically listed as a hazardous waste by the EPA or exhibits a defined hazardous characteristic. Although domestic sewage and mixtures of domestic sewage and other wastes that pass through a sewer system to a POTW are specifically exempted from the definition of solid waste, once treated by the POTW, the sewage sludge is considered a solid waste. Although neither the alkaline admixture nor wastewater sludge used in the N-Viro Process are regulated as hazardous waste under RCRA, states may impose restrictions that are more stringent than federal regulations. Accordingly, the raw materials used in the N-Viro Process may be regulated under some state hazardous waste laws as "special wastes," in which case specific storage and record keeping requirements may apply.

The Comprehensive Environmental Response, Compensation and Liability Act of 1980. CERCLA imposes strict, joint and several liability upon owners and operators of facilities where a release of hazardous substances has occurred, upon parties who generated hazardous substances into the environment that were released at such facilities and upon parties who arranged for the transportation of hazardous substances to such facilities. We believe the N-Viro Process poses little risk of releasing hazardous substances into the environment that presently could result in liability under CERCLA.

Other Environmental Laws. The Pollution Prevention Act of 1990 establishes pollution prevention as a national objective, naming it a primary goal wherever feasible. The act states that where pollution cannot be prevented, materials should be recycled in an environmentally safe manner. Additional laws or regulations impacting use or negatively classifiying products like those produced by N-Viro are also a possibility. We believe that the N-Viro Process contributes to pollution prevention by providing an alternative to disposal.

State Regulations. State regulations typically require an N-Viro facility to obtain a permit for the sale of N-Viro Soil™ for agricultural use, and may require a site-specific permit by the user of N-Viro Soil™. In addition, in some jurisdictions, state and/or local authorities have imposed permit requirements for, or have prohibited, the land application or agricultural use of sludge products, including "exceptional quality" sludge products. Certain of our licensees operate in jurisdictions that require permits and have been able to obtain them for the N-Viro product. There can be no assurance that any such permits will be issued or that any further attempts to require permits for, or to prohibit, the land application or agricultural use of sludge products will not be successful.

In addition, many states enforce landfill restrictions for non-hazardous sludge. These regulations typically require a permit to sell or use sludge products as landfill cover material. There can be no assurance that N-Viro facilities or landfill operators will be able to obtain required permits.

Environmental impact studies may be required in connection with the development of future N-Viro facilities. Such studies are generally time consuming and may create delays in the construction process. In addition, unfavorable conclusions reached in connection with such a study could result in termination of or expensive alterations to the N-Viro facility being developed.

The costs of compliance are typically borne by our licensees, except in the case of direct sludge processing into a facility. Normally this cost is not material to us in relation to the total contract revenue.

Employees

As of December 31, 2011, we had 28 employees. Five of our employees were engaged in sales and marketing; three were in finance and administration and twenty were in operations. We consider our relationship with our employees to be satisfactory.

Throughout 2011 we were a party to a collective bargaining agreement (the "Labor Agreement") covering three employees of National N-Viro Tech, Inc., our wholly-owned subsidiary. The employees that were covered by the Labor Agreement worked at the Toledo, Ohio N-Viro facility, which was operated by us for the City of Toledo on a contract management basis and was terminated at the end of 2011. See Part I, “N-Viro Process Facilities” for additional explanation. These employees were members of the International Brotherhood of Teamsters, Chauffeurs, Warehouseman and Helpers Local Union No. 20, and we consider our relationship with the organization to be satisfactory. As of the filing of this Form 10-K, we no longer have any employees of National N-Viro Tech, Inc., and have ceased all work at the City of Toledo under the contract that was not renewed in 2011.

Current Developments

We are currently in discussions with several companies in the cement and fuel/power generation industries for the development and commercialization of the patented N-Viro Fuel™ technology. There can be no assurance that these discussions will be successful. We continue to focus on the development of regional biosolids processing facilities. Currently we are in negotiations with several privatization firms to permit and develop independent, regional facilities.

Securities and Exchange Commission

As a public company, we are required to file periodic reports, as well as other information, with the Securities and Exchange Commission (SEC) within established deadlines. Any document we file with the SEC may be viewed or copied at the SEC's Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549. Additional information regarding the Public Reference Room can be obtained by calling the SEC at (800) SEC-0330. Our SEC filings are also available to the public through the SEC's web site located at www.sec.gov.

We maintain a corporate Web site at www.nviro.com, on which investors may access free of charge our annual report on Form 10-K, quarterly reports on Form 10-Q and amendments to those reports as soon as is reasonably practicable after furnishing such material with the SEC. In addition, we will voluntarily provide electronic or paper copies of our filings free of charge upon request to James K. McHugh, our Chief Financial Officer, at (419) 535-6374 or via e-mail to jmchugh@nviro.com.

Item 1A. Risk Factors

We have a history of losses and there can be no assurances regarding if and when we will achieve profitability. If we are unable to achieve profitable operations, we may need to raise additional capital to continue our operations, which may not be available on commercially reasonable terms or at all, and which may dilute our stockholders.

Since 2000, we have experienced net losses and we have not been consistently profitable on an annual basis. For the years ended December 31, 2011 and 2010, we incurred net losses of $1.6 million and $3.0 million, respectively. We believe our history of net losses is primarily due to our inability to add enough new sources of revenue to replace decreasing business from existing sources of revenue and, more recently, through a shift of our business toward lower margin products and services. Further, for the years ended December 31, 2011 and 2010, we experienced much higher than expected expenditures for stock-related fees and compensation in excess of our increase in gross revenue. To achieve profitability, we must accomplish numerous objectives, including growth in our business, the development of new products and commercial relationships, and decreasing our costs. We can not foresee with any certainty whether we will be able to achieve these objectives in the future. Accordingly, we may not generate sufficient net revenue to achieve profitability.

Failure to maintain effective internal controls could have a material adverse effect on our business, operating results and stock price.

We have evaluated and will continue to evaluate our internal control procedures in order to satisfy the requirements of Section 404 of the Sarbanes-Oxley Act, which requires an annual management assessment of the design and effectiveness of our internal controls over financial reporting. We have previously identified a material weakness in our internal controls over financial reporting due to a lack of personnel to sufficiently monitor and process transactions. Due to our continuing lack of financial resources to hire and train accounting and financial personnel, we have not yet remedied this material weakness. At the beginning of 2012, as part of continued cost-cutting measures, we laid off one of our financial personnel that reported directly to the Chief Financial Officer. While we are not aware of any material errors to date, our inability to maintain the adequate internal controls may result in a material error in our financial statements. Moreover, effective internal controls, particularly those related to revenue recognition, are necessary for us to produce reliable financial reports and are important to helping prevent financial fraud. If we experience a material error in our financial statements or if we cannot provide reliable financial reports or prevent fraud, our business and operating results could be harmed, investors could lose confidence in our reported financial information, and the trading price of our stock could drop significantly.

Compliance with environmental laws and regulations may reduce, delay or prevent our realization of license revenues and/or facility revenue.

Our operations and our licensees and their operations are subject to increasingly strict environmental laws and regulations, including laws and regulations governing the emission, discharge, disposal and transportation of certain substances and related odor. Wastewater treatment plants and other plants at which our biosolids products or processes may be implemented are usually required to have permits, registrations and/or approvals from state and/or local governments for the operation of such facilities. Some facilities using our processes require air, wastewater, storm water, biosolids processing, use or siting permits, registrations or approvals. These licensees may not be able to maintain or renew their current permits or registrations or to obtain new permits or registrations. The process of obtaining a required permit or registration can be lengthy and expensive. They may not be able to meet applicable regulatory or permit requirements, and therefore may be subject to related legal or judicial proceedings that could have a materially adverse effect on our income derived from these facilities.

Any of the permits, registrations or approvals noted above, or related applications may be subject to denial, revocation or modification, or challenge by a third party, under various circumstances. In addition, if new environmental legislation or regulations are enacted or existing legislation or regulations are amended or are enforced differently, these facilities may be required to obtain additional, or modify existing, operating permits, registrations or approvals.

Maintaining, modifying or renewing current permits or registrations or obtaining new permits or registrations after new environmental legislation or regulations are enacted or existing legislation or regulations are amended or enforced differently may be subject to public opposition or challenge. Much of this public opposition and challenge, as well as related complaints, relates to odor issues, even when a facility is operated in compliance with odor requirements and even though they have worked hard to minimize odor from their operations. Public misperceptions about the business and any related odor could influence the governmental process for issuing such permits or registrations or for responding to any such public opposition or challenge. Community groups could pressure local municipalities or state governments to implement laws and regulations which could increase our costs of their operations that in turn could have a material and adverse effect on our business and financial condition.

Our ability to grow our revenues and operations may be limited by competition.

We provide a variety of technology and services relating to the treatment of wastewater residuals. We are in direct and indirect competition with other businesses that provide some or all of the same services including regional residuals management companies and national and international water and wastewater operations/privatization companies, technology suppliers, municipal solid waste companies and farming operations. Many of these competitors are larger and have significantly greater capital resources.

We derive a substantial portion of our revenue from services provided under municipal contracts, and many of these are subject to competitive bidding. We also intend to bid on additional municipal contracts, however, and may not be the successful bidder. In addition, some of our contracts will expire in the future and those contracts may not be renewed or may be renewed on less attractive terms. In 2011, we experienced just this possibility with respect to existing contracts in Toledo, Ohio and Seminole County, Florida, both of which were not renewed albeit for different reasons. If we are not able to replace revenues from contracts lost through competitive bidding or from the renegotiation of existing contracts with other revenues within a reasonable time period, the lost revenue could have a material and adverse effect on our business, financial condition and results of operation.

Our customer contracts may be terminated prior to the expiration of their term.

A substantial portion of our revenue is derived from services provided under contracts and agreements with existing licensees. Some of these contracts, especially those contracts with large municipalities, provide for termination of the contract by the customer after giving relative short notice (in some cases as little as ten days). In addition, some of these contracts contain liquidated damages clauses, which may or may not be enforceable in the event of early termination of the contracts. If one or more of these contracts are terminated prior to the expiration of its term, and we are not able to replace revenues from the terminated contract or receive liquidated damages pursuant to the terms of the contract, the lost revenue could have a material and adverse effect on our business, financial condition and results of operations.

A significant amount of our business comes from a limited number of customers and our revenue and profits could decrease significantly if we lost one or more of them as customers. Further, the agreement with our second largest customer expired in November 2011, and our failure to renew that agreement has, in the short-term, had a material adverse effect on our business, financial conditions and results of operations.

Our business depends on providing services to a limited number of customers. One or more of these customers may stop contracting for services from us or may substantially reduce the amount of services we provide them. Any cancellation, deferral or significant reduction in the services we provide these principal customers or a significant number of smaller customers could seriously harm our business and financial condition. For the years ended December 31, 2011 and 2010, one of our largest customers accounted for approximately 17% and 22%, respectively, of our revenues and our top three customers accounted for approximately 55% and 60%, respectively, of our revenues. Our sludge processing agreement with the City of Toledo, Ohio, who was our largest customer for many years through 2010 and represented approximately 17% of our revenues in 2011, was not renewed at the end of 2011. Our failure to renew that agreement has had a material adverse effect on our business, financial conditions and results of operations. Also at the end of 2011, we were notified by a Florida customer, Seminole County, that represented gross revenue of $353,000 and $402,000 in 2011 and 2010, respectively, was terminating our services effective January 2012. This was approximately 6% and 8% of 2011 and 2010 gross revenue, respectively. Additionally, economic considerations have made the supply of admixtures used in our processes more difficult to acquire due to coal-burning facilities operating less or not at all.

The current economic downturn may cause us to experience delays of payment from our customers.

Our accounts receivable are derived primarily from municipal or local governments. Although our collection history has been good, from time to time a customer may not pay us on a timely basis because of adverse market conditions. In light of the current economic downturn, we may experience larger than expected delays in receiving payments on our accounts receivable. Given our history of losses and our limited cash resources, any significant payment delay by one of our customers, may force us to delay payment to our creditors, which may have a material and adverse effect on our business, financial condition and results of operations.

We are affected by unusually adverse weather conditions.

Our present business is adversely affected by unusual weather conditions and unseasonably heavy rainfall which can temporarily reduce the availability of land application sites in close proximity to our operations. In addition, revenues and operational results are adversely affected during months of inclement weather which limits the amount of land application that can be performed. Long periods of adverse weather could have a material negative effect on our business and financial condition. For example, our Daytona Florida operation is sometimes affected by unusually adverse weather conditions by lowering the demand for N-Viro Soil(TM) distribution to the local agricultural community.

Fuel cost variation could adversely affect our operating results and expenses.

The price and supply of fuel is unpredictable and fluctuates based on events outside our control, including demand for oil and gas, actions by OPEC and other oil and gas producers, and war in oil producing countries. Because fuel is needed for the trucks that transport the processing materials and supplies for our operations and customers, price escalations or reductions in the supply of fuel could increase our operating expenses and have a negative impact on the results of operations. We are not always able to pass through all or part of the increased fuel costs due to the terms of certain customers' contracts and the inability to negotiate such pass through costs in a timely manner.

We are highly dependent on the services of our management team, the loss of any of whom may have a material adverse effect on our business and financial condition.

In 2010 we entered into employment agreements with our Chief Executive Officer, Timothy Kasmoch, our Executive Vice President and Chief Counsel, Robert Bohmer and our Chief Financial Officer, James McHugh, each of which contains non-compete and other provisions. The laws of each state differ concerning the enforceability of non-competition agreements. We cannot predict with certainty whether or not a court will enforce a non-compete covenant in any given situation based on the facts and circumstances at that time. If one of our key executive officers were to leave our employ and the courts refused to enforce the non-compete covenant, we might be subject to increased competition, which could have a material and adverse effect on our business and financial condition.

Our intellectual property may be misappropriated or subject to claims of infringement.

We attempt to protect our intellectual property rights through a combination of patent, trademark, and trade secret laws, as well as the use of non-disclosure and licensing agreements. Our failure to obtain or maintain adequate protection of our intellectual property rights for any reason could have a material adverse effect on our business and financial condition.

Our competitors, many of whom have substantially greater resources and have made substantial investments in competing technologies, may have applied for or obtained, or may in the future apply for and obtain, patents that will prevent, limit or otherwise interfere with our ability to offer services.

We also rely on unpatented proprietary technology. It is possible that others will independently develop the same or similar technology or otherwise obtain access to our unpatented technology. If we are unable to maintain the proprietary nature of our technologies, we could be materially adversely affected.

There is only a limited trading market for our common stock, and it is possible that you may not be able to sell your shares easily.

There is currently only a limited trading market for our common stock. Our common stock trades on the OTCQB, which is one of the quotation services for SEC-registered and reporting companies that trade over the counter ("OTC Markets"), under the symbol “NVIC”, with limited trading volume. We cannot assure you that a trading market will exist for our common stock.

We have never paid dividends on our shares of common stock.

We have not paid any cash dividends on our common stock heretofore, and we have no present intention of paying any cash dividends for the foreseeable future. Any determination to pay dividends in the future will be at the discretion of the board of directors.

Volatility in the trading price of our common stock could negatively impact the price of our common stock, and may eliminate a source of our potential revenue from exercises of stock options and stock purchase warrants.

During the period from January 1, 2010 through March 2, 2012, our common stock closing price fluctuated between a high of $3.85 and a low of $1.00. The trading price of our common stock could be subject to wide fluctuations in response to many factors, some of which are beyond our control, including general economic conditions, the thinly-traded nature of our common stock and the outlook of analysts and investors on our industry. Further, significant market fluctuations, such as over the past six months, may adversely affect the trading price of our common stock. Over the past several years, we have relied on, in part, exercises of stock options by current and former officers and directors and stock purchase warrants by investors for operating cash. Wide fluctuations in the price of our common stock or a stock price that is not significantly above the exercise price of outstanding stock options or warrants, would likely reduce future exercises of stock options or warrants, and which would reduce or eliminate a historic source of cash for our operations.

Item 2. Properties

Our executive and administrative offices are located in Toledo, Ohio. Through April 2011, we operated under a month to month lease at our former location. The total rental expense for this former location included in the statements of operations for the twelve months ended December 31, 2011 and 2010 is approximately $12,850 and $38,500, respectively. In April 2011, we signed a 68 month lease with a new lessor in Toledo, Deerpoint Development Company, Ltd. The total minimum rental commitment for the year ending December 31, 2011 is approximately $15,600, for 2012 is $37,400, for 2013 is $30,600 and for the years 2014 through 2016 is $40,800 each year. The total rental expense for the new, current location included in the statements of operations for the twelve months ended December 31, 2011 is approximately $15,600. We also lease various equipment on a month-to-month basis.

In October 2010, we began to lease property in Emlenton, Pennsylvania under a lease with A-C Valley Industrial Park, for one year. The total rental expense included in the statements of operations for the twelve months ended December 31, 2011 and 2010 is $23,000 and $6,000, respectively. Currently we are operating under a month-to-month lease at this location for one-half the rate under the original lease agreement.

In June 2009, we began to maintain an office in West Unity, Ohio under a lease with D&B Colon Leasing, LLC, for one year. In June 2010, we renewed the lease for an additional year through May 31, 2011, and are currently operating under a month to month lease. The total rental expense included in the statements of operations for each of the twelve months ended December 31, 2011 and 2010 is $30,000.

We maintain an office in Daytona Beach under a lease with the County of Volusia, Florida, which was renewed in March 2009 for five years. The total minimum rental commitment for the years ending December 31, 2012 through 2013 is $48,000 each year, and for 2014 is $12,000. The total rental expense included in the statements of operations for each of the twelve months ended December 31, 2011 and 2010 is $48,000.

We also leased other processing equipment at our Florida location which began in February 2008 under a three-year lease. The total rental expense included in the statements of operations for each of the twelve months ended December 31, 2011 and 2010 is approximately $3,900 and $46,200, respectively. In February 2011, we purchased the equipment through a financing arrangement with an equipment leasing company.

Management believes that all of our properties are adequately covered by insurance.

Item 3. Legal Proceedings

None

Item 4. Mine Safety Disclosures

None.

PART II

Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

Market Information

Our shares of Common Stock are quoted on the OTCQB, which is one of the quotation services for SEC-registered and reporting companies that trade over the counter ("OTC Markets"), under the symbol "NVIC". The prices quoted below reflect inter-dealer prices, without retail mark-up, mark-down or commission and may not represent actual transactions. The closing price range per share of the Common Stock since January 1, 2010, was as follows:

Quarter	High	Low
First 2010	$3.85	$2.39
Second 2010	$3.30	$2.70
Third 2010	$3.10	$1.95
Fourth 2010	$3.25	$1.51
First 2011	$3.25	$1.50
Second 2011	$2.75	$1.45
Third 2011	$2.45	$1.50
Fourth 2011	$2.00	$1.01

Our stock price closed at $1.10 per share on March 5, 2012.

Holders

As of March 5, 2012, the number of holders of record of our Common Stock was approximately 177.

Dividends

We have never paid dividends with respect to our Common Stock. Payment of dividends is within the discretion of our Board of Directors and would depend, among other factors, on our earnings, capital requirements and our operating and financial condition.

Recent Sales of Unregistered Securities

None

Item 6. Selected Financial Data

As a smaller reporting company we are not required to provide this information under Item 301 of Regulation S-K.

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

Overview

The following is a discussion of our results of operations and financial position for the periods described below, and should be read in conjunction with our Financial Statements and Supplementary Data appearing elsewhere in this Form 10-K. The discussion includes various forward-looking statements about our markets, products, services and our results. These statements are based on certain assumptions that we consider reasonable. Our actual results may differ materially from these indicated forward-looking statements. Please see "Cautionary Statement with Respect to Forward-Looking Comments" and "Risk Factors" elsewhere in this annual report on Form 10-K.

The following table sets forth, as a percentage of total revenues for the periods presented, revenues related to each of (i) technology fees, (ii) facility management, (iii) products and services:

	For the Year Ended December 31, 2011	2010
Technology fees	0.1%	0.1%
Facility management	68.3%	66.2%
Products and services	31.6%	33.7%
Totals	100.0%	100.0%

Technology fee revenue is defined as: royalty revenue, which represent ongoing amounts received from licensees for continued use of the N-Viro Process and are typically based on volumes of sludge processed; license and territory fees, which represent non-recurring payments for the right to use the N-Viro Process in a specified geographic area or at a particular N-Viro facility; and research and development revenue, which represent payments from federal and state agencies awarded to us to fund ongoing site-specific research utilizing the N-Viro technology.

Facility management revenues are recognized under contracts where we manage the N-Viro Process ourselves to treat sludge, pursuant to a fixed price contract.

Product and service revenue is defined as: alkaline admixture revenue, which represent ongoing payments from licensees arising from the sale and distribution of alkaline admixture by us to N-Viro facilities; service fee revenue for the management of alkaline admixture, which represent fees charged by us to manage and sell the alkaline admixture on behalf of a third party customer; N-Viro SoilTM sales, which represent revenue received from sales of N-Viro Soil sold by us; commissions earned on sales of equipment to an N-Viro facility; rental of equipment to a licensee or agent; and equipment sales, which represent the price charged for equipment held for subsequent sale.

Our policy is to record the revenues payable to us pursuant to agency and license agreements when we have fulfilled our obligations under the relevant contract, except when it pertains to a foreign license agreement. In the case of foreign licenses, revenue is recorded when cash is received and when we have fulfilled our obligations under the relevant foreign license agreement.

Results of Operations

The following tables set forth, for the periods presented, (i) certain items in the Combined Statement of Operations, (ii) the percentage change of each such item from period to period and (iii) each such item as a percentage of total revenues in each period presented.

(Dollars in thousands)	Year Ended December 31, 2011	Period to Period Percentage Change	Year Ended December 31, 2010

Combined Statement of
Operations Data:

Revenues	$	5,5947.1%		$	5,222
Cost of revenues		4,5618.1%			4,218
Gross profit		1,0332.8%			1,004
Operating expenses		3,516(8.6%)			3,767
		(2,483)	*		(2,763)
Other income (expense)		843	*		(206)
Loss before income tax expense		(1,640)	*		(2,969)
Federal and state income tax expense		-	*		-
Net loss	$	(1,640)	*	$	(2,969)

Percentage of Revenues:

Revenues	100.0%	100.0%
Cost of revenues	81.5	80.8
Gross profit	18.5	19.2
Operating expenses	62.8	72.1
	(44.3)	(52.9)
Other income (expense)	15.1	(4.0)
Loss before income tax expense	(29.2)	(56.9)
Federal and state income tax expense	-	-
Net loss	(29.2%)	(56.9%)

* Period to period percentage change comparisons have only been calculated for positive numbers.

Comparison of Year Ended December 31, 2011 with Year Ended December 31, 2010

Our overall revenue increased $372,000, or 7%, to $5,594,000 for the year ended December 31, 2011 from $5,222,000 for the year ended December 31, 2010. The net increase in revenue was due primarily to the following:

a) Sales of alkaline admixture decreased $40,000 from the same period ended in 2010 – this decrease was primarily the result of a decrease in demand with our Ohio-area customers, approximately $19,000 directly from the Toledo operation;

b) Revenue from the service fees for the management of alkaline admixture increased $93,000 from the same period ended in 2010 – this increase was attributed primarily to our Florida-area customers, which increased $89,000 compared to the same period in 2010; and

c) Our processing revenue, including facility management revenue, showed a net increase of $314,000 over the same period ended in 2010. This was primarily from our Florida operation, which showed an increase of $491,000 in facility management fees over 2010, of which $221,000 was from our agreement with Orange County Utilities that began in December 2010 and ended in March 2011. Orange County has not nor do we expect them to renew that agreement in the near future. The start up in April 2011 of the Pennsylvania fuel pilot plant contributed approximately $18,000 to the increase in facility management fee revenue. Offsetting the increase was a decrease in both facility management and product revenue from the Toledo operation, a decrease of $192,000 from 2010, as contracted operations ceased in November 2011; and

d) Our license fee revenue showed no net change over the same period ended in 2010 – both years revenue was $-0-.

Our gross profit increased $28,000, or 3%, to $1,033,000 for the year ended December 31, 2011 from $1,004,000 for the year ended December 31, 2010, and the gross profit margin decreased to 18.5% from 19.2% for the same periods. The minor overall movements from the prior year in gross profit and gross profit margin are due primarily to three sources of operations in 2011:

1. An increase in total revenue and gross margin from our Florida operation. The total revenue attributable to Florida in 2011 was $4,442,000, an increase of $583,000 from 2010. This revenue was generated at a gross margin of 20%, up from 17% in 2010. Florida contributed $869,000 of gross profit, an increase of $223,000 over the same period in 2010. A majority of this increase in Florida's gross profit was from the increased revenue from sludge management fees, which were realized at a lower cost percentage as a result of economies of scale and increased efficiency in sludge handled at the facility.

2. An increase in total revenue of $18,000 from our Pennsylvania fuel pilot start up in April 2011, but which sustained a gross loss of $231,000 for the year.

3. A decrease in total revenue and a small increase in gross profit from our Toledo operation. The total revenue attributable to Toledo in 2011 was $949,000, a decrease of $201,000 from 2010. This revenue was generated at a gross margin of approximately 36%. The Toledo operation contributed $339,000 of gross profit, which was an increase of $40,000 of gross profit over the same period in 2010. The Toledo operation was more efficient in 2011 due primarily to re-priced alkaline admixture supply contracts at the end of 2010 and a decrease in labor costs.

Our operating expenses decreased $252,000, or 7%, to $3,516,000 for the year ended December 31, 2011 from $3,767,000 for the year ended December 31, 2010. The decrease was primarily due to decreases of $799,000 in consulting fees and expenses, $56,000 in office and miscellaneous expenses, $35,000 in legal and related fees and $15,000 of gain on the disposal of assets, offset by an increase of $386,000 in payroll and related costs and $267,000 in director costs. Of the total net decrease of $146,000 in consulting, director and payroll costs, $71,000 were non-cash costs relating to the issuances of stock and stock options. Therefore, for the year ended December 31, 2011 actual cash outlays in these categories decreased by a total of $75,000 over the same period in 2010.

As a result of the foregoing factors, we recorded an operating loss of $2,483,000 for the year ended December 31, 2011 compared to an operating loss of $2,763,000 for the year ended December 31, 2010, a decrease in the loss of

$280,000.

Our net nonoperating income (expense) increased by $1,049,000 to net nonoperating income of $843,000 for the year ended December 31, 2011 from net nonoperating expense of $206,000 for the similar period in 2010. The increase in net nonoperating income was primarily due to an increase of $873,000 from the gain recorded on warrants issued whose value and number of shares outstanding had decreased from the issuance date, an increase of $93,000 in the gain on extinguishment of certain liabilities no longer due, a decrease of $48,000 in amortization of the stock discount on convertible debentures issued and a decrease of $33,000 from 2010 to 2011 in the gain on the modification of certain debt. Included in the increase in the gain on extinguishment of certain liabilities no longer due is $174,000 of gain recognized for the reversal of a recorded sales tax liability management determined in the fourth quarter 2011 is no longer due.

We recorded a net loss of $1,640,000 for the year ended December 31, 2011 compared to a net loss of $2,969,000 for the same period ended in 2010, a decrease in the loss of $1,401,000. Adding back non-cash expenses such as depreciation, amortization, stock and stock options charges and subtracting cash out for capitalized assets and debt repayments, resulted in an adjusted cash loss (non-GAAP) of $329,000 for the year ended in 2011. Similar non-cash expenses, cash out and debt repayments for the same period in 2010 resulted in an adjusted cash loss (non-GAAP) of $445,000, a decrease in the adjusted cash loss (non-GAAP) of $116,000 for the year ended in 2011 versus 2010, as follows:

	2011	2010
GAAP net loss	$(1,640,000)	$(2,969,000)
Depreciation + Amortization	540,000	449,000
Net cash out for fixed assets capitalized or sold	(71,000)	(15,000)
Stock, stock options and warrants expense	2,216,000	2,286,000
Amortization of discount on debentures	28,000	108,000
Loss (gain) on market price change of stock warrants issued	(732,000)	140,000
Loss (gain) on bad debts recovered or liabilities written off	(174,000)	20,000
Debt service payments	(496,000)	(464,000)
"Adjusted cash loss (non-GAAP)"	$(329,000)	$(445,000)

For the years ended December 31, 2011 and 2010, we have not recognized the future tax benefit of current or prior period losses due to our history of operating losses. Accordingly, our effective tax rate for each period was zero.

Liquidity and Capital Resources

We had a working capital deficit of $409,000 at December 31, 2011, compared to a working capital deficit of $932,000 at December 31, 2010, resulting in an increase in working capital of $524,000. Current assets at December 31, 2011 included cash and cash equivalents of $253,000 (including restricted cash of $209,000), which is an increase of $8,000 from December 31, 2010. The net positive change in working capital from December 31, 2010 was primarily from a reclassification of $578,000 of debentures to long-term debt as a result of the replacement debentures issued in August 2011, a reduction of $186,000 in accrued liabilities and a reduction of $125,000 in the short-term debt due banks and financing entities, offset by a $200,000 increase in notes payable to a related party, a net decrease of $90,000 in trade receivables decreasing more than trade payables, and, a decrease to the net deferred current asset of $75,000 for amortization of common stock and warrants given pursuant to consulting contracts entered into in 2010.

In 2011 our cash flow provided by operating activities was $333,000, an increase of $329,000 over 2010. The components of the increase in cash flow provided by operating activities from 2010 was principally due to a decrease in the net loss of $1,329,000 and a decrease of $556,000 in trade accounts receivable, offset by a decrease of $873,000 in the market price of derivatives issued, a decrease of $575,000 in trade accounts payable and accrued liabilities, a $71,000 decrease in stock warrants and stock options issued for fees and services, a net decrease of $1,000 in fixed asset and investment gains and losses, and, a decrease in prepaid and other assets of $36,000.

We have modified our business model and have been evolving away from sales of alkaline admixture and royalty-based revenue agreements that typically generate a higher gross profit margin, to long-term and sustainable revenue based on integrated N-Viro technology and operations, but typically generating a lower gross profit margin. From 2006 to 2011, the percentage of combined revenues generated from our owned and operated facilities in Toledo and Volusia County was: 2006 – 46%; 2007 – 77%; 2008 – 94%; 2009 – 95%; 2010 – 96%; 2011 – 96%. We believe this shift will allow us to enhance future revenue and profits through growth, efficiency and revenue optimization.

The normal collection period for accounts receivable is approximately 30-45 days for the majority of customers. This is a result of the nature of the license contracts, type of customer and the amount of time required to obtain the information to prepare the billing. For 2009 and throughout 2010, our customers slowed the overall payment rate on our outstanding receivables, which in turn contributed to us extending payment times to our vendors on our payables. We make no assurances that payments from our customers or payments to our vendors will become shorter and this may have an adverse impact on our continuing operations.

During 2011 we renewed our line of credit with Monroe Bank + Trust, or the Bank, up to $400,000 bearing interest at the Wall Street Journal Prime Rate (3.25% at December 31, 2011) plus 0.75%, but in no event less than 5.00%, and secured by a first lien on all our assets (except equipment), with a new maturity date of August 15, 2012. Two certificates of deposit totaling $141,430 from the Bank are held as a condition of maintaining the line of credit. At December 31, 2011, we had $100,000 of borrowing capacity under the credit facility.

On August 1, 2011, we borrowed $200,000 with a Promissory Note payable to a related party of Timothy Kasmoch, our President and Chief Executive Officer, at 12% interest prepaid for a period of three months, renewable for an additional three months by the prepayment of additional interest and secured by certain equipment. Mr. Kasmoch has personally guaranteed the repayment of this Note. We extended the Note on October 30, 2011 and again on January 30, 2012, and it is now due April 30, 2012. We expect to extend the Note on or before the due date but pay the Note in full during 2012.

From the beginning of 2006 through 2011, we have borrowed a total of $1,677,100 from ten lenders to purchase processing and automotive equipment. As of December 31, 2011, a total of thirteen term notes are outstanding, ranging from 6.2% to 10.9% interest for terms ranging three to five years, monthly payments totaling approximately $26,000 and all secured by equipment. The total amount owed on all equipment-secured notes as of December 31, 2011 was approximately $442,000 and all notes are expected to be paid in full on the applicable maturity date, the last of which is in March 2016.

In 2009 we approved an offering of up to $1,000,000 of Convertible Debentures (the “Debentures”), convertible at any time into our unregistered common stock at $2.00 per share. The Debentures are issuable in $5,000 denominations, are unsecured and have a stated interest rate of 8%, payable quarterly to holders of record. We have timely paid all accrued interest due to all Debenture holders of record as of each quarter-end date starting in July 2009. At any time, we may redeem all or a part of the Debentures at face value plus unpaid interest.

During 2009 we issued $765,000 of Debentures to a total of twenty three accredited investors, and one investor converted $10,000 of Debentures into unregistered common stock. During 2010 we issued $55,000 of Debentures, and three investors converted a total of $90,000 of Debentures into unregistered common stock. The Debentures matured at June 30, 2011, however fifteen investors holding Debentures totaling $365,000 elected to replace them with new ones that now mature at June 30, 2013. All other features of the "expired" Debentures remained the same in the replacement ones, except for the new maturity date. Of the four investors totaling $355,000 who did not replace their existing Debentures with new ones, two investors totaling $215,000 had their Debentures repaid; one investor converted $50,000 into unregistered common stock (at June 30, 2011) and one holding $90,000 of Debentures has not made a final decision. As of December 31, 2011, we held $455,000 of Debentures.

Because the fair market value of our common stock (the underlying security in the Debentures) may have been above the conversion price of $2.00 per share at the date of issuance, we were required under GAAP to record a discount given for certain (now) "expired" Debentures sold, which totaled $184,975. The discount was then required to be amortized as a period expense over the periods the Debentures were scheduled to be outstanding, which averaged 20 months, through the maturity date of June 30, 2011. For the year ended December 31, 2011 and 2010, amortization expense on the "expired" Debentures amounted to $52,326 and $108,334, respectively.

For periods subsequent to June 30, 2011, we are required under GAAP to record a discount totaling $32,737 for certain Debentures replaced, and a gain on debt modification during the quarter ended June 30, 2011. The discount is required to be amortized as a period expense over the next eight quarters the Debentures are scheduled to be outstanding. For the six months ended December 31, 2011 these "replacement" debentures have been outstanding, amortization expense amounted to $8,184.

For 2012, we expect to improve operating results and have adequate cash or access to cash to adequately fund operations and debt service by focusing on existing and expected new sources of revenue, especially from our N-Viro Fuel technology, and cash generated from equity issuances and exercises of outstanding warrants and options. We expect that market developments favoring cleaner burning renewable energy sources and ongoing discussions with companies in the fuel and wastewater industries could provide enhanced liquidity and have a positive impact on future operations. We continue to pursue opportunities with strategic partners for the development and commercialization of the patented N-Viro Fuel technology. In addition, we are focusing on the development of regional biosolids processing facilities, and are currently in negotiations with potential partners to permit and develop independent, regional facilities.

There can be no assurance these discussions will be successful or result in new revenue or cash funding sources for the company. Our failure to achieve improvements in operating results, including through these potential sources of revenue, or in our ability to adequately finance or secure additional sources of funds would likely have a material adverse effect on our continuing operations.

Off-Balance Sheet Arrangements

At December 31, 2011, we did not have any material commercial commitments, including guarantees or standby repurchase obligations, or any relationships with unconsolidated entities or financial partnerships, including entities often referred to as structured finance or special purpose entities or variable interest entities, which would have been established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes.

From time to time, during the normal course of business, we may make certain indemnities, commitments and guarantees under which we may be required to make payments in relation to certain transactions. These include: (i) indemnities to vendors and service providers pertaining to claims based on our negligence or willful misconduct and (ii) indemnities involving the accuracy of representations and warranties in certain contracts. Pursuant to Delaware law, we may indemnify certain officers and directors for certain events or occurrences while the officer or director is, or was, serving at our request in such capacity. We also have director and officer insurance coverage that limits our exposure and enables us to recover a portion of any future amounts that we may pay for indemnification purposes. We believe the applicable insurance coverage is generally adequate to cover any estimated potential liability for which we may provide indemnification. The majority of these indemnities, commitments and guarantees do not provide for any limitation of the maximum potential for future payments we could be obligated to make. We have not recorded any liability for these indemnities, commitments and other guarantees in the accompanying Consolidated Balance Sheets.

Critical accounting policies, estimates and assumptions

In preparing financial statements in conformity with accounting principles generally accepted in the United States, management makes estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements, as well as the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. The following are the significant estimates and assumptions made in preparation of the financial statements:

Non-domestic license and territory fees – We do not recognize revenue on any non-domestic license or territory fee contracts until the cash is received, assuming all other tests of revenue recognition are met. Canada is excluded from this definition of non-domestic.

Allowance for Doubtful Accounts – We estimate losses for uncollectible accounts based on the aging of the accounts receivable and the evaluation and the likelihood of success in collecting the receivable. The balance of the allowance at December 31, 2011 and 2010 is $70,000.

Property and Equipment/Long-Lived Assets – Property and equipment is reviewed for impairment. The carrying amount of an asset (group) is considered impaired if it exceeds the sum of our estimate of the undiscounted future cash flows expected to result from the use and eventual disposition of the asset (group), excluding interest charges. Property, machinery and equipment are stated at cost less accumulated depreciation. We believe the carrying amount is not impaired based upon estimated future cash flows.

Intangible Assets – Intangible assets deemed to have indefinite lives are tested for impairment by comparing the fair value with its carrying value. Significant estimates used in the determination of fair value include estimates of future cash flows. As required under current accounting standards, we test for impairment when events and circumstances indicate that the assets might be impaired and the carrying value of those assets may not be recoverable.

Income Taxes – We assume the deductibility of certain costs in income tax filings and estimate the recovery of deferred income tax assets, all of which is fully reserved.

New Accounting Standards – The Financial Accounting Standards Board, or FASB, has issued the following new accounting and interpretations, which may be applicable in the future to us:

There are no Accounting Standards Updates expected to have a significant effect on the Company’s consolidated financial position or results of operations.

Actual results could differ materially from the estimates and assumptions that we use in the preparation of our financial statements.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk

As a smaller reporting company we are not required to provide this information under Item 305 of Regulation S-K.

Item 8. Financial Statements and Supplementary Data

Index to Financial Statements

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors
N-Viro International Corporation

We have audited the accompanying consolidated balance sheets of N-Viro International Corporation (a Delaware corporation) and Subsidiaries as of December 31, 2011 and 2010, and the related consolidated statements of operations, stockholders' equity (deficit), and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Company'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 the standards of the Public Company Accounting Oversight Board (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. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audit included 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 company'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 consolidated financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of N-Viro International Corporation and Subsidiaries as of December 31, 2011 and 2010, and the results of their operations and their cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

/s/ UHY LLP
UHY LLP
Farmington Hills, Michigan
March 30, 2012

N-VIRO INTERNATIONAL CORPORATION

CONSOLIDATED BALANCE SHEETS

December 31, 2011 and 2010

	2011	2010
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents:		
Unrestricted	$44,498	$37,112
Restricted	208,510	207,465
Receivables, net:		
Trade	416,192	780,844
Related party - Mahoning Valley N-Viro	-	24,325
Other	18,073	-
Deferred costs - stock and warrants issued for services	547,012	622,086
Prepaid expenses and other assets	97,155	80,994
Total current assets	1,331,440	1,752,826
PROPERTY AND EQUIPMENT, NET	1,327,320	1,490,865
INTANGIBLE AND OTHER ASSETS, NET	91,800	159,304
	$2,750,560	$3,402,995

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

N-VIRO INTERNATIONAL CORPORATION

CONSOLIDATED BALANCE SHEETS

December 31, 2011 and 2010

	2011	2010
LIABILITIES AND STOCKHOLDERS' EQUITY (DEFICIT)		
CURRENT LIABILITIES		
Current maturities of long-term debt	$277,190	$337,799
Note Payable - related party	200,000	-
Convertible debentures, net of discount	90,000	667,674
Line of credit	300,000	364,000
Accounts payable	833,068	1,089,513
Accrued liabilities	39,798	226,062
Total current liabilities	1,740,056	2,685,048
Long-term debt, less current maturities	211,716	230,931
Fair value of warrant liability	12,196	744,476
Convertible debentures - long-term, net of discount	340,447	-
Total liabilities	2,304,415	3,660,455
COMMITMENTS AND CONTINGENCIES		
STOCKHOLDERS' EQUITY (DEFICIT)		
Preferred stock, $.01 par value, Authorized - 2,000,000 shares		
Issued - -0- shares in 2011 and 2010	-	-
Common stock, $.01 par value		
Authorized - 35,000,000 shares		
Issued - 6,191,420 shares in 2011 and 6,062,214 shares in 2010	61,914	60,622
Note receivable for common stock	-	(300,000)
Additional paid-in capital	26,883,156	24,548,644
Accumulated deficit	(25,814,035)	(23,881,836)
	1,131,035	427,430
Less treasury stock, at cost, 123,500 shares	684,890	684,890
Total stockholders' equity (deficit)	446,145	(257,460)
	$2,750,560	$3,402,995

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

N-VIRO INTERNATIONAL CORPORATION

CONSOLIDATED STATEMENTS OF OPERATIONS

Years Ended December 31, 2011 and 2010

	2011	2010
REVENUES	$5,593,665	$5,222,146
COST OF REVENUES	4,560,852	4,217,773
GROSS PROFIT	1,032,813	1,004,373
OPERATING EXPENSES		
Selling, general and administrative	3,515,617	3,767,262
OPERATING LOSS	(2,482,804)	(2,762,889)
OTHER INCOME (EXPENSE)		
Interest income	1,073	1,110
Gain on extinguishment of liabilities	217,342	124,233
Amortization of discount on convertible debentures	(60,510)	(108,335)
Gain on debt modification (debentures)	32,737	-
Gain (loss) on market price change of warrants issued	732,280	(140,326)
Interest expense	(79,911)	(82,938)
	843,011	(206,256)
LOSS BEFORE INCOME TAXES	(1,639,793)	(2,969,145)
Federal and state income taxes	-	-
NET LOSS	$(1,639,793)	$(2,969,145)
Basic and diluted loss per share	$(0.27)	$(0.55)
Weighted average common shares outstanding - basic and diluted	5,988,077	5,396,018

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

N-VIRO INTERNATIONAL CORPORATION

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY (DEFICIT)

Years Ended December 31, 2011 and 2010

	Shares of Common Stock	Common Stock	Note Receivable for Common Stock	Additional Paid-in Capital	Accumulated Deficit	Treasury Stock	Total
BALANCE – JANUARY 1, 2010	5,269,553	$52,696	$ -	$21,453,168	$(20,300,837)	$(684,890)	$520,137
Net loss	-	-	-	-	(2,969,145)	-	(2,969,145)
Deemed dividend on extension of stock warrants	-	-	-	611,854	(611,854)	-	-
Issuance of common stock for cash and Note Receivable - net	400,000	4,000	(300,000)	996,000	-	-	700,000
Share-based compensation expense	-	-	-	1,031,770	-	-	1,031,770
Exercise of stock options	54,125	541	-	101,306	-	-	101,847
Exercise of stock warrants	15,050	150	-	27,640	-	-	27,790
Conversion of debentures to stock	45,136	451	-	89,725	-	-	90,176
Discount on convertible debentures issued	2,750	28	-	21,958	-	-	21,986
Issuance of common stock	275,600	2,756	-	215,223	-	-	217,979
BALANCE – DECEMBER 31, 2010	6,062,214	60,622	(300,000)	24,548,644	(23,881,836)	(684,890)	(257,460)
Net loss	-	-	-	-	(1,639,793)	-	(1,639,793)
	-	-	-	132,642	(132,642)	-	-

Deemed dividend on extension of stock warrants								
Cancellation of common stock and Note Receivable on Agreement termination - net	(120,000)	(1,200)		300,000	(282,310)	-	-	16,490
Extension of stock warrants	-	-	-		26,236	-	-	26,236
Share-based compensation expense	-	-	-		1,781,842	-	-	1,781,842
Exercise of stock options	515	5	-		979	-	-	984
Exercise of stock warrants	800	8	-		7	-	-	15
Purchase of stock warrants	-	-	-		169,765	(159,764)	-	10,001
Conversion of debentures to stock	27,028	270	-		49,690	-	-	49,960
Issuance of common stock	220,863	2,209	-		455,661	-	-	457,870
BALANCE – DECEMBER 31, 2011	6,191,420	$61,914	$	-	$26,883,156	$(25,814,035)	$(684,890)	$446,145

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

N-VIRO INTERNATIONAL CORPORATION

CONSOLIDATED STATEMENTS OF CASH FLOWS

Years Ended December 31, 2011 and 2010

	2011	2010
Cash Flows From Operating Activities		
Net loss	$(1,639,793)	$(2,969,145)
Adjustments to reconcile net loss to net cash from operating activities:		
Depreciation and amortization	539,744	449,122
Amortization of debenture stock discount	60,510	108,334
Debenture stock discount	(32,737)	-
Issuance of stock options and warrants for services	1,794,642	1,183,270
Issuance of stock for debt and services	420,973	1,103,153
Loss on investment in Mahoning Valley N-Viro	24,279	-
Provision (reduction) for bad debts	-	20,000
(Gain) loss on the sale of fixed assets	(23,978)	(8,741)
(Increase) decrease in market price of warrants issued	(732,280)	140,326
Changes in Operating Assets and Liabilities		
Decrease (increase) in trade receivables	351,852	(203,809)
Decrease (increase) in prepaid expenses and other assets	(3,437)	33,148
Increase (decrease) in accounts payable and accrued liabilities	(426,396)	148,263
Net cash provided by operating activities	333,379	3,921
Cash Flows From Investing Activities		
Proceeds from sale of property and equipment	56,405	10,834
Advances to related parties	-	(9,000)
Increases from restricted cash and cash equivalents	(1,045)	(67,305)
Purchases of property and equipment	(357,384)	(532,454)
Net cash used in investing activities	(302,024)	(597,925)
Cash Flows From Financing Activities		
Borrowings under long-term debt	418,037	196,869
Borrowings from related party - short-term	200,000	-
Net proceeds from issuance of common stock in private placement	96,850	611,994
Proceeds from stock warrant transactions	87,021	27,735
Proceeds from stock options exercised	984	101,873
Proceeds from convertible debentures issued, net of issuance costs	-	54,865
Net advances (repayments) on line-of-credit	(64,000)	39,000

Repayments of convertible debentures	(265,000)	-
Principal payments on long-term obligations	(497,861)	(462,600)
Net cash provided (used) by financing activities	(23,969)	569,736
Net Increase (Decrease) in Cash and Cash Equivalents	7,386	(24,268)
Cash and Cash Equivalents - Beginning	37,112	61,380
Cash and Cash Equivalents - Ending	$44,498	$37,112
Supplemental disclosure of cash flows information:		
Cash paid during the year for interest	$129,818	$138,477

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

N-VIRO INTERNATIONAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010

Note 1. Operations and Summary of Significant Accounting Policies

The following is a summary of certain accounting policies followed in the preparation of these financial statements. The policies conform to generally accepted accounting principles and have been consistently applied in the preparation of the financial statements:

A. Nature of Business – The Company owns and licenses the N-Viro Process, a patented technology to treat and recycle wastewater sludges and other bio-organic wastes, utilizing certain alkaline by-products produced by the cement, lime, electric utilities and other industries. Revenue and the related accounts receivable are due from companies acting as independent agents or licensees, principally municipalities.

B. 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 as of 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.

C. Principles of Consolidation – The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. All significant intercompany accounts and transactions have been eliminated in consolidation.

D. Cash and Cash Equivalents – The Company has cash on deposit primarily in one financial institution which, at times, may be in excess of FDIC insurance limits.

For purposes of the statements of cash flows, the Company considers all certificates of deposit with initial maturities of 90 days or less to be cash equivalents.

Restricted cash consists of: two certificates of deposit and corresponding accrued interest which are held as collateral against the Company's line-of-credit; one certificate of deposit and corresponding accrued interest which is held as collateral with a performance bond on behalf of one of the Company’s licensees; one certificate of deposit and corresponding accrued interest which is held as collateral on behalf of the Florida Department of Agriculture for the Company’s soil distribution license.

E. Accounts Receivable – The Company extends unsecured credit to customers under normal trade agreements, which require payment within 30 days. Accounts greater than 90 days past due amounted to $67,344 and $61,698 of receivables for the years ended December 31, 2011 and 2010, respectively. The Company's policy is not to accrue and record interest income on past due trade receivables. The Company does bill the customer finance charges on past due accounts and records the interest income when collected. Credit is generally granted on an unsecured basis. Periodic credit evaluations of customers are conducted and appropriate allowances are established.

Management estimates an allowance for doubtful accounts, which was $70,000 as of both December 31, 2011 and 2010. The estimate is based upon management’s review of delinquent accounts and an assessment of the Company’s historical evidence of collections.

N-VIRO INTERNATIONAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010

Note 1. Operations and Summary of Significant Accounting Policies (Continued)

F. Property and Equipment – Property, machinery and equipment are stated at cost less accumulated depreciation. Depreciation has been computed primarily by the straight-line method over the estimated useful lives of the assets. Generally, useful lives are five to fifteen years. Leasehold improvements are capitalized and amortized over the lesser of the life of the lease or the estimated useful life of the asset. Depreciation expense amounted to $514,748 and $416,172 in 2011 and 2010, respectively. Management has reviewed property and equipment for impairment when events and circumstances indicate that the assets might be impaired and the carrying values of those assets may not be recoverable. Management believes the carrying amount is not impaired based upon estimated future cash flows.

G. Intangible Assets – Patent costs and territory rights are recorded at cost and then amortized by the straight-line method over their estimated useful lives (periods ranging from one and one-half to seventeen years; weighted-average amortization periods for patents/related intangibles and territory rights were 14.2 and 15.8 years at December 31, 2011 and 2010, respectively). Amortization expense amounted to $23,276 and $26,691 in 2011 and 2010, respectively. Estimated amortization expense, based on these patent costs and territory rights at December 31, 2011, for each of the ensuing five years is as follows: 2012 - $13,000; 2013 - $13,000; 2014 - $13,000; 2015 - $12,000; 2016 - $9,000. Management has reviewed intangible assets for impairment when events and circumstances indicate that the assets might be impaired and the carrying values of those assets may not be recoverable.

The Company has capitalized the cost of acquiring certain customer licenses and contracts as part of the acquisition of Florida N-Viro on December 31, 2006. Amortization expense amounted to $1,719 in 2011 and $6,259 in 2010. Estimated amortization expense, based on these capitalized license and contracts at December 31, 2011, for each of the ensuing five years is as follows: 2012 - $1,700; 2013 - $1,700; 2014 - $1,700; 2015 - $1,700; 2016 - $500.

H. Revenue Recognition – Facility management revenue and royalty fees are recognized under contracts where the Company or licensees utilize the N-Viro Process to treat sludge, either pursuant to a fixed-price contract or based on volumes of sludge processed. Revenue is recognized as services are performed.

Alkaline admixture sales, alkaline admixture management service revenue and N-Viro SoilTM revenue are recognized upon shipment.

License and territory fees are generated by selling the right to market or use the N-Viro Process in a specified territory. The Company's policy is to record revenue for the license agreements when all material services relating to the revenue have been substantially performed, conditions related to the contract have been met and no material contingencies exist. We do not recognize revenue on any non-domestic license or territory fee contracts until the cash is received, assuming all other tests of revenue recognition are met. Canada is excluded from this definition of non-domestic. Research and development revenue is recognized as work is performed and billed to the contracting entity in accordance with the contract.

The Company records the amount of shipping and handling costs billed to customers as revenue. The cost incurred for shipping and handling has been included in the cost of sales.

N-VIRO INTERNATIONAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010

Note 1. Operations and Summary of Significant Accounting Policies (Continued)

I. Loss Per Common Share – Loss per common share has been computed on the basis of the weighted-average number of common shares outstanding during each period presented. For the years ended December 31, 2011 and 2010, the effects of 2,924,985 and 2,273,300 stock options outstanding, respectively, 1,444,585 and 1,147,350 warrants to purchase common stock, respectively, and, debentures that are convertible to 227,500 and 360,000 shares of common stock, respectively, are excluded from the diluted per share calculation because they would be antidilutive.

J. Stock Options – The Company records share-based compensation expense using a fair-value based method of measurement that results in compensation costs for essentially all awards of stock-based compensation to employees. Compensation costs are recognized over the requisite period or periods that services are rendered.

K. New Accounting Standards – There are no Accounting Standards Updates expected to have a significant effect on the Company’s consolidated financial position or results of operations.

L. Income Taxes – Deferred income tax assets and liabilities are computed annually for differences between the financial statement and tax bases of assets and liabilities that will result in taxable or deductible amounts in the future based on enacted tax laws and rates applicable to the periods in which the differences are expected to affect taxable income. Valuation allowances are established when necessary to reduce deferred tax assets to the amount expected to be realized. Income tax expense is the tax payable or refundable for the current period plus or minus the change during the period in deferred tax assets and liabilities.

The accounting for uncertain tax positions requires the Company to evaluate each income tax position using a two step process which includes a determination as to whether it is more likely than not that the income tax position will be sustained, based upon technical merit and upon examination by the taxing authorities. At December 31, 2011 and 2010, there were no uncertain tax positions that required accrual. None of the Company’s federal or state income tax returns are currently under examination by the Internal Revenue Service (“IRS”) or state authorities. However, fiscal years 2008 and later remain subject to examination by the IRS and respective states.

M. Supplemental Disclosure of Non-Cash Activity:

	2011	2010
Common Stock issued for commissions on debentures $	-	$5,500
Burnham Hill Consulting - commission not due on cancellation of license of VC Energy agreement	18,000	-
VC Energy - issuance of common stock warrants -		604,150
Deemed dividend on extension of outstanding stock warrants	132,642	611,854
SLD Consulting - value of stock issued on consulting agreement -		334,400
	210,307	304,500

SAMI - value of stock issued on public relations agreement		
Rakgear - value of stock issued on consulting agreement	73,000	-
Conversion of debentures to Common Stock -		90,204
	$433,949	$1,950,608

N. Segment Information – During 2011, the Company determined that it currently operates in one segment based on the financial information upon which the chief operating decision maker regularly assesses performance and allocates resources. The chief operating decision maker is the Chief Executive Officer.

Note 2. Balance Sheet Data

Property and equipment (at cost):

	2011	2010
Buildings and leasehold improvements	$290,129	$121,411
Equipment	3,169,055	3,296,751
Furniture, fixtures and computers	63,838	50,089
	3,523,022	3,468,251
Less accumulated depreciation	2,195,702	1,977,386
	$1,327,320	$1,490,865

Deferred costs:

In December 2010, the Company executed a Financial Public Relations Agreement with Strategic Asset Management, Inc., or SAMI. The Company engaged SAMI as its non-exclusive financial public relations counsel for a term of three years. For its services, the Company issued SAMI 150,000 shares of the Company's unregistered common stock. The Company is recording a non-cash charge to earnings of approximately $305,000 ratably over a 36-month period starting in December 2010. For the year ended December 31, 2011, the charge to earnings was approximately $101,500.

In August 2011, the Company issued 100,000 shares of common stock and granted 100,000 stock warrants to SAMI for additional services performed in connection with the December 2010 Financial Public Relations Agreement. To reflect the entire value of the stock and warrants issued, the Company is taking a charge to earnings of $285,700 through December 2013, the ending date of the agreement. For the year ended December 31, 2011, the charge to earnings was approximately $99,200.

In December 2010, the Company executed a Consulting Agreement, with SLD Capital Corporation, or SLD. The Company engaged SLD to provide business consulting services for a term of eighteen months. For its services, the Company issued SLD 110,000 shares of the Company's unregistered common stock. The Company is recording a non-cash charge to earnings of approximately $334,000 ratably over an 18-month period starting in December 2010. For the year ended December 31, 2011, the charge to earnings was approximately $223,000.

In November, 2011, the Company executed a Consulting Agreement with Rakgear, Inc. The Company engaged Rakgear to provide business consulting services for a term of one year. For its services, the Company issued Rakgear 50,000 shares of the Company's unregistered common stock. The Company is recording a non-cash charge to earnings of $73,000 ratably over a 12-month period starting in November 2011. For the year ended December 31, 2011, the charge to earnings was approximately $10,000.

N-VIRO INTERNATIONAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010

Note 2. Balance Sheet Data (Continued)

The following is a summary of Deferred Costs – capitalized stock value on contracts, net as of December 31:

	2011	2010
Deferred costs - Rakgear, Inc., less accumulated amortization (2011 - $10,139; 2010 - $-0-)	$62,861	$ -
Deferred costs - SAMI, less accumulated amortization (2011 - $204,931; 2010 - $4,229)	385,269	300,271
Deferred costs - SLD Capital, less accumulated amortization (2011 - $235,518; 2010 - $12,585)	98,882	321,815
	$547,012	$622,086

Intangible and other assets:

The following is a summary of intangible and other assets, net as of December 31:

	2011	2010
Patents and related intangibles, less accumulated amortization (2011 - $103,908; 2010 - $294,327)	$64,581	$99,926
Territory rights, less accumulated amortization (2011 - $-0-; 2010 - $6,470)	-	3,530
Customer list, less accumulated amortization (2011 - $55,365; 2010 - $53,646)	7,390	9,109
Debenture issuance costs, less accumulated amortization (2011 - $61,667; 2010 - $44,925)	-	16,742

Other	19,829	29,997
	$91,800	$159,304

N-VIRO INTERNATIONAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010

Note 2. Balance Sheet Data (Continued)

Accrued liabilities:

	2011	2010
Accrued payroll and employee benefits	$29,062	$32,192
Sales tax payable	-	177,421
Interest payable	10,735	16,449
	$39,797	$226,062

During the fourth quarter of 2011, the Company recognized $174,000 of gain for the reversal of a recorded sales tax liability management determined is no longer due.

Note 3. Pledged Assets, Line-of-Credit and Long-Term Debt

During 2011, the Company maintained a line of credit with Monroe Bank + Trust, or the Bank, up to $400,000 bearing interest at the Wall Street Journal Prime Rate (3.25% at December 31, 2011) plus 0.75%, but in no event less than 5.00%, and secured by a first lien on all our assets (except equipment), with a new maturity date of August 15, 2012. Two certificates of deposit totaling $141,430 from the Bank are held as a condition of maintaining the line of credit. At December 31, 2011, we had $100,000 of borrowing capacity under the credit facility.

Long-term debt at December 31, 2011 and 2010 is as follows:

	2011	2010
Notes payable - banks	$209,527	$365,703
Notes payable - equipment vendors	279,379	203,027
Convertible debentures, net of discount of $24,553 in 2011 and $52,326 in 2010	430,447	667,674
	919,353	1,236,404
Less current maturities	367,190	1,005,473
	$552,163	$230,931

During 2011, the Company borrowed a total of $163,853 from two lenders to purchase insurance policies for general, property and directors & officers' insurance coverage during the year. A total of two term notes were issued, ranging from 6% to 6.6% interest for a term not more than one year, monthly payments totaling $16,844 and each are unsecured. The total amount owed on these notes as of December 31, 2011 was approximately $46,200 and these notes are expected to be paid in full on the applicable maturity date, the last of which is August 2012.

N-VIRO INTERNATIONAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010

Note 3. Pledged Assets, Line-of-Credit and Long-Term Debt (Continued)

From the beginning of 2006 through 2011, the Company borrowed a total of $1,677,100 from ten lenders to purchase processing and automotive equipment. As of December 31, 2011, a total of thirteen term notes are outstanding, ranging from 6.2% to 10.9% interest for terms ranging three to five years, monthly payments totaling approximately $26,000 and all secured by equipment. The total amount owed on all equipment-secured notes as of December 31, 2011 was approximately $442,000 and all notes are expected to be paid in full on the applicable maturity date, the last of which is in March 2016.

In 2009 the Company approved an offering of up to $1,000,000 of Convertible Debentures (the “Debentures”), convertible at any time into the Company’s unregistered common stock at $2.00 per share. The Debentures are issuable in $5,000 denominations, are unsecured and have a stated interest rate of 8%, payable quarterly to holders of record. The Company has timely paid all accrued interest due to all Debenture holders of record as of each quarter-end date starting in July 2009. At any time, the Company may redeem all or a part of the Debentures at face value plus unpaid interest.

During 2009 the Company issued $765,000 of Debentures to a total of twenty-three accredited investors, and one investor converted $10,000 of Debentures into unregistered common stock. During 2010 the Company issued $55,000 of Debentures, and three investors converted a total of $90,000 of Debentures into unregistered common stock. The Debentures matured at June 30, 2011, however fifteen investors holding Debentures totaling $365,000 elected to replace them with new ones that now mature at June 30, 2013. All other features of the “expired” Debentures remained the same in the replacement ones, except for the new maturity date. Of the four investors totaling $355,000 who did not replace their existing Debentures with new ones, two investors totaling $215,000 had their Debentures repaid; one investor converted $50,000 into unregistered common stock (at June 30, 2011) and one holding $90,000 of Debentures has not made a final decision. As of December 31, 2011, the Company held $455,000 of Debentures.

Because the fair market value of the Company’s common stock (the underlying security in the Debentures) may have been above the conversion price of $2.00 per share at the date of issuance, the Company was required under GAAP to record a discount given for certain (now) “expired” Debentures sold, which totaled $184,975. The discount was then required to be amortized as a period expense over the periods the Debentures were scheduled to be outstanding, which averaged 20 months, through the maturity date of June 30, 2011. For the year ended December 31, 2011 and 2010, amortization expense on the “expired” Debentures amounted to $52,326 and $108,334, respectively.

For periods subsequent to June 30, 2011, the Company is required under GAAP to record a discount totaling $32,737 for certain Debentures replaced, and a gain on debt modification during the quarter ended June 30, 2011. The discount is required to be amortized as a period expense over the next eight quarters the Debentures are scheduled to be outstanding. For the six months ended December 31, 2011 these “replacement” debentures have been outstanding, amortization expense amounted to $8,184.

Approximate aggregate maturities of long-term debt for the years ending December 31 are as follows: 2012 - $567,000; 2013 - $460,000; 2014 - $59,000; 2015 - $27,000; 2016 - $6,000.

Note 4. Related Party Transactions

On August 1, 2011, the Company borrowed $200,000 with a Promissory Note payable to a related party of Timothy Kasmoch, the Company's President and Chief Executive Officer, at 12% interest prepaid for a period of three months, renewable for an additional three months by the prepayment of additional interest and secured by certain equipment. Mr. Kasmoch has personally guaranteed the repayment of this Note. The Company extended the Note on October 30, 2011 and again on January 30, 2012, and is now due April 30, 2012. The Company expects to extend the Note on or before the due date but pay the Note in full during 2012.

N-VIRO INTERNATIONAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010

Note 4. Related Party Transactions (Continued)

During the year ended December 31, 2010 the Company advanced funds for operating capital of $9,000 to its joint venture limited liability company, Mahoning Valley N-Viro. Mahoning Valley N-Viro is owned 50% by the Company and 50% by SouthSide Environmental Group of Struthers, Ohio. As no financial activity occurred in Mahoning Valley N-Viro during 2010 and 2011 and the outlook unlikely of having future operations, the Company determined that the total $24,325 loaned by the Company to date would not be repaid and wrote down the investment to a net realizable value of zero as of December 31, 2011.

Also during 2011 and 2010, the Company paid Terri Kasmoch, the spouse of President and Chief Executive Officer Timothy Kasmoch, outside consulting fees for business development, web site and company media marketing and stock promotion efforts for the Company, and as an employee with the same duties starting in the 4th quarter of 2010.

During the year ended December 31, 2011, the Company rented and purchased equipment, and contracted for repair services with Tri-State Garden Supply dba Gardenscape, a company owned and managed by the extended family of the Company's Chief Executive Officer, Timothy Kasmoch.

During the year ended December 31, 2010, the Company paid Thomas L. Kovacik, a member of the Board of Directors, a fee for consulting services. The fee was paid with 10,000 stock options at an exercise price of $3.53, which vested immediately and are exercisable over 10 years. To reflect the value of the options, the Company recorded an expense of $31,421. The fee was exclusive of director fees and expenses paid for with cash and stock options.

The following table summarizes these payments for 2011 and 2010 and the balance to each of any monies owed as of December 31, 2011:

Payee	Year	Consulting fees	Gross Payroll	Rental, Equipment and Repairs	Total	Account payable balance at December 31
Terri Kasmoch	2011	$ -	$52,000	$ -	$52,000	$ -
Terri Kasmoch	2010	10,685	10,833	-	21,518	-
Gardenscape	2011	-	-	15,214	15,214	12,500
Thomas L. Kovacik	2010	31,421	-	-	31,421	-

Note 5. Equity Transactions

In January 2010, the Company executed a Placement Agent Agreement, or the Agreement, with Burnham Hill Partners of New York, NY, or BHP. The Company engaged BHP as its placement agent in connection with the issuance of debt or equity securities through a transaction exempt from registration for a term of six months from the date of the Agreement. For its services, the Company issued BHP 10,000 shares of the Company's unregistered common stock. The shares were issued in a private transaction pursuant to an exemption under Section 4(2) of the Securities Act of 1933. If the Company had secured a financing placement through BHP, the Company would have issued common stock placement warrants equal to 8% of the number of common stock shares issued in the financing, for a term of seven years and would have been exercisable at 120% of the price paid per share by the investors. The Company accounted for this transaction by recording a deferred current asset of $30,000 that was amortized ratably over the subsequent six month period the services were rendered in 2010.

N-VIRO INTERNATIONAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010

Note 5. Equity Transactions (continued)

In December 2010, the Company issued 110,000 shares of unregistered Common Stock to SLD Capital Corporation ("SLD"), as compensation for services rendered by SLD to the Company under a Consulting Agreement, effective as of December 10, 2010. The agreement is for a term of eighteen months from the effective date. More details of this Agreement are contained in Note 2.

In July 2010, the Company executed a Purchase Agreement, License and Development Agreement and Registration Rights Agreement (the "Agreements"), with VC Energy I, LLC of Las Vegas, NV, or VC Energy. Concurrently, the Company sold VC Energy 200,000 shares of the Company's unregistered common stock at a price of $2.50 per share, issued VC Energy 200,000 warrants exercisable at $2.75 per share, and also granted VC Energy an option to acquire another 400,000 shares of the Company's unregistered common stock at a price of $2.50 per share, and 400,000 warrants exercisable at $2.75 per share.

In September 2010, the Company executed Amendment Number 1, effective September 15, 2010 (the "Amendment") to the Purchase Agreement with VC Energy. The purpose of the Amendment was to modify certain of the purchase terms in the Purchase Agreement, and VC Energy exercised its option to purchase 200,000 shares of the Company's common stock for $500,000 which VC Energy paid for by delivering its unsecured promissory note to the Company for $500,000, payable in installments over a 12 month period, with the first $200,000 of such installments due bi-weekly between September 30, 2010 and December 30, 2010 and the final $300,000 due September 15, 2011. The promissory note provided for acceleration in the event of default and a default interest rate of 8% per annum. The Company also delivered 200,000 warrants to purchase shares of its common stock at an exercise price of $2.50 per share. Under the Amendment, the Company transferred all 200,000 shares and 200,000 warrants to an Escrow Agent, and the shares and warrants were to be released ratably to VC Energy as installments payments due the Company were received. VC Energy made all installment payments due through December 2010, and the escrow agent delivered 80,000 shares and 80,000 warrants to VC Energy, with the remaining shares and warrants continuing to be held by the escrow agent. In addition, VC Energy's option to purchase the remaining 200,000 shares of the Company's common stock was extended to December 31, 2010 and then a second time to March 1, 2011, on the same terms as the original Purchase Agreement. VC Energy did not exercise the purchase option for the additional 200,000 shares on or before March 1, 2011. At each extension date, the Company recorded a deemed dividend for the increase in value of the purchase option as a reduction to Accumulated Deficit and an increase to the Additional Paid In Capital accounts, totaling $150,387 in 2010.

In August 2011, the Company and VC Energy signed a Termination Agreement and terminated the License and Development Agreement dated June 29, 2010, the Promissory Note dated September 15, 2010 and the Escrow Agreement dated September 15, 2010. Included in these agreements was VC Energy's option to purchase the unpaid balance of 120,000 shares of the Company's common stock for $300,000. All other agreements between the Company and VC Energy remain in force, except to the extent the provisions contained in them are inconsistent with the terms and conditions of the Termination Agreement. In September 2011, the Company cancelled the 120,000 shares of common stock that were returned by operation of the Termination Agreement.

In both the VC Energy Agreements and the Amendment, the Company accounted for the warrants issued within the transaction with a provision that protects holders from declines in the stock price ("down-round" provisions) as a derivative security at fair value with future changes in fair value recorded in earnings. As of December 31, 2011, the Company has recorded a liability of $12,196 to reflect the fair value of the outstanding warrants. The Company will be periodically required to re-measure the fair value of the remaining warrants at the Balance Sheet date, with adjustments in the value recorded through the income statement as a gain or loss. During the twelve months ended December 31, 2011 and 2010, the Company recorded a gain of $732,280 and a loss of $140,326, respectively, on the revaluation and partial cancellation from the two issuances of the warrants to the end of the period, which includes the gain in 2011 from the cancellation of 120,000 warrants as a result of the Termination Agreement.

N-VIRO INTERNATIONAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010

Note 5. Equity Transactions (continued)

In December 2010, the Company issued 150,000 shares of unregistered Common Stock to Strategic Asset Management, Inc., ("SAMI"), as compensation for services rendered by SAMI to the Company under a Financial Public Relations Agreement, effective as of December 15, 2010. The agreement is for a term of two years from the effective date. More details of this Agreement are contained in Note 2.

In August 2011, the Company issued 100,000 shares of common stock to SAMI for additional services performed in connection with the December 2010 consulting agreement. To reflect the entire value of the stock issued, the Company is taking a charge to earnings of $150,000 through December 2013, the ending date of the consulting agreement. For the twelve months ended December 31, 2011, the charge to earnings was $52,100. The Company also granted 100,000 stock warrants in connection with this transaction. All the warrants are exercisable over a five year term, vest immediately and were priced at a premium over the fair market value of the Company's common stock as of the date of the grant, or $1.65 per warrant. To reflect the entire value of the stock warrants granted, the Company is taking a charge to earnings totaling approximately $136,000 through December 2013. For the twelve months ended December 31, 2011, the charge to earnings was approximately $47,100.

In November 2011, the Company issued 50,000 shares of unregistered common stock to Rakgear, Inc. for business consulting services. To reflect the entire value of the stock issued, the Company is taking a non-cash charge to earnings of $73,000 ratably through December 2013, the ending date of the agreement. For the twelve months ended December 31, 2011, the charge to earnings was approximately $10,000.

During 2011, we sold a total of 70,863 shares of unregistered restricted stock to five non-beneficial owners for total gross cash proceeds of $112,400. These proceeds were all used for operating expenses. Simultaneously and subject to the same terms and conditions, we issued a total of 64,263 warrants to two non-beneficial owners to acquire shares of our common stock at a price above the purchase price each owner paid for our common stock, which was the fair market value of the stock on the date of each transaction. In all instances the shares and the warrants issued and sold were in a private offering transaction pursuant to an exemption under Section 4(2) of the Securities Act of 1933 for transactions by an issuer not involving a public offering.

Also during 2011, the Convertible Debentures matured, fifteen investors elected to replace their Debentures with new ones, two investors had theirs repaid and one investor converted $50,000 into 25,000 shares of unregistered common stock. The amount of Debentures outstanding at the end of 2011 was $455,000, convertible at $2.00 per share or 227,500 shares. More details on these transactions can be found in Note 3.

In addition to its first stock option plan approved in 1993, the Company has a stock option plan approved in May 2004, amended in June 2008 and again in August 2009 (the "2004 Plan"), for directors and key employees under which 2,500,000 shares of common stock may be issued. The Company also has a stock option plan approved in July 2010 (the "2010 Plan"), for directors and key employees under which 5,000,000 shares of common stock may be issued. Unless otherwise stated in the stock option agreement, options are 20% vested on the date of grant, with the balance vesting 20% per year over the next four years, except for directors whose options vest six months from the date of grant. Options were granted in 2011 from the 2010 Plan and in 2010 from the 2004 Plan at the approximate market value of the stock at date of grant, as defined in each of the plans.

Pursuant to their respective five-year employment agreements, in March 2010 a total of 890,000 stock options were granted to the three executive officers of the Company. Twenty percent of the options vested immediately on the date of grant, with the balance of the options to vest in equal annual installments over the next four years on the anniversary date of the original grant. These options were granted pursuant to the 2004 Plan, are for a period of ten years and are intended as Incentive Stock Options. To reflect the value of the stock options granted for the employment services provided, the Company is taking a charge to

N-VIRO INTERNATIONAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010

Note 5. Equity Transactions (continued)

earnings totaling approximately $2,358,000 through March 2014. For the years ended December 31, 2011 and 2010, this charge was $471,539 and $844,840, respectively.

In August 2011, the Company granted 500,000 stock options to its Chief Executive Officer, Timothy Kasmoch. The options are for a period of ten years, are pursuant to the 2010 Plan, are exercisable at $1.63 and vest immediately. To reflect the value of the stock options granted, the Company took an immediate charge to earnings during the third quarter of 2011 totaling approximately $720,000.

More information on these equity transactions is contained in this Form 10-K under Item 11, “Executive Compensation”.

During the year ended December 31, 2011, the Company granted stock options totaling 180,000 shares, exclusive of the officers, to all outside directors. All options granted are for a period of ten years. The options became fully vested six months after the date of grant, and were priced, pursuant to the 2010 Plan, at $1.78 for a total expense of approximately $321,000, expensed ratably and fully in 2011 over the subsequent six-month period. More information on these equity transactions is contained in this Form 10-K under Item 10, “Directors, Executive Officers and Corporate Governance”.

During the year ended December 31, 2010, the Company granted additional stock options totaling 175,000 shares, exclusive of the officers: 90,000 options to outside directors, 10,000 options to an outside director acting in his capacity as a consultant and 75,000 options to three employees. All options granted are for a period of ten years. The options granted in 2010 to the directors became fully vested six months after the date of grant, and were priced, pursuant to the 2004 Plan, at a weighted average price of $3.08 for a total expense of approximately $209,000, expensed ratably over the subsequent six-month period. The options granted to the consultant vested immediately and were priced, pursuant to the 2004 Plan, at $3.53 for a total expense of approximately $31,400, expensed immediately. More information on these equity transactions is contained in this Form 10-K under Item 10, “Directors, Executive Officers and Corporate Governance”.

The options granted in 2010 to the three employees vested twenty percent on the date of grant, with the balance of the options to vest in equal annual installments over the next four years on the anniversary date of the original grant. All of the options are exercisable at $1.89 per share and were granted pursuant to the 2004 Plan and are intended as Incentive Stock Options.

N-VIRO INTERNATIONAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010

Note 5. Equity Transactions (continued)

The following summarizes the stock options activity for the years ended December 31, 2011 and 2010:

	2011		2010	
	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price
Outstanding, beginning of year	2,273,300	$2.67	1,279,825	$2.24
Granted	680,000	$1.67	1,065,000	$3.16
Exercised	(515)	$1.94	(54,125)	$1.91
Expired/forfeited during the year	(27,800)	$1.71	(17,400)	$3.75
Outstanding, end of year	2,924,985	$2.44	2,273,300	$2.67
Eligible for exercise at end of year	2,360,985	$2.26	1,501,300	$2.41
Weighted average fair value per option for options granted during the year	$1.67		$3.16	
Options expected to vest over the life of the Plan	2,924,985		2,273,300	

The Company records compensation expense for stock options based on the estimated fair value of the options on the date of grant using the Black-Scholes valuation model. The Company uses historical data among other factors to estimate the expected price volatility, the expected option term and the expected forfeiture rate. The risk-free rate is based on the U.S. Treasury yield curve in effect at the date of grant for the expected term of the option.

The following assumptions were used to estimate the fair value of options granted:

	Year Ended December 31,	
	2011	2010
Expected dividend yield	0.00%	0.00%
Weighted average volatility	203.4%	73.7%
Risk free interest rate	2.1 - 3.2%	2.5 - 3.6%
Expected term (in years)	5	7

On two occasions during 2010, all holders of N-Viro International Corporation warrants were granted an automatic extension of time to exercise their respective warrants. On one more occasion in August 2011, an automatic extension of time was granted to certain warrant holders of record to exercise their respective warrants. For all of the extensions, all other terms of the warrant remained in place, other than the expiration date. The incremental fair value associated with the extension of the warrant expiration dates has been determined using the Black-Scholes model and has been recorded as a deemed dividend to common stockholders in the accompanying Statement of Stockholders' Equity (Deficit). For the years ended December 31, 2011 and 2010, the deemed dividend was $132,642 and $461,467 respectively.

N-VIRO INTERNATIONAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010

Note 6. Revenue and Major Customers

Revenues for the years ended December 31, 2011 and 2010 billed through N-Viro International Corporation include revenues from one major customer, the City of Toledo, Ohio (included in the facility management, and, products and services classifications), which represented approximately 17% for 2011 and 22% for 2010 of total consolidated revenue. The accounts receivable balance due (which is unsecured) from this customer at December 31, 2011 and 2010 was approximately $1,000 and $68,000, respectively. The Company's agreement with the City of Toledo, our largest customer for many years through 2010, was not renewed at the end of 2011. The City of Toledo's failure to renew that agreement has had a material adverse effect on the Company's business, financial conditions and results of operations.

The Company's six largest customers billed through Florida N-Viro each represent between 5% - 22% of the consolidated revenue for the Company, or a collective total of approximately 62% for these six customers for 2011 and 63% for 2010. Florida operations accounted for approximately 80% and 74% of consolidated revenue during the years ended December 31, 2011 and 2010, respectively. The accounts receivable balance due (which are unsecured) for these six Florida N-Viro customers at December 31, 2011 and 2010 was approximately $286,000 and $328,000, respectively. A seventh Florida customer, Orange County Utilities, provided approximately $367,000 or 7% of the consolidated revenue in 2011, but the agreement began December 2010 and ended March 2011. The Company does not expect Orange County to resume that agreement in the near future. At the end of 2011, the Company was notified that a Florida customer, Seminole County, who represented gross revenue of $353,000 and $402,000 in 2011 and 2010, respectively, was terminating services for the Company effective January 2012. This was approximately 6% and 8% of 2011 and 2010 gross revenue, respectively.

A substantial portion of the Company's revenue is derived from services provided under contracts and agreements with existing licensees. Some of these contracts, especially those contracts with large municipalities, provide for termination of the contract by the customer after giving relatively short notice (in some cases as little as ten days). In addition, some of these contracts contain liquidated damages clauses, which may or may not be enforceable in the event of early termination of the contracts. If one or more of these contracts are terminated prior to the expiration of its term, and the Company is not able to replace revenues from the terminated contract or receive liquidated damages pursuant to the terms of the contract, the lost revenue could have a material and adverse effect on its business and financial condition.

Note 7. Commitments and Contingencies

On March 17, 2010, the Company and Timothy R. Kasmoch, the President and Chief Executive Officer, entered into an Employment Agreement for a five-year term. Mr. Kasmoch is to receive an annual base salary of $150,000, subject to an annual discretionary increase. In addition, Mr. Kasmoch is eligible for an annual cash bonus and was granted stock options from the Company's Second Amended and Restated 2004 Stock Option Plan. Generally, the Agreement may be terminated by the Company with or without cause or by the Employee for any reason.

On March 17, 2010, the Company and Robert W. Bohmer, the Executive Vice President and General Counsel, entered into an Employment Agreement for a five-year term. Mr. Bohmer is to receive an annual base salary of $150,000, subject to an annual discretionary increase. In addition, Mr. Bohmer is eligible for an annual cash bonus and was granted stock options from the Company's Second Amended and Restated 2004 Stock Option Plan. Generally, the Agreement may be terminated by the Company with or without cause or by the Employee for any reason.

On March 17, 2010, the Company and James K. McHugh, the Chief Financial Officer, Secretary and Treasurer, entered into an Employment Agreement for a five-year term. Mr. McHugh is to receive an annual base salary of $125,000, subject to an annual discretionary increase. In addition, Mr. McHugh is eligible for an annual cash bonus and was granted stock options from the Company's Second Amended and

N-VIRO INTERNATIONAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010

Note 7. Commitments and Contingencies (continued)

Restated 2004 Stock Option Plan. Generally, the Agreement may be terminated by the Company with or without cause or by the Employee for any reason.

The Company's executive and administrative offices are located in Toledo, Ohio. Through April 2011, the Company operated under a month to month lease at its former location. The total rental expense for this former location included in the statements of operations for the years ended December 31, 2011 and 2010 is approximately $12,800 and $38,500, respectively. In April 2011, the Company signed a 68 month lease with a new lessor in Toledo. The total minimum rental commitment for the year ending December 31, 2012 is approximately $37,400, for 2013 is $30,600 and for the years 2014 through 2016 is $40,800 each year. The total rental expense for this current location included in the statements of operations for the year ended December 31, 2011 is approximately $15,600. The Company also leases various equipment on a month-to-month basis.

In October 2010, the Company began to lease property in Emlenton, Pennsylvania under a lease with A-C Valley Industrial Park, for one year. After September 2011, the Company operated under a month to month lease agreement. The total rental expense included in the statements of operations for the years ended December 31, 2011 and 2010 is $23,000 and $6,000, respectively.

In June 2009, the Company began to maintain an office in West Unity, Ohio under a lease with D&B Colon Leasing, LLC, for one year. In June 2010, the Company renewed the lease for an additional year through May 31, 2011, and is currently operating under a month to month lease. The total rental expense included in the statements of operations for each of the twelve months ended December 31, 2011 and 2010 is $30,000.

The Company maintains an office in Daytona Beach under a lease with the County of Volusia, Florida, which was renewed in March, 2009 for five years. The total minimum rental commitment for the years ending December 31, 2012 through 2013 is $48,000 each year, and for 2014 is $12,000. The total rental expense included in the statements of operations for each of the years ended December 31, 2011 and 2010 is $48,000.

The Company also leased processing equipment at its Florida location which began in February 2008 under a three-year lease. The total rental expense included in the statements of operations for the years ended December 31, 2011 and 2010 is approximately $3,900 and $46,200, respectively. In February 2011, the Company purchased the equipment through a financing arrangement with an equipment leasing company.

Management believes that all of the Company's properties are adequately covered by insurance.

The Company operates in an environment with many financial risks, including, but not limited to, major customer concentrations, customer contract termination provisions, competing technologies, infringement and/or misappropriation of intellectual property rights, the highly competitive and, at times, seasonal nature of the industry and worldwide economic conditions. Various federal, state and governmental agencies are considering, and some have adopted, laws and regulations regarding environmental protection which could adversely affect the business activities of the Company. The Company cannot predict what effect, if any, current and future regulations may have on the operations of the Company.

From time to time the Company is involved in legal proceedings and subject to claims which may arise in the ordinary course of business. The Company is not aware of any legal proceedings or material claims at this time.

N-VIRO INTERNATIONAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010

Note 8. Income Tax Matters

The composition of the deferred tax assets and liabilities at December 31, 2011 and 2010 is as follows:

	2011	2010
Gross deferred tax liabilities:		
Property and equipment and intangible assets	$(19,200)	$(72,800)
Gross deferred tax assets:		
Loss carryforwards	4,350,300	4,167,100
Loss on market price of derivatives	4,100	47,700
Section 754 basis step up	107,100	128,500
Allowance for doubtful accounts	23,800	23,800
Other	500	500
Less valuation allowance	(4,466,600)	(4,294,800)
	$ -	$ -

The income tax provisions differ from the amount of income tax determined by applying the U.S. Federal income tax rate to pre-tax income from continuing operations for the years ended December 31, 2011 and 2010 and are as follows:

	2011	2010
Computed "expected" tax expense (credit)	$(557,500)	$(1,009,500)
State taxes, net of federal tax benefit	-	-
(Decrease) increase in income taxes resulting from:		
Change in valuation allowance	171,800	140,200
Net operating loss carryfoward expiration	-	520,300
Nondeductible stock options and warrants	568,400	351,800
Derivative adjustment - permanent	(205,400)	-
Other	22,700	(2,800)
	$ -	$ -

The net operating losses available at December 31, 2011 to offset future taxable income total approximately $12,800,000 and expire principally in years 2018 - 2031. Approximately $685,000 will expire if not used to offset taxable income for the 2012 tax year.

N-VIRO INTERNATIONAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010

Note 9. Fair Value Measurements and Disclosures

The Company has adopted the provisions of ASC 820, Fair Value Measurements and Disclosures ("ASC 820") related to nonfinancial assets and liabilities on a prospective basis. ASC820 establishes the authoritative definition of fair value, sets out a framework for measuring fair value and expands the required disclosures about fair value measurement. The valuation techniques required by ASC 820 are based on observable and unobservable inputs using the following three-tier hierarchy:

- Level 1 – Inputs are unadjusted quoted prices in active markets for identical assets or liabilities.
- Level 2 – Inputs are quoted prices for similar assets and liabilities in active markets, quoted prices for identical or similar assets and liabilities in markets that are not active, or inputs that are observable for assets or liabilities, either directly or indirectly, through market corroboration.
- Level 3 – Inputs are unobservable inputs based on the Company's own assumptions.

The following table summarizes the basis used to measure assets and liabilities at fair value on a recurring basis in the balance sheet:

	Level 1	Level 2	Level 3	Total
		as of December 31, 2011		
Warrants	$0	$0	($12,196)	($12,196)
		as of December 31, 2010		
Warrants	$0	$0	($744,476)	($744,476)

The following table sets forth a summary of the changes in the fair value of the Company's Level 3 assets for the year ended December 31, 2011:

Balance, beginning of year	($744,476)
Gain on market price change of warrants issued	732,280
Balance, end of year	($ 12,196)

Note 10. Subsequent Events

The Company has performed a review of events subsequent to the balance sheet date and no matters required disclosure.

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure

None

Item 9A. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

We maintain disclosure controls and procedures (as defined in Rule 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934) that are designed to ensure that information required to be disclosed in our Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the Commission's rules and forms, and that such information is accumulated and communicated to our management, including our principal executive officer and principal financial officer, as appropriate, to allow timely decisions regarding required disclosures. In designing and evaluating the disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives.

As of the end of the period covered by this report, management carried out an evaluation, under the supervision and with the participation of our principal executive officer and principal financial officer, of our disclosure controls and procedures (as defined in Rule 13a-15(e) and Rule 15d-15(e) of the Exchange Act). Based upon the evaluation, our principal executive officer and principal financial officer concluded that our disclosure controls and procedures were not effective at a reasonable assurance level to ensure that information we are required to disclose in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms. Our history of losses has severely limited our budget to hire and train enough accounting and financial personnel needed to adequately provide this function. Consequently, we lack sufficient technical expertise, reporting standards and written policies and procedures regarding disclosure controls and procedures.

Because of the inherent limitations in all disclosure control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, will be or have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty and that breakdowns can occur because of simple error or mistake. Additionally, disclosure controls can be circumvented by the individual acts of some persons, by collusion of two or more people and/or by management override of such controls. The design of any system of disclosure controls also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Over time, disclosure controls and procedures may become inadequate because of changes in conditions, and/or the degree of compliance with the policies and procedures may deteriorate. Also, misstatements due to error or fraud may occur and not be detected.

Management’s Annual Report on Internal Control over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting. Our internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of consolidated financial statements for external purposes in accordance with generally accepted accounting principles.

Under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we conducted an evaluation of the effectiveness of our internal control over financial reporting based on the framework established by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) as set forth in Internal Control - Integrated Framework. Based on our evaluation, our principal executive officer and our principal financial officer concluded that our internal controls over financial reporting were not effective as of December 31, 2011 for the reasons described below.

We lack personnel in accounting and financial staff to sufficiently monitor and process financial transactions in an efficient and timely manner. Our history of losses has severely limited our budget to hire and train enough accounting and financial personnel needed to adequately provide this function. Consequently, we lacked sufficient technical expertise, reporting standards and written policies and procedures. Specifically, controls were not effective to ensure that significant non-routine transactions, accounting estimates, and other adjustments were appropriately reviewed, analyzed and monitored by competent accounting staff on a timely basis.

We continue to develop and implement a remediation plan to address the material weakness. To date, our remediation efforts have included adoption of an expense reimbursement policy and the hiring of an employee to assist in the financial area of our business. However, due to our continuing lack of financial resources to hire and train accounting and financial personnel, we have not yet fully remedied this material weakness.

During the quarter ended December 31, 2011, there were no material changes in the Company's internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

While we are not aware of any material errors to date, our inability to maintain the adequate internal controls may result in a material error in our financial statements. Further, because of its inherent limitations, internal controls over financial reporting may not prevent or detect misstatements. It should be noted that any system of controls, however well designed and operated, can provide only reasonable, and not absolute, assurance that the objectives of the system will be met. In addition, the design of any control system is based in part upon certain assumptions about the likelihood of future events. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

This annual report does not include an audit or attestation report of our registered public accounting firm regarding our internal control over financial reporting because the attestation report requirement has been removed for “smaller reporting companies” under the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010.

Item 9B. Other Information

None

PART III

Item 10. Directors, Executive Officers and Corporate Governance

DIRECTORS OF THE COMPANY

Currently the Board is currently composed of three Class I Directors: Carl Richard, Joseph H. Scheib and Mark D. Hagans; and three Class II Directors: James H. Hartung, Timothy R. Kasmoch and Thomas L. Kovacik (whose terms will expire upon the election and qualification of directors at the annual meetings of stockholders to be held in 2011 and 2012, respectively). At each annual meeting of stockholders, directors will be elected for a full term of two years to succeed those directors whose terms are expiring. During 2011 Joan B. Wills was a director until her resignation in December 2011. See the Form 8-K filed on December 7, 2011 for more details.

The following table sets forth the names and ages of our directors.

Name	Age	Position
Mark D. Hagans	45	Class I Director
James H. Hartung	69	Class II Director, Chairman of the Board*
Timothy R. Kasmoch	50	Class II Director, President and Chief Executive Officer*
Thomas L. Kovacik	64	Class II Director*
Carl Richard	85	Class I Director
Joseph H. Scheib	55	Class I Director

* Directors currently nominated for re-election.

Mark D. Hagans is an attorney and partner with the law firm of Plassman, Rupp, Hagans & Newton, of Archbold, Ohio, and his practice focuses on corporation, taxation and banking law. Mr. Hagans serves on numerous Boards of directors, including the Fulton County Health Center, where he is presently chair of the Finance Committee. Mr. Hagans earned his law degree from the University of Toledo. Mr. Hagans has served as our director since December 2006 and is a member of the Board's Audit, Finance and Technology Committees. Mr. Hagans' experience as a lawyer and businessman enables him to bring valuable resources to the Board.

James H. Hartung is the former President and Chief Executive Officer of the Toledo-Lucas County (Ohio) Port Authority, a position he held from 1994 until 2008. Mr. Hartung has served as our Director since January 2006 and is a member of the Board's Compensation and Nominating Committees. Mr. Hartung presently also serves as the Chairman of the Board/Executive Vice-President at Seasnake World Wide Marketing LLC, a marketing concern commercializing the Seasnake shipping system for the marine transportation of liquid, dry bulk, break-bulk and inter-modal container cargo; and is actively engaged in maritime/economic development consulting in domestic and international markets for Development Solutions, LLC, where he serves as a Senior Associate/Partner. Mr. Hartung's qualifications to serve as a director and our Chairman of the Board consist of several years experience as a businessman, as an organizational leader and community organizer, and in dealings with local government and related agencies that enable him to bring valuable insights to the Board.

Timothy R. Kasmoch has been our President and Chief Executive Officer since February 2006 and a director since January 2006. Until April 1, 2007, Mr. Kasmoch was also President and CEO of Tri-State Garden Supply, d/b/a Gardenscape, a bagger and distributor of lawn and garden products, which has provided trucking and equipment services to our Company. Mr. Kasmoch is a graduate of Penn State University. Mr. Kasmoch is a member of the Board's Finance and Technology Committees. Mr. Kasmoch's qualifications to serve as a director of the Company consist of his experience in the soil and distribution business as well as an extensive knowledge of the transportation and trucking industry. Mr. Kasmoch's strength is in strategic planning and he possesses a broad, fundamental understanding of the business drivers affecting us. He is the only "insider" on the Board.

Thomas L. Kovacik is the Executive Director of Transportation Advocacy Group of Northwest Ohio ("TAGNO"), a strategic planning organization working with local and Ohio transportation and economic development officials, and the President of Kovacik Consulting, a business consulting company. Mr. Kovacik was previously employed by us from 1992 to 1995 as President of Great Lakes N-Viro, at the time one of our divisions. Mr. Kovacik has also held various positions with local government, utilities and environmental companies, and earned a masters degree from Bowling Green State University in Geochemistry. Mr. Kovacik has served as our Director since December 2006, and is a member of the Board's Compensation and Technology Committees. Mr. Kovacik's qualifications to serve as a director of the Company consist of his experience in the environmental, government and utilities industries, and his prior position with us as a divisional president. His strength in strategic planning and transactional experience offers a unique perspective to the Board.

Carl Richard is the former Executive Vice-President of P.R. Transportation, a trucking company that was located in Toledo, Ohio, and was a consultant to us from January 2006 to April 2007. Mr. Richard served as Vice-President of C.A. Transportation from 1988 through 2000 and as Vice-President of R.O.S.S. Investments, a real estate holding company, from 1980 through 2000. Mr. Richard has served as our director since December 2004 and is a member of the Board's Nominating Committee. Mr. Richard's qualifications to serve as a director of the Company consist of his extensive experience in the transportation and trucking industry.

Joseph H. Scheib is the Controller for Verity Financial Group, Inc., a holding company for Verity Asset Management, Inc. and Verity Investments, Inc., a Registered Investment Advisor and a Registered Broker-Dealer, respectively. He has held this position since June 2011. Mr. Scheib was the Chief Financial Officer of Broad Street Software Group, a comprehensive software technology company located in Edenton, North Carolina, a position he held until 2010. From May 2000 until February 2003, Mr. Scheib was the Financial Operation Principal/Compliance Officer of Triangle Securities, LLC of Raleigh, North Carolina, an asset management, brokerage and investment banking firm. Mr. Scheib is a graduate of East Carolina University with a degree in accounting. Mr. Scheib has served as our Director since December 2004, and is a member of the Board's Audit, Finance and Nominating Committees. Mr. Scheib's qualifications to serve as a director of the Company consist of his strong financial and asset management experience and serving the Company in a financial oversight role as the Chair of the Audit Committee. Given his extensive knowledge and experience in finance, Mr. Scheib has been determined to be an audit committee financial expert by the board.

Key Relationships

None

CORPORATE GOVERNANCE AND BOARD MATTERS

Our Board of Directors

Our business, property and affairs are managed under the direction of our Board. We have determined that the Company's interests are best served by having a Chairman of the Board who is independent of the management of the Company because it is our view this inherently strengthens board independence in dealing with issues that closely involve management. Our Chief Executive Officer has responsibility for setting our strategic direction and the day-to-day leadership and performance, while the Chairman of the Board has a greater focus on long-range Company goals and plans and governance of our Board of Directors. This balance between the two positions enables Mr. Kasmoch to focus on the operational and strategic challenges we presently face, with Mr. Hartung providing board leadership on matters of governance and management oversight.

Our Board, as a whole, has the responsibility for risk oversight of management. The role of our Board of Directors is to oversee the President and Chief Executive Officer, the Executive Vice President and the Chief Financial Officer in the operation of the Company, including management's establishment and implementation of appropriate practices and policies with respect to areas of potentially significant risk to us. Our Board considers risks to the Company as part of the strategic planning process and thorough review of compliance issues in committees of our Board, as appropriate. While the Board has the ultimate oversight responsibility for such risk management process, various committees of the Board are structured to oversee specific risks in the areas covered by their respective assignments such as audits or compensation. In addition, our Board may retain, on such terms as determined by the Board and in its sole discretion, independent legal, financial and other consultants and advisors to advise and assist the Board in fulfilling its oversight responsibilities. Currently, there are no such consultants in any category assisting or advising the Company.

Management is responsible for N-Viro’s day-to-day risk management, and the entire Board’s role is to engage in informed oversight. Our Chief Executive Officer is a member of the Board of Directors, and our Chief Financial Officer and Executive Vice President/General Counsel regularly attend Board meetings, which helps facilitate discussions regarding risk between the Board and our senior management, as well as the exchange of risk-related information or concerns between the Board and the senior management. The Board believes Mr. Kasmoch’s service as Chief Executive Officer and on the Board is appropriate because it bridges a critical gap between our management and the Board, enabling the Board to benefit from management’s perspective on our business while the Board performs its oversight function.

The Company’s philosophy about diversity among its Board members is discussed below under “Nominating Committee.”

Meetings of the Board of Directors

Our Board held six meetings during 2011, consisting of two regular meeting and four special meetings. Each director attended 100% of the aggregate number of meetings held by the Board of Directors and the Committees of the Board of Directors on which he served. It is the policy of the Company that the members of the Board attend our annual stockholder meeting. Failure to attend annual meetings without good reason is a factor the Nominating Committee and Board will consider in determining whether or not to renominate a current Board member. All members of the Board serving at the time attended the 2011 Annual Meeting, except Mr. Scheib and Ms. Wills.

Shareholder Communications with the Board

We encourage stockholder communications with directors. Stockholders may communicate with a particular director, all directors or the Chairman of the Board by mail or courier addressed to him or the entire Board in care of James K. McHugh, Corporate Secretary, N-Viro International Corporation, 2254 Centennial Road, Toledo, OH 43617. All correspondence should be in a sealed envelope marked “Confidential” and will be forwarded unopened to the director as appropriate.

Board Independence

Although we are not subject to the listing requirements of any stock exchange, we are committed to a board in which a majority of our members consist of independent directors, as defined under the NASDAQ rules. The Board has reviewed the independence of its members, applying the NASDAQ standards and considering other commercial, legal, accounting and familial relationships between the directors and us. The Board has determined that all of the directors and director nominees are independent other than Mr. Kasmoch, who is not an independent director by virtue of his current position as our Chief Executive Officer.

Code of Ethics

We have adopted a Code of Ethics which covers the Chief Executive Officer and Chief Financial Officer, which is administered and monitored by the Audit Committee of the Board. A copy of the Code of Ethics is attached as Exhibit 14.1 to this Annual Report on Form 10-K for the year ended December 31, 2011, and is posted on our web site at www.nviro.com.

Committees of the Board of Directors

The Board has the following standing committees: the Audit Committee, the Compensation Committee, the Finance Committee, the Nominating Committee and the Technology Committee. The composition and function of each Committee is set forth below:

Director	Audit	Compensation	Nominating	Finance	Technology
Mark D. Hagans	X			X*	X
James H. Hartung		X	X		
Timothy R. Kasmoch				X	X*
Thomas L. Kovacik		X*			X
Carl Richard			X		
Joseph H. Scheib	X*		X*	X	
Joan B. Wills**		X			

* Committee Chair
** Until Ms. Wills' retirement from the Board in December 2011.

Audit Committee

Our Audit Committee consisted of Messrs. Scheib and Hagans. In accordance with our Audit Committee Charter, each of the Audit Committee members must be "independent" as determined under the NASDAQ rules. The Audit Committee currently is not subject to, and does not follow, the independence criteria set forth in Section 10A of the Securities Exchange Act 1934, as amended. The Board has determined that each of the directors who serve on the Audit Committee are "independent" under the NASDAQ rules, meaning that none of them has a relationship with us that may interfere with their independence from us and our management. Further, the Board has determined that Mr. Scheib qualifies as a "financial expert" as defined by the Securities and Exchange Commission (the "SEC").

The Audit Committee recommends the appointment of the outside auditor, oversees our accounting and internal audit functions and reviews and approves the terms of transactions between us and related party entities. During 2011, the Audit Committee met two times. The Audit Committee has retained UHY LLP to conduct the audit for the year ended December 31, 2012. The Audit committee is governed by a written charter, a copy of which was attached to the Proxy Statement for our annual meeting held on June 8, 2007.

Compensation Committee

The Compensation Committee determines officers' salaries and bonuses and administers the grant of stock options pursuant to our stock option plans. The Compensation Committee does not have a written charter. The Compensation Committee consisted of Messrs. Kovacik and Hartung and Ms. Wills until her retirement from the Board in December 2011. The Compensation Committee met three times during 2011.

The Board has determined that all of the members of the committee are "independent" as determined under the NASDAQ standards.

Finance Committee

The Finance Committee, consisting of Messrs. Hagans, Kasmoch and Scheib, assists in monitoring our cash flow requirements and approves any internal or external financing or leasing arrangements. The Finance Committee does not have a written charter. The Finance Committee met one time during 2011.

Nominating Committee

The Nominating Committee, consisting of Messrs. Scheib, Richard and Hartung, considers and recommends to the Board qualified candidates for election as Board members, and establishes and periodically reviews criteria for selection of directors. The Nominating Committee does not have a written charter. The Nominating Committee met one time during 2011.

The Board has determined that all of the members of the committee are "independent" as determined under the NASDAQ standards.

The Nominating Committee will consider candidates recommended by stockholders, directors, officers, third-party search firms and other sources for nomination as a director. The Committee considers the needs of the Board and evaluates each director candidate in light of, among other things, the candidate's qualifications. Recommended candidates must be of the highest character and integrity, free of any conflicts of interest and possess the ability to work collaboratively with others, and have the time to devote to Board activities. All candidates will be reviewed in the same manner, regardless of the source of the recommendation. Presently, the Nominating Committee does not consider diversity as a characteristic in its selection of candidates except to the extent that the Nominating Committee seeks to expand the range of categories of experience and relationships in different aspects of the waste management process the Company requires for the different foci of its business and potential contacts with sources of business opportunity for the Company.

The Nominating Committee will consider all stockholder recommendations of proposed director nominees, if such recommendations are timely received under applicable SEC regulations and include all of the information required to be included as set forth in the By-Laws. To be considered "timely received," recommendations must be received in writing at our principal executive offices, at N-Viro International Corporation, 2254 Centennial Road, Toledo, OH 43617, Attention: Chairman, Nominating Committee, c/o James K. McHugh, Corporate Secretary, no later than March 1, 2013

All candidates recommended by stockholders should be independent and possess substantial and significant experience which would be of value to us in the performance of the duties of a director. In addition, any stockholder director nominee recommendation must include, at a minimum, the following information: the stockholder's name; address; the number and class of shares owned; the candidate's biographical information, including name, residential and business address, telephone number, age, education, accomplishments, employment history (including positions held and current position), and current and former directorships; and the stockholder's opinion as to whether the stockholder recommended candidate meets the definitions of "independent" under the NASDAQ standards. In addition, the recommendation letter must provide the information that would be required to be disclosed in the solicitation of proxies for election of directors under federal securities laws. The stockholder must include the candidate's statement that he/she meets these requirements; is willing to promptly complete the Questionnaire required of all officers, directors and candidates for nomination to the Board; will provide such other information as the Committee may reasonably request; consents to serve on the Board if elected; and a statement whether such candidate, if elected, intends to tender, promptly following such person's election or re-election, an irrevocable resignation effective upon such person's failure to receive the required vote for re-election at the next meeting at which such person would face re-election.

Compensation of Directors

Our Board of Directors has approved the payment of cash compensation to non-employee directors in exchange for their service on the Board. The amount of cash compensation to be received by each non-employee director is $1,000 per regular meeting attended during each calendar year, and $500 per special meeting attended. Our Board of Directors generally has four meetings per calendar year. The Directors are reimbursed for out-of-pocket expenses incurred in attending meetings of the Board of Directors or any committees thereof. During 2011, the Board voluntarily waived the cash compensation for the special meetings.

Under our current stock option plan, the N-Viro International Corporation 2010 Stock Option Plan ("2010 Plan"), each non-employee Director automatically receives a grant of options to purchase 5,000 shares of Common Stock for each regular meeting attended, and an option to purchase 2,500 shares of Common Stock for each special meeting attended, subject to a maximum of 30,000 options in any calendar year.

Directors who are our employees do not receive any additional compensation for serving as Directors. Directors who are our consultants do not receive any additional cash compensation for serving as Directors, but do receive stock options per the provisions of the 2010 Plan.

See "Certain Relationships and Related Transactions" for additional compensation to directors.

DIRECTOR COMPENSATION

Name	Fees Earned or Paid in Cash	Stock Awards (1)	Option Awards	Non-Equity Incentive Plan Compensation	Non-Qualified Incentive Plan Compensation	Non-Qualified Deferred Compensation Earnings	All Other Compensation	Total
Joseph Scheib	$2,000	$27,250	$53,570	-	-	-	-	$82,820
Carl Richard	$2,000	$27,250	$53,570	-	-	-	-	$82,820
James Hartung	$2,000	$27,250	$53,570	-	-	-	-	$82,820
Mark Hagans	$2,000	$27,250	$53,570	-	-	-	-	$82,820
Thomas Kovacik	$2,000	$27,250	$53,570	-	-	-	-	$82,820
Joan Wills *	$1,000	$27,250	$53,570	-	-	-	-	$81,820
Timothy Kasmoch	-	-	-	-	-	-	-	$0
	$11,000	$163,500	$321,420	$0	$0	$0	$0	$495,920

* No longer a director effective December 2011

(1) Represents 20,000 stock warrants issued to each board member in August 2011

EXECUTIVE OFFICERS OF THE COMPANY

Executive officers of the Company are appointed by the Board of Directors and hold office at the pleasure of the Board. Set forth below is biographical and other information on the current executive officers of the Company. Mr. Kasmoch also serves as a member of the Board and his biographical information is set forth above under the caption "Directors of the Company."

Name	Age	Position
Timothy R. Kasmoch	50	President and Chief Executive Officer
Robert W. Bohmer	42	Executive Vice-President and General Counsel
James K. McHugh	53	Chief Financial Officer, Secretary and Treasurer

Robert W. Bohmer has been our Executive Vice-President and General Counsel since July 2007. From 1996 until joining the Company, Mr. Bohmer had been a partner with the law firm of Watkins, Bates and Carey, LLP, Toledo, Ohio. From 2005 through June 2007, Mr. Bohmer had served as general outside counsel to the Company.

James K. McHugh has served as our Chief Financial Officer, Secretary and Treasurer since January 1997. Prior to that date, Mr. McHugh served the Company in various financial positions since April 1992, and was a key member of the team that took the Company public in 1993.

SECTION 16(A) BENEFICIAL OWNERSHIP REPORTING COMPLIANCE

Section 16(a) of the Securities Exchange Act of 1934, as amended, requires our directors and executive officers, and persons who own beneficially more than ten percent (10%) of the shares of our Common Stock, to file reports of ownership and changes of ownership with the Securities and Exchange Commission, or SEC. Copies of all filed reports are required to be furnished to us pursuant to Section 16(a). Based solely on the reports received by us and on written representations from reporting persons, we believe that the current directors and executive officers complied with all applicable filing requirements during the fiscal year ended December 31, 2011.

Item 11. Executive Compensation

Compensation of Executive Officers

The following table presents the total compensation paid to our Chief Executive Officer, Executive Vice President and Chief Financial Officer during 2011 and 2010. There were no other executive officers who were serving at the end of 2011 or 2010 and whose total compensation exceeded $100,000.

SUMMARY COMPENSATION TABLE

Name and Principal Position	Year	Salary	Bonus	Stock Awards (4)	Option Awards (5)	Non-Equity Incentive Plan Compensation	Nonqualified Deferred Compensation Earnings	All Other Compensation	Total
Timothy R. Kasmoch	2011	$150,000	-	$27,233	$969,115	-	-	$52,000	$1,198,348
President and Chief	2010	$150,000	-	-	$446,152	-	-	$21,518	$617,670
Executive Officer (1)									
Robert W. Bohmer	2011	$150,000	-	$27,233	$169,542	-	-	-	$346,775
Executive Vice-President +	2010	$150,000	-	-	$373,763	-	-	-	$523,763
General Counsel (2)									
James K. McHugh	2011	$125,000	-	$27,233	$52,982	-	-	$399	$205,614
Chief Financial Officer,	2010	$125,000	$7,810	-	$94,926	-	-	$399	$228,135
Secretary + Treasurer (3)									

(1) For the “All Other Compensation” column, Mr. Kasmoch’s spouse was compensated for outside consulting services rendered to the Company during 2010, in addition to employee wages paid starting the fourth quarter of 2010 into 2011. All compensation was in cash.

(2) For Mr. Bohmer, the value of the Option Award includes the 2007 Option Award recorded as an expense in 2010 in the amount of $70,000.

(3) For the “All Other Compensation” column, Mr. McHugh is taxed on the imputed benefit of a life insurance policy that benefits his personal beneficiary for one-half the face value of the policy and N-Viro International Corporation for the other one-half.

(4) The amounts included in the Stock Awards column include the aggregate fair value of stock warrants granted in the fiscal year computed in accordance with FASB ASC Topic 718. We use the Black-Scholes model to measure the grant date fair value of stock warrants.

(5) The amounts included in the Option Awards column include the aggregate fair value of options granted and/or expensed in the fiscal year computed in accordance with FASB ASC Topic 718. We continue to use the Black-Scholes model to measure the grant date fair value of stock options. For a discussion of the valuation assumptions used to value the options, see Note 5 to our Consolidated Financial Statements included in this annual report on Form 10-K for the fiscal year ended December 31, 2011.

2011 GRANTS OF PLAN BASED AWARDS

			Estimated Future Payouts Under Non-Equity Incentive Plan Awards			Estimated Future Payouts Under Equity Incentive Plan Awards			Full Grant Date Fair Value	Base Price of Option Awards
Name	Grant Date	Approval Date	Threshold ($)	Target ($)	Maximum ($)	Threshold (#)	Target (#)	Maximum (#)	($)	($/shr.)
Timothy R. Kasmoch	8/10/2011	8/10/2011	-	-	-	-	-	500,000	1.50	1.63
Robert W. Bohmer	none		-	-	-	-	-	-	-	-
James K. McHugh	none		-	-	-	-	-	-	-	-

OUTSTANDING EQUITY AWARDS AT FISCAL YEAR-END

	OPTION AWARDS					STOCK AWARDS			
	# of Securities Underlying Unexercised Options (#)	# of Securities Underlying Unexercised Options (#)	Equity Incentive Plan Awards: # Securities Underlying Unexercised Unearned	Option Exercise	Option Expiration	# of Shares or Units of Stock That	Market Value of Shares or Units of Stock That	Equity Incentive Plan Awards: # Unearned Shares, Units or Other Rights That Have Not	Equity Incentive Plan Awards: Market or Payout Value of Unearned Shares, Units or Other Rights That Have

Name	Exercisable	Unexercisable	Options (#)	Price (#)	Date	Have Not Vested (#)	Have Not Vested ($)	Vested (#)	Not Vested (#)
Timothy R. Kasmoch	250,000	-	-	$2.00	12/30/16	-	-	-	-
Timothy R. Kasmoch	2,500	-	-	$1.70	2/15/16	-	-	-	-
Timothy R. Kasmoch	25,000	-	-	$1.94	7/11/19	-	-	-	-
Timothy R. Kasmoch	243,000	-	-	$2.23	7/22/19	-	-	-	-
Timothy R. Kasmoch	282,000	188,000	-	$3.27	3/18/20	-	-	-	-
Timothy R. Kasmoch	500,000	-	-	$1.63	8/10/21				
Robert W. Bohmer	100,000	-	-	$2.80	6/13/17	-	-	-	-
Robert W. Bohmer	25,000	-	-	$1.94	7/11/19	-	-	-	-
Robert W. Bohmer	168,000	-	-	$2.23	7/22/19	-	-	-	-
Robert W. Bohmer	192,000	128,000	-	$3.27	3/18/20	-	-	-	-
James K. McHugh	12,000	-	-	$2.10	11/11/14	-	-	-	-
James K. McHugh	50,000	-	-	$2.00	12/31/16	-	-	-	-
James K. McHugh	25,000	-	-	$1.94	7/11/19	-	-	-	-
James K. McHugh	68,000	-	-	$2.23	7/22/19	-	-	-	-
James K. McHugh	60,000	40,000	-	$3.27	3/18/20	-	-	-	-

All options awards were made granted under the Company's current stock option plan described under the caption "Equity Compensation Plan Information."

Employment Agreements

Effective March 17, 2010, we entered into an Employment Agreement (the “Agreement”) with Mr. Timothy R. Kasmoch as our President and Chief Executive Officer, commencing February 26, 2010. The Agreement is for a five-year term commencing on February 26, 2010 and provides for automatic renewal of successive one-year terms unless notice is provided ninety (90) days prior to the expiration of the then current term. The agreement provides that Mr. Kasmoch is to receive an annual base salary of $150,000, subject to annual increase at the discretion of our Board of Directors. In addition, Mr. Kasmoch is eligible for an annual cash bonus in an amount to be determined, and otherwise subject to the discretion of the Board of Directors. Under the agreement, this determination is to be based upon the Board of Directors review of Mr. Kasmoch's performance. The Agreement also provides for a stock option grant of 470,000 options that vest over a five year period, pursuant to the Second Amended and Restated 2004 Stock Option Plan. While employed with the Company, the Agreement allows Mr. Kasmoch to engage in other limited business activities that are not competitive with and do not involve the Company, subject to the prior disclosure to the Company's Audit Committee. The Employment Agreement permits Mr. Kasmoch to terminate his employment in the event of a change of control or certain enumerated material breaches thereof by the Company. A copy of this employment agreement was attached to a Form 8-K as Exhibit 10.1, filed by us on March 19, 2010.

Effective March 17, 2010, we entered into an Employment Agreement (the "Agreement") with Mr. Robert W. Bohmer as our Executive Vice President and General Counsel, commencing February 26, 2010. The Agreement is for a five-year term commencing on February 26, 2010 and provides for automatic renewal of successive one-year terms unless notice is provided ninety (90) days prior to the expiration of the then current term. The Agreement provides that Mr. Bohmer is to receive an annual base salary of $150,000, subject to an annual increase at the discretion of our Board of Directors. In addition, Mr. Bohmer is eligible for an annual cash bonus in an amount to be determined, and otherwise subject to the discretion of the Board of Directors. Under the agreement, this determination is to be based upon the President/Chief Executive Officer's and Board of Directors review of Mr. Bohmer's performance. The Agreement also provides for a stock option grant of 320,000 options that vest over a five year period, pursuant to the Second Amended and Restated 2004 Stock Option Plan. While employed with the Company, the Agreement allows Mr. Bohmer to engage in other limited business activities that are not competitive with and do not involve the Company, subject to the prior disclosure to the Company's Audit Committee. The Employment Agreement permits Mr. Bohmer to terminate his employment in the event of a change of control or certain enumerated material breaches thereof by the Company. A copy of this employment agreement was attached to a Form 8-K as Exhibit 10.1, filed by us on March 19, 2010.

Effective March 17, 2010, we entered into an Employment Agreement (the "Agreement") with James K. McHugh to serve as the Company's Chief Financial Officer commencing February 26, 2010. The Agreement is for a five-year term commencing on February 26, 2010 and provides for automatic renewal of successive one-year terms unless notice is provided ninety (90) days prior to the expiration of the then current term. The agreement provides that Mr. McHugh is to receive an annual base salary of $125,000, subject to annual increase at the discretion of the Board of Directors of the Company. In addition, Mr. McHugh is eligible for an annual cash bonus in an amount to be determined, and otherwise subject to the discretion of, the Board of Directors. Under the agreement, this determination is to be based upon the President/Chief Executive Officer's and Board of Directors review of Mr. McHugh's performance. The Agreement also provides for a stock option grant of 100,000 shares that vest over a five year period, pursuant to the Second Amended and Restated 2004 Stock Option Plan. While employed with the Company, the Agreement allows Mr. McHugh to engage in other limited business activities that are not competitive with and do not involve the Company, subject to the prior disclosure to the Company's Audit Committee. The Employment Agreement permits Mr. McHugh to terminate his employment in the event of a change of control or certain enumerated material breaches thereof by the Company. A copy of this employment agreement was attached to a Form 8-K as Exhibit 10.1, filed by us on March 19, 2010.

Equity Compensation Plan Information

We maintain three stock option plans (two are able to issue new grants) for directors, executive officers and key employees or outside subcontractors. The most recent plan ("2010 Plan") was approved by the stockholders in August 2010. The 2010 Plan authorizes the Board of Directors or a committee thereof, to grant awards of incentive stock options and non-qualified stock options for up to a maximum of 5,000,000 shares of Common Stock. For all of the plans, the total number of options granted and outstanding as of March 5, 2012 was 2,924,281, and the number of options available for future issuance was 4,339,075. Currently, all of the plans are administered by the Board of Directors via a committee.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

We had outstanding 6,083,624 shares of Common Stock, $.01 par value per share, or the Common Stock, on March 5, 2012, which constitutes the only class of our outstanding voting securities.

Five Percent Stockholders

As of March 5, 2012, the following were the only persons known to us to own beneficially more than 5% of the outstanding shares of Common Stock:

Title of Class	Name and Address of Beneficial Owner	Amount and Nature of Beneficial Ownership	Percentage of Outstanding Shares of Common Stock
Common Stock	Cooke Family Trust 90 Grande Brook Circle, #1526 Wakefield, Rhode Island 02879	627,717 (1)	10.3%
Common Stock	VC Energy I, LLC 3900 Paradise Road, Suite U Las Vegas, NV 89169	800,000 (2)	12.3%

1. The shares attributed to the Cooke Family Trust include 627,267 shares owned beneficially and 450 in Common Stock warrants exercisable to purchase an equal number of shares of Common Stock. This information was derived from the Schedule 13D Amendment #5 filed on May 10, 2010.

2. The shares attributed to VC Energy I, LLC include 400,000 shares owned beneficially and 400,000 in Common Stock warrants exercisable to purchase an equal number of shares of Common Stock. This information was derived from the Schedule 13G filed on July 8, 2010.

Security Ownership of Management

The following table sets forth, as of March 5, 2012, unless otherwise specified, certain information with respect to the beneficial ownership of our shares of Common Stock by each person who is our director, a nominee for the Board, each of the Named Executive Officers, and by our directors and executive officers as a group. Unless otherwise noted, each person has voting and investment power, with respect to all such shares, based on 6,083,624 shares of Common Stock outstanding on the record date. Pursuant to the rules of the SEC, shares of Common Stock which a person has the right to acquire within 60 days of the date hereof pursuant to the exercise of stock warrants or stock options are deemed to be outstanding for the purpose of computing the percentage ownership of such person but are not deemed outstanding for the purpose of computing the percentage ownership of any other person.

Title of Class	Name of Beneficial Owner	1

		Amount and Nature of Beneficial Ownership	Percent of Class
Common Stock	Mark D. Hagans	94,1302	1.52%
Common Stock	James H. Hartung	112,2503	1.81%
Common Stock	Timothy R. Kasmoch	1,480,5004	19.86%
Common Stock	Thomas L. Kovacik	102,5005	1.66%
Common Stock	Carl Richard	242,7906	3.88%
Common Stock	Joseph H. Scheib	291,8727	4.67%
Common Stock	Robert W. Bohmer	507,6008	7.70%
Common Stock	James K. McHugh	248,9209	3.94%
Common Stock	All directors and executive officers as a group (8 persons)	3,080,56210	34.89%

1. Except as otherwise indicated, all shares are directly owned with voting and investment power held by the person named.

2. Represents 4,965 shares of Common Stock owned by Mr. Hagans, 69,165 shares issuable upon exercise of options which are currently exercisable at prices ranging from $1.78 to $3.90 per share and 20,000 unregistered shares issuable upon exercise of warrants which are currently exercisable at a price of $1.53 per share.

3. Represents 3,314 shares of Common Stock owned by Mr. Hartung, 78,046 shares issuable upon exercise of options which are currently exercisable at prices ranging from $1.42 to $3.90 per share and 30,890 unregistered shares issuable upon exercise of warrants which are currently exercisable at prices ranging from $1.53 to $2.00 per share.

4. Represents 100,000 unregistered shares and 8,000 registered shares of Common Stock owned by Mr. Kasmoch, 70,000 unregistered shares issuable upon exercise of warrants which are currently exercisable at prices ranging from $1.53 to $1.85 per share and 1,302,500 shares issuable upon exercise of options which are currently exercisable at prices ranging from $1.63 to $3.27 per share.

5. Represents 1,000 shares of Common Stock owned by Mr. Kovacik, 81,500 shares issuable upon exercise of options which are currently exercisable at prices ranging from $1.78 to $3.90 per share and 20,000 unregistered shares issuable upon exercise of warrants which are currently exercisable at a price of $1.53 per share.

6. Represents 75,351 shares of Common Stock owned by Mr. Richard, 90,000 shares issuable upon exercise of options which are currently exercisable at prices ranging from $0.70 to $3.90 per share and 77,439 unregistered shares issuable upon exercise of warrants which are currently exercisable at prices ranging from $1.53 to $2.00 per share.

7. Represents 125,722 shares of Common Stock owned by Mr. Scheib, 91,250 shares issuable upon exercise of options which are currently exercisable at prices ranging from $0.70 to $3.90 per share, 600 shares owned by a family member over which Mr. Scheib acts as custodian and 74,300 unregistered shares issuable upon exercise of warrants which are currently exercisable at prices ranging from $1.53 to $2.52 per share.

8. Represents 2,600 shares of Common Stock owned by Mr. Bohmer, 485,000 shares issuable upon exercise of options which are currently exercisable at prices ranging from $1.94 to $3.27 per share and 20,000 unregistered shares issuable upon exercise of warrants which are currently exercisable at a price of $1.53 per share.

9. Represents 13,920 shares of Common Stock owned by Mr. McHugh, 215,000 shares issuable upon exercise of options which are currently exercisable at prices ranging from $1.94 to $3.27 per share and 20,000 unregistered shares issuable upon exercise of warrants which are currently exercisable at a price of $1.53 per share.

10. Represents 334,872 shares of Common Stock owned by the directors and officers, 600 shares owned indirectly, 2,412,461 shares issuable upon exercise of options which are currently exercisable at prices ranging from \$0.70 to \$3.90 per share and a total of 332,629 unregistered shares issuable upon exercise of warrants which are currently exercisable at prices ranging from \$1.53 to \$2.52 per share.

Item 13. Certain Relationships and Related Transactions and Director Independence

During 2011 and 2010, we paid Terri Kasmoch, the spouse of President and Chief Executive Officer Timothy Kasmoch, outside consulting fees for business development, web site and company media marketing and stock promotion efforts for the Company, and as an employee with the same duties starting in the fourth quarter of 2010.

Director Independence

Although we are not subject to the listing requirements of any stock exchange, we are committed to a board in which a majority of our members consist of independent directors, as defined under the NASDAQ rules. The Board has reviewed the independence of its members, applying the NASDAQ standards and considering other commercial, legal, accounting and familial relationships between the Directors and us. The Board has determined that all of the Directors and director nominees are independent other than Mr. Kasmoch, who is not an independent Director by virtue of his current position as our chief executive officer.

Item 14. Principal Accountant Fees and Services

Audit Fees

Audit services of UHY LLP ("UHY") included the audit of our annual financial statements for 2011 and 2010, and services related to quarterly filings with the SEC through the reporting period ended September 30 in each of those years. Fees for these services totaled approximately $68,500 for 2011 and $73,500 for 2010.

Audit Related Fees

There were no fees billed for the years ended December 31, 2011 and December 31, 2010 for assurance and related services by UHY that are reasonably related to the performance of the audit or review of our financial statements.

Tax Fees

There were no fees billed for the years ended December 31, 2011 and December 31, 2010 for professional services rendered by UHY for tax compliance, tax advice, and tax planning.

All Other Fees

There were no fees billed for the years ended December 31, 2011 and December 31, 2010 for assistance on accounting related matters.

Although the Audit Committee Charter does not explicitly require it, the Audit Committee approves all engagements of outside auditors before any work is begun on the engagement.

UHY LLP personnel work under the direct control of UHY LLP partners and are leased from wholly-owned subsidiaries of UHY Advisors, Inc. in an alternative practice structure.

PART IV

Item 15. Exhibits, Financial Statement Schedules

Exhibit No.	Description
10.1	Commercial Line of Credit Agreement and Note dated October 15, 2008, between N-Viro International Corporation and Monroe Bank + Trust (incorporated by reference to Exhibit 99.1 to Form 8-K filed October 27, 2008).
10.2	Employment Agreement, dated March 17, 2010 between Timothy R. Kasmoch and N-Viro International Corporation (incorporated by reference to Exhibit 10.1 to Form 8-K filed March 19, 2010)
10.3	Employment Agreement, dated March 17, 2010 between Robert W. Bohmer and N-Viro International Corporation (incorporated by reference to Exhibit 10.2 to Form 8-K filed March 19, 2010)
10.4	Employment Agreement, dated March 17, 2010 between James K. McHugh and N-Viro International Corporation (incorporated by reference to Exhibit 10.3 to Form 8-K filed March 19, 2010)
10.5	The N-Viro International Corporation 2004 Stock Option Plan (incorporated by reference to Form S-8 filed December 20, 2004).*
10.6	The N-Viro International Corporation Amended and Restated 2004 Stock Option Plan (incorporated by reference to the Proxy Statement on Schedule 14A filed May 14, 2008).*
10.7	The N-Viro International Corporation Second Amended and Restated 2004 Stock Option Plan (incorporated by reference to the Definitive Proxy Statement on Schedule 14A filed July 13, 2009).*
10.8	The N-Viro International Corporation 2010 Stock Option Plan (incorporated by reference to the Definitive Proxy Statement on Schedule 14A filed June 23, 2010).*
21.1	List of subsidiaries of the Company.#
23.1	Consent of UHY LLP.
24.1	Power(s) of Attorney.#
31.1	Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of Chief Executive Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification of Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS	XBRL Instance Document #
101.SCH	XBRL Taxonomy Extension Schema #

101.CAL	XBRL Taxonomy Extension Calculation Linkbase #
101.LAB	XBRL Taxonomy Extension Label Linkbase #
101.PRE	XBRL Taxonomy Extension Presentation Linkbase #
101.DEF	XBRL Taxonomy Definition Linkbase Document #

Only included in Form 10-K filed electronically with the Securities and Exchange Commission.

* Indicates a management contract or compensatory plan or arrangement.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Exchange Act, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

N-VIRO INTERNATIONAL CORPORATION
Dated: March 30, 2012

By: /s/ Timothy R. Kasmoch
Timothy R. Kasmoch, Chief Executive Officer and President
(Principal Executive Officer)

POWER OF ATTORNEY

Know all persons by these presents, that each person whose signature appears below constitutes and appoints James K. McHugh his attorney-in-fact, each with the power of substitution, for him in any and all capacities, to sign any amendments to this Form 10-K, and to file the same, with exhibits thereto and other documents in connection therewith, with the Securities and Exchange Commission, hereby ratifying and confirming all that each of said attorneys-in-fact, or his substitutes, may do or cause to be done by virtue hereof.

Pursuant to the requirements of the Exchange Act, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the date indicated.

Dated: March 30, 2012

/s/ Timothy R. Kasmoch
Timothy R. Kasmoch, Chief Executive Officer, President and Director
(Principal Executive Officer)

/s/ James K. McHugh
James K. McHugh
Chief Financial Officer, Secretary and Treasurer
(Principal Financial Officer)

/s/ James H. Hartung*
James H. Hartung, Director & Chairman of the Board

/s/ Mark D. Hagans*
Mark D. Hagans, Director

/s/ Joseph H. Scheib*
Joseph H. Scheib, Director

/s/ Thomas L. Kovacik*
Thomas L. Kovacik, Director

/s/ Carl Richard*
Carl Richard, Director

* by James K. McHugh, Attorney-In-Fact