

McGladrey & Pullen

Certified Public Accountants

The Spencer Foundation

(An Illinois Not-for-Profit Corporation)

Financial Report

March 31, 2008 and 2007

Contents

Independent Auditor's Report	1
Financial Statements	
Statements of Financial Position	2
Statements of Activities	3
Statements of Cash Flows	4
Notes to the Financial Statements	5 - 7

McGladrey & Pullen

Certified Public Accountants

Independent Auditor's Report

Board of Directors of
The Spencer Foundation

We have audited the accompanying statements of financial position of The Spencer Foundation (an Illinois not-for-profit corporation) as of March 31, 2008 and 2007, and the related statements of activities and cash flows for the years then ended. These financial statements are the responsibility of the Foundation's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of The Spencer Foundation as of March 31, 2008 and 2007 and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

McGladrey & Pullen, LLP

Chicago, Illinois
June 3, 2008

The Spencer Foundation
(An Illinois Not-for-Profit Corporation)

Statements of Financial Position (In Thousands of Dollars)
March 31, 2008 and 2007

	<u>2008</u>	<u>2007</u>
Assets		
Investments, at fair value	\$ 448,024	\$ 481,933
Cash	379	171
Other assets	761	875
	<u>\$ 449,164</u>	<u>\$ 482,979</u>
Liabilities and Unrestricted Net Assets		
Grants payable	\$ 16,608	\$ 14,651
Deferred federal excise tax	1,365	1,982
Accrued expenses	102	37
Accounts payable	85	74
	<u>18,160</u>	<u>16,744</u>
Unrestricted net assets	<u>431,004</u>	<u>466,235</u>
	<u>\$ 449,164</u>	<u>\$ 482,979</u>

The Spencer Foundation
(An Illinois Not-for-Profit Corporation)

Statements of Activities (In Thousands of Dollars)
Years Ended March 31, 2008 and 2007

	<u>2008</u>	<u>2007</u>
Investment returns		
Net realized gain on sales of investments	\$ 8,092	\$ 9,271
Net change in unrealized gain (loss) on investments	(30,824)	31,161
Interest income	42	30
Dividend income	14,321	11,980
	<u>(8,369)</u>	<u>52,442</u>
Program services		
Grants authorized, net of refunds (grant payments made were \$19,458 in 2008 and \$16,486 in 2007)	21,238	17,861
Foundation administered projects	1,364	1,402
Administrative expenses	3,681	3,094
Investment management expenses	786	737
Current federal excise tax	410	420
Deferred federal excise tax	(617)	623
	<u>26,862</u>	<u>24,137</u>
Change in net assets	(35,231)	28,305
Unrestricted net assets		
Beginning of year	<u>466,235</u>	<u>437,930</u>
End of year	<u>\$ 431,004</u>	<u>\$ 466,235</u>

**The Spencer Foundation
(An Illinois Not-for-Profit Corporation)**

**Statements of Cash Flows (In Thousands of Dollars)
Years Ended March 31, 2008 and 2007**

	<u>2008</u>	<u>2007</u>
Operating activities		
Change in net assets	\$ (35,231)	\$ 28,305
Net realized gain on sales of investments	(8,092)	(9,271)
Net change in unrealized gain (loss) on investments	30,824	(31,161)
Changes in		
Other assets	114	92
Grants payable	1,957	1,501
Deferred federal excise tax	(617)	623
Accrued expenses	65	13
Accounts payable	11	(1)
Net cash used in operating activities	<u>(10,969)</u>	<u>(9,899)</u>
Investing activities		
Purchases of investments	(13,238)	(15,262)
Proceeds from sales of investments	24,415	25,007
Net cash provided by investing activities	<u>11,177</u>	<u>9,745</u>
Increase (decrease) in cash	208	(154)
Cash		
Beginning of year	<u>171</u>	<u>325</u>
End of year	<u>\$ 379</u>	<u>\$ 171</u>

**The Spencer Foundation
(An Illinois Not-for-Profit Corporation)**

Notes to the Financial Statements

Note 1 Nature of Activities and Significant Accounting Policies

Nature of Activities—The Spencer Foundation (the Foundation), organized in 1962, is the residuary legatee under the will of Lyle M. Spencer, deceased. The Foundation was established to support research aimed at the improvement of education. Support is derived primarily from returns on the Foundation's investments.

The Foundation qualifies as a tax-exempt organization under Section 501(c)(3) of the Internal Revenue Code and, accordingly, is not subject to federal income taxes. However, in accordance with Section 4940(e) of the Code, the Foundation is subject to a federal excise tax of 2 percent of net investment income and net realized taxable gains on security transactions, or 1 percent if the Foundation meets certain specified distribution requirements. The Foundation did not meet the specified requirements for fiscal years 2008 and 2007 and was subject to a 2 percent federal excise tax.

Financial Statement Presentation—The financial statements have been prepared following accounting principles applicable to nonprofit organizations.

Investments—Index funds are carried based on fair values provided by the fund managers. Real estate partnerships are carried at approximate fair value, as determined by the management of the partnerships, using appraised values, and at market value, based on quoted prices. Purchases and sales of securities are recorded on a trade date basis.

Deferred Federal Excise Tax—Deferred federal excise tax represents taxes provided on the net unrealized appreciation on investments, using a rate of 2 percent.

Awards and Grants—Awards and grants, including multiyear grants, are considered obligations when approved by the Foundation's Board of Directors.

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 affecting the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

Fair Value of Financial Instruments—Substantially all of the Foundation's assets and liabilities are considered financial instruments and are either already reflected at fair value or are short-term or replaceable on demand. Therefore, their carrying amounts approximate fair value.

Reclassifications—Certain amounts from the 2007 financial statements have been reclassified to conform to the 2008 presentation without affecting previously reported net assets.

Note 2 Investments

Investments at March 31, 2008 and 2007 are summarized as follows:

	2008		2007	
	Cost	Market or Fair Value	Cost	Market or Fair Value
Marketable securities				
Equity funds	\$ 312,004,000	\$ 379,348,000	\$ 313,257,000	\$ 414,097,000
Bond funds	67,032,000	67,951,000	68,865,000	66,914,000
Real estate investments	510,000	725,000	510,000	922,000
	<u>\$ 379,546,000</u>	<u>\$ 448,024,000</u>	<u>\$ 382,632,000</u>	<u>\$ 481,933,000</u>

**The Spencer Foundation
(An Illinois Not-for-Profit Corporation)**

Notes to the Financial Statements

Note 2 Investments, Continued

The Foundation's investments are exposed to various risks, such as interest rate, credit, and overall market volatility. Due to the level of risk associated with certain investment securities, it is reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect the amounts reported in the financial statements.

Note 3 Grants Payable

Grants payable consist primarily of multiyear unconditional grants that are generally payable over one to five years. Management estimates these grants will be paid as follows:

2009	\$ 10,166,000
2010	4,275,000
2011	1,921,000
2012	<u>246,000</u>
	<u>\$ 16,608,000</u>

Grants authorized are shown net of rescissions and refunds of \$177,000 in 2008 and \$126,000 in 2007. Payments on authorized but unpaid grants may be accelerated upon mutual agreement between the Foundation and the grantees.

Note 4 Unrestricted Net Assets

Unrestricted net assets are comprised of the following amounts:

	<u>2008</u>	<u>2007</u>
Principal	\$ 82,203,000	\$ 82,203,000
Cumulative excess of grants and other expenses over revenue (cumulative grants authorized of \$392,792,000 at March 31, 2008)	(236,800,000)	(224,301,000)
Cumulative net realized gains on sales of investments	518,482,000	510,390,000
Unrealized gains in investment portfolio	<u>67,119,000</u>	<u>97,943,000</u>
	<u>\$ 431,004,000</u>	<u>\$ 466,235,000</u>

Note 5 Retirement Plans

The Foundation maintains a defined contribution retirement plan covering all active full-time employees. Under the terms of the plan, the Foundation must contribute specified percentages of an employee's salary. The plan is currently invested in employee-designated individual annuity contracts and various approved mutual funds. The Foundation's contribution to the plan was \$249,000 for fiscal year 2008 (\$233,000 - 2007).

In addition, the Foundation maintains a supplemental retirement plan that allows employees to defer a portion of their pretax salaries. No contributions are made to this plan by the Foundation.

**The Spencer Foundation
(An Illinois Not-for-Profit Corporation)**

Notes to the Financial Statements

Note 6 Commitments

The Foundation currently occupies office space in Chicago, under the terms of an operating lease which expires in 2015. The lease requires the Foundation to pay monthly base rents ranging from \$16,000 to \$21,000, plus a proportionate share of operating and real estate taxes. At March 31, 2008, the Foundation had the following commitments for base rentals under these leases:

2009	\$	212,000
2010		218,000
2011		225,000
2012		231,000
2013		238,000
Thereafter		<u>665,000</u>
	\$	<u>1,789,000</u>

Rent expense was \$355,000 for fiscal year 2008 (\$116,000 - 2007).

Note 7 Pending Adoptions of New Accounting Principles

In June 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation No. 48 (FIN 48), *Accounting for Uncertainty in Income Taxes - an Interpretation of FASB Statement No. 109*. FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with FASB Statement No. 109, *Accounting for Income Taxes*. FIN 48 prescribes a comprehensive model for recognizing, measuring, presenting and disclosing in the financial statement tax position taken or expected to be taken on a tax return. If there are changes in net assets as a result of application of FIN 48 these will be accounted for as an adjustment to the opening balance of net assets. Additional disclosures about the amounts of such liabilities will be required also. The Foundation will be required to adopt FIN 48 in its 2009 annual financial statements. Management is currently assessing the impact of FIN 48 on its financial statements.

In September 2006, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards No. 157, *Fair Value Measurements* (SFAS 157). SFAS 157 defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurement. SFAS 157 also emphasizes that fair value is a market-based measurement, not an entity-specific measurement, and sets out a fair value hierarchy with the highest priority being quoted prices in active markets. Under SFAS 157, fair value measurements are disclosed by level within that hierarchy. SFAS 157 is effective for fiscal years beginning after November 15, 2007, except for nonfinancial assets and nonfinancial liabilities that are recognized or disclosed at fair value in the financial statements on a nonrecurring basis for which delayed application is permitted until fiscal years beginning after November 15, 2008. The Foundation is currently assessing the potential effect of SFAS 157 on its financial position, results of operations and cash flows.