

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

Financial Statements

March 31, 2005 and 2004



Altschuler, Melvoin and Glasser LLP
Certified Public Accountants and Consultants

The Spencer Foundation
(An Illinois Not-for-Profit Corporation)
Table of Contents
March 31, 2005 and 2004

| | Page |
|-------------------------------------|-------|
| Independent Auditors' 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 |



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Independent Auditors' 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, 2005 and 2004 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 U.S. generally accepted auditing standards. 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, 2005 and 2004 and its changes in net assets and cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

Altschuler, Melvoin & Glasser LLP

Chicago, Illinois
May 13, 2005

The Spencer Foundation
(An Illinois Not-for-Profit Corporation)
Statements of Financial Position (In Thousands of Dollars)
March 31, 2005 and 2004

| | <u>2005</u> | <u>2004</u> |
|--|-------------------|-------------------|
| Assets | | |
| Investments, at market value | \$ 409,631 | \$ 397,310 |
| Cash | 238 | 234 |
| Other assets | <u>579</u> | <u>928</u> |
| | <u>\$ 410,448</u> | <u>\$ 398,472</u> |
| Liabilities and Unrestricted Net Assets | | |
| Grants payable | \$ 15,855 | \$ 15,387 |
| Accrued expenses | 46 | 119 |
| Accounts payable | <u>118</u> | <u>166</u> |
| | 16,019 | 15,672 |
| Unrestricted net assets | <u>394,429</u> | <u>382,800</u> |
| | <u>\$ 410,448</u> | <u>\$ 398,472</u> |

The Spencer Foundation
(An Illinois Not-for-Profit Corporation)
Statements of Activities (In Thousands of Dollars)
Years Ended March 31, 2005 and 2004

| | <u>2005</u> | <u>2004</u> |
|---|-------------------|-------------------|
| Investment returns | | |
| Net realized gain on sales of investments | \$ 59,884 | \$ 1,026 |
| Net change in unrealized gain (loss) on investments | (37,639) | 69,739 |
| Interest income | 40 | 379 |
| Dividend income | 10,043 | 9,663 |
| | <u>32,328</u> | <u>80,807</u> |
| Program services | | |
| Grants authorized, net of refunds (grant payments made were \$14,189 in 2005 and \$14,592 in 2004) | 14,294 | 4,142 |
| Foundation administered projects | 840 | 888 |
| Administrative expenses | 3,734 | 3,019 |
| Investment management expenses | 435 | 561 |
| Current federal excise taxes | 1,396 | 214 |
| | <u>20,699</u> | <u>8,824</u> |
| Change in net assets | 11,629 | 71,983 |
| Unrestricted net assets | | |
| Beginning of year | <u>382,800</u> | <u>310,817</u> |
| End of year | <u>\$ 394,429</u> | <u>\$ 382,800</u> |

The Spencer Foundation
(An Illinois Not-for-Profit Corporation)
Statements of Cash Flows (In Thousands of Dollars)
Years Ended March 31, 2005 and 2004

| | <u>2005</u> | <u>2004</u> |
|---|----------------|----------------|
| Operating activities | | |
| Change in net assets | \$ 11,629 | \$ 71,983 |
| Net realized gain on sales of investments | (59,884) | (1,026) |
| Net change in unrealized (gain) loss on investments | 37,639 | (69,739) |
| Changes in | | |
| Other assets | 349 | 138 |
| Grants payable | 468 | (8,550) |
| Accrued expenses | (73) | (5) |
| Accounts payable | (48) | 22 |
| Net cash used in operating activities | <u>(9,920)</u> | <u>(7,177)</u> |
| Investing activities | | |
| Purchases of investments | (320,473) | (34,663) |
| Proceeds from sales of investments | 330,397 | 41,768 |
| Net cash provided by investing activities | <u>9,924</u> | <u>7,105</u> |
| Increase (decrease) in cash | 4 | (72) |
| Cash | | |
| Beginning of year | <u>234</u> | <u>306</u> |
| End of year | <u>\$ 238</u> | <u>\$ 234</u> |

The Spencer Foundation
(An Illinois Not-for-Profit Corporation)
Notes to the Financial Statements
Years Ended March 31, 2005 and 2004

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 2005 and 2004 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—Marketable securities are carried at market value based on quoted prices. 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. The deferred federal excise tax liability is reflected as a reduction of investments in the statements of financial position. The change in deferred taxes is reflected within the change in unrealized gain (loss) on investments in the statements of activities.

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 U.S. generally accepted accounting principles 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.

The Spencer Foundation
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Notes to the Financial Statements
Years Ended March 31, 2005 and 2004

Note 2 Investments

Investments at March 31, 2005 and 2004 are summarized as follows:

| | 2005 | | 2004 | |
|-----------------------------|----------------|-------------------------|----------------|-------------------------|
| | Cost | Market or Fair Value | Cost | Market or Fair Value |
| Marketable securities | | | | |
| Equity index funds | \$ 305,948,000 | \$ 334,202,000 | \$ 218,546,000 | \$ 282,088,000 |
| Bond funds | 74,494,000 | 74,928,000 | 111,649,000 | 114,883,000 |
| Real estate investments | 1,005,000 | 1,072,000 | 1,292,000 | 1,374,000 |
| | 381,447,000 | 410,202,000 | 331,487,000 | 398,345,000 |
| Deferred federal excise tax | - | (571,000) | - | (1,035,000) |
| | \$ 381,447,000 | \$ 409,631,000 | \$ 331,487,000 | \$ 397,310,000 |

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:

| | |
|------|---------------|
| 2006 | \$ 9,197,000 |
| 2007 | 4,979,000 |
| 2008 | 1,464,000 |
| 2009 | 215,000 |
| | \$ 15,855,000 |

Grants authorized are shown net of rescissions and refunds of \$362,000 in 2005 and \$1,888,000 in 2004. 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:

| | 2005 | 2004 |
|---|----------------|----------------|
| Principal | \$ 82,203,000 | \$ 82,203,000 |
| Cumulative excess of grants and other expenses over revenue (cumulative grants authorized of \$339,643,000 at March 31, 2005) | (206,762,000) | (196,147,000) |
| Cumulative net realized gains on sales of investments | 490,804,000 | 430,921,000 |
| Unrealized gains in investment portfolio | 28,184,000 | 65,823,000 |
| | \$ 394,429,000 | \$ 382,800,000 |

The Spencer Foundation
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Notes to the Financial Statements
Years Ended March 31, 2005 and 2004

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 \$217,000 for fiscal year 2005 (\$211,000 - 2004).

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.

Note 6 Commitments

During fiscal 2005, the Foundation exercised its right to terminate their office space lease prior to the expiration date. A cancellation fee of \$325,000 was paid in May 2004 and the Foundation will vacate the premises in November 2005. The Foundation entered into a 10-year lease agreement in March 2005 for new office space. The terms of the new lease require 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, 2005, the Foundation had the following commitments for base rentals under these leases:

| | |
|------------|---------------------|
| 2006 | \$ 380,000 |
| 2007 | 199,000 |
| 2008 | 205,000 |
| 2009 | 212,000 |
| 2010 | 218,000 |
| Thereafter | <u>1,359,000</u> |
| | <u>\$ 2,573,000</u> |

Rent expense was \$363,000 for fiscal year 2005 (\$459,000 - 2004).