

# **The Spencer Foundation**

**(An Illinois Not-for-Profit Corporation)**

Financial Report

March 31, 2010 and 2009

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# McGladrey & Pullen

Certified Public Accountants

## Independent Auditor's Report

To the Board of Directors  
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, 2010 and 2009, 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, 2010 and 2009 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 14, 2010

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

**Statements of Financial Position (In Thousands of Dollars)**  
**March 31, 2010 and 2009**

	2010	2009
<b>Assets</b>		
Investments, at fair value	\$ 390,751	\$ 278,939
Cash	136	3,695
Other assets	795	1,081
	<u>\$ 391,682</u>	<u>\$ 283,715</u>
<b>Liabilities and Unrestricted Net Assets</b>		
Grants payable	\$ 9,807	\$ 15,186
Deferred federal excise tax	580	-
Accrued expenses	67	39
Accounts payable	97	86
	<u>10,551</u>	<u>15,311</u>
Unrestricted net assets	<u>381,131</u>	<u>268,404</u>
	<u>\$ 391,682</u>	<u>\$ 283,715</u>

See Notes to Financial Statements.

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

**Statements of Activities (In Thousands of Dollars)**  
**Years Ended March 31, 2010 and 2009**

	2010	2009
Investment returns:		
Net realized gain on sales of investments	\$ 299	\$ 5,134
Net change in unrealized gain (loss) on investments	116,156	(160,096)
Interest income	6	17
Dividend income	9,873	13,388
	<u>126,334</u>	<u>(141,557)</u>
Program services:		
Grants authorized, net of refunds (grant payments made were \$13,291 in 2010 and \$18,186 in 2009)	7,601	16,425
Foundation administered projects	902	1,216
Administrative expenses	3,878	3,777
Investment management expenses	639	636
Current federal excise tax	7	354
Deferred federal excise tax	580	(1,365)
	<u>13,607</u>	<u>21,043</u>
<b>Change in net assets</b>	<b>112,727</b>	<b>(162,600)</b>
Unrestricted net assets:		
Beginning of year	<u>268,404</u>	<u>431,004</u>
End of year	<u>\$ 381,131</u>	<u>\$ 268,404</u>

See Notes to Financial Statements.

**The Spencer Foundation**  
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**Statements of Cash Flows (In Thousands of Dollars)**  
**Years Ended March 31, 2010 and 2009**

	2010	2009
<b>Cash Flows from Operating Activities</b>		
Change in net assets	\$ 112,727	\$ (162,600)
Net realized gain on sales of investments	(299)	(5,134)
Net change in unrealized (gain) loss on investments	(116,156)	160,096
Changes in:		
Other assets	286	(320)
Grants payable	(5,379)	(1,422)
Deferred federal excise tax	580	(1,365)
Accrued expenses	28	(63)
Accounts payable	11	1
<b>Net cash used in operating activities</b>	<b>(8,202)</b>	<b>(10,807)</b>
<b>Cash Flows from Investing Activities</b>		
Purchases of investments	(6,942)	(8,393)
Proceeds from sales of investments	11,585	22,516
<b>Net cash provided by investing activities</b>	<b>4,643</b>	<b>14,123</b>
<b>Net increase (decrease) in cash</b>	<b>(3,559)</b>	<b>3,316</b>
<b>Cash:</b>		
Beginning of year	3,695	379
End of year	\$ 136	\$ 3,695

See Notes to Financial Statements.

**The Spencer Foundation  
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**Notes to Financial Statements**

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**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.

**Financial statement presentation:** The financial statements have been prepared following accounting principles applicable to nonprofit organizations.

**Investments:** Index funds are carried at fair values based on quoted prices in an active market. Real estate investments are carried at approximate fair value, as determined by management based on appraisals, when available, or estimated based on current market prices for similar properties. 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.

**Tax status:** 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 year 2010 and was subject to a 2 percent federal excise tax. In fiscal year 2009, the Foundation met the specified requirements and was subject to a 1 percent federal excise tax.

**The Spencer Foundation  
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**Notes to Financial Statements**

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**Note 1. Nature of Activities and Significant Accounting Policies (Continued)**

On April 1, 2009, the Foundation adopted the accounting standard on accounting for uncertainty in income taxes, which addresses the determination of whether tax benefits claimed or expected to be claimed on a tax return should be recorded in the financial statements. Under this guidance, the Foundation may recognize the tax benefit from an uncertain tax position only if it is more likely than not that the tax position will be sustained on examination by taxing authorities, based on the technical merits of the position. Examples of tax positions include the tax-exempt status of the Foundation, and various positions related to the potential sources of unrelated business taxable income. The tax benefits recognized in the financial statements from such a position are measured based on the largest benefit that has a greater than 50 percent likelihood of being realized upon ultimate settlement. The guidance on accounting for uncertainty in income taxes also addresses de-recognition, classification, interest and penalties on income taxes, and accounting in interim periods. As of March 31, 2010, there were no unrecognized tax positions identified or recorded as liabilities.

The Foundation files forms 990PF in the U.S. federal jurisdiction and the State of Illinois. With few exceptions, the Foundation is no longer subject to examination by the Internal Revenue Service for fiscal years before 2006.

**Subsequent events:** The Foundation has evaluated subsequent events for potential recognition and/or disclosure through June 14, 2010, the date the financial statements were available to be issued.

**Note 2. Investments**

Investments at March 31, 2010 and 2009 are summarized as follows:

	2010		2009	
	Cost	Market or Fair Value	Cost	Market or Fair Value
Marketable securities:				
Equity funds	\$ 307,652,000	\$ 329,881,000	\$ 301,420,000	\$ 213,405,000
Bond funds	57,592,000	59,696,000	68,224,000	64,415,000
Real estate investments	970,000	1,174,000	914,000	1,119,000
	<u>\$ 366,214,000</u>	<u>\$ 390,751,000</u>	<u>\$ 370,558,000</u>	<u>\$ 278,939,000</u>

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. Fair Value Measurements**

The Foundation has adopted accounting guidance related to fair value measurements, which provides a framework for measuring fair value under generally accepted accounting principles. This guidance applies to all financial instruments that are being measured and reported on a fair value basis.



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**Notes to Financial Statements**

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**Note 3. Fair Value Measurements (Continued)**

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. In determining fair value, the Foundation uses various methods including market, income and cost approaches. Based on these approaches, the Foundation often utilizes certain assumptions that market participants would use in pricing the asset or liability, including assumptions about risk and/or the risks inherent in the inputs to the valuation technique. These inputs can be readily observable, market corroborated, or generally unobservable inputs. The Foundation utilizes valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs. Based on the observability of the inputs used on the valuation techniques, the Foundation is required to provide the following information according to the fair value hierarchy. The fair value hierarchy ranks the quality and reliability of the information used to determine fair values. Financial assets and liabilities carried at fair value will be classified and disclosed in one of the following three categories:

Level 1. Valuations for assets and liabilities traded in active exchange markets, such as the New York Stock Exchange. Level 1 also includes U.S. Treasury and federal agency securities and federal agency mortgage-backed securities, which are traded by dealers or brokers in active markets. Valuations are obtained from readily available pricing sources for market transactions involving identical assets or liabilities.

Level 2. Valuations for assets and liabilities traded in less active dealer or broker markets. Valuations are obtained from third party pricing services for identical or similar assets or liabilities.

Level 3. Valuations for assets and liabilities that are derived from other valuation methodologies, including option pricing models, discounted cash flow models and similar techniques, and not based on market exchange, dealer, or broker traded transactions. Level 3 valuations incorporate certain assumptions and projections in determining the fair value assigned to such assets or liabilities.

For the fiscal years ended March 31, 2010 and 2009, the application of valuation techniques applied to similar assets and liabilities has been consistent. The following is a description of the valuation methodologies used for instruments at fair value:

**Marketable Securities**

The fair value of investment securities is the market value based on quoted market prices, when available, or market prices provided by recognized broker dealers.

**Real Estate Investments**

The fair value of real estate investments is based on independent appraisals, when available, or estimated based on current market prices for similar properties.

In determining the appropriate levels, the Foundation performs a detailed analysis of the assets and liabilities that are subject to fair value measurement. At each reporting period, all assets and liabilities for which the fair value measurement is based on significant unobservable inputs would be classified as Level 3.

**The Spencer Foundation  
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**Notes to Financial Statements**

**Note 3. Fair Value Measurements (Continued)**

**Fair Value on a Recurring Basis**

The table below presents the balances of assets and liabilities measured at fair value on a recurring basis:

	March 31, 2010			
	Level 1	Level 2	Level 3	Total
Equity funds	\$ 329,881,000	\$ -	\$ -	\$ 329,881,000
Bond funds	59,696,000	-	-	59,696,000
Real estate investments	-	1,174,000	-	1,174,000
	<u>\$ 389,577,000</u>	<u>\$ 1,174,000</u>	<u>\$ -</u>	<u>\$ 390,751,000</u>

	March 31, 2009			
	Level 1	Level 2	Level 3	Total
Equity funds	\$ 213,405,000	\$ -	\$ -	\$ 213,405,000
Bond funds	64,415,000	-	-	64,415,000
Real estate investments	-	1,119,000	-	1,119,000
	<u>\$ 277,820,000</u>	<u>\$ 1,119,000</u>	<u>\$ -</u>	<u>\$ 278,939,000</u>

**Note 4. 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:

2011	\$ 7,368,000
2012	2,042,000
2013	109,000
Thereafter	288,000
	<u>\$ 9,807,000</u>

Grants authorized are shown net of rescissions and refunds of \$313,000 in 2010 and \$339,000 in 2009. Payments on authorized but unpaid grants may be accelerated upon mutual agreement between the Foundation and the grantees.

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**Notes to Financial Statements**

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**Note 5. Unrestricted Net Assets**

Unrestricted net assets are comprised of the following amounts:

	2010	2009
Principal	\$ 82,203,000	\$ 82,203,000
Cumulative excess of grants and other expenses over revenue (cumulative grants authorized of \$418,979,000 at March 31, 2010)	(248,167,000)	(244,439,000)
Cumulative net realized gains on sales of investments	523,916,000	523,617,000
Unrealized gains (losses) in investment portfolio	23,179,000	(92,977,000)
	<u>\$ 381,131,000</u>	<u>\$ 268,404,000</u>

**Note 6. 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 \$270,000 for fiscal year 2010 (\$260,000 - 2009).

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 7. 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, 2010, the Foundation had the following commitments for base rentals under these leases:

2011	\$ 225,000
2012	231,000
2013	238,000
2014	244,000
2015	251,000
Thereafter	170,000
	<u>\$ 1,359,000</u>

Rent expense was \$426,000 for fiscal year 2010 (\$449,000 - 2009).