



THE WALLACE FOUNDATION

Financial Statements

December 31, 2011 and 2010

(With Independent Auditors' Report Thereon)



KPMG LLP
345 Park Avenue
New York, NY 10154-0102

Independent Auditors' Report

The Board of Directors
The Wallace Foundation:

We have audited the accompanying balance sheets of The Wallace Foundation (the Foundation) as of December 31, 2011 and 2010, 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 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 Foundation's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by 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 Wallace Foundation as of December 31, 2011 and 2010, and the changes in its net assets and its cash flows for the years then ended, in conformity with U.S. generally accepted accounting principles.

KPMG LLP

July 25, 2012

THE WALLACE FOUNDATION

Balance Sheets

December 31, 2011 and 2010

Assets	2011	2010
Cash equivalents and cash	\$ 10,947,553	7,792,642
Investments (note 3)	1,313,314,703	1,398,045,154
Other assets and receivables	954,902	1,223,183
Fixed assets, net of accumulated depreciation of \$1,868,998 in 2011 and \$1,589,909 in 2010	<u>2,362,911</u>	<u>2,629,172</u>
Total assets	<u><u>\$ 1,327,580,069</u></u>	<u><u>1,409,690,151</u></u>
Liabilities and Net Assets		
Liabilities:		
Accrued expenses and other payables	\$ 1,015,615	1,442,096
Grants payable (note 4)	14,736,893	13,546,802
Deferred liabilities (note 5)	<u>4,234,540</u>	<u>5,853,138</u>
Total liabilities	19,987,048	20,842,036
Net assets – unrestricted	<u>1,307,593,021</u>	<u>1,388,848,115</u>
Total liabilities and net assets	<u><u>\$ 1,327,580,069</u></u>	<u><u>1,409,690,151</u></u>

See accompanying notes to financial statements.

THE WALLACE FOUNDATION
 Statements of Activities
 Years ended December 31, 2011 and 2010

	2011	2010
Revenues:		
Interest and dividends	\$ 15,271,129	14,455,820
Realized gains	56,836,061	30,395,177
Total investment income	72,107,190	44,850,997
Investment fees	(3,257,487)	(4,998,471)
Excise and income taxes (note 6)	(2,074,602)	(210,966)
Total investment expenses	(5,332,089)	(5,209,437)
Unrealized (losses) gains, net of deferred tax (note 6)	(75,220,230)	135,977,212
Net (loss) revenues	(8,445,129)	175,618,772
Expenses:		
Grants and related activities	63,889,246	20,793,813
Operating expenses	8,920,719	8,998,631
Total expenses	72,809,965	29,792,444
Change in net assets	(81,255,094)	145,826,328
Net assets:		
Beginning of year	1,388,848,115	1,243,021,787
End of year	\$ 1,307,593,021	1,388,848,115

See accompanying notes to financial statements.

THE WALLACE FOUNDATION

Statements of Cash Flows

Years ended December 31, 2011 and 2010

	2011	2010
Cash flows from operating activities:		
Change in net assets	\$ (81,255,094)	145,826,328
Adjustments to reconcile change in net assets to net cash used in operating activities:		
Unrealized losses (gains) on investments	76,755,717	(138,778,011)
Realized gains on investments	(56,836,061)	(30,395,177)
Loss on disposal of fixed assets	—	336
Depreciation	285,818	295,355
Change in assets and liabilities:		
Accrued investment income	(362,771)	(40,913)
Other assets and receivables	268,281	1,389,632
Accrued expenses and other payable	(426,481)	141,169
Deferred liabilities	(1,618,598)	2,727,081
Grants payable	1,190,091	(18,837,281)
Net cash used in operating activities	(61,999,098)	(37,671,481)
Cash flows from investing activities:		
Sales of investments	471,098,617	507,574,193
Purchases of investments	(405,925,051)	(470,050,702)
Purchases of fixed assets	(19,557)	(14,604)
Net cash provided by investing activities	65,154,009	37,508,887
Net increase (decrease) in cash equivalents and cash	3,154,911	(162,594)
Cash equivalents and cash at beginning of year	7,792,642	7,955,236
Cash equivalents and cash at end of year	\$ 10,947,553	7,792,642

See accompanying notes to financial statements.

THE WALLACE FOUNDATION

Notes to Financial Statements

December 31, 2011 and 2010

(1) Nature of Operations

The Wallace Foundation (the Foundation) is the philanthropic legacy of DeWitt and Lila Acheson Wallace, the co-founders of Reader's Digest. The mission of the Foundation is to improve learning and enrichment opportunities for children. The Foundation's approach is to identify areas where a gap in knowledge is a barrier to progress. By working to fill those knowledge gaps through grants for innovation, research, and communication, the Foundation aims to spur beneficial changes for fields as a whole, not just for individual grantees. As a result, the Foundation gathers and publishes insights useful to policymakers and those who work in the areas where the Foundation concentrates its philanthropy. Today, the Foundation works in five areas: strengthening education leadership to improve student achievement, helping disadvantaged students gain more time for learning during summer learning and the school year, enhancing after-school opportunities, engaging more young people in high-quality arts learning experiences, and building appreciation and demand for the arts.

(2) Summary of Significant Accounting Policies

(a) Basis of Accounting

The accounts of the Foundation are maintained on the accrual basis of accounting.

(b) Income Taxes

The Foundation is exempt from federal income tax under Section 501(c)(3) of the Internal Revenue Code (the Code) and is a private foundation as defined in Section 509(a) of the Code. As required by the Code, the Foundation distributes annually at least 5% of the average of the fair market value of its assets no later than the 12-month period following the end of its fiscal year.

The Foundation recognizes the effects of income tax positions only if those positions are more likely than not of being sustained.

(c) Fair Value Measurements

Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. The fair value hierarchy maximizes the use of observable inputs and minimizes the use of unobservable inputs when measuring fair value. The Foundation uses three levels of inputs to measure fair value:

Level 1: Quoted prices in active markets for identical assets. Level 1 assets include debt and equity securities that are traded in an active exchange market.

Level 2: Observable inputs other than Level 1 prices such as quoted prices for similar assets; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets. Level 2 assets include debt securities with quoted market prices that are traded less frequently than exchange-traded instruments and investment funds redeemable at or near December 31 (note 2(d)).

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Level 3: Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the asset. Level 3 assets include financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation. Level 3 assets also include investment funds which are not redeemable at or near December 31 (note 2(d)).

Fair value estimates are made at a specific point in time, based on available market information and judgments about the financial instrument, including estimates of timing, amount of expected future cash flows, and the credit standing of the issuer. In some cases, the fair value estimates cannot be substantiated by comparison to independent markets. In addition, the disclosed fair value may not be realized in the immediate settlement of the financial asset. The disclosed fair values do not reflect any premium or discount that could result from offering for sale at one time an entire holding of a particular financial asset.

Potential taxes and other expenses that would be incurred in an actual sale or settlement are not reflected in amounts disclosed.

(d) Investments

Investments in equity securities with readily determinable fair values are reported at fair value based on quoted market prices. Investments in debt securities are measured using quoted market prices where available. If quoted market prices for debt securities are not available, the fair value is determined using an income approach valuation technique that considers, among other things, rates currently observed in publicly traded markets for debt of similar terms to companies with comparable credit risk, the issuer's credit spread, and illiquidity by sector and maturity.

The Foundation follows the accounting standards of Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) Subtopic 820-10-35-59, *Fair Value Measurement and Disclosures – Fair Value Measurements of Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)*. This allows for the estimation of the fair value of investments in investment companies for which the investment does not have a readily determinable fair value using net asset value per share or its equivalent. Those estimated fair values may differ significantly from the values that would have been used had a ready market for these securities existed.

Most investments classified in Levels 2 and 3 consist of shares or units in investment funds as opposed to direct interests in the funds' underlying holdings, which may be marketable. Because the net asset value reported by each fund is used as a practical expedient to estimate fair value of the Foundation's interest therein, its classification in Level 2 or Level 3 is based on the Foundation's ability to redeem its interest at or near December 31. If the interest can be redeemed in the near term, the investment is classified as Level 2. The classification of investments in the fair value hierarchy is not necessarily an indication of the risks, liquidity, or degree of difficulty in estimating the fair value of each investment's underlying assets and liabilities.

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Notes to Financial Statements

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(e) Fixed Assets

Fixed assets consist of furniture, fixtures, equipment, and leasehold improvements. All assets are depreciated on a straight-line basis over the estimated useful lives of the assets. Computers are depreciated over 3 years, office equipment is depreciated over 5 years, and furniture and fixtures are depreciated over 15 years. Leasehold improvements are depreciated over the life of the lease or the estimated life of the leasehold improvement, whichever is shorter.

(f) Grants

Grants are reported as an expense and liability of the Foundation when approved by the Foundation's board of directors and communicated to the grantee. Payments due in more than one year are discounted to present value.

(g) Cash Equivalents

Cash equivalents represent short-term investments with original maturities of three months or less at the time of purchase, except for those short-term investments managed by the Foundation's investment managers as part of their long-term investment strategies.

(h) Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

(i) Reclassifications

Certain reclassifications of 2010 amounts have been made to conform to the 2011 presentation.

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Notes to Financial Statements

December 31, 2011 and 2010

(3) Investments

(a) Fair Value Hierarchy

The following tables present the Foundation's fair value hierarchy for investments, the only financial instruments measured at fair value as of December 31, 2011 and 2010:

	2011			Total fair value
	Level 1	Level 2	Level 3	
Stocks:				
Direct ownership:				
United States	\$ 179,999,679	—	—	179,999,679
International	36,074,907	—	1,009,024	37,083,931
Subtotal	216,074,586	—	1,009,024	217,083,610
Mutual funds – international	48,589,540	—	—	48,589,540
Commingled funds – international	—	117,883,250	—	117,883,250
Total	264,664,126	117,883,250	1,009,024	383,556,400
Fixed income:				
Direct ownership:				
United States				
government/agency	—	138,633,815	—	138,633,815
United States corporate and other	—	50,688,825	773,583	51,462,408
Subtotal	—	189,322,640	773,583	190,096,223
Mutual funds:				
United States				
government/agency	43,216,139	—	—	43,216,139
United States corporate and other	23,796,901	—	—	23,796,901
International	10,710,793	—	—	10,710,793
Subtotal	77,723,833	—	—	77,723,833
Commingled funds:				
United States corporate and other	—	—	3,489,340	3,489,340
Total	77,723,833	189,322,640	4,262,923	271,309,396
Hedge funds:				
Multistrategy	—	69,728,514	27,934,635	97,663,149
Credit – redeemable	—	93,867,368	—	93,867,368
Credit – nonredeemable	—	—	42,656,158	42,656,158
Total	—	163,595,882	70,590,793	234,186,675
Inflation hedges:				
Direct ownership – natural resources stocks	24,456,018	—	—	24,456,018
Public energy and commodity funds	—	64,291,552	—	64,291,552
Public real estate funds	—	33,847,782	—	33,847,782
Private energy funds	—	—	29,185,882	29,185,882
Private real estate funds	—	—	28,802,578	28,802,578
Total	24,456,018	98,139,334	57,988,460	180,583,812
Private equity funds	—	—	177,379,752	177,379,752
Short-term investments	10,516,519	4,459,441	—	14,975,960
Accrued investment income	2,031,979	—	—	2,031,979
Receivable for investments sold, net	49,290,729	—	—	49,290,729
Total	\$ 428,683,204	573,400,547	311,230,952	1,313,314,703

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Notes to Financial Statements

December 31, 2011 and 2010

	2010			
	Level 1	Level 2	Level 3	Total fair value
Stocks:				
Direct ownership:				
United States	\$ 182,167,133	—	—	182,167,133
International	48,092,288	—	864,997	48,957,285
Subtotal	<u>230,259,421</u>	<u>—</u>	<u>864,997</u>	<u>231,124,418</u>
Mutual funds – international	68,381,924	—	—	68,381,924
Commingled funds:				
United States	—	18,169,061	—	18,169,061
International	—	162,160,050	—	162,160,050
Subtotal	<u>—</u>	<u>180,329,111</u>	<u>—</u>	<u>180,329,111</u>
Total	<u>298,641,345</u>	<u>180,329,111</u>	<u>864,997</u>	<u>479,835,453</u>
Fixed income:				
Direct ownership:				
United States government/agency	—	94,882,055	—	94,882,055
United States corporate and other	<u>—</u>	<u>58,684,672</u>	<u>786,332</u>	<u>59,471,004</u>
Subtotal	<u>—</u>	<u>153,566,727</u>	<u>786,332</u>	<u>154,353,059</u>
Mutual funds:				
United States government/agency	35,339,450	—	—	35,339,450
United States corporate and other	30,172,075	—	—	30,172,075
International	10,204,467	—	—	10,204,467
Subtotal	<u>75,715,992</u>	<u>—</u>	<u>—</u>	<u>75,715,992</u>
Commingled funds:				
United States corporate and other	<u>—</u>	<u>—</u>	<u>3,696,322</u>	<u>3,696,322</u>
Total	<u>75,715,992</u>	<u>153,566,727</u>	<u>4,482,654</u>	<u>233,765,373</u>
Hedge funds:				
Multistrategy	—	150,033,472	36,544,514	186,577,986
Credit – redeemable	—	52,521,829	50,121,488	102,643,317
Credit – nonredeemable	<u>—</u>	<u>—</u>	<u>43,390,965</u>	<u>43,390,965</u>
Total	<u>—</u>	<u>202,555,301</u>	<u>130,056,967</u>	<u>332,612,268</u>
Inflation hedges:				
Direct ownership – natural resources stocks	31,049,117	—	—	31,049,117
Public energy funds	—	39,834,717	—	39,834,717
Public real estate funds	—	24,007,434	24,248,967	48,256,401
Private energy funds	—	—	26,333,328	26,333,328
Private real estate funds	<u>—</u>	<u>—</u>	<u>26,537,281</u>	<u>26,537,281</u>
Total	<u>31,049,117</u>	<u>63,842,151</u>	<u>77,119,576</u>	<u>172,010,844</u>
Private equity funds	—	—	152,015,019	152,015,019
Short-term investments	15,061,892	10,997,063	—	26,058,955
Accrued investment income	1,669,208	—	—	1,669,208
Receivable for investments sold, net	<u>78,034</u>	<u>—</u>	<u>—</u>	<u>78,034</u>
Total	<u>\$ 422,215,588</u>	<u>611,290,353</u>	<u>364,539,213</u>	<u>1,398,045,154</u>

Short-term investments include money market funds, U.S. government securities, commercial paper, and cash managed by the Foundation's investment managers as part of their long-term investment strategies.

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Notes to Financial Statements

December 31, 2011 and 2010

The following tables present reconciliations for all Level 3 assets measured at fair value at December 31, 2011 and 2010:

	2011						Ending balance
	Beginning balance	Transfers	Realized gains (losses)	Unrealized gains (losses)	Purchases	Settlements	
Stocks – Direct ownership	\$ 864,997	—	(146,960)	122,579	1,215,085	(1,046,677)	1,009,024
Fixed income – Direct ownership	786,332	—	—	(12,749)	—	—	773,583
Fixed income – Commingled funds	3,696,322	—	142,983	186,719	—	(536,684)	3,489,340
Hedge funds – Multistrategy	36,544,514	(11,350,025)	—	2,740,146	—	—	27,934,635
Hedge funds – Credit – redeemable	50,121,488	(50,121,488)	—	—	—	—	—
Hedge funds – Credit – nonredeemable	43,390,965	—	—	(734,807)	—	—	42,656,158
Inflation hedges – Public real estate funds	24,248,967	(24,248,967)	—	—	—	—	—
Inflation hedges – Private energy funds	26,333,328	—	495,917	2,082,534	4,038,125	(3,764,022)	29,185,882
Inflation hedges – Private real estate funds	26,537,281	—	(277,599)	2,561,334	2,250,000	(2,268,438)	28,802,578
Private equity funds	152,015,019	—	6,555,839	12,990,661	31,510,109	(25,691,876)	177,379,752
Total	\$ <u>364,539,213</u>	<u>(85,720,480)</u>	<u>6,770,180</u>	<u>19,936,417</u>	<u>39,013,319</u>	<u>(33,307,697)</u>	<u>311,230,952</u>

	2010						Ending balance
	Beginning balance	Transfers	Realized gains (losses)	Unrealized gains (losses)	Purchases	Settlements	
Stocks – Direct ownership	\$ —	—	196,662	(90,193)	1,463,611	(705,083)	864,997
Fixed income – Direct ownership	1,181,717	—	(175,373)	20,158	—	(240,170)	786,332
Fixed income – Commingled funds	3,944,189	—	116,629	191,673	—	(556,169)	3,696,322
Hedge funds – Multistrategy	59,575,679	(41,615,651)	251,929	10,435,486	10,000,000	(2,102,929)	36,544,514
Hedge funds – Credit – redeemable	34,324,346	(10,620,664)	—	3,417,806	23,000,000	—	50,121,488
Hedge funds – Credit – nonredeemable	36,518,978	—	—	6,871,987	—	—	43,390,965
Inflation hedges – Public real estate funds	23,897,951	—	(6,808,601)	11,104,623	960,241	(4,905,247)	24,248,967
Inflation hedges – Private energy funds	22,568,307	—	2,048,343	2,576,254	2,457,152	(3,316,728)	26,333,328
Inflation hedges – Private real estate funds	18,783,278	—	—	4,956,823	2,797,180	—	26,537,281
Private equity funds	107,135,374	—	2,247,848	23,567,467	27,073,222	(8,008,892)	152,015,019
Total	\$ <u>307,929,819</u>	<u>(52,236,315)</u>	<u>(2,122,563)</u>	<u>63,052,084</u>	<u>67,751,406</u>	<u>(19,835,218)</u>	<u>364,539,213</u>

The Foundation recognizes transfers between levels of the fair value hierarchy on the date of the event or change in circumstance that caused the transfer.

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Notes to Financial Statements

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(b) *Portfolio Liquidity*

The Foundation reviews the liquidity of its investments to ensure that it is able to meet its cash needs for grants, operating expenses, and capital calls. As of December 31, 2011, the Foundation had investments of \$644.5 million that could be sold on a daily basis under normal market conditions. This included \$436.1 million in direct ownership investments held in separate accounts with the Foundation's custodial trustee, \$136.8 million in mutual fund investments, \$36.8 million in a public energy fund, which is part of the Foundation's inflation hedge portfolio, and \$34.8 million in an international commingled stock fund.

The Foundation's investments in commingled bond and stock funds, hedge funds, inflation hedge funds (except direct ownership fund), and private equity funds, including the \$36.8 million public energy fund and the \$34.8 million international commingled stock fund noted above, totaled \$689.1 million as of December 31, 2011. The liquidity of these investments is determined by the redemption period for each fund, which differs among investments and is detailed in note 3(c).

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Notes to Financial Statements

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(c) Strategies of Commingled, Hedge, Inflation Hedge, and Private Equity Funds

The following tables list the investment strategies, redemption terms, and assets for commingled, hedge, inflation hedge, and private equity funds measured at fair value as of December 31, 2011 and 2010:

	2011			
	Total fair value	Unfunded commitments	Redemption dates per year	Redemption notice period
Commingled bond fund	\$ 3,489,340	—	None	N/A
Commingled stock funds:				
International	<u>117,883,250</u>	<u>—</u>	Daily/12	3 – 6 days
Total	<u>117,883,250</u>	<u>—</u>		
Hedge funds:				
Multistrategy	97,663,149	—	1/2/4/None	45 – 180 days
Credit – redeemable	93,867,368	—	1	60/90 days
Credit – nonredeemable	<u>42,656,158</u>	<u>—</u>	None	N/A
Total	<u>234,186,675</u>	<u>—</u>		
Inflation hedge funds:				
Public energy and commodity	64,291,552	—	Daily/12	1/65 days
Public real estate	33,847,782	—	4	30 days
Private energy	29,185,882	23,276,687	None	N/A
Private real estate	<u>28,802,578</u>	<u>7,525,947</u>	None	N/A
Total	156,127,794	30,802,634		
Private equity funds	<u>177,379,752</u>	<u>74,145,346</u>	None	N/A
Total	\$ <u>689,066,811</u>	<u>104,947,980</u>		

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	2010			
	<u>Total fair value</u>	<u>Unfunded commitments</u>	<u>Redemption dates per year</u>	<u>Redemption notice period</u>
Commingled bond fund	\$ 3,696,322	—	None	N/A
Commingled stock funds:				
United States	18,169,061	—	12	6 – 10 days
International	<u>162,160,050</u>	<u>—</u>	Daily/12	3 – 6 days
Total	<u>180,329,111</u>	<u>—</u>		
Hedge funds:				
Multistrategy	186,577,986	—	1/2/4	45 – 180 days
Credit – redeemable	102,643,317	—	1	60/90 days
Credit – nonredeemable	<u>43,390,965</u>	<u>—</u>	None	N/A
Total	<u>332,612,268</u>	<u>—</u>		
Inflation hedge funds:				
Public energy	39,834,717	—	Daily	1 day
Public real estate	48,256,401	—	1/4	1/45 days
Private energy	26,333,328	12,953,451	None	N/A
Private real estate	<u>26,537,281</u>	<u>8,302,820</u>	None	N/A
Total	140,961,727	21,256,271		
Private equity funds	<u>152,015,019</u>	<u>83,940,824</u>	None	N/A
Total	<u>\$ 809,614,447</u>	<u>105,197,095</u>		

The following provides details for the investment strategies as of December 31, 2011 listed above:

Commingled Bond Fund

This consists of \$3.5 million invested in a fund that invests in co-op mortgage loans that are not traded on public markets. This fund is not redeemable but makes distributions to investors at the manager's discretion. The fund is expected to fully distribute its assets over the next two years approximately.

Commingled Stock Funds

This includes \$117.9 million invested in three funds that invest in publicly traded common stock.

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Multistrategy Hedge Funds

This consists of \$97.7 million invested in three hedge funds, of which \$69.8 million is redeemable and \$27.9 million is invested in private investments that are expected to be sold by the funds' managers as market opportunities arise. These hedge funds invest in equity, fixed income, and derivative investments and vary their investment strategies in response to changing market opportunities. As of December 31, 2011, the Foundation's combined investments in these funds included 34% equity strategies, 29% credit strategies, 28% private investments, and 9% cash.

Credit Hedge Funds – Redeemable

This includes \$93.9 million invested in two hedge funds that invest primarily in publicly traded debt securities purchased at discounts to par value, including publicly traded bonds, bank debt, residential and commercial mortgage-backed securities, and other asset-backed securities.

Credit Hedge Fund – Nonredeemable

This consists of \$42.7 million invested in a hedge fund that makes distributions to investors at the manager's discretion and is expected to fully distribute its assets over the next five years approximately. The fund invests in publicly traded and private debt securities purchased at discounts to par value.

Public Energy and Commodity Funds

This includes \$36.8 million invested in a fund that invests on a global basis in the publicly traded common stock of energy companies and \$27.5 million in a fund that invests on a global basis in publicly traded common stock and futures related to investments in energy, metals, grains, cotton, cocoa, sugar, and other commodities.

Public Real Estate Fund

This consists of \$33.8 million invested in a fund that invests primarily in publicly traded equity and debt securities issued by Real Estate Investment Trusts (REITs) and other companies with significant real estate holdings.

Private Energy Funds

This consists of \$29.2 million in five funds that make distributions to investors at the managers' discretion and are expected to fully distribute their assets over the next ten years approximately. As of December 31, 2011, the Foundation's combined investments in these funds included 82% private energy funds of funds that invest in diversified portfolios of direct private energy funds and 18% in two direct private energy funds that invest in companies that acquire or develop natural resource reserves, power generation facilities, and energy infrastructure assets.

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Private Real Estate Funds

This includes \$28.8 million invested in three funds that make distributions to investors at the managers' discretion and are expected to fully distribute their assets over the next ten years approximately. These funds invest directly in real estate properties that are not traded on public markets. As of December 31, 2011, the Foundation's combined investments in these funds included 41% value add and 59% opportunistic investments.

Private Equity Funds

This includes \$177.4 million invested in 20 funds that make distributions to investors at the managers' discretion and are expected to fully distribute their assets over the next ten years approximately. As of December 31, 2011, the Foundation's combined investments in these funds included 33% primary funds of funds that invest in a diversified portfolio of buyout and venture capital funds, 34% secondary funds of funds that purchase interests in buyout and venture capital funds on a secondary basis at discounts to net asset value, 10% buyout funds that invest directly in media and financial companies, 16% venture capital funds that invest directly in technology and media companies, and 7% buyout funds that invest directly in companies in several sectors.

(4) Grants Payable

At December 31, 2011 and 2010, grants scheduled to be paid in future years are as follows:

	2011	2010
Year:		
2011	\$ —	9,597,180
2012	9,035,575	2,548,500
2013	5,504,500	935,000
2014	250,000	630,000
2015	250,000	—
	15,040,075	13,710,680
Discount to present value (based on interest rates from 0.10% to 4.37% for 2011 and 0.25% to 4.37% for 2010)	(303,182)	(163,878)
	\$ 14,736,893	13,546,802

(5) Deferred Liabilities

At December 31, 2011 and 2010, deferred liabilities consisted of the following:

	2011	2010
Federal excise tax (note 6)	\$ 2,307,260	3,842,747
5 Penn Plaza landlord incentives	1,927,280	2,010,391
	\$ 4,234,540	5,853,138

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(6) Federal Excise Tax

As a private foundation, the Foundation is normally subject to a federal excise tax equal to 2% of its net investment income for tax purposes. However, under Section 4940(e) of the Code, this tax is reduced to 1% if certain conditions are met. The Foundation's current taxes are estimated at 1% of net investment income for December 31, 2011 and 2% for December 31, 2010.

The Foundation records a liability for deferred federal excise tax at the 2% rate on the total unrealized appreciation in the fair value of investments. The federal excise tax will be paid as realized gains are reported for tax purposes. The unrealized losses/gains on investments are reported net of the deferred federal excise tax benefit of \$1,535,487 and expense of \$2,800,799 for the years ended December 31, 2011 and 2010, respectively, on the statements of activities.

(7) Fair Value Disclosures

The carrying amount of cash equivalents and cash, other assets and receivables, accrued expenses and other payables, and grants payable approximates fair value because of the short maturities of these financial instruments.

The Foundation permits several of its investment managers to invest, within prescribed limits, in financial futures (primarily, U.S. Treasury futures) and options, and to sell securities not yet purchased for hedging purposes and for managing the asset allocation and duration of the fixed income portfolios. At December 31, 2011 and 2010, the Foundation held no futures contracts.

(8) Lease Commitments

The Foundation occupies office space under a lease agreement expiring in 2021.

The Foundation's total contractual lease commitments are as follows:

	<u>5 Penn Plaza</u>
Year:	
2012	\$ 939,000
2013	948,000
2014	948,000
2015	948,000
2016	1,017,000
2017 and thereafter	<u>4,548,000</u>
	<u>\$ 9,348,000</u>

During the years ended December 31, 2011 and 2010, rent expense, including escalations, was \$861,218 and \$865,821, respectively.

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(9) Pension Plans

The Foundation provides a defined contribution retirement plan for all eligible employees, whereby the Foundation contributes 15% of a participant's eligible earnings on an annual basis. In addition, the Foundation provides a supplemental executive retirement plan for the benefit of certain eligible employees. Total pension expense for the years ended December 31, 2011 and 2010 was \$654,370 and \$730,158, respectively.

(10) Subsequent Events

The Foundation evaluated subsequent events after the balance sheet date of December 31, 2011 through July 25, 2012, which was the date the financial statements were available to be issued, and determined there were no additional matters that are required to be disclosed.