THE WALLACE FOUNDATION

Financial Statements

December 31, 2012 and 2011

(With Independent Auditors' Report Thereon)

KPMG LLP
345 Park Avenue
New York, NY 10154

Independent Auditors' Report

The Board of Directors
The Wallace Foundation:

We have audited the accompanying financial statements of The Wallace Foundation (the Foundation), which comprise the balance sheets as of December 31, 2012 and 2011, and the related statements of activities and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

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 from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

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, 2012 and 2011, and changes in its net assets and its cash flows for the years then ended in accordance with U.S. generally accepted accounting principles.

KPMG LLP

June 10, 2013

THE WALLACE FOUNDATION

Balance Sheets

December 31, 2012 and 2011

Assets	2012	2011
Cash equivalents and cash	$ 11,663,605	10,947,553
Investments (note 3)	1,384,923,340	1,313,314,703
Other assets and receivables	1,935,669	954,902
Fixed assets, net of accumulated depreciation of $2,143,376 in 2012 and $1,868,998 in 2011	2,131,710	2,362,911
Total assets	$ 1,400,654,324	1,327,580,069
Liabilities and Net Assets		
Liabilities:		
Accrued expenses and other payables	$ 1,606,307	1,015,615
Grants payable (note 4)	17,731,020	14,736,893
Deferred liabilities (note 5)	6,301,029	4,234,540
Total liabilities	25,638,356	19,987,048
Net assets – unrestricted	1,375,015,968	1,307,593,021
Total liabilities and net assets	$ 1,400,654,324	1,327,580,069

See accompanying notes to financial statements.

THE WALLACE FOUNDATION

Statements of Activities

Years ended December 31, 2012 and 2011

	2012	2011
Revenues:		
Interest and dividends	$ 13,009,589	13,835,180
Realized gains	29,508,255	56,836,061
Total investment income	42,517,844	70,671,241
Investment fees	(3,207,131)	(3,257,487)
Excise and income taxes (note 6)	(156,634)	(2,074,602)
Total investment expenses	(3,363,765)	(5,332,089)
Unrealized gains (losses), net of deferred tax (note 6)	103,737,635	(73,784,281)
Contributions	2,360	—
Net revenues (loss)	142,894,074	(8,445,129)
Expenses:		
Grants and related activities	66,077,726	63,889,246
Operating expenses	9,393,401	8,920,719
Total expenses	75,471,127	72,809,965
Change in net assets	67,422,947	(81,255,094)
Net assets:		
Beginning of year	1,307,593,021	1,388,848,115
End of year	$ 1,375,015,968	1,307,593,021

See accompanying notes to financial statements.

THE WALLACE FOUNDATION

Statements of Cash Flows

Years ended December 31, 2012 and 2011

	2012	2011
Cash flows from operating activities:		
Change in net assets	$ 67,422,947	(81,255,094)
Adjustments to reconcile change in net assets to net cash used in operating activities:		
Unrealized (gains) losses on investments	(105,933,196)	75,319,768
Realized gains on investments	(29,508,255)	(56,836,061)
Depreciation	286,956	285,818
Changes in assets and liabilities:		
Accrued investment income	1,801,027	(362,771)
Other assets and receivables	(980,767)	268,281
Accrued expenses and other payable	590,692	(426,481)
Deferred liabilities	2,066,489	(1,618,598)
Grants payable	2,994,127	1,190,091
Net cash used in operating activities	(61,259,980)	(63,435,047)
Cash flows from investing activities:		
Sales of investments	430,304,670	472,534,566
Purchases of investments	(368,272,883)	(405,925,051)
Purchases of fixed assets	(55,755)	(19,557)
Net cash provided by investing activities	61,976,032	66,589,958
Net increase in cash equivalents and cash	716,052	3,154,911
Cash equivalents and cash at beginning of year	10,947,553	7,792,642
Cash equivalents and cash at end of year	$ 11,663,605	10,947,553

See accompanying notes to financial statements.

(1) Nature of Operations

The Wallace 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 the summer break 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 to be sustained in the future.

(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.

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.

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.

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.

(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 or the president, under authority delegated by the 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 and Revisions to Prior Year Amounts

Certain reclassifications of 2011 amounts have been made to conform to the 2012 presentation.

Certain revisions of 2011 amounts have been made to correct immaterial errors in the statements of activities and cash flows. The effect on the 2011 statement of activities was to decrease interest and dividends by approximately $1.4 million and to decrease unrealized losses by the same amount. In the 2011 statement of cash flows, net unrealized losses were reduced by approximately $1.4 million and sales of investments were increased by the same amount.

(Continued)

(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, 2012 and 2011:

	2012			
	Level 1	Level 2	Level 3	Total fair value
Stocks:				
Direct ownership:				
United States	$ 176,212,604	379,102	756,218	177,347,924
International	40,674,105	—	—	40,674,105
Subtotal	216,886,709	379,102	756,218	218,022,029
Mutual funds – international	41,973,532	—	—	41,973,532
Commingled funds:				
United States	—	—	17,342,051	17,342,051
International	—	133,897,623	—	133,897,623
Subtotal	—	133,897,623	17,342,051	151,239,674
Total	258,860,241	134,276,725	18,098,269	411,235,235
Fixed income:				
Direct ownership:				
United States government/agency	—	140,689,126	—	140,689,126
United States corporate and other	—	43,388,257	—	43,388,257
Subtotal	—	184,077,383	—	184,077,383
Mutual funds:				
United States government/agency	32,473,066	—	—	32,473,066
United States corporate and other	23,272,025	—	—	23,272,025
International	9,646,129	—	—	9,646,129
Subtotal	65,391,220	—	—	65,391,220
Commingled funds:				
United States corporate and other	—	—	3,052,712	3,052,712
Total	65,391,220	184,077,383	3,052,712	252,521,315
Hedge funds:				
Multistrategy	—	57,476,544	26,346,138	83,822,682
Long/short equity	—	83,429,663	—	83,429,663
Credit – redeemable	—	82,681,242	—	82,681,242
Credit – nonredeemable	—	—	33,005,706	33,005,706
Total	—	223,587,449	59,351,844	282,939,293
Inflation hedges:				
Direct ownership – natural resources stocks	25,762,362	—	—	25,762,362
Commodity funds	—	26,041,750	—	26,041,750
Public energy funds	—	25,524,685	—	25,524,685
Public real estate funds	—	32,257,010	—	32,257,010
Private energy funds	—	—	34,582,203	34,582,203
Private real estate funds	—	—	31,495,862	31,495,862
Total	25,762,362	83,823,445	66,078,065	175,663,872
Private equity funds	—	—	210,362,974	210,362,974
Short-term investments	11,691,129	—	—	11,691,129
Accrued investment income	230,952	—	—	230,952
Receivable for investments sold, net	40,278,570	—	—	40,278,570
Total	$ 402,214,474	625,765,002	356,943,864	1,384,923,340

	2011			
	Level 1	Level 2	Level 3	Total fair value
Stocks:				
Direct ownership:				
United States	$ 179,999,679	—	773,583	180,773,262
International	37,083,931	—	—	37,083,931
Subtotal	217,083,610	—	773,583	217,857,193
Mutual funds – international	48,589,540	—	—	48,589,540
Commingled funds – international	—	117,883,250	—	117,883,250
Total	265,673,150	117,883,250	773,583	384,329,983
Fixed income:				
Direct ownership:				
United States government/agency	—	138,633,815	—	138,633,815
United States corporate and other	—	50,688,825	—	50,688,825
Subtotal	—	189,322,640	—	189,322,640
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	3,489,340	270,535,813
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
Commodity funds	—	27,488,208	—	27,488,208
Public energy funds	—	36,803,344	—	36,803,344
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	$ 429,692,228	573,400,547	310,221,928	1,313,314,703

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

The following tables present reconciliations for all Level 3 assets measured at fair value at December 31, 2012 and 2011:

	2012						
	Beginning balance	**Transfers**	**Realized gains (losses)**	**Unrealized gains (losses)**	**Purchases**	**Settlements**	**Ending balance**
Stocks – Direct ownership	$ 773,583	—	—	(17,365)	—	—	756,218
Stock - Commingled US	—	—	—	465,817	16,876,234	—	17,342,051
Fixed income – Commingled funds	3,489,340	—	178,189	(32,410)	—	(582,407)	3,052,712
Hedge funds – Multistrategy	27,934,635	(6,958,391)	—	5,369,894	—	—	26,346,138
Hedge funds – Credit – nonredeemable	42,656,158	—	6,200,718	616,789	—	(16,467,959)	33,005,706
Inflation hedges – Private energy funds	29,185,882	—	844,905	(267,504)	8,853,369	(4,034,449)	34,582,203
Inflation hedges – Private real estate funds	28,802,578	—	(559,506)	2,965,012	3,750,000	(3,462,222)	31,495,862
Private equity funds	177,379,752	—	7,608,501	13,724,601	45,215,182	(33,565,062)	210,362,974
Total	$ 310,221,928	(6,958,391)	14,272,807	22,824,834	74,694,785	(58,112,099)	356,943,864

	2011						
	Beginning balance	**Transfers**	**Realized gains (losses)**	**Unrealized gains (losses)**	**Purchases**	**Settlements**	**Ending balance**
Stocks – 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	$ 363,674,216	(85,720,480)	6,917,140	19,813,838	37,798,234	(32,261,020)	310,221,928

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. There were no transfers between Levels 1 and 2 during the years ended December 31, 2012 and 2011.

(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, 2012, the Foundation had investments of $614.7 million that could be sold on a daily basis under normal market conditions. This included $11.7 million in short-term investments, $427.9 million in direct ownership investments held in separate accounts with the Foundation's custodial trustee, $107.4 million in mutual fund investments, $25.5 million in a public energy fund, which is part of the Foundation's inflation hedge portfolio, and $42.2 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 investments), and private equity funds, including the $25.5 million public energy fund and the $42.2 million international commingled stock fund noted above, totaled $797.5 million as of December 31, 2012. 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).

(Continued)

(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, 2012 and 2011:

	2012			
	Total fair value	**Unfunded commitments**	**Redemption dates per year**	**Redemption notice period**
Commingled bond fund	$ 3,052,712	—	None	N/A
Commingled stock funds:				
United States	17,342,051	8,123,766	Biennial	90 days
International	133,897,623	—	Daily/12	3 – 6 days
Total	151,239,674	8,123,766		
Hedge funds:				
Multistrategy	83,822,682	—	1/None	45 – 180 days
Long/short equity	83,429,663	—	1/4	45/60 days
Credit – redeemable	82,681,242	—	1	60/90 days
Credit – nonredeemable	33,005,706	—	None	N/A
Total	282,939,293	—		
Inflation hedge funds:				
Commodity	26,041,750	—	12	65 days
Public energy	25,524,685	—	Daily	1 day
Public real estate	32,257,010	—	4	30 days
Private energy	34,582,203	39,419,919	None	N/A
Private real estate	31,495,862	5,015,367	None	N/A
Total	149,901,510	44,435,286		
Private equity funds	210,362,974	89,424,647	None	N/A
Total	$ 797,496,163	141,983,699		

	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	117,883,250	—	Daily/12	3 – 6 days
Total	117,883,250	—		
Hedge funds:				
Multistrategy	97,663,149	—	1/2/4/None	45 – 180 days
Credit – redeemable	93,867,368	—	1	60/90 days
Credit – nonredeemable	42,656,158	—	None	N/A
Total	234,186,675	—		
Inflation hedge funds:				
Commodity	27,488,208	—	12	65 days
Public energy	36,803,344	—	Daily	1 day
Public real estate	33,847,782	—	4	30 days
Private energy	29,185,882	23,276,687	None	N/A
Private real estate	28,802,578	7,525,947	None	N/A
Total	156,127,794	30,802,634		
Private equity funds	177,379,752	74,145,346	None	N/A
Total	$ 689,066,811	104,947,980		

The following provides details for the investment strategies as of December 31, 2012 listed above:

Commingled Bond Fund

This consists of $3.1 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. While the fund has been making distributions that suggest it may fully distribute its assets over the next two years, we are not able to determine when it will be fully paid out.

Commingled Stock Funds

This includes $151.2 million invested in four funds that invest in publicly traded common stock.

Multistrategy Hedge Funds

This consists of $83.8 million invested in two hedge funds, of which $57.5 million is redeemable and $26.3 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, 2012, the Foundation's combined investments in these funds included 32% equity strategies, 28% credit strategies, 14% private investments, and 26% cash.

Long/Short Equity Hedge Funds

This includes $83.4 million invested in three hedge funds that invest in publicly traded equity securities using a combination of long and short positions.

Credit Hedge Funds – Redeemable

This includes $82.7 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 $33 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 four years approximately. The fund invests in publicly traded and private debt securities purchased at discounts to par value.

Commodity Funds

This includes $26 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 Energy Funds

This includes $25.5 million invested in a fund that invests on a global basis in the publicly traded common stock of energy companies.

Public Real Estate Fund

This consists of $32.3 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 $34.6 million in seven 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, 2012, the Foundation's combined investments in these funds included 67% in three private energy funds of funds that invest in diversified portfolios of direct private energy funds and

33% in four direct private energy funds that invest in companies that acquire or develop natural resource reserves, power generation facilities, and energy infrastructure assets.

Private Real Estate Funds

This includes $31.5 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, 2012, the Foundation's combined investments in these funds include 34% value add and 66% opportunistic investments.

Private Equity Funds

This includes $210.4 million invested in 23 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, 2012, the Foundation's combined investments in these funds includes 28% in seven primary funds of funds that invest in a diversified portfolio of buyout and venture capital funds, 36% in seven secondary funds of funds that purchase interests in buyout and venture capital funds on a secondary basis at discounts to net asset value, 18% in four venture capital funds that invest directly in technology and media companies, and 18% in five buyout funds that invest in specific sectors.

(4) Grants Payable

At December 31, 2012 and 2011, grants scheduled to be paid in future years are as follows:

	2012	2011
Year:		
2012	$ —	9,035,575
2013	12,333,384	5,504,500
2014	4,278,100	250,000
2015	901,302	250,000
2016	250,000	—
	17,762,786	15,040,075
Discount to present value (based on interest rates from 0.10% to 1.47% for 2012 and 0.10% to 4.37% for 2011)	(31,766)	(303,182)
	$ 17,731,020	14,736,893

(5) Deferred Liabilities

At December 31, 2012 and 2011, deferred liabilities consisted of the following:

		2012	2011
Federal excise tax (note 6)	$	4,502,821	2,307,260
5 Penn Plaza landlord incentives		1,798,208	1,927,280
	$	6,301,029	4,234,540

(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, 2012 and 2011.

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 expense of $2,195,561 and tax benefit of $1,535,487 for the years ended December 31, 2012 and 2011, 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-term 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 in addition to the duration of the fixed income portfolios. At December 31, 2012 and 2011, 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:

		5 Penn Plaza
Year:		
2013	$	948,000
2014		948,000
2015		948,000
2016		1,018,000
2017		1,031,000
2018 and thereafter		3,517,000
	$	8,410,000

During the years ended December 31, 2012 and 2011, rent expense, including escalations, was $881,171 and $861,218, respectively.

(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, 2012 and 2011 was $650,219 and $654,370, respectively.

(10) Subsequent Events

The Foundation evaluated subsequent events after the balance sheet date of December 31, 2012 through June 10, 2013, 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.