

**John D. and Catherine T. MacArthur Foundation**

**Financial Statements**

*December 31, 2007 and 2006*

(With Independent Auditors' Report Thereon)



**KPMG LLP**  
303 East Wacker Drive  
Chicago, IL 60601-5212

## **Independent Auditors' Report**

The Board of Directors  
John D. and Catherine T. MacArthur Foundation:

We have audited the accompanying statements of financial position of John D. and Catherine T. MacArthur Foundation (the Foundation) as of December 31, 2007 and 2006, 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 John D. and Catherine T. MacArthur Foundation as of December 31, 2007 and 2006, 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**

June 27, 2008

# John D. and Catherine T. MacArthur Foundation

## Statements of Financial Position

December 31, 2007 and 2006

	2007 (000's omitted)	2006
<b>Assets</b>		
Cash and cash equivalents	\$ 1,057	\$ 3,499
Investments	6,896,207	6,054,150
Program-related investments	118,394	92,871
Assets held for charitable use	28,310	27,370
Other assets	<u>6,663</u>	<u>2,301</u>
Total assets	<u>\$ 7,050,631</u>	<u>\$ 6,180,191</u>
<b>Liabilities and net assets</b>		
Grants payable	\$ 281,261	\$ 225,561
Other liabilities	44,313	27,857
Excise and income taxes	<u>30,267</u>	<u>24,502</u>
Total liabilities	355,841	277,920
Unrestricted net assets	<u>6,694,790</u>	<u>5,902,271</u>
Total liabilities and net assets	<u>\$ 7,050,631</u>	<u>\$ 6,180,191</u>

*The accompanying notes are an integral part of the financial statements.*

# John D. and Catherine T. MacArthur Foundation

## Statements of Activities

For the years ended December 31, 2007 and 2006

	2007	2006
	(000's omitted)	
<b>Investment income</b>		
Interest and dividends	\$ 113,379	\$ 226,394
Realized gain	543,738	557,568
Other	<u>4,700</u>	<u>4,096</u>
Total investment income	<u>661,817</u>	<u>788,058</u>
<b>Investment expenses</b>		
Fees and expenses	83,694	67,979
Excise and income taxes	<u>13,107</u>	<u>25,970</u>
Total investment expenses	<u>96,801</u>	<u>93,949</u>
<b>Unrealized gain on investments</b>	<u>553,861</u>	<u>233,723</u>
Net investment income	<u>1,118,877</u>	<u>927,832</u>
<b>Operating expenses</b>		
Grants authorized	288,067	205,516
Direct program	1,378	1,442
Administrative	27,462	26,123
Other	<u>9,451</u>	<u>2,337</u>
Total operating expenses	<u>326,358</u>	<u>235,418</u>
Change in unrestricted net assets	792,519	692,414
<b>Unrestricted net assets, beginning of year</b>	<u>5,902,271</u>	<u>5,209,857</u>
<b>Unrestricted net assets, end of year</b>	<u>\$ 6,694,790</u>	<u>\$ 5,902,271</u>

*The accompanying notes are an integral part of the financial statements.*

# John D. and Catherine T. MacArthur Foundation

## Statements of Cash Flows

For the years ended December 31, 2007 and 2006

	2007	2006
	(000's omitted)	
<b>Cash flows from operating activities</b>		
Change in unrestricted net assets	\$ 792,519	\$ 692,414
Adjustments to reconcile change in unrestricted net assets to net cash used in operations		
Depreciation	1,974	1,168
Realized gain on investments	(543,738)	(557,568)
Unrealized gain on investments	(553,861)	(233,723)
Increase in non-investment assets	(31,668)	(6,273)
Increase (decrease) in grants payable	55,700	(7,158)
Increase (decrease) in other liabilities	16,456	(1,564)
Increase in excise and income taxes	<u>5,765</u>	<u>6,050</u>
Net cash used in operating activities	<u>(256,853)</u>	<u>(106,654)</u>
<b>Cash flows from investment activities</b>		
Proceeds from sale of investments	5,360,934	5,707,605
Purchase of investments	<u>(5,106,523)</u>	<u>(5,599,527)</u>
Net cash provided by investment activities	<u>254,411</u>	<u>108,078</u>
Net (decrease) increase in cash and cash equivalents	(2,442)	1,424
<b>Cash and cash equivalents at beginning of year</b>	<u>3,499</u>	<u>2,075</u>
<b>Cash and cash equivalents at end of year</b>	<u>\$ 1,057</u>	<u>\$ 3,499</u>

*The accompanying notes are an integral part of the financial statements.*

# **John D. and Catherine T. MacArthur Foundation**

## **Notes to Financial Statements**

*December 31, 2007 and 2006*

### **1. Organization**

The John D. and Catherine T. MacArthur Foundation is a private, independent grant making institution that supports creative people and effective institutions committed to building a more just, verdant, and peaceful world. The Foundation makes grants and program-related investments through four programs. The Program on Global Security and Sustainability focuses on international issues, including human rights and international justice, peace and security, conservation and sustainable development, higher education, migration, and population and reproductive health. The Program on Human and Community Development addresses issues in the United States that include community and economic development; housing, with a focus on the preservation of affordable rental housing; juvenile justice reform; and education, with an interest in how technology is affecting children and society. The General Program supports public interest media, including public radio and television. Grants are also made to arts and cultural institutions in the Chicago area and for special initiatives. The MacArthur Fellows Program awards five-year, unrestricted fellowships to individuals across all ages and fields who show exceptional merit and promise of continued creative work.

### **2. Summary of Significant Accounting Policies**

The Foundation prepares its financial statements on the accrual basis of accounting. The Foundation's significant accounting policies are as follows:

#### ***Cash Equivalents***

Cash and cash equivalents held by the Foundation for use in its operations consist of temporary investments with original maturities of three months or less. Cash and cash equivalents used by the Foundation in managing its investments are reported in investments.

#### ***Investments***

Investments are reported at fair value. Fair value is based on quoted market prices when available. For investments in limited partnerships and other similar investments, the fair value is based on valuations provided by external investment managers, which are reviewed by management for reasonableness. The Foundation believes the carrying amount of these financial instruments is a reasonable estimate of fair value. Because alternative investments are not readily marketable, their estimated value is subject to uncertainty and may differ from the value that would have been used had a ready market for such investments existed.

#### ***Program-related Investments***

In accordance with Section 4944 of the Internal Revenue Code, the Foundation is permitted to make investments that are related to its philanthropic programs. These investments are anticipated to have a less than market return and are recorded net of appropriate reserves for collectibility. In the year of the investment, the Foundation receives a credit toward its distribution requirement. Return of principal of program-related investments increases the Foundation's distribution requirement in the year of receipt. The Foundation had open program-related investment commitments of \$18.8 million and \$10.8 million as of December 31, 2007 and 2006, respectively.

# **John D. and Catherine T. MacArthur Foundation**

## **Notes to Financial Statements**

*December 31, 2007 and 2006*

### **2. Summary of Significant Accounting Policies, continued**

#### ***Assets Held for Charitable Purposes***

The Foundation holds certain assets, primarily real estate, for charitable purposes. The Foundation receives a credit toward its distribution requirement equal to the fair value, as determined by appraisal, of the assets at the time they are put into charitable use.

#### ***Grants***

Grant awards are expensed when approved. Grants payable that are expected to be paid in future years are recorded at the present value of expected future payments. The Foundation discounted grants payable using an average rate of 3.09 percent and 4.77 percent as of December 31, 2007 and 2006, respectively.

#### ***Federal Taxes***

The Foundation has received a determination letter from the Internal Revenue Service indicating that it qualifies as a tax-exempt organization under Section 501(c)(3) of the Internal Revenue Code and is not subject to federal income taxes except for income from its unrelated business activities. Under Section 4940 of the Internal Revenue Code, a federal excise tax of 2 percent is imposed on the Foundation's net investment income and realized capital gains.

Deferred tax expense results from certain income and expense items, primarily unrealized gains or losses, being accounted for in different time periods for financial statement purposes than for federal excise and income tax purposes. Appropriate provisions are made in the financial statements for deferred taxes in recognition of these timing differences.

#### ***Employee Retirement Plan***

The Foundation sponsors a defined contribution retirement plan for its eligible employees. Plan participants are fully vested after one year of service. The Foundation is current with its contributions to the plan. Employer contributions to the plan totaled \$2.3 million and \$2.2 million in 2007 and 2006, respectively.

#### ***Post-retirement Benefits***

The Foundation provides health care and life insurance benefits to certain of its retired employees and their eligible dependents. In 2007, the Foundation adopted Financial Accounting Standards Board Statement No. 158 (FAS No. 158), *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans*. FAS No. 158 requires the Foundation to recognize the funded status of its post-retirement benefit plan in the statement of financial position at year end and to recognize the change in the funded status in unrestricted net assets.

# John D. and Catherine T. MacArthur Foundation

## Notes to Financial Statements

December 31, 2007 and 2006

### 2. Summary of Significant Accounting Policies, continued

The Foundation recorded post-retirement benefit obligations of \$29.9 million and \$19.2 million as of December 31, 2007 and 2006, respectively. The incremental effect for the adoption of FAS No. 158 in 2007 was an increase in the accrued post-retirement obligation of \$9.9 million.

#### *Investment Expenses*

Total investment expenses as shown are \$96.8 million and \$93.9 million in 2007 and 2006, respectively. The Foundation includes indirect fees and expenses reported by investment partnerships in total investment expenses. These indirect costs are \$47.6 million and \$32.2 million in 2007 and 2006, respectively. Total investment expenses excluding indirect costs are \$49.2 million and \$61.7 million in 2007 and 2006, respectively.

Total investment income as shown is \$661.8 million and \$788.1 million in 2007 and 2006, respectively. Total investment income net of indirect costs is \$614.2 million and \$755.9 million in 2007 and 2006, respectively.

#### *Estimates*

The preparation of the Foundation's financial statements in conformity with 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 income and expenses during the reporting period. Actual results could differ from those estimates.

### 3. Investments

Investments as of December 31, 2007 and 2006 are as follows:

	2007 (000's omitted)		2006 (000's omitted)	
	<u>Fair Value</u>	<u>Cost</u>	<u>Fair value</u>	<u>Cost</u>
Public investments				
Equities	\$ 2,596,341	\$ 1,941,999	\$ 2,685,950	\$ 2,160,076
Fixed income	869,783	793,722	905,338	786,545
Marketable alternatives	433,368	320,000	328,466	260,000
Private investments				
Equities	1,080,120	761,889	870,609	802,056
Fixed income	677,270	557,617	271,355	251,005
Real estate and energy	<u>1,239,325</u>	<u>954,792</u>	<u>992,432</u>	<u>794,788</u>
Total investments	\$ <u>6,896,207</u>	\$ <u>5,330,019</u>	\$ <u>6,054,150</u>	\$ <u>5,054,470</u>

# **John D. and Catherine T. MacArthur Foundation**

## **Notes to Financial Statements**

*December 31, 2007 and 2006*

### **3. Investments, continued**

The Foundation's exposure in limited partnership investments and certain corporate equity investments, which totaled \$5,368.7 million and \$4,414.8 million as of December 31, 2007 and 2006, respectively, is limited to its partnership or equity investments in these entities.

The Foundation had pending trade purchases of \$3.2 million and \$6.5 million and pending sales of \$6.1 million and \$7.1 million as of December 31, 2007 and 2006, respectively, which are included in investments.

Through a securities lending program, managed by its investment custodians, the Foundation loans certain marketable securities included in its investment portfolio. The custodians' loan agreements require the borrowers to maintain collateral equal to 102 percent to 105 percent of the fair value of the securities loaned. This collateral is in the form of cash, U.S. Treasury Bills, or guaranteed letters of credit and is revalued on a daily basis. The average amount of loaned securities outstanding was \$282.9 million and \$300.8 million during 2007 and 2006, respectively. No amounts were outstanding as of December 31, 2007 and 2006.

The Foundation's investment strategy incorporates certain financial instruments, which involve, to varying degrees, elements of market risk, credit risk and counterparty insolvency risk in excess of the carrying value of assets recorded in the financial statements. These instruments include securities sold but not yet purchased, forward currency contracts, limited partnership investments and certain corporate equity investments.

The Foundation invests directly with some managers whose strategies include shorting securities in accordance with investment management agreements. Securities sold but not yet purchased on the Foundation's behalf amounted to \$66.5 million and \$51.0 million as of December 31, 2007 and 2006, respectively. A third party held cash collateral of \$81.2 and \$63.6 million against these short positions as of December 31, 2007 and 2006, respectively. These securities have market risk to the extent that the Foundation's managers, in satisfying their obligations, may have to purchase securities at higher amounts than recorded. The Foundation also invests in funds that may short securities where the value of such shorted securities cannot be readily determined.

The Foundation enters into forward contracts to manage currency exchange risk inherent in its portfolio. At December 31, 2007 and 2006, the nominal value of contracts purchased totaled \$1,619.0 million and \$1,477.6 million, respectively, and the nominal value of contracts sold totaled \$1,628.1 million and \$1,487.7 million, respectively. Such contracts involve, to varying degrees, risk of loss arising from the possible inability of counterparties to meet the terms of the contracts. The unrealized gain or loss from these contracts is recorded in investments.

The Foundation had open private investment funding commitments of approximately \$1,632.6 million and \$1,531.1 million as of December 31, 2007 and 2006, respectively.

# John D. and Catherine T. MacArthur Foundation

## Notes to Financial Statements

December 31, 2007 and 2006

### 4. Excise and Income Taxes

Excise and income taxes provided for in the financial statements for the years ended December 31, 2007 and 2006, include the following components:

	2007	2006
	(000's omitted)	
Federal excise taxes		
Current	\$ 9,899	\$ 12,141
Deferred	<u>11,330</u>	<u>4,541</u>
Total	21,229	16,682
Federal and state income taxes		
Current	<u>3,208</u>	<u>13,829</u>
Total taxes	\$ <u>24,437</u>	\$ <u>30,511</u>

### 5. Commitments and Contingencies

In 2003 the Foundation entered into agreements under which it is obligated to make guarantees up to \$15.0 million in support of loans to finance a portion of the cost of constructing new, mixed income communities on the sites of former public housing developments in the City of Chicago. The loans are disbursed in phases as the sites are developed. The source of repayment for the loans are incremental property taxes paid by the households that purchase new subsidized and market rate homes on the sites. The Foundation's guarantees can be called if the incremental property tax revenue is not sufficient to meet the loan obligations or if certain other events occur that trigger a default under the terms of the agreements. Based on estimates of future property tax receipts, the Foundation may be required to make disbursements under the guarantees.

The Foundation increased the amount of its uncommitted line of credit demand note to \$150.0 million in 2007 from \$100.0 million in 2006. The interest rate will be agreed upon at the time advances are made. No amounts were outstanding at December 31, 2007 and 2006.

The Foundation is involved in several legal actions. The Foundation believes it has defenses for these claims, believes the claims are substantially without merit and is vigorously defending the actions. In the opinion of management, based on advice of legal counsel, the final disposition of these matters is not expected to have a material effect on the Foundation's financial statements.