# *The Lynde and Harry Bradley Foundation, Inc.*

*Financial Statements as of and for the Years Ended December 31, 2005 and 2004, and Independent Auditors' Report*

# THE LYNDE AND HARRY BRADLEY FOUNDATION, INC.

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## INDEPENDENT AUDITORS' REPORT

To the Board of Directors of
The Lynde and Harry Bradley Foundation, Inc.:

We have audited the accompanying statements of financial position of The Lynde and Harry Bradley Foundation, Inc. (the "Foundation") as of December 31, 2005 and 2004, and the related statements of activities and cash flows for the years then ended. These financial statements are the responsibility of the Foundation's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with 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, such financial statements present fairly, in all material respects, the financial position of the Foundation as of December 31, 2005 and 2004, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Deloitte & Touche LLP

February 10, 2006

# THE LYNDE AND HARRY BRADLEY FOUNDATION, INC.

## STATEMENTS OF FINANCIAL POSITION
## AS OF DECEMBER 31, 2005 AND 2004

| | 2005 | 2004 |
|---|---|---|
| | (000's omitted) | |
| **ASSETS** | | |
| CASH AND CASH EQUIVALENTS | $ 36,696 | $ 14,118 |
| ACCRUED INVESTMENT INCOME RECEIVABLE | 815 | 803 |
| DUE FROM BROKERS FOR SECURITIES SOLD | 982 | 135 |
| COLLATERAL HELD FOR SECURITIES LOANED | 49,818 | 52,687 |
| PREPAID EXPENSES AND OTHER ASSETS | | 328 |
| INVESTMENTS, At fair value (cost of $542,258 and $512,580 at December 31, 2005 and 2004, respectively): | | |
| Fixed income mutual funds | 17,728 | 16,318 |
| U.S. government and agency obligations | 22,838 | 21,490 |
| Corporate bonds | 21,501 | 21,178 |
| Mortgage-backed securities | 4,366 | 4,421 |
| Other asset-backed securities | 3,834 | 4,144 |
| Common and preferred stocks | 309,630 | 344,161 |
| Alternative investments | 282,922 | 220,988 |
| Other | 387 | 984 |
| Total investments | 663,206 | 633,684 |
| LAND, BUILDINGS, FURNITURE, AND FIXTURES—Net | 4,377 | 4,411 |
| TOTAL | $ 755,894 | $ 706,166 |
| **LIABILITIES AND NET ASSETS** | | |
| LIABILITIES: | | |
| Accrued expenses | $ 1,715 | $ 1,597 |
| Grants payable | 9,864 | 7,163 |
| Due to brokers for securities purchased | 1,802 | 1,752 |
| Payable under securities loan agreements | 49,818 | 52,687 |
| Notes payable | 328 | 507 |
| Long term grants payable | 7,809 | |
| Total liabilities | 71,336 | 63,706 |
| UNRESTRICTED NET ASSETS | 684,558 | 642,460 |
| TOTAL | $ 755,894 | $ 706,166 |

See notes to financial statements.

# THE LYNDE AND HARRY BRADLEY FOUNDATION, INC.

## STATEMENTS OF ACTIVITIES
## FOR THE YEARS ENDED DECEMBER 31, 2005 AND 2004

| | 2005 | 2004 |
|---|---|---|
| | (000's omitted) | |
| UNRESTRICTED REVENUES AND GAINS: | | |
| Investment activity: | | |
| Interest and dividend income | $ 14,208 | $ 12,815 |
| Realized gain on investments | 84,473 | 79,263 |
| Unrealized gain on investments | 123 | 16,898 |
| Less investment expenses | (8,533) | (7,844) |
| Total investment activity | 90,271 | 101,132 |
| Donor Intent Contributions | 3,307 | 2,553 |
| Total unrestricted revenues and gains | 93,578 | 103,685 |
| GRANTS AND EXPENSES: | | |
| Grants approved for charitable purposes—net | 45,222 | 33,169 |
| General and administrative | 4,848 | 4,072 |
| Excise and income taxes | 1,410 | 1,748 |
| Total grants and expenses | 51,480 | 38,989 |
| INCREASE IN UNRESTRICTED NET ASSETS | 42,098 | 64,696 |
| NET ASSETS: | | |
| Beginning of year | 642,460 | 577,764 |
| End of year | $ 684,558 | $ 642,460 |

See notes to financial statements.

# THE LYNDE AND HARRY BRADLEY FOUNDATION, INC.

## STATEMENTS OF CASH FLOWS
## FOR THE YEARS ENDED DECEMBER 31, 2005 AND 2004

| | 2005 | 2004 |
|---|---|---|
| | (000's omitted) | |
| OPERATING ACTIVITIES: | | |
| Increase in unrestricted net assets | $ 42,098 | $ 64,696 |
| Adjustments to reconcile increase in net assets to net cash used in operating activities: | | |
| Depreciation | 300 | 238 |
| Net realized and unrealized gains on investments | (84,396) | (95,639) |
| Grants paid with stock transfers | 11,784 | 8,506 |
| Change in provision for losses on limited partnerships | (200) | (522) |
| Decrease in accrued investment income receivable | (12) | (54) |
| (Decrease) increase in due to (from) brokers for securities purchased (sold) | (797) | 1,251 |
| Decrease (increase) in prepaid expenses and other assets | 328 | (294) |
| Increase in accrued expenses | 118 | 72 |
| Increase (decrease) in grants payable | 2,701 | (111) |
| Increase in long term grants payable | 7,809 | |
| Net cash used in operating activities | (20,267) | (21,857) |
| INVESTING ACTIVITIES: | | |
| Proceeds from the sale of investments | 416,306 | 456,296 |
| Purchase of investments | (373,016) | (429,910) |
| Purchase of property and equipment | (266) | |
| Net cash provided by investing activities | 43,024 | 26,386 |
| FINANCING ACTIVITIES—Payments on notes payable | (179) | (159) |
| NET INCREASE IN CASH AND CASH EQUIVALENTS | 22,578 | 4,370 |
| CASH AND CASH EQUIVALENTS: | | |
| Beginning of year | 14,118 | 9,748 |
| End of year | $ 36,696 | $ 14,118 |
| SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION: | | |
| Cash payments for interest | $ 16 | $ 17 |
| Cash payments for excise and income taxes | $ 1,592 | $ 1,950 |

See notes to financial statements.

# THE LYNDE AND HARRY BRADLEY FOUNDATION, INC.

## NOTES TO FINANCIAL STATEMENTS
## AS OF AND FOR THE YEARS ENDED DECEMBER 31, 2005 AND 2004

### 1. ORGANIZATION AND PURPOSE

The Lynde and Harry Bradley Foundation, Inc. (the "Foundation"), a nonprofit organization, was incorporated under the laws of Wisconsin on June 29, 1942, to raise, invest and reinvest money, and devote the principal and net earnings therefrom perpetually and exclusively for charitable, scientific, literary, and educational purposes. The programs and funding decisions of the Foundation are the responsibility of the Foundation's Board of Directors.

### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

***Basis of Presentation***—The financial statements of the Foundation have been prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America and comply with the guidance in the American Institute of Certified Public Accountants Audit and Accounting Guide for Not-for-Profit Organizations.

Net assets and revenues, expenses, gains, and losses are classified based on the existence or absence of donor-imposed restrictions. Net assets of the Foundation and changes therein are not subject to donor-imposed stipulations and therefore are classified as unrestricted net assets.

***Use of Estimates***—Management of the Foundation has made a number of estimates and assumptions relating to the reporting of assets, liabilities, and the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues, gains, grants and expenses during the reporting period. Actual results could differ from those estimates.

***Cash Equivalents***—Cash equivalents consist of short-term highly liquid instruments purchased with an original maturity date of three months or less. Such instruments are valued at cost, which approximates market value.

***Investments***—Investment transactions are recorded on the trade date. Realized gains and losses on sales of investments are determined on the specific identification basis and include the effects of currency transactions related to holdings of foreign securities. Investments, including derivative instruments and hedge funds, are generally recorded at fair value based upon quoted market prices. Investments without quoted market prices are reported at the lower of cost or fair value. Investments without quoted market prices include certain limited partnerships (see Note 4). Fair value for certain limited partnerships is determined in good faith using procedures approved by the Foundation's Board of Directors. However, because of the inherent uncertainty of valuation, the estimated fair values for investments without quoted market prices may differ significantly from the values that would have been used had a ready market for the investments existed. These differences could be material.

The Foundation establishes a valuation allowance against investments without quoted market prices when the estimated fair value of an investment is less than the Foundation's cost. If a limited partnership is determined to be permanently impaired, it is written down to its net realizable value. The net realizable value then becomes its new cost basis.

The Foundation's investments denominated in foreign currencies are translated into U.S. dollars as follows: (1) securities, financial instruments and other assets and liabilities denominated in a foreign currency are translated on the last business day of each month at the spot exchange rate; (2) forward foreign currency contracts are marked to market or net settlement value on the last business day of each month; and (3) purchases, sales, income, and expenses are translated at the spot exchange rate prevailing on the respective dates of such transactions. The effect of changes in foreign currency exchange rates on investments denominated in foreign currencies are included in the statement of activities as a component of unrealized gain (loss) on investments.

***Land, Buildings, Furniture, and Fixtures***—Land, buildings, furniture, and fixtures are stated at cost as of the date of acquisition. Depreciation of buildings and furniture and fixtures is provided on the straight-line basis over the estimated useful lives of the related assets as follows:

| Assets | Years |
|---|---|
| Buildings | 30 |
| Land improvements | 10 |
| Furniture and fixtures | 10 |

The cost of office equipment is consistently charged to expense because the Foundation does not deem such amounts sufficiently material to warrant capitalization and depreciation. The Foundation recorded $300,000 and $238,000 of depreciation expense in 2005 and 2004, respectively.

***Grants Payable***—Unconditional grants, authorized by the Foundation's Board of Directors but not yet paid, are reported as liabilities to be paid in future years.

***Federal Income Tax***—The Foundation has received a determination letter from the Internal Revenue Service indicating that it is exempt from Federal income taxes under Section 501(c)(3) of the Internal Revenue Code of 1986 (the "Code"). The Foundation is, however, subject to Federal income taxes on any net unrelated business income under the provisions of Section 511 of the Code.

***Federal Excise Tax and Distribution Requirements***—The Foundation is subject to an excise tax on net investment income, including realized gains, as defined in the Code. The excise tax is 2% for foundations but is reduced to 1% if certain distribution requirements are met. The Foundation recognized excise tax at a rate of 2% in 2005 and 2004 and accrued excise tax of $241,000 and $241,000 at December 31, 2005 and 2004, respectively.

In addition, certain minimum annual qualifying distributions are to be made approximating 5% of average net investment assets less the excise tax on investment income. Meeting the minimum distribution requirement avoids a 15% excise tax on the difference between the distributed amount and the required minimum distribution.

During 2005 and 2004, the Foundation exceeded its minimum distribution requirements by approximately $6,023,000 and $8,847,000, respectively. At December 31, 2005, total excess qualifying distributions available from 2005 and prior years to be carried forward are approximately $34,999,000 and expire as follows:

| Year | (000's omitted) |
|---|---|
| 2006 | $ 6,791 |
| 2007 | 5,406 |
| 2008 | 7,932 |
| 2009 | 8,847 |
| 2010 | 6,023 |
| | $ 34,999 |

***Reclassifications***—Certain 2004 amounts have been reclassified to conform to the 2005 presentation.

## 3. INVESTMENTS

***International Securities and Foreign Currency Contracts***—The Foundation's investments in international securities are denominated in various foreign currencies and therefore are subject to fluctuations in foreign currency exchange rates. At times, the Foundation enters into forward currency contracts whereby the Foundation agrees to exchange one currency for another on an agreed-upon date at an agreed-upon exchange rate in the future. The Foundation enters into these contracts primarily to hedge its foreign currency exposure related to international holdings. Foreign currency contracts are recorded at fair market value based upon net settlement amount. Such contracts involve, to varying degrees, risk of loss associated with the inability of counterparties to meet the terms of their contracts. Changes in the value of forward currency contracts are recognized as unrealized gains or losses until such contracts are closed. The maturities of those contracts are generally less than nine months. Unrealized losses on open foreign currency exchange contracts at December 31, 2005 and 2004, were $(6,200) and $(202,000), respectively. Net realized and unrealized gains (losses) on foreign currency exchange contracts recognized in the statement of activities were $1,500,000 and $195,800, respectively, during the year ended December 31, 2005, and $(285,000) and $(77,000), respectively, during the year ended December 31, 2004.

***Securities Lending Activities***—The Foundation has security lending arrangements with The Northern Trust Company (Northern) whereby certain of the Foundation's marketable securities are loaned to designated counterparties (borrowers) in exchange for acceptable collateral (cash, government securities, and irrevocable letters of credit). Such arrangements involve risk of loss arising from the potential nonperformance of the borrowers. The minimum collateral required is 102% of the market value of the securities on loan at the time of initiating the loan. On a daily basis, securities on loan are marked to market and collateral levels are adjusted to maintain a minimum of 102% of the loan. Northern or a third-party agent holds collateral in custody.

The market value of the loaned securities was $50,810,000 and $53,224,000 at December 31, 2005 and 2004, respectively. In exchange for loaned securities, the Foundation received cash collateral of $49,818,000 and non-cash collateral of $2,663,000 at December 31, 2005, and cash collateral of $52,687,000 and non-cash collateral of $2,094,000 at December 31, 2004. In accordance with SFAS No. 140, the cash collateral is shown as both an asset and liability of the Foundation. The income earned from securities lending activities was $108,000 and $108,000 for the years ended December 31, 2005 and 2004, respectively.

## 4. ALTERNATIVE INVESTMENTS

The Foundation has alternative investments totaling $282,922,000 and $220,988,000 as of December 31, 2005 and 2004, respectively. $226,225,000 and $180,886,000 of the investments as of December 31, 2005 and 2004, respectively, comprise liquid partnerships and real assets that are recorded at fair value based upon quoted market prices. $56,697,000 and $40,102,000 of the investments as of December 31, 2005 and 2004, respectively, comprise investments in private equities and hedge funds without quoted market prices.

## 5. LAND, BUILDINGS, FURNITURE, AND FIXTURES

Land, buildings, furniture, and fixtures at December 31, 2005 and 2004, comprises of the following:

| | 2005 (000's omitted) | 2004 (000's omitted) |
|---|---|---|
| Land and land improvements | $ 530 | $ 530 |
| Buildings and building improvements | 4,876 | 4,876 |
| Furniture and fixtures | 867 | 601 |
| | 6,273 | 6,007 |
| Less accumulated depreciation | 1,896 | 1,596 |
| | $ 4,377 | $ 4,411 |

## 6. GRANTS

Unconditional grants approved for charitable purposes during 2005 and 2004 are summarized as follows:

| | 2005 (000's omitted) | 2004 (000's omitted) |
|---|---|---|
| Total grants approved for charitable purposes | $ 45,339 | $ 33,222 |
| Returned or cancelled grants | (117) | (53) |
| Grants approved for charitable purposes—net | $ 45,222 | $ 33,169 |

Grants payable in more than one year are stated at fair value. Fair value is determined as the present value of estimated future cash flows using a discount rate of 4.3%. Grants payable as of December 31, 2005, are scheduled to be disbursed as follows:

| Year | (000's omitted) |
|---|---|
| Less than one year | $ 9,864 |
| One to three years | 9,000 |
| | 18,864 |
| Discount | (1,191) |
| | $ 17,673 |

## 7. NOTES PAYABLE

The Foundation had a $2,500,000 revolving credit note agreement with a bank bearing interest at prime less 1.25%. The Foundation terminated the line of credit on September 15, 2004, and financed the remaining balance with a fixed rate note that bears interest of 3.5% over a three year term. Loan balances were $328,000 and $507,000 at December 31, 2005 and 2004, respectively. The note is collateralized by investments held in a custodial account.

## 8. DONOR INTENT PROGRAM

In 2002, the Foundation established a Donor Intent Program whereby unrestricted contributions are received from independent donors. Donors are permitted to recommend that grants be made to organizations that are qualified as a public charity under Section 501(c)(3) of the Internal Revenue Code in an amount up to the donor's contribution. Although guided by the donor's recommendation, the Foundation has no legal obligation to follow that recommendation. Contributions to the Donor Intent Program are irrevocable and all donor recommended grants must by reviewed and approved by the Board of Directors of the Bradley Foundation. Donor contributions were $3,307,000 and $2,553,000 in 2005 and 2004, respectively. The 2005 and 2004 donor contributions were awarded and paid in the year the contributions were received.

## 9. EMPLOYEE BENEFIT PLANS

The Foundation sponsors a defined contribution plan for substantially all employees. Contributions by the Foundation are determined as a percentage of the covered employee's annual salary. Amounts expensed under this plan totaled $199,000 and $197,000 in 2005 and 2004, respectively.

The Foundation provides for certain post employment and supplemental retirement benefits for certain officers and other executives of the Foundation. Amounts expensed under these plans totaled $66,000 and $69,000 for 2005 and 2004, respectively.

## 10. CONFLICT OF INTEREST

It is the policy of the Foundation that all officers and directors shall avoid any conflict of interest between their individual interests and the interests of the Foundation. The Foundation has a conflict of interest policy whereby officers and directors must advise the board of any direct or indirect financial interest in any organization that had transactions with the Foundation. There were no such transactions in 2004 and 2005. The directors must disclose grantee charitable organizations for which they serve as a board member or have a close relationship, and abstain from voting for the approval of grants to those organizations. During 2005 and 2004, the Foundation awarded grants of $4,495,000 and $2,613,000, respectively, to such charitable organizations.

## 11. COMMITMENTS

As part of its investment management activity, the Foundation is committed to additional funding of $8,317,000 for private equities at December 31, 2005. In addition, as part of its grant activity, the Foundation has committed grants to certain organizations of $10,000,000 at December 31, 2005.

## 12. REMAINDER INTEREST IN TRUST

The Foundation has a remainder interest in an independent trust (the Trust) for which an unrelated third party acts as trustee. The Foundation is entitled to receive 70% of the trust principal upon the death of the primary beneficiary of the Trust, contingent upon actions exercised during the life of the Trust by other parties to the Trust Agreement. The total market value of the Trust at December 31, 2005, as reported by the trustee, was $174,283,000. The Trust has not been included within the Foundation's financial statements because of the contingencies associated with determining the final amount of the Foundation's remainder interest in the Trust.

## 13. SUBSEQUENT EVENT

Effective February 22, 2006, four board members of the Foundation became board members of Encounter for Culture and Education, Inc., a grantee of the Foundation.

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