

CONSOLIDATED AUDITED FINANCIAL STATEMENTS

The Cleveland Foundation
December 31, 2006 and 2005
With Report of Independent Auditors

The Cleveland Foundation
Consolidated Audited Financial Statements

December 31, 2006 and 2005

Contents

Consolidated Audited Financial Statements

Report of Independent Auditors.....	1
Consolidated Statements of Financial Position.....	2
Consolidated Statement of Activities	3
Consolidated Statements of Cash Flows.....	5
Notes to Consolidated Financial Statements.....	6

Report of Independent Auditors

The Board of Trustees
The Cleveland Foundation

We have audited the accompanying consolidated statements of financial position of The Cleveland Foundation as of December 31, 2006 and 2005, and the related consolidated 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. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of The Cleveland Foundation's internal control over financial reporting. Our audits included 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, and 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 consolidated financial position of The Cleveland Foundation at December 31, 2006 and 2005, and the consolidated results of its activities and cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States.



October 19, 2007

The Cleveland Foundation

Consolidated Statements of Financial Position

	December 31	
	2006	2005
Assets		
Cash	\$ 1,890,203	\$ 1,386,984
Short-term investments	140,271,263	117,999,569
Investments	1,721,920,976	1,571,886,398
Other investments	20,740,080	18,948,330
Property and other assets	4,276,309	5,914,884
	<u>\$1,889,098,831</u>	<u>\$1,716,136,165</u>
Liabilities and net assets		
Accounts payable and accrued expenses	\$ 1,669,755	\$ 3,651,511
Grants payable	19,210,282	17,664,612
Notes payable	1,523,454	3,285,040
Organizational endowments and other obligations	58,366,725	55,387,119
Total liabilities	<u>80,770,216</u>	<u>79,988,282</u>
Net assets:		
Unrestricted:		
For grantmaking purposes	5,864,985	6,937,903
Board-designated:		
Administrative purposes	6,263,226	4,278,522
Property	965,532	1,233,487
Total unrestricted	<u>13,093,743</u>	<u>12,449,912</u>
Temporarily restricted	642,398,222	578,739,871
Permanently restricted	1,152,836,650	1,044,958,100
	<u>1,808,328,615</u>	<u>1,636,147,883</u>
	<u>\$1,889,098,831</u>	<u>\$1,716,136,165</u>

See accompanying notes.

The Cleveland Foundation

Consolidated Statement of Activities

Year Ended December 31, 2006

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Revenue, gains, and other support				
Donor contributions	\$ 80,871	\$ 26,633,975	\$ 4,626,721	\$ 31,341,567
Dividend income	-	2,858,043	1,060	2,859,103
Interest income	826,051	5,755,418	-	6,581,469
Common trust funds income	-	1,041,105	-	1,041,105
Common investment funds income	-	20,191,220	-	20,191,220
Partial benefit funds income	-	11,301,390	-	11,301,390
Net realized and unrealized investment gains	2,465,196	82,424,399	103,250,769	188,140,364
Net assets released from restrictions	87,331,524	(87,331,524)	-	-
Other income	90,192	784,325	-	874,517
Total revenue, gains, and other support	<u>90,793,834</u>	<u>63,658,351</u>	<u>107,878,550</u>	<u>262,330,735</u>
Expenses				
Trustee and investment management fees	6,271,208	-	-	6,271,208
Other expenses	310,160	-	-	310,160
Grants expensed	73,693,899	-	-	73,693,899
Administrative expenses:				
Program	6,333,354	-	-	6,333,354
Development	1,892,971	-	-	1,892,971
Fund management	1,648,411	-	-	1,648,411
Total administrative expenses	<u>9,874,736</u>	<u>-</u>	<u>-</u>	<u>9,874,736</u>
Total expenses	<u>90,150,003</u>	<u>-</u>	<u>-</u>	<u>90,150,003</u>
Increase in net assets	643,831	63,658,351	107,878,550	172,180,732
Net assets at beginning of year	12,449,912	578,739,871	1,044,958,100	1,636,147,883
Net assets at end of year	<u>\$ 13,093,743</u>	<u>\$ 642,398,222</u>	<u>\$ 1,152,836,650</u>	<u>\$ 1,808,328,615</u>

See accompanying notes.

The Cleveland Foundation

Consolidated Statement of Activities

Year Ended December 31, 2005

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Revenue, gains, and other support				
Donor contributions	\$ 141,078	\$ 22,661,743	\$ 5,596,592	\$ 28,399,413
Dividend income	–	2,918,854	–	2,918,854
Interest income	487,751	3,671,082	–	4,158,833
Common trust funds income	–	659,472	–	659,472
Common investment funds income	–	18,675,834	–	18,675,834
Partial benefit funds income	–	11,636,959	–	11,636,959
Net realized and unrealized investment gains	2,206,901	54,417,772	39,762,795	96,387,468
Net assets released from restrictions	80,135,418	(80,135,418)	–	–
Other income	163,125	960,321	5,000	1,128,446
Total revenue, gains, and other support	83,134,273	35,466,619	45,364,387	163,965,279
Expenses				
Trustee and investment management fees	5,914,201	–	–	5,914,201
Other expenses	250,655	–	–	250,655
Grants expensed	66,352,407	–	–	66,352,407
Administrative expenses:				
Program	5,691,155	–	–	5,691,155
Development	2,599,597	–	–	2,599,597
Fund management	1,466,577	–	–	1,466,577
Total administrative expenses	9,757,329	–	–	9,757,329
Total expenses	82,274,592	–	–	82,274,592
Increase in net assets	859,681	35,466,619	45,364,387	81,690,687
Net assets at beginning of year	11,590,231	543,273,252	999,593,713	1,554,457,196
Net assets at end of year	<u>\$ 12,449,912</u>	<u>\$ 578,739,871</u>	<u>\$ 1,044,958,100</u>	<u>\$ 1,636,147,883</u>

See accompanying notes.

The Cleveland Foundation

Consolidated Statements of Cash Flows

	Year Ended December 31	
	2006	2005
Operating activities		
Increase in net assets	\$ 172,180,732	\$ 81,690,687
Adjustments to reconcile increase in net assets to net cash used in operating activities:		
Depreciation and amortization	704,539	910,942
Net unrealized and realized investment gain	(188,140,364)	(96,387,468)
Permanently restricted contributions	(4,626,721)	(5,596,592)
Increase (decrease) in other assets	1,083,953	(1,104,036)
(Decrease) increase in accounts payable and accrued expenses	(1,981,756)	2,175,190
Increase (decrease) in grants payable	1,545,670	(69,448)
Net cash used in operating activities	(19,233,947)	(18,380,725)
Investing activities		
Purchases of property	(149,917)	(70,679)
Proceeds from sale or maturity of investments	267,472,737	226,464,786
Purchases of investments	(250,450,789)	(215,733,867)
Net cash provided by investing activities	16,872,031	10,660,240
Financing activities		
Principal payments on notes payable	(1,761,586)	(270,018)
Permanently restricted contributions	4,626,721	5,596,592
Net cash provided by financing activities	2,865,135	5,326,574
Net increase (decrease) in cash and cash equivalents	503,219	(2,393,911)
Cash at beginning of year	1,386,984	3,780,895
Cash at end of year	\$ 1,890,203	\$ 1,386,984

See accompanying notes.

The Cleveland Foundation

Notes to Consolidated Financial Statements

December 31, 2006 and 2005

1. Description and Purpose of the Foundation

The Cleveland Foundation is a not-for-profit organization established in 1914. The mission statement of The Cleveland Foundation is “to enhance the quality of life for all citizens of Greater Cleveland, now and for generations to come, by building community endowment, addressing needs through grantmaking and providing leadership on key community issues.”

The consolidated financial statements include the accounts of The Cleveland Foundation (charitable corporation), The Greater Cleveland Foundation, The Cleveland Foundation (community trust approved by Resolutions of Trust) and the following affiliated supporting organizations: The City of Cleveland’s Cable Television Minority Arts and Education Fund, The Davis Fund, The Goodrich Social Settlement Fund, The Higley Fund, The McDonald Fund, The Sherwick Fund, The Billie Howland Steffee Family Fund and Medical Mutual of Ohio Charitable Foundation. The affiliated supporting organizations were established under the provisions of Section 509(a)(3) of the Internal Revenue Code. The Cleveland Foundation is responsible for expenditures of these affiliated supporting organizations for specific charitable purposes. All significant interorganizational balances and transactions have been eliminated in the preparation of the accompanying consolidated financial statements.

The Internal Revenue Service has ruled that the charitable corporation, the Greater Cleveland Foundation, the community trust and the affiliated supporting organizations are tax-exempt organizations which are exempt from Federal income taxation under Section 501(c)(3) of the Internal Revenue Code.

2. Significant Accounting Policies

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States 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. Estimates also affect the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

The Cleveland Foundation

Notes to Financial Statements (continued)

2. Significant Accounting Policies (continued)

Concentration of Credit Risk

Financial instruments which potentially expose The Cleveland Foundation to concentrations of credit risk include cash and cash equivalents and investments. As a matter of policy, The Cleveland Foundation only maintains cash balances with financial institutions having a high credit quality. Concentration of credit risk for investments is mitigated by both the distribution of investment funds among asset managers and the overall diversification of managed investment portfolios.

Short-Term Investments

Short-term investments consist of certificates of deposit, repurchase agreements and money market funds held at its trustee banks.

Financial Instruments

The carrying values of cash, short-term investments, accounts payable, accrued expenses, and grants payable are reasonable estimates of fair value due to the short-term nature of these financial instruments. Investments and other investments are reported at fair value. The reported amounts of organizational endowments and other obligations, and notes payable approximate fair value.

Investments and Investment Income

Investments are reported at their fair value. Investments traded on a national securities exchange are valued at the last reported sales price on the last business day of the year; investments traded in the over-the-counter market and listed securities for which no sale was reported on that date are valued at fair value based upon the most recently reported bid prices.

Alternative investments (principally limited partnership interests in hedged equity, private equity, absolute returns, and real assets) are valued at fair value using the equity method of accounting. Fair value reflects the current market values where determinable and the partner's contributed capital as well as the partner's share of the underlying limited partnership's realized and unrealized gains and losses. The fair value of investments held by the underlying limited partnerships is determined by the respective general partners.

The Cleveland Foundation

Notes to Financial Statements (continued)

2. Significant Accounting Policies (continued)

Realized investment gains or losses are determined by comparison of the carrying value to net proceeds received on settlement date. Unrealized gains or losses are determined by the difference between carrying value and fair value. These amounts are reported in the statements of activities as net realized and unrealized investment gains.

Investment income generated by permanently restricted net assets (excluding net realized and unrealized investment gains and losses) is reported as temporarily restricted until the program restriction of the donor is met. Investment income on temporarily restricted net assets is reported as temporarily restricted until the program restriction of the donor is met. Net unrealized and realized investment gains and losses are reported as unrestricted, temporarily restricted, or permanently restricted based upon the absence or presence of a restriction of the underlying asset.

Other Investments

Other investments include primarily notes receivable from various not-for-profit organizations approximating \$17.0 million and \$15.5 million at December 31, 2006 and 2005, respectively, real estate approximating \$0.6 million and \$2.0 million at December 31, 2006 and 2005, respectively, and miscellaneous assets approximating \$3.1 million and \$1.4 million at December 31, 2006 and 2005, respectively.

Organizational Endowments and Other Obligations

The Cleveland Foundation acts as fiduciary agent for various not-for-profit organizations. The Cleveland Foundation's responsibilities as fiduciary agent include, but are not limited to, safeguarding of assets, recordkeeping of transactions, investment management and ensuring appropriate distributions. The Cleveland Foundation's policy as fiduciary agent is to record the receipt of funds as an asset and record an equal liability. The Cleveland Foundation, as fiduciary agent, has recorded \$58,366,725 in 2006 and \$55,387,119 in 2005 in investments and an equal amount recorded in organizational endowments and other obligations in the statements of financial position. Approximately \$43,300,000 in 2006 and \$39,700,000 in 2005 of organizational endowments and other obligations are attributable to The Deaconess Community Foundation Fund.

The Cleveland Foundation excluded the change in investments and endowments and other obligations related to organizational endowments from the statements of cash flows in December 31, 2006 and 2005, respectively.

The Cleveland Foundation

Notes to Financial Statements (continued)

3. Temporarily and Permanently Restricted Net Assets

Temporarily restricted net assets are used to differentiate resources, the use of which is restricted by donors or grantors to a specific time period or purpose, from resources on which no restrictions have been placed or that arise from the general operations of The Cleveland Foundation. Temporarily restricted gifts, grants and bequests are recorded as an addition to temporarily restricted net assets in the period received. Resources restricted by donors or grantors for specific operating purposes are reported in unrestricted revenue, gains and other support to the extent expended within the period. Permanently restricted net assets consist of amounts held in perpetuity or for terms designated by donors. Temporarily restricted and permanently restricted net assets are restricted primarily for purposes which enhance the quality of life for all citizens of Greater Cleveland.

When the intent of the donor is that the assets are to remain in perpetuity, the assets are reported in accordance with the stipulations of the governing instruments of The Cleveland Foundation. Per the governing instruments, the Distribution Committee/Board of Trustees of the Foundation may distribute 20% of the principal of the donated trust assets over a five-year period. This amount is recognized as temporarily restricted net assets, with the remainder of net assets recognized as permanently restricted net assets in accordance with the intent of the donor that the assets remain in perpetuity.

When a donor restriction expires, that is, when a stipulated time restriction ends or program restriction is accomplished, temporarily restricted net assets are transferred to unrestricted net assets and reported in the statement of activities as net assets released from restrictions. Temporarily restricted net assets are available for program purposes in accordance with published standards established by The Cleveland Foundation. Net assets are released from donor restrictions by incurring expenses including grants authorized that satisfy the restricted purposes or by occurrence of other events specified by donors.

Unconditional promises to give cash and other assets to The Cleveland Foundation are reported at net realizable value at the date the promise is received. Conditional promises to give and indications of intentions to give are reported at fair value at the date received.

The Cleveland Foundation

Notes to Financial Statements (continued)

4. Contributions and Donations

The Cleveland Foundation receives donor contributions from various sources. Receipts of organizational endowments are included in organizational endowments and other obligations in the statements of financial position, and includes donor contributions received during fiscal 2006 and 2005. The following table summarizes contributions received during the year ended December 31:

	<u>2006</u>	<u>2005</u>
Organizational endowments	\$ 518,172	\$ 630,261
Donor contributions	<u>31,341,567</u>	<u>28,399,413</u>
	<u>\$ 31,859,739</u>	<u>\$ 29,029,674</u>

5. Spending Policy

The Cleveland Foundation has multiple spending policies to determine the amount of grantmaking dollars available each year. The spending policy related to trusts was modified in 2000 to calculate the “current year’s” grantmaking dollars by a formula based upon the market performance of the investments over the previous twelve quarters.

The Cleveland Foundation

Notes to Financial Statements (continued)

6. Investments

At December 31, investments are comprised of the following:

	December 31	
	2006	2005
U.S. government obligations	\$ 11,329,039	\$ 15,341,292
Bonds	14,529,386	24,495,911
Common and preferred stocks	91,333,785	88,147,599
Common trust funds	81,795,427	75,232,061
Mutual funds	100,742,877	105,591,537
Alternative investments	66,107,558	41,998,836
Other investments	3,562,197	-
Common investment funds:		
Short-term investments	32,317,320	31,661,503
U.S. government obligations	113,014,228	118,840,990
Bonds	117,943,789	97,033,704
Common and preferred stocks	455,804,704	383,079,597
Common trust funds	122,270,994	163,456,358
Mutual funds	385,789,588	344,574,272
Other investments	125,380,084	82,432,738
	1,352,520,707	1,221,079,162
Total investments	\$ 1,721,920,976	\$ 1,571,886,398

The Cleveland Foundation has established five common investment funds which allow for the commingling of various trust assets. The common investment funds are managed by four separate trustee banks with custody residing at one. Investment in the funds is limited only to the trust funds of The Cleveland Foundation.

Alternative investments are valued using the equity method of accounting. Alternative investments include hedged equity, hedge equity fund of funds, private equity, absolute return, and real assets investments. The common investment funds hold alternative investments of \$179,390,289 and \$127,133,200 at December 31, 2006 and 2005, respectively.

At December 31, 2006, The Cleveland Foundation is committed to invest an additional \$91,050,809 in alternative investments over ten years.

The Cleveland Foundation

Notes to Financial Statements (continued)

6. Investments (continued)

Alternative investments include certain interests in absolute return (hedge funds), private equity, or fixed income depending on the legal structure, and investment strategy of the underlying manager. The Foundation invests in limited partnerships and commingled vehicles, some of which employ traditional strategies (long only) in readily marketable securities (liquid equities or bonds) and others of which employ less traditional strategies (long and short equity or fixed income, event driven, macro, relative value and arbitrage strategies) that may include the use of options, futures, and other derivative instruments. Because alternative investments are not readily marketable, their estimated fair value is subject to uncertainty and therefore may differ from the value that would have been used had a ready market for such investments existed. Such difference could be material.

7. Partial Benefit Funds

Partial benefit funds provide, each in varying amounts, payment of annuities to certain individuals, trustees' fees and other expenses of the trusts, prior to payment of the balance of the corpus to The Cleveland Foundation (community trust). The fair value of partial benefit funds less related beneficiary liabilities is included in the accompanying financial statements. The community trust received approximately 95% in 2006 and 2005 of the income from partial benefit funds. At December 31, 2006 and 2005, the fair value of partial benefit funds included in investments on the statement of financial position was \$340,432,306 and \$306,685,331, respectively.

8. Notes Payable

Notes payable to a commercial bank consist of the following:

Interest Rate	Due Date	December 31	
		2006	2005
6.0%	June 1, 2011	\$ 1,523,454	\$ 1,810,040
6.5%	July 31, 2012	–	1,475,000
		<u>\$ 1,523,454</u>	<u>\$ 3,285,040</u>

The Cleveland Foundation

Notes to Financial Statements (continued)

8. Notes Payable (continued)

In 2001, the Foundation borrowed \$2,800,000 to pay for the Foundation's corporate office renovation costs. In 1999 the Foundation borrowed \$1,475,000 to purchase an adjacent parking lot next to the Hanna Building; this note was repaid in 2006 from the proceeds of the sale of the parking lot.

Future minimum notes payable payments are as follows at December 31, 2006: 2007 – \$304,172; 2008 – \$322,838; 2009 – \$342,648; 2010 – \$363,674; and 2011 – \$190,122.

9. Grants

Unconditional grants expensed are considered incurred at the time of approval by the Distribution Committee/Board of Trustees. Conditional grants are approved by the Distribution Committee/Board of Trustees and are payable upon the performance of specified conditions by the grantees. Therefore, they are not reflected in grants payable in the accompanying statements of activities until the specified conditions are satisfied.

The Distribution Committee/Board of Trustees authorized grants and an administrative budget of \$84,399,984 for 2006 and \$85,027,815 for 2005.

The following summarizes the changes in grants payable for the years ending December 31:

	<u>2006</u>	<u>2005</u>
Grants payable at beginning of year	\$ 17,664,612	\$ 17,734,060
Unconditional grants expensed	73,693,899	66,352,407
Payments made	(72,148,229)	(66,421,855)
Grants payable at end of year	<u>\$ 19,210,282</u>	<u>\$ 17,664,612</u>

The grant expense of \$73,693,899 in 2006 and \$66,352,407 in 2005 does not include program related investments of \$3,340,000 in 2006 and \$2,650,000 in 2005. Program related investments include loans, compensating balances, and shares in limited partnerships that support certain program initiatives.

Grants payable at December 31, 2006, are scheduled to be disbursed as follows: 2007 – \$15,616,578; 2008 – \$2,861,961; and 2009 and thereafter – \$731,743.

At December 31, 2006 and 2005, total authorized conditional grants were \$7,720,396 and \$11,546,474, respectively, which are not reflected in the accompanying financial statements.

The Cleveland Foundation

Notes to Financial Statements (continued)

10. Administrative Expenses

Administrative expenses, as reported on the statements of activities, consist of the following:

	December 31	
	2006	2005
Salaries and employee benefits	\$ 5,928,626	\$ 5,462,513
Occupancy and office expense	1,913,343	1,992,525
Professional and consulting fees and staff expenses	1,391,572	1,578,718
Other	641,195	723,573
	\$ 9,874,736	\$ 9,757,329

11. Affiliated Supporting Organizations

The total assets of affiliated supporting organizations, which are consolidated in the statements of financial position, are comprised of the following:

	December 31	
	2006	2005
The City of Cleveland's Cable Television Minority Arts and Education Fund	\$ 4,392,947	\$ 4,136,398
The Davis Fund	2,546,812	2,270,353
The Goodrich Social Settlement Fund	1,424,145	1,268,328
The Higley Fund	5,842,817	5,459,264
The McDonald Fund	3,647,356	3,339,209
The Sherwick Fund	28,582,781	28,977,506
The Billie Howland Steffee Family Fund	5,374,808	5,072,793
Medical Mutual of Ohio Charitable Foundation	2,273,344	2,070,900
	\$ 54,085,010	\$ 52,594,751

The Treu-Mart Fund is a supporting organization of both The Cleveland Foundation and the Jewish Community Federation of Cleveland. Financial transactions and account balances of The Treu-Mart Fund are not included in the accompanying financial statements. Fair value of investments held by The Treu-Mart Fund at December 31, 2006 and 2005, are \$19,984,108 and \$18,567,610, respectively.

The Cleveland Foundation

Notes to Financial Statements (continued)

12. Operating Lease

The Cleveland Foundation leases office space under an operating lease agreement, which expires September 1, 2011. Rental expense was \$802,185 in 2006 and \$705,168 in 2005. Future minimum rental commitments under the noncancelable operating lease at December 31, 2006 are as follows: 2007 – \$694,064; 2008 – \$714,721; 2009 – \$739,509; 2010 – \$764,297; and 2011 – \$524,679.

13. Retirement Plan

The Cleveland Foundation has a defined contribution retirement plan with Foundation contributions made, based upon specified percentages of salary, for all employees. Retirement plan expense was \$323,578 in 2006 and \$359,792 in 2005. All contributions under the plan vest with employees at the time the contributions are made.