Financial Report December 31, 2007



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# McGladrey & Pullen

Certified Public Accountants

**Independent Auditor's Report** 

To the Board of Trustees The Heritage Foundation Washington, D.C.

We have audited the accompanying balance sheets of The Heritage 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 examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of The Heritage 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 accounting principles generally accepted in the United States of America.

McGladrey of Pullen, LLP

Vienna, Virginia May 2, 2008

Balance Sheets December 31, 2007 And 2006

Assets		2007		2006
Current Assets				_
Cash and cash equivalents	\$	7,159,395	\$	7,578,073
Contributed stock		60,880		126,842
Contributions receivable		6,360,741		4,056,474
Prepayments and other assets		850,166		646,207
Total current assets		14,431,182		12,407,596
Long-Term Assets				
Investments		136,499,458		119,361,770
Deferred compensation investments		3,519,555		3,163,857
Contributions receivable, net		3,658,645		4,139,726
Property and equipment, net		38,220,475		37,921,760
Cash surrender value of insurance		516,983		509,231
Total long-term assets		182,415,116		165,096,344
Total assets	\$	196,846,298	\$	177,503,940
Liabilities And Net Assets				
Current Liabilities				
Accounts payable and accrued expenses	\$	6,448,110	\$	4,580,830
Notes payable	*	242,600	Ψ	242,600
Total current liabilities		6,690,710		4,823,430
Long-Term Liabilities				_
Notes payable		4,076,200		4,213,518
Deferred compensation obligations		3,519,555		3,163,857
Split-interest obligations		11,840,723		10,996,636
Total long-term liabilities	_	19,436,478		18,374,011
Total liabilities		26,127,188		23,197,441
Net Assets				
Unrestricted				
Board designated		116,502,056		101,029,822
Undesignated		39,597,299		39,163,940
Temporarily restricted – gifts from annuities, trusts and promises to give		13,419,755		12,915,026
Permanently restricted		1,200,000		1,197,711
•		170,719,110		154,306,499
	\$	196,846,298	\$	177,503,940

See Notes To Financial Statements.

## Statements Of Activities Years Ended December 31, 2007 And 2006

	2007	2006
Changes in Unrestricted Net Assets		
Revenue and support:		
Public support – contributions	\$ 41,832,170	\$ 42,259,180
Publications, subscriptions, and registration fees	65,167	126,008
Investment income	16,561,712	11,408,272
Other income	1,108,651	1,572,253
Net assets released from restriction – satisfaction of		
program restrictions	 4,692,142	3,415,105
Total unrestricted revenue and support	 64,259,842	58,780,818
Expenses:		
Program services:		
Research	20,337,144	19,233,544
Media and government relations	8,278,763	6,661,430
Educational programs	10,365,558	7,820,896
Total program services	 38,981,465	33,715,870
Supporting services:		
Management and general	1,352,094	1,269,817
Fundraising	8,020,688	5,552,641
Total supporting services	 9,372,782	6,822,458
•		
Total expenses	 48,354,247	40,538,328
Change in unrestricted net assets	 15,905,595	18,242,490
Changes in Temporarily Restricted Net Assets		
Contributions	5,211,239	1,151,463
Investment income	678,931	1,837,794
Change in value of split-interest agreements	(786,106)	(1,010,118)
Change in value of pledges and irrevocable trusts	92,805	212,068
Net assets released from restrictions	(4,692,142)	(3,415,105)
Change in temporarily restricted net assets	504,727	(1,223,898)
Changes in Permanently Restricted Net Assets – Contributions	2,289	6,826
Change in net assets	16,412,611	17,025,418
Net Assets		
Beginning	154,306,499	137,281,081
Ending	\$ 170,719,110	\$ 154,306,499
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See Notes To Financial Statements.

## Statements Of Cash Flows Years Ended December 31, 2007 And 2006

		2007		2006
Cash Flows From Operating Activities				
Change in net assets	\$	16,412,611	\$	17,025,418
Adjustments to reconcile change in net assets to net cash				
provided by operating activities:				
Net unrealized gain on investments		(5,019,429)		(7,253,776)
Net realized gains on sale of investments		(9,344,432)		(3,166,523)
Change in value of split-interest agreements		786,106		1,010,118
Discount on contributions receivable		(99,293)		(123,358)
Change in value of terminated split-value agreements		129,379		122,294
Depreciation and amortization		2,478,893		2,472,688
Loss on disposal of assets		22,908		68,875
Change in value of interest rate swap		177,071		15,821
Contributions for permanent restricted endowment		(2,289)		(6,826)
Contributed stock		65,962		(55,504)
Changes in assets and liabilities:				(55,551)
(Increase) decrease in:				
Contributions receivable		(1,723,894)		2,945,485
Prepayments and other assets		(203,959)		(188,499)
Increase (decrease) in:		(=00//0//		(100,100)
Accounts payable and accrued expenses		1,867,281		809,820
Split-interest obligations		(71,398)		(886,488)
Net cash provided by operating activities		5,475,517		12,789,545
Cash Flows From Investing Activities				
Purchases of long-term investments		(66,085,707)		(56,049,562)
Sales of long-term investments		63,243,640		45,439,600
Purchases of property, and equipment		(2,800,515)		(1,792,115)
Investment in life insurance		(2,000,313)		(74,010)
Net cash used in investing activities		(5,650,334)		(12,476,087)
9	-	(5,050,554)		(12,470,007)
Cash Flows From Financing Activities				
Contributions for permanent restricted endowment		2,289		6,826
Principal payments on notes payable		(246,150)		(268,474)
Net cash used in financing activities		(243,861)		(261,648)
Net (decrease) increase in cash and cash equivalents		(418,678)		51,810
Cash And Cash Equivalents				
Beginning		7,578,073		7,526,263
Ending	\$	7,159,395	\$	7,578,073
Litality	<u> </u>	7,107,070	Ψ	1,010,010
Supplemental Disclosures Of Cash Flow Information				
Interest paid	\$	188,203	\$	253,439
·	l <del></del>			
Contributed stock	<u>\$</u>	60,880	\$	126,842
Contributed equipment		-	\$	110,000

See Notes To Financial Statements.

#### **Notes To Financial Statements**

#### Note 1. Nature Of Activities And Significant Accounting Policies

Nature of activities: Founded in 1973, The Heritage Foundation (the Foundation) is an educational and research institute – a think tank – whose mission is to formulate and promote conservative public policies based on the principles of free enterprise, limited government, individual freedom, traditional American values, and a strong national defense. The organization pursues this mission by performing timely, accurate research on key policy issues, and effectively marketing these findings to its primary audiences who are members of Congress, key congressional staff, policy makers in the Executive Branch, the nation's news media, and the academic and policy communities. The Foundation's vision is to build an America where freedom, opportunity, prosperity and civil society flourish.

A summary of significant accounting policies of the Foundation follows:

<u>Basis of accounting</u>: The accompanying financial statements are presented in accordance with the accrual basis of accounting, whereby, revenue is recognized when earned and expenses are recognized when incurred.

<u>Basis of presentation</u>: The financial statement presentation follows the recommendation of the Financial Accounting Standards Board in its Statement of Financial Accounting Standards (SFAS) No. 117, *Financial Statements of Not-for-Profit Organizations*. Under SFAS No. 117, the Foundation is required to report information regarding its financial position and activities according to three classes of net assets: unrestricted net assets, temporarily restricted net assets, and permanently restricted net assets.

*Unrestricted net assets* – Net assets representing unrestricted resources available to support the Foundation's operations and temporarily restricted resources that become available for use by satisfying donor-imposed time or purpose restrictions. Unrestricted net assets include both board-designated and undesignated funds. The Board of Trustees has approved the establishment of an operating reserve (designated fund) to provide working capital and financing stability for the Foundation in the future. Funds have also been designated for certain programs and capital acquisitions. Total designated funds at December 31, 2007 and 2006, totaled \$116,502,056 and \$101,029,822, respectively. The undesignated fund constitutes the Foundation's operating fund and investment in property, plant, and equipment net of related liabilities.

Temporarily restricted net assets – Net assets subject to donor-imposed stipulations that will be met either by actions of the Foundation and/or the passage of time. When a donor-imposed restriction expires due to accomplishing the stipulated purpose or through passage of time, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of activities as net assets released from restrictions.

Permanently restricted net assets – Net assets subject to donor-imposed stipulations that they be maintained permanently by the Foundation, typically with earned investment income used for donor-designated purposes.

<u>Cash and cash equivalents</u>: The Foundation considers all highly liquid investments purchased with an initial maturity of three months or less to be cash equivalents.

<u>Financial risk</u>: The Foundation maintains its cash in bank deposit accounts, which, at times, may exceed federally insured limits. The Foundation has not experienced any losses in such accounts and believes it is not exposed to any significant financial risk on cash.

The Foundation invests in a professionally managed portfolio that contains corporate debt securities, U.S. government securities, and equity securities. Such investments are exposed to various risks such as market and credit. Due to the level of risk associated with such investments, and the level of uncertainty related to changes in the value of such investments, it is at least reasonably possible that changes in risks in the near term would materially affect investment balances and the amounts reported in the financial statements.

#### **Notes To Financial Statements**

#### Note 1. Nature Of Activities And Significant Accounting Policies (Continued)

<u>Contributed stock</u>: Contributed stock consists of donated securities that are recorded at fair value at the date of receipt and liquidated in a timely manner.

<u>Investments</u>: Investments in equity securities with readily determinable fair values and all investments in debt securities are reported at fair value with gains and losses included in the statement of activities. The Foundation accounts for investments in limited partnerships under the equity method of accounting and adjusts these investments based on the Foundation's share of the partnership's net income or loss.

<u>Property and equipment</u>: Property and equipment consists of land, buildings, building improvements, office furniture, and equipment, which are stated at cost as of the date of acquisition or, for gifts-in-kind, the fair market value at the date of donation. Depreciation is recognized on a straight-line basis over estimated useful lives of 30 years for building and building improvements, and three to ten years for office furniture and equipment. Depreciation for all assets was based on a half-year convention for the year of acquisition and the last year of useful life for assets purchase prior to 2006. Beginning in 2006, assets are depreciated on a full-year convention. The Foundation capitalizes all property and equipment with a cost of \$2,500 or more.

<u>Derivative financial instruments</u>: The Foundation has entered into an interest rate swap agreement to manage interest rate exposure on approximately \$4,000,000 of an original \$10,000,000 note payable to finance construction and building improvements and refinance existing debt (Note 5). The interest rate swap exchanged the floating rate (one-month LIBOR plus 60 basis points) for a fixed effective rate of 4.24% for seven years and matures in 2009.

Such interest rate swaps are accounted for under Statement of Financial Accounting Standards No. 133, *Accounting for Derivative Instruments and Hedging Activities*. As a not-for-profit organization, the Foundation is not allowed to use cash flow hedging. Therefore, the interest rate swap is recorded in the balance sheet at fair value. The change in the fair value is reflected in other income in the statement of activities. The fair value of the interest rate swap at December 31, 2007 and 2006, was \$(108,831) and \$68,240, respectively, and is included in debt and investments, respectively, in the accompanying balance sheet.

<u>Valuation of long-lived assets</u>: The Foundation accounts for the valuation of long-lived assets under Statement of Financial Accounting Standards (SFAS) No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*. SFAS No. 144 requires that long-lived assets and certain identifiable intangible assets be reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of the long-lived asset is measured by a comparison of the carrying amount of the asset to future undiscounted net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the estimated fair value of the assets. Assets to be disposed of are reportable at the lower of the carrying amount or fair value, less costs to sell. The Foundation had no impairment of long-lived assets during 2007 or 2006.

<u>Contributions receivable and revenue</u>: The Foundation recognized revenue for contributions received, including those contributions received in the form of unconditional promises to give or pledges. These promises to give are classified as contributions receivable on the statement of financial position.

Contributions receivable that are expected to be collected within one year are recorded at net realizable value. Contributions receivable that are expected to be collected in future years are recorded at the present value of estimated future cash flows. The discounts on those amounts are computed using an appropriate risk free rate of return at the date of the promise to give. Amortization of the discounts is included in contribution revenue. An allowance for uncollectible pledges is recorded based on estimated amounts not expected to be collected. At December 31, 2007 and 2006, there was no reserve for uncollectible amounts recorded.

#### Notes To Financial Statements

#### Note 1. Nature Of Activities And Significant Accounting Policies (Continued)

<u>Cash surrender value of insurance</u>: During 1999, the Foundation entered into a split-dollar insurance agreement with the Foundation's president. The Foundation makes premium payments to fund the life insurance policy. The president assigned the cash surrender value and proceeds from the death benefit of the policy to the Foundation to the extent of the Foundation's cumulative premium payments.

<u>Split-interest agreements</u>: Contributions received in the form of irrevocable split-interest agreements (charitable gift annuities and charitable trusts) are recorded as contribution revenue at the present value of amounts expected to transfer to the Foundation at the estimated date of death of the current beneficiaries, which is estimated using Internal Revenue Service mortality tables and discount rates ranging from 3% to 6%. Any subsequent changes in the value of the split-interest agreements are recorded as change in value of split-interest agreements in the statement of activities. Assets are recorded at the present value of amounts to be received and are discounted using an appropriate risk-free rate of return.

During the life of the beneficiary or for the specified period of time, the Foundation pays the donor or other specified parties, amounts as determined in the donor agreement. Upon fulfillment of the beneficiary payments or termination of the trust, the remaining assets are available to the Foundation for unrestricted purposes.

Income tax status: The Foundation is a not-for-profit organization exempt from federal income taxes under Section 501(a), as an entity described in Section 501(c)(3) of the Internal Revenue Code of 1986, as amended. The Foundation has been classified by the Internal Revenue Service as a public charity and is not a private foundation. Contributions to the Foundation are deductible for federal income, estate, and gift tax purposes. Income, which is not related to exempt purposes, is subject to tax.

<u>Allocation of joint costs</u>: The Foundation incurred joint costs of \$8,983,109 and \$7,102,416 for the years ended December 31, 2007 and 2006, respectively. The Foundation allocated these joint costs among program and fundraising expenses as follows:

	2007	2006
Educational programs for public information expense	\$ 5,165,004	\$ 4,771,272
Fundraising expense	3,818,105	2,331,144
	\$ 8,983,109	\$ 7,102,416

<u>Donated materials</u>: The Foundation receives donations of property and equipment. The property is recorded at fair value at the date of donation. Total amount of donated property was \$110,000 during the year ended December 31, 2006. The donated property was sold during 2007 for \$160,000, producing a realized gain of \$50,000.

<u>Advertising costs</u>: Advertising costs are expensed when incurred. Total advertising expense was \$253,244 and \$27,132 for the years ended December 31, 2007 and 2006, respectively.

<u>Estimates</u>: The preparation of financial statements 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 revenue and expenses during the reporting period. Actual results could differ from those estimates.

<u>Fair value of financial instruments</u>: Fair values of cash and cash equivalents, prepayments, and accounts payable approximate cost due to the short period of time to maturity. Fair values of investments are based on market prices. The carrying amount reported for notes payable approximates fair value as the interest rate on the underlying instruments fluctuate with market rates.

#### **Notes To Financial Statements**

#### Note 1. Nature Of Activities And Significant Accounting Policies (Continued)

Recently issued accounting pronouncements: In September 2006, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards No. 157, *Fair Value Measurements* ("FAS 157"). This standard defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurement. FAS 157 also emphasizes that fair value is a market based measurement, not an entity-specific measurement, and sets out a fair value hierarchy with the highest priority being quoted prices in active markets. Under FAS 157, fair value measurements are disclosed by level within that hierarchy. FAS 157 is effective for fiscal years beginning after November 15, 2007, except for non-financial assets and non-financial liabilities that are recognized or disclosed at fair value in the financial statements on a nonrecurring basis for which delayed application is permitted until fiscal years beginning after November 15, 2008. The adoption of FAS 157 is not expected to have a material impact on the Foundation's financial position, results of operations or cash flows.

In July 2006, the Financial Accounting Standards Board ("FASB") issued Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* ("FIN 48"). FIN 48 prescribes a minimum threshold for financial statement recognition of the benefit of a tax position taken or expected to be taken by a filer in the filer's tax return. FIN 48 will become effective for the fiscal years beginning after December 15, 2007. The Foundation has not yet determined the impact of the adoption of FIN 48 on its financial statements.

Note 2. Promises To Give

The following are unconditional promises to give at December 31, 2007 and 2006:

	2007	2006
Due in less than one year	\$ 6,360,741	\$ 4,056,474
Due in one to five years	3,938,535	4,154,145
Due in greater than five years	296,111	660,875
Total to be received	10,595,387	8,871,494
Less amounts representing discounting (2%-4.43%)	(576,001)	(675,294)
	\$ 10,019,386	\$ 8,196,200

# Note 3. Investments Investments at December 31, 2007 and 2006, consist of the following:

	2007	2006
Equity funds	\$ 83,939,074	\$ 60,082,571
Trusts and annuities	17,880,779	16,456,009
Investments in limited partnerships	15,479,495	18,568,068
Fixed income	14,907,542	19,615,668
Money market funds	4,292,568	4,639,454
	\$ 136,499,458	\$ 119,361,770

## **Notes To Financial Statements**

#### Note 3. Investments (Continued)

The following summarizes investment income for the years ended December 31, 2007 and 2006:

	2007	2006
Net realized gain	\$ 9,344,432	\$ 3,166,523
Net unrealized gain	5,019,429	7,253,776
Interest and dividends	2,876,782	2,825,767
	\$ 17,240,643	\$ 13,246,066

### Note 4. Property And Equipment

Property and equipment and accumulated depreciation consist of the following at December 31, 2007 and 2006:

	2007	2006
Land, building, and improvements	\$ 46,398,104	\$ 44,588,719
Office furniture and equipment	7,171,372	6,262,405
	53,569,476	50,851,124
Less accumulated depreciation	(15,349,001)	(12,929,364)
Property and equipment, net	\$ 38,220,475	\$ 37,921,760

Depreciation expense for the years ended December 31, 2007 and 2006, totaled \$2,478,893 and \$2,472,688, respectively.

## Note 5. Notes Payable

Notes payable as of December 31, 2007 and 2006, are as follows:

	2007	2006
Note payable (construction and building improvements) –		
fixed rate (4.24% at December 31,2007)	\$ 4,149,999	\$ 4,349,999
Note payable (office equipment) – interest free	49,969	96,119
Interest rate swap liability (Note 1)	108,832	-
Mortgage note payable	10,000	10,000
	4,318,800	4,456,118
Less current portion	(242,600)	(242,600)
Notes payable, net	\$ 4,076,200	\$ 4,213,518

#### **Notes To Financial Statements**

#### Note 5. Notes Payable (Continued)

Note Payable (Construction and Building Improvements) - The Foundation has a \$4.15 million note which was used to finance construction and building improvements and refinance existing debt. The outstanding balance of the note is subject to an interest-rate swap agreement, with a fixed interest rate at an effective rate of 4.5% over seven years (Note 1). Principal for the note is payable monthly based on a 25-year amortization with the outstanding principal balance due in full in 2009. The note is secured by certain assets held in the Foundation's investment portfolio. The note requires that the Foundation maintain a debt service coverage ratio (as defined by the lending institution) of at least 1.35 to 1 and a ratio of unrestricted liquidity to funded debt of at least 5 to 1.

*Line of Credit* - The Foundation has a \$2 million line of credit which was used to finance building improvements and fund short-term working capital needs. The line bears interest at LIBOR plus 60 basis points and is unsecured. The line of credit had no outstanding balance as of December 31, 2007 and 2006.

*Note Payable (Office Equipment)* - The Foundation has a three-year, interest-free note used to finance the purchase of office equipment. Principal payments are made monthly. The note was used to pay off existing capital lease obligations, allowing the Foundation to enter into new operating lease agreements. The note is secured by the related office equipment.

Mortgage Note Payable - During 2005, the Foundation obtained an interest-only term loan in the amount of \$10,000 to finance the cost of preliminary design and planning for use of property at 426 3rd Street, NE. The loan bears interest at LIBOR plus 60 basis points (5.825% at December 31, 2007) with principal due at maturity in 2010 and is secured with a deed of trust placed on the property.

Minimum future payments under these notes payable as of December 31, 2007, are as follows:

Years	Ending	December	31

2008	\$ 242,600
2009	4,066,200
2010	10,000
	\$ 4,318,800

#### Note 6. Employee Benefits

Discretionary Contribution Plan - The Foundation provides a non-contributory discretionary contribution plan to all employees with at least one year of service who have attained the age of 21 and who worked at least 1,000 hours during the year. Contributions to the plan by the Foundation were \$907,407 and \$774,183 for the years ended December 31, 2007 and 2006, respectively. Employees vest at 25% per year of service beginning after two years and are fully vested after five years.

Deferred Compensation Plan - The Foundation provides employees the opportunity to defer current compensation under both 403(b) and a 457(b) plan. Although the Foundation makes no contributions to these plans, the 457(b) plan assets and related liability to employees of \$942,159 and \$786,727 at December 31, 2007 and 2006, respectively, are included on the Foundation's balance sheet within deferred compensation obligations under both 403(b) and 457(b) plans.

#### **Notes To Financial Statements**

#### Note 6. Employee Benefits (Continued)

In addition, the Foundation had an option-based compensation plan under which certain employees were granted options to buy shares of designated mutual funds at a specified exercise price. No additional grants will be awarded under this plan, and no grants were made during the 2007 and 2006. The market value of these assets was \$0 and \$145,675 as of December 31, 2007 and 2006, respectively. The Foundation dissolved this plan during 2007.

The Foundation also maintained a deferred compensation plan for a key employee under which the last annual contribution of \$35,000 was made during the year ended December 31, 2006.

The total market value of all deferred compensation investments and the related deferred compensation obligations to employees were \$3,519,555 and \$3,163,857 at December 31, 2007 and 2006, respectively.

#### Note 7. Restricted Net Assets

Temporarily restricted net assets at December 31, 2007 and 2006, consist of the following:

	2007	2006
Contributions restricted by passage of time	\$ 13,419,755	\$ 12,915,026

Permanently restricted net assets represent funds that are subject to donor-imposed restrictions requiring the corpus to be held in perpetuity. At December 31, 2007 and 2006, permanently restricted net assets consist of the following:

	2007	2006
William E. Simon Fellow – Study of Religion and Free Society	\$ 1,000,000	\$ 1,000,000
Westerman Intern Program	100,000	100,000
John R. & Margrite Davis Intern Endowment	100,000	97,711
	\$ 1,200,000	\$ 1,197,711

#### Note 8. Operating Leases

The Foundation leases equipment under noncancelable operating lease agreements. Future minimum lease payments under noncancelable operating leases with initial or remaining terms in excess of one year at December 31, 2007, are as follows:

#### Years Ending December 31,

2008	\$ 107,736
2009	8,978
	\$ 116,714

Expense incurred under these leases for the years ended December 31, 2007 and 2006, totaled \$142,218 and \$232,153, respectively.

#### **Notes To Financial Statements**

#### Note 9. Related Party Transactions

During 2005, the Foundation renewed a lease to provide space to a company affiliated with a member of the Board of Trustees. The lease runs from September 1, 2005, through August 31, 2008. Annual lease payments total \$48,964. Future minimum lease payments relating to this lease amount to approximately \$49,000 for the year ending December 31, 2007, and approximately \$33,000 for the year ending December 31, 2008. Rental income recognized during each year ended December 31, 2007 and 2006, was \$48,964.

### Note 10. Subsequent Event

Subsequent to year-end the Foundation purchased property at 227 Pennsylvania Ave., SE, Washington, D.C. for \$2.2 million. Upon completion of necessary renovations, the property will be used for meetings, events and office space.

# McGladrey & Pullen

**Certified Public Accountants** 

Independent Auditor's Report On The Supplementary Information

To the Board of Trustees The Heritage Foundation Washington, D.C.

Our audit was made for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplemental schedule of functional expenses for the year ended December 31, 2007, is presented for the purposes of additional analysis and is not a required part of the basic financial statements. This schedule is the responsibility of the Foundation's management. The schedule has been subjected to the auditing procedures applied in our audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects, when considered in relation to the basic financial statements taken as a whole. The supplementary information for the year ended December 31, 2006, has been derived from the Foundation's 2006 financial statements and, in our report dated March 12, 2007, we expressed an unqualified opinion on such information in relation to the basic financial statements taken as a whole.

McGladrey of Pullen, LLP

Vienna, Virginia May 2, 2008

The Heritage Foundation

## Schedule Of Functional Expenses Year Ended December 31, 2007

	Program Services						Supporting Services							
				Media and										
				Government		Educational			Management					Total
		Research		Relations		Programs	Total		and General		Fund-raising		Total	Expenses
Supplies	\$	283,117	\$	87,637	\$	57,693	\$ 428,447	\$	13,788	\$	29,497	\$	43,285	\$ 471,732
Telephone		199,455		90,204		30,301	319,960		10,905		25,106		36,011	355,971
Leased equipment		157,132		63,965		26,264	247,361		10,447		-		10,447	257,808
Staff training		208,559		58,109		44,264	310,932		10,104		6,934		17,038	327,970
Postage		106,190		112,295		2,518,462	2,736,947		4,095		1,213,406		1,217,501	3,954,448
Professional fees		180,970		67,926		49,222	298,118		59,202		817		60,019	358,137
Rent		33,352		13,577		8,724	55,653		2,235		3,655		5,890	61,543
Occupancy charges		848,865		345,314		141,785	1,335,964		56,396		50		56,446	1,392,410
Insurance		118,687		48,314		19,838	186,839		7,891		-		7,891	194,730
Data processing		12,655		5,108		2,097	19,860		16,044		127,066		143,110	162,970
Photography, copying, and recording		28,441		37,616		7,385	73,442		672		22,712		23,384	96,826
Books		61,186		36,747		37,675	135,608		6,574		114,466		121,040	256,648
Subscriptions		99,592		86,698		6,672	192,962		4,413		5,122		9,535	202,497
Taxes and licenses		151,695		26,701		18,884	197,280		52,670		7,643		60,313	257,593
Maintenance		91,737		42,990		15,581	150,308		6,061		-		6,061	156,369
Travel and subsistence		57,055		23,149		32,342	112,546		1,153		265,393		266,546	379,092
Miscellaneous		22,446		7,432		78,831	108,709		1,587		47,300		48,887	157,596
Printing and mailing		25,264		60,974		3,581,822	3,668,060		863		1,565,454		1,566,317	5,234,377
Conferences		2,159,351		920,593		87,222	3,167,166		50,778		854,102		904,880	4,072,046
Advertising		45,018		20,462		11,398	76,878		1,813		174,553		176,366	253,244
Other programs and grants		37,938		13,698		4,001	55,637		2,138		386		2,524	58,161
Salaries		10,214,844		4,281,146		1,459,677	15,955,667		739,824		1,828,095		2,567,919	18,523,586
Fringe benefits		2,163,398		844,477		399,000	3,406,875		154,456		396,784		551,240	3,958,115
Scholars and consultants		1,163,276		261,587		1,353,705	2,778,568		23,028		1,273,711		1,296,739	4,075,307
Honoraria and writer's fees		116,269		3,556		26,337	146,162		1,752		825		2,577	148,739
Temporary assistance and agency fees		24,967		624		22,275	47,866		126		11,041		11,167	59,033
Agency fees		7,314		2,977		1,223	11,514		486		-		486	12,000
On-line service fees		92,987		53,255		51,207	197,449		4,184		46,570		50,754	248,203
Interest expense		114,517		46,594		19,132	180,243		7,961		-		7,961	188,204
Depreciation and amortization		1,510,867		615,038		252,539	2,378,444		100,448		-		100,448	2,478,892
Total expenses	\$	20,337,144	\$	8,278,763	\$	10,365,558	\$ 38,981,465	\$	1,352,094	\$	8,020,688	\$	9,372,782	\$ 48,354,247

The Heritage Foundation

## Schedule Of Functional Expenses Year Ended December 31, 2006

		Progran	n Services			Supporting Service	S	
		Media and						
		Government	Educational		Management			Total
	Research	Relations	Programs	Total	and General	Fund-raising	Total	Expenses
Supplies	238,362	57,715	44,559	340,636	12,035	38,385	50,420	391,056
Telephone	177,157	80,629	28,295	286,081	11,035	12,090	23,125	309,206
Leased equipment	147,781	51,183	23,432	222,396	9,756	-	9,756	232,152
Staff training	142,501	48,875	38,060	229,436	10,545	14,736	25,281	254,717
Postage	130,538	84,352	1,595,384	1,810,274	5,073	1,006,767	1,011,840	2,822,114
Professional fees	163,305	48,119	34,675	246,099	107,276	1,388	108,664	354,763
Rent	18,415	6,088	9,057	33,560	1,159	2,407	3,566	37,126
Occupancy charges	830,386	287,503	131,613	1,249,502	54,795	11	54,806	1,304,308
Insurance	156,054	54,030	26,271	236,355	10,299	40	10,339	246,694
Data processing	14,912	5,165	2,364	22,441	15,630	37,101	52,731	75,172
Photography, copying, and recording	30,468	48,511	6,084	85,063	562	28,574	29,136	114,199
Books	30,150	33,782	7,248	71,180	5,335	56,771	62,106	133,286
Subscriptions	213,810	92,598	8,496	314,904	8,977	8,360	17,337	332,241
Taxes and licenses	181,117	29,014	21,005	231,136	5,679	6,773	12,452	243,588
Maintenance	95,565	33,210	15,112	143,887	6,305	3	6,308	150,195
Travel and subsistence	58,580	21,340	16,880	96,800	1,592	133,315	134,907	231,707
Miscellaneous	18,490	7,760	47,465	73,715	1,878	45,474	47,352	121,067
Printing and mailing	46,766	55,831	2,659,851	2,762,448	4,472	1,341,947	1,346,419	4,108,867
Conferences	2,222,590	678,621	64,428	2,965,639	42,954	131,167	174,121	3,139,760
Advertising	7,385	12,290	4,307	23,982	1,222	1,928	3,150	27,132
Other programs and grants	56,419	15,457	2,690	74,566	1,145	110	1,255	75,821
Salaries	9,412,982	3,248,629	1,311,520	13,973,131	663,640	1,457,601	2,121,241	16,094,372
Fringe benefits	1,972,478	734,051	415,839	3,122,368	145,743	336,520	482,263	3,604,631
Scholars and consultants	904,044	278,310	971,665	2,154,019	21,548	869,054	890,602	3,044,621
Honoraria and writer's fees	89,730	5,550	25,000	120,280	-	-	-	120,280
Temporary assistance and agency fees	37,681	11,808	14,048	63,537	1,839	21,210	23,049	86,586
On-line service fees	100,920	30,117	20,458	151,495	4,137	909	5,046	156,541
Interest expense	160,922	55,734	25,515	242,171	11,267	-	11,267	253,438
Depreciation and amortization	1,574,036	545,158	249,575	2,368,769	103,919	-	103,919	2,472,688
Total expenses	\$ 19,233,544	\$ 6,661,430	\$ 7,820,896	\$ 33,715,870	\$ 1,269,817	\$ 5,552,641	\$ 6,822,458	\$ 40,538,328