



SOUTHERN EDUCATION FOUNDATION, INC.

Financial Statements and Schedule

December 31, 2004

(With Independent Auditors' Report Thereon)



KPMG LLP
Suite 2000
303 Peachtree Street, NE
Atlanta, GA 30308

Independent Auditors' Report

The Board of Trustees
Southern Education Foundation, Inc.:

We have audited the accompanying statement of financial position of Southern Education Foundation, Inc. (the Foundation) as of December 31, 2004, and the related statements of activities and cash flows for the nine-month period ended December 31, 2004. 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 audit.

We conducted our audit 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 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 Southern Education Foundation, Inc. as of December 31, 2004, and its changes in net assets and its cash flows for the nine-month period ended December 31, 2004 in conformity with accounting principles generally accepted in the United States of America.

As discussed in note 1(c) to the financial statements, the Foundation changed its fiscal year-end from March 31 to December 31.

Our audit was made for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplementary information included in Schedule 1 is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

KPMG LLP

April 8, 2005

SOUTHERN EDUCATION FOUNDATION, INC.

Statement of Financial Position

December 31, 2004

Assets

Cash and cash equivalents (note 2)	\$ 3,789,657
Investment securities (note 5)	10,104,992
Grants receivable (note 4)	530,000
Other assets (note 3)	6,385
Building, furniture, and fixtures, net (note 6)	<u>747,751</u>
Total assets	<u><u>\$ 15,178,785</u></u>

Liabilities and Net Assets

Liabilities:	
Accounts payable	\$ 126,045
Other liabilities	<u>113,172</u>
Total liabilities	<u>239,217</u>
Net assets:	
Unrestricted:	
Board-designated (note 1(b))	8,000,000
Undesignated	<u>3,587,848</u>
Total unrestricted	11,587,848
Temporarily restricted (note 9)	3,339,320
Permanently restricted (note 10)	<u>12,400</u>
Total net assets	14,939,568
Commitments (notes 7 and 8)	
Total liabilities and net assets	<u><u>\$ 15,178,785</u></u>

See accompanying notes to financial statements.

SOUTHERN EDUCATION FOUNDATION, INC.

Statement of Activities

Nine-month period ended December 31, 2004

Changes in unrestricted net assets:

Revenue, gains, and other support:

Contributions	\$ 31,130
Other revenue	635
Investment income	544,432
Net realized and unrealized gains	330,041
Net assets released from restrictions (note 9)	4,910,142

Total unrestricted revenue, gains, and other support	<u>5,816,380</u>
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Expenses:

Program	4,325,470
Management and general	541,435
Fund raising	7,563

Total expenses	<u>4,874,468</u>
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Change in unrestricted net assets	<u>941,912</u>
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Changes in temporarily restricted net assets:

Grant revenue	1,599,150
Investment income	79,350
Net assets released from restrictions (note 9)	(4,910,142)

Change in temporarily restricted net assets	<u>(3,231,642)</u>
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Changes in permanently restricted net assets:

Private gifts and grants	<u>350</u>
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Change in net assets	(2,289,380)
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Net assets at beginning of period	<u>17,228,948</u>
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Net assets at end of period	<u><u>\$ 14,939,568</u></u>
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See accompanying notes to financial statements.

SOUTHERN EDUCATION FOUNDATION, INC.

Statement of Cash Flows

Nine-month period ended December 31, 2004

Cash flows from operating activities:	
Change in net assets	\$ (2,289,380)
Adjustments to reconcile change in net assets to net cash provided by operating activities:	
Depreciation and amortization	87,809
Net realized and unrealized gains	(330,041)
Decrease in grants receivable	3,074,500
Decrease in other assets	64,653
Increase in accounts payable	10,568
Decrease in grants payable	(4,398)
Increase in other liabilities	37,260
Net cash provided by operating activities	<u>650,971</u>
Cash flows from investing activities:	
Purchase of furniture and fixtures	(237,454)
Proceeds from the sale of investment securities	16,097,141
Purchase of investment securities	<u>(16,347,494)</u>
Net cash used in investing activities	<u>(487,807)</u>
Increase in cash and cash equivalents	163,164
Cash and cash equivalents:	
Beginning of period	<u>3,626,493</u>
End of period	<u><u>\$ 3,789,657</u></u>

See accompanying notes to financial statements.

SOUTHERN EDUCATION FOUNDATION, INC.

Notes to Financial Statements

December 31, 2004

(1) Summary of Significant Accounting Policies

(a) Description of Business

Southern Education Foundation, Inc. (the Foundation) is a public charity which was established to promote equity and quality in education primarily for disadvantaged citizens in the South.

(b) Basis of Accounting and Presentation

The accompanying financial statements have been prepared on the accrual basis of accounting and reflect all significant receivables and payables.

The Foundation's net assets and revenue, expenses, gains, and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, the net assets of the Foundation and changes therein are classified as unrestricted and temporarily restricted.

Unrestricted net assets include amounts that are not subject to donor-imposed stipulations which are used to account for resources which are available to carry out the purposes of the Foundation in accordance with the limitations of its charter and bylaws. The principal sources of unrestricted funds are grants, contributions, bequests, and investment income. The Foundation's governing board has designated \$8,000,000 as the historic dollar value of unrestricted net assets for long-term investment as of December 31, 2004.

Temporarily restricted net assets are those resources currently available for use, but expendable only for purposes specified by the donor or grantor. Such resources originate from grants, contributions, and investment income restricted for specific purposes. When a donor or grantor restriction expires, 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 are those resources subject to donor-imposed stipulations that they be maintained permanently by the Foundation. Generally, the donors of these assets permit the Foundation to use all or part of the income earned on related investments for general or specified purposes.

(c) Fiscal Year-End

The Foundation changed its fiscal year-end from March 31 to December 31. The Foundation's financial statements are presented for a nine-month period ended December 31, 2004. The Foundation changed its fiscal year-end to reflect financial information that is consistent with the programs and operations of the Foundation.

(d) Investment Securities

Investment securities include both debt and equity securities. The fair value of investments in marketable equity and debt securities is based on quoted market prices. Realized gains and losses on sales of investments are computed using the specific identification method. Unrealized gains and losses are calculated based on the securities' fair values as determined by an active market as of December 31, 2004.

SOUTHERN EDUCATION FOUNDATION, INC.

Notes to Financial Statements

December 31, 2004

(e) Cash Equivalents

Cash equivalents consist primarily of money market accounts and other short-term cash investments. For purposes of the statement of cash flows, the Foundation considers all short-term, interest-bearing deposits with maturities of three months or less to be cash equivalents.

(f) Building, Furniture, and Fixtures

The building consists of a condominium interest in an office building and is being depreciated on a straight-line basis over an estimated useful life of 30 years. Furniture and fixtures are being depreciated on a straight-line basis over estimated lives of five to ten years.

(g) Functional Allocation of Expenses

The costs of providing the various programs and other activities have been summarized on a functional basis in the statement of activities. Accordingly, certain costs have been allocated among the programs and supporting services benefited on the basis of square footage, payroll, or other relevant bases.

(h) Federal Taxes

The Foundation is recognized as an organization exempt from Federal income tax under Section 501(a) of the Internal Revenue Code as an organization described in Section 501(c)(3).

(i) Use of Estimates

Management of the Foundation has made certain estimates and assumptions relating to the reporting of assets and liabilities and the disclosure of contingent assets and liabilities to prepare the financial statements in conformity with accounting principles generally accepted in the United States of America. Actual results could differ from those estimates.

(2) Cash and Cash Equivalents

Cash and cash equivalents at December 31, 2004 consist of cash, short-term investments, and cash management trust.

Cash and cash equivalents totaled \$3,789,657 for the nine-month period ended December 31, 2004.

(3) Other Assets

Included in other assets is a note receivable from another not-for-profit organization.

In December 1998, the Foundation paid \$50,000 to a financial institution related to the purchase of a note receivable. The note and any rights to it were assigned to the Foundation. The principal balance of the note at the time of purchase was approximately \$150,000 with a fixed interest rate of 10% per annum and the note is collateralized by the office space of the original debtor. As of December 31, 2004, the Foundation reported the note receivable, net of allowance for doubtful accounts, totaling \$50,000 to fully reserve the outstanding balance.

SOUTHERN EDUCATION FOUNDATION, INC.

Notes to Financial Statements

December 31, 2004

(4) Grants Receivable

Grants receivable consists of the following at December 31, 2004:

Ford Foundation	\$ 210,000
Kresge Foundation	160,000
Winthrop Rockefeller Foundation	160,000
Total	<u>\$ 530,000</u>

(5) Investment Securities

Investment securities at December 31, 2004 consist of the following:

	<u>Fair value</u>	<u>Cost</u>
Investment securities:		
U.S. Government obligations	\$ 1,394,483	1,353,620
Corporate bonds	1,445,007	1,402,664
Federal agency bonds	1,010,495	980,884
Equity securities	6,255,007	6,071,671
Total investment securities	<u>\$ 10,104,992</u>	<u>9,808,839</u>

(6) Building, Furniture, and Fixtures

Building, furniture, and fixtures consist of the following at December 31, 2004:

Building	\$ 867,058
Furniture and fixtures	519,875
Building improvements	282,225
	<u>1,669,158</u>
Less accumulated depreciation	921,407
	<u>\$ 747,751</u>

Depreciation expense totaled \$87,809 for the nine-month period ended December 31, 2004.

(7) Pension Plan

The Foundation has a defined contribution (money purchase) retirement plan covering substantially all employees. The plan provides for the Foundation to contribute 15% of the participant's regular base salary which is used to purchase annuity contracts for participants. The annuity contracts are the property of each participant and retirement benefits are provided solely from such contracts. For the nine-month period

SOUTHERN EDUCATION FOUNDATION, INC.

Notes to Financial Statements

December 31, 2004

ended December 31, 2004, contributions to the plan totaled \$ 101,138. The pension contributions have been allocated to the various expense classifications on the same basis as salary costs.

(8) Operating Leases

The Foundation leases office equipment under various operating leases. At December 31, 2004, future minimum lease payments under noncancelable operating leases are as follows:

2005	\$	12,386
2006		12,386
2007		12,386
2008		12,386
2009		5,295
	\$	<u>54,839</u>

Total lease expense for the nine-month period ended December 31, 2004 was \$7,493.

(9) Temporarily Restricted Net Assets

At December 31, 2004, temporarily restricted net assets are available for the following purposes:

Programs	\$	<u>3,339,320</u>
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Temporarily restricted net assets were released from restrictions by incurring expenses satisfying the restricted purposes specified by donors or grantors, as follows:

Programs	\$	4,266,955
Management and general		260,096
Administrative cost recovery		<u>383,091</u>
Total restrictions released	\$	<u>4,910,142</u>

(10) Permanently Restricted Net Assets

At December 31, 2004, permanently restricted net assets consist of the following:

McMillan Fund	\$	<u>12,400</u>
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SOUTHERN EDUCATION FOUNDATION, INC.

Supplementary Schedule of Functional Expenses

December 31, 2004

	Program	Management and general	Fundraising	Total December 31, 2004
Personnel costs	\$ 1,407,717	193,875	7,400	1,608,992
Travel costs	573,154	32,060	102	605,316
Communication costs	114,165	14,465	61	128,691
Depreciation and amortization	—	87,809	—	87,809
Office and building costs	43,982	44,285	—	88,267
Institutional management	28,245	49,881	—	78,126
Research and development	9,532	—	—	9,532
Grants committed	2,027,289	—	—	2,027,289
Contributions paid by SEF	121,386	50,250	—	171,636
Investment management fees	—	68,810	—	68,810
Total	<u>\$ 4,325,470</u>	<u>541,435</u>	<u>7,563</u>	<u>4,874,468</u>

See accompanying independent auditors' report.