

FINANCIAL STATEMENTS

John S. and James L. Knight Foundation  
Years Ended Dec. 31, 2006 and 2005  
With Report of Independent Certified Public Accountants

John S. and James L. Knight Foundation

Financial Statements

Years Ended Dec. 31, 2006 and 2005

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## Report of Independent Certified Public Accountants

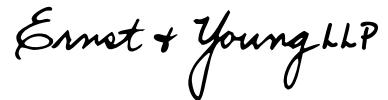
The Trustees  
John S. and James L. Knight Foundation

We have audited the accompanying statements of financial position of the John S. and James L. Knight Foundation (the foundation) as of Dec. 31, 2006 and 2005, 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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the 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 financial position of the foundation at Dec. 31, 2006 and 2005, 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.

As discussed in Note 9, the foundation restated the accompanying financial statements as of and for the year ended Dec. 31, 2005.



Feb. 28, 2007

John S. and James L. Knight Foundation

Statements of Financial Position

	Dec. 31	
	2006	2005
		<i>(As Restated – Note 9)</i>
<b>Assets</b>		
Investments:		
Cash and cash equivalents	\$ 18,458,633	\$ 62,995,431
Interest, dividends and other investment receivables	79,178,622	23,771,432
(Payable) receivable related to derivative instrument	(1,807,168)	4,165,311
U.S. government and agency obligations	254,810,619	124,571,283
International bonds and other obligations	84,030,856	83,965,404
Corporate bonds and other obligations	67,936,849	184,282,261
Common stock of Knight Ridder	–	31,650,000
Other equity securities	757,886,057	656,166,445
Hedge fund investments	474,635,091	482,656,572
Alternative equity investments	421,566,126	318,937,744
Real estate investments	105,101,412	97,191,678
Total investments	<u>2,261,797,097</u>	2,070,353,561
Beneficial interest in remainder trusts	80,827,304	71,369,705
Other assets	–	1,153,730
Total assets	<u>\$ 2,342,624,401</u>	<u>\$ 2,142,876,996</u>
<b>Liabilities and net assets</b>		
Liabilities:		
Grants payable	\$ 76,363,523	\$ 105,782,618
Other liabilities	1,606,264	664,265
Pension and other postretirement benefits	843,896	724,765
Deferred taxes payable	2,399,297	1,542,523
Total liabilities	<u>81,212,980</u>	108,714,171
Net assets:		
Temporarily restricted	80,827,304	71,369,705
Unrestricted	2,180,584,117	1,962,793,120
Total net assets	<u>2,261,411,421</u>	2,034,162,825
Total liabilities and net assets	<u>\$ 2,342,624,401</u>	<u>\$ 2,142,876,996</u>

See accompanying notes.

John S. and James L. Knight Foundation

Statements of Activities

	<b>Year Ended Dec. 31</b>	
	<b>2006</b>	<b>2005</b>
		<i>(As Restated – Note 9)</i>
Changes in unrestricted net assets:		
Investment activity:		
Interest	\$ 20,034,804	\$ 21,950,145
Dividends	16,894,591	13,629,283
Net realized gain on sale of investments	191,819,821	205,659,188
Net change in fair value of investments	86,561,557	1,834,077
Less: investment expenses	<u>(8,272,948)</u>	<u>(7,319,212)</u>
Total investment activity	307,037,825	235,753,481
Contributions received	<u>540,292</u>	1,364,567
Total investment activity and other support	307,578,117	237,118,048
Grants approved and expenses:		
Community Partners grants	44,542,100	34,652,325
Journalism Initiative grants	21,751,750	25,922,667
National Venture Fund grants	5,965,000	13,261,855
Other grants	1,220,444	4,387,300
Grant forfeitures and other	(1,857,367)	(4,226,985)
Direct charitable activities	3,101,317	2,885,404
General and administrative expenses	11,015,462	10,596,494
Federal excise and other taxes, net	3,347,533	4,065,260
Total grants and expenses	<u>89,086,239</u>	91,544,320
Increase in unrestricted net assets from operating activities	218,491,878	145,573,728
Effect of adoption of recognition provision of SFAS No. 158	<u>700,881</u>	–
Increase in unrestricted net assets	217,790,997	145,573,728
Changes in temporarily restricted net assets:		
Change in value of beneficial interest in remainder trusts	<u>9,457,599</u>	(9,822,924)
Total increase in net assets	227,248,596	135,750,804
Net assets at beginning of year, as restated – Note 9	<u>2,034,162,825</u>	1,898,412,021
Net assets at end of year	<u><u>\$ 2,261,411,421</u></u>	<u><u>\$ 2,034,162,825</u></u>

See accompanying notes.

John S. and James L. Knight Foundation

Statements of Cash Flows

	<b>Year Ended Dec. 31</b>	
	<b>2006</b>	<b>2005</b>
		<i>(As Restated – Note 9)</i>
<b>Operating activities</b>		
Change in net assets	\$ 227,248,596	\$ 135,750,804
Adjustments to reconcile change in net assets to net cash used in operating activities:		
Net realized gain on sale of investments	(191,819,821)	(205,659,188)
Net change in fair value of investments	(86,561,557)	(1,834,077)
Change in value of beneficial interest in remainder trusts	(9,457,599)	9,822,924
Changes in operating assets and liabilities:		
Interest, dividends and other investment receivables	(49,434,711)	(19,935,154)
Other assets	1,153,730	(443,308)
Grants payable	(29,419,095)	(14,964,139)
Deferred taxes	856,774	1,542,523
Pension and postretirement liability	941,999	(120,938)
Other liabilities	119,132	135,213
Net cash used in operating activities	<u>(136,372,552)</u>	<u>(95,705,340)</u>
<b>Investing activities</b>		
Proceeds from sale of investments	620,840,164	763,833,772
Purchases of investments	(529,004,410)	(653,602,940)
Net cash provided by investing activities	<u>91,835,754</u>	<u>110,230,832</u>
Net change in cash and cash equivalents	(44,536,798)	14,525,492
Cash and cash equivalents at beginning of year	62,995,431	48,469,939
Cash and cash equivalents at end of year	<u>\$ 18,458,633</u>	<u>\$ 62,995,431</u>

*See accompanying notes.*

# John S. and James L. Knight Foundation

## Notes to Financial Statements

Dec. 31, 2006

### **1. The Organization**

The John S. and James L. Knight Foundation (the foundation), a nonprofit corporation, promotes excellence in journalism worldwide and invests in the vitality of 26 U.S. communities.

### **2. Significant Accounting Policies**

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

Cash and cash equivalents are composed of various operating accounts and highly liquid investments with original maturities of 90 days or less.

#### **Property, Plant and Equipment**

The foundation records property, plant and equipment as an expense in the year purchased. Property, plant and equipment purchased for 2006 and 2005 was approximately \$132,000 and \$276,000, respectively, of which approximately \$121,000 and \$243,000, respectively, are reflected in “General and administrative expenses” with the remainder being reflected in “investment expense” in the Statements of Activities.

#### **Program-Related Investments (PRIs)**

In accordance with Section 4944 of the Internal Revenue Code (the code), the foundation is permitted to make investments that are related to its philanthropic programs. These investments are anticipated to have a return lower than fair value. In the year of the investment, the foundation receives a credit toward its distribution requirement. These investments are treated as grants in the year they are approved. To the extent the investment is recovered by the foundation, the recovery is recognized as a negative distribution. Recoveries are reflected in “Grant forfeitures and other” in the Statements of Activities.

#### **Use of Estimates**

The presentation 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 amount 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 investment activity and expenses during the reporting period. Actual results could differ from those estimates.

John S. and James L. Knight Foundation

Notes to Financial Statements (continued)

**2. Significant Accounting Policies (continued)**

**Deferred taxes**

The foundation follows the policy of providing for federal excise tax on the net appreciation (both realized and unrealized) of investments. The deferred federal excise tax in the accompanying financial statements represents tax provided on the net unrealized appreciation of investments.

**Implementation of FASB Statement No. 158**

On Sept. 29, 2006, the Financial Accounting Standards Board (FASB) issued Statement No. 158, Employers' Accounting for Defined Benefit Pension and other Postretirement Plans, an amendment of FASB Statements No. 87, 88, 106, and 132(R) (Statement 158). Statement 158 requires entities to:

- Recognize the overfunded or underfunded status of a single employer defined benefit postretirement plan as an asset or liability in its statement of financial position and to recognize changes in that funded status in unrestricted net assets in the year in which the changes occur. The funded status of the plan is measured as the difference between the fair value of plan assets and the benefit obligation at the measurement date for each plan.
- Measure the funded status of a plan as of the date of its year-end statement of financial position, with limited exceptions.

All entities must implement the recognition and disclosure requirements related to the funding status for fiscal years ending after Jun. 15, 2007, and the measurement date requirements for fiscal years ending after Dec. 15, 2008. As early adoption of Statement 158 was permitted by FASB, the foundation has decided to adopt the provisions of Statement 158 for the fiscal year ended Dec. 31, 2006.

During 2005, the foundation pension asset was reported in the statement of financial position as "other assets" while the liability for other postretirement benefits was included in the "other liabilities" category. As a result of implementing Statement 158 in 2006, pension and postretirement liabilities are combined in one caption in the statement of financial position.

## John S. and James L. Knight Foundation

### Notes to Financial Statements (continued)

#### **2. Significant Accounting Policies (continued)**

##### **Reclassification**

Certain amounts in the prior year's financial statements have been reclassified to conform with the current year's presentation.

##### **Net Asset Accounting**

The foundation reports information regarding its financial position and activities according to the following two classes of net assets:

- Unrestricted net assets are not subject to donor-imposed stipulation or the restrictions have expired.
- Temporarily restricted net assets are subject to donor-imposed stipulations that can be fulfilled by actions of the foundation or that expire by the passage of time.

#### **3. Investments**

The investment goal of the foundation is to invest its assets in a manner that will achieve a total rate of return sufficient to replace the assets spent for grants and expenses and to recoup any value lost due to inflation. To achieve this goal, some investment risk must be taken. To minimize such risk, the foundation diversifies its investments among various financial instruments and asset categories, and uses multiple investment strategies and investment managers. Key decisions in this regard are made by the foundation's investment committee, which has oversight responsibility for the foundation's investment program. The committee identifies appropriate asset categories for investments, determines the allocation of assets to each category and approves the investment strategies employed. Effective Mar. 1, 2005, the Foundation engaged Cambridge Associates LLC (Cambridge), an independent consulting firm, to execute the investment program, including the engagement of investment managers, legal advisers, and management of the foundation's holdings in Knight Ridder common stock and strategic allocations to index funds and limited partnerships. All financial assets are held in custody for the foundation in proprietary accounts by a major commercial bank, except those assets that have been invested in limited partnerships, hedge funds or in certain products with multiple investors, such as index funds, all of which have separate custodial arrangements appropriate to their legal structure.

## John S. and James L. Knight Foundation

### Notes to Financial Statements (continued)

#### **3. Investments (continued)**

Approximately 49 percent and 52 percent of the foundation's financial assets at Dec. 31, 2006 and 2005, respectively, are invested in institutional mutual funds, publicly traded securities that are listed on national exchanges, treasury and agency bonds of the U.S. government, bonds of sovereign foreign governments and investment and non-investment grade corporate bonds for which active trading markets exist. Such assets are valued at quoted closing prices at year end. Realized gains and losses and increases and decreases in fair value on such investments are reflected in the Statements of Activities.

Approximately 23 percent and 24 percent of the foundation's financial assets at Dec. 31, 2006 and 2005, respectively, were invested in hedge funds and derivative instruments. The hedge funds utilize a variety of investment strategies which can be broadly categorized as absolute return and long/short equities strategies. The derivative instruments consisted of a "portable alpha" product and a swap agreement. These investments are not publicly listed or traded, and are not liquid investments. Each fund's investment manager calculates the fair value of investments on a monthly basis using the valuation guidelines stipulated in the respective investment agreements. Realized gains and losses and increases and decreases in fair value on the investments in hedge funds and derivative instruments are reflected in the Statements of Activities.

Approximately 23 percent and 20 percent of the foundation's financial assets at Dec. 31, 2006 and 2005, respectively, were invested with numerous partnerships, in which the foundation is a limited partner, that specialize in making venture capital, buyout, distressed debt, and equity-based real estate investments. Such investments, typically investments in private equity or debt securities of companies or properties that are not publicly listed or traded, are not liquid investments. The value of such investments is determined by the partnerships' general partners, who must follow the valuation guidelines, such as appraisals and comparable company trade data, stipulated in the respective limited partnership agreements. The Dec. 31 valuations of the investments in limited partnerships are based upon the value determined by the partnerships' general partner as of Sept. 30, adjusted for capital contributions and distributions that occur during the quarter ended Dec. 31. These amounts may differ from values that would be determined if the investments in limited partnerships were publicly traded or if the Dec. 31 valuation amount were currently available. Realized gains and losses and increases and decreases in fair value on the investments in limited partnerships are reflected in the Statements of Activities. All limited partnerships are audited annually by independent certified public accounting firms. As of Dec. 31, 2006, pursuant to its limited partnership agreements, the

John S. and James L. Knight Foundation

Notes to Financial Statements (continued)

**3. Investments (continued)**

Foundation is committed to contributing approximately \$314,972,000 in additional capital over the next 10 years to various partnerships. Unpaid commitments at Dec. 31, 2005, were approximately \$308,459,000.

During 2006, the foundation sold all of its holdings in the common stock of Knight Ridder. At Dec. 31, 2005, the foundation held 500,000 shares of Knight Ridder common stock, which represented 1.5 percent of the foundation's assets.

A detail of fair value and cost by investment class follows:

	Dec. 31, 2006		Dec. 31, 2005	
	Fair Value	Cost	Fair Value	Cost
Cash and cash equivalents	\$ 18,458,633	\$ 18,458,633	\$ 62,995,431	\$ 62,995,431
Interest, dividends and other investment receivables	79,178,622	77,720,723	23,771,432	24,056,633
(Payable) receivable related to derivative instrument	(1,807,168)	–	4,165,311	–
U.S. government and agency obligations	254,810,619	259,379,428	124,571,283	126,630,656
International bonds and other obligations	84,030,856	83,302,780	83,965,404	89,409,383
Corporate bonds and other obligations	67,936,849	68,170,671	184,282,261	184,268,296
Common stock of Knight Ridder	–	–	31,650,000	13,937,500
Other equity securities	757,886,057	600,231,751	656,166,445	566,676,373
Hedge fund investments	474,635,091	294,803,297	482,656,572	315,515,710
Alternative equity investments	421,566,126	532,386,279	318,937,744	452,057,031
Real estate investments	105,101,412	87,413,906	97,191,678	80,554,298
Total	<u>\$ 2,261,797,097</u>	<u>\$ 2,021,867,468</u>	<u>\$ 2,070,353,561</u>	<u>\$ 1,916,101,311</u>

Highly liquid investments with original maturities of three months or less are reported as cash equivalents.

## John S. and James L. Knight Foundation

### Notes to Financial Statements (continued)

#### 4. Derivative Financial Instruments

Some investment managers retained by the foundation have been authorized to use certain derivative financial instruments in a manner set forth by the foundation's written investment policy, specific manager guidelines or partnership/fund agreement documents. Specifically, derivative financial instruments may be used for the following purposes: (1) currency forward contracts and options may be used to hedge nondollar exposure in foreign investments; (2) covered call options may be sold to enhance yield on major equity positions; (3) futures contracts may be used to equitize excess cash positions, rebalance asset categories within the portfolio, adjust risk exposures within the portfolio, or to rapidly increase or decrease exposure to specific investment positions in anticipation of subsequent cash trades; and (4) futures contracts and options may be used by hedge fund managers to hedge or leverage positions in portfolios in their respective funds. Authorization to use these derivative financial instruments currently is restricted to 24 hedge fund managers, who manage investments totaling approximately \$474,635,000.

Cambridge is also authorized to use derivatives to execute certain investment strategies. Derivative financial instruments are recorded at fair value in the Statements of Financial Position with changes in fair value reflected in the Statements of Activities.

During fiscal 2006 the foundation invested in a "portable alpha" product which is designed to provide a return in excess of a certain benchmark. The investment manager invests the principal in a basket of securities that replicates the benchmark, and then leverages the principal investment and invests in fixed income strategies. The foundation's equity investment is benchmarked to the Standard & Poor's 500 Index and is valued at approximately \$27,671,000 at Dec. 31, 2006. The foundation's fixed income investment is benchmarked to the Lehman Brothers Treasury 5+Year Index and is valued at approximately \$25,571,000 at Dec. 31, 2006. At Dec. 31, 2006, a payable of approximately \$1,807,000 reflecting the fair value of the leveraged investments was reported in "(payable) receivable related to derivative instrument" on the Statements of Financial Position, and an equal amount was included in "net change in fair value of investments" in the Statements of Activities.

## John S. and James L. Knight Foundation

### Notes to Financial Statements (continued)

#### **4. Derivative Financial Instruments (continued)**

During fiscal 2006 the foundation's exposure to commodities included an account administered by one manager to replicate the return of the Dow Jones AIG Commodity Index by using swaps. The account had a swap agreement with two counterparties. The agreements had three-month terms. The foundation invested collateral equal to the notional value of the swaps in an investment account also managed by this manager. At Dec. 31, 2006, the foundation was a party to swap agreements with a total notional value of approximately \$80,000,000. At Dec. 31, 2005, the foundation was a party to swap agreements with a total notional value of approximately \$136,076,000. At Dec. 31, 2006, no valuation adjustment was required related to the swap agreements.

The foundation had no futures contracts as of Dec. 31, 2006 or 2005.

In Cambridge's opinion, the use of derivative financial instruments in its investment program is appropriate and customary for the investment strategies employed. The foundation's management concurs with this opinion. Using those instruments reduces certain investment risks and generally adds value to the portfolio. The instruments themselves, however, do involve some investment and counterparty risk not fully reflected in the foundation's financial statements. Cambridge does not anticipate that losses, if any, from such instruments would materially affect the financial position of the foundation, and the foundation's management concurs.

#### **5. Grants**

The foundation records grants in full as expenses when approved. Grants payable at Dec. 31, 2006 and 2005 represents the present value of multiyear grants using an 8.25 percent and 7.25 percent discount rate, respectively. The foundation made grant payments of approximately \$104,310,000 and \$92,577,000 in 2006 and 2005, respectively.

John S. and James L. Knight Foundation

Notes to Financial Statements (continued)

**5. Grants (continued)**

As of Dec. 31, 2006, the foundation had future grant commitments, which are scheduled for payment in future years as follows:

2007	\$ 46,217,400
2008	27,961,976
2009	8,549,546
2010	3,845,000
2011	390,000
	<hr/>
	86,963,922
Discounted to present value	(10,600,399)
Grants payable	<hr/> <hr/>
	\$ 76,363,523

**6. Federal Excise Taxes**

The foundation qualifies as a tax-exempt organization under Section 501(c)(3) of the code and, with the exception of unrelated business income from debt-financed, passive investments, is not subject to federal or state income tax. However, the foundation is classified as a private foundation and is subject to a federal excise tax of 2 percent (or 1 percent under certain circumstances) on net investment income and net realized gains, as defined by the code. The foundation expects to qualify for the 1 percent tax rate in 2006 and was subject to the 1 percent tax rate in 2005. A deferred excise tax provision of approximately \$857,000 on net unrealized gains on investments was recognized during the year ended Dec. 31, 2006.

Total excise and other taxes paid by the foundation for the years ended Dec. 31, 2006 and 2005 amounted to approximately \$2,544,000 and \$2,287,000, respectively.

John S. and James L. Knight Foundation

Notes to Financial Statements (continued)

**7. Employee Pension Plan and Other Postretirement Benefit Plans**

The foundation sponsors a pension plan with defined benefit and cash balance features for its eligible employees. The pension benefits for all employees hired prior to Jan. 1, 2000, will be the greater of the benefits as determined under the defined benefit feature of the pension plan or the cash balance feature of the pension plan. The pension benefits for all employees hired on or subsequent to Jan. 1, 2000, will be determined under the cash balance feature of the pension plan. The foundation also sponsors postretirement medical and life insurance benefit plans.

The following table sets forth the pension and other postretirement benefits plans' funded status and amounts recognized in the foundation's Statements of Activities and Financial Position:

	Pension Plan		Other Postretirement Benefit Plans	
	Year Ended Dec. 31 2006	2005	Year Ended Dec. 31 2006	2005
<b>Funded status</b>				
Fair value of plan assets	\$ 9,337,058	\$ 8,824,722	\$ 762,365	\$ 555,529
Benefit obligation	(9,536,751)	(9,530,853)	(1,406,568)	(1,245,156)
Funded status of the plan	<u>\$ (199,693)</u>	<u>\$ (706,131)</u>	<u>\$ (644,203)</u>	<u>\$ (689,627)</u>
Prior service cost	\$ (178,858)	N/A	\$ —	N/A
Accumulated gain (loss)	<u>(756,254)</u>	N/A	<u>234,231</u>	N/A
Effect of FAS 158 implementation on unrestricted net assets	(935,112)	N/A	234,231	N/A
Cumulative employer contribution in excess (deficiency) of net periodic benefit costs	<u>735,419</u>	N/A	<u>(878,434)</u>	N/A
Accrued benefit liability recognized in the Statements of Financial Position (after FAS 158)	<u>\$ (199,693)</u>	N/A	<u>\$ (644,203)</u>	N/A
Accrued benefit asset (liability) recognized in the Statements of Financial Position (prior to FAS 158)	N/A	\$ 1,153,730	N/A	\$ (724,765)

John S. and James L. Knight Foundation

Notes to Financial Statements (continued)

**7. Employee Pension Plan and Other Postretirement Benefit Plans (continued)**

	<b>Pension Plan</b>		<b>Other Postretirement Benefit Plans</b>	
	<b>Year Ended Dec. 31</b>		<b>Year Ended Dec. 31</b>	
	<b>2006</b>	<b>2005</b>	<b>2006</b>	<b>2005</b>
<b>Components of net periodic benefit cost</b>				
Service cost	\$ 463,735	\$ 587,500	\$ 180,825	\$ 137,196
Interest cost	499,207	471,211	67,584	82,582
Expected return on plan assets	(663,734)	(565,797)	(49,024)	(32,848)
Amortization of prior service cost	42,798	45,674	84,972	84,973
Recognized actuarial loss	76,305	68,104	–	10,865
Net periodic benefit cost	<u>\$ 418,311</u>	<u>\$ 606,692</u>	<u>\$ 284,357</u>	<u>\$ 282,768</u>
Actual return on plan assets	\$ 1,152,568	\$ 438,727	\$ 107,816	\$ 23,853
Employer contributions	–	1,050,000	130,688	147,556
Employee contributions	–	–	1,187	1,252
Benefits paid	640,232	342,262	32,855	28,390
<b>Actuarial assumptions</b>				
Discount rate	5.75%	5.50%	5.75%	5.50%
Expected return on plan assets	8.00	8.00	8.00	8.00
Rate of compensation increase	4.50	4.50	4.50	4.50
<b>Health care cost trend rate assumptions</b>				
Initial trend rate	N/A	N/A	12.00%	13.00%
Ultimate trend rate	N/A	N/A	5.25	5.25
Year ultimate trend is reached	N/A	N/A	2014	2014

The expected long-term rate of return on plan assets for determining net periodic pension cost is chosen by the foundation from a best estimate range determined by the actuary by applying anticipated long-term returns and long-term volatility for various asset categories to the target asset allocation of the plan.

The calculations related to other postretirement benefit plans do not anticipate any savings from the Medicare Prescription Drug, Improvement and Modernization Act of 2003.

John S. and James L. Knight Foundation

Notes to Financial Statements (continued)

**7. Employee Pension Plan and Other Postretirement Benefit Plans (continued)**

Expected benefit payments are as follows:

	<u>Pension Plan</u>	<u>Other Postretirement Benefit Plans</u>
2007	\$ 491,701	\$ 42,768
2008	670,720	55,612
2009	956,454	71,247
2010	636,253	81,254
2011	619,593	86,650
2012-2016	5,237,769	520,464

During 2007, the foundation is not required to make any contributions to the pension or to the other postretirement benefit plans. The foundation may choose to make a contribution during 2007.

The investment goal for plan assets is to provide sufficient liquidity to meet payout requirements while maintaining safety of principal through prudent diversification. During 2006 asset allocation targets for the pension plan were large-cap domestic equity, 40 percent, small-cap domestic equity, 10 percent, international equity, 20 percent, domestic fixed income, 20 percent, and TIPS, 10 percent. During 2006 asset allocation targets for the other postretirement benefit plans were large-cap domestic equity, 65 percent, small-cap domestic equity, 10 percent, international equity, 10 percent, domestic fixed income, 10 percent, and domestic high yield, 5 percent.

John S. and James L. Knight Foundation

Notes to Financial Statements (continued)

**7. Employee Pension Plan and Other Postretirement Benefit Plans (continued)**

A detail of fair value of plan assets by investment class follows:

	Pension Plan		Other Postretirement Benefit Plans	
	Dec. 31		Dec. 31	
	2006	2005	2006	2005
Cash and cash equivalents	\$ 96,878	\$ 680,119	\$ 29,123	\$ 21,597
Interest, dividends and other investment receivables	25,905	28,794	104	66
U.S. government and agency obligations	1,760,568	1,516,581	–	–
Corporate bonds and other obligations	703,453	465,845	87,038	44,131
Equity securities	6,750,254	6,133,383	646,100	489,735
Total	<b>\$ 9,337,058</b>	<b>\$ 8,824,722</b>	<b>\$ 762,365</b>	<b>\$ 555,529</b>

In addition, the foundation sponsors a defined contribution plan for its eligible employees for which it has no fixed liabilities. Effective Jan. 1, 2002, the foundation's defined contribution plan was amended to add an employer matching contribution component. During 2006 and 2005, the foundation made contributions to the defined contribution plan of approximately \$155,000 and \$152,000, respectively.

**8. Leases**

The foundation has a lease for approximately 21,300 square feet of office space in Miami, Fla., which expires in 2013. The foundation also had one lease for equipment, which expired in 2006. Rental expense for office and equipment leases for 2006 and 2005 was approximately \$799,000 and \$758,000, respectively. Future minimum lease payments for the office lease are as follows:

2007	\$ 705,066
2008	721,029
2009	736,993
2010	752,957
2011	768,921
Thereafter	1,244,286
Total	<b>\$ 4,929,252</b>

## John S. and James L. Knight Foundation

### Notes to Financial Statements (continued)

#### **9. Beneficial Interest in Remainder Trusts**

The foundation has a beneficial interest in charitable remainder trusts established by John S. Knight. Under the terms of the trusts, distributions are made from the trusts to designated beneficiaries for the remainder of their lives. The remainder of the assets in the trusts will be transferred to the foundation. All of the assets of the trusts are administered and held in the custody of a commercial bank.

The foundation values its interest in the trusts using the methodology described in the National Committee on Planned Giving's 2004 publication, *Valuation Standards for Charitable Planned Gifts*. This methodology is a two-step process starting with the fair market value of the assets. The first step uses a 5 percent payout rate, life expectancy based on IRS Mortality Tables and assumed investment returns to determine the value of the interest at its projected termination. The second step discounts this future value using the Consumer Price Index. As of Dec. 31, 2006 and 2005 the value of the foundation's interest in the remainder trusts was approximately \$80,827,000 and \$71,370,000.

The trusts were established in 1975 and became irrevocable in 1981, however, the foundation had not recognized its beneficial interest in the trusts. The accompanying financial statements have been restated in order to reflect the foundation's beneficial interest in the trusts and the related impact on the statement of activities. As a result of the restatement, temporarily restricted net assets as of Dec. 31, 2004 increased by \$81,193,000 and net assets at the end of 2004 increased from \$1,817,219,000 to \$1,898,412,000. A reduction in the value of the beneficial interest of \$9,823,000 was reflected in the 2005 statement of activities, and a beneficial interest in remainder trusts and temporarily restricted net assets of \$71,370,000 are reported in the Dec. 31, 2005 statement of financial position. As a result, the following changes occurred on the statement of financial position: total assets and total liabilities and net assets increased from \$2,071,507,000 to \$2,142,877,000 and total net assets increased from \$1,962,793,000 to \$2,034,163,000. In addition, the increase in net assets changed from \$145,574,000 to \$135,751,000.