

Save the Children Federation, Inc.
Financial Statements
September 30, 2006

Report of Independent Auditors

The Board of Trustees
Save the Children Federation, Inc.

In our opinion, the accompanying statement of financial position and the related statements of activities and changes in net assets, cash flows and expenses by function, present fairly, in all material respects, the financial position of Save the Children Federation, Inc. ("SC") at September 30, 2006, and the changes in its net assets and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of SC's management. Our responsibility is to express an opinion on these financial statements based on our audit. The prior year summarized comparative information has been derived from SC's 2005 financial statements, and in our report dated December 15, 2005, we expressed an unqualified opinion on those financial statements. We conducted our audit of these statements 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, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

PricewaterhouseCoopers LLP

December 15, 2006

Save the Children Federation, Inc.
Statements of Financial Position
As of September 30, 2006 and 2005 (in thousands)

	<u>2006</u>	<u>2005</u>
Assets		
Cash and cash equivalents	\$ 51,578	\$ 38,713
Grants and contracts receivable (Note 14)	18,792	14,077
Contributions receivable, net (Note 6)	16,477	17,251
Investments, at fair value (Note 5)	116,009	109,140
Restricted investments, at fair value (Note 7)	16,137	12,022
Commodities inventory	10,678	2,242
Prepaid expenses and other assets	10,537	7,353
Assets of pooled income fund and charitable gift annuities	2,900	2,566
Land, buildings, and equipment, net (Note 8)	18,280	13,867
Loan program fund assets held for others (Note 4)	2,035	2,163
Beneficial interests in perpetual trusts held by third parties (Note 11)	1,451	1,393
Total assets	<u>\$ 264,874</u>	<u>\$ 220,787</u>
Liabilities and Net Assets		
Liabilities		
Accounts payable and accrued liabilities	\$ 18,003	\$ 17,704
Deferred amounts received under grants and contracts (Note 14)	36,593	17,714
Refundable advances on conditional contributions received (Note 7)	16,137	12,022
Deferred revenue	472	1,379
Severance benefits for foreign national employees	6,154	5,371
Loan program funds due communities (Note 4)	2,035	2,163
Postretirement benefits other than pensions (Note 10)	3,312	3,130
Total liabilities	<u>82,706</u>	<u>59,483</u>
Commitments and contingencies (Notes 12 and 13)		
Net assets		
Unrestricted		
Undesignated	10,733	14,453
Board designated	51,345	35,058
Investment in land, buildings, and equipment	18,280	13,867
Total unrestricted net assets	<u>80,358</u>	<u>63,378</u>
Temporarily restricted - other SC (Note 11)	40,103	32,881
Temporarily restricted - AETRF (Note 11)	47,113	53,233
Total temporarily restricted net assets	<u>87,216</u>	<u>86,114</u>
Permanently restricted (Note 11)	14,594	11,812
Total net assets	<u>182,168</u>	<u>161,304</u>
Total liabilities and net assets	<u>\$ 264,874</u>	<u>\$ 220,787</u>

See accompanying notes to these financial statements.

**Save the Children Federation, Inc.
Statement of Activities and Changes in Net Assets
For the year ended September 30, 2006 with comparative totals for the year ended
September 30, 2005 (in thousands)**

	Unrestricted		Temporarily Restricted			2006 Total	2005 Total
	Other SC	Earthquake/ Tsunami Relief Fund	Unrestricted Total	Other SC	Earthquake/ Tsunami Relief Fund		
Operating revenue	\$ 49,424	\$ 17,150	\$ 66,574	\$ 46,419	\$ 1,325	\$ 47,744	\$ 114,318
Contributions and private grants							
U.S. government grants and contracts (Note 14)	124,165	809	124,974	32,335		32,335	124,974
Sponsorships							
Commodities and ocean freight (Note 3)	41,243	5,409	46,652				32,335
Fee for service contracts	4,031	1,826	5,857				46,652
Bequests	2,040		2,040	460		460	5,857
Investment return - spending rate (Note 5)	2,951		2,951	1,321	1,292	2,613	2,500
Other	220		220				5,564
	224,074	25,194	249,268	80,535	2,617	83,152	332,420
Net assets released from restrictions	74,047	10,385	84,432	(74,047)	(10,385)	(84,432)	-
Total operating revenue	298,121	35,579	333,700	6,488	(7,768)	(1,280)	332,420
Operating expenses							
Program services							
Program activities	254,024	33,789	287,813				287,813
Program development and public policy support	13,476	206	13,682				13,682
Total program services	267,500	33,995	301,495				301,495
Supporting services							
Management and general	11,172	554	11,726				11,726
Fund raising	19,315	1,030	20,345				20,345
Total supporting services	30,487	1,584	32,071				32,071
Total operating expenses	297,987	35,579	333,566				333,566
(Deficit) excess of operating revenue over expenses	134	-	134	6,488	(7,768)	(1,280)	(1,146)
Nonoperating activities							
Investment return in excess of spending rate (Note 5)	1,739		1,739				1,739
Foreign currency exchange gain	549		549		1,648	1,648	2,197
Contributions and change in value of split-interest agreements				734		734	18,074
Total nonoperating activities	14,558		14,558	734	1,648	2,382	22,010
Change in net assets	16,980	-	16,980	7,222	(6,120)	1,102	22,864
Net assets, beginning of year	63,378		63,378	32,881	53,233	86,114	161,304
Net assets, end of year	\$ 80,358	\$ -	\$ 80,358	\$ 40,103	\$ 47,113	\$ 87,216	\$ 182,168

See accompanying notes to these financial statements.

Save the Children Federation, Inc.
Statement of Functional Expenses
For the year ended September 30, 2006 with comparative totals for the year ended
September 30, 2005 (in thousands)

	Program Services			Supporting Services			2005 Total Expenses
	Program Activities	Program Development and Public Policy Support	Total Program Services	Management and General	Fund Raising	Total Supporting Services	
Salaries	\$ 55,052	\$ 6,614	\$ 61,666	\$ 4,879	\$ 6,103	\$ 10,982	\$ 61,161
Employee fringe benefits	19,583	1,818	21,401	1,529	1,453	2,982	17,785
Payroll taxes	2,205	426	2,631	309	422	731	3,021
Total salaries and related expenses	76,840	8,858	85,698	6,717	7,978	14,695	81,967
Commodities and ocean freight	46,652		46,652			55	53,711
Grants to other agencies	60,025	67	60,092	32	23		56,632
Professional fees	5,848	1,314	7,162	1,645	1,465	3,110	9,198
Supplies, materials, etc.	44,772	623	45,395	236	491	727	61,392
Other project costs	8,888		8,888				7,341
Telecommunications	3,458	148	3,606	99	236	335	3,382
Postage and shipping	3,600	35	3,635	46	1,154	1,200	3,387
Advertising					6,381	6,381	6,420
Printing	1,108	95	1,203	12	1,183	1,195	2,683
Occupancy	9,221	200	9,421	260	307	567	7,734
Travel	25,078	2,089	27,167	611	471	1,082	23,497
Depreciation	996	45	1,041	233	290	523	1,434
Miscellaneous	1,327	208	1,535	1,835	366	2,201	4,231
Total expenses	\$ 287,813	\$ 13,682	\$ 301,495	\$ 11,726	\$ 20,345	\$ 32,071	\$ 323,009

See accompanying notes to these financial statements.

Save the Children Federation, Inc.
Statements of Cash Flows
For the years ended September 30, 2006 and 2005 (in thousands)

	<u>2006</u>	<u>2005</u>
Cash flows from operating activities		
Change in net assets	\$ 20,864	\$ 84,033
Adjustments to reconcile change in net assets to net cash provided by operating activities		
Depreciation	1,564	1,434
Contributed capital assets	(2,929)	(103)
Net loss on sale and disposal of equipment	(2)	439
Net realized gain on sale of investments	(846)	(878)
Net unrealized appreciation in fair value of investments	(2,084)	(3,132)
Contributions and changes in value of split-interest agreements restricted for long-term investment	(2,596)	(1,464)
Changes in operating assets and liabilities		
Grants and contracts receivable	(4,715)	(1,536)
Contributions receivable, net	774	(5,203)
Commodities inventory	(8,436)	1,687
Prepaid expenses and other assets	(3,576)	(3,455)
Accounts payable, accrued liabilities and severance benefits for foreign national employees	1,082	4,933
Deferred amounts received under grants and contracts and refundable advances on conditional contributions	22,994	(2,922)
Deferred revenue	(907)	(3,204)
Postretirement benefits other than pensions	182	115
Net cash provided by operating activities	<u>21,369</u>	<u>70,744</u>
Cash flows from investing activities		
Purchases of investments	(59,545)	(85,679)
Proceeds from sale of investments	55,606	30,317
Purchases of restricted investments	(11,538)	(4,961)
Proceeds from sales of restricted investments	7,423	10,180
Expenditures for land, building and equipment	(3,073)	(2,414)
Proceeds from sale and disposal of equipment	27	48
Net cash used in investing activities	<u>(11,100)</u>	<u>(52,509)</u>
Cash flows from financing activities		
Contributions and changes in value of split-interest agreements restricted for long-term investment	2,596	1,464
Net cash provided by financing activities	<u>2,596</u>	<u>1,464</u>
Net increase in cash and cash equivalents	12,865	19,699
Cash and cash equivalents at beginning of year	38,713	19,014
Cash and cash equivalents at end of year	<u>\$ 51,578</u>	<u>\$ 38,713</u>
Supplemental cash flow information		
Gifts in-kind for computer licenses, books and other materials	<u>\$ 8,273</u>	<u>\$ 6,285</u>

See accompanying notes to these financial statements.

Save the Children Federation, Inc.

Notes to Financial Statements (dollars in thousands)

1. Organization and Purpose

Save the Children Federation, Inc. ("SC" or the "Agency") was established in 1932 and operates as a voluntary, nonsectarian, nonprofit organization in the United States of America and throughout the world providing services for children and community self-help assistance.

SC is a member of The International Save the Children Alliance (the "Alliance"), an international association of autonomous, nonprofit, private, and voluntary organizations bearing the name Save the Children or a related designation. The financial position, changes in net assets and cash flows of the Alliance are not reflected in the accompanying financial statements.

2. Summary of Significant Accounting Policies

Basis of Accounting and Presentation

The financial statements of SC have been prepared on the accrual basis of accounting in conformity with accounting principles generally accepted in the United States of America, which requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingencies at the date of the financial statements and revenues and expenses recognized during the reporting period. Actual results could differ from those estimates.

The net assets of SC and changes therein are classified and reported as follows:

Permanently restricted net assets – Net assets subject to donor-imposed stipulations that they be maintained permanently by SC. The donors permit SC to use all or part of the income earned on these assets for general or specific purposes of SC.

Temporarily restricted net assets – Net assets whose use by SC is limited by donor-imposed stipulations that either expire by passage of time or can be fulfilled and released by actions of SC pursuant to those donor-imposed stipulations.

Unrestricted net assets – Net assets whose use by SC is not subject to donor-imposed restrictions. Board-designated net assets represent resources designated by the Board of Trustees to contribute to the long-term sustainability of current programs.

Revenues are reported as increases in unrestricted net assets unless their use is limited by donor-imposed restrictions. Expenses are reported as decreases in unrestricted net assets. Gains and losses on investments are reported as increases or decreases in unrestricted net assets unless their use is restricted by donors or state law. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported as net assets released from restrictions in the statement of activities.

Fair Value of Financial Instruments

The carrying value of cash equivalents, receivables, payables, deferred income and loans receivable approximate fair values as of September 30, 2006 and 2005, due to the relative short maturities of these instruments.

Save the Children Federation, Inc.

Notes to Financial Statements (dollars in thousands)

Contributions

Contributions, which include unconditional promises to give (contributions receivable), are recognized as revenue when received. Unconditional promises to give appear as contributions receivable and revenues of the appropriate net asset category. Pledges are recorded as temporarily restricted after recognizing an allowance for uncollectible contributions and a discount (for those pledges which will be realized one year beyond the statement of financial position), at a risk free rate, to reflect the net present value based on projected cash flows. Bequest income is recorded when the will is declared legally valid.

Contributions received with donor-imposed conditions are recognized as revenue when the conditions have been substantially met. Amounts received in advance of satisfying the donor-imposed conditions are reported as refundable advances until the conditions are met.

Measure of Operations

SC includes in its measure of operations (operating revenue over expenses) all revenue that is an integral part of its programs and supporting activities. The measure of operations includes the investment return equal to SC's spending policy and excludes investment returns in excess of or less than the spending policy, increases or decreases in permanently restricted net assets, contributions and changes in value of split-interest agreements, total bequests in excess of \$2,500 or as needed to balance operations to the extent current year bequest revenue is in excess of \$2,500, and contributions designated as quasi-endowments by the Board of Trustees.

Split-Interest Agreements

SC has the following split-interest agreements with donors:

- Charitable Gift Annuities which SC manages and invests — These gifts are arrangements between a donor and SC in which the donor contributes an asset to SC to manage, in exchange for a promise to pay the donor or other third party(ies) identified by the donor, a fixed amount for a specified period of time. SC has established a liability for the present value of these future commitments. The liability is calculated annually and the asset is recorded at fair value. The difference between the fair value of the asset and liability is recorded in the nonoperating section of the statement of activities as changes in split-interest agreements. The remaining asset at the death of a donor reverts to SC as unrestricted nonoperating revenue, unless specifically restricted by the donor.
- Irrevocable Charitable Remainder Unitrusts (CRUTs) for which SC is not the trustee — CRUTs are reported as contributions receivable and temporarily restricted contribution revenue at the present value of the estimated future benefits to be received. Adjustments to the receivable to reflect amortization of the discount and changes in actuarial assumptions are recognized in the nonoperating section of the statement of activities as changes in value of split-interest agreements.
- Pooled Income Funds which SC manages and invests — These contributions are accounted for at the fair value of assets to be received discounted for the estimated life of the donor. SC recognizes its remainder interest in the assets received as temporarily restricted nonoperating contribution revenue in the period in which the assets are received. The difference between the fair value of the assets and the contribution revenue recognized is recorded as deferred revenue, representing the amount of discount for future interest.
- Perpetual Trusts held and administered by others — Perpetual trusts are recognized as permanently restricted contribution revenue and as an asset at the present value of estimated future cash receipts from the trust assets, which generally has been determined to approximate the fair value of SC's portion of the trust assets. Subsequent changes in the

Save the Children Federation, Inc.

Notes to Financial Statements (dollars in thousands)

value of perpetual trusts are reported as nonoperating revenue. Income received from the trusts is recorded as unrestricted revenue, unless specifically restricted by the donor.

Grants and Contracts

SC receives funding under grants and contracts from the government of the United States of America, United Nations agencies, and other grantors, for direct and indirect program costs and to provide certain whole or partial subgrants to other agencies. This funding is subject to contractual restrictions which must be met through incurring qualifying expenses for particular programs.

Revenue from grants and contracts is recognized only when funds are utilized by SC to carry out the activity stipulated in the grant or contract agreement. Grants and contracts receivable represent amounts due from funding organizations for reimbursable expenses incurred. Deferred amounts received under grants and contracts represent cash received in advance of earning revenue and incurring the related expenses.

Donated Materials and Services

Donated materials are reported as contributions and expenses in amounts equal to the estimated fair value on the date of receipt.

A substantial number of individuals have donated significant amounts of their time to SC's program and supporting functions; however, these services do not meet the criteria for recognition in accordance with accounting principles generally accepted in the United States of America and, therefore, are not recorded in the financial statements.

Foreign Currency Translation

Assets and liabilities denominated in foreign currencies are translated into United States of America dollars, the reporting currency, at exchange rates in effect on reporting dates, and revenue and expenses are translated at rates which approximate those in effect on transaction dates. Net transaction and translation gains and losses are included in the accompanying statement of activities as part of miscellaneous management and general expenses. Translation gains and losses are not significant.

Cash and Cash Equivalents

Cash and cash equivalents include cash on hand, demand deposits, and short-term, highly liquid investments with maturity dates of 90 days or less that are readily convertible to known amounts of cash, except for short-term investments purchased by SC's investment manager held as part of a long-term investment strategy.

Investments

SC's investments consist of publicly traded fixed income and equity securities, alternative investments and cash held for reinvestment. Alternative investments include hedge fund investments and private equity fund investments. Alternative investments are carried at estimated fair value provided by the management of the respective fund as of September 30. All other investments are stated at fair value as of September 30 based upon independent third party markets.

SC believes that the carrying amount of its alternative investments is a reasonable estimate of fair value as of September 30, 2006. Because alternative investments are not readily marketable, the estimated value is subject to uncertainty and, therefore, may differ from the value that would have been used had a ready market for the investment existed. Such differences could be material. The amount of gain or loss associated with these investments is reflected in the accompanying financial statements.

Save the Children Federation, Inc.

Notes to Financial Statements (dollars in thousands)

Securities sold, but not yet purchased, represent obligations of SC to deliver specified securities at contracted prices and thereby create a liability to repurchase the securities at prevailing future market prices. Accordingly, these transactions result in off-balance-sheet risk as SC's ultimate obligation to satisfy the sale of investments sold, but not yet purchased, may exceed the amount recognized in the financial statements.

SC records purchases and sales of securities on a trade-date basis. Realized gains and losses are determined on the basis of average cost of securities sold and are reflected in the statement of activities. Dividend income is recorded on the ex-dividend date and interest income is recorded on an accrual basis.

Commodities Inventory

SC recorded agricultural and food commodities in-transit and on-hand in warehouses as of September 30, 2006 and has recorded deferred amounts received under grants and contracts in an equal amount.

Foreign Currency Contracts

Save the Children purchases forward currency contracts whereby SC agrees to exchange one currency for another on an agreed-upon date at an agreed-upon exchange rate to help minimize the exposure to adverse fluctuations in currency markets. At September 30, 2006, SC had open forward foreign currency contracts with notional amounts totaling \$10,000. Included in the statement of financial position at September 30, 2006 at fair value were pending receivables of \$1,648, which represents cumulative unrealized gains on these contracts at September 30, 2006. Such contracts involve, to varying degrees, the possible inability of counterparties to meet the terms of their contracts. Changes in the value of forward foreign currency contracts are recognized as unrealized gains or losses at each reporting period.

Land, Buildings, and Equipment

Land, buildings, and equipment are stated at cost. Depreciation is computed on a straight-line basis over the estimated useful lives of the respective assets. Capitalizable costs incurred in connection with ongoing capital projects are recorded as capital projects-in-progress. These costs will be reclassified into their proper building and equipment categories and depreciated once placed in service.

SC has adopted a policy of implying a time restriction that expires over the useful life of long-lived assets acquired, donated or constructed with contributions restricted for that purpose and, therefore, releases amounts from temporarily restricted net assets equal to the current year's depreciation expense of fixed assets built, donated or constructed with temporarily restricted contributions.

The estimated useful lives by year are as follows:

	<u>Years</u>
Buildings	25-50
Building improvements	10
Equipment	3-10
Computer software	3-5

Save the Children Federation, Inc.

Notes to Financial Statements (dollars in thousands)

Functional Expenses

SC allocates expenses on a functional basis among its various programs and supporting services. Expenses that can be identified with a specific program or supporting service are charged directly. Other expenses that are common to several functions are allocated by various statistical bases. Other project costs represent the aggregate of various other program service costs not individually classified in the accompanying statement of functional expenses due to their varying nature and amount from year to year.

Program services are further broken down into program activities and program development and advocacy. Program activities represents the costs associated with the delivery of programs relating to education, primary health, economic opportunity, food security and resource management, emergency, refugee and civil society. Program development and advocacy relate to the development and technical support of programs and the advocacy efforts in support of the children.

Tax-Exempt Status

The Agency qualifies as a tax-exempt organization under Section 501(c)(3) of the Internal Revenue Code and has been determined not to be a private foundation under Section 509(a)(1) of the Code.

Comparative Financial Information

The accompanying statements of activities and functional expenses are presented with prior year summarized financial information in total, but not by net asset class or functional category. Such information does not include sufficient detail to constitute a presentation in conformity with accounting principles generally accepted in the United States of America. Accordingly, such information should be read in conjunction with SC's September 30, 2005 financial statements, from which the summarized information was derived.

Reclassifications

Certain reclassifications have been made to amounts previously reported to conform to the current year's presentation. Such reclassifications had no effect on changes in net assets.

3. Commodities and Ocean Freight

During fiscal year 2006 and 2005, SC was granted and distributed certain agricultural commodities under famine relief contracts with the United States government. These commodities and related ocean freight, which amounted to \$16,855 and \$27,607 in fiscal year 2006 and 2005, respectively, are recorded as grant and contract revenue and program expense. SC also received and distributed commodities under contract with World Food Program. These commodities and related ocean freight, which amounted to \$29,797 and \$26,104 in fiscal years 2006 and 2005, respectively, are also recorded as grant and contract revenue and program expense.

4. Loan Program Fund Assets Held for Others

SC currently manages, on behalf of certain communities, a number of loan programs which have been funded primarily by the United States Agency for International Development. Pursuant to this program, SC holds cash for certain constituent community organizations that provide loans to various indigent people concerning child welfare issues.

Save the Children Federation, Inc.
Notes to Financial Statements (dollars in thousands)

5. Investments

Investments consisted of the following at September 30:

	2006		2005	
	Fair Value	Cost	Fair Value	Cost
Common stocks	\$ 34,552	\$ 31,776	\$ 19,892	\$ 17,814
Corporate bonds	33,164	34,214	46,015	47,125
Government securities	2,151	2,197	5,872	5,926
Mutual funds (principally equity)	22,925	21,413	16,105	15,318
Real estate equities	2,901	2,036	2,143	1,645
Hedge funds (limited partnerships and corporations) and private equity (limited partnerships)	9,903	8,540	7,144	6,000
Short-term investments (primarily money market funds)	10,413	10,460	11,969	12,023
	<u>\$ 116,009</u>	<u>\$ 110,636</u>	<u>\$ 109,140</u>	<u>\$ 105,851</u>

U.S. Public Equities and Mutual Funds and Foreign Public Equities and Mutual Funds

The fair value of publicly traded fixed income and equity securities investments are based on quoted market prices. Investments that are listed on an exchange are valued, in general, at the last reported sale price (or, if there is no sales price, at the last reported bid price, or, in the absence of reported bid prices, at the mean between the last reported bid and asked prices thereof). If an investment is restricted, SC may discount the price to reflect the nature of the restriction. Fees paid to investment managers are netted against investment income.

Alternative Investments

Alternative investments include interests in private equity and hedge funds partnerships. Since private equity and hedge funds partnerships do not have readily ascertainable market values and may be subject to withdrawal restrictions, SC values these investments in accordance with valuations provided by the general partners of the underlying partnerships. SC's management may consider other factors in assessing the fair value of these investments.

As a rule, the general partners of the private equity funds partnerships initially values investments held by the funds at cost and requires that changes in these values be established by meaningful third-party transactions or a significant impairment in the financial condition or operating performance of the issuer. Such values usually represent SC's proportionate share of the net assets of the private equity partnerships as reported by the general partners of the underlying partnerships. The values of the investments in the underlying partnerships are increased by additional contributions to the underlying partnerships and SC's share of undistributed net earnings from the underlying partnerships and decreased by distributions from the underlying partnerships and SC's share of undistributed net losses.

Hedge funds are also valued in accordance with valuations provided by the general partners of the underlying partnerships. Hedge funds do not have readily ascertainable market values and may be subject to withdrawal restrictions. The fair value of the hedge funds represents the amount SC expects to receive at September 30, 2006 if it had liquidated its investments in the hedge funds on these dates.

Save the Children Federation, Inc.
Notes to Financial Statements (dollars in thousands)

SC is obligated under certain limited partnership investment fund agreements to advance additional funding periodically up to specified levels. At September 30, 2006, SC had unfunded commitments of \$2,400, which are likely to be called through 2012.

Cash Held for Reinvestment

Cash equivalents included in the portfolio consist primarily of liquid short-term instruments.

Spending Policy

In order to preserve the value of the investment portfolio in real terms (after inflation) and to eliminate the impact of market fluctuations on operations, SC has adopted a spending rate that limits the amounts of investment return (interest, dividends, and net realized and unrealized appreciation or depreciation) made available for operating activities to 5% on a rolling average of the fair value of investments. Any excess above or deficit below the spending rate for the period is recognized as nonoperating activity.

The following summarizes total investment return and its classification in the accompanying financial statements for the years ended September 30, 2006 with comparative totals for 2005:

	2006			2005 Total
	Unrestricted	Temporarily Restricted	Total	
Net dividends and interest	\$ 2,454	\$ 1,919	\$ 4,373	\$ 2,481
Net realized gains	549	297	846	879
Net unrealized appreciation in fair value of investments	1,687	397	2,084	3,132
	4,690	2,613	7,303	6,492
Investment income released from restrictions	2,613	(2,613)	-	-
	7,303	-	7,303	6,492
Less - Investment return - spending rate	5,564	-	5,564	3,925
Nonoperating investment return in excess of spending rate	\$ 1,739	\$ -	\$ 1,739	\$ 2,567

Save the Children Federation, Inc.
Notes to Financial Statements (dollars in thousands)

6. Contributions Receivable, net

Contributions receivable consisted of the following at September 30:

	2006	2005
Pledges receivable		
Due within one year	\$ 9,088	\$ 7,083
Due within two to five years	4,381	7,829
Due beyond five years	600	800
	<u>14,069</u>	<u>15,712</u>
Less - Discount to present value at rates ranging between 4% and 7%	<u>(391)</u>	<u>(718)</u>
Pledges receivable, net	13,678	14,994
Charitable remainder unitrusts receivable, at fair value	1,153	1,182
Bequests receivable	<u>1,646</u>	<u>1,075</u>
Total contributions receivable, net	<u>\$ 16,477</u>	<u>\$ 17,251</u>

7. Conditional Contributions

During fiscal year 2006, SC was awarded a five-year conditional grant totaling \$50,456 restricted for SC's Global Neonatal Survival Initiative. As donor conditions have not yet been met, the balance of cash receipts on this conditional grant, inclusive of unspent investment return, have been included in restricted investments and refundable advances on conditional contributions at September 30, 2006 and 2005.

In fiscal year 2004, SC received a conditional pledge to donate approximately \$10,000 each year for an unspecified time period. These items will be recorded in the financial statements in the fiscal year all related contingencies have been substantially met.

During fiscal year 2006, SC was awarded a six-year conditional grant of \$60,000 for its continued focus on newborn health and mortality. The initial award under the grant of \$10,000 was received in November 2005, with the remaining \$50,000 to be received over the period of the grant, based upon receipt of satisfactory interim requirements.

8. Land, Buildings, and Equipment, Net

Land, buildings, and equipment consisted of the following at September 30:

	2006	2005
Land	\$ 1,027	\$ 1,035
Buildings and improvements	13,057	12,841
Furniture and equipment	12,895	10,312
	<u>26,979</u>	<u>24,188</u>
Less - Accumulated depreciation	(12,019)	(11,007)
Capital projects-in-progress	<u>3,320</u>	<u>686</u>
Total land, buildings, and equipment, net	<u>\$ 18,280</u>	<u>\$ 13,867</u>

Save the Children Federation, Inc.
Notes to Financial Statements (dollars in thousands)

For September 30, 2006 and 2005, within capital projects-in-progress are donated software licenses in the amount of \$2,600 and \$100, respectively. The licenses for this software do not begin to expire until they are placed into service. Accordingly, the related revenue will be released from temporarily restricted assets at the same level as annual depreciation.

9. Pension Plans

SC maintains two defined contribution plans covering all eligible employees. The plans require SC to contribute 4% of each eligible employee's compensation and match 100% of the first 4% contributed by each eligible employee. During fiscal years 2006 and 2005, SC's total pension expense under the defined contribution plans was \$1,823 and \$1,746, respectively.

10. Postretirement Benefits Other Than Pensions

In addition to providing pension benefits, SC provides health care benefits for certain retired employees. To be eligible for these benefits employees must complete at least ten years of service with SC after they reach age 45. SC also provides dental, life, and accidental death and dismemberment benefits for participants who retired before October 1, 1995. SC accrues the expected cost of providing postretirement benefits to employees and their beneficiaries and covered dependents, if applicable, during the years that the employees render service.

The following table sets forth SC's unfunded status and amounts recognized as of and for the year ended September 30:

	2006	2005
Actuarial present value of benefit obligation at September 30	\$ (3,237)	\$ (3,185)
Fair value of plan assets at September 30		
Unfunded status	<u>\$ (3,237)</u>	<u>\$ (3,185)</u>
Accrued benefit cost included in the statement of financial position	\$ 3,312	\$ 3,130
Weighted average assumptions used for obligations as of September 30		
Discount rate	5.66%	5.36%
Rate of compensation increase	-	-
Net periodic cost	\$ 289	\$ 270
Employer contributions	\$ 107	\$ 154
Plan participants' contributions	\$ 207	\$ 246
Benefits paid	\$ 107	\$ 154

The following future benefit payments, which reflect expected future service, as appropriate, are expected to be paid:

2007	231
2008	220
2009	240
2010	239
2011	248
2012-2016	1,279

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The basis for claims costs are future payable medical claims (before administrative expenses) projected from current levels based on the medical trend rate. Current claims levels vary by age and sex and are modeled based on the plan provisions and actual retiree claims history. SC utilizes the RP 2000 White Collar Mortality Tables projected to 2006. The turnover is based on a 3-year select and ultimate table. The medical trend rates do not affect the employer liabilities because of the employer cap effective January 1, 2001 (i.e., retirees pay for cost increases after that time).

On December 8, 2003, the Medical Prescription Drug, Improvement and Modernization Act of 2003 (the "Act") was signed into law. The Act introduces a prescription drug benefit under Medicare Part D as well as a Federal subsidy to employers whose plans provide an "actuarial equivalent" prescription drug benefit.

FASB Staff Position FSP 106-2, *Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003*, has also been issued and requires that employers recognize the Act no later than the first interim measurement date following June 15, 2004. As management decided not to apply for the subsidy, FSP 106-2 had no impact on the fiscal 2005 financial statements.

11. Restricted Net Assets

Temporarily restricted net assets at September 30 are available for the following purposes and periods:

	2006	2005
Field office program activities, including sponsorships	\$ 67,842	\$ 69,712
Other donor restricted for specific program purposes	7,624	2,607
Split-interest agreements	1,670	1,792
Donor-restricted for future periods	10,080	12,003
	<u>\$ 87,216</u>	<u>\$ 86,114</u>

From December 2005 to the end of the current fiscal year, SC has received \$138,000 of revenue in the Asia Earthquake/Tsunami Relief Fund ("AETRF") consisting of \$115,000 in contributions, private grants, and other private revenues and \$23,000 in U.S. government grants and commodities.

AETRF spending is planned over the five-year period from fiscal years 2005 through fiscal years 2009. Accounting principles generally accepted in the United States of America require that contributions be recognized as revenue in the year all substantial conditions are met regardless of when the intended expenses for these funds are incurred. As discussed in Note 2 purpose and time restricted revenue, whereby there are no current fiscal year expenses, is recorded as temporarily restricted revenue. Subsequent expenditures related to these funds are recorded as unrestricted expenses with a release of temporarily restricted net assets to the extent of current fiscal year expenses.

Because of this accounting treatment, it is possible there will be a net decrease in changes in net assets in fiscal years 2007 through 2009 (i.e., annual total deficits) because the full contribution revenue of \$138,000 has been recognized in fiscal years 2006 and 2005, the \$47,100 of unspent funds, as of September 30, 2006, are anticipated to be expended in fiscal years 2007 through 2009. SC has invested the remaining \$47,100 of temporarily restricted net assets and will utilize these funds to satisfy future AETRF expenditures as noted above.

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SC has provided for a columnar approach in the statement of activities to clearly display both temporarily restricted and unrestricted AETRF funds.

The following is a summarized depiction of the AETRF funds and related fiscal year 2006 activities, by net asset classification:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>2006 Total</u>
Operating revenue				
Contributions and private grants	\$ 17,150	\$ 1,325		\$ 18,475
U.S. government grants and contracts	809			809
Commodities and ocean freight	5,409			5,409
Fee for service contracts	1,826			1,826
Investment return - spending rate		1,292		1,292
Total operating revenue	<u>25,194</u>	<u>2,617</u>		<u>27,811</u>
Net assets released from restrictions	<u>10,385</u>	<u>(10,385)</u>		<u>-</u>
Total operating revenue	<u>35,579</u>	<u>(7,768)</u>		<u>27,811</u>
Operating expenses				
Program services				
Program activities	33,789			33,789
Program development and public policy support	206			206
Total program services	<u>33,995</u>			<u>33,995</u>
Supporting services				
Management and general	554			554
Fund raising	1,030			1,030
Total supporting services	<u>1,584</u>			<u>1,584</u>
Total operating expenses	<u>35,579</u>			<u>35,579</u>
Deficit of operating revenue over expenses	-	(7,768)		(7,768)
Nooperating activities				
Foreign currency exchange gain		1,648		1,648
Change in net assets	-	(6,120)		(6,120)
Net assets, beginning of year		53,233		53,233
Net assets, end of year	<u>\$ -</u>	<u>\$ 47,113</u>		<u>\$ 47,113</u>

Permanently restricted net assets at September 30, 2006 and 2005 included \$13,143 and \$10,420, respectively, of permanent endowment funds and \$1,451 and \$1,393, respectively, of beneficial interests in perpetual trusts held by third parties. The income is expendable primarily to support donor-specified purposes such as emergency relief and scholarships.

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12. Lease Commitments

The following is a schedule of minimum future rentals for the next five years and thereafter, for operating leases having initial or remaining noncancelable lease terms as of September 30:

2007	\$	4,492
2008		1,871
2009		1,565
2010		1,457
2011		719
Thereafter		2,002
	\$	<u>12,106</u>

Rent expense, included in Occupancy on the Statement of Expenses by Function, amounted to \$4,454 and \$3,735 for the years ended September 30, 2006 and 2005, respectively.

13. Commitments and Contingencies

SC is involved in various legal proceedings and claims arising in the normal course of business. Management does not expect the ultimate resolution of these actions to have a material adverse effect on SC's financial position.

SC receives funding from governmental agencies for various activities which are subject to audit. Although such audits may result in disallowance of certain expenditures, which would be absorbed by SC, in management's opinion, the ultimate outcome of such audits would not have a significant effect on the financial position, changes in net assets, or cash flows of SC.

14. Significant Funders and Concentrations of Credit Risk

During the fiscal years ended September 30, 2006 and 2005, 95% and 96%, respectively, of revenues from U.S. government grants and contracts were received from the U.S. Agency for International Development (USAID). The operations of SC's programs at present levels are dependent upon continued funding from USAID.

Financial instruments which potentially subject SC to concentrations of credit risk consist principally of cash and cash equivalents and grants and contracts receivable. At September 30, 2006 and 2005, 30% and 31%, respectively, of cash and cash equivalents was deposited in banks in foreign locations. At September 30, 2006 and 2005, 38% and 17%, respectively, of grants and contracts receivable and 26% and 21%, respectively, of deferred amounts under grants and contracts related to USAID.

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15. Program Activities

A summary of program expenses by sector and type for fiscal year 2006, with comparative totals for fiscal year 2005, is as follows:

	Education	Primary Health	HIV/Aids	Economic Opportunity	Food Security and Resource Management	Emergency, Refugee, and Civil Society	2006 Total Program Activities	2005 Total Program Activities
Salaries	\$ 11,248	\$ 9,405	\$ 4,473	\$ 2,650	\$ 7,774	\$ 19,502	\$ 55,052	\$ 46,056
Employee fringe benefits	4,001	3,346	1,591	943	2,765	6,937	19,583	14,740
Payroll taxes	451	377	179	106	311	781	2,205	1,985
Total salaries and related expenses	15,700	13,128	6,243	3,699	10,850	27,220	76,840	62,781
Commodities and ocean freight								
Grants to other agencies	12,264	10,254	4,877	2,890	16,855	29,797	46,652	53,711
Professional fees	1,195	999	475	282	826	2,126	60,025	56,448
Supplies, material, etc.	9,148	7,649	3,638	2,155	6,322	15,860	5,848	5,851
Other project costs	1,816	1,518	722	428	1,255	3,149	44,772	60,235
Telecommunications	707	591	281	166	488	1,225	8,888	7,341
Postage and shipping	735	615	292	173	508	1,277	3,458	2,815
Printing	226	189	90	53	156	394	3,600	2,316
Occupancy	1,884	1,575	749	444	1,302	3,267	1,108	1,157
Travel	5,124	4,284	2,038	1,207	3,541	8,884	9,221	7,045
Depreciation	203	170	81	48	141	353	25,078	21,011
Miscellaneous	271	226	110	66	188	466	996	894
Total program activities	\$ 49,273	\$ 41,198	\$ 19,596	\$ 11,611	\$ 50,908	\$ 115,227	\$ 287,813	\$ 282,991