



Keegan, Linscott & Kenon, PC

Certified Public Accountants
Certified Fraud Examiners
Certified Insolvency & Restructuring Advisors

RESEARCH CORPORATION FOR SCIENCE ADVANCEMENT

FINANCIAL STATEMENTS
AS OF AND FOR THE YEARS ENDED
DECEMBER 31, 2008 AND 2007

RSM! McGladrey Network

An Independently Owned Member

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INDEPENDENT AUDITORS' REPORT

To the Board of Directors
Research Corporation for Science Advancement
Tucson, AZ

We have audited the accompanying statements of financial position of Research Corporation for Science Advancement (the "Foundation") as of December 31, 2008 and 2007, and the related statements of activities and changes in net assets, and cash flows for the years then ended. These financial statements are the responsibility of the Foundation's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our 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 Research Corporation for Science Advancement as of December 31, 2008 and 2007, and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Keegan, Linscott & Kenon, P.C.

Tucson, Arizona
June 23, 2009

KEEGAN, LINSOTT & KENON, PC IS A MEMBER OF RSM MCGGLADREY, INC.

33 N Stone Avenue • Suite 1100 • Tucson, Arizona 85701
(520) 884-0176 • www.klkcpa.com



RSM McGladrey Network
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STATEMENTS OF FINANCIAL POSITION
AS OF DECEMBER 31,

	2008	2007
Assets:		
Investments:		
Investments held in Common Trust Fund	\$ 56,543,104	\$ 106,026,317
Other investments	30,936,545	40,353,270
Program-related investment in Research Corporation Technologies, Inc.	25,000,000	25,000,000
Total investments	112,479,649	171,379,587
Cash and cash equivalents	1,987,535	3,031,977
Accrued dividends and interest receivable	156,482	182,867
Other receivables	1,558,958	1,389,922
Notes receivable	-	19,003
Property and equipment, net	393,034	334,880
Interest in LLC	-	1,820,439
Prepaid pension cost	-	196,639
Other assets	289,466	100,113
Total assets	\$ 116,865,124	\$ 178,455,427
Liabilities and net assets:		
Liabilities:		
Line of credit	\$ 9,625,000	\$ 4,000,000
Accounts payable and accrued expenses	366,858	422,420
LSST liability	325,000	275,000
Grants payable	4,491,692	3,600,476
LBT liability	1,548,970	1,598,194
Pension liability	529,031	-
Postretirement pension liability	1,141,073	1,049,873
Total liabilities	18,027,624	10,945,963
Net assets, unrestricted	98,837,500	167,509,464
Total liabilities and net assets	\$ 116,865,124	\$ 178,455,427

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THESE FINANCIAL STATEMENTS

STATEMENTS OF ACTIVITIES AND CHANGES IN NET ASSETS
FOR THE YEARS ENDED DECEMBER 31,

	2008	2007
Revenues:		
Unrestricted revenues:		
Net realized and unrealized gains and losses on investments	\$ (63,704,610)	\$ 12,875,745
Interest and dividends, net	3,313,263	1,983,283
Interest income from program-related investments	1,750,000	1,750,000
Earnings on investment in LLC	-	179,662
Gain on sale of investment in LLC	1,240,061	-
Other interest and miscellaneous income	23,580	253,275
Total unrestricted revenues	(57,377,706)	17,041,965
Expenses:		
Unrestricted expenses:		
Grants approved	6,345,827	3,748,887
Science advancement	1,637,144	1,430,039
Program-related	325,000	300,000
Information and communications	307,084	361,768
General and administrative	2,046,485	1,387,100
Legal fees	6,057	554,777
Interest	234,040	138,414
Tax expense	392,621	103,790
Total unrestricted expenses	11,294,258	8,024,775
Increase in recurring net assets before effect of adoption of FASB Statement No. 158	(68,671,964)	9,017,190
Nonrecurring gain	-	2,100,000
Increase in net assets before effect of adoption of FASB Statement No. 158	(68,671,964)	11,117,190
Effect of adoption and recognition provisions of FASB Statement No. 158	-	(161,166)
Change in net assets	(68,671,964)	10,956,024
Net assets at beginning of year	167,509,464	156,553,440
Net assets at end of year	\$ 98,837,500	\$ 167,509,464

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THESE FINANCIAL STATEMENTS

STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31,

	2008	2007
Cash flows from operating activities:		
Change in net assets	\$ (68,671,964)	\$ 10,956,024
Adjustments to reconcile change in net assets to net cash used in operating activities:		
Net realized losses (gains) on sales of common trust fund	11,961,132	(18,509,125)
Unrealized (appreciation) depreciation of common trust fund	32,489,966	9,755,408
Unrealized depreciation (appreciation) of other investments	19,253,512	(4,124,780)
Earnings on interest in LLC	-	(179,662)
Gain on sale of investment in LLC	(1,240,061)	-
Depreciation and amortization	90,300	78,700
Gain on rescinded award	-	(2,100,000)
Effect of adoption of FASB statement No. 158	-	161,166
Gain on sale of property and equipment	(100)	-
Change in operating assets and liabilities:		
Accrued dividends and interest receivable	26,385	44,071
Other receivables	(150,033)	(667,109)
Prepaid pension cost	196,639	272,020
Other assets	(189,353)	182,320
LBT liability	(49,224)	(203,718)
Grants payable	891,216	(1,560,062)
Accounts payable and accrued expenses	(55,562)	(179,983)
Accrued LSST Obligation	50,000	(357,000)
Pension liability	529,031	-
Postretirement pension liability	91,200	28,195
Net cash used in operating activities	(4,776,916)	(6,403,535)
Cash flows from investing activities:		
Proceeds from sale of common trust fund investments	5,032,115	5,000,000
Purchase of other investments	(12,675,000)	(8,337,500)
Distributions received from other investments	2,838,213	9,817,317
Distributions received from LLC	3,060,500	237,500
Proceeds received from repayments on notes receivable	-	2,218,240
Proceeds from the sale of property and equipment	100	-
Purchases of property and equipment	(148,454)	(583)
Net cash (used in) provided by investing activities	(1,892,526)	8,934,974
Cash flows from financing activities:		
Borrowings on line of credit	17,534,359	8,545,992
Repayments on line of credit	(11,909,359)	(6,831,843)
Repayments on note payable	-	(1,213,611)
Net cash provided by financing activities	5,625,000	500,538
Net (decrease) increase in cash and cash equivalents	(1,044,442)	3,031,977
Cash and cash equivalents at beginning of year	3,031,977	-
Cash and cash equivalents at end of year	\$ 1,987,535	\$ 3,031,977
Supplemental disclosure of cash flow information:		
Cash paid during the year for interest	\$ 234,040	\$ 161,682
Cash paid during the year for taxes	\$ 551,449	\$ 18,220

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THESE FINANCIAL STATEMENTS

NOTES TO FINANCIAL STATEMENTS

1. Organization

Research Corporation for Science Advancement (the “Foundation”) is a private operating foundation incorporated in the State of New York. The Foundation is dedicated to the advancement of science.

2. Summary of Significant Accounting Policies

Basis of Presentation

The accompanying financial statements have been prepared on the accrual basis of accounting in accordance with standards set forth in Statement of Financial Accounting Standards SFAS No. 117, *Financial Statements of Not-for-Profit Organizations* and the AICPA audit and accounting guide, *Not-for-Profit Organizations*.

The Foundation is required under generally accepted accounting principles to report information regarding its financial position and activities according to three classes of net assets: unrestricted net assets, temporarily restricted net assets, and permanently restricted net assets.

All contributions are considered to be available for unrestricted use unless specifically restricted by the donor. Amounts received that are designated for future periods or restricted by the donor for specific purposes are reported as temporarily restricted support. However, if a restriction is fulfilled in the same time period in which the contribution is received, the Foundation reports the support as unrestricted. Contributions of long-lived assets not having donor imposed time or purpose restrictions are reported as unrestricted contributions in amounts equal to the fair market value of the contributed asset.

Cash and Cash Equivalents

For purposes of reporting cash flows, cash and cash equivalents include cash on hand, demand deposits, savings accounts and highly liquid debt investments purchased with an original maturity of three months or less that are not carried in the Foundation’s portfolio of investments.

The Foundation places its cash and cash equivalents with high credit quality institutions. At times, such investments may be in excess of the FDIC insurance limit; however, management does not believe it is exposed to any significant credit risk on cash and cash equivalents.

Investments

The Foundation carries its investments in the common trust fund at fair value. Realized gains and losses are computed based on the difference between the net proceeds received and cost at time of acquisition using the average cost method. Unrealized net appreciation or depreciation of investments in the common trust fund represents the change in the difference between acquisition cost and current market value at the beginning of the year versus the end of the year, and is recognized currently in the statement of activities and changes in net assets.

Other investments consisting of unconsolidated limited partnership interests are stated at fair value. The cost of investments sold is determined using the specific identification method.

NOTES TO FINANCIAL STATEMENTS

Summary of Significant Accounting Policies (continued)***Investments (continued)***

Investments are considered to be impaired when a decline in fair value is judged to be other-than-temporary. The Foundation employs a systematic methodology on an annual basis that considers available quantitative and qualitative evidence in evaluating potential impairment of our investments. If the cost of an investment exceeds its fair value, we evaluate, among other factors, general market conditions, the duration and extent to which the fair value is less than cost, and our intent and ability to hold the investment. The Foundation also considers specific adverse conditions related to the financial health of and business outlook for the investee, including industry and sector performance, changes in technology, operational and financing cash flow factors, and rating agency actions. Once a decline in fair value is determined to be other-than-temporary, an impairment charge is recorded and a new cost basis in the investment is established.

Property and Equipment

Property and equipment are stated at cost. Depreciation is calculated using the straight-line method over estimated useful lives as follows:

Tenant improvements	10 years
Furniture, fixtures and equipment	5 years
Software	5 years

Maintenance and repairs are charged to expense as incurred. Major renewals and improvements are capitalized.

Interest in LLC

The Foundation's interest in a limited liability company ("LLC") is accounted for under the equity method of accounting, which provides for recognition of the Foundation's proportionate share of the limited liability company's income or loss in its statement of activities and changes in net assets with any distributions received reported as a reduction in the Foundation's interest in the LLC.

Grants Payable

The Foundation accounts for unconditional promises to give, which is normally in the form of grants, as an expense in the year the unconditional promise is made and approved by the Board of Directors, and unpaid promises to give are reported as grants payable.

Revenue Recognition

Interest income is recorded as earned; dividends are accrued as of the ex-dividend date.

Income Taxes

The Foundation qualifies as a tax-exempt private operating foundation under Internal Revenue Code Section 4940(d).

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Significant estimates pertain to the determination of fair value for alternative investments and the Foundation's liability related to the Large Binocular Telescope Project.

NOTES TO FINANCIAL STATEMENTS

Summary of Significant Accounting Policies (continued)

Investment Risk

The Foundation utilizes various investment instruments. Investment securities, in general, are exposed to various risks, such as interest rate, credit and overall market volatility. Due to the level of risk associated with certain investment securities, it is reasonably possible that changes in the values of investment securities will occur in the near term and those changes could materially affect the amounts reported in the statement of financial position.

3. Recent Accounting Pronouncements

In June 2006, the Financial Accounting Standards Board ("FASB") issued Interpretation No. 48 ("FIN 48"), Accounting for Uncertainty in Income Taxes — an interpretation of FASB Statement No. 109. This interpretation clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with FASB Statement No. 109, Accounting for Income Taxes. FIN 48 prescribes a recognition threshold and measurement standard for the financial statement recognition and measurement of an income tax position taken or expected to be taken in a tax return including positions that the organization is exempt from income taxes or not subject to income taxes on unrelated business income. In addition, FIN 48 provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition.

The Foundation's policy is to disclose or recognize income tax positions based on management's estimate of whether it is reasonably possible or probable, respectively, that a liability has been incurred for unrecognized income tax benefits by applying FASB Statement No. 5, Accounting for Contingencies.

The Foundation has elected to defer the application of Interpretation 48 in accordance with FASB Staff Position ("FSP") FIN 48-3. This FSP defers the effective date of Interpretation 48 for nonpublic enterprises included within its scope to the annual financial statements for fiscal years beginning after December 15, 2008. The Foundation will be required to adopt FIN 48 in its fiscal year 2009 annual financial statements. The provisions of FIN 48 are to be applied to all tax positions upon initial application of this standard.

Only tax positions that meet the more-likely-than-not recognition threshold at the effective date may be recognized or continue to be recognized upon adoption. The adoption of FIN 48 is not expected to have a material impact on the Foundation's financial statements. However, the Foundation's conclusions regarding FIN 48 may be subject to review and adjustment at a later date based on on-going analyses of tax laws, regulations, and interpretations thereof and other factors.

NOTES TO FINANCIAL STATEMENTS

Recent Accounting Pronouncements (continued)

In September 2006, the Financial Accounting Standards Board (“FASB”) issued Statement of Financial Accounting Standards No. 157, *Fair Value Measurements* (“SFAS No. 157”). SFAS No. 157 defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurement. SFAS No. 157 also emphasizes that fair value is a market-based measurement, not an entity-specific measurement, and sets out a fair value hierarchy with the highest priority being quoted prices in active markets. Under SFAS No. 157, fair value measurements are disclosed by level within that hierarchy. In February 2008, the FASB issued FASB Staff Position No. 157-2, *Effective Date of FASB Statement No. 157*, which permits a one-year deferral for the implementation of SFAS No. 157 with regard to non-financial assets and liabilities that are not recognized or disclosed at fair value in the financial statements on a recurring basis. The Foundation adopted SFAS No. 157 for the fiscal year beginning January 1, 2008, except for non-financial assets and non-financial liabilities that are recognized or disclosed at fair value in the financial statements on a nonrecurring basis for which delayed application is permitted until the fiscal year beginning January 1, 2009. The adoption of the remaining provisions of SFAS No. 157 is not expected to have material impact on the Foundation’s financial position, results of operations, or cash flows.

In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities* (“SFAS 159”). SFAS 159 permits entities to choose to measure at fair value many financial instruments and certain other items that are not currently required to be measured at fair value. Subsequent changes in fair value for designated items will be required to be reported in earnings in the current period. SFAS 159 also establishes presentation and disclosure requirements for similar types of assets and liabilities measured at fair value. SFAS 159 is effective for financial statements issued for fiscal years beginning after November 15, 2007. During 2008, the Foundation reviewed items eligible for fair value adoption per SFAS 159 and has elected not to adopt the SFAS 159 option.

In December 2008, the FASB issued Staff Position No. FAS 132(R)-1, *Employers’ Disclosures about Postretirement Benefit Plan Assets* (“FSP FAS 132(R)-1”). FSP FAS 132(R)-1 requires more detailed disclosures about employers’ plan assets in a defined benefit pension or other postretirement plan, including employers’ investment strategies, major categories of plan assets, concentration of risk within plan assets, and inputs and valuation techniques used to measure the fair value of plan assets. FSP FAS 132(R)-1 also requires, for fair value measurement using significant unobservable inputs (Level 3), disclosure of the effect of the measurements on changes in plan assets for the period. The disclosures about plan assets required by FSP FAS 132(R)-1 must be provided for fiscal years ending after December 15, 2009. As this pronouncement is only disclosure-related, it will not have an impact on the financial position and results of operations.

4. Fair Value Measurements

Effective January 1, 2008, the Foundation adopted FASB Statement No. 157, *Fair Value Measurements* (“SFAS 157”) for financial assets and liabilities measured at fair value on a recurring basis. This statement provides a definition of fair value which focuses on an exit price rather than an entry price, establishes a framework for measuring fair value which emphasizes that fair value is a market-based measurement, not an entity-specific measurement, and requires expanded disclosure about fair value measurements. In accordance with SFAS 157, the Foundation may use valuation techniques consistent with the market, income, and cost approach to measure fair value. The adoption of SFAS 157 did not have a material impact on the Foundation’s financial position or results of operations on the effective date.

NOTES TO FINANCIAL STATEMENTS

Fair Value Measurements (continued)

To increase consistency and comparability in fair value measurements and related disclosures, the Foundation utilizes the fair value hierarchy required by SFAS 157 which prioritizes the inputs to valuation techniques used to measure fair value into three levels:

Level 1	Valuations based on unadjusted quoted prices in active markets for identical assets or liabilities that the Foundation has the ability to access at the measurement date;
Level 2	Valuations based on quoted prices in markets that are not active or for which all significant inputs are observable, directly or indirectly.
Level 3	Valuations based on inputs that are unobservable and significant to the overall fair value measurement.

Inputs are used in applying the various valuation techniques and broadly refer to the assumptions that market participants use to make valuation decisions, including assumptions about risk. Inputs may include price information, volatility statistics, specific and broad credit data, liquidity statistics, and other factors. The availability of observable inputs can vary from product to product and is affected by a wide variety of factors, including, for example, the type of product, whether the product is new and not yet established in the marketplace, and other characteristics particular to the transaction. To the extent that valuation is based on models or inputs that are less observable or unobservable in the market, the determination of fair value requires more judgment. Accordingly, the degree of judgment exercised by the Foundation in determining fair value is greatest for instruments categorized in level 3. In certain cases, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such cases, for disclosure purposes the level in the fair value hierarchy within which the fair value measurement in its entirety falls is determined based on the lowest level input that is significant to the fair value measurement in its entirety. Fair value is a market-based measure considered from the perspective of a market participant who holds the asset or owes the liability rather than an entity-specific measure. Therefore, even when market assumptions are not readily available, the Foundation's own assumptions are set to reflect those that market participants would use in pricing the asset or liability at the measurement date. The Foundation uses prices and inputs that are current as of the measurement date, including during periods of market dislocation. In periods of market dislocation, the observability of prices and inputs may be reduced for many instruments. This condition could cause an instrument to be reclassified from Level 1 to Level 2 or Level 2 to Level 3.

NOTES TO FINANCIAL STATEMENTS

Fair Value Measurements (continued)

The following table presents the Foundation's financial assets and liabilities that are measured at fair value on a recurring basis at December 31, 2008, consistent with the fair value hierarchy provisions of SFAS No. 157:

Description	12/31/2008	Fair Value Measurements at December 31, 2008 Using:		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Cash and cash equivalents	\$ 1,987,535	\$ 1,987,535	\$ -	\$ -
Investments held in				
Common Trust Fund	56,543,104	54,438,441	2,104,663	-
Other investments	30,936,545	3,284,071	467,173	27,185,301
Total	\$ 89,467,184	\$ 59,710,047	\$ 2,571,836	\$ 27,185,301

The following is a reconciliation of assets which significant unobservable inputs (Level 3) were used in determining fair value:

Description	Fair Value Measurements at December 31, 2008 Using Significant Unobservable Inputs (Level 3)	
	Other Investments	Total
Beginning balance	\$ 36,199,832	\$ 36,199,832
Total gains or losses (realized/unrealized)		
Included in changes in net assets	(17,581,312)	(17,581,312)
Purchases, issuances, and settlements	8,566,781	8,566,781
Transfers in and/or out of Level 3	-	-
Ending balance	\$ 27,185,301	\$ 27,185,301

NOTES TO FINANCIAL STATEMENTS

5. Investments**A. Investments Held in Common Trust Fund**

The Foundation invests in various special purpose funds within the Capital Guardian Common Trust Fund (the "Trust"). The Trust operates as a mutual fund invested in marketable securities and is available only to participants that are exempt from taxation under Internal Revenue Code of 1986 and are qualified institutional buyers and qualified purchasers as defined by applicable securities rules.

Investments consist of the following as of December 31:

	2008		2007	
	Fair Value	Cost	Fair Value	Cost
Capital Guardian Trust Funds:				
Global Equity Fund	\$ 7,613,913	\$16,687,575	\$ 76,280,638	\$64,221,093
Emerging Markets Growth Fund	2,161,318	2,626,717	15,577,092	14,428,302
Absolute Income Grower	39,368,620	47,254,464	10,527,709	10,213,756
U. S. Value Equity Fund	7,399,253	8,965,214	3,640,878	3,664,066
Total	<u>\$ 56,543,104</u>	<u>\$75,533,970</u>	<u>\$106,026,317</u>	<u>\$92,527,217</u>

Net loss or gain on investments consists of the following for the year ended December 31:

	2008	2007
Net realized (loss)/gain on sales of investments	\$ (11,961,132)	\$ 18,509,125
Unrealized net depreciation of investments	(32,489,966)	(9,755,408)
Net (loss)/gain on marketable investments	<u>\$ (44,451,098)</u>	<u>\$ 8,753,717</u>

Proceeds from sale of investments were either reinvested, used to fund purchases of other investments, used to repay line of credit borrowings or to pay grants payable.

Investment fees incurred for the year ended December 31, 2008 and 2007 were \$238,433 and \$344,610, respectively. These fees are reported as a reduction of investment interest and dividend income in the statement of activities.

NOTES TO FINANCIAL STATEMENTS

Investments (continued)**B. Other Investments**

Other investments consist of the following as of December 31:

	2008	2007
Angelo Gordon Super Fund L.P.	\$ 15,572,443	\$ 21,160,975
Angelo Gordon Real Estate Strategies	4,980,490	7,863,942
Angelo Gordon Credit Strategies	6,331,414	2,830,638
Angelo Gordon CLO & Other Debt Strategies	4,052,198	8,497,715
Total other investments	<u>\$ 30,936,545</u>	<u>\$ 40,353,270</u>

Annual activity for other investments consists of the following for the year ended December 31, 2008:

	AG Super Fund	AG Real Estate Strategies	AG Credit Strategies	CLO & Other Debt Strategies	Total 2008
Opening balance	\$21,160,975	\$ 7,863,942	\$ 2,830,638	\$ 8,497,715	\$40,353,270
Capital contributions	-	825,000	6,100,000	5,750,000	12,675,000
Distributions	-	(2,800,000)	(17,510)	(20,703)	(2,838,213)
Appreciation/(depreciation)	(5,588,532)	(908,452)	(2,581,714)	(10,174,814)	(19,253,512)
Ending balance	<u>\$15,572,443</u>	<u>\$ 4,980,490</u>	<u>\$ 6,331,414</u>	<u>\$ 4,052,198</u>	<u>\$30,936,545</u>

A description of the Angelo Gordon (“AG”) funds is as follows:

Angelo Gordon Super Fund L.P.

The AG Superfund L.P. (“AGSF”) is an open-end fund that was established to engage in various strategies including investments in special situations, financially distressed issuers, convertible hedging and real estate. Capital withdrawals may be made annually as of the close of business on the last day of the quarter in which the anniversary of the investment occurs, upon not less than 60 days notice. AG Superfund designates certain illiquid investments as Special Investments (i.e., side pocket investments). Redemption proceeds from capital balances related to the Special Investments are distributed over time as each investment is realized. The Foundation has contributed \$10 million of capital to AGSF. There are no remaining commitments at December 31, 2008. As of December 31, 2008, the fair value hierarchy classification of investments is 16%, 3% and 81% within Level 1, Level 2 and Level 3, respectively.

Angelo Gordon Real Estate Strategies

AG Realty IV, L.P. (“AGRIV”) is a closed-end fund that is in the process undergoing an orderly liquidation of its investments, with some residual assets still being managed by the general partner. The Foundation has contributed \$4.75 million to AGRIV. There are no remaining commitments at December 31, 2008. As of December 31, 2008, all investments are classified as Level 3 within the fair value hierarchy.

NOTES TO FINANCIAL STATEMENTS

Investments (continued)**B. Other Investments (continued)***Angelo Gordon Real Estate Strategies (continued)*

AG Realty V, L.P. (“AGRV”) is a closed-end fund without redemption rights. AGRV’s principle investment objective is current income and capital appreciation through investments in distressed real estate assets, sub-performing and non-performing mortgages. On January 31, 2009, AGRV exercised the first of two available one year extensions to facilitate the orderly liquidation of its investments. The Foundation has contributed \$4.50 million to AGRV. There are no remaining commitments at December 31, 2008. As of December 31, 2008, all investments are classified as Level 3 within the fair value hierarchy.

AG Realty VI, L.P. (“AGRVI”) is a closed-end fund without redemption rights. AGRVI’s principle investment objective is current income and capital appreciation through investments in distressed real estate assets, sub-performing and non-performing mortgages. The primary term of the AGRVI expires on January 10, 2013. Two additional one year extensions are available. The Foundation has contributed \$4.825 million of its \$5 million capital commitment to AGRVI. Open commitments at December 31, 2008 are estimated to be 3.5 percent of committed capital (\$175,000) and are expected to be contributed in the third quarter of 2009. As of December 31, 2008, all investments are classified as Level 3 within the fair value hierarchy.

AG Core Plus Realty Fund L.P. (“AGCPR”), is a closed-end fund without redemption rights. AGCPR’s principle investment objective is current income and capital appreciation through investments in real estate assets. The primary term of the AGCPR expires on May 27, 2013. Two additional one year extensions are available. The Foundation has contributed \$4.75 million of its \$5 million capital commitment to AGCPR. There are no open commitments at December 31, 2008. As of December 31, 2008, all investments are classified as Level 3 within the fair value hierarchy.

Angelo Gordon Credit Strategies

AG Capital Recovery Partners, L.P. (“AGCRP”) is a closed-end fund without redemption rights. AGCRP was established primarily to invest in financially distressed issuers. The primary term of the AGCRP expired on March 14, 2008, at which time AGCRP exercised the first of two available one year extensions to facilitate the orderly liquidation of its investments. The Foundation has contributed \$5 million of capital to AGCRP. There are no remaining commitments at December 31, 2008. As of December 31, 2008, all investments are classified as Level 1 within the fair value hierarchy.

AG Capital Recovery Partners V, L.P. (“AGCRPV”) is a closed-end fund without redemption rights. AGCRPV was established primarily to invest in financially distressed issuers. The primary term of the AGCRPV expires on June 30, 2013. Two additional one year extensions are available. The Foundation has contributed \$5 million of capital to AGCRPV. There are no remaining commitments at December 31, 2008. As of December 31, 2008, all investments are classified as Level 3 within the fair value hierarchy.

AG Capital Recovery Partners VI, L.P. (“AGCRPVI”) is a closed-end fund without redemption rights. AGCRPVI was established primarily to invest in financially distressed issuers. The primary term of the AGCRPVI expires on June 30, 2015. Two additional one year extensions are available. The Foundation has contributed \$4 million of its \$5 million capital commitment to AGCRPVI. Open commitments at December 31, 2008 are estimated to be between 5-10% (\$250,000-\$500,000) of committed capital for the second and third quarters of 2009 and 10-15% (\$500,000-\$750,000) of committed capital for the fourth quarter of 2009 and the first quarter 2010. As of December 31, 2008, the fair value hierarchy classification of investments is 18% and 82% within Level 1 and Level 3, respectively.

NOTES TO FINANCIAL STATEMENTS

Investments (continued)**B. Other Investments (continued)*****Angelo Gordon CLO & Other Debt Strategies***

AG Diversified Credit Strategies Fund Ltd (“AGDCS”) is an open-end fund that was established to execute an absolute, total return investment strategy through investments in non-investment grade credit instruments. Capital withdrawals may be made annually as of the close of business on the last day of the quarter in which the anniversary of the investment occurs, upon not less than 60 days notice. Capital withdrawals are subject to withdrawal reductions of 3% and 2% prior to 2nd anniversary and 3rd anniversary, respectively. The Foundation has contributed \$4 million of capital to AGDCS. There are no remaining commitments at December 31, 2008. As of December 31, 2008, all investments are classified as Level 3 within the fair value hierarchy.

AG Commercial Real Estate Debt Fund, L.P. (“AGREDF”) is a closed-end fund without redemption rights. AGREDF was established primarily to invest in commercial real estate debt securities including commercial mortgage backed securities, REIT debt, real estate operating company debt, and collateralized debt obligations. The primary term of the AGREDF expires on March 28, 2017. Two additional one year extensions are available. The Foundation has contributed \$4.75 million of its \$5 million capital commitment to AGREDF. Open commitments at December 31, 2008 are estimated to be 3% (\$150,000) of committed capital and are expected to be contributed in the third quarter of 2009. As of December 31, 2008, the fair value hierarchy classification of investments is 12% and 88% within Level 1 and Level 3, respectively.

Northwoods Capital VII, Ltd (“NCVII”) and Northwoods Capital VIII, Ltd (“NCVIII”) have maturity dates of October 22, 2021 and July 28, 2022 respectively. The Foundation has committed \$5 million and \$2 million of capital to NCVIII and NCVIII, respectively. There are no remaining commitments at December 31, 2008. As of December 31, 2008, all investments are classified as Level 3 within the fair value hierarchy.

C. Program-Related Investment in Research Corporation Technologies, Inc.

On March 2, 1987, as amended on March 25, 1994, in accordance with Section 1605(c) of the Tax Reform Act of 1986, the Foundation and Research Corporation Technologies, Inc. (“RCT”), a nonprofit corporation subject to regular corporate income tax laws, entered into agreements through which RCT assumed responsibility for the Technology Transfer Program (the “Program”), which the Foundation had operated for many years. In addition to the transfer of the Program, the Foundation transferred \$35,000,000 in cash and securities in exchange for a \$35,000,000 fully subordinated unsecured note from RCT (the “Note”) due February 28, 2017.

RCT has prepaid \$10,000,000 of the Note, and the remaining \$25,000,000 principal amount of the amended Note is due on February 28, 2017, subject to acceleration at the option of the Foundation after December 31, 2012, provided RCT’s retained earnings exceed \$100,000,000. Interest at the rate of 7% per annum on the outstanding principal amount is due semiannually.

To qualify as a program-related investment under Section 4944(c) of the Tax Reform Act of 1986, the terms of the loan were required to be less than prevailing terms. In addition, this investment is a vehicle for the Foundation to continue one of its charter purposes, the furthering of technology.

NOTES TO FINANCIAL STATEMENTS

6. Property and Equipment

Property and equipment consist of the following as of December 31:

	2008	2007
Tenant improvements	\$ 496,312	\$ 377,359
Furniture, fixtures and equipment	193,478	163,978
Software	108,401	108,401
	798,191	649,738
Less accumulated depreciation	405,157	314,858
Property and equipment, net	\$ 393,034	\$ 334,880

Depreciation expense was \$90,300 and \$78,700 for 2008 and 2007, respectively.

7. Investment in LLC

Prior to January 2008, the Foundation had a 50% interest in 4703 Camp Lowell, LLC, an Arizona Limited Liability Company (the "LLC"), whose principal activity is ownership of the office building, which the Foundation partially utilizes for its operations (see Note 9). At December 31, 2007, the Foundation recognized income of \$179,662 which represented its proportionate share of the LLC's 2007 net income. The Foundation received \$237,500 in cash distributions from the LLC during 2007.

The LLC finalized the sale of the office building on January 17, 2008 to an unrelated party. As a result of the sale, the Foundation received \$3,060,500 in cash distributions and realized a \$1,240,061 gain in 2008 which is reported as a gain on sale of investment in LLC in the accompanying statement of activities. Consequently, at December 31, 2008, the Foundation no longer has an interest in the LLC. There were no changes made to the Foundation's facility lease agreement as a result of the sale of the office building.

8. Line of Credit

The Foundation has a \$15,000,000 uncollateralized revolving line of credit with interest at LIBOR plus 1.0% (3% at December 31, 2008). Borrowings against the line of credit totaled \$9,625,000 and \$4,000,000 in 2008 and 2007, respectively. The Foundation incurred interest expense of \$234,040 and \$138,414 for the years ended December 31, 2008 and 2007, respectively.

The revolving line of credit agreement contains certain covenants, the most restrictive of which requires the Foundation to maintain a tangible net worth of \$110 million as defined by the agreement. At December 31, 2008, the Foundation did not meet its tangible net worth covenant. Consequently, the Foundation obtained a loan modification, effective March 26, 2009, whereby interest was amended to LIBOR plus 2.0% and the covenants were amended. The most restrictive of the amended covenants requires the Foundation to maintain a tangible net worth of \$80 million. At December 31, 2008, the Foundation was in compliance with the amended loan covenants.

NOTES TO FINANCIAL STATEMENTS

9. Operating Leases

The Foundation leases approximately 33% of 4703 Camp Lowell, LLC, a related party (see Note 7), under a 10-year non-cancelable operating lease, which expires in 2013. In March 2004, the Foundation entered into an arrangement to lease an additional 17% of the building and sublet the additional space at identical terms to the LSST Corporation, a related party. Rental expense was \$262,300 and \$228,327 in 2008 and 2007, respectively.

LSST early vacated the premises during April 2008. Pursuant to its sublease, the Foundation holds a rent deposit from LSST. The rent deposit of \$146,672 and \$202,050 at December 31, 2008 and 2007, respectively, is reported as a liability in the accompanying financial statements. The Foundation does not expect to incur any losses due to the early termination of the sublease agreement since it is recouping lost rents and re-leasing costs against the rent deposit. The Foundation expects to sublease the premises under similar terms.

Future minimum rental payments under the lease as of December 31, 2008 are as follows:

2009	\$	306,525
2010		306,525
2011		306,525
2012		306,525
2013		306,525

10. Related Party Transactions***LSST Project***

LSST Corporation was formed to build a large-aperture synoptic survey telescope. The LSST Corporation is a 501(c)(3) organization made up of universities and other not-for-profit organizations focused on astronomy, of which the Foundation is a 1/16th member. During the years ended December 31, 2008 and 2007 Research Corporation for Science Advancement made cash contributions of approximately \$325,000 and \$300,000 to LSST. At December 31, 2008 and 2007, the amount payable to LSST totaled \$325,000 and \$275,000, respectively. The Foundation had granted LSST \$2.1 million in 2006 for the purpose of funding a mirror. LSST was able to fund this mirror with alternative funding. Consequently, the Foundation rescinded the \$2.1 million grant which is reported as a nonrecurring gain in the accompanying statement of activities and changes in net assets as of December 31, 2007.

11. Pension Plan and Postretirement Benefits***Defined Contribution Pension Plan***

The Foundation maintains a noncontributory defined contribution plan, eligible to all employees hired after June 1, 2005 who have completed one year of employment. The Foundation makes fully vested contributions ranging from 10% - 15%, based on years of experience, for all participating employees. The Foundation incurred defined contribution plan expenses of \$29,992 and \$27,726 for the years ended December 31, 2008, and 2007, respectively.

NOTES TO FINANCIAL STATEMENTS

Pension Plan and Postretirement Benefits (continued)***Defined Benefit Pension Plan***

The Foundation maintains a noncontributory defined benefit pension plan (the "Plan"), which covers 45% of its employees at the 2008 measurement date. The benefits provided by the Plan are generally based on years of service and employees' salary history. It is the Foundation's policy to contribute amounts sufficient to at least meet the Employee Retirement Income Security Act's minimum funding requirements.

During the year ended December 31, 2007, the Company adopted SFAS No. 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans*. This statement requires employers to recognize the funded status of a benefit plan in the statement of financial position and recognize changes in the funded status through beginning net assets.

The following table illustrates the incremental effect of applying FASB Statement No. 158 on individual line items in the statement of financial position as of December 31, 2007:

	<u>Pre-Statement 158</u>	<u>Adjustments</u>	<u>Statement 158 Implementation</u>
Prepaid pension cost	\$ 406,985	\$ (210,346)	\$ 196,639
Total assets	178,665,773	(210,346)	178,455,427
Net assets	167,719,810	(210,346)	167,509,464

The following table sets forth the funded status of the plan and amounts recognized in the Foundation's accompanying statements of financial position as of December 31:

	<u>2008</u>	<u>2007</u>
Projected benefit obligations for services rendered to date	\$ (1,372,360)	\$ (1,588,710)
Fair value of plan assets	843,329	1,785,349
Funded Status/Net amount recognized in the statements of financial position	<u>\$ (529,031)</u>	<u>\$ 196,639</u>

The following table reflects the components of net periodic benefit cost for the years ending December 31:

	<u>2008</u>	<u>2007</u>
Service cost	\$ 220,295	\$ 229,943
Interest cost	85,155	107,141
Expected return on assets	(104,932)	(150,751)
Amortization of prior service costs	32,007	36,507
Amortization of loss	3,266	-
	<u>\$ 235,791</u>	<u>\$ 222,840</u>

Amortization of prior service costs that will be recognized into net periodic benefit cost during the year ended December 31, 2009 is \$32,007.

NOTES TO FINANCIAL STATEMENTS

Pension Plan and Postretirement Benefits (continued)**Defined Benefit Pension Plan (continued)**

The following table reflects the amounts that have not yet been recognized as components of net periodic benefit cost:

	2008	2007
Unrecognized prior service cost	\$ (345,981)	\$ (385,989)
Unrecognized net (loss)/gain	(380,773)	126,799

Plan assets were fully invested in a balanced mutual fund as of December 31, 2008 and 2007, which is consistent with the Foundation's investment policy.

Assumptions used in the accounting for the pension plan as of December 31:

	2008	2007
Discount rate	6.50%	6.00%
Rate of increase in compensation levels	4.25%	4.25%
Expected long-term rate of return on assets	7.50%	7.50%

The expected long-term rate of return on assets was based on expected future rates of return and average historical returns.

Pertinent information related to the Plan is as follows:

	2008	2007
Accumulated benefit obligation	\$ 1,011,007	\$ 1,291,724
Net periodic benefit cost	235,791	222,840
Foundation contributions	-	-
Benefits paid	578,453	194,048

Benefits payments expected to be paid in each of the next five fiscal years, and in the aggregate for the next five fiscal years are as follows:

2009	\$ 5,729
2010	5,794
2011	5,847
2012	858,158
2013	6,807
2014 through 2018	92,364
Total	<u>\$ 974,699</u>

The Foundation expects to contribute \$200,000 to the Plan in 2009.

In 2006, the Foundation froze entry into its noncontributory defined benefit pension plan to all employees hired after June 1, 2005.

NOTES TO FINANCIAL STATEMENTS

Pension Plan and Postretirement Benefits (continued)***Postretirement Plan***

In addition to providing pension benefits, the Foundation provides certain health care benefits to retired employees and their spouses. One of the Foundation's employees may become eligible for these benefits if the normal retirement age is met while working for the Foundation. Estimated contributions to the plan for 2009 are \$108,168.

During the year ended December 31, 2007, the Company adopted SFAS No. 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans*. This statement requires employers to recognize the funded status of a benefit plan in the statement of financial position and recognize changes in the funded status through beginning net assets.

The following table illustrates the incremental effect of applying FASB Statement No. 158 on individual line items in the statement of financial position as of December 31, 2007:

	<u>Pre-Statement 158</u>	<u>Adjustments</u>	<u>Statement 158 Implementation</u>
Postretirement pension liability	\$ 1,099,053	\$ (49,180)	\$ 1,049,873
Total liabilities	10,995,143	(49,180)	10,945,963
Net assets	167,460,284	49,180	167,509,464

The following table sets forth the funded status of the plan and amounts recognized in the foundations accompanying statements of financial position as of December 31:

	<u>2008</u>	<u>2007</u>
Accumulated benefit obligation	\$ (1,141,073)	\$ (1,049,873)
Plan assets at fair value	-	-
Funded status	(1,141,073)	(1,049,873)
Unrecognized net gain subsequent to transition	-	-
Unrecognized transition obligations	-	-
Accrued postretirement benefit liability	<u>\$ (1,141,073)</u>	<u>\$ (1,049,873)</u>

The following table reflects the components of net periodic benefit cost for the years ending December 31:

	<u>2008</u>	<u>2007</u>
Service cost	\$ 31,590	\$ 30,591
Interest cost	63,837	58,238
Amortization of transition obligation	75,812	75,812
Amortization of gains	(43,658)	(28,636)
Net periodic benefit cost	<u>\$ 127,581</u>	<u>\$ 136,005</u>

Amortization of the net obligation and net gain that will be recognized into net periodic benefit cost during the year ended December 31, 2009 is \$75,812.

NOTES TO FINANCIAL STATEMENTS

Pension Plan and Postretirement Benefits (continued)***Postretirement Plan (continued)***

The following table reflects the amounts that have not yet been recognized as components of net periodic benefit cost:

	2008	2007
Net gain	\$ 561,423	\$ 655,677
Net transition obligation	511,732	606,497

Pertinent information related to benefits for the plan is as follows:

	2008	2007
Net periodic benefit cost	\$ 127,581	\$ 136,005
Foundation contributions	53,895	58,630
Benefits paid	53,895	58,630

Benefits payments expected to be paid in each of the next five fiscal years, and in the aggregate for the next five fiscal years are as follows:

2009	\$ 108,168
2010	111,518
2011	123,923
2012	124,807
2013	128,133
2014 through 2018	358,155
Total	\$ 954,704

The actuarial calculations in 2008 assume a dental inflation assumption of 4.5% and a medical inflation assumption of 8% decreasing uniformly to 5% over 6 years. The assumed discount rate is 6.15%. The health care cost trend rate assumptions impact the service and interest cost and the accumulated benefit obligation. A 1% increase in these rates would increase service and interest cost by approximately \$9,600 and the accumulated benefit obligation by approximately \$96,800, while a 1% decrease would decrease service and interest cost by approximately \$8,200 and decrease the accumulated benefit obligation by approximately \$82,800.

The actuarial calculations in 2007 assume a dental inflation assumption of 4.5% and a medical inflation assumption of 7.25% decreasing uniformly to 4.5% over 4 years. The assumed discount rate is 6.0%. The health care cost trend rate assumptions impact the service and interest cost and the accumulated benefit obligation. A 1% increase in these rates would increase service and interest cost by approximately \$10,200 and the accumulated benefit obligation by approximately \$85,000, while a 1% decrease would decrease service and interest cost by approximately \$8,500 and decrease the accumulated benefit obligation by approximately \$73,000.

During the year ended December 31, 2006, the Foundation froze eligibility for participation in its postretirement plan to those employees hired before June 1, 2005.

NOTES TO FINANCIAL STATEMENTS

Pension Plan and Postretirement Benefits (continued)***Postretirement Plan (continued)***

During the year ended December 31, 2006, the Foundation established a flexible benefits plan whereby it will contribute 10% of employee compensation on behalf of employees to be used for medical, retirement, education and other expenses. Employees hired after June 1, 2005 are automatically enrolled in the new plan after completion of three months service. Employees hired before June 1, 2005 who chose to elect out of the postretirement plan are eligible for this new plan.

12. Commitments and Contingencies***Large Binocular Telescope (“LBT”) Project***

The Foundation is a partner with a 12.5% interest in the Large Binocular Telescope Project (the “Project”), which is building and managing an astronomical observatory. The Foundation has sold or granted to other astronomy research institutions (the “Institutions”) all of its viewing rights in the observatory along with the obligation to pay related operating costs under various agreements. The Foundation remains liable for its proportionate share of observatory construction and certain other project development costs and has accrued its best estimate of these costs.

The Foundation remains contingently liable for its proportionate share of future commissioning, operating and instrumentation costs, to the extent the Institutions become unable to pay and forfeit their viewing rights or in the event these costs exceed any caps specified in the agreement with the Institutions. In addition, the Foundation’s agreement with one of the Institutions contains an escape clause, which would allow that Institution the right to rescind the agreement and recover all capital payments made. In the event that occurs, the Foundation would re-assume the viewing rights forfeited and be liable for future commissioning, operating and instrumentation costs. Management believes that the Institution would exercise its escape clause only in the event the Project does not achieve its scientific objectives, the likelihood of which Management believes is highly unlikely.

The Institution with an escape clause in its agreement has made a total of \$2.1 million in capital payments through December 31, 2008.

Excise Taxes

During 2003, the Foundation terminated a pension plan, and replaced it with their current Plan, the Research Corporation Employee’s Replacement Plan (the “Replacement Plan”). Accumulated benefits totaling approximately \$3,600,000 under the Plan were paid out to participants. The remaining Plan assets of \$5,061,653 reverted to the Foundation, of which \$1,470,818 was contributed to fund the Replacement Plan. In 2005, the Internal Revenue Service (“IRS”) sent Research Corporation a draft verification of facts letter that the Foundation might owe approximately \$879,000 in additional excise tax with respect to the reversion, plus interest and penalties. On December 12, 2007, the Foundation received a 30-day letter from the IRS claiming a deficiency of \$879,000 and penalties of \$219,000. The management of the Foundation in consultation with its external legal counsel believes they are exempt from the reversion tax and timely notified the IRS of such, including a request for appeal. During 2008, the IRS requested an extension of the examination period until December 31, 2009, which the Foundation granted.