The F.B. Heron Foundation

Financial Statements

December 31, 2006 and 2005

Independent Auditors' Report

The Board of Directors
The F.B. Heron Foundation

We have audited the accompanying statements of financial position of The F.B. Heron Foundation (the Foundation) as of December 31, 2006 and 2005, and the related statements of activities and cash flows for the years then ended. These financial statements are the responsibility of the Foundation's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Foundation's internal control over financial reporting. Accordingly, we express no such opinion. An audit 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 The F.B. Heron Foundation as of December 31, 2006 and 2005, and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Our 2006 audit was made for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplementary information included in schedule 1 is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the 2006 basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the 2006 basic financial statements taken as a whole.

New York, New York
March 26, 2007

The F.B. Heron Foundation

Statements of Financial Position

December 31, 2006 and 2005

	2006	2005
ASSETS		
Cash and cash equivalents	$ 2,500,912	$ 498,845
Traditional investments	238,664,076	220,201,187
Mission-related investments	65,093,288	58,502,393
Other assets	435,234	467,068
Property and equipment, net	164,803	226,654
	$ 306,858,313	$ 279,896,147
LIABILITIES AND NET ASSETS		
Liabilities		
Accounts payable and accrued expenses	$ 152,838	$ 101,526
Grants payable	4,540,000	3,017,500
Deferred Federal excise tax payable	417,648	197,778
Total Liabilities	5,110,486	3,316,804
Unrestricted net assets	301,747,827	276,579,343
	$ 306,858,313	$ 279,896,147

See notes to financial statements.

The F.B. Heron Foundation

Statements of Activities

Years Ended December 31, 2006 and 2005

	2006	2005
NET INVESTMENT INCOME		
Interest and dividends	$ 7,953,753	$ 7,228,411
Investment expenses	(1,448,409)	(1,030,893)
Current Federal excise tax	(336,836)	(318,000)
Net Investment Income	6,168,508	5,879,518
EXPENSES		
Program services		
Grants	10,623,610	11,960,523
Program expenses	1,941,194	1,720,057
Total Program Services	12,564,804	13,680,580
Administrative expenses	444,427	472,710
Total Expenses	13,009,231	14,153,290
Appreciation in fair value of investments, net of deferred Federal excise tax	32,009,207	14,723,415
Change in Net Assets	25,168,484	6,449,643
NET ASSETS		
Net assets at beginning of year	276,579,343	270,129,700
Net assets at end of year	$ 301,747,827	$ 276,579,343

See notes to financial statements.

The F.B. Heron Foundation

Statements of Cash Flows

Years Ended December 31, 2006 and 2005

	2006	2005
CASH FLOWS FROM OPERATING ACTIVITIES		
Change in net assets	$ 25,168,484	$ 6,449,643
Adjustments to reconcile change in net assets to net cash used in operating activities:		
Depreciation and amortization	61,851	67,845
Net (appreciation) in fair value of investments	(32,229,077)	(14,612,447)
Increase (decrease) in Deferred Federal excise tax	219,870	(110,968)
Changes in operating assets and liabilities		
Other assets	31,834	(63,320)
Accounts payable and accrued expenses	51,312	27,061
Grants payable	1,522,500	302,500
Net Cash Used in Operating Activities	(5,173,226)	(7,939,686)
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of traditional investments	(34,549,402)	(244,484,387)
Proceeds from traditional investments sold	45,690,764	262,888,524
Purchases of mission-related investments	(13,136,726)	(24,139,362)
Proceeds from mission-related investments sold or repaid	9,170,657	11,681,034
Net Cash Provided by Investing Activities	7,175,293	5,945,809
Net increase (decrease) in cash and cash equivalents	2,002,067	(1,993,877)
CASH AND CASH EQUIVALENTS		
Beginning of year	498,845	2,492,722
End of year	$ 2,500,912	$ 498,845
SUPPLEMENTAL DISCLOSURE		
Federal excise tax paid	$ 325,000	$ 306,000

See notes to financial statements.

The F.B. Heron Foundation

Notes to Financial Statements

1. Organization and Summary of Significant Accounting Policies

Organization

The F.B. Heron Foundation (the Foundation) is a not-for-profit, charitable corporation formed in December 1991 under the General Corporation Law of the State of Delaware. The Foundation is exempt from income tax under Section 501(c)(3) of the Internal Revenue Code (the Code) and is classified as a private foundation under Section 509(a) of the Code.

To advance its mission of helping people and communities to help themselves, the Foundation supports organizations that help people with low income to create wealth and take control of their lives. The Foundation makes grants to and investments in organizations engaged in the following wealth-creation strategies for urban and rural communities: advancing home ownership; supporting enterprise development; reducing the barriers to full participation in the economy by providing quality child care; increasing access to capital; and employing comprehensive community development approaches with a strong focus on the wealth-creation strategies noted above.

2. Summary of Significant Accounting Policies

Basis of Accounting

The accompanying financial statements are prepared on the accrual basis.

Basis of Presentation

Net assets and revenues, expenses, gains and losses are classified based on the existence or absences of donor-imposed restrictions. Accordingly, net assets are classified as permanently restricted, temporarily restricted or unrestricted. All of the activity and net assets of the Foundation are unrestricted.

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 disclosures of contingencies 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.

2. Summary of Significant Accounting Policies (*Continued*)

Cash Equivalents

Cash equivalents include short-term investments with maturities of three months or less at the time of purchase, which are intended to be used for payment of expenses and grants and exclude those amounts used by investment managers for long-term investment strategies.

Investments

Investments (both traditional and mission-related), with the exception of program-related investments, are stated at fair value. For marketable securities, fair value is determined by the last sales price reported by a national securities exchange. For other fixed-income and equity funds, the fair value is determined and reported by the fund manager or custodian. For limited partnerships, fair value is the latest value reported by the partnerships adjusted for any cash transactions occurring between the reported date and the balance sheet date. Because of the inherent uncertainty of valuation for limited partnerships, estimated values may differ significantly from the values that would have been used had a ready market for the entities existed. For insured deposits, fair value is the amount of the deposit. Program related investments are stated at cost.

Property and Equipment

Property and equipment are capitalized at cost and are being depreciated over seven years and five years, respectively. Leasehold improvements have been capitalized at cost less amounts reimbursed by the landlord, and are being amortized over the life of the lease, which is ten years.

Grants

Grants are recorded when approved by the board of directors, unless conditions imposed on the grantee have not been fulfilled. Such conditional grants are recorded when the conditions have been satisfied. All multiyear grants are subject to review and approval of program and financial reports, a work plan, and a budget for the ensuing period of the grant.

3. Traditional Investments

At December 31, 2006 and 2005, traditional investments consisted of the following:

	2006		2005	
	Fair value	**Cost**	**Fair value**	**Cost**
Invested cash and cash equivalents	$ 1,177,938	$ 1,177,938	$ 29,231	$ 29,231
Fixed-income securities	46,141,421	47,109,241	51,119,259	53,130,546
Common and preferred stock and stock and equity funds	191,344,717	151,186,108	169,052,697	147,516,985
	$ 238,664,076	$ 199,473,287	$ 220,201,187	$ 200,676,762

4. Mission-Related Investments

Mission-related investments advance the mission of the Foundation using the core program strategies articulated in note 1. These include both risk-adjusted, market rate investments that advance the mission and program-related investments (PRIs).

PRIs, defined in IRC 4944(c), have a primary purpose of advancing the mission of the Foundation without a significant purpose of the production of income or the appreciation of property. PRIs are treated as charitable distributions on Internal Revenue Service form 990-PF, the tax and information return filed by private foundations for minimum-distribution requirement purposes. The Foundation's PRI loans bear interest at below-market rates, from 1% to 6%, generally payable on March 31 and September 30 of each year. Five PRIs are limited partnerships interests in community development venture funds and two are preferred stock in regulated community development banks. The Foundation expects to hold all PRIs to maturity.

4. Mission-Related Investments (*Continued*)

At December 31, 2006 and 2005, mission-related investments consisted of the following:

	2006		2005	
	Fair or carrying value	**Cost**	**Fair or carrying value**	**Cost**
Invested cash and cash equivalents	$ 1,237,528	$ 1,237,528	$ 487,116	$ 487,116
Insured deposits in low income designated Credit Unions and Community Development Banks	5,800,000	5,800,000	5,000,000	5,000,000
Fixed-income securities	19,926,436	20,072,130	19,743,300	19,718,494
Common and preferred stock	11,681,563	10,193,999	10,221,087	10,013,091
Limited partnership interests	7,492,867	6,260,731	5,474,846	5,454,314
Program-related investments	18,954,894	18,954,894	17,576,044	17,576,044
	$ 65,093,288	$ 62,519,282	$ 58,502,393	$ 58,249,059

At December 31, 2006 and 2005, the Foundation had capital commitments of approximately $4,752,000 and $8,546,000, to mission-related limited partnerships.

The following summarizes changes in PRIs as of December 31, 2006 and 2005:

	2006	2005
Balance at beginning of year	$ 17,576,044	$ 16,977,391
Disbursements	4,000,000	3,353,234
Collections	(2,621,150)	(2,754,581)
Balance at end of year	$ 18,954,894	$ 17,576,044

4. Mission-Related Investments (*Continued*)

PRI principal repayments are scheduled as follows:

2007	$	2,877,418
2008		1,585,000
2009		2,719,500
2010		3,000,000
2011		3,272,976
Thereafter		5,500,000
	$	18,954,894

5. Property and Equipment

Property and equipment consisted of the following at December 31, 2006 and 2005:

		2006		**2005**
Leasehold improvements	$	446,255	$	446,255
Furniture		120,581		120,581
Equipment		59,948		59,948
		626,784		626,784
Accumulated depreciation and amortization		(461,981)		(400,130)
	$	164,803	$	226,654

6. Grants Payable

The following summarizes changes in grants payable as of December 31, 2006 and 2005:

		2006		**2005**
Balance at beginning of year	$	3,017,500	$	2,715,000
Grants authorized		10,623,610		11,960,523
Grants paid		(9,101,110)		(11,658,023)
Balance at end of year	$	4,540,000	$	3,017,500

7. Federal Excise Tax

As a private foundation, the Foundation is normally subject to a Federal excise tax equal to 2% of its net investment income for tax purposes. However, under Section 4940(e) of the Code, this tax is reduced to 1% if certain conditions are met. Since the Foundation failed to meet the requirements for the reduced tax rate in 2006, current taxes are estimated at 2% of net investment income, as defined in the Code. In 2005, the Foundation qualified for the 1% rate.

Deferred taxes are recorded on the unrealized appreciation of investments using the Foundation's normal excise tax rate of 1%. For 2006 and 2005, deferred taxes were $417,648 and $197,778.

For Federal excise tax purposes, realized gains and losses from the sale of securities are determined on the specific-identification basis. Net realized gain or loss on funds is based on the Foundation's allocated share, and, on sale, average cost is used. In 2006 and 2005, realized gains for tax purposes were $10,242,041 and $25,709,255. Unrealized gains are recorded net of deferred excise taxes.

8. Lease Commitment

In November 1999, the Foundation entered into a lease agreement expiring August 31, 2010 for office space. The future minimum rental payments under this agreement are as follows:

2007	$ 325,900
2008	325,900
2009	325,900
2010	220,000
	$ 1,197,700

Rent expense for 2006 and 2005 was $336,987 and $313,762.

9. Retirement Plans

The Foundation sponsors a defined contribution retirement plan under Section 401(a) of the IRC in which all employees, as defined, are eligible to participate. The Foundation is obligated to contribute 12% of the employee's basic compensation for all eligible employees. The Foundation also sponsors a 401(k) savings plan. Eligible participants, as defined, may make voluntary contributions into the savings plan. The Foundation is obligated to match 50% of participant contributions, not to exceed 3% of base compensation. For 2006 and 2005 the Foundation expense was $188,807 and $182,322.

In 2006, the Foundation also established a qualified deferred compensation plan for its President. Contributions to the plan were $15,000.

SUPPLEMENTAL SCHEDULE OF PROGRAM, ADMINISTRATIVE AND INVESTMENT EXPENSES

The F.B. Heron Foundation

Schedule of Program, Administrative and Investment Expenses

Year ended December 31, 2006

	Program	Administrative	Investment	Total
Salary and related costs	$ 1,304,826	$ 285,385	$ 453,711	$ 2,043,922
Consulting fees	172,430	27,731	37,657	237,818
Equipment rental and repair	12,619	2,760	4,338	19,717
Office expenses	37,331	8,166	12,833	58,330
Occupancy	229,081	50,112	78,747	357,940
Travel, meetings, and conferences	94,803	16,578	27,597	138,978
Telephone	10,576	2,314	3,635	16,525
Legal fees	15,105	30,496	28,204	73,805
Audit expenses	8,695	8,695	8,958	26,348
Insurance	16,143	3,531	5,549	25,223
Depreciation and amortization	39,585	8,659	13,607	61,851
Custody fees	-	-	54,985	54,985
Investment, management and advisory	-	-	718,588	718,588
	$ 1,941,194	$ 444,427	$ 1,448,409	$ 3,834,030

See independent auditors' report.