Financial Statements

REPORT OF INDEPENDENT AUDITORS

To the Board of Trustees of
The Andrew W. Mellon Foundation:

In our opinion, the accompanying balance sheets and the related statements of activities and cash flows present fairly, in all material respects, the financial position of The Andrew W. Mellon Foundation (the "Foundation") at December 31, 2007 and 2006, 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. These financial statements appearing on pages 122 through 132 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 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 audits provide a reasonable basis for our opinion.

PricewaterhouseCoopers LLP

May 22, 2008
New York, New York

The Andrew W. Mellon Foundation

Balance Sheets
December 31, 2007 and 2006

	2007	*2006*
	(in thousands)	
ASSETS		
Investments		
Marketable securities	$ 3,378,517	$ 3,542,133
Limited liquidity investments	2,692,836	2,145,404
	6,071,353	5,687,537
Payable from unsettled securities purchases, net	(87,089)	(148,940)
	5,984,264	5,538,597
Cash	2,676	772
Collateral under securities loan agreement	486,749	524,382
Investment and other income receivable	7,470	10,405
Other assets	1,188	1,060
Taxes receivable	4,817	—
Property, at cost, less accumulated depreciation of $12,379 and $10,630 at December 31, 2007 and 2006, respectively	52,701	55,632
Total assets	$ 6,539,865	$ 6,130,848
LIABILITIES AND NET ASSETS		
Liabilities		
Grants payable	$ 4,289	$ 11,360
Accrued expenses	6,473	6,609
Payable under securities loan agreement	486,749	524,382
Deferred federal excise tax	23,100	22,200
Taxes payable	—	3,754
Long term debt	44,000	44,000
Total liabilities	564,611	612,305
Net assets (unrestricted)	5,975,254	5,518,543
Total liabilities and net assets	$ 6,539,865	$ 6,130,848

The accompanying notes are an integral part of these financial statements.

The Andrew W. Mellon Foundation

Statements of Activities

Years Ended December 31, 2007 and 2006

	2007	2006
	(in thousands)	
INVESTMENT RETURN		
Gain on investments		
Realized, net	$ 684,367	$ 644,582
Unrealized, net	51,358	172,290
Interest	19,871	18,231
Dividends	44,390	42,154
Other income	559	18,872
	800,545	896,129
Less: Investment management expenses	(20,697)	(19,152)
Net investment return	779,848	876,977
EXPENSES		
Program grants and contributions, net	292,507	180,803
Grantmaking operations	14,590	13,487
Direct charitable activities	5,288	6,803
Investment operations	4,898	5,134
Current provision for taxes	5,649	15,163
Other expenses	205	315
	323,137	221,705
Change in net assets	456,711	655,272
Net assets (unrestricted) at beginning of year	5,518,543	4,863,271
Net assets (unrestricted) at end of year	$ 5,975,254	$ 5,518,543

The accompanying notes are an integral part of these financial statements.

The Andrew W. Mellon Foundation

Statements of Cash Flows
Years Ended December 31, 2007 and 2006

	2007	2006
	(in thousands)	
Cash flow from investment income and operations		
Interest and dividends received	$ 72,014	$ 67,997
Other income received	2,525	18,766
Grant refunds received	621	1,321
Grants and contributions paid	(300,199)	(176,129)
Investment expenses paid	(20,807)	(19,475)
Salaries and other operating expenses paid	(22,478)	(22,153)
Taxes paid	(14,220)	(12,500)
Net cash used by investment income and operations	(282,544)	(142,173)
Cash flow from investing activities		
Proceeds from sales of marketable securities		
Short-term	1,116,531	1,642,024
Other	4,319,850	4,164,170
Receipts from limited liquidity investments	476,246	332,153
Capital gain distributions received	53,591	30,820
Net returns on financial instruments	(1,161)	(773)
Purchases of marketable securities		
Short-term	(1,054,849)	(1,583,543)
Other	(3,989,391)	(3,707,158)
Purchases of limited liquidity investments	(637,000)	(734,845)
Disposals of (additions to) property	631	(2,228)
Net cash provided by investing activities	284,448	140,620
Net increase (decrease) in cash	1,904	(1,553)
Cash		
Beginning of year	772	2,325
End of year	$ 2,676	$ 772
Supplemental disclosure of noncash investing activities		
Distributions of securities received from limited liquidity investments	$ 27,276	$ 27,835

The accompanying notes are an integral part of these financial statements.

The Andrew W. Mellon Foundation

Statements of Cash Flows (continued)

Years Ended December 31, 2007 and 2006

Reconciliation of Change in Net Assets to Net Cash Used by Investment Income and Operations

	2007	2006
	(in thousands)	
Change in net assets	$ 456,711	$ 655,272
Adjustments to reconcile change in unrestricted net assets to net cash used by investment income and operations		
Realized gain on investments, net	(684,367)	(643,641)
Unrealized gain of investments, net	(52,258)	(175,890)
Decrease (increase) in investment and other income receivable	2,935	(1,437)
(Increase) decrease in other assets	(128)	496
(Decrease) increase in grants payable	(7,071)	4,895
(Decrease) increase in accrued expenses	(136)	138
Depreciation and amortization expense	2,657	2,630
Increase in deferred federal excise tax payable	900	3,600
(Increase) decrease in net taxes receivable	(8,571)	2,658
Net effect of bond amortization/accretion	6,784	9,106
Total adjustments	(739,255)	(797,445)
Net cash used by investment income and operations	$(282,544)	$(142,173)

The accompanying notes are an integral part of these financial statements.

The Andrew W. Mellon Foundation

NOTES TO FINANCIAL STATEMENTS
December 31, 2007 and 2006

NOTE 1—ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

The Andrew W. Mellon Foundation (the "Foundation") is a not-for-profit corporation under the laws of the State of New York. The Foundation makes grants in five core program areas: higher education; museums and art conservation; performing arts; libraries and scholarly communication; and conservation and the environment. In addition to grantmaking activities, Foundation staff engage in research in areas that support the Foundation's mission, principally on issues that relate to higher education.

The financial statements of the Foundation have been prepared in conformity with generally accepted accounting principles. The significant accounting policies followed are described below.

Investments

Investments in marketable securities are stated at market value. Market value is determined using daily closing last trade prices, where available, for all tradeable instruments on any global stock exchange. Realized gains and losses on investments in securities are calculated based on the first-in, first-out identification method. Included in payable from unsettled securities purchases in the accompanying Balance Sheets are receivables from unsettled securities sales of $57.0 million and $24.0 million at December 31, 2007 and 2006, respectively.

Limited liquidity investments are stated at estimated fair value. Limited liquidity investments are primarily made under agreements to participate in limited partnerships and are generally subject to certain withdrawal restrictions. These investments are valued on the basis of the Foundation's equity in the net assets of such partnerships. Values for these partnerships, which may include investments in both nonmarketable and market-traded securities, are provided by the general partner and may be based on appraisals, market values discounted for concentration of ownership, or other estimates. Because of the inherent uncertainty of valuing the investments in such partnerships and certain of the underlying investments held by the partnerships, the Foundation's estimate of fair value may differ significantly from the values that would have been used had a ready market for the investments existed. The financial statements of the limited partnerships are audited annually by independent auditing firms. Investments in these partnerships may be illiquid, and thus there can be no assurance that the Foundation will be able to realize the value of such investments in a timely manner.

During 2006, the Foundation owned a 100% interest in a trust which owned property from which the Foundation received the net income. Other income in 2006 is principally the income from this trust, derived primarily from coal mining royalties. On December 1, 2006, the Foundation's interest in the trust was sold to Natural Resource Partners, LP, for cash of

$110.0 million. The sale resulted in a pre-tax gain of $107.2 million in 2006 which is included in realized gain on investments in the accompanying Statement of Activities.

Grants

Grant appropriations include both conditional and unconditional grants. Unconditional grants are expensed when appropriated. Certain grants are approved by the Trustees subject to the grantee fulfilling specific conditions, most frequently that all or a portion of the grant funds be matched in a specified ratio. Such conditional grants are considered commitments and are not recorded as expense until the Foundation determines that the material conditions of the grant are substantially met or such meeting of conditions are probable.

Substantially all grants payable are due within one year and are recorded at face value.

Taxes

The Foundation qualifies as a tax-exempt organization under Section 501(c)(3) of the Internal Revenue Code and, accordingly, is not subject to federal income taxes. However, the Foundation is subject to a federal excise tax. The Foundation follows the policy of providing for federal excise tax on the net appreciation (both realized and unrealized) of investments. The deferred federal excise tax in the accompanying financial statements represents tax provided on the net unrealized appreciation of investments. The Foundation is subject to income tax at corporate rates on certain income that is considered unrelated business income under the Internal Revenue Code.

Property

Property primarily consists of land held at cost, and buildings and their improvements located in New York City. These buildings are depreciated on a straight-line basis over their useful lives, generally twenty-five to twenty-eight years. Building improvements are depreciated over the remaining useful life of the building.

Investment Return

Investment return includes income and realized and unrealized gains or losses on all investments. Unrealized gain or loss comprises the change in unrealized appreciation on marketable securities and the limited liquidity investments, net of deferred federal excise tax provided on such unrealized appreciation. Realized gains or losses include gains or losses realized on the sale of marketable securities and the Foundation's share of the operating results of the partnership investments, whether distributed or undistributed.

Expenses

Grantmaking operations include all costs related to appropriating, paying and administering grants. Direct charitable activities are the active programs conducted by the Foundation or supported by it and include expenditures for two digital initiatives, ARTstor Inc. ("ARTstor") and Ithaka Harbors, Inc. ("Ithaka"), which are independent not-for-profit entities, and expenditures for research. Investment operations include the costs of supervising the Foundation's investment portfolio. Current provision for taxes includes federal and state taxes. Other expenses include certain expenses that the Foundation is not permitted to report either as an expense of distribution or an expense of earning income.

Salaries and benefits are allocated to each activity listed above, and also to core administration, based on estimates of the time each staff member devoted to that activity. Core administration expenses are then prorated among the activities listed above on the basis of the direct salary allocations. Identifiable costs, such as consultants, are charged directly to each activity.

Notes to Financial Statements, (continued)

Amounts for program grants, grantmaking operations, and direct charitable activities shown on the Statement of Activities will not agree with the amounts on the Foundation's Form 990PF, the federal excise tax return, because a cash basis is required for reporting the expenses of distribution for tax purposes as contrasted with the accrual basis used in preparing the accompanying financial statements.

The administrative expenses of distribution, including direct charitable activities, were $19.9 million (6.9% of appropriated program grants) in 2007 compared to $20.3 million (9.5% of appropriated program grants) in 2006. The decrease in administrative expenses in 2007 is primarily due to lower usage of outside consultants and reductions in technology and communication expenses. Excluding direct charitable activities and investment expenses, the Foundation's grantmaking expenses in 2007 were $14.6 million (5.1% of appropriated program grants), compared to $13.5 million (6.3% of appropriated program grants) in 2006.

Investment management expenses are the direct costs of portfolio management, including fees for investment management, custody, and advisory services.

The Foundation's expenses by natural classification are as follows for 2007 and 2006:

	2007	2006
	(in thousands)	
Program grants and contributions, net	$292,507	$180,803
Salaries, pensions and benefits	13,012	12,836
Other operating expenses	11,969	12,903
Current provision for taxes	5,649	15,163
	$323,137	$221,705

Use of Estimates

The preparation of financial statements in accordance with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reported periods. Actual results could differ from those estimates.

Reclassifications

Certain 2006 amounts have been reclassified to conform to the 2007 presentation.

New Accounting Pronouncements

On February 1, 2008, the Financial Accounting Standards Board ("FASB") issued Interpretation No. 48-2, *Accounting for Uncertainty in Income Taxes, an Interpretation of FASB Statement No. 109 for Certain Nonpublic Enterprises ("FIN 48"),* which allows the Foundation to defer the adoption of FIN 48 until annual periods beginning after December 15, 2007. The Foundation has elected to take advantage of this deferral. Based on its continued analysis, the Foundation believes that the adoption of FIN 48 will not have a material impact on its financial statements.

In September 2006, the FASB issued Statement of Financial Accounting Standards No. 157, *Fair Value Measurements* ("SFAS 157"). SFAS 157 defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. SFAS 157 applies to reporting periods beginning after November 15, 2007. The

Foundation believes that the adoption of SFAS 157 will not have a material impact on its financial statements.

NOTE 2—INVESTMENTS:

Marketable securities held at December 31, 2007 and 2006 are summarized as follows:

	December 31, 2007		*December 31, 2006*	
	Market Value	*Cost*	*Market Value*	*Cost*
	(in thousands)			
Equities	$2,513,023	$2,018,796	$2,519,470	$1,868,287
Fixed income	690,404	659,178	790,301	780,387
Short-term	171,712	171,658	231,808	228,152
Derivative financial instruments	3,378	(1,286)	554	1,108
	$3,378,517	$2,848,346	$3,542,133	$2,877,934

As a result of its investing strategies, the Foundation is a party to a variety of forward contracts, options, swaps and other derivative financial instruments, all of which are carried at fair value. The extent of the Foundation's involvement in these instruments is determined by the composition of the investment portfolio and the Foundation's expectations as to the direction and volatility of equity and fixed income markets as well as other economic factors. These transactions involve elements of market risk in excess of amounts reflected in the accompanying Balance Sheets. Changes in the market value of these financial instruments are recognized currently in the Statement of Activities.

Through certain investment managers, the Foundation purchases and sells forward currency contracts whereby the Foundation agrees to exchange one currency for another on an agreed-upon date at an agreed-upon exchange rate to minimize the exposure of certain of its marketable securities to adverse fluctuations in financial and currency markets. As of December 31, 2007 and 2006, the Foundation had forward currency contracts with notional amounts totaling $16.6 million and $32.3 million, respectively. At December 31, 2007, approximately $16.6 million in assets and $16.5 million in liabilities related to open foreign currency contracts, at market value, are included in derivative financial instruments.

Through a securities lending program managed by its investment custodian, the Foundation loans certain stocks and bonds included in its investment portfolio to qualified investors. The custodian maintains collateral in excess of the value of the securities on loan. The Foundation's investment custodian has indemnified the program against counterparty risk. The Foundation's gross securities loaned to certain investors at December 31, 2007 and 2006 amounted to approximately $474 million and $508 million, respectively.

Financial instruments such as those described above involve, to varying degrees, elements of market risk and credit risk in excess of the amounts recorded on the balance sheet. Market risk represents the potential loss the Foundation faces due to the decrease in the value of financial instruments. Credit risk represents the maximum potential loss the Foundation faces due to possible non-performance by obligors and counterparties as to the terms of their contracts.

Management does not anticipate that losses, if any, resulting from its market or credit risks would materially affect the financial position and operations of the Foundation.

Pursuant to its limited partnership agreements, the Foundation is committed to contribute approximately $1.4 billion as of December 31, 2007 in additional capital over the next ten years. Unpaid commitments at December 31, 2006 were $1.1 billion.

Notes to Financial Statements, (continued)

The Foundation invests in a variety of fixed income securities and contractual instruments, which by their nature are interest rate sensitive. Changes in interest rates will affect the value of such securities and contractual instruments.

NOTE 3—BONDS PAYABLE:

At December 31, 2007 and 2006, the Foundation had outstanding $44.0 million of taxable term bonds ("the Bonds") with a final maturity date of December 1, 2032. Bond interest was payable monthly, based upon results of monthly auction procedures. The average interest rate applicable in 2007 was 5.4%. Interest incurred in 2007 and 2006 was $2.4 million and $2.2 million, respectively.

In March 2008, in response to the turmoil in the credit markets, the Foundation redeemed all of its outstanding taxable term bonds at par. The redemption will result in a 2008 loss of $407 thousand resulting from the write-off of unamortized deferred debt costs. The Foundation currently anticipates that it will re-issue debt once the credit markets are more stable.

NOTE 4—TAXES:

The Internal Revenue Code imposes an excise tax on private foundations equal to 2 percent of net investment income (principally interest, dividends, and net realized capital gains, less expenses incurred in the production of investment income). This tax is reduced to 1 percent when a foundation meets certain distribution requirements under Section 4940(e) of the Internal Revenue Code. The Foundation was subject to the 1% rate in 2007 and a 2% rate in 2006. Certain income defined as unrelated business income by the Code may be subject to tax at ordinary corporate rates.

The provision for taxes consists of a current provision for the federal excise taxes on net investment income and federal and state taxes on unrelated business income and a deferred provision on the change in unrealized appreciation of investments. The current tax provision for 2007 comprises $5.7 million of federal excise tax on net investment income. Federal and state taxes on unrelated business income were immaterial in 2007. The current tax provision for 2006 comprises $14.7 million of federal excise tax on net investment income and $495 thousand in federal and state taxes on unrelated business income. The change in unrealized appreciation reflected on the Statement of Activities includes a provision for deferred taxes based on net unrealized appreciation of investments at 2 percent. The increase in unrealized appreciation resulted in an increase of the deferred federal excise tax liability of $900 thousand and $3.6 million in 2007 and 2006, respectively.

NOTE 5—GRANTS, CONTRIBUTIONS, AND COMMITMENTS:

The following table of grant activity by major program area includes all grant appropriations approved during 2007.

	Payable and Committed December 31, 2006	*2007 Grants and Commitments*		*Payable and Committed December 31, 2007*
		Appropriated	*Paid*	
		(in thousands)		
Conservation and the environment	$ 4,230	$ 12,880	$ 12,819	$ 4,291
Museums and art conservation	31,407	25,096	41,033	15,470
Performing arts	13,738	42,336	49,592	6,482
Higher education and scholarship	48,310	176,242	161,813	62,739
Libraries and scholarly communication	13,050	28,422	33,517	7,955
Population	3	—	3	—
Other (1)	—	1,560	1,076	484
Program grants and commitments - totals	110,738	286,536	299,853	97,421
Contributions and matching gifts	—	346	346	—
	$110,738	$286,882	$300,199	$97,421

(1) Other is comprised of grants made to certain grantees that were directly affected by Hurricane Katrina.

Grant and grant commitment activity is summarized below.

	2007	*2006*
	(in thousands)	
Grants Payable		
Grants payable at January 1	$ 11,360	$ 6,465
Grant expense	293,128	182,124
Less grants paid	(300,199)	(177,229)
Grants payable at December 31	$ 4,289	$ 11,360
Net Grant Expense		
Unconditional grants	$ 225,886	$ 150,381
Less grants cancelled	—	(300)
Conditional grants meeting conditions for payment	67,242	32,043
	293,128	182,124
Less grant refunds	(621)	(1,321)
Net grant expense at December 31	$ 292,507	$ 180,803
Grant Commitments		
Grant commitments at January 1	$ 99,378	$ 67,623
Conditional grants appropriated	60,996	63,798
Less grants meeting conditions for payment	(67,242)	(32,043)
Grant commitments at December 31	$ 93,132	$ 99,378

Notes to Financial Statements, (continued)

NOTE 6—OTHER SERVICES:

Pursuant to agreements between the Foundation and Ithaka and ARTstor, the following services and arrangements have been provided:

- Ithaka provides information technology services to the Foundation. In 2007 and 2006, Ithaka charged $943 thousand and $815 thousand, respectively, to the Foundation for these services. Included in the 2007 and 2006 amounts are pass-through expenses of $46 thousand and $31 thousand, respectively.
- Ithaka provided human resource services to the Foundation for the first three months of 2007 and full year 2006, and charged $61 thousand and $263 thousand, respectively, to the Foundation for these services. Beginning March 2007, the Foundation engaged its own human resource staff and, accordingly, Ithaka no longer provides this service.
- Commencing January 1, 2005, the Foundation provides office space, free of charge, to Ithaka and ARTstor in a building owned by the Foundation in New York City. The office space will be provided for a period of five years, subject to certain ongoing termination provisions.