

**SECOND HARVEST FOOD BANK OF SANTA CLARA
AND SAN MATEO COUNTIES
(A California Nonprofit Public Benefit Corporation)**

**FINANCIAL STATEMENTS
INCLUDING SUPPLEMENTAL INFORMATION
ON FEDERAL FINANCIAL AWARDS**

**Year Ended June 30, 2006 with Comparative Totals
for the Year Ended June 30, 2005**

SECOND HARVEST FOOD BANK OF SANTA CLARA AND SAN MATEO COUNTIES
(A California Nonprofit Public Benefit Corporation)

TABLE OF CONTENTS

| | <u>Pages</u> |
|--|--------------|
| I. FINANCIAL SECTION | |
| INDEPENDENT AUDITOR'S REPORT | 1-2 |
| FINANCIAL STATEMENTS | |
| Statement of Financial Position | 3 |
| Statement of Activities | 4 |
| Statement of Functional Expenses | 5 |
| Statement of Cash Flows | 6 |
| Notes to Financial Statements | 7-15 |
| II. SUPPLEMENTARY INFORMATION | |
| Schedule of Expenditures of Federal Awards | 16-18 |
| Notes to Schedule of Expenditures of Federal Awards | 19 |
| III. REPORTS | |
| Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <i>Government Auditing Standards</i> | 20-21 |
| Report on Compliance with Requirements Applicable to Each Major Program and on Internal Control Over Compliance in Accordance with OMB Circular A-133 | 22-23 |
| IV. SCHEDULE OF FINDINGS AND QUESTIONED COSTS | |
| Schedule of Findings and Questioned Costs | 24 |
| Summary Schedule of Prior Audit Findings | 25 |

SECTION I

FINANCIAL SECTION

FINANCIAL STATEMENTS

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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors

Second Harvest Food Bank of Santa Clara and San Mateo Counties
(A California Nonprofit Public Benefit Corporation)
San Jose, California

We have audited the accompanying statement of financial position of Second Harvest Food Bank of Santa Clara and San Mateo Counties (a California nonprofit public benefit corporation) as of June 30, 2006, and the related statements of activities, functional expenses, and cash flows for the year then ended. These financial statements are the responsibility of the Agency's management. Our responsibility is to express an opinion on these financial statements based on our audit. The prior year summarized comparative information has been derived from the Agency's financial statements for the year ended June 30, 2005 and, in our report dated August 11, 2005, we expressed an unqualified opinion on those financial statements.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. 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 the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides 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 Second Harvest Food Bank of Santa Clara and San Mateo Counties as of June 30, 2006, and the changes in its net assets and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated August 15, 2006, on our consideration of Second Harvest Food Bank of Santa Clara and San Mateo Counties' internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, 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 basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

Berger/Lewis Accountancy Corporation

BERGER/LEWIS ACCOUNTANCY CORPORATION
San Jose, California
August 15, 2006

SECOND HARVEST FOOD BANK OF SANTA CLARA AND SAN MATEO COUNTIES
(A California Nonprofit Public Benefit Corporation)

STATEMENT OF FINANCIAL POSITION

June 30, 2006 with Comparative Totals as of June 30, 2005

| | OPERATING FUND | | LAND, BUILDING AND EQUIPMENT FUND | TOTAL | |
|--|----------------------|---------------------------|--|----------------------|----------------------|
| | Unrestricted | Temporarily Restricted | | 2006 | 2005 |
| ASSETS | | | | | |
| Cash and Cash Equivalents | \$ 3,166,646 | \$ 512,943 | \$ - | \$ 3,679,589 | \$ 2,304,682 |
| Accounts Receivable | 8,020 | - | - | 8,020 | 7,486 |
| Grants Receivable | 244,790 | - | - | 244,790 | 200,042 |
| Pledges Receivable | - | 273,524 | - | 273,524 | 71,247 |
| Inventory | 1,813,152 | - | - | 1,813,152 | 2,077,651 |
| Prepaid Expenses and Other Assets | 319,696 | - | 96,332 | 416,028 | 319,002 |
| Investments (Note 3) | 5,387,230 | - | 4,271,992 | 9,659,222 | 9,689,453 |
| Land, Building and Equipment, Net (Note 4) | - | - | 6,240,122 | 6,240,122 | 6,473,474 |
| TOTAL ASSETS | \$ 10,939,534 | \$ 786,467 | \$ 10,608,446 | \$ 22,334,447 | \$ 21,143,037 |
| LIABILITIES AND NET ASSETS | | | | | |
| LIABILITIES: | | | | | |
| Accounts Payable | \$ 229,769 | \$ - | \$ - | \$ 229,769 | \$ 123,784 |
| Accrued Expenses | 203,263 | - | - | 203,263 | 232,219 |
| Deferred Revenue (Note 5) | 171,025 | - | - | 171,025 | 92,556 |
| Total Liabilities | 604,057 | - | - | 604,057 | 448,559 |
| NET ASSETS: | | | | | |
| Unrestricted Net Assets: | | | | | |
| Undesignated | 760,684 | - | - | 760,684 | 629,908 |
| Board Designated (Note 8) | 9,574,793 | - | 4,271,992 | 13,846,785 | 13,315,356 |
| Land, Building and Equipment | - | - | 6,336,454 | 6,336,454 | 6,515,517 |
| Total Unrestricted Net Assets | 10,335,477 | - | 10,608,446 | 20,943,923 | 20,460,781 |
| Temporarily Restricted Net Assets (Note 9) | - | 786,467 | - | 786,467 | 233,697 |
| Total Net Assets | 10,335,477 | 786,467 | 10,608,446 | 21,730,390 | 20,694,478 |
| TOTAL LIABILITIES AND NET ASSETS | \$ 10,939,534 | \$ 786,467 | \$ 10,608,446 | \$ 22,334,447 | \$ 21,143,037 |

The Accompanying Notes are an Integral Part of these Financial Statements.

SECOND HARVEST FOOD BANK OF SANTA CLARA AND SAN MATEO COUNTIES
(A California Nonprofit Public Benefit Corporation)

STATEMENT OF ACTIVITIES

Year Ended June 30, 2006 with Comparative Totals for the Year Ended June 30, 2005

| | 2006 | | 2005 |
|--|---------------|------------------------|---------------|
| | Unrestricted | Temporarily Restricted | TOTAL |
| SUPPORT AND REVENUE: | | | |
| Support: | | | |
| Contributions | \$ 10,293,662 | \$ 762,549 | \$ 11,056,211 |
| Contributions In-Kind (Note 10) | 26,954,162 | - | 26,954,162 |
| Special Events (Net of Direct Costs of \$70,972 - 2006, \$77,283 - 2005) | 127,707 | - | 127,707 |
| United Way Support | 159,958 | 23,918 | 183,876 |
| Total Support | 37,535,489 | 786,467 | 38,321,956 |
| Revenue: | | | |
| Governmental Assistance - Cash | 1,227,491 | - | 1,227,491 |
| Governmental Assistance - In-Kind | 1,664,633 | - | 1,664,633 |
| Service Fees | 141,163 | - | 141,163 |
| Net Investment Income (Note 3) | 827,854 | - | 827,854 |
| Gain (Loss) on Sale of Equipment | (32,742) | - | (32,742) |
| Other Income | 15,620 | - | 15,620 |
| Total Revenue | 3,844,019 | - | 3,844,019 |
| Total Support and Revenue | 41,379,508 | 786,467 | 42,165,975 |
| Net Assets Released from Restrictions (Note 11) | 233,697 | (233,697) | - |
| Total Support, Revenue and Net Assets Released from Restrictions | 41,613,205 | 552,770 | 42,165,975 |
| EXPENSES: | | | |
| Program Services: | | | |
| Food Distribution (Note 1) | 39,431,623 | - | 39,431,623 |
| Supporting Services: | | | |
| Management and General | 652,879 | - | 652,879 |
| Fundraising | 1,045,561 | - | 1,045,561 |
| Total Supporting Services Expenses | 1,698,440 | - | 1,698,440 |
| Total Expenses | 41,130,063 | - | 41,130,063 |
| CHANGE IN NET ASSETS | | | |
| NET ASSETS, Beginning of Year | 483,142 | 552,770 | 1,035,912 |
| NET ASSETS, End of Year | 20,460,781 | 233,697 | 20,694,478 |
| | \$ 20,943,923 | \$ 786,467 | \$ 21,730,390 |
| | | | \$ 20,694,478 |

The Accompanying Notes are an Integral Part of these Financial Statements.

SECOND HARVEST FOOD BANK OF SANTA CLARA AND SAN MATEO COUNTIES
(A California Nonprofit Public Benefit Corporation)

STATEMENT OF FUNCTIONAL EXPENSES

Year Ended June 30, 2006 with Comparative Totals for the Year Ended June 30, 2005

| | PROGRAM SERVICES | | SUPPORTING SERVICES | | | TOTAL EXPENSES | |
|--|-------------------|------------------------|---------------------|--------------|----|----------------|---------------|
| | Food Distribution | Management and General | Fundraising | Total | | 2006 | 2005 |
| Salaries | \$ 3,089,951 | \$ 334,425 | \$ 524,261 | \$ 858,686 | \$ | 3,948,637 | \$ 3,980,165 |
| Employee Benefits | 616,078 | 76,557 | 82,071 | 158,628 | | 774,706 | 774,012 |
| Payroll Taxes | 279,671 | 30,292 | 43,758 | 74,050 | | 353,721 | 338,596 |
| Total Salaries and Related Expenses | 3,985,700 | 441,274 | 650,090 | 1,091,364 | | 5,077,064 | 5,092,773 |
| Donated Food and Supplies Distributed | 28,372,527 | - | - | - | | 28,372,527 | 24,263,283 |
| Purchased Food and Supplies Distributed | 4,439,307 | - | - | - | | 4,439,307 | 4,394,864 |
| Occupancy, Including In-Kind | 430,560 | 27,482 | 30,819 | 58,301 | | 488,861 | 640,335 |
| Freight and Storage | 454,253 | - | - | - | | 454,253 | 215,845 |
| Advertising and Media, Including In-Kind | 321,268 | - | 1,905 | 1,905 | | 323,173 | 281,474 |
| Postage and Printing | 215,261 | 3,609 | 7,478 | 11,087 | | 226,348 | 188,589 |
| Direct Mailing Costs, Including In-Kind | - | - | 213,493 | 213,493 | | 213,493 | 180,429 |
| Vehicle Operating Costs | 198,215 | - | - | - | | 198,215 | 186,479 |
| Professional Fees, Including In-Kind | 84,843 | 66,733 | 10,974 | 77,707 | | 162,550 | 192,053 |
| Insurance | 129,937 | 15,210 | 8,350 | 23,560 | | 153,497 | 183,837 |
| Equipment Rental and Maintenance | 91,909 | 9,574 | 32,438 | 42,012 | | 133,921 | 146,785 |
| Supplies, Including In-Kind | 114,999 | 5,533 | 6,654 | 12,187 | | 127,186 | 166,309 |
| Telephone | 67,646 | 9,921 | 8,949 | 18,870 | | 86,516 | 83,666 |
| Dues and Subscriptions | 11,597 | 10,925 | 3,102 | 14,027 | | 25,624 | 33,069 |
| Conferences, Conventions and Meetings | 8,498 | 6,845 | 6,099 | 12,944 | | 21,442 | 32,651 |
| Volunteer Expenses | 12,933 | - | - | - | | 12,933 | 14,591 |
| Affiliation Fees (Note 12) | 10,072 | - | - | - | | 10,072 | 12,428 |
| Travel | 4,604 | 2,604 | 1,803 | 4,407 | | 9,011 | 15,841 |
| Recruitment Expenses | 5,402 | 258 | 501 | 759 | | 6,161 | 6,554 |
| Equipment, In-Kind | - | - | - | - | | - | 20,200 |
| Total Expenses Before Depreciation | 38,959,531 | 599,968 | 982,655 | 1,582,623 | | 40,542,154 | 36,352,055 |
| Depreciation and Amortization | 472,092 | 52,911 | 62,906 | 115,817 | | 587,909 | 631,209 |
| Total Functional Expenses | \$ 39,431,623 | \$ 652,879 | \$ 1,045,561 | \$ 1,698,440 | \$ | 41,130,063 | \$ 36,983,264 |
| Percentage of Total | 95.9 % | 1.6 % | 2.5 % | 4.1 % | | 100.0 % | |

The Accompanying Notes are an Integral Part of these Financial Statements.

SECOND HARVEST FOOD BANK OF SANTA CLARA AND SAN MATEO COUNTIES
(A California Nonprofit Public Benefit Corporation)

STATEMENT OF CASH FLOWS

Year Ended June 30, 2006 with Comparative Totals for the Year Ended June 30, 2005

| | <u>2006</u> | <u>2005</u> |
|---|----------------------------|----------------------------|
| CASH FLOWS FROM OPERATING ACTIVITIES: | | |
| Change in Net Assets | \$ 1,035,912 | \$ 617,127 |
| Adjustments to Reconcile Change in Net Assets to Net Cash | | |
| Provided by Operating Activities: | | |
| Depreciation and Amortization | 587,909 | 631,209 |
| (Gain) Loss on Sale of Equipment | 32,742 | (49,163) |
| Donated Equipment | (220,186) | - |
| In-Kind Contributions of Food and Non-Food (Including USDA) | (27,960,738) | (24,575,784) |
| Distribution of Food and Non-Food Received In-Kind | 28,302,626 | 24,251,314 |
| Realized and Unrealized Gains on Investments | (546,876) | (335,203) |
| (Increase) Decrease in Assets: | | |
| Accounts Receivable | (533) | 20,878 |
| Grants Receivable | (44,748) | 43,698 |
| Pledges Receivable | (202,277) | (41,350) |
| Purchased Inventory (Food) | (77,390) | 99,881 |
| Prepaid Expenses and Other Assets | (97,024) | (8,871) |
| Increase (Decrease) in Liabilities: | | |
| Accounts Payable | 105,984 | (279,442) |
| Accrued Expenses | (28,956) | (51,441) |
| Deferred Revenue | <u>78,468</u> | <u>(11,597)</u> |
| Net Cash Provided by Operating Activities | <u>964,913</u> | <u>311,256</u> |
| CASH FLOWS FROM INVESTING ACTIVITIES: | | |
| Purchase of Equipment | (191,313) | (332,647) |
| Proceeds from Sale of Equipment | 24,200 | 66,857 |
| Purchase of Investments | (3,036,134) | (2,422,757) |
| Proceeds from Sale of Investments | <u>3,613,241</u> | <u>3,671,486</u> |
| Net Cash Provided by Investing Activities | <u>409,994</u> | <u>982,939</u> |
| NET INCREASE IN CASH AND CASH EQUIVALENTS | 1,374,907 | 1,294,195 |
| CASH AND CASH EQUIVALENTS, Beginning of Year | <u>2,304,682</u> | <u>1,010,487</u> |
| CASH AND CASH EQUIVALENTS, End of Year | <u><u>\$ 3,679,589</u></u> | <u><u>\$ 2,304,682</u></u> |

The Accompanying Notes are an Integral Part of these Financial Statements.

SECOND HARVEST FOOD BANK OF SANTA CLARA AND SAN MATEO COUNTIES
(A California Nonprofit Public Benefit Corporation)

NOTES TO FINANCIAL STATEMENTS

NOTE 1 - NATURE OF ACTIVITIES:

Second Harvest Food Bank of Santa Clara and San Mateo Counties ("Agency" or "Second Harvest") is a non-profit 501(c)(3) organization incorporated in 1979. The Agency's service area covers a population of 2.4 million where nearly 170,000 people live below the federal poverty line (FPL). With the area's high cost of living, even families living at 300% - 400% of the FPL are struggling to afford enough to eat. The Agency provides food through both direct distribution and by supplying food to hundreds of area non-profit programs.

Second Harvest procures large food donations through corporate food drives, from the USDA and FEMA, and through membership in America's Second Harvest. But simply distributing donated food would not provide nutritious, nor balanced, meals. The Agency spent over \$5.3 million procuring, packaging and transporting protein and other food to supplement donated items; ensuring nutritious meals to over 160,000 people per month. This involved the distribution of 30.7 million pounds of food, equivalent to about 23 million meals and up 9% over last year, making the agency the 12th largest food bank in the nation. With an emphasis on procuring donated food whenever possible, such donations rose by more than \$4.1 million year over year.

The Agency's Direct Service Programs, distributed at 120 sites, include:

- Brown Bag - Groceries provided on a weekly basis to an average of 12,233 people: for seniors and disabled individuals on fixed incomes.
- Family Harvest - Groceries provided monthly to low-income families with dependent children serving an average of 11,497 per month.
- Partners in Need - Weekly groceries for an average of 443 people in exchange for volunteer hours.

In-direct and Community Service Programs:

Second Harvest's Food Assistance Program supports nearly 300 community-based non-profit organizations running about 400 programs through 800 different sites. The Agency removes much of the burden for those managing food programs by providing free highly nutritious foods, appropriate storage and handling, delivery options, as well as training workshops. These hundreds of community programs can focus their resources on their own primary missions, not on procuring food.

Food Connection, a phone referral program, further ensures that those in need have access to nutritious food. In the past year, Food Connection helped thousands of people each month and made over 44,000 referrals to Second Harvest's food program partners. Community Nutrition offers training, workshops and technical assistance to agencies and program participants in the areas of nutrition education, food safety and handling practices.

Our Support - The Agency has strong donor and volunteer support. Over 23,000 individuals made donations and over 1,300 companies ran food drives or donated funds. Every month volunteers worked an average of 14,888 hours on Second Harvest's behalf: the equivalent of nearly 86 full-time employees and more manpower than the Agency employs. This saved the Agency over \$3 million in wages in the past year.

SECOND HARVEST FOOD BANK OF SANTA CLARA AND SAN MATEO COUNTIES
(A California Nonprofit Public Benefit Corporation)

NOTES TO FINANCIAL STATEMENTS
(Continued)

NOTE 1 - NATURE OF ACTIVITIES (Continued):

New Programs - After achieving goals set out in a three year Strategic Plan, the Agency recently conducted a Food Gap Analysis that showed tremendous need still exists in the community. Approximately half the need is being met even when considering all food programs, including Food Stamps. As Second Harvest develops a new plan, the focus is on procuring and distributing more food, especially fresh produce. The Agency's Board of Directors has designated approximately \$2.2 million of reserves to grow capacity over the next few years.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

Basis of Accounting - The financial statements of Second Harvest Food Bank of Santa Clara and San Mateo Counties have been prepared on the accrual basis of accounting.

Basis of Presentation - The Agency follows standards of accounting and financial reporting for voluntary health and welfare organizations as prescribed by the American Institute of Certified Public Accountants. In accordance with Statement of Financial Accounting Standards (SFAS) No. 117, *Financial Statements of Non-for-Profit Organizations*, the Agency reports its financial position and operating activities in three classes of net assets: unrestricted net assets, temporarily restricted net assets, and permanently restricted net assets.

Unrestricted net assets include those assets over which the Board of Directors has discretionary control in carrying out the operations of the Agency. Under this category, the Agency maintains an operating fund, any net assets designated by the Board for specific purposes and the unrestricted land, building and equipment fund.

Temporarily restricted net assets include those assets which are subject to donor restriction and for which the applicable restriction was not met as of the year end of the current reporting period.

Permanently restricted net assets include those assets which are subject to a non-expiring donor restriction, such as endowments.

Land, building and equipment funds are designated for equipment acquisitions and for recording the cost of the land, building, equipment and accumulated depreciation. The net asset value of those items that are temporarily or permanently restricted are included in the appropriate net asset category, otherwise the net asset value is included in unrestricted net assets.

Comparative Financial Information - The financial statements include certain prior-year summarized comparative information in total but not by net asset class or functional expense categories. Such information does not include sufficient detail to constitute a presentation in conformity with generally accepted accounting principles. Accordingly, such information should be read in conjunction with the Agency's financial statements for the year ended June 30, 2005, from which the summarized information was derived.

SECOND HARVEST FOOD BANK OF SANTA CLARA AND SAN MATEO COUNTIES
(A California Nonprofit Public Benefit Corporation)

NOTES TO FINANCIAL STATEMENTS
(Continued)

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued):

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 at the date of the financial statements and the reported amounts of revenue and expenses during the period. Accordingly, actual results could differ from those estimates.

Revenue Recognition - The Agency recognizes support and revenue on the accrual basis of accounting. Revenue from grants which have been classified as "exchange transactions" and program fees are recognized as revenue in the period in which the service is provided.

Contributions - Contributions are reported in accordance with SFAS No. 116, *Accounting for Contributions Received and Contributions Made*. Contributions are recognized when the donor makes a pledge to give that is, in substance, an unconditional promise. Contributions are recorded as unrestricted, temporarily restricted, or permanently restricted depending on the nature of donor restrictions. Restricted contributions are reported as increases in restricted net assets. When the restriction is met the amount is shown as a reclassification of restricted net assets to unrestricted net assets. If a donor's restriction is met in the same period that the revenue is recognized, the contribution is reported as an increase in unrestricted net assets.

Contributions In-Kind - Contributions in-kind are also recognized in accordance with the provisions of SFAS No. 116. Donated equipment and other donated goods are recorded at their estimated fair value as of the date of the donation. Contributed services, which require a specialized skill and which the Agency would have paid for if not donated, are recorded at the estimated fair value at the time the services are rendered. The Agency also receives donated services that do not require specific expertise but which are nonetheless central to the Agency's operations. While these contributed services are not reflected in the financial statements the estimated value of these services is disclosed in Note 10.

Cash and Cash Equivalents - Cash equivalents include highly liquid investments and investments with a maturity of three months or less, and exclude donor restricted receipts and amounts designated for long-term purposes. The Agency maintains its cash in bank deposit accounts which, at times, may exceed federally insured limits. The Agency has not experienced any losses in such accounts. Management believes it is not exposed to any significant risk on cash accounts.

Accounts, Grants and Pledges Receivable - The Agency considers all accounts, grants and pledges receivable to be fully collectible; accordingly, no allowance for doubtful accounts is considered necessary.

Inventory - Inventory consists of donated food and non-food items, purchased food and United States Department of Agriculture (USDA) commodities received from the government. Donated food for the years ended June 30, 2006 and 2005 was valued at \$1.50 and \$1.49 per pound, respectively. This valuation is based on a cost study conducted for America's Second Harvest. Purchased food is valued at latest purchase price. USDA commodities are valued based on published USDA fair market values.

SECOND HARVEST FOOD BANK OF SANTA CLARA AND SAN MATEO COUNTIES
(A California Nonprofit Public Benefit Corporation)

NOTES TO FINANCIAL STATEMENTS
(Continued)

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued):

Investments - Investments in marketable securities with readily determinable fair values and all investments in debt securities are reported at their fair values in the statement of financial position. Unrealized gains or losses are included in the change in net assets. Investment income and gains restricted by a donor are reported as increases in unrestricted net assets if the restrictions are met (either by passage of time or by use) in the reporting period in which the income and gains are recognized.

Land, Building and Equipment - Land, building and equipment are recorded at cost or estimated fair value for donated items. Depreciation is computed on the straight-line method based on the estimated useful lives of the assets, which range from 3 to 30 years. Equipment purchases over \$5,000 are capitalized. Depreciation is recorded as a decrease in unrestricted net assets and the expense is charged to the activity benefiting from the use of the facilities or equipment. Amounts expended for maintenance and repairs are charged to operations as incurred.

Accrued Vacation - Accrued vacation represents vacation earned, but not taken as of June 30. The maximum vacation time that can be accrued and carried over to the next year is 200 hours. The accrued vacation balance as of June 30, 2006 and 2005 was \$133,005 and \$162,368, respectively, and is included in accrued expenses.

Allocation of Functional Expenses - Directly identifiable expenses are charged to program and supporting services. Expenses related to more than one function are charged to program and supporting services on the basis of periodic time studies.

Income Taxes - Second Harvest Food Bank of Santa Clara and San Mateo Counties is exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code and state income taxes under Section 23701(d) of the California Revenue Taxation Code. Accordingly, no provision for income taxes has been made in the accompanying statements.

Advertising - Advertising costs are charged to operations when incurred. Advertising costs for the years ended June 30, 2006 and 2005 totaled \$323,173 and \$281,474, respectively. The total cost for the years ended June 30, 2006 and 2005 includes \$275,000 and \$150,941 in donated advertising, respectively.

NOTE 3 - INVESTMENTS:

The Agency's investment policy is to maintain a moderately conservative but balanced portfolio, with the primary investment objectives being the preservation of purchasing power and the preservation of capital. The Agency's investment portfolio is structured and maintained with the overall objective of providing the resources and liquidity for the Agency to fulfill its Mission Statement. The fair value of investments as of June 30, was as follows:

SECOND HARVEST FOOD BANK OF SANTA CLARA AND SAN MATEO COUNTIES
(A California Nonprofit Public Benefit Corporation)

NOTES TO FINANCIAL STATEMENTS
(Continued)

NOTE 3 - INVESTMENTS (Continued):

| | <u>2006</u> | <u>2005</u> |
|---|---------------------|---------------------|
| Investments at Fair Value: | | |
| Money Market Investments | \$ 538,162 | \$ 1,007,500 |
| Certificates of Deposit | 103,945 | 101,209 |
| U.S. Government Securities and Agency Obligations | 1,922,032 | 1,326,215 |
| Corporate Bonds and Notes | 1,331,627 | 1,543,767 |
| Equity Investments | 5,247,778 | 4,855,826 |
| Mutual Funds | <u>515,678</u> | <u>854,936</u> |
| Total Investments at Fair Value | <u>\$ 9,659,222</u> | <u>\$ 9,689,453</u> |
| Net Investment Income: | | |
| Interest and Dividends, Net of Investment | | |
| Expenses of \$58,905 and \$74,178 | \$ 287,773 | \$ 273,532 |
| Net Realized and Unrealized Gains | <u>540,081</u> | <u>329,179</u> |
| Total Net Investment Income | <u>\$ 827,854</u> | <u>\$ 602,711</u> |

NOTE 4 - LAND, BUILDING AND EQUIPMENT:

The cost and accumulated depreciation of land, building and equipment as of June 30, consisted of the following:

| | <u>2006</u> | <u>2005</u> |
|-----------------------------------|---------------------|---------------------|
| Land | \$ 838,453 | \$ 838,453 |
| Building and Improvements | 7,888,263 | 7,846,503 |
| Equipment | <u>3,267,116</u> | <u>3,450,896</u> |
| | 11,993,832 | 12,135,852 |
| Less: Accumulated Depreciation | <u>(5,753,710)</u> | <u>(5,662,378)</u> |
| Land, Building and Equipment, Net | <u>\$ 6,240,122</u> | <u>\$ 6,473,474</u> |

Depreciation expense for the years ended June 30, 2006 and 2005 totaled \$587,909 and \$631,209, respectively.

SECOND HARVEST FOOD BANK OF SANTA CLARA AND SAN MATEO COUNTIES
(A California Nonprofit Public Benefit Corporation)

NOTES TO FINANCIAL STATEMENTS
(Continued)

NOTE 5 - DEFERRED REVENUE:

The Agency's deferred revenue as of June 30, consisted of the following:

| | <u>2006</u> | <u>2005</u> |
|-------------------------------------|-------------------|------------------|
| Golf Tournament Deposits | \$ 91,915 | \$ 71,181 |
| Federal Emergency Management Agency | 78,910 | 21,375 |
| Other | <u>200</u> | <u>-</u> |
| Total Deferred Revenue | <u>\$ 171,025</u> | <u>\$ 92,556</u> |

NOTE 6 - RETIREMENT PLAN:

The Agency maintains a tax deferred 403(b) retirement plan to provide retirement benefits for all eligible employees. The plan provides for Agency contributions of 5% of eligible employee compensation. Vesting is based on years of service, with 100% vesting after six years of credited service. Agency contributions for the years ended June 30, 2006 and 2005 were \$126,482 and \$127,983, respectively. All of the costs of the Plan's administration were paid for by participants.

NOTE 7 - OPERATING LEASE COMMITMENTS:

The Agency leases from the County of Santa Clara the land on which the San Jose distribution center is located. The lease term is 50 years, commencing July 30, 1991, at the rate of \$1 per year, with three 10-year renewal options. In the event the premises cease to be used as a nonprofit food collection and distribution facility, the County of Santa Clara has the right to terminate the lease. Due to the impracticality of determining the fair value of the lease, the financial statements do not include an in-kind contribution for this amount.

SECOND HARVEST FOOD BANK OF SANTA CLARA AND SAN MATEO COUNTIES
(A California Nonprofit Public Benefit Corporation)

NOTES TO FINANCIAL STATEMENTS
(Continued)

NOTE 8 - BOARD DESIGNATED NET ASSETS:

Board designated net assets as of June 30, consisted of the following:

| | <u>2006</u> | <u>2005</u> |
|---|----------------------|----------------------|
| Unrestricted Operating Fund: | | |
| Designated for Operating Reserves | \$ 6,395,830 | \$ 7,217,819 |
| Designated for Disaster Relief | 1,365,811 | 800,006 |
| Inventory | <u>1,813,152</u> | <u>2,077,651</u> |
| Total Unrestricted Operating Fund | <u>9,574,793</u> | <u>10,095,476</u> |
| Land, Building and Equipment Fund: | | |
| Designated for Capacity Building Fund | 2,200,000 | - |
| Designated for Capital Replacement Fund | <u>2,071,992</u> | <u>3,219,880</u> |
| Total Land, Building and Equipment | <u>4,271,992</u> | <u>3,219,880</u> |
| Total Board Designated Net Assets | <u>\$ 13,846,785</u> | <u>\$ 13,315,356</u> |

As part of the Agency's annual review of designated assets, the Board recently adopted specific guidelines for establishing the level of each designation. Operating Reserves include a full six months of the coming year's annual budget, with adjustments for purchased inventory on hand and current liabilities. Disaster Relief funds are based on the cost of meals expected to be provided immediately following a local disaster. Long-term disaster support would be funded through government agreements. Current investment in inventory is reviewed on a monthly basis and is generally below one month's distribution. The Capital Replacement designation is calculated as the present-value of a ten year current asset replacement plan. The Capacity Building Fund designation is based on expectations that the Agency will be pursuing significant distribution capacity building, as part of a strategic plan, in the next one to five years.

SECOND HARVEST FOOD BANK OF SANTA CLARA AND SAN MATEO COUNTIES
(A California Nonprofit Public Benefit Corporation)

NOTES TO FINANCIAL STATEMENTS
(Continued)

NOTE 9 - TEMPORARILY RESTRICTED NET ASSETS:

The Agency's temporarily restricted net assets as of June 30, consisted of the following:

| | <u>2006</u> | <u>2005</u> |
|---|-------------------|-------------------|
| Temporarily Restricted Net Assets: | | |
| Equipment Purchase | \$ 270,300 | \$ - |
| Family Harvest | 192,234 | - |
| Season of Sharing | 144,792 | 72,800 |
| Warehouse Bar Coding | 91,075 | - |
| General Support for Next Year | 60,000 | - |
| United Way Allocation and Designations for Next Year | 23,918 | 29,897 |
| Staff Holiday | 3,000 | - |
| Hurricane Relief | 1,148 | - |
| Summer Feeding | - | 35,000 |
| Holiday Food Drive Sponsorship | - | 96,000 |
| Total Temporarily Restricted Net Assets | <u>\$ 786,467</u> | <u>\$ 233,697</u> |

NOTE 10 - CONTRIBUTIONS IN-KIND:

The estimated fair value of donated food, supplies and expert services received are recorded as contributions. During the years ended June 30, the following in-kind contributions were received by the Agency:

| | <u>2006</u> | <u>2005</u> |
|-----------------------------|----------------------|----------------------|
| Food and Non-Food Inventory | \$ 26,334,331 | \$ 22,077,694 |
| Media | 275,000 | 150,941 |
| Vehicle and Equipment | 220,186 | 25,790 |
| Warehouse Space | 80,988 | 187,850 |
| Professional Services | 18,725 | 70,791 |
| Gift Certificates | 16,979 | 26,695 |
| Racks and Supplies | 6,849 | 14,195 |
| Printing | 1,104 | - |
| Mailings | - | 5,710 |
| Total Contributions In-Kind | <u>\$ 26,954,162</u> | <u>\$ 22,559,666</u> |

The Agency also receives donated services that do not require specific expertise but which are nonetheless central to the Agency's operations. For the years ended June 30, 2006 and 2005 the estimated value of these services, based on the estimated dollar value of volunteer time calculated by average rate by job category, totaled \$3,018,049 and \$2,859,212, respectively. In accordance with SFAS No. 116, *Accounting for Contributions Received and Contributions Made*, the value of these services is not reflected in the financial statements.

SECOND HARVEST FOOD BANK OF SANTA CLARA AND SAN MATEO COUNTIES
(A California Nonprofit Public Benefit Corporation)

NOTES TO FINANCIAL STATEMENTS
(Continued)

NOTE 11 - NET ASSETS RELEASED FROM RESTRICTIONS:

Net assets were released from restrictions during the year by incurring expenses satisfying the restricted purpose or by the expiration of time as follows:

| | <u>2006</u> |
|--|-------------------|
| Net Assets Released from Restrictions: | |
| Holiday Food Drive Sponsorship | \$ 96,000 |
| United Way Allocation and Designations for Next Year | 29,897 |
| Summer Feeding | 35,000 |
| Season of Sharing | <u>72,800</u> |
| Total Net Assets Released from Restrictions | <u>\$ 233,697</u> |

NOTE 12 - PAYMENTS TO AFFILIATES:

In accordance with the affiliation agreement between America's Second Harvest and the Second Harvest Food Bank of Santa Clara and San Mateo Counties, the Agency pays fees based on total poundage of food received from America's Second Harvest. Affiliation payments for the years ended June 30, 2006 and 2005 were \$10,072 and \$12,428, respectively.

NOTE 13 - CONFLICT OF INTEREST POLICY:

Included among the Agency's Board of Directors and Officers are volunteers from the community who provide valuable assistance to the Agency in the development of policies and programs and in the evaluation of business transactions. The Agency has adopted a conflict of interest policy whereby board members are disqualified from participation in the final decisions regarding any action affecting their related company or organization.

NOTE 14 - CONTINGENCIES:

Grants and contracts awarded to Second Harvest Food Bank of Santa Clara and San Mateo Counties are subject to the funding agencies' criteria, contract terms and regulations under which expenditures may be charged and are subject to audit under such terms, regulations and criteria. Occasionally, such audits may determine that certain costs incurred against the grants do not comply with the established criteria that govern them. In such cases, the Agency could be held responsible for repayments to the funding agency for the costs or be subject to the reductions of future funding in the amount of the costs. Management does not anticipate any material questioned costs for the contracts and grants administered during the period.

SECTION II

SUPPLEMENTARY INFORMATION

SECOND HARVEST FOOD BANK OF SANTA CLARA AND SAN MATEO COUNTIES
(A California Nonprofit Public Benefit Corporation)

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

Year Ended June 30, 2006

| Government Grantor Pass-through Grantor Program Title | Federal CFDA Number | Grant Period/ Period in Current Fiscal Year | Pass-through Grantor's Number/ Grant Number | Award Amount | Receivable (Deferred Revenue) From Prior Year | Receipt of Federal Awards | Federal Expenditures | Receivable (Deferred Revenue) at June 30, 2006 |
|---|---------------------------|--|--|-----------------|---|---------------------------------|-------------------------|---|
| MAJOR PROGRAMS | | | | | | | | |
| <u>U.S. Department of Agriculture</u> | | | | | | | | |
| Passed through: | | | | | | | | |
| State of California Department of Social Services: | | | | | | | | |
| Emergency Food Assistance Program (Administrative Costs) | 10.568 | 10-1-04 to 9-30-05 | L61059 | \$ - | \$ 32,750 | \$ 32,750 | - \$ | - |
| Emergency Food Assistance Program (Administrative Costs) | 10.568 | 7-1-05 to 6-30-06 | L61059 | 127,897 | - | 96,181 | 127,897 | 31,716 |
| Emergency Food Assistance Program (Tax Check Off Funds) | 10.568 | 7-1-05 to 6-30-06 | | 11,258 | - | 11,258 | 11,258 | - |
| Emergency Food Assistance Program (Supplemental Funds) | 10.568 | 7-1-05 to 6-30-06 | | 3,435 | - | 3,435 | 3,435 | - |
| Emergency Food Assistance Program (Food Commodities) (Note A) | 10.569 | 7-1-05 to 6-30-06 | E65088 | 1,634,933 | - | 1,634,933 | 1,723,599 | - |
| Total U.S. Department of Agriculture | | | | 1,777,523 | 32,750 | 1,778,557 | 1,866,189 | 31,716 |
| <u>U.S. Department of Health and Human Services</u> | | | | | | | | |
| CNN - Food Stamp Outreach | | | | 23,407 | - | 10,144 | 23,407 | 13,263 |
| CNN - Nutrition Education | | | | 41,445 | - | - | 41,445 | 41,445 |
| Total U.S. Department of Health and Human Services | | | | 64,852 | - | 10,144 | 64,852 | 54,708 |

NOTE A - Emergency Food Assistance Program (Food Commodities):
Nonmonetary assistance is reported in the schedule at the USDA fair value of the commodities received. At June 30, 2006, the Agency had USDA food commodities totaling \$110,994 in inventory.

See Accompanying Notes to Schedule of Expenditures of Federal Awards.

SECOND HARVEST FOOD BANK OF SANTA CLARA AND SAN MATEO COUNTIES
(A California Nonprofit Public Benefit Corporation)

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
(Continued)

Year Ended June 30, 2006

| Government Grantor Pass-through Grantor Program Title | Federal CFDA Number | Grant Period/ Period in Current Fiscal Year | Pass-through Grantor's Number/ Grant Number | Award Amount | Receivable (Deferred Revenue) From Prior Year | Receipt of Federal Awards | Federal Expenditures | Receivable (Deferred Revenue) at June 30, 2006 |
|---|---------------------------|--|--|-----------------|---|---------------------------------|-------------------------|---|
| NON-MAJOR PROGRAMS | | | | | | | | |
| <u>Federal Emergency Management Agency</u> | | | | | | | | |
| Direct Program: | | | | | | | | |
| Emergency Food and Shelter National Board Program (Santa Clara County) | 83.523 | 10-1-04 to 9-30-05 10-1-05 to 9-30-06 | 24-0880-00 007 Phase XXIV | - 133,194 | 53,403 - | 74,777 66,000 | 21,374 64,284 | - (1,716) |
| Emergency Food and Shelter National Board Program (Santa Mateo County) | 83.523 | 1-1-06 to 12-31-06 | 24-0880-00 007 Phase XXIV | 25,000 | - | 12,500 | 15,000 | 2,500 |
| Total Federal Emergency Management Agency | | | | 158,194 | 53,403 | 153,277 | 100,658 | 784 |
| <u>U.S. Department of Housing and Urban Development</u> | | | | | | | | |
| Community Development Block Grants, passed through: | | | | | | | | |
| City of Campbell | 14.218 | 7-1-05 to 6-30-06 | N/A | 7,200 | - | 7,200 | 7,200 | - |
| Town of Colma | 14.218 | 7-1-05 to 6-30-06 | N/A | 2,000 | - | 2,000 | 2,000 | - |
| City of Cupertino | 14.218 | 7-1-05 to 6-30-06 | N/A | 3,511 | - | 3,511 | 3,511 | - |
| City of Gilroy | 14.218 | 7-1-05 to 6-30-06 | N/A | 5,200 | - | 5,200 | 5,200 | - |
| Town of Los Gatos | 14.218 | 7-1-05 to 6-30-06 | N/A | 3,802 | - | 3,802 | 3,802 | - |
| City of Milpitas | 14.218 | 7-1-04 to 6-30-05 | N/A | - | 1,419 | 1,419 | - | - |
| | | 7-1-05 to 6-30-06 | N/A | 5,000 | - | 3,750 | 5,000 | 1,250 |
| City of Morgan Hill | 14.218 | 7-1-05 to 6-30-06 | N/A | 4,165 | - | 3,124 | 4,165 | 1,041 |
| City of Mountain View | 14.218 | 7-1-04 to 6-30-05 | N/A | - | 2,115 | 2,115 | - | - |
| City of Palo Alto | 14.218 | 7-1-05 to 6-30-06 | N/A | 4,741 | - | 3,556 | 4,741 | 1,185 |
| | | 7-1-04 to 6-30-05 | N/A | - | 1,789 | 1,789 | - | - |
| City of San Jose | 14.218 | 7-1-05 to 6-30-06 | N/A | 7,372 | - | 5,529 | 7,372 | 1,843 |
| | | 7-1-04 to 6-30-05 | N/A | - | 4,655 | 4,655 | - | - |
| City of San Mateo | 14.218 | 7-1-05 to 6-30-06 | N/A | 17,687 | - | 13,265 | 17,687 | 4,422 |
| City of Santa Clara | 14.218 | 7-1-05 to 6-30-06 | N/A | 10,000 | - | 7,500 | 10,000 | 2,500 |
| | | 7-1-04 to 6-30-05 | N/A | - | 1,338 | 1,338 | - | - |
| | | 7-1-05 to 6-30-06 | N/A | 6,500 | - | 5,281 | 6,500 | 1,219 |
| City of South San Francisco | 14.218 | 7-1-05 to 6-30-06 | N/A | 4,000 | - | 3,000 | 4,000 | 1,000 |
| City of Sunnyvale | 14.218 | 7-1-05 to 6-30-06 | N/A | 5,490 | - | 5,490 | 5,490 | - |
| City of Daly City | 14.218 | 7-1-05 to 6-30-06 | N/A | 9,000 | - | 9,000 | 9,000 | - |
| City of Redwood City | 14.218 | 7-1-05 to 6-30-06 | N/A | 5,000 | - | 5,000 | 5,000 | - |
| See Accompanying Notes to Schedule of Expenditures of Federal Awards. | | | | | | | | |

SECOND HARVEST FOOD BANK OF SANTA CLARA AND SAN MATEO COUNTIES
(A California Nonprofit Public Benefit Corporation)

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
(Continued)

Year Ended June 30, 2006

| Government Grantor Pass-through Grantor Program Title | Federal CFDA Number | Grant Period/ Period in Current Fiscal Year | Pass-through Grantor's Number/ Grant Number | Award Amount | Receivable (Deferred Revenue) From Prior Year | Receipt of Federal Awards | Federal Expenditures | Receivable (Deferred Revenue) at June 30, 2006 |
|--|---------------------------|--|--|-----------------|---|---------------------------------|-------------------------|---|
| Menlo Park | 14.218 | 7-1-05 to 6-30-06 | N/A | 6,600 | - | 6,600 | 6,600 | - |
| Total U.S. Department of Housing and Urban Development | | | | 107,268 | 11,316 | 104,124 | 107,268 | 14,460 |
| Total Federal Awards | | | | 2,107,837 | 97,469 | 2,046,102 | 2,138,967 | 101,668 |
| OTHER GOVERNMENTAL AWARDS | | | | | | | | |
| Santa Clara County - Department of Social Services | N/A | 7-1-04 to 6-30-05 | N/A | - | 38,147 | 38,147 | - | - |
| San Mateo County - Department of Social Services | N/A | 7-1-05 to 6-30-06 | N/A | 705,075 | - | 671,346 | 705,075 | 33,729 |
| | N/A | 7-1-04 to 6-30-05 | N/A | - | 2,921 | 2,921 | - | - |
| | N/A | 7-1-04 to 6-30-05 | N/A | - | 11,700 | 11,700 | - | - |
| | N/A | 7-1-05 to 6-30-06 | N/A | 59,658 | - | 44,743 | 59,658 | 14,915 |
| Aging and Adult Services of San Mateo (Gift Certificates) | N/A | 7-1-05 to 6-30-06 | N/A | 29,700 | - | 29,700 | 29,700 | - |
| Aging and Adult Services of San Mateo | N/A | 7-1-04 to 6-30-05 | N/A | - | 8,431 | 8,431 | - | - |
| | N/A | 7-1-04 to 6-30-05 | N/A | - | 20,000 | 20,000 | - | - |
| | N/A | 7-1-05 to 6-30-06 | N/A | 24,369 | - | 20,310 | 24,369 | 4,059 |
| | N/A | 7-1-05 to 6-30-06 | N/A | 23,020 | - | 11,510 | 23,020 | 11,510 |
| Total Other Governmental Awards | | | | 841,822 | 81,199 | 858,808 | 841,822 | 64,213 |
| TOTAL GOVERNMENTAL AWARDS | | | | \$ 2,949,659 | \$ 178,668 | \$ 2,904,910 | \$ 2,980,789 | \$ 165,881 |

See Accompanying Notes to Schedule of Expenditures of Federal Awards.

SECOND HARVEST FOOD BANK OF SANTA CLARA AND SAN MATEO COUNTIES
(A California Nonprofit Public Benefit Corporation)

NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

NOTE 1 - BASIS OF PRESENTATION:

The accompanying schedule of expenditures of federal awards includes the federal grant activity of Second Harvest Food Bank of Santa Clara and San Mateo Counties and is presented on the accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the basic financial statements.

SECTION III

REPORTS

EMERITUS

Alexander W. Berger (1916-2005)
Griffith R. Lewis

CERTIFIED PUBLIC ACCOUNTANTS AND BUSINESS ADVISORS

REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE
AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED
IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

To the Board of Directors
Second Harvest Food Bank of Santa Clara and San Mateo Counties
(A California Nonprofit Public Benefit Corporation)
San Jose, California

We have audited the financial statements of Second Harvest Food Bank of Santa Clara and San Mateo Counties (a California nonprofit public benefit corporation) as of and for the year ended June 30, 2006, and have issued our report thereon dated August 15, 2006. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Second Harvest Food Bank of Santa Clara and San Mateo Counties' internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Second Harvest Food Bank of Santa Clara and San Mateo Counties' financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of the audit committee, management, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Berger/Lewis Accountancy Corporation

BERGER/LEWIS ACCOUNTANCY CORPORATION
San Jose, California
August 15, 2006

EMERITUS

Alexander W. Berger (1916-2005)
Griffith R. Lewis

CERTIFIED PUBLIC ACCOUNTANTS AND BUSINESS ADVISORS

REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO EACH MAJOR
PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH
OMB CIRCULAR A-133

To the Board of Directors
Second Harvest Food Bank of Santa Clara and San Mateo Counties
(A California Nonprofit Public Benefit Corporation)
San Jose, California

Compliance

We have audited the compliance of Second Harvest Food Bank of Santa Clara and San Mateo Counties (a California nonprofit public benefit corporation) with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) *Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended June 30, 2006. Second Harvest Food Bank of Santa Clara and San Mateo Counties' major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of Second Harvest Food Bank of Santa Clara and San Mateo Counties' management. Our responsibility is to express an opinion on Second Harvest Food Bank of Santa Clara and San Mateo Counties' compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about Second Harvest Food Bank of Santa Clara and San Mateo Counties' compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of Second Harvest Food Bank of Santa Clara and San Mateo Counties' compliance with those requirements.

In our opinion, Second Harvest Food Bank of Santa Clara and San Mateo Counties complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2006.

Internal Control Over Compliance

The management of Second Harvest Food Bank of Santa Clara and San Mateo Counties is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered Second Harvest Food Bank of Santa Clara and San Mateo Counties' internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on the internal control over compliance in accordance with OMB Circular A-133.

Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with applicable requirements of laws, regulations, contracts, and grants caused by error or fraud that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over compliance and its operation that we consider to be material weaknesses.

This report is intended solely for the information and use of the audit committee, management, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Berger/Lewis Accountancy Corporation

BERGER/LEWIS ACCOUNTANCY CORPORATION
San Jose, California
August 15, 2006

SECTION IV

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

SECOND HARVEST FOOD BANK OF SANTA CLARA AND SAN MATEO COUNTIES
(A California Nonprofit Public Benefit Corporation)

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

Year Ended June 30, 2006

SUMMARY OF AUDITOR'S RESULTS:

1. The auditor's report expresses an unqualified opinion on the financial statements of Second Harvest Food Bank of Santa Clara and San Mateo Counties.
2. No reportable conditions relating to the audit of the financial statements are reported in the Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance With *Government Auditing Standards*.
3. No instances of noncompliance material to the financial statements of Second Harvest Food Bank of Santa Clara and San Mateo Counties, which would be required to be reported in accordance with *Government Auditing Standards*, were disclosed during the audit.
4. No reportable conditions relating to the audit of the major federal award programs are reported in the Report on Compliance with Requirements Applicable to Each Major Program and on Internal Control Over Compliance in Accordance with OMB Circular A-133.
5. The auditors' report on compliance for the major federal award programs for Second Harvest Food Bank of Santa Clara and San Mateo Counties expresses an unqualified opinion on all major federal programs.
6. No audit findings which would be required to be reported in accordance with Section 510(a) of OMB Circular A-133 are reported in this Schedule.
7. The program tested as a major program included: Emergency Food Assistance Program (Food Commodities) - CFDA 10.569, Grant No. E65088.
8. The threshold for distinguishing Type A and B programs was \$300,000.
9. Second Harvest Food Bank of Santa Clara and San Mateo Counties qualified as a low-risk auditee.

FINDINGS - FINANCIAL STATEMENT AUDIT:

None

FINDINGS AND QUESTIONED COSTS - MAJOR FEDERAL AWARD PROGRAMS AUDIT:

U.S. DEPARTMENT OF AGRICULTURE

Name of program - Emergency Food Assistance Program (Food Commodities)

CFDA No. - 10.569

Grant No. - E65088

Grant period - 7/1/05 to 6/30/06

None

SECOND HARVEST FOOD BANK OF SANTA CLARA AND SAN MATEO COUNTIES
(A California Nonprofit Public Benefit Corporation)

SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS

Year Ended June 30, 2006

NONE