

**Second Harvest Food Bank of Santa Clara and  
San Mateo Counties**

Financial Statements  
and Single Audit Reports and Schedules

June 30, 2016  
(With Comparative Totals for 2015)



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## INDEPENDENT AUDITOR'S REPORT

To the Board of Directors  
Second Harvest Food Bank of Santa Clara and San Mateo Counties  
San Jose, California

We have audited the accompanying financial statements of Second Harvest Food Bank of Santa Clara and San Mateo Counties (a California nonprofit corporation) (the "Food Bank"), which comprise the statement of financial position as of June 30, 2016, and the related statements of activities, functional expenses, and cash flows for the year then ended, and the related notes to the financial statements.

### **Management's Responsibility for the Financial Statements**

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America (the "U.S."); this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

### **Auditor's Responsibility**

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the U.S. and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the U.S. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### **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, 2016, and the changes in its net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the U.S.

## **Other Matter**

Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The accompanying schedule of expenditures of federal and other governmental awards, as required by Title 2 U.S. *Code of Federal Regulations* (CFR) Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards*, is presented for purposes of additional analysis and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the U.S. In our opinion, the information is fairly stated, in all material respects, in relation to the financial statements as a whole.

## **Other Reporting Required by *Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated October 5, 2016, on our consideration of the Food Bank's 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 internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Food Bank's internal control over financial reporting and compliance.

## **Report on Summarized Comparative Information**

We have previously audited Second Harvest Food Bank of Santa Clara and San Mateo Counties' 2015 financial statements, and our report dated October 15, 2015 expressed an unmodified opinion on those audited financial statements. In our opinion, the summarized comparative information presented herein as of and for the year ended June 30, 2015, is consistent, in all material respects, with the audited financial statements from which it has been derived.



Armanino<sup>LLP</sup>  
San Jose, California

October 5, 2016

Second Harvest Food Bank of Santa Clara and San Mateo Counties  
Statement of Financial Position  
June 30, 2016  
(With Comparative Totals for 2015)

	Unrestricted	Temporarily Restricted	2016 Total	2015 Total
ASSETS				
Cash and cash equivalents	\$ 11,877,619	\$ 2,569,061	\$ 14,446,680	\$ 15,626,840
Accounts receivable	14,949	-	14,949	14,234
Grants receivable	545,980	65,000	610,980	596,519
Pledges receivable (Note 3)	491,000	4,849,931	5,340,931	896,352
Inventory (Note 4)	3,557,758	-	3,557,758	2,193,673
Prepaid expenses and other assets	732,323	-	732,323	688,750
Investments - board-designated endowment (Notes 5 and 6)	5,404,985	-	5,404,985	4,938,117
Investments - other (Notes 5 and 6)	18,467,110	-	18,467,110	18,320,036
Land, buildings and equipment, net (Note 7)	23,630,429	-	23,630,429	23,656,774
Total assets	\$ 64,722,153	\$ 7,483,992	\$ 72,206,145	\$ 66,931,295
LIABILITIES AND NET ASSETS				
Liabilities				
Accounts payable	\$ 1,395,245	\$ -	\$ 1,395,245	\$ 1,707,361
Accrued expenses	1,035,673	-	1,035,673	1,134,843
Deferred revenue	3,000	-	3,000	-
Total liabilities	2,433,918	-	2,433,918	2,842,204
Net assets				
Unrestricted				
Undesignated	500,000	-	500,000	500,000
Board designated (Note 12)	38,157,806	-	38,157,806	35,374,723
Land, building and equipment fund	23,630,429	-	23,630,429	23,656,774
Total unrestricted	62,288,235	-	62,288,235	59,531,497
Temporarily restricted (Note 14)	-	7,483,992	7,483,992	4,557,594
Total net assets	62,288,235	7,483,992	69,772,227	64,089,091
Total liabilities and net assets	\$ 64,722,153	\$ 7,483,992	\$ 72,206,145	\$ 66,931,295

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

Second Harvest Food Bank of Santa Clara and San Mateo Counties  
Statement of Activities  
For the Year Ended June 30, 2016  
(With Comparative Totals for 2015)

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>2016 Total</u>	<u>2015 Total</u>
Support and revenue				
Support				
Contributions	\$ 26,890,711	\$ 12,634,086	\$ 39,524,797	\$ 35,374,299
Contributions - capital campaign	-	24,745	24,745	35,000
Contributions in-kind - non-government (Note 15)	76,496,786	-	76,496,786	77,233,947
Special events, net	-	-	-	68,390
United Way support	<u>185,001</u>	<u>-</u>	<u>185,001</u>	<u>178,175</u>
Total support	<u>103,572,498</u>	<u>12,658,831</u>	<u>116,231,329</u>	<u>112,889,811</u>
Revenue				
Government assistance - cash	1,868,555	130,000	1,998,555	2,112,830
Government assistance - in-kind (Note 15)	9,236,486	-	9,236,486	8,219,838
Net investment income (Note 5)	87,585	-	87,585	126,646
Other gains	<u>67,903</u>	<u>-</u>	<u>67,903</u>	<u>57,298</u>
Total revenue	<u>11,260,529</u>	<u>130,000</u>	<u>11,390,529</u>	<u>10,516,612</u>
Total support and revenue	114,833,027	12,788,831	127,621,858	123,406,423
Net assets released from restriction (Note 14)	<u>9,862,433</u>	<u>(9,862,433)</u>	<u>-</u>	<u>-</u>
Total support, revenue, and net assets released from restriction	<u>124,695,460</u>	<u>2,926,398</u>	<u>127,621,858</u>	<u>123,406,423</u>
Functional expenses				
Program services	<u>116,194,917</u>	<u>-</u>	<u>116,194,917</u>	<u>113,666,712</u>
Support services				
Management and general	2,390,707	-	2,390,707	2,034,816
Fundraising	<u>3,353,098</u>	<u>-</u>	<u>3,353,098</u>	<u>3,117,562</u>
Total support services	<u>5,743,805</u>	<u>-</u>	<u>5,743,805</u>	<u>5,152,378</u>
Total functional expenses	<u>121,938,722</u>	<u>-</u>	<u>121,938,722</u>	<u>118,819,090</u>
Change in net assets	2,756,738	2,926,398	5,683,136	4,587,333
Net assets, beginning of year	<u>59,531,497</u>	<u>4,557,594</u>	<u>64,089,091</u>	<u>59,501,758</u>
Net assets, end of year	<u>\$ 62,288,235</u>	<u>\$ 7,483,992</u>	<u>\$ 69,772,227</u>	<u>\$ 64,089,091</u>

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

Second Harvest Food Bank of Santa Clara and San Mateo Counties  
Statement of Functional Expenses  
For the Year Ended June 30, 2016  
(With Comparative Totals for 2015)

	Program services	Support services		Total support services	2016 Total	2015 Total
		Management and general	Fundraising			
Personnel expenses						
Salaries and wages	\$ 7,734,924	\$ 1,095,444	\$ 1,134,141	\$ 2,229,585	\$ 9,964,509	\$ 8,799,252
Employee benefits	1,584,428	224,391	232,319	456,710	2,041,138	1,889,266
Payroll taxes	550,885	77,077	84,460	161,537	712,422	683,800
Worker's compensation insurance	<u>213,052</u>	<u>4,083</u>	<u>8,576</u>	<u>12,659</u>	<u>225,711</u>	<u>176,056</u>
Total personnel expenses	10,083,289	1,400,995	1,459,496	2,860,491	12,943,780	11,548,374
Donated food and supplies distributed	84,419,887	-	-	-	84,419,887	85,423,742
Procured food and supplies distributed	14,205,345	-	-	-	14,205,345	12,080,653
Depreciation	1,407,810	134,522	141,524	276,046	1,683,856	1,695,656
Occupancy	937,773	85,823	88,873	174,696	1,112,469	851,752
Freight and storage	986,746	-	-	-	986,746	1,065,793
Professional services	506,230	365,780	90,266	456,046	962,276	541,143
Outside services	809,503	8,752	58,524	67,276	876,779	684,988
Equipment for agency infrastructure	756,759	-	-	-	756,759	801,982
Supplies, including in-kind	572,716	15,217	90,599	105,816	678,532	709,229
Direct mailing costs	-	-	646,481	646,481	646,481	637,705
Advertising and media, including in-kind	102,680	-	462,747	462,747	565,427	657,189
Vehicle operating costs	447,602	163	213	376	447,978	502,940
Postage and printing	147,682	7,379	219,560	226,939	374,621	418,434
Equipment rental and maintenance	280,939	29,272	28,945	58,217	339,156	306,186
Bank and payroll charges	-	237,315	-	237,315	237,315	223,134
Insurance	180,298	36,651	3,081	39,732	220,030	207,279
Telephone	149,136	21,121	21,867	42,988	192,124	178,298
Conferences, conventions, and meetings	71,063	23,497	18,347	41,844	112,907	86,352
Dues and subscriptions	33,922	16,131	14,110	30,241	64,163	50,449
Travel	32,523	2,362	4,847	7,209	39,732	40,014
Volunteer expenses	31,494	-	-	-	31,494	25,571
Recruitment expenses	12,542	5,727	3,618	9,345	21,887	55,059
Affiliation fees (Note 16)	18,978	-	-	-	18,978	18,424
Interest	-	-	-	-	-	8,744
	<u>\$ 116,194,917</u>	<u>\$ 2,390,707</u>	<u>\$ 3,353,098</u>	<u>\$ 5,743,805</u>	<u>\$ 121,938,722</u>	<u>\$ 118,819,090</u>
Percentage of total	<u>95.3 %</u>	<u>2.0 %</u>	<u>2.7 %</u>	<u>4.7 %</u>	<u>100.0 %</u>	

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

Second Harvest Food Bank of Santa Clara and San Mateo Counties  
Statement of Cash Flows  
For the Year Ended June 30, 2016  
(With Comparative Totals for 2015)

	2016	2015
Cash flows from operating activities		
Changes in net assets	\$ 5,683,136	\$ 4,587,333
Adjustments to reconcile changes in net assets to net cash provided by operating activities		
Depreciation	1,683,856	1,695,656
(Gain) loss on sale of equipment	1,337	(10,729)
Donated vehicles and equipment	(13,794)	(28,348)
Net present value amortization adjustment	250,889	(43,753)
Contributions restricted for long-term purposes	-	(1,486,413)
In-kind contributions of food and non-food (including USDA)	(85,616,010)	(85,220,016)
Distribution of food and non-food received in-kind	84,419,887	85,423,742
Net realized and unrealized losses on investments	374,849	316,106
Changes in operating assets and liabilities		
Accounts receivable	(715)	(5,309)
Grants receivable	(14,461)	(197,888)
Pledges receivable	(4,695,468)	1,471,873
Purchased inventory (food)	(167,961)	(53,882)
Prepaid expenses and other assets	(43,576)	25,298
Accounts payable	87,629	(586,088)
Accrued expenses	(99,170)	130,681
Deferred revenue	3,000	-
Net cash provided by operating activities	1,853,428	6,018,263
Cash flows from investing activities		
Purchase of land, building and equipment	(2,049,197)	(1,479,251)
Proceeds from sale of equipment	4,400	16,557
Purchase of investments	(9,004,166)	(11,347,085)
Proceeds from sale of investments	8,015,375	9,410,673
Net cash used in investing activities	(3,033,588)	(3,399,106)
Cash flows from financing activities		
Contributions restricted for long-term purposes	-	1,486,413
Payment on note payable	-	(1,000,000)
Net cash provided by financing activities	-	486,413
Net increase (decrease) in cash and cash equivalents	(1,180,160)	3,105,570
Cash and cash equivalents, beginning of year	15,626,840	12,521,270
Cash and cash equivalents, end of year	\$ 14,446,680	\$ 15,626,840

Supplemental schedule of noncash investing and financing activities

Land, building and equipment acquired with short-term debt	\$ -	\$ 399,744
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The accompanying notes are an integral part of these financial statements.



Second Harvest Food Bank of Santa Clara and San Mateo Counties  
Notes to Financial Statements  
June 30, 2016  
(With Comparative Totals for 2015)

1. ORGANIZATION

A New Hunger Paradigm

Second Harvest Food Bank of Santa Clara and San Mateo Counties, a nonprofit 501(c)(3) organization founded in 1979, realized significant progress in achieving its strategic goals during its 2015-2016 fiscal year. Also known as the "Food Bank" or "Second Harvest," the organization enhanced its traditional food banking operations and pursued innovative solutions to address a new hunger paradigm. Second Harvest serves a region that is today the epicenter of California's Silicon Valley. The home to leading technology companies, like Facebook, Google and Oracle, Silicon Valley faces a unique and growing hunger challenge.

The Silicon Valley economy has generated immense prosperity for a select few. At the same time, the cost of living has soared. This duality has created a paradox, where over the past few years, economic growth ironically led to the Food Bank serving more, not fewer, clients. Those living in the shadow of the technology economy, who do not benefit from high paying tech jobs, find themselves increasingly food insecure. Many middle class families are only one crisis away from facing food scarcity. Rising medical costs, along with other living costs, increase the hunger vulnerability of the elderly. Escalating college expenses, including housing costs, increasingly put university students at risk.

The profiles of those in need are changing in ways that create new challenges in terms of both reaching and serving them. The dynamism of the Silicon Valley economy generates unusually high population movement around transplants, immigrants and commuters who hold down jobs critical to the area's economy but often don't earn enough to be food secure. Soaring rent costs not only leave families with less money for meals but sometimes force them to live in a garage or other atypical arrangement. Without access to a kitchen, families often turn to a poor diet of fast-food specials to stretch their available food budgets. Along with facing greater risks around malnutrition, they also cannot make good use of unprepared foods.

Enhancing Traditional Food Banking

Responding to this new hunger paradigm, Second Harvest enhanced its existing operations. Investing in its infrastructure to support expanded services enabled the Food Bank to distribute over 54 million meals during the fiscal year to hungry people in the community. Over the past three years, Second Harvest has invested approximately \$1.9 million – including \$757,000 this year alone – in mission-critical equipment and facilities for many of its distribution partners, thereby strengthening the nutritional safety net for hundreds of thousands of local residents. During the fiscal year, the number of unique sites of the Food Bank and its 317 member nonprofit network increased by 26 percent to 858 sites, with particularly notable growth in family and children sites, school pantries, multi-service sites and soup kitchens.

Second Harvest Food Bank of Santa Clara and San Mateo Counties  
Notes to Financial Statements  
June 30, 2016  
(With Comparative Totals for 2015)

1. ORGANIZATION (continued)

Enhancing Traditional Food Banking (continued)

The Food Bank continued to develop an especially robust organizational structure well beyond its own facilities and employees, as well as those of partners, to also encompass extensive volunteer and donor networks. During the fiscal year, Food Bank volunteers contributed over 310,000 hours of time, valued at \$6.6 million. To duplicate this amount of work would have necessitated almost 150 full-time employees. Instead, funds were able to go into providing more food. Second Harvest's dynamic donor base made more than 93,000 gifts totaling over \$34 million. As a result, the Food Bank provided enormous quantities of food to its partner agencies. It also remained one of the few in the Feeding America national network of 200 regional food banks to do so free of charge to often cash-strapped local shelters, soup kitchens and pantries.

Despite the outward appearance of prosperity in Silicon Valley, the Food Bank served an average of almost 253,000 people a month during the fiscal year. This marked an increase of approximately 9,000 from the prior period - a number only exceeded in the depths of the Great Recession. Impressive numbers served and sites added were not the only measures of achievement. Charity Navigator, the nation's largest and most-utilized evaluator of charities, ranked Second Harvest among the top 50 charities in the United States, based on accountability, transparency and financial health. The Food Bank also passed AIB food safety audits at each of its three facilities, including Second Harvest's 75,000-square-foot produce distribution center.

Improving Community Health

During the fiscal year, the Food Bank redoubled efforts to improve community health. Already providing more fresh produce to its clients than any other food bank in the country, Second Harvest raised the bar even higher in terms of food mix quality. The Grocery Rescue program, which involves rescuing mostly perishable proteins, produce and dairy from being wasted by local retailers, was expanded by an impressive 25 percent. The Food Bank also aggressively sourced donations, increased its purchased food budget, and bought in bulk with other food banks to reduce the cost of acquiring protein items. As a result, the amount of high-quality dairy and protein items provided to clients jumped an impressive 42 percent.

The dramatic improvement in food quality was part of a focused effort to solve health issues arising from hunger in Silicon Valley. Local populations unable to afford nutritious meals are at particular risk for diabetes and high blood pressure. In one innovative solution focused on diabetes, Second Harvest worked with a local free clinic to open what the Food Bank believes is the first Food Pharmacy in California. Following a doctor's visit, a patient can receive education on how to prepare healthy meals and then obtain free food. In addition to providing economic access to those in need, the location also provides physical access by being located in the same building with clients' health service providers.

Second Harvest Food Bank of Santa Clara and San Mateo Counties  
Notes to Financial Statements  
June 30, 2016  
(With Comparative Totals for 2015)

1. ORGANIZATION (continued)

Improving Community Health (continued)

Second Harvest also introduced a new Healthy Food and Beverage Policy that highlighted its commitment to enhance the health of all members of the community. This policy will guide ongoing improvements in the food mix. Because access to nutritious meals is a key ingredient to success at school, Second Harvest continued to expand its school programs. Impressively, working with a variety of local nonprofit partners, the Food Bank opened 24 new school pantries – including several on college campuses – representing a 41 percent jump in their number.

Working Smarter to Overcome Hunger

Despite all of these achievements, the sobering reality is that the Food Bank must do more to solve a local hunger problem, which is only becoming more challenging. To overcome hunger in Silicon Valley will require working harder and smarter by both enhancing existing operations and innovating new solutions, like the Food Pharmacy. To serve those without access to a kitchen, for example, Second Harvest is investigating new prepared meal solutions. The Food Bank also initiated a comprehensive market research study to size and segment the hunger "market" during the fiscal year. In addition, a new strategic plan was developed to realize the vision of building a hunger-free community by addressing the Silicon Valley hunger paradigm.

The new strategic plan incorporates five key initiatives. The first confronts hunger by expanding operations to capacity and piloting new food sourcing models. The second, epitomized by the new Healthy Food and Beverage Policy, incorporates health as a key focus. A community access initiative will pursue new ways to deliver food by better understanding client needs. In addition, Second Harvest will lead efforts to both increase participation in existing but underutilized government programs and make hunger a top priority for public policy makers in order to harness the resources needed to solve this problem. Lastly, the Moonshot initiative envisions the Food Bank essentially disrupting itself – reimagining traditional food banking and incorporating new innovative solutions to address hunger.

Second Harvest believes that creating a hunger-free community in Silicon Valley requires a smart, comprehensive and deeply ambitious effort. The scope of that endeavor is best represented in the goals of the new strategic plan, which include increasing the number of people served by 40 percent to 350,000 and growing the number of meals provided by 15 million over the next three years. Although ambitious, these goals are also attainable. To be ready to meet them, Second Harvest enhanced its traditional food banking operations while exploring new innovative hunger solutions during the fiscal year. Building on a foundation of an enhanced infrastructure and a track record of success, Second Harvest is today leading the effort to solve the paradoxical problem around troubling levels of hunger amidst the prosperity of Silicon Valley.

Second Harvest Food Bank of Santa Clara and San Mateo Counties  
Notes to Financial Statements  
June 30, 2016  
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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.

Financial statement presentation

In accordance with accounting principles generally accepted in the United States of America, the Food Bank 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 Food Bank. Under this category, the Food Bank 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 nonexpiring donor restriction, such as endowments. There are currently no permanently restricted net assets.
- Land, building and equipment fund is 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.

Use of estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the U.S. 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 support, revenue and expenses during the period. Accordingly, actual results could differ from those estimates.

Second Harvest Food Bank of Santa Clara and San Mateo Counties  
Notes to Financial Statements  
June 30, 2016  
(With Comparative Totals for 2015)

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

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 accounting principles generally accepted in the United States of America. Accordingly, such information should be read in conjunction with the Food Bank's financial statements for the year ended June 30, 2015, from which the summarized information was derived.

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 Food Bank maintains its cash in bank deposit accounts which, at times, may exceed federally insured limits. The Food Bank 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 Food Bank 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 non-government food and donated government food was valued at \$1.67 and \$1.70 per pound for the years ended June 30, 2016 and 2015, respectively. This valuation is based on a cost study conducted for Feeding America. Purchased food is valued at the latest purchase price.

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 and losses are included in the change in net assets.

Fair value measurements

Fair value is defined as "the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date."

Second Harvest Food Bank of Santa Clara and San Mateo Counties  
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2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Fair value measurements (continued)

A hierarchy has been established to prioritize the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest ranking to fair values determined using unadjusted quoted prices in active markets for identical assets (Level 1) and the lowest ranking to fair values determined using methodologies and models with unobservable inputs (Level 3). Observable inputs are those that market participants would use in pricing the asset based on market data obtained from sources independent of the Food Bank. Unobservable inputs reflect the Food Bank's assumption about the inputs market participants would use in pricing the asset or liability developed based on the best information available in the circumstances.

The fair value hierarchy is categorized into three levels based on the inputs as follows:

- *Level 1* - Values are unadjusted quoted prices for identical assets and liabilities in active markets accessible at the measurement date.
- *Level 2* - Inputs include quoted prices for similar assets or liabilities in active markets, quoted prices from those willing to trade in markets that are not active, or other inputs that are observable or can be corroborated by market data for the term of the instrument. Such inputs include market interest rates and volatilities, spreads and yield curves.
- *Level 3* - Certain inputs are unobservable (supported by little or no market activity) and significant to the fair value measurement. Unobservable inputs reflect the Food Bank's best estimate of what hypothetical market participants would use to determine a transaction price for the asset or liability at the reporting date.

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 flexible time off (FTO)

Accrued FTO represents vacation and sick time earned, but not taken as of June 30, 2016 and 2015. The maximum FTO that can be accrued and carried over to the next year is 300 hours for employees hired prior to March 10, 2008 and 240 hours for employees hired after March 10, 2008. The accrued FTO balance as of June 30, 2016 and 2015 was \$684,761 and \$679,731, respectively, and is included in accrued expenses.

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2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Revenue recognition

The Food Bank 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 recognized when the donor makes a pledge to give that is, in substance, an unconditional promise. Second Harvest will not recognize a conditional promise to give until the conditions on which the promise depends are substantially met. A promise that calls for specific outcomes to be achieved will be treated as a conditional promise to give. 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.

Contributions in-kind

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 Food Bank would have paid for if not donated, are recorded at the estimated fair value at the time the services are rendered. The Food Bank also receives donated services that do not require specific expertise but which are nonetheless central to the Food Bank's operations. While these contributed services are not reflected in the financial statements the estimated value of these services is disclosed in Note 15.

Functional expense allocations

Management estimates Second Harvest's indirect salary expense allocation based on individual employees estimated time spent by function or time studies. Management's estimate of other indirect costs are based on salary expense, poundage, or actual food distribution by counties.

Income tax status

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.

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2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Income tax status (continued)

Accounting principles generally accepted in the United States of America provide accounting and disclosure guidance about positions taken by an organization in its tax returns that might be uncertain. Management has considered its tax positions and believes that all of the positions taken by the Food Bank in its federal and state exempt organization tax returns are more-likely-than-not to be sustained upon examination.

The Food Bank's federal returns for the years ended June 30, 2015, 2014 and 2013 could be subject to examination by federal taxing authorities, generally for 3 years after they are filed. The Food Bank's state returns for the years ended June 30, 2015, 2014, 2013 and 2012 could be subject to examination by state taxing authorities, generally for 4 years after they are filed.

Advertising costs

Advertising costs are charged to operations when incurred. Advertising costs for the years ended June 30, 2016 and 2015 totaled \$565,427 and \$657,189, respectively. Of these costs, \$46,499 and \$103,389, respectively were in-kind contributions.

Subsequent events

Management of the Food Bank has evaluated events and transactions subsequent to June 30, 2016 for potential recognition or disclosure in the financial statements. The Food Bank did not have subsequent events that required recognition or disclosure in the financial statements for the fiscal year ended June 30, 2016. Subsequent events have been evaluated through the date the financial statements became available to be issued, October 5, 2016.

Reclassifications

Certain amounts in the prior year have been reclassified in order to be consistent with the current year presentation.



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3. PLEDGES RECEIVABLE

Pledges receivable consist of the following:

	2016	2015
Pledges receivable in less than one year	\$ 1,823,500	\$ 528,032
Pledges receivable in one to five years	3,800,000	400,000
	5,623,500	928,032
Less discounts to net present value	(282,569)	(31,680)
	\$ 5,340,931	\$ 896,352

Cypress Semiconductor pledged \$4 million to enable the acquisition of the new facility. The amount and timing of the pledge payments coincides with the terms of the installment loan (see Note 9).

4. 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 non-government food and donated government food was valued at \$1.67 and \$1.70 per pound for the years ended June 30, 2016 and 2015, respectively. This valuation is based on a cost study conducted for Feeding America. Purchased food is valued at the latest purchase price. All donated food, non-food items and USDA commodities inventory are classified as Level 2 assets and all purchased food inventory is classified as a Level 1 asset (see Note 2).

Inventory consists of the following:

	2016	2015
Donated non-government food and non-food	\$ 2,137,579	\$ 1,333,578
USDA food commodities	742,763	350,640
Purchased food	677,416	509,455
	\$ 3,557,758	\$ 2,193,673

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5. INVESTMENTS

Investments consist of the following:

	2016	2015
Investments - board designated endowment (Note 12)	\$ 5,404,985	\$ 4,938,117
Investments - other	18,467,110	18,320,036
	\$ 23,872,095	\$ 23,258,153

Investment earnings (losses) consist of the following:

	2016	2015
Interest and dividends	\$ 656,690	\$ 579,673
Net realized and unrealized losses	(374,849)	(316,106)
	281,841	263,567
Investment fees	(194,256)	(136,921)
	\$ 87,585	\$ 126,646

6. FAIR VALUE MEASUREMENTS

The Food Bank'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 Food Bank's investment portfolio is structured and maintained with the overall objective of providing the resources and liquidity for the Food Bank to fulfill its mission statement. All of the following investments are classified as Level 1 investments (see Note 2).

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6. FAIR VALUE MEASUREMENTS (continued)

The following table sets forth by level, within the fair value hierarchy, the Food Bank's assets at fair value as of June 30, 2016:

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Equity investments	\$ 11,018,324	\$ -	\$ -	\$ 11,018,324
Corporate bonds and notes	-	6,979,454	-	6,979,454
U.S. government securities and agency obligations	3,138,638	-	-	3,138,638
Money market investments	1,070,054	-	-	1,070,054
Mutual funds	914,565	-	-	914,565
Real estate investment trusts	-	638,324	-	638,324
Master limited partnership	-	112,736	-	112,736
	<u>\$ 16,141,581</u>	<u>\$ 7,730,514</u>	<u>\$ -</u>	<u>\$ 23,872,095</u>

The following table sets forth by level, within the fair value hierarchy, the Food Bank's assets at fair value as of June 30, 2015:

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
Equity investments	\$ 9,048,974	\$ -	\$ -	\$ 9,048,974
U.S. government securities and agency obligations	4,785,915	-	-	4,785,915
Corporate bonds and notes	-	4,707,307	-	4,707,307
Mutual funds	2,888,725	-	-	2,888,725
Money market investments	1,009,574	-	-	1,009,574
Real estate investment trusts	-	542,715	-	542,715
Commodities	274,943	-	-	274,943
	<u>\$ 18,008,131</u>	<u>\$ 5,250,022</u>	<u>\$ -</u>	<u>\$ 23,258,153</u>

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7. LAND, BUILDING AND EQUIPMENT

Land, building and equipment consist of the following:

	2016	2015
Land	\$ 3,865,858	\$ 3,865,858
Building and improvements	23,553,013	22,876,564
Equipment	10,673,321	9,805,312
Construction-in-progress	449,653	346,976
	38,541,845	36,894,710
Accumulated depreciation	(14,911,416)	(13,237,936)
	\$ 23,630,429	\$ 23,656,774

Depreciation expense for the years ended June 30, 2016 and 2015 totaled \$1,683,856 and \$1,695,656, respectively.

8. LINE OF CREDIT

The Food Bank established a revolving line of credit with Wells Fargo Bank to meet short-term working capital borrowing needs. Borrowings under the line of credit for the fiscal years ended June 30, 2016 and 2015 were limited to a maximum of \$4,000,000. Interest on outstanding funds is payable monthly at the bank's prime rate and has a floor rate of 3.5%. The maturity date was April 10, 2016 and has been extended to May 10, 2017. The credit line is secured by certain assets owned by the Food Bank and contains a covenant clause that requires \$8,000,000 of liquidity in cash and investments. There was no balance outstanding or related interest expense on this line of credit for either of the years ended June 30, 2016 and 2015.

9. NOTE PAYABLE

During the year ended June 30, 2011 the Food Bank acquired from Cypress Semiconductor a building to be used as a food distribution warehouse. To acquire the building, the Food Bank entered into a loan payable in the amount \$4,000,000 to Cypress Semiconductor. The loan bore 0% interest and was payable in four equal annual payments of \$1,000,000 beginning on December 31, 2011. During the year ended June 30, 2015 the final payment of \$1,000,000 was made.

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10. COMMITMENTS AND CONTINGENCIES

Operating leases

The Food Bank 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.

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 Food Bank 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 through the year ended June 30, 2016.

11. RETIREMENT PLAN

The Food Bank maintains a tax deferred 403(b) retirement plan (the "Plan") to provide retirement benefits for all eligible employees. The plan provides for Food Bank contributions of 5% of eligible employee compensation. Vesting is based on years of service, with 100% vesting of employer matching contributions upon eligibility. Food Bank contributions for the years ended June 30, 2016 and 2015 were \$407,996 and \$377,938, respectively. All of the Plan's administration costs were paid for by the Plan.

12. BOARD DESIGNATED NET ASSETS

As part of the Food Bank's annual review of designated assets, the Board adopted specific guidelines for establishing the level of each designation. Operating reserves include approximately six months of the coming year's annual budget, with adjustments for purchased inventory on hand and current liabilities. Current investment in inventory is reviewed on a monthly basis and is generally below one month's distribution. The designation for capital replacement fund is calculated as the present-value of a ten year asset replacement plan.

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12. BOARD DESIGNATED NET ASSETS (continued)

Board designated net assets consist of the following:

	2016	2015
Operating fund		
Designated for operating reserves	\$ 18,784,228	\$ 18,056,128
Urgent food and infrastructure fund	1,500,000	1,500,000
Inventory	3,557,758	2,193,673
Board-designated endowment fund (pledges)	900	900
Board-designated endowment fund (investment)	5,404,985	4,938,117
	29,247,871	26,688,818
Land, building and equipment fund		
Designated for capital replacement	8,909,935	8,685,905
	\$ 38,157,806	\$ 35,374,723

13. BOARD DESIGNATED ENDOWMENT FUND

Second Harvest Food Bank of Santa Clara and San Mateo Counties' Board Designated Endowment consists of unrestricted net assets which the Board of Directors has chosen to hold as a general endowment fund (the "Fund") to support the mission of the Food Bank.

Interpretation of relevant law

The Food Bank's Board of Directors has interpreted UPMIFA as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the Food Bank classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Food Bank in a manner consistent with the standard of prudence prescribed by UPMIFA.

In accordance with UPMIFA, the Food Bank considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

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13. BOARD DESIGNATED ENDOWMENT FUND (continued)

Interpretation of relevant law (continued)

- (1) The duration and preservation of the fund
- (2) The purposes of the Food Bank and the donor-restricted endowment fund
- (3) General economic conditions
- (4) The possible effect of inflation and deflation
- (5) The expected total return from income and the appreciation of investments
- (6) Other resources of the Food Bank
- (7) The investment policies of the Food Bank

Return objectives and risk parameters

The Board Designated Endowment (the "Fund") was created to ensure a reasonable, predictable, and sustainable source of funds. The Food Bank will designate 90% of each unrestricted donor bequest to the endowment. The Fund will be used to produce a growing level of income in order to support future activities, programs and the capital needs of the Food Bank. The Food Bank's objective is to provide a predictable stream of funding while seeking to maintain the purchasing power of the Fund's assets and preserve capital. The primary goal is to seek a total return (net of fees and expenses) that equals at least 500 basis points over the inflation rate, as measured by the Consumer Price Index on an annualized basis. These objectives and goals are expected to be achieved over 6-10 years.

Strategies employed for achieving objectives

The Board has determined that the assets of the Fund will be professionally managed in a moderately conservative manner. Management of the Fund's portfolio should focus on satisfying these objectives through the optimal allocation of stocks and fixed income securities. Fixed income securities should be used to satisfy current income requirements and control total portfolio volatility. Common stocks should generate income and capital growth to preserve and enhance the purchasing power of the portfolio. The nature of the assets involved and the long-term objectives of the Fund suggest utilizing a "total return approach" to investment management.

The Equity portion of the Fund will consist of publicly traded common and preferred stocks and convertible debt. It is expected that 40% to 70% (with a target of 57%) of the Fund will be invested in equity and/or equity mutual funds. It is expected that 30% to 60% (with a target of 38%) of the Fund will be invested in fixed income securities. It is expected that 0% to 7% (with a target of 5%) of the Fund will be invested in alternative investments.

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13. BOARD DESIGNATED ENDOWMENT FUND (continued)

Spending policy and how investment objectives relate to spending policy

The Board's first objective was to grow the fund to \$1,000,000 which was achieved as of June 30, 2014. Starting July 1, 2014 the Fund's spending policy aims to ensure a prudent tradeoff between current program needs and long-term purchasing power. Therefore, the spending range of 4% to 5.75%, with a desired optimal target of 5%, is considered prudent.

The amount of funds allocated for expenditure ("Spending Allocation") will be calculated in April of each year and based on the rolling prior 12-quarter average. If less than 12 quarters are available then the available quarters will be used. The Spending Allocation will be transferred to the operations account between July and October in the fiscal year following the calculation.

Endowment composition

Changes in board-designated endowment net assets are as follows:

	2016	2015
Balance, beginning of year	\$ 4,939,017	\$ 4,551,615
Transfers to board designated endowment fund	407,245	406,748
Investment income	100,674	15,829
Investment fees	(41,051)	(35,175)
Balance, end of year	\$ 5,405,885	\$ 4,939,017



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14. TEMPORARILY RESTRICTED NET ASSETS

Temporarily restricted net assets consist of the following:

	<u>2016</u>	<u>2015</u>
Purpose restrictions		
Capacity building	\$ 1,454,592	\$ -
Capital campaign	508,614	619,627
Stand Up for Kids	347,065	1,597,021
Holiday food drive	310,000	26,090
Season of sharing	146,250	84,000
Food assistance	125,000	89,278
Family harvest program	40,931	-
School pantry	25,000	991,666
Produce mobile	2,500	50,000
CalFresh	-	170,000
Fuel	-	25,000
	<u>2,959,952</u>	<u>3,652,682</u>
Time restrictions		
General support for future periods	4,394,040	804,912
Government - Sequoia (program)	<u>130,000</u>	<u>100,000</u>
	<u>\$ 7,483,992</u>	<u>\$ 4,557,594</u>

Temporarily restricted net assets released from restriction during the year were as follows:

	<u>2016</u>	<u>2015</u>
Stand Up for Kids	\$ 7,630,139	\$ 2,231,157
School pantry	991,666	83,332
Time restrictions	441,433	857,197
Food assistance	189,278	33,722
CalFresh	170,000	220,000
Capital campaign	135,758	854,651
Family harvest program	69,069	50,000
Season of sharing	84,000	128,700
Brown bag	50,000	86,667
Produce mobile	50,000	-
Holiday food drive	26,090	25,000
Fuel	<u>25,000</u>	<u>-</u>
	<u>\$ 9,862,433</u>	<u>\$ 4,570,426</u>

Second Harvest Food Bank of Santa Clara and San Mateo Counties  
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15. CONTRIBUTIONS IN-KIND

The estimated fair value of donated food, gift certificates, property and equipment, advertisements, supplies and expert services received are recorded as contributions. Donated food for the years ended June 30, 2016 and 2015 was valued at \$1.67 and \$1.70 per pound, respectively. This valuation is based on a cost study conducted for Feeding America.

In-kind contributions received during the year were as follows:

	2016	2015
Contributions in-kind - non-government		
Food and non-food inventory	\$ 75,889,014	\$ 76,643,753
Supplies and minor equipment	518,866	429,597
Media	46,498	103,389
Gift certificates	28,114	28,860
Services	500	-
Vehicles and equipment	13,794	28,348
	76,496,786	77,233,947
 Government assistance - in-kind		
Food - government	9,236,486	8,219,838
	\$ 85,733,272	\$ 85,453,785

The Food Bank also receives donated services that do not require specific expertise but which are nonetheless central to the Food Bank's operations. For the years ended June 30, 2016 and 2015 the estimated value of these services, based on the estimated dollar value of volunteer time calculated by average rate by job category, totaled \$6,646,180 and \$6,425,218, respectively. The value of these services are not reflected in the financial statements.

16. PAYMENTS TO AFFILIATES

In accordance with the affiliation agreement between Feeding America and the Food Bank, the Food Bank pays fees based on total poundage of food received from Feeding America. Affiliation payments for the years ended June 30, 2016 and 2015 were \$18,978 and \$18,424, respectively.

17. CONFLICT OF INTEREST POLICY

Included among the Food Bank's Board of Directors and Officers are volunteers from the community who provide valuable assistance to the Food Bank in the development of policies and programs and in the evaluation of business transactions. The Food Bank 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.

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18. NATURE OF OPERATIONS

Approximately 20% of the organization's employees are covered by a collective bargaining agreement with the Teamsters Union, Local 287. The agreement became effective on August 24, 2015 and expires three years hence on August 23, 2018. It shall be renewed year to year thereafter, unless either party gives written notice of a desire to change the agreement at least ninety days prior to expiration.

SINGLE AUDIT REPORTS AND SCHEDULES

INDEPENDENT AUDITOR'S 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  
San Jose, California

We have audited, in accordance with the auditing standards generally accepted in the United States of America (the "U.S.") and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of Second Harvest Food Bank of Santa Clara and San Mateo Counties (a California nonprofit corporation) (the "Food Bank"), which comprise the statement of financial position as of June 30, 2016, and the related statements of activities, functional expenses, and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated October 5, 2016.

### **Internal Control Over Financial Reporting**

In planning and performing our audit of the financial statements, we considered the Food Bank's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Food Bank's internal control. Accordingly, we do not express an opinion on the effectiveness of the Food Bank's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies.

Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

## **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the Food Bank's financial statements are free from 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*.

## **Purpose of this Report**

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the Food Bank's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Food Bank's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

A handwritten signature in black ink that reads "Armanino LLP". The signature is written in a cursive, flowing style.

Armanino<sup>LLP</sup>  
San Jose, California

October 5, 2016



INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE FOR EACH MAJOR  
PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE REQUIRED BY  
THE UNIFORM GUIDANCE

To the Board of Directors  
Second Harvest Food Bank of Santa Clara and San Mateo Counties  
San Jose, California

### **Report on Compliance for Each Major Federal Program**

We have audited Second Harvest Food Bank of Santa Clara and San Mateo Counties' (a California nonprofit corporation) (the "Food Bank") compliance with the types of compliance requirements described in the *OMB Compliance Supplement* that could have a direct and material effect on each of the Food Bank's major federal programs for the year ended June 30, 2016. The Food Bank's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

### **Management's Responsibility**

Management is responsible for compliance with federal statutes, regulations, and the terms and conditions of its federal awards applicable to its federal programs.

### **Auditor's Responsibility**

Our responsibility is to express an opinion on compliance for each of the Food Bank's major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America (the "U.S."); the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the U.S.; and the audit requirements of Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (the "Uniform Guidance"). Those standards and the Uniform Guidance 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 the Food Bank's 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 on compliance for each major federal program. However, our audit does not provide a legal determination of the Food Bank's compliance.

### **Opinion on Each Major Federal Program**

In our opinion, the Food Bank complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2016.

## Report on Internal Control Over Compliance

Management of the Food Bank is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the Food Bank's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with the Uniform Guidance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Food Bank's internal control over compliance.

*A deficiency in internal control over compliance* exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. *A material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. *A significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weakness or significant deficiencies.

We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of the Uniform Guidance. Accordingly, this report is not suitable for any other purpose.



Armanino<sup>LLP</sup>  
San Jose, California

October 5, 2016



Second Harvest Food Bank of Santa Clara and San Mateo Counties  
 Schedule of Expenditures of Federal and Other Governmental Awards  
 For the Year Ended June 30, 2016

Federal Grantor/Pass-Through Grantor/ Program or Cluster Title	Federal CFDA Number	Pass-Through Entity Identifying Number	Total Federal Expenditures
<u>Expenditures of Federal Awards</u>			
U.S. Department of Agriculture			
Passed through			
California Department of Social Services			
Food Distribution Cluster			
Emergency Food Assistance Program (Food Commodities)	10.569	N/A	\$ 9,236,486
Emergency Food Assistance Program (Administrative Costs)	10.568	MOU#10-6060	242,909
Emergency Food Assistance Program (Supplemental Costs)	10.568	MOU#10-6060	<u>16,163</u>
Total Food Distribution Cluster			9,495,558
State Administrative Matching Grants for the Supplemental Nutrition Assistance Program	10.561	N/A	<u>193,206</u>
Total U.S. Department of Agriculture			<u>9,688,764</u>
Total Expenditures of Federal Awards			<u>9,688,764</u>
<u>Expenditures of Other Governmental Awards</u>			
Santa Clara County - Department of Social Services	N/A	N/A	746,190
Santa Clara County - Get Fresh	N/A	N/A	52,291
San Mateo County - Sequoia Healthcare district	N/A	N/A	130,000
San Mateo County - Measure A	N/A	N/A	450,000
San Mateo County - Food Assistance	N/A	N/A	54,047
San Mateo County - Brown Bag	N/A	N/A	13,038
San Mateo County - Food Stamp Outreach	N/A	N/A	30,000
State of California - Pacific Gas & Electric Company solar rebate	N/A	N/A	70,711
State of California Department of Social Services Passed through - Emergency Food Assistance Program (Tax Check Off)	N/A	N/A	<u>16,163</u>
Total Expenditures of Other Governmental Awards			<u>1,562,440</u>
Total Expenditures of Federal and Other Governmental Awards			<u>\$ 11,251,204</u>

The accompanying notes to the Schedule of Expenditures of Federal and Other Governmental Awards are an integral part of this schedule.

Second Harvest Food Bank of Santa Clara and San Mateo Counties  
Notes to Schedule of Expenditures of Federal and Other Governmental Awards  
June 30, 2016

1. BASIS OF PRESENTATION

The accompanying schedule of expenditures of federal and other governmental awards (the "Schedule") includes the federal and other governmental award activity of Second Harvest Food Bank of Santa Clara and San Mateo Counties (the "Food Bank") under programs of the federal, state and local governments for the year ended June 30, 2016. The information in this Schedule is presented in accordance with the requirements of Title 2 U.S. *Code of Federal Regulations* (CFR), *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards (Uniform Guidance)*. Because the Schedule presents only a selected portion of the operations of the Food Bank, it is not intended to and does not present the financial position, changes in net assets, or cash flows of the Food Bank.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

- Expenditures reported on the Schedule are reported on the accrual basis of accounting.
- Expenditures of federal awards made on or after December 26, 2014 are recognized following the cost principles contained in the Uniform Guidance, wherein certain types of expenditures are not allowable or are limited as to reimbursement.
- Expenditures of federal awards made prior to December 26, 2014 are recognized following the cost principles contained in OMB Circular A-122, Cost Principles for Non-Profit Organizations, wherein certain types of expenditures are not allowable or are limited as to reimbursement.

3. SUBRECIPIENTS

Of the federal expenditures presented in the Schedule, Second Harvest Food Bank of Santa Clara and San Mateo Counties provided federal awards to Subrecipients as follows:

CFDA Number	Program Name	Amount Provided to Subrecipients
10.569	Emergency Food Assistance Program (Food Commodities)	\$8,828,924
97.024	Emergency Food and Shelter National Board Program	\$64,409

4. FOOD DISTRIBUTION

Nonmonetary assistance for commodities received are reported in the Schedule based on a cost study conducted for Feeding America. At June 30, 2016, the Food Bank had food commodities totaling \$742,763 in inventory.

Second Harvest Food Bank of Santa Clara and San Mateo Counties  
Notes to Schedule of Expenditures of Federal and Other Governmental Awards  
June 30, 2016

5. INDIRECT COST RATE

Second Harvest Food Bank of Santa Clara and San Mateo Counties has not elected to use the 10% de minimis indirect cost rate as allowed under the Uniform Guidance.

Second Harvest Food Bank of Santa Clara and San Mateo Counties  
 Schedule of Findings and Questioned Costs  
 For the Year Ended June 30, 2016

SECTION I - SUMMARY OF AUDITOR'S RESULTS

Financial Statements

Type of auditor's report issued:	Unmodified
Internal control over financial reporting:	
Material weakness(es) identified?	No
Significant deficiency(ies) identified that are not considered to be material weaknesses?	None reported
Noncompliance material to financial statements noted?	No

Federal Awards

Internal control over major programs:	
Material weakness(es) identified?	No
Significant deficiency(ies) identified that are not considered to be material weaknesses?	None reported
Type of auditor's report issued on compliance for major programs:	Unmodified
Any audit findings disclosed that are required to be reported in accordance with 2 CFR 200.516(a)?	No
Identification of major programs:	

<u>Name of Federal Program or Cluster</u>	<u>CFDA Number</u>
State Administrative Matching Grant for the Supplemental Nutrition Assistance Program	10.561
<u>Food Distribution Cluster</u>	
Emergency Food Assistance Program (Administrative Costs)	10.568
Emergency Food Assistance Program (Food Commodities)	10.569
Dollar threshold used to distinguish between Type A and Type B programs	\$750,000
Auditee qualified as low-risk auditee?	Yes

Second Harvest Food Bank of Santa Clara and San Mateo Counties  
Schedule of Findings and Questioned Costs  
For the Year Ended June 30, 2016

SECTION II - SUMMARY OF FINANCIAL STATEMENT FINDINGS

There are no financial statement findings to be reported.

SECTION III - SUMMARY OF FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

There are no federal award findings to be reported.

SECTION IV - STATUS OF PRIOR YEAR FINDINGS

There were no prior year findings.

SECTION V - CORRECTIVE ACTION PLAN

There is no corrective action plan required.