

FOODLINK, INC. AND AFFILIATE

**Consolidating Financial Statements as of
June 30, 2016
Together with
Independent Auditor's Report**

Bonadio & Co., LLP
Certified Public Accountants

INDEPENDENT AUDITOR'S REPORT

October 11, 2016

To the Boards of Directors of
Foodlink, Inc. and Affiliate:

Report on the Financial Statements

We have audited the accompanying consolidating financial statements of Foodlink, Inc. and Affiliate (New York not-for-profit corporations) (the Organizations) which comprise the consolidating balance sheet as of June 30, 2016, and the related consolidating statements of activities and change in net assets, 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 consolidating financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidating 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 consolidating financial statements based on our audit. 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 consolidating financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidating financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidating 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 consolidating 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 consolidating financial statements.

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

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INDEPENDENT AUDITOR'S REPORT

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Opinion

In our opinion, the consolidating financial statements referred to above present fairly, in all material respects, the individual and consolidated financial positions of Foodlink, Inc. and Affiliate as of June 30, 2016, and the changes in their net assets and cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Report on Summarized Comparative Information

We have previously audited Foodlink Inc. and Affiliate's 2015 consolidating financial statements, and we expressed an unmodified audit opinion on those audited financial statements in our report dated September 30, 2015. 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.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated October 11, 2016 on our consideration of the Organizations' 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 Organizations' internal control over financial reporting and compliance.

FOODLINK, INC. AND AFFILIATE
CONSOLIDATING BALANCE SHEET
JUNE 30, 2016

(With Comparative Totals for 2015)

	Foodlink, Inc.	Foodlink Foundation, Inc. and Subsidiary	Eliminations	Total	
				2016	2015
ASSETS					
CURRENT ASSETS:					
Cash and equivalents	\$ 2,128,608	\$ 32,714	\$ -	\$ 2,161,322	\$ 1,129,549
Accounts receivable, net of allowance for doubtful accounts of \$10,000	340,721	2,892	-	343,613	406,778
Grants receivable	894,402	-	-	894,402	852,283
United Way receivable	16,667	-	-	16,667	16,667
Current portion of pledges receivable	-	31,558	-	31,558	36,304
Inventory	359,018	-	-	359,018	471,792
Prepaid expenses and other current assets	63,094	-	-	63,094	51,897
Total current assets	3,802,510	67,164	-	3,869,674	2,965,270
DUE FROM FOODLINK FOUNDATION, INC. AND SUBSIDIARY	16,456	-	(16,456)	-	-
INVESTMENTS	-	569,370	-	569,370	412,671
PLEDGES RECEIVABLE, net of current portion	-	18,086	-	18,086	24,982
INTEREST IN NET ASSETS OF FOODLINK FOUNDATION, INC. AND SUBSIDIARY	930,949	-	(930,949)	-	-
PROPERTY AND EQUIPMENT, net	3,700,828	-	-	3,700,828	2,540,395
ASSETS HELD FOR SALE	-	357,703	-	357,703	136,800
	<u>\$ 8,450,743</u>	<u>\$ 1,012,323</u>	<u>\$ (947,405)</u>	<u>\$ 8,515,661</u>	<u>\$ 6,080,118</u>
LIABILITIES AND NET ASSETS					
CURRENT LIABILITIES:					
Line-of-credit	\$ -	\$ -	\$ -	\$ -	\$ 97,550
Accounts payable and accrued expenses	1,087,531	41,818	-	1,129,349	638,603
Current portion of capital lease obligations	145,478	-	-	145,478	70,602
Current portion of long-term debt	4,772	-	-	4,772	20,028
Deferred revenue	208,051	23,100	-	231,151	248,112
Total current liabilities	1,445,832	64,918	-	1,510,750	1,074,895
DUE TO FOODLINK, INC.	-	16,456	(16,456)	-	-
CAPITAL LEASE OBLIGATIONS, net of current portion	612,902	-	-	612,902	224,940
LONG-TERM DEBT, net of current portion	-	-	-	-	58,058
Total liabilities	<u>2,058,734</u>	<u>81,374</u>	<u>(16,456)</u>	<u>2,123,652</u>	<u>1,357,893</u>
NET ASSETS (DEFICIT):					
Unrestricted	2,576,544	107,937	(107,937)	2,576,544	2,620,137
Temporarily restricted	3,266,423	273,970	(273,970)	3,266,423	1,602,088
Permanently restricted	549,042	549,042	(549,042)	549,042	500,000
Total net assets	<u>6,392,009</u>	<u>930,949</u>	<u>(930,949)</u>	<u>6,392,009</u>	<u>4,722,225</u>
	<u>\$ 8,450,743</u>	<u>\$ 1,012,323</u>	<u>\$ (947,405)</u>	<u>\$ 8,515,661</u>	<u>\$ 6,080,118</u>

The accompanying notes are an integral part of these statements.

FOODLINK, INC. AND AFFILIATE

**CONSOLIDATING STATEMENT OF ACTIVITIES AND CHANGE IN NET ASSETS
FOR THE YEAR ENDED JUNE 30, 2016**
(With Comparative Totals for 2015)

	Foodlink, Inc.				Foodlink Foundation, Inc. and Subsidiary				Total		
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total	Unrestricted	Temporarily Restricted	Permanently Restricted	Total	Eliminations	2016	2015
PUBLIC SUPPORT AND REVENUE:											
Public support -											
Donated food	\$ 23,175,955	\$ -	\$ -	\$ 23,175,955	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 23,175,955	\$ 23,781,603
Government grants	1,971,726	-	-	1,971,726	-	-	-	-	-	1,971,726	1,593,840
Contributions	1,415,961	2,500,400	-	3,916,361	112,168	1,086,994	49,042	1,248,204	(1,874,498)	3,290,067	2,717,574
Bequests	-	-	-	-	-	107,020	-	107,020	-	107,020	1,476,069
Government grants received for nutritious children's meals	856,041	-	-	856,041	-	-	-	-	-	856,041	970,326
Check Out Hunger	787,750	-	-	787,750	-	-	-	-	-	787,750	803,527
Government grants received for shared maintenance	844,811	-	-	844,811	-	-	-	-	-	844,811	789,500
Government grants received for wholesale distribution	527,510	-	-	527,510	-	-	-	-	-	527,510	491,085
United Way	120,279	200,000	-	320,279	-	-	-	-	-	320,279	312,299
Total public support	29,700,033	2,700,400	-	32,400,433	112,168	1,194,014	49,042	1,355,224	(1,874,498)	31,881,159	32,935,823
Revenue -											
Wholesale food distribution	2,209,185	-	-	2,209,185	-	-	-	-	-	2,209,185	1,876,729
Vended meals	692,293	-	-	692,293	-	-	-	-	-	692,293	522,523
Shared maintenance	445,239	-	-	445,239	-	-	-	-	-	445,239	406,609
Rental income	-	-	-	-	671,479	-	-	671,479	(625,717)	45,762	307,147
Value added processing revenue	72,941	-	-	72,941	-	-	-	-	-	72,941	143,857
Membership fees	78,850	-	-	78,850	-	-	-	-	-	78,850	76,700
Catering revenue	-	-	-	-	130,425	-	-	130,425	-	130,425	89,182
Interest	3,088	-	-	3,088	-	-	-	-	-	3,088	1,111
Other	91,766	-	-	91,766	-	-	-	-	-	91,766	80,979
Total revenue	3,593,362	-	-	3,593,362	801,904	-	-	801,904	(625,717)	3,769,549	3,504,837
Net assets released from restriction -											
Other	771,111	(771,111)	-	-	1,466,546	(1,466,546)	-	-	-	-	-
Total public support and revenue	34,064,506	1,929,289	-	35,993,795	2,380,618	(272,532)	49,042	2,157,128	(2,500,215)	35,650,708	36,440,660
EXPENSES:											
Program services	32,175,978	-	-	32,175,978	2,776,928	-	-	2,776,928	(2,500,215)	32,452,691	32,773,966
Management and general services	636,360	-	-	636,360	20,178	-	-	20,178	-	656,538	586,827
Fundraising	819,963	-	-	819,963	85,507	-	-	85,507	-	905,470	791,478
Total expenses	33,632,301	-	-	33,632,301	2,882,613	-	-	2,882,613	(2,500,215)	34,014,699	34,152,271
CHANGE IN NET ASSETS BEFORE OTHER ITEMS	432,205	1,929,289	-	2,361,494	(501,995)	(272,532)	49,042	(725,485)	-	1,636,009	2,288,389
OTHER ITEMS:											
Investment income	-	-	-	-	5,819	7,658	-	13,477	-	13,477	1,496
Change in interest in net assets of Foodlink Foundation, Inc.	(480,976)	(264,874)	49,042	(696,808)	-	-	-	-	696,808	-	-
Gain on sale of property and equipment	5,098	-	-	5,098	15,200	-	-	15,200	-	20,298	60,375
Impairment of property and equipment	-	-	-	-	-	-	-	-	-	-	-
Change in value of assets held for sale	-	-	-	-	-	-	-	-	-	-	(104,396)
Total other items	(475,878)	(264,874)	49,042	(691,710)	21,019	7,658	-	28,677	696,808	33,775	(42,525)
CHANGE IN NET ASSETS	(43,673)	1,664,415	49,042	1,669,784	(480,976)	(264,874)	49,042	(696,808)	696,808	1,669,784	2,245,864
NET ASSETS - beginning of year	2,620,217	1,602,008	500,000	4,722,225	588,913	538,844	500,000	1,627,757	(1,627,757)	4,722,225	2,476,361
NET ASSETS - end of year	\$ 2,576,544	\$ 3,266,423	\$ 549,042	\$ 6,392,009	\$ 107,937	\$ 273,970	\$ 549,042	\$ 930,949	\$ (930,949)	\$ 6,392,009	\$ 4,722,225

The accompanying notes are an integral part of these statements.

FOODLINK, INC. AND AFFILIATE

CONSOLIDATING STATEMENT OF FUNCTIONAL EXPENSES

FOR THE YEAR ENDED JUNE 30, 2016

(With Comparative Totals for 2015)

	Foodlink, Inc.				Foodlink Foundation,	
	Program Services	Management and General	Fundraising	Total	Program Services	Management and General
EXPENSES:						
Donated food	\$ 23,175,955	\$ -	\$ -	\$ 23,175,955	\$ -	\$ -
Purchased food	3,389,298	-	-	3,389,298	-	-
Salaries	2,185,614	259,358	272,912	2,717,884	-	-
Donations	-	-	-	-	1,874,498	-
Occupancy	1,042,098	32,171	80,644	1,154,913	618,450	137
Employee benefits and payroll taxes	795,903	142,548	105,332	1,043,783	-	-
Depreciation and amortization	355,612	18,343	3,498	377,453	90,915	-
Professional fees	131,477	64,589	29,304	225,370	128,300	16,472
Operational support	323,794	-	650	324,444	-	-
Office expenses	53,032	26,797	193,466	273,295	854	453
Program supplies	300,884	-	-	300,884	-	-
Transportation and distribution	275,572	381	37	275,990	-	-
Advertising	15,041	2,716	111,401	129,158	-	-
Travel and meetings	44,995	27,225	20,795	93,015	498	20
Operational supplies and equipment	-	-	-	-	51,448	-
Interest	825	45,864	-	46,689	1,159	2,227
Shipping	36,853	40	-	36,893	-	-
Provision for bad debts	14,633	-	-	14,633	-	-
Security	-	-	-	-	5,545	-
Bank fees	-	-	-	-	117	196
Other	34,392	16,328	1,924	52,644	5,144	673
Total expenses	<u>\$ 32,175,978</u>	<u>\$ 636,360</u>	<u>\$ 819,963</u>	<u>\$ 33,632,301</u>	<u>\$ 2,776,928</u>	<u>\$ 20,178</u>

Inc. and Subsidiary		Eliminations			Total	
<u>Fundraising</u>	<u>Total</u>	<u>Program Services</u>	<u>Management and General</u>	<u>Total</u>	<u>2016</u>	<u>2015</u>
\$ -	\$ -	\$ -	\$ -	\$ -	\$ 23,175,955	\$ 23,781,603
-	-	-	-	-	3,389,298	3,058,596
-	-	-	-	-	2,717,884	2,292,554
-	1,874,498	(1,874,498)	-	(1,874,498)	-	5,458
3,052	621,639	(625,717)	-	(625,717)	1,150,835	1,255,600
-	-	-	-	-	1,043,783	781,981
-	90,915	-	-	-	468,368	455,892
32,526	177,298	-	-	-	402,668	703,963
-	-	-	-	-	324,444	257,965
4,575	5,882	-	-	-	279,177	404,864
-	-	-	-	-	300,884	260,605
-	-	-	-	-	275,990	347,549
12,733	12,733	-	-	-	141,891	107,740
1,145	1,663	-	-	-	94,678	90,446
-	51,448	-	-	-	51,448	84,266
-	3,386	-	-	-	50,075	110,363
-	-	-	-	-	36,893	48,356
-	-	-	-	-	14,633	9,091
-	5,545	-	-	-	5,545	3,820
3,900	4,213	-	-	-	4,213	6,924
<u>27,576</u>	<u>33,393</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>86,037</u>	<u>84,635</u>
<u>\$ 85,507</u>	<u>\$ 2,882,613</u>	<u>\$ (2,500,215)</u>	<u>\$ -</u>	<u>\$ (2,500,215)</u>	<u>\$ 34,014,699</u>	<u>\$ 34,152,271</u>

The accompanying notes are an integral part of these statements.

FOODLINK, INC. AND AFFILIATE

CONSOLIDATING STATEMENT OF CASH FLOWS FOR THE YEAR ENDED JUNE 30, 2016

(With Comparative Totals for 2015)

	Foodlink, Inc.	Foodlink Foundation, Inc. and Subsidiary	Eliminations	Total	
				2016	2015
CASH FLOW FROM OPERATING ACTIVITIES:					
Change in net assets	\$ 1,669,784	\$ (696,808)	\$ 696,808	\$ 1,669,784	\$ 2,245,864
Adjustments to reconcile change in net assets to net cash flow from operating activities:					
Realized and unrealized investment gains	-	713	-	713	251
Depreciation and amortization	377,453	90,915	-	468,368	455,892
Provision for bad debts	14,633	-	-	14,633	-
Change in interest of net assets of Foodlink Foundation, Inc.	696,808	-	(696,808)	-	-
Gain on sale of property and equipment	(5,098)	(15,200)	-	(20,298)	(60,375)
Change in value of assets held for sale	-	-	-	-	104,396
Changes in:					
Accounts receivable	44,768	3,764	-	48,532	(241,391)
Grants receivable	(42,119)	-	-	(42,119)	(284,854)
Pledges receivable	-	11,642	-	11,642	5,145
Inventory	112,774	-	-	112,774	(71,654)
Prepaid expenses and other current assets	(11,197)	-	-	(11,197)	(19,193)
Accounts payable and accrued expenses	478,246	12,506	-	490,752	(136,283)
Due to (from) affiliate	(16,456)	16,456	-	-	-
Deferred revenue	(10,886)	(6,075)	-	(16,961)	79,674
Net cash flow from operating activities	<u>3,308,710</u>	<u>(582,087)</u>	<u>-</u>	<u>2,726,623</u>	<u>2,077,472</u>
CASH FLOW FROM INVESTING ACTIVITIES:					
Purchases of property and equipment	(1,407,463)	-	-	(1,407,463)	(163,983)
Proceeds from sale of property and equipment	7,063	151,592	-	158,655	618,888
Purchases of investments	-	(357,970)	-	(357,970)	(853,254)
Proceeds from sales of investments	-	200,558	-	200,558	755,331
Net cash flow from investing activities	<u>(1,400,400)</u>	<u>(5,820)</u>	<u>-</u>	<u>(1,406,220)</u>	<u>356,982</u>
CASH FLOW FROM FINANCING ACTIVITIES:					
Repayments on line-of-credit, net	-	(97,550)	-	(97,550)	97,550
Principal payments on capital lease obligations	(117,766)	-	-	(117,766)	(568,753)
Principal payments on long-term debt	(4,606)	(68,708)	-	(73,314)	(1,206,700)
Net cash flow from financing activities	<u>(122,372)</u>	<u>(166,258)</u>	<u>-</u>	<u>(288,630)</u>	<u>(1,677,903)</u>
CHANGE IN CASH AND EQUIVALENTS	1,785,938	(754,165)	-	1,031,773	756,551
CASH AND EQUIVALENTS - beginning of year	<u>342,670</u>	<u>786,879</u>	<u>-</u>	<u>1,129,549</u>	<u>372,998</u>
CASH AND EQUIVALENTS - end of year	<u>\$ 2,128,608</u>	<u>\$ 32,714</u>	<u>\$ -</u>	<u>\$ 2,161,322</u>	<u>\$ 1,129,549</u>
NON-CASH TRANSACTIONS					
Capital lease obligations terminated	\$ -	\$ -	\$ -	\$ -	\$ 45,902
Disposal of property, plant and equipment under lease obligations	\$ -	\$ -	\$ -	\$ -	\$ 45,902
Capital lease obligations entered into Property, plant and equipment acquired under lease obligations	\$ 580,604	\$ -	\$ -	\$ 580,604	\$ -
	<u>\$ 580,604</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 580,604</u>	<u>\$ -</u>

The accompanying notes are an integral part of these statements.

FOODLINK, INC. AND AFFILIATE

NOTES TO CONSOLIDATING FINANCIAL STATEMENTS JUNE 30, 2016

1. THE ORGANIZATIONS

Foodlink, Inc. (Foodlink) and Foodlink Foundation, Inc. (the Foundation) are not-for-profit organizations incorporated under New York State not-for-profit corporation laws.

Foodlink was created to provide, in the most efficient and effective manner, food, skills and resources to emergency food providers, other charitable organizations and individuals in Monroe County, New York and nine surrounding counties. Foodlink purchases and solicits donations of nutritious surplus food from the food industry and distributes these products to qualified 501(c)(3) charities for feeding the ill, the needy, and children. A significant portion of the food product is obtained through local food distributors, local farms and retailers. Foodlink provides the food industry with a way to avoid the waste of edible but unsaleable products and creates an opportunity to provide food to charities in need of such assistance.

The Foundation was formed to provide funding and support for anti-hunger organizations in the greater Rochester, New York area. The Foundation also includes FreshLink, LLC (FreshLink) a wholly-owned for-profit subsidiary. FreshLink leases real estate property and subleases this property to Foodlink.

Foodlink is the sole corporate member of the Foundation.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Consolidation

The accompanying consolidating financial statements include the accounts of Foodlink and the Foundation (collectively, the Organizations). The accounts of the Foundation include the accounts of FreshLink. All significant inter-company balances and transactions have been eliminated in consolidation.

Basis of Accounting

The financial statements of the Organizations have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP).

Financial Reporting

Resources for various purposes are classified for accounting and reporting purposes by net asset categories established according to their nature and purpose. The following net asset categories are maintained by the Organizations:

- Unrestricted - Includes resources expendable for the support of the Organizations operating activities.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Financial Reporting (Continued)

- Temporarily Restricted - Includes resources that have donor-imposed restrictions that permits the Organizations to use up or expend the donated asset as specified and are satisfied by the passage of time or by actions of the Organizations. When a donor restriction is met, temporarily restricted net assets are reclassified as unrestricted net assets and reported in the statement of activities and change in net assets as “net assets released from restrictions.” At June 30, 2016 and 2015, temporarily restricted net assets had time restrictions, were restricted for program activities, or long-lived assets acquired with gifts of cash or other assets restricted for those acquisitions. The Organizations’ policy is to release net assets from restriction in order to match recognized depreciation expense on long-lived assets purchased with donor-restricted funds.
- Permanently Restricted - Amounts that have donor-imposed restrictions that stipulate that resources be maintained permanently, but which permit the Organizations to use or expend all of the income derived from the donated assets at its discretion.

Comparative Information

The financial statements include certain prior-year summarized comparative information in total but not by net asset class or functional expense classification. 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 Organizations’ financial statements for the year ended June 30, 2015, from which the summarized information was derived.

Cash and Equivalents

Cash and equivalents include bank demand deposit, cash management, and money market accounts. At times, the balances in the demand deposit accounts may exceed federally insured limits. Balances in money market accounts are not federally insured. The Organizations have not experienced any losses in such accounts and believe they are not exposed to any significant credit risk with respect to cash and equivalents.

Accounts Receivable

The Organizations provide services that are paid for primarily by other tax-exempt agencies. Accounts for which no payments have been received for several months are considered delinquent and are written off when customary collection efforts are exhausted. The Organizations record an allowance for doubtful accounts in anticipation of future write-offs. The allowance for doubtful accounts is based on the Organizations’ historical collection experience and a review of outstanding balances.

Pledges Receivable and Contributions

The Foundation records pledges receivable when an unconditional contribution commitment is received. Pledges receivable are recorded net of a discount relative to the present value of future cash flows unless they are expected to be received within one year. In addition, the Foundation records an allowance for doubtful pledges receivable based on past collection experience and a review of specific accounts. Pledges are written-off when reasonable collection efforts have been exhausted. No allowance for doubtful pledges was considered necessary at June 30, 2016 and 2015.

Investments

Investments are recorded at fair value, based on quoted market prices. Investments are exposed to various risks, such as interest rate, market, and credit risk. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect the amount reported in the accompanying financial statements.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Advertising

Advertising costs are expensed as incurred.

Deferred Revenue

Deferred revenue consists of cash received in advance of program service provision.

Property and Equipment

Property and equipment are recorded at cost or at the fair value on the date of donation. The Organizations' policy is to capitalize all property and equipment purchases greater than \$2,500 having an estimated useful life in excess of one year. Amortization of the costs of property and equipment is provided using the straight-line method over the shorter of the remaining term of the lease or the estimated useful life of the asset. Depreciation is computed on the straight-line method based on the following estimated useful lives:

Buildings	40 years
Leasehold improvements	15 years
Furniture and equipment	5 years
Vehicles	5 years

Assets Held for Sale

Real estate holdings that are intended to sell within one year are classified as assets held for sale. At each reporting date, the Foundation evaluates the recorded value by obtaining information from real estate professionals and evaluating sales prices of comparable properties. If the current estimated fair value is less than the recorded value, the Foundation records a valuation adjustment to reduce the recorded value to estimated net realizable value.

Purchased Product Inventory

Food that has been purchased by Foodlink, but which has not been distributed, is reported as inventory. This inventory will be distributed at no charge, or sold at an amount equal to cost, to qualified organizations. This inventory is valued at cost determined on a first-in, first-out (FIFO) basis.

Donated Product

The majority of product that is distributed has been donated. Donated product is not recorded by Foodlink until distributed.

Donated Services

Donated rent totaled approximately \$42,000 in 2016. These amounts have been reflected as contribution revenue and occupancy expense in the accompanying financial statements. There was no donated rent in 2015.

Donated legal services totaled approximately \$29,000 in 2015. These amounts have been reflected as contribution revenue and professional fees expense in the accompanying financial statements. There were no donated legal services in 2016.

Shared Maintenance

Foodlink requests that participating not-for-profit agencies contribute various amounts depending on the type of product received for each pound of product they receive. This revenue is used to cover the cost of food handling as well as general operating expenses.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Income Taxes

Foodlink and the Foundation are not-for-profit corporations and are exempt from income taxes as organizations qualified under Section 501(c)(3) of the Internal Revenue Code. Foodlink and the Foundation have also been classified by the Internal Revenue Service as entities that are not private foundations.

FreshLink is a for-profit limited liability corporation. No income tax expense has been accrued for the years ended June 30, 2016 and 2015 due to FreshLink's net operating losses. In addition, no deferred income tax assets have been recognized because the timing of realization of such assets is not estimable. FreshLink has available net operating loss carryforwards of approximately \$1,007,000 available to offset future taxable income through 2033, if any. The loss carryforwards expire between 2024 and 2033.

Fair Value Measurement - Definition and Hierarchy

GAAP defines fair value 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.

The Foundation uses various valuation techniques in determining fair value. GAAP establishes a hierarchy for inputs used in measuring fair value that maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that the observable inputs be used when available. Observable inputs are inputs that market participants would use in pricing the asset or liability, developed based on market data obtained from sources independent of the Organizations. Unobservable inputs are inputs that reflect the Organizations' assumptions about the assumptions that market participants would use in pricing the asset or liability, developed based on the best information available in the circumstances. The input hierarchy is broken down into three levels based on the reliability of inputs as follows:

- Level 1 - Valuations based on quoted prices in active markets for identical assets or liabilities that the Foundation has the ability to access. Valuation adjustments are not applied to Level 1 instruments. Since valuations are based on quoted prices that are readily and regularly available in an active market, valuation of these products does not entail a significant degree of judgment.
- Level 2 - Valuations based on quoted prices in markets that are not active or for which all significant inputs are observable, directly or indirectly.
- Level 3 - Valuations based on inputs that are unobservable and significant to the overall fair value measurement.

Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

Reclassifications

Certain reclassifications have been made to the 2015 financial statements in order to conform with current year presentation.

3. TEMPORARILY RESTRICTED NET ASSETS

The Foundation's temporarily restricted net assets were available for the following purposes at June 30:

	<u>2016</u>	<u>2015</u>
Capital campaign	\$ 253,642	\$ 512,913
WellVentions	-	13,261
Unappropriated endowment earnings	<u>20,328</u>	<u>12,670</u>
	<u>\$ 273,970</u>	<u>\$ 538,844</u>

The Foundation's temporarily restricted net assets were released from restriction as follows during the years ended June 30:

	<u>2016</u>	<u>2015</u>
Capital campaign	\$ 1,453,285	\$ 317,137
WellVentions	<u>13,261</u>	<u>103,746</u>
	<u>\$ 1,466,546</u>	<u>\$ 420,883</u>

Foodlink's temporarily restricted net assets were available for the following purposes at June 30:

	<u>2016</u>	<u>2015</u>
Capital project for kitchen move	\$ 1,662,836	\$ 653,755
Capital assets, net	1,186,865	291,670
Foodbank Programs	80,727	85,301
Child Nutrition Meal Programs	18,750	-
Community Nutrition Programs		
• Food Access Programs	32,660	12,438
• Nutrition Education Programs	<u>10,615</u>	<u>20,000</u>
	<u>\$ 2,992,453</u>	<u>\$ 1,063,164</u>

Foodlink's temporarily restricted net assets were released from restriction as follows during the years ended June 30:

	<u>2016</u>	<u>2015</u>
Capital project for kitchen move	\$ 163,738	\$ 117,293
Capital assets, net	36,292	39,837
Foodbank Programs	454,318	336,119
Child Nutrition Meal Programs	75,000	75,000
Community Nutrition Programs		
• Food Access Programs	19,628	28,212
• Nutrition Education Programs	<u>22,135</u>	<u>29,167</u>
	<u>\$ 771,111</u>	<u>\$ 625,628</u>

4. PLEDGES RECEIVABLE

The Foundation's outstanding pledges are due as follows for the years ending June 30:

2017	\$ 31,558
2018	11,104
2019	<u>6,982</u>
	49,644
Less: Current portion	<u>31,558</u>
	<u>\$ 18,086</u>

5. INVESTMENTS

The Foundation's investments consisted of the following at June 30:

	<u>2016</u>	<u>2015</u>
Cash and cash equivalents	\$ 11,347	\$ 6,969
Fixed income mutual funds	53,986	97,827
Equity mutual funds	60,873	54,461
Corporate bonds	113,572	-
Government bonds	72,320	118,128
Common stock	<u>257,272</u>	<u>135,286</u>
	<u>\$ 569,370</u>	<u>\$ 412,671</u>

The Foundation's Investment income for the years ended June 30 consisted of the following:

	<u>2016</u>	<u>2015</u>
Interest and dividends	\$ 14,190	\$ 1,747
Net realized gains (losses)	(9,767)	693,415
Net unrealized gains (losses)	<u>9,054</u>	<u>(693,666)</u>
	<u>\$ 13,477</u>	<u>\$ 1,496</u>

5. INVESTMENTS (Continued)

The Foundation's investments are measured at fair value on a recurring basis. Investments are segregated by the level of valuation inputs within the fair value hierarchy utilized to measure fair value as follows as of June 30:

	2016			
	<u>Level 1 Inputs</u>	<u>Level 2 Inputs</u>	<u>Level 3 Inputs</u>	<u>Total Fair Value</u>
Cash and cash equivalents	\$ 11,347	\$ -	\$ -	\$ 11,347
Fixed income mutual funds	53,986	-	-	53,986
Equity mutual funds	60,873	-	-	60,873
Corporate bonds	-	113,572	-	113,572
Government bonds	72,320	-	-	72,320
Common stock	<u>257,272</u>	<u>-</u>	<u>-</u>	<u>257,272</u>
	<u>\$ 455,798</u>	<u>\$ 113,572</u>	<u>\$ -</u>	<u>\$ 569,370</u>
	2015			
	<u>Level 1 Inputs</u>	<u>Level 2 Inputs</u>	<u>Level 3 Inputs</u>	<u>Total Fair Value</u>
Cash and cash equivalents	\$ 6,969	\$ -	\$ -	\$ 6,969
Fixed income mutual funds	97,827	-	-	97,827
Equity mutual funds	54,461	-	-	54,461
Government bonds	118,128	-	-	118,128
Common stock	<u>135,286</u>	<u>-</u>	<u>-</u>	<u>135,286</u>
	<u>\$ 412,671</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 412,671</u>

The Foundation's corporate bonds are valued using Level 2 inputs. Fair value of the Foundation's bonds is determined by entering observable inputs, including benchmark yields, reported trades, broker/dealer quotes, issuer spreads, bids and offers into a pricing model.

6. PROPERTY AND EQUIPMENT

Property and equipment consisted of the following at June 30:

	2016			2015		
	Foodlink	Foundation	Total	Foodlink	Foundation	Total
Buildings	\$ -	\$ -	\$ -	\$ -	\$ 625,575	\$ 625,575
Building and land improvements	1,621,456	-	1,621,456	1,467,901	1,162,037	2,629,938
Furniture and equipment	1,326,415	-	1,326,415	948,640	24,342	972,982
Vehicles	1,350,089	31,240	1,381,329	796,837	49,890	846,727
Construction in progress	<u>1,005,130</u>	<u>-</u>	<u>1,005,130</u>	<u>153,555</u>	<u>-</u>	<u>153,555</u>
	5,303,090	31,240	5,334,330	3,366,933	1,861,844	5,228,777
Less:						
Accumulated depreciation and amortization	<u>(1,602,262)</u>	<u>(31,240)</u>	<u>(1,633,502)</u>	<u>(1,274,748)</u>	<u>(1,413,634)</u>	<u>(2,688,382)</u>
	<u>\$ 3,700,828</u>	<u>\$ -</u>	<u>\$ 3,700,828</u>	<u>\$ 2,092,185</u>	<u>\$ 448,210</u>	<u>\$ 2,540,395</u>

7. ASSETS HELD FOR SALE

The Foundation listed the Exchange Street property for sale and received a signed purchase agreement for the purchase of the property. As a result, at June 30, 2016, the property was valued at liquidation value, which is fair value, and has been included as assets held for sale on the accompanying balance sheet. As of June 30, 2016, the Foundation did not need to record a valuation adjustment on the property based on the following estimated expected cash proceeds to be received from sale of the property.

The following table indicates the level of valuation inputs within the fair value hierarchy utilized to measure fair value for assets held for sale as of June 30, 2016 on a nonrecurring basis:

	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs	Total Fair Value
Assets held for sale	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 357,703</u>	<u>\$ 357,703</u>

The Foundation sold the Penfield Center Road facility in the current year, which was reported at liquidation value, which was fair value, and included as assets held for sale as of June 30, 2015. As of June 30, 2015, the Foundation recorded a valuation adjustment on the property based on the following estimated expected cash proceeds to be received from sale of the property.

The following table indicates the level of valuation inputs within the fair value hierarchy utilized to measure fair value for assets held for sale as of June 30, 2015 on a nonrecurring basis:

	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs	Total Fair Value
Assets held for sale	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 136,800</u>	<u>\$ 136,800</u>

8. INVENTORY

The following table presents a summary of donated and distributed food:

	<u>June 30, 2016</u>		<u>June 30, 2015</u>	
	<u>Pounds</u>	<u>Foodlink Value</u>	<u>Pounds</u>	<u>Foodlink Value</u>
Inventory, beginning of year	485,058	\$ 1,011,069	350,092	\$ 788,628
Revision of inventory value	-	(14,552)	-	(7,002)
Donated food received	12,257,838	20,470,589	12,309,947	20,926,910
Less:				
Food distributed to participating agencies	(11,127,902)	(18,583,596)	(11,290,542)	(19,193,921)
Food scrapped	<u>(1,102,404)</u>	<u>(1,841,015)</u>	<u>(884,439)</u>	<u>(1,503,546)</u>
Inventory, end of year	<u>512,590</u>	<u>\$ 1,042,496</u>	<u>485,058</u>	<u>\$ 1,011,069</u>

Donated product is included as revenue and expense in the accompanying financial statements and consists of \$18,583,596 and \$19,193,921 in distributed donated product for the years ending June 30, 2016 and 2015, respectively.

Inventory, End of Year

Foodlink's inventory value was determined using a rate of \$1.67 and \$1.70 per pound in 2016 and 2015, respectively. The rate per pound was estimated by Feeding America, a national organization, as being the average value of one pound of donated food.

USDA Product

Foodlink has an agreement with the New York State Bureau of Government Donated Food Distribution to deliver food received from the United States Department of Agriculture (USDA) free of charge to qualifying centers.

The following table presents a summary of USDA food donated and distributed for the years ended June 30:

	<u>2016 Pounds</u>	<u>2015 Pounds</u>
Inventory, beginning of year	267,144	324,718
Donated food received	3,034,754	2,641,062
Less:		
Food distributed to participating agencies	(2,747,640)	(2,698,636)
Food scrapped	<u>(2,276)</u>	<u>-</u>
Inventory, end of year	<u>551,982</u>	<u>267,144</u>

Donated product is included as revenue and expense in the accompanying financial statements and consists of \$4,592,359 and \$4,587,682 in distributed USDA product for the years ending June 30, 2016 and 2015, respectively.

Foodlink's value is determined by taking the ending inventory in pounds and multiplying that amount by the Feeding America rate. The value of the USDA inventory was \$921,810 and \$454,145 at June 30, 2016 and 2015, respectively. USDA food inventory is owned by USDA until distributed by Foodlink and, therefore, is not recorded as an asset by Foodlink.

9. FINANCING ARRANGEMENTS

Long-Term Debt

Long-term debt consisted of the following at June 30:

	<u>2016</u>	<u>2015</u>
Foodlink:		
Note payable to a bank in monthly installments of \$405, including interest at 3.55% through June 2017. This loan is collateralized by the related vehicle.	\$ 4,772	\$ 9,378
Total Foodlink	4,772	9,378
Less: Current portion	<u>(4,772)</u>	<u>(4,603)</u>
	<u>\$ -</u>	<u>\$ 4,775</u>
The Foundation:		
Note payable to a bank was paid in full during 2016.	\$ -	\$ 68,708
Consolidated:		
Total Consolidated	\$ 4,772	\$ 78,086
Less: Current portion	<u>(4,772)</u>	<u>(20,028)</u>
	<u>\$ -</u>	<u>\$ 58,058</u>

Minimum future principal payments required under Foodlink's long-term debt agreement is \$4,772 for the year ending June 30, 2017.

Lines-of-Credit

At June 30, 2016 and 2015, Foodlink had available an annually renewable \$750,000 bank line-of-credit, with interest at the prime rate (3.50% at June 30, 2016), but not lower than 4.00%. Amounts borrowed on the line-of-credit are collateralized by a general lien on substantially all of Foodlink's assets. The Foundation has guaranteed Foodlink's line-of-credit. There were no outstanding borrowings on the line-of-credit at June 30, 2016 and 2015.

Subsequent to year end in August 2016, Foodlink increased their line-of-credit agreement with the bank to the amount of \$2,000,000, and there is no longer an interest rate floor of 4.00%. All remaining terms stayed the same.

At June 30, 2016 and 2015, the Foundation had available an annually renewable \$600,000 bank line-of-credit, with interest at the prime rate (3.50% at June 30, 2016), but not lower than 4.00%. Amounts borrowed on the line-of-credit are collateralized by a general lien on substantially all of the Foundation's assets. Foodlink has guaranteed the Foundation's line-of-credit. There was \$97,550 outstanding on this line-of-credit at June 30, 2015. There were no amounts outstanding on this line-of-credit at June 30, 2016.

Subsequent to year end in August 2016, the Foundation decreased their line-of-credit agreement with the bank to the amount of \$500,000, and there is no longer an interest rate floor of 4.00%. All remaining terms stayed the same.

Capital Leases

Foodlink has financed leasehold improvements, equipment and vehicles under the terms of capital lease agreements which expire at various dates through May 2023 and bear interest at rates ranging from 2.99% to 10.64%.

9. FINANCING ARRANGEMENTS (Continued)

Capital Leases (Continued)

At June 30, 2016, cost and accumulated amortization of capital lease assets included in property and equipment on the accompanying balance sheet are as follows:

Leasehold improvements	\$	596,757
Furniture and equipment		433,918
Vehicles		<u>996,593</u>
		2,027,268
Less: Accumulated amortization		<u>(706,829)</u>
	\$	<u>1,320,439</u>

Future scheduled payments on capital lease obligations are as follows for the years ended June 30:

2017	\$	181,592
2018		181,592
2019		159,381
2020		125,992
2021		92,721
Thereafter		<u>126,056</u>
		867,334
Less: Amount representing interest		<u>(108,954)</u>
Present value of net minimum capital lease payments		758,380
Less: Current portion		<u>(145,478)</u>
	\$	<u>612,902</u>

Paid Interest

Interest paid on financing arrangements totaled approximately \$50,000 (approximately \$3,000 paid by the Foundation and \$47,000 paid by Foodlink) and \$111,000 (approximately \$41,000 paid by the Foundation and \$70,000 paid by Foodlink) for the years ended June 30, 2016 and 2015, respectively.

10. RETIREMENT PLANS

Foodlink maintains a 401(k) plan that provides employer contributions of 2% of eligible compensation for employees having at least one year of service, as well as employer match of employee contributions up to 5% of eligible compensation. Foodlink contributed approximately \$114,700 and \$97,200 to the plan in the years ended June 30, 2016 and 2015, respectively.

11. INTERCOMPANY TRANSACTIONS

Administrative Support

Foodlink provides administrative support to the Foundation in the form of personnel and other operating costs. These costs are charged to the Foundation based on agreed-upon methodologies. The administrative costs charged were approximately \$14,000 and \$12,000 for the years ended June 30, 2016 and 2015, respectively.

Facility Use

The Foundation owns a facility, formally used by Foodlink, on Exchange Street. Foodlink leased a portion of the space at this facility from the Foundation, on a month-to-month basis through June 30, 2015, for \$850 per month, which management believes approximated fair market value rent for the space. Effective July 1, 2015, Foodlink is no longer leasing space at Exchange Street.

The Foundation also owned a facility on Joseph Avenue. In March 2015, this property was sold to an unrelated third-party and the Foundation signed a new lease agreement with the unrelated third-party, as described in Note 11. The Foundation is continuing to sublease the property to Foodlink for \$3,693 on a month-to-month basis, through December 2016.

FreshLink leases space in a building on Mt. Read Boulevard for \$19,912 per month plus Common Area Maintenance (CAM) costs. Effective July 1, 2015, FreshLink increased the space leased in this building, increasing the monthly payment to \$6,561 per month, through December 31, 2019, with increases every 5 years through the expiration of the lease on December 31, 2031. This space was subleased to Foodlink for \$19,912 per month through June 30, 2015 and then \$26,473 per month plus CAM costs from July 1, with increases every 5 years through the expiration of the lease on September 30, 2031.

Expected payments under the terms of the leases is as follows for the years ending:

2017	\$ 339,834
2018	317,676
2019	317,676
2020	324,834
2021	331,992
Thereafter	<u>3,555,024</u>
	<u>\$ 5,187,036</u>

Inter-Company Loan

As part of the administrative support functions that Foodlink provides to the Foundation, Foodlink pays the expenses of the Foundation and the Foundation reimburses Foodlink. Foodlink paid \$138,152 and \$265,602 of expenses on behalf of the Foundation during 2016 and 2015, respectively. The non-interest bearing amounts outstanding from the Foundation were \$16,456 as of June 30, 2016. There were no non-interest bearing amounts outstanding from the Foundation as of June 30, 2015.

12. ENDOWMENT

The Foundation's endowment net asset balance consisted of temporarily and permanently restricted net assets. Changes in the endowment net assets were as follows for the years ended June 30:

	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>
Endowment net assets, July 1, 2014	\$ 14,999	\$ 300,000
Contributions	-	200,000
Unappropriated losses	<u>(2,329)</u>	<u>-</u>
Endowment net assets, June 30, 2015	12,670	500,000
Contributions	-	49,042
Unappropriated earnings	<u>7,658</u>	<u>-</u>
Endowment net assets, June 30, 2016	<u>\$ 20,328</u>	<u>\$ 549,042</u>

Interpretation of Relevant Laws

The Foundation's Board of Directors has interpreted the applicable provisions of the New York Prudent Management of Institutional Funds Act (NYPMIFA) 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 Foundation classifies as endowment net assets (a) the original value of the gifts donated to the endowment, (b) the original value of subsequent gifts to the endowment, and (c) accumulations of investment income of the endowment are added to the fund in accordance with the direction of the donor gift instrument. Any unappropriated earnings or appreciation are classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Board of Directors in a manner consistent with the standard of prudence prescribed by New York State law.

Return Objectives and Risk Parameters

The Foundation has adopted investment and spending policies for endowment assets that provides for long-term growth for possible support of the Foundation's budget when other funding sources may not be adequate. A secondary objective is to minimize volatility so that assets are available when they are needed.

Strategies Employed for Achieving Objectives

The Foundation has adopted target asset allocations of no more than 70% in equity securities and no less than 30% in fixed income securities at the time of purchase.

Spending Policy and Related Investment Objectives

The Foundation has adopted a target spending policy whereby 3%-5% of the average value over the trailing 20 quarters will be available for withdrawal annual from the fund. The Foundation will rely on a total return strategy in which assets available for withdrawal will come from either capital appreciation and/or income. The amount to be withdrawn will be calculated as of the last day of the fiscal year. This amount will be available, if needed, to support the operating budget and capital expenses.

13. CONDITIONAL ASSET RETIREMENT OBLIGATIONS

Environmental regulations exist that require the Organizations to handle and dispose of contaminated soil in a special manner if a property undergoes major renovations or excavation. Otherwise, the Organizations are not required to evaluate the level of potential contamination at their properties.

The Organizations have not recorded any liability in connection with these obligations because they cannot estimate the fair value of their potential obligation due to a lack of sufficient information about the timetable over which these obligations may be settled through excavation or sale/transfer of any affected properties.

14. COMMITMENTS AND CONTINGENCIES

Lease Commitments

The Foundation is leasing space at a building on Joseph Avenue under the terms of an operating lease agreement through December 2016. Under the terms of this agreement, the Foundation will begin monthly payments of \$3,693, plus CAM costs, through December 2016.

Additionally, FreshLink leases space in a building on Mt. Read Boulevard for \$19,912 per month plus Common Area Maintenance (CAM) costs. Effective July 1, 2015, FreshLink increased the space leased in this building, increasing the monthly payment to \$6,561 per month, through December 31, 2019, with increases every 5 years through the expiration of the lease on September 30, 2031. This space was subleased to Foodlink for \$19,912 per month through June 30, 2015 and then \$26,473 per month plus CAM costs from July 1, with increases every 5 years through the expiration of the lease on September 30, 2031.

Under the terms of these agreements, the future minimum cash rental payments are as follows for the years ending:

2017	\$ 339,834
2018	317,676
2019	317,676
2020	324,834
2021	331,992
Thereafter	<u>3,555,024</u>
	<u>\$ 5,187,036</u>

Construction Commitment

In 2016, Foodlink entered into a construction contract in the amount of \$3,516,760 for the construction of a new kitchen at the Mt. Read location. The cost of this construction is being funded by capital funding from grants and capital campaign contributions raised by Foodlink and the Foundation. The amount of construction not yet completed as of June 30, 2016 is estimated to be \$2,133,195.

15. SUBSEQUENT EVENTS

Subsequent events have been evaluated through October 11, 2016, which is the date the financial statements were available to be issued.

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

October 11, 2016

To the Board of Directors of
Foodlink, Inc. and Affiliate:

We have audited, in accordance with the 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, the consolidating financial statements of Foodlink, Inc. and Affiliate (New York not-for-profit corporations) (the Organizations), which comprise the consolidating balance sheet as of June 30, 2016, and the related consolidating statements of activities and change in net assets, 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 11, 2016.

Internal Control Over Financial Reporting

In planning and performing our audit of the consolidating financial statements, we considered the Organizations' 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 consolidating financial statements, but not for the purpose of expressing an opinion on the effectiveness of Organizations' internal control. Accordingly, we do not express an opinion on the effectiveness of the Organizations' 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 combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's consolidating 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.

(Continued)

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

(Continued)

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Organizations' consolidating 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 Organization'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 Organization's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.