

*Consolidated financial statements of:*

**SECOND HARVEST HEARTLAND AND SUBSIDIARY**

Years ended  
September 30, 2016 and 2015

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## INDEPENDENT AUDITOR'S REPORT

Board of Directors  
Second Harvest Heartland and Subsidiary  
1140 Gervais Ave.  
Maplewood, MN 55109

### **Report on the Financial Statements**

We have audited the accompanying consolidated financial statements of Second Harvest Heartland and Subsidiary (the Organization) which comprise the consolidated statements of financial position as of September 30, 2016 and 2015, and the related consolidated statements of activities and changes in net assets, cash flows and functional expenses for the years then ended and the related notes to the consolidated financial statements.

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

Management is responsible for the preparation and fair presentation of these consolidated 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 consolidated 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 consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated 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 consolidated 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 consolidated 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 consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Organization as of September 30, 2016 and 2015, and the results of its activities and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

*Schechter Dokken Kanter  
Andrews & Selzer Ltd.*

December 7, 2016

## SECOND HARVEST HEARTLAND AND SUBSIDIARIES

	<u>2016</u>	<u>2015</u>
<b>Assets:</b>		
Current assets:		
Cash and cash equivalents	\$ 2,539,192	\$ 4,154,880
Investments	4,160,621	2,855
Receivables:		
Trade, net	858,898	975,162
Grants	455,846	422,188
Pledges, current portion, net	531,433	140,750
Other	21,168	18,275
Inventory	4,852,048	5,256,059
Prepaid expenses	314,073	260,975
	<u>13,733,279</u>	<u>11,231,144</u>
Property and equipment, net	<u>4,814,467</u>	<u>5,264,731</u>
Investments	914,845	
Pledges receivable, net of current portion	1,229,960	100,000
Other assets	18,649	18,649
	<u>2,163,454</u>	<u>118,649</u>
Total assets	<u>\$ 20,711,200</u>	<u>\$ 16,614,524</u>

See notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

SEPTEMBER 30

	<u>2016</u>	<u>2015</u>
<b><i>Liabilities and net assets:</i></b>		
Current liabilities:		
Accounts payable	\$ 942,635	\$ 772,825
Line of credit	500,000	
Fiscal agent payable	14,361	66,333
Accrued expenses	978,565	1,096,395
Deferred revenue		222,922
Current portion of:		
Note payable	324,006	312,311
Capital leases	234,950	164,114
Deferred rent	22,220	17,592
	<u>3,016,737</u>	<u>2,652,492</u>
Long-term liabilities, net of current portion:		
Note payable	221,933	545,195
Capital leases	1,327,542	1,176,585
Deferred rent	14,554	36,774
	<u>1,564,029</u>	<u>1,758,554</u>
	<u>4,580,766</u>	<u>4,411,046</u>
Net assets:		
Unrestricted:		
Operations	8,039,135	6,892,117
Other	4,349,149	4,638,131
	<u>12,388,284</u>	<u>11,530,248</u>
Temporarily restricted	<u>3,742,150</u>	<u>673,230</u>
	<u>16,130,434</u>	<u>12,203,478</u>
Total liabilities and net assets	<u>\$ 20,711,200</u>	<u>\$ 16,614,524</u>

## SECOND HARVEST HEARTLAND AND SUBSIDIARIES

	2016		
	Unrestricted	Temporarily restricted	Total
Support and revenues:			
Program services	\$ 2,495,987		\$ 2,495,987
Purchase program	6,523,992		6,523,992
Government contracts	2,550,101		2,550,101
Contributions	13,943,874	\$ 4,043,224	17,987,098
Special events, net of expenses of \$289,709 and \$269,134 2016 and 2015, respectively	749,915		749,915
In-kind donations	129,651,051		129,651,051
Investment and miscellaneous income	401,389		401,389
	<u>156,316,309</u>	<u>4,043,224</u>	<u>160,359,533</u>
Less: In-kind donations received as agent	<u>15,711,231</u>		<u>15,711,231</u>
	<u>140,605,078</u>	<u>4,043,224</u>	<u>144,648,302</u>
Net assets released from restrictions	<u>974,304</u>	<u>(974,304)</u>	
Total support and revenues	<u>141,579,382</u>	<u>3,068,920</u>	<u>144,648,302</u>
Expenses:			
Programs	133,381,056		133,381,056
General, administrative and marketing	3,186,873		3,186,873
Fundraising	4,153,417		4,153,417
Total expenses	<u>140,721,346</u>		<u>140,721,346</u>
Change in net assets	858,036	3,068,920	3,926,956
Change in net assets, increase (decrease) from:			
Operations	1,147,018	3,068,920	4,215,938
Other	(288,982)		(288,982)
Total change in net assets	858,036	3,068,920	3,926,956
Net assets, beginning	<u>11,530,248</u>	<u>673,230</u>	<u>12,203,478</u>
Net assets, ending	<u>\$ 12,388,284</u>	<u>\$ 3,742,150</u>	<u>\$ 16,130,434</u>

See notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF ACTIVITIES  
AND CHANGES IN NET ASSETS  
YEARS ENDED SEPTEMBER 30

2015		
Unrestricted	Temporarily restricted	Total
\$ 2,015,041		\$ 2,015,041
8,058,602		8,058,602
2,495,597		2,495,597
14,075,234	\$ 1,022,750	15,097,984
773,101		773,101
119,824,938		119,824,938
87,644		87,644
147,330,157	1,022,750	148,352,907
18,880,265		18,880,265
128,449,892	1,022,750	129,472,642
2,297,491	(2,297,491)	
130,747,383	(1,274,741)	129,472,642
122,721,281		122,721,281
3,085,320		3,085,320
4,024,733		4,024,733
129,831,334		129,831,334
916,049	(1,274,741)	(358,692)
598,927	(864,280)	(265,353)
317,122	(410,461)	(93,339)
916,049	(1,274,741)	(358,692)
10,614,199	1,947,971	12,562,170
<u>\$ 11,530,248</u>	<u>\$ 673,230</u>	<u>\$ 12,203,478</u>



**SECOND HARVEST HEARTLAND AND SUBSIDIARIES**CONSOLIDATED STATEMENTS OF  
CASH FLOWS  
YEARS ENDED SEPTEMBER 30

	<u>2016</u>	<u>2015</u>
Cash flows from operating activities:		
Change in net assets	\$ 3,926,956	\$ (358,692)
Adjustments to reconcile change in net assets to cash provided by (used in) operating activities:		
Depreciation and amortization	1,389,276	1,244,833
Donated securities	(367,839)	(667,679)
Gain on disposal of equipment	(88,464)	(2,345)
Realized and unrealized gains	(191,940)	(3,946)
Temporarily restricted cash contributions	(1,122,559)	
Decrease (increase) in:		
Receivables, net	(1,440,930)	487,853
Prepaid expenses	(53,098)	137,780
Inventory	404,011	28,475
Decrease (increase) in:		
Accounts payable	169,810	(542,799)
Fiscal agent payable	(51,972)	49,972
Accrued expenses	(117,830)	195,654
Deferred:		
Revenue	(222,922)	(171,078)
Rent	(17,592)	(13,055)
Net cash provided by operating activities	<u>2,214,907</u>	<u>384,973</u>
Cash flows from investing activities:		
Purchase of:		
Property and equipment	(506,035)	(375,832)
Investments	(9,864,905)	
Proceeds from sale of:		
Property and equipment	88,464	28,000
Investments	5,352,073	1,433,952
Net cash (used in) provided by investing activities	<u>(4,930,403)</u>	<u>1,086,120</u>

See notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF  
CASH FLOWS  
YEARS ENDED SEPTEMBER 30

**SECOND HARVEST HEARTLAND AND SUBSIDIARIES**

	<b>2016</b>	2015
Cash flows from financing activities:		
Capital campaign cash contributions	<b>\$ 1,122,559</b>	
Payments on:		
Capital leases	<b>(211,184)</b>	\$ (44,518)
Long-term debt	<b>(311,567)</b>	(301,507)
Proceeds from line of credit	<b>500,000</b>	
Net cash provided by (used in) financing activities	<b>1,099,808</b>	(346,025)
Net (decrease) increase in cash and cash equivalents	<b>(1,615,688)</b>	1,125,068
Cash and cash equivalents, beginning	<b>4,154,880</b>	3,029,812
Cash and cash equivalents, ending	<b>\$ 2,539,192</b>	\$ 4,154,880
Supplemental disclosure of cash flow information:		
Cash paid for interest	<b>\$ 81,965</b>	\$ 44,851
Purchase of equipment through capital leases	<b>\$ 432,977</b>	\$ 1,349,471

See notes to consolidated financial statements.

## SECOND HARVEST HEARTLAND AND SUBSIDIARIES

	Programs				
	CSFP	Food Bank	Food Rescue	Agency Relations	Community Outreach
Wages and temporary services	\$ 267,975	\$ 3,136,332	\$ 778,916	\$ 438,996	\$ 670,603
Fringe benefits and payroll taxes	63,457	739,339	192,829	126,392	156,310
Professional fees		6,595		9,205	161,295
In-kind professional fees					
Occupancy	109,834	638,481	3,282	5,809	9,110
Vehicles operation	105,094	545,775	309,730	20	11,561
Procurement	58,334	1,900,414	86	25	1,683
Equipment	22,808	401,364	41,506	24,619	45,053
Supplies	24,516	55,826	5,364	9,876	19,753
Meeting, travel and staff development	4,769	28,951	16,030	33,328	77,042
Promotions and marketing	272	3,094			29,640
Special events					
Direct mail					
Cluster/network fees					
Agency assistance				9,761	45,000
Subgrant awards - HFMN					
In-kind distributed*	6,442,814	123,593,366			
Cost of purchased product disbursed	80	6,336,014			175,558
Other					
Depreciation and amortization	24,439	1,036,308	85,228	24,272	44,542
Bad debt		40			
Interest	2,407	67,516	9,056	306	435
	<u>7,126,799</u>	<u>138,489,415</u>	<u>1,442,027</u>	<u>682,609</u>	<u>1,447,585</u>
Less:					
In-kind distributed as agent		15,807,379			
Special events					
	<u>\$ 7,126,799</u>	<u>\$ 122,682,036</u>	<u>\$ 1,442,027</u>	<u>\$ 682,609</u>	<u>\$ 1,447,585</u>

\*Food Bank in-kind distributed includes Food Rescue Product.

See notes to consolidated financial statements.

CONSOLIDATED STATEMENT OF FUNCTIONAL EXPENSES  
YEAR ENDED SEPTEMBER 30, 2016  
(WITH COMPARATIVE TOTALS FOR 2015)

Programs total	Support services			Total	2015 Total
	G&A and marketing	Fundraising	Support total		
\$ 5,292,822	\$ 1,868,117	\$ 1,547,413	\$ 3,415,530	\$ 8,708,352	\$ 9,167,189
1,278,327	421,875	352,613	774,488	2,052,815	2,302,169
177,095	493,769	285,000	778,769	955,864	811,453
					19,366
766,516	98,661	57,687	156,348	922,864	876,645
972,180	6,298	353	6,651	978,831	1,236,493
1,960,542				1,960,542	1,294,314
535,350	34,264	76,837	111,101	646,451	636,403
115,335	17,128	147,481	164,609	279,944	328,019
160,120	54,001	33,192	87,193	247,313	247,757
33,006	88,008	177,074	265,082	298,088	225,333
		289,709	289,709	289,709	269,134
	3,515	1,362,520	1,366,035	1,366,035	1,212,153
	30,002		30,002	30,002	632,819
54,761				54,761	84,748
					677,975
130,036,180				130,036,180	119,988,232
6,511,652				6,511,652	7,759,070
	5,235		5,235	5,235	11,096
1,214,789	62,062	112,425	174,487	1,389,276	1,244,833
40	2,515		2,515	2,555	
79,720	1,423	822	2,245	81,965	44,851
149,188,435	3,186,873	4,443,126	7,629,999	156,818,434	149,070,052
15,807,379				15,807,379	18,969,584
		289,709	289,709	289,709	269,134
<u>\$ 133,381,056</u>	<u>\$ 3,186,873</u>	<u>\$ 4,153,417</u>	<u>\$ 7,340,290</u>	<u>\$ 140,721,346</u>	<u>\$ 129,831,334</u>

## SECOND HARVEST HEARTLAND AND SUBSIDIARIES

	Programs			
	CSFP	Food Bank	Food Rescue	Agency Relations
Wages and temporary services	\$ 255,536	\$ 3,488,741	\$ 693,874	\$ 451,510
Fringe benefits and payroll taxes	72,620	955,759	190,812	126,894
Professional fees		375		
In-kind professional fees				
Occupancy	94,957	627,387	3,174	5,211
Vehicles operation	57,228	831,479	324,918	
Procurement	62,110	1,221,600	59	
Equipment	17,095	414,966	34,385	23,736
Supplies	22,826	79,524	4,899	9,824
Meeting, travel and staff development	6,207	43,796	12,064	33,912
Promotions and marketing		16,159		1,432
Special events				
Direct mail				
Cluster/network fees		606,510		
Agency assistance			622	8,042
Subgrant awards - HFMM				
In-kind distributed*	5,988,395	113,999,837		
Cost of purchased product disbursed		7,622,058		
Other	68	3,563	1,152	264
Depreciation and amortization	39,232	913,252	88,209	26,499
Bad debt				
Interest	3,274	37,100	1,371	407
	<u>6,619,548</u>	<u>130,862,106</u>	<u>1,355,539</u>	<u>687,731</u>
Less:				
In-kind distributed as agent		18,969,584		
Special events				
	<u>\$ 6,619,548</u>	<u>\$ 111,892,522</u>	<u>\$ 1,355,539</u>	<u>\$ 687,731</u>

\*Food Bank in-kind distributed includes Food Rescue Product.

See notes to consolidated financial statements.

CONSOLIDATED STATEMENT OF FUNCTIONAL EXPENSES  
YEAR ENDED SEPTEMBER 30, 2015

Community Outreach	Programs total	Support services			Total
		G&A and marketing	Fundraising	Support total	
\$ 664,765	\$ 5,554,426	\$ 2,096,049	\$ 1,516,714	\$ 3,612,763	\$ 9,167,189
146,395	1,492,480	435,318	374,371	809,689	2,302,169
219,546	219,921	192,566	398,966	591,532	811,453
		19,366		19,366	19,366
12,958	743,687	111,783	21,175	132,958	876,645
16,255	1,229,880	6,588	25	6,613	1,236,493
7,130	1,290,899	398	3,017	3,415	1,294,314
36,312	526,494	37,871	72,038	109,909	636,403
19,015	136,088	32,639	159,292	191,931	328,019
70,315	166,294	48,935	32,528	81,463	247,757
40,761	58,352	8,694	158,287	166,981	225,333
			269,134	269,134	269,134
		2,597	1,209,556	1,212,153	1,212,153
	606,510	26,309		26,309	632,819
75,562	84,226	522		522	84,748
677,975	677,975				677,975
	119,988,232				119,988,232
137,012	7,759,070				7,759,070
2,939	7,986	2,838	272	3,110	11,096
38,431	1,105,623	61,881	77,329	139,210	1,244,833
570	42,722	966	1,163	2,129	44,851
<u>2,165,941</u>	<u>141,690,865</u>	<u>3,085,320</u>	<u>4,293,867</u>	<u>7,379,187</u>	<u>149,070,052</u>
	18,969,584				18,969,584
			269,134	269,134	269,134
<u>\$ 2,165,941</u>	<u>\$ 122,721,281</u>	<u>\$ 3,085,320</u>	<u>\$ 4,024,733</u>	<u>\$ 7,110,053</u>	<u>\$ 129,831,334</u>

1. Summary of significant accounting policies:

Nature of activities:

Second Harvest Heartland (the Organization) is a not-for-profit organization dedicated to ending hunger through community partnerships and increasing public awareness of hunger. The Organization obtains, stores and distributes donated and purchased food to member agencies and directly to low income individuals in Minnesota and Western Wisconsin. The Organization is a member of Feeding America, an association of more than 200 food banks serving the entire county. The Organization administers two government programs: The Emergency Food Assistance Program (TEFAP) and the Commodity Supplemental Food Program (CSFP). The organization is engaged in a capital campaign for funding of capital expansion and improvements. Private and governmental funding was raised in 2016 to pursue expansion of services in partnership with the Health care industry. The Organization also administers a food rescue program as well as provides food to member agencies (food bank program) and other programs that address hunger issues. Financial funding for the Organization comes from general contributions, grants, fees charged to member agencies and non-financial funding comes from donations and grants of food.

During fiscal year 2011, Second Harvest Heartland created a single member LLC called Hunger-Free Minnesota, LLC. Hunger-Free Minnesota has a strategic, three-year action plan to close the gap of 100 million missing meals every year across the state of Minnesota. In fiscal year 2015, after providing grants to more than 400 partner agencies, and sponsoring media to create hunger insecurity awareness statewide, Hunger-Free Minnesota LLC operations sunsetted. There was no activity for Hunger-Free Minnesota LLC in 2016.

Principles of consolidation:

The consolidated financial statements include the accounts of Second Harvest Heartland and its wholly owned subsidiary, Hunger-Free Minnesota, LLC. All significant intercompany accounts and transactions have been eliminated in the consolidated financial statements.

Use of estimates:

The financial statements have been prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America which requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Actual results could differ from those estimates. Significant estimates include in-kind donated food inventory, receipts and distributions.

Major source of revenue:

The Organization received approximately 15% and 13% of total support and revenue from one governmental agency for the years ended September 30, 2016 and 2015, respectively.

Contributions and grants:

All contributions and grants are considered to be available for unrestricted use unless specifically restricted by the donor. Donor-restricted contributions are reported as increases in temporarily or permanently restricted net assets depending on the nature of the restrictions. When a restriction expires, temporarily restricted net assets are reclassified to unrestricted net assets. If a restriction expires in the same fiscal year in which the contribution was recognized, the contribution is reported as an increase in unrestricted net assets. At the end of fiscal years 2016 and 2015, the Organization did not have any permanently restricted net assets.

1. Summary of significant accounting policies (continued):

Unrestricted net assets:

The Organization presents its unrestricted net assets in two categories, operations and other. The other category is the accumulated effect that in-kind activity has on ending inventory, along with the repayment of administrative expenses for prior years made by its single member LLC, Hunger-Free MN, while the operations amount is the accumulated effect of change in net assets excluding those other activities.

Functional allocation of expenses:

The costs of providing various programs and other activities have been summarized on a functional basis in the statements of activities and change in net assets. Expenses that relate to more than one program or function have been allocated based on the best estimates of management.

Received product:

The Organization reports contributions of food over which it has control as unrestricted in-kind donations. Public donations of food and food obtained through USDA commodity programs (TEFAP and CSFP) are valued based on a weighted average wholesale price per pound. This valuation is determined using a report provided annually by Feeding America based on an annual study. During fiscal years 2016 and 2015, the Organization received 96,570,000 and 91,254,000 pounds of food, respectively. The Organization reported in-kind donations for donated food, along with purchased product valued at cost, as follows:

	<u>2016</u>	
	<u>Pounds</u>	<u>Dollars</u>
Donated product	<b>71,141,000</b>	<b>\$ 109,169,000</b>
TEFAP	<b>8,432,000</b>	<b>13,967,000</b>
CSFP	<b>3,812,000</b>	<b>6,515,000</b>
Donated services		
In-kind donations	<b>83,385,000</b>	<b>129,651,000</b>
Purchased	<b>13,185,000</b>	<b>6,397,000</b>
Total received	<b><u>96,570,000</u></b>	<b><u>\$ 136,048,000</u></b>
In-kind donations as agent	<b><u>7,880,000</u></b>	<b><u>\$ 15,711,231</u></b>
	<u>2015</u>	
	<u>Pounds</u>	<u>Dollars</u>
Donated product	65,440,000	\$ 102,902,000
TEFAP	7,281,000	11,048,000
CSFP	3,449,000	5,856,000
Donated services		19,000
In-kind donations	76,170,000	119,825,000
Purchased	<u>15,084,000</u>	<u>7,806,000</u>
Total received	<b><u>91,254,000</u></b>	<b><u>\$ 127,631,000</u></b>
In-kind donations as agent	<b><u>8,104,000</u></b>	<b><u>\$ 18,880,000</u></b>



1. Summary of significant accounting policies (continued):

The Organization acts as an agent for five other Feeding America entities with locations in Minnesota. Per contractual arrangements, the Organization re-distributes certain products to these other Feeding America locations.

Distributed product:

During fiscal years 2016 and 2015, the Organization distributed 93,385,000 and 88,912,000 pounds of food, respectively, to member agencies and partners. The following reflects all of the Organization's distributions (including purchased product, but excluding waste and non-waste adjustments) during fiscal years 2016 and 2015:

	<u>2016</u>	
	<u>Pounds</u>	<u>Dollars</u>
Donated product	<b>67,792,000</b>	<b>\$ 105,049,000</b>
TEFAP	<b>8,555,000</b>	<b>14,166,000</b>
CSFP	<b>3,783,000</b>	<b>6,460,000</b>
In-kind distributions	<b>80,130,000</b>	<b>125,675,000</b>
Purchased	<b>13,255,000</b>	<b>6,506,000</b>
Total distributions	<b><u>93,385,000</u></b>	<b><u>\$ 132,181,000</u></b>
In-kind distributions as agent	<b><u>7,850,000</u></b>	<b><u>\$ 15,279,000</u></b>
	<u>2015</u>	
	<u>Pounds</u>	<u>Dollars</u>
Donated product	63,019,000	\$ 99,613,000
TEFAP	7,312,000	10,831,000
CSFP	<u>3,717,000</u>	<u>6,078,000</u>
In-kind distributions	74,048,000	116,522,000
Purchased	<u>14,864,000</u>	<u>7,714,000</u>
Total distributions	<b><u>88,912,000</u></b>	<b><u>\$ 124,236,000</u></b>
In-kind distributions as agent	<b><u>8,070,000</u></b>	<b><u>\$ 18,899,000</u></b>

1. Summary of significant accounting policies (continued):

Contributed services:

The Organization received donated in-kind professional business services in 2016 and 2015 which were recorded as revenue and expense at the fair value as established by the donor of \$0 and \$19,366, respectively.

Members of the Organization and volunteers have donated significant amounts of their time to enhancing the Organization's activities. The number of unique volunteers and hours of service totaled 28,800 and 132,800 in 2016, respectively. The number of unique volunteers and hours of service totaled 30,500 and 140,750 in 2015, respectively. However, the value of these donated services is generally not reflected in the accompanying financial statements since there is no objective basis available by which to measure the value of such services.

Cash and cash equivalents:

Cash and cash equivalents include interest bearing money market accounts and any investments with an original maturity of three months or less. The Organization maintains its cash and cash equivalents with various financial institutions. At times, these balances may exceed federally insured limits. The Organization has not experienced a loss as a result of these deposits.

Investments:

Investments in marketable securities with readily determinable fair value and all investments in debt securities are valued 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:

The Organization's investments are reported using a framework for measuring fair value. The framework provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements).

The three levels of the fair value hierarchy are described below:

Level 1 - Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets, for which prices are available at the measurement date.

Level 2 - Inputs to the valuation methodology include:

- Quoted prices for similar assets or liabilities in active markets;
- Quoted prices for identical or similar assets or liabilities in inactive markets;
- Inputs other than quoted prices that are observable for the asset or liability;
- Inputs that are derived principally from or corroborated by observable market data by correlation or other means.

1. Summary of significant accounting policies (continued):

Fair value measurements (continued):

If the asset or liability has a specified (contractual) term, the Level 2 input must be observable for substantially the full term of the asset or liability.

Level 3 - Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

The asset's or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques used must maximize the use of observable inputs and minimize the use of unobservable inputs.

Inventory:

Inventory is valued on a first-in, first-out basis. Public donations of food and food obtained through USDA commodity programs (TEFAP and CFSP) are valued based on a weighted average wholesale price per pound. This valuation is determined using a report provided annually by Feeding America based on an annual study. Purchased food is valued based on actual cost. Inventory is shown net of any inventory on-hand that is allocated to Feeding America entities for which the Organization is only acting as an agent.

Property and equipment:

Property and equipment are stated at cost. Contributed property and equipment are recorded at fair value at the date of donation. Depreciation is provided over the estimated useful lives of the assets by the straight-line method. The capitalization policy of the Organization is to capitalize all property and equipment over \$5,000. Asset lives are as follows:

Buildings	40 years
Building improvements	10-25 years
Equipment	3-10 years
Autos and trucks	3-10 years

Computer software:

The Organization capitalizes the costs of obtaining or developing internal use software including directly related payroll costs and amortizes those costs over a period of three years, beginning when the software is ready for its intended use.

Trade receivable and bad debt:

Trade receivables are stated at original invoice amount less an estimate for doubtful receivables based on management's review of all outstanding amounts and historical experience. Accounts receivable are written-off when deemed uncollectible. Recoveries of accounts previously written-off are recorded when received. The allowance for doubtful accounts was \$32,109 as of September 30, 2016 and 2015. The Organization transacts with its member agencies on open credit and such accounts receivable are uncollateralized. The maximum loss that would be incurred if a member agency failed to pay amounts owed would be limited to the recorded amount due after any allowances provided.

An account is considered past due if the balance is outstanding for more than 90 days.

1. Summary of significant accounting policies (continued):

Grants receivable:

Grants receivable are stated at the estimated net realizable value after provision for doubtful accounts. There was no allowance related to grants receivable at September 30, 2016 and 2015. Grants receivable at September 30, 2016 and 2015 are due in less than one year.

Pledges receivable:

Unconditional promises to give are recorded at net realizable value. The allowance for uncollectible pledges was \$54,476 and \$0 as of September 30, 2016 and 2015, respectively. Conditional promises to give are recognized when the conditions are met.

Deferred revenue:

Deferred revenue represents governmental grants collected before the related service has been performed.

Income taxes:

The Organization is exempt, as a public charity, from federal and state income taxes under Section 501(c)(3) of the Internal Revenue Code and applicable state statutes. However, income from certain activities not directly related to the Organization's tax-exempt purpose could result in taxable income.

The Organization has evaluated its tax positions for uncertainty and has no unrecognized tax matters that are required to be disclosed.

The Organization is open to examination for tax years 2012 through 2014. The Organization had no income tax expense and there were no cash payments for income taxes in fiscal years 2016 or 2015.

Advertising costs:

Advertising costs are expensed as incurred. Total advertising expense was \$1,579,178 and \$1,342,011 for the years ended September 30, 2016 and 2015, respectively.

Reclassifications:

Certain reclassifications have been made to the 2015 financial statements to conform to the 2016 presentation.

Subsequent events:

The Organization evaluated for subsequent events through December 7, 2016, the date the financial statements were available for issuance.

**SECOND HARVEST HEARTLAND  
AND SUBSIDIARY**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
YEARS ENDED SEPTEMBER 30, 2016 AND 2015

2. Fair value measurements:

The following table presents the fair value hierarchy for the balances of the assets of the Organization measured at fair value on a recurring basis as of September 30, 2016 and 2015.

	2016			
	Level 1	Level 2	Level 3	Total
Equities:				
Large value	\$ 179,764			\$ 179,764
Large blend	556,152			556,152
Foreign large blend	125,672			125,672
Other	329,844			329,844
Fixed income:				
Corporate bond	2,801,108			2,801,108
Foreign bond	150,732			150,732
Hedged bond	284,241			284,241
Short-term bond	267,391			267,391
Intermediate bond	319,345			319,345
Other	61,217			61,217
	<u>\$ 5,075,466</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 5,075,466</u>
	2015			
	Level 1	Level 2	Level 3	Total
Equities, other	<u>\$ 2,855</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 2,855</u>

3. Inventory:

Ending inventory is comprised of the following:

	2016	2015
Donated	\$ 2,148,633	\$ 2,322,951
TEFAP	755,292	942,631
CSFP	1,445,224	1,372,549
Purchased	<u>502,899</u>	<u>617,928</u>
	<u>\$ 4,852,048</u>	<u>\$ 5,256,059</u>

**SECOND HARVEST HEARTLAND  
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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
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4. Pledges receivable:

Unconditional promises to give are recorded as pledges receivable and revenue of the appropriate net asset category.

Unconditional promises to give at September 30 are as follows:

	<u>2016</u>	<u>2015</u>
Unrestricted promises	\$ 202,393	\$ 25,750
Restricted promises	<u>1,559,000</u>	<u>215,000</u>
Contributions receivable	<u>\$ 1,761,393</u>	<u>\$ 240,750</u>
Amounts due in:		
Less than one year	\$ 672,869	\$ 140,750
One to five years	\$ 1,088,524	\$ 100,000

During the fiscal year ending September 30, 2016, the Organization received conditional pledges in the total of \$3,000,000 dollars dependent on the receipt of private and governmental funds for future capital expenditures.

5. Property and equipment:

	<u>2016</u>	<u>2015</u>
Building	\$ 1,235,416	\$ 1,235,416
Building improvements	4,535,956	4,350,379
Office equipment	2,368,841	2,322,378
Warehouse equipment	2,242,555	2,172,805
Autos and trucks	4,921,167	4,283,945
Land	<u>220,000</u>	<u>220,000</u>
	<u>15,523,935</u>	14,584,923
Less accumulated depreciation and amortization	<u>10,709,468</u>	<u>9,320,192</u>
	<u>\$ 4,814,467</u>	<u>\$ 5,264,731</u>

6. Line of credit:

The Organization has a bank line of credit, secured by certain assets, in the amount of \$1,200,000. The line carries an interest rate of prime less .25% (3.25% at September 30, 2016 and 2015). The balance of the line was \$500,000 and \$0 at September 30, 2016 and 2015, respectively. The line is scheduled to expire on May 1, 2017.

**SECOND HARVEST HEARTLAND  
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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
YEARS ENDED SEPTEMBER 30, 2016 AND 2015

7. Long-term debt:

	<u>2016</u>	<u>2015</u>
Mortgage payable with interest at .25% over the prime rate with a ceiling of 5.25%. The prime rate was 3.25% as of September 30, 2016 and 2015. Payable in monthly installments of \$28,148 and maturing in May 2018. Mortgage is collateralized by building and accessories.	\$ 545,939	\$ 857,506
Less current portion	<u>324,006</u>	<u>312,311</u>
	<u>\$ 221,933</u>	<u>\$ 545,195</u>

Future maturities of long-term debt are as follows:

<u>Year ending September 30</u>	<u>Amount</u>
2017	\$ 324,006
2018	<u>221,933</u>
	<u>\$ 545,939</u>

8. Operating leases:

The Organization leases vehicles and warehouse equipment expiring through 2020. Total rent expense for the years ended September 30, 2016 and 2015 was \$146,100 and \$276,309, respectively.

The Organization also leases space to carry out organization objectives. This lease expires in May 2018. In addition to minimum base rental payments, the Organization is required to pay its proportional share of real estate taxes and operating expenses. Rent expense was \$337,339 and \$332,583 for the years ended September 30, 2016 and 2015, respectively.

Future minimum lease payments are as follows:

<u>Year ending September 30</u>	<u>Amount</u>
2017	\$ 240,563
2018	143,818
2019	4,552
2020	<u>379</u>
	<u>\$ 389,312</u>

**SECOND HARVEST HEARTLAND  
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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
YEARS ENDED SEPTEMBER 30, 2016 AND 2015

9. Capital lease:

The Organization has thirteen capital leases for vehicles and warehouse equipment which expire at various dates during fiscal years 2016 – 2023. The vehicles and warehouse equipment were recorded at fair value on the lease commitment date.

The cost and accumulated amortization related to an asset that was held under capital leases are as follows:

	<u>2016</u>	<u>2015</u>
Equipment cost	\$ 1,782,448	\$ 1,384,386
Less accumulated amortization	<u>256,191</u>	<u>50,978</u>
	<u>\$ 1,526,257</u>	<u>\$ 1,333,408</u>

Future principal and interest payments under the capital lease as of September 30, 2016, are as follows:

<u>Year ending September 30</u>	<u>Amount</u>
2017	\$ 287,320
2018	279,324
2019	279,324
2020	279,324
2021	279,324
Thereafter	<u>339,643</u>
	1,744,259
Less amounts representing interest	<u>181,767</u>
Present value of net minimum lease obligation payments	<u>\$ 1,562,492</u>

10. Temporarily restricted net assets:

Temporarily restricted net assets are available for the following purposes:

	<u>2016</u>	<u>2015</u>
SNAP	\$ 14,000	\$ 108,000
Produce		10,000
Child Nutrition	295,492	127,802
Capital investment	5,931	338,600
Equipment	6,877	24,788
Hunger and Health	809,953	
Capital Campaign	2,131,756	
Other programming and fundraising	<u>478,141</u>	<u>64,040</u>
	<u>\$ 3,742,150</u>	<u>\$ 673,230</u>



11. Net assets released from restriction:

Net assets were released from donor restrictions by incurring expenses satisfying the restricted purpose or by occurrence of other events specified by donors as follows:

	<u>2016</u>	<u>2015</u>
SNAP	\$ 114,000	\$ 82,213
Produce	74,040	278,620
Child Nutrition	153,893	399,013
Capital investment	137,069	379,502
Equipment	17,910	22,463
Hunger-Free MN		1,069,270
Hunger and Health	189,047	
Capital Campaign	149,745	
Other programming and fundraising	<u>138,600</u>	<u>66,410</u>
	<u>\$ 974,304</u>	<u>\$ 2,297,491</u>

12. Fiscal agent:

During the years ending September 30, 2016 and 2015, the Organization received cash from donors for which it is acting as a fiscal agent, which were not fully disbursed at September 30, 2016 and 2015. As such, these funds have been treated as current liabilities in the accompanying financial statements.

The Organization has received food donations that are, by contract, allocated to other food banks. Amounts of inventory on-site that were so allocated were \$446,082 and \$542,223 for September 30, 2016 and 2015, respectively. These amounts were not included in the final inventory as presented on the statement of financial position.

13. Retirement plan:

The Organization has a defined contribution 403(b) thrift plan, in which employees are eligible to participate on the first of the month following 30 days of employment. The Organization contributes 4% of the employees' annual salaries to the Plan regardless of whether the employees contributes any of their pretax wages to the Plan. The Organization also matches 50% of employees' contributions up to 4%. The employees vest at a rate of 25% per year and are fully vested after four years in the plan. The expense for the plan was \$384,337 and \$446,580 for the years ended September 30, 2016 and 2015, respectively.