

**LARSON &
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Certified Public Accountants



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**DIRECT RELIEF INTERNATIONAL
(A NON-PROFIT CORPORATION)**

**Independent Auditor's Report
And
Accompanying Financial Statements**

March 31, 2006

**DIRECT RELIEF INTERNATIONAL
(A NON-PROFIT CORPORATION)**

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INDEPENDENT AUDITOR'S REPORT


Board of Directors
Direct Relief International
Santa Barbara, California

We have audited the accompanying statements of financial position of Direct Relief International, a non-profit corporation, as of March 31, 2006 and 2005 and the related statements of activities, changes in net assets, functional expenses and cash flows for the years then ended. These financial statements are the responsibility of Direct Relief International's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audits in accordance with generally accepted auditing standards in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the accompanying financial statements referred to above present fairly, in all material respects, the financial position of Direct Relief International at March 31, 2006 and 2005 and the results of its operations for the years then ended, in conformity with generally accepted accounting principles in the United States of America.

June 21, 2006
Santa Barbara, California


Larson & Ridge LLP
Certified Public Accountants

**DIRECT RELIEF INTERNATIONAL
(A NON-PROFIT CORPORATION)
STATEMENT OF FINANCIAL POSITION
MARCH 31, 2006**

WITH COMPARATIVE TOTALS AS OF MARCH 31, 2005

	Unrestricted Funds	Temporarily Restricted Funds	Permanently Restricted Funds	Total All Funds March 31, 2006	Total All Funds March 31, 2005
Assets					
Current assets:					
Cash and cash equivalents	\$ 1,792,275	\$ 6,081,410	\$ -	\$ 7,873,684	\$ 12,836,987
Investments in marketable securities	9,334,980	-	25,036	9,360,016	6,596,966
Contributions receivable	140,784	-	-	140,784	298,711
Inventories	24,210,039	-	-	24,210,039	95,445,318
Prepaid expenses	77,403	-	-	77,403	40,903
Total current assets	<u>35,555,481</u>	<u>6,081,410</u>	<u>25,036</u>	<u>41,661,927</u>	<u>115,218,885</u>
Property and equipment - net of accumulated depreciation of \$666,518	3,666,840			3,666,840	3,169,394
Contributions receivable from remainder unitrusts	37,485			37,485	67,219
Investment in real estate	-			-	-
Other assets	3,332			3,332	5,437
Total assets	<u>\$ 39,263,138</u>	<u>\$ 6,081,410</u>	<u>\$ 25,036</u>	<u>\$ 45,369,584</u>	<u>\$ 118,460,935</u>
Liabilities and Net Assets					
Liabilities:					
Current liabilities:					
Accounts payable	\$ 78,257	\$ -	\$ -	\$ 78,257	\$ 314,660
Current portion of long-term debt	51,821			51,821	49,242
Other current liabilities	313,075			313,075	219,975
Total current liabilities	<u>443,153</u>	<u>-</u>	<u>-</u>	<u>443,153</u>	<u>583,877</u>
Long-term debt	1,467,282			1,467,282	1,519,104
Capital Lease Obligation	20,990			20,990	-
Distribution payable - split interest agreements		28,542		28,542	27,121
Total liabilities	<u>1,931,425</u>	<u>28,542</u>	<u>-</u>	<u>1,959,967</u>	<u>2,130,102</u>
Net assets:					
Unrestricted net assets:					
Board designated reserve fund	9,549,798			9,549,798	7,358,570
Undesignated	27,781,915			27,781,915	99,457,873
Total unrestricted net assets	<u>37,331,713</u>	<u>-</u>	<u>-</u>	<u>37,331,713</u>	<u>106,816,443</u>
Temporarily restricted assets		6,052,868		6,052,868	9,504,390
Permanently restricted assets			25,036	25,036	10,000
Total net assets	<u>37,331,713</u>	<u>6,052,868</u>	<u>25,036</u>	<u>43,409,617</u>	<u>116,330,833</u>
Total liabilities and net assets	<u>\$ 39,263,138</u>	<u>\$ 6,081,410</u>	<u>\$ 25,036</u>	<u>\$ 45,369,584</u>	<u>\$ 118,460,935</u>

See notes to financial statements.

DIRECT RELIEF INTERNATIONAL
(A NON-PROFIT CORPORATION)
STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED MARCH 31, 2006

WITH COMPARATIVE TOTALS FOR THE YEAR ENDED MARCH 31, 2005

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total All Funds March 31, 2006</u>	<u>Total All Funds March 31, 2005</u>
Public support and revenue					
Public support:					
In cash and securities:					
Contributions	\$ 4,134,403	\$ 8,331,075	\$ 15,152	\$ 12,480,629	\$ 19,534,756
Corporate and foundation grants	923,000	761,850	-	1,684,850	560,850
Freight reimbursements - U.S. Agency for International Development				-	104,544
Workplace giving campaigns	138,430	-	-	138,430	51,970
Special events	135,666	-	-	135,666	297,357
Total public support from cash and securities	<u>5,331,499</u>	<u>9,092,925</u>	<u>15,152</u>	<u>14,439,576</u>	<u>20,549,477</u>
From donated goods and services:				-	-
Pharmaceuticals, medical supplies and equipment	120,995,512	-	-	120,995,512	199,570,989
Contributed freight	516,962	-	-	516,962	592,806
Professional services received				-	24,608
Total from goods and services	<u>121,512,474</u>	<u>-</u>	<u>-</u>	<u>121,512,474</u>	<u>200,188,403</u>
Total Public support	126,843,973	9,092,925	15,152	135,952,050	220,737,880
Revenue:					
Investment income	670,992	216,325	-	887,317	143,013
Gain on sale of investments	51,965	(218)	(115)	51,632	43,534
Change in value - split interest agreements	6,772	(8,531)	-	(1,759)	26,046
Unrealized gain on investments	600,782	(289)	-	600,493	338,548
Program service fees	-	6,625	-	6,625	10,625
Other income	(33,480)	11,836	-	(21,644)	45,789
Total revenue	<u>1,297,030</u>	<u>225,748</u>	<u>(115)</u>	<u>1,522,663</u>	<u>607,555</u>
Net assets released from restrictions:					
Restrictions satisfied by payments	12,770,195	(12,770,195)		-	-
Total public support and revenue	<u>140,911,198</u>	<u>(3,451,522)</u>	<u>15,036</u>	<u>137,474,712</u>	<u>221,345,435</u>
Expenses					
Program services:					
Medical supplies and related expenses	208,716,879			208,716,879	126,574,389
Supporting services:					
Fundraising	680,955			680,955	676,219
Administration	998,093			998,093	583,173
Total supporting services	<u>1,679,048</u>	<u>-</u>	<u>-</u>	<u>1,679,048</u>	<u>1,259,392</u>
Total expenses	<u>210,395,928</u>	<u>-</u>	<u>-</u>	<u>210,395,928</u>	<u>127,833,781</u>
(Decrease) Increase in net assets	<u>\$ (69,484,730)</u>	<u>\$ (3,451,522)</u>	<u>\$ 15,036</u>	<u>\$ (72,921,216)</u>	<u>\$ 93,511,654</u>

See notes to financial statements.

**DIRECT RELIEF INTERNATIONAL
(A NON-PROFIT CORPORATION)
STATEMENTS OF CHANGES IN NET ASSETS
FOR THE YEAR ENDED MARCH 31, 2006**

WITH COMPARATIVE TOTALS FOR THE YEAR ENDED MARCH 31, 2005

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Balance at March 31, 2004	\$ 22,652,640	\$ 166,539	\$ -	\$ 22,819,179
Increase in net assets for the year ended March 31, 2005	84,163,803	9,337,851	10,000	93,511,654
Balance at March 31, 2005	<u>\$ 106,816,443</u>	<u>\$ 9,504,390</u>	<u>\$ 10,000</u>	<u>\$ 116,330,833</u>
Balance at March 31, 2005	\$ 106,816,443	\$ 9,504,390	\$ 10,000	\$ 116,330,833
Decrease in net assets for the year ended March 31, 2006	(69,484,730)	(3,451,522)	15,036	(72,921,216)
Balance at March 31, 2006	<u>\$ 37,331,713</u>	<u>\$ 6,052,868</u>	<u>\$ 25,036</u>	<u>\$ 43,409,617</u>

See notes to financial statements.

DIRECT RELIEF INTERNATIONAL
(A NON-PROFIT CORPORATION)
STATEMENT OF FUNCTIONAL EXPENSES
FOR THE YEAR ENDED MARCH 31, 2006

WITH COMPARATIVE TOTALS FOR THE YEAR ENDED MARCH 31, 2005

	Domestic Services	Program Services International Services	Tsunami Services	Katrina Services	Pakistan Services	Total Program Services	Supporting Services Administration	Fundraising	Total Program and Supporting Services March 31, 2006	Total Program and Supporting Services March 31, 2005
Compensation and related benefits:										
Contributed services	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 10,000	\$ -	\$ 10,000	\$ -
Salaries	208,541	1,016,240	63,294	-	-	1,288,075	472,034	248,024	2,008,133	1,585,696
Payroll taxes	15,815	76,940	4,842	-	-	97,596	35,350	17,598	150,543	123,908
Employee benefits	31,491	153,782	1,032	-	-	186,304	35,310	13,605	235,220	224,589
Total compensation and related benefits	255,846	1,246,962	69,168	-	-	1,571,975	552,694	279,226	2,403,896	1,958,801
Other expenses										
Pharmaceuticals, medical equipment and supplies distributed	1,047,317	140,381,105	15,374,510	26,411,431	6,842,320	190,056,683	-	-	190,056,683	119,419,491
Inventry valuation adjustments	-	2,179,103	-	-	-	2,179,103	-	-	2,179,103	296,270
Accounting and legal	1,117	5,469	40	-	-	6,625	33,674	348	40,647	19,991
Advertising	1,162	792	-	-	-	953	443	11,636	13,032	27,524
Bank charges and brokerage fees	2,234	10,936	41	-	-	13,210	44,866	58,077	58,077	94,809
Contract services	33,979	69,943	41,095	1,562	-	146,579	247,191	29,935	423,705	127,872
Contributed freight expense	131,124	642,012	-	-	-	773,136	-	-	773,136	592,806
Development education	923	4,517	-	-	-	5,440	1,319	7,599	14,358	8,793
Dues and subscriptions	1,795	8,787	-	-	-	10,582	7,498	1,612	19,692	14,141
Duplicating and printing	1,676	5,128	4,281	1,234	-	12,320	18,814	83,997	114,831	127,578
Equipment repairs and maintenance	2,259	11,061	4,948	-	-	18,269	644	815	19,929	56,679
Freight and processing charges	127,139	624,588	108,307	56,277	129,220	1,045,530	-	-	1,045,530	594,204
Grants and stipends	119,000	226,618	5,541,731	3,764,765	590,041	10,242,155	-	-	10,242,155	3,389,746
Insurance	4,752	23,267	-	-	-	28,019	8,411	811	37,241	32,608
Interest	12,590	61,646	-	-	-	74,236	6,650	2,221	83,106	83,127
Meetings, Conferences, Special Events	3,911	7,001	155	9,234	-	20,300	6,419	95,542	122,262	242,851
Miscellaneous	-	-	-	-	-	288	288	-	288	245
Outside Computer Services	44	217	-	-	-	261	102	15,561	15,924	-
Postage and mailing services	1,983	10,401	576	72	3,085	16,117	1,920	77,134	95,171	29,165
Procurement	95,952	332,552	1,329,279	68,873	60,327	1,886,983	-	1,886,983	380,236	380,236
Supplies	7,616	36,535	383	-	-	44,534	10,433	16,231	71,199	53,781
Taxes, licenses and fees	106	719	-	-	-	825	3,135	4	3,965	15,829
Travel and auto expenses	15,091	76,297	38,694	10,031	22,906	163,019	22,997	51,086	237,103	102,741
Utilities and telephone	8,423	41,243	6,003	130	151	55,950	6,292	2,278	64,520	43,966
Warehouse operations	19,242	94,214	115,652	-	-	229,107	6,670	1,154	236,932	8,166
Total expenses before depreciation	1,894,281	146,101,111	22,634,864	30,323,608	7,648,050	208,601,914	980,663	676,890	210,259,467	127,721,420
Depreciation and amortization	19,498	95,467	-	-	-	114,965	17,430	4,065	136,461	112,361
Total functional expenses	\$ 1,913,779	\$ 146,196,578	\$ 22,634,864	\$ 30,323,608	\$ 7,648,050	\$ 208,716,879	\$ 998,093	\$ 680,955	\$ 210,395,928	\$ 127,833,781

See notes to financial statements.

**DIRECT RELIEF INTERNATIONAL
(A NON-PROFIT CORPORATION)
STATEMENTS OF CASH FLOWS
FOR THE YEAR ENDED MARCH 31, 2006**

WITH COMPARATIVE TOTALS FOR THE YEAR ENDED MARCH 31, 2005

	<u>Total All Funds March 31, 2006</u>	<u>Total All Funds March 31, 2005</u>
Cash flows from operating activities:		
(Decrease) Increase in net assets	\$ (72,921,217)	\$ 93,511,654
Adjustments to reconcile changes in net assets to net cash (used by) provided by operating activities:		
Increase in inventory	71,235,278	(79,855,228)
Depreciation and amortization	136,461	110,419
Loss on fixed assets disposed of	31,614	-
Realized gain on sale of investments	51,632	(43,534)
Unrealized gain on investments	(600,493)	(338,548)
Changes in operating assets and liabilities:		
Contributions receivable	156,886	(256,236)
Prepaid expenses	(43,118)	1,406
Accounts payable	(233,307)	238,650
Accrued expenses	109,839	35,665
Other liabilities	(15,381)	38,395
Net cash (used by) provided by operating activities	<u>(2,091,806)</u>	<u>13,442,643</u>
Cash flows from investing activities:		
Purchases of property and equipment	(668,355)	(214,687)
Proceeds from sale of property and equipment	9,500	-
Proceeds from the sale of real estate	-	600,000
Proceeds from sales and maturities of investments	914,212	436,541
Purchases of investments	(3,128,399)	(1,984,371)
Investment in split interest agreements	29,734	(32,471)
Fund held in trust by others	-	-
Distribution payable	1,421	-
Net cash used by investing activities	<u>(2,841,887)</u>	<u>(1,194,989)</u>
Cash flows from financing activities:		
Principal reduction on first and second trust deeds	(49,242)	(46,793)
Line of credit	(1,358)	1,358
Capital Lease Obligation	20,990	-
Net cash used by financing activities	<u>(29,611)</u>	<u>(45,435)</u>
 Net (decrease) increase in cash and cash equivalents	 (4,963,303)	 12,202,219
Cash and cash equivalents - beginning of period	<u>12,836,987</u>	<u>634,768</u>
Cash and cash equivalents - end of period	<u><u>\$ 7,873,684</u></u>	<u><u>\$ 12,836,987</u></u>
 Supplemental disclosures of cash flow information:		
Cash paid during the year for interest	\$ 80,660	\$ 83,127

See notes to financial statements

Note 1: Summary of Significant Accounting Policies

Organization and basis of presentation:

Direct Relief International (the Organization), a California non-profit public benefit corporation, was founded in 1948.

The Organization's program services consist of providing essential pharmaceuticals, medical supplies and medical equipment on a humanitarian basis to support health services in developing countries worldwide. In the United States, the Organization conducts programs to improve the oral health of low-income children and enhance disaster preparedness in local communities. It also furnishes medicines and supplies through California free and community health clinics to serve low-income, medically uninsured patients. Under agreements with local emergency response authorities, the Organization's medical inventories are available on an as-needed basis in the event of a health emergency.

The medical material resources provided as part of the Organization's assistance program are either purchased or received by donation from pharmaceutical and medical supplies manufacturers, wholesalers, and other organizations involved in the health care industry.

Revenues, expenses, gains, and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, the net assets of the Organization and changes therein are classified and reported as follows:

Unrestricted net assets — Net assets that are not subject to any donor-imposed restrictions.

Temporarily restricted net assets — Net assets subject to donor-imposed restrictions on their use that may be met either by actions of the Organization or the passage of time.

Permanently restricted net assets — Net assets subject to donor-imposed or other legal restrictions requiring that the principal be maintained permanently by the Organization.

To present comparative financial statements, the Organization has included summarized comparative information for the year ended March 31, 2005.

Use of estimates:

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

Cash equivalents:

The Organization considers all highly liquid investments purchased with an average maturity of three months or less to be cash equivalents. Cash equivalents, consisting of money market mutual funds and checking account balances, were valued at \$7.874 million and \$12.837 million as of March 31, 2006 and March 31, 2005, respectively.

Fair Values of Financial Instruments:

Various methods and assumptions were used to estimate the fair value of each class of financial instruments. Cash and cash equivalents are valued at their carrying amount due to their short maturities. Investments are reported at fair value based on quoted market prices or, in the case of alternative investments, at values provided by the fund managers or general partners based on quoted market prices, if available, or other valuation methods.

The estimated fair values of the Organization's financial instruments were as follows at March 31, 2006 and March 31, 2005 (in thousands):

	2006		2005	
	Carrying amount	Fair value	Carrying amount	Fair value
Assets				
Cash and cash equivalents	\$ 7,874	\$ 7,874	\$ 12,837	\$ 12,837
Investments				
Current	-	-	-	-
Non current	9,360	9,360	6,597	6,597
Liabilities				
Current debt	52	52	49	49
Non current debt	1,467	1,467	1,519	1,519

The carrying value of all other financial instruments approximates fair value.

Investments:

Investments are reported at fair value. The separately managed Board Restricted Investment Fund accumulates portfolio income and realized gains and losses on security transactions which are available to meet current expenses to the extent approved by the Board of Directors. Amounts annually available for expenditure are based on the Board of Directors approved distribution rate, currently five percent (5%) of Fund's portfolio assets.

Inventory:

Purchased inventory is carried at cost. Donated inventory is carried at estimated wholesale value as of the date of receipt. Inventory balances as of March 31, 2006 were composed of the following (in thousands):

		<u>2006</u>
Pharmaceuticals	\$	18,870
Medical supplies		4,726
Equipment		<u>614</u>
Total inventory	\$	<u>24,210</u>

Land, buildings and other property:

Property and equipment purchased are recorded at cost. Donated assets are capitalized at the estimated fair value on date of receipt. Depreciation is computed using the straight-line method over the estimated useful lives of the assets as follows:

<u>Class of property</u>	<u>Estimated useful life</u>
Buildings	40
Building improvements	20-40
Equipment and software	3-10

Revenue recognition:

Contributions, which include unconditional promises to give (pledges), are recognized as revenues in the period received or promised. Conditional contributions are recorded when the conditions have been met. Contributions are considered to be unrestricted unless specifically restricted by the donor.

The Organization reports contributions in the temporarily or permanently restricted net asset class if they are received with donor-imposed restrictions as to their use. When the restriction expires - the time restriction ends or purpose restriction is accomplished - temporarily restricted net assets are released and reclassified to unrestricted net assets in the statement of activities. Donor-restricted contributions are initially reported in the temporarily restricted net asset class, even if it is anticipated such restrictions will be met in the current reporting period.

Program service revenues are generally recognized upon delivery of the product or service to the customer.

Contributed materials and services:

Contributions of pharmaceutical and medical supplies are recorded at estimated wholesale value on the date received, based on published wholesale price indexes for pharmaceuticals and medical supplies. Contributions of medical equipment are recorded at estimated wholesale value based upon wholesale price guides or, when necessary, judgmentally determined.

Donated shipping is valued at full published rates in effect at the time of shipment. Contributed services are reported at fair value in the financial statements for voluntary donations of services when those services (1) create or enhance non-financial assets or (2) require

specialized skills provided by individuals possessing those skills and are services which would be typically purchased if not provided by donation.

The Organization recorded the following revenues for the years ended March 31, 2006 and March 31, 2005 (in thousands):

	<u>2006</u>	<u>2005</u>
Donated pharmaceuticals, supplies, and equipment	\$ 120,996	\$ 199,571
Donated shipping	517	592
Contributed services	-	25
Total donated goods and services	<u>\$ 121,513</u>	<u>\$ 200,188</u>

Valuation of Future Interests

The Organization serves as trustee of a unitrust, of which it is the charitable beneficiary. The Organization is also the beneficiary of several charitable gift annuities. The future interests in the gift annuities and unitrust are recorded as assets and valued at fair value on the date of each gift. Investments in the trust and in the gift annuities are adjusted to market value at the end of each year. The present value of the total estimated future distributions to the donors on the date of each gift is recorded as a liability.

Income Taxes

The Organization is a not-for-profit organization that is exempt from income taxes under Section 501(c)(3) of the Internal Revenue Code.

Note 2: Contributions Receivable

As of March 31, 2006, and March 31, 2005, the Organization had recorded contributions receivable of \$140,834 and \$298,711, respectively. The receivables were primarily composed of mailed checks and credit card charge authorizations postmarked prior to period end but received after period end.

Note 3: Investments

The Organization has adopted SFAS No. 124, "Accounting for Certain Investments Held by Not-for-Profit Organizations". This statement requires that nonprofit organizations record investments at fair market value in the statements of financial position. Investment holdings as of March 31, 2006, and March 31, 2005 are composed of the following (in thousands):

	<u>2006</u>		<u>2005</u>	
	Cost	Market	Cost	Market
Mutual funds	\$ 6,470	\$ 7,521	\$ 4,103	\$ 5,070
Alternative investments	1,521	1,831	1,404	1,519
Other	8	8	8	8
Total Investments	<u>\$ 7,999</u>	<u>\$ 9,360</u>	<u>\$ 5,515</u>	<u>\$ 6,597</u>

Note 4: Property and Equipment

The Organization's investment in property and equipment as of March 31, 2006, and March 31, 2005, consisted of the following (in thousands):

	<u>2006</u>	<u>2005</u>
Land	\$ 1,364	\$ 1,364
Office and Warehouse	2,218	1,864
Vehicles, equipment and software	752	663
Total	<u>4,334</u>	<u>3,891</u>
Less: Accumulated Depreciation	<u>-667</u>	<u>-721</u>
Net Property and Equipment	<u>\$ 3,667</u>	<u>\$ 3,170</u>

Note 5: Debt

The Organization's long-term debt consists of the following as of March 31, 2006, and March 31, 2005 (in thousands):

	<u>2006</u>	<u>2005</u>
Mortgage note payable, requiring monthly payments of \$ 7,604 including interest at 5.50%, maturing on October 1, 2007	\$ 1,093	\$ 1,122
Mortgage note payable, requiring monthly payments of \$ 3,222 including interest at 4.50%, maturing on November 1, 2007	426	446
Total long-term debt	<u>1,519</u>	<u>1,568</u>
Less: current portion	<u>-52</u>	<u>-49</u>
Long-term portion	<u>\$ 1,467</u>	<u>\$ 1,519</u>

The mortgage notes are secured by the Organization's warehouse facility. The following is a summary of principal maturities of long-term debt during the next five fiscal years (in thousands):

2007	52
2008	<u>1,467</u>
Total	<u>\$ 1,519</u>

Note 6: Net Assets

Unrestricted net assets consisted of the following at March 31, 2006, and March 31, 2005 (in thousands):

	<u>2006</u>	<u>2005</u>
Designated by the Board of Directors for:		
Operating reserves	\$ 9,448	\$ 7,359
Undesignated	<u>27,884</u>	<u>99,458</u>
Total unrestricted net assets	<u>\$ 37,332</u>	<u>\$ 106,817</u>

Temporarily restricted net assets are available for the following purposes at March 31, 2006 and March 31, 2005 (in thousands):

	<u>2006</u>	<u>2005</u>
Tsunami recovery efforts	\$ 3,738	\$ 9,292
Hurricane Katrina recovery efforts	838	-
Pakistan earthquake recovery efforts	748	-
Local health initiatives and programs	275	33
Country-specific assistance shipments	250	53
Bolivian rural health clinic	-	48
Caribbean hurricane recovery efforts	-	42
Capital expenditures	165	-
Other activities	<u>39</u>	<u>36</u>
Total temporarily restricted net assets	<u>\$ 6,053</u>	<u>\$ 9,504</u>

Permanently restricted net assets consisted of endowed contributions, the income from which is available to fund the following at March 31, 2006 and March 31, 2005 (in thousands):

	<u>2006</u>	<u>2005</u>
General operations	\$ 25	\$ 10
Specific purposes	<u>-</u>	<u>-</u>
Total unrestricted net assets	<u>\$ 25</u>	<u>\$ 10</u>

Donor-restricted endowment gifts shall be invested and accounted for according to the terms of the specific gift(s) and/or the provisions of California Probate Code sections 18500-18509 (Uniform Management of Institutional Funds Act).

Note 7: Board Restricted Investment Fund

In 1998, the Organization established a board-designated investment fund (formerly known as the "Quasi-Endowment Fund"). The purpose of the fund was to provide a reserve for future operations. The Fund's resources come from board-designated unrestricted bequests and gifts,

return on the Fund's portfolio assets and operating surpluses (measured annually) in excess of current operational needs.

The Fund is currently authorized to distribute up to five percent (5%) of the average market value (measured January 1 for the three preceding years) of the Fund's portfolio assets to support general operations. Distributions in excess of five (5%) require a 75% vote of the Board of Directors. No distributions were made during the twelve month period ending March 31, 2006, and a distribution of \$283,000 was made in the twelve month period ending March 31, 2005. The previous distribution policy, which called for distributions of up to six (6%) percent of the Fund's portfolio assets, measured at the beginning of the current fiscal year, was changed in September 2004.

For the years ended March 31, 2006 and March 31, 2005, the fund received support and revenues consisting of the following (in thousands):

	<u>2006</u>	<u>2005</u>
Board designated bequests and donations	\$ 250	\$ 2,095
Dividends and interest	616	109
Funds transferred in/(out)	678	(283)
Realized gains	57	61
Unrealized gains	588	339
Change in value – split interest agreements	<u>2</u>	<u>26</u>
Total	\$ <u>2,191</u>	\$ <u>2,347</u>

The Fund incurred expenses of \$10,880 and \$6,850, respectively, during the years ended March 31, 2006 and March 31, 2005.

Note 8: Pension Expense

The Organization established the Direct Relief International 401(k) Plan (the Plan) on January 1, 2004. Employees of the Organization are eligible to participate upon hire and are vested 100% percent in all contributions to the Plan. The Organization matches every dollar contributed, up to five (5) percent of the employee's annual compensation, subject to Board approval.

Prior to 2004, the Organization maintained a tax deferred annuity plan established under Internal Revenue Code section 403(b).

The Organizations contributions to the various pension plans amounted to \$60,165 and \$52,272, respectively, for the years ended March 31, 2006 and March 31, 2005.

Note 9: Non-Qualified Deferred Compensation Agreement

The Organization is party to a non-qualified deferred compensation agreement with the surviving spouse of a co-founder of the Organization. Under the terms of the agreement, beginning January 1, 1971, the Organization is obligated to make monthly payments in acknowledgement of his 23 years of service. The retirement agreement expense for the years ended March 31, 2006, and March 31, 2005, was \$9,920 and \$10,020, respectively.

Note 10: Concentrations of Credit Risk

Financial instruments that potentially subject the Organization to concentrations of credit risk consist principally of bank and brokerage deposits. The Organization places its temporary cash investments with financial institutions and brokerages. For the year ended March 31, 2006, the Organization was at risk for \$4,356,174 in cash deposited at individual financial institutions. The Federal Deposit Insurance Corporation (FDIC) insures individual deposits up to \$ 100,000. In addition, the Organization's investments are exposed to various risks, such as interest rate fluctuations and market valuations. Due to the level of risk associated with certain investment securities and the level of uncertainty related to changes in the value of investment securities, it is at least reasonably possible that changes in risks in the near term could materially affect the Organization's statement of financial position and the statement of activities.

Note 11: Operating Lease

On July 21, 2005, in response to a significant increase in product donations, the Organization signed a sublease to acquire an additional 23,000 square feet of storage space. The terms of the lease call for an initial monthly base rent of \$23,043, with a provision for periodic index-based adjustments. The lease term is twenty nine months, beginning August 1, 2005 and ending December 31, 2007. Total monthly base rents due during the term of the lease are \$668,247.

Note 12: Functional Allocation of Expenses

The costs of providing the various programs and other activities have been summarized on a functional basis in the statement of functional expenses. Accordingly, certain costs have been allocated among the program and supporting services benefited. The allocation of the costs is based upon hours spent or square footage occupied.