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The William and Flora Hewlett Foundation

Financial Statements
December 31, 2007 and 2006

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Report of Independent Auditors

To The Board of Directors of
The William and Flora Hewlett Foundation:

In our opinion, the accompanying statement of financial position and the related statements of activities, changes in net assets and cash flows present fairly, in all material respects, the financial position of The William and Flora Hewlett Foundation (the "Foundation") at December 31, 2007 and 2006, and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Foundation’s management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audit of these statements 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 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, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

PricewaterhouseCoopers LLP

March 7, 2008

The William and Flora Hewlett Foundation
Statements of Financial Position
December 31, 2007 and 2006
(dollars in thousands)

	December 31, 2007	December 31, 2006
Assets		
Cash	$ 5,820	$ 4,478
Investments, at fair value (Note 3)	9,195,759	8,268,826
Collateral under securities lending agreement	22,721	179,346
Prepaid expenses and other assets	2,496	4,456
Receivables (Note 4)	25,660	30,086
Fixed assets, net of accumulated depreciation and amortization	32,461	33,573
	$ 9,284,917	$ 8,520,765
Liabilities and Net Assets		
Accounts payable and accrued liabilities	$ 30,925	$ 15,967
Line of credit	90,000	-
Accrued post-retirement health care benefit	3,135	3,620
Payable under securities lending agreement	22,721	179,346
Federal excise tax payable currently	795	1,334
Deferred federal excise tax	20,643	17,596
Grants payable (Note 7)	242,786	193,727
Gift payable, net of discount (Note 8)	86,221	88,476
Total liabilities	497,226	500,066
Commitments (Note 3)		
Unrestricted net assets	8,759,347	7,980,613
Temporarily restricted net assets	28,344	40,086
Total net assets	8,787,691	8,020,699
	$ 9,284,917	$ 8,520,765

See accompanying notes to the financial statements.

The William and Flora Hewlett Foundation
Statements of Activities and Changes in Net Assets
December 31, 2007 and 2006
(dollars in thousands)

	Year Ended December 31, 2007	2006
Unrestricted Net Assets:		
Net investment revenues and gains:		
Interest, dividends and other	$ 198,893	$ 163,619
Gain on investment portfolio	1,131,314	1,291,749
Investment management expense	(27,977)	(31,019)
Net investment income	1,302,230	1,424,349
Tax expense on net investment income (Note 10)	(28,497)	(27,547)
Net investment revenues	1,273,733	1,396,802
Expenses:		
Grants and gift awarded, net of cancellations	(482,778)	(287,087)
Change in gift discount (Note 8)	9,779	(5,108)
Direct and other charitable activities	(12,346)	(6,118)
Administrative expenses	(21,799)	(18,970)
Total expenses	(507,144)	(317,283)
Income over expenses before net assets released from time restriction	766,589	1,079,519
Net assets released from time restriction	12,145	41
Change in unrestricted net assets	778,734	1,079,560
Temporarily Restricted Net Assets:		
Change in temporarily restricted net assets:		
Change in value	403	10
Gates Foundation contribution	-	40,000
Net assets released from time restriction	(12,145)	(41)
Net change in temporarily restricted net assets	(11,742)	39,969
Change in total net assets	766,992	1,119,529
Net assets at beginning of year	8,020,699	6,901,170
Net assets at end of year	$ 8,787,691	$ 8,020,699

See accompanying notes to the financial statements.

The William and Flora Hewlett Foundation
Statements of Cash Flows
December 31, 2007 and 2006
(dollars in thousands)

	Year Ended December 31, 2007	2006
Cash flows used in operating activities:		
Interest and dividends received	$ 194,825	$ 162,450
Cash paid for federal excise tax	(8,439)	(12,951)
Cash paid to suppliers and employees	(43,926)	(51,258)
Cash contributions (paid) received	(12,145)	10,041
Grants and gifts paid	(426,195)	(209,942)
Net cash used in operating activities	(295,880)	(101,660)
Cash flows from investing activities:		
Purchases of fixed assets	(1,176)	(194)
Proceeds from sale of fixed assets	-	2
Cash received from partnership distributions	413,735	409,797
Proceeds from sale of investments	23,632,749	20,023,221
Purchase of investments	(23,838,086)	(20,331,394)
Net cash from investing activities	207,222	101,432
Cash flows from financing activities:		
Cash received from line of credit	90,000	-
Net cash from financing activities	90,000	-
Net increase (decrease) in cash	1,342	(228)
Cash at beginning of year	4,478	4,706
Cash at end of year	$ 5,820	$ 4,478

See accompanying notes to the financial statements.

The William and Flora Hewlett Foundation
Statements of Cash Flows, continued
December 31, 2007 and 2006
(dollars in thousands)

	Year Ended December 31, 2007	2006
Reconciliation of change in net assets to net cash used in operating activities:		
Change in total net assets	$ 766,992	$ 1,119,529
Adjustments to reconcile change in net assets to net cash used in operating activities:		
Depreciation and amortization on fixed assets	1,763	1,734
Loss on disposal of fixed assets	525	-
Loss on sale of fixed assets	-	1
Change in value on gift payable	(9,779)	5,108
Net unrealized and realized gain on investments	(1,131,314)	(1,291,749)
Increase in deferred federal excise tax	3,047	7,820
(Decrease) increase in accrued post-retirement health care benefit	(485)	408
Decrease (increase) in value of Trust receivable	38	(10)
Changes in operating assets and liabilities:		
(Increase) in interest and dividends receivable	(4,055)	(1,152)
(Decrease) increase in federal excise tax	(539)	4,533
Decrease in prepaid expenses and other assets	1,960	303
Decrease (increase) in Gates and other receivable	4,426	(29,959)
Increase in accounts payable and accrued liabilities	14,958	4,629
Increase in grants payable	49,059	77,145
Increase in gift payable	7,524	-
Net cash used in operating activities	$ (295,880)	$ (101,660)

	2007	2006
Supplemental data for non-cash activities:		
Stock contributions received from Hewlett Trust	$ -	$ 1

See accompanying notes to the financial statements.

1. The Organization

The William and Flora Hewlett Foundation (the "Foundation") is a private foundation incorporated in 1966 as a non-profit charitable organization. The Foundation's grantmaking activities are concentrated in the program areas of education, environment, performing arts, population and global development. More detailed information regarding the Foundation's charitable activities can be obtained from the Foundation's website at www.hewlett.org.

2. Significant Accounting Policies

Basis of presentation

The accompanying financial statements have been prepared on the accrual basis of accounting.

Investments

Investments in stocks and bonds which are listed on national securities exchanges, quoted on NASDAQ or on the over-the-counter market are valued at the last reported sale price, or in the absence of a recorded sale, at the value between the most recent bid and asked prices. Futures, forwards, swaps and options which are traded on exchanges are valued at the last reported sale price or, if they are traded over-the-counter, at the most recent bid price. Index and credit swaps, which gain exposure to equities and fixed income securities in a leveraged form, are traded with a counterparty and are valued at each month end. Equity swaps are valued based on the last reported price of the relevant index or ETF. Fixed income swaps are valued at the last reported sale price, or in the absence of a recorded sale, at the value between the most recent bid and asked prices. Short-term investments are valued at amortized cost, which approximates market value. Since there is no readily available market for investments in limited partnerships, such investments are valued at amounts reported to the Foundation by the general partners of such entities. The investments of these limited partnerships, such as venture capital, buyout firms and real estate partnerships, include securities of companies that may not be immediately liquid. Accordingly, their values are based upon guidelines established by the general partners. The December 31 valuation of certain of the investments in limited partnerships are based upon the value determined by each partnership's general partner as of September 30 and adjusted for cash flows that occurred during the quarter ended December 31. Management believes this method provides a reasonable estimate of fair value. These values may differ significantly from values that would have been used had a readily available market existed for such investments, and the differences could be material to the change in net assets of the Foundation.

Investment transactions are recorded on trade date. Realized gains and losses on sales of investments are determined on the specific identification basis.

Foreign currency amounts are translated into U.S. dollars based upon exchange rates as of December 31. Transactions in foreign currencies are translated into U.S. dollars at the exchange rate prevailing on the transaction date.

Cash equivalents consist of money market mutual funds and foreign currency held for investment purposes.

Cash

Cash consists of funds held in commercial interest-bearing accounts, for operating expenses.

Fixed Assets

Fixed assets are recorded at cost and depreciated using the straight-line basis over their estimated useful lives. The headquarters building and associated fixtures are generally depreciated using the straight-line basis over ten to fifty years. Furniture and computer and office equipment are depreciated over estimated useful lives of three to ten years.

Net Asset Classification

The Foundation's activities and related assets and liabilities are classified as unrestricted and temporarily restricted according to the terms of the various contributions. The Foundation has no permanently restricted net assets.

Unrestricted balances consist of funds undesignated and currently available for all Foundation activities. Temporarily restricted balances consist of funds available for support of the Foundation’s activities, which are expendable only for purposes specified by the donor or within a specified period.

The net assets included in the temporarily restricted class at December 31, 2007 relate to a donor-restricted contribution for which the requirements have not yet been met.

Grants

Grants are accrued when awarded by the Foundation.

Administrative Expenses

Administrative expenses represent those expenses incurred in managing programs funded by the William and Flora Hewlett Foundation. Expenses associated with managing programs funded by other organizations are reimbursed at the time they are incurred.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements. Estimates also affect the reported amounts of changes in net assets during the reporting period. Actual results could differ from those estimates.

Reclassifications

Certain reclassifications have been made to the 2006 balances to conform to the 2007 presentation of tax expenses. In 2007, the Foundation further clarified its tax expense categories. These reclassifications had no effect on the change in net assets in 2006 or total net assets at December 31, 2006.

(dollars in thousands)

3. Investments

The Foundation's investment portfolio, at December 31 consists of the following:

	2007	2006
Investments, at fair value		
Hewlett-Packard and Agilent common stock	$ 445,565	$ 465,334
Global equities	3,550,037	3,560,392
Private equities, real assets and absolute return	3,101,210	2,199,475
Fixed income	3,191,410	2,557,830
Net payable on forward fixed income transactions	(1,093,621)	(849,271)
Cash equivalents	141,882	331,399
Net (payable) receivable from unsettled securities purchases and sales	(165,183)	2,960
Other	24,459	707
Total	$ 9,195,759	$ 8,268,826

The investment goal of the Foundation is to maintain or grow its asset size and spending power in real (inflation adjusted) terms with risk at a level appropriate to the Foundation's program objectives. The Foundation diversifies its investments among various financial instruments and asset categories, and uses multiple investment strategies. As a general practice, except for the Foundation's holdings in Hewlett-Packard and Agilent stock and certain index swaps, all financial assets of the Foundation are managed by external investment management firms selected by the Foundation. All financial assets of the Foundation are held in custody by a major commercial bank, except for assets invested with partnerships, commingled funds, the overlay swaps and the covered call program, which have separate arrangements related to their legal structure.

The majority of the Foundation's assets are invested in equities, which are listed on national exchanges, quoted on NASDAQ, or in the over-the-counter market; treasury and agency bonds of the U.S. government; and investment grade corporate bonds for which active trading markets exist. Net realized and unrealized gains and losses on investments are reflected in the Statements of Activities and Changes in Net Assets.

Global equities include those held directly by the Foundation and those held in commingled entities including partnerships and trusts. At December 31, 2007 and 2006, global equities held in partnerships and trusts were $1,448,262 and $1,183,621.

The gain on the Foundation's investment portfolio for the years ended December 31, 2007 and 2006 consists of the following:

(dollars in thousands)

	2007	2006
Net realized gain	$ 669,230	$ 797,387
Net unrealized gain	462,084	494,362
	$1,131,314	$1,291,749

Approximately 34 percent of the Foundation's investments at December 31, 2007 were invested with various limited partnerships that invest in the securities of companies that are not immediately liquid, such as venture capital and buyout firms, and in real estate limited partnerships or private REITs that have investments in various types of properties. As of December 31, 2007 the Foundation is committed to contribute approximately $2,036,226 in additional capital in future years to various partnerships.

Investment securities are exposed to various risks, such as changes in interest rates or credit ratings and market fluctuations. 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 possible that the value of the Foundation's investments and total net assets balance could fluctuate materially.

The investments of the Foundation include a variety of financial instruments involving contractual commitments for future settlements, including futures, swaps, forwards and options which are exchange traded or are executed over-the-counter. Some investment managers retained by the Foundation have been authorized to use certain financial derivative instruments in a manner set forth by either the Foundation's written investment policy, specific manager guidelines or partnership/fund agreement documents. Specifically, financial derivative instruments may be used for the following purposes: (1) currency forward contracts and options may be used to hedge nondollar exposure in foreign investments, or to take positions in managed currency portfolios; (2) futures and swap contracts may be used to rebalance asset categories within the portfolio or to manage market exposures in managed portfolios; and (3) futures contracts, swaps and options may be used to hedge or leverage positions in managed portfolios. Financial derivative instruments are recorded at fair value in the Statements of Financial Position with changes in fair value reflected in the Statements of Activities and Changes in Net Assets.

The total value of investments pledged with respect to options and futures contracts at December 31, 2007 and 2006 was $14,884 and $8,391 respectively. The value of restricted cash held at brokers as collateral for variation margin at December 31, 2007 and 2006 was $10,941 and $10,099 respectively.

Certain of the Foundation's managers purchase or sell fixed income securities on a delayed delivery or forward settled basis. These transactions involve a commitment by the Foundation to purchase or sell securities for a predetermined price or yield, with payment and delivery taking place beyond the customary settlement period, from about 1 to 3 months. When purchasing a security on a delayed delivery basis, the Foundation assumes the rights and risks of ownership of the security, including the risk of price and yield fluctuations, and reflects such fluctuations in its net assets. The manager may dispose of or renegotiate a delayed delivery transaction after it is entered into, and may sell the securities before they are delivered, which may result in a capital gain or loss. At December 31, 2007 and 2006 the net liability for these forward purchases and sales was $1,093,621 and $849,271 respectively.

Premiums received with respect to open options contracts at December 31, 2007 and 2006 were $5,908 and $1,631, respectively.

Other investment assets of $24,459 and $707 at December 31, 2007 and 2006, respectively, consist of receivables for interest and dividends and certain derivatives held at fair market value. At December 31, 2007 and 2006 these derivatives included swap contracts, futures contracts, foreign exchange contracts, covered call options and put and call options, as shown in the table on the following page.

In the opinion of the Foundation’s management, the use of financial derivative instruments in its investment program is appropriate and customary for the investment strategies employed. Using those instruments reduces certain investment risks and may add value to the portfolio. The instruments themselves, however, do involve investment and counterparty risk in amounts greater than what are reflected in the Foundation’s financial statements. Management does not anticipate that losses, if any, from such instruments would materially affect the financial position of the Foundation.

Fair values of the Foundation’s derivative financial instruments at December 31, 2007 and 2006 are summarized in the following table. This table excludes exposures relating to derivatives held indirectly through commingled funds.

Derivative Financial Instruments	December 31 2007 Fair Value (in thousands)	December 31 2006 Fair Value (in thousands)
- Equity contracts:		
Futures and swap contracts		
Assets	$ 190	$ 4,896
Put and call options:		
Assets / (Liabilities)	$ 698	$ (40)
Covered call options:		
Liabilities	$ (1,145)	$ (1,477)
- Fixed income contracts:		
Futures and swap contracts		
Assets / (Liabilities)	$ (6,723)	$ 371
Put and call options:		
Liabilities	$ (667)	$ (738)
Forward net purchases and sales		
Liabilities	$ (1,093,621)	$ (849,271)
- Foreign currency contracts:		
Forward contracts		
Unrealized gain on currency contracts	$ 40,100	$ 19,537
Unrealized loss on currency contracts	$ (23,618)	$ (31,890)

The Foundation's custodian maintains a securities lending program on behalf of the Foundation, and maintains collateral at all times in excess of the value of the securities on loan. Investment of this collateral is in accordance with specified guidelines; these investments include A1-rated commercial paper, repurchase agreements, asset backed securities, certificates of deposit and floating rate notes. Income earned on these transactions is included in net investment revenue in the Statements of Activities and Changes in Net Assets. The value of securities on loan at December 31, 2007 and 2006 was $21,430 and $171,038 respectively. The value of the collateral received at December 31, 2007 and 2006 aggregated $22,721 and $179,346 respectively, of which $22,721 and $179,346 respectively, was received in cash and was invested in accordance with the investment guidelines.

At December 31, 2007, the net receivable from unsettled securities purchases and sales includes a receivable from brokers of $462,826 and a payable to brokers of $628,009. At December 31, 2006, the net receivable from unsettled securities purchases and sales included a receivable from brokers of $177,984 and a payable to brokers of $175,024.

The Foundation held 5.3 million shares of Hewlett-Packard Company ("Hewlett-Packard") stock with a market price of $50.48 per share at December 31, 2007. At December 31, 2006, the

(dollars in thousands)

Foundation held 7.1 million shares with a market price of $41.19 per share. The Foundation held 4.8 million shares of Agilent Company ("Agilent") stock with a market price of $36.74 per share at December 31, 2007. At December 31, 2006, the Foundation held 4.8 million shares of Agilent stock with a market price of $34.85. At December 31, 2006, the Foundation held 98 thousand shares of Verigy with a market price of $17.75 per share; Verigy was a 2006 spin-off from Agilent. During 2007, all Verigy shares were sold.

4. Receivables

In 2006 the Foundation entered into an agreement with the Bill and Melinda Gates Foundation to administer a program charged with improving quality education in developing countries. In addition to reimbursing associated administrative expenses, the Bill and Melinda Gates Foundation pledged $40,000 over five years to the William and Flora Hewlett Foundation to do grant-making in this area; this contribution was reported as a change in temporarily restricted net assets during 2006. $10,000 of this pledge was received during 2006, and $4,340 was received during 2007. $25,660 is reported as a receivable at December 31, 2007.

Upon the death of William R. Hewlett on January 12, 2001, the Foundation became the residuary beneficiary of the William R. Hewlett Revocable Trust ("the Trust") and was entitled to receive the trust assets remaining after payment of expenses of administration and federal and state estate taxes. The Trust was fully distributed during 2007. The receivable from the Trust was $86 at December 31, 2006. During 2007, the Trust incurred expenses of $38, and the final distribution from the Trust was $48 of cash.

The Foundation is also the residuary beneficiary of the Hewlett Marital Trust. As of December 31, 2007, the assets which the Foundation is entitled to receive are not material and cannot be reasonably estimated.

5. Fixed Assets

Fixed assets consist of the following at December 31, 2007 and 2006:

	2007	2006
Building, land lease and land improvements	$ 34,277	$ 34,013
Furniture and fixtures	4,654	4,793
Computer and office equipment	3,274	3,346
	42,205	42,151
Less accumulated depreciation and amortization	(9,744)	(8,578)
	$ 32,461	$ 33,573

(dollars in thousands)

6. Postretirement Healthcare Benefit

The Foundation implemented Statement of Financial Accounting Standards (SFAS) No. 106, "Employers' Accounting for Postretirement Benefits Other Than Pensions" effective January 1, 2004. Effective January 1, 2007 the Foundation adopted Statement No. 158 of the Financial Accounting Standards Board, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans" and recognizes the accumulated liability for its postretirement healthcare benefit obligation.

The incremental effect of adopting SFAS 158 is as follows:

	Before Application	SFAS 158 Adjustment	After Application
Consolidated financial statements:			
Accrued post retirement benefit costs	$ 4,194	$ (1,059)	$ 3,135
Total liabilities	4,194	(1,059)	3,135
Total net assets	0	0	0
Change in net assets		1,059	1,059
Cumulative effect of change in accounting principle:			
Unrecognized net actuarial gain		(1,059)	(1,059)
Unrecognized prior service cost		0	0
	$ 0	$ (1,059)	$ (1,059)

The changes in accumulated postretirement healthcare benefit obligation, plan assets, and the amounts recognized in the financial statements are as follows:

	2007	2006
Change in accumulated postretirement healthcare benefit obligation (APBO):		
Accumulated postretirement benefit obligation as of January 1	$ 2,928	$ 2,552
Service cost	465	358
Interest cost	192	158
Actuarial gain	(423)	(101)
Benefits paid by employer	(27)	(39)
Accumulated postretirement benefit obligation as of December 31	3,135	2,928
Unrecognized: Net gain	0	693
Accrued postretirement benefit cost as of December 31	$ 3,135	$ 3,620

By Foundation policy, the postretirement healthcare benefit plan is not funded.

(dollars in thousands)

	2007	2006
Change in plan assets:		
Fair value of plan assets as of January 1	$ 0	$ 0
Actual return on plan assets		
Company contributions	27	39
Participants contributions		
Benefits paid	(27)	(39)
Fair value of plan assets, December 31	$ 0	$ 0

Amount recognized in Statement of Financial Position as of December 31:		
Accrued postretirement healthcare benefit cost as of December 31	$ 3,135	$ 3,620
Assets	0	0
Net amount recognized	$ 3,135	$ 3,620

Amounts included in unrestricted net assets:		
Unrecognized prior service cost	$ 0	$ 0
Unrecognized net gain	(1,059)	(693)
Net gain included in unrestricted net assets	$ (1,059)	$ (693)

Net periodic postretirement healthcare benefit cost:		
Service cost	$ 465	$ 358
Interest cost	192	158
Expected return on plan assets		
Amortization of prior service cost		
Amortization of unrecognized net gain	(57)	(70)
Net periodic postretirement healthcare benefit cost:	$ 600	$ 446

(dollars in thousands)

The prior service cost and net actuarial gain expected to be amortized from change in net assets to net periodic benefit expense over the next fiscal year are as follows:

Net actuarial gain	$ (93)
Prior service cost	0

Actuarial assumptions:

The weighted average discount rate assumptions used for the postretirement healthcare benefit plan are shown below:

	2007	**2006**
Discount rate to determine benefit obligations	6.50%	5.75%
Discount rate to determine the net periodic benefit cost	5.75%	5.50%

To determine the accumulated postretirement healthcare benefit obligation as of December 31, 2007, a 12% annual rate of increase in per capita costs of covered health care was assumed for 2007-2008, declining gradually to 6% by 2013 and remaining at this rate thereafter.

Assumed health care cost trend rates have a significant effect on the amounts reported for the health care plans. Increasing the health care cost trend rate by 1% in each future year would increase the accumulated postretirement healthcare benefit obligation by $589, and the aggregate annual service and interest cost by $119. Decreasing the health care cost trend rate by 1% in each future year would decrease the accumulated postretirement healthcare benefit obligation by $408, and the aggregate annual service and interest cost by $91.

Expected contributions:

The Foundation expects to contribute $52 in postretirement healthcare benefits during the fiscal year ending December 31, 2008.

(dollars in thousands)

Expected benefit payments:

The following benefit payments, which reflect expected future service, are expected to be paid for the fiscal years ending December 31:

Fiscal Year	Expected Benefit Payments
2008	$ 52
2009	47
2010	72
2011	87
2012	144
2013-2017 (Aggregate)	1,370

7. Grants Payable

Grant requests are recorded as grants payable when they are awarded. Some of the grants are payable in installments, generally over a three-year period. Grants authorized but unpaid at December 31, 2007 are payable as follows:

Year Payable	Amount
2008	$ 167,375
2009	53,645
2010 and thereafter	21,766
	$ 242,786

8. Gift Payable

The Foundation pledged a gift of $113,000 in August of 2007 to University of California, Berkeley for a challenge grant to endow 100 faculty chairs and for support of an in-house investment organization. The gift will be paid over a period of seven years and was discounted to a net present value as of December 31, 2007 using a discount rate of 4.39 %. Payment of $17,000 was made in 2007. The final payment is expected to be made in 2013.

(dollars in thousands)

The gift payable, net of discount, at December 31, 2007 is as follows:

	2007
Gift payable	$ 96,000
Less unamortized discount	(9,779)
Gift payable, net of discount	$ 86,221

9. Credit Facility

The Foundation has a collateralized revolving line of credit ("LOC") of $90,000 with BNY Mellon Bank. This LOC note does not have an expiration date. At December 31, 2007, the Foundation had a $90,000 outstanding balance on the LOC. The interest rate on the LOC is variable and is indexed to the one month London Interbank Offered Rate ("Libor").

10. Federal Excise and Unrelated Business Income Tax

The William and Flora Hewlett Foundation is a private foundation and qualifies as a tax-exempt organization under Section 501(c)(3) of the Internal Revenue Code and corresponding California provisions. Private foundations are subject to a federal excise tax on net investment income and may reduce their federal excise tax rate from 2% to 1% by exceeding a certain payout target for the year. The Foundation qualified for the 1% tax rate in 2007. Each year, current federal excise tax is levied on interest and dividend income and net realized gains of the Foundation; net investment losses do not reduce investment income. At December 31, 2007 and 2006, deferred federal excise tax is provided at 1.33%, which is the average effective rate expected to be paid on unrealized gains on investments. The income from certain investments is subject to unrelated business income tax.

The expense for federal excise tax is as follows:

	2007	2006
Current	$ 7,900	$ 17,484
Deferred	3,047	7,820
	$ 10,947	$ 25,304

The expense for unrelated business income tax is as follows:

	2007	2006
	$ 17,555	$ 2,205