Habitat for Humanity® of the Chesapeake

HABITAT FOR HUMANITY OF THE CHESAPEAKE, INC. AND AFFILIATES

CONSOLIDATED FINANCIAL STATEMENTS
JUNE 30, 2016 AND 2015

GSG Gorfine Schiller Gardyn
Certified Public Accountants and Consultants

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INDEPENDENT AUDITORS' REPORT

To the Board of Directors
Habitat for Humanity of the Chesapeake, Inc. and Affiliates
Baltimore, Maryland

We have audited the accompanying consolidated financial statements of Habitat for Humanity of the Chesapeake, Inc. and Affiliates, which comprise the consolidated statements of financial position as of June 30, 2016 and 2015, and the related consolidated statements of activities, functional expenses and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Consolidated 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.

Auditors' 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 auditors' 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.

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Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Habitat for Humanity of the Chesapeake, Inc. and Affiliates as of June 30, 2016 and 2015, and the changes in their net assets and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note U to the financial statements, for the years ended June 30, 2016 and 2015 the entity has elected to change its method of accounting for impairment relating to inventory of homes. Our opinion is not modified with respect to this matter.

Gorfine, Schiller + Gardyn, P.A.

January 6, 2017
Owings Mills, Maryland

CONSOLIDATED FINANCIAL STATEMENTS

HABITAT FOR HUMANITY OF THE CHESAPEAKE, INC. AND AFFILIATES
CONSOLIDATED STATEMENTS OF FINANCIAL POSITION
June 30, 2016 and 2015

	2016	2015
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	$ 1,047,512	$ 801,179
Contributions receivable - current portion	714,542	670,017
Mortgages receivable - current portion	980,969	945,490
Accounts receivable	281,240	255,701
Grants receivable	428,821	655,985
Inventory of homes	4,206,771	5,080,429
ReStore inventory	53,683	43,978
Prepaid expenses	110,654	85,630
Total current assets	7,824,192	8,538,409
PROPERTY AND EQUIPMENT		
Land and buildings	625,000	1,290,106
Furniture and fixtures and equipment	88,496	88,496
Leasehold improvements	266,911	226,610
Vehicles	367,746	309,145
Computers	227,779	204,824
	1,575,932	2,119,181
Less accumulated depreciation	(640,312)	(718,093)
Net property and equipment	935,620	1,401,088
OTHER ASSETS		
Long-term contributions receivable, net	623,187	114,400
Long-term mortgages receivable, net	6,860,706	7,504,115
Leveraged mortgages receivable, net	9,252,596	8,970,299
Capitalized interest on leveraged mortgages	3,539,152	3,334,420
Investments in limited liability companies	13,186,106	13,067,495
Prepaid interest	306,305	343,190
Deposits	49,329	43,076
Loan fees, net of accumulated amortization	42,133	45,596
Total other assets	33,859,514	33,422,591
TOTAL ASSETS	$ 42,619,326	$ 43,362,088

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

	2016	2015
LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES		
Accounts payable and accrued expenses	$ 836,948	$ 877,857
Lines of credit and notes payable - current portion	1,116,472	1,433,373
Deferred rent	106,264	57,661
Total current liabilities	2,059,684	2,368,891
LONG-TERM LIABILITIES		
Notes payable, related parties	14,846,758	14,846,758
Lines of credit and notes payable - net of current portion	5,005,963	5,667,216
Program debt	218,282	643,189
Leveraged mortgages receivable liability	9,252,596	8,970,299
Total long-term liabilities	29,323,599	30,127,462
Total liabilities	31,383,283	32,496,353
NET ASSETS		
Unrestricted	10,219,431	10,514,811
Temporarily restricted	1,016,612	350,924
Total net assets	11,236,043	10,865,735
TOTAL LIABILITIES AND NET ASSETS	$ 42,619,326	$ 43,362,088

HABITAT FOR HUMANITY OF THE CHESAPEAKE, INC. AND AFFILIATES
CONSOLIDATED STATEMENTS OF ACTIVITIES
For the Years Ended June 30, 2016 and 2015

	2016			2015		
	Unrestricted	Temporarily Restricted	Total	Unrestricted	Temporarily Restricted	Total
REVENUES, GAINS AND SUPPORT						
Contributions	$ 3,189,761	$ 1,032,287	$ 4,222,048	$ 3,205,419	$ 411,132	$ 3,616,551
Donated goods and services	236,477	-	236,477	150,267	-	150,267
Donated property	44,500	-	44,500	353,800	-	353,800
Government grants	440,163	-	440,163	435,911	-	435,911
Real estate sales	1,984,344	-	1,984,344	2,159,411	-	2,159,411
ReStore income	3,251,451	-	3,251,451	2,564,333	-	2,564,333
Special events, net of expenses of $19,157 and $-0-, respectively	1,776	-	1,776	-	-	-
Miscellaneous income	41,760	-	41,760	46,887	-	46,887
Debt forgiveness	269,864	-	269,864	256,030	-	256,030
Amortization of mortgage discounts	366,257	-	366,257	846,043	-	846,043
	9,826,353	1,032,287	10,858,640	10,018,101	411,132	10,429,233
NET ASSETS RELEASED FROM RESTRICTIONS						
Satisfaction of program restrictions	297,599	(297,599)	-	71,561	(71,561)	-
Satisfaction of time restrictions	69,000	(69,000)	-	-	-	-
	366,599	(366,599)	-	71,561	(71,561)	-
Total revenues, gains and support	10,192,952	665,688	10,858,640	10,089,662	339,571	10,429,233
EXPENSES						
Program services						
House construction	5,651,638	-	5,651,638	6,255,659	-	6,255,659
ReStore	2,907,703	-	2,907,703	2,271,504	-	2,271,504
Total program services	8,559,341	-	8,559,341	8,527,163	-	8,527,163
Supporting services						
Management and general	1,269,689	-	1,269,689	1,273,745	-	1,273,745
Fundraising	790,474	-	790,474	609,105	-	609,105
Total expenses	10,619,504	-	10,619,504	10,410,013	-	10,410,013
OPERATING INCOME (LOSS)	(426,552)	665,688	239,136	(320,351)	339,571	19,220
OTHER INCOME (EXPENSES)						
Investment income from limited liability companies	118,706	-	118,706	118,557	-	118,557
Gain on sale of property and equipment	6,942	-	6,942	-	-	-
Gain (loss) on sale of homes	5,524	-	5,524	(9,518)	-	(9,518)
Net other income (expenses)	131,172	-	131,172	109,039	-	109,039
CHANGES IN NET ASSETS BEFORE TRANSFER OF NET ASSETS	(295,380)	665,688	370,308	(211,312)	339,571	128,259
Transfer of net assets from Sandtown Habitat for Humanity, Inc.	-	-	-	2,609,290	-	2,609,290
CHANGES IN NET ASSETS	(295,380)	665,688	370,308	2,397,978	339,571	2,737,549
NET ASSETS - Beginning of year as originally stated	12,068,328	350,924	12,419,252	9,493,577	11,353	9,504,930
EFFECT OF RESTATEMENT	(1,553,517)	-	(1,553,517)	(1,376,744)	-	(1,376,744)
NET ASSETS - Beginning of year, restated	10,514,811	350,924	10,865,735	8,116,833	11,353	8,128,186
NET ASSETS - End of year	$ 10,219,431	$ 1,016,612	$ 11,236,043	$ 10,514,811	$ 350,924	$ 10,865,735

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

HABITAT FOR HUMANITY OF THE CHESAPEAKE, INC. AND AFFILIATES
CONSOLIDATED STATEMENTS OF FUNCTIONAL EXPENSES
For the Years Ended June 30, 2016 and 2015

	2016					
	Program Services			Supporting Services		
	House Construction	ReStore	Total Program Services	Management and General	Fundraising	Total
Advertising	$ 18,747	$ 125,942	$ 144,689	$ -	$ 93,033	$ 237,722
Amortization of loan fees	3,463	-	3,463	-	-	3,463
Amortization of capitalized interest	127,144	-	127,144	-	-	127,144
Bad debt expense	16,500	180	16,680	671	37,803	55,154
Computer and software maintenance	67,638	10,500	78,138	2,094	30,734	110,966
Conference expenses	3,174	1,930	5,104	4,700	425	10,229
Construction and rehabilitation costs on houses sold and settled	3,434,862	-	3,434,862	-	-	3,434,862
Depreciation	19,109	58,027	77,136	14,020	4,510	95,666
Discounts of mortgages receivable	142,649	-	142,649	-	-	142,649
Dues and subscriptions	935	14,756	15,691	6,218	2,598	24,507
Employee benefits	51,732	123,584	175,316	76,903	43,396	295,615
Habitat for Humanity International tithe	15,500	-	15,500	-	-	15,500
Homeownership	129,002	-	129,002	-	-	129,002
Insurance	7,280	12,539	19,819	4,449	1,618	25,886
Interest	67,372	21,354	88,726	29,275	-	118,001
Impairment on inventory of homes	583,049	-	583,049	-	-	583,049
Meals and entertainment	10,929	7,559	18,488	19,303	18,981	56,772
Miscellaneous expenses	559	9,610	10,169	2,194	373	12,736
Office administration and supplies	36,321	62,555	98,876	22,197	8,072	129,145
Postage	4,503	1,134	5,637	2,752	1,001	9,390
Printing and production	8,116	13,977	22,093	4,959	1,803	28,855
Professional fees	85,134	41,591	126,725	174,325	66,715	367,765
Purchased merchandise	-	212,537	212,537	-	-	212,537
Remediation of houses previously sold	3,484	-	3,484	-	-	3,484
Rent	133,433	502,335	635,768	81,543	29,652	746,963
Repair and renew	89,896	-	89,896	-	-	89,896
Repairs and maintenance	21,673	78,548	100,221	13,246	4,817	118,284
ReStore start-up expenses	-	117,911	117,911	-	-	117,911
Salaries	472,264	1,128,208	1,600,472	702,059	396,170	2,698,701
Special events	-	-	-	-	-	-
Taxes - other	3,918	22,411	26,329	13,769	-	40,098
Taxes - payroll	42,276	100,997	143,273	62,848	35,465	241,586
Telephone	27,543	34,159	61,702	16,833	6,121	84,656
Travel	2,965	16,953	19,918	5,588	3,540	29,046
Truck expenses	-	144,857	144,857	-	-	144,857
Utilities	15,942	43,296	59,238	9,743	3,543	72,524
Volunteers	4,526	253	4,779	-	104	4,883
Total	$ 5,651,638	$ 2,907,703	$ 8,559,341	$ 1,269,689	$ 790,474	$ 10,619,504

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

	2015					
	Program Services			Supporting Services		
	House Construction	ReStore	Total Program Services	Management and General	Fundraising	Total
Advertising	$ 14,689	$ 60,649	$ 75,338	$ -	$ 83,272	$ 158,610
Amortization of loan fees	3,463	-	3,463	-	-	3,463
Amortization of capitalized interest	110,033	-	110,033	-	-	110,033
Bad debt expense	20,000	-	20,000	6,865	-	26,865
Computer and software maintenance	12,200	3,158	15,358	2,652	27,719	45,729
Conference expenses	895	6,525	7,420	121	2,245	9,786
Construction and rehabilitation costs on houses sold and settled	3,403,003	-	3,403,003	-	-	3,403,003
Depreciation	16,520	50,487	67,007	14,880	14,738	96,625
Discounts of mortgages receivable	29,146	-	29,146	-	-	29,146
Dues and subscriptions	1,355	4,310	5,665	2,630	2,787	11,082
Employee benefits	94,806	136,649	231,455	78,550	36,155	346,160
Habitat for Humanity International tithe	25,000	-	25,000	-	-	25,000
Homeownership	55,548	-	55,548	-	-	55,548
Insurance	7,972	10,071	18,043	4,196	2,518	24,757
Interest	61,250	38,355	99,605	22,500	-	122,105
Impairment on inventory of homes	996,276	-	996,276	-	-	996,276
Meals and entertainment	9,417	9,730	19,147	14,849	29,521	63,517
Miscellaneous expenses	4,516	7,529	12,045	-	635	12,680
Office administration and supplies	46,079	58,207	104,286	24,253	14,552	143,091
Postage	5,860	1,740	7,600	3,084	1,850	12,534
Printing and production	9,907	12,515	22,422	5,215	3,129	30,766
Professional fees	190,384	41,443	231,827	272,886	26,100	530,813
Purchased merchandise	-	191,655	191,655	-	-	191,655
Remediation of houses previously sold	41,239	-	41,239	-	-	41,239
Rent	110,797	299,683	410,480	58,314	34,989	503,783
Repair and renew	110,943	-	110,943	-	-	110,943
Repairs and maintenance	14,238	65,398	79,636	7,493	4,496	91,625
Restore start-up expenses	-	1,799	1,799	-	-	1,799
Salaries	732,004	995,080	1,727,084	666,494	279,159	2,672,737
Special events	5,792	113	5,905	-	429	6,334
Taxes - other	-	14,430	14,430	1,810	-	16,240
Taxes - payroll	64,247	92,602	156,849	53,231	24,501	234,581
Telephone	33,429	29,170	62,599	17,595	10,557	90,751
Travel	4,181	11,408	15,589	5,509	3,382	24,480
Truck expenses	-	87,188	87,188	-	-	87,188
Utilities	20,174	41,610	61,784	10,618	6,371	78,773
Volunteers	296	-	296	-	-	296
Total	$ 6,255,659	$ 2,271,504	$ 8,527,163	$ 1,273,745	$ 609,105	$ 10,410,013

HABITAT FOR HUMANITY OF THE CHESAPEAKE, INC. AND AFFILIATES
CONSOLIDATED STATEMENTS OF CASH FLOWS
For the Years Ended June 30, 2016 and 2015

	2016	2015
CASH FLOWS FROM OPERATING ACTIVITIES:		
Changes in net assets	$ 370,308	$ 2,737,549
Adjustments to reconcile changes in net assets to net cash provided by (used in) operating activities:		
Depreciation	95,666	96,625
Amortization of loan fees	3,463	3,463
Amortization of prepaid interest	36,885	36,780
Transfer of net assets from Sandtown Habitat for Humanity, Inc.	-	(2,609,290)
Impairment on inventory of homes	583,049	996,276
Amortization of capitalized interest on leveraged mortgages	127,144	110,033
Capitalized interest from leveraging of mortgages receivable	(331,876)	(424,726)
Mortgages assumed on real estate sales	(283,526)	(82,000)
Bad debt expense	55,154	26,865
Gain on sale of property and equipment	(6,942)	-
Changes in equity in investments in limited liability companies	(118,611)	(118,614)
Forgiveness of program debt	(269,864)	(256,030)
Discounts of mortgages receivable	142,649	29,145
Amortization of mortgage discounts	(366,257)	(846,042)
Changes in operating assets and liabilities:		
Contributions receivable	(608,466)	(649,674)
Accounts receivable	(25,539)	26,277
Grants receivable	227,164	(116,212)
Inventory of homes	521,058	96,412
ReStore inventory	(9,705)	8,098
Prepaid expenses	(25,024)	(35,278)
Accounts payable and accrued expenses	(40,909)	(1,089,792)
Deferred rent	48,603	9,761
Net cash provided by (used in) operating activities	124,424	(2,050,374)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Acquisition of property and equipment	(127,472)	(22,719)
Proceeds from transfer of assets from Sandtown Habitat for Humanity, Inc.	-	278,844
Proceeds from leveraging of mortgages receivable	-	1,030,041
Principal payments collected on mortgages receivable	884,615	749,663
Payment for repurchase of leveraged mortgage receivable	-	(110,100)
Increase in deposits	(6,253)	(4,937)
Net cash provided by investing activities	750,890	1,920,792
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from lines of credit and notes payable	1,028,360	1,186,914
Proceeds from program debt	27,628	18,555
Principal payments on lines of credit and notes payable	(1,502,298)	(2,283,128)
Principal payments on program debt	(182,671)	(106,878)
Net cash used in financing activities	(628,981)	(1,184,537)
NET CHANGES IN CASH AND CASH EQUIVALENTS	246,333	(1,314,119)
CASH AND CASH EQUIVALENTS - Beginning of year	801,179	2,115,298
CASH AND CASH EQUIVALENTS - End of year	$ 1,047,512	$ 801,179

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

NOTE A – NATURE OF ACTIVITIES

Habitat for Humanity of the Chesapeake, Inc. and Affiliates (the Organization) is composed of Habitat for Humanity of the Chesapeake, Inc. (Habitat), JLR Investments LLC (JLR), Habitat for Humanity of the Chesapeake CHDO, LLC (Chesapeake CHDO), Chesapeake Funding Company I, LLC (Chesapeake Funding) and BOTF, Inc. (BOTF).

Habitat was incorporated under the laws of the state of Maryland in 1982, and has been recognized by the Internal Revenue Service (IRS) as a not-for-profit, tax-exempt organization as defined by Section 501(c)(3) of the Internal Revenue Code (IRC) that is publicly supported, and therefore, not a private foundation.

In 2015, Habitat entered into an Articles of Merger with Sandtown Habitat for Humanity, Inc. (Sandtown), effective September 30, 2014. Sandtown provided similar services to the Organization in the Sandtown area of Baltimore, using the same approach as the Organization by providing affordable low income housing to families.

JLR is a limited liability company created by Habitat that was incorporated in Maryland in 2005. Habitat is the sole member of JLR. JLR was formed to own, operate, lease and sell real property, including certain property located in Baltimore, Maryland together with all improvements thereon.

Chesapeake CHDO is a limited liability company formed for charitable purposes, including assisting community organizations in the planning and managing of housing and economic development projects and providing decent housing that is affordable to low and moderate income people, including, for such purposes, the making of distributions to organizations that qualify as exempt organizations under Section 501(c)(3) of the IRC. Habitat is the sole member of Chesapeake CHDO.

Chesapeake Funding is a limited liability company formed for the purpose of holding certain real estate investment portfolios, and to do any and all things necessary, convenient or incidental to that purpose. Habitat is the sole member of Chesapeake Funding.

BOTF was incorporated in Maryland in 2013 and has been recognized by the IRS as a not-for-profit, tax-exempt organization as defined by Section 501(c)(2) of the IRC. BOTF was formed to hold title to the building housing the Sandtown ReStore on behalf of and for the exclusive benefit of Sandtown and is consolidated as a result of Habitat's merger with Sandtown.

The Organization is a Christian organization, unaffiliated with any denomination, that aims to demonstrate the Christian gospel by working to establish affordable housing and decent habitat through the acquisition and rehabilitation of homes for those that are in need in Anne Arundel County, Baltimore City, Baltimore County and Howard County. The Organization is supported primarily through contributions, home sponsorships, government grants, real estate sales, ReStore sales and donated goods and services.

The Organization is an affiliate of Habitat for Humanity International, Inc. (HFHI), a nondenominational Christian non-profit organization whose purpose is to create decent, affordable housing for those in need and to make decent shelter a matter of conscience with people everywhere. Although HFHI assists with information resources, training, publications, prayer support and in other ways, the Organization is primarily and directly responsible for its own operations.

NOTE A – NATURE OF ACTIVITIES – Continued

The Organization operates six Habitat for Humanity ReStores (the ReStores), one of which was previously operated by Sandtown. The ReStores are retail operations, where home furnishings, appliances, and other miscellaneous items are donated or purchased and then sold to the community at a greatly reduced price.

Program Services

Program services encompass activities directly and indirectly related to establishing affordable and decent housing through acquisition, rehabilitation, sale of homes, and retail operations. Program service expenses are categorized as House construction or ReStore expenses.

Management and General

Management and general services are those related to operating and managing the Organization and its programs on a day to day basis. The Organization's management and general services consist of activities not directly related to the programs for which the Organization exists, including all activities related to the Organization's internal management and accounting for program services.

Fundraising

Fundraising consists of activities performed either directly or indirectly to induce contributions, which will be utilized to enhance the program service activities and related management and general activities.

NOTE B – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

1. Principles of Consolidation

The accompanying consolidated financial statements include the accounts of Habitat, and those of its affiliates JLR, Chesapeake CHDO, Chesapeake Funding, and BOTF. Habitat is the sole member of its affiliates. All intercompany transactions and balances have been eliminated in consolidation.

2. Basis of Accounting

The Organization prepares its consolidated financial statements in accordance with accounting principles generally accepted in the United States of America, which involves the application of accrual basis accounting. Accordingly, revenues and gains are recognized when earned, expenses and losses are recognized when incurred and all significant receivables, payables and other liabilities are reflected in the accompanying consolidated financial statements.

3. Cash and Cash Equivalents

For purposes of financial reporting, the Organization considers demand deposits and money market accounts with an original maturity of three months or less and any certificates of deposit that do not contain material early withdrawal penalties, to be cash and cash equivalents. At various times during the year, bank balances may have exceeded the Federal Deposit Insurance Corporation (FDIC) insurance limitation for interest bearing accounts. The Organization does not believe it is exposed to any significant loss on such deposits.

4. Investments in Limited Liability Companies

The Organization has investments in limited liability companies in which it owns more than 20% of the entity, which are accounted for under the equity method. The initial investment is recorded at cost.

5. Contributions Receivable

Contributions receivable represents amounts due from contributors based on unconditional promises to give. The Organization provides an allowance for potentially uncollectible contributions based upon a review of their outstanding pledges receivable and their historical experience with individual accounts. As of June 30, 2016 and 2015, the Organization had unconditional promises to give, all of which management considered fully collectible of $1,337,729 and $784,417, respectively. Contributions receivable includes amounts receivable in more than one year in the amount of $623,187 and $114,400 as of June 30, 2016 and 2015, respectively, which are included in temporarily restricted net assets in Note N.

6. Mortgages Receivable

First Mortgages

Mortgages receivable consists of non-interest bearing mortgages, which are secured by real estate and payable in monthly installments, with maturities ranging from 20 to 30 years. All of the mortgages are related to new construction and the rehabilitation of existing homes rehabilitated by the Organization. These mortgages are shown on the consolidated statements of financial position discounted at the prevailing interest rate, for the time value of money, between 2.30% and 3.11% for the years ended June 30, 2016 and 2015. Amortization revenue is recorded using the straight-line method over the lives of the mortgages.

The Organization is a secured creditor. Management therefore records a provision for loan losses at the time that it is determined that the mortgage balance exceeds the fair market value of the related home. Management has not provided a provision for loan losses because the fair market value of the homes exceeds the related mortgage balances.

The Organization has pledged some of the mortgage loans as collateral for lines of credit and notes payable (see Note J).

Second, Third and Fourth Mortgages Receivable

In addition to the mortgages receivable included in the consolidated statements of financial position, the Organization also holds non-interest bearing second, third and fourth mortgages. These mortgages originate at the same time as the first mortgage and reflect the difference between the purchase price and the fair market value of the house. These mortgages are legal documents executed for protection against homeowners who may sell their house for a profit before the mortgage is repaid and to protect the homeowner by preventing predatory lenders from paying off the first mortgage and saddling the homeowners with an onerous new mortgage.

These mortgages are not included on the consolidated statements of financial position based on Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC), *Contingencies*, which relates to the accounting concept of conservatism. Since these mortgages are contingent receivables, they are not recorded on the books because there is a significant uncertainty that they will be exercised and collected.

NOTE B – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued

7. Leveraged Mortgages Receivable

When a mortgage receivable is leveraged, the Organization receives a discounted cash amount in exchange for the transfer of the mortgage receivable to a bank. Under these agreements, the Organization is liable to repurchase or replace a mortgage transferred to the bank in the event that the homeowner does not make the required payments. In accordance with ASC *Broad Transactions*, the leveraging of the mortgage receivable with a conditional obligation to repurchase or replace the mortgage is not considered a sale.

The leveraged mortgage receivables are shown on the consolidated statements of financial position discounted at the prevailing interest rate for the time value of money. The difference between the cash received and the gross mortgage receivable transferred is recorded as capitalized interest on leveraged mortgages receivable in the consolidated statements of financial position. The capitalized interest on leveraged mortgages receivable is amortized over the term of the leveraged mortgage receivable. The liability in the event that the homeowner does not make the required payments is included in the consolidated statements of financial position as a leveraged mortgage receivable liability, carried at fair market value.

8. Inventory of Homes

Inventory of homes consists of houses and lots purchased by or donated to the Organization for rehabilitation and resale and the cost of homes that are under construction. Donated properties, materials, and services relating to the homes are recognized at fair market value as of the date of the donation. The houses and lots are valued at net realizable value. Impairment on the inventory of homes of $583,049 and $996,276 is included in the consolidated statements of activities for the years ending June 30, 2016 and 2015, respectively. See Note U for restatement relating to impairment. When homes are sold the related costs and impairments are removed by recording construction and rehabilitation costs on houses sold and settled.

9. Property and Equipment

Property and equipment is stated at cost. The Organization capitalizes all costs that are in excess of $1,000 and have a useful life of at least one year. Expenditures for maintenance, repairs and renewals are charged against income as incurred. Expenditures for additions, improvements and replacements are added to the property and equipment accounts and depreciated over their useful lives. When assets are retired or sold, the related costs and accumulated depreciation are removed from the accounts, and any gain or loss on disposition is recognized in income.

Depreciation is calculated under the straight-line method over the estimated useful lives of the respective assets, which range from 5 to 39 years. Depreciation expense amounted to $95,666 and $96,625 for the years ended June 30, 2016 and 2015, respectively.

10. Impairment of Long-Lived Assets

In accordance with ASC *Impairment and Disposal of Long-Lived Assets,* the Organization reviews its property and equipment and all other non-current assets for impairments whenever events or changes in circumstances indicate that the carrying value of an asset may not be recoverable. If the fair value is less than the carrying amount of an asset, an impairment loss is recognized for the difference. No impairment loss relating to long-lived assets has been recognized during the years ended June 30, 2016 and 2015.

11. Warranties

The Organization provides homeowner warranties on the homes it rehabilitates and records an accrual for estimated future claims. Such accruals are based upon historical experience and management's estimate of the level of future claims. No accruals were considered necessary as of June 30, 2016 and 2015.

12. Restricted and Unrestricted Revenue

Contributions received by the Organization are presented at their fair market value on the date of such gifts. Contributions received are recorded as unrestricted, temporarily restricted or permanently restricted support depending on the existence and/or nature of any donor imposed restrictions.

Unconditional promises to give are recognized as revenue when the underlying promises are received by the Organization. Conditional promises to give are recognized when the conditions on which they depend are substantially met.

The Organization reports contributions of cash and other assets as restricted support if they are received with donor stipulations that limit the time period or manner of use of the contribution. Donor-restricted support is reported as an increase in temporarily or permanently restricted net assets, depending on the nature of the restriction. Support that is restricted by the donor is reported as an increase in unrestricted net assets if the restriction expires in the reporting period in which the support is recognized. When a donor restriction expires (that is, when a stipulated time restriction or purpose restriction is accomplished), temporarily restricted net assets are reclassified to unrestricted net assets and reported in the consolidated statements of activities as net assets released from restrictions.

13. Donated Services

Donated services meeting the requirements for recognition in the consolidated financial statements and donated materials are included in support and expense at their estimated fair values on the date they were contributed. The requirements for recognition of donated services in the consolidated financial statements are (a) the donated services create or enhance non-financial assets, or (b) the donated services require special skills, are provided by individuals who possess those special skills and donated services would typically be purchased by the Organization if they had not been provided by contribution.

14. Donated ReStore Items

Donations of ReStore items are not valued, nor is an inventory of such items used for financial reporting. This accounting treatment is based on ASC, *Contributions Received* where a major uncertainty about the existence of value may indicate that an item received or given should not be recognized. ASC, *Initial Measurement* also applies that fair value should be regarded as not determinable within reasonable limits if major uncertainties exist about the realizability of the value.

15. ReStore Inventory

ReStore inventory consists of purchased merchandise to be sold in the ReStores and is valued at the lower of cost or market.

NOTE B – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued

16. Allocation of Expenses

The costs of providing the Organization's various programs and other activities have been presented in the consolidated statements of functional expenses. Accordingly, estimates have been made to allocate certain costs among the program services, management and general and fundraising sources benefited.

17. Income Taxes

The Organization is exempt from Federal and State income taxes under Section 501(c)(3) of the IRC and is not considered a private foundation. Habitat's activities are not subject to the tax on unrelated business income. All of the ReStores' activities are classified as exempt activities since sales of purchased merchandise are less than 15% of the ReStores' total sales. JLR, Chesapeake CHDO and Chesapeake Funding are disregarded entities for tax purposes. Therefore, they do not generate taxable income. BOTF is exempt from Federal and State income taxes under Section 501(c)(2) of the IRC.

ASC, *Accounting for Income Taxes,* requires the Organization to recognize or disclose any tax positions that would result in unrecognized tax benefits. The Organization has no positions that would require disclosure or recognition under the topic. The Organization's tax returns for fiscal years ending June 30, 2013 and after are subject to examinations by the IRS and state taxing authorities.

18. Net Assets

The Organization is required to report information regarding its financial position and activities according to three classes of net assets: unrestricted net assets, temporarily restricted net assets, and permanently restricted net assets. The Organization had no permanently restricted net assets at June 30, 2016 and 2015.

19. Use of Estimates

The preparation of consolidated 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 and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

20. Reclassifications

Certain prior year amounts have been reclassified to conform to the current year presentation.

21. Merger Accounting

Upon merger with another entity, the Organization recognizes all identifiable assets and liabilities acquired at their fair value at the date of acquisition. Any difference between the fair value of the assets and liabilities acquired is recognized in the consolidated statements of activities as contribution from merger.

22. Recent Accounting Pronouncement

In August 2016, the FASB issued Accounting Standards Updated 2016-14 *Not-for-Profit Entities,* which contains significant changes to the financial statements requirements under the *Not-for-Profit Entities* topic of the ASC. The new standard is effective for the year ending June 30, 2019. The Organization will evaluate the effect that implementation of the new standard will have on its financial position, results of operations and cash flows.

NOTE B – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued

23. Reclassifications

Certain reclassifications have been made to the prior financial statements to confirm to the current year presentation.

24. Subsequent Events

In preparing these consolidated financial statements, the Organization has evaluated events and transactions for potential recognition or disclosure through January 6, 2017, the date the consolidated financial statements were available to be issued. During this period, the Organization had material recognizable subsequent events as discussed in Note I, Note J, and Note T.

NOTE C – MORTGAGES RECEIVABLE

The Organization directly finances a number of the homes that it sells. Each mortgage is issued as a zero-interest mortgage to the buyer. The Organization discounts the mortgages using the current interest rates at the time the home is sold. The discounts are amortized using the straight-line method over the lives of the mortgages.

Mortgages receivable as of June 30, 2016 and 2015 are as follows:

	2016	2015
Mortgages receivable	$ 12,427,761	$ 13,420,575
Less: discount on mortgages	(4,586,086)	(4,970,970)
	$ 7,841,675	$ 8,449,605

At June 30, 2016, the balances due on the mortgages that are scheduled to be received for the next five years and thereafter are as follows:

Years ending June 30,	2017	$ 980,969
	2018	957,677
	2019	930,766
	2020	893,654
	2021	842,555
	Thereafter	7,822,140
	Total	$ 12,427,761

NOTE D – LEVERAGED MORTGAGES RECEIVABLE

The Organization leverages mortgages receivable to banks. Leveraged mortgages receivable as of June 30, 2016 and 2015 are as follows:

	2016	2015
Leveraged mortgages receivable	15,699,136	14,573,811
Less: discount on leveraged mortgages	(6,446,540)	(5,603,512)
	$ 9,252,596	$ 8,970,299

NOTE E – LOAN FEES

At June 30, 2016 and 2015, loan fees are as follows:

	2016	2015
Loan fees at cost	$ 63,955	$ 63,955
Less: accumulated amortization	(21,822)	(18,359)
Loan fees, net of amortization	$ 42,133	$ 45,596

Loan fees are amortized using the straight-line method over the life of the related loans, ranging from fifteen to twenty-five years. Amortization expense for each of the years ending June 30, 2016 and 2015 was $3,463. Amortization expense for each of the next five years will be $3,463.

NOTE F – FAIR VALUE MEASUREMENTS

ASC *Fair Value Measurements and Disclosure* topic requires financial assets and liabilities to be valued and disclosed based on the following structure:

Level I - Investments included in this designation are valued based on quoted prices for identical investments in active markets as of the reporting date.

Level II - Investments included in this designation are valued based on observable market based inputs or unobservable inputs that are corroborated by market data.

Level III - Investments included in this designation are valued based on unobservable inputs that are significant to the valuation of a particular investment. The inputs into the determination of fair value in this level require significant management judgment or estimates.

In determining the appropriate levels for each investment, Management performs a detailed analysis of the assets and liabilities that are subject to the ASC *Fair Value Measurements and Disclosures* topic. In some instances, an investment may be valued using a combination of inputs. In such instances, the investment is to be classified based on the lowest significant level used in the valuation. Management's assessment of the significance of a particular input in the fair value measurement of an investment requires judgment and considers factors specific to the investment.

Following is a description of the valuation methodology used for assets and liabilities measured at fair value. There have been no changes in the methodology used at June 30, 2016 and 2015.

Leveraged mortgages receivable liability: Valued at the carrying amount of the related leveraged mortgage receivable asset which approximates the value of the replacement mortgage to be transferred to the bank in the event that the homeowner does not make the required payments.

The methods described above may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the Organization believes its valuation method is appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

NOTE F – FAIR VALUE MEASUREMENTS – Continued

The following table is set forth by level, within the fair value hierarchy, the Organization's liabilities at fair value as of June 30, 2016 and 2015:

Assets and Liabilities at Fair Value as of June, 30 2016

	Level 1	Level 2	Level 3	Total
Leveraged mortgages receivable liability	$ -	$ 9,252,596	$ -	$ 9,252,596

Assets and Liabilities at Fair Value as of June, 30 2015

	Level 1	Level 2	Level 3	Total
Leveraged mortgages receivable liability	$ -	$ 8,970,299	$ -	$ 8,970,299

NOTE G – INVESTMENTS IN LIMITED LIABILITY COMPANIES

The Investments in Limited Liability Companies on the consolidated statements of financial position includes investments from participation in three New Market Tax Credit (NMTC) Programs. NMTC programs provide funds to eligible organizations for investment in "qualified low-income community investment". Program compliance requirements included creation of a promissory note and investment in a qualified community development entity (CDE). Tax credit recapture is required if compliance requirements are not met by the CDE over a seven-year period. Details of the transactions follow.

HFHI-SA Leverage III, LLC (Habitat Affiliate 1)

In 2010, the Organization invested, along with 5 other Habitat affiliates, in Habitat Affiliate 1 with 20.526% ownership, to take advantage of NMTC financing. The Organization invested $3,716,144 with Habitat Affiliate 1 and was able to secure a 15-year loan in the amount of $4,455,113 payable to City First Capital 21, LLC (CDE) (a subsidiary of Habitat Affiliate 1). The loan proceeds are to be used solely for the purpose of constructing and selling qualified housing properties to low income residents subject to certain conditions. See Note I for loan terms.

The following is a summary of the activity for Habitat Affiliate 1 for the years ending June 30:

	2016	2015
Beginning balance	$ 4,050,882	$ 4,001,640
Investment activity	49,242	49,242
Ending balance	$ 4,100,124	$ 4,050,882

NOTE G – INVESTMENTS IN LIMITED LIABILITY COMPANIES - Continued

The following is the condensed financial information of Habitat Affiliate 1 as of and for the years ending June 30:

	2016	2015
Cash	$ 5	$ 5
Interest receivable	1,985,084	1,686,576
Note receivable	17,518,157	17,518,157
Total assets	$ 19,503,246	$ 19,204,738
Equity	$ 19,503,246	$ 19,204,738
Revenue and net income	$ 473,688	$ 473,688

HFHI-SA Leverage VIII, LLC (Habitat Affiliate 2)

In 2011, the Organization invested, along with three other Habitat affiliates, in Habitat Affiliate 2 with 43.223% ownership to take advantage of NMTC financing. As a result, the Organization invested $4,298,956 and was able to secure a 15-year loan in the amount of $5,277,163 payable to HFHI-SA NMTC V, LLC (CDE) (a subsidiary of Habitat Affiliate 2). The loan proceeds are to be used solely for the purpose of constructing and selling qualified housing properties to low income residents. See Note I for loan terms.

The following is a summary of the activity for Habitat Affiliate 2 for the years ending June 30:

	2016	2015
Beginning balance	$ 4,469,304	$ 4,426,633
Investment activity	42,668	42,671
Ending balance	$ 4,511,972	$ 4,469,304

The following is the condensed financial information of Habitat Affiliate 2 as of and for the years ending June 30:

	2016	2015
Interest receivable	$ 957,130	$ 778,320
Note receivable	9,322,862	9,322,862
Total assets	$ 10,279,992	$ 10,101,182
Equity	$ 10,279,992	$ 10,101,182
Revenue and net income	$ 271,144	$ 271,144

Habitat Harbor Leverage, LLC (Habitat Affiliate 3)

In 2013, the Organization invested, along with 2 other nonprofit organizations, in Habitat Affiliate 3 with 50.915% ownership, to take advantage of NMTC financing. NMTC financing allows an entity to receive a loan or investment capital from outside investors, who will receive new market tax credits to be applied against their federal tax liability.

NOTE G – INVESTMENTS IN LIMITED LIABILITY – Continued

The Organization invested $4,469,199 with Habitat Affiliate 3 and was able to secure a 15-year loan in the amount of $5,114,482 payable to Harbor Community Fund VI LLC (CDE) (a subsidiary of Habitat Affiliate 3). The loan proceeds are to be used solely for the purpose of constructing and selling qualified housing properties to low income residents subject to certain conditions. See Note I for loan terms.

The following is a summary of the activity for Habitat Affiliate 3 for the years ending June 30:

	2016	2015
Beginning balance	$ 4,547,309	$ 4,520,608
Investment activity	26,701	26,701
Ending balance	$ 4,574,010	$ 4,547,309

The following is the condensed financial information of Habitat Affiliate 3 as of and for the years ending June 30:

	2016	2015
Interest receivable	$ 630,078	$ 464,510
Note receivable	7,347,785	7,347,785
Total assets	$ 7,977,863	$ 7,812,295
Equity	$ 7,977,863	$ 7,812,295
Revenue and net income	$ 239,046	$ 239,046

Additionally, in 2015, as part of the merger with Sandtown (see Note A), the Organization acquired an additional 18.740% ownership in Habitat Affiliate 3. This investment is carried at fair market value and is netted against the related note payable, related party for financial statement purposes (see Note I). This results in a net fair market value of $-0- since the cash inflows from the interest received from the investment and cash outflows from the interest paid on the note are approximately the same amount.

NOTE H – DEFERRED RENT

The Organization's lease agreements for its main office and for its Dundalk, Columbia, Glen Burnie, and Timonium ReStore buildings have provisions for rent payments with fixed annual increases (see Note P). In accordance with generally accepted accounting principles, the total rent commitment is recognized on a straight-line basis over the term of the lease. Accordingly, the difference between the actual monthly payments and the rent expense being recognized for consolidated financial statement purposes is recorded as deferred rent.

Future amortization of deferred rent over the remaining life of the lease is as follows:

Years ending June 30,	2017	$ (11,908)
	2018	(27,404)
	2019	(27,678)
	2020	(31,048)
	2021	(8,226)
		$ (106,264)

NOTE I – NOTES PAYABLE, RELATED PARTIES

During 2010, in connection with the investment in Habitat Affiliate 1 (see Note G), the Organization received a $4,455,113 note from City First Capital 21, LLC (a related party). The note requires interest only payments at 0.8126%. The note is secured by substantially all the assets acquired by the Organization from the project loan proceeds. The note has a put option feature that is exercisable on or before December 1, 2016. Subsequent to year end, the option was exercised and the debt was forgiven in full.

During 2011, in connection with the investment in Habitat Affiliate 2 (see Note G), the Organization received a $5,277,163 note from HFHI-SA NMTC V, LLC (a related party). The note requires interest only payments at 0.756432%. The note is secured by substantially all the assets acquired by the Organization from the project loan proceeds. The note has a put option feature that is exercisable on or before March 11, 2018. Management expects that the option will be exercised and the debt will thereby be forgiven. In the event that the option is not exercised principal and interest payments will be made through February 24, 2026.

During 2013, in connection with the investment in Habitat Affiliate 3 (see Note G), the Organization received a $5,114,482 note from Harbor Community Fund VI, LLC (a related party). The note requires interest only payments at 0.7316%. The note is secured by substantially all the assets acquired by the Organization from the project loan proceeds. The note has a put option feature that is exercisable on or before September 10, 2019. Management expects that the option will be exercised and the debt will thereby be forgiven. In the event that the option is not exercised principal and interest payments will be made through September 10, 2027.

Additionally, during 2015, as part of the merger with Sandtown (see Note A), the Organization acquired an additional note payable in the amount of $1,882,483 due to Harbor Community Fund VI. LLC, subject to the same terms as the note from Harbor Community Fund VI. LLC, disclosed above. This note is carried at fair market value and is netted against the related investment for financial statement purposes (see Note G).

Interest expense on the notes payable, related parties included in investment income from limited liability companies on the consolidated statements of activities was $127,310 for each of the years ended June 30, 2016 and 2015.

NOTE J – LINES OF CREDIT AND NOTES PAYABLE

Lines of credit and notes payable consisted of the following as of June 30:

	2016	2015
M & T Revolving Note	$ 200,000	$ 200,000
Severn Savings Bank	2,289,286	2,419,286
Neighborhood Housing Services of Baltimore, Inc.	359,722	376,389
Self-help Homeownership Opportunity Program	114,049	144,889
SECU	-	509,489
Rosedale Federal Savings and Loan Association	-	240,000
BOKF, NA dba Bank of Texas	326,446	105,826
PNC Community Development Company, LLC	1,510,286	1,613,046
City of Annapolis - 55 Clay	125,000	125,000
City of Annapolis - 123 Clay	82,000	82,000
MECU	25,773	-
HABC	307,513	307,513
CDFC, net	309,690	447,192
M & T Notes	466,187	518,845
MECU Auto	6,483	11,114
Total long-term debt	$ 6,122,435	$ 7,100,589
Less current portion	(1,116,472)	(1,433,373)
Long-term portion	$ 5,005,963	$ 5,667,216

M & T Bank – Credit Line

The Organization has a $50,000 credit line with M & T, bearing interest at the bank's prime rate plus 1.5%, (5.00% and 4.75% as of June 30, 2016 and 2015, respectively) and due on demand. The credit line is secured by all business assets of the Organization. There were no outstanding borrowings as of June 30, 2016 and 2015.

M & T Bank – Revolving Note

The Organization has a $350,000 revolving demand note with M & T, bearing interest at the bank's prime rate, (3.50% and 3.25% as of June 30, 2016 and 2015, respectively) and due on demand. The revolving demand note is secured by all deposits or other sums credited by or due from M & T to the Organization, as well as any cash, securities, instruments or other property. Subsequent to year end, the maximum draw amount was reduced to $200,000.

Severn Savings Bank

The Organization has a $2,500,000 line of credit with Severn Savings Bank (Severn). The line of credit bore interest at 3.25% through January 1, 2015. On January 1, 2015, the interest rate was amended to 4.25%. The amendment also requires the Organization to make $10,000 principal payments monthly. This line is secured by mortgages receivable in the amount of $3,588,111 and $4,232,275 as of June 30, 2016 and 2015, respectively. This line of credit contains covenants with which the Organization must comply. Subsequent to year end, the line of credit was amended, and is now due August 1, 2017.

NOTE J – LINES OF CREDIT AND NOTES PAYABLE – Continued

Neighborhood Housing Services of Baltimore

Note payable to Neighborhood Housing Services of Baltimore, Inc. (NHS), with 0% interest, with monthly principal payments of $1,389 maturing January 31, 2038. This note is secured by 5 real estate properties.

Self-help Homeownership Opportunity Program

The Self-help Homeownership Opportunity Program (SHOP) notes payable to HFHI are noninterest-bearing and unsecured notes used for building homes. These notes represent a 25% portion of the SHOP grants received as of June 30, 2016 and 2015, respectively, payable through 2021.

SECU

Note payable for $600,000 with SECU, bearing interest at 6%. The note was to be repaid with monthly principal and interest payments of $3,898 until May 2018, at which time the balance of the note was scheduled to be due. During 2016, the Organization sold the Pasadena ReStore building and the note was paid in full.

Rosedale Federal Savings and Loan Association

Construction loan up to a maximum amount of $1,800,000 from Rosedale Federal Savings and Loan Association, with 5.25% interest. During 2016, the loan was paid in full.

BOKF, NA dba Bank of Texas

During 2013, the Organization obtained a note payable for $150,000 from BOKF, NA dba Bank of Texas, with 4.03% interest. The note requires interest only payments for the first year followed by monthly payments of principal and interest in the amount of $2,768, maturing November 30, 2018. This note contains covenants with which the Organization must comply.

During 2016, the Organization obtained two notes of $125,000 each from BOKF, NA dba Bank of Texas, with 4.71% interest. The notes require monthly payments of principal and interest in the amount of $2,346 each, maturing July 15, 2021. These notes contain covenants with which the Organization must comply.

PNC Community Development Company, LLC

During 2013, the Organization obtained a note payable for $1,847,867 from PNC Community Development Company, LLC. Proceeds from the loan were $1,401,012. The note includes $416,855 of prepaid interest and $30,000 of loan fees. The note is secured by approximately $1,510,000 and $1,607,000 of mortgages receivable as of June 30, 2016 and 2015, respectively, and requires monthly payments ranging from $89 to $8,800, based on a payment schedule that is based on the anticipated amounts to be received from those mortgages receivable. The note matures July 15, 2038.

City of Annapolis – 55 Clay

During 2013, the Organization obtained a note payable for $125,000 from the city of Annapolis, with 0% interest. During 2016, the note was extended to be repaid in full at the earlier of the sale of the home at 55 Clay Street or June 30, 2016. Subsequent to year end, the note was amended to require four equal installment payments of $31,250 to be made from March 2017 through September 2017 with a maturity date of October 31, 2017.

NOTE J – LINES OF CREDIT AND NOTES PAYABLE – Continued

City of Annapolis – 123 Clay

During 2014, the Organization obtained a note payable for $82,000 from the city of Annapolis, with 0% interest. During 2016, the note was extended to be repaid in full at the earlier of the sale of the home at 123 Clay Street or on December 31, 2016. Subsequent to year end, the note was extended to be repaid in full at the earlier of the sale of the home at 123 Clay Street or on December 31, 2017.

MECU

During 2014, the Organization obtained a note payable for $685,000 from the Municipal Employees Credit Union of Baltimore (MECU), with interest at 4.5%. The note is a construction loan that calls for interest only payments until the maturity date of April 1, 2017 on which date the note is due in full and, as required, the Organization has repaid funds borrowed against collateral houses when the houses settled. This note contains covenants with which the Organization must comply.

HABC

During 2015, the Organization obtained a bridge promissory note from the Housing Authority of Baltimore City (HABC) for $307,513. The note is interest free and is due the earlier of July 15, 2015 or upon HABC receiving written approval from the United States Department of Housing and Urban Development that they intend to release the final five percent of the grant funds to HABC. Subsequent to year end, HABC agreed that in lieu of the Organization repaying the bridge promissory note, the Organization will assign to HABC all of its rights to receive the remaining $307,513 in grant funds in consideration for the cancellation of the bridge promissory note.

CDFC, net

During 2015, as part of the merger with Sandtown (see Note A) the Organization acquired notes payable to Baltimore Community Development Financing Corporation (CDFC). The notes are secured by mortgages receivable, and are non-interest bearing with various maturity dates through 2021. The Organization imputed interest on these notes using a 4.25% interest rate at the date of the merger in order to approximate fair market value of the liability. The notes are shown net of a discount of $41,044 and $43,562 as of June 30, 2016 and 2015, respectively.

M & T Notes

During 2015, as part of the merger with Sandtown (see Note A) the Organization acquired notes payable to M&T Bank. The notes are secured by mortgages receivable, and bear interest at rates from 5.7% to 5.8% with various maturity dates through 2033.

MECU Auto

During 2015, as part of the merger with Sandtown (see Note A) the Organization acquired a note payable to MECU. The note is secured by a truck, bears interest at 3.74%, and matures in 2018.

NOTE J – LINES OF CREDIT AND NOTES PAYABLE – Continued

The future minimum principal payments for the next five years and thereafter, based on maturity dates, including extensions obtained subsequent to year end, are as follows:

Years ending June 30,	2017	$ 1,116,472
	2018	618,717
	2019	441,341
	2020	364,868
	2018	347,557
	Thereafter	3,233,480
		$ 6,122,435

Interest expense on the lines of credit and notes payable was $96,730 and $122,105 for the years ended June 30, 2016 and 2015, respectively. In addition, the Organization paid interest of $242,878 and $202,556 for the years ending June 30, 2016 and 2015, respectively, which has been capitalized as part of inventory of homes on the consolidated statements of financial position.

Subsequent to year end, the Organization obtained a note in the amount of $1,150,000 from Rosedale Federal Savings and Loan Association with prime plus 0.50% interest but no less than 4.00% interest per year. The note requires interest only payments and matures August 2019.

Subsequent to year end, the Organization obtained a line of credit in the amount of $100,000 from MECU with interest of 4.50%. The note requires monthly interest only payments and matures September 2017. The Organization has pledged six properties included in inventory of homes as collateral.

NOTE K – PROGRAM DEBT

The Organization entered into a development agreement with Healthy Neighborhoods, Inc. (HNI). Under the development agreement, the Organization is required to expend no less than $5,000,000 to acquire and rehabilitate 50 residential properties. This expenditure requirement has been fulfilled by the Organization. Loan proceeds are drawn by the Organization for purposes of acquiring and rehabilitating homes. Upon settlement of such homes, the Organization has the option of remitting the proceeds from the sale of the home as a prepayment to HNI. Under this option, the remaining liability relating to this home will be forgiven. This forgiving of the remaining liability is recognized in the consolidated statements of activities as debt forgiveness revenue. Any outstanding liabilities will become due two years after the date of the acquisition of the property. Interest will accrue on the loan at prime plus 3%. Interest does not accrue until after the payment of the final portion of the developer's fee associated with the property. As of June 30, 2016, there is one remaining property to be sold under the agreement with HNI.

NOTE L – REAL ESTATE SALES

During the years ended June 30, 2016 and 2015, the Organization sold 16 homes in each year. Income and related costs on the sale of each home are not recognized until the home goes to settlement and the deed is transferred to the purchaser.

NOTE M – DONATED MATERIALS AND SERVICES

Many individuals volunteer their time and perform a variety of tasks that assist the Organization with its program, fundraising and administrative activities. Due to the criteria regarding the recognition of donated goods and services, many of the Organization's donated services are not reflected in the accompanying consolidated financial statements.

The following amounts are included as donated property and donated goods or services in the accompanying consolidated statements of financial position and consolidated activities as of and for the year ended June 30:

	2016	2015
Donated property – capitalized in homes inventory	$ 44,500	$ 353,800
Materials and equipment – capitalized in homes inventory	40,164	24,753
Individual support meeting requirements for recognition	196,313	125,514
	$ 280,977	$ 504,067

NOTE N – TEMPORARILY RESTRICTED NET ASSETS

Temporarily restricted net assets were available for the following purposes and time restrictions as of June 30:

	2016	2015
Purpose restrictions		
Workforce development	$ 201,147	$ -
Youth passenger bus	20,855	50,000
ReStore vehicle	-	35,000
Volunteer engagement	-	38,005
House construction and rehabilitation		
Home sponsorships	170,918	77,382
Repair and renew	-	35,632
Chesapeake Matched Savings Account	505	505
Total purpose restrictions	393,425	236,524
Time restrictions		
Long-term contributions receivable, net	623,187	114,400
	$ 1,016,612	$ 350,924

NOTE O – LOSS ON SALE OF HOMES

During the year ended June 30, 2016, nine homes were sold that were originally held as inventory to be sold within the House construction program. The proceeds were $54,960 and accumulated costs totaled $49,436 resulting in a gain of $5,524. During the year ended June 30, 2015, three such homes were sold. The proceeds were $145,116 and accumulated costs totaled $154,634 resulting in a loss of $9,518.

NOTE P – LEASES

The Organization leases a building for its Dundalk ReStore location under a non-cancelable operating lease agreement. In 2015, the lease agreement was amended so that the lease term will end in February 2018. The lease provides for basic annual rent of $115,308 for the first year with annual increases of 3% of the previous year's base rental.

The Organization leases its office and warehouse space under a non-cancelable operating lease agreement. During 2015, the lease agreement was renewed for a five-year period from January 1, 2015 to December 31, 2019. The lease provides for annual rent of $177,650 for the first year with annual increases.

In February 2013, the Organization leased a building for its Columbia ReStore location under a non-cancellable operating lease agreement. The lease agreement is for 66 months and through 2018. The lease provides for basic annual rent of $82,886 with annual increases of 2% of the previous year's base rental.

In 2015, the Organization leased a building for its Glen Burnie ReStore location under a non-cancellable operating lease agreement. The lease agreement is for 63 months through July 2020. The lease provides for basic annual rent of $128,700 with annual increases.

During the year, the Organization leased a building for its new Timonium ReStore location under a non-cancellable operating lease agreement. The lease is for 63 months through November 2020. The lease provides for basic annual rent of $138,060 with annual increases.

Rent expense for the years ended June 30, 2016 and 2015 was $746,963 and $503,783, respectively.

The minimum annual lease payments under these leases for the next five years and thereafter are as follows:

Years ending June 30,	2017	$ 665,759
	2018	641,656
	2019	490,119
	2020	392,565
	2021	88,095
		$ 2,278,194

NOTE Q – EMPLOYEE BENEFITS

The Organization maintains a tax deferred annuity plan for its employees under IRC Section 403(b). Under the terms of the plan, the Organization will match 40% of the employee’s deferral up to a maximum 8% of employee compensation. The Organization's contributions totaled $24,628 and $26,821 for the years ended June 30, 2016 and 2015, respectively.

NOTE R – SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION

Cash paid for interest during the years ended June 30, 2016 and 2015 was $302,723 and $287,776, respectively.

During the years ended June 30, 2016 and 2015, HNI paid $58,197 and $64,670, respectively, of settlement costs, directly to banks on behalf of the Organization. These payments were recorded as increases in debt and decreases in debt forgiveness income on the consolidated statements of financial position and the consolidated statements of activities, respectively.

NOTE R – SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION – Continued

During the years ended June 30, 2016 and 2015, the Organization foreclosed or received the home back with a deed in lieu on homes for which the mortgagees were not making payments. These amounts were transferred from mortgages receivable to inventory of homes in the amounts of $230,449 and $162,133, respectively.

During the years ended June 30, 2016 and 2015, the Organization capitalized $350,579 and $306,917 of interest from leveraging of mortgages receivable. The differences between the gross value of the mortgage receivable and the cash received were recorded as decreases in mortgages receivable and increases of capitalized interest from leveraging of mortgages receivable in the consolidated statements of financial position.

During the year ended June 30, 2015, the Organization received assets and liabilities through a merger with Sandtown (see Note A). The assets, net of liabilities were valued at $2,609,290, including $278,044 of cash at the time of the merger.

During the year ended June 30, 2016, the Organization directly remitted proceeds in the amount of $504,216 from the sale of property to pay off a mortgage on the property in connection with the Pasadena ReStore.

NOTE S – TRANSACTIONS WITH HABITAT INTERNATIONAL

The Organization annually makes an election to remit to HFHI a tithe based on undesignated contributions. These funds are used to construct homes in economically depressed areas around the world. The Organization contributed $15,500 and $25,000 to HFHI for the years ended June 30, 2016 and 2015, respectively. Such amounts are included in program services expense in the consolidated statements of activities.

NOTE T – GRANT RESTRICTIONS

During 2011, the Organization received a grant in the amount of $367,101, all of which was recognized as revenue in the year ended June 30, 2013, pursuant to the terms of a certain Project and Loan Agreement for the Disposition of Up-Front Grant Funds dated December 20, 2007, by and between Orchard Ridge Homeownership I, Inc. and HABC. $307,513 relating to this grant is included in grants receivable at June 30, 2016 and 2015. Under the provisions of the grant agreement, if the Organization is not in compliance with the terms of the grant, HABC has the right to recover the grant proceeds.

Subsequent to year end, expenditures related to this grant were approved. The Organization plans to assign the rights of the revenue over to HABC, and the City of Baltimore (the grantor) is going to pay them directly for the receivable. When the money is received by HABC the loan obligation will be paid and written off.

NOTE U – RESTATEMENT – CHANGE IN ACCOUNTING POLICY

During the current year, the Organization determined that impairment relating to inventory of homes should be included in the consolidated financial statements. Net assets as of July 1, 2014 were restated by reducing construction in progress and unrestricted net assets by $1,376,744. The consolidated statement of activities for the year ended June 30, 2015 was also restated resulting in an increase in program services expense of $207,573 and a decrease in the loss on sale of homes of $30,800. Net assets as of July 1, 2015 were restated by reducing inventory of homes and unrestricted net assets by $1,553,517.