HABITAT FOR HUMANITY METRO MARYLAND, INC.

FINANCIAL STATEMENTS
WITH
INDEPENDENT AUDITORS' REPORT

Years Ended June 30, 2016 and 2015

DELEON & STANG
CERTIFIED PUBLIC ACCOUNTANTS AND ADVISORS

HABITAT FOR HUMANITY METRO MARYLAND, INC.

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Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion and analysis of the financial condition and results of our operations should be read in conjunction with the financial statements and the notes to those statements included elsewhere in this report. This discussion contains forward-looking statements reflecting our current expectations that involve risks and uncertainties. Actual results and the timing of events may differ materially from those contained in these forward-looking statements due to a number of factors.

Background

Habitat for Humanity of Montgomery County Maryland, Inc. was formed as a nonprofit corporation under the laws of the State of Maryland on October 29, 1982 (inception). In April 2013, the Board of Directors approved a resolution to expand into Prince George's County, Maryland and operate going forward under Habitat for Humanity Metro Maryland, Inc.

In 2006, Habitat for Humanity Metro Maryland opened its first retail operation that sells donated usable goods and surplus building materials to the public and operates under the name "ReStore". Currently, there are two ReStores in operation. One is in Rockville, Maryland and the other is in Silver Spring, Maryland. Total combined ReStore sales for the years ending June 30, 2016 and 2015 were $1,546,133 and $1,160,153, respectively.

Overview

In a spirit of collaboration and fellowship, Habitat for Humanity Metro Maryland ("HFHMM") works with individuals, institutions, faith organizations, businesses, and the Habitat families themselves to build and rehabilitate decent and energy efficient affordable housing for those living in substandard conditions in our community.

Our vision is a community in which everyone has a decent and affordable place to live. While Montgomery and Prince George's Counties are part of the most affluent, fastest growing communities in the nation, thousands of its residents are living in poverty. Housing costs have sky-rocked, while income growth in many jobs has remained the same – making the dream of homeownership almost impossible for low-income families.

However, Habitat's unique homeownership model and programs provide a solution to this problem by offering low-income individuals the opportunity to purchase their own decent and affordable home or repair, rehabilitate, and weatherize the home.

Our mission is to create simple, decent and affordable homeownership opportunities in Montgomery and Prince George's Counties, MD. HFHMM supports the notion that good, stable housing matters for neighborhoods. Better quality of living leads to stronger citizens and families. Habitat for Humanity is about changing lives, one home at a time.

Strategic Planning

Community Impact

For the fiscal years 2014 through 2018, HFHMM set a goal to serve 250 families through new construction, neighborhood revitalization, weatherization, minor home repair, and major home repair. We are happy to report that we served 37 families in 2014, 43 families in 2015, and 52 families in 2016. To achieve this goal, we are prepared to respond quickly as opportunities to serve arise. HFHMM currently has 60 projects in its pipeline, comprised of 19 in Montgomery County and 41 in Prince George's County.

Sector Impact

HFHMM strives to be the go-to organization for affordable housing and for owner-occupied neighborhood revitalization. HFHMM plans to strategically facilitate and support increased opportunities for affordable housing through collaborations with the affordable housing sector.

Societal Impact

HFHMM believes it is an organization that inspires action to end poverty housing. One of our goals is to increase awareness of the need and value of affordable housing. We study and forecast the impact of our work in the communities we service. In a recent *Habitat Homeowner Study,* conducted by *Habitat for Humanity International,* Habitat homeownership contributes to self-esteem and well-being, improved family mental and physical health, community awareness, and a feeling of neighborhood pride. Habitat homeowners pay taxes and are more likely to vote. As well, Habitat homeowners are able to save more, pursue advanced educational opportunities, and work towards achieving financial stability. By providing a stable home, Habitat homeownership is more likely to prevent the fracturing of families. We will continue to maintain and grow the volunteer base in Montgomery County and Prince George's County. In addition, we will continue to serve families internationally through our global partnerships to which we have tithed $54,996 and $45,229, respectively.

Build a Sustainable Organization

HFHMM will continue to mobilize resources and steward them faithfully. We will continue to fund our mission strategically, grow our skills and leadership capabilities, and operate with excellence.

Organizational Data, Statistics, and Financial Reporting

Since 1982 (inception), HFHMM has served 244 families through new construction, neighborhood revitalization, weatherization, minor home repair, and major home repair, of which 52 were served in 2016 and 43 were served in 2015.

Management's Discussion and Analysis of Financial Condition and Results of Operations (Continued)

From an organization and financial reporting perspective, Habitat for Humanity Metro Maryland is a nonprofit corporation that follows accounting principles generally accepted in the United States (GAAP).

- Habitat for Humanity Metro Maryland operates under a unique business model. In addition to its retail operation, new home construction, home renovation initiatives, HFHMM acts as the mortgage servicer and lends money to homebuyers at a below market interest rate (0%). HFHMM records the loan receivable at their face value, but net of the mortgage discounts using interest rates established by Habitat International (7.48% for 2016). Other non-cash transactions that impact HFHMM's financial reporting represent amortization of deferred gains on home sales, depreciation and amortization, and amortization of the discount of notes payable. The result of those non-cash entries in a year with significant home sales results in the statement of activities reflecting significant losses. We encourage the readers' of our financial statements to focus on the statement of cash flows as part of the overall financial statement package.

A reader will notice that for the years ending June 30, 2016 and 2015:

- The change in net assets were ($531,702) and ($3,491,631), respectively, while producing a net positive change in cash from operating activities of $126,596 and $3,455,246, respectively.
- As of June 30, 2016 and 2015 mortgage loan receivable, net of discounts included in the statements of financial position were $4,742,900 and $4,529,927, respectively. These mortgage loans receivable have gross or face values of $10,902,451 and $10,580,124, respectively. This compares to notes payable net of discounts $6,682,547 and $6,436,279, respectively. These notes payable have gross or face values of $8,102,791 and $7,904,806, respectively.

HFHMM also retains an equity interest in the properties. Presently, if the home is sold in years 1 through 5, then HFHMM retains 100% equity, then HFHMM's equity interest is reduced 3% in each succeeding year thereafter with HFHMM always retaining a 25% equity in the home.

To facilitate operating cash flow in the effort to support its mission and goals, HFHMM has the option to assign its mortgages to a bank, whereby HFHMM receives approximately 80% of the value of the mortgage in cash while still guaranteeing 100% of the loan. As of June 30, 2016, HFHMM had assigned 45 loans under this arrangement. HFHMM, under its strategic plan, has set goals to increase fundraising to permit land acquisition and construction from operating cash and thus avoid mortgage assignments and construction loans. This would allow HFHMM to re-invest the mortgage payments into additional projects. In addition, HFHMM will look to enhance the ReStore's profitability and examine future locations to further assist in funding the mission and goals.

Since 1982, HFHMM has closed on 88 mortgage loans with its homebuyers, of which 80 are still active as of June 30, 2016. Mortgage note receivables, net, at June 30, 2016 and 2015 were $4,742,900 and $4,529,927, respectively (see Note 3).

Please refer to the following accompanying financial statements and the notes to the financial statements.

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INDEPENDENT AUDITORS' REPORT

Board of Directors
Habitat for Humanity Metro Maryland, Inc.
Silver Spring, Maryland

We have audited the accompanying financial statements of **Habitat for Humanity Metro Maryland, Inc.** (a nonprofit organization), which comprise the statements of financial position as of June 30, 2016 and 2015, and the related statements of activities, functional expenses, and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these 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 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 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 financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditors consider internal control relevant to the entity's preparation and fair presentation of the 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 financial statements.

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

Opinion

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

DeLeon & Stang

DeLeon & Stang, CPAs
Gaithersburg, Maryland
November 2, 2016

HABITAT FOR HUMANITY METRO MARYLAND, INC.
STATEMENTS OF FINANCIAL POSITION
June 30, 2016 and 2015

	2016	2015
Assets		
Cash and cash equivalents	$ 658,750	$ 1,095,646
Restricted cash	5,160	25,027
Grants and contracts receivable	38,761	45,477
Mortgage loans receivable, net of discounts of $6,159,551 and $6,050,197, respectively	4,742,900	4,529,927
Inventories	570,551	427,784
Property and equipment, net of accumulated depreciation of $226,617 and $172,840, respectively	790,044	297,085
Other assets	180,673	41,627
Total Assets	$ 6,986,839	$ 6,462,573
Liabilities and net (deficit) assets		
Liabilities:		
Accounts payable and accrued expenses	$ 214,948	$ 162,158
Homeowner escrow deposits	13,786	30,429
Lines of credit	433,767	250,000
Deferred rent	856,940	250,781
Notes payable and mortgage note assignments	6,682,547	6,436,279
Deferred gain on home sales	825,986	842,359
Total liabilities	9,027,974	7,972,006
Net (deficit) assets:		
Net deficit, unrestricted	(2,075,565)	(1,509,433)
Net assets, temporarily restricted	34,430	-
Total net deficit	(2,041,135)	(1,509,433)
Total liabilities and net (deficit) assets	$ 6,986,839	$ 6,462,573

HABITAT FOR HUMANITY METRO MARYLAND, INC.
STATEMENTS OF ACTIVITIES
Years Ended June 30, 2016 and 2015

	2016	2015
Unrestricted net assets		
Revenue and support:		
Contributions, grants and contracts	$ 929,585	$ 919,640
Home sales	811,500	4,800,000
ReStore sales	1,546,133	1,160,153
Special events income	253,076	205,517
In-kind contributions	11,215	74,542
Imputed mortgage interest income	355,146	294,172
Mortgage subsidy recapture	28,226	106,242
Loss on extinguishment of notes payable	(8,245)	-
Loss on disposal of assets	(7,137)	(108,283)
Interest and other income (loss)	(6,030)	16,320
Total unrestricted revenue and support	3,913,469	7,468,303
Expenses:		
Program services:		
Affordable residential housing	2,235,309	9,160,283
ReStore operating expenses	1,618,085	1,206,264
HFHI tithe expense	54,996	45,229
Total program services	3,908,390	10,411,776
Supporting services:		
Fundraising	421,556	403,935
Management and general	149,655	144,223
Total supporting services	571,211	548,158
Total expenses	4,479,601	10,959,934
Change in unrestricted net (deficit) assets	(566,132)	(3,491,631)
Temporarily restricted net assets		
Contributions and grants	34,430	-
Change in temporarily restricted net assets	34,430	-
Change in net (deficit) assets	(531,702)	(3,491,631)
Net (deficit) assets, beginning of year	(1,509,433)	1,982,198
Net deficit, end of year	$ (2,041,135)	$ (1,509,433)

HABITAT FOR HUMANITY METRO MARYLAND, INC.
STATEMENTS OF FUNCTIONAL EXPENSES
Years Ended June 30, 2016 and 2015

2016

	Affordable Residential Housing	ReStore	Grant to Habitat for Humanity, International	Total Program Expenses	Fundraising	Management and General	Total Expenses
Salaries and wages	$ 330,864	$ 574,065	$ -	$ 904,929	$ 281,257	$ 76,573	$ 1,262,759
Cost of home sales	809,048	-	-	809,048	-	-	809,048
Rent	50,827	449,960	-	500,787	18,916	14,011	533,714
Mortgage subsidies	492,726	-	-	492,726	-	-	492,726
Home weatherization	147,993	-	-	147,993	-	-	147,993
Interest	127,333	19,517	-	146,850	-	-	146,850
Critical repair	113,210	-	-	113,210	-	-	113,210
Health benefits	14,285	64,295	-	78,580	13,451	8,613	100,644
Payroll taxes	22,127	47,296	-	69,423	19,966	6,599	95,988
Utilities	9,286	54,171	-	63,457	2,264	2,385	68,106
Professional expenses	2,000	55,339	-	57,339	936	2,076	60,351
Depreciation and amortization	3,229	54,547	-	57,776	897	359	59,032
HFHI tithe expense	-	-	54,996	54,996	-	-	54,996
Printing and publication	5,677	1,859	-	7,536	46,730	-	54,266
Real estate taxes	3,017	49,985	-	53,002	836	335	54,173
Insurance	16,921	31,338	-	48,259	2,232	2,291	52,782
Rent CAM	2,864	46,725	-	49,589	797	318	50,704
Equipment maintanence	7,684	29,659	-	37,343	5,601	4,064	47,008
Miscellaneous	38,553	5,462	-	44,015	1,069	1,434	46,518
Supplies	11,958	21,798	-	33,756	7,200	4,155	45,111
Bank fees	-	25,358	-	25,358	-	3,494	28,852
Advertising	-	24,348	-	24,348	-	-	24,348
Facility maintenance	1,961	20,994	-	22,955	694	667	24,316
Accounting fees	-	-	-	-	-	15,300	15,300
Equipment	475	14,243	-	14,718	475	-	15,193
Inventory pickup	-	12,690	-	12,690	2,345	-	15,035
Travel	7,147	-	-	7,147	6,191	-	13,338
Conference, convention	5,675	2,990	-	8,665	1,705	2,863	13,233
Postage and delivery	1,376	891	-	2,267	5,140	556	7,963
Retirement plan contributions	3,524	2,918	-	6,442	1,859	1,285	9,586
Dues and fees	-	5,800	-	5,800	-	1,275	7,075
Team building	5,208	-	-	5,208	49	-	5,257
Payroll processing	949	1,837	-	2,786	946	1,002	4,734
Volunteers	1,945	-	-	1,945	-	-	1,945
Construction	(2,553)	-	-	(2,553)	-	-	(2,553)
	$ 2,235,309	$ 1,618,085	$ 54,996	$ 3,908,390	$ 421,556	$ 149,655	$ 4,479,601

HABITAT FOR HUMANITY METRO MARYLAND, INC.
STATEMENTS OF FUNCTIONAL EXPENSES
Years Ended June 30, 2016 and 2015

2015

	Affordable Residential Housing	ReStore	Grant to Habitat for Humanity, International	Total Program Expenses	Fundraising	Management and General	Total Expenses
Cost of home sales	$ 5,390,317	$ -	$ -	$ 5,390,317	$ -	$ -	$ 5,390,317
Mortgage subsidies	2,921,186	-	-	2,921,186	-	-	2,921,186
Salaries and wages	315,662	424,068	-	739,730	274,895	84,073	1,098,698
Rent	49,585	354,504	-	404,089	13,798	5,524	423,411
Loan interest	96,225	9,233	-	105,458	-	-	105,458
Home weatherization	104,134	-	-	104,134	-	-	104,134
Payroll taxes	21,895	38,071	-	59,966	22,212	7,117	89,295
Critical repair	85,154	-	-	85,154	-	-	85,154
Utilities	17,811	45,644	-	63,455	5,129	2,421	71,005
Health benefits	15,215	31,171	-	46,386	14,753	7,955	69,094
Insurance	25,229	28,008	-	53,237	2,035	2,129	57,401
Real estate taxes	5,369	44,503	-	49,872	1,489	597	51,958
HFHI tithe expense	-	-	45,229	45,229	-	-	45,229
Equipment maintanence	7,397	30,870	-	38,267	2,959	2,959	44,185
Rent CAM	4,099	38,066	-	42,165	1,138	455	43,758
Supplies	9,586	24,444	-	34,030	4,529	1,784	40,343
Miscellaneous	36,428	3,335	-	39,763	-	21	39,784
Printing and publication	6,141	-	-	6,141	33,241	-	39,382
Bank fees	-	26,483	-	26,483	-	5,137	31,620
Depreciation and amortization	4,260	21,888	-	26,148	1,183	473	27,804
Advertising	-	23,695	-	23,695	-	-	23,695
Conference, convention	9,356	6,593	-	15,949	4,563	2,168	22,680
Facility maintenance	5,439	13,400	-	18,839	2,175	1,088	22,102
Equipment	1,224	18,199	-	19,423	340	136	19,899
Inventory pickup	-	17,140	-	17,140	744	-	17,884
Bad debt	15,539	-	-	15,539	-	-	15,539
Accounting fees	-	-	-	-	-	14,950	14,950
Postage and delivery	1,500	948	-	2,448	10,364	496	13,308
Retirement plan contributions	4,084	2,158	-	6,242	2,469	1,884	10,595
Travel	3,000	-	-	3,000	4,779	-	7,779
Professional expenses	5,000	1,868	-	6,868	-	771	7,639
Volunteers	4,533	-	-	4,533	-	-	4,533
Payroll processing	1,085	1,175	-	2,260	1,085	1,085	4,430
Team building	3,132	-	-	3,132	55	-	3,187
Dues and fees	-	800	-	800	-	1,000	1,800
Vista intern	1,070	-	-	1,070	-	-	1,070
Construction	(10,372)	-	-	(10,372)	-	-	(10,372)
	$ 9,160,283	$ 1,206,264	$ 45,229	$10,411,776	$ 403,935	$ 144,223	$ 10,959,934

HABITAT FOR HUMANITY METRO MARYLAND, INC.
STATEMENTS OF CASH FLOWS
Years Ended June 30, 2016 and 2015

	2016	2015
Cash Flows From Operating Activities:		
Change in net assets	$ (531,702)	$ (3,491,631)
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation and amortization	59,032	27,804
Loss on disposal of property and equipment	7,137	-
Loss on disposal of developed lot inventory	-	108,283
Amortization of deferred gain on sale of homes	(16,373)	(13,607)
Amortization of discount on notes payable	103,827	84,595
Accretion of discount on mortgage notes receivable	(355,146)	(294,172)
Loss on extinguishment of notes payable	8,245	-
Mortgage subsidy recapture	(28,226)	(106,242)
Mortgage subsidies-mortgage discount on homes sold	492,726	2,921,186
Decrease (increase) in operating assets:		
Restricted cash	19,867	75,398
Grants and contracts receivable	6,716	200,430
Inventories	(142,767)	3,969,972
Other assets	(139,046)	(5,755)
(Decrease) increase in operating liabilities:		
Accounts payable and accrued expenses	52,790	(26,340)
Homeowner escrow deposits	(16,643)	(45,456)
Deferred rent	606,159	50,781
Net cash provided by operating activities	126,596	3,455,246
Cash Flows From Investing Activities:		
Issuance of mortgage loans, net of repayments	(322,327)	(4,258,494)
Purchases of property and equipment	(559,128)	(273,399)
Net cash used in investing activities	(881,455)	(4,531,893)
Cash Flows From Financing Activities:		
Proceeds from nonsale transfer of mortgage loans receivable-secured borrowing	255,153	3,609,394
Proceeds from lines of credit, net of repayments	433,767	250,000
Proceeds from notes payable	-	433,302
Repayment of notes payable	(370,957)	(3,689,348)
Net cash provided by financing activities	317,963	603,348
Net decrease in cash and cash equivalents	(436,896)	(473,299)
Cash and cash equivalents at beginning of year	1,095,646	1,568,945
Cash and cash equivalents at end of year	$ 658,750	$ 1,095,646
Supplemental Cash Flow Information:		
Cash paid for interest	$ 43,024	$ 20,862
Noncash financing activities:		
Line of credit converted to note payable	$ 250,000	$ -

See Accompanying Notes to the Financial Statements

NOTE 1 - ORGANIZATION

Habitat for Humanity of Montgomery County Maryland, Inc. (Habitat) is a nonprofit corporation that was formed under the laws of the State of Maryland on October 29, 1982, for the purpose of constructing affordable housing for qualified low-income families. Habitat also has a retail operation that sells donated reusable and surplus building materials to the public. In April 2013, Habitat's Board of Directors approved a resolution to operate as Habitat for Humanity Metro Maryland, Inc., to better represent Habitat's service area which has expanded to one additional county in Maryland.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

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

Basis of Presentation

Habitat complies with the Not-for-Profit Entities Revenue Recognition Subtopic and the Not-For-Profit Entities Presentation of Financial Statements Subtopic of the FASB Accounting Standards Codification. Under the provisions of these standards, net assets and revenues, expenses, gains and losses are classified based on the existence or absence of donor-imposed restrictions. These standards require a statement of financial position, a statement of activities, and a statement of cash flows. Accordingly, the net assets of Habitat and the changes therein, are classified and reported as follows:

Unrestricted net assets – This category is used to record activity that has not been restricted by a donor or funding source.

Temporarily restricted net assets – This classification is used to record contributions that have been specifically restricted by time or purpose of the donor. Restricted contributions are recorded as revenue when the donor has made a gift rather than when the cash is actually received. Once the restriction has been satisfied, a reclassification is made from temporarily restricted net assets to unrestricted net assets.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Basis of Presentation (Continued)

Permanently restricted net assets – This classification is used for net assets subject to donor imposed stipulations that they be maintained permanently by Habitat. There are no permanently restricted net assets at June 30, 2016 and 2015.

Cash and Cash Equivalents

Cash and cash equivalents include cash on hand, cash at bank, money market accounts, and short-term investments purchased with original maturities of three months or less, if any. Cash at bank may, at times, exceed federally insured limits.

Grants and Contracts Receivable

Habitat is funded through various grants, cost reimbursements, and performance-based contracts. Habitat accounts for the grants and contracts as exchange transactions. Revenue is recognized as an increase in the statements of activities assets as stipulated performance is executed, or as expenditures are incurred in accordance with applicable agreements under expenditure reimbursement contracts. A receivable is recorded to the extent grant and contract revenue exceeds payment.

Inventories

Inventories consist of construction-in-progress, developed lots available for construction, and ReStore (thrift store) inventory. Construction-in-progress represents the costs incurred on housing units under construction. Costs include direct material and labor costs and those indirect costs related to construction completion such as indirect labor, fringe benefits, and allocated overhead. Assets are removed from investing to construction-in progress when construction begins. Assets under construction are classified as construction in progress until completed and transferred to the homeowner. Real estate taxes and interest are capitalized during the construction period. Interest included in construction-in-progress at June 30, 2016 and 2015 was $2,581 and $1,289, respectively. ReStore inventory consists of donated building materials and home furnishings that are sold to the public at a discounted price. ReStore inventory is carried at fair value and estimated using historical turnover in lieu of a physical count.

NOTE 2 - <u>SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES</u> (Continued)

<u>Property and Equipment</u>

Property and equipment purchased with a cost basis greater than $1,000 are recorded at cost when acquired and depreciated over three to five years.

<u>Mortgage Loans Receivable</u>

In accordance with accounting principles generally accepted in the United States of America (U.S. GAAP) and the Habitat for Humanity International Accounting Manual, when a house is sold and title transferred to a homeowner, revenue is recorded for the house price and a mortgage loan receivable, discounted to the present value of cash payments to be received over the term of the note (see Note 3), set up. At the same time, construction in progress inventory cost for the house is transferred to program services expense. Habitat obtains a note and deed of trust on the property from the homebuyer. In addition, Habitat retains a second lien on the property in the event the lower of cost or fair market value is greater than the sales price of the home. The homeowner will pay off the second lien to Habitat only if the home is sold prior to paying off the first mortgage. Habitat orders an appraisal of the home when it is completed, and the property cannot have a combined first and second note that is higher than the appraised value. Habitat also retains an equity interest in property. If the home is sold in years 1 through 5, Habitat retains a 100% equity interest. Habitat's equity interest is reduced by 3% each succeeding year to maturity. The mortgage note receivable is reduced by monthly payments made by the homebuyer, usually over a 20 to 30 year period. Habitat has a collection policy in force, which requires collection action at a regular interval beginning with 15 days delinquency. Defaults over 90 days are subject to possible foreclosure if the default is not cured. At June 30, 2016 and 2015, no amounts were more than 90 days delinquent.

<u>Deferred Gain on Home Sales</u>

Habitat accounts for home sales in accordance with the provisions of the Real Estate Sales Subtopic of the FASB Accounting Standards Codification. Losses on the sale of homes are recognized as they are incurred, but gains are deferred and credited to earnings over the life of the mortgage notes receivable using the installment sale method, which apportions each cash receipt and principal payment by the buyer on debt assumed between cost recovered and profit. The apportionment is in the same ratio as total cost and total profit bear to the sales value.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Contributions, Grants and Contracts

All contributions, grants and contracts to Habitat are considered to be available for unrestricted use in the year received, unless specifically restricted by the donor. Amounts received that are designated for future periods or that are restricted by the donor for specific purposes, if any, are reported as temporarily restricted or permanently restricted support that increases those net asset classes. If a restriction is fulfilled in the same period in which the donation was received, the amount is reported as unrestricted. If conditional promises to give are received, those contributions are recorded as the conditions are met.

Habitat also operates a ReStore operation which re-sells donated furniture and household appliances and materials. Revenue and expenses are recognized at the time merchandise is transferred to the customer. Sales returns have not been significant.

In-Kind Contributions

Habitat receives donations of land, products, and services from individual and corporate donors. These contributions are recorded at their estimated fair market value at their date of donation.

Contributions of services are recognized in the financial statements if the services enhance or create non-financial assets or require specialized skills, are provided by individuals possessing those skills, and would typically need to be purchased if not provided by donation. Otherwise, volunteer services are not recorded in the financial statements as these contributions do not meet the requirements to be recorded as revenue and expense.

Allocation of Costs

The cost of providing the various programs and other activities have been summarized on a functional basis in the statements of activities. Accordingly, certain costs have been allocated among the programs benefited.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Sales Tax

The State imposes a sales tax of 6% on all of Habitat's sales to non-exempt customers. Habitat collects that sales tax from customers and remits the entire amount to the State. Habitat's policy is to report sales net of sales tax.

Advertising

Habitat expenses the costs of advertising as they are incurred.

Income Taxes

Habitat is exempt from Federal income taxes through the group exemption of Habitat for Humanity International under Section 501(c)(3) of the Internal Revenue Code.

Habitat's tax returns are subject to audit for three years after filling, hence Habitat's returns for tax years 2012 onwards are open to tax examination.

Evaluation of Subsequent Events

Management has evaluated the financial statements for subsequent events requiring accrual or disclosure through November 2, 2016, which is the date the financial statements were available to be issued.

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NOTE 3 - MORTGAGE LOANS RECEIVABLE

For each property sold, Habitat lends money to the homebuyer at a below-market interest rate (generally zero percent). The receivable is recorded at the face value and discounted to reflect the present value of the receivable using rates between 7.7% and 8.48% based upon guidelines established by Habitat for Humanity International. The amount of the discount is charged to program expenses when the mortgage loans are issued. The amount of discount charged to program expenses in 2016 and 2015 was $492,726 and $2,921,186, respectively. The discount is accreted to income over the life of the note. The amount of discount accredited to income in 2016 and 2015 was $355,146 and $294,172, respectively. Mortgage loans receivable at June 30, 2016 and 2015 consist of the following:

	2016	2015
Mortgage loans receivable	$ 10,902,451	$ 10,580,124
Less: mortgage discount	(6,159,551)	(6,050,197)
	$ 4,742,900	$ 4,529,927

Habitat transfers mortgage loans receivable to financial institutions in accordance with the Transfer and Servicing Topic of the FASB Accounting Standards Codification, under separate transfer and servicing agreements. As of June 30, 2016, Habitat had transferred forty five mortgage loans receivable. As of June 30, 2015, Habitat had transferred forty four mortgage loans receivable. All mortgage loans receivable were transferred with full recourse at present value. Under the terms of the agreements, Habitat continues to service these loans and remits payments to the transferees. Habitat retains full responsibility for defaults or delinquencies. Accordingly, the transfers are accounted for as a secured borrowing. As of June 30, 2016, total recourse mortgage loans receivable have a face and present value of $7,600,520 and $1,401,283, respectively. As of June 30, 2015, total recourse mortgage loans receivable have a face and present value of $7,569,533 and $1,436,525, respectively.

NOTE 4 - INVENTORIES

Inventories consist of the following components at June 30:

	2016	2015
Homes under construction or renovation	$ 379,930	$ 242,901
ReStore inventory	190,621	184,883
	$ 570,551	$ 427,784

NOTE 5 - PROPERTY AND EQUIPMENT

Property and equipment consist of the following at June 30:

	2016	2015
Equipment-contruction	$ 7,064	$ 7,064
Equipment-office	55,372	59,784
ReStore leasehold improvements	856,195	310,004
Vehicles	76,541	76,541
Leashold improvements	21,489	16,532
	1,016,661	469,925
Accumulated depreciation and amortization	(226,617)	(172,840)
	$ 790,044	$ 297,085

Depreciation and amortization expense for the years ended June 30, 2016 and 2015 was $59,032 and $27,804, respectively.

NOTE 6 - LOANS, LINES OF CREDIT AND COMMITMENTS

Notes Payable

On January 6, 2003, Habitat entered into an agreement with OBA Federal Savings Bank (First National Bank) (Note A) for four separate notes payable of $80,000 each, totaling $320,000. The notes are collateralized by the homes funded by those notes payable. Each note payable matures on October 1, 2023, carries a zero interest rate, and is repayable in 240 equal monthly payments of approximately $333. During 2016, Habitat repaid one of these notes payable in full. The principal balance outstanding on these notes at June 30, 2016 and 2015 was $88,811 and $134,547, respectively. At June 30, 2016 and 2015, these notes payable are included in the statements of financial position at discounted values of approximately $69,850 and $102,544, respectively, which represent the present value of the remaining monthly payments at the statement of financial position date. Interest expense imputed on these notes for years ended June 30, 2016 and 2015 payable was $4,797 and $6,986, respectively.

On December 1, 2010, Habitat entered into an agreement with OBA Federal Savings Bank (First National Bank) (Note B) for a note payable of $215,000. The note is collateralized by four properties constructed in Burtonsville, Maryland. This note payable matures on December 1, 2040 and carries a fixed interest rate of 5.5%. Payments of $1,231 are due monthly. The principal balance outstanding on this note at June 30, 2016 and 2015 was $196,963 and $200,727, respectively.

In March 2012, Habitat obtained a construction credit facility, which allows for draws up to $3,450,000 with OBA Bank (Note C). Outstanding balance accrues interest at the greater of 1% above the Prime Index (3.5% at June 30, 2016) or 5%. Interest only payments are due on the first of each month with principal and accrued interest due in full on March 12, 2015. This note was paid in full and terminated in November 2014 in connection with the transfer of mortgage loans discussed in Note 3.

NOTE 6 - LOANS, LINES OF CREDIT AND COMMITMENTS (Continued)

Secured Borrowing—Nonsale Transfer of Mortgage Loans Receivable

As discussed in Note 3, Habitat services a total of forty five mortgage loans receivable that were transferred with full recourse to three financial institutions (Note C). Under the terms of transfer and servicing agreements, Habitat collects and remits the homeowners mortgage payments to each financial institution, retaining full responsibility for any defaults or delinquencies. Under the Transfers and Servicing Topic of FASB Accounting Standards Codification, the transfer is accounted for as a secured borrowing and included in notes payable in the accompanying statements of financial position. The present value of these transferred mortgage loans receivable at June 30, 2016 and 2015 was $6,199,237 and $6,133,008, respectively.

Habitat maintained a $250,000 line of credit with First National Bank. In October 2015, the outstanding balance on this line of credit ($250,000) was converted into a 5 year amortizing note payable (Note D). The note requires monthly installments of $4,726 and charges interest at 5%. The loan matures in 2020. The principal outstanding on this note payable was $216,497 at June 30, 2016.

Future principal payments of notes payable and transferred mortgage loans for fiscal years ending June 30 are as follows:

	Note A	Note B	Note C	Note D	Total
2017	$ 7,686	$ 3,839	$ 195,273	$ 46,760	$ 253,558
2018	8,200	4,060	198,455	49,201	259,916
2019	8,750	4,293	201,688	51,770	266,501
2020	9,336	4,540	204,972	54,473	273,321
2021	9,961	4,800	208,312	14,293	237,366
Thereafter	25,917	175,431	5,190,537	-	5,391,885
	$ 69,850	$ 196,963	$ 6,199,237	$ 216,497	$ 6,682,547

NOTE 6 - LOANS, LINES OF CREDIT AND COMMITMENTS (Continued)

Lines of Credit

Habitat has a $150,000 line of credit with Sandy Spring Bank. Loan terms are 1% under the Prime Index (3.5% at June 30, 2016). Interest only payments are due on the first of each month with principal and accrued interest due on November 1st, annually, on which date the line of credit is renewable. There was no outstanding balance at June 30, 2016 and 2015.

Habitat has a $200,000 line of credit with Eagle Bank. Loan terms are the greater of 1% above the Prime Index (3.5% at June 30, 2016) or 5%. Interest only payments are due on the first of each month with principal and accrued interest due on November 1st, annually, on which date the line of credit is renewable. There was no outstanding balance at June 30, 2016 and 2015.

During 2016, Habitat executed a $250,000 line of credit with United Bank. Interest is fixed the current average weekly yield on five year U.S. Treasury Securities plus 2.75% (1.64% at June 30, 2016). The line of credit requires month payment of interest only for the first twelve months after execution of the line of credit. Following the interest only period, any outstanding borrowings will be converted to an amortizing note payable over a five year period. The Outstanding balance on this line of credit at June 30, 2016 was $250,000.

During 2016, Habitat executed a $500,000 line of credit with Old Line Bank. Loan terms are the greater of .5% above the Prime Index (3.5% at June 30, 2016) or 4.5%. Interest-only payments are due each month. The line of credit renews annually. Outstanding principal is due on due at maturity (March, 2017). However, Habitat anticipates that an additional one year renewal will be granted by Old Line Bank upon Maturity The Outstanding balance on this line of credit at June 30, 2016 was $183,767.

NOTE 6 - LOANS, LINES OF CREDIT AND COMMITMENTS (Continued)

Lease Commitments

In October 2015, Habitat entered into a lease for 22,125 square feet of retail space in Rockville, Maryland. The space will be used to facilitate Habitat's Rockville Maryland ReStore location. The lease commenced November 2015. The lease is a ten-year operating lease with a monthly base rent of $20,742, which is subject to an annual 2.5% increase. Terms of the agreement provide a rent abatement for an eight month period beginning November 2015. In addition, Habitat received a $442,500 improvement allowance. Rent adjustments, abatement, and the improvement allowance are recognized as an adjustment to rent expense on a straight-line basis over the lease term.

In March 2014, Habitat entered into a lease for 15,000 square feet of retail space in Silver Spring, Maryland. The space will be used to facilitate a second ReStore location in Silver Spring, Maryland. The lease commenced August 2014. The lease is a ten-year operating lease with a monthly base rent of $17,070, which is subject to an annual 2.5% increase. Terms of the agreement provide a rent abatement for the months of September, October and November 2014. In addition, Habitat received a $200,000 improvement allowance. Rent adjustments, abatement, and the improvement allowance are recognized as an adjustment to rent expense on a straight-line basis over the lease term.

In February 2016, Habitat entered into a lease for office space in Silver Spring, Maryland. The lease commenced February 2016. The lease is for a period of ten years and six months. The lease requires monthly base rent of $9,561, which is subject to an annual 2.5% increase. Terms of the agreement provide a 50% rent abatement for the first twelve months of occupancy. Rent abatements are recognized as an adjustment to rent expense on a straight-line basis over the lease term.

On November 1, 2005, Habitat entered into a lease for 15,965 square feet of retail and office space. This is a ten-year operating lease with a monthly base rent of $15,300 and an annual escalation of 3% on each anniversary date. Habitat pays its portion of real-estate taxes and common area maintenance fees on a pro-rata basis. This was terminated January 2016.

NOTE 6 - <u>LOANS, LINES OF CREDIT AND COMMITMENTS</u> (Continued)

<u>Lease Commitments</u> (Continued)

Future minimum payments required under the lease are as follows:

<u>Year ending June 30:</u>

2017	$	541,133
2018		583,818
2019		598,419
2020		613,370
2021		628,709
Thereafter		2,903,136
	$	5,868,585

Total rent expense for the year ended June 30, 2016 and 2015 was $533,714 and $423,411, respectively.

NOTE 7 - <u>IN-KIND CONTRIBUTIONS</u>

During the years ended June 30, 2016 and 2015, Habitat received in-kind contributions in the form of labor, materials and services valued at $11,215 and $74,542, which reflect the fair market value of similar materials and services. These in-kind donations appear as part of contribution revenue in the statements of activities.

NOTE 8 - <u>RELATED PARTY TRANSACTIONS</u>

Habitat is an affiliate of Habitat for Humanity International (HFHI), who works as a partner with HFHI for the purpose of accomplishing their mission to construct affordable housing for qualified low-income families. Although HFHI assists Habitat with information resources, training, publications, and in other ways, the Habitat is primarily and directly responsible for the legal, organizational, fundraising, family selection and nurture, financial and construction aspects of the work. In recognition of and commitment to the global partnership that exists with Habitat for Humanity, the affiliate is expected to contribute a tithe to HFHI based on 10 percent of various unrestricted revenue items. The international tithe expense paid to HFHI for the years ended June 30, 2016 and 2015 was $54,996 and $45,229, respectively.

NOTE 9 - <u>RETIREMENT PLAN</u>

Habitat has a defined contribution plan in which all employees at least 21 years of age are eligible to participate. Employees may enter the plan after three consecutive calendar months of employment in which the individual is credited with at least 83-1/3 hours of service per month. Employees are 100% vested in voluntary contributions. Habitat may make a matching contribution, which is determined annually by the Board of Directors. Matching contributions are vested after 36 months of service. Habitat's contributions to the plan for the years ended June 30, 2016 and 2015 totaled $9,586 and $10,595, respectively.