

HABITAT FOR HUMANITY OF ORANGE COUNTY, INC.  
(A NON-PROFIT ORGANIZATION)

FINANCIAL STATEMENTS WITH  
INDEPENDENT AUDITORS' REPORT

June 30, 2015 and 2014

HABITAT FOR HUMANITY OF ORANGE COUNTY, INC.

June 30, 2015 and 2014

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## INDEPENDENT AUDITORS' REPORT

To the Board of Directors  
Habitat for Humanity of Orange County, Inc.  
Santa Ana, California

We have audited the accompanying financial statements of Habitat for Humanity of Orange County, Inc. (the Organization), which comprise the statements of financial position as of June 30, 2015 and 2014, and the related statements of activities 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.

### *Auditor's 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 auditor's 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 auditor considers 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 of Orange County, Inc. as of June 30, 2015 and 2014, 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.

*Ronald Blue & Co.  
CPAs and Consultants, LLP*

Santa Ana, California  
November 11, 2015

HABITAT FOR HUMANITY OF ORANGE COUNTY, INC.

STATEMENTS OF FINANCIAL POSITION

June 30, 2015 and 2014

	2015	2014
<b>Assets</b>		
Cash and cash equivalents	\$ 995,959	\$ 1,581,239
Cash and cash equivalents - restricted	928,344	898,374
Promises to give	474,128	245,834
Other receivable	176,536	282,273
Inventory - Homes for sale	4,674,859	1,344,858
Inventory - ReStores	162,787	199,989
Prepaid expenses and deposits	122,573	165,672
Housing assets, at net realizable value	6,348,498	7,656,580
Investment in joint venture - HFHI-SA Leverage VI, LLC (Note 4)	5,748,407	5,808,816
Mortgages receivable, net of unamortized discount	4,468,371	4,257,973
Property and equipment, net	104,302	128,319
Loan costs - joint venture, net	83,828	106,357
	<u>                    </u>	<u>                    </u>
Total assets	<u>\$ 24,288,592</u>	<u>\$ 22,676,284</u>
<b>Liabilities</b>		
Accounts payable and accrued expenses	\$ 804,372	\$ 998,407
Property tax and insurance impounds	124,392	115,399
Deferred mortgage receipts	201,372	146,441
Security deposits	45,771	35,111
Notes payable	5,637,254	4,660,616
Long-term debt - Clearinghouse NMTC (Sub 21), LLC (Note 10)	7,883,619	7,883,619
	<u>                    </u>	<u>                    </u>
Total liabilities	<u>14,696,780</u>	<u>13,839,593</u>
<b>Net assets</b>		
Unrestricted	8,797,820	7,600,081
Temporarily restricted	793,992	1,236,610
	<u>                    </u>	<u>                    </u>
Total net assets	<u>9,591,812</u>	<u>8,836,691</u>
	<u>                    </u>	<u>                    </u>
Total liabilities and net assets	<u>\$ 24,288,592</u>	<u>\$ 22,676,284</u>

See accompanying notes and independent auditors' report

HABITAT FOR HUMANITY OF ORANGE COUNTY, INC.

STATEMENTS OF ACTIVITIES

For the Years Ended June 30, 2015 and 2014

	2015	2014
<b>Unrestricted net assets</b>		
Support and revenue		
Contributions	\$ 739,776	\$ 840,337
Donated materials and services	150,427	194,992
Interest income	423,049	252,041
Rental income	93,505	79,710
ReStore revenues	2,050,033	1,867,169
Special events revenues	867,035	522,998
Other income	19,567	33,570
	<hr/>	<hr/>
Total unrestricted support and revenues	4,343,392	3,790,817
Net assets released from restrictions	1,702,149	2,242,988
	<hr/>	<hr/>
Total unrestricted support, revenues and reclassifications	6,045,541	6,033,805
	<hr/>	<hr/>
<b>Expenses</b>		
Program services:		
Construction costs	8,297,590	6,312,507
Construction costs - joint venture	171,317	211,556
ReStore expenses	1,843,551	1,996,579
Special events	78,974	49,752
Public relations	217,780	166,676
Faith relations	22,074	22,406
Family relations	280,111	260,189
Rental expenses	57,733	37,404
Contributions to Habitat for Humanity International	41,462	61,640
Costs in excess of estimated sales price	541,006	1,349,993
Less costs capitalized as housing assets	(7,662,336)	(5,862,361)
	<hr/>	<hr/>
Total program services	3,889,262	4,606,341
	<hr/>	<hr/>

See accompanying notes and independent auditors' report

HABITAT FOR HUMANITY OF ORANGE COUNTY, INC.

STATEMENTS OF ACTIVITIES (continued)  
For the Years Ended June 30, 2015 and 2014

	2015	2014
<b>Unrestricted net assets (continued)</b>		
Supporting services:		
General and administrative	462,891	403,727
Fundraising	495,649	417,323
	<u>958,540</u>	<u>821,050</u>
Total supporting services		
	<u>958,540</u>	<u>821,050</u>
Total expenses	4,847,802	5,427,391
	<u>4,847,802</u>	<u>5,427,391</u>
Change in unrestricted net assets	1,197,739	606,414
	<u>1,197,739</u>	<u>606,414</u>
<b>Temporarily restricted net assets</b>		
Contributions	1,060,380	1,632,125
Donated materials and services	199,151	183,945
Donated land	-	955,940
Net assets released from restrictions	(1,702,149)	(2,242,988)
	<u>(1,702,149)</u>	<u>(2,242,988)</u>
Change in temporarily restricted net assets	(442,618)	529,022
	<u>(442,618)</u>	<u>529,022</u>
Change in net assets	755,121	1,135,436
	<u>755,121</u>	<u>1,135,436</u>
<b>Net assets, beginning of year</b>	8,836,691	7,701,255
	<u>8,836,691</u>	<u>7,701,255</u>
<b>Net assets, end of year</b>	<u>\$ 9,591,812</u>	<u>\$ 8,836,691</u>

See accompanying notes and independent auditors' report

HABITAT FOR HUMANITY OF ORANGE COUNTY, INC.

STATEMENTS OF CASH FLOWS

For the Years Ended June 30, 2015 and 2014

	2015	2014
<b>Cash flows from operating activities</b>		
Change in net assets	\$ 755,121	\$ 1,135,436
Adjustments to reconcile change in net assets to net cash flows from operating activities:		
Depreciation and amortization	46,548	51,220
Changes in:		
Promises to give	(228,294)	10,588
Other receivable	105,737	(243,830)
Inventory - Homes for sale	(3,330,001)	(295,949)
Inventory - ReStores	37,202	23,608
Prepaid expenses and deposits	43,099	73,717
Housing assets	1,308,082	(2,439,266)
Acquisition of mortgages receivable	(271,710)	(338,744)
Payments on mortgages receivable	380,436	369,358
Discounts on mortgage receivable	(264,094)	(76,818)
Buybacks of mortgages	(55,030)	180,186
Accounts payable and accrued expenses	(194,036)	315,516
Property tax and insurance impounds	8,993	10,633
Deferred mortgage receipts	54,931	34,269
Security deposits	10,660	1,989
	<u>(1,592,356)</u>	<u>(1,188,087)</u>
<b>Net cash from operating activities</b>		
<b>Cash flows from investing activities</b>		
Distributions from joint venture	60,409	60,409
Purchase of property and equipment	<u>-</u>	<u>(51,908)</u>
<b>Net cash from investing activities</b>	<u>60,409</u>	<u>8,501</u>

See accompanying notes and independent auditors' report

HABITAT FOR HUMANITY OF ORANGE COUNTY, INC.

STATEMENTS OF CASH FLOWS (continued)  
For the Years Ended June 30, 2015 and 2014

	2015	2014
<b>Cash flows from financing activities</b>		
Loan proceeds	1,674,144	2,447,234
Loan principal payments	<u>(697,507)</u>	<u>(1,449,802)</u>
Net cash from financing activities	<u>976,637</u>	<u>997,432</u>
Net change in cash and cash equivalents	(555,310)	(182,154)
<b>Cash and cash equivalents, beginning of year</b>	<u>2,479,613</u>	<u>2,661,767</u>
<b>Cash and cash equivalents, end of year</b>	<u>\$ 1,924,303</u>	<u>\$ 2,479,613</u>

See accompanying notes and independent auditors' report

## HABITAT FOR HUMANITY OF ORANGE COUNTY, INC.

### NOTES TO FINANCIAL STATEMENTS

June 30, 2015 and 2014

#### Note 1 – Summary of significant accounting policies

This summary of significant accounting policies is presented to assist in understanding the accompanying financial statements. The financial statements and notes are the representations of Habitat for Humanity of Orange County, Inc.'s management, which is responsible for their integrity and objectivity. These accounting policies conform to generally accepted accounting policies and have been consistently applied in the preparation of the financial statements.

##### Nature of activities

Habitat for Humanity of Orange County, Inc. (the Organization) is a non-profit corporation under Section 501(c)(3) of the Internal Revenue Code and was incorporated on January 26, 1988, under the laws of the State of California. The Organization is an ecumenical grass-roots Christian ministry whose purpose is to transform lives and communities by helping families in need build and purchase or renovate their own homes. The Organization aims to accomplish its purpose through privately operated and financed programs to sell such housing to low-income families at cost, utilizing non-interest bearing instruments.

The Organization builds new homes and rehabilitates properties repurchased by the Organization to ready them for resale; homes owned by qualifying families; and buildings owned by other non-profits to help them accomplish their mission in a more cost effective manner.

Prior to the dissolution of the Redevelopment Agencies in California in 2012, public land was donated to the Organization. Generally land is secured by debt payable to the purveyor of the land. In many cases, this debt is non-interest bearing and no principal payments are required. The debt is then reconveyed to the Organization upon the successful sale of the home to a qualified buyer as defined in the Disposition and Development Agreement with the purveyor. June 2014 was the first time the Organization had to purchase land.

Debt is also incurred to meet construction commitments, but only to the extent these can be repaid via mortgages from the sales of homes.

Fourteen (14) homes are under construction as of the year ended June 30, 2015. Fourteen (14) more were completed and being readied for sale. During the year ended June 30, 2015, the Organization sold four homes (two new construction and two resales of homes purchased from the prior Habitat family), and has sold 179 newly constructed homes since inception. Additionally, one home was repurchased and has been prepared for resale to another qualifying family. By serving families, the Organization has changed 977 lives since inception. Fourteen homes (14) were rehabilitated in the year ended June 30, 2015. Twelve of these were for Veterans as part of a Veteran Home Repair Program. The Organization has also funded the building of 420 homes worldwide as of June 30, 2015 and it currently tithes to the Habitat affiliates in Nicaragua and Macedonia.

# HABITAT FOR HUMANITY OF ORANGE COUNTY, INC.

## NOTES TO FINANCIAL STATEMENTS

June 30, 2015 and 2014

### Note 1 – Summary of significant accounting policies (continued)

The Organization also operates two ReStore retail outlets that sell predominantly donated materials to the public. ReStore revenue comprises approximately 37% and 30% of total revenue for the years ended June 30, 2015 and 2014, respectively. Purchased product represents approximately 9% and 7% of total retail sales for the years ended June 30, 2015 and 2014, respectively. In 2014, the Organization incurred approximately \$15,000 of costs to close one ReStore facility, and approximately \$99,000 of costs to re-open in a comparably sized retail facility.

#### Basis of accounting

The financial statements of the Organization have been prepared on the accrual basis of accounting and, accordingly, reflect all significant receivables, payables and other liabilities.

#### Basis of presentation

The Organization reports 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. At June 30, 2015 and 2014, there were no net assets or activities classified as permanently restricted net assets.

#### Use of estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from these estimates.

#### Cash and cash equivalents

For the purposes of the statements of cash flows, the Organization considers all temporary cash investments purchased with a maturity of three months or less to be cash equivalents.

#### Concentration of credit risk

The Organization maintains its cash deposit accounts at various commercial banks located in Southern California. Cash accounts at banks are insured by the Federal Deposit Insurance Corporation (FDIC) up to \$250,000. The balances in these accounts may, at times, exceed federally insured limits. Management believes the Organization is not exposed to any significant risk in connection with cash accounts.

#### Promises to give

Unconditional promises to give are recognized as support and revenues or gains in the period promised and as assets, decreases of liabilities, or expenses depending on the form of the benefits to be received.

## HABITAT FOR HUMANITY OF ORANGE COUNTY, INC.

### NOTES TO FINANCIAL STATEMENTS

June 30, 2015 and 2014

#### Note 1 – Summary of significant accounting policies (continued)

##### Other receivable

Other receivable consists of miscellaneous items related to properties. As of June 30, 2015 and 2014, this includes a grant receivable of \$153,500 and \$243,499, respectively.

##### Inventory - ReStores

The Organization operates two ReStore retail outlets, which are located in Santa Ana and Anaheim, that sell predominantly donated materials to the public. Donated inventories on hand at year end are valued at estimated fair market value. Purchased inventories are valued at the lower of cost or market.

##### Mortgages receivable

Mortgages receivable are non-interest bearing and exchanged for homes to low-income families, fulfilling the Organization's exempt purposes. The notes are recorded at their present value based on the prevailing market rate of interest at the time the mortgage was originated. Prevailing market rates are determined annually based on current mortgage interest rates offered by our banking partners. The difference between the face amount of the note and its present value is accounted for as a discount and recorded as a reduction in the receivable. The resulting discount is amortized over the life of the mortgage using the interest method. Amortization of the discount is recognized as interest income in the statements of activities. Also see Note 5.

##### Housing assets

Housing assets represent amounts expended for the construction of new or refurbished homes and include costs of construction, donated materials and donated land. Housing assets are recorded at cost if materials are purchased, and at estimated fair market value if donated.

The Organization constructs housing for sale to low income families. In furtherance of this purpose a substantial amount of the cost of housing assets is not passed on to the homeowners but absorbed by the Organization. When the sales price of homes can be reasonably estimated, housing assets are reduced to their net realizable value. The reduction in these housing assets is recorded as "costs in excess of estimated sales price" in the statements of activities.

##### Property and equipment

All acquisitions of property and equipment in excess of \$2,000 and all expenditures in excess of \$2,000 for repairs, maintenance, and renewals that materially prolong the useful lives of assets are capitalized. Property and equipment is carried at cost, or, if donated, at the approximate market value at the date of donation. Depreciation is computed over the estimated useful lives of the assets on a straight-line basis. Depreciation expense for the years ended June 30, 2015 and 2014, was \$24,017 and \$28,692, respectively.

## HABITAT FOR HUMANITY OF ORANGE COUNTY, INC.

### NOTES TO FINANCIAL STATEMENTS

June 30, 2015 and 2014

#### Note 1 – Summary of significant accounting policies (continued)

##### Loan costs

Amortization is computed over the life of the loan on a straight-line basis. Amortization expense for the years ended June 30, 2015 and 2014, was \$22,528 and \$22,528, respectively

##### Deferred mortgage receipts / rental income

At various times approved homeowners reside in homes which have not closed escrow. From the rental payments received from these homeowners, the Organization designates a portion of these rents to be applied to the homeowners' mortgages once escrow closes.

##### Revenue recognition

Contributions received are recorded as unrestricted, temporarily restricted, or permanently restricted net assets depending on the existence or nature of any donor restrictions. All donor-restricted net assets are reported as an increase in temporarily restricted or permanently restricted net assets depending on the nature of the restriction. When a restriction expires (that is, when a stipulated time restriction ends or purpose restriction is accomplished), temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statements of activities as net assets released from restrictions. During the years ended June 30, 2015 and 2014, there were no contributions received that were classified as permanently restricted.

##### Donated services

Donated services are recognized as contributions if the services (a) create or enhance nonfinancial assets or (b) require specialized skills, are performed by people with those skills, and would otherwise be purchased by the Organization. Numerous volunteers provided many services throughout the year that are not recognized as contributions in the financial statements since the criteria for recognition are not met. Donated services are recognized as revenues in the period received and as assets or expenses depending on the services performed.

##### Donated materials

Donated materials and other non-monetary items are reflected as contributions in the accompanying statements at their estimated fair market values as of the date of receipt.

##### Reclassifications

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

HABITAT FOR HUMANITY OF ORANGE COUNTY, INC.

NOTES TO FINANCIAL STATEMENTS

June 30, 2015 and 2014

**Note 1 – Summary of significant accounting policies (continued)**

Functional allocation of expenses

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

An additional program service is costs in excess of estimated sales price. This includes the cost of offering a zero percent interest loan to families, actual costs incurred in excess of the sales price, donated land, and donated services.

Income taxes

The Organization is exempt from Federal and California income tax under Internal Revenue Code Section 501(c)(3). The Organization is subject, however, to Federal and California income tax on unrelated business income as stipulated in Internal Revenue Code Section 511 and Regulation Section 1.511. During the years ended June 30, 2015 and 2014, the Organization had revenue from the sale of purchased goods in the ReStores, which constitutes unrelated business income. However, since purchased product represents approximately 9% and 7% of total retail sales for the years ended June 30, 2015 and 2014, respectively, and the applicable expenses of the activity exceeded the income from the activity, the Organization did not have unrelated business taxable income, and therefore incurred no tax liability due to unrelated business income.

The Organization does not believe its financial statements include (or reflect) any uncertain tax positions.

**Note 2 – Restricted cash**

Restricted cash consists of amounts held for legal or contract compliance and amounts reserved for homeowner impounds and delinquencies.

**Note 3 – Promises to give**

Promises to give may include restricted and unrestricted pledges. Restricted pledges are generally restricted to payment for the costs of construction for several projects.

Since March 2012, the organization held an annual five year unrestricted pledge program. These unrestricted and unconditional promises to give have had over two years of collection history. The unrestricted promises to give as of June 30, 2015 and 2014 include current portions of \$166,756 and \$106,036, respectively and long-term portions of \$307,372 and \$139,798, respectively.

HABITAT FOR HUMANITY OF ORANGE COUNTY, INC.

NOTES TO FINANCIAL STATEMENTS

June 30, 2015 and 2014

**Note 4 – Investment in joint venture - HFHI-SA Leverage VI, LLC**

In July 2010, the Organization participated in a New Markets Tax Credit (NMTC) program. This Federal program provides 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 (sub-CDE). Tax credit recapture is required if compliance requirements are not met over a seven-year period.

This NMTC program included a consortium of California Habitat affiliates. In July 2010 the Organization recorded its 32.178% investment in HFHI-SA Leverage VI, LLC at the initial cost of \$6,040,887, of which all funds were ultimately invested in the sub-CDE. A promissory note is payable to Clearinghouse NMTC (Sub 21), LLC (the sub-CDE) for funds loaned back to the Organization. See Note 10.

The resulting benefit of the Organization’s participation in the NMTC program was \$1,100,000 in cash proceeds used to build homes: \$750,000 to build 26 homes and \$350,000 to build 4 homes in San Juan Capistrano and Fullerton, respectively.

In July, 2017, Habitat California Investment Fund LLC (the Fund), the effective upstream owner of Clearinghouse NMTC (Sub 21), LLC (the sub-CDE), holder of the promissory note due from the Organization, is expected to exercise its put option. Under the terms of the put option agreement, HFHI-SA Leverage VI, LLC is expected to purchase the ownership interest of the Fund. Exercise of the option will effectively allow the Organization to extinguish its outstanding debt owed to the Fund. See Note 10.

The balance of the investment in HFHI-SA Leverage VI, LLC as of June 30, is as follows:

	2015	2014
Beginning balance	\$ 5,808,816	\$ 5,869,225
Distributions	<u>(60,409)</u>	<u>(60,409)</u>
Ending balance	<u>\$ 5,748,407</u>	<u>\$ 5,808,816</u>

HABITAT FOR HUMANITY OF ORANGE COUNTY, INC.

NOTES TO FINANCIAL STATEMENTS

June 30, 2015 and 2014

**Note 5 – Mortgages receivable**

In general, mortgages receivable carry imputed interest rates between 4.5% and 8.0% and are presented in the accompanying statements of financial position net of unamortized discount. The face amount and unamortized discount of mortgages receivable as of June 30, 2015 and 2014, were \$9,409,576 and \$9,470,748, respectively. Imputed interest rates for June 30, 2015 and 2014, ranged from 4.5% to 5.0%. Interest income resulting from the amortization of discounted notes for the years ended June 30, 2015 and 2014 totaled \$423,024 and \$251,913, respectively.

Certain mortgages have been pledged as collateral under financing agreements with Habitat for Humanity International and California Bank and Trust (See Note 8). As of June 30, 2015 and 2014, the amount of receivables pledged (at face value) in connection with specific loan agreements are shown in the table below. On the statements of financial position, these same non-interest bearing mortgages are included net of discounts. In the table below, the payment streams represent cash paid out by the Organization to the specified lenders and cash received by the Organization from mortgage payments from homeowners related to the collateralized Habitat mortgages.

<u>Lender</u>	<u>Loan name</u>	<u>Payment streams</u>		<u>Balance of mortgages receivable pledged</u>	
		<u>Paid out</u>	<u>Receipts</u>	<u>2015</u>	<u>2014</u>
Habitat for Humanity International	AAR 2007	\$ 13,110	\$ 15,043	\$ -	\$ 593,769
	FlexCap 2009	25,462	24,485	<u>720,034</u>	<u>741,881</u>
	Subtotal			720,034	1,335,650
California Bank & Trust	2011 - 15 yr	61,743	61,743	1,928,682	1,995,347
California Bank & Trust	2014 - 7 yr	35,009	35,009	346,446	-
California Bank & Trust	2014 - 15 yr	30,215	30,215	<u>632,578</u>	<u>-</u>
Total mortgages receivable pledged				<u>\$ 3,627,740</u>	<u>\$ 3,330,997</u>

These agreements are also subject to certain guarantees and may contain substitution requirements or options. See Note 15.

HABITAT FOR HUMANITY OF ORANGE COUNTY, INC.

NOTES TO FINANCIAL STATEMENTS

June 30, 2015 and 2014

**Note 6 – Property and equipment**

A summary of property and equipment follows:	2015	2014
Equipment	\$ 308,099	308,099
Automobiles	145,224	145,224
Improvements	<u>80,743</u>	<u>80,743</u>
Total property and equipment	534,066	534,066
Less: accumulated depreciation	<u>(429,764)</u>	<u>(405,747)</u>
Property and equipment, net	<u>\$ 104,302</u>	<u>\$ 128,319</u>

**Note 7 – Loan costs – joint venture**

A summary of loan costs follows:	2015	2014
Closing costs	\$ 69,178	\$ 69,178
Guarantor fee	<u>125,415</u>	<u>125,415</u>
Total loan costs	194,593	194,593
Less: accumulated amortization	<u>(110,765)</u>	<u>(88,236)</u>
Loan costs, net	<u>\$ 83,828</u>	<u>\$ 106,357</u>

**Note 8 – Notes payable**

Notes payable at June 30, 2015 and 2014, was comprised of the following:	2015	2014
Loan payable dated November 9, 2007, to Habitat for Humanity International, collateralized by mortgages receivable, with principal and interest at an annual rate of 4.0% payable in quarterly installments of \$6,555 through December 31, 2014.	\$ -	12,916

HABITAT FOR HUMANITY OF ORANGE COUNTY, INC.

NOTES TO FINANCIAL STATEMENTS

June 30, 2015 and 2014

Note 8 – Notes payable (continued)

	2015	2014
Loan payable dated April 30, 2009, to Habitat for Humanity International, collateralized by Deeds of Trust for mortgages receivable, with principal and interest at an annual rate of 5.3% payable in quarterly installments of \$6,366 through June 30, 2016.	24,641	48,017
Loan payable dated December 1, 2011, to California Bank and Trust, collateralized by mortgages receivable, with principal and interest at an annual rate of 4.75% payable in monthly installments of \$5,145 through December 20, 2026.	546,959	581,439
Loan payable dated February 15, 2012, to the City of Huntington Beach. The loan term is for 12 months from the date of the loan. The loan is payable in full upon the sale of the identified property to an eligible purchaser.	261,604	261,604
Loan payable dated September 23, 2011, to Cypress Redevelopment Agency, collateralized by a deed of trust. The loan is reconveyed in full upon sale of the last condominium in the project to a qualified homebuyer. The note does not accrue interest, however, in the event of default, the note will begin to accrue interest at the lesser of 10% or the highest rate permitted by law.	1,437,389	1,437,389
Loan payable dated September 12, 2012, to Housing Authority of the City of Santa Ana, collateralized by deed of trust, with principal due upon sale to a qualified homebuyer. The note does not accrue interest.	-	174,937
Loan payable dated September 12, 2012, to Housing Authority of the City of Santa Ana, collateralized by deed of trust, with principal due upon sale to a qualified homebuyer. The note does not accrue interest.	-	174,937

HABITAT FOR HUMANITY OF ORANGE COUNTY, INC.

NOTES TO FINANCIAL STATEMENTS

June 30, 2015 and 2014

Note 8 – Notes payable (continued)

	2015	2014
Loan payable dated September 12, 2012, to Housing Authority of the City of Santa Ana, collateralized by deed of trust, with principal due upon sale to a qualified homebuyer. The note does not accrue interest.	174,937	174,937
Loan payable dated September 12, 2012, to Housing Authority of the City of Santa Ana, collateralized by deed of trust, with principal due upon sale to a qualified homebuyer. The note does not accrue interest.	240,933	240,933
Loan payable dated March 22, 2013, to Neighborworks (Orange County Housing Trust). The loan term is for 24 months from the date of the loan. The note is collateralized by a deed of trust, with principal and interest at an annual rate of 5.00%.	896,066	717,856
Loan payable dated June 30, 2014, to Sunwest Bank, collateralized by the property in Santa Ana, CA. The loan term is extended to October 24, 2015, with principal and interest at an annual rate of 5.00%. The loan will be replaced by a construction loan.	160,000	160,000
Loan payable dated July 5, 2013, to Sunwest Bank, collateralized by the property under construction in Santa Ana, CA and donations. The loan term is for 18 months from the date of the loan, with principal and interest at an annual rate of 5.00%.	-	396,366
Loan payable dated December 3, 2013, to Sunwest Bank, collateralized by the land and property under construction in La Habra, CA and donations. The loan term is extended until December 3, 2015, with principal and interest at an annual rate of 5.00%.	671,979	279,285

HABITAT FOR HUMANITY OF ORANGE COUNTY, INC.

NOTES TO FINANCIAL STATEMENTS

June 30, 2015 and 2014

Note 8 – Notes payable (continued)

	2015	2014
Loan payable dated October 17, 2014 to Sunwest Bank, collateralized by the property under construction in Santa Ana, and donations. The loan term is for 18 months from the date of the loan, with principal and interest at an annual rate of 5.00%	111,329	-
Loan payable dated August 11, 2014 to California Bank & Trust, collateralized by mortgages receivable with principal and interest at an annual rate of 4.00% payable in monthly installments of \$3,501 through August 20, 2021.	230,401	-
Loan payable dated August 11, 2014 to California Bank & Trust, collateralized by mortgages receivable with principal and interest at an annual rate of 5.00% payable in monthly installments of \$3,021 through August 20, 2029.	369,675	-
Loan payable dated October 22, 2014, to Housing Authority of the City of Santa Ana, collateralized by deed of trust, with principal due upon sale to a qualified homebuyer. The note does not accrue interest.	180,435	-
Loan payable dated October 22, 2014, to Housing Authority of the City of Santa Ana, collateralized by deed of trust, with principal due upon sale to a qualified homebuyer. The note does not accrue interest.	180,435	-
Loan payable dated December 29, 2014 to Sunwest Bank, collateralized by the property under construction in Cypress, and donations. The loan term is for 18 months from the date of the loan with principal and interest at an annual rate of 5.00%.	<u>150,471</u>	<u>-</u>
Total notes payable	<u>\$ 5,637,254</u>	<u>\$ 4,660,616</u>

HABITAT FOR HUMANITY OF ORANGE COUNTY, INC.

NOTES TO FINANCIAL STATEMENTS

June 30, 2015 and 2014

**Note 8 – Notes payable (continued)**

Maturities of notes payable for the years ended June 30, are as follows:

2016	\$ 4,630,227
2017	140,008
2018	140,008
2019	140,008
2020 and thereafter	<u>587,003</u>
	<u>\$ 5,637,254</u>

Interest expense related to notes payable for the years ended June 30, 2015 and 2014, totaled \$141,850 and \$94,831, respectively.

**Note 9 – Line of credit**

The Organization secured a line of credit of up to \$125,000 dated June 29, 2015 from Sunwest Bank. The line is unsecured and matures January 26, 2017 with a variable interest rate at 1.00% over the index (Wall Street Journal Prime Rate), which was 4.25% at June 30, 2015. There have been no draws, and there is no outstanding balance at June 30, 2015.

**Note 10 – Long-term debt – Clearinghouse NMTC (Sub 21), LLC**

Long-term debt consists of the following:

Clearinghouse NMTC (Sub 21), LLC	<u>\$7,883,619</u>
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Debt requires interest only payments until December 5, 2017 at 0.76633%. The loan matures on July 28, 2025. The loan is secured by substantially all the assets acquired by the Organization from the project loan proceeds. Debt has a put option feature that is exercisable in July 2017. Management expects that the put option will be exercised. Exercise of the option will effectively allow the Organization to extinguish its outstanding debt owed to the Fund. See Note 4.

HABITAT FOR HUMANITY OF ORANGE COUNTY, INC.

NOTES TO FINANCIAL STATEMENTS

June 30, 2015 and 2014

**Note 11 – Temporarily restricted net assets**

Temporarily restricted net assets were comprised of the following at June 30:

	2015	2014
Land	\$ 302,000	\$ 302,000
Capital campaign	-	50,000
Fullerton II	177,851	-
Neighborhood Revitalization Initiative	33,718	-
NR Veterans	101,716	
Home Depot Critical Repair	-	18,317
Santa Ana VI	-	150,000
La Habra	153,500	243,500
Cypress II	-	350,000
Future projects	25,207	122,186
Other	-	607
	<u>                    </u>	<u>                    </u>
Total temporarily restricted net assets	<u>\$ 793,992</u>	<u>\$ 1,236,610</u>

**Note 12 – Costs in excess of estimated sales price**

Costs in excess of estimated sales price were comprised of the following at June 30:

	2015	2014
Sales of homes	\$ (1,203,800)	\$ (1,815,400)
Rehab revenue	(39,500)	(67,545)
Cost of home sales	1,600,126	3,135,188
Discount of sales	184,180	97,750
	<u>                    </u>	<u>                    </u>
Costs in excess of estimated sales price	<u>\$ 541,006</u>	<u>\$ 1,349,993</u>

## HABITAT FOR HUMANITY OF ORANGE COUNTY, INC.

### NOTES TO FINANCIAL STATEMENTS

June 30, 2015 and 2014

#### Note 13 – Operating leases

The Organization leases office space, ReStore warehouse/retail space, and various office equipment under operating leases totaling \$56,965 per month for terms through August 2021. Rental expenses related to these leases totaled \$645,368 and \$740,182 for the years ended June 30, 2015 and 2014, respectively.

Future minimum lease payments for operating leases for the years ended June 30, are as follows:

2016	\$	570,689
2017		501,724
2018		342,229
2019		288,983
2020		310,287

#### Note 14 – Retirement Plan

The Organization offers a retirement plan to eligible employees. The Organization does not provide any employer contributions.

#### Note 15 – Guarantees

The Organization uses cash leveraging programs to generate cash today from years of future monthly mortgage payments by Habitat homeowners.

#### Habitat for Humanity International (See Note 16)

The Organization has guaranteed payment streams in connection with some of its debt instruments. These include the notes payable to Habitat for Humanity International (HFHI) under the AAR and FlexCap programs. On a monthly basis, the amount specified in the respective agreements is remitted to the appropriate party to the agreement. The term of these agreements is seven years. The Organization continues to service these mortgages, monitors payments, and is responsible for collections.

Under the agreements, if a mortgage has significant reported delinquencies, despite on-time remittance of the quarterly payments, the Organization could be required to substitute the loan with a loan that is consistently current. The Organization also retains the right to substitute a mortgage of equal or greater value in the event of the homeowner requesting a buyback of their property or in the event that the Organization plans to renegotiate the terms of the mortgage with the homeowner.

## HABITAT FOR HUMANITY OF ORANGE COUNTY, INC.

### NOTES TO FINANCIAL STATEMENTS

June 30, 2015 and 2014

#### Note 15 – Guarantees (continued)

##### Vertical US Recovery Fund, LLC

The Organization entered into agreements with unrelated investors, Vertical US Recovery Fund LLC, Vertical US Recovery Fund II LLC, and Vertical Capital Income Fund (collectively Vertical) which purchased certain of the Organization's mortgages. In conjunction with the purchase agreements, the Organization will continue to service these mortgages, monitor payments, and be responsible for collections. Under the terms of the agreement the Organization will remit to Vertical on a monthly basis for a period up to 40 years, an amount equal to the monthly payments due from the homeowners. This amount will vary as homeowners pay off their mortgages.

Under the agreements, the Organization retains the right to substitute a mortgage of equal or greater value in the event of the homeowner requesting a buyback of their property or in the event that the Organization plans to renegotiate the terms of the mortgage with the family. The Organization has guaranteed the full and prompt payment of all obligations in conjunction with the mortgages. The Organization's obligation to Vertical will not change irrespective of the payments collected on the mortgages.

##### First Republic Bank

First Republic Bank has made loans direct to Habitat homeowners. First Republic services these loans. The Organization retains the right to cure the loan for up to 180 days of consecutive late payments by the homeowner or up to 12 months of non-consecutive late payments by the homeowner. After the 180 days or 12 months passes, the loan balance outstanding would be purchased by the Organization. The Organization would then renegotiate a Habitat loan with the homeowner. The Organization has guaranteed mortgages made by First Republic Bank in the outstanding principal amount of \$1,884,019 and \$1,925,560 as of June 30, 2015 and 2014, respectively.

##### California Bank and Trust

The Organization has also guaranteed payment streams in connection with three California Bank and Trust notes payable. The Organization continues to service these mortgages, monitors payments, and is responsible for collections, and will remit to California Bank and Trust on a monthly basis per the term of each agreement as follows: \$5,145 for 15 years through December 2026; \$3,501 for 7 years through August 2021, \$3,021 for 15 years through August 2029.

The Organization retains the right to substitute a mortgage of equal or greater value in the event of the homeowner requesting a buyback of their property or in the event that the Organization plans to renegotiate the terms of the mortgage with the family. The Organization has encumbered eleven loans, of which their total present value equates to approximately forty percent of the notes payable to California Bank and Trust, as possible substitution loans. See Notes 5 and 8.

## HABITAT FOR HUMANITY OF ORANGE COUNTY, INC.

### NOTES TO FINANCIAL STATEMENTS

June 30, 2015 and 2014

#### **Note 16 – Related party transactions**

##### Habitat for Humanity International

The Organization is affiliated, by agreement, with Habitat for Humanity International, a tax-exempt organization incorporated under the laws of the state of Georgia. The Organization has been added to the roster of exempt subordinates by the Internal Revenue Service within a group exemption granted to Habitat for Humanity International under Section 501(c)(3) of the Internal Revenue Code.

Under its affiliate agreement the Organization is expected to contribute a certain portion of its unrestricted cash donations to Habitat for Humanity International to continue its international programs. These contributions are accounted for as program services and are recorded when due.

The Organization has entered into two loans through HFHI, and these loans are collateralized by pledged mortgages receivables. See Notes 5 and 8.

#### **Note 17 – Agreement with Humanity Housing, Inc.**

The Organization has an Agreement of Purchase and Sale and Joint Escrow Instructions (the "Purchase Agreement") with an unrelated entity, Humanity Housing, Inc., a California non-profit corporation. Humanity Housing, Inc. is working in cooperation with the Organization pursuant to the HOME program regulations requiring Humanity Housing, Inc. to convey the properties and assign all rights and obligations to the Organization which has qualified to rehabilitate the properties, complete the housing construction, and offer for sale and sell the completed units to eligible homebuyers. During the year ended June 30, 2015, one property was transferred from the Organization to Humanity Housing, Inc. through a Quit Claim Deed transfer for \$1.00. The property will be returned to the Organization through a Quit Claim Deed for \$1.00 in the fiscal year ended June 30, 2016. No properties were transferred between the entities in the fiscal year ended June 30, 2014.

The Organization has an accommodation agreement with Humanity Housing, Inc. whereby the Organization pays Humanity Housing, Inc. a sum of \$400 upon the close of escrow for each Affordable Housing Agreement (AHA) in which Humanity Housing, Inc. serves as the counterparty in the role of beneficiary of the AHA.

HABITAT FOR HUMANITY OF ORANGE COUNTY, INC.

NOTES TO FINANCIAL STATEMENTS

June 30, 2015 and 2014

**Note 18 – Supplemental disclosures of cash flow information**

	2015	2014
Cash paid during the year for:		
Interest	<u>\$ 141,850</u>	<u>\$ 94,831</u>
Noncash investing activities:		
Costs capitalized as housing assets	<u>\$ 7,662,336</u>	<u>\$ 5,862,361</u>

Contributed housing assets represents program costs which have been capitalized until the homes are sold. These costs include land, construction in progress, donated materials and services, and incurred losses prior to sale of the homes.

**Note 19 – Reclassification of revenue and expenses**

The Organization allocates a portion of various overhead costs to Construction in Progress as the services provided by the departments directly impact the specific developments under construction. During the year ended June 30, 2015, management discovered that allocations of various department overhead costs to Construction in Progress had not been reduced from the departmental costs. Instead, the allocations had been included in unrestricted donations. The result was that both expenses and revenues were overstated by \$730,473. The overstatement had no effect on the change in unrestricted net assets.

Additionally, depreciation expense was reclassified out of Costs in excess of estimated sales price in the amount of \$28,692 and into Construction, ReStore and General and Administrative expenses, as applicable.

HABITAT FOR HUMANITY OF ORANGE COUNTY, INC.

NOTES TO FINANCIAL STATEMENTS

June 30, 2015 and 2014

Note 19 – Reclassification of revenue and expenses (continued)

	<u>Original</u> <u>presentation</u> 2014	<u>Reclassification</u> 2014	<u>Adjusted</u> <u>presentation</u> 2014
Unrestricted net assets			
Support and revenue			
Contributions	\$ 1,570,810	\$ (730,473)	\$ 840,337
Donated materials and services	194,992	-	194,992
Interest income	252,041	-	252,041
Rental income	79,710	-	79,710
ReStore revenues	1,867,169	-	1,867,169
Special events revenues	522,998	-	522,998
Other income	<u>33,570</u>	<u>-</u>	<u>33,570</u>
Total unrestricted support revenues	4,521,290	(730,473)	3,790,817
Net assets released from restrictions	<u>2,242,988</u>	<u>-</u>	<u>2,242,988</u>
Total unrestricted support and reclassifications	<u>6,764,278</u>	<u>(730,473)</u>	<u>6,033,805</u>
Expenses:			
Program Services:			
Construction Costs	6,487,239	(174,732)	6,312,507
Construction Costs - joint venture	211,556	-	211,556
ReStore expenses	1,982,951	13,628	1,996,579
Special events	70,919	(21,167)	49,752
Public relations	234,568	(67,892)	166,676
Faith relations	31,938	(9,532)	22,406
Family relations	370,887	(110,698)	260,189
Rental expenses	37,404	-	37,404
Contributions to HFHI	61,640	-	61,640
Costs in excess of estimated sales price	1,378,685	(28,692)	1,349,993
Less costs capitalized as housing assets	<u>(5,862,361)</u>	<u>-</u>	<u>(5,862,361)</u>
Total program services	5,005,426	(399,085)	4,606,341
Supporting services:			
General and administrative	557,564	(153,837)	403,727
Fundraising	<u>594,874</u>	<u>(177,551)</u>	<u>417,323</u>
Total supporting services	<u>1,152,438</u>	<u>(331,388)</u>	<u>821,050</u>
Total expenses	<u>6,157,864</u>	<u>(730,473)</u>	<u>5,427,391</u>
Change in unrestricted net assets	606,414	-	606,414

HABITAT FOR HUMANITY OF ORANGE COUNTY, INC.

NOTES TO FINANCIAL STATEMENTS

June 30, 2015 and 2014

**Note 20 – Subsequent events**

Loans payable

In July and September 2015, the Organization sold two homes. There was no outstanding construction loan and the outstanding debt to the Housing Authority of the City of Santa Ana was reconveyed without payment in the amounts of \$174,937 and \$240,933, respectively.

In August 2015, the Organization sold five homes of which proceeds were used to repay in full the \$896,066 note payable to NeighborWorks. Additionally, the Organization repaid in full the \$261,604 note payable to the City of Huntington Beach.

Loan payable to Sunwest Bank in the amount of \$160,000 was due October 24, 2015. The Organization approved a resolution to modify the loan agreement, and is currently awaiting final loan documents.

Management's review

Management has evaluated subsequent events through November 11, 2015, the date on which the financial statements were available to be issued.