

**San Diego Habitat for Humanity, Inc.**

**Consolidated Financial Statements  
and Independent Auditor's Report**

**June 30, 2017 and 2016**

**San Diego Habitat for Humanity, Inc.**

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## Independent Auditor's Report

To the Board of Directors  
San Diego Habitat for Humanity, Inc.

We have audited the accompanying consolidated financial statements of San Diego Habitat for Humanity, Inc., which comprise the consolidated statement of financial position as of June 30, 2017, and the related consolidated statements of activities and changes in net assets, functional expenses and cash flows for the year then ended, and the related notes to the consolidated financial statements.

### *Management's Responsibility for the 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.

### *Auditor's Responsibility*

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit 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 auditor's 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.

### *Opinion*

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of San Diego Habitat for Humanity, Inc. as of June 30, 2017, and the changes in its net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

*Prior Period Financial Statements*

The consolidated financial statements of San Diego Habitat for Humanity, Inc. as of June 30, 2016, were audited by other auditors whose report dated November 7, 2016, expressed an unmodified opinion on those consolidated statements.

*JJD & Associates, LLP*

San Diego, California

October 24, 2017

**San Diego Habitat for Humanity, Inc.**

**Consolidated Statements of Financial Position  
June 30, 2017 and 2016**

|  | 2017          | 2016          |
|--|---------------|---------------|
| Cash and cash equivalents  | \$ 2,803,246  | \$ 1,773,929  |
| Restricted cash  | 220,436       | 145,588       |
| Accounts receivable, net of allowance for doubtful accounts of \$70,165 and \$54,631 (2017 and 2016) | 68,462        | 65,121        |
| Mortgage notes receivable, net of unamortized discount   | 5,226,765     | 6,294,577     |
| Inventory - ReStores and other   | 417,650       | 381,276       |
| Prepaid expenses and deferred charges  | 57,375        | 750,808       |
| Construction-in-process  | 2,140,791     | 2,336,987     |
| Finished homes held for sale   | 580,194       | 1,874,779     |
| Corporate building held for sale   | -             | 2,134,852     |
| Property and equipment, net of accumulated depreciation  | 5,438,411     | 122,850       |
| Beneficial interest in assets held by community foundation   | 345,588       | 323,621       |
| Deposits and other assets  | 95,503        | 140,050       |
| Total assets   | \$ 17,394,421 | \$ 16,344,438 |
| <u>Liabilities and Net Assets</u>  |               |               |
| Accounts payable, accrued expenses, and other liabilities  | \$ 481,529    | \$ 843,700    |
| Secured obligations  | 3,224,234     | 3,351,869     |
| Homeowner impounds   | 22,292        | 86,803        |
| Deferred revenue   | -             | 60,000        |
| Notes payable - governmental agencies, net   | 521,766       | 551,981       |
| Forgivable notes payable - governmental agencies   | 270,000       | 1,037,630     |
| Refundable advances  | 220,436       | 686,578       |
| Note payable - Bank  | 3,667,220     | 1,844,764     |
| Note payable - HFHI  | -             | 653,069       |
| Notes payable - Construction   | 275,000       | -             |
| Total liabilities  | 8,682,477     | 9,116,394     |
| Commitments and contingencies  |               |               |
| Net assets   |               |               |
| Unrestricted   | 8,295,618     | 6,904,423     |
| Temporarily restricted   | 113,267       | 20,562        |
| Permanently restricted   | 303,059       | 303,059       |
| Total net assets   | 8,711,944     | 7,228,044     |
| Total liabilities and net assets   | \$ 17,394,421 | \$ 16,344,438 |

See Notes to Consolidated Financial Statements.

**San Diego Habitat for Humanity, Inc.**

**Consolidated Statement of Activities and Changes in Net Assets  
Year Ended June 30, 2017**

|  | <u>Unrestricted</u> | <u>Temporarily<br/>restricted</u> | <u>Permanently<br/>restricted</u> | <u>Total</u>        |
|--|---------------------|-----------------------------------|-----------------------------------|---------------------|
| Support and revenue                        |                     |                                   |                                   |                     |
| Support                                    |                     |                                   |                                   |                     |
| Contributions                              | \$ 1,645,584        | \$ 512,343                        | \$ -                              | \$ 2,157,927        |
| In-kind contributions                      | -                   | 115,886                           | -                                 | 115,886             |
| Retail store, net                          | 1,557,212           | -                                 | -                                 | 1,557,212           |
| Special events                             | 128,329             | -                                 | -                                 | 128,329             |
| Grants                                     | 466,142             | -                                 | -                                 | 466,142             |
| Net assets released from restrictions      |                     |                                   |                                   |                     |
| Satisfaction of program/donor restrictions | 572,551             | (572,551)                         | -                                 | -                   |
| Total support                              | <u>4,369,818</u>    | <u>55,678</u>                     | <u>-</u>                          | <u>4,425,496</u>    |
| Revenue                                    |                     |                                   |                                   |                     |
| Sales of homes                             | 5,177,000           | -                                 | -                                 | 5,177,000           |
| Mortgage loan discount amortization        | 577,092             | -                                 | -                                 | 577,092             |
| Investment income                          | 1,234               | 37,027                            | -                                 | 38,261              |
| Other income                               | 2,291,602           | -                                 | -                                 | 2,291,602           |
| Total revenue                              | <u>8,046,928</u>    | <u>37,027</u>                     | <u>-</u>                          | <u>8,083,955</u>    |
| Total support and revenue                  | <u>12,416,746</u>   | <u>92,705</u>                     | <u>-</u>                          | <u>12,509,451</u>   |
| Expenses                                   |                     |                                   |                                   |                     |
| Cost of homes sold and program support     | 9,794,126           | -                                 | -                                 | 9,794,126           |
| Management and general                     | 545,499             | -                                 | -                                 | 545,499             |
| Fundraising                                | 685,926             | -                                 | -                                 | 685,926             |
| Total expenses                             | <u>11,025,551</u>   | <u>-</u>                          | <u>-</u>                          | <u>11,025,551</u>   |
| Change in net assets                       | 1,391,195           | 92,705                            | -                                 | 1,483,900           |
| Net assets at beginning                    | <u>6,904,423</u>    | <u>20,562</u>                     | <u>303,059</u>                    | <u>7,228,044</u>    |
| Net assets at end                          | <u>\$ 8,295,618</u> | <u>\$ 113,267</u>                 | <u>\$ 303,059</u>                 | <u>\$ 8,711,944</u> |

See Notes to Consolidated Financial Statements.

**San Diego Habitat for Humanity, Inc.**

**Consolidated Statement of Activities and Changes in Net Assets  
Year Ended June 30, 2016**

|  | Unrestricted        | Temporarily<br>restricted | Permanently<br>restricted | Total               |
|--|---------------------|---------------------------|---------------------------|---------------------|
| Support and revenue                        |                     |                           |                           |                     |
| Support                                    |                     |                           |                           |                     |
| Contributions                              | \$ 771,028          | \$ 495,783                | \$ -                      | \$ 1,266,811        |
| In-kind contributions                      | 21,500              | 158,799                   | -                         | 180,299             |
| Retail store, net                          | 1,476,682           | -                         | -                         | 1,476,682           |
| Special events                             | 162,194             | -                         | -                         | 162,194             |
| Grants                                     | 56,389              | -                         | -                         | 56,389              |
| Net assets released from restrictions      |                     |                           |                           |                     |
| Satisfaction of program/donor restrictions | 669,604             | (669,604)                 | -                         | -                   |
| Total support                              | <u>3,157,397</u>    | <u>(15,022)</u>           | <u>-</u>                  | <u>3,142,375</u>    |
| Revenue                                    |                     |                           |                           |                     |
| Sales of homes                             | 4,563,906           | -                         | -                         | 4,563,906           |
| Mortgage loan discount amortization        | 527,683             | -                         | -                         | 527,683             |
| Investment income (loss)                   | 685                 | (7,046)                   | -                         | (6,361)             |
| Other income                               | 88,167              | -                         | -                         | 88,167              |
| Total revenue                              | <u>5,180,441</u>    | <u>(7,046)</u>            | <u>-</u>                  | <u>5,173,395</u>    |
| Total support and revenue                  | <u>8,337,838</u>    | <u>(22,068)</u>           | <u>-</u>                  | <u>8,315,770</u>    |
| Expenses                                   |                     |                           |                           |                     |
| Cost of homes sold and program support     | 8,675,973           | -                         | -                         | 8,675,973           |
| Management and general                     | 459,540             | -                         | -                         | 459,540             |
| Fundraising                                | 601,706             | -                         | -                         | 601,706             |
| Total expenses                             | <u>9,737,219</u>    | <u>-</u>                  | <u>-</u>                  | <u>9,737,219</u>    |
| Change in net assets                       | (1,399,381)         | (22,068)                  | -                         | (1,421,449)         |
| Net assets at beginning                    | <u>8,303,804</u>    | <u>42,630</u>             | <u>303,059</u>            | <u>8,649,493</u>    |
| Net assets at end                          | <u>\$ 6,904,423</u> | <u>\$ 20,562</u>          | <u>\$ 303,059</u>         | <u>\$ 7,228,044</u> |

See Notes to Consolidated Financial Statements.

**San Diego Habitat for Humanity, Inc.**

**Consolidated Statement of Functional Expenses  
Year Ended June 30, 2017**

|  | Cost of Homes<br>Sold and<br>Program<br>Support | Management and<br>General | Fundraising       | Total                |
|--|---|---------------------------|-------------------|----------------------|
| Cost of homes sold - construction costs                    | \$ 4,628,425                                    | \$ -                      | \$ -              | \$ 4,628,425         |
| Mortgage discount subsidy                                  | 1,084,603                                       | -                         | -                 | 1,084,603            |
| Salaries   | 1,336,208                                       | 328,469                   | 389,109           | 2,053,786            |
| Payroll taxes  | 115,869   | 25,985                    | 31,566            | 173,420              |
| Employee benefits  | 144,226   | 30,216                    | 24,599            | 199,041              |
| Advertising and public relations                           | 129,809   | -                         | 27,225            | 157,034              |
| Bank charges and fees                                      | 29,423  | 1,255                     | 8,929             | 39,607               |
| Conferences, conventions and meetings                      | 4,464   | 1,996                     | 1,841             | 8,301                |
| Depreciation   | 49,650  | 1,963                     | 2,248             | 53,861               |
| Homeowner and homeowner association support                | 28,064  | -                         | -                 | 28,064               |
| Insurance  | 133,502   | 13,948                    | 5,016             | 152,466              |
| Interest and amortization of loan fees                     | 213,570   | 20,754                    | 6,286             | 240,610              |
| Meals and entertainment                                    | 2,055   | 2,113                     | 1,715             | 5,883                |
| Non-capitalized construction materials and services        | 457,187   | -                         | -                 | 457,187              |
| Occupancy and utilities                                    | 252,122   | 9,901                     | 6,488             | 268,511              |
| Office, supplies and other expenses                        | 141,093   | 29,346                    | 34,278            | 204,717              |
| Outside services, consulting and volunteer expenses        | 157,804   | 28,897                    | 2,469             | 189,170              |
| Postage and shipping                                       | 679   | 2,034                     | 1,204             | 3,917                |
| Professional services                                      | 19,096  | 41,367                    | 14,733            | 75,196               |
| Real estate development costs                              | 23,801  | -                         | -                 | 23,801               |
| Taxes and licenses   | 1,835   | 204                       | -                 | 2,039                |
| Telephone  | 29,305  | 3,097                     | 3,234             | 35,636               |
| Tithes to HFHI   | 40,000  | -                         | -                 | 40,000               |
| HFHI affiliate fee   | 25,000  | -                         | -                 | 25,000               |
| Travel, mileage reimbursements and vehicle operating costs | 102,494   | 3,954                     | 5,187             | 111,635              |
| Loss on abandoned projects                                 | 634,639   | -                         | -                 | 634,639              |
| Corporate partnership projects                             | 9,203   | -                         | 89,384            | 98,587               |
| Special event costs  | -   | -                         | 30,415            | 30,415               |
|  | <u>          </u>                               | <u>          </u>         | <u>          </u> | <u>          </u>    |
| Total  | <u>\$ 9,794,126</u>                             | <u>\$ 545,499</u>         | <u>\$ 685,926</u> | <u>\$ 11,025,551</u> |

See Notes to Consolidated Financial Statements.



**San Diego Habitat for Humanity, Inc.**

**Consolidated Statement of Functional Expenses  
Year Ended June 30, 2016**

|  | Sold and<br>Program<br>Support | Management and<br>General | Fundraising       | Total               |
|--|--------------------------------|---------------------------|-------------------|---------------------|
| Cost of homes sold - construction costs                    | \$ 3,946,698                   | \$ -                      | \$ -              | \$ 3,946,698        |
| Mortgage discount subsidy                                  | 2,013,613                      | -                         | -                 | 2,013,613           |
| Salaries   | 1,040,945                      | 265,673                   | 348,215           | 1,654,833           |
| Payroll taxes  | 90,659                         | 21,284                    | 27,211            | 139,154             |
| Employee benefits  | 107,549                        | 29,777                    | 22,014            | 159,340             |
| Advertising and public relations                           | 100,017                        | -                         | 20,188            | 120,205             |
| Bank charges and fees                                      | 26,002                         | 2,499                     | 8,239             | 36,740              |
| Conferences, conventions and meetings                      | 3,255                          | 2,430                     | 800               | 6,485               |
| Depreciation   | 54,131                         | 5,214                     | 4,613             | 63,958              |
| Homeowner and homeowner association support                | 6,060                          | -                         | -                 | 6,060               |
| Insurance  | 99,197                         | 14,477                    | 4,129             | 117,803             |
| Interest and amortization of loan fees                     | 209,731                        | 20,511                    | 6,002             | 236,244             |
| Meals and entertainment                                    | 2,443                          | 1,551                     | 1,350             | 5,344               |
| Non-capitalized construction materials and services        | 500,302                        | -                         | -                 | 500,302             |
| Occupancy and utilities                                    | 112,881                        | 7,554                     | 4,945             | 125,380             |
| Office, supplies and other expenses                        | 80,207                         | 14,334                    | 31,545            | 126,086             |
| Outside services, consulting and volunteer expenses        | 48,362                         | 26,006                    | 2,309             | 76,677              |
| Postage and shipping                                       | 1,042                          | 1,849                     | 1,630             | 4,521               |
| Professional services                                      | 16,658                         | 40,349                    | 54,740            | 111,747             |
| Real estate development costs                              | 26,581                         | -                         | -                 | 26,581              |
| Taxes and licenses   | 1,956                          | 626                       | -                 | 2,582               |
| Telephone  | 24,403                         | 2,546                     | 3,401             | 30,350              |
| Tithes to HFHI   | 40,500                         | -                         | -                 | 40,500              |
| HFHI affiliate fee   | 25,000                         | -                         | -                 | 25,000              |
| Travel, mileage reimbursements and vehicle operating costs | 73,268                         | 2,860                     | 4,156             | 80,284              |
| Corporate partnership projects                             | 7,754                          | -                         | 22,786            | 30,540              |
| Special event costs  | 16,759                         | -                         | 33,433            | 50,192              |
|  | <u>\$ 8,675,973</u>            | <u>\$ 459,540</u>         | <u>\$ 601,706</u> | <u>\$ 9,737,219</u> |
| Total  | <u>\$ 8,675,973</u>            | <u>\$ 459,540</u>         | <u>\$ 601,706</u> | <u>\$ 9,737,219</u> |

See Notes to Consolidated Financial Statements.

**San Diego Habitat for Humanity, Inc.**  
**Consolidated Statements of Cash Flows**  
**Years Ended June 30, 2017 and 2016**

|  | 2017             | 2016             |
|--|------------------|------------------|
| Cash flows from operating activities   |                  |                  |
| Change in net assets   | \$ 1,483,900     | \$ (1,421,449)   |
| Adjustments to reconcile change in net assets to net cash used in operating activities |                  |                  |
| Origination of non-interest bearing mortgages  | (2,692,305)      | (3,101,940)      |
| Mortgages retired for reacquisition of homes, net                                      | 145,364          | -                |
| Discount on origination of non-interest bearing mortgages                              | 1,084,603        | 2,013,613        |
| In-kind contributions of property, equipment and construction costs                    | (52,861)         | (120,665)        |
| Change in value - beneficial interest in assets held by community foundation           | (21,967)         | 22,068           |
| (Gain) Loss on disposal of fixed assets  | (1,480,473)      | 3,916            |
| Gain on sale of mortgage notes receivable  | (755,469)        | -                |
| Depreciation   | 53,861           | 63,958           |
| Mortgage discount amortization   | (577,092)        | (527,683)        |
| Amortization of loan fees  | 21,234           | 7,811            |
| Amortization of discount on notes payable  | 121,318          | 105,953          |
| Changes in operating assets and liabilities  |                  |                  |
| Accounts receivable  | (3,341)          | (30,344)         |
| Unconditional promise to give  | -                | 100,000          |
| Inventory  | (36,374)         | (6,784)          |
| Prepaid expenses and deferred charges  | 693,433          | (582,738)        |
| Finished homes held for sale   | 1,294,585        | (678,519)        |
| Construction-in-process, net in-kind   | 241,135          | 2,649,748        |
| Deposits and other assets  | 44,547           | (84,466)         |
| Accounts payable, accrued expenses and other liabilities                               | (362,171)        | 156,166          |
| Mortgage payments received   | 872,101          | 831,022          |
| Homeowner impounds   | (64,511)         | 18,121           |
| Deferred revenue   | (60,000)         | (213,350)        |
| Refundable advances  | (466,142)        | (37,186)         |
|  | <u>(516,625)</u> | <u>(832,748)</u> |
| Net cash used in operating activities  |                  |                  |

See Notes to Consolidated Financial Statements.

**San Diego Habitat for Humanity, Inc.**  
**Consolidated Statements of Cash Flows**  
**Years Ended June 30, 2017 and 2016**

|   |                     |                     |
|---|---------------------|---------------------|
| Cash flows from investing activities                            |                     |                     |
| Purchases of property and equipment                             | (5,361,501)         | (55,865)            |
| Proceeds from sale of property and equipment                    | 500                 | -                   |
| Proceeds from sale of corporate building held for sale          | <u>3,614,826</u>    | <u>-</u>            |
| Net cash used in investing activities                           | <u>(1,746,175)</u>  | <u>(55,865)</u>     |
| Cash flows from financing activities                            |                     |                     |
| Payments of deferred financing fees                             | (9,670)             | (101,010)           |
| Proceeds from issuance of notes payable                         | 4,289,348           | 151,182             |
| Proceeds from sales of mortgage notes receivable, net           | 2,990,610           | -                   |
| Proceeds from issuance of secured obligations, net of discounts | -                   | 2,366,432           |
| Principal payments on notes payable, including grants forgiven  | (3,679,892)         | (832,475)           |
| Payments on secured obligations                                 | (223,431)           | (193,084)           |
| Restricted cash   | <u>(74,848)</u>     | <u>99,881</u>       |
| Net cash provided by financing activities                       | <u>3,292,117</u>    | <u>1,490,926</u>    |
| Net increase in cash and cash equivalents                       | 1,029,317           | 602,313             |
| Cash and cash equivalents, beginning                            | <u>1,773,929</u>    | <u>1,171,616</u>    |
| Cash and cash equivalents, end                                  | <u>\$ 2,803,246</u> | <u>\$ 1,773,929</u> |
| Supplemental disclosure of cash flow information                |                     |                     |
| Interest paid   | <u>\$ 98,059</u>    | <u>\$ 122,481</u>   |
| Supplemental disclosure of non-cash financing activities        |                     |                     |
| Notes forgiven - governmental grants                            | <u>\$ 806,000</u>   | <u>\$ 596,300</u>   |

See Notes to Consolidated Financial Statements.

## San Diego Habitat for Humanity, Inc.

### Notes to Consolidated Financial Statements June 30, 2017 and 2016

#### Note 1 - Organization and summary of significant accounting policies

##### **Nature of activities**

San Diego Habitat for Humanity, Inc. (a nonprofit corporation) is the local affiliate of Habitat for Humanity International, Inc. ("HFHI"), a nonprofit, ecumenical Christian housing ministry. By building homes in partnership with families in need, San Diego Habitat for Humanity, Inc. seeks to eliminate poverty housing and substandard living conditions in San Diego County, and to make decent shelter a matter of conscience and action. San Diego Habitat for Humanity, Inc. invites people of all backgrounds, faiths, or no faith, races and religions to build houses together in partnership with families in need. Although HFHI assists with information resources, training, publications and prayer support, San Diego Habitat for Humanity, Inc. is an independently governed entity.

An equal housing lender and provider, San Diego Habitat for Humanity, Inc. addresses the issues of substandard housing through home ownership. The purpose is to offer families a "hand up" instead of a "hand out," fostering self-sufficiency and independence. To be considered for home ownership, San Diego Habitat for Humanity, Inc. families must demonstrate a need for better housing, an ability to make mortgage payments, and a willingness to work in partnership with San Diego Habitat for Humanity, Inc. This partnership consists, in part, of each family completing 250-500 hours of "sweat equity" and making monthly mortgage payments. San Diego Habitat for Humanity, Inc. acquires the land, finds and qualifies the families, raises the funding, finds and supervises construction volunteers, builds the houses, and provides the mortgages.

##### **Method of reporting**

San Diego Habitat for Humanity, Inc.'s financial statements are prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America.

##### **Principles of consolidation**

The accompanying consolidated financial statements include the accounts of San Diego Habitat for Humanity, Inc. and San Diego HFH Community Housing Corporation (collectively, "SDHFH" or the "Organization"). All material intra-organization transactions have been eliminated in consolidation.

##### **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 as of the date of the consolidated financial statements, and revenues and expenses recognized during the reporting period. Actual results could differ from these estimates.

##### **Net assets**

SDHFH's net assets, revenues, gains, expenses and losses are classified as unrestricted, temporarily restricted and permanently restricted based on the existence or absence of donor-imposed restrictions. These classifications are defined as follows:

*Unrestricted net assets* - Net assets that do not contain donor restrictions or the donor-imposed restrictions have expired due to the Organization's fulfillment of the restrictions and/or the passage of time.

## San Diego Habitat for Humanity, Inc.

### Notes to Consolidated Financial Statements June 30, 2017 and 2016

*Temporarily restricted net assets* - Net assets that contain donor-imposed restrictions that permit the Organization to use or expend the donated net assets as specified and are satisfied either by the passage of time and/or by the actions of SDHFH.

*Permanently restricted net assets* - Net assets that contain donor-imposed stipulations that neither expire by passage of time nor can be fulfilled or otherwise removed by actions of the Organization.

#### **Cash and cash equivalents**

SDHFH considers all highly liquid investments with an original maturity of three months or less, when purchased, to be cash equivalents.

#### **Restricted cash**

Restricted cash represents Community Housing Development Organization proceeds to be used to acquire, rehabilitate or develop additional real properties located in the respective city for resale to low-income households.

#### **Accounts receivable**

Accounts receivable consist primarily of mortgage principal amounts collected in June by AmeriNat, a loan servicing organization that services 88 mortgage loans for SDHFH, and amounts due from homeowners for property taxes and insurance premiums; pursuant to the homeowners' impound agreements. The Organization has evaluated these accounts and has recorded an allowance for doubtful accounts based on the estimated eventual collection of these impound account deficits. Bad debt expense of \$17,000 was recorded for the fiscal year ended June 30, 2017 while there was no bad debt expense recorded in the prior year.

It is the Organization's policy to charge off uncollectible accounts receivable when management determines the receivable will not be collected.

#### **Mortgage notes receivable**

Mortgage notes receivable consist of non-interest bearing residential home loans made to qualified borrowers that are secured by a deed of trust, payable in monthly installments over the term of the note, generally ranging from 5 to 35 years. These non-interest bearing mortgages have been discounted based on historical experience from SDHFH's portfolio of mortgages and upon prevailing market rates for low-income housing at the inception of each mortgage. SDHFH's portfolio of mortgage notes receivable includes first trust deeds for direct loans made by SDHFH and second trust deeds funded by Cal Home Program First-Time Homebuyer loans. The Cal Home Program loans are non-interest bearing loans with a balloon payment due in 30 years.

Additionally, homes may be encumbered with a second, third and/or fourth trust deed in favor of either SDHFH or a local governmental agency to ensure compliance with the terms of the Organization's homeownership programs. These mortgage notes receivable are referred to as "silent." The primary purpose of these silent mortgages is to allow SDHFH or the agency to capture a portion of any equity appreciation over and above a specified amount if the home is sold or transferred to a nonqualified homeowner before a certain number of years have elapsed since the original sale to the qualified homeowner, usually 25 to 55; and to protect the homeowner by preventing predatory lenders from paying off the first mortgage and saddling the homeowner with an onerous new mortgage. These silent mortgage notes receivable typically bear no interest and are forgiven if the homeowner lives in the home for the required period of time and complies with all other covenants and restrictions per the deed of trust. Accordingly, since these silent mortgage notes receivable have no value unless or until a homeowner fails to comply with the covenants and

## San Diego Habitat for Humanity, Inc.

### Notes to Consolidated Financial Statements June 30, 2017 and 2016

restrictions of the terms of the home sale, SDHFH does not record a value for these silent mortgage notes receivable.

#### **Allowance for mortgage notes receivable losses**

SDHFH uses established underwriting criteria to ensure that only families who meet the Organization's financial and credit criteria are approved to be partner families and receive a non-interest bearing mortgage loan from SDHFH. This includes, but is not limited to, a thorough review of each prospective homeowner's credit report, sources of income and financial history.

SDHFH regularly reviews its portfolio of mortgage notes receivable and monitors the accounts for delinquencies. Homeowners whose mortgages are more than 30 days past due are considered to be in an early stage of default. During the period of delinquency of 16 to 60 days past due, the Organization contacts the homeowner using collection efforts and establishes a payment plan with the homeowner, if necessary. Thereafter, if forgoing collection efforts are not successful, the Organization attempts to enter into a mutually agreed-upon deed-in-lieu of foreclosure with the homeowner. Homeowners whose mortgages are more than 60 days past due, who have not made satisfactory payment arrangements or reached a deed-in-lieu of foreclosure agreement with SDHFH are subject to foreclosure proceedings. As of the date of these consolidated financial statements, there are no mortgages subject to foreclosure proceedings.

Non-interest bearing mortgages originated are discounted at the time of sale based on historical experience from SDHFH's portfolio mortgages and upon prevailing market rates. This results in the net mortgage receivable balances being 40-60% of the home's fair market value. Therefore, SDHFH believes that losses resulting from non-payment of mortgage notes receivable, given its collateral value, are not likely. Accordingly, SDHFH has not recorded an allowance for mortgage notes receivable losses.

#### **Contributions**

Unconditional promises to give are recognized as support when the underlying promises are received by SDHFH and are recorded at fair value, based on management's initial estimate of the present value of future cash flows expected to be received. Subsequent changes in estimates are recorded as an allowance for uncollectible promises to give.

Gifts of cash and other assets are reported as temporarily restricted support if they are received with donor stipulations that specify the use of the donated assets. When a donor 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 consolidated statements of activities and changes in net assets as net assets released from restrictions. Conditional promises to give are not recognized until they become unconditional, that is, when the conditions on which they depend are substantially met.

#### **Donated services**

Donated services are recognized as contributions in accordance with Accounting Standards Codification ("ASC") 958-605 and subsections, *Not-for-profit Entities - Revenue Recognition*, if the services (a) create or enhance nonfinancial assets or (b) require licensed skills, are performed by people with those skills, and would otherwise be purchased by SDHFH. A substantial number of volunteers have contributed their time during the years ended June 30, 2017 and 2016 to SDHFH's construction program and supporting services. The value of this contributed time is not reflected in the consolidated financial statements since it does not require a licensed skill.

## San Diego Habitat for Humanity, Inc.

### Notes to Consolidated Financial Statements June 30, 2017 and 2016

#### **Donated construction materials, property and equipment and other donated goods**

Donations of construction materials, property and equipment, and other goods are recorded as in-kind contributions at their estimated fair value at the date of donation.

Various companies and individuals have provided licensed labor and materials for current projects. During the years ended June 30, 2017 and 2016, the Organization recognized \$91,891 and \$132,621, respectively, of in-kind materials and licensed labor as contribution revenue. The estimated value of these materials and services was capitalized into construction-in-process and allocated accordingly to the projects receiving benefit. The Organization also recognized \$0 and \$21,500 of donated fixed assets and land during the fiscal years ended June 30, 2017 and 2016, respectively.

In addition to the construction-related in-kind contributions, SDHFH recognized \$23,995 and \$26,178 for donated goods and services supporting various programs and fundraising activities during the fiscal years ended June 30, 2017 and 2016, respectively. Accordingly, the Organization recognized total in-kind contributions of \$115,886 and \$180,299 during the fiscal years ended June 30, 2017 and 2016, respectively.

#### **Government funding**

SDHFH receives funds from various governmental agencies for land acquisition, development and construction costs pursuant to various types of agreements. The following are details on the various types of funding agreements:

*Grants* - SDHFH receives grants from various sources to assist in purchasing and developing properties. These grants include various compliance requirements to be followed by SDHFH. These funds are recognized as grants in the consolidated statements of activities and changes in net assets.

*Forgivable loans* - SDHFH enters into various funding agreements that result in receiving funds to acquire and develop qualified properties, where funding received is considered a forgivable loan. The loans are typically forgiven after homes have been sold to qualified borrowers. Certain forgivable loans are transferred to the qualified home buyer at the time of purchase and the loans with the borrowers require the homeowner to continue to comply with certain provisions for specified periods of time. SDHFH records these forgivable loans as notes payable until they are forgiven.

*Refundable advances* - SDHFH enters into certain agreements that result in the receipt of funds that require SDHFH to continue to utilize these funds for specified low-income housing purposes until a certain number of units have been sold. These advances are often sourced from federal funds and require ongoing compliance with certain specified federal requirements. Once related compliance requirements are satisfied, SDHFH will recognize these as unrestricted grants. SDHFH records these funds as refundable advances until the compliance requirements are satisfied.

#### **Concentrations of credit risk**

Financial instruments that potentially subject the Organization to concentrations of credit risk consist principally of cash, cash equivalents, and investments. The Organization places its cash, cash equivalents and investments with high credit quality financial institutions. At times, such amounts may exceed federally insured limits. At June 30, 2017, the Organization had approximately \$2,475,000 in excess of federally insured limits.

## **San Diego Habitat for Humanity, Inc.**

### **Notes to Consolidated Financial Statements June 30, 2017 and 2016**

#### **Inventories**

Inventories consist primarily of donated home furnishings and building and home improvement materials which are sold in the ReStore. SDHFH believes that the inventory of donated goods and materials does not possess an attribute that is easily measurable or verifiable with sufficient reliability to determine an inventory value at the time of donation.

Accordingly, donated inventory is valued at zero prior to being offered for sale. At the end of its fiscal year, SDHFH generally estimates the value of donated goods on hand and records the amount as merchandise inventory with corresponding adjustments to cost of sales. It is not practical to determine the fair value of donated merchandise inventory during the course of the year.

#### **Pre-acquisition costs**

The Organization capitalizes costs related to properties, generally including costs of surveying, zoning studies, design, engineering and legal, that are incurred for the express purpose of, but prior to, obtaining the properties. These costs are reported as prepaid expenses and deferred charges.

#### **Property, equipment and depreciation**

Property and equipment are recorded at acquisition cost, including costs necessary to ready the asset for its intended use, or at fair market value, if donated. Expenses that materially increase property lives are capitalized. The costs of maintenance and repairs are charged to expenses as incurred. Depreciation expense is provided on a straight-line basis over the estimated useful lives of the respective assets, currently ranging from 3 to 7 years for equipment and vehicles and from 5 to 39 years for buildings and building improvements. When depreciable property is retired or otherwise disposed of, the related cost and accumulated depreciation are removed from the accounts and any gain or loss is reflected in the consolidated statements of activities and changes in net assets.

#### **Construction-in-process and finished homes held for sale**

Construction-in-process represents costs incurred to build or rehabilitate single-family homes and condominiums for eventual sale to SDHFH partner families. The Organization's projects consist of new single-family home and condominium developments and major rehabilitations of existing homes acquired by SDHFH. Since the purpose and mission of SDHFH is to build affordable housing for low-income families, the Organization does not generally write down the value of construction-in-process to estimated sales value, because any excess cost over sales value is a component of program services. Projects are classified as construction-in-process until the build/rehabilitation project is substantially completed, at which time they are reclassified as "finished homes held for sale."

Finished homes held for sale may include homes purchased from SDHFH partner families, acquired as part of a deed-in-lieu of foreclosure or as part of a foreclosure. These homes usually require repairs or rehabilitation and then are resold to a qualifying family.

#### **Corporate building held for sale**

SDHFH recorded the corporate building as held for sale in anticipation of being sold within one year of June 30, 2016 and no longer depreciated it going forward. Total land, buildings and improvements related to the corporate building were \$2,134,852 (net of \$291,626 accumulated depreciation) as of June 30, 2016. The corporate building held for sale was sold in May 2017. There were no buildings held for sale as of June 30, 2017.

#### **Revenue and costs on homes sold**

Revenue is recognized on the sale of homes when title passes to eligible purchasers. The amount of home sale revenue SDHFH records is the total of the cash down payment, the face value of the



## San Diego Habitat for Humanity, Inc.

### Notes to Consolidated Financial Statements June 30, 2017 and 2016

non-interest bearing mortgage receivable, and the value of any government funding, such as notes payable forgiven and/or transferred to the homeowner at the time of sale (see *Government funding* above).

Cost of homes sold and program support consists of capitalized home construction costs and certain other related costs associated with the sale of a home. A mortgage discount subsidy, which is the discount on the non-interest mortgage with the borrower, is recognized as a cost of sale at the closing of the sale. Cost of homes sold and program support is considered a program expense in the consolidated statements of functional expenses.

#### **Deferred revenue**

Deferred revenue consists of amounts advanced to SDHFH pursuant to two down payment assistance grants (the "Grants") from the State of California Department of Housing and Community Development ("Cal Home"). The Grants allow SDHFH to receive a maximum of \$1,860,000 in funds to provide down payment assistance to eligible low and moderate income homeowners. Actual assistance to each homeowner is limited based on a calculated gap between the price of the home and the financial resources available to the homeowner, but cannot exceed \$60,000 per eligible family. At June 30, 2016, SDHFH reported deferred revenue of \$60,000, which all came from Cal Home funds, representing Grant draws in excess of down payment assistance and expenses incurred. SDHFH reported no deferred revenue as of June 30, 2017.

#### **Homeowner impounds**

As part of the mortgage servicing process, SDHFH collects monthly payments for property taxes and insurance from homeowners, along with their monthly mortgage payments. SDHFH then remits the property taxes and insurance, when due, directly to the County Tax Collector and insurance providers, using the impounded funds. The homeowner impounds balance at June 30, 2017 and 2016 represents amounts collected by SDHFH for property taxes and insurance that has not yet been paid to the County Tax Collector and insurance providers.

#### **Retirement plan**

During the fiscal year ended June 30, 2013, SDHFH adopted a 403(b) plan. SDHFH does not contribute to the plan. All employees are eligible to participate in the plan commencing upon their date of hire.

#### **Income taxes**

SDHFH, a California nonprofit public benefit corporation, is exempt from federal and state income taxes under Section 501(c)(3) of the Internal Revenue Code of 1954, as amended, and the Revenue and Taxation Code of the State of California.

For the years ended June 30, 2017 and 2016, management of SDHFH believes it has adequate support for all material tax positions and that it is more likely than not, based on the technical merits, that the positions will be sustained upon examination. SDHFH has analyzed the tax positions taken in its filings with the Internal Revenue Service and the California Franchise Tax Board. SDHFH believes that its income tax filing positions will be sustained upon examination and does not anticipate any adjustments that would result in a material adverse effect on the SDHFH's financial condition, results of operations or cash flows. Accordingly, SDHFH has not recorded any reserves, or related accruals for interest and penalties, for uncertain income tax positions at June 30, 2017 and 2016.

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The Organization's federal and state income tax returns prior to fiscal years 2014 and 2013, respectively, are closed. Management continually evaluates expiring statutes of limitations, audits, proposed settlements, changes in tax law and new authoritative rulings.

**Functional expenses**

Expenses related to more than one functional expense category are allocated based on reasonable estimates by the Organization. Salaries, benefits and other related expenses are allocated based on job function. Directly identifiable expenses are charged to construction and program support, management and general, or fundraising as applicable.

**Change in accounting principle - deferred financing fees and amortization**

During 2017, the Company adopted the provision of ASU No. 2015-03, *Simplifying the Presentation of Debt Issuance Costs* which modifies the presentation of debt issuance costs and the related amortization. The change in accounting under ASU 2015-03 improves the reporting of debt issuance costs by no longer reporting them as assets. It also improves the reporting of the related amortization by including it as a component of interest expense. ASU 2015-03 has been adopted by the Company on a retrospective basis. As a result, total assets and long-term debt for the years ended June 30, 2017 and 2016 have been reduced by the effect of the reclassification of debt issuance costs, net of accumulated amortization. The long-term debt accounts affected by the change in accounting principle include Secured obligations, Note payable – bank, and Note payable - HFHI. The reclass effect for 2016 was \$206,525.

**Reclassification**

Certain amounts in the 2016 financial statements have been reclassified to conform to the 2017 presentation.

**Subsequent events**

Subsequent events have been evaluated through October 24, 2017, which is the date the consolidated financial statements were available to be issued.

**Note 2 - Prepaid expenses and deferred charges**

Prepaid expenses and deferred charges are summarized as follows:

|                            | <u>2017</u>      | <u>2016</u>       |
|----------------------------|------------------|-------------------|
| Prepaid expenses           | \$ 55,748        | \$ 34,180         |
| Pre-acquisition costs      |                  |                   |
| Veteran project - Poway    | -                | 529,730           |
| Comm22 project - San Diego | -                | 178,263           |
| Other                      | <u>1,627</u>     | <u>8,635</u>      |
| Total                      | <u>\$ 57,375</u> | <u>\$ 750,808</u> |

The Veteran project - Poway was not approved in a public hearing on November 15, 2016 and as a result, SDHFH was forced to terminate the project. The pre-acquisition costs for this project were written off to Cost of homes sold and program support on the consolidated statement of activities for the year ended June 30, 2017.

**San Diego Habitat for Humanity, Inc.**

**Notes to Consolidated Financial Statements  
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**Note 3 - Mortgage notes receivable**

Mortgage notes receivable consist primarily of non-interest bearing residential home loans made to qualified borrowers that are secured by a deed of trust and payable in monthly installments over the terms of the notes, generally ranging from 5 to 35 years. These non-interest bearing mortgages have been discounted to net present values. In previous years, SDHFH used a discount rate that was based on the higher risk of default associated with the national low income population. For the year ended June 30, 2017, SDHFH used a rate that is more reflective of its actual experience over the past several years. During the years ended June 30, 2017 and 2016, new mortgages were discounted at rates of 3.74% and 7.48%, respectively, resulting in mortgage discount subsidy expense of \$1,084,603 and \$2,013,613, respectively. The mortgage discount subsidy is amortized over the lives of the underlying mortgages and included as revenue. Mortgage loan discount amortization revenue was \$577,092 for the year ended June 30, 2017 and \$527,683 for the year ended June 30, 2016.

Mortgage notes receivable and the related discount at June 30, 2017 and 2016 are summarized as follows:

|  | 2017          | 2016          |
|--|---------------|---------------|
| Mortgage notes receivable                      | \$ 11,413,524 | \$ 13,947,068 |
| Less unamortized discount                      | (6,186,759)   | (7,652,491)   |
| Net present value of mortgage notes receivable | \$ 5,226,765  | \$ 6,294,577  |

In previous years, SDHFH was party to several transactions in which it used non-interest bearing mortgage notes receivable as security to obtain operating loans from various banks. The details of these loans are shown in Note 10 – Secured Obligations. The mortgage notes receivable used as security remain as assets in the consolidated statements of financial position with a corresponding liability in the form of secured obligations. The terms and payment schedules of the secured obligations are coincident with those of the underlying mortgage notes receivable. At June 30, 2017 and 2016, the book value of these secured obligations, net of unamortized discount and deferred finance fees, was \$3,224,234 and \$3,351,869, respectively. See Note 10.

Scheduled mortgage notes receivable collections for five years subsequent to June 30, 2017 and thereafter are summarized as follows:

|            |    |            |
|------------|----|------------|
| 2018       | \$ | 563,998    |
| 2019       |    | 545,678    |
| 2020       |    | 522,276    |
| 2021       |    | 507,333    |
| 2022       |    | 483,874    |
| Thereafter |    | 8,790,365  |
| Total      | \$ | 11,413,524 |

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On September 28, 2016, the Organization sold 19 mortgage notes receivable to City National Bank for \$1,850,544 before transaction costs. These mortgage notes receivable, which had balances of \$2,293,027 (\$1,245,731 net of unamortized discount) as of the cut-off date for the transaction, had previously been used as collateral for the Organization's FlexCap Note payable to HFHI. As part of this transaction, SDHFH paid off the FlexCap note and accrued interest totaling \$638,949 and recovered its FlexCap deposit of \$40,026. The net cash generated by this transaction after transaction costs and the FlexCap payoff was \$1,174,033. On March 30, 2017, the Organization sold 9 additional mortgage notes receivable to City National Bank for \$1,249,533 before transaction costs. These mortgage notes receivable had balances of \$1,755,778 (\$989,410 net of unamortized discount) as of the cut-off date for the transaction. The net cash generated by this transaction after transaction costs was \$1,217,654. SDHFH recorded gains on the sale of mortgages of \$755,469 for the year ended June 30, 2017. See Note 22. As per the terms of the sale agreements, SDHFH remains responsible for the servicing of the mortgage notes receivable sold to City National Bank. The mortgage notes receivable sold to City National Bank are no longer included as assets in the consolidated statements of financial position.

**Note 4 - Construction-in-process**

Construction-in-process and real estate development costs are summarized by project as follows:

|                               | <u>2017</u>             | <u>2016</u>             |
|-------------------------------|-------------------------|-------------------------|
| El Cajon - Ballantyne         | \$ 556,669              | \$ -                    |
| El Cajon - Foundation Lane II | -                       | 1,983,745               |
| Escondido - Citracado Parkway | 62,536                  | 60,967                  |
| National City - Rachael Ave   | -                       | 291,675                 |
| Oceanside - Libby Village Way | -                       | 600                     |
| San Diego - Comm22            | <u>1,521,586</u>        | <u>-</u>                |
| <br>Total                     | <br><u>\$ 2,140,791</u> | <br><u>\$ 2,336,987</u> |

The following is a summary of home building activity for the years ended June 30, 2017 and 2016:

|  | <u>2017</u>                |                         | <u>2016</u>                |                         |
|--|----------------------------|-------------------------|----------------------------|-------------------------|
|  | <u>Number of<br/>homes</u> | <u>Cost</u>             | <u>Number of<br/>homes</u> | <u>Cost</u>             |
| Home construction-in-process,<br>beginning balance   | 8                          | \$ 2,336,987            | 25                         | \$ 4,911,509            |
| Costs incurred on homes                              |                            |                         |                            |                         |
| New and existing projects                            | 16                         | 2,494,829               | 1                          | 1,993,277               |
| Costs transferred to finished homes                  | <u>(7)</u>                 | <u>(2,691,025)</u>      | <u>(18)</u>                | <u>(4,567,799)</u>      |
| <br>Home construction-in-progress,<br>ending balance | <br><u>17</u>              | <br><u>\$ 2,140,791</u> | <br><u>8</u>               | <br><u>\$ 2,336,987</u> |

**San Diego Habitat for Humanity, Inc.**

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**Note 5 - Finished homes held for sale**

Finished homes held for sale consist of the following developments:

|                               | <u>2017</u>           | <u>2016</u>             |
|-------------------------------|-----------------------|-------------------------|
| Lakeside - Lakeshore Drive    | \$ -                  | \$ 300,956              |
| Oceanside - Libby Village Way | 580,194               | -                       |
| Imperial Beach - 10th & Donax | -                     | <u>1,573,823</u>        |
| <br>Total                     | <br><u>\$ 580,194</u> | <br><u>\$ 1,874,779</u> |

Following is a summary of finished homes activity for the years ended June 30, 2017 and 2016:

|   | <u>2017</u>                |                       | <u>2016</u>                |                         |
|---|----------------------------|-----------------------|----------------------------|-------------------------|
|   | <u>Number of<br/>homes</u> | <u>Cost</u>           | <u>Number of<br/>homes</u> | <u>Cost</u>             |
| Finished homes, beginning balance                 | 7                          | \$ 1,874,779          | 4                          | \$ 1,196,260            |
| Costs transferred<br>from construction-in-process | 7                          | 2,691,025             | 18                         | 4,567,799               |
| Reacquisition of previously sold homes            | 2                          | 569,074               | -                          | -                       |
| Homes sold to new owners                          | <u>(14)</u>                | <u>(4,554,684)</u>    | <u>(15)</u>                | <u>(3,889,280)</u>      |
| <br>Finished homes, ending balance                | <br><u>2</u>               | <br><u>\$ 580,194</u> | <br><u>7</u>               | <br><u>\$ 1,874,779</u> |

**Note 6 - Property and equipment, net**

Property and equipment consist of the following:

|                                 | <u>2017</u>             | <u>2016</u>           |
|---------------------------------|-------------------------|-----------------------|
| Land                            | \$ 1,874,778            | \$ -                  |
| Buildings and improvements      | 3,106,581               | -                     |
| Vehicles                        | 245,788                 | 222,289               |
| Equipment                       | 276,577                 | 227,648               |
| Construction in progress        | <u>307,641</u>          | <u>-</u>              |
| <br>Total                       | <br>5,811,365           | <br>449,937           |
| Less accumulated depreciation   | <u>(372,954)</u>        | <u>(327,087)</u>      |
| <br>Property and equipment, net | <br><u>\$ 5,438,411</u> | <br><u>\$ 122,850</u> |

The buildings, land and improvements housing SDHFH's corporate office and ReStore in the Mission Valley area of San Diego were under contract to be sold at June 30, 2016 and were classified as Corporate building held for sale on the consolidated statement of financial position. See Note 7. The sale of the property was completed on May 11, 2017. On May 31, 2017, SDHFH purchased property in the Kearny Mesa area of San Diego consisting of three buildings and land.

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Depreciation expense for the years ended June 30, 2017 and 2016 was \$53,861 and \$63,958, respectively.

**Note 7 - Corporate building held for sale**

As of March 2016, SDHFH anticipated the property to be sold within one year and classified the building as held for sale on the consolidated statement of financial position. Total land, buildings and improvements were \$2,134,852 (net of \$291,626 accumulated depreciation) as of June 30, 2016.

On May 11, 2017, the Organization sold its corporate building for \$3,575,000. The Organization recorded a gain on the sale of \$1,479,973. See Note 22.

**Note 8 - Retail store, net**

SDHFH operates three home improvement stores (the "ReStores") in San Diego, Escondido and National City, California. The ReStores sell new and used home furnishings and building and home improvement materials to the general public. Donations to the ReStores are made by contractors and other businesses, organizations and individuals that have surplus or discontinued merchandise.

The purpose of the ReStores is to raise funds to support SDHFH programs. Accordingly, expenses of operating the ReStores are reported as program expenses in the consolidated statements of functional expenses. The amount of revenue reported from the ReStores includes cash receipts plus the fair market value of donated goods sold, net of the cost of purchased inventory sold. As most revenue earned by the ReStores is from the sale of donated goods, ReStore revenue is classified as support in the consolidated statements of activities and changes in net assets.

Net ReStore revenue is summarized as follows:

|  | <u>2017</u>         | <u>2016</u>         |
|--|---------------------|---------------------|
| Donations to retail store  | \$ 1,623,883        | \$ 1,543,108        |
| Sales of donated and purchased items   | 1,587,509           | 1,536,324           |
| Delivery contributions and other income                                      | 19,669              | 34,806              |
| Fair market value of donated items sold and cost of purchased inventory sold | <u>(1,673,849)</u>  | <u>(1,637,556)</u>  |
| Net revenue from retail store  | <u>\$ 1,557,212</u> | <u>\$ 1,476,682</u> |

**San Diego Habitat for Humanity, Inc.**  
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**Note 9 - Accounts payable, accrued expenses and other liabilities**

Accounts payable, accrued expenses, and other liabilities consist of the following:

|  | <u>2017</u>           | <u>2016</u>           |
|--|-----------------------|-----------------------|
| Accounts payable and other<br>accrued expenses | \$ 285,281            | \$ 440,889            |
| Accrued compensation and payroll liabilities   | 137,754               | 129,317               |
| Deposit on sale of building                    | -                     | 215,000               |
| Contingent liability - project                 | <u>58,494</u>         | <u>58,494</u>         |
| <br>Total                                      | <br><u>\$ 481,529</u> | <br><u>\$ 843,700</u> |

The contingent liability - project relates to estimated costs for a completed construction project in El Cajon, California (see Note 18).

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**Note 10 - Secured obligations - mortgage notes receivable**

The Organization has entered into agreements with several financial institutions in which SDHFH used a portion of its mortgage notes receivable as security for operating loans (see Note 3). Secured obligations consist of the following at June 30, 2017 and 2016:

|   | 2017         | 2016         |
|---|--------------|--------------|
| Four non-interest mortgage notes with Northern Trust Company, entered into on December 18, 2014, originally in the amount of \$651,130, payable in monthly installments, due in July 2040.  | \$ 581,661   | \$ 609,448   |
| Seven non-interest mortgage notes with Pacific Premier Bank, entered into on April 9, 2015, originally in the amount of \$971,654, payable in monthly installments, due in July 2043.   | 876,119      | 920,212      |
| Five non-interest mortgage notes with Pacific Premier Bank, entered into on October 23, 2015, originally in the amount of \$664,639, payable in monthly installments, due in April 2043.  | 607,322      | 643,523      |
| Five non-interest mortgage notes with Northern Trust Company, entered into on October 29, 2015, originally in the amount of \$631,959, payable in monthly installments, due in May 2043.  | 573,882      | 608,728      |
| Eleven non-interest mortgage notes with Pacific Western Bank, entered into on December 23, 2015, originally in the amount of \$1,908,897, payable in monthly installments, due in December 2045.  | 1,812,616    | 1,876,803    |
| Non-interest mortgage notes with Northern Trust Company, entered into on various dates between June 24, 1997 and December 27, 2002, originally in the amount of \$272,377, payable in monthly installments, due in various periods through June 2021. | 36,315       | 52,632       |
| Secured obligations, gross  | 4,487,915    | 4,711,346    |
| Less unamortized discount   | (1,076,500)  | (1,165,056)  |
| Less deferred finance fees, net   | (187,181)    | (194,421)    |
| Net present value of secured obligations  | \$ 3,224,234 | \$ 3,351,869 |



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The following table summarizes the payments due for secured obligations for five years subsequent to June 30, 2017 and thereafter:

|            |           |                  |
|------------|-----------|------------------|
| 2018       | \$        | 218,990          |
| 2019       |           | 218,989          |
| 2020       |           | 213,615          |
| 2021       |           | 213,180          |
| 2022       |           | 207,114          |
| Thereafter |           | 3,416,027        |
|            | <b>\$</b> | <b>4,487,915</b> |

**Note 11 - Notes payable - bank**

Notes payable - Bank consists of the following:

|  | 2017                | 2016                |
|--|---------------------|---------------------|
| <p>The mortgage note with California Bank &amp; Trust originally in the amount of \$1,925,000 bore interest at 4.933% per annum and was payable in 119 monthly installments of \$11,270, with a final balloon payment of approximately \$1,433,000 due in August 2024. The mortgage note was secured by a deed of trust on the Organization's corporate headquarters and retail store in San Diego, California. The corporate headquarters and retail store were sold and the mortgage was paid off in May 2017.</p> | \$ -                | \$ 1,850,568        |
| <p>SDHFH purchased a new property to house its corporate headquarters and San Diego ReStore in May 2017 and obtained a short-term bridge loan from Pacific Western Bank in the amount of \$3,675,000. This interest-only loan bears interest at 4.0% per annum and is due on November 18, 2017. The mortgage loan is secured by a deed of trust on the Organization's new corporate headquarters and ReStore in San Diego.</p>   | 3,675,000           | -                   |
| Total notes payable  | 3,675,000           | 1,850,568           |
| Less deferred finance fees, net  | (7,780)             | (5,804)             |
| Total notes payable, net deferred finance fees, net  | <b>\$ 3,667,220</b> | <b>\$ 1,844,764</b> |

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The following table summarizes the principal payments due for notes payable - Bank subsequent to June 30, 2017 and thereafter:

|            |  |                     |
|------------|--|---------------------|
| 2018       |  | \$ 3,675,000        |
| Thereafter |  | <u>-</u>            |
| Total      |  | <u>\$ 3,675,000</u> |

On August 31, 2017, the Organization refinanced the short-term mortgage note with Pacific Western Bank with a new loan in the amount of \$3,760,000. The new mortgage note bears interest at 3.5% per annum and is owed in full on September 1, 2027. The mortgage note is secured by a deed of trust on the Organization's corporate headquarters and retail store in San Diego, California.

As of June 30, 2017, the Organization was in compliance with its loan covenants with Pacific Western Bank.

**Note 12 - Notes payable - governmental agencies**

Notes payable - governmental agencies as of June 30, 2017 and 2016 consist of the following:

|   | <u>2017</u>       | <u>2016</u>       |
|---|-------------------|-------------------|
| Notes payable, San Diego Housing Commission, require payments of \$248 per month through 2021. The notes have been discounted using imputed interest rates from 9.75% to 11.50%.  | \$ 11,457         | \$ 14,434         |
| Note payable, City of Oceanside, secured by certain mortgage receivables. The note bears no interest, requires monthly payments of \$5,000 and matures in August 2029. The note has been discounted using a 6.0% imputed interest rate. | <u>720,000</u>    | <u>780,000</u>    |
| Total   | 731,457           | 794,434           |
| Less unamortized discount   | <u>(209,691)</u>  | <u>(242,453)</u>  |
| Net present value of notes payable - governmental agencies  | <u>\$ 521,766</u> | <u>\$ 551,981</u> |

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Notes payable to the San Diego Housing Commission and City of Oceanside require monthly payments. The following table summarizes the scheduled principal payments on these notes for five years subsequent to June 30, 2017 and thereafter:

|            |    |                       |
|------------|----|-----------------------|
| 2017       | \$ | 62,976                |
| 2018       |    | 62,976                |
| 2019       |    | 62,976                |
| 2020       |    | 62,529                |
| 2021       |    | 60,000                |
| Thereafter |    | <u>420,000</u>        |
| Total      | \$ | <u><u>731,457</u></u> |

**Note 13 - Forgivable notes payable - governmental agencies**

Forgivable notes payable - governmental agencies as of June 30, 2017 and 2016 consist of the following:

|  | <u>2017</u>              | <u>2016</u>                |
|--|--------------------------|----------------------------|
| Note payable, City of Imperial Beach, secured by the development at 10th and Donax with no interest or payments, forgivable and transferrable to the purchaser of each home. The note was forgiven and transferred to the home buyers as of June 30, 2017.   | \$ -                     | \$ 755,304                 |
| Notes payable, City of El Cajon, pursuant to Home Investment Partnership Program Funds from HUD, secured by deeds of trust on land acquired for construction of low-income housing. These loans require no payments and will be transferred to the purchasers of the homes in the Foundation Lane Phase II development. The promissory notes bear no interest unless SDHFH defaults under the terms of the note. The notes were forgiven and transferred to the home buyers as of June 30, 2017. | -                        | 282,326                    |
| Notes payable, City of Oceanside, secured by two homes at Libby Lake, with no interest or payments, forgivable and transferrable to the purchaser of each home.  | <u>270,000</u>           | -                          |
| Total  | <u><u>\$ 270,000</u></u> | <u><u>\$ 1,037,630</u></u> |

SDHFH is awarded funding by various governmental agencies, generally in the form of a loan to finance, in part, the acquisition and/or development of specific housing projects. These loans are secured by deeds of trust on the related project property. The loans generally are non-interest bearing and have a maturity date of the earlier of one to two years or the sale/transfer of the

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property. Upon project completion, if SDHFH sells/transfers the property to a qualified buyer, the proportionate debt owed by SDHFH on the property is forgiven and transfers to the buyer as a mortgage on the property.

The grant/loan agreements usually require a written disposition and development agreement ("DDA") between SDHFH and the city. These agreements require SDHFH to comply with a number of requirements, including a promise to complete the project within a reasonable period of time and an agreement to sell the home or homes to moderate to low-income families as defined in the DDA. If SDHFH were to fail to comply with the terms of the DDA, it could be required to repay principal and interest as specified in the DDA. As of June 30, 2017 and 2016, management believes that SDHFH is in material compliance with all DDAs and related grant/loan agreements.

As set forth herein, the terms and conditions do not require SDHFH to utilize cash to repay the obligation. Moreover, there are no scheduled maturities of the related debt, since SDHFH is relieved of an obligation to repay the loan upon transfer of the property to a qualified buyer. Accordingly, SDHFH does not believe a table setting forth scheduled maturities of this debt would be meaningful.

**Note 14 - Refundable advances**

Refundable advances as of June 30, 2017 and 2016 consist of the following:

|   | <u>2017</u>       | <u>2016</u>       |
|---|-------------------|-------------------|
| Home funds - City of National City - refundable advances to be utilized for purchase and development of qualifying properties. Utilization of these funds must continue to meet compliance requirements during compliance period. After compliance activities and periods are met, these funds shall become unrestricted. | \$ 220,436        | \$ 406,173        |
| Home funds - City of El Cajon - refundable advances to be utilized for purchase and development of qualifying properties. Utilization of these funds must continue to meet compliance requirements during compliance period. After compliance activities and periods are met, these funds shall become unrestricted.      | <u>-</u>          | <u>280,405</u>    |
| Total   | <u>\$ 220,436</u> | <u>\$ 686,578</u> |

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**Note 15 - Note payable - HFHI**

Note payable - HFHI as of June 30, 2017 and 2016 consists of the following:

|  | <u>2017</u>        | <u>2016</u>              |
|--|--------------------|--------------------------|
| On December 12, 2013, SDHFH entered into a Loan and Security Agreement (the "FlexCap Note") with HFHI under which SDHFH borrowed \$980,000 with a maturity date of December 31, 2020. This loan represented a refinancing of two existing FlexCap notes, resulting in lower quarterly payments. The FlexCap Note was payable in quarterly installments of \$40,026 including interest at 3.80% per annum. SDHFH was required to establish a reserve fund of \$40,026, reported herein as "deposits and other assets." The note was paid off in September 2016. | \$ -               | \$ 659,369               |
| Less deferred financing fees, net  | <u>-</u>           | <u>(6,300)</u>           |
| Totals   | <u><u>\$ -</u></u> | <u><u>\$ 653,069</u></u> |

As of June 30, 2017 and 2016, management believes SDHFH was in compliance with the terms and conditions of the FlexCap Note.

On September 28, 2016, the Organization sold 19 mortgage notes receivable that had previously been used as collateral for the Organization's FlexCap Note payable to HFHI. As part of this transaction, SDHFH paid off the FlexCap Note and accrued interest. See Note 3.

**Note 16 - Notes Payable - construction**

On April 4, 2017, SDHFH purchased land from COMM22, LLC upon which it will build 11 units of affordable for-sale housing. The purchase price for the land was \$200,000, of which \$75,000 was paid at closing and the remaining \$125,000 is due in the form of a non-interest-bearing promissory note. The first \$50,000 payment on the promissory note is due one year from the closing date and the remaining \$75,000 is payable upon the sale of the first home in phase I of the project.

Also as part of the purchase agreement, SDHFH is required to pay \$150,000 to the San Diego Unified School District (SDUSD). Payments representing 5% of the home buyer's first mortgage will be due to SDUSD upon the sale of each of the 11 homes. If after the sale of the final home the total of these payments is less than \$150,000, the payment for the final home shall be increased so that the total of the payments for all 11 homes will be equal to \$150,000.

Total amounts due for these notes payable as of June 30, 2017 were \$275,000.

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**Note 17 - Related party transactions**

SDHFH remits a discretionary portion of its unrestricted contributions (excluding in-kind contributions) to HFHI on an annual basis. These funds are used to construct homes in economically depressed areas around the world. For the years ended June 30, 2017 and 2016, SDHFH remitted \$40,000 and \$40,500, respectively, in tithes to HFHI.

In addition, during the years ended June 30, 2017 and 2016, SDHFH paid a U.S. Stewardship and Organizational Sustainability Fee of \$25,000 to HFHI for each year. Furthermore, for the years ended June 30, 2017 and 2016, SDHFH paid HFHI approximately \$70,000 and \$30,000, respectively, for services provided by Americorps on behalf of SDHFH.

As described in Note 15, SDHFH was party to the FlexCap Note with HFHI. Total amounts due under this note payable as of June 30, 2017 and 2016 were \$0 and \$659,369, respectively.

**Note 18 - Commitments and contingencies**

**Contingent liability**

At June 30, 2017 and 2016, the Organization had certain contingent liabilities related to Phase I of its Foundation Lane project in the City of El Cajon ("El Cajon"). Pursuant to an agreement with El Cajon, SDHFH was permitted to finalize and sell the four-unit development on Foundation Lane prior to the completion of two required infrastructure improvements - the construction of a masonry fence ("Fence Improvement") and the construction of street access to an adjacent arterial street. SDHFH accrued \$58,494 to record the estimated cost of the Fence Improvement at June 30, 2011 and expensed it as a component of cost of homes sold. During the year ended June 30, 2013, SDHFH acquired property adjacent to the Foundation Lane site. SDHFH believes that it will not be required to complete the improvements. However, until a formal release is received from El Cajon's City Council, SDHFH will maintain its existing reserve and as a result retains a liability for \$58,494 as of June 30, 2017 and 2016.

**Leases**

SDHFH leases various systems and equipment under noncancelable leases running through April 2020. Equipment rental expense for the years ended June 30, 2017 and 2016 was \$17,852 and \$16,714, respectively.

In January 2014, SDHFH entered into a lease agreement for its ReStore located in Escondido, California for a 27-month term. In December 2015, SDHFH executed an amendment, extending the original lease term by an additional five years. In October 2016, SDHFH entered into another lease agreement for its new ReStore located in National City, California for 60-month term. The rent expense for the years ended June 30, 2017 and 2016 was \$171,235 and \$67,274.

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Future minimum rental payments under these leases for the five years subsequent to June 30, 2017 are as follows:

|       |                     |
|-------|---------------------|
| 2018  | \$ 237,638          |
| 2019  | 226,800             |
| 2020  | 232,995             |
| 2021  | 217,281             |
| 2022  | <u>87,855</u>       |
| Total | <u>\$ 1,002,569</u> |

**Note 19 - Temporarily restricted net assets**

Temporarily restricted net assets as of June 30, 2017 and 2016 consist of amounts restricted by donor-imposed stipulations as follows:

|                                  | <u>2017</u>       | <u>2016</u>      |
|----------------------------------|-------------------|------------------|
| Unappropriated investment income | \$ 42,529         | \$ 20,562        |
| COMM 22 - Logan Heights project  | <u>70,738</u>     | <u>-</u>         |
| Total                            | <u>\$ 113,267</u> | <u>\$ 20,562</u> |

**Note 20 - Permanently restricted net assets**

Permanently restricted net assets as of June 30, 2017 and 2016 consist of a beneficial interest in assets held by The San Diego Foundation (the "Foundation") which is holding them as an endowed component fund ("Fund") for the benefit of the Organization. The Fund is subject to the Foundation's investment and spending policies, which currently result in a distribution to the Organization of 5%, annually, of the 36-month average principal market value of the Fund. Distributions are generally made semi-annually. The Organization reports the fair value of the Fund as a beneficial interest in assets held at a community foundation in the consolidated statements of financial position and reports distributions received as a reduction to the Fund balance. Changes in the value of the Fund are reported as temporarily restricted investment income in the consolidated statements of activities and changes in net assets.

**Interpretation of relevant law**

The Organization has interpreted the State of California's Uniform Prudent Management of Institutional Funds Act ("UPMIFA") as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the Organization has classified as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The earnings of the donor-restricted endowment fund are classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Foundation in a manner consistent with the standard of prudence prescribed by UPMIFA. In accordance with UPMIFA, the Organization considers the following factors in making a determination to appropriate or accumulate donor-restricted endowment funds:

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- (1) The duration and preservation of the fund;
- (2) The purposes of the Organization and the donor-restricted endowment fund;
- (3) General economic conditions;
- (4) The possible effect of inflation and deflation;
- (5) The expected total return from income and the appreciation of investments;
- (6) Other resources of the Organization; and
- (7) The investment policies of the Organization.

The following is a summary of changes in endowment net assets for the year ended June 30, 2017:

|                               | Unrestricted | Temporarily<br>restricted | Permanently<br>restricted | Total             |
|-------------------------------|--------------|---------------------------|---------------------------|-------------------|
| Fund balance, beginning       | \$ -         | \$ 20,562                 | \$ 303,059                | \$ 323,621        |
| Fund appreciation             | -            | 38,675                    | -                         | 38,675            |
| Investment expenses           | -            | (1,648)                   | -                         | (1,648)           |
| Distributable grants approved | -            | (15,060)                  | -                         | (15,060)          |
| Fund balance, end             | <u>\$ -</u>  | <u>\$ 42,529</u>          | <u>\$ 303,059</u>         | <u>\$ 345,588</u> |

The following is a summary of changes in endowment net assets for the year ended June 30, 2016:

|                               | Unrestricted | Temporarily<br>restricted | Permanently<br>restricted | Total             |
|-------------------------------|--------------|---------------------------|---------------------------|-------------------|
| Fund balance, beginning       | \$ -         | \$ 42,630                 | \$ 303,059                | \$ 345,689        |
| Fund appreciation             | -            | (5,456)                   | -                         | (5,456)           |
| Investment expenses           | -            | (1,590)                   | -                         | (1,590)           |
| Distributable grants approved | -            | (15,022)                  | -                         | (15,022)          |
| Fund balance, end             | <u>\$ -</u>  | <u>\$ 20,562</u>          | <u>\$ 303,059</u>         | <u>\$ 323,621</u> |

**Funds with deficiencies**

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level that the donor or UPMIFA requires the Organization to retain as a fund of perpetual duration. There were no deficiencies of this nature that were reported in unrestricted net assets as of June 30, 2017 and 2016.

**Return objectives and risk parameters**

The Organization has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of the endowment assets. Endowment assets include those assets of donor-restricted funds that the Organization must hold in perpetuity. Under this policy, as approved by the Board of Directors, the endowment assets are invested in a manner that follows the policies of the Foundation. Actual returns in any given year may vary from this expected return. See Note 21.



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**Strategies for achieving objectives**

To satisfy its long-term rate-of-return objectives, the Organization relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). The Organization uses a diversified asset allocation that places a greater emphasis on equity-based investments to achieve its long-term objectives within prudent risk parameters.

**Spending policy and how the investment objectives relate to the spending policy**

The Organization follows the policies of the Foundation in determining the distribution amount to be appropriated each year. In establishing this policy, the Organization considered the long-term expected return on its endowment. Accordingly, over the long term, the Organization expects the current spending policy to allow its endowment to grow at an average annual rate equal to the general inflation rate. This is consistent with the Organization's objective to maintain the purchasing power of the endowment assets held in perpetuity or for a specified term as well as to provide additional real growth through new gifts and investment return.

**Note 21 - Assets and liabilities measured at fair value on a recurring basis**

The Organization values its financial assets and liabilities based on the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. In order to increase consistency and comparability in fair value measurements, a fair value hierarchy that prioritizes observable and unobservable inputs is used to measure fair value into three broad levels, which are described below:

- Level 1: Quoted prices are available in active markets for identical investments as of the reporting date. The type of investments in Level 1 include listed equities, bond instruments, and mutual funds held in the name of the Organization, and exclude listed equities and other securities held indirectly through commingled funds.
- Level 2: Pricing inputs, including broker quotes, are generally those other than exchange quoted prices in active markets, which are either directly or indirectly observable as of the reporting date, and fair value is determined through the use of models or other valuation methodologies.
- Level 3: Pricing inputs are unobservable for the investment, including situations where there is little, if any, market activity for the investment. The inputs into the determination of fair value require significant management judgment or estimation. Investments that are included in this category generally include privately held investments and partnership interests.

The inputs and methodology used for valuing the Organization's financial assets and liabilities are not indicators of the risks associated with those instruments.

There have been no changes in methodology during the year.

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The following table sets forth by level, within the fair value hierarchy, SDHFH's assets at fair value as of June 30, 2017:

|  | <u>Level 1</u> | <u>Level 2</u> | <u>Level 3</u>    | <u>Total</u>      |
|--|----------------|----------------|-------------------|-------------------|
| Beneficial interest in assets held by community foundation | \$ -           | \$ -           | \$ 345,588        | \$ 345,588        |
| Total assets at fair value                                 | <u>\$ -</u>    | <u>\$ -</u>    | <u>\$ 345,588</u> | <u>\$ 345,588</u> |

The following table sets forth by level, within the fair value hierarchy, SDHFH's assets at fair value as of June 30, 2016:

|  | <u>Level 1</u> | <u>Level 2</u> | <u>Level 3</u>    | <u>Total</u>      |
|--|----------------|----------------|-------------------|-------------------|
| Beneficial interest in assets held by community foundation | \$ -           | \$ -           | \$ 323,621        | \$ 323,621        |
| Total assets at fair value                                 | <u>\$ -</u>    | <u>\$ -</u>    | <u>\$ 323,621</u> | <u>\$ 323,621</u> |

The following table sets forth a summary of changes in the fair value of SDHFH's Level 3 assets for the years ended June 30, 2017 and 2016:

|                      | <u>2017</u>       | <u>2016</u>       |
|----------------------|-------------------|-------------------|
| Balance, beginning   | \$ 323,621        | \$ 345,689        |
| Investment return    | 37,027            | (7,046)           |
| Distributed to SDHFH | <u>(15,060)</u>   | <u>(15,022)</u>   |
| Balance, end         | <u>\$ 345,588</u> | <u>\$ 323,621</u> |

The following table represents SDHFH's Level 3 financial instruments, the valuation techniques used to measure the fair value of those financial instruments, and the significant unobservable inputs and the ranges of values for those inputs for 2017:

| <u>Instrument</u>  | <u>Fair value</u> | <u>Principal valuation technique</u>                  | <u>Unobservable inputs</u>    | <u>Significant input values</u> | <u>Weighted average</u> |
|--|-------------------|---|-------------------------------|---------------------------------|-------------------------|
| Beneficial interest in assets held by community foundation | \$ 345,588        | Valuation of underlying assets as provided by trustee | Investment period (liquidity) | N/A                             | N/A                     |

The following table represents SDHFH's Level 3 financial instruments, the valuation techniques used to measure the fair value of those financial instruments, and the significant unobservable inputs and the ranges of values for those inputs for 2016:

| <u>Instrument</u>  | <u>Fair value</u> | <u>Principal valuation technique</u>                  | <u>Unobservable inputs</u>    | <u>Significant input values</u> | <u>Weighted average</u> |
|--|-------------------|---|-------------------------------|---------------------------------|-------------------------|
| Beneficial interest in assets held by community foundation | \$ 323,621        | Valuation of underlying assets as provided by trustee | Investment period (liquidity) | N/A                             | N/A                     |

The Organization's investments consist entirely of the beneficial interest in assets held at the Foundation and are classified as Level 3 investments as described above. Accordingly, the changes in the value of Level 3 financial instruments are set forth in the tables above.

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The beneficial interest in assets held at the Foundation has been valued, as a practical expedient, at the fair value of the Organization's share of the Foundation's investment pool as of June 30, 2017 and 2016. The Foundation values securities and other financial instruments on a fair value basis of accounting. The estimated fair values of certain investments of the Foundation, which include private placements and other securities for which prices are not readily available, are determined by the management of the Foundation and may not reflect amounts that could be realized upon immediate sale, nor amounts that ultimately may be realized. Accordingly, the estimated fair values may differ significantly from the values that would have been used had a ready market existed for these investments. The Foundation's target asset allocation for the Fund is 45% global equities, 17% fixed income instruments (domestic and international), 25% alternative investments and 13% real assets. The beneficial interest in assets held at the Foundation is not redeemable by the Organization.

**Note 22 - Other income**

|   | <u>2017</u>         | <u>2016</u>      |
|---|---------------------|------------------|
| Gain on sale of mortgage notes receivable | \$ 755,469          | \$ -             |
| Gain on sale of corporate building        | 1,479,973           | -                |
| Other income                              | <u>56,160</u>       | <u>88,167</u>    |
| Total                                     | <u>\$ 2,291,602</u> | <u>\$ 88,167</u> |

**Note 23 - Subsequent event**

On August 31, 2017, the Organization refinanced the short-term mortgage note with Pacific Western Bank with a new loan in the amount of \$3,760,000. See Note 11.