VALUE LINE US GOVERNMENT SECURITIES FUND INC
Form DEF 14A
September 20, 2010

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

SCHEDULE 14A
(Rule 14a-101)

INFORMATION REQUIRED IN PROXY STATEMENT
SCHEDULE 14A INFORMATION
Proxy Statement Pursuant to Section 14(a) of the
Securities Exchange Act of 1934
(Amendment No. ___)

Filed by the Registrant x

Filed by a Party other than the Registrant o

Check the appropriate box:

o	Preliminary Proxy Statement
o	Confidential, for Use of the Commission Only (as permitted by Rule 14a-6(e)(2))
x	Definitive Proxy Statement
o	Definitive Additional Materials
o	Soliciting Material under Rule 14a-12

Value Line Aggressive Income Trust
Value Line Asset Allocation Fund, Inc.
Value Line U.S. Government Money Market Fund, Inc.
Value Line Centurion Fund, Inc.
Value Line Convertible Fund, Inc.
Value Line Emerging Opportunities Fund, Inc.
The Value Line Fund, Inc.
Value Line Income and Growth Fund, Inc.
Value Line Larger Companies Fund, Inc.
Value Line New York Tax Exempt Trust
Value Line Premier Growth Fund, Inc.
Value Line Strategic Asset Management Trust
The Value Line Tax Exempt Fund, Inc.
Value Line U.S. Government Securities Fund, Inc.
(Name of Registrant as Specified in its Charter)

(Name of Person(s) Filing Proxy Statement, if other than the Registrant)

Payment of Filing Fee (Check the appropriate box):

x No fee required.

o Fee computed on table below per Exchange Act Rules 14a-6(i)(1) and 0-11.

(1) Title of each class of securities to which transaction applies:

(2) Aggregate number of securities to which transaction applies:

(3) Per unit price or other underlying value of transaction computed pursuant to Exchange Act Rule 0-11 (set forth the amount on which the filing fee is calculated and state how it was determined):

(4) Proposed maximum aggregate value of transaction:

(5) Total fee paid:

o Fee paid previously with preliminary materials:

o Check box if any part of the fee is offset as provided by Exchange Act Rule 0-11 (a)(2) and identify the filing for which the offsetting fee was paid previously. Identify the previous filing by registration statement number, or the Form or Schedule and the date of its filing.

(1) Amount previously paid:

(2) Form, Schedule or Registration Statement No.:

(3) Filing Party:

(4) Date Filed:

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Value Line Premier Growth Fund, Inc.
Value Line Strategic Asset Management Trust
The Value Line Tax Exempt Fund, Inc.
Value Line U.S. Government Securities Fund, Inc.

220 East 42nd Street
New York, New York 10017-5891

NOTICE OF SPECIAL MEETING OF SHAREHOLDERS
TO BE HELD ON OCTOBER 26, 2010

Notice is hereby given that a first Special Meeting of Shareholders (the “Meeting”) of each of the investment companies set forth above (each, a “Fund” and collectively, the “Funds”) will be held at the offices of Wilmer Cutler Pickering Hale and Dorr LLP, 399 Park Avenue, New York, New York 10022 on October 26, 2010 at 2:00 p.m. (Eastern Time).

The Meeting is being called to consider and act upon the following proposal for each Fund and to transact such other business as may properly come before the Meeting:

> To elect three nominees for Directors, as named in the Proxy Statement, of each Fund, each of whom will serve until he or she resigns, is removed, dies or becomes incapacitated.

The close of business on August 25, 2010 has been fixed as the record date for the determination of shareholders entitled to notice of and to vote at the Meeting and any adjournment(s) or postponement(s) thereof.

PLEASE EXECUTE AND RETURN THE ENCLOSED PROXY CARD PROMPTLY IN THE ENVELOPE PROVIDED WHETHER OR NOT YOU INTEND TO BE PRESENT AT THE MEETING. YOU MAY REVOKE YOUR PROXY AT ANY TIME BEFORE IT IS VOTED. NO POSTAGE IS REQUIRED IF THE PROXY IS MAILED IN THE UNITED STATES.

THE BOARD (INCLUDING ALL OF THE INDEPENDENT DIRECTORS) OF EACH FUND RECOMMENDS THAT YOU VOTE IN FAVOR OF THE PROPOSAL.

This is a Joint Notice and Proxy Statement for the Funds. The shares you own in a particular Fund may only be voted with respect to that Fund. If you own shares in more than one of the Funds listed, please vote with respect to each such Fund.

If you have any questions regarding the proposal or need assistance in completing your proxy cards or casting your vote by the live operator, the touchtone phone process or via the Internet, please call D. F. King & Co., Inc., a professional proxy solicitation firm that has been engaged to assist shareholders in the voting process, at 1-800-545-3393 (toll-free). Representatives are available Monday through Friday, 8:00 a.m.- 10:00 p.m. (Eastern Time), and Saturday, 11:00 a.m. - 6:00 p.m. (Eastern Time).

Important Notice Regarding the Availability of Proxy Materials for the Meeting: This Notice of Special Meeting of Shareholders, the Proxy Statement and the forms of proxy cards are available on the Internet at www.kingproxy.com/vl. On this website, you will be able to access the Notice of Special Meeting of Shareholders, the Proxy Statement, the form of proxy cards and any amendments or supplements to the foregoing material that are required to be furnished to shareholders.

By Order of the Boards of Directors,

/s/ Howard A. Brecher

Howard A. Brecher
Secretary

September 20, 2010

Value Line Aggressive Income Trust
Value Line Asset Allocation Fund, Inc.
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The Value Line Tax Exempt Fund, Inc.
Value Line U.S. Government Securities Fund, Inc.

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New York, New York 10017-5891

NOTICE OF SPECIAL MEETING OF SHAREHOLDERS

TO BE HELD ON OCTOBER 26, 2010

Notice is hereby given that a second Special Meeting of Shareholders (the “Meeting”) of each of the investment companies set forth above (each, a “Fund” and collectively, the “Funds”) will be held at the offices of Wilmer Cutler Pickering Hale and Dorr LLP, 399 Park Avenue, New York, New York 10022 on October 26, 2010 at 2:30 p.m. (Eastern Time).

The Meeting is being called to consider and act upon the following proposal for each Fund and to transact such other business as may properly come before the Meeting:

To approve a new investment advisory agreement between each Fund and EULAV Asset Management.

The close of business on August 25, 2010 has been fixed as the record date for the determination of shareholders entitled to notice of and to vote at the Meeting and any adjournment(s) or postponement(s) thereof.

PLEASE EXECUTE AND RETURN THE ENCLOSED PROXY CARD PROMPTLY IN THE ENVELOPE PROVIDED WHETHER OR NOT YOU INTEND TO BE PRESENT AT THE MEETING. YOU MAY REVOKE YOUR PROXY AT ANY TIME BEFORE IT IS VOTED. NO POSTAGE IS REQUIRED IF THE PROXY IS MAILED IN THE UNITED STATES.

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By Order of the Boards of Directors,

/s/ Howard A. Brecher

Howard A. Brecher
Secretary

September 20, 2010

PROXY STATEMENT

Value Line Aggressive Income Trust
Value Line Asset Allocation Fund, Inc.
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The Value Line Tax Exempt Fund, Inc.
Value Line U.S. Government Securities Fund, Inc.

220 East 42nd Street
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SPECIAL MEETINGS OF SHAREHOLDERS

This Proxy Statement contains the information that you should know before voting on the proposals summarized below. If you attend either of the two special meetings of shareholders (the " Meetings ") of the Value Line Mutual Funds listed above (each, a "Fund" and collectively, the "Funds") to which this Proxy Statement relates, you may vote your shares in person. This is a Joint Proxy Statement for the Funds. The shares you own in a particular Fund may only be voted with respect to that Fund. If you own shares in more than one Fund, please vote with respect to each such Fund. Even if you do not attend the Meetings , you may vote by proxy in one of the following three simple ways:

Internet – Simply log on to the website address located on your Proxy Cards . You will need the control number found on the Proxy Cards at the time you execute your vote.

Touchtone Phone – Simply dial the toll-free number on the enclosed Proxy Cards and follow the automated instructions. Please have the Proxy Cards available at the time of the call.

Mail – Simply sign, date, and complete the reverse side of the Proxy Cards and return them in the postage-paid envelope provided.

The Board plans to begin sending this Proxy Statement, the attached notices of the Meetings and the enclosed Proxy Cards on or about September 20, 2010 to all shareholders entitled to vote.

Your vote is very important. If many shareholders choose not to vote, a Fund may not receive enough votes to reach a quorum in order to conduct the Meetings for that Fund. Whether or not you plan to attend the Meetings in person, please mark, sign, date, and return the enclosed Proxy Cards in the enclosed postage-paid envelope or vote by touchtone phone or via the Internet today.

Photographic identification will be required for admission to the Meetings .

Each Fund will furnish, without charge, a copy of its most recent annual report and most recent semi-annual report to any shareholder upon request. Shareholders who want to obtain a copy of their Fund's report (excluding Value Line Strategic Asset Management Trust and Value Line Centurion Fund, Inc.) should call 1-800-243-2729 (toll-free), write to the Fund at the above address or visit the Funds' website, www.vlfunds.com, and click on Annual Reports. Copies of annual and semi-annual reports of each Fund are also available on the EDGAR Database on the Securities and Exchange Commission's Internet site at www.sec.gov. For annual and semi-annual reports for Value Line Strategic Asset Management Trust and Value Line Centurion Fund, Inc., please call The Guardian Insurance & Annuity Company, Inc. at 800-221-3253 or visit online at www.guardianinvestor.com/public/products/prospectus.aspx, then click on Underlying Funds and then click on EULAV.

Please note that only one annual or semi-annual report or this Proxy Statement may be delivered to two or more shareholders of a Fund who share an address, unless the Fund has received instructions to the contrary. To request a separate copy of an annual report, semi-annual report or this Proxy Statement, shareholders should contact the applicable Fund at the address and phone number set forth above.

Introduction

This Proxy Statement is being furnished to shareholders of each Fund in connection with the solicitation of proxies by each Fund's Board of Directors (collectively, the "Board") for the Meetings to be held at the offices of Wilmer Cutler Pickering Hale and Dorr LLP located at 399 Park Avenue, New York, New York 10022 on October 26, 2010. The first Meeting will be held at 2:00 p.m. (Eastern Time) and the second Meeting will be held at 2:30 p.m. (Eastern Time).

Each Fund is registered with the Securities and Exchange Commission (the "SEC") as an open-end management investment company under the Investment Company Act of 1940, as amended (the "1940 Act").

PROPOSALS

The following table summarizes the proposals to be presented at the Meetings and the Funds to which they apply:

FIRST MEETING ("MEETING #1")

PROPOSAL	FUNDS	PAGE NUMBER
Elect three nominees for Directors of the Funds, as named in this Proxy Statement, each of whom will serve until he or she resigns, is removed, dies, retires or becomes incapacitated.	All Funds	5

SECOND MEETING ("MEETING #2")

PROPOSAL	FUNDS	PAGE NUMBER
Approve a new investment advisory agreement between each Fund and EULAV Asset Management ("EULAV" or "Adviser").	All Funds	17

The proposals are being submitted to a vote of shareholders in light of the intention by Value Line, Inc. ("VLI"), the parent company of the Adviser and EULAV Securities, Inc., the Funds' principal underwriter (the "Distributor" or "ESI"), to restructure the ownership and control of the Adviser and the Distributor as more fully described below in this Proxy Statement under "Description of the Restructuring" (the "Restructuring") under the heading " Meeting #2 - Investment Advisory Proposal "

A new investment advisory agreement between the restructured Adviser (which will be named EULAV Asset Management) and each Fund (the "New Investment Advisory Agreement") is being proposed because each Fund's current investment advisory agreement with the Adviser (the "Current Investment Advisory Agreement") will terminate upon the closing of the Restructuring (the "Closing"). The Restructuring will result in a change of control of the Adviser and, as a result, the Current Investment Advisory Agreements will automatically terminate. Consequently, each Fund's new investment advisory agreement, which must be approved by that Fund's shareholders, will be necessary in order for the investment management of each Fund to continue uninterrupted after the Closing.

Under the New Investment Advisory Agreements, the services to be provided by the restructured Adviser after the Closing and the rates at which fees are to be paid by each Fund are the same as under the Current Investment Advisory Agreements. In addition, the other terms of the New Investment Advisory Agreement are the same as the Current Investment Advisory Agreements, except for the date of execution, the two-year initial term, immaterial updating changes and immaterial changes in form.

As described in greater detail under the heading "Meeting #1 - Election of Directors" below in this Proxy Statement, the Board also recommends that each Fund's shareholders elect three persons, Ms. Joyce Heinzerling and Messrs. Mitchell E. Appel and Daniel S. Vandivort, to serve as directors. Each of Ms. Heinzerling and Mr. Vandivort are currently serving as directors who are not "interested persons" (within the meaning of the 1940 Act) ("Independent Directors") of each Fund and were previously appointed by the Board in accordance with the requirements of the 1940 Act. Mr. Appel is the President of the Adviser and the Funds but is not currently serving as a director of the Funds.

No business other than the Election of Directors Proposal (Meeting #1) and the Investment Advisory Proposal (Meeting #2) may properly be presented for consideration at the Meetings . If any other procedural matter relating to a proposal at one of the Meetings is properly presented at such Meeting, it is the intention of the persons named in the enclosed forms of proxy to vote in accordance with their discretion.

THE BOARD (INCLUDING ALL OF THE INDEPENDENT DIRECTORS) RECOMMENDS THAT YOU VOTE IN FAVOR OF THE PROPOSALS.

Each shareholder is entitled to one vote for each share (and a fractional vote for each fractional share) outstanding in such shareholder's name on the books of each Fund on August 25, 2010 (the "Record Date"). Shareholders who owned shares of any Fund at the close of business on the Record Date are entitled to vote on all of their Fund's business at the Meetings and any adjournments thereof.

The following table sets forth the number of shares outstanding as of the Record Date for each Fund:

FUND	SHARES OUTSTANDING AS OF THE RECORD DATE
Value Line Aggressive Income Trust	7,308,001.170
Value Line Asset Allocation Fund, Inc.	3,116,549.805
Value Line U.S. Government Money Market Fund, Inc.	115,819,737.383
Value Line Centurion Fund, Inc.	11,832,889.460
Value Line Convertible Fund, Inc.	2,127,079.749
Value Line Emerging Opportunities Fund, Inc.	11,954,345.067
The Value Line Fund, Inc.	12,665,515.992
Value Line Income and Growth Fund, Inc.	41,768,630.332
Value Line Larger Companies Fund, Inc.	11,855,253.900
Value Line New York Tax Exempt Trust	1,917,085.140
Value Line Premier Growth Fund, Inc.	12,013,208.777
Value Line Strategic Asset Management Trust	20,836,818.417
The Value Line Tax Exempt Fund, Inc.	8,829,488.058
Value Line U.S. Government Securities Fund, Inc.	7,054,974.346

It is important for you to vote on the proposals described in this Proxy Statement. We recommend that you read this Proxy Statement in its entirety. The explanation provided in the Proxy Statement will help you to decide on the issues.

MEETING #1

ELECTION OF DIRECTORS PROPOSAL 1

The purpose of the proposal being submitted to a vote at Meeting #1 is to elect three nominees as Directors to the Board: Ms. Joyce E. Heinzerling and Messrs. Mitchell E. Appel and Daniel S. Vandivort (the "Nominees"). Ms. Heinzerling and Mr. Vandivort are currently serving as Independent Directors on the Board by Board appointment in accordance with the requirements of the 1940 Act, and Mr. Vandivort is currently serving as the Board's Chairman. Mr. Appel, President of the Adviser and the Funds, is not currently serving on the Board.

The Board currently consists of seven Directors - Mmes. Heinzerling and Nancy-Beth Sheerr, and Messrs. Thomas T. Sarkany, Francis C. Oakley, David H. Porter, Paul Craig Roberts and Vandivort. All of the current Directors, except for Mr. Sarkany, are Independent Directors. Four of the current Directors - Ms. Sheerr and Messrs. Oakley, Porter, and Roberts - were previously duly elected by shareholders, while three - Ms. Heinzerling and Messrs. Sarkany and Vandivort - are serving by Board appointment in accordance with the requirements of the 1940 Act.

If the Nominees are elected, Ms. Heinzerling and Mr. Vandivort will continue as Directors and Mr. Appel will become a Director. Mr. Sarkany has stated that he will resign from the Board effective upon the election of Mr. Appel and completion of the Restructuring. As a result, the Board will continue to consist of seven Directors - all of whom will have been elected by shareholders. If the Nominees are elected, the Independent Directors will continue to constitute more than 75% of the Board and the Funds will continue to have an Independent Director (Mr. Vandivort) serving as their Chairperson. A person is referred to as "Independent" if he or she is not an "interested person" (as defined in the 1940 Act) of the Fund and a person is referred to as "Interested" if he or she is an "interested person" (as so defined) of the Fund.

Each Nominee will be elected by shareholders to hold office until he or she resigns, is removed, dies, retires or becomes incapacitated. Each Nominee has consented to being named in this Proxy Statement and has indicated his or her willingness to serve if elected. In the unanticipated event that any Nominee should be unable to serve, the persons named as proxies on the enclosed Proxy Card may vote for such other person as shall be designated by the Board. The persons named as proxies on the enclosed Proxy Card intend to vote at Meeting #1 (unless otherwise directed) for the election of the Nominees.

1 Some of the Funds are organized as Massachusetts business trusts and the other Funds are organized as Maryland corporations. References in this Proxy Statement to "directors" include both the trustees of those Funds that are Massachusetts business trusts and directors of those Funds that are Maryland corporations.

The following table sets forth each Nominee's name, year of birth, position(s) with the Funds, principal occupation and employment during the past five years, the number of portfolios in the same "fund complex" as the Funds that the Nominee would oversee if elected, and other directorships held by the Nominee. The address of each Nominee for purposes of Fund business is c/o Value Line Mutual Funds, 220 East 42nd Street, New York, NY 10017.

Name and Year of Birth	Position(s) with the Funds, Length of Service	Principal Occupation During Past Five Years	Number of Portfolios in Fund Complex Overseen by Nominee(1)	Other Directorships
Independent Nominees:				
Joyce E. Heinzerling (1956)	Director (since 2008).	Principal, Meridian Fund Advisers LLC. (consultants) since April 2009; General Counsel, Archery Capital LLC (private investment fund), until April 2009.	14	Director, each of the Value Line Mutual Funds since 2008 (14 Funds); Trustee, Burnham Investors Trust, since 2004 (4 funds)
Daniel S. Vandivort (1954)	Director (since 2008); Chair (since 2010).	President, Chief Investment Officer, Weiss, Peck and Greer/Robeco Investment Management 2005–2007; Managing Director, Weiss, Peck and Greer, 1995–2005.	14	Director (since 2008) and Chairperson (since 2010), each of the Value Line Mutual Funds (14 Funds)
Interested Nominee:				
Mitchell E. Appel* (1970)	President (since 2008)/ Nominee	President of each of the Funds since June 2008; Chief Financial Officer of VLI since April 2008 and from September 2005 to November 2007 and Treasurer from June 2005 to September 2005; Chief Financial Officer of XTF Asset Management from November 2007 to April 2008; Chief Financial Officer of the Distributor since April 2008 and President since February 2009; President of the Adviser since February 2009.	14	Director of VLI since February 2010

(1) In accordance with SEC rules, the number of portfolios included in this column assumes that the Nominee has been elected.

* Mr. Appel, the President of the Adviser and each Fund, does not currently serve as a Director of any Funds. If he becomes a Director, he will resign all of his positions with VLI and will serve as an Interested Director by virtue of his positions with the Adviser and the Distributor. Each of Ms.

Heinzerling and Mr. Vandivort currently serves as an Independent Director of each Fund.

The following table sets forth each Director's (unless disclosed in the prior table) name, year of birth, position(s) with the Funds, principal occupation and employment during the past five years, the number of portfolios in the same "fund complex" as the Funds that the Director oversees, and other directorships held by the Director. The address of each Director for purposes of Fund business is c/o Value Line Mutual Funds, 220 East 42nd Street, New York, NY 10017.

Name and Year of Birth	Position(s) with the Funds, Length of Service	Principal Occupation During Past Five Years	Number of Portfolios in Fund Complex Overseen by Director	Other Directorships
Independent Director:				
Francis C. Oakley (1931)	Director (since 2000)	Professor Emeritus of History, Williams College since 2002, President Emeritus since 1994 and President, 1985–1994; Trustee since 1997 and Chairman of the Board since 2005, National Humanities Center.	14	**
David H. Porter (1935)	Director (since 1997).	Professor, Skidmore College since 2008; Visiting Professor of Classics, Williams College, 1999–2008; President Emeritus, Skidmore College since 1999 and President, 1987–1998.	14	**
Paul Craig Roberts (1939)	Director (since 1983).	Chairman, Institute for Political Economy.	14	**
Nancy-Beth Sheerr (1949)	Director (since 1996).	Senior Financial Advisor, Veritable, L.P. (investment advisor).	14	**

** Each Director currently serves as an Independent Director of each Fund. Mr. Thomas T. Sarkany currently serves as an Interested Director of each Fund by virtue of his positions with VLI, the Adviser and the Distributor. Since he will not continue as a Director after closing of the Restructuring, which is anticipated to occur shortly after the Meetings , his information is omitted from this Proxy Statement.

Board of Directors Structure.

The Board is comprised of seven Directors, six of whom (85%) are Independent Directors. The Board has appointed Mr. Vandivort (an Independent Director) as its Chairperson. The Board has established three standing committees: the Audit Committee, the Nominating/Governance Committee and the Valuation Committee. The Audit Committee and the Nominating/Governance Committee are chaired by, and composed entirely of, Independent Directors. The Valuation Committee is composed of an Independent Director and an Interested Director. See “Committees and Board Meetings” below for a further description of the composition, duties and responsibilities of these committees.

The Directors and the members of the Board’s committees annually evaluate the performance of the Board and the committees, which evaluation includes considering the effectiveness of the Board’s committee structure. The Board believes that its leadership structure, including an Independent Director as the Board’s Chairperson, is appropriate in light of the asset size of the Funds, the number of Funds, and the nature of the Funds’ business, and is consistent with industry best practices. In particular, the Board believes that having a super-majority of Independent Directors and an Independent Chairperson are appropriate and in the best interests of the Funds’ shareholders.

Risk Oversight by the Board.

As part of its responsibilities for oversight of the Funds, the Board oversees risk management of the Funds’ investment programs and business affairs. The Board performs its oversight responsibilities as part of its Board and Committee activities. The Independent Directors also regularly meet outside the presence of management and have engaged independent legal counsel to assist them in performing their oversight responsibilities. The Board has delegated to the Audit Committee oversight responsibility of the integrity of the Funds’ financial statements, the Funds’ compliance with legal and regulatory requirements as they relate to the financial statements, the independent auditor’s qualifications and independence, the Funds’ internal controls over financial reporting, the Funds’ disclosure controls and procedures and the Funds’ code of business conduct and ethics pursuant to the Sarbanes-Oxley Act of 2002. The Audit Committee reports areas of concern, if any, to the Board for discussion and action.

The Board, including the Independent Directors, has approved the Funds’ compliance program and appointed the Funds’ Chief Compliance Officer, who is responsible for testing the compliance procedures of the Funds and certain of their service providers. Senior management and the Chief Compliance Officer report at least quarterly to the Board regarding compliance matters relating to the Funds, and the Chief Compliance Officer annually assesses (and reports to the Board regarding) the operation of the Funds’ compliance program. The Independent Directors generally meet at least quarterly with the Chief Compliance Officer outside the presence of management.

Qualifications and Experience of the Board and Nominees.

The Board believes that each Director's and Nominee's experience, qualifications, attributes and skills on an individual basis and in combination with those of the other Directors and Nominees lead to the conclusion that each Director and Nominee should serve in such capacity. Among other attributes common to all Directors are their ability to review critically, evaluate, question and discuss information provided to them, to interact effectively with the Adviser, other service providers, counsel and the independent registered public accounting firm, to exercise effective business judgment in the performance of their duties, and to represent the interests of all the shareholders. The ability of a Director and Nominee to perform his duties effectively may have been attained through his educational background or professional training; business, consulting or academic leadership positions; experience from service as a Director or officer (in the case of Mr. Appel) of the Funds, or in various roles at public companies, private entities or other organizations; and/or other life experiences. In addition to these shared characteristics, set forth below is a brief discussion of the specific qualifications, attributes or skills of each Director and Nominee that lead to the conclusion that each person is qualified to serve as a Director. The charter of the Nominating/Governance Committee specifically requires the value of diversity on the Board to be considered and precludes discrimination against nominees on the basis of age, race, religion, national origin, sex, sexual orientation, disability or any other basis proscribed by law.

Ms. Heinzerling has served as an Independent Director on the Board since 2008. Her relevant experience includes being a principal of a regulatory consulting company, former general counsel to an investment adviser and a director of an unaffiliated mutual fund family.

Dr. Oakley has served as an Independent Director on the Board since 2000. His relevant experience includes being the former president of a college with endowment fund oversight responsibility and serving in other leadership positions and serving on other boards.

Dr. Porter has served as an Independent Director on the Board since 1997. His relevant experience includes being the former president of a college with endowment fund oversight responsibility and serving in other leadership positions and serving on other boards.

Dr. Roberts has served as an Independent Director on the Board since 1983. His relevant experience includes being an economist and a former Assistant Secretary of the U.S. Treasury and a nationally syndicated columnist.

Ms. Sheerr has served as an Independent Director on the Board since 1996. Her relevant experience includes being a senior financial adviser of an investment adviser and serving on other boards, including as chairman, with endowment fund oversight responsibility.

Mr. Vandivort has served as an Independent Director on the Board since 2008. His relevant experience includes being the former president and chief investment officer of an investment adviser and former chairman of a mutual fund group.

Mr. Appel has served as President of each Fund since 2008 and Chief Financial Officer of VLI since September 2005 (excluding November 2007 – April 2008). His relevant experience also includes being a Director of VLI, and serving in senior officer positions with other asset management companies.

Material Relationships of the Independent Director Nominees.

As of July 31, 2010, none of the Independent Directors (including the Nominees that are Independent Directors), nor any of their “immediate family members” (as defined below), had any direct or indirect interest whether by contract, arrangement or otherwise, in any of (i) EULAV, the Funds’ current investment adviser, (ii) VLI, the Funds’ investment adviser prior to June 30, 2008, (iii) the Distributor, the Funds’ principal underwriter and distributor or (iv) any other “entity in a control relationship” (as defined below) to EULAV, VLI or the Distributor.

During the calendar years 2008 and 2009, none of the Independent Directors (including the Nominees that are Independent Directors), nor any of their immediate family members, had an interest in a transaction or a series of similar transactions, or in any currently proposed transaction, or series of similar transactions, in which the aggregate amount involved exceeded $120,000 and to which any of the following were a party (each, a “Fund Related Party”):

a Fund

an officer of a Fund

a “related fund” (as defined below)

an officer of any related fund

EULAV, VLI or the Distributor

an officer of EULAV, VLI or the Distributor

an entity in a control relationship with EULAV, VLI, or the Distributor

an officer of an entity in a control relationship with EULAV, VLI or the Distributor

During the calendar years 2008 and 2009, none of the Independent Directors (including the Nominees that are Independent Directors), nor any of their immediate family members, had any relationship (the value of which exceeded $120,000) with any Fund Related Party, including, but not limited to, relationships arising out of (i) the payment for property and services, (ii) the provision of legal services, (iii) the provision of investment banking services (other than as a member of the underwriting syndicate) or (iv) the provision of consulting services.

The "immediate family members" of any person are his or her spouse, children in the person's household (including step and adoptive children) and any dependent of the person. An "entity in a control relationship" means any person who controls, is controlled by or is under common control with the named person. A "related fund" is a registered investment company or an entity exempt from the definition of an investment company pursuant to Sections 3(c)(1) or 3(c)(7) of the 1940 Act for which EULAV or any of its affiliates act as investment adviser.

Since the beginning of the most recently completed fiscal year of each Fund, no Nominee has purchased or sold any securities of EULAV, its parents, or their respective subsidiaries.

Committees and Board Meetings.

The Board has three standing committees – the Nominating/Governance Committee, Valuation Committee and the Audit Committee.

Nominating and Governance Committee. The current members of the Nominating/Governance Committee are Mrs. Nancy-Beth Sheerr (Chairman), and Messrs. David H. Porter and Paul Craig Roberts, all of whom are Independent Directors. The Nominating/Governance Committee of each Fund met three times during 2009.

The Nominating/Governance Committee operates pursuant to a written charter, a copy of which is attached to this Proxy Statement as Appendix A. The Nominating/Governance Committee is responsible for recommending to the Board persons to be nominated for election as Directors. Pursuant to the rules under the 1940 Act, only Independent Directors may select and nominate other Independent Directors for the Funds. The Nominating/Governance Committee generally does not consider nominees recommended by shareholders, but may do so if the Nominating/Governance Committee deems it appropriate. Shareholders who want to recommend nominees can contact the Nominating/Governance Committee by sending a signed letter that provides relevant information regarding the nominee and includes: (i) the shareholder's name and address; (ii) the number of shares owned by the shareholder; (iii) the Fund(s) of which the shareholder owns shares; and (iv) if such shares are owned indirectly through a broker, financial intermediary or other record owner, the name of the broker, financial intermediary or other record owner. The letter should be addressed to Value Line Mutual Funds Board of Directors – Nominating/Governance Committee, c/o Value Line Mutual Funds, 220 East 42nd Street, New York, New York 10017-5891.

The Nominating/Governance Committee's charter provides for certain criteria to be used in evaluating candidates for Independent Directors. The Nominating/Governance Committee expects that all candidates should generally have the following characteristics:

1. The candidate may not be an "interested person" (within the meaning of the 1940 Act) of the Funds, any adviser to the Funds, or the Funds' principal underwriter.

2. The candidate should have a reputation for integrity, honesty and adherence to high ethical standards. The Nominating/Governance Committee's consideration of this criterion may be accomplished through personal knowledge of the candidate or through inquiries of other persons that know the candidate or by receipt of references.

3. The candidate should have demonstrated business acumen, experience and ability to exercise sound judgment in matters that relate to the current and long-term objectives of the Funds and should be willing and able to contribute positively to the decision-making process of the Funds.

4. The candidate should be committed to understanding the Funds and the responsibilities of an Independent Director of an investment company and to regularly attending and participating in meetings of the Board and the committees on which the candidate would be a member.

5. The candidate should have the ability to understand the sometimes conflicting interests of the various constituencies of the Funds and to act in the interests of all shareholders.

6. The candidate should not have a conflict of interest that would impair the candidate's ability to represent the interests of all the shareholders and to fulfill the responsibilities of an Independent Director.

7. The candidate should have the ability to serve a sufficient number of years before reaching any mandatory retirement age for Directors that may be adopted by the Board.

Nominees will not be discriminated against on the basis of race, religion, national origin, sex, sexual orientation, disability or any other basis proscribed by law. For each candidate, the Nominating/Governance Committee will evaluate specific experience in light of the makeup of the then-current Board. The Nominating/Governance Committee may determine that a candidate who does not have the type of previous experience or knowledge referred to above should nevertheless be considered as a nominee if the Nominating/Governance Committee finds that the candidate has additional qualifications such that his/her qualifications, taken as a whole, demonstrate the same level of fitness to serve as an Independent Director.

In evaluating candidates, the Nominating/Governance Committee will seek to have at least one Independent Director qualify as an "audit committee financial expert," as such term is defined by rules under the 1940 Act, and will give preference to candidates that the Nominating/Governance Committee believes would so qualify.

Any re-nomination of an existing Independent Director is not viewed as automatic, but is based on continuing qualification under the criteria set forth above. In addition, the Nominating/Governance Committee will consider the existing Independent Director's performance on the Board and any Board committees.

The Nominating/Governance Committee has the authority to retain and terminate any search firm or other consultant to be used to identify Independent Director candidates, including the authority to approve such firm's or consultant's fees and other retention terms. The Nominating/Governance Committee is empowered to cause the Funds to pay the compensation of any search firm or other consultant engaged by the Nominating/Governance Committee.

In addition to members of the Nominating/Governance Committee, the President and other officers of the Funds, even if not members of the Nominating/Governance Committee, may be solicited for their input on candidates and to recruit candidates for the Board. The Nominating/Governance Committee will give candidates recommended by the President and other officers of the Funds the same consideration given any other candidate.

The Nominating/Governance Committee makes nominations for the appointment or election of Independent Directors in accordance with its charter and by applying the criteria and principles set forth above.

Each Independent Director Nominee has been selected by the Nominating/Governance Committee on this basis. Each Independent Director Nominee was selected as a candidate to be a Director by the current Independent Directors.

Valuation Committee. The current members of the Valuation Committee are Ms. Joyce E. Heinzerling and Mr. Thomas T. Sarkany. The Valuation Committee reviews any action taken by the Pricing Committee, which consists of certain officers and employees of the Fund and EULAV, in accordance with the valuation procedures adopted by the Board. The Valuation Committee of each Fund met three times during 2009.

Audit Committee. The current members of the Audit Committee are Mmes. Joyce E. Heinzerling and Nancy-Beth Sheerr, and Messrs. Francis C. Oakley, David H. Porter, Paul Craig Roberts and Daniel S. Vandivort (Chairman), all of whom are Independent Directors. The Audit Committee has determined that Mr. Vandivort is an "audit committee financial expert," as such term is defined by the rules of the 1940 Act. The Audit Committee of each Fund met five times during 2009.

The Audit Committee operates pursuant to a written charter and is responsible for, among other things, overseeing the Funds' accounting and financial reporting practices, reviewing the results of the annual audit of the Funds' financial statements and interacting with the Funds' independent registered public accountants on behalf of the full Board.

Board Meetings. The Board held four regularly scheduled meetings and one telephonic meeting during 2009. All of the current Directors and committee members then serving attended at least 75% of the meetings of the Board or applicable committee held during 2009. The Funds do not have a policy regarding the attendance of Directors at annual shareholder meetings. The Directors are not expected to attend Meeting #1 or Meeting #2. In accordance with the requirements of the 1940 Act and applicable state law, the Funds did not hold an annual shareholder meeting during 2009.

Shareholder Communications with the Board.

The Board has established a process for shareholders to communicate with the Board. Shareholders may contact the Board by mail. Correspondence should be addressed to Value Line Mutual Funds Board of Directors, c/o Value Line Mutual Funds, 220 East 42nd Street, New York, New York 10017-5891. A shareholder communication to the Board should include the following information: (i) the name and address of the shareholder; (ii) the number of shares owned by the shareholder; (iii) the Fund(s) of which the shareholder owns shares; and (iv) if the shares are owned indirectly through a broker, financial intermediary or other record owner, the name of the broker, financial intermediary or other record owner. All correspondence received as set forth above shall be reviewed by the Secretary of the Funds and reported to the Board.

Director and Nominee Ownership of Fund Shares.

Appendix B sets forth the dollar range of equity securities beneficially owned by each Director and Nominee individually and in the aggregate, as of July 31, 2010. Securities that are beneficially owned, as defined under the Securities Exchange Act of 1934 (the “1934 Act”) include direct and indirect ownership of securities where the economic interest of the Director or Nominee is tied to the securities, employment ownership and securities when the Director or Nominee can exert voting power and when the Director or Nominee has authority to sell the securities. The dollar ranges in Appendix B are in accordance with SEC requirements.

Compensation of Directors and Officers.

Appendix C sets forth the compensation received from the Funds by the Directors during 2009. No officers receive any compensation from the Funds for their services to the Fund and the fund complex. None of the Independent Directors, Interested Director or any Officers receive any retirement benefits or deferred compensation from any Fund or the fund complex.

Additional Executive Officers.

The following table provides information about the executive officers of the Funds. Each executive officer is appointed by the Board and serves until his or her successor is chosen and qualified or until his or her resignation or removal by the Board. The business address of all of the executive officers of the Funds is Value Line Mutual Funds, 220 East 42nd Street, New York, New York 10017-5891.

Name and Year of Birth	Position(s), Length of Service	Principal Occupation During Past Five Years
Mitchell E. Appel (1970)	President (since 2008).	President of each of the 14 Value Line Funds since June 2008; Chief Financial Officer of VLI since April 2008 and from September 2005 to November 2007 and Treasurer from June 2005 to September 2005; Director of VLI since February 2010; Chief Financial Officer of XTF Asset Management from November 2007 to April 2008; Chief Financial Officer of the Distributor since April 2008 and President since February 2009; President of the Adviser since February 2009.
Howard A. Brecher (1953)	Vice President and Secretary (since 2008).	Vice President and Secretary of each of the 14 Value Line Funds since 2008; Secretary of VLI until January 2010; Chief Legal Officer and Director of VLI; Acting Chairman and Acting CEO of VLI since November 2009; Secretary and Treasurer of the Adviser since February 2009; Vice President, Secretary, Treasurer, General Counsel and a Director of Arnold Bernhard & Co., Inc., the parent company of VLI.
Michael Wagner (1950)	Chief Compliance Officer (since 2009).	Chief Compliance Officer of each of the 14 Value Line Funds since June 2009; President of Northern Lights Compliance Services, LLC (formerly Fund Compliance Services, LLC (2006-present); Director of Constellation Trust Company until 2008.
Emily D. Washington (1979)	Treasurer and Chief Financial Officer (since 2008).	Treasurer and Chief Financial Officer (Principal Financial and Accounting Officer) of each of the 14 Value Line Funds since 2008; Associate Director of Mutual Fund Accounting at VLI until 2008.

Vote Necessary to Approve this Proposal.

If a quorum is present at Meeting #1, the following votes are required for the election of the Nominees. Quorum requirements for each Fund are set out in Appendix D.

Each Fund (other than Value Line Aggressive Income Trust, Value Line Asset Allocation Fund, Inc., Value Line Emerging Opportunities Fund, Inc., Value Line New York Tax Exempt Trust and Value Line Strategic Asset Management Trust) requires a majority of the votes cast to elect the Nominees.

Value Line Aggressive Income Trust, Value Line Asset Allocation Fund, Inc., Value Line Emerging Opportunities Fund, Inc., Value Line New York Tax Exempt Trust and Value Line Strategic Asset Management require a plurality of votes cast to elect the Nominees, which means that the three Nominees that receive the greatest number of votes will be elected to fill the three Directors seats being voted upon.

There is no cumulative voting in the election of Directors. If elected, Mr. Appel will join the Board upon the resignation of Mr. Sarkany in connection with completion of the Restructuring. Because Ms. Heinzerling and Mr. Vandivort currently are serving as Independent Directors, they will continue to so serve regardless of whether they are elected by shareholders.

THE BOARD RECOMMENDS
A VOTE “FOR” ALL NOMINEES.

MEETING #2

INVESTMENT ADVISORY PROPOSAL

At Meeting #2, you will be asked to vote in favor of a new investment advisory agreement between each Fund and the restructured Adviser, which will be named EULAV Asset Management (the "restructured Adviser " or "EAM"). The services to be provided by the restructured Adviser and the rates at which fees are to be paid by each Fund under its new investment advisory agreement ("New Investment Advisory Agreements") are the same as under that Fund's current investment advisory agreement (the "Current Investment Advisory Agreements"). In addition, the other terms of each New Investment Advisory Agreement are identical to its corresponding Current Investment Advisory Agreement, except for the date of execution, the two-year initial term, immaterial updating changes and immaterial changes in form. For a further description of the New Investment Advisory Agreements and a comparison of the New Investment Advisory Agreements and the Current Investment Advisory Agreements, see "The New Investment Advisory Agreements" and "Comparison of the New Investment Advisory Agreements to the Current Investment Advisory Agreements" below. The forms of the New Investment Advisory Agreement are also attached as Appendix E to this Proxy Statement.

VLI has told the Board that it intends to restructure its ownership and operations of EULAV and the Distributor (the "Restructuring"), as more fully described under "Description of the Restructuring" below. Because the Restructuring involves a change of control of EULAV, it will result in the automatic termination of the Current Investment Advisory Agreements in accordance with their terms, as required by the 1940 Act. Therefore, the shareholders of each Fund are being asked to approve the New Investment Advisory Agreements. If so approved, the New Investment Advisory Agreements would become effective upon the consummation of the Restructuring.

Description of the Restructuring

Currently, EULAV and the Distributor are both separate wholly-owned subsidiaries of VLI, together with its publishing and licensing business. VLI is a New York corporation the shares of common stock of which trade on the NASDAQ stock market. Arnold Bernhard & Co., Inc., a New York corporation controlled by Jean Bernhard Buttner, beneficially owns 86.5% of the common stock of (and therefore controls) VLI. EULAV is organized as a Delaware limited liability company and ESI is organized as a New York corporation. Structurally, this can be depicted as follows:

Under the Restructuring, the Distributor would be restructured as a Delaware limited liability company, VLI would contribute all the securities representing its ownership of the Distributor to the Adviser , and the Adviser would then be converted to a Delaware statutory trust. The Restructuring of the Adviser and the Distributor will not affect the ownership of VLI, which will continue to be a New York corporation the shares of common stock of which trade on the NASDAQ stock market. Particularly, Arnold Bernhard & Co., Inc., a New York corporation controlled by Jean Bernhard Buttner, will continue to own 86.5% of the common stock of (and therefore control) VLI. However, the Adviser 's capital structure would be revised so that VLI would own only nonvoting revenue and profits interests and five individuals would each own 20% of the voting profits interests. The holders of the restructured Adviser 's voting securities would have the right to elect five trustees of the restructured Adviser , who would manage the combined company consisting of the restructured Adviser and the Distributor much like a board of directors. Day-to-day management of the restructured Adviser and the Distributor would be delegated to its senior executive, Mr. Appel. This revised structure can be depicted as follows:

VLI's independent directors have approved the five initial holders of the restructured Adviser 's voting profit interests. Those persons are: Mr. Appel, Avi T. Aronovitz , Richard Berenger, Howard B. Sirota and R. Alastair Short. It is expected that these persons will elect themselves as the five initial trustees of the restructured Adviser although there is no requirement that they do so and there is no agreement among them to do so.

Each of these shareholders will be granted voting profits interest having 20% of the voting power for trustees and other matters to put to shareholders. Collectively, these interests will represent 50% of the residual profit of the business, in which the share of Mr. Appel will be 45% and the others each 1.25%. VLI will retain nonvoting profits interest representing the remaining 50% of residual profits and will have no power to vote for the election, removal or replacement of trustees. VLI will also have an interest in nondistribution revenues of the business ranging from 41% at business levels lower than approximately 75% of current levels to as high as 55% at business levels higher than approximately 300% of current levels. In the event the business is sold or liquidated, the first $56.1 million of net proceeds (the current value of the business as determined by the independent directors of VLI after reviewing a valuation report by the directors' financial advisors) will be distributed in accordance with capital accounts, 20% of the next $56.1 million will be distributed to the holders of the voting profits interests and 80% to the holders of the nonvoting profits interests (initially VLI) and the excess will be distributed 45% to the holders of the voting profits interests and 55% to the holders of the nonvoting profits interests.

In connection with completion of the Restructuring, VLI will (1) grant the restructured Adviser, the Distributor and each existing Fund a permanent right to use of the name "Value Line" so long as the restructured Adviser remains the Fund's adviser and the Fund does not alter its investment objectives or fundamental policies as they exist on the date of the New Investment Advisory Agreements to use leverage for investment purposes, short selling or other complex or unusual investment strategies to create a risk profile similar to that of so-called hedge funds, (2) provide the restructured Adviser its ranking information without charge on as favorable a basis as to its best institutional customers and (3) capitalize the business with $7 million of cash and cash equivalents.

VLI will have with respect to the restructured Adviser the benefit of certain consent rights, such as selling all or a significant part of the restructured Adviser, making material acquisitions, entering into businesses other than asset management and fund distribution, paying compensation in excess of 22.5 %-30% of nondistribution revenues (depending on the level of such revenues), declaring bankruptcy, making material changes in tax or accounting policies or making material borrowings, and entering into related party transactions.

VLI expects that each Fund's portfolio manager will remain as such and all or substantially all of the current employees of the Adviser will remain employees of the restructured Adviser after the Restructuring.

VLI's independent directors have unanimously determined to pursue the Restructuring as the most favorable way to VLI and its shareholders for ensuring compliance with the terms of the SEC settlement pursuant to which the SEC found violations of federal securities laws stemming from VLI's retention of brokerage commissions from nine of the Funds over an 18-year period prior to November 2004, and to which settlement VLI, the Distributor and two of VLI's former officers consented without admitting or denying the findings. The VLI independent directors had the benefit of advice from independent counsel and financial advisors and reviewed several possible structures and types of transactions before unanimously approving the Restructuring. VLI's independent directors believe that the Restructuring will end a period of uncertainty for the Funds relating to the SEC investigation and settlement and provides favorable economic incentives for the management of the Adviser to enhance the performance of the Funds and its business for the benefit of the Funds and their shareholders, the Adviser and its management team and VLI as a passive investor in the Adviser .

VLI has stated that, as a result of the Restructuring, it will no longer "control" (as that term is defined in the 1940 Act) the restructured Adviser or the Distributor. Under the terms of the settlement with the SEC stemming from VLI's brokerage practices with the Funds prior to November 2004, Jean Bernhard Buttner, who controls Arnold Bernhard & Co., Inc. which owns 86.5% of VLI's common stock (the "Control Person"), will be barred from association with any broker, dealer, or investment adviser and will be prohibited from serving or acting in various capacities, including as an "affiliated person" (as that term is defined in the 1940 Act) of the Funds, EULAV or the Distributor. If the Control Person were to directly or indirectly "control" (as that term is defined in the 1940 Act) EULAV or the Distributor, the Control Person would be an "affiliated person" of EULAV or the Distributor and not in compliance with the SEC settlement.

VLI has stated that, as a result of the Restructuring, it will no longer control the restructured Adviser or the Distributor. The SEC staff has expressed no view and provided no assurances that the Restructuring will effect compliance with the SEC settlement.

The New Investment Advisory Agreements

Under the New Investment Advisory Agreements, the restructured Adviser will be required to provide the same advisory services to each Fund as under the Current Investment Advisory Agreements. The rate at which the fees are to be paid by each Fund under its New Investment Advisory Agreement is identical to the rate at which the fees are currently paid by that Fund under its Current Investment Advisory Agreement.

All the terms of each Fund's New Investment Advisory Agreement are identical to the terms of its Current Investment Advisory Agreement except for the date of execution, the two-year initial term, immaterial updating changes and immaterial changes in form (see "Comparison of Current Investment Advisory Agreements to the New Investment Advisory Agreement").

Board Approvals and Considerations

The Board, including the Independent Directors, held an in-person meeting on July 20, 2010 for the purposes of considering whether it would be in the best interests of each Fund and its shareholders, to approve the New Investment Advisory Agreement between the restructured Adviser and each Fund. At that meeting, after consideration of the factors discussed below, the Board, including a majority of the Independent Directors, approved the New Investment Advisory Agreement for each Fund as being in the best interests of the Fund and its shareholders and recommended its approval by shareholders.

In preparation for their consideration of the New Investment Advisory Agreements, the Directors received, in response to a written due diligence request prepared by the Board and its independent legal counsel and provided to the Adviser and the Distributor, written information covering a range of issues and received, in response to their additional requests, further information in advance of and at the in-person Board meeting. To assist the Board in its consideration of the New Investment Advisory Agreements, VLI provided materials and information about the Adviser, the restructured Adviser and the Distributor, including their history, management, investment, risk management and compliance capabilities and processes, compensation levels and financial condition and provided materials and information about the Restructuring. In addition, the Independent Directors consulted with their independent legal counsel on numerous occasions, discussing, among other things, the legal standards and certain other considerations relevant to the Board's deliberations.

In considering the New Investment Advisory Agreements, the Board, including the Independent Directors, took into account, as it deemed relevant, the fact that on March 10-11, 2010, it had performed a full annual review of the Current Investment Advisory Agreements. At that time, the Board approved the selection of the Adviser and the continuance of the Current Investment Advisory Agreements based on its review of qualitative and quantitative information provided by the Adviser . In selecting the Adviser and approving the Current Investment Advisory Agreements, the Board, including the Independent Directors, advised by their independent legal counsel, considered the nature, extent and quality of services provided by the Adviser , the Funds' expenses and performance, costs of services provided to the Funds and profits realized by the Adviser , economies of scale, fees and services provided for other comparable accounts by the Adviser and other benefits to the Adviser and/or its affiliates, all as described in the Factors Considered by the Board in Approving the Current Investment Advisory Agreements attached to this Proxy Statement as Appendix F. The Board reconsidered these matters at its July 20, 2010 meeting.

In connection with the Board's review of the New Investment Advisory Agreements, the Adviser provided the Board with information about a variety of matters. The Board considered, among other things, the following information:

that the Adviser has no present intention to alter the advisory fee rates and expense arrangements currently in effect for the Funds for a period of two years from the date of the closing of the Restructuring;

that neither VLI nor the Adviser expects that there will be any diminution in the nature, quality and extent of services provided to the Funds and their shareholders by the restructured Adviser , including portfolio management and compliance services, as a result of the Restructuring;

that it is expected that each Fund's portfolio manager will remain unchanged as a result of the Restructuring and that all or substantially all of the current employees of the Adviser will remain employees of the restructured Adviser and will continue to provide services to the Funds after the Restructuring and will no longer be employees of VLI after the Restructuring;

VLI's representation to the Board regarding its belief that the restructured Adviser will have adequate resources after giving effect to the Restructuring to perform its services at a reasonable level under the New Investment Advisory Agreements, and in any event such resources will not be less than those the Adviser currently has, and that the restructured Adviser would continue to have access to the Value Line timeliness rankings after the Restructuring without cost ; and

VLI has agreed to pay: (i) all costs of the Funds in connection with the consideration by the Board of the Restructuring; and (ii) all costs associated with both Meeting #1 and Meeting #2 , including delivering proxy materials to shareholders and soliciting proxies.

In approving the restructured Adviser as adviser and approving the New Investment Advisory Agreements for the Funds, the Board, including the Independent Directors, advised by their independent legal counsel, considered the information provided and the factors described both above and below and reached the conclusions described herein. The Board also recognized that VLI's board of directors engaged, with the advice of its financial and legal advisors, in an extensive process and considered, with the advice of its financial and legal advisors, a range of options in relation to the requirement that Jean Bernhard Buttner disassociate from the Adviser and the Distributor, including the sale of these businesses, the spin-off of these businesses and the transfer of these businesses to a blind trust. The Board further recognized that one of the organizations with which VLI stated it had explored a business relationship may have unintentionally contacted one of the members of the Board but that organization never replied to that Board member's responsive letter whether such contact was intentional. Moreover, VLI informed the Board that the tentative proposal from that organization was not acceptable to VLI and therefore VLI decided not to pursue it further and VLI further informed the Board that the organization agreed not to contact the Board.

In approving the restructured Adviser as advisor and approving the New Investment Advisory Agreements, the Board did not identify any particular information that was all-important or controlling, and each Director who voted may have attributed different weights to the various factors discussed both above and below.

Nature, Extent and Quality of Services Provided. The Board noted that the terms of the New Investment Advisory Agreements are identical in all material respects to the Current Investment Advisory Agreements and considered representations by VLI and the Adviser that there would be no diminution in the scope of services provided by the restructured Adviser under the New Investment Advisory Agreements as compared to the scope of services provided by the Adviser under the Current Investment Advisory Agreements. The Board also relied upon the representations by VLI regarding its belief that the restructured Adviser and the Distributor will have adequate resources after giving effect to the Restructuring to perform their respective services at a reasonable level under the New Investment Advisory Agreements and the new principal underwriting agreement between the Distributor and each Fund and in any event such resources will not be less than those currently available to the Adviser and the Distributor , and that the restructured Adviser would continue to have access to the Value Line timeliness rankings after the Restructuring without cost . The Board also considered and viewed favorably that Mr. Appel, who is currently the Chief Executive Officer of the Adviser , would continue in that position at the time of the Restructuring and would be responsible for the day-to-day management of the restructured Adviser . The Board also considered the restructured Adviser 's compliance programs and their compliance resources. The Board viewed favorably the increased emphasis being placed by the Adviser on its overall compliance program as well as steps being undertaken to enhance the shareholders' experience with the Funds, such as a more robust website. The Board also reviewed the services provided by the Adviser and its affiliates in supervising third party service providers.

The Board discussed the Adviser 's current financial condition and the restructured Adviser's anticipated financial condition after the completion of the Restructuring. The Board discussed the Adviser 's current ownership and management structure and the restructured Adviser's expected ownership and management structure after the completion of the Restructuring.

Based on the discussions held and the materials presented at the July 20, 2010 Board meeting, and in significant reliance on VLI's and the Adviser 's representations, the Board determined that the Restructuring would not likely cause an adverse change in the nature, extent and quality of the services to be provided by the restructured Adviser under the New Investment Advisory Agreements compared with the services provided by the Adviser under the Current Investment Advisory Agreements and that the Board believes that the quality of such services will continue to be appropriate.

The Funds' Expenses and Performance. The Board took into account that the fee rate for each Fund under its New Investment Advisory Agreement is identical to the fee rate under its Current Investment Advisory Agreement. Further, the Board noted that representatives of VLI and the Adviser had confirmed that there is no present intention to alter the advisory fee rates, expense waivers or expense reimbursement arrangements currently in effect for the Funds for a period of two years. The Adviser advised that, in connection with the Restructuring, it will enter into contractual advisory fee waivers for each Fund currently subject to such a waiver on the same terms as the current contractual advisory fee waivers, all of which would otherwise terminate at the consummation of the Restructuring. In addition, there will not be any increase in the Funds' expense structures as a result of the Restructuring.

Costs of Services Provided to the Funds and Profits Realized by EULAV. In evaluating the costs of the services to be provided by the restructured Adviser under the New Investment Advisory Agreements, the Board considered, among other things, whether advisory fee rates or other expenses would change as a result of the Restructuring. The Board noted that the New Investment Advisory Agreements are substantially identical to the Current Investment Advisory Agreements, including the fact that the fee rates under the agreements are identical and that representatives of VLI and the Adviser represented that there is no present intention due to the Restructuring to alter the advisory fee rates, expense waivers or expense reimbursement arrangements currently in effect as described above. The Board considered the level of profitability of the Adviser and its affiliates with respect to each Fund individually and in the aggregate for all the Funds, including the impact of certain actions taken during prior years. These actions included the Adviser 's reduction (voluntary in some instances and contractual in other instances) of management and/or Rule 12b-1 fees for certain funds, the Adviser's termination of the use of soft dollar research, and the cessation of trading through the Distributor. The Board concluded that the profitability of the Adviser and its affiliates with respect to each Fund, including the financial results derived from the Fund's Agreement, were within a range the Board considered reasonable.

Economies of Scale. The Board noted that for certain Funds, the restructured Adviser contractually agreed to waive a portion of its advisory fee for certain Funds . The Board noted that, given the current and anticipated size of many of the Funds, any perceived and potential economies of scale were not yet a significant consideration for the Funds and the addition of break points was determined not to be necessary at this time.

The Board determined that changes to the fee structure were not currently necessary. For more information about the fees paid by the Funds, please see Appendices G and H, which list the rate of compensation described in each Fund's Current Investment Advisory Agreement and New Investment Advisory Agreement, and the amount of advisory fees paid to the Adviser for each Fund's most recent fiscal year. It was noted that it was not possible to evaluate how the Restructuring would create opportunities for additional economies of scale, but the Board did not expect economies of scale to be significant given the size of the Funds.

Fees and Services Provided for Other Comparable Funds/Accounts Managed by the Adviser . The Adviser informed the Board that it manages non-mutual fund asset management accounts that have similar objectives and policies to certain of the Funds, but are not generally comparable for a number of reasons (including different services provided). The Board determined that the investment advisory fee rates charged to the Funds do not constitute fees that are so disproportionately large as to bear no reasonable relationship to the services rendered and that could not have been the product of arm's-length bargaining, and concluded that the advisory fee rates are fair and reasonable.

Other Benefits to the Adviser . The Board also considered the character and amount of other direct and incidental benefits received by the Adviser and its affiliates from their association with the Funds. The Board concluded that potential "fall-out" benefits that the Adviser and its affiliates may receive, such as greater name recognition, appear to be reasonable, and may in some cases benefit the Funds.

Conclusions. The Board examined the totality of the information it was provided at the July 20, 2010 Board meeting, and information it received at other meetings held during the past year, and did not identify any single factor discussed previously as controlling. Based on this analysis, the Board determined that the New Investment Advisory Agreements, including the investment advisory fee rates thereunder, are fair and reasonable in light of all relevant circumstances and concluded that it is in the best interest of the Funds and their shareholders to approve the New Investment Advisory Agreements.

The Board also approved an interim investment advisory agreement for each Fund with the restructured Adviser (each, an "Interim Investment Advisory Agreement") pursuant to Rule 15a-4 under the 1940 Act , which would, if signed by the Fund and the restructured Adviser, take effect upon closing of the Restructuring in the event that shareholder approval of that Fund's New Investment Advisory Agreement has not yet been obtained. In reliance on Rule 15a-4, the Interim Investment Advisory Agreement will allow the restructured Adviser to continue performing advisory services with respect to a Fund for a maximum of 150 days after the Closing of the Restructuring, while such Fund continues to seek shareholder approval of its New Investment Advisory Agreement. Compensation earned by the restructured Adviser under each Interim Investment Advisory Agreement will be held in an interest-bearing escrow account pending shareholder approval of the New Investment Advisory Agreement. If shareholders of a Fund approve the New Investment Advisory Agreement within the 150 day-period, the amount held in the escrow account, including interest, will be paid to the restructured Adviser . If shareholders of a Fund do not approve that Fund's New Investment Advisory Agreement, the restructured Adviser will be paid the lesser of the costs incurred in performing services under the Interim Investment Advisory Agreement or the total amount in the escrow account, including interest earned. Shareholder approval of the Interim Investment Advisory Agreements is not required by the 1940 Act and is not being sought. The terms of each Fund's Interim Investment Advisory Agreement, and the fee rates paid thereunder, are identical in all material respects to the Current Investment Advisory Agreements and the New Investment Advisory Agreement, except for the fee escrow, termination provisions and the time periods covered by the agreements. In its approval of the Interim Investment Advisory Agreement, the Board considered substantially the same factors and drew substantially the same conclusions as those described in connection with the approval of the New Investment Advisory Agreements (see "Board Approvals and Considerations" above).

If, 150 days after the closing of the Restructuring, a Fund's shareholders still have not approved its New Investment Advisory Agreement, the Board would be required to take such actions as it deems to be in the best interests of such Fund and its shareholders. Such actions may include negotiating a new investment advisory agreement with an advisory organization selected by such Board, the re-solicitation of shareholders, or making other arrangements.

Comparison of Current Investment Advisory Agreements to the New Investment Advisory Agreements

Set forth below is a more detailed description of the terms of the New Investment Advisory Agreements and a comparison to the terms of the Current Investment Advisory Agreements. Copies of the forms of the New Investment Advisory Agreements are attached to this Proxy Statement as Appendix E and you should refer to Appendix E for the complete terms of the New Investment Advisory Agreement. Two of the Funds, Value Line Asset Allocation Fund, Inc. and Value Line Emerging Opportunities Fund, Inc., utilize investment advisory agreements that are slightly different as compared to the other 12 Funds. The investment advisory agreements for Value Line Asset Allocation Fund, Inc. and Value Line Emerging Opportunities Fund, Inc. require those funds to pay their own fund accounting expenses, while the Adviser is required to bear such expenses for the other 12 Funds. Each New Investment Advisory Agreement is substantially identical to the Current Investment Advisory Agreement it is replacing.

Investment Advisory Services. The investment advisory services required to be provided by the restructured Adviser to each Fund under the New Investment Advisory Agreements are the same as the services provided by the Adviser to the Funds under the Current Investment Advisory Agreements. Both the Current Investment Advisory Agreements and the New Investment Advisory Agreements require that the Adviser or the restructured Adviser (1) provide the Funds with such investment research, data advice and, supervision as the Adviser or the restructured Adviser from time to time considers necessary for proper supervision of the Funds; (2) act as manager and investment adviser of the Funds and, as such, furnish continuously an investment program and determine from time to time what securities shall be purchased or sold by the Funds, and what portion of the assets of the Funds shall be held uninvested.

Advisory Fee Rates. Under the Current Investment Advisory Agreements and the New Investment Advisory Agreements, the Funds have agreed to pay the Adviser or the restructured Adviser respectively a fee on a monthly basis at an annual rate based on the average daily value of the applicable Fund's net assets during the preceding month. The proposed fee rates under the New Investment Advisory Agreements are identical to the fee rates payable to the Adviser under the Current Investment Advisory Agreements with respect to all Funds, and the same contractual fee waivers will apply to the New Investment Advisory Agreements. The fee rate for each Fund under its Current Investment Advisory Agreement and its New Investment Advisory Agreement is set forth in Appendix G.

In connection with the Current Investment Advisory Agreements, the Adviser has contractually agreed to waive a portion of its advisory fees for certain Funds, as indicated in Appendix G, and these contractual waivers will terminate upon the closing of the Restructuring. The restructured Adviser has agreed to enter into new contractual waivers with the same effectiveness and otherwise identical terms at the same time the New Investment Advisory Agreements are entered into.

Payment of Expenses. The New Investment Advisory Agreements require the restructured Adviser to pay the costs of all administrative services, office space, equipment and administrative, bookkeeping and clerical personnel necessary for managing the affairs of the Funds. As noted above, Value Line Asset Allocation Fund, Inc. and Value Line Emerging Opportunities Fund, Inc. have entered into investment advisory agreements that require those Funds to pay their own fund accounting expenses; the restructured Adviser is required to pay fund accounting costs for all of the other Funds. Each New Investment Advisory Agreement provides for the same payment of expenses by the restructured Adviser as under the Current Investment Advisory Agreement it is replacing.

Limitation on Liability. Under the New Investment Advisory Agreements, the restructured Adviser will not be liable for any error of judgment, or mistake of law, or any loss suffered by the Funds, in connection with the matters to which the New Investment Advisory Agreements relate, except for loss resulting from willful misfeasance, bad faith or gross negligence of the restructured Adviser in the performance of its duties or from reckless disregard by the restructured Adviser of its obligations and duties under the New Investment Advisory Agreements. Each New Investment Advisory Agreement provides for the same liability provisions as the Current Investment Advisory Agreement it is replacing.

Term, Continuance, and Termination. The New Investment Advisory Agreements provide that they may be terminated at any time with respect to any Fund, on sixty days written notice by either party. They also provide that they shall terminate automatically in the event of assignment as defined in the 1940 Act. The Current Investment Advisory Agreements have the same termination terms. Each New Investment Advisory Agreement includes an initial two year term as permitted by the 1940 Act.

Form of Agreement. The New Investment Advisory Agreements will be separate agreements for each Fund. The Current Investment Advisory Agreements are separate agreements for each Fund.

In connection with the Restructuring, VLI and the Adviser have agreed that for a period of at least three years after the Restructuring at least 75% of the Board will be independent of VLI and the restructured Adviser and that for a period of at least two years after the Restructuring neither of them will impose any unfair burden on any of the Funds as a result of any of the terms of the Restructuring.

Shareholder Approval

As required by the 1940 Act, to become effective with respect to a particular Fund, the New Investment Advisory Agreement for that Fund must be approved by (a) the vote of 67% of the Fund's Shares present at Meeting #2 if more than 50% of the outstanding shares of that Fund are present, or (b) the vote of more than 50% of the outstanding shares of that Fund, whichever is less. Approval of the Investment Advisory Proposal is contingent upon the consummation of the Restructuring.

THE BOARD RECOMMENDS A VOTE "FOR" THIS PROPOSAL .

OTHER INFORMATION

Share Ownership of Directors and Management.

As of July 31, 2010, the percentage of shares of each Fund beneficially owned by all Directors and Nominees, each executive officer of the Funds, and by the Directors and officers of the Funds (as a group) was not more than 1% of the Funds.

Other Matters.

There have been no material legal proceeding, pending or otherwise, against any Director or Nominee during the past ten years.

There is no arrangement or understanding in connection with the New Investment Advisory Agreements with respect to the composition of the Board , the Adviser or the restructured Adviser with respect to the selection or appointment of any person to any office with either the Funds , the Adviser or the restructured Adviser.

There are no material pending legal proceedings to which any Director or Nominee or affiliated person of such Director or Nominee is a party adverse to the Funds or any of their affiliated persons or has a material interest adverse to the Fund or any of its affiliated persons. Legal proceedings are material only to the extent that they are likely to have a material adverse effect on the Funds or the ability of the restructured Adviser to perform its contracts with the Funds.

The restructured Adviser provides investment advisory services to certain other clients that may have investment objectives and policies similar to those of the Funds. The restructured Adviser does not provide investment advisory services to any other investment funds.

As of July 31, 2010, the shareholders identified in Appendix I were known by the Funds to own, beneficially or of record, more than 5% of any class of outstanding shares of a Fund

Investment Adviser.

The Adviser serves as the investment adviser to each Fund. The principal business address of the Adviser is 220 East 42nd Street, New York, NY 10017. The Adviser is currently a wholly-owned subsidiary of VLI, a New York company also located at 220 East 42nd Street, New York, NY 10017, which in turn is a subsidiary of Arnold Bernhard & Co., Inc., a New York corporation controlled by Jean Bernhard Buttner. VLI has stated that, after giving effect to the Restructuring, Mrs. Buttner will no longer directly or indirectly control the restructured Adviser or the Distributor or own any of their voting securities. As of July 31, 2010, the Adviser provided investment advisory services for approximately $2.1 billion of assets. The name and principal occupation of directors and principal executive officers of the Adviser are provided in Appendix J attached to this Proxy Statement.

Other Service Providers.

Principal Underwriter. EULAV Securities, Inc. is the principal underwriter of the Funds. EULAV Securities, Inc.'s principal business address is 220 East 42nd Street, New York, NY 10017.

Administrator. State Street Bank and Trust Company ("State Street") provides certain bookkeeping, accounting and administrative services for the Funds. State Street, whose address is 225 Franklin Street, Boston, MA 02110, also acts as the Funds' custodian, transfer agent and dividend-paying agent. As custodian, State Street is responsible for safeguarding the Funds' cash and securities, handling the receipt and delivery of securities and collecting interest and dividends on the Funds' investments. As transfer agent and dividend-paying agent, State Street effects transfers of Fund shares by the registered owners and transmits payments for dividends and distributions declared by the Fund. Boston Financial Data Services, Inc., a State Street affiliate, whose address is 330 West 9th Street, Kansas City, MO 64105, provides certain transfer agency functions to the Funds as an agent for State Street.

Independent Registered Public Accountants. PricewaterhouseCoopers LLP ("PWC"), 300 Madison Avenue, New York, NY 10017, serves as the independent registered public accounting firm for each Fund. Representatives of PWC will not be present at either Meeting.

The Funds' Audit Committee has established certain pre-approval policies and procedures relating to the engagement of the Funds' independent registered public accountants to provide non-audit services to the Funds or to the Funds' investment adviser, or the Funds' investment adviser's affiliates, that provides ongoing services to the Funds if the engagement relates directly to the operations and financial reporting of the Funds (the "Non-Audit Services Pre-Approval Policies").

Independence of PWC . The Audit Committee has considered whether the provision of non-audit services rendered to the Funds' investment adviser and any Adviser Affiliate that were not pre-approved pursuant to paragraph (c)(7)(ii) of Rule 2-01 of Regulation S-X, if any, are compatible with maintaining PWC 's independence, and has determined that the provision of these services does not compromise PWC 's independence.

Disclosure of Fees. Appendix K sets forth for each Fund's two most recent fiscal years, the fees billed by PWC for all audit and non-audit services provided directly to the Fund and adviser affiliates. The fee information in Appendix K is presented under the following captions:

(a) Audit Fees—fees related to the audit and review of the financial statements included in annual reports and registration statements, and other services that are normally provided in connection with statutory and regulatory filings or engagements, including out-of-pocket expenses.

(b) Audit-Related Fees—fees related to assurance and related services that are reasonably related to the performance of the audit or review of financial statements, but not reported under "Audit Fees," including accounting consultations, agreed-upon procedure reports, attestation reports, comfort letters, out-of-pocket expenses and internal control reviews not required by regulators.

(c) Tax Fees—fees associated with tax compliance, tax advice and tax planning, including services relating to the filing or amendment of federal, state or local income tax returns, regulated investment company qualification reviews, tax distribution and analysis reviews and miscellaneous tax advice.

(d) All Other Fees—fees for products and services provided to the Fund and adviser affiliates other than those reported under "Audit Fees," "Audit-Related Fees" and "Tax Fees."

Other Business at the Meetings .

No other matter may come before either Meeting other than as stated in this Proxy Statement. In connection with any proposal to adjourn a Meeting to permit the continued solicitation of proxies in favor of the Election of Directors Proposal or the Investment Advisory Proposal (as applicable) , proxies that do not contain specific restrictions to the contrary will be voted on such matters in accordance with the judgment of the persons named as proxies in the enclosed Proxy Cards.

If you do not plan to attend the Meetings in person, please complete, sign, date, and return the enclosed Proxy Cards or cast your vote by touchtone phone or via the Internet promptly. Even if you do plan to attend a Meeting, please so note where provided and return the Proxy Cards promptly.

Future Shareholder Proposals.

Pursuant to rules adopted by the SEC under the 1934 Act, shareholders may request for inclusion in the Board's proxy statement for future shareholder meetings certain proposals for actions which they intend to introduce at such meeting. Any shareholder proposals must be presented a reasonable time before the proxy materials for the next meeting are sent to shareholders. The submission of a proposal does not guarantee its inclusion in the Funds' proxy statement and is subject to limitations under the 1934 Act. Because the Funds do not hold regular meetings of shareholders, no anticipated date of the next meeting can be provided.

Voting of Proxies.

Shares represented by properly given proxies and received by the Secretary of the Funds prior to a Meeting, unless revoked before or at such Meeting, will be voted according to the shareholder's instructions. If you sign a proxy but do not fill in a vote, your shares will be voted in favor of each of the Nominees for Director and in favor of each of the other Proposals. If any other business properly comes before such Meeting, your shares will be voted at the discretion of the persons named as proxies on the enclosed Proxy Cards .

A proxy with respect to shares held in the name of two or more persons will be valid if executed by one of them, unless at or prior to the exercise of such proxy, the Funds receive specific written notice to the contrary from one of such persons.

A proxy purporting to be exercised by or on behalf of a shareholder will be valid unless challenged at or prior to its exercise. The burden of proving the invalidity of the proxy will rest with the person seeking to challenge it.

Revocation of Proxies; Counting of Votes.

Any shareholder giving a proxy may revoke it at any time before it is exercised by: (i) submitting to the Funds a written notice of revocation; (ii) submitting to the Funds a subsequently dated and executed proxy; (iii) attending the Meeting to which the proxy relates and voting in person; or (iv) notifying the Funds of the revocation by calling the toll-free number on the Proxy Cards. Proxies voted by telephone or through the Internet may be revoked at any time before they are voted in the same manner that proxies voted by mail may be revoked.

At Meeting #1, “broker non-votes” (i.e., proxies from brokers or nominees indicating that such persons have not received instructions from the beneficial owners or other persons entitled to vote shares as to a particular matter with respect to which the brokers or nominees do not have discretionary power to vote) will not be counted for or against any proxy to which they relate, but will be counted as votes present for purposes of determining whether a quorum is present. Abstentions will have the effect of a vote against the Investment Advisory Proposal and will not affect the vote on the Election of Directors Proposal.

Quorum Requirements.

A quorum of shareholders of a Fund is necessary to hold a valid meeting for that Fund. The quorum requirement for each Fund is set forth in Appendix D.

A quorum will exist at a Fund’s Meeting #1 or Meeting #2 if the percentage of shareholders, as listed above, who are entitled to vote on the Record Date with respect to each Fund are present in person or by proxy at such Meeting . In the event that a quorum is not present, or if a quorum is present but sufficient votes to approve a Proposal are not received, the duly appointed proxies may propose one or more adjournments of such Meeting to permit further solicitation of proxies with respect to the Proposal. In case any such adjournment is proposed, the proxies will vote for those proxies which they are entitled to vote for the Proposal in favor of adjournment, and will vote those proxies required to be voted against the Proposal against adjournment. At any such adjourned meeting at which a quorum shall be present, any business may be transacted which might have been transacted at the meeting originally called. A shareholder vote may be taken on one or more of the Proposals prior to such adjournment if sufficient votes for its approval have been received and it is otherwise appropriate. Any such vote will be final regardless of whether such Meeting is adjourned with respect to any other Proposal. A Meeting may be held for any Fund for which a quorum is present irrespective that a quorum may not be achieved for such Meeting of any other Fund.

Solicitation of Proxies and Payment of Expenses.

This solicitation of proxies for the Meetings is being made by the Funds. All costs associated with the Meetings , including delivering proxy materials to shareholders, soliciting proxies and conducting the Meetings will be borne by VLI. The solicitation of proxies may include telephonic, Internet, mail or oral communication by officers and service providers of the Funds, who will not be paid for these services, and/or by D. F. King & Co., Inc. (the "Proxy Solicitation Firm"), which has been retained by VLI for an estimated fee of $ 500,000.00 plus out-of-pocket expenses.

Shareholders may authorize the Proxy Solicitation Firm to execute proxies on their behalf by telephonic instruction. Proxies that are submitted telephonically will be recorded in accordance with the procedures set forth below. The Directors believe that these procedures are reasonably designed to ensure that the identity of the shareholder casting the vote is accurately determined and that the voting instructions of the shareholder are accurately determined. In all cases where a telephonic proxy is solicited, the D. F. King representative is required to ask for certain identifying information from each shareholder. Then the representative will ask the shareholder to vote their shares by telephone , and ask for the shareholder's instructions on the proposal

The representative of the Proxy Solicitation Firm, although he or she is permitted to answer questions about the process, is not permitted to recommend to any shareholder how to vote, other than to read any recommendation set forth in the Proxy Statement or in any additional soliciting materials. The Proxy Solicitation Firm will record the shareholder's instructions. Within 72 hours, but in any event before the Meeting to which the vote relates , the shareholder will be sent a letter to confirm his or her vote and asking the shareholder to call the Proxy Solicitation Firm immediately if his or her instructions are not correctly reflected in the confirmation. If a shareholder wishes to participate in a Meeting, but does not wish to give a proxy by telephone, the shareholder may still submit the Proxy Cards originally sent with the Proxy Statement or attend such Meeting in person. Should shareholders require additional information regarding the proxy or replacement Proxy Cards, they may contact the Proxy Solicitation Firm (toll-free) at 1-800-545-3393 (toll-free) . Representatives are available Monday through Friday, 8:00 a.m.- 10:00 p.m. (Eastern Time) , and Saturday, 11:00 a.m. - 6:00 p.m. (Eastern Time) . Any proxy given by a shareholder, whether in writing or by telephone or the Internet, is revocable until voted at the Meeting to which such proxy relates .

Persons holding shares as nominees will be reimbursed by VLI, upon request, for the reasonable expenses of mailing soliciting materials to the principals of the accounts.

By Order of the Boards of Directors,

/s/ Howard A. Brecher

Howard A. Brecher
Secretary

September 20, 2010

APPENDIX A

VALUE LINE FAMILY OF FUNDS

NOMINATING/GOVERNANCE COMMITTEE CHARTER

I. Purposes of the Nominating/Governance Committee. The Nominating/Governance Committees (the "Committee") of the Boards of Directors (the "Boards," and each member of a Board, a "Trustee") of the Value Line family of funds (the "Funds") have two primary roles: (a) nomination of the Independent Trustees (as defined in Section IV below); and (b) supervision of fund governance matters.

II. Nomination Role. With regard to the nomination of Independent Trustees, the Committee is authorized to:

Identify individuals qualified to serve as Independent Trustees on the Boards;

Review the qualifications of any person properly identified or nominated to serve as an Independent Trustee on the Boards;

Recommend to the Boards and the then-current Independent Trustees: (i) the nominee(s) for appointment as Independent Trustee(s) by the Boards and the then-current Independent Trustees, and (ii) the nominee(s) for election as Independent Trustee(s) by shareholders to fill any vacancy for a position of Independent Trustee on the Boards;

Recommend to the Boards and the then-current Independent Trustees, the size and composition of the Boards and Board committees and determine the composition of the Boards and Board committees is as prescribed by the Investment Company Act of 1940, as amended (the "1940 Act"), and other applicable laws and regulations and industry best practices as applicable to the Funds; and

Recommend to the Boards and the then-current Independent Trustees, an Independent Trustee to either serve as a "lead" Independent Trustee or as the Chairperson of the Boards, in accordance with the rules and regulations under the 1940 Act as in effect from time to time and industry best practices as applicable to the Funds.

The Committee performs these functions to assist the Boards and the Independent Trustees in carrying out their fiduciary responsibilities and the requirements of the 1940 Act and the rules thereunder with respect to the selection and nomination of members of the Boards. Nomination of any person to serve on the Boards as an Independent Trustee shall initially be acted upon by the Independent Trustees and then by the entire Boards. Nomination of any persons to serve on the Boards other than as Independent Trustees shall be made by the Boards.

The Committee shall have the authority to retain and terminate any search firm or other consultant to be used to identify Independent Trustee candidates, including the authority to approve its fees and other retention terms. The Committee is empowered to cause the Funds to pay the compensation of any search firm or other consultant engaged by the Committee.

The Committee shall make nominations for the appointment or election of Independent Trustees in accordance with this Charter and shall apply the criteria and principles set forth in the "General Guidelines for Selecting Independent Trustees" attached hereto as Annex A.

The Boards believe that shareholders as a group are best served, considering the efficient allocation of Fund and Board resources, by maintaining a policy not to consider Trustee nominations recommended by individual shareholders. Thus, it is the Boards' policy not to consider Trustee nominations recommended by shareholders (although such persons may be considered if recommended by other persons, such as an Independent Trustee, or if the Committee deems it appropriate after considering all circumstances its members deem relevant).

In addition to members of the Committee, the President and other officers of the Funds, even if not members of the Committee, may be solicited for their input on candidates and to recruit candidates for the relevant Board. The Committee shall give candidates recommended by the President and other officers of the Funds the same consideration given to any other candidate.

III. Fund Governance Role. With regard to fund governance, the Committee is authorized to:

Monitor and evaluate industry and legal developments with respect to fund governance matters, and seek to comply with all applicable requirements, with a view to identifying and recommending to the Boards "best practices" that may be applicable to the Funds;

Consider and make appropriate recommendations to the Boards regarding the adoption of a retirement policy for the Trustees, and periodically review any such retirement policy and make any recommendations to the Boards with respect thereto;

Periodically review the role and responsibilities of any lead Independent Trustee (or, if required by Rule 0-1 under the 1940 Act, or otherwise implemented, review the role and responsibilities of the Independent Chairperson of the Boards);

Periodically consider and make appropriate recommendations to the Boards on the appropriate level of compensation to be paid to the Independent Trustees, members or chairpersons of committees of the Boards, any lead Independent Trustee or Chairperson of the Boards, and such other positions as the Committee considers appropriate;

Recommend to the Boards any new or revised policies and guidelines or revisions to this Charter regarding fund governance matters, as the Committee deems necessary;

Recommend to the Boards procedures for evaluating the performance of the Trustees and Board committees, including the chairpersons thereof, and, at least once annually, evaluate the performance of the Boards and the committees of the Boards, pursuant to the requirements of Rule 0-1 under the 1940 Act or other applicable requirements;

Consider, with the assistance of counsel to the Funds and counsel to the Independent Trustees, any issues or controversies arising as to whether or not any Trustees designated as an Independent Trustee in fact satisfies all of the criteria for such status (whether imposed by law or any such more stringent policies as may be adopted by the Boards). This assessment may occur upon: (i) the consideration of a new Trustee, (ii) a Trustee's joining the board of another entity, or (iii) at such other time as the Committee in its discretion may deem appropriate. The Committee shall make recommendations to the Boards regarding the same;

At least once annually, evaluate the independence (pursuant to the requirements of Rule 0-1 of the 1940 Act) of counsel to the Independent Trustees; and

Consider other fund governance related issues or conflicts that are brought before the Committee and make recommendations to the Board, as appropriate.

IV. Committee Operations. The Committee shall be composed of all the members of the Boards that are not "interested persons," as defined in Section 2(a)(19) of the 1940 Act, of the Funds (each, an "Independent Trustee").

The Committee shall elect a Chairperson by majority vote. When a Chairperson is appointed, he or she shall preside at all Committee meetings at which he or she is present and have such other duties and powers as may be determined by the Committee members. The Chairperson shall serve until he or she resigns, is removed by the Committee, or is replaced by a duly appointed successor.

The compensation, if any, of Committee members and its Chairperson shall be as determined from time to time by the Boards.

The Committee shall meet with such frequency as the members of the Committee shall from time to time determine to be appropriate. Meetings of the Committee shall be open to all Board members; however, no member of any Board other than a member of the Committee shall have the right to vote on any matter brought before the Committee and the Committee may hold executive sessions during which only members of the Committee are present. An affirmative vote or consent of a majority of all the members of the Committee is required for the Committee to take action. Any action permitted to be taken by the Committee may be taken by written action signed by at least a majority of the members of the Committee. The Committee shall cause to be kept such records of its meetings as it shall deem appropriate.

As it deems necessary and at the Funds' expense, the Committee is authorized to confer with, and to seek the help of, outside advisors, including without limitation, counsel to the Funds and counsel to the Independent Trustees, and officers or other employees of the Funds, as well as officers and employees of Value Line, Inc. and its affiliates.

The Committee shall, from time to time as it deems appropriate, review and reassess the adequacy of this Charter, including Annex A, and recommend any proposed changes to the Board for consideration.

IV. Approval of Charter. This Charter and any amendments are subject to approval by the Boards.

ANNEX A to APPENDIX A

General Guidelines for Selecting Independent Trustees

I. Application of Criteria to Prospective Independent Trustees. The Committee expects that all candidates should generally have the following characteristics:

1. The candidate may not be an "interested person" (within the meaning of the 1940 Act) of the Funds, any adviser to the Funds or the Funds' principal underwriter.

2. The candidate should have a reputation for integrity, honesty and adherence to high ethical standards. As fiduciaries, mutual fund trustees must affirmatively consider a candidate's reputation prior to recommending the candidate to serve as a trustee. The Committee's consideration of this criterion may be accomplished through personal knowledge of the candidate or through inquiries of other persons that know the candidate or by receipt of references.

3. The candidate should have demonstrated business acumen, experience and ability to exercise sound judgment in matters that relate to the current and long-term objectives of the Funds and should be willing and able to contribute positively to the decision-making process of the Funds.

4. The candidate should be committed to understanding the Funds and the responsibilities of an Independent Trustee of an investment company and to regularly attending and participating in meetings of the Boards and the committees on which the candidate would be a member.

5. The candidate should have the ability to understand the sometimes conflicting interests of the various constituencies of the Funds and to act in the interests of all shareholders.

6. The candidate should not have a conflict of interest that would impair the candidate's ability to represent the interests of all the shareholders and to fulfill the responsibilities of an Independent Trustee.

7. The candidate should have the ability to serve a sufficient number of years before reaching any mandatory retirement age for Trustees that may be adopted by the Boards.

Nominees shall not be discriminated against on the basis of race, religion, national origin, sex, sexual orientation, disability or any other basis proscribed by law.

For each candidate, the Committee shall evaluate specific experience in light of the makeup of the then-current Boards.

The Committee may determine that a candidate who does not have the type of previous experience or knowledge referred to above should nevertheless be considered as a nominee if the Committee finds that the candidate has additional qualifications such that his/her qualifications, taken as a whole, demonstrate the same level of fitness to serve as an Independent Trustee.

In evaluating candidates, the Committee shall seek to have at least one Independent Trustee qualify as an "audit committee financial expert," as such term is defined by rules under the 1940 Act, and the Committee shall give preference to candidates that the Committee believes would qualify as audit committee financial experts.

II. Application of Criteria to Existing Independent Trustees. Each existing Independent Trustee shall continue to serve in such capacity in accordance with, and subject to, the Funds' charter documents and any policies adopted by the Boards relating thereto, including, without limitation, the Funds' retirement policy (if any) for Trustees. Any re-nomination of an existing Independent Trustee should not be viewed as automatic, but should be based on continuing qualification under the criteria set forth above. In addition, the Committee shall consider the existing Independent Trustee's performance on the Boards and any committees thereof.

APPENDIX B

This Appendix sets forth the dollar range of equity securities beneficially owned by each Director and Nominee, individually and in the aggregate, as of July 31, 2010.

	Joyce E. Heinzerling	Daniel S. Vandivort	Francis C. Oakley	David H. Porter
Value Line Aggressive Income Trust	none	none	$1-$10,000	$1-$10,000
Value Line Asset Allocation Fund, Inc.	none	none	$1-$10,000	$1-$10,000
Value Line U.S. Government Money Market Fund, Inc.	none	$1-$10,000	$1-$10,000	$1-$10,000
Value Line Centurion Fund, Inc.	none	none	none	none
Value Line Convertible Fund, Inc.	none	none	$1-$10,000	$1-$10,000
Value Line Emerging Opportunities Fund, Inc.	none	$1-$10,000	$10,001-$50,000	$1-$10,000
The Value Line Fund, Inc.	none	none	$1-$10,000	$1-$10,000
Value Line Income and Growth Fund, Inc.	none	$1-$10,000	$1-$10,000	$1-$10,000
Value Line Larger Companies Fund, Inc.	none	$1-$10,000	$1-$10,000	$1-$10,000
Value Line New York Tax Exempt Trust	none	none	none	$1-$10,000
Value Line Premier Growth Fund, Inc.	none	none	$1-$10,000	$1-$10,000
Value Line Strategic Asset Management Trust	none	none	none	none
The Value Line Tax Exempt Fund, Inc.	none	$1-$10,000	$1-$10,000	$1-$10,000
Value Line U.S. Government	none	none	$1-$10,000	$1-$10,000

Securities Fund, Inc.				
Aggregate Dollar Range of Fund Shares in all Funds Overseen or to be Overseen by the Nominee in Family of Investment Companies	none	$10,001-$50,000	$10,001-$50,000	$10,001-$50,000

	Paul Craig Roberts	Nancy-Beth Sheerr	Mitchell E. Appel
Value Line Aggressive Income Trust	none	$1-$10,000	none
Value Line Asset Allocation Fund, Inc.	$1-$10,000	$1-$10,000	none
Value Line U.S. Government Money Market Fund, Inc.	none	$1-$10,000	none
Value Line Centurion Fund, Inc.	none	none	none
Value Line Convertible Fund, Inc.	none	$1-$10,000	none
Value Line Emerging Opportunities Fund, Inc.	$1-$10,000	$1-$10,000	$1-$10,000
The Value Line Fund, Inc.	none	$1-$10,000	$1-$10,000
Value Line Income and Growth Fund, Inc.	$1-$10,000	$1-$10,000	$1-$10,000
Value Line Larger Companies Fund, Inc.	$1-$10,000	$1-$10,000	$1-$10,000
Value Line New York Tax Exempt Trust	none	none	none
Value Line Premier Growth Fund, Inc.	$1-$10,000	$1-$10,000	$1-$10,000
Value Line Strategic Asset Management Trust	none	none	none
The Value Line Tax Exempt Fund, Inc.	none four- family	$1-$10,000	none

Home
equity

Commercial
and multifamily

Construction

and land

Manufactured
homes

Other
consumer

Commercial
business

Total

Grade:

Pass

$
136,879

$
30,310

$
169,072

$
55,984

$
13,621

$
22,967

$
18,449

$
447,282

Watch

1,015

609

4,810

1,059

96

58

846

8,493

Special Mention

1,409

-

1,430

-

33

-

-

2,872

Substandard

1,822

654

-

-

48

5

-

2,529

Doubtful

-

-

-

-

-

-

-

-

Loss

-

-

-

-

-

-

-

-

Total

$
141,125

$
31,573

$
175,312

$
57,043

$
13,798

$
23,030

$
19,295

$
461,176

Nonaccrual and Past Due Loans. Loans are considered past due if the required principal and interest payments have not been received as of the date such payments were due. Loans are automatically placed on nonaccrual once the loan is 90 days past due or sooner if, in management's opinion, the borrower may be unable to meet payment of obligations as they become due, as well as when required by regulatory authorities.

The following table presents the recorded investment in nonaccrual loans as of June 30, 2016 and December 31, 2015, by type of loan (in thousands):

	June 30, 2016	December 31, 2015
One- to four- family	$875	$ 1,157
Home equity	494	344
Commercial and multifamily	2,143	-
Construction and land	164	-
Manufactured homes	79	27
Other consumer	22	-
Total	$3,777	$ 1,528

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The following table represents the aging of the recorded investment in past due loans as of June 30, 2016 by type of loan (in thousands):

	30-59 Days Past Due	60-89 Days Past Due	90 Days and Greater Past Due	90 Days and Greater Past Due and Still Accruing	Total Past Due	Current	Total Loans
One-to four- family	$ -	$ 458	$ 730	$ -	$ 1,188	$ 148,686	$ 149,874
Home equity	469	120	354	-	943	30,861	31,804
Commercial and multifamily	231	-	-	-	231	164,685	164,916
Construction and land	-	64	-	-	64	57,728	57,792
Manufactured homes	61	-	62	-	123	14,991	15,114
Other consumer	11	3	21	-	35	24,918	24,953
Commercial business	5	-	-	-	5	21,962	21,967
Total	$ 777	$ 645	$ 1,167	$ -	$ 2,589	$ 463,831	$ 466,420

The following table represents the aging of the recorded investment in past due loans as of December 31, 2015 by type of loan (in thousands):

	30-59 Days Past Due	60-89 Days Past Due	90 Days and Greater Past Due	90 Days and Greater Past Due and Still Accruing	Total Past Due	Current	Total Loans
One-to four- family	$ 2,453	$ 265	$ 881	$ 117	$ 3,716	$ 137,409	$ 141,125
Home equity	352	60	296	-	708	30,865	31,573
Commercial and multifamily	203	-	-	-	203	175,109	175,312
Construction and land	65	-	-	-	65	56,978	57,043
Manufactured homes	103	27	-	-	130	13,668	13,798
Other consumer	17	26	-	-	43	22,987	23,030
Commercial business	154	8	-	-	162	19,133	19,295
Total	$ 3,347	$ 386	$ 1,177	$ 117	$ 5,027	$ 456,149	$ 461,176

Nonperforming Loans. Loans are considered nonperforming when they are placed on nonaccrual and/or when they are considered to be nonperforming troubled debt restructurings (“TDRs”) and/or when they are 90 days or greater past due and still accruing. A TDR is a loan to a borrower that is experiencing financial difficulty that has been modified from its original terms and conditions in such a way that the Company is granting the borrower a concession of some kind. Nonperforming TDRs include TDRs that do not have sufficient payment history (typically greater than six months) to be considered performing or TDRs that have become 30 or more days past due.

The following table represents the credit risk profile of our loan portfolio based on payment activity as of June 30, 2016 by type of loan (in thousands):

	One- to four-family	Home equity	Commercial and multifamily	Construction and land	Manufactured homes	Other consumer	Commercial business	Total
Performing	$148,631	$31,143	$ 162,772	$ 57,792	$ 14,964	$24,931	$ 21,706	$461,939
Nonperforming	1,244	661	2,144	-	150	22	261	4,482
Total	$149,874	$31,804	$ 164,916	$ 57,792	$ 15,114	$24,953	$ 21,967	$466,420

The following table represents the credit risk profile of our loan portfolio based on payment activity as of December 31, 2015 by type of loan (in thousands):

	One- to four-family	Home equity	Commercial and multifamily	Construction and land	Manufactured homes	Other consumer	Commercial business	Total
Performing	$139,484	$31,146	$ 175,312	$ 57,043	$ 13,736	$23,030	$ 19,295	$459,046
Nonperforming	1,641	427	-		62	-	-	2,130
Total	$141,125	$31,573	$ 175,312	$ 57,043	$ 13,798	$23,030	$ 19,295	$461,176

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Impaired Loans. A loan is considered impaired when we have determined that we may be unable to collect payments of principal or interest when due under the terms of the loan. In the process of identifying loans as impaired, we take into consideration factors which include payment history and status, collateral value, financial condition of the borrower, and the probability of collecting scheduled payments in the future. Minor payment delays and insignificant payment shortfalls typically do not result in a loan being classified as impaired. The significance of payment delays and shortfalls is considered on a case by case basis, after taking into consideration the totality of circumstances surrounding the loans and the borrowers, including payment history. Impairment is measured on a loan by loan basis for all loans in the portfolio. All TDRs are also classified as impaired loans and are included in the loans individually evaluated for impairment in the calculation of the allowance for loan losses.

Impaired loans at June 30, 2016 and December 31, 2015 by type of loan were as follows (in thousands):

	June 30, 2016			
		Recorded Investment		
	Unpaid Principal Balance	Without Allowance	With Allowance	Related Allowance
One- to four- family	$6,066	$2,482	$ 3,129	$ 639
Home equity	1,079	606	443	100
Commercial and multifamily	4,862	2,191	2,671	424
Construction and land	87	-	87	23
Manufactured homes	414	129	265	56
Other consumer	24	-	24	24
Commercial business	646	149	497	37
Total	$13,178	$5,558	$ 7,116	$ 1,303

	December 31, 2015			
		Recorded Investment		
	Unpaid Principal Balance	Without Allowance	With Allowance	Related Allowance
One- to four- family	$6,011	$499	$5,280	$ 647
Home equity	994	162	742	110
Commercial and multifamily	1,966	1,430	536	36
Construction and land	91	-	91	18
Manufactured homes	366	-	361	63
Other consumer	5	-	5	-
Commercial business	114	-	114	8
Total	$9,547	$2,091	$7,129	$ 882

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Income on impaired loans for the three and six months ended June 30, 2016 and December 31, 2015 by type of loan were as follows (in thousands):

	Three Months Ended June 30, 2016		Three Months Ended June 30, 2015	
	Average Recorded Investment	Interest Income Recognized	Average Recorded Investment	Interest Income Recognized
One- to four- family	$5,539	$ 72	$4,829	$ 57
Home equity	993	15	1,149	9
Commercial and multifamily	4,887	66	2,767	40
Construction and land	88	1	158	1
Manufactured homes	387	9	387	7
Other consumer	26	1	60	-
Commercial business	573	11	121	1
Total	$12,493	$ 175	$9,471	$ 115

	Six Months Ended June 30, 2016		Six Months Ended June 30, 2015	
	Average Recorded Investment	Interest Income Recognized	Average Recorded Investment	Interest Income Recognized
One- to four- family	$5,619	$ 140	$4,614	$ 122
Home equity	963	27	1,181	23
Commercial and multifamily	3,913	133	2,829	70
Construction and land	89	2	165	2
Manufactured homes	378	16	393	13
Other consumer	19	2	57	1
Commercial business	420	18	122	3
Total	$11,401	$ 338	$9,361	$ 234

Forgone interest on nonaccrual loans was $78,000 and $40,000 for the six months ended June 30, 2016 and 2015, respectively. There were no commitments to lend additional funds to borrowers whose loans were classified as nonaccrual, TDR or impaired at June 30, 2016 or December 31, 2015.

Troubled debt restructurings. Loans classified as TDRs totaled $5.7 million and $6.0 million at June 30, 2016 and December 31, 2015, respectively, and are included in impaired loans. The Company has granted in its TDRs a variety of concessions to borrowers in the form of loan modifications. The modifications granted can generally be described in the following categories:

Rate Modification: A modification in which the interest rate is changed.

Term Modification: A modification in which the maturity date, timing of payments or frequency of payments is changed.

Payment Modification: A modification in which the dollar amount of the payment is changed. Interest only modifications in which a loan in converted to interest only payments for a period of time are included in this category.

Combination Modification: Any other type of modification, including the use of multiple categories above.

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There were no new TDRs that occurred during the six months ended June 30, 2016 and 2015. There were no loans modified as TDRs within the previous 12 months.

There were no post-modification changes for the recorded investment in loans that were recorded as a result of the TDRs for the three and six months ended June 30, 2016 and 2015, respectively. The allowance for loan losses allocated to TDRs at June 30, 2016 and December 31, 2015 was $655,000 and $349,000, respectively.

Note 5 – Fair Value Measurements

The following tables present information about the level in the fair value hierarchy for the Company's financial assets and liabilities, whether or not recognized or recorded at fair value as of June 30, 2016 and December 31, 2015 (in thousands):

	June 30, 2016		Fair Value Measurements Using:		
	Carrying Value	Estimated Fair Value	Level 1	Level 2	Level 3
FINANCIAL ASSETS:					
Cash and cash equivalents	$45,187	$45,187	$45,187	$-	$-
Available-for-sale securities	7,393	7,393	-	7,393	-
Loans held for sale	687	687	-	687	-
Loans, net	459,810	462,150	-	-	462,150
Accrued interest receivable	1,592	1,592	1,592	-	-
Mortgage servicing rights	3,026	3,026	-	-	3,026
FHLB stock	2,073	2,073	-	-	2,073
FINANCIAL LIABILITIES:					
Non-maturity deposits	283,329	283,329	-	283,329	-
Time deposits	160,538	159,874	-	159,874	-
Borrowings	35,613	35,605	-	35,605	-
Accrued interest payable	90	90	-	90	-

	December 31, 2015		Fair Value Measurements Using:		
	Carrying Value	Estimated Fair Value	Level 1	Level 2	Level 3
FINANCIAL ASSETS:					
Cash and cash equivalents	$48,264	$48,264	$48,264	$-	$-
Available-for-sale securities	6,696	6,696	-	6,268	428
Loans held for sale	2,091	2,091	-	2,091	-
Loans, net	454,833	454,854	-	-	454,854
Accrued interest receivable	1,608	1,608	1,608	-	-
Mortgage servicing rights	3,249	3,249	-	-	3,249
FHLB Stock	2,212	2,212	-	-	2,212
FINANCIAL LIABILITIES:					
Non-maturity deposits	271,639	271,639	-	271,639	-

Time deposits	168,385	168,091	-	168,091	-
Borrowings	40,435	40,421	-	40,421	-
Accrued interest payable	72	72	-	72	-

The following table presents the balance of assets measured at fair value on a recurring basis as of June 30, 2016 and December 31, 2015 (in thousands):

	Fair Value at June 30, 2016			
Description	Total	Level 1	Level 2	Level 3
Municipal bonds	$3,554	$ -	$3,544	$-
Agency mortgage-backed securities	3,470	-	3,470	-
Non-agency mortgage-backed securities	379	-	-	379
Mortgage servicing rights	3,026	-	-	3,026

	Fair Value at December 31, 2015			
Description	Total	Level 1	Level 2	Level 3
Municipal bonds	$2,096	$ -	$2,096	$-
Agency mortgage-backed securities	4,172	-	4,172	-
Non-agency mortgage-backed securities	428	-	-	428
Mortgage servicing rights	3,249	-	-	3,249

For the three and six months ended June 30, 2016 and 2015 there were no transfers between Level 1 and Level 2 nor between Level 2 and Level 3.

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The following table provides a description of the valuation technique, unobservable input, and qualitative information about the unobservable inputs for the Company's assets and liabilities classified as Level 3 and measured at fair value on a recurring basis at June 30, 2016:

Financial Instrument	Valuation Technique	Unobservable Input(s)	Range (Weighted Average)
Mortgage Servicing Rights	Discounted cash flow	Prepayment speed assumption	105-462% (177%)
		Discount rate	8-12% (10%)
Non-agency mortgage-backed securities	Discounted cash flow	Discount rate	(8%)

Generally, any significant increases in the constant prepayment rate and discount rate utilized in the fair value measurement of the mortgage servicing rights will result in a negative fair value adjustment (and decrease in the fair value measurement). Conversely, a decrease in the constant prepayment rate and discount rate will result in a positive fair value adjustment (and increase in the fair value measurement). An increase in the weighted average life assumptions will result in a decrease in the constant prepayment rate and conversely, a decrease in the weighted average life will result in an increase of the constant prepayment rate.

The following table provides a reconciliation of non-agency mortgage backed securities measured at fair value using significant unobservable inputs (Level 3) on a recurring basis during the three and six months ended June 30, 2016 and 2015 (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
Beginning balance, at fair value	$415	$496	$428	$2,345
OTTI impairment losses	-	-	-	-
Principal payments	(37)	(26)	(52)	(187)
Sales	-	-	-	(1,702)
Change in unrealized loss	1	13	3	27
Ending balance, at fair value	$379	$483	$379	$483

Mortgage servicing rights are measured at fair value using significant unobservable input (Level 3) on a recurring basis and a reconciliation of this asset can be found in Note 6 – Mortgage Servicing Rights.

The following tables present the balance of assets measured at fair value on a nonrecurring basis at the dates indicated (in thousands):

	Fair Value at June 30, 2016			
	Total	Level 1	Level 2	Level 3
OREO and repossessed assets	$780	$ -	$ -	$780
Impaired loans	12,673	-	-	12,673

Fair Value at December 31, 2015

	Total	Level 1	Level 2	Level 3
OREO and repossessed assets	$ 769	$ -	$ -	$ 769
Impaired loans	9,220	-	-	9,220

There were no liabilities carried at fair value, measured on a recurring or nonrecurring basis, at June 30, 2016 or December 31, 2015.

The following table provides a description of the valuation technique, observable input, and qualitative information about the unobservable inputs for the Company's assets and liabilities classified as Level 3 and measured at fair value on a nonrecurring basis at June 30, 2016:

Financial Instrument	Valuation Technique(s)	Unobservable Input(s)	Range (Weighted Average)
OREO	Market approach	Adjustment for differences between comparable sales	5-48% (21%)
Impaired loans	Market approach	Adjustment for differences between comparable sales	0-100% (7%)

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A description of the valuation methodologies used for impaired loans and OREO is as follows:

Impaired Loans - The fair value of collateral dependent loans is based on the current appraised value of the collateral or internally developed models utilizing a calculation of expected discounted cash flows which contain management's assumptions.

OREO and Repossessed Assets – The fair value of OREO and repossessed assets is based on the current appraised value of the collateral.

The following methods and assumptions were used to estimate the fair value of other financial instruments:

Cash and cash equivalents, accrued interest receivable and payable, and advance payments from borrowers for taxes and insurance - The estimated fair value is equal to the carrying amount.

Available-for-sale ("AFS") Securities – AFS securities are recorded at fair value based on quoted market prices, if available. If quoted market prices are not available, management utilizes third-party pricing services or broker quotations from dealers in the specific instruments. Level 2 securities include those traded on an active exchange, as well as U.S. government and its agencies securities. Level 3 securities include private label mortgage-backed securities.

Loans Held for Sale - Residential mortgage loans held for sale are recorded at the lower of cost or fair value. The fair value of fixed-rate residential loans is based on whole loan forward prices obtained from government sponsored enterprises. At June 30, 2016 and December 31, 2015, loans held for sale were carried at cost, as no impairment was required.

Loans - The estimated fair value for all fixed rate loans is determined by discounting the estimated cash flows using the current rate at which similar loans would be made to borrowers with similar credit ratings and maturities. The estimated fair value for variable rate loans is the carrying amount. The fair value for all loans also takes into account projected loan losses as a part of the estimate.

Mortgage Servicing Rights –The fair value of mortgage servicing rights is determined though a discounted cash flow analysis, which uses interest rates, prepayment speeds, discount rates, and delinquency rate assumptions as inputs.

FHLB stock - The estimated fair value is equal to the par value of the stock, which approximates fair value.

Deposits - The estimated fair value of deposit accounts (savings, demand deposit, and money market accounts) is the carrying amount. The fair values of fixed-maturity time certificates of deposit are estimated by discounting the estimated cash flows using the current rate at which similar certificates would be issued.

Borrowings - The fair value of borrowings are estimated using discounted cash flow analyses, based on the Company's current incremental borrowing rates for similar types of borrowing arrangements.

Off-balance-sheet financial instruments - The fair value for the Company's off-balance-sheet loan commitments are estimated based on fees charged to others to enter into similar agreements taking into account the remaining terms of the agreements and credit standing of the Company's customers. The estimated fair value of these commitments is not significant.

We assume interest rate risk (the risk that general interest rate levels will change) as a result of our normal operations. As a result, the fair values of our financial instruments will change when interest rate levels change, which may be favorable or unfavorable to us. Management attempts to match maturities of assets and liabilities to the extent necessary or possible to minimize interest rate risk. However, borrowers with fixed-rate obligations are less likely to prepay in a rising rate environment and more likely to prepay in a falling rate environment. Conversely, depositors who are receiving fixed rates are more likely to withdraw funds before maturity in a rising rate environment and less likely to do so in a falling rate environment. Management monitors rates and maturities of assets and liabilities and attempts to minimize interest rate risk by establishing early withdrawal penalties for certificates of deposit, creating interest rate floors for certain variable rate loans, adjusting terms of new loans and deposits, by borrowing at fixed rates for fixed terms and investing in securities with terms that mitigate our overall interest rate risk.

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Note 6 – Mortgage Servicing Rights

The unpaid principal balances of loans serviced for Federal National Mortgage Association at June 30, 2016 and December 31, 2015, totaled approximately $369.6 million and $360.4 million, respectively, and was not included in the Company’s financial statements. We also service loans for other financial institutions.

A summary of the change in the balance of mortgage servicing rights during the three and six months ended June 30, 2016 and 2015 were as follows (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
Beginning balance, at fair value	$3,095	$2,890	$3,249	$3,028
Servicing rights that result from transfers of financial assets	151	214	259	431
Changes in fair value:				
Due to changes in model inputs or assumptions[1]	(77)	352	(190)	174
Other[2]	(143)	(185)	(292)	(362)
Ending balance, at fair value	$3,026	$3,271	$3,026	$3,271

(1) Represents changes in discount rates and prepayment speed assumptions, which are primarily affected by changes in interest rates
(2) Represents changes due to collection or realization of expected cash flows over time.

The key economic assumptions used in determining the fair value of mortgage servicing rights at the dates indicated are as follows:

	At June 30,	
	2016	2015
Prepayment speed (Public Securities Association “PSA” model)	223 %	177 %
Weighted-average life (years)	5.8	6.7
Yield to maturity discount rate	10.0%	10.0%

The amount of contractually specified servicing, late and ancillary fees earned and recorded in mortgage servicing income on the Condensed Consolidated Statements of Income was $208,000 and $413,000 for the three and six months ended June 30, 2016, respectively and $214,000 and $469,000 for the three and six months ended June 30, 2015, respectively.

Note 7 – Commitments and Contingencies

In the normal course of operations, the Company engages in a variety of financial transactions that are not recorded in our financial statements. These transactions involve varying degrees of off-balance sheet credit, interest rate and liquidity risks. These transactions are used primarily to manage customers’ requests for funding and take the form of loan commitments and lines of credit.

Note 8 – Borrowings and FHLB Stock

The Company utilizes a loan agreement with the FHLB of Seattle. The terms of the agreement call for a blanket pledge of a portion of the Company's mortgage and commercial and multifamily portfolio based on the outstanding balance. At June 30, 2016 and December 31, 2015, the amount available to borrow under this credit facility was $180.6 million and $174.0 million, respectively. At June 30, 2016, the credit facility was collateralized as follows: one- to four- family mortgage loans with a market value of $105.0 million, commercial and multifamily mortgage loans with a market value of $135.6 million and home equity loans with a market value of $7.9 million. The Company had outstanding borrowings under this arrangement of $35.6 million and $40.4 million at June 30, 2016 and December 31, 2015, respectively. Additionally, the Company had outstanding letters of credit from the FHLB with a notional amount of $43.5 million and $47.5 million at June 30, 2016 and December 31, 2015, respectively to secure public deposits which exceeded the collateral requirements established by the Washington Public Deposit Protection Commission. The remaining amount available to borrow as of June 30, 2016 and December 31, 2015, was $101.5 million and $86.1 million, respectively.

As a member of the FHLB system, the Bank is required to maintain a minimum level of investment in FHLB stock based on specific percentages of its outstanding FHLB advances. At June 30, 2016 and December 31, 2015, the Company had an investment of $2.1 million and $2.2 million, respectively, in FHLB stock.

The Company participates in the Federal Reserve Bank Borrower-in-Custody program, which gives the Company access to the discount window. The terms of the program call for a pledge of specific assets. The Company had unused borrowing capacity of $27.4 million and $25.9 million and no outstanding borrowings under this program at June 30, 2016 and December 31, 2015, respectively.

The Company has access to a Fed Funds line of credit from the Pacific Coast Banker's Bank. The line has a one-year term maturing on June 30, 2017 and is renewable annually. The Company had unused borrowing capacity of $2.0 million and no outstanding borrowings under this agreement at June 30, 2016 and December 31, 2015.

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The Company has access to a Fed Funds line of credit from Zions Bank under a Fed Funds Sweep and Line Agreement dated September 26, 2014. The agreement allows access to a Fed Funds line of up to $9.0 million and requires the Company to maintain cash balances with Zions Bank of $250,000. The agreement has no maturity date. There were no outstanding borrowings on this line of credit at June 30, 2016 or December 31, 2015.

Note 9 – Earnings Per Common Share

Basic earnings per common share is computed by dividing net income (which has been adjusted for distributed and undistributed earnings to participating securities) by the weighted-average number of common shares outstanding for the period, reduced for average unallocated ESOP shares and average unvested restricted stock awards. Unvested share-based awards contain non-forfeitable rights to dividends or dividend equivalents (whether paid or unpaid) at the same rate as common stockholders. Therefore, under the two-class method, the difference in earnings per share is not significant for these participating securities. Diluted earnings per common share reflects the potential dilution that could occur if securities or other contracts to issue common stock (such as stock awards and options) were exercised or converted to common stock, or resulted in the issuance of common stock that then shared in the Company's earnings. Diluted earnings per common share is computed by dividing net income by the weighted-average number of common shares outstanding for the period increased for the dilutive effect of unexercised stock options and unvested restricted stock awards. The dilutive effect of the unexercised stock options and unvested restricted stock awards is calculated under the treasury stock method utilizing the average market value of the Company's stock for the period.

Earnings per share are summarized in the following table (all figures in thousands except earnings per share):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
Net income	$ 1,254	$ 1,247	$ 2,360	$ 2,455
Weighted average number of shares outstanding, basic	2,481	2,511	2,479	2,517
Effect of potentially dilutive common shares[1]	77	91	73	85
Weighted average number of shares outstanding, diluted	2,558	2,602	2,552	2,603
Earnings per share, basic	$ 0.51	$ 0.50	$ 0.95	$ 0.98
Earnings per share, diluted	$ 0.49	$ 0.48	$ 0.92	$ 0.94

[1] Represents the effect of the assumed exercise of stock options and vesting of non-participating restricted shares based on the treasury stock method.

There were no anti-dilutive securities at June 30, 2016 or 2015.

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Note 10 – Stock-based Compensation

Stock Options and Restricted Stock

The Company currently has two existing Equity Incentive Plans, a 2008 Equity Inventive Plan (the"2008 Plan") and a 2013 Equity Incentive Plan (the "2013 Plan"), and together with the 2008 Plan, (the "Plans"), both of which were approved by shareholders. The Plans permit the grant of restricted stock, restricted stock units, stock options, and stock appreciation rights. Under the 2008 Plan, 126,287 shares of common stock were approved for awards for stock options and stock appreciation rights and 50,514 shares of common stock were approved for awards for restricted stock and restricted stock units. Under the 2013 Plan, 141,750 shares of common stock were approved for awards for stock options and stock appreciation rights and 56,700 shares of common stock were approved for awards for restricted stock and restricted stock units.

As of June 30, 2016, awards for stock options totaling 233,532 shares and awards for restricted stock totaling 106,630 shares of Company common stock have been granted, net of any forfeitures, to participants in the Plans. During the three months ended June 30, 2016 and June 30, 2015, share-based compensation expense totaled $126,000 and $104,000, respectively. During the six months ended June 30, 2016 and June 30, 2015, share-based compensation expense totaled $228,000 and $207,000, respectively.

Stock Option Awards

The stock option awards granted to date under the 2008 Plan vest in 20 percent annual increments commencing one year from the grant date in accordance with the requirements of the 2008 Plan. The stock option awards granted to date under the 2013 Plan vest in equal annual installments over two to four years. All of the options granted are exercisable for a period of 10 years from the date of grant, subject to vesting. The following is a summary of the Company's stock option plan awards during the six months ended June 30, 2016:

	Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term In Years	Aggregate Intrinsic Value
Outstanding at the beginning of the year	184,407	$ 14.47	6.97	$1,490,009
Granted	10,993	$ 22.31		
Exercised	(1,077)	$ 15.02		
Forfeited	(3,487)	$ 17.23		
Expired	-	-		
Outstanding at June 30, 2016	190,836	$ 14.87	6.63	$1,732,752
Exercisable	110,772	$ 13.08	5.68	$1,204,575
Expected to vest, assuming a 0% forfeiture rate over the vesting term	80,064	$ 17.35	7.95	$528,177

As of June 30, 2016, there was $463,000 of total unrecognized compensation cost related to non-vested stock options granted under the Plans. The cost is expected to be recognized over the remaining weighted-average vesting period of 2.5 years.

The fair value of each option award granted is estimated on the date of grant using a Black-Scholes model. The assumptions used for the six months ended June 30, 2016 are presented in the table below:

Annual dividend yield	1.03	%
Expected volatility	25.48	%
Risk-free interest rate	1.64	%
Expected term	6.92 years	
Weighted-average grant date fair value per option granted	$ 5.78	

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SOUND FINANCIAL BANCORP, INC. AND SUBSIDIARY
Notes to Condensed Consolidated Financial Statements (unaudited)

Restricted Stock Awards

The fair value of the restricted stock awards is equal to the fair value of the Company's stock at the date of grant. Compensation expense is recognized over the vesting period that the awards are based. The restricted stock awards granted under the 2008 Plan vest in 20 percent annual increments commencing one year from the grant date in accordance with the requirements of the 2008 plan. The restricted stock awards granted to date under the 2013 Plan vest in equal annual installments over two to four years.

The following is a summary of the Company's outstanding restricted stock awards during the six months ended June 30, 2016:

Non-vested Shares	Shares	Weighted-Average Grant-Date Fair Value Per Share
Non-vested at January 1, 2016	31,553	$ 16.32
Granted	11,606	22.31
Vested	(15,962)	17.59
Forfeited	(1,059)	17.36
Expired	-	-
Non-vested at June 30, 2016	26,138	$ 18.08
Expected to vest assuming a 0% forfeiture rate over the vesting term	26,138	$ 18.08

As of June 30, 2016, there was $574,000 of unrecognized compensation cost related to non-vested restricted stock granted under the Plan remaining. The cost is expected to be recognized over the weighted-average vesting period of 1.53 years. The total fair value of shares vested for the six months ended June 30, 2016 and 2015 was $345,000 and $240,000, respectively.

Employee Stock Ownership Plan

In January 2008, the ESOP borrowed $1.2 million from the Company to purchase common stock of the Company. In August 2012, in conjunction with the Company's "second step" conversion to become a fully converted public company, the ESOP borrowed $1.1 million from the Company to purchase additional common stock of the Company. Both loans are being repaid principally by the Bank through contributions to the ESOP over a period of ten years. The interest rate on the loans is fixed at 4.0% and 2.25%, per annum, respectively. As of June 30, 2016, the remaining balances of the ESOP loans were $270,000 and $701,000, respectively.

Neither the loan balances nor the related interest expense are reflected on the condensed consolidated financial statements.

At June 30, 2016, the ESOP was committed to release 21,443 shares of the Company's common stock to participants and held 88,243 unallocated shares remaining to be released in future years. The fair value of the 188,981 shares of Company common stock held by the ESOP trust was $4.5 million at June 30, 2016. ESOP compensation expense included in salaries and benefits was $135,000 and $271,000 for the three and six months ended June 30, 2016 and $102,000 and $204,000 for the three and six months ended June 30, 2015, respectively.

Note 11 – Subsequent Event

On July 26, 2016, the Company declared a quarterly cash dividend of $0.075 per common share, payable August 26, 2016 to shareholders of record at the close of business August 12, 2016.

On July 26, 2016, the Company's Board of Directors authorized the repurchase of up to 50,000 shares or approximately 2% of the Company's outstanding shares. The shares may be purchased in the open market or in privately negotiated transactions, from time to time, over a twelve-month period depending upon market conditions and other factors.

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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operation

MANAGEMENT'S DISCUSSION AND ANALYSIS OF

FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Special Note Regarding Forward-Looking Statements

Certain matters discussed in this Form 10-Q constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These statements relate to our financial condition, results of operations, plans, objectives, future performance or business. Forward-looking statements are not statements of historical fact, are based on certain assumptions and are generally identified by use of the words "believes," "expects," "anticipates," "estimates," "forecasts," "intends," "plans," "targets," "potentially," "probably," "projects," "outlook" or similar expressions or future or co verbs such as "may," "will," "should," "would" and "could." Forward-looking statements include statements with respect to ou beliefs, plans, objectives, goals, expectations, assumptions and statements about, among other things, expectations of the business environment in which we operate, projections of future performance or financial items, perceived opportunities in the market, potential future credit experience, and statements regarding our mission and vision. These forward-looking statements are based upon current management expectations and may, therefore, involve risks and uncertainties. Our actual results, performance, or achievements may differ materially from those suggested, expressed, or implied by forward-looking statements as a result of a wide variety or range of factors including, but not limited to:

- changes in economic conditions, either nationally or in our market area;
- fluctuations in interest rates;
- the risks of lending and investing activities, including changes in the level and direction of loan delinquencies and write-offs and changes in estimates of the adequacy of our allowance for loan losses;
- the possibility of other-than-temporary impairments of securities held in our securities portfolio;
- our ability to access cost-effective funding;
- fluctuations in the demand for loans, the number of unsold homes, land and other properties, and fluctuations in real estate values and both residential and commercial and multifamily real estate market conditions in our market area;
- secondary market conditions for loans and our ability to sell loans in the secondary market;
- our ability to attract and retain deposits;
- our ability to successfully integrate any assets, liabilities, customers, systems, and management personnel we may acquire into our operations and our ability to realize related revenue synergies and expected cost savings and other benefits within the anticipated time frames or at all;
- legislative or regulatory changes such as the Dodd-Frank Wall Street Reform and Consumer Protection Act and its implementing regulations that adversely affect our business, as well as changes in regulatory policies and principles, or the interpretation of regulatory capital or other rules including changes related to Basel III;
- monetary and fiscal policies of the Board of Governors of the Federal Reserve System ("Federal Reserve") and the U.S. Government and other governmental initiatives affecting the financial services industry;

- results of examinations of Sound Financial Bancorp and Sound Community Bank by their regulators, including the possibility that the regulators may, among other things, require us to increase our allowance for loan losses or to write-down assets, change Sound Community Bank's regulatory capital position or affect our ability to borrow funds or maintain or increase deposits, which could adversely affect our liquidity and earnings;

- increases in premiums for deposit insurance;

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- our ability to control operating costs and expenses;
- the use of estimates in determining fair value of certain of our assets, which estimates may prove to be incorrect and result in significant declines in valuation;
- difficulties in reducing risks associated with the loans on our balance sheet;
- staffing fluctuations in response to product demand or the implementation of corporate strategies that affect our workforce and potential associated charges;
- computer systems on which we depend could fail or experience a security breach;
- our ability to retain key members of our senior management team;
- costs and effects of litigation, including settlements and judgments;
- our ability to implement our business strategies;
- increased competitive pressures among financial services companies;
- changes in consumer spending, borrowing and savings habits;
- the availability of resources to address changes in laws, rules, or regulations or to respond to regulatory actions;
- our ability to pay dividends on our common stock;
- adverse changes in the securities markets;
- the inability of key third-party providers to perform their obligations to us;
- changes in accounting policies and practices, as may be adopted by the financial institution regulatory agencies or the Financial Accounting Standards Board, including additional guidance and interpretation on accounting issues and details of the implementation of new accounting methods; and
- other economic, competitive, governmental, regulatory, and technological factors affecting our operations, pricing, products and services and the other risks described from time to time in this Form 10-Q and our 2015 Form 10-K and other filings with the SEC.

We wish to advise readers not to place undue reliance on any forward-looking statements and that the factors listed above could materially affect our financial performance and could cause our actual results for future periods to differ materially from any such forward-looking statements expressed with respect to future periods and could negatively affect our stock price performance.

We do not undertake and specifically decline any obligation to publicly release the result of any revisions which may be made to any forward-looking statements to reflect events or circumstances after the date of such statements or to reflect the occurrence of anticipated or unanticipated events.

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General

References in this document to Sound Financial Bancorp refer to Sound Financial Bancorp, Inc. and its predecessor, Sound Financial, Inc., a federal corporation, and references to the "Bank" refer to Sound Community Bank. References to "we," "us," "our" and the Company means Sound Financial Bancorp and its wholly-owned subsidiary, Sound Community Bank, unless the context otherwise requires.
Sound Financial Bancorp, a Maryland corporation, is a bank holding company for its wholly owned subsidiary, Sound Community Bank. Substantially all of Sound Financial Bancorp's business is conducted through Sound Community Bank, a Washington state-chartered commercial bank. As a Washington commercial bank, the Bank's regulators are the Washington State Department of Financial Institutions ("WDFI") and the Federal Deposit Insurance Corporation ("FDIC"). The Federal Reserve is the primary federal regulator for Sound Financial Bancorp.

Sound Community Bank's deposits are insured up to applicable limits by the FDIC. At June 30, 2016, Sound Financial Bancorp had total consolidated assets of $541.8 million, net loans of $459.8 million, deposits of $443.9 million and stockholders' equity of $56.8 million. The shares of Sound Financial Bancorp are traded on The NASDAQ Capital Market under the symbol "SFBC." Our executive offices are located at 2005 5th Avenue, Suite 200, Seattle, Washington, 98121.

Our principal business consists of attracting retail and commercial deposits from the general public and investing those funds, along with borrowed funds, in loans secured by first and second mortgages on one- to four-family residences (including home equity loans and lines of credit), commercial and multifamily, consumer and commercial business loans and construction and land loans. We offer a variety of secured and unsecured consumer loan products, including manufactured home loans, floating home loans, automobile loans, boat loans and recreational vehicle loans. As part of our business, we focus on residential mortgage loan originations, many of which we sell to Fannie Mae. We sell the majority of these loans with servicing retained to maintain the direct customer relationship and to continue providing quality customer service to our borrowers. We also originate loans which do not conform to the underwriting standards of Fannie Mae (“non-conforming”) to be held in our loan portfolio and for sale with servicing released. We originate and retain a significant amount of commercial real estate loans, including those secured by owner-occupied and non owner-occupied commercial real estate, multifamily property, manufactured home parks and construction and land development loans.

Critical Accounting Policies

Certain of our accounting policies are important to an understanding of our financial condition, since they require management to make difficult, complex or subjective judgments, which may relate to matters that are inherently uncertain. Estimates associated with these policies are susceptible to material changes as a result of changes in facts and circumstances. Facts and circumstances that could affect these judgments include, but are not limited to, changes in interest rates, changes in the performance of the economy and changes in the financial condition of borrowers. Management believes that its critical accounting policies include determining the allowance for loan losses, accounting for other-than-temporary impairment of securities, accounting for mortgage servicing rights, accounting for other real estate owned and accounting for deferred income taxes. Our methodologies for analyzing the allowance for loan losses, other than other-then-temporary impairment, mortgage servicing rights, other real estate owned and deferred tax asset accounts are described in our 2015 Form 10-K. There have been no significant changes in the Company’s application of accounting policies since December 31, 2015.

Comparison of Financial Condition at June 30, 2016 and December 31, 2015

General. Total assets increased $1.0 million, or 0.2%, to $541.8 million at June 30, 2016 from $540.8 million at December 31, 2015. This increase was primarily the result of a $5.0 million, or 1.1%, increase in the net loan portfolio, partially offset by a $3.1 million, or 6.4%, decrease in cash and cash equivalents and a $1.4 million decrease

in loans held for sale. The decline in the cash and cash equivalents, along with the $3.8 million, or 0.9%, increase in deposits was primarily used to fund $5.2 million loan growth and to pay down in borrowings which declined $4.8 million or 11.9% from December 31, 2015 to June 30, 2016.

Cash and Securities. Cash and cash equivalents decreased $3.1 million, or 6.4%, to $45.2 million at June 30, 2016 from $48.3 million at December 31, 2015. Available-for-sale securities, which consist primarily of agency mortgage-backed securities, increased $697,000, or 10.4%, from $6.7 million at December 31, 2015 to $7.4 million at June 30, 2016 as a result of purchases of municipal bonds of $1.3 million, partially offset by principal repayments on securities during the second quarter.

Loans. Our gross loan portfolio increased $5.2 million, or 1.1%, to $466.4 million at June 30, 2016 from $461.2 million at December 31, 2015.

The following table reflects the changes in the types of loans in our portfolio at June 30, 2016, as compared to December 31, 2015 (dollars in thousands):

	June 30, 2016	December 31, 2015	Amount Change	Percent Change
One-to-four-family	$149,874	$ 141,125	$8,749	6.2 %
Home equity	31,804	31,573	231	0.7
Commercial and multifamily	164,916	175,312	(10,396)	(5.9)
Construction and land	57,792	57,043	749	1.3
Manufactured homes	15,114	13,798	1,316	9.5
Other Consumer	24,953	23,030	1,923	8.3
Commercial business	21,967	19,295	2,672	13.8
Total loans, before deferred fees and allowance for loan losses	$466,420	$ 461,176	5,244	1.1 %

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The increases in our loan portfolio were primarily a result of our loan production exceeding loan repayments . At June 30, 2016, our loan portfolio remained well-diversified with commercial and multifamily real estate loans accounting for 35.4% of the portfolio. One-to-four-family loans account for 32.1% of the portfolio. Home equity, manufactured and other consumer loans account for 15.4% of the portfolio. Construction and land loans account for 12.4% of the portfolio and commercial business loans account for the remaining 4.7% of total loans.

Loans held for sale decreased $1.4 million, or 67.1%, to $687,000 at June 30, 2016 from $2.1 million at December 31, 2015. The decrease in loans held for sale was a result of the timing of originations and sales between the two period ending dates.

Mortgage Servicing Rights. At June 30, 2016 and December 31, 2015, we had $3.0 million and $3.2 million, respectively, in mortgage servicing rights recorded at fair value. We record mortgage servicing rights on loans sold to Fannie Mae and other financial institutions with servicing retained and upon acquisition of a servicing portfolio. We stratify our capitalized mortgage servicing rights based on the type, term and interest rates of the underlying loans. Mortgage servicing rights are carried at fair value. If the fair value of our mortgage servicing rights fluctuates significantly, our financial results could be materially impacted.

Nonperforming Assets. At June 30, 2016, nonperforming assets totaled $5.3 million, or 0.97% of total assets, compared to $2.9 million, or 0.54% of total assets at December 31, 2015.

The table below sets forth the amounts and categories of nonperforming assets at the dates indicated (dollars in thousands):

	Nonperforming Assets			
	At June 30, 2016	At December 31, 2015	Amount Change	Percent Change
Nonaccrual loans	$3,777	$ 1,528	$2,249	147.19%
Accruing loans 90 days or more delinquent	-	117	(117)	Nm
Nonperforming TDRs	705	485	(230)	(32.62)
Total nonperforming loans	4,482	2,130	2,352	114.57
OREO and repossessed assets	780	769	11	1.43
Total nonperforming assets	$5,262	$ 2,899	$2,363	81.51 %

Nonperforming loans, consisting of nonaccrual loans, accruing loans 90 days or more delinquent and nonperforming TDRs, increased to $4.5 million, or 0.96% of total loans at June 30, 2016 from $2.1 million or 0.47% of total loans, at December 31, 2015. This increase reflects the inclusion of a $2.3 million multifamily loan in Port Angeles, WA in nonaccrual loans during the six months ended June 30, 2016. The loan, while currently performing, was transferred into nonaccrual in the second quarter due to the uncertainty of full collection. At June 30, 2016, we had a specific reserve of $387,000 on this credit to reflect impairment based on recent collateral valuation.

OREO and repossessed assets decreased due to the sale of three properties in the portfolio. During the six months ended June 30, 2016, we repossessed one manufactured home valued at $18,000 and we sold a parcel of land valued at $124,000. The aggregate gain on all sales during the three and six months ended June 30, 2016 was $8,000 and $0, respectively. The gain on sales of properties was offset by expenses related to OREO properties. Our largest OREO at June 30, 2016 consisted of a commercial building with a recorded value of $600,000 located in Clallam County, Washington that we acquired as a part of the the Columbia Bank branch purchase. Our next largest OREO property is a $170,000 one- to four- family property located in Clallam County, Washington.

Allowance for Loan Losses. Our allowance for loan losses at June 30, 2016 was $4.8 million, or 1.04% of total loans receivable compared to $4.6 million, or 1.01% of total loans receivable at December 31, 2015. The allowance for loan losses is maintained to cover losses that are probable and can be estimated on the date of evaluation in accordance with generally accepted accounting principles in the United States. It is our best estimate of probable credit losses inherent in our loan portfolio. The increase in the allowance for loan losses compared to December 31, 2015 was primarily due to increased loan balances and the increase in non-performing loans.

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The following table reflects the adjustments in our allowance during the periods indicated (dollars in thousands):

	At and For the Three Months Ended June 30,		At and For the Six Months Ended June 30,	
	2016	2015	2016	2015
Balance at beginning of period	$ 4,709	$4,436	$ 4,636	$4,387
Charge-offs	(39)	(75)	(122)	(139)
Recoveries:	68	11	74	24
Net Recoveries (charge-offs)	29	(64)	(48)	(115)
Provisions charged to operations	100	200	250	300
Balance at end of period	$ 4,838	$4,572	$ 4,838	$4,572
Ratio of net charge-offs (recoveries) during the period to average loans outstanding during the period	(0.02)%	0.06 %	0.02 %	0.05 %

	June 30, 2016	December 31, 2015
Allowance as a percentage of nonperforming loans	107.94 %	217.65 %
Allowance as a percentage of total loans (end of period)	1.04	1.01

Specific loan loss reserves increased to $1.3 million at June 30, 2016 compared to $882,000 at December 31, 2015, while general loan loss reserves decreased to $3.5 million at June 30, 2016, compared to $3.8 million at December 31, 2015. The increase in specific loan loss reserves was primarily due to the inclusion of a $2.3 million multifamily loan in Port Angeles, WA during the six months ended June 30, 2016. This is our largest nonperforming loan as of June 30, 2016. The specific reserve for this loan is $389,000, which management believes is adequate to cover the expected loss on this loan. The decrease in general loan loss reserves was due to lower historical loss rates. Net charge-offs for the six months ended June 30, 2016 were $48,000, or 0.02%, of average loans on an annualized basis, compared to $115,000, or 0.05% of average loans on an annualized basis for the same period in 2015. The decrease in net charge-offs was primarily due to improving economic conditions in our market area and continued efforts in credit administration. As of June 30, 2016, the allowance for loan losses as a percentage of total loans receivable and nonperforming loans was 1.04% and 107.94%, respectively, compared to 1.01% and 217.65%, respectively, at December 31, 2015. The allowance for loan losses as a percentage of nonperforming loans decreased due to a $2.3 million increase in nonperforming loans to $4.5 million at June 30, 2016 from $2.1 million at December 31, 2015. This decrease was primarily due to the transfer of a $2.3 million multifamily loan in Port Angeles, WA to nonaccrual status during the six months ended June 30, 2016 as discussed above.

Deposits. Total deposits increased $3.8 million, or 0.9%, to $443.9 million at June 30, 2016 from $440.0 million at December 31, 2015, primarily as a result of a $3.0 million, or 2.3%, increase in interest-bearing demand accounts, an $8.5 million, or 17.8% increase in noninterest-bearing demand accounts, and a $1.7 million, or 4.3%, increase in savings accounts. These increases were partially offset by a $1.1 million, or 2.1%, decrease in money market accounts and an $8.3 million, or 4.9%, decrease in certificates of deposit. The increases were the result of retail sales efforts during the period as we continued our emphasis on attracting low-cost core deposit accounts. The decrease in money market accounts was primarily the result of some customers shifting these funds into interest-bearing demand accounts. The decrease in certificate of deposit accounts was primarily due to a decrease in public funds.

A summary of deposit accounts with the corresponding weighted average cost of funds is presented below (dollars in thousands):

	As of June 30, 2016			As of December 31, 2015		
	Amount	Wtd. Avg. Rate		Amount	Wtd. Avg. Rate	
Noninterest-bearing demand	$56,621	0.00	%	$ 48,067	0.00	%
Interest-bearing demand	130,379	0.42		127,392	0.42	
Savings	40,486	0.21		38,833	0.18	
Money market	52,919	0.20		54,046	0.16	
Certificates	160,539	1.13	[1]	168,880	1.22	[1]
Escrow	2,923	0.00		2,806	0.00	
Total deposits	$443,867	0.55	[1]	$ 440,024	0.63	[1]

[1] Includes the amortization expense from the deposit premium paid on the purchase of deposits from Columbia State Bank in the third quarter of 2015.

Borrowings. FHLB advances decreased $4.8 million, or 11.9%, to $35.6 million at June 30, 2016, with a weighted-average cost of 0.55%, from $40.4 million at December 31, 2015, with a weighted-average cost of 0.39%. The increase in average borrowing rate was due to a greater percentage of short term borrowings in the current period compared to December 31, 2015, as well as an increase to the overnight borrowing rate with the FHLB. We rely on FHLB advances to fund interest-earning assets when deposits alone cannot fully fund interest-earning asset growth. This reliance on borrowings, rather than deposits, may increase our overall cost of funds.

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Stockholders' Equity. Total stockholders' equity increased $2.3 million, or 4.2%, to $56.8 million at June 30, 2016 from $54.5 million at December 31, 2015. This increase primarily reflects $2.4 million in net income for the six months ended June 30, 2016, partially offset by the payment of cash dividends of $372,000 to common stockholders.

Comparison of Results of Operation for the Three and Six Months Ended June 30, 2016 and 2015

General. Net income was $1.3 million, or $0.49 per diluted common share, for the three months ended June 30, 2016, an increase of $7,000 from the three months ended June 30, 2015. The primary reasons for the increase in net income during the three months ended June 30, 2016 compared to the same period last year was an increase in net interest income, which was partially offset by an increase in noninterest expense and decrease in the fair value adjustment on mortgage servicing rights. Net income decreased $95,000 to $2.4 million, or $0.92 per diluted common share, for the six months ended June 30, 2016, compared to $2.5 million, or $0.94 per diluted common share, for the six months ended June 30, 2015. The primary reasons for the decrease in net income during the six months ended June 30, 2016 compared to the same period last year was an increase in noninterest expense, and decreases to the fair value adjustment on mortgage servicing rights and gain on sale of loans. These decreases were partially offset by higher net interest income and a lower provision for loan losses.

Interest Income. Interest income increased $733,000, or 13.5%, to $6.1 million for the three months ended June 30, 2016, from $5.4 million for the three months ended June 30, 2015. Interest income increased $1.4 million, or 13.0%, to $12.2 million for the six months ended June 30, 2016, from $10.8 million for the six months ended June 30, 2015. The increases in interest income for the three and six months ended June 30, 2016, primarily reflect the increase in the average balance of interest-earning assets and a higher weighted average yield on earning assets in the current period.

Our weighted average yield on interest-earning assets was 4.78% for both the three and six months ended June 30, 2016, compared to 4.70% for both the three and six months ended June 30, 2015. The weighted average yield on loans increased to 5.17% for both the three and six months ended June 30, 2016, from 5.01% and 4.97% for the three and six months ended June 30, 2015, respectively. The weighted average yield on available-for-sale securities (including OTTI) was 0.83% for both the three and six months ended June 30, 2016, compared to 0.62% and 0.70% for the three and six months ended June 30, 2015, respectively. The increase in the average yields for both the interest bearing cash and the securities portfolio was due to the increase in the federal funds rate in December 2015 from 0.25% to 0.50%.

Interest Expense. Interest expense increased $29,000, or 4.3%, to $709,000 for the three months ended June 30, 2016, from $680,000 for the three months ended June 30, 2015. Interest expense increased $57,000, or 4.2%, to $1.43 million for the six months ended June 30, 2016, from $1.37 million for the six months ended June 30, 2015. We also had a $15.1 million and a $19.7 million increase in the average balances of FHLB advances for the three and six months ended June 30, 2016, respectively, compared to the same period ended June 30, 2015. Our weighted average cost of interest-bearing liabilities was 0.66% and 0.68% for the three and six months ended June 30, 2016, respectively, compared to 0.70% and 0.71% for the three and six months ended June 30, 2015, respectively.

Interest expense on deposits decreased $7,000, or 1.1%, to $654,000 for the three months ended June 30, 2016, from $661,000 for the three months ended June 30, 2015. Interest expense on deposits increased $20,000, or 1.5%, to $1.3 million for the six months ended June 30, 2016, from $1.3 million for the six months ended June 30, 2015. These increases resulted from higher average balances of interest-bearing deposits outstanding in the period. Our weighted average cost of deposits during the three and six months ended June 30, 2016 was 0.59% and 0.60%, respectively, as compared to 0.63% and 0.64% during the three and six months ended June 30, 2015, respectively. The decrease in average rates during the three and six months ended June 30, 2016 was primarily a result of the re-pricing of matured certificates of deposit.

Interest expense on borrowings increased $36,000, or 189.5%, to $55,000 for the three months ended June 30, 2016, from $19,000 for the three months ended June 30, 2015. Interest expense on borrowings increased $37,000, or 78.7%, to $84,000 for the six months ended June 30, 2016, from $47,000 for the six months ended June 30, 2015. The increases were a result of an increase in our average cost of borrowings to 0.55% for both the three and six months ended June 30, 2016, as compared to 0.50% and 0.48% for the three and six months ended June 30, 2015, respectively, reflecting the December 2015 increase in the federal funds rate.

Net Interest Income. Net interest income increased $704,000 or 14.9%, to $5.4 million for the three months ended June 30, 2016, from $4.7 million for the three months ended June 30, 2015. Net interest income increased $1.3 million, or 14.2 %, to $10.8 million for the six months ended June 30, 2016, from $9.4 million for the six months ended June 30, 2015. The increase for three and six months ended June 30, 2016 resulted from increased interest income due to higher average loan balances. Our average yield on loans receivable increased during the three and six months ended June 30, 2016 as compared to the same periods last year as new loan originations are pricing higher than pay downs and paid loans. Our net interest margin was 4.26% for both the three and six months ended June 30, 2016, respectively, compared to 4.11% for both the three and six months ended June 30, 2015, respectively.

Provision for Loan Losses. We establish provisions for loan losses, which are charged to earnings, at a level required to reflect management's best estimate of the probable incurred credit losses in the loan portfolio. In evaluating the level of the allowance for loan losses, management considers historical loss experience, the types of loans and the amount of loans in the loan portfolio, adverse situations that may affect borrowers' ability to repay, estimated value of any underlying collateral, peer group data, prevailing economic conditions, and current factors. Large groups of smaller balance homogeneous loans, such as one-to four-family, small commercial and multifamily, home equity and consumer loans, are evaluated in the aggregate using historical loss factors adjusted for current economic conditions and other relevant data. Loans for which management has concerns about the borrowers' ability to repay, are evaluated individually, and specific loss allocations are provided for these loans when necessary.

Provision for loan losses totaled $100,000 and $250,000 during the three and six months ended June 30, 2016, respectively, compared to a provision of $200,000 and $300,000 during the three and six months ended June 30, 2015, respectively. The reduced provision primarily reflects a decline in loan charge-offs and lower historical loss ratios, which were partially offset by higher average loan balances and changes in the composition of our loan portfolio.

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For the three months ended June 30, 2016, the annualized percentage of net recoveries to average loans was 0.02%, compared to net charge-offs of 0.06% for the three months ended June 30, 2015. For the six months ended June 30, 2016, the annualized percentage of net charge-offs to average loans decreased to 0.02%, from 0.05% for the six months ended June 30, 2015.

The ratio of nonperforming loans to total loans increased to 0.96% at June 30, 2016 from 0.46% at June 30, 2015. This increase reflects the inclusion, as discussed above, of a $2.3 million multifamily loan in Port Angeles, WA as a nonaccrual loan as of June 30, 2016.

While we believe the estimates and assumptions used in our determination of the adequacy of the allowance are reasonable, there can be no assurance that such estimates and assumptions will not be proven incorrect in the future, or that the actual amount of future provisions will not exceed the amount of past provisions or that any increased provisions that may be required will not adversely impact our financial condition and results of operations. In addition, the determination of the amount of our allowance for loan losses is subject to review by bank regulators as part of the routine examination process, which may result in the adjustment of reserves based upon their judgment of information available to them at the time of their examination.

Noninterest Income. Noninterest income decreased $496,000, or 29.1%, to $1.2 million for the three months ended June 30, 2016, as compared to $1.7 million for the three months ended June 30, 2015 as reflected below (dollars in thousands):

	Three Months Ended June 30,		Amount	Percent
	2016	2015	Change	Change
Service charges and fee income	$ 652	$ 671	$ (19)	(2.8)%
Earnings on cash surrender value of BOLI	84	84	-	-
Mortgage servicing income	209	214	(5)	(2.3)
Fair value adjustment on mortgage servicing rights	(76)	347	(423)	(121.9)
Net gain on sale of loans	341	390	(49)	(12.6)
Total noninterest income	$ 1,210	$ 1,706	$ (496)	(29.1)%

The primary reason for the decrease in noninterest income during the three months ended June 30, 2016 compared to the same period last year was the change in the fair value adjustment on mortgage servicing rights. The decrease in gain on sale of loans was primarily reflective of lower volume of loans sold and secondarily lower average premiums on loans sold.

Noninterest income decreased $690,000, or 24.0%, to $2.2 million for the six months ended June 30, 2016, as compared to $2.9 million for the six months ended June 30, 2015 as reflected below (dollars in thousands):

	Six Months Ended June 30,		Amount	Percent
	2016	2015	Change	Change
Service charges and fee income	$ 1,245	$ 1,316	$ (71)	(5.4)%
Earnings on cash surrender value of BOLI	168	168	-	-
Mortgage servicing income	413	469	(56)	(11.9)
Fair value adjustment on mortgage servicing rights	(190)	169	(359)	(212.4)
Other-than-temporary impairment losses	-	(31)	31	nm
Net gain on sale of loans	551	786	(235)	(29.9)
Total noninterest income	$ 2,187	$ 2,877	$ (690)	(24.0)%

NM-not meaningful.

The primary reason for the decrease in noninterest income during the six months ended June 30, 2016 compared to the same period last year was the negative change in the fair value adjustment on the mortgage servicing rights and the decrease in gain on sale of loans. The change in the fair value adjustment on mortgage servicing rights was primarily a result of the duration on the underlying loans being projected to shorten due to lower interest rates and increased refinance activity. The decrease in gain on sale of loans was primarily reflective of a lower volume of loans sold as well as a lower average premium on loans sold. Mortgage servicing income and services charges and fee income also decreased during the six months ended June 30, 2016 compared to the same period the prior year. The decrease in service charges and fee income was due to lower loan origination fees. The decrease in mortgage servicing income was due to the turnover in the mortgage servicing portfolio and the rates associated with loans paid off and originated.

Noninterest Expense. Noninterest expense increased $257,000, or 5.8%, to $4.7 million during the three months ended June 30, 2016 as compared to $4.4 million during the three months ended June 30, 2016, as reflected below (dollars in thousands):

	Three Months Ended June 30,		Amount	Percent
	2016	2015	Change	Change
Salaries and benefits	$ 2,618	$ 2,205	$ 413	18.7 %
Operations	1,084	1,053	31	2.9
Regulatory assessments	125	230	(105)	(45.7)
Occupancy	380	448	(68)	(15.2)
Data processing	444	454	(10)	(2.2)
Losses and expenses on OREO and repossessed assets	6	10	(4)	(40.0)
Total noninterest expense	$ 4,657	$ 4,400	$ 257	5.8 %

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The increase in noninterest expense during the three months ended June 30, 2016 compared to the same period last year was primarily due to an increase in salaries and benefits expense and, to a lesser extent, an increase in operations expense. Salaries and benefits expense increased primarily due to an increase in full time equivalent employees during the current period compared to the same period last year. Operations expense increased due to higher depreciation, credit administration costs, and general administration expenses. These increases were partially offset by decreases in regulatory assessments, occupancy expense and data processing expense. Regulatory assessments decreased due, in part, to lower fees paid to the Washington State Department of Financial Institutions. Occupancy expense declined due to higher maintenance costs in the same period last year. Data processing expense decreased due to vendor management and contract renewals.

Noninterest expense increased $694,000, or 8.2%, to $9.1 million during the six months ended June 30, 2016 as compared to $8.4 million during the six months ended June 30, 2015, as reflected below (dollars in thousands):

	Six Months Ended June 30,		Amount	Percent
	2016	2015	Change	Change
Salaries and benefits	$ 5,181	$ 4,460	$ 721	16.2 %
Operations	2,056	1,957	99	5.1
Regulatory assessments	280	296	(16)	(5.4)
Occupancy	765	773	(8)	(1.0)
Data processing	830	856	(26)	(3.0)
Losses and expenses on OREO and repossessed assets	6	82	(76)	(92.7)
Total noninterest expense	$ 9,118	$ 8,424	$ 694	8.2 %

The increase in noninterest expense during the six months ended June 30, 2016 compared to the same period last year was primarily due to an increase in salaries and benefits expense and, to a lesser degree, operations expense. Salaries and benefits expense increased primarily due to an increase in full time equivalent employees during the period and higher medical benefit expense. Operations expense increased due to higher depreciation, credit administration and general administration expense. These increases were partially offset by decreases in losses and expenses on OREO and repossessed assets, data processing expenses and regulatory assessments. Losses and expenses on OREO and repossessed assets decreased primarily to lower levels of OREO and other repossessed assets during the six months ended June 30, 2016 as compared to the same period last year and improving values for real estate in the markets where we lend. Data processing decreased primarily due to the impact of vendor management and contract renewal negotiations. Regulatory assessments decreased, due in part, to lower fees paid to the Washington State Department of Financial Institutions.

The efficiency ratio for the quarter ended June 30, 2016 was 69.51%, compared to 68.21% for the quarter ended June 30, 2015 and was 69.88% for the six months ended June 30, 2016, compared to 67.36% for the six months ended June 30, 2015. The increase in the efficiency ratio was primarily due to higher salaries and benefits, operations expense and lower noninterest income, partially offset by higher net interest income.

Income Tax Expense. For the three and six months ended June 30, 2016, we incurred income tax expense of $633,000 and $1.2 million on our pre-tax income as compared to $589,000 and $1.1 million for the three and six months ended June 30, 2015, respectively. The effective tax rates for the three and six months ended June 30, 2016 were 33.6% and 34.0%, respectively. The effective tax rates for the three and six months ended June 30, 2015 were 32.1% and 31.3%, respectively.

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Liquidity

The Management Discussion and Analysis in Item 7 of the Company's 2015 Form 10-K contains an overview of Sound Financial Bancorp's and the Bank's liquidity management, sources of liquidity and cash flows. This discussion updates that disclosure for the six months ended June 30, 2016.

The Bank's primary sources of funds are deposits, principal and interest payments on loans and borrowings. While maturities and scheduled amortization of loans are a predictable source of funds, deposit flows and loan prepayments are greatly influenced by general interest rates, economic conditions and competition. The Bank's primary investing activity is loan originations. The Bank maintains liquidity levels it believes to be adequate to fund loan commitments, investment opportunities, deposit withdrawals and other financial commitments. At June 30, 2016, the Bank had $52.6 million in cash and investment securities available for sale and $687,000 in loans held for sale generally available for its cash needs. Also, based on existing collateral pledged, the Bank had the ability to borrow an additional $101.5 million in Federal Home Loan Bank advances, $27.4 million through the Federal Reserve's Discount Window, $9.0 million through a Fed Funds line at Zions Bank and $2.0 million through a Fed Funds line at Pacific Coast Banker's Bank. The Bank uses these sources of funds primarily to meet ongoing commitments, pay maturing deposits and fund withdrawals, and to fund loan commitments. At June 30, 2016, outstanding loan commitments, including unused lines and letters of credit totaled $66.7 million. Certificates of deposit scheduled to mature in one year or less at June 30, 2016, totaled $95.8 million. Based on our competitive pricing, we believe that a majority of maturing deposits will remain with the Bank.

Cash and cash equivalents decreased $3.1 million to $45.2 million as of June 30, 2016, from $48.3 million as of December 31, 2015. Net cash provided by operating activities was $4.2 million for the six months ended June 30, 2016. Net cash of $5.9 million was used in investing activities during the six months ended June 30, 2016 and consisted principally of investment purchase and loan originations, net of principal repayments. The $1.4 million of cash used by financing activities during the six months ended June 30, 2016 was primarily a result of a $3.8 million net increase in deposits offset by a $4.8 million decrease in FHLB advances.

As a separate legal entity from the Bank, Sound Financial Bancorp must provide for its own liquidity. At June 30, 2016, Sound Financial Bancorp, on an unconsolidated basis, had $468,000 in cash, noninterest-bearing deposits and liquid investments generally available for its cash needs. Sound Financial Bancorp's principal source of liquidity is dividends from the Bank.

Except as set forth above, management is not aware of any trends, events, or uncertainties that will have, or that are reasonably likely to have a material impact on liquidity, capital resources or operations.

Off-Balance Sheet Activities

In the normal course of operations, we engage in a variety of financial transactions that are not recorded in our financial statements. These transactions involve varying degrees of off-balance sheet credit, interest rate and liquidity risks. These transactions are used primarily to manage customers' requests for funding and take the form of loan commitments and lines of credit. For the six months ended June 30, 2016, we engaged in no off-balance sheet transactions likely to have a material effect on our financial condition, results of operations or cash flows.

A summary of our off-balance sheet loan commitments at June 30, 2016, is as follows (in thousands):

Off-balance sheet loan commitments:	At June 30, 2016
Residential mortgage commitments	$7,918

Undisbursed portion of loans originated	34,011
Unused lines of credit	24,624
Irrevocable letters of credit	185
Total loan commitments	$66,738

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Capital

Sound Community Bank is subject to minimum capital requirements imposed by regulations of the FDIC. Effective January 1, 2015 (with some changes transitioned into full effectiveness over two to four years), the Bank became subject to new minimum capital adequacy adopted by the FDIC, which creates a new required ratio for common equity Tier 1 ("CET1") capital, increases the leverage and Tier 1 capital ratios, changes the risk-weightings of certain assets for purposes of the risk-based capital ratios, creates an additional capital conservation buffer over the required capital ratios and changes what qualifies as capital for purposes of meeting these various capital requirements. Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary actions by bank regulators that, if undertaken, could have a direct material effect on the Company's financial statements. The Bank is also required to maintain additional levels of CET1 over the minimum risk-based capital levels before it may pay dividends, repurchase shares or pay discretionary bonuses.

The new minimum requirements are a ratio of CET1 to total risk-weighted assets ("CET1 risk-based ratio") of 4.5%, a Tier 1 capital ratio of 6.0%, a total capital ratio of 8.0%, and a leverage ratio of 4.0%.

In addition to the capital requirements, there are a number of changes in what constitutes regulatory capital, subject to a certain transition periods. These changes include the phasing-out of certain instruments as qualifying capital. The Bank does not have any of these instruments. Mortgage servicing and deferred tax assets over designated percentages of CET1 are be deducted from capital, subject to a transition period ending December 31, 2017. CET1 consists of Tier 1 capital less all capital components that are not considered common equity. In addition, Tier 1 capital includes accumulated other comprehensive income, which includes all unrealized gains and losses on available for sale debt and equity securities, subject to a transition period end December 31, 2017. Because of our asset size, we are not are considered an "advanced approaches banking organization" and have elected to permanently opt-out of the inclusion of unrealized gains and losses on available for sale debt and equity securities in our capital calculations.

The new requirements also include changes in the risk-weighting of assets to better reflect credit risk and other risk exposure. These include a 150% risk weight (up from 100%) for certain high volatility commercial real estate acquisition, development and construction loans and for non-residential mortgage loans that are 90 days past due or otherwise in nonaccrual status; a 20% (up from 0%) credit conversion factor for the unused portion of a commitment with an original maturity of one year or less that is not unconditionally cancellable (currently set at 0%); and a 250% risk weight (up from 100%) for mortgage servicing and deferred tax assets that are not deducted from capital.

In addition to the minimum CET1, Tier 1 and total capital ratios, the Bank will be required to maintain a capital conservation buffer consisting of additional CET1 capital equal to 2.5% of risk-weighted assets above the required minimum levels in order to avoid limitations on paying dividends, engaging in share repurchases, and paying discretionary bonuses based on percentages of eligible retained income that could be utilized for such actions. This new capital conservation buffer requirement began to be phased in beginning in January 2016 at 0.625% of risk-weighted assets and will increase each year until fully implemented in January 2019.

Under the new standards, in order to be considered well-capitalized, the Bank must have to have a CET1 risk-based ratio of 6.5% (new), a Tier 1 risk-based ratio of 8% (increased from 6%), a total risk-based capital ratio of 10% (unchanged) and a leverage ratio of 5% (unchanged).

Based on its capital levels at June 30, 2016, Sound Community Bank exceeded these requirements as of that date. Consistent with our goals to operate a sound and profitable organization, our policy is to maintain a "well-capitalized" status as Sound Community Bank under the regulatory capital categories of the FDIC. Based on capital levels at June 30, 2016, Sound Community Bank was considered to be well-capitalized under applicable regulatory requirements. Management monitors the capital levels to provide for current and future business opportunities and to maintain Sound Community Bank's "well-capitalized" status.

The actual regulatory capital amounts and ratios calculated for Sound Community Bank at June 30, 2016 were as follows (dollars in thousands):

	Actual		For Capital Adequacy Purposes		To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of June 30, 2016						
Tier 1 Capital to average assets	$55,239	10.14%	$ 21,801	>4.0 %	$ 27,252	>5.0 %
Common Equity Tier 1 risk-based capital ratio	$55,239	12.80%	$ 19,424	> 4.5 %	$ 28,057	>6.5 %
Tier 1 Capital to risk-weighted assets	$55,239	12.80%	$ 25,899	>6.0 %	$ 34,532	>8.0 %
Total Capital to risk-weighted assets	$60,232	13.95%	$ 34,532	>8.0 %	$ 43,165	>10.00 %

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For a bank holding company with less than $1.0 billion in assets, the capital guidelines apply on a bank only basis and the Federal Reserve expects the holding company's subsidiary banks to be well capitalized under the prompt corrective action regulations. If Sound Financial Bancorp was subject to regulatory guidelines for bank holding companies with $1.0 billion or more in assets, at June 30, 2016 Sound Financial Bancorp would have exceeded all regulatory capital requirements. The estimated regulatory capital ratios calculated for Sound Financial Bancorp as of June 30, 2016 were 10.32% for Tier 1 leverage-based capital, 13.03% for both Common Equity Tier 1 risk-based capital, Tier 1 Capital to risk-based assets and 14.19% for total risk-based capital.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

The Company provided information about market risk in Item 7A of its 2015 Form 10-K. There have been no material changes in our market risk since our 2015 Form 10-K.

Item 4. Controls and Procedures

(a) Evaluation of Disclosure Controls and Procedures.

An evaluation of the Company's disclosure controls and procedures (as defined in Rule 13a -15(e) under the Securities Exchange Act of 1934 (the "Act")), as of June 30, 2016, was carried out under the supervision and with the participation of the Company's Chief Executive Officer, Chief Financial Officer and several other members of the Company's senior management. The Chief Executive Officer and Chief Financial Officer concluded that, as of June 30, 2016, the Company's disclosure controls and procedures were effective in ensuring that the information required to be disclosed by the Company in the reports it files or submits under the Act is: (i) accumulated and communicated to the Company's management (including the Chief Executive Officer and the Chief Financial Officer) in a timely manner, and (ii) recorded, processed, summarized and reported within the time periods specified in the SEC’s rules and forms.

We intend to continually review and evaluate the design and effectiveness of the Company’s disclosure controls and procedures and to improve the Company’s controls and procedures over time and to correct any deficiencies that we may discover in the future. The goal is to ensure that senior management has timely access to all material financial and non-financial information concerning the Company's business. While we believe the present design of the disclosure controls and procedures is effective to achieve this goal, future events affecting our business may cause the Company to modify its disclosure controls and procedures.

The Company does not expect that its disclosure controls and procedures will prevent all error and all fraud. A control procedure, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control procedure are met. Because of the inherent limitations in all control procedures, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the control. The design of any control procedure is also based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions; over time, controls may become inadequate because of changes in conditions, or the degree of compliance with the policies and procedures may deteriorate. Because of the inherent limitations in a cost-effective control procedure, misstatements due to error or fraud may occur and not be detected.

(b) Changes in Internal Control over Financial Reporting.

There were no changes in our internal control over financial reporting (as defined in Rule 13a - 15(f) under the Act) that occurred during the three months ended June 30, 2016, that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

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PART II OTHER INFORMATION

Item 1 Legal Proceedings

In the normal course of business, the Company occasionally becomes involved in various legal proceedings. In the opinion of management, any liability from such proceedings would not have a material adverse effect on the business or financial condition of the Company.

Item 1A Risk Factors

Not required; the Company is a smaller reporting company.

Item 2 Unregistered Sales of Equity Securities and use of Proceeds

Nothing to report

Item 3 Defaults Upon Senior Securities

Nothing to report.

Item 4 Mine Safety Disclosures

Not Applicable

Item 5. Other Information

Nothing to report.

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EXHIBIT INDEX

Exhibits:

3.1	Articles of Incorporation of Sound Financial Bancorp, Inc. (incorporated herein by reference to the Registration Statement on Form S-1 filed with the SEC on March 27, 2012 (File No. 333-180385))
3.2	Bylaws of Sound Financial Bancorp, Inc. (incorporated herein by reference to the Registration Statement on Form S-1 filed with the SEC on March 27, 2012 (File No. 333-180385))
4.0	Form of Common Stock Certificate of Sound Financial Bancorp, Inc. (incorporated herein by reference to the Registration Statement on Form S-1 filed with the SEC on March 27, 2012 (File No. 333-180385))
10.1	Employment Agreement by and between Sound Community Bank and Laura Lee Stewart (incorporated herein by reference to the Registration Statement on Form SB-2 filed with the SEC on September 20, 2007 (File No. 333-146196))
10.2	Amended and Restated Supplemental Executive Retirement Agreement by and between Sound Community Bank and Laura Lee Stewart (incorporated herein by reference to the Current Report on Form 8-K filed with the SEC on November 27, 2015 (File No. 001-35633))
10.3	Amended and Restated Long Term Compensation Agreement by and between Sound Community Bank and Laura Lee Stewart (incorporated herein by reference to the Current Report on Form 8-K filed with the SEC on November 27, 2015 (File No. 001-35633))
10.4	Amended and Restated Confidentiality, Non-Competition and Non-Solicitation Agreement by and between Sound Community Bank and Laura Lee Stewart (incorporated herein by reference to the Current Report on Form 8-K filed with the SEC on November 27, 2015 (File No. 001-35633))
10.5	2008 Equity Incentive Plan (incorporated herein by reference to the Annual Report on Form 10-K filed with the SEC on March 31, 2009 (File No. 000-52889))
10.6	Forms of Incentive Stock Option Agreement, Non-Qualified Stock Option Agreement and Restricted Stock Agreements under the 2008 Equity Incentive Plan (incorporated herein by reference to the Current Report on Form 8-K filed with the SEC on January 29, 2009 (File No. 000-52889))
10.7	Summary of Annual Bonus Plan (incorporated herein by reference to the Registration Statement on Form SB-2 filed with the SEC on September 20, 2007 (File No. 333-146196))
10.8	2013 Equity Inventive Plan (included as Exhibit 10.13 to the Registrant’s Quarterly Report on Form 10-Q for the quarter ended September 30,2013 and incorporated herein by reference (File No. 001-35633))
10.9	Form of Incentive Stock Option Agreement, Non-Qualified Stock Option Agreement and Restricted Stock Agreement under the 2013 Equity Incentive Plan (included as Exhibit 10.14 to the Registrant’s Quarterly Report on Form 10-Q for the quarter ended September 30, 2013 and incorporated herein by reference (File No. 001-35633))
10.10	Amended and Restated Change of Control Agreement dated June 21, 2016, by and among Sound Financial Bancorp, Inc., Sound Community Bank and Matthew P. Deines (incorporated herein by reference to the Current Report on Form 8-K filed with the SEC on June 24, 2016 (File No. 001-35633))
10.10	Form of Separation Agreement and Release of All Claims dated May 11, 2016, by and among Sound Financial Bancorp, Inc., Sound Community Bank and Kelli Nielson (incorporated herein by reference to the Current Report on Form 8-K filed with the SEC on May 16, 2016 (File No. 001-35633))
11	Statement re computation of per share earnings (See Note 9 of the Notes to Condensed Consolidated Financial Statements contained in Item 1, Part I of this Current Report on Form 10-Q.)
31.1	Rule 13(a)-14(a) Certification (Chief Executive Officer)

31.2	Rule 13(a)-14(a) Certification (Chief Financial Officer)
32	Section 1350 Certification
101	Interactive Data Files

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Sound Financial Bancorp, Inc.

Date: August 12, 2016 By: /s/ Laura Lee Stewart
Laura Lee Stewart
President and Chief Executive Officer

Date: August 12, 2016 By: /s/ Matthew P. Deines
Matthew P. Deines
Executive Vice President and Chief Financial Officer