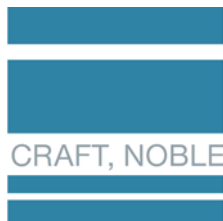


FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.
BEREA, KENTUCKY

* * * * *

AUDITED FINANCIAL STATEMENTS AND
INDEPENDENT AUDITORS' REPORT
FOR THE YEARS ENDED
JUNE 30, 2009 AND 2008



CRAFT, NOBLE & COMPANY
PLLC

Certified Public Accountants
Post Office Box 827
Richmond, KY 40476
www.craftnoble.com

TABLE OF CONTENTS

| | PAGE |
|---|---------|
| INDEPENDENT AUDITORS' REPORT | 1 |
| FINANCIAL STATEMENTS | |
| Statements of Financial Position | 2 |
| Statements of Activities | 3 |
| Statements of Cash Flows | 4 |
| Notes to Financial Statements | 5 - 14 |
| SUPPLEMENTAL INFORMATION | |
| Schedule of Expenditures of Federal Awards | 15 |
| Notes to Schedule of Expenditures of Federal Awards | 16 |
| Report on Compliance and on Internal Control Over Financial Reporting Based on an Audit of Financial Statements Performed in Accordance with <i>Government Auditing Standards</i> | 17 - 18 |
| Report on Compliance with Requirements Applicable to Each Major Program and Internal Control Over Compliance in Accordance With OMB Circular A-133 | 19 - 20 |
| Schedule of Findings and Questioned costs | 21 |
| Statements of Functional Expenses | 22 - 23 |
| Statement of Financial Position - Neighborworks America Capital Fund | 24 |
| Statement of Activities - Neighborworks America Capital Fund | 25 |
| Computation of Adjusted Net Worth for Approval of Non-Supervised Mortgagees Other Than Loan Correspondents | 26 |
| Computation of Adjusted Net Worth for Approval and Recertification of Non-Supervised Mortgagees other Than Loan Correspondents | 27 |
| Computation of Adjusted Net Worth for Approval and Recertification of Non-Supervised Mortgagees Other Than Loan Correspondents | 28 |
| Report on Compliance with Specific Requirements Applicable to Non-Major HUD Program Transactions | 29 |

INDEPENDENT AUDITORS' REPORT

To the Board of Directors
Federation of Appalachian Housing Enterprises, Inc.
Berea, Kentucky

We have audited the accompanying statements of financial position of Federation of Appalachian Housing Enterprises, Inc. (a non-profit organization) as of June 30, 2009 and 2008, and the related statements of activities, changes in net assets, and cash flows for the years then ended. These financial statements are the responsibility of the Organization's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Federation of Appalachian Housing Enterprises, Inc., as of June 30, 2009 and 2008, and the changes in its net assets and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated September 15, 2009, on our consideration of Federation of Appalachian Housing Enterprises, Inc.'s internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grants agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and important for assessing the results of our audit.

Our audit was performed for the purpose of forming an opinion on the basic financial statements of Federation of Appalachian Housing Enterprises, Inc. taken as a whole. The schedules of functional expenses on pages 22 and 23, the statement of financial position – Neighborworks America Capital Fund on page 24, and the statement of activities – Neighborworks America Capital Fund on page 25, the computation of Adjusted Net Worth for Approval of Other than Loan Correspondents on page 26, the Computation of Adjusted Net Worth for Approval and Recertification of Non-Supervised Mortgagees Other than Loan Correspondents on pages 27 and 28, and the Report on Compliance with Specific Requirements Applicable to Non-Major HUD Program Transactions are presented for purposes of additional analysis and are not a required part of the basic financial statements. The accompanying schedule of expenditures of federal awards on page 14 is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, "Audits of States, Local Governments, and Non-Profit Organizations," and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

Craft, Noble & Company, PLLC

Craft, Noble & Company, PLLC
September 15, 2009

CRAFT, NOBLE & COMPANY
PLLC

Certified Public Accountants
Post Office Box 827
Richmond, KY 40476
www.craftnoble.com

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.
STATEMENT OF FINANCIAL POSITION
JUNE 30, 2009 AND 2008

| | 2009 | | | 2008 | | | |
|---|----------------------|------------------------|------------------------|----------------------|------------------------|------------------------|----------------------|
| | Unrestricted | Temporarily Restricted | Permanently Restricted | Unrestricted | Temporarily Restricted | Permanently Restricted | Total |
| Assets | | | | | | | |
| Cash and cash equivalents | \$ 2,986,814 | \$ 1,419,477 | \$ - | \$ 1,293,823 | \$ 1,185,063 | \$ - | 2,478,886 |
| Accounts receivable | 217,531 | 40,300 | - | 859,377 | - | - | 859,377 |
| Grants receivable | 2,100,000 | - | - | 225,000 | - | - | 225,000 |
| Accrued interest receivable | 231,044 | 5,122 | - | 225,759 | 7,320 | - | 233,079 |
| Deposits | 153,120 | - | - | 2,735 | - | - | 2,735 |
| Prepaid expenses | 61,466 | - | - | 41,981 | - | - | 41,981 |
| Property and equipment, net | 285,724 | - | - | 320,139 | - | - | 320,139 |
| Interfund balances | (219,945) | 38,823 | 181,122 | (228,070) | (18,250) | 246,320 | - |
| Mortgage notes receivable, net | 12,500,888 | 9,424,578 | - | 13,616,678 | 9,533,702 | - | 23,150,380 |
| Notes receivable, net | 10,343,032 | 646,791 | - | 10,448,297 | 418,213 | - | 10,866,510 |
| Property held for sale | 743,686 | 111,255 | - | 670,592 | 184,033 | - | 854,625 |
| Deferred compensation | 4,750 | - | - | - | - | - | - |
| Total Assets | <u>\$ 29,408,110</u> | <u>\$ 11,686,346</u> | <u>\$ 181,122</u> | <u>\$ 27,476,311</u> | <u>\$ 11,310,081</u> | <u>\$ 246,320</u> | <u>\$ 39,032,712</u> |
| Liabilities and Net Assets | | | | | | | |
| Liabilities | | | | | | | |
| Accounts payable | \$ 37,262 | \$ - | \$ - | \$ 45,062 | \$ - | \$ - | \$ 45,062 |
| Payroll taxes payable | 22,254 | - | - | - | - | - | - |
| Client advances and deposits | 245,959 | 314,957 | - | 165,891 | 138,674 | - | 304,565 |
| Accrued interest payable | 64,320 | 4,521 | - | 48,425 | 5,300 | - | 53,725 |
| Compensated absences payable | 143,185 | 500 | - | 68,012 | - | - | 68,012 |
| Deferred revenue | 321,794 | - | - | 145,512 | - | - | 145,512 |
| Notes payable | 18,865,858 | 639,593 | - | 18,814,393 | 646,939 | - | 19,461,332 |
| Deferred compensation | 4,750 | - | - | - | - | - | - |
| Total Liabilities | <u>19,705,382</u> | <u>959,571</u> | <u>-</u> | <u>19,287,295</u> | <u>790,913</u> | <u>-</u> | <u>20,078,208</u> |
| Other Liabilities | | | | | | | |
| Equity equivalent | 2,000,000 | - | - | 2,000,000 | - | - | 2,000,000 |
| Total Liabilities | <u>21,705,382</u> | <u>959,571</u> | <u>-</u> | <u>21,287,295</u> | <u>790,913</u> | <u>-</u> | <u>22,078,208</u> |
| Net Assets | | | | | | | |
| Net assets | 7,102,728 | 10,726,775 | 181,122 | 5,589,016 | 10,519,168 | 246,320 | 16,354,504 |
| Net assets, board restricted | 600,000 | - | - | 600,000 | - | - | 600,000 |
| Total Net Assets | <u>7,702,728</u> | <u>10,726,775</u> | <u>181,122</u> | <u>6,189,016</u> | <u>10,519,168</u> | <u>246,320</u> | <u>16,954,504</u> |
| Total Liabilities and Net Assets | <u>\$ 29,408,110</u> | <u>\$ 11,686,346</u> | <u>\$ 181,122</u> | <u>\$ 27,476,311</u> | <u>\$ 11,310,081</u> | <u>\$ 246,320</u> | <u>\$ 39,032,712</u> |

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

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.
STATEMENTS OF ACTIVITIES
YEARS ENDING JUNE 30, 2009 AND 2008

| | 2009 | | | 2008 | | | | |
|--|------------------|------------------------|------------------------|----------------------|------------------|------------------------|------------------------|----------------------|
| | Unrestricted | Temporarily Restricted | Permanently Restricted | Total | Unrestricted | Temporarily Restricted | Permanently Restricted | Total |
| Revenue | | | | | | | | |
| Mortgage and note interest | \$ 1,005,159 | \$ 59,708 | \$ - | 1,064,867 | \$ 920,858 | \$ 69,699 | \$ - | 990,557 |
| Contributions, grants | 240,500 | - | - | 240,500 | 540,500 | - | - | 540,500 |
| State grants | 328,784 | - | - | 328,784 | 114,917 | 97,870 | - | 212,787 |
| Pass-through grants | 648,328 | - | - | 648,328 | 923,556 | - | - | 923,556 |
| Federal grants | 2,125,500 | 192,000 | - | 2,317,500 | 155,700 | - | 246,320 | 402,020 |
| Rental income | 200 | 1,000 | - | 1,200 | 3,905 | 5,550 | - | 9,455 |
| Investment income | 27,219 | 13,154 | - | 40,373 | 85,498 | 33,042 | - | 118,540 |
| Administration income | 43,154 | - | - | 43,154 | 91,300 | - | - | 91,300 |
| Gain on Acquisition of Assets | 246,878 | - | - | 246,878 | - | - | - | - |
| Gain/(Loss) on Sale of Property | 5,422 | 5,664 | - | 11,086 | 2,200 | (16,816) | - | (14,616) |
| Fees and service charges | 608,888 | 1,207 | - | 610,095 | 1,013,126 | 1,846 | - | 1,014,972 |
| Miscellaneous income | 99 | - | - | 99 | 4,043 | - | - | 4,043 |
| Net assets released from restrictions | | | | | | | | |
| Satisfaction of program restrictions | 130,324 | (65,126) | (65,198) | - | 99,558 | (99,558) | - | - |
| Total Revenue | 5,410,455 | 207,607 | (65,198) | 5,552,864 | 3,955,161 | 91,633 | 246,320 | 4,293,114 |
| Expenses | | | | | | | | |
| Program services | 2,240,627 | - | - | 2,240,627 | 2,189,705 | - | - | 2,189,705 |
| General and administrative | 1,266,441 | - | - | 1,266,441 | 1,237,660 | - | - | 1,237,660 |
| Fundraising | 251,665 | - | - | 251,665 | 134,873 | - | - | 134,873 |
| Membership | 138,010 | - | - | 138,010 | 245,945 | - | - | 245,945 |
| Total Expenses | 3,896,743 | - | - | 3,896,743 | 3,808,183 | - | - | 3,808,183 |
| Excess of Revenue Over Expenses | 1,513,712 | 207,607 | (65,198) | 1,656,121 | 146,978 | 91,633 | 246,320 | 484,931 |
| Increase in Net Assets | | | | 1,656,121 | | | | 484,931 |
| Net Assets at Beginning of Period | | | | 16,954,504 | | | | 16,469,573 |
| Net Assets End of Period | | | | <u>\$ 18,610,625</u> | | | | <u>\$ 16,954,504</u> |

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

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDING JUNE 30, 2009 AND 2008

| | <u>2009</u> | <u>2008</u> |
|--|---------------------|---------------------|
| CASH FLOWS FROM OPERATING ACTIVITIES | | |
| Changes in Net Assets | \$ 1,656,121 | \$ 484,931 |
| Adjustments to reconcile increase in net assets to net cash provided by operating activities | | |
| Depreciation and amortization | 58,482 | 44,565 |
| (Gain)/Loss on disposal of assets | (26,743) | (18,788) |
| (Increase) decrease in operating assets | | |
| Accounts receivable | 601,546 | (806,831) |
| Grants receivable | (1,875,000) | (125,000) |
| Accrued interest receivable | (3,087) | (130,754) |
| Prepaid expenses | (19,485) | (8,908) |
| Deferred Compensation | (4,750) | - |
| Deposits | (150,385) | (2,035) |
| Increase (decrease) in operating liabilities | | |
| Accounts payable | (7,800) | (10,416) |
| Payroll taxes payable | 22,254 | (9,233) |
| Client advances and deposits | 256,350 | 45,051 |
| Accrued interest payable | 15,116 | 16,479 |
| Compensated absences payable | 75,674 | 29,223 |
| Deferred Revenue | 176,282 | 145,512 |
| Deferred Compensation | 4,750 | - |
| NET CASH PROVIDED BY OPERATING ACTIVITIES | <u>779,325</u> | <u>(346,204)</u> |
| CASH FLOWS FROM INVESTING ACTIVITIES | | |
| Purchase of property and equipment | (623,324) | (581,207) |
| Proceeds from sale of property and equipment | 598,942 | 599,077 |
| Payments received on notes receivable | 8,334,001 | 6,826,825 |
| Disbursement of loans receivable funds | (7,205,668) | (10,866,678) |
| NET CASH PROVIDED (USED) BY INVESTING ACTIVITIES | <u>1,103,951</u> | <u>(4,021,983)</u> |
| CASH FLOWS FROM FINANCING ACTIVITIES | | |
| Proceeds from long-term debt borrowings | 1,290,494 | 3,397,365 |
| Payments on long-term debt | (1,246,375) | (1,557,093) |
| NET CASH PROVIDED BY FINANCING ACTIVITIES | <u>44,119</u> | <u>1,840,272</u> |
| NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS | 1,927,395 | (2,527,915) |
| CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR | <u>2,478,886</u> | <u>5,006,801</u> |
| CASH AND CASH EQUIVALENTS AT END OF YEAR | <u>\$ 4,406,281</u> | <u>\$ 2,478,886</u> |
| Supplemental Information | | |
| Interest paid | <u>\$ 558,957</u> | <u>\$ 559,657</u> |

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

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2009 AND 2008

Note 1 – Organization

Federation of Appalachian Housing Enterprises, Inc. (FAHE or the Organization) is a non-profit, membership organization formed by a collaborative of non-profits in Central Appalachia in 1981. FAHE was created to provide a unified voice for the cause of eliminating sub-standard housing conditions that are so prevalent in the Central Appalachian region. FAHE currently has 46 members located throughout its service region of Kentucky, West Virginia, Virginia and Tennessee. Members include housing authorities, community housing developers, and community action agencies with a commitment to improving their local community by providing safe, decent and affordable housing options. FAHE's main office is located at 106 Pasco Street in Berea, Kentucky. In addition, FAHE has branch offices located in Elkins, West Virginia, Maryville, Tennessee and Morehead, Kentucky.

FAHE achieves its mission by leveraging State and Federal monies with private resources to provide creative financing products to its members to promote community development; administering Federal and State housing programs to provide low-interest mortgages to individuals through its member network; maintaining revolving loan portfolios from both private and public sources to provide sustainable, affordable mortgage and commercial financing; creating innovative mortgage servicing standards to encourage and promote long-term homeowner success; providing access to pass-through grant and loan resources for members to assist them in achieving their individual missions; providing specialized services to members, such as mortgage servicing or mortgage loan processing and underwriting, to allow them to focus their resources on mission critical programs; working directly with local governments and private organizations to promote community economic development and increased capacity and availability of public infrastructure; and by providing networking opportunities through various state caucuses and semi-annual membership meetings to create a public forum for advocacy on behalf of its members and their causes in both the private and public sectors.

FAHE works through three significant venues to assist achieving its mission. The first of these is FAHE Capital Corporation I, which was formed in fiscal year 2000. FAHE Capital, a wholly owned, subsidiary, limited liability company, was established to create, in partnership with other organizations, an equity fund to finance, develop and operate low-income housing tax credit (LIHTC) eligible development properties. Through the efforts of FAHE Capital and its partners, enough equity capital has been raised to develop several multi-million dollar LIHTC development projects throughout the state of Kentucky.

The second venue a wholly owned, subsidiary, limited liability company, FAHE Consulting, LLC, founded in fiscal year 2006 provides consulting services to municipalities and others through all stages of special projects development. In conjunction with FAHE and its members, FAHE Consulting assists with finding new projects, filing applications for funding or development approval, securing construction and permanent financing, facilitating and tracking construction progress and preparing any and all required project reports.

Last, FAHE developed a direct origination mortgage program in 2007. The program, JustChoice Lending, provides access directly for customers at the Berea, Elkins and Maryville locations, and through FAHE members for the individuals and families they serve, to conventional lending mortgage products. By offering traditional conventional mortgage products with lower overall closing costs, and combining them with subsidies and homeowner counseling not normally available through traditional mortgage brokers, FAHE is able to provide a more divergent population with affordable, sustainable, quality mortgage financing.

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2009 AND 2008

Note 2 – Summary of Significant Accounting Policies

Principles of Combination

The financial statements include the combined statements of the Organization and its subsidiaries, FAHE Capital Corporation I, and FAHE Consulting, LLC. Accordingly, all significant inter-company balances and transactions have been eliminated.

Basis of Accounting

The accompanying financial statements have been prepared on the accrual basis of accounting in accordance with generally accepted accounting principles. Net assets and revenues, expenses, gains, and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, net assets of the Organization and changes therein are classified and reported as follows:

- Unrestricted net assets – Net assets that are not subject to donor-imposed stipulations.
- Temporarily restricted net assets – Net assets subject to donor-imposed stipulations that may or will be met, either by actions of the Organization and/or the passage of time. When a restriction expires, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the Statement of Activities as net assets released from restriction.
- Permanently restricted net assets – Net assets subject to donor-imposed stipulations that they be maintained permanently by the Organization. Generally, the donors of these assets permit the Organization to use all or part of the income earned on any related investments for general or specific purposes.

Cash and Cash Equivalents

For purposes of the Statement of Financial Position and the Statements of Cash Flows, the Organization considers all highly liquid investments with an initial maturity of three months or less to be cash equivalents unless held by investment managers as part of the investment portfolio.

FAHE maintains an \$800,000 compensating balance arrangement with Wachovia Bank against a \$4.5 million line of credit.

Investments

The organization carries investments in equity securities with readily determinable fair values and all investments in debt securities at their fair values in the Statement of Financial Position. Unrealized gains and losses are included in the change in net assets in the accompanying Statement of Activities.

Mortgage Notes Receivable

Mortgage notes receivable are stated at the outstanding principal balance, less an allowance for loan losses. The allowance for loan losses is increased by charges to the change in net assets and decreased by charge-offs (net of recoveries). Interest income on the notes is recognized at the stated rate in the promissory note net of an interest allowance given to the borrower by the Organization based upon the need of the individual.

Since the interest rate charged to the borrowers corresponds with the customary rates applicable to the low-income housing industry, the Organization considers these rates to be reasonable and has not made any adjustment for imputed interest that would be applicable to higher interest rate conventional housing loans.

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2009 AND 2008

Allowance for Loan Losses

It is the policy of the Organization to provide valuation allowances for estimated loan losses. The allowance for loan losses represents management's best estimate of future bad debts. Additions to the allowance are charged to earnings. Accounts written off are charged against the allowance. Recoveries are credited to the allowance reserve.

Fixed Assets

The Organization capitalizes all expenditures for fixed asset acquisitions in excess of \$500. Fixed assets are carried at cost or, if donated, at the approximate fair value at the date of donation. Depreciation is computed on a straight-line basis over the useful lives of the assets generally as follows:

| | | |
|---|----|-------|
| • Building and improvements | 39 | Years |
| • Computers and data handling equipment | 3 | Years |
| • Vehicles and equipment | 5 | Years |
| • Furniture and fixtures | 5 | Years |

During the year ended June 30, 2009 and 2008, depreciation expense was \$49,263 and \$42,855, respectively.

The Organization amortizes leasehold improvements over the shorter of the term of the lease or the economic life of the asset purchased. Improvements for the loan origination offices, beginning in May 08 were amortized over a period of 12 months, the term of the lease agreement. FAHE entered a lease for office space for FAHE Capital and FAHE Consulting in June 2009. These improvements are being amortized over the shorter of the term of the lease of one year.

Amortization expense for the year ended June 30, 2009 and 2008 was \$9,219 and \$1,710, respectively.

Revenue Recognition

Contributions received are recorded as increases in unrestricted, temporarily restricted, or permanently restricted net assets, depending on the existence and/or nature of any donor imposed restrictions. All donor-restricted contributions are reported as increases in temporarily or permanently restricted net assets, depending on the nature of the restriction. When a restriction expires (that is, when a stipulated time restriction ends or purpose restriction is satisfied), temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statements of activities as net assets released from restrictions.

Income Tax Status

The organization is recognized as a tax-exempt organization under code Section 501(c)(3) of the Internal Revenue Code. Accordingly, no provision for federal income tax has been made. In addition, the Organization has been classified as an Organization that is not a private foundation under Section 509(a).

The Organization has elected to defer implementation of FIN 48, Accounting for Uncertainty in Income Taxes, under guidance issued in FASB Staff Position FIN48-3. Additionally, the Organization is not aware of any uncertain tax positions that may affect the financial statements.

Compensated Absences

The Organization's employees earn vacation and sick time throughout the year based on job classification, length of service and other factors. The liability accrued for compensated absences is limited to the actual amount that would be payable to the employee in the event of separation from employment. The amount is calculated based on multiplying the representative hourly wage by the number of accrued hours.

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2009 AND 2008

Note 2-Summary of Significant Accounting Policies (Continued)

Estimates

Management uses estimates and assumptions in preparing financial statements. Those estimates and assumptions affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, and the reported revenues and expenses. Actual results could differ from those estimates.

Functional Allocation of Expenses

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

Note 3 – Grant Funds Receivable

Unconditional promises to give are expected to be realized in one year or less. Unconditional promises to give amounted to \$2,100,000 and \$225,000 at June 30, 2009 and 2008, respectively. The \$2,000,000 grant was received within forty-five days of year-end.

Note 4 – Property Held for Resale

Property held for resale consists of foreclosure properties (REO) and land held for sale for future development by various members (Investment Property). Investment property is recorded at actual cost with an allowance made to reflect the lower of cost or market. REO property is recorded at the lower of cost or market when recovered from the foreclosure proceedings or by a deed-in-lieu of foreclosure. Gains or losses from the sale of properties are recorded in the statement of activities as either gains or losses on disposal of property. At June 30, 2009 and 2008, the organization held \$348,104 and \$479,483, respectively in REO property and \$506,837 and \$375,142 respectively, in investment property.

Note 5 – Mortgage Notes Receivable

Loans are granted to low- and moderate-income residents of Central Appalachia for the purchase of new homes and the rehabilitation of existing homes. Mortgage lending funds are made available from several different sources. These sources include Federal and State grants awarded to the Organization, borrowings of lower interest funds made available by state housing agencies, grants from foundations, and revolved funds in the Organization's various lending portfolios. Loans are made in accordance with the restrictions imposed by the various funding sources.

Mortgage loans are secured by real estate. Interest rates vary from 0% to prevailing market rates. Terms range from five to 40 years, with some containing deferred and/or forgivable features.

At June 30, 2009 delinquencies were as follows: \$470,814 or 1.40% for 30-59 days; \$629,045 or 1.87% for 60-89 days; \$179,339 or 0.53% for loans 90+ days; \$352,787 or 1.05% for loans in foreclosure. Overall, loan delinquencies were \$1,279,197 or 3.80% on total loans of \$33,660,824 at June 30, 2009.

At June 30, 2008 delinquencies were as follows: \$202,327 or 0.59% for 30-59 days; \$22,504 or 0.07% for 60-89 days; \$352,965 or 1.03% for loans 90+ days; \$248,888 or 0.73% for loans in foreclosure; and \$182,898 or 0.54% for loans in bankruptcy. Overall, loan delinquencies were \$577,797 or 1.68% on total loans of \$34,397,371 at June 30, 2008.

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2009 AND 2008

Note 5 – Mortgage Notes Receivable (Continued)

Mortgage notes receivable as of June 30, 2009 consist of the following balances in each fund:

| | | |
|---|----|--------------------------|
| Kentucky Home Loan Fund | \$ | 3,712,280 |
| AHTF Fund | | 254,025 |
| HOME Program of Kentucky | | 7,331,796 |
| Virginia Home Loan Fund | | 5,364,312 |
| NHPR Kentucky | | 240,062 |
| HOME Program of Virginia | | 2,194,903 |
| West Virginia Home Loan Fund | | 1,900,337 |
| Tennessee Home Loan Fund | | <u>1,300,784</u> |
| Total | | \$ 22,298,499 |
| Less: Allowance for Loan Losses | | <u>(373,033)</u> |
| Mortgage Notes Receivable, Net of Allowance | \$ | <u><u>21,925,466</u></u> |

Mortgage notes receivable as of June 30, 2008 consist of the following balances in each fund:

| | | |
|---|----|--------------------------|
| Kentucky Home Loan Fund | \$ | 4,295,847 |
| AHTF Fund | | 260,766 |
| HOME Program of Kentucky | | 7,605,198 |
| Virginia Home Loan Fund | | 5,469,039 |
| NHPR Kentucky | | 248,449 |
| HOME Program of Virginia | | 2,071,302 |
| West Virginia Home Loan Fund | | 2,609,690 |
| Tennessee Home Loan Fund | | <u>1,113,619</u> |
| Total | | \$ 23,673,910 |
| Less: Allowance for Loan Losses | | <u>(523,530)</u> |
| Mortgage Notes Receivable, Net of Allowance | \$ | <u><u>23,150,380</u></u> |

The Organization has loan covenants with certain foundations that require the Organization to maintain certain levels of allowances to cover potential loan losses. In lieu of charging the full amount of the requirements to earnings, the Organization's Board of Directors has chosen to voluntarily designate a portion of its net assets for this purpose. The balance of the Board Designated Net Assets as of June 30, 2009, is \$600,000. This provides aggregate loan loss coverage of 4.0% on the FAHE loan portfolio. Based on actual, historical delinquency trends, the Organization's management does not expect to incur any charges against this designation.

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2009 AND 2008

Note 6 – Notes Receivable

The Organization makes loans to promote community development, to provide additional resources for operations, and to facilitate housing construction and financing to other non-profits and local housing authorities throughout Central Appalachia. Combined borrower balances of the Organization’s commercial loan portfolio as of June 30, 2009 and 2008 are presented below:

| | <u>2009</u> | <u>2008</u> |
|--|----------------------|----------------------|
| Appalachia Habitat For Humanity | \$ 170,412 | \$ 176,025 |
| Appalachia Service Project | 51,219 | 57,891 |
| Beattyville Housing Development | 136,847 | 100,894 |
| Beattyville School | 371,900 | - |
| Blueberry Hill Estates | 75,000 | 75,000 |
| Boodry Place, LLC | 138,945 | 1,329,613 |
| Cambria House | 41,492 | - |
| Clinch Valley Community | 106,575 | - |
| COAP | 461,947 | 488,140 |
| Community Housing Partners | 2,525,837 | 2,795,377 |
| Community Housing, Inc. | 605,383 | 444,609 |
| Cumberland Plateau | - | 1,010 |
| Eastern Eight CDC | 846,631 | 478,595 |
| Frontier Housing, Inc. | 944,855 | 1,048,780 |
| Giles County Housing & Development Corporation | - | 62,017 |
| Hazard/Perry County Community Ministries | 31,791 | 34,098 |
| Hazard/Perry County Housing Development Alliance | - | 373,544 |
| Homeownership Center | 112,250 | 112,250 |
| HOMES, Inc. | 947,865 | 726,313 |
| HOPE Inc. | 293,524 | - |
| Housing Development | 391,755 | - |
| Housing Equity Fund | 800,000 | - |
| Irvine Renaissance, LLP | 299,948 | 310,712 |
| KDVA Homes 07, LLP | 116,027 | 114,017 |
| Kentucky Mountain Housing Corporation | 529,448 | 536,563 |
| Lil' Britches Child Care Center | 70,119 | 72,794 |
| LINKS, Inc. | 57,200 | 12,348 |
| Mountain Cap, Inc. | 236,306 | 116,874 |
| Mountain Shelter, Inc. | - | 436,996 |
| Pearisburg Community Development Corporation | - | 57,387 |
| People Inc. Financial Services | 99,900 | 99,900 |
| Randolph County Housing Authority | 457,650 | 215,198 |
| Safe Housing & Economic Development | 229,786 | 237,710 |
| Sterling Housing, Inc. | 42,422 | 42,422 |
| Southern Appalachian | 98,477 | - |
| Virginia Community Development Fund | 5,000 | 559,079 |
| Woodlands Development | 66,712 | - |
| Total Notes Receivable | <u>11,363,223</u> | <u>11,116,156</u> |
| Less: Allowance for Loan Loss | (373,400) | (249,646) |
| Notes Receivable, Net of Allowance | <u>\$ 10,989,823</u> | <u>\$ 10,866,510</u> |

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2009 AND 2008

Note 7 – Notes Payable

Notes payable at June 30, 2009 and 2008 consists of notes payable to governmental agencies, banks, non-profit organizations and individuals as detailed below:

| | Rate | Term | Maturity | | Balance | |
|---|-------|----------|--------------------|----|-------------|-------------|
| | | | | | <u>2009</u> | <u>2008</u> |
| Kentucky Housing Corporation: | | | | | | |
| Kentucky Home Loan Fund/AHTF | | | | | | |
| Special Contract #1 | 1.00% | 20 Years | November 1, 2010 | \$ | 12,500 | \$ 22,500 |
| Special Contract #2 | 1.00% | 20 Years | January 01, 2012 | | 28,500 | 38,000 |
| Special Contract #3 | 1.00% | 20 Years | February 01, 2013 | | 55,600 | 69,500 |
| Special Contract #4 | 1.00% | 20 Years | July 1, 2013 | | 102,500 | 123,000 |
| Special Contract #5 | 1.00% | 20 Years | July 1, 2014 | | 123,000 | 143,500 |
| Special Contract #6 | 1.00% | 20 Years | July 1, 2015 | | 145,250 | 166,000 |
| Special Contract #7 | 1.00% | 20 Years | July 1, 2016 | | 168,025 | 189,028 |
| Special Contract #8 | 3.00% | 20 Years | October 1, 2035 | | 467,311 | 478,531 |
| Affordable Housing Trust Fund | 1.00% | 30 Years | July 1, 2033 | | 56,321 | 58,296 |
| Affordable Housing Trust Fund | 1.00% | 30 Years | September 1, 2035 | | 45,694 | 47,144 |
| NHPL, NHRL, NHPR | | | | | | |
| NHPL 1997-1998 | 1.00% | 20 Years | July 1, 2017 | | 244,350 | 271,500 |
| NHPL 1998-1999 | 1.00% | 20 Years | July 1, 2018 | | 332,572 | 365,831 |
| NHPL 1999-2000 | 1.00% | 20 Years | July 1, 2019 | | 323,004 | 352,368 |
| NHRL 1999-2000 | 1.00% | 10 Years | July 1, 2009 | | 8,772 | 17,544 |
| NHPR 2000-2001 | 1.00% | 20 Years | July 1, 2020 | | 379,350 | 410,962 |
| NHPR 2001-2002 | 1.00% | 20 Years | July 1, 2022 | | 347,588 | 374,325 |
| NHPR 2002-2003 | 1.00% | 20 Years | July 1, 2023 | | 470,676 | 504,038 |
| NHPR 2003-2004 | 1.00% | 20 Years | July 1, 2024 | | 455,063 | 485,400 |
| NHPR 2004-2005 | 1.00% | 20 Years | July 1, 2025 | | 370,800 | 393,975 |
| NHPR 2005-2006 | 1.00% | 20 Years | July 1, 2026 | | 329,400 | 341,600 |
| NHPR 2006-2007 | 1.00% | 20 Years | September 1, 2027 | | 156,600 | 165,300 |
| NHPR 2007-2008 | 1.00% | 20 Years | September 1, 2028 | | 234,818 | - |
| NHPR 2009 | 1.00% | 20 Years | November 1, 2028 | | 130,742 | - |
| Virginia Housing Development Authority: | | | | | | |
| Housing Fund #1 | 3.00% | 30 Years | July 5, 2028 | | 221,097 | 350,415 |
| VHPRF Phase I & II | 3.00% | 20 Years | November 5, 2026 | | 203,708 | 220,308 |
| Regional Loan Demo | 3.00% | 20 Years | May 20, 2010 | | 10,448 | 114,322 |
| Housing Fund #2 | 3.00% | 30 Years | December 5, 2018 | | 297,818 | 377,301 |
| Housing Fund #3 | 2.00% | 30 Years | March 1, 2014 | | 573,497 | 590,863 |
| 2004 Line of Credit | 2.00% | 30 Years | September 1, 2026 | | 857,933 | 882,148 |
| 2005 Line of Credit | 2.00% | 30 Years | February 1, 2037 | | 937,274 | 962,607 |
| 2007 Reach | 3.00% | 30 Years | April 1, 2038 | | 990,986 | 566,052 |
| Wachovia Bank | | | | | | |
| Fifteen Year Note | 4.50% | 15 Years | February 5, 2009 | | | 18,936 |
| Fifteen Year Note | 4.50% | 15 Years | February 15, 2009 | | | 19,725 |
| Five Year Note | .81% | 5 Years | November 30, 2011 | | 750,000 | 1,250,000 |
| Various Lenders | | | | | | |
| Sisters of Loretto | 3.00% | 3 Years | June 30, 2012 | | 50,000 | 50,000 |
| Literary Society of St. Catherine | 3.00% | 3 Years | June 30, 2009 | | - | 20,000 |
| Calvert Social Investment Foundation | 4.50% | 3 Years | June 30, 2010 | | 1,000,000 | 1,000,000 |
| Richard Hettrick | 3.00% | 3 Years | January 31, 2010 | | 5,500 | 5,500 |
| Opportunity Finance Network | 4.00% | 5 Years | October 31, 2012 | | 500,000 | 500,000 |
| Opportunity Finance Network | 6.00% | 10 Years | April 28, 2015 | | 918,260 | 939,775 |
| Andrew Schenker | 3.00% | 5 Years | May 31, 2011 | | 25,000 | 25,000 |
| Carter Garber | 4.00% | 5 Years | September 30, 2011 | | 35,000 | 35,000 |
| Franciscan Sisters of Mary | 2.00% | 5 Years | October 31, 2009 | | 50,000 | 50,000 |
| F. B. Heron Foundation | 3.00% | 6 Years | June 30, 2010 | | 400,000 | 500,000 |
| Allison Conant | 0.00% | 5 Years | July 13, 2009 | | 9,000 | 9,000 |
| Tides Foundation | 0.00% | 5 Years | July 13, 2012 | | 75,000 | 75,000 |
| Funding Exchange Endowment | 0.00% | 5 Years | July 13, 2009 | | 20,000 | 20,000 |
| Funding Exchange Pooled Investment | 0.00% | 5 Years | July 13, 2009 | | 6,000 | 6,000 |
| Ethel Ackley | 3.00% | 3 Years | July 13, 2010 | | 5,000 | 5,000 |
| E & H Stowell | 3.00% | 3 Years | July 13, 2008 | | - | 7,000 |

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2009 AND 2008

Note 7 – Notes Payable (Continued)

| | | | | | |
|---|-------|----------|--------------------|---------------|---------------|
| Woodlands Investment Management | 3.00% | 4 Years | September 30, 2011 | 100,000 | 100,000 |
| St. Paul's Church in Buffalo | 3.00% | 3 Years | August 29, 2009 | 5,000 | 5,000 |
| Trust U/AGR D3/1/84, Fay Chandler | 3.00% | 3 Years | December 31, 2009 | 25,000 | 25,000 |
| Trust U/AGR D3/1/84, Fay Chandler | 3.00% | 3 Years | March 21, 2010 | 50,000 | 50,000 |
| Glenmary Home Missioners | 3.00% | 3 Years | September 30, 2010 | 25,000 | 25,000 |
| Seton Enablement Fund | 3.00% | 5 Years | June 1, 2013 | 81,173 | 100,000 |
| The Ford Foundation | 1.00% | 10 Years | June 2, 2014 | 1,000,000 | 1,000,000 |
| Florida Community Loan Fund | 6.00% | 10 Years | April 28, 2015 | 459,130 | 469,888 |
| Stookey Trust | 3.00% | 5 Years | September 30, 2010 | 25,000 | 25,000 |
| U.S. Department of Agriculture | 1.00% | 30 Years | October 16, 2031 | 639,593 | 664,818 |
| Cg of the Sisters of the Incarnate Word | 2.00% | 5 Years | August 24, 2011 | 200,000 | 200,000 |
| Fannie Mae | 1.13% | 5 Years | May 7, 2012 | 2,000,000 | 1,500,000 |
| Kentucky Housing Corporation | 3.00% | 23 Years | July 1, 2016 | 265,598 | 274,490 |
| Peoples Self Help Housing | 4.00% | 2 Years | Jan 5, 2011 | 500,000 | |
| Fannie Mae | 5.00% | 10 Years | August 30, 2014 | 250,000 | 250,000 |
| Dominican Sisters of Peace | 3.00% | 1 Day | June 30, 2009 | 20,000 | |
| Kentucky Housing Corporation | 1.00% | 20 Years | September 1, 2028 | - | 222,459 |
| Central Bank | 5.00% | 1 Year | May 13, 2009 | - | 1,383 |
| CDFI Fund | 1.25% | 20 Years | September 10, 2019 | 930,000 | 930,000 |
| | | | | 930,000 | 930,000 |
| Total Notes Payable | | | | \$ 19,505,451 | \$ 19,461,332 |

The principal repayment requirements at June 30, 2009 relating to the above notes payable are as follows:

| | | | | |
|-------------|----|------------|----|------------|
| 2009 | \$ | - | \$ | 217,044 |
| 2010 | | 1,609,720 | | 1,802,366 |
| 2011 | | 592,500 | | 102,500 |
| 2012 | | 3,163,500 | | 3,023,000 |
| 2013 | | 711,773 | | 244,500 |
| 2014 | | 1,675,997 | | - |
| Later Years | | 11,751,961 | | 14,071,922 |
| Totals | \$ | 19,505,451 | \$ | 19,461,332 |

At June 30, 2009 and 2008 approximately \$3.212 million and \$3.343 million notes payable, respectively, are unsecured and represent private investments by individuals and groups.

At June 30, 2009 and 2008, respectively the Organization has a \$4.5 million line of credit with Wachovia secured by \$7.7 million commercial loan assets in 2009; a \$3.0 million line of credit with Fannie Mae backed by an unsecured letter of credit with Peoples Bank for \$450,000; a \$1.5 million line of credit with VHDA which is used to table fund loans and is immediately reimbursed; and a \$500,000 line of credit with Central Bank secured by real estate.

At June 30, 2009 the organization had available balances on lines of credit with Wachovia Bank of \$3.75 million, Fannie Mae of \$1.0 million and Central Bank of \$500,000.

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2009 AND 2008

Note 8-Other Liabilities

The Organization carries a \$2,000,000, ten-year note with Wachovia Bank classified as EQ2 funds. This note is shown under Other Liabilities on the balance sheet in order to represent more clearly the nature of the payable and to adhere to industry practice. The EQ2 is defined by having six attributes as follows (1) the EQ2 investment is carried as an investment on the investor's balance sheet in accordance with GAAP. (2) the EQ2 investment is a general obligation of FAHE that is not secured by any of FAHE's assets; (3) the EQ2 investment is fully subordinated to the right of repayment of all FAHE's other creditors; (4) the EQ2 investment does not give the investor the right to accelerate payment unless FAHE ceases its normal operations; (5) the EQ2 investment carries an interest rate that is not tied to any income received by FAHE; and (6) the EQ2 investment has a rolling term, and therefore, an indeterminate maturity. This note had an outstanding balance of \$2,000,000 as of June 30, 2009 and 2008, respectively.

Note 9 – Commitments and Contingencies

The Organization receives Federal and State grant funds that are subject to review by the granting agencies. If an agency finds that the funds are considered not to have been used in accordance with the purposes of the grant, the grantor may request a refund of such funds. The amount of future potential refunds, if any, is not expected to be significant.

The Organization has an agreement with the Tennessee Housing Development Agency (THDA) to guarantee and service New Start loans to individuals, as well as guaranteeing and servicing member loan agreements with THDA. The Organization entered into the agreements to facilitate THDA working with the Organization's members located in Tennessee. Although management of the Organization feels these loans will be repaid and are fully secured by real estate, the Organization has a contingent liability of \$9,566,781 and \$5,141,279 as of June 30, 2009 and 2008, respectively. To further clarify, of the \$9,566,781 balance, FAHE is the first guarantor on \$1,481,598 and takes the position of second guarantor on the remaining member loan agreements. Historically, there has not been a loss on these loans since inception in 2003.

The Organization has a contractual agreement with NHSA to sell mortgage notes, off the balance sheet, while retaining the servicing rights. The notes, with a balance of \$10,616,830 and \$1,470,523 at June 30, 2009 and 2008, respectively, were sold with recourse. The Organization has posted letters of credit totaling \$1.5million with Peoples Bank to stand against potential delinquent notes required to be repurchased. Ultimately, all the notes are fully secured by real estate and the Organization feels even in the event of repurchase the loans will be repaid.

Note 10 – Concentrations of Credit Risk

Financial instruments that potentially subject the Organization to a concentration of credit risk consist principally of cash and cash equivalents and notes receivable. The Organization maintains cash balances in FDIC insured accounts up to \$250,000 per account with excess values invested in sweep accounts collateralized with mortgages. The Organization provides mortgage loans primarily to low- and moderate-income individuals. Mortgage notes totaling \$22,297,600 and \$23,356,215 at June 30, 2009 and 2008, respectively, are secured by the property purchased or improved. These mortgage receivables are a concentration of credit risk. The Organization provides loans to groups to support the growth of low-income housing opportunities in its service area. Notes receivable totaling \$11,363,223 and \$11,437,674 at June 30, 2009 and 2008, respectively, are secured by the assets of the Organization. Additionally, at June 30, 2009 and 2008, \$1,180,858 and \$1,362,126 respectively, were unsecured. Finally, the Organization receives a substantial percentage of its funding from government grants and other contributions. The Organization's management does not anticipate a reduction in such funding.

The Organization maintains a 4% loan loss reserve on the aggregate balance of the loan portfolio.

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2009 AND 2008

Note 11–Prior Period Corrections

The Organization corrected prior period accounting errors for loans that had not been previously recorded when originated in 1991-1995. An increase of \$316,900 was made to beginning net assets to reflect non-interest bearing notes receivable made to Shelbyville/Martinsville residents. The notes are to be repaid by the mortgagee upon the transfer of property either at sale or death. Additionally, beginning net assets were increased by \$75,000 and \$52,425 to record principal and cumulative interest, respectively, on an interest-bearing note originating in 1995 for the Blueberry Hill development project. The total prior period adjustments represent an increase of \$444,325 to the July 1, 2007 beginning net assets.

Note 12–Deposits

As of June 30, 2009 the Organization entered into a contract for the purchase of the Parker-Hannifin property located in Berea. The property consists of a building and nine acres of land. FAHE plans to move the Berea headquarters to this location after clean up and renovation. The \$150,000 increase in deposits represents the funds wired to secure the transaction. The closing took place July 1, 2009.

Note 13–Subsequent Events

Management of the Organization has considered subsequent events through September 15, 2009, the date this report becomes available for issue.

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.
 SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
 FOR THE YEAR ENDED JUNE 30, 2009

| <u>Federal Grantor/Pass-Through Grantor/Program Title</u> | <u>Federal CFDA Number</u> | <u>Pass-Through Grantor's Number</u> | <u>Expenditures</u> |
|---|------------------------------------|--|---------------------|
| <u>Department of Treasury</u> | | | |
| NeighborWorks America | 21.000 | | 317,500 |
| <u>Appalachian Regional Commission</u> | | | |
| <u>Passed through Kentucky Housing Corporation</u> | | | |
| Appalachian Regional Development | 23.001 | * KY-16138-302-09 | 354,150 |
| <u>Department of Housing & Urban Development</u> | | | |
| <u>Passed through Kentucky Housing Corporation</u> | | | |
| Home Investment Partnership Program (HOME) | 14.239 | HB08-0201-01 | 192,000 |
| TOTAL FEDERAL AWARDS | | | \$ 863,650 |

* Major Program Circular A-133

See accompanying notes to Schedule of Expenditures of Federal Awards.

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.
NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2009

NOTE A – BASIS OF PRESENTATION

The accompanying schedule of expenditures of federal awards includes the federal grant activity of Federation of Appalachian Housing Enterprises, Inc. and is presented on the cash basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, Audits of States, Local Governments and Non-Profit Organizations. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in, the preparation of the financial statements.

NOTE B – INSURANCE

The Organization carried insurance coverage during the entire year in amounts sufficient or in excess of required levels, including coverage for general and professional liability, real and personal property, workers compensation and fidelity bonding of employees who have access to funds.

REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING
BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN
ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

To the Board of Directors
Federation of Appalachian Housing Enterprises, Inc.
Berea, Kentucky

We have audited the financial statements of Federation of Appalachian Housing Enterprises, Inc. (a non-profit organization) as of and for the year ended June 30, 2009, and have issued our report thereon dated September 15, 2009. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Federation of Appalachian Housing Enterprises, Inc.'s internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Federation of Appalachian Housing Enterprises, Inc.'s internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Organization's internal control over financial reporting.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the organization's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles, such that there is more than a remote likelihood that a misstatement of the organization's financial statement that is more than inconsequential will not be prevented or detected by the organization's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that result in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the organization's internal control.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

Compliance

As part of obtaining reasonable assurance about whether Federation of Appalachian Housing Enterprises, Inc.'s financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.



Certified Public Accountants
Post Office Box 827
Richmond, KY 40476
www.craftnoble.com

This report is intended for the information of the Board of Directors, management, federal and state awarding agencies, and pass-through entities and is not intended to be, and should not be, used by anyone other than these specified parties.

Craft, Noble & Company, PLLC

Craft, Noble & Company, PLLC
September 15, 2009

REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO
EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER
COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133

To the Board of Directors
Federation of Appalachian Housing Enterprises, Inc.
Berea, Kentucky

Compliance

We have audited the compliance of Federation of Appalachian Housing Enterprises, Inc. (a non-profit organization) with the types of compliance requirements described in the “U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement” that are applicable to each of its major federal programs for the year ended June 30, 2009. Federation of Appalachian Housing Enterprises, Inc.’s major federal programs are identified in the summary of auditors’ results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of Federation of Appalachian Housing Enterprises, Inc.’s management. Our responsibility is to express an opinion on Federation of Appalachian Housing Enterprises, Inc.’s compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America, the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, and OMB Circular A-133, “Audits of States, Local Governments, and Non-Profit Organizations”. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about Federation of Appalachian Housing Enterprises, Inc.’s compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of Federation of Appalachian Housing Enterprises, Inc.’s compliance with those requirements.

In our opinion, Federation of Appalachian Housing Enterprises, Inc. complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2009.

Internal Control Over Compliance

The management of Federation of Appalachian Housing Enterprises, Inc. is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered Federation of Appalachian Housing Enterprises, Inc.’s internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the organization’s internal control over compliance.



CRAFT, NOBLE & COMPANY
PLLC

Certified Public Accountants
Post Office Box 827
Richmond, KY 40476
www.craftnoble.com

A control deficiency in an organization's internal control over compliance exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the organization's ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program is more than inconsequential will not be prevented or detected by the organization's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that result in more than a remote likelihood that a material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected by the organization's internal control.

Our consideration of the internal control over compliance was for the limited purpose of described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control over compliance that we consider to be material weaknesses, as described above.

This report is intended for the information of the Board of Directors, management, and federal and state awarding agencies and pass-through entities and is not intended to be, and should not be, used by anyone other than these specified parties.

Craft, Noble & Company, PLLC

Craft, Noble & Company, PLLC
September 15, 2009

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2009

SUMMARY OF AUDITORS' RESULTS

1. The auditors' report expresses an unqualified opinion on the financial statements of Federation of Appalachian Housing Enterprises, Inc.
2. Our report on the financial statements disclosed no significant deficiencies in the internal control structure.
3. No instances of noncompliance material to the financial statements of Federation of Appalachian Housing Enterprises, Inc. were disclosed during our audit.
4. The auditors' report on compliance for the major federal awards program for Federation of Appalachian Housing Enterprises, Inc. expresses an unqualified opinion on all major federal programs.
5. Our audit report disclosed no audit finding required to be reported under Section 510(a) of OMB Circular A-133.
6. The programs tested as major programs included:
Appalachian Regional Commission CFDA #23.001 Type A.
7. The threshold to determine Type A: \$300,000.
8. Federation of Appalachian Housing Enterprises, Inc. was determined to be a low-risk auditee.
9. In connection with tests of internal control and compliance with laws and regulations, no material weaknesses were noted in internal control, and the Organization was in substantial compliance with laws and regulations.
10. There were no questioned costs with respect to major programs selected for compliance tests.

FEDERATION OF APPALACHIAN ENTERPRISES, INC.
STATEMENT OF FUNCTIONAL EXPENSES
FOR THE YEAR ENDED JUNE 30, 2009

| Expenses | Program Services | | | | | | | | | | Total | | | | | | | | | | |
|--------------------------------|--------------------------|--|----------------|--|----------------|--|----------------|--|----------------|--|---------------|-------|----------------|------------------|----------------|-------|----------------|----|------------------|--|------------------|
| | General & Administrative | | Membership | | Fundraising | | Home Lending | | Community | | | Grant | | Program Services | | Total | | | | | |
| | \$ | | \$ | | \$ | | \$ | | \$ | | \$ | | \$ | | \$ | | | \$ | | | |
| Personnel Expenses | 533,175 | | 105,952 | | 58,102 | | 300,766 | | 157,218 | | 20,507 | | 246,081 | | 102,534 | | 116,205 | | 943,311 | | 1,640,540 |
| Travel Expenses | 25,986 | | 5,164 | | 2,832 | | 14,658 | | 7,662 | | 999 | | 11,993 | | 4,997 | | 5,664 | | 45,973 | | 79,955 |
| Board & Committee Meetings | 11,101 | | 2,206 | | 1,210 | | 6,262 | | 3,274 | | 427 | | 5,124 | | 2,135 | | 2,420 | | 19,642 | | 34,159 |
| Conference & Workshops | 8,642 | | 1,717 | | 942 | | 4,875 | | 2,548 | | 332 | | 3,989 | | 1,662 | | 1,884 | | 15,290 | | 26,591 |
| Occupancy Expense | 16,991 | | 3,376 | | 1,852 | | 9,585 | | 5,010 | | 654 | | 7,842 | | 3,268 | | 3,703 | | 30,062 | | 52,281 |
| Supplies & Publications | 5,955 | | 1,183 | | 649 | | 3,359 | | 1,756 | | 229 | | 2,748 | | 1,145 | | 1,298 | | 10,535 | | 18,322 |
| Postage & Shipping | 6,192 | | 1,230 | | 675 | | 3,493 | | 1,826 | | 238 | | 2,858 | | 1,191 | | 1,350 | | 10,956 | | 19,053 |
| Communications | 12,900 | | 2,563 | | 1,406 | | 7,277 | | 3,804 | | 496 | | 5,954 | | 2,481 | | 2,811 | | 22,823 | | 39,692 |
| Equipment & Maintenance | 16,646 | | 3,308 | | 1,814 | | 9,390 | | 4,909 | | 640 | | 7,683 | | 3,201 | | 3,628 | | 29,451 | | 51,219 |
| Subscriptions | 667 | | 133 | | 73 | | 376 | | 197 | | 26 | | 308 | | 128 | | 145 | | 1,180 | | 2,053 |
| Licenses, Fees & Permits | 1,446 | | 287 | | 158 | | 816 | | 426 | | 56 | | 667 | | 278 | | 315 | | 2,558 | | 4,449 |
| Employee Education | 1,039 | | 206 | | 113 | | 586 | | 306 | | 40 | | 479 | | 200 | | 226 | | 1,837 | | 3,195 |
| Memberships | 4,886 | | 971 | | 532 | | 2,756 | | 1,441 | | 188 | | 2,255 | | 940 | | 1,065 | | 8,645 | | 15,034 |
| Marketing & Advertising | 13,150 | | 2,613 | | 1,433 | | 7,418 | | 3,878 | | 506 | | 6,069 | | 2,529 | | 2,866 | | 23,266 | | 40,462 |
| Liability & Property Insurance | 9,999 | | 1,987 | | 1,090 | | 5,640 | | 2,948 | | 385 | | 4,615 | | 1,923 | | 2,179 | | 17,690 | | 30,766 |
| Service Charges | 3,008 | | 598 | | 328 | | 1,697 | | 887 | | 116 | | 1,388 | | 578 | | 656 | | 9,256 | | 9,256 |
| Depreciation & Amortization | 19,007 | | 3,777 | | 2,071 | | 10,722 | | 5,605 | | 731 | | 8,772 | | 3,655 | | 4,142 | | 33,627 | | 58,482 |
| Organizational Expenses | 153 | | 30 | | 17 | | 86 | | 45 | | 6 | | 70 | | 29 | | 33 | | 269 | | 469 |
| Contributions | 2,688 | | 534 | | 293 | | 1,516 | | 793 | | 103 | | 1,240 | | 517 | | 586 | | 4,755 | | 8,270 |
| Software Lease | 7,924 | | 1,575 | | 864 | | 4,470 | | 2,337 | | 305 | | 3,657 | | 1,524 | | 1,727 | | 14,020 | | 24,383 |
| Professional Fees | 28,550 | | 5,673 | | 3,111 | | 16,105 | | 8,419 | | 1,098 | | 13,177 | | 5,490 | | 6,222 | | 50,511 | | 87,845 |
| Contract Services | 41,266 | | 8,200 | | 4,497 | | 23,278 | | 12,168 | | 1,587 | | 19,046 | | 7,936 | | 8,994 | | 73,009 | | 126,972 |
| Loan Processing Expense | 1,399 | | 278 | | 152 | | 789 | | 413 | | 54 | | 646 | | 269 | | 305 | | 2,476 | | 4,305 |
| Loan Servicing Expense | 2,710 | | 539 | | 295 | | 1,529 | | 799 | | 104 | | 1,251 | | 521 | | 591 | | 4,795 | | 8,339 |
| Pass Thru Grants | 217,859 | | 43,292 | | 23,741 | | 122,895 | | 64,240 | | 8,379 | | 100,550 | | 41,896 | | 47,482 | | 385,442 | | 670,334 |
| Over/Short | 67 | | 13 | | 7 | | 38 | | 20 | | 3 | | 31 | | 13 | | 15 | | 120 | | 207 |
| Administration | 9,787 | | 1,945 | | 1,067 | | 5,521 | | 2,886 | | 376 | | 4,517 | | 1,882 | | 2,133 | | 17,315 | | 30,114 |
| Bad Debt Expense | 73,578 | | 14,621 | | 8,018 | | 41,505 | | 21,696 | | 2,830 | | 33,959 | | 14,150 | | 16,036 | | 130,176 | | 226,393 |
| Interest Expense | 186,574 | | 37,076 | | 20,332 | | 105,247 | | 55,015 | | 7,176 | | 86,111 | | 35,880 | | 40,664 | | 330,093 | | 574,075 |
| Loans Forgiving | 2,588 | | 514 | | 282 | | 1,460 | | 763 | | 100 | | 1,194 | | 498 | | 564 | | 4,579 | | 7,963 |
| Miscellaneous Expense | 508 | | 104 | | 54 | | 288 | | 151 | | 20 | | 236 | | 98 | | 112 | | 905 | | 1,571 |
| State Income Tax | - | | - | | - | | - | | - | | - | | - | | - | | - | | - | | - |
| Total Expenses | <u>1,266,441</u> | | <u>251,665</u> | | <u>138,010</u> | | <u>714,403</u> | | <u>373,440</u> | | <u>48,711</u> | | <u>584,510</u> | | <u>243,548</u> | | <u>276,021</u> | | <u>2,240,633</u> | | <u>3,896,749</u> |

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

FEDERATION OF APPALACHIAN ENTERPRISES, INC.
STATEMENT OF FUNCTIONAL EXPENSES
FOR THE YEAR ENDED JUNE 30, 2008

Program Services

| Expenses | Program Services | | | | | | | | | | Total |
|------------------------------|--------------------------|------------|-------------|--------------|-----------------------|----------------------|----------------|-----------------|--------------|------------------------|--------------|
| | General & Administrative | Membership | Fundraising | Home Lending | Community Development | Grant Administration | Loan Servicing | FAHE Consulting | FAHE Capital | Total Program Services | |
| Personnel Expenses | \$ 424,704 | \$ 84,396 | \$ 46,282 | \$ 239,577 | \$ 125,233 | \$ 16,335 | \$ 196,017 | \$ 81,674 | \$ 92,564 | \$ 751,400 | \$ 1,306,782 |
| Travel Expenses | 21,627 | 4,298 | 2,357 | 12,200 | 6,377 | 832 | 9,982 | 4,159 | 4,714 | 38,264 | 66,546 |
| Board & Committee Meetings | 9,662 | 1,920 | 1,053 | 5,450 | 2,849 | 372 | 4,459 | 1,858 | 2,106 | 17,094 | 29,729 |
| Conference & Workshops | 4,846 | 963 | 528 | 2,734 | 1,429 | 186 | 2,237 | 932 | 1,056 | 8,574 | 14,911 |
| Occupancy Expense | 8,667 | 1,722 | 944 | 4,889 | 2,556 | 333 | 4,000 | 1,667 | 1,889 | 15,334 | 26,667 |
| Supplies & Publications | 7,960 | 1,582 | 867 | 4,490 | 2,347 | 306 | 3,674 | 1,531 | 1,735 | 14,083 | 24,492 |
| Postage & Shipping | 4,618 | 918 | 503 | 2,605 | 1,362 | 178 | 2,131 | 888 | 1,006 | 8,170 | 14,209 |
| Communications | 10,273 | 2,041 | 1,119 | 5,795 | 3,029 | 395 | 4,741 | 1,975 | 2,239 | 18,174 | 31,607 |
| Equipment & Maintenance | 14,718 | 2,925 | 1,604 | 8,303 | 4,340 | 566 | 6,793 | 2,830 | 3,208 | 26,040 | 45,287 |
| Subscriptions | 1,311 | 261 | 143 | 740 | 387 | 50 | 605 | 252 | 286 | 2,320 | 4,035 |
| Licenses, Fees, & Permits | 1,951 | 388 | 213 | 1,101 | 575 | 75 | 901 | 375 | 425 | 3,452 | 6,004 |
| Employee education | 2,831 | 563 | 309 | 1,597 | 835 | 109 | 1,307 | 544 | 617 | 5,009 | 8,712 |
| Memberships | 3,803 | 756 | 414 | 2,145 | 1,122 | 146 | 1,755 | 731 | 829 | 6,728 | 11,701 |
| Marketing & Advertising | 30,536 | 6,068 | 3,328 | 17,225 | 9,004 | 1,174 | 14,093 | 5,872 | 6,655 | 54,023 | 93,955 |
| Liability/Property Insurance | 5,920 | 1,176 | 645 | 3,339 | 1,746 | 228 | 2,732 | 1,138 | 1,290 | 10,473 | 18,214 |
| Service Charges | 1,890 | 376 | 206 | 1,066 | 557 | 73 | 872 | 363 | 412 | 3,343 | 5,815 |
| Depreciation/Amortization | 14,484 | 2,878 | 1,578 | 8,170 | 4,271 | 557 | 6,685 | 2,785 | 3,157 | 25,625 | 44,565 |
| Organizational Expense | 135 | 27 | 15 | 76 | 40 | 5 | 62 | 26 | 29 | 238 | 415 |
| Contributions | 1,853 | 368 | 202 | 1,045 | 546 | 71 | 855 | 356 | 404 | 3,277 | 5,700 |
| Software Lease | 7,015 | 1,394 | 764 | 3,957 | 2,069 | 270 | 3,238 | 1,349 | 1,529 | 12,412 | 21,585 |
| Professional Fees | 21,538 | 4,280 | 2,347 | 12,150 | 6,351 | 828 | 9,941 | 4,142 | 4,694 | 38,106 | 66,271 |
| Contract Services | 88,435 | 17,574 | 9,637 | 49,887 | 26,077 | 3,401 | 40,816 | 17,007 | 19,274 | 156,462 | 272,108 |
| Loan Processing Expense | 552 | 110 | 60 | 311 | 163 | 21 | 255 | 106 | 120 | 976 | 1,698 |
| Loan Servicing Expense | 814 | 162 | 89 | 459 | 240 | 31 | 376 | 157 | 177 | 1,440 | 2,505 |
| Pass thru Grants | 274,471 | 54,542 | 29,910 | 154,830 | 80,934 | 10,557 | 126,679 | 52,783 | 59,820 | 485,603 | 844,526 |
| Loss On Disposal Of Property | 9,549 | 1,898 | 1,041 | 5,387 | 2,816 | 367 | 4,407 | 1,836 | 2,081 | 16,894 | 29,382 |
| Administration | 17,908 | 3,559 | 1,951 | 10,102 | 5,280 | 689 | 8,265 | 3,444 | 3,903 | 31,683 | 55,101 |
| Bad Debt Expense | 41,466 | 8,240 | 4,519 | 23,391 | 12,227 | 1,595 | 19,138 | 7,974 | 9,038 | 73,363 | 127,588 |
| Interest Expense | 187,244 | 37,209 | 20,405 | 105,625 | 55,213 | 7,202 | 86,420 | 36,009 | 40,810 | 331,279 | 576,137 |
| Loans Forgiven | 15,945 | 3,169 | 1,738 | 8,995 | 4,702 | 613 | 7,359 | 3,066 | 3,475 | 28,210 | 49,062 |
| Miscellaneous Expense | 618 | 119 | 68 | 347 | 182 | 24 | 284 | 118 | 142 | 1,097 | 1,902 |
| State Income tax | 316 | 63 | 34 | 178 | 93 | 12 | 146 | 61 | 69 | 559 | 972 |
| Total Expenses | \$ 1,237,660 | \$ 245,945 | \$ 134,873 | \$ 698,166 | \$ 364,952 | \$ 47,601 | \$ 571,225 | \$ 238,008 | \$ 269,753 | \$ 2,189,705 | \$ 3,808,183 |

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

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.
 STATEMENTS OF FINANCIAL POSITION - NEIGHBORWORKS AMERICA CAPITAL FUND
 JUNE 30, 2009 AND 2008

| | <u>2009</u> | <u>2008</u> |
|---------------------------|-------------------|-------------------|
| ASSETS | | |
| Cash and cash equivalents | \$ 206,034 | \$ 246,320 |
| TOTAL ASSETS | <u>\$ 206,034</u> | <u>\$ 246,320</u> |
| NET ASSETS | | |
| Temporarily Rstricted | \$ 24,912 | \$ - |
| Permanently restricted | <u>181,122</u> | <u>\$ 246,320</u> |
| TOTAL NET ASSETS | <u>\$ 206,034</u> | <u>\$ 246,320</u> |

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC
 STATEMENTS OF ACTIVITIES - NEIGHBORWORKS AMERICA CAPITAL FUND
 FOR THE YEARS ENDED JUNE 30, 2009 AND 2008

| | <u>2009</u> | <u>2008</u> |
|---|-------------|-------------|
| TEMPORARILY RESTRICTED NET ASSETS | | |
| Restrictions released from permanently restricted net asset | \$ 24,912 | \$ - |
| INCREASE IN TEMPORARILY RESTRICTED NET ASSETS | 24,912 | - |
| PERMANENTLY RESTRICTED NET ASSETS | | |
| Revenues and Other Support | | |
| Capital Grant - NeighborWorks America | \$ 195,000 | \$ 246,320 |
| Net assets released from restriction | (260,198) | - |
| INCREASE/(DECREASE) IN PERMANENTLY RESTRICTED NET ASSETS | (65,198) | 246,320 |
| CHANGE IN NET ASSETS | (40,286) | 246,320 |
| NET ASSETS AT BEGINNING OF YEAR | 246,320 | - |
| NET ASSETS AT END OF YEAR | \$ 206,034 | \$ 246,320 |

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.
 COMPUTATION OF ADJUSTED NET WORTH FOR APPROVAL OF NONSUPERVISED
 MORTGAGEES OTHER THAN LOAN CORRESPONDENTS
 FOR THE YEAR ENDING JUNE 30, 2009

| | | |
|---|---------------|-----------------------------|
| Minimum net worth required | | <u>\$ 250,000</u> |
| Stockholders equity(net worth) Per balance sheet | \$ 18,610,625 | |
| Less unacceptable assets | <u>\$ -</u> | |
| Adjusted net worth for HUD Requirement purposes | | <u><u>\$ 18,610,625</u></u> |
| Adjusted net worth above amount Required | | <u>\$ 18,360,625</u> |
| Adjusted net worth below amount Required | | <u>\$ -</u> |

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.
 COMPUTATION OF ADJUSTED NET WORTH FOR APPROVAL AND RECERTIFICATION OF
 NONSUPERVISED MORTGAGEES OTHER THAN LOAN CORRESPONDENTS
 FOR THE YEAR ENDING JUNE 30, 2009

| | | |
|---|---------------|----------------------------|
| Home office | | \$ <u>63,000</u> |
| Add: | | |
| Branch office | \$ 25,000 | |
| x Number of branch offices | <u>3</u> | |
| Subtotal | | \$ <u>75,000</u> |
| Total | | \$ <u><u>138,000</u></u> |
| Net worth required (lesser of \$250,000 or Line 3) | | \$ <u><u>250,000</u></u> |
| Owner's equity (net worth) per Balance sheet | \$ 18,610,625 | |
| Less unacceptable assets | <u>\$ -</u> | |
| Adjusted net worth for HUD Requirement purposes | | <u><u>\$18,610,625</u></u> |
| Adjusted net worth above amount Required | | <u>\$18,360,625</u> |
| Adjusted net worth below amount Required | | <u>\$ -</u> |

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.
 COMPUTATION OF ADJUSTED NET WORTH FOR APPROVAL AND RECERTIFICATION OF
 NONSUPERVISED MORTGAGEES OTHER THAN LOAN CORRESPONDENTS
 FOR THE YEAR ENDING JUNE 30, 2009

| | | |
|--|----------------------------|----------------------------|
| Servicing portfolio at June 30,2009 | | \$ <u> -</u> |
| Add: | | |
| Originated during fiscal year | <u> -</u> | |
| Purchased from loan correspondent during fiscal year | <u> -</u> | |
| Subtotal | | <u> -</u> |
| Less: | | |
| Amounts included in Line 2 | <u> -</u> | |
| Servicing retained | <u> -</u> | |
| Loan correspondent purchases retained | <u> -</u> | |
| Subtotal | | <u> -</u> |
| Total | | |
| 1% of line 4 | | |
| Minimum net worth required (Greater of \$250,000 or Line 5) | | \$ <u> 250,000</u> |
| Net worth required (lesser of \$1,000,000 or line 6) | | \$ <u> 250,000</u> |
| Stockholders equity (net worth) Per balance sheet | <u> 18,610,625</u> | |
| Less unacceptable assets | <u> -</u> | |
| Adjusted net worth | | <u> 18,610,625</u> |
| Adjusted net worth above amount required | | <u> 18,360,625</u> |
| Adjusted net worth below amount Required | | <u> -</u> |

INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE WITH SPECIFIC
REQUIREMENTS APPLICABLE TO NON-MAJOR HUD PROGRAM TRANSACTIONS

To the Board of Directors
Federation of Appalachian Housing Enterprises, Inc.
Berea, Kentucky

We have audited the financial statements of Federation of Appalachian Housing Enterprises, Inc. as of and for the year ended June 30, 2009, and have issued our report thereon dated September 15, 2009.

In connection with that audit and with our consideration of Federation of Appalachian Housing Enterprises, Inc.'s internal control used to administer HUD programs, as required by the *Consolidated Audit Guide for Audits of HUD Programs* (the "Guide") issued by the U.S. Department of Housing and Urban Development, Office of the Inspector General, we selected certain transactions applicable to certain non-major HUD-assisted programs for the year ended June 30, 2009.

As required by the Guide, we performed auditing procedures to test compliance with the requirements governing HUD Approved Title II Non-supervised Mortgages and Loan Correspondents that are applicable to those transactions. Our procedures were substantially less in scope than an audit, the objective of which is the expression of an opinion on Federation of Appalachian Housing Enterprises, Inc.'s compliance with these requirements. Accordingly, we do not express such an opinion.

The results of our tests disclosed no instances of noncompliance that are required to be reported herein under the Guide.

This report is intended solely for the information of the audit committee, management, and the Department of Housing and Urban Development and is not intended to be and should not be used by anyone other than these specified parties.

Craft, Noble & Company, PLLC

Craft, Noble & Company, PLLC
September 15, 2009

