

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.  
BEREA, KENTUCKY

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AUDITED FINANCIAL STATEMENTS AND  
INDEPENDENT AUDITORS' REPORT  
FOR THE YEARS ENDED  
JUNE 30, 2011 AND 2010



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## 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, 2011 and 2010, 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 audits 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 audits 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 audits provides a reasonable basis for our opinions.

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, 2011 and 2010, and the changes in its net assets and its cash flows for the years 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, 2011 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, grant 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 statements of financial position – Neighborworks America Capital Fund on page 24, and the statements of activities – Neighborworks America Capital Fund on page 25 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 16 is presented for purposes of additional analysis as required by the 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 audits 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, 2011

FEDERATION OF APPALACHIAN HOUSING, INC.  
STATEMENT OF FINANCIAL POSITION  
JUNE 30, 2011

|                                     | Unrestricted         | Temporarily<br>Restricted | Permanently<br>Restricted | Total                |
|-------------------------------------|----------------------|---------------------------|---------------------------|----------------------|
| <u>Assets</u>                       |                      |                           |                           |                      |
| Cash and cash equivalents           | \$ 4,026,274         | \$ 1,570,545              | \$ 256,213                | \$ 5,853,032         |
| Accounts receivable                 | 161,219              | -                         | -                         | 161,219              |
| Accrued interest receivable         | 289,961              | 4,484                     | -                         | 294,445              |
| Investments                         | 71,300               | -                         | -                         | 71,300               |
| Deposits                            | 2,820                | -                         | -                         | 2,820                |
| Prepaid expenses                    | 105,819              | -                         | -                         | 105,819              |
| Property and equipment, net         | 800,908              | -                         | -                         | 800,908              |
| Interfund balances                  | 7,135                | (7,135)                   | -                         | -                    |
| Mortgage notes receivable, net      | 12,530,499           | 9,239,107                 | 67,421                    | 21,837,027           |
| Notes receivable, net               | 13,688,728           | 668,450                   | 37,500                    | 14,394,678           |
| Property held for sale              | 1,100,508            | 446,609                   | -                         | 1,547,117            |
| Deferred compensation               | 21,002               | -                         | -                         | 21,002               |
|                                     | <hr/>                | <hr/>                     | <hr/>                     | <hr/>                |
| Total Assets                        | <u>\$ 32,806,173</u> | <u>\$ 11,922,060</u>      | <u>\$ 361,134</u>         | <u>\$ 45,089,367</u> |
| <u>Liabilities &amp; Net Assets</u> |                      |                           |                           |                      |
| <u>Liabilities</u>                  |                      |                           |                           |                      |
| Accounts payable                    | \$ 100,133           | \$ -                      | \$ -                      | \$ 100,133           |
| Payroll taxes payable               | 22,768               | -                         | -                         | 22,768               |
| Client advances and deposits        | 542,769              | -                         | -                         | 542,769              |
| Accrued interest payable            | 49,597               | 4,375                     | -                         | 53,972               |
| Compensated absences payable        | 257,509              | -                         | -                         | 257,509              |
| Deferred revenue                    | 64,510               | 486,407                   | -                         | 550,917              |
| Notes payable                       | 21,497,510           | 584,892                   | -                         | 22,082,402           |
| Deferred compensation               | 21,002               | -                         | -                         | 21,002               |
|                                     | <hr/>                | <hr/>                     | <hr/>                     | <hr/>                |
| Total Liabilities                   | <u>22,555,798</u>    | <u>1,075,674</u>          | <u>-</u>                  | <u>23,631,472</u>    |
| <u>Other Liabilities</u>            |                      |                           |                           |                      |
| Equity equivalent                   | <u>2,000,000</u>     | <u>-</u>                  | <u>-</u>                  | <u>2,000,000</u>     |
| Total Liabilities                   | <u>24,555,798</u>    | <u>1,075,674</u>          | <u>-</u>                  | <u>25,631,472</u>    |
| <u>Net Assets</u>                   |                      |                           |                           |                      |
| Net assets                          | 7,650,375            | 10,846,386                | 361,134                   | 18,857,895           |
| Net assets, board designated        | <u>600,000</u>       | <u>-</u>                  | <u>-</u>                  | <u>600,000</u>       |
| Total Net Assets                    | <u>8,250,375</u>     | <u>10,846,386</u>         | <u>361,134</u>            | <u>19,457,895</u>    |
|                                     | <hr/>                | <hr/>                     | <hr/>                     | <hr/>                |
| Total Liabilities & Net Assets      | <u>\$ 32,806,173</u> | <u>\$ 11,922,060</u>      | <u>\$ 361,134</u>         | <u>\$ 45,089,367</u> |

FEDERATION OF APPALACHIAN HOUSING, INC.  
STATEMENT OF FINANCIAL POSITION  
JUNE 30, 2010

|                                   | Unrestricted         | Temporarily<br>Restricted | Permanently<br>Restricted | Total                |
|-----------------------------------|----------------------|---------------------------|---------------------------|----------------------|
| <u>Assets</u>                     |                      |                           |                           |                      |
| Cash and cash equivalents         | \$ 5,246,225         | \$ 1,278,615              | \$ 149,148                | \$ 6,673,988         |
| Accounts receivable               | 784,675              | (2,772)                   | -                         | 781,903              |
| Grants receivable                 | -                    | 537,500                   | -                         | 537,500              |
| Accrued interest receivable       | 252,878              | 12,747                    | -                         | 265,625              |
| Deposits                          | 3,120                | -                         | -                         | 3,120                |
| Prepaid expenses                  | 98,470               | -                         | -                         | 98,470               |
| Property and equipment, net       | 860,177              | -                         | -                         | 860,177              |
| Interfund balances                | (4,173)              | 4,173                     | -                         | -                    |
| Mortgage notes receivable, net    | 10,861,643           | 9,726,093                 | 69,175                    | 20,656,911           |
| Notes receivable, net             | 11,222,393           | 523,310                   | 12,811                    | 11,758,514           |
| Property held for sale            | 1,002,665            | 224,068                   | -                         | 1,226,733            |
| Deferred compensation             | 15,513               | -                         | -                         | 15,513               |
|                                   | <u>\$ 30,343,586</u> | <u>\$ 12,303,734</u>      | <u>\$ 231,134</u>         | <u>\$ 42,878,454</u> |
| <u>Liabilities and Net Assets</u> |                      |                           |                           |                      |
| <u>Liabilities</u>                |                      |                           |                           |                      |
| Accounts payable                  | \$ 102,963           | \$ 53,735                 | \$ -                      | \$ 156,698           |
| Payroll taxes payable             | 26,356               | -                         | -                         | 26,356               |
| Client advances and deposits      | 645,337              | -                         | -                         | 645,337              |
| Accrued interest payable          | 43,076               | 4,568                     | -                         | 47,644               |
| Compensated absences payable      | 207,844              | -                         | -                         | 207,844              |
| Deferred revenue                  | 4,510                | 428,520                   | -                         | 433,030              |
| Notes payable                     | 19,591,799           | 610,806                   | -                         | 20,202,605           |
| Deferred compensation             | 15,513               | -                         | -                         | 15,513               |
|                                   | <u>20,637,398</u>    | <u>1,097,629</u>          | <u>-</u>                  | <u>21,735,027</u>    |
| <u>Other Liabilities</u>          |                      |                           |                           |                      |
| Equity equivalent                 | 2,000,000            | -                         | -                         | 2,000,000            |
|                                   | <u>22,637,398</u>    | <u>1,097,629</u>          | <u>-</u>                  | <u>23,735,027</u>    |
| <u>Net Assets</u>                 |                      |                           |                           |                      |
| Net assets                        | 7,106,188            | 11,206,105                | 231,134                   | 18,543,427           |
| Net assets, board restricted      | 600,000              | -                         | -                         | 600,000              |
|                                   | <u>7,706,188</u>     | <u>11,206,105</u>         | <u>231,134</u>            | <u>19,143,427</u>    |
| Total Liabilities and Net Assets  | <u>\$ 30,343,586</u> | <u>\$ 12,303,734</u>      | <u>\$ 231,134</u>         | <u>\$ 42,878,454</u> |

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.  
STATEMENT OF ACTIVITIES  
YEAR ENDING JUNE 30, 2011

|                                       | <u>Unrestricted</u> | <u>Temporarily<br/>Restricted</u> | <u>Permanently<br/>Restricted</u> | <u>Total</u>         |
|---------------------------------------|---------------------|-----------------------------------|-----------------------------------|----------------------|
| <u>Revenue</u>                        |                     |                                   |                                   |                      |
| Mortgage and note interest            | \$ 970,913          | \$ 55,103                         | \$ -                              | \$ 1,026,016         |
| Contributions, grants                 | 15,660              | 135,000                           | -                                 | 150,660              |
| State grants                          | 105,000             | -                                 | -                                 | 105,000              |
| Pass-through grants                   | 1,184,323           | 24,000                            | -                                 | 1,208,323            |
| Federal grants                        | 985,000             | -                                 | 130,000                           | 1,115,000            |
| Rental income                         | 23,550              | -                                 | -                                 | 23,550               |
| Investment income                     | 142,244             | 6,540                             | -                                 | 148,784              |
| Administration income                 | 27,800              | (8,160)                           | -                                 | 19,640               |
| Gain on acquisition of assets         | 1,060,802           | 14,394                            | -                                 | 1,075,196            |
| Fees and service charges              | 917,683             | 1,658                             | -                                 | 919,341              |
| Miscellaneous income                  | 4,820               | -                                 | -                                 | 4,820                |
| Net assets released from restrictions |                     |                                   |                                   |                      |
| Satisfaction of program restrictions  | 588,254             | (588,254)                         | -                                 | -                    |
| Total Revenue                         | <u>6,026,049</u>    | <u>(359,719)</u>                  | <u>130,000</u>                    | <u>5,796,330</u>     |
| <u>Expenses</u>                       |                     |                                   |                                   |                      |
| Program services                      | 3,106,388           | -                                 | -                                 | 3,106,388            |
| General and administrative            | 1,690,241           | -                                 | -                                 | 1,690,241            |
| Fundraising                           | 264,957             | -                                 | -                                 | 264,957              |
| Membership                            | 420,276             | -                                 | -                                 | 420,276              |
| Total Expenses                        | <u>5,481,862</u>    | <u>-</u>                          | <u>-</u>                          | <u>5,481,862</u>     |
| Increase(decrease) in net assets      | 544,187             | (359,719)                         | 130,000                           | 314,468              |
| Net Assets at Beginning of Period     | <u>7,706,188</u>    | <u>11,206,105</u>                 | <u>231,134</u>                    | <u>19,143,427</u>    |
| Net Assets at End of Period           | <u>\$ 8,250,375</u> | <u>\$ 10,846,386</u>              | <u>\$ 361,134</u>                 | <u>\$ 19,457,895</u> |

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

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.  
STATEMENT OF ACTIVITIES  
YEAR ENDING JUNE 30, 2010

|                                       | Unrestricted     | Temporarily<br>Restricted | Permanently<br>Restricted | Total            |
|---------------------------------------|------------------|---------------------------|---------------------------|------------------|
| <u>Revenue</u>                        |                  |                           |                           |                  |
| Mortgage and note interest            | \$ 783,420       | \$ 67,211                 | \$ -                      | \$ 850,631       |
| Contributions, grants                 | 851,850          | 572,500                   | -                         | 1,424,350        |
| State grants                          | 52,251           | 68,349                    | -                         | 120,600          |
| Pass-through grants                   | 555,804          | 39,652                    | -                         | 595,456          |
| Federal grants                        | 440,000          | -                         | 92,500                    | 532,500          |
| Rental income                         | 2,700            | 400                       | -                         | 3,100            |
| Investment income                     | 96,867           | 5,250                     | -                         | 102,117          |
| Administration income                 | 52,130           | 10,000                    | -                         | 62,130           |
| Gain(Loss) on sale of property        | 293,144          | -                         | -                         | 293,144          |
| Fees and service charges              | 1,005,920        | 1,732                     | -                         | 1,007,652        |
| Miscellaneous income                  | 1,269            | -                         | -                         | 1,269            |
| Net assets released from restrictions |                  |                           |                           |                  |
| Satisfaction of program restrictions  | 328,252          | (285,764)                 | (42,488)                  | -                |
| <b>Total Revenue</b>                  | <b>4,463,607</b> | <b>479,330</b>            | <b>50,012</b>             | <b>4,992,949</b> |
| <u>Expenses</u>                       |                  |                           |                           |                  |
| Program services                      | 2,708,334        | -                         | -                         | 2,708,334        |
| General and administrative            | 1,530,798        | -                         | -                         | 1,530,798        |
| Fundraising                           | 166,818          | -                         | -                         | 166,818          |
| Membership                            | 304,197          | -                         | -                         | 304,197          |
| <b>Total Expenses</b>                 | <b>4,710,147</b> | <b>-</b>                  | <b>-</b>                  | <b>4,710,147</b> |
| Increase(decrease) in net assets      | (246,540)        | 479,330                   | 50,012                    | 282,802          |
| Extraordinary Gain                    | 250,000          | -                         | -                         | 250,000          |
| Net Assets at Beginning of Period     | 7,702,728        | 10,726,775                | 181,122                   | 18,610,625       |
| Net Assets End of Period              | \$ 7,706,188     | \$ 11,206,105             | \$ 231,134                | \$ 19,143,427    |

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, 2011 AND 2010

|  | <u>2011</u>         | <u>2010</u>         |
|--|---------------------|---------------------|
| <b>CASH FLOWS FROM OPERATING ACTIVITIES</b>  |                     |                     |
| Changes in Net Assets  | \$ 314,468          | \$ 532,802          |
| Adjustments to reconcile increase in net assets to net cash provided by operating activities |                     |                     |
| Depreciation and amortization  | 86,212              | 71,737              |
| (Gain)Loss on disposal of assets   | 70,870              | 92,964              |
| (Increase)decrease in operating assets   |                     |                     |
| Accounts receivable  | 774,640             | (524,072)           |
| Grants receivable  | 537,500             | 1,562,500           |
| Accrued interest receivable  | (28,820)            | (29,459)            |
| Prepaid expenses   | (7,349)             | (37,003)            |
| Deferred compensation  | (5,489)             | (10,763)            |
| Deposits   | 300                 | 150,000             |
| Increase(decrease) in operating liabilities  |                     |                     |
| Accounts payable   | (249,952)           | 119,436             |
| Payroll taxes payable  | (3,588)             | 4,101               |
| Client advances and deposits   | (31,400)            | 84,430              |
| Accrued interest payable   | 6,328               | (21,197)            |
| Compensated absences payable   | 17,929              | 64,159              |
| Deferred revenue   | 117,886             | 111,237             |
| Deferred compensation  | 5,487               | 10,763              |
| <b>NET CASH PROVIDED BY OPERATING ACTIVITIES</b>   | <u>1,605,022</u>    | <u>2,181,635</u>    |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES</b>  |                     |                     |
| Purchase of property and equipment   | (702,881)           | (1,339,892)         |
| Proceeds from sale of property and equipment   | 355,554             | 321,910             |
| Payments received on notes receivable  | 14,269,031          | (11,343,263)        |
| Disbursement of loans receivable funds   | (18,156,180)        | 11,750,163          |
| <b>NET CASH USED BY INVESTING ACTIVITIES</b>   | <u>(4,234,476)</u>  | <u>(611,082)</u>    |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES</b>  |                     |                     |
| Proceeds from long-term debt borrowings  | 5,053,741           | 4,977,034           |
| Payments on long-term debt   | (3,173,943)         | (4,279,880)         |
| <b>NET CASH PROVIDED BY FINANCING ACTIVITIES</b>   | <u>1,879,798</u>    | <u>697,154</u>      |
| <b>NET INCREASE IN CASH</b>  | (749,656)           | 2,267,707           |
| <b>CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR</b>  | <u>6,673,988</u>    | <u>4,406,281</u>    |
| <b>CASH AND CASH EQUIVALENTS AT END OF YEAR</b>  | <u>\$ 5,924,332</u> | <u>\$ 6,673,988</u> |
| <b>SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION</b>                                      |                     |                     |
| Cash paid during the year for:   |                     |                     |
| Interest   | <u>\$ 530,191</u>   | <u>\$ 546,810</u>   |



FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.  
NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2011 AND 2010

**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 47 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 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 four 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.

Third, FAHE developed a direct origination mortgage program in 2007. The program, JustChoice Lending, provides access directly for customers at the Berea 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.

Additionally, in fiscal year 2011 FAHE established FAHE TN, LLC. This entity domiciled in Tennessee provides for greater access to funds that would not normally be provided under the current organizational structure.

In fiscal year 2010 FAHE achieved a \$25 million set aside of USDA 502 funds, which also resulted in a national demonstration between USDA and nonprofits. In addition, a pipeline of \$15 million exists in NSP funds, \$15 million in TCAP and Exchange, and \$5 million in other ARRA projects. Also, in fiscal year 2011 FAHE

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.  
NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2011 AND 2010

**Note 1 – Organization (Continued)**

became a member of the Federal Home Loan Bank Cincinnati Division. This will allow access to additional resources for FAHE's membership.

**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, FAHE Consulting, LLC and FAHE TN, 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 Statements 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/Wells Fargo 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 Statements of Financial Position. Unrealized gains and losses are included in the change in net assets in the accompanying Statements 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.

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.  
NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2011 AND 2010

**Note 2 – Summary of Significant Accounting Policies (Continued)**

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.

**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 years ended June 30, 2011 and 2010, depreciation expense was \$81,191 and \$64,413, respectively. The increase in depreciation is primarily related to the purchase of new loan servicing software which was placed in service in May of 2010 with fiscal year 2011 reflecting the first full year of depreciation.

The Organization amortizes leasehold improvements over the shorter of the term of the lease or the economic life of the asset purchased. FAHE moved the Capital and Consulting operations from the Abney building to the Peoples Bank Building in June 2010. These improvements are being amortized over the term of the lease which is two years.

Amortization expense for the years ended June 30, 2011 and 2010 was \$5,021 and \$7,324, 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).

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.  
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**Note 2 – Summary of Significant Accounting Policies (Continued)**

The Organization is not aware of any unrelated business income as of September 15, 2011. In Accounting Standards Codification (ASC) 740-10-50, *Income Taxes*, (formerly FIN 48, *Accounting for Uncertainty in Income Taxes*) the Financial Accounting Standards Board (FASB) requires entities to disclose known or anticipated positions of income tax uncertainty. The Organization is not aware of any uncertain tax positions that would require adjustment to the financial statements. The Organization files income tax returns in the U.S. federal jurisdiction. Generally, the Organization is no longer subject to income tax examination by the U.S. federal, state or local tax authorities for years before 2008.

**Compensated Absences**

The Organization revised human resource policies regarding employee vacation and sick time beginning calendar year 2010. Previously upon separation of service employees could be paid up to a maximum of 80 accrued sick hours and 160 accrued vacation hours. As of January 1, 2010 employees will not receive pay for accrued sick time upon separation of service with the exception of sick hours earned and not spent as of December 31, 2009. However, accrued vacation time can now be paid out up to a maximum of 352 hours. The employee earns accrued time 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.

**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 statements of activities and detailed in the statements of functional expenses. Accordingly, certain costs have been allocated among the programs and supporting services benefited.

**Note 3 – Investments and Fair Value Measurements**

Investments held by the Organization consisted of the following as of June 30, 2011:

|                                | <u>Cost</u>      | <u>Market Value</u> | <u>Unrealized<br/>Appreciation</u> |
|--------------------------------|------------------|---------------------|------------------------------------|
| FHLB stock                     | \$ 71,300        | \$ 71,300           | \$ -                               |
| Balance, June 30, 2011         | <u>\$ 71,300</u> | <u>\$ 71,300</u>    | -                                  |
| Balance, June 30, 2010         | <u>\$ -</u>      | <u>\$ -</u>         | -                                  |
| Unrealized loss on investments |                  |                     | <u>\$ -</u>                        |

The Organization has categorized its financial instruments, based on the priority of the inputs to the valuation technique, into a three-level fair value hierarchy. The hierarchy gives the highest priority to unadjusted quoted prices in an active market for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). If the inputs used to measure the financial instruments fall within different levels of

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.  
 NOTES TO FINANCIAL STATEMENTS  
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**Note 3 – Investments and Fair Value Measurements (Continued)**

the hierarchy, the categorization is based on the lowest level input that is significant to the fair value measurement of the instrument. Financial assets and liabilities recorded on the statement of financial position are categorized based on the inputs to the valuation techniques as follows:

*Level 1* – Financial assets and liabilities whose values are based on unadjusted quoted prices for identical assets or liabilities in an active market that the Organization has the ability to access.

*Level 2* – Financial assets and liabilities whose values are based on quoted prices in markets that are not active or model inputs that are observable wither directly or indirectly for substantially the full term of the asset or liability. Level 2 inputs include the following:

- quoted prices for similar assets or liabilities in active markets;
- quoted prices for identical or similar assets or liabilities in non-active markets;
- pricing models whose inputs are observable for substantially the full term of the asset or liability; and
- pricing models whose inputs are derived principally from or corroborated by observable market data through correlation or other means for substantially the full term of the asset or liability.

*Level 3* – Financial assets and liabilities whose values are based on prices or valuation techniques that require inputs that are both unobservable and significant to the overall fair value measurement.

The Organization’s fair value of securities available for sale measured on a recurring basis at June 30, 2011 is as follows:

|            | <u>Fair Value Measurements at Reporting Date Using</u> |   |  |  |
|------------|--|---|--|--|
|            | <u>Fair Value</u>                                      | <u>Quoted Prices<br/>in Active Markets<br/>for Identical<br/>Assets/Liabilities<br/>(Level 1)</u> | <u>Significant<br/>Other<br/>Observable<br/>Inputs<br/>(Level 2)</u> | <u>Significant<br/>Unobservable<br/>Inputs<br/>(Level 3)</u> |
| FHLB Stock | <u>\$ 71,300</u>                                       | <u>\$ -</u>   | <u>\$ 71,300</u>   | <u>\$ -</u>  |

Investments are included in the following items in the statement of financial position as of June 30, 2011:

|             |                  |
|-------------|------------------|
| Investments | <u>\$ 71,300</u> |
|-------------|------------------|

Fair value for investments are determined by reference to quoted market prices and other relevant information generated by market transactions. There have been no changes in valuation techniques and related inputs.

**Note 4 – Grant Funds Receivable**

Unconditional promises to give amounted to \$537,000 as of June 30, 2010. Those funds were received in fiscal year 2011.

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.  
NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2011 AND 2010

**Note 5 – Property Held for Resale**

Property held for resale consists of foreclosure properties (REO), properties owned by default, death or abandonment for which title has not yet passed (Conveyances) 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. Conveyances are recorded at book value less an adjustment of 25% to allowance for loan loss. FAHE has adopted a conservative approach to the valuation of Conveyances lacking an appraisal. Gains or losses from the sale of properties are recorded in the statements of activities as either gains or losses on disposal of property. At June 30, 2011 and 2010, the organization held \$904,159 and \$740,639, respectively in REO property. At June 30, 2011, the organization held \$472,863 in conveyances. The organization held no conveyances at June 30, 2010. At June 30, 2011 and 2010, the organization held \$170,094 and \$486,094 respectively, in investment property.

**Note 6 – 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 Organizations various lending portfolios. Loans are made in accordance with the restrictions imposed by the various funding sources.

At June 30, 2011 delinquencies were as follows: \$315,272 or 0.85% for 30-59 days; \$228,046 or 0.62% for 60-89 days; \$208,227 or 0.56% for loans 90+ days; \$133,227 or 0.36% for loans in foreclosure. Overall, loan delinquencies were \$751,545 or 2.03% on total loans of \$36,994,972 at June 30, 2011.

At June 30, 2010 delinquencies were as follows: \$250,643 or 0.76% for 30-59 days; \$167,495 or 0.51% for 60-89 days; \$370,446 or 1.11% for loans 90+ days; \$357,789 or 1.08% for loans in foreclosure. Overall, loan delinquencies were \$788,584 or 2.37% on total loans of \$33,246,514 at June 30, 2010.

Mortgage notes receivable as of June 30, 2011 consist of the following balances in each fund:

|   |                             |
|---|-----------------------------|
| Kentucky Home Loan Fund                     | \$ 3,745,053                |
| AHTF Fund                                   | 401,374                     |
| HOME Program of Kentucky                    | 7,122,471                   |
| Virginia Home Loan Fund                     | 5,310,938                   |
| NHPR Kentucky                               | 166,606                     |
| HOME Program of Virginia                    | 2,210,661                   |
| West Virginia Home Loan Fund                | 1,266,622                   |
| Tennessee Home Loan Fund                    | 1,054,437                   |
| Chase/NHSA                                  | <u>962,823</u>              |
| Total                                       | 22,240,985                  |
| Less: Allowance for Loan Losses             | <u>(403,958)</u>            |
| Mortgage Notes Receivable, Net of Allowance | <u><u>\$ 21,837,027</u></u> |

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.  
NOTES TO FINANCIAL STATEMENTS  
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**Note 6 – Mortgage Notes Receivable (Continued)**

Mortgage notes receivable as of June 30, 2010 consist of the following balances in each fund:

|   |                             |
|---|-----------------------------|
| Kentucky Home Loan Fund                     | \$ 2,684,364                |
| AHTF Fund                                   | 394,173                     |
| HOME Program of Kentucky                    | 7,583,191                   |
| Virginia Home Loan Fund                     | 5,547,664                   |
| NHPR Kentucky                               | 211,644                     |
| HOME Program of Virginia                    | 2,278,249                   |
| West Virginia Home Loan Fund                | 1,260,091                   |
| Tennessee Home Loan Fund                    | 1,035,490                   |
| Neighborhood Stabilization Program          | <u>114,100</u>              |
| Total                                       | 21,108,966                  |
| Less: Allowance for Loan Losses             | <u>(452,055)</u>            |
| Mortgage Notes Receivable, Net of Allowance | <u><u>\$ 20,656,911</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, 2011, is \$600,000. This provides an 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.

**Note 7 – 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 community loan portfolio as of June 30, 2011 and 2010 are presented below:

|  | <u>2011</u> | <u>2010</u> |
|--|-------------|-------------|
| Appalachia Habitat For Humanity          | \$ 328,764  | \$ 273,993  |
| Appalachia Service Project               | 42,261      | 51,219      |
| Beattyville Housing Development          | 306,843     | 384,438     |
| Beattyville School                       | 4,716       | 426,528     |
| Blueberry Hill Estates                   | 75,000      | 75,000      |
| Cambria House                            | 39,449      | 40,501      |
| Clinch Valley Community                  | 77,937      | 93,735      |
| COAP                                     | 143,951     | 460,202     |
| Community Housing Partners               | 1,999,034   | 2,802,242   |
| Eastern Eight CDC                        | 988,019     | 1,078,228   |
| Frontier Housing, Inc.                   | 1,371,079   | 1,302,984   |
| Green Acres Development                  | 60,783      | 64,000      |
| Hazard/Perry County Community Ministries | 27,525      | 29,782      |
| Highland Community Builders, Inc.        | 36,346      | -           |
| Homeownership Center                     | 44,935      | 112,250     |
| HOMES, Inc.                              | 1,009,241   | 1,084,810   |
| HOPE Inc.                                | 392,294     | 213,952     |

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.  
NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2011 AND 2010

**Note 7 – Notes Receivable (Continued)**

|                                       | <u>2011</u>          | <u>2010</u>          |
|---------------------------------------|----------------------|----------------------|
| Housing Authority of Mingo County     | 200,640              | -                    |
| Housing Development Alliance          | 308,367              | 349,151              |
| Housing Equity Fund of KY I           | 999,820              | 805,020              |
| Housing Equity Fund of KY II          | 1,758,245            | 56,300               |
| Housing Equity Fund of VA XII         | 776,837              | -                    |
| Irvine Renaissance, LLP               | 270,418              | 285,300              |
| KDVA Homes 07, LLP                    | 1,309,322            | 264,658              |
| Knox Housing Partners, Inc.           | 254,594              | 13,714               |
| Kentucky Mountain Health Alliance     | 323,905              | 323,905              |
| Kentucky Mountain Housing Corporation | 487,513              | 492,763              |
| Lil' Britches Child Care Center       | 64,275               | 67,283               |
| Mountain Cap, Inc.                    | 229,866              | 233,571              |
| People Inc. Financial Services        | 99,896               | 99,900               |
| Randolph County Housing Authority     | 436,996              | 295,847              |
| Safe Housing & Economic Development   | 210,520              | 220,762              |
| Southern Appalachian Labor School     | 90,988               | 95,164               |
| Sterling Housing, Inc.                | 42,422               | 42,422               |
| The Housing Partnership, Inc.         | 82,350               | -                    |
| Virginia Community Development Fund   | 5,836                | 6,232                |
|                                       | <hr/>                | <hr/>                |
| Total Notes Receivable                | 14,900,987           | 12,145,856           |
| Less: Allowance for Loan Loss         | (506,309)            | (387,342)            |
|                                       | <hr/>                | <hr/>                |
| Notes Receivable, Net of Allowance    | <u>\$ 14,394,678</u> | <u>\$ 11,758,514</u> |

**Note 8 – Notes Payable**

Notes payable at June 30, 2011 and 2010 consists of notes payable to governmental agencies, banks, non-profit organizations and individuals as detailed below.

|                               | Rate  | Term     | Maturity          | Balance     |             |
|-------------------------------|-------|----------|-------------------|-------------|-------------|
|                               |       |          |                   | <u>2011</u> | <u>2010</u> |
| Kentucky Housing Corporation: |       |          |                   |             |             |
| Kentucky Home Loan Fund/AHTF  |       |          |                   |             |             |
| Special Contract #2           | 1.00% | 20 Years | January 1, 2012   | \$ 9,500    | \$ 19,000   |
| Special Contract #3           | 1.00% | 20 Years | February 1, 2013  | 27,800      | 41,700      |
| Special Contract #4           | 1.00% | 20 Years | July 1, 2013      | 61,500      | 82,000      |
| Special Contract #5           | 1.00% | 20 Years | July 1, 2014      | 82,000      | 102,500     |
| Special Contract #6           | 1.00% | 20 Years | July 1, 2015      | 103,750     | 124,500     |
| Special Contract #7           | 1.00% | 20 Years | July 1, 2016      | 126,019     | 147,022     |
| Special Contract #8           | 3.00% | 20 Years | October 1, 2035   | 443,851     | 455,755     |
| Affordable Housing Trust Fund | 1.00% | 30 Years | July 1, 2033      | 52,313      | 54,327      |
| Affordable Housing Trust Fund | 1.00% | 30 Years | September 1, 2035 | 3,973       | 5,783       |



FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.  
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**Note 8 – Notes Payable (Continued)**

|   | Rate  | Term     | Maturity           | Balance      | Balance      |
|---|-------|----------|--------------------|--------------|--------------|
|   |       |          |                    | 2011         | 2010         |
| Kentucky Housing Corporation:           |       |          |                    |              |              |
| NHPL, NHRL, NHPR                        |       |          |                    |              |              |
| NHPL 1998-1999                          | 1.00% | 20 Years | July 1, 2018       | -            | 262,307      |
| NHPL 1999-2000                          | 1.00% | 20 Years | July 1, 2019       | 243,324      | 293,640      |
| NHPR 2000-2001                          | 1.00% | 20 Years | July 1, 2020       | 316,125      | 347,738      |
| NHPR 2001-2002                          | 1.00% | 20 Years | July 1, 2022       | 294,113      | 320,850      |
| NHPR 2002-2003                          | 1.00% | 20 Years | July 1, 2023       | 403,551      | 437,114      |
| NHPR 2003-2004                          | 1.00% | 20 Years | July 1, 2024       | 394,388      | 424,725      |
| NHPR 2004-2005                          | 1.00% | 20 Years | July 1, 2025       | 324,450      | 347,625      |
| NHPR 2005-2006                          | 1.00% | 20 Years | July 1, 2026       | 305,000      | 317,200      |
| NHPR 2006-2007                          | 1.00% | 20 Years | November 1, 2027   | 139,200      | 147,900      |
| NHPR 2007-2008                          | 1.00% | 20 Years | September 1, 2028  | 210,100      | 222,457      |
| NHPR 2009                               | 1.00% | 20 Years | February 1, 2030   | 232,381      | 244,423      |
| Virginia Housing Development Authority: |       |          |                    |              |              |
| Housing Fund #1                         | 3.00% | 30 Years | July 5, 2028       | 74,430       | 138,306      |
| VHPRF Phase I & II                      | 3.00% | 20 Years | November 5, 2026   | 149,779      | 165,010      |
| Housing Fund #2                         | 3.00% | 30 Years | December 5, 2018   | 238,625      | 246,336      |
| Housing Fund #3                         | 2.00% | 30 Years | March 1, 2014      | 537,707      | 555,781      |
| 2004 Line of Credit                     | 2.00% | 30 Years | September 1, 2026  | 748,298      | 771,654      |
| 2005 Line of Credit                     | 2.00% | 30 Years | February 1, 2037   | 779,828      | 803,022      |
| 2007 Reach                              | 3.00% | 30 Years | April 1, 2038      | 663,048      | 679,064      |
| 2009 Reach                              | 3.00% | 30 Years | May 1, 2039        | 283,604      | 290,087      |
| 2010 Reach                              | 3.00% | 30 Years | July 1, 2040       | 527,589      | 312,610      |
| Wachovia/Wells Fargo Bank               |       |          |                    |              |              |
| Five Year Note                          | 0.81% | 5 Years  | July 31, 2011      | 3,550,000    | 1,050,000    |
| Various Lenders                         |       |          |                    |              |              |
| Sisters of Loretto                      | 3.00% | 3 Years  | June 30, 2012      | 50,000       | 50,000       |
| Richard Hettrick                        | 3.00% | 3 Years  | January 31, 2013   | 5,500        | 5,500        |
| Opportunity Finance Network             | 4.00% | 5 Years  | October 31, 2012   | 500,000      | 500,000      |
| Andrew Schenker                         | 3.00% | 5 Years  | June 1, 2013       | 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  | November 1, 2014   | 50,000       | 50,000       |
| F. B. Heron Foundation                  | 3.00% | 6 Years  | September 30, 2016 | 500,000      | 300,000      |
| Tides Foundation                        | 0.00% | 5 Years  | July 13, 2012      | 75,000       | 75,000       |
| Ethel Ackley                            | 3.00% | 3 Years  | July 13, 2010      | -            | 5,000        |
| 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 31, 2012    | 5,000        | 5,000        |
| Trust U/AGR D3/1/84, Fay Chandler       | 3.00% | 3 Years  | December 31, 2012  | 25,000       | 25,000       |
| Trust U/AGR D3/1/84, Fay Chandler       | 3.00% | 3 Years  | March 21, 2013     | 50,000       | 50,000       |
| Glenmary Home Missioners                | 2.00% | 3 Years  | September 30, 2013 | 25,000       | 25,000       |
| Seton Enablement Fund                   | 3.00% | 5 Years  | June 1, 2013       | 41,795       | 61,777       |
| The Ford Foundation                     | 1.00% | 10 Years | June 2, 2014       | 1,000,000    | 1,000,000    |
| Stookey Trust                           | 3.00% | 5 Years  | September 30, 2010 | -            | 25,000       |
| U.S. Department of Agriculture          | 1.00% | 30 Years | October 16, 2031   | 584,892      | 610,806      |
| 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    | 2,000,000    |
| Kentucky Housing Corporation            | 3.00% | 23 Years | July 1, 2016       | 240,889      | 253,428      |
| Peoples Self Help Housing               | 2.50% | 2 Years  | January 5, 2013    | 500,000      | 500,000      |
| Dominican Sisters of Peace              | 3.00% | 3 Years  | July 1, 2012       | 20,000       | 20,000       |
| CDFI Fund                               | 1.25% | 20 Years | September 10, 2019 | 930,000      | 930,000      |
| Domestic Foreign Missionary Society     | 3.50% | 5 Years  | September 30, 2014 | 350,000      | 350,000      |
| Calvert Social Investment Foundation    | 4.50% | 3 Years  | June 30, 2013      | 200,000      | 1,000,000    |
| Opportunity Finance Network             | 3.00% | 10 Years | November 30, 2019  | 2,500,000    | 2,500,000    |
| Seton Enablement Fund                   | 3.00% | 5 Years  | October 1, 2014    | 71,547       | 90,658       |
| Mercy Investment Services               | 2.00% | 5 Years  | July 15, 2015      | 300,000      | -            |
| Episcopal, Diocese of Iowa              | 2.50% | 3 Years  | March 31, 2014     | 25,000       | -            |
| Stookey, Byron                          | 3.00% | 5 Years  | September 30, 2015 | 25,000       | -            |
| Stookey, Lee                            | 3.00% | 5 Years  | November 15, 2015  | 25,000       | -            |
| NHPR CLF Fund                           | 1.00% | 20 Years | December 1, 2030   | 296,533      | -            |
| Total Notes Payable                     |       |          |                    | \$22,082,402 | \$20,202,605 |

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.  
NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2011 AND 2010

**Note 8 – Notes Payable (Continued)**

The principal repayment requirements at June 30, 2011 and 2010 relating to the above notes payable are as follows:

|             | <u>2011</u>          | <u>2010</u>          |
|-------------|----------------------|----------------------|
| 2011        | \$ -                 | \$ 1,930,000         |
| 2012        | 5,944,500            | 2,404,000            |
| 2013        | 1,433,300            | 1,783,977            |
| 2014        | 1,691,002            | 1,637,781            |
| 2015        | 553,547              | 593,158              |
| 2016        | 453,750              | -                    |
| Later Years | <u>12,006,303</u>    | <u>11,853,689</u>    |
| Totals      | <u>\$ 22,082,402</u> | <u>\$ 20,202,605</u> |

At June 30, 2011 and 2010 approximately \$12.029 million and \$5.998 million notes payable, respectively, are unsecured and represent private investments by individuals and groups.

At June 30, 2011 and 2010, respectively the Organization has a \$4.5 million line of credit with Wachovia/Wells Fargo Bank secured by \$4.8 million in commercial loan assets in 2011; a \$2.0 million line of credit with Fannie Mae backed by an unsecured letter of credit with Peoples Bank for \$450,000; a \$1.0 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, 2011 the organization had available balances on lines of credit with Wachovia/Wells Fargo Bank of \$950,000, Central Bank of \$500,000, and capacity to drawn down another \$1.8 million on the Calvert Social Investment Foundation loan of \$2.0 million.

**Note 9 - Other Liabilities**

The Organization carries a \$2,000,000, ten year note with Wachovia/Wells Fargo Bank classified as EQ2 funds. This note is shown under Other Liabilities on the statements of financial position 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 of 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, 2011 and 2010, respectively.

As of June 30, 2011, FAHE's unrestricted net assets to total assets ratio was 18.3%. If EQ2 funds are included as unrestricted net assets, then the modified ratio of unrestricted net assets to total assets is 22.7%.

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.  
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JUNE 30, 2011 AND 2010

**Note 10 – 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 \$16,503,802 and \$15,128,774 as of June 30, 2011 and 2010, respectively. To further clarify, of the \$16,503,802 balance, FAHE is the first guarantor on the original \$1,481,598 and takes the position of second guarantor on the remaining member loan agreements.

**Note 11 – 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 various financial institutions. The cash accounts are primarily non-interest bearing and thus are fully insured by the Federal Deposit Insurance Corporation. Interest bearing accounts are insured up to \$250,000. The Organization manages the cash position to mitigate and or eliminate any associated risk. The Organization provides mortgage loans primarily to low- and moderate-income individuals. Mortgage notes totaling \$22,240,985 and \$21,108,966 at June 30, 2011 and 2010, respectively, are secured by the property purchased or improved except as noted. At June 30, 2011 notes totaling \$219,450 were deed restricted only. 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 \$14,900,987 and \$12,145,856 at June 30, 2011 and 2010, respectively, are secured by the assets of the Organization with the exception of the unsecured amount as noted. At June 30, 2011 and 2010, \$5,836 and \$922,363 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. These reserves may be found in the following balance sheet accounts: Mortgage Notes Receivable, Notes Receivable (netted against total loans) and Board Designated Net Assets. See notes 5 and 6 for additional information.

**Note 12 – Subsequent Events**

Management of the Organization has considered subsequent events through September 15, 2011, 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, 2011

| <u>Federal Grantor/Pass-Through Grantor/Program Title</u> | <u>Federal<br/>CFDA<br/>Number</u> | <u>Pass-Through<br/>Grantor's<br/>Number</u> | <u>Expenditures</u> |
|---|------------------------------------|--|---------------------|
| <u>Department of Treasury</u>                             |                                    |  |                     |
| NeighborWorks America                                     | 21.000                             |  | 365,000             |
| Community Development Financial Institutions              | 21.020                             | *  | 750,000             |
| <u>Department of Housing &amp; Urban Development</u>      |                                    |  |                     |
| <u>Passed through Kentucky Housing Corporation</u>        |                                    |  |                     |
| Home Investment Partnership Program (HOME)                | 14.239                             | HB09-0201-01                                 | 90,000              |
| Home Investment Partnership Program (HOME)                | 14.239                             | HB10-0201-01                                 | 15,000              |
| <u>Department of Housing &amp; Urban Development</u>      |                                    |  |                     |
| <u>Passed through Department for Local Government</u>     |                                    |  |                     |
| Neighborhood Stabilization Program                        | 14.228                             | 09N-045                                      | 306,095             |
| TOTAL FEDERAL AWARDS                                      |                                    |  | <u>\$ 1,526,095</u> |

\* 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, 2011

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 accrual 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 to 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 INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS  
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, 2011, and have issued our report thereon dated September 15, 2011. 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 *deficiency in internal control* 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 and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, 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 and Other Matters

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*.

This report is intended solely for the information and use 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, 2011

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 Federation of Appalachian Housing Enterprises, Inc. (a non-profit organization) with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on each of the organization's major federal programs for the year ended June 30, 2011. 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 could have a direct and material effect on each of its major federal programs for the year ended June 30, 2011.

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 the requirements that could have a direct and material effect on a major federal program to determine the auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an 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.



A *deficiency in internal control over compliance* exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A *material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis.

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

This report is intended solely for the information and use of management, the Board of Directors, 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, 2011



FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.  
SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
FOR THE YEAR ENDED JUNE 30, 2011

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:  
  
    NeighborWorks America CFDA #21.000 Type A.  
    Neighborhood Stabilization Program CFDA #14.228 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, 2011

| Expenses                       | Program Services         |                   |                   |                   |                       |                      |                   |                   |                   |                        |                     |
|--------------------------------|--------------------------|-------------------|-------------------|-------------------|-----------------------|----------------------|-------------------|-------------------|-------------------|------------------------|---------------------|
|                                | General & Administrative | Membership        | Fundraising       | Home Lending      | Community Development | Grant Administration | Loan Servicing    | FAHE Consulting   | FAHE Capital      | Total Program Services | Total               |
| Personnel Expenses             | \$ 647,327               | \$ 160,957        | \$ 101,473        | \$ 297,421        | \$ 87,477             | \$ 87,477            | \$ 297,421        | \$ 209,944        | \$ 209,944        | \$ 1,189,684           | \$ 2,099,441        |
| Travel Expenses                | 28,004                   | 6,963             | 4,391             | 12,867            | 3,784                 | 3,784                | 12,867            | 9,082             | 9,082             | 51,466                 | 90,824              |
| Board & Committee Meetings     | 5,693                    | 1,416             | 892               | 2,616             | 769                   | 769                  | 2,616             | 1,846             | 1,846             | 10,462                 | 18,463              |
| Conference & Workshops         | 6,227                    | 1,548             | 976               | 2,861             | 842                   | 842                  | 2,861             | 2,020             | 2,020             | 11,446                 | 20,197              |
| Occupancy Expense              | 30,928                   | 7,690             | 4,848             | 14,212            | 4,179                 | 4,179                | 14,210            | 10,031            | 10,031            | 56,842                 | 100,308             |
| Supplies & Publications        | 5,316                    | 1,322             | 833               | 2,442             | 718                   | 718                  | 2,443             | 1,724             | 1,724             | 9,769                  | 17,240              |
| Postage & Shipping             | 7,237                    | 1,800             | 1,134             | 3,325             | 978                   | 978                  | 3,326             | 2,347             | 2,347             | 13,301                 | 23,472              |
| Communications                 | 11,834                   | 2,942             | 1,855             | 5,437             | 1,599                 | 1,599                | 5,437             | 3,838             | 3,838             | 21,748                 | 38,379              |
| Equipment & Maintenance        | 19,141                   | 4,759             | 3,000             | 8,794             | 2,587                 | 2,587                | 8,794             | 6,208             | 6,208             | 35,178                 | 62,078              |
| Subscriptions                  | 1,741                    | 433               | 273               | 800               | 235                   | 235                  | 800               | 565               | 565               | 3,200                  | 5,647               |
| Licenses, Fees & Permits       | 1,310                    | 326               | 205               | 602               | 177                   | 177                  | 602               | 425               | 425               | 2,408                  | 4,249               |
| Employee Education             | 1,477                    | 367               | 232               | 679               | 200                   | 200                  | 679               | 479               | 479               | 2,716                  | 4,792               |
| Memberships                    | 5,643                    | 1,403             | 885               | 2,593             | 763                   | 763                  | 2,593             | 1,830             | 1,830             | 10,372                 | 18,303              |
| Marketing & Advertising        | 11,179                   | 2,780             | 1,752             | 5,136             | 1,511                 | 1,511                | 5,136             | 3,626             | 3,626             | 20,546                 | 36,257              |
| Liability & Property Insurance | 21,275                   | 5,290             | 3,335             | 9,775             | 2,875                 | 2,875                | 9,775             | 6,900             | 6,900             | 39,100                 | 69,000              |
| Service Charges                | 2,181                    | 542               | 342               | 1,002             | 295                   | 295                  | 1,002             | 707               | 707               | 4,008                  | 7,073               |
| Depreciation & Amortization    | 26,582                   | 6,610             | 4,167             | 12,213            | 3,592                 | 3,592                | 12,213            | 8,621             | 8,621             | 48,852                 | 86,211              |
| Organizational Expenses        | 286                      | 71                | 45                | 131               | 39                    | 39                   | 131               | 93                | 93                | 526                    | 928                 |
| Contributions                  | 9,645                    | 2,398             | 1,512             | 4,432             | 1,303                 | 1,303                | 4,432             | 3,128             | 3,128             | 17,726                 | 31,281              |
| Software Lease                 | 11,394                   | 2,833             | 1,786             | 5,235             | 1,540                 | 1,540                | 5,235             | 3,695             | 3,695             | 20,940                 | 36,953              |
| Professional Fees              | 38,245                   | 9,510             | 5,995             | 17,572            | 5,168                 | 5,168                | 17,572            | 12,404            | 12,404            | 70,288                 | 124,038             |
| Contract Services              | 65,714                   | 16,340            | 10,301            | 30,193            | 8,880                 | 8,880                | 30,193            | 21,313            | 21,313            | 120,772                | 213,127             |
| Loan Processing Expense        | 737                      | 183               | 115               | 338               | 100                   | 100                  | 338               | 239               | 239               | 1,354                  | 2,389               |
| Loan Servicing Expense         | 426                      | 106               | 67                | 196               | 58                    | 58                   | 196               | 138               | 138               | 784                    | 1,383               |
| Pass Thru Grants               | 329,005                  | 81,807            | 51,574            | 151,164           | 44,460                | 44,460               | 151,164           | 106,704           | 106,704           | 604,656                | 1,067,042           |
| Over/Short                     | 1,721                    | 428               | 270               | 791               | 233                   | 233                  | 791               | 558               | 558               | 3,164                  | 5,583               |
| Administration                 | 8,572                    | 2,131             | 1,344             | 3,938             | 1,158                 | 1,158                | 3,938             | 2,780             | 2,780             | 15,752                 | 27,799              |
| Bad Debt Expense               | 217,249                  | 54,019            | 34,055            | 99,817            | 29,358                | 29,358               | 99,817            | 70,459            | 70,459            | 399,268                | 704,591             |
| Interest Expense               | 165,427                  | 41,133            | 25,932            | 76,007            | 22,355                | 22,355               | 76,007            | 53,652            | 53,652            | 304,028                | 536,520             |
| Loans Forgiven                 | 6,705                    | 1,667             | 1,051             | 3,080             | 906                   | 906                  | 3,080             | 2,174             | 2,174             | 12,320                 | 21,743              |
| Miscellaneous Expense          | 2,020                    | 502               | 317               | 928               | 273                   | 273                  | 928               | 655               | 655               | 3,712                  | 6,551               |
| <b>Total Expenses</b>          | <b>\$ 1,690,241</b>      | <b>\$ 420,276</b> | <b>\$ 264,957</b> | <b>\$ 776,597</b> | <b>\$ 228,412</b>     | <b>\$ 228,412</b>    | <b>\$ 776,597</b> | <b>\$ 548,185</b> | <b>\$ 548,185</b> | <b>\$ 3,106,388</b>    | <b>\$ 5,481,862</b> |

See Independent Auditors' Report.

FEDERATION OF APPALACHIAN ENTERPRISES, INC.  
STATEMENT OF FUNCTIONAL EXPENSES  
FOR THE YEAR ENDED JUNE 30, 2010

| Expenses                       | Program Services         |                   |                   |                   |                       |                      |                   |                   |                   |                        |                     |
|--------------------------------|--------------------------|-------------------|-------------------|-------------------|-----------------------|----------------------|-------------------|-------------------|-------------------|------------------------|---------------------|
|                                | General & Administrative | Membership        | Fundraising       | Home Lending      | Community Development | Grant Administration | Loan Servicing    | FAHE Consulting   | FAHE Capital      | Total Program Services | Total               |
| Personnel Expenses             | \$ 654,437               | \$ 130,048        | \$ 71,317         | \$ 369,170        | \$ 192,975            | \$ 25,171            | \$ 302,048        | \$ 125,853        | \$ 142,633        | \$ 1,157,850           | \$ 2,013,652        |
| Travel Expenses                | 33,346                   | 6,626             | 3,634             | 18,810            | 9,833                 | 1,283                | 15,390            | 6,413             | 7,268             | 58,997                 | 102,603             |
| Board & Committee Meetings     | 4,101                    | 815               | 447               | 2,313             | 1,209                 | 158                  | 1,893             | 789               | 894               | 7,256                  | 12,619              |
| Conference & Workshops         | 5,484                    | 1,090             | 598               | 3,093             | 1,617                 | 211                  | 2,531             | 1,055             | 1,195             | 9,702                  | 16,874              |
| Occupancy Expense              | 27,129                   | 5,391             | 2,956             | 15,304            | 8,000                 | 1,043                | 12,521            | 5,217             | 5,913             | 47,998                 | 83,474              |
| Supplies & Publications        | 8,830                    | 1,755             | 962               | 4,981             | 2,604                 | 340                  | 4,075             | 1,698             | 1,924             | 15,622                 | 27,169              |
| Postage & Shipping             | 7,422                    | 1,475             | 809               | 4,187             | 2,189                 | 285                  | 3,426             | 1,427             | 1,618             | 13,132                 | 22,838              |
| Communications                 | 12,433                   | 2,471             | 1,355             | 7,013             | 3,666                 | 478                  | 5,738             | 2,391             | 2,710             | 21,996                 | 38,255              |
| Equipment & Maintenance        | 18,623                   | 3,701             | 2,029             | 10,505            | 5,491                 | 716                  | 8,595             | 3,581             | 4,059             | 32,947                 | 57,300              |
| Subscriptions                  | 1,406                    | 279               | 153               | 793               | 415                   | 54                   | 649               | 270               | 307               | 2,488                  | 4,326               |
| Licenses, Fees & Permits       | 1,449                    | 288               | 158               | 817               | 427                   | 56                   | 669               | 279               | 316               | 2,564                  | 4,459               |
| Employee Education             | 2,609                    | 518               | 284               | 1,472             | 769                   | 100                  | 1,204             | 502               | 569               | 4,616                  | 8,027               |
| Memberships                    | 6,105                    | 1,213             | 665               | 3,444             | 1,800                 | 235                  | 2,818             | 1,174             | 1,331             | 10,802                 | 18,785              |
| Marketing & Advertising        | 26,487                   | 5,263             | 2,886             | 14,942            | 7,810                 | 1,019                | 12,225            | 5,094             | 5,773             | 46,863                 | 81,499              |
| Liability & Property Insurance | 16,760                   | 3,331             | 1,826             | 9,454             | 4,942                 | 645                  | 7,735             | 3,223             | 3,653             | 29,652                 | 51,569              |
| Service Charges                | 4,730                    | 940               | 515               | 2,668             | 1,395                 | 182                  | 2,183             | 910               | 1,031             | 8,369                  | 14,554              |
| Depreciation & Amortization    | 23,314                   | 4,633             | 2,541             | 13,152            | 6,875                 | 897                  | 10,761            | 4,484             | 5,080             | 41,249                 | 71,737              |
| Organizational Expenses        | 437                      | 87                | 48                | 247               | 129                   | 17                   | 202               | 84                | 95                | 774                    | 1,346               |
| Contributions                  | 1,170                    | 233               | 128               | 660               | 345                   | 45                   | 540               | 225               | 255               | 2,070                  | 3,601               |
| Software Lease                 | 9,288                    | 1,846             | 1,012             | 5,240             | 2,739                 | 357                  | 4,287             | 1,786             | 2,024             | 16,433                 | 28,579              |
| Professional Fees              | 22,853                   | 4,541             | 2,490             | 12,891            | 6,739                 | 879                  | 10,548            | 4,395             | 4,981             | 40,433                 | 70,317              |
| Contract Services              | 77,257                   | 15,352            | 8,419             | 43,581            | 22,781                | 2,971                | 35,657            | 14,857            | 16,838            | 136,685                | 237,713             |
| Loan Processing Expense        | 593                      | 118               | 65                | 335               | 175                   | 23                   | 274               | 114               | 129               | 1,050                  | 1,826               |
| Loan Servicing Expense         | 780                      | 155               | 85                | 440               | 230                   | 30                   | 360               | 150               | 170               | 1,380                  | 2,400               |
| Pass Thru Grants               | 247,666                  | 49,216            | 26,989            | 139,709           | 73,030                | 9,526                | 114,308           | 47,628            | 53,979            | 438,180                | 762,051             |
| Over/Short                     | 2,145                    | 426               | 234               | 1,210             | 633                   | 83                   | 990               | 413               | 468               | 3,797                  | 6,602               |
| Administration                 | 9,464                    | 1,881             | 1,031             | 5,339             | 2,791                 | 364                  | 4,368             | 1,820             | 2,063             | 16,745                 | 29,121              |
| Bad Debt Expense               | 132,394                  | 26,309            | 14,428            | 74,684            | 39,039                | 5,092                | 61,105            | 25,460            | 28,855            | 234,235                | 407,366             |
| Interest Expense               | 170,824                  | 33,946            | 18,615            | 96,362            | 50,371                | 6,570                | 78,842            | 32,851            | 37,231            | 302,227                | 525,612             |
| Loans Forgiven                 | 912                      | 181               | 99                | 514               | 269                   | 35                   | 421               | 175               | 199               | 1,613                  | 2,805               |
| Miscellaneous Expense          | 350                      | 69                | 40                | 196               | 101                   | 12                   | 159               | 66                | 75                | 609                    | 1,068               |
| <b>Total Expenses</b>          | <b>\$ 1,530,798</b>      | <b>\$ 304,197</b> | <b>\$ 166,818</b> | <b>\$ 863,526</b> | <b>\$ 451,389</b>     | <b>\$ 58,877</b>     | <b>\$ 706,522</b> | <b>\$ 294,384</b> | <b>\$ 333,636</b> | <b>\$ 2,708,334</b>    | <b>\$ 4,710,147</b> |

See Independent Auditors' Report.

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.  
 STATEMENTS OF FINANCIAL POSITION - NEIGHBORWORKS AMERICA CAPITAL FUND  
 JUNE 30, 2011 AND 2010

|                           | <u>2011</u>           | <u>2010</u>           |
|---------------------------|-----------------------|-----------------------|
| ASSETS                    |                       |                       |
| Cash and cash equivalents | \$301,251             | \$194,186             |
| Mortgages receivable      | <u>104,921</u>        | <u>81,986</u>         |
| <br>TOTAL ASSETS          | <br><u>\$ 406,172</u> | <br><u>\$ 276,172</u> |
| NET ASSETS                |                       |                       |
| Temporarily restricted    | \$45,038              | \$45,038              |
| Permanently restricted    | <u>\$ 361,134</u>     | <u>\$ 231,134</u>     |
| <br>TOTAL NET ASSETS      | <br><u>\$ 406,172</u> | <br><u>\$ 276,172</u> |

See Independent Auditors' Report.

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.  
STATEMENTS OF ACTIVITIES - NEIGHBORWORKS AMERICA CAPITAL FUND  
FOR THE YEARS ENDED JUNE 30, 2011 AND 2010

|  | <u>2011</u>       | <u>2010</u>       |
|--|-------------------|-------------------|
| TEMPORARILY RESTRICTED NET ASSETS                            |                   |                   |
| Restrictions released from permanently restricted net assets | \$ -              | \$ 42,488         |
| INCREASE IN TEMPORARILY RESTRICTED NET ASSETS                | <u>-</u>          | <u>42,488</u>     |
| Revenues and Other Support                                   |                   |                   |
| Capital Grant-NeighborWorks America                          | 130,000           | 92,500            |
| Net assets released from restriction                         | <u>-</u>          | <u>(42,488)</u>   |
| INCREASE(DECREASE ) IN PERMANENTLY RESTRICTED NET ASSETS     | 130,000           | 50,012            |
| CHANGE IN NET ASSETS   | 130,000           | 70,138            |
| NET ASSETS AT BEGINNING OF YEAR                              | <u>276,172</u>    | <u>206,034</u>    |
| NET ASSETS AT END OF YEAR                                    | <u>\$ 406,172</u> | <u>\$ 276,172</u> |

See Independent Auditors' Report.