

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, 2010 AND 2009



CRAFT, NOBLE & COMPANY
PLLC

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

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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, 2010 and 2009, and the related statements of activities, changes in net assets, and cash flows for the years then ended. These financial statements are the responsibility of the Organization's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Federation of Appalachian Housing Enterprises, Inc., as of June 30, 2010 and 2009, and the changes in its net assets and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated September 30, 2010, on our consideration of Federation of Appalachian Housing Enterprises, Inc.'s internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grants agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and important for assessing the results of our audit.

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

Craft, Noble & Company, PLLC

Craft, Noble & Company, PLLC
September 30, 2010

CRAFT, NOBLE & COMPANY
PLLC

Certified Public Accountants
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www.craftnoble.com

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.
STATEMENT OF FINANCIAL POSITION
JUNE 30, 2010 AND 2009

	2010				2009			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
<u>Assets</u>								
Cash and cash equivalents	\$ 5,246,225	\$ 1,278,615	\$ 149,148	\$ 6,673,988	\$ 2,986,814	\$ 1,419,477	\$ -	4,406,291
Accounts receivable	784,675	(2,772)	-	781,903	217,531	40,300	-	257,831
Grants receivable	-	537,500	-	537,500	2,100,000	-	-	2,100,000
Accrued interest receivable	252,878	12,747	-	265,625	231,044	5,122	-	236,166
Deposits	3,120	-	-	3,120	153,120	-	-	153,120
Prepaid expenses	98,470	-	-	98,470	61,466	-	-	61,466
Property and equipment, net	860,177	-	-	860,177	285,724	-	-	285,724
Interfund balances	(4,173)	4,173	-	-	(219,945)	38,823	181,122	-
Mortgage notes receivable, net	10,861,643	9,726,093	69,175	20,656,911	12,500,888	9,424,578	-	21,925,466
Notes receivable, net	11,222,393	523,310	12,811	11,758,514	10,343,032	646,791	-	10,989,823
Property held for sale	1,002,665	224,068	-	1,226,733	743,686	111,255	-	854,941
Deferred compensation	15,513	-	-	15,513	4,750	-	-	4,750
Total Assets	\$ 30,343,586	\$ 12,303,734	\$ 231,134	\$ 42,878,454	\$ 29,408,110	\$ 11,686,346	\$ 181,122	\$ 41,275,578
<u>Liabilities and Net Assets</u>								
<u>Liabilities</u>								
Accounts payable	\$ 102,963	\$ 53,735	\$ -	\$ 156,698	\$ 37,262	\$ -	\$ -	\$ 37,262
Payroll taxes payable	26,356	-	-	26,356	22,254	-	-	22,254
Client advances and deposits	645,337	-	-	645,337	560,916	-	-	560,916
Accrued interest payable	43,076	4,568	-	47,644	64,320	4,521	-	68,841
Compensated absences payable	207,844	-	-	207,844	143,185	500	-	143,685
Deferred revenue	4,510	428,520	-	433,030	6,837	314,957	-	321,794
Notes payable	19,591,799	610,806	-	20,202,605	18,865,858	639,593	-	19,505,451
Deferred compensation	15,513	-	-	15,513	4,750	-	-	4,750
Total Liabilities	20,637,398	1,097,629	-	21,735,027	19,705,382	959,571	-	20,664,953
<u>Other Liabilities</u>								
Equity equivalent	2,000,000	-	-	2,000,000	2,000,000	-	-	2,000,000
Total Liabilities	22,637,398	1,097,629	-	23,735,027	21,705,382	959,571	-	22,664,953
<u>Net Assets</u>								
Net assets	7,106,188	11,206,105	231,134	18,543,427	7,102,728	10,726,775	181,122	18,010,625
Net assets, board restricted	600,000	-	-	600,000	600,000	-	-	600,000
Total Net Assets	7,706,188	11,206,105	231,134	19,143,427	7,702,728	10,726,775	181,122	18,610,625
Total Liabilities and Net Assets	\$ 30,343,586	\$ 12,303,734	\$ 231,134	\$ 42,878,454	\$ 29,408,110	\$ 11,686,346	\$ 181,122	\$ 41,275,578

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

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.
STATEMENTS OF ACTIVITIES
YEARS ENDING JUNE 30, 2010 AND 2009

	2010				2009			
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Revenue								
Mortgage and note interest	\$ 783,420	\$ 67,211	\$ -	850,631	\$ 1,005,159	\$ 59,708	\$ -	\$ 1,064,867
Contributions, grants	851,850	572,500	-	1,424,350	240,500	-	-	240,500
State grants	52,251	68,349	-	120,600	328,784	-	-	328,784
Pass-through grants	555,804	39,652	-	595,456	648,328	-	-	648,328
Federal grants	440,000	-	92,500	532,500	2,125,500	192,000	-	2,317,500
Rental income	2,700	400	-	3,100	200	1,000	-	1,200
Investment income	96,867	5,250	-	102,117	27,219	13,154	-	40,373
Administration income	52,130	10,000	-	62,130	43,154	-	-	43,154
Gain on Acquisition of Assets	-	-	-	-	246,878	-	-	246,878
Gain/(Loss) on Sale of Property	293,144	-	-	293,144	5,422	5,664	-	11,086
Fees and service charges	1,005,920	1,732	-	1,007,652	608,888	1,207	-	610,095
Miscellaneous income	1,269	-	-	1,269	99	-	-	99
Net assets released from restrictions								-
Satisfaction of program restrictions	328,252	(285,764)	(42,488)	-	130,324	(65,126)	(65,198)	-
Total Revenue	4,463,607	479,330	50,012	4,992,949	5,410,455	207,607	(65,198)	5,552,864
Expenses								
Program services	2,708,334	-	-	2,708,334	2,240,627	-	-	2,240,627
General and administrative	1,530,798	-	-	1,530,798	1,266,441	-	-	1,266,441
Fundraising	166,818	-	-	166,818	251,665	-	-	251,665
Membership	304,197	-	-	304,197	138,010	-	-	138,010
Total Expenses	4,710,147	-	-	4,710,147	3,896,743	-	-	3,896,743
Increase/(decrease) in net assets	(246,540)	479,330	50,012	282,802	1,513,712	207,607	(65,198)	1,656,121
Extraordinary Gain	250,000	-	-	250,000	-	-	-	-
Net Assets at Beginning of Period	7,702,728	10,726,775	181,122	18,610,625	6,189,016	10,519,168	246,320	16,954,504
Net Assets End of Period	<u>\$ 7,706,188</u>	<u>\$ 11,206,105</u>	<u>\$ 231,134</u>	<u>\$ 19,143,427</u>	<u>\$ 7,702,728</u>	<u>\$ 10,726,775</u>	<u>\$ 181,122</u>	<u>\$ 18,610,625</u>

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

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDING JUNE 30, 2010 AND 2009

	<u>2010</u>	<u>2009</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Changes in Net Assets	\$ 532,802	\$ 1,656,121
Adjustments to reconcile increase in net assets to net cash provided by operating activities		
Depreciation and amortization	71,737	58,482
(Gain)/Loss on disposal of assets	92,964	(26,743)
(Increase) decrease in operating assets		
Accounts receivable	(524,072)	601,546
Grants receivable	1,562,500	(1,875,000)
Accrued interest receivable	(29,459)	(3,087)
Prepaid expenses	(37,003)	(19,485)
Deferred Compensation	(10,763)	(4,750)
Deposits	150,000	(150,385)
Increase (decrease) in operating liabilities		
Accounts payable	119,436	(7,800)
Payroll taxes payable	4,101	22,254
Client advances and deposits	84,430	256,350
Accrued interest payable	(21,197)	15,116
Compensated absences payable	64,159	75,674
Deferred Revenue	111,237	176,282
Deferred Compensation	10,763	4,750
NET CASH PROVIDED BY OPERATING ACTIVITIES	<u>2,181,635</u>	<u>779,325</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of property and equipment	(1,339,892)	(623,324)
Proceeds from sale of property and equipment	321,910	598,942
Payments received on notes receivable	(11,343,263)	8,334,001
Disbursement of loans receivable funds	11,750,163	(7,205,668)
NET CASH PROVIDED (USED) BY INVESTING ACTIVITIES	<u>(611,082)</u>	<u>1,103,951</u>
CASH FLOWS FROM FINANCING ACTIVITIES		
Proceeds from long-term debt borrowings	4,977,034	1,290,494
Payments on long-term debt	(4,279,880)	(1,246,375)
NET CASH PROVIDED BY FINANCING ACTIVITIES	<u>697,154</u>	<u>44,119</u>
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	2,267,707	1,927,395
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	<u>4,406,281</u>	<u>2,478,886</u>
CASH AND CASH EQUIVALENTS AT END OF YEAR	<u>\$ 6,673,988</u>	<u>\$ 4,406,281</u>
Supplemental Information		
Interest paid	<u>\$ 546,810</u>	<u>\$ 558,957</u>

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

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010 AND 2009

Note 1 – Organization

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

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

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

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

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

In fiscal year 2010 FAHE was able to achieve 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.

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010 AND 2009

Note 2 – Summary of Significant Accounting Policies

Principles of Combination

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

Basis of Accounting

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

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

Cash and Cash Equivalents

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

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

Investments

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

Mortgage Notes Receivable

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

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

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010 AND 2009

Allowance for Loan Losses

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

Fixed Assets

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

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

During the year ended June 30, 2010 and 2009, depreciation expense was \$64,413 and \$49,263, respectively. The increase in depreciation is attributed to the purchase of the Parker Hannifin building, which will house all FAHE operations after completion of renovations. FAHE is working with an environmental consultant and the Kentucky EPA, Superfund Branch, Division of Waste Management to obtain environmental clearance on the property. Additionally, this year FAHE committed to the purchase of a new loan servicing software package. The software is increasing efficiencies, cutting processing costs and will allow the company to expand its servicing capabilities.

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 shorter of the term of the lease of two years.

Amortization expense for the year ended June 30, 2010 and 2009 was \$7,324 and \$9,219, respectively.

Revenue Recognition

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

Income Tax Status

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

The Organization is not aware of any unrelated business income as of September 30, 2010. The Financial Accounting Standards Board (FASB) has issued an Interpretation (FIN48), Accounting for Uncertainty in Income Taxes, which requires entities to disclose known or anticipated positions of income tax uncertainty. The Organization has never been audited by the Internal Revenue Service (IRS), however, the tax years 2007 forward could be subject to examination by the IRS or other applicable tax jurisdictions.

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010 AND 2009

Note 2-Summary of Significant Accounting Policies (Continued)

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

Note 3 – Grant Funds Receivable

The Organization received two multi-year private foundation grants in 2010. The contributions are recorded as income at face value as of the date of the award letter. The second and third installments totaling \$537,500 expected in the next fiscal year are recorded as temporarily restricted, due to timing restrictions, and will be reclassified to unrestricted assets as expended over fiscal years 2011 and 2012.

Unconditional promises to give amounted to \$537,500 and \$2,100,000 at June 30, 2010 and 2009, respectively.

Note 4 – Property Held for Resale

Property held for resale consists of foreclosure properties (REO) and land held for sale for future development by various members (Investment Property). Investment property is recorded at actual cost with an allowance made to reflect the lower of cost or market. REO property is recorded at the lower of cost or market when recovered from the foreclosure proceedings or by a deed-in-lieu of foreclosure. Gains or losses from the sale of properties are recorded in the statement of activities as either gains or losses on disposal of property. At June 30, 2010 and 2009, the organization held \$740,639 and \$348,104, respectively in REO property and \$486,094 and \$506,837 respectively, in investment property.

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010 AND 2009

Note 5 – Mortgage Notes Receivable

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

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.

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

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>

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

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

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010 AND 2009

Note 5 – Mortgage Notes Receivable (Continued)

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, 2010, is \$600,000. This provides aggregate loan loss coverage of 4.0% on the FAHE loan portfolio. Based on actual, historical delinquency trends, the Organization’s management does not expect to incur any charges against this designation.

Note 6 – Notes Receivable

The Organization makes loans to promote community development, to provide additional resources for operations, and to facilitate housing construction and financing to other non-profits and local housing authorities throughout Central Appalachia. Combined borrower balances of the Organization’s commercial loan portfolio as of June 30, 2010 and 2009 are presented below:

	<u>2010</u>	<u>2009</u>
Appalachia Habitat For Humanity	\$ 273,993	\$ 170,412
Appalachia Service Project	51,219	51,219
Beattyville Housing Development	384,438	136,847
Beattyville School	426,528	371,900
Blueberry Hill Estates	75,000	75,000
Boodry Place, LLC	-	138,945
Cambria House	40,501	41,492
Clinch Valley Community	93,735	106,575
COAP	460,202	461,947
Community Housing Partners	2,802,242	2,525,837
Community Housing, Inc.	-	605,383
Eastern Eight CDC	1,078,228	846,631
Frontier Housing, Inc.	1,302,984	944,855
Hazard/Perry County Community Ministries	29,782	31,791
Homeownership Center	112,250	112,250
HOMES, Inc.	1,084,810	947,865
HOPE Inc.	213,952	293,524
Housing Development	349,151	391,755
Housing Equity Fund of KY I	805,020	800,000
Housing Equity Fund of KY II	56,300	-
Irvine Renaissance, LLP	285,300	299,948
KDVA Homes 07, LLP	264,658	116,027
Knox Housing Partners, Inc.	13,714	-
Kentucky Mountain Health Alliance	323,905	-
Kentucky Mountain Housing Corporation	492,763	529,448
Lil' Britches Child Care Center	67,283	70,119
LINKS, Inc.	-	57,200
Mountain Cap, Inc.	233,571	236,306
People Inc. Financial Services	99,900	99,900
Randolph County Housing Authority	295,847	457,650
Safe Housing & Economic Development	220,762	229,786
Southern Appalachian Labor School	95,164	98,477
Sterling Housing, Inc.	42,422	42,422

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010 AND 2009

Note 6 – Notes Receivable (Continued)

Virginia Community Development Fund	6,232	5,000
Woodlands Development	-	<u>66,712</u>
Total Notes Receivable	<u>12,145,856</u>	<u>11,363,223</u>
Less: Allowance for Loan Loss	(387,342)	(373,400)
Notes Receivable, Net of Allowance	<u>\$ 11,758,514</u>	<u>\$ 10,989,823</u>

Note 7 – Notes Payable

Notes payable at June 30, 2010 and 2009 consists of notes payable to governmental agencies, banks, non-profit organizations and individuals as detailed below:

	Rate	Term	Maturity		Balance	
					<u>2010</u>	<u>2009</u>
Kentucky Housing Corporation:						
Kentucky Home Loan Fund/AHTF						
Special Contract #1	1.00%	20 Years	November 1, 2010	\$	-	\$ 12,500
Special Contract #2	1.00%	20 Years	January 01, 2012		19,000	28,500
Special Contract #3	1.00%	20 Years	February 01, 2013		41,700	55,600
Special Contract #4	1.00%	20 Years	July 1, 2013		82,000	102,500
Special Contract #5	1.00%	20 Years	July 1, 2014		102,500	123,000
Special Contract #6	1.00%	20 Years	July 1, 2015		124,500	145,250
Special Contract #7	1.00%	20 Years	July 1, 2016		147,022	168,025
Special Contract #8	3.00%	20 Years	October 1, 2035		455,755	467,311
Affordable Housing Trust Fund	1.00%	30 Years	July 1, 2033		54,327	56,321
Affordable Housing Trust Fund	1.00%	30 Years	September 1, 2035		5,783	45,694
NHPL, NHRL, NHPR						
NHPL 1997-1998	1.00%	20 Years	July 1, 2017		-	244,350
NHPL 1998-1999	1.00%	20 Years	July 1, 2018		262,307	332,572
NHPL 1999-2000	1.00%	20 Years	July 1, 2019		293,640	323,004
NHRL 1999-2000	1.00%	10 Years	July 1, 2009		-	8,772
NHPR 2000-2001	1.00%	20 Years	July 1, 2020		347,738	379,350
NHPR 2001-2002	1.00%	20 Years	July 1, 2022		320,850	347,588
NHPR 2002-2003	1.00%	20 Years	July 1, 2023		437,114	470,676
NHPR 2003-2004	1.00%	20 Years	July 1, 2024		424,725	455,063
NHPR 2004-2005	1.00%	20 Years	July 1, 2025		347,625	370,800
NHPR 2005-2006	1.00%	20 Years	July 1, 2026		317,200	329,400
NHPR 2006-2007	1.00%	20 Years	September 1, 2027		147,900	156,600
NHPR 2007-2008	1.00%	20 Years	September 1, 2028		222,457	234,818
NHPR 2009	1.00%	20 Years	February 1, 2030		244,423	130,742
Virginia Housing Development Authority:						
Housing Fund #1	3.00%	30 Years	July 5, 2028		138,306	221,097
VHPRF Phase I & II	3.00%	20 Years	November 5, 2026		165,010	203,708
Regional Loan Demo	3.00%	20 Years	May 20, 2010		-	10,448
Housing Fund #2	3.00%	30 Years	December 5, 2018		246,336	297,818
Housing Fund #3	2.00%	30 Years	March 1, 2014		555,781	573,497
2004 Line of Credit	2.00%	30 Years	September 1, 2026		771,654	857,933
2005 Line of Credit	2.00%	30 Years	February 1, 2037		803,022	937,274
2007 Reach	3.00%	30 Years	April 1, 2038		679,064	990,986
2009 Reach	3.00%	30 Years	May 1, 2039		290,087	-
2010 Reach	3.00%	30 Years	January 1, 2040		312,610	-
Wachovia Bank						
Five Year Note	0.81%	5 Years	April 30, 2011		1,050,000	750,000
Various Lenders						
Sisters of Loretto	3.00%	3 Years	June 30, 2012		50,000	50,000
Calvert Social Investment Foundation	4.50%	3 Years	June 30, 2010		-	1,000,000
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
Opportunity Finance Network	6.00%	10 Years	April 28, 2015		-	918,260
Andrew Schenker	3.00%	5 Years	May 31, 2011		25,000	25,000
Carter Garber	4.00%	5 Years	September 30, 2011		35,000	35,000

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010 AND 2009

Note 7 – Notes Payable (Continued)

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, 2010	300,000	400,000
Allison Conant	0.00%	5 Years	July 13, 2009	-	9,000
Tides Foundation	0.00%	5 Years	July 13, 2012	75,000	75,000
Funding Exchange Endowment	0.00%	5 Years	July 13, 2009	-	20,000
Funding Exchange Pooled Investment	0.00%	5 Years	July 13, 2009	-	6,000
Ethel Ackley	3.00%	3 Years	July 13, 2010	5,000	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	3.00%	3 Years	September 30, 2010	25,000	25,000
Seton Enablement Fund	3.00%	5 Years	June 1, 2013	61,777	81,173
The Ford Foundation	1.00%	10 Years	June 2, 2014	1,000,000	1,000,000
Florida Community Loan Fund	6.00%	10 Years	April 28, 2015	-	459,130
Stokey Trust	3.00%	5 Years	September 30, 2010	25,000	25,000
U.S. Department of Agriculture	1.00%	30 Years	October 16, 2031	610,806	639,593
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	253,428	265,598
Peoples Self Help Housing	4.00%	2 Years	Jan 5, 2011	500,000	500,000
Fannie Mae	5.00%	10 Years	August 30, 2014	-	250,000
Dominican Sisters of Peace	3.00%	1 Day	June 30, 2009	-	20,000
Dominican Sisters of Peace	3.00%	3 Years	July 1, 2012	20,000	-
Central Bank	5.00%	1 Year	May 13, 2011	-	-
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	-
Calvert Social Investment Foundation	4.50%	3 Years	June 30, 2013	1,000,000	-
Opportunity Finance Network	3.00%	10 Years	November 30, 2019	2,500,000	-
Seton Enablement Fund	3.00%	5 Years	October 1, 2014	90,658	-
				90,658	-
Total Notes Payable				\$ 20,202,605	\$ 19,505,451

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

	<u>2010</u>	<u>2009</u>
2010	\$ -	\$ 1,609,720
2011	1,930,000	592,500
2012	2,404,000	3,163,500
2013	1,783,977	711,773
2014	1,637,781	1,675,997
2015	593,157	-
Later Years	11,853,690	11,751,961
Totals	\$ 20,202,605	\$ 19,505,451

At June 30, 2010 and 2009 approximately \$5.998 million and \$3.212 million notes payable, respectively, are unsecured and represent private investments by individuals and groups.

At June 30, 2010 and 2009, respectively the Organization has a \$4.5 million line of credit with Wachovia secured by \$4.2 million commercial loan assets in 2010; a \$3.0 million line of credit with Fannie Mae backed by an unsecured letter of credit with Peoples Bank for \$450,000; a \$1.0 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, 2010 the Organization had available balances on lines of credit with Wachovia Bank of \$3.45 million and Central Bank of \$500,000. The additional \$1.0 million availability on the Fannie Mae line of credit has been frozen by regulators at Fannie Mae as a result of Fannie Mae being insolvent. Though not owing to anything the Organization has or has not done the line of credit has very little probability of being restored.

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010 AND 2009

Note 8-Other Liabilities

The Organization carries a \$2,000,000, ten-year note with Wachovia Bank classified as EQ2 funds. This note is shown under Other Liabilities on the balance sheet in order to represent more clearly the nature of the payable and to adhere to industry practice. The EQ2 is defined by having six attributes as follows (1) the EQ2 investment is carried as an investment on the investor's balance sheet in accordance with GAAP. (2) the EQ2 investment is a general obligation of FAHE that is not secured by any of FAHE's assets; (3) the EQ2 investment is fully subordinated to the right of repayment of all FAHE's other creditors; (4) the EQ2 investment does not give the investor the right to accelerate payment unless FAHE ceases its normal operations; (5) the EQ2 investment carries an interest rate that is not tied to any income received by FAHE; and (6) the EQ2 investment has a rolling term, and therefore, an indeterminate maturity. This note had an outstanding balance of \$2,000,000 as of June 30, 2010 and 2009, respectively.

Note 9 – Commitments and Contingencies

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

The Organization has an agreement with the Tennessee Housing Development Agency (THDA) to guarantee and service New Start loans to individuals, as well as guaranteeing and servicing member loan agreements with THDA. The Organization entered into the agreements to facilitate THDA working with the Organization's members located in Tennessee. Although management of the Organization feels these loans will be repaid and are fully secured by real estate, the Organization has a contingent liability of \$15,128,774 and \$9,566,781 as of June 30, 2010 and 2009, respectively. To further clarify, of the \$15,128,774 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. Historically, there has not been a loss on these loans since inception in 2003.

The Organization has a contractual agreement with NHTSA to sell mortgage notes, off the balance sheet, while retaining the servicing rights. The notes, with a balance of \$11,911,011 and \$10,616,830 at June 30, 2010 and 2009, respectively, were sold with recourse applicable only to notes 90 days past due. The Organization has posted letters of credit totaling \$1.5 million with Peoples Bank to stand against potential delinquent notes required to be repurchased. Ultimately, all the notes are fully secured by real estate and the Organization feels even in the event of repurchase the loans will be repaid. As of the close of this report NHTSA is in liquidation and it is unknown when the assets will be sold. It is uncertain whether FAHE will continue to service these loans for a fee or whether or not the loans will still be subject to recourse.

Note 10-Extraordinary Gain

On July 01, 2009 the Organization closed on the purchase contract of the Parker-Hannifin property located in Berea. The property consists of a building and nine acres of land. FAHE plans to move the Berea headquarters to this location after clean up and renovation. The company recorded a \$250,000 extraordinary gain on the purchase resulting from the difference between the purchase price of \$150,000 and the appraised value of the property at its highest and best use of \$400,000.

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2010 AND 2009

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 FDIC insured accounts up to \$250,000 per account with excess values invested in sweep accounts collateralized with mortgages. The Organization provides mortgage loans primarily to low and moderate income individuals. Mortgage notes totaling \$20,994,866 and \$22,298,449 at June 30, 2010 and 2009, respectively, are secured by the property purchased or improved. These mortgage receivables are a concentration of credit risk. The Organization provides loans to groups to support the growth of low-income housing opportunities in its service area. Notes receivable totaling \$12,145,856 and \$11,363,223 at June 30, 2010 and 2009, respectively, are secured by the assets of the Organization. Additionally, at June 30, 2010 and 2009, \$922,363 and \$1,180,858 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.

Note 12–Subsequent Events

Management of the Organization has considered subsequent events through September 30, 2010, 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, 2010

<u>Federal Grantor/Pass-Through Grantor/Program Title</u>	<u>Federal CFDA Number</u>	<u>Pass-Through Grantor's Number</u>	<u>Expenditures</u>
<u>Department of Treasury</u>			
NeighborWorks America	21.000		546,000
Community Development Financial Institutions	21.020	*	2,000,000
<u>Appalachian Regional Commission</u>			
<u>Passed through Kentucky Housing Corporation</u>			
Appalachian Regional Development	23.001	KY-16138-302-09	416,487
<u>Department of Housing & Urban Development</u>			
<u>Passed through Kentucky Housing Corporation</u>			
Home Investment Partnership Program (HOME)	14.239	* HB08-0201-01	48,000
Home Investment Partnership Program (HOME)	14.239	* HB09-0201-01	60,000
<u>Department of Housing & Urban Development</u>			
HUD Approved Title II Nonsupervised Mortgagees and Loan Correspondents	14.000	*	<u>361,131</u>
TOTAL FEDERAL AWARDS			<u><u>\$ 3,431,618</u></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, 2010

NOTE A – BASIS OF PRESENTATION

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

NOTE B – INSURANCE

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

REPORT ON 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, 2010, and have issued our report thereon dated September 30, 2010. 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*.

We noted certain matters that we reported to management of Federation of Appalachian Housing Enterprises, Inc. in a separate letter dated September 30, 2010.



This report is intended 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 30, 2010

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

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

Compliance

We have audited the compliance of Federation of Appalachian Housing Enterprises, Inc. (a non-profit organization) with the types of compliance requirements described in the “U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement” that are applicable to each of its major federal programs for the year ended June 30, 2010. Federation of Appalachian Housing Enterprises, Inc.’s major federal programs are identified in the summary of auditors’ results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of Federation of Appalachian Housing Enterprises, Inc.’s management. Our responsibility is to express an opinion on Federation of Appalachian Housing Enterprises, Inc.’s compliance based on our audit.

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

In our opinion, Federation of Appalachian Housing Enterprises, Inc. complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2010.

Internal Control Over Compliance

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



CRAFT, NOBLE & COMPANY
PLLC



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

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

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

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

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

Craft, Noble & Company, PLLC

Craft, Noble & Company, PLLC
September 30, 2010

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2010

SUMMARY OF AUDITORS' RESULTS

1. The auditors' report expresses an unqualified opinion on the financials 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:
 - Community Development Financial Institutions CFDA #21.020 Type A.
 - HUD Approved Title II Nonsupervised Mortgagees and Loan Correspondents CFDA #14.000 Type A.
 - HOME Investment Partnership Program CFDA #14.239 Type B.
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, 2010

Expenses	General & Administrative			Community			Grant			Program Services			Total
	Administrative	Membership	Fundraising	Home Lending	Development	Administration	Loan Servicing	FAHE Consulting	FAHE Capital	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	6,026	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	22,838	38,255		
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	4,326	7,346		
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	13,132	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 Forgivin	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		
Total Expenses	\$ 1,530,798	\$ 304,197	\$ 166,818	\$ 863,526	\$ 451,389	\$ 58,877	\$ 706,522	\$ 294,384	\$ 333,636	\$ 2,708,334	\$ 4,710,147		

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

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

Expenses	Program Services										Total										
	General & Administrative		Membership		Fundraising		Home Lending		Community			Grant		Program Services		Total					
	\$		\$		\$		\$		\$		\$		\$		\$			\$			
Personnel Expenses	533,175		105,952		58,102		300,766		157,218		20,507		246,081		102,534		116,205		943,311		1,640,540
Travel Expenses	25,986		5,164		2,832		14,658		7,662		999		11,993		4,997		5,664		45,973		79,955
Board & Committee Meetings	11,101		2,206		1,210		6,262		3,274		427		5,124		2,135		2,420		19,642		34,159
Conference & Workshops	8,642		1,717		942		4,875		2,548		332		3,989		1,662		1,884		15,290		26,591
Occupancy Expense	16,991		3,376		1,852		9,585		5,010		654		7,842		3,268		3,703		30,062		52,281
Supplies & Publications	5,955		1,183		649		3,359		1,756		229		2,748		1,145		1,298		10,535		18,322
Postage & Shipping	6,192		1,230		675		3,493		1,826		238		2,858		1,191		1,350		10,956		19,053
Communications	12,900		2,563		1,406		7,277		3,804		496		5,954		2,481		2,811		22,823		39,692
Equipment & Maintenance	16,646		3,308		1,814		9,390		4,909		640		7,683		3,201		3,628		29,451		51,219
Subscriptions	667		133		73		376		197		26		308		128		145		1,180		2,053
Licenses, Fees & Permits	1,446		287		158		816		426		56		667		278		315		2,558		4,449
Employee Education	1,039		206		113		586		306		40		479		200		226		1,837		3,195
Memberships	4,886		971		532		2,756		1,441		188		2,255		940		1,065		8,645		15,034
Marketing & Advertising	13,150		2,613		1,433		7,418		3,878		506		6,069		2,529		2,866		23,266		40,462
Liability & Property Insurance	9,999		1,987		1,090		5,640		2,948		385		4,615		1,923		2,179		17,690		30,766
Service Charges	3,008		598		328		1,697		887		116		1,388		578		656		9,256		9,256
Depreciation & Amortization	19,007		3,777		2,071		10,722		5,605		731		8,772		3,655		4,142		33,627		58,482
Organizational Expenses	153		30		17		86		45		6		70		29		33		269		469
Contributions	2,688		534		293		1,516		793		103		1,240		517		586		4,755		8,270
Software Lease	7,924		1,575		864		4,470		2,337		305		3,657		1,524		1,727		14,020		24,383
Professional Fees	28,550		5,673		3,111		16,105		8,419		1,098		13,177		5,490		6,222		50,511		87,845
Contract Services	41,266		8,200		4,497		23,278		12,168		1,587		19,046		7,936		8,994		73,009		126,972
Loan Processing Expense	1,399		278		152		789		413		54		646		269		305		2,476		4,305
Loan Servicing Expense	2,710		539		295		1,529		799		104		1,251		521		591		8,339		8,339
Pass Thru Grants	217,859		43,292		23,741		122,895		64,240		8,379		100,550		41,896		47,482		385,442		670,334
Over/Short	67		13		7		38		20		3		31		13		15		120		207
Administration	9,787		1,945		1,067		5,521		2,886		376		4,517		1,882		2,133		17,315		30,114
Bad Debt Expense	73,578		14,621		8,018		41,505		21,696		2,830		33,959		14,150		16,036		130,176		226,393
Interest Expense	186,574		37,076		20,332		105,247		55,015		7,176		86,111		35,880		40,664		330,093		574,075
Loans Forgiving	2,588		514		282		1,460		763		100		1,194		498		564		4,579		7,963
Miscellaneous Expense	508		104		54		288		151		20		236		98		106		899		1,565
State Income Tax	-		-		-		-		-		-		-		-		-		-		-
Total Expenses	1,266,441		251,665		138,010		714,403		373,440		48,711		584,510		243,548		276,015		2,240,627		3,896,743

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

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.
 STATEMENTS OF FINANCIAL POSITION - NEIGHBORWORKS AMERICA CAPITAL FUND
 JUNE 30, 2010 AND 2009

	<u>2010</u>	<u>2009</u>
ASSETS		
Cash and cash equivalents	\$ 194,186	\$ 206,034
Mortgages receivable	<u>81,986</u>	<u>-</u>
TOTAL ASSETS	<u>\$ 276,172</u>	<u>\$ 206,034</u>
NET ASSETS		
Temporarily restricted	\$ 45,038	\$ 24,912
Permanently restricted	<u>231,134</u>	<u>181,122</u>
TOTAL NET ASSETS	<u>\$ 276,172</u>	<u>\$ 206,034</u>

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC
 STATEMENTS OF ACTIVITIES - NEIGHBORWORKS AMERICA CAPITAL FUNI
 FOR THE YEARS ENDED JUNE 30, 2010 AND 2009

	<u>2010</u>	<u>2009</u>
TEMPORARILY RESTRICTED NET ASSETS		
Restrictions released from permanently restricted net asset	\$ 20,126	\$ 24,912
INCREASE IN TEMPORARILY RESTRICTED NET ASSETS	<u>20,126</u>	<u>24,912</u>
PERMANENTLY RESTRICTED NET ASSETS		
Revenues and Other Support		
Capital Grant - NeighborWorks America	\$ 92,500	\$ 195,000
Net assets released from restriction	<u>(42,488)</u>	<u>(260,198)</u>
INCREASE/(DECREASE) IN PERMANENTLY RESTRICTED NET ASSETS	50,012	(65,198)
CHANGE IN NET ASSETS	70,138	(40,286)
NET ASSETS AT BEGINNING OF YEAR	<u>206,034</u>	<u>246,320</u>
NET ASSETS AT END OF YEAR	<u>\$ 276,172</u>	<u>\$ 206,034</u>

FEDERATION OF APPALACHIAN HOUSING ENTERPRISES, INC.
 COMPUTATION OF ADJUSTED NET WORTH FOR APPROVAL AND RECERTIFICATION OF
 NONSUPERVISED LOAN CORRESPONDENTS
 FOR THE YEAR ENDING JUNE 30, 2010

Home office		\$ <u>63,000</u>
Add:		
Branch office	\$ 25,000	
x Number of branch offices	<u>-</u>	
Subtotal		\$ <u>-</u>
Total		\$ <u><u>63,000</u></u>
Net worth required (lesser of \$250,000 or Line 3)		\$ <u><u>63,000</u></u>
Owner's equity (net worth) per Balance sheet	\$ 19,143,427	
Less unacceptable assets	<u>\$ -</u>	
Adjusted net worth for HUD Requirement purposes		\$ <u><u>19,143,427</u></u>
Adjusted net worth above amount Required		\$ <u><u>19,080,427</u></u>
Adjusted net worth below amount Required		\$ <u>-</u>