

**NEIGHBORHOOD HOUSING SERVICES  
OF PHOENIX, INC. AND  
SUBSIDIARIES**

**CONSOLIDATED FINANCIAL STATEMENTS**

Year Ended December 31, 2009

**NEIGHBORHOOD HOUSING SERVICES  
OF PHOENIX, INC. AND  
SUBSIDIARIES**

**CONSOLIDATED FINANCIAL STATEMENTS**

Year Ended December 31, 2009

CONTENTS

	<u>Pages</u>
INDEPENDENT AUDITORS' REPORT	1
FINANCIAL STATEMENTS	
Consolidated Statement of Financial Position	2
Consolidated Statement of Activities	3
Consolidated Statement of Functional Expenses	4
Consolidated Statement of Cash Flows	5
Notes to Consolidated Financial Statements	6 - 18



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**INDEPENDENT AUDITORS' REPORT**

To the Board of Directors of

**NEIGHBORHOOD HOUSING SERVICES OF PHOENIX, INC.**

We have audited the accompanying consolidated statement of financial position of **Neighborhood Housing Services of Phoenix, Inc. and Subsidiaries**, at December 31, 2009, and the related consolidated statements of activities, functional expenses and cash flows for the year then ended. These consolidated financial statements are the responsibility of **Neighborhood Housing Services of Phoenix, Inc. and Subsidiaries'** management. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

We conducted our audit in accordance with U.S. generally accepted auditing standards 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 consolidated 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 consolidated financial statements referred to above present fairly, in all material respects, the financial position of **Neighborhood Housing Services of Phoenix, Inc. and Subsidiaries** at December 31, 2009, and the change in their net assets and their cash flows for the year then ended, in conformity with U.S. generally accepted accounting principles.

Phoenix, Arizona  
April 28, 2010

*Mayer Hoffman McCann P.C.*

**NEIGHBORHOOD HOUSING SERVICES OF PHOENIX, INC.  
AND SUBSIDIARIES**

**CONSOLIDATED STATEMENT OF FINANCIAL POSITION**

December 31, 2009

**ASSETS**

<b>Neighborhood Housing Services of Phoenix, Inc.</b>									
	<b>Homeowner</b>				<b>Phoenix Housing</b>				
	<b>Operating</b>	<b>Development</b>	<b>NWA</b>	<b>Agency</b>	<b>Total</b>	<b>Partnership,</b>	<b>La Ciudad,</b>	<b>Eliminations</b>	<b>Total</b>
	<b>Funds</b>	<b>Funds</b>	<b>Loan Fund</b>	<b>Funds</b>	<b>All Funds</b>	<b>LLC</b>	<b>LLC</b>		
Cash and cash equivalents	\$ 944,293	\$ 2,448,792	\$ 253,940	\$ 143,854	\$ 3,790,879	\$ 44,845	\$ 14,902	\$ -	\$ 3,850,626
Restricted cash	351,724	-	-	-	351,724	-	38,448	-	390,172
Governmental receivables	141,567	123,217	-	-	264,784	-	-	-	264,784
Other receivables	78,812	61,357	100,000	-	240,169	-	-	(161,634)	78,535
Property held for re-sale	558,705	1,822,818	1,400,000	-	3,781,523	151,600	-	-	3,933,123
Prepaid expenses and deposits	23,950	5,808	-	-	29,758	-	4,213	-	33,971
Mortgage loans receivable, net	3,475,879	504,645	792,980	-	4,773,504	-	-	-	4,773,504
Property and equipment, net	98,600	-	-	-	98,600	-	2,460,618	-	2,559,218
Investment in subsidiaries	-	1,653,792	-	-	1,653,792	-	-	(1,653,792)	-
<b>TOTAL ASSETS</b>	<b>\$ 5,673,530</b>	<b>\$ 6,620,429</b>	<b>\$ 2,546,920</b>	<b>\$ 143,854</b>	<b>\$ 14,984,733</b>	<b>\$ 196,445</b>	<b>\$ 2,518,181</b>	<b>\$ (1,815,426)</b>	<b>\$ 15,883,933</b>

**LIABILITIES AND NET ASSETS**

<b>LIABILITIES</b>									
Accounts payable and accrued expenses	\$ 68,781	\$ 362,896	\$ -	\$ 825	\$ 432,502	\$ 17	\$ 112,202	\$ (161,634)	\$ 383,087
Accrued compensated absences	36,301	-	-	-	36,301	-	-	-	36,301
Advances on contracts	-	4,839	-	-	4,839	-	-	-	4,839
Loan impounds and client deposits	-	678,499	-	-	678,499	-	-	-	678,499
Deferred revenue	327,000	1,053,654	-	-	1,380,654	-	-	-	1,380,654
Recoverable grant	-	75,000	-	-	75,000	-	-	-	75,000
Notes payable	3,483,427	1,249,214	-	-	4,732,641	-	948,742	-	5,681,383
<b>TOTAL LIABILITIES</b>	<b>3,915,509</b>	<b>3,424,102</b>	<b>-</b>	<b>825</b>	<b>7,340,436</b>	<b>17</b>	<b>1,060,944</b>	<b>(161,634)</b>	<b>8,239,763</b>
<b>NET ASSETS</b>									
Unrestricted	1,758,021	-	758,311	-	2,516,332	-	1,457,237	(1,457,261)	2,516,308
Temporarily restricted	-	3,196,327	200,000	143,029	3,539,356	196,428	-	(196,531)	3,539,253
Permanently restricted	-	-	1,588,609	-	1,588,609	-	-	-	1,588,609
<b>TOTAL NET ASSETS</b>	<b>1,758,021</b>	<b>3,196,327</b>	<b>2,546,920</b>	<b>143,029</b>	<b>7,644,297</b>	<b>196,428</b>	<b>1,457,237</b>	<b>(1,653,792)</b>	<b>7,644,170</b>
<b>TOTAL LIABILITIES AND NET ASSETS</b>	<b>\$ 5,673,530</b>	<b>\$ 6,620,429</b>	<b>\$ 2,546,920</b>	<b>\$ 143,854</b>	<b>\$ 14,984,733</b>	<b>\$ 196,445</b>	<b>\$ 2,518,181</b>	<b>\$ (1,815,426)</b>	<b>\$ 15,883,933</b>

See Notes to Consolidated Financial Statements

**NEIGHBORHOOD HOUSING SERVICES OF PHOENIX, INC.  
AND SUBSIDIARIES**

**CONSOLIDATED STATEMENT OF ACTIVITIES**

Year Ended December 31, 2009

	<u>Neighborhood Housing Services of Phoenix, Inc.</u>					Phoenix Housing Partnership, LLC	La Ciudad, LLC	Eliminations	Total	Unrestricted	Temporarily Restricted	Permanently Restricted
	Operating	Homeowner	NWA	Agency	Total							
	Funds	Development Funds	Loan Fund	Funds	All Funds							
<b>SUPPORT AND REVENUE</b>												
Public support												
Governmental grants	\$ 629,934	\$ 3,116,644	\$ 190,000	\$ 115,610	\$ 4,052,188	\$ -	\$ -	\$ -	\$ 4,052,188	\$ 3,791,537	\$ 70,651	\$ 190,000
Nongovernmental grants and contributions	311,069	30,000	-	5,000	346,069	-	-	-	346,069	346,069	-	-
Contributions in kind	10,664	12,145	-	-	22,809	-	-	-	22,809	22,809	-	-
Total support	<u>951,667</u>	<u>3,158,789</u>	<u>190,000</u>	<u>120,610</u>	<u>4,421,066</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>4,421,066</u>	<u>4,160,415</u>	<u>70,651</u>	<u>190,000</u>
Revenue												
Fees	642,311	156,286	-	-	798,597	-	134,998	(137,298)	796,297	796,297	-	-
Interest income on mortgages	250,786	1,721	30,293	-	282,800	-	-	(8,386)	274,414	274,414	-	-
Investment income	4,766	1,414	384	-	6,564	180	76	-	6,820	6,820	-	-
Loss on investment in subsidiaries	-	(46,703)	-	-	(46,703)	-	-	46,703	-	-	-	-
Total revenue	<u>897,863</u>	<u>112,718</u>	<u>30,677</u>	<u>-</u>	<u>1,041,258</u>	<u>180</u>	<u>135,074</u>	<u>(98,981)</u>	<u>1,077,531</u>	<u>1,077,531</u>	<u>-</u>	<u>-</u>
Net assets released from program restrictions - satisfaction of restrictions	-	-	-	-	-	-	-	-	-	883,310	75,001	(958,311)
Total support and revenue	<u>1,849,530</u>	<u>3,271,507</u>	<u>220,677</u>	<u>120,610</u>	<u>5,462,324</u>	<u>180</u>	<u>135,074</u>	<u>(98,981)</u>	<u>5,498,597</u>	<u>6,121,256</u>	<u>145,652</u>	<u>(768,311)</u>
<b>EXPENSES</b>												
Program services												
Homebuyer education	850,030	-	-	-	850,030	-	-	(81,944)	768,086	768,086	-	-
Loan services	641,669	2,780,187	-	-	3,421,856	-	-	(15,207)	3,406,649	3,406,649	-	-
Affordable housing development	171,442	430,768	-	-	602,210	-	-	(16,281)	585,929	585,929	-	-
Agency funds	-	-	-	49,959	49,959	-	-	-	49,959	49,959	-	-
La Ciudad, LLC	-	-	-	-	-	-	181,957	-	181,957	181,957	-	-
Total program services	<u>1,663,141</u>	<u>3,210,955</u>	<u>-</u>	<u>49,959</u>	<u>4,924,055</u>	<u>-</u>	<u>181,957</u>	<u>(113,432)</u>	<u>4,992,580</u>	<u>4,992,580</u>	<u>-</u>	<u>-</u>
Supporting services												
Management and general	396,440	45,183	-	-	441,623	-	-	(20,713)	420,910	420,910	-	-
Community outreach	110,324	-	-	-	110,324	-	-	(8,539)	101,785	101,785	-	-
Resource development	90,019	-	-	-	90,019	-	-	(3,000)	87,019	87,019	-	-
Total supporting services	<u>596,783</u>	<u>45,183</u>	<u>-</u>	<u>-</u>	<u>641,966</u>	<u>-</u>	<u>-</u>	<u>(32,252)</u>	<u>609,714</u>	<u>609,714</u>	<u>-</u>	<u>-</u>
Total expenses	<u>2,259,924</u>	<u>3,256,138</u>	<u>-</u>	<u>49,959</u>	<u>5,566,021</u>	<u>-</u>	<u>181,957</u>	<u>(145,684)</u>	<u>5,602,294</u>	<u>5,602,294</u>	<u>-</u>	<u>-</u>
Change in net assets before transfers in (out)	(410,394)	15,369	220,677	70,651	(103,697)	180	(46,883)	46,703	(103,697)	518,962	145,652	(768,311)
Transfers in (out)	171,068	(182,891)	(30,677)	42,500	-	-	-	-	-	-	-	-
Change in net assets	(239,326)	(167,522)	190,000	113,151	(103,697)	180	(46,883)	46,703	(103,697)	518,962	145,652	(768,311)
NET ASSETS, beginning of year	<u>1,997,347</u>	<u>3,363,849</u>	<u>2,356,920</u>	<u>29,878</u>	<u>7,747,994</u>	<u>196,248</u>	<u>1,504,120</u>	<u>(1,700,495)</u>	<u>7,747,867</u>	<u>1,997,346</u>	<u>3,393,601</u>	<u>2,356,920</u>
NET ASSETS, end of year	<u>\$ 1,758,021</u>	<u>\$ 3,196,327</u>	<u>\$ 2,546,920</u>	<u>\$ 143,029</u>	<u>\$ 7,644,297</u>	<u>\$ 196,428</u>	<u>\$ 1,457,237</u>	<u>\$ (1,653,792)</u>	<u>\$ 7,644,170</u>	<u>\$ 2,516,308</u>	<u>\$ 3,539,253</u>	<u>\$ 1,588,609</u>

See Notes to Consolidated Financial Statements

**NEIGHBORHOOD HOUSING SERVICES OF PHOENIX, INC.  
AND SUBSIDIARIES**

**CONSOLIDATED STATEMENT OF FUNCTIONAL EXPENSES**

Year Ended December 31, 2009

	Program Services					Supporting Services					Total
	Homebuyer Education	Loan Services	Affordable Housing Development	Agency Funds	La Ciudad, LLC	Subtotal	Management and General	Community Outreach	Resource Development	Subtotal	
Salaries and wages	\$ 506,556	\$ 147,757	\$ 118,633	\$ -	\$ -	\$ 772,946	\$ 184,950	\$ 66,811	\$ 66,950	\$ 318,711	\$ 1,091,657
Employee benefits/payroll taxes	88,926	28,962	15,976	-	-	133,864	19,086	10,799	7,487	37,372	171,236
Total salaries, wages and related expenses	595,482	176,719	134,609	-	-	906,810	204,036	77,610	74,437	356,083	1,262,893
Professional fees	30,678	62,927	8,735	19,219	-	121,559	46,092	456	429	46,977	168,536
Rent	82,482	15,306	5,632	-	-	103,420	20,849	8,595	3,020	32,464	135,884
Operating supplies	24,019	4,993	2,907	25,266	-	57,185	3,781	1,764	1,651	7,196	64,381
Property taxes	-	-	3,704	-	17,470	21,174	241	-	-	241	21,415
Telephone and utilities	7,531	2,640	1,322	206	15,863	27,562	3,031	1,033	1,336	5,400	32,962
Postage and printing	690	5,554	172	-	-	6,416	1,950	694	258	2,902	9,318
Equipment rental and maintenance	21,430	11,362	2,366	154	-	35,312	3,888	2,074	1,667	7,629	42,941
Advertising and marketing	9,007	455	2,367	3,672	-	15,501	868	12,825	3,599	17,292	32,793
Travel and training	35,285	3,187	4,978	1,442	-	44,892	3,882	798	733	5,413	50,305
Repairs and maintenance	13,347	2,337	4,271	-	13,427	33,382	3,900	1,312	461	5,673	39,055
Insurance	6,487	2,863	3,918	-	3,263	16,531	2,235	1,014	793	4,042	20,573
Dues and subscriptions	1,730	1,586	3,201	-	-	6,517	828	660	529	2,017	8,534
Other expenses	1,954	42,362	2	-	-	44,318	10,329	-	-	10,329	54,647
Interest	-	109,500	3,099	-	75,744	188,343	128,761	-	-	128,761	317,104
Subsidies to clients	-	2,777,083	352,568	-	-	3,129,651	-	-	-	-	3,129,651
Property loss reserve	-	-	66,500	-	-	66,500	-	-	-	-	66,500
Bad debt expense	6,625	200,000	-	-	-	206,625	3,347	-	-	3,347	209,972
Hospitality	3,324	-	-	-	-	3,324	-	-	-	-	3,324
Total expenses before depreciation and amortization	840,071	3,418,874	600,351	49,959	125,767	5,035,022	438,018	108,835	88,913	635,766	5,670,788
Depreciation and amortization	9,959	2,982	1,859	-	56,190	70,990	3,605	1,489	1,106	6,200	77,190
Total expenses before eliminations	850,030	3,421,856	602,210	49,959	181,957	5,106,012	441,623	110,324	90,019	641,966	5,747,978
Eliminations	(81,944)	(15,207)	(16,281)	-	-	(113,432)	(20,713)	(8,539)	(3,000)	(32,252)	(145,684)
Total Expenses	<u>\$ 768,086</u>	<u>\$ 3,406,649</u>	<u>\$ 585,929</u>	<u>\$ 49,959</u>	<u>\$ 181,957</u>	<u>\$ 4,992,580</u>	<u>\$ 420,910</u>	<u>\$ 101,785</u>	<u>\$ 87,019</u>	<u>\$ 609,714</u>	<u>\$ 5,602,294</u>

See Notes to Consolidated Financial Statements

**NEIGHBORHOOD HOUSING SERVICES OF PHOENIX, INC.  
AND SUBSIDIARIES**

**CONSOLIDATED STATEMENT OF CASH FLOWS**

Year Ended December 31, 2009

<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>	
Change in net assets	\$ (103,697)
Adjustments to reconcile change in net assets to net cash provided by operating activities:	
Depreciation and amortization	77,190
Change in allowance for receivables	3,126
Change in allowance for mortgage loans receivable	81,152
Change in imputed interest	134,246
Impairment of inventory	66,500
Gain on sale of properties held for sale	(53,231)
Changes in operating assets and liabilities:	
Decrease (increase) in:	
Governmental receivables	(213,129)
Other receivables	8,221
Prepaid expenses and deposits	(8,123)
Increase (decrease) in:	
Accounts payable and accrued expenses	5,000
Accrued compensated absences	7,174
Deferred revenues	1,380,654
Advances on contracts	(12)
Net cash provided by operating activities	<u>1,385,071</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>	
Purchase of property and equipment	(81,256)
Change in loan impounds and client deposits	51,408
Payments received on mortgage loans receivable	835,504
Proceeds from sale of property held for re-sale	1,192,365
Purchase of property held for re-sale	(2,294,237)
Change in restricted cash	(252,091)
Mortgage loans issued	(866,176)
Net cash used in investing activities	<u>(1,414,483)</u>
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>	
Proceeds from recoverable grant	3,549
Proceeds from notes payable	1,450,000
Payments on notes payable	(206,188)
Net cash provided by financing activities	<u>1,247,361</u>
<b>NET CHANGE IN CASH AND CASH EQUIVALENTS</b>	1,217,949
<b>CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR</b>	<u>2,632,677</u>
<b>CASH AND CASH EQUIVALENTS, END OF YEAR</b>	<u><u>\$ 3,850,626</u></u>
<b>SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION</b>	
Cash paid for interest	<u><u>\$ 240,729</u></u>

See Notes to Consolidated Financial Statements

# NEIGHBORHOOD HOUSING SERVICES OF PHOENIX, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Year Ended December 31, 2009

### (1) Organization operations and summary of significant accounting policies

Neighborhood Housing Services of Phoenix, Inc. (the "Organization") and its subsidiary, Phoenix Housing Partnership, LLC, are dedicated to the revitalization of Phoenix neighborhoods by providing a full range of services and programs to encourage, create and support homeownership.

The Organization provides services in four major program areas, which are as follows:

*Homebuyer education* – All borrowers are required to attend an eight hour homebuyer education class on the process of purchasing a home and the responsibilities of homeownership. Classes are taught in English and Spanish. Clients who want to pursue homeownership are also provided individual counseling on budget and credit issues, as needed. A twelve hour financial literacy curriculum is also offered to all clients to improve personal financial management skills.

*Loan services* – The Organization is a licensed mortgage bank in the State of Arizona, an approved Fannie Mae seller/servicer, and a U.S. Department of Housing and Urban Development (HUD) approved FHA correspondent. The Organization originates and services first and second mortgage loans and down payment/closing cost assistance grants and loans. The Organization develops and/or administers special mortgage programs that meet the credit needs of low and moderate income borrowers. Loan terms may vary from conventional interest-bearing and fully amortizing to fully-forgivable loans which subsidize a home purchase.

*Affordable housing development* – The Organization develops affordable single family homes in neighborhoods targeted for revitalization efforts by its board of directors. These development programs primarily focus on new construction of single family homes on in-fill lots. The majority of homes developed by the Organization are located in low to moderate-income census track areas and are funded with governmental grants to subsidize the cost of development.

New construction standards exceed the minimum requirements of both HUD and the City of Phoenix. The new construction standards seek to eliminate the need for major replacement or repair costs for homebuyers in the first five years of ownership.

In 2004, the Organization created the Phoenix Housing Partnership, LLC, a wholly-owned subsidiary. In 2005, the Partnership purchased land on which to build a 65-unit single-family subdivision. The only activity in 2009 was predevelopment costs for engineering, infrastructure and legal costs. These costs totaled approximately \$22,600 and were capitalized as part of property held for re-sale.

During 2006, La Ciudad, LLC ("La Ciudad") was formed as a wholly-owned subsidiary of Neighborhood Housing Services of Phoenix, Inc. for the purpose of owning and managing a 10,600 square foot office building. The Organization is the only tenant currently occupying 7,714 square feet (73%) of rentable space. Subsequent to year-end the Organization expanded their occupancy, and when build out of the leasehold improvements is completed, will occupy 80% of the office building.

The Financial Accounting Standards Board ("FASB") sets U.S. generally accepted accounting principles ("GAAP") to ensure consistent reporting. References to GAAP are to the *FASB Accounting Standards Codification* ("FASB ASC").

# NEIGHBORHOOD HOUSING SERVICES OF PHOENIX, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Year Ended December 31, 2009

### (1) Organization operations and summary of significant accounting policies (continued)

**Basis of consolidation** – Neighborhood Housing Services of Phoenix, Inc. and its wholly-owned subsidiaries, Phoenix Housing Partnership, LLC and La Ciudad, LLC, have adopted the provisions of FASB ASC 958-810, *Not-for-Profit Entities - Consolidation*, which requires consolidated financial statements for certain related entities. Accordingly, the financial statements include the consolidated transactions and balances of the Organization and its subsidiaries and have been prepared in accordance with the accrual basis of accounting. Significant transactions and balances between the Organization and its subsidiaries have been eliminated.

**Basis of presentation** – The accompanying financial statements are presented in accordance with FASB ASC 958-205, *Presentation of Financial Statements*. Under FASB ASC 958-205, the Organization is required to report information regarding its financial position and activities according to three classes of net assets: unrestricted net assets, temporarily restricted net assets, and permanently restricted net assets. Temporarily restricted net assets consist of funds held for down-payment assistance, mortgage loans, and education counseling. Permanently restricted net assets consist of funds held for financing development projects or mortgage loans.

**Fund accounting** – To ensure observance of limitations and restrictions placed on the use of resources available to Neighborhood Housing Services of Phoenix, Inc., the accounts of the Organization are maintained in accordance with the principles of fund accounting. This is the procedure by which resources for various purposes are classified for accounting and reporting purposes into funds established according to their nature and purpose. Separate accounts are maintained for each fund. Accordingly, all financial transactions have been recorded and reported by fund group. The assets, liabilities, and net assets of the Organization are reported in the following fund groups:

- Operating funds represent resources that are available for the general operations and certain lending activities of the Organization.
- Homeowner development, NeighborWorks America (NWA) loan fund, Agency funds and Phoenix Housing Partnership, LLC arise from contributions and grants from a variety of sources (including interest and other revenues earned thereon) which may be used only in accordance with the purposes established by the donors and grantors.
- La Ciudad, LLC receives rental income from Neighborhood Housing Services of Phoenix, Inc.

**Management's use of estimates** – The preparation of consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements. Estimates also affect the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

**Restricted and unrestricted revenue and support** – The Organization accounts for contributions in accordance with FASB ASC 958-605, *Revenue Recognition*. In accordance with FASB ASC 958-605, contributions received are recorded as unrestricted, temporarily restricted or permanently restricted support, depending on the existence and/or nature of any donor restrictions. All donor-restricted support is reported as an increase 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 accomplished), temporarily or permanently restricted net assets are reclassified to unrestricted net assets and reported in the consolidated statement of activities as net assets released from restrictions. However, if a restriction is fulfilled in the same time period in which the contribution is received, the Organization reports the support as unrestricted.

**NEIGHBORHOOD HOUSING SERVICES OF PHOENIX, INC.  
AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

Year Ended December 31, 2009

**(1) Organization operations and summary of significant accounting policies (continued)**

**Cash and cash equivalents** – Cash includes cash and, at times, cash equivalents, which consist of highly liquid financial instruments purchased with an original maturity of ninety days or less. Any cash held in trust is guaranteed by the financial institution. Cash held for operations and programs and cash held for reserve are insured up to a maximum limit of \$250,000 by the Federal Deposit Insurance Corporation (FDIC). The Organization has a \$400,000 collateralization agreement with the financial institution for operating and reserve cash balances in excess of the FDIC \$250,000 limit. Therefore, the maximum operating and reserve cash amounts either insured or collateralized is equal to \$650,000. Operating and reserve cash balances in excess of \$650,000 are uninsured. Cash held for construction of commercial building is insured by the FDIC up to a maximum limit of \$250,000.

**Restricted cash** – Restricted cash consists of \$38,448 specifically reserved for the replacement and leasing reserve. Additionally, in 2009, the Organization received cash under grant agreements to be used for specific purposes. At December 31, 2009, \$351,724 of these funds had not been spent for these intended purposes, and, accordingly, these amounts are reported as restricted cash in the accompanying consolidated statement of financial position.

**Property held for re-sale** – Real estate held for sale is stated at the lower of cost or market and includes land under development, developed lots, direct and indirect costs of housing construction and overhead incurred during the development period. Cost is determined by the specific identification method.

**Mortgage loans receivable** – Mortgage loans receivable are stated at unpaid principal balances, less an allowance for uncollectible loans. Interest on amortizing loans is recognized over the term of the loan and is calculated using conventional mortgage methods on principal amounts outstanding.

The allowance for uncollectible loans is increased by charges to income and decreased by charge-offs (net of recoveries). Management's periodic evaluation of the adequacy of the allowance is based on the Organization's past loan loss experience, known and other risk elements inherent in the portfolio, specified impaired loans, adverse situations that may affect the borrower's ability to repay, estimated value of the underlying collateral and current economic conditions.

The Organization considers a loan impaired when, based on current information or factors, it is probable that the Organization will not collect the principal and interest payments according to the loan agreement. Management considers many factors in determining whether a loan is impaired, such as payment history, value of collateral and other factors. Loans that are contractually delinquent less than three months are generally not considered impaired. Management continually monitors delinquent loans to ensure collection and to determine, if necessary, impairment. The Organization measures impairment on a loan-by-loan basis by using the fair value of collateral. At December 31, 2009, the Organization recorded approximately \$102,000 as a reserve for impaired loans.

**Property and equipment** – Property and equipment is recorded at cost. Donated property and equipment is recorded at fair value at the date of gift to the Organization. Maintenance and repairs are charged to operations when incurred. Betterments and renewals in excess of \$500 are capitalized. When property and equipment is sold or otherwise disposed of, the asset account and related accumulated depreciation account are relieved and any gain or loss is included in operations. Depreciation and amortization is computed using the straight-line method over the following general range of estimated useful lives:

	<u>Estimated Useful Lives</u>
Office building	39 years
Furniture, fixtures, and equipment	3 - 7 years
Leasehold improvements	9 years

**NEIGHBORHOOD HOUSING SERVICES OF PHOENIX, INC.  
AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

Year Ended December 31, 2009

**(1) Organization operations and summary of significant accounting policies (continued)**

Donations of property and equipment are recorded as contributions at their estimated fair value at the date of donation. Such donations are reported as increases in unrestricted net assets unless the donor has restricted the donated asset to a specific purpose. Assets donated with explicit restrictions regarding their use and contributions of cash that must be used to acquire property and equipment are reported as restricted contributions absent donor stipulations regarding how long those donated assets must be maintained. The Organization reports expirations of donor restrictions when the donated or acquired assets are placed in service as instructed by the donor. The Organization reclassifies temporarily restricted net assets to unrestricted net assets at that time.

**Impairment of long-lived assets** – The Organization accounts for long-lived assets in accordance with the provisions of FASB ASC 360, *Property, Plant, and Equipment*. FASB ASC 360 requires that long-lived assets be reviewed for the impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future undiscounted net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the fair value of the assets. Assets to be disposed of are reported at the lower of the carrying amount or fair value less costs to sell. Management does not believe impairment indicators are present.

**Donated materials and services** – Donated services are recognized as contributions in accordance with FASB ASC 958-605 at their estimated fair value if the services (a) create or enhance the Organization's non-financial assets or (b) required specialized skills, are performed by people with those skills, and would otherwise be purchased. Donated materials are recorded at their estimated fair market value as of the date of donation. Volunteers donate a significant amount of time to the Organization's program services, but these amounts have not been reflected in the accompanying consolidated financial statements because these donated services did not meet the recognition conditions under FASB ASC 958-605.

**Government grants** – The Organization receives grants from various city, state and federal agencies. The Organization recognizes revenues for these grants as services are provided. A receivable is recorded to the extent the amount earned exceeds cash advances. Conversely, deferred revenue is recorded when cash advances exceed amounts earned. Funding sources may, at their discretion, request reimbursement for expenses or return of funds, or both, as a result of noncompliance by the Organization with the terms of the grants or contracts.

**Fees** – Fee revenue consists primarily of fees related to homebuyer education and loan services provided by the Organization. Fees are recognized as services are provided.

**Advertising costs** – Advertising costs are charged to operations as incurred. Advertising expenses totaled \$32,793 in 2009.

**Functional allocations of expenses** – The costs of providing various programs and other activities have been summarized on a functional basis in the consolidated statement of activities. Accordingly, certain costs have been allocated among the programs and supporting services benefited based on the percentage of total full-time employees in each line of business.

**NEIGHBORHOOD HOUSING SERVICES OF PHOENIX, INC.  
AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

Year Ended December 31, 2009

**(1) Organization operations and summary of significant accounting policies (continued)**

**Income tax status** – Neighborhood Housing Services of Phoenix, Inc. (“NHSP”) qualifies as a tax-exempt organization under Section 501(c)(3) of the Internal Revenue Code (the “Code”) and, accordingly, there is no provision for income taxes in the accompanying consolidated financial statements. In addition, the Organization qualifies for the charitable contribution deduction under Section 170 of the Code and has been classified as an organization that is not a private foundation. Income determined to be unrelated business taxable income (UBTI) would be taxable. Phoenix Housing Partnership, LLC and La Ciudad, LLC are organized as Arizona limited liability companies whose sole member is NHSP. For income tax purposes, these are disregarded entities and are treated as departments of NHSP. Accordingly, they are exempt from income taxes under applicable sections of the IRC and the Arizona Revised Statutes and have been classified as organizations that are not private foundations.

In June 2006, the FASB issued FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* (“FIN 48”), which was subsequently incorporated into FASB ASC 740. In 2009, the Organization implemented the provisions FIN 48 that are included in FASB ASC 740. The Organization evaluates its uncertain tax positions, if any, on a continual basis through review of its policies and procedures, review of its regular tax filings, and discussions with outside experts.

**Subsequent events** – The Organization has evaluated events through April 28, 2010, which is the date the consolidated financial statements were available to be issued. Management is not aware of any events that have occurred subsequent to the date of the consolidated statement of financial position that would require adjustment to, or disclosure in, the consolidated financial statements.

**(2) Governmental receivables**

Governmental receivables consist of:

	<u>2009</u>
State of Arizona	\$ 216,843
City of Phoenix	24,703
NeighborWorks Arizona	10,668
Navajo Housing Authority	10,000
City of Glendale	1,775
Local Initiatives Support Corp.	795
Total governmental receivables	<u>\$ 264,784</u>

Governmental receivables are stated at the amount management expects to collect. Management provides for probable uncollectible amounts through a charge to earnings and a credit to the allowance for uncollectible accounts based on their assessment of the current status of individual receivables. Balances that are still outstanding after management has used reasonable collection efforts are written off through a charge to the allowance for uncollectible accounts and a credit to governmental receivables. At December 31, 2009, management considers governmental receivables to be fully collectible; therefore, no allowance has been recorded.

**(3) Property held for re-sale**

The Organization purchases in-fill lots for construction of new single-family homes under various programs. At December 31, 2009, the Organization held 8 completed homes, 9 homes under construction, and 39 parcels of land. The parcels of land are intended for use in future projects. All property is carried at the lower of cost or market. In 2009, the Organization recorded losses on impairment of \$66,500 for assets held for re-sale. Depreciation is not recorded on property held for re-sale.

**NEIGHBORHOOD HOUSING SERVICES OF PHOENIX, INC.  
AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

Year Ended December 31, 2009

**(3) Property held for re-sale (continued)**

In February 2009, the Organization acquired a subdivision consisting of sixteen nearly completed homes and eighteen vacant lots for a total cost of approximately \$1.4 million. The acquisition was financed through the issuance of a \$2.0 million loan from Neighborhood Housing Services of America – Community Development Financing Institution, a nonprofit public benefit corporation. See Note 8.

**(4) Property and equipment**

Property and equipment consist of:	<b>2009</b>
Cost and donated value:	
Land	\$ 458,964
Office building	2,134,786
Furniture, fixtures, and equipment	166,842
Leasehold improvements	59,393
Total cost and donated value	2,819,985
Accumulated depreciation and amortization	(260,767)
Property and equipment, net	\$ 2,559,218

Depreciation and amortization expense charged to operations was \$77,190 for 2009.

**(5) Mortgage loans receivable**

The Organization extends long-term (up to 30 years) mortgage loans under several programs to enable clients to purchase homes. Interest rates on existing amortizing loans receivable range from 2.0% to 9.5%. The majority of these loans carry interest rates in the range of 5.0% to 7.5%. Deferred and forgivable loans are non-interest bearing. Forgivable loans are generally provided for down payment assistance and the balance is assigned to the City of Phoenix. These forgivable loans require the homeowner to occupy the premises for a period of five to ten years, after which the loan is forgiven. In the event that the homeowner sells the property before the forgivable period has expired, the homeowner must repay the original assistance amount. Therefore, forgivable loans are fully reserved. All loans are generally secured by a deed of trust on the property and certain loans are forgivable if the client meets certain ongoing requirements. Mortgage loans are carried at net realizable value, and consist of the following at December 31, 2009. Management believes that the amount of the allowance is adequate given the nature of the loans and the value of the related collateral.

<b><u>Amortizing loans:</u></b>	<b>2009</b>
Phoenix Family Housing fund	\$ 3,570,531
Homeowner development funds	23,182
NWA loan fund	670,071
	4,263,784
<b><u>Deferred loans (due on sale):</u></b>	
Homeowner development funds	486,463
NWA loan fund	124,909
	611,372

**NEIGHBORHOOD HOUSING SERVICES OF PHOENIX, INC.  
AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

Year Ended December 31, 2009

**(5) Mortgage loans receivable (continued)**

	<b>2009</b>
<b><u>Forgivable loans:</u></b>	
Homeowner development funds	\$ 400,473
Total loans receivable	5,275,629
Less: allowance for uncollectible mortgage loans	(502,125)
Net mortgage loans receivable	\$ 4,773,504

The Organization sells loans to Neighborhood Housing Services of America, Inc. (NHS) on an annual basis. At December 31, 2009 there were no loans outstanding that were specifically held for sale. Amortizing loans totaling approximately \$756,000 are held as security for loans sold with recourse to NHS. Deferred loans are repaid upon sale or transfer of the underlying assets.

Loans are expected to be collected as follows for the years ending December 31,

	<b><u>Amortizing Loan Collections</u></b>
2010	\$ 69,508
2011	74,371
2012	76,936
2013	87,893
2014	83,844
Thereafter	3,871,232
Total	\$ 4,263,784

As of December 31, 2009, amortizing loans were delinquent as follows:

	<b>Number of loans</b>	<b>Operating funds</b>
30 to 60 days	5	\$ 180,274
60 to 90 days	7	460,270
Over 90 days	15	1,290,542
Total	27	\$ 1,931,086

**(6) Loan contingencies**

The Organization occasionally sells certain mortgage loans receivable to NHS. All loans are sold at carrying value. Some loans are sold with recourse under a continuing arrangement with NHS whereby the Organization may sell a certain percentage of its loan portfolio if certain loan reserve criteria are met. Other loans are sold without recourse and are not subject to loan reserve requirements. All such loans are serviced by the Organization in exchange for a .375 percent monthly servicing fee on the outstanding balances of the loans.

Loans sold with recourse under this agreement, which become delinquent, must be substituted with a current loan or repurchased by the Organization. The principal balance of loans sold to NHS and subject to recourse was approximately \$3,750,000 at December 31, 2009. In accordance with FASB ASC 860, *Transfers and Servicing*, this amount is not included in mortgage loans receivable. Management believes that the impact of substituting or repurchasing any delinquent loans would not have a significant impact on consolidated financial results.

**NEIGHBORHOOD HOUSING SERVICES OF PHOENIX, INC.  
AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

Year Ended December 31, 2009

**(7) Recoverable grant**

The Organization has a \$75,000 recoverable grant from a community foundation at 0% interest, which matures April 13, 2010. The outstanding balance at December 31, 2009 was \$75,000. The recoverable grant is to be used to develop single family homes.

**(8) Notes payable**

Notes payable at December 31, 2009 consist of the following:

	<u>Maturity Value</u>	<u>Discount</u>	<u>Current Note Balance</u>
\$250,000 face amount note payable to a bank in quarterly installments of interest only at 2%. Interest is imputed at 6% in accordance with below-market-rate interest rules. The note is due July 6, 2013 and is unsecured.	\$ 250,000	\$ 31,358	\$ 218,642
\$50,000 face amount note payable to a bank in quarterly installments of interest only at 2%-4%. Interest is imputed at 8% in accordance with below-market-rate interest rules. The note is due December 10, 2011 and is unsecured.	50,000	3,569	46,431
\$2,000,000 face amount note payable to a nonprofit public benefit corporation in monthly installments of interest at 6% with periodic principal payments upon sale of subject purchase inventory. The note is due September 29, 2010 and is secured.	959,324	-	959,324
\$1,000,000 face amount note payable to a U.S. Government Corporation in quarterly installments of interest only at 3%. Interest is imputed at 4.75% in accordance with below-market-rate interest rules. The note is due May 17, 2010 and is unsecured.	1,000,000	10,168	989,832
\$250,000 face amount note payable to a bank in quarterly installments of interest only at 2%. Interest is imputed at 5% in accordance with below-market-rate interest rules. The note is due September 8, 2018 and is unsecured.	250,000	67,528	182,472
\$250,000 face amount note payable to a bank payable in quarterly installments of interest only at 3%. Interest is imputed at 5.25% in accordance with below-market-rate interest rules. The note is due June 23, 2011 and is unsecured.	250,000	8,063	241,937

**NEIGHBORHOOD HOUSING SERVICES OF PHOENIX, INC.  
AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

Year Ended December 31, 2009

**(8) Notes payable (continued)**

	<u>Maturity Value</u>	<u>Discount</u>	<u>Current Note Balance</u>
\$250,000 face amount note payable to a bank payable in quarterly installments of interest only at 3%. Interest is imputed at 6% in accordance with below-market-rate interest rules. The note is due June 23, 2011 and is unsecured.	\$ 250,000	\$ 10,682	\$ 239,318
\$250,000 face amount note payable to a bank payable in quarterly installments of interest only at 3%. Interest is imputed at 6.75% in accordance with below-market-rate interest rules. The note is due June 23, 2011 and is unsecured.	250,000	13,268	236,732
\$250,000 face amount note payable to a bank payable in quarterly installments of interest only at 3%. Interest is imputed at 8% in accordance with below-market-rate interest rules. The note is due June 23, 2011 and is unsecured.	250,000	18,775	231,225
\$250,000 face amount note payable to a bank payable in quarterly installments of interest only at 3%. Interest is imputed at 8.25% in accordance with below-market-rate interest rules. The note is due June 23, 2011 and is unsecured.	250,000	20,118	229,882
\$500,000 face amount note payable to a bank payable in quarterly installments of interest only at 3%. Interest is imputed at 8.75% in accordance with below-market-rate interest rules. The note is due June 23, 2011 and is unsecured.	500,000	42,449	457,551
\$250,000 face amount note payable to a bank payable in quarterly installments of interest only at 3%. Interest is imputed at 8.75% in accordance with below-market-rate interest rules. The note is due June 23, 2011 and is unsecured.	250,000	17,504	232,496
\$250,000 face amount note payable to a bank payable in quarterly installments of interest only at 3%. Interest is imputed at 8.25% in accordance with below-market-rate interest rules. The note is due June 5, 2017 and is unsecured.	250,000	73,091	176,909
\$300,000 face amount note payable to a bank payable in quarterly installments of interest only at 2%. Interest is imputed at 2% in accordance with below-market-rate interest rules. The note is due June 24, 2012 and is unsecured.	300,000	10,111	289,889

**NEIGHBORHOOD HOUSING SERVICES OF PHOENIX, INC.  
AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

Year Ended December 31, 2009

**(8) Notes payable (continued)**

	<b>Maturity Value</b>	<b>Discount</b>	<b>Current Note Balance</b>
<p>\$1,100,000 face amount note payable to a bank payable in monthly installments of principal and interest at 5.10%. Interest is imputed at 8% in accordance with below-market-rate interest rules. The note is due May 1, 2014 and is secured by an office building.</p>	1,057,693	108,950	948,743
Total notes payable	\$ 6,117,017	\$ 435,634	\$ 5,681,383

Maturities of notes payable are as follows:

**Years Ending December 31,**

2010	\$ 1,972,017
2011	2,050,000
2012	300,000
2013	250,000
2014	1,045,000
Thereafter	500,000
Total	\$ 6,117,017

Certain loans contain various financial and non-financial covenants that require the Organization to obtain a minimum net revenue and maintain certain debt coverage ratio. The Organization did not meet certain of these financial covenants for the year ended December 31, 2009. The Organization obtained waiver letters from the respective lenders for the covenant violations.

**(9) Temporarily restricted net assets**

Temporarily restricted net assets were restricted for the following purposes:

**Homeowner development funds:**

Providing down payment grants and loans to low and moderate income families borrowing under various programs, and development of affordable housing units, included in cash and cash equivalents, property held for re-sale and mortgage loans receivable in the accompanying consolidated statement of financial position.

\$ 3,196,327

**NWA loan funds:**

Providing down payment grants and loans to low and moderate income families borrowing under various programs, and development of affordable housing units, included in cash and cash equivalents, property held for re-sale and mortgage loans receivable in the accompanying consolidated statement of financial position.

200,000

**NEIGHBORHOOD HOUSING SERVICES OF PHOENIX, INC.  
AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

Year Ended December 31, 2009

**(9) Temporarily restricted net assets (continued)**

**Agency funds:**

Providing education and resources to Arizona Housing Counseling Collaborative, included in cash and cash equivalents in the accompanying consolidated statement of financial position.

\$ 34,003

Arizona Foreclosure Prevention Task Force

104,522

Glendale FWRA

4,504

**Phoenix Housing Partnership, LLC:**

Development of affordable housing units included in property held for re-sale in the accompanying consolidated statement of financial position.

196,428

Total temporarily restricted net assets

\$ 3,735,784

Revenue earned from the use of the above net assets is also temporarily restricted for eligible activities.

**(10) Permanently restricted net assets**

The Organizations' endowment consists of funds restricted for the NWA loan fund. Net assets associated with endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions.

In September 2008, the State of Arizona enacted ARS § 10-1180 et seq. Investments for Elecnosynary Purposes (IFEP). The Board of Directors of the Organization has interpreted IFEP as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary.

As a result of this interpretation, the Organization classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, and (b) the original value of subsequent gifts to the permanent endowment. The earnings of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Organization in a manner consistent with the standard of prudence prescribed by IFEP.

In accordance with NWA Fund agreement, the Organization is required to invest and use the endowment and its earnings to purchase housing opportunities for qualifying low-income individuals. In addition, the Organization may fund mortgage loans to low-income qualifying individuals to purchase these properties or other qualifying properties.

**NEIGHBORHOOD HOUSING SERVICES OF PHOENIX, INC.  
AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

Year Ended December 31, 2009

**(10) Permanently restricted net assets (continued)**

The changes in endowment net assets for the year ended December 31, 2009 are as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Endowment net assets, January 1, 2009	\$ -	\$ -	\$ 2,356,920	\$ 2,356,920
Contributions	-	-	190,000	190,000
Investment return:				
Investment income	-	30,677	-	30,677
Appropriation of endowment earnings for expenditure	30,677	(30,677)	-	-
Expenditure of endowment earnings	(30,677)	-	-	(30,677)
Capital conversion of endowment net assets	<u>758,311</u>	<u>200,000</u>	<u>(958,311)</u>	<u>-</u>
Endowment net assets, December 31, 2009	<u>\$ 758,311</u>	<u>\$ 200,000</u>	<u>\$ 1,588,609</u>	<u>\$ 2,546,920</u>

During 2009, NeighborWorks America converted \$958,311 of the endowment funds to be used for operating activities, thereby releasing the funds from restriction.

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level that the donor or IFEP requires the Organization to retain as a fund of perpetual duration. There were no such deficiencies as of December 31, 2009.

**(11) Commitments and other contingencies**

The Organization participates in numerous program grants and contracts. These grants, contracts and agreements are subject to financial and compliance audits by other parties. The purpose of these audits is to ensure compliance with the terms of the grant, contract, or agreement. Grantor agencies may, at their discretion, request reimbursement for expenses or return of funds, or both, as a result of noncompliance by the Organization with terms of the grants or contracts. Lenders may, at their discretion, request repayment of the outstanding loan balances as a result of noncompliance with the debt agreements.

The Organization leases equipment under a lease agreement expiring in May 2013. Minimum future rental payments under the operating lease at December 31, 2009 are as follows:

**Years Ending December 31,**

2010	\$ 8,640
2011	8,640
2012	8,640
2013	<u>3,600</u>
Total future minimum lease payments	<u>\$ 29,520</u>

In the normal course of business, operating leases are generally renewed or replaced by other leases. Total rental expense for operating leases with terms in excess of one month was \$13,708 for the year ended December 31, 2009.

**NEIGHBORHOOD HOUSING SERVICES OF PHOENIX, INC.  
AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

Year Ended December 31, 2009

**(11) Commitments and other contingencies (continued)**

The Organization has the following commitments under construction and predevelopment contracts at December 31, 2009 which are typically funded through operations:

Predevelopment contracts for the Isaac development	\$ 52,289
Predevelopment contracts for the Target Area B development	<u>17,493</u>
Total commitments under construction and predevelopment contracts	<u>\$ 69,782</u>

**(12) Adjusted net worth – HUD Title II Loan Correspondent**

As a Title II Loan Correspondent, the Organization is required by the U.S. Department of Housing and Urban Development (HUD) to maintain adjusted net worth of \$50,000, as defined in the *Consolidated Audit Guide for Audits of HUD Programs*.

The calculation of net worth is as follows:

Unrestricted net assets per the consolidated statement of financial position of Neighborhood Housing Services of Phoenix, Inc.	\$ 2,516,332
Less: unacceptable assets	<u>(415)</u>
Adjusted net worth for HUD retirement programs	2,515,917
Amount required by HUD	<u>50,000</u>
Adjusted net worth above HUD requirement	<u>\$ 2,465,917</u>

**(13) Economic dependency**

The Organization receives a significant amount, approximately 53%, of public support and revenue either directly or indirectly from the Arizona Department of Housing. Loss of this revenue in the future could have a materially adverse effect on the programs offered by the Organization.

**(14) Concentration of credit risk**

The Organization extends loans to low and moderate-income residents of a limited geographic area. Although loans are collateralized by the borrowers' property, a risk exists that property values may fall below the loan values creating a concentration of credit risk.

**(15) Pension plan**

The Organization established a 401(k) plan effective January 1, 2004. The plan covers all employees over the age of 21 who work at least 1,000 hours and have one year of service. Employees may contribute up to 100% of compensation not to exceed \$16,500 in 2009. The Organization may make a discretionary matching contribution to be determined annually by the board of directors. No matching contributions have been determined for 2009.