

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

**CONSOLIDATED FINANCIAL STATEMENTS AND
OMB CIRCULAR A-133 SUPPLEMENTARY REPORTS**

Year Ended December 31, 2008

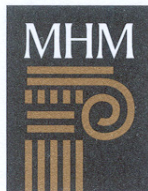
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CONTENTS

	<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 - 19
OMB CIRCULAR A-133 SUPPLEMENTARY REPORTS	
Schedule of Expenditures of Federal Awards	20
Notes to the Schedule of Expenditures of Federal Awards	21
Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <i>Government Auditing Standards</i>	22 - 23
Report on Compliance with Requirements Applicable to Each Major Program and on Internal Control Over Compliance in Accordance with OMB Circular A-133	24 - 25
Schedule of Findings and Questioned Costs	26- 27



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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, 2008, 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, 2008, 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.

In accordance with *Government Auditing Standards*, we have also issued our report dated March 18, 2009 on our consideration of **Neighborhood Housing Services of Phoenix, Inc. and Subsidiaries'** internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Our audit was performed for the purpose of forming an opinion on the basic consolidated financial statements taken as a whole. The accompanying Schedule of Expenditures of Federal Awards is presented for purpose of additional analysis and is not a required part of the basic consolidated financial statements. The Schedule of Expenditures of Federal Awards is required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. The information in that schedule has been subjected to the auditing procedures applied in the audit of the basic consolidated financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic consolidated financial statements taken as a whole.

Phoenix, Arizona
March 18, 2009

Mayer Hoffman McCann P.C.

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

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

December 31, 2008

ASSETS

Neighborhood Housing Services of Phoenix, Inc.

	Operating Funds	Homeowner Development Funds	NWA Loan Fund	Total All Funds	Phoenix Housing Partnership, LLC	La Ciudad, LLC	Eliminations	Total
Cash and cash equivalents	\$ 1,003,376	\$ 1,458,563	\$ 93,855	\$ 2,555,794	\$ 66,248	\$ 10,635	\$ -	\$ 2,632,677
Restricted cash	113,868	-	-	113,868	-	24,213	-	138,081
Governmental receivables	4,781	50,000	-	54,781	-	-	-	54,781
Other receivables	85,756	2,033	100,000	187,789	-	-	(101,033)	86,756
Property held for re-sale	450,683	783,837	1,480,000	2,714,520	130,000	-	-	2,844,520
Prepaid expenses and deposits	20,662	1,000	-	21,662	-	4,186	-	25,848
Mortgage loans receivable, net	3,714,376	426,543	683,065	4,823,984	-	-	-	4,823,984
Property and equipment, net	38,344	-	-	38,344	-	2,516,808	-	2,555,152
Investment in subsidiaries	-	1,700,495	-	1,700,495	-	-	(1,700,495)	-
TOTAL ASSETS	\$ 5,431,846	\$ 4,422,471	\$ 2,356,920	\$ 12,211,237	\$ 196,248	\$ 2,555,842	\$ (1,801,528)	\$ 13,161,799

LIABILITIES AND NET ASSETS

LIABILITIES								
Accounts payable and accrued expenses	\$ 45,126	\$ 325,351	\$ -	\$ 370,477	\$ -	\$ 108,643	\$ (101,033)	\$ 378,087
Accrued compensated absences	29,127	-	-	29,127	-	-	-	29,127
Advances on contracts	-	4,851	-	4,851	-	-	-	4,851
Loan impounds and client deposits	-	627,091	-	627,091	-	-	-	627,091
Recoverable grant	-	71,451	-	71,451	-	-	-	71,451
Notes payable	3,360,246	-	-	3,360,246	-	943,079	-	4,303,325
TOTAL LIABILITIES	3,434,499	1,028,744	-	4,463,243	-	1,051,722	(101,033)	5,413,932
NET ASSETS								
Unrestricted	1,997,347	-	-	1,997,347	-	1,504,120	(1,504,121)	1,997,346
Temporarily restricted	-	3,393,727	-	3,393,727	196,248	-	(196,374)	3,393,601
Permanently restricted	-	-	2,356,920	2,356,920	-	-	-	2,356,920
TOTAL NET ASSETS	1,997,347	3,393,727	2,356,920	7,747,994	196,248	1,504,120	(1,700,495)	7,747,867
TOTAL LIABILITIES AND NET ASSETS	\$ 5,431,846	\$ 4,422,471	\$ 2,356,920	\$ 12,211,237	\$ 196,248	\$ 2,555,842	\$ (1,801,528)	\$ 13,161,799

See Notes to Consolidated Financial Statements

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

CONSOLIDATED STATEMENT OF ACTIVITIES

Year Ended December 31, 2008

	<u>Neighborhood Housing Services of Phoenix, Inc.</u>				<u>Phoenix Housing Partnership,</u>		<u>La Ciudad,</u>				
	<u>Operating Funds</u>	<u>Homeowner Development Funds</u>	<u>NWA Loan Fund</u>	<u>Total All Funds</u>	<u>LLC</u>	<u>LLC</u>	<u>Eliminations</u>	<u>Total</u>	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>
SUPPORT AND REVENUE											
Public support											
Governmental grants	\$ 267,799	\$ 278,414	\$ 185,000	\$ 731,213	\$ -	\$ -	\$ -	\$ 731,213	\$ 267,799	\$ 278,414	\$ 185,000
Nongovernmental grants and contributions	500,956	2,500	-	503,456	-	-	-	503,456	500,956	2,500	-
Contributions in kind	77,861	5,255	-	83,116	-	-	-	83,116	77,861	5,255	-
Total support	846,616	286,169	185,000	1,317,785	-	-	-	1,317,785	846,616	286,169	185,000
Revenue											
Fees	675,085	174,810	-	849,895	-	122,907	(123,707)	849,095	674,285	174,810	-
Interest income on mortgages	181,404	1,579	17,818	200,801	-	-	-	200,801	199,222	1,579	-
Investment income	74,567	13,203	5,389	93,159	1,100	344	(21,602)	73,001	58,698	14,303	-
Loss on investment in subsidiaries	-	(250,783)	-	(250,783)	-	-	250,783	-	-	-	-
Total revenue	931,056	(61,191)	23,207	893,072	1,100	123,251	105,474	1,122,897	932,205	190,692	-
Net assets released from program restrictions - satisfaction of restrictions	-	-	-	-	-	-	-	-	368,180	(368,180)	-
Total support and revenue	1,777,672	224,978	208,207	2,210,857	1,100	123,251	105,474	2,440,682	2,147,001	108,681	185,000
EXPENSES											
Program services											
Homebuyer education	607,558	285	-	607,843	-	-	(64,615)	543,228	543,228	-	-
Loan services	318,272	-	-	318,272	-	-	(10,961)	307,311	307,311	-	-
Affordable housing development	224,067	182,229	-	406,296	-	-	(42,172)	364,124	364,124	-	-
Phoenix Housing Partnership, LLC	-	-	-	-	196,378	-	-	196,378	196,378	-	-
La Ciudad, LLC	-	-	-	-	-	178,758	-	178,758	178,758	-	-
Total program services	1,149,897	182,514	-	1,332,411	196,378	178,758	(117,748)	1,589,799	1,589,799	-	-
Supporting services											
Management and general	378,479	33,717	-	412,196	-	-	(23,419)	388,777	388,777	-	-
Community outreach	85,480	-	-	85,480	-	-	(2,071)	83,409	83,409	-	-
Resource development	113,775	-	-	113,775	-	-	(2,071)	111,704	111,704	-	-
Total supporting services	577,734	33,717	-	611,451	-	-	(27,561)	583,890	583,890	-	-
Total expenses	1,727,631	216,231	-	1,943,862	196,378	178,758	(145,309)	2,173,689	2,173,689	-	-
Change in net assets before transfers in (out)	50,041	8,747	208,207	266,995	(195,278)	(55,507)	250,783	266,993	(26,688)	108,681	185,000
Transfers in (out)	(76,728)	99,935	(23,207)	-	-	-	-	-	-	-	-
Change in net assets	(26,687)	108,682	185,000	266,995	(195,278)	(55,507)	250,783	266,993	(26,688)	108,681	185,000
NET ASSETS, beginning of year	2,024,034	3,284,920	2,171,920	7,480,874	391,526	1,559,627	(1,951,153)	7,480,874	2,024,034	3,284,920	2,171,920
Equity contributions	-	125	-	125	-	-	(125)	-	-	-	-
Equity distributions	-	-	-	-	-	-	-	-	-	-	-
NET ASSETS, end of year	\$ 1,997,347	\$ 3,393,727	\$ 2,356,920	\$ 7,747,994	\$ 196,248	\$ 1,504,120	\$ (1,700,495)	\$ 7,747,867	\$ 1,997,346	\$ 3,393,601	\$ 2,356,920

See Notes to Consolidated Financial Statements

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

CONSOLIDATED STATEMENT OF FUNCTIONAL EXPENSES

Year Ended December 31, 2008

	Program Services						Supporting Services				
	Homebuyer Education	Loan Services	Affordable Housing Development	Phoenix Housing Partnership, LLC		Subtotal	Management and General	Community Outreach	Resource Development	Subtotal	Total
				La Ciudad, LLC							
Salaries and wages	\$ 349,093	\$ 120,913	\$ 151,907	\$ -	\$ -	\$ 621,913	\$ 178,438	\$ 54,105	\$ 57,935	\$ 290,478	\$ 912,391
Employee benefits/payroll taxes	61,321	20,710	25,489	-	-	107,520	22,646	7,005	7,263	36,914	144,434
Total salaries, wages and related expenses	<u>410,414</u>	<u>141,623</u>	<u>177,396</u>	<u>-</u>	<u>-</u>	<u>729,433</u>	<u>201,084</u>	<u>61,110</u>	<u>65,198</u>	<u>327,392</u>	<u>1,056,825</u>
Professional fees	30,186	20,930	26,302	-	-	77,418	35,186	5,750	14,257	55,193	132,611
Rent	64,614	10,961	19,771	-	-	95,346	23,419	2,071	2,071	27,561	122,907
Operating supplies	20,530	6,987	5,248	-	305	33,070	3,979	2,125	2,135	8,239	41,309
Property taxes	-	-	581	-	18,863	19,444	140	-	-	140	19,584
Telephone and utilities	9,574	2,067	3,623	-	14,110	29,374	3,290	718	1,819	5,827	35,201
Postage and printing	1,127	3,122	234	-	-	4,483	922	700	824	2,446	6,929
Equipment rental and maintenance	13,081	8,027	3,976	-	332	25,416	5,766	977	2,310	9,053	34,469
Advertising and marketing	2,007	269	910	-	-	3,186	-	9,826	19,493	29,319	32,505
Travel and training	15,399	2,180	3,171	-	-	20,750	1,393	486	3,142	5,021	25,771
Repairs and maintenance	10,053	1,628	9,624	-	10,205	31,510	3,191	307	307	3,805	35,315
Insurance	5,616	2,198	2,473	-	3,124	13,411	2,606	606	826	4,038	17,449
Dues and subscriptions	969	253	838	-	23	2,083	299	70	446	815	2,898
Other expenses	747	135	4,753	-	-	5,635	3,682	-	47	3,729	9,364
Interest	-	116,017	21,601	-	75,610	213,228	122,579	-	-	122,579	335,807
Subsidies to clients	-	-	123,223	-	-	123,223	-	-	-	-	123,223
Property loss reserve	-	-	-	196,304	-	196,304	-	-	-	-	196,304
Bad debt expense	12,000	-	-	-	-	12,000	1,800	-	-	1,800	13,800
Hospitality	5,360	-	-	-	-	5,360	-	75	-	75	5,435
Total expenses before depreciation and amortization	<u>601,677</u>	<u>316,397</u>	<u>403,724</u>	<u>196,304</u>	<u>122,572</u>	<u>1,640,674</u>	<u>409,336</u>	<u>84,821</u>	<u>112,875</u>	<u>607,032</u>	<u>2,247,706</u>
Depreciation and amortization	6,165	1,875	2,572	74	56,186	66,872	2,860	659	900	4,419	71,291
Total expenses before eliminations	<u>607,842</u>	<u>318,272</u>	<u>406,296</u>	<u>196,378</u>	<u>178,758</u>	<u>1,707,546</u>	<u>412,196</u>	<u>85,480</u>	<u>113,775</u>	<u>611,451</u>	<u>2,318,997</u>
Eliminations	(64,614)	(10,961)	(42,172)	-	-	(117,747)	(23,419)	(2,071)	(2,071)	(27,561)	(145,308)
Total Expenses	<u>\$ 543,228</u>	<u>\$ 307,311</u>	<u>\$ 364,124</u>	<u>\$ 196,378</u>	<u>\$ 178,758</u>	<u>\$ 1,589,799</u>	<u>\$ 388,777</u>	<u>\$ 83,409</u>	<u>\$ 111,704</u>	<u>\$ 583,890</u>	<u>\$ 2,173,689</u>

See Notes to Consolidated Financial Statements

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

CONSOLIDATED STATEMENT OF CASH FLOWS

Year Ended December 31, 2008

CASH FLOWS FROM OPERATING ACTIVITIES	
Change in net assets	\$ 266,993
Adjustments to reconcile change in net assets to net cash provided by operating activities:	
Depreciation and amortization	71,291
Unrealized loss on real estate held for sale	196,304
Change in imputed interest rate	139,027
Changes in operating assets and liabilities:	
Decrease (increase) in:	
Governmental receivables	(23,246)
Other receivables	(3,115)
Prepaid expenses and deposits	(12,120)
Increase (decrease) in:	
Accounts payable and accrued expenses	193,929
Accrued compensated absences	6,644
Advances on contracts	306
Net cash provided by operating activities	<u>836,013</u>
CASH FLOWS FROM INVESTING ACTIVITIES	
Purchase of property and equipment	(42,187)
Change in loan impounds and client deposits	69,482
Payments received on mortgage loans receivable	139,910
Proceeds from sale of property held for re-sale	731,900
Purchase of property held for re-sale	(1,914,518)
Change in restricted cash	(25,764)
Mortgage loans issued	<u>(2,629,760)</u>
Net cash used in investing activities	<u>(3,670,937)</u>
CASH FLOWS FROM FINANCING ACTIVITIES	
Payments on line of credit	(213,991)
Proceeds from recoverable grant	71,451
Proceeds from notes payable	176,714
Payments on notes payable	<u>(516,924)</u>
Net cash used in financing activities	<u>(482,750)</u>
NET CHANGE IN CASH AND CASH EQUIVALENTS	(3,317,674)
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	<u>5,950,351</u>
CASH AND CASH EQUIVALENTS, END OF YEAR	<u>\$ 2,632,677</u>
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION	
Cash paid for interest	<u>\$ 179,192</u>

See Notes to Consolidated Financial Statements

NEIGHBORHOOD HOUSING SERVICES OF PHOENIX, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Year Ended December 31, 2008

(1) Organization operations and summary of significant accounting policies

Neighborhood Housing Services of Phoenix, Inc. 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 2008 was predevelopment costs for engineering, infrastructure and legal costs. These costs totaled approximately \$37,800 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 main tenant occupying 6,600 square feet (62%) of the rentable space. La Ciudad intends to rent the remaining available space to unrelated tenants.

Basis of consolidation – Neighborhood Housing Services of Phoenix, Inc. (the “Organization”) and its wholly-owned subsidiaries, Phoenix Housing Partnership, LLC and La Ciudad, LLC, have adopted the provisions of the American Institute of Certified Public Accountants Statement of Position 94-3, *Reporting for Related Entities by Not-for-Profit Organizations*, 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.

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Year Ended December 31, 2008

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

Basis of presentation – The accompanying financial statements are presented in accordance with Statement of Financial Accounting Standards (SFAS) No. 117, *Financial Statements of Not-for-Profit Organizations*. Under SFAS No. 117, 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 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. and unrelated tenants.

Management's use of estimates – The preparation of consolidated financial statements in conformity with U.S. generally accepted accounting principles 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 SFAS No. 116, *Accounting for Contributions Received and Contributions Made*. In accordance with SFAS No. 116, 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 restrictions 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, 2008

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

Cash – 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 \$24,213 specifically reserved for the replacement and leasing reserve. Additionally, in 2008, the Organization received cash to be used for specific purposes. At December 31, 2008, \$113,868 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 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, 2008, the Organization recorded approximately \$20,000 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 gifts 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 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, 2008

(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 SFAS No. 144, *Accounting for the Impairment of Long-Lived Assets*. SFAS No. 144 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 SFAS No. 116 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 donations. 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 for these donated services did not meet the recognition conditions under SFAS No. 116.

Government grants – The Organization receives grants from various city, state and federal agencies. The Organization recognizes revenues for these grants as services are provided. Funding sources may, at their discretion, request reimbursement for expense 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 \$32,505 in 2008.

Functional allocations of expenses – The costs of providing various programs and other activities has been summarized on a functional basis in the 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, 2008

(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 Cuidad, 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”). FIN 48 was originally effective for fiscal years beginning after December 15, 2006. FIN 48 clarifies the accounting for uncertainty in income taxes recognized in accordance with FASB Statement No. 109. In December 2008, the FASB issued FASB Staff Position No. FIN 48-3, *Effective Date of FASB Interpretation No. 48 for Certain Nonpublic Enterprises* (“FSP FIN 48-3”) which extended the period of adoption of FIN 48 to fiscal years beginning after December 15, 2008. The Organization has elected to defer the application of FIN 48 in accordance with FSP FIN 48-3. 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.

(2) Governmental receivables

Governmental receivables consist of:

	2008
Navajo Housing Authority – U.S. Department of Housing and Urban Development (HUD)	\$ 50,000
NeighborWorks America – U.S. Department Treasury Counseling Reimbursement	2,624
Arizona State University	1,500
City of Phoenix – Community Development Block Grant (CDGB) Counseling Reimbursement	657
Total governmental receivables	\$ 54,781

Government 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 its 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 government receivables. At December 31, 2008, management considers government 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, 2008, the Organization held four completed homes, three homes under construction, and twenty one 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 2008, the Organization recorded a loss of \$196,304 on impairment for certain assets held for re-sale. The loss is included in property loss reserve on the consolidated statement of functional expenses. 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, 2008

(4) Fair value measurements

SFAS No. 157 establishes a common definition for fair value to be applied to U.S. generally accepted accounting principles requiring use of fair value, establishes a framework for measuring fair value, and expands disclosures about such fair value measurements. Issued in February 2008, FASB Staff Position No. 157-1, *Application of FASB Statement No. 157 to FASB Statement No. 13 and Other Accounting Pronouncements That Address Fair Value Measurements for Purposes of Lease Classification or Measurement under Statement 13*, removed leasing transactions accounted for under Statement No. 13 and related guidance from the scope of SFAS No. 157. FASB Staff Position No. 157-2, *Partial Deferral of the Effective Date of Statement 157*, deferred the effective date of SFAS No. 157 for all nonfinancial assets and nonfinancial liabilities to fiscal years beginning after November 15, 2008. The Organization is still assessing the impact of SFAS No. 157 on their nonfinancial assets.

The Organization adopted SFAS No. 157 as of January 1, 2008 for financial assets and financial liabilities subject to fair value measurement on a recurring basis. There was no material impact on the Organization's consolidated financial statements for the adoption of this standard.

SFAS No. 157 establishes a hierarchy for ranking the quality and reliability of the information used to determine fair values. SFAS No. 157 requires that assets and liabilities carried at fair value be classified and disclosed in one of the following three categories:

- Level 1: Unadjusted quoted market prices in active markets for identical assets or liabilities.
- Level 2: Unadjusted quoted prices in active markets for similar assets or liabilities, unadjusted quoted prices for identical or similar assets or liabilities in markets that are not active, or inputs other than quoted prices that are observable for the asset or liability.
- Level 3: Unobservable inputs for the asset or liability.

The following table summarizes the valuation of the Organization's financial instruments by the above SFAS No. 157 categories as of December 31, 2008:

	<u>Total</u>	<u>Unadjusted Quoted Market Prices (Level 1)</u>	<u>Significant Other Observable Inputs (Level 2)</u>
Cash and cash equivalents	\$ 2,632,677	\$ 2,632,677	\$ -
Restricted cash	138,081	138,081	-
Property held for re-sale	2,844,520	-	2,844,520

The financial instruments above were valued utilizing quoted market prices. The property held for re-sale was valued utilizing quoted prices in active markets for similar assets. The Organization currently has no other financial instruments subject to fair value measurement on a recurring basis.

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Year Ended December 31, 2008

(5) Property, equipment and construction in process

	2008
Property and equipment consist of:	
Cost and donated value:	
Land	\$ 458,964
Office building	2,134,786
Furniture, fixtures, and equipment	143,700
Leasehold improvements	1,279
Total cost and donated value	2,738,729
Accumulated depreciation	(183,577)
Property and equipment, net	\$ 2,555,152

Depreciation expense charged to operations was \$71,291 for 2008.

(6) Mortgage loans receivable

The Organization extends long-term, up to 30 year, mortgage loans under several programs to enable clients to purchase homes. Interest rates on existing amortizing loans receivable range from 5.5% to 9.5%. The majority of these loans carry interest rates in the range of 5.5% to 6.5%. 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, 2008. Management believes that the amount of the allowance is adequate given the nature of the loans and the value of the related collateral.

<u>Amortizing loans:</u>	2008
Phoenix Family Housing fund	\$ 3,716,468
Homeowner development funds	25,488
NWA loan fund	555,065
	4,297,021
<u>Deferred loans (due on sale):</u>	
Homeowner development funds	406,055
NWA loan fund	130,000
Phoenix Family Housing Fund	11,408
	547,463
<u>Forgivable loans:</u>	
Homeowner development funds	314,054
Total loans receivable	5,158,538
Less: allowance for uncollectible mortgage loans	(334,554)
Net mortgage loans receivable	\$ 4,823,984

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Year Ended December 31, 2008

(6) Mortgage loans receivable (continued)

The Organization sells loans to Neighborhood Housing Services of America, Inc. (NHTSA) on an annual basis. At December 31, 2008 there were no loans outstanding that were specifically held for sale. Amortizing loans totaling approximately \$776,000 are held as security for loans sold with recourse to NHTSA. 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,

	Amortizing Loan Collections
2009	\$ 67,661
2010	73,566
2011	77,497
2012	80,123
2013	91,367
Thereafter	<u>3,906,807</u>
Total	<u>\$ 4,297,021</u>

As of December 31, 2008, amortizing loans were delinquent as follows:

	Number of loans	Operating funds
30 to 60 days	4	\$ 304,255
60 to 90 days	5	358,461
Over 90 days	<u>5</u>	<u>503,710</u>
Total	<u>14</u>	<u>\$ 1,166,426</u>

(7) Loan contingencies and line of credit

The Organization occasionally sells certain mortgage loans receivable to NHTSA. All loans are sold at carrying value. Some loans are sold with recourse under a continuing arrangement with NHTSA 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 .3750 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 NHTSA and subject to recourse was approximately \$3,800,000 at December 31, 2008. In accordance with SFAS No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishment of Liabilities*, this amount is not included in loans receivable. Management believes that the impact of substituting or repurchasing any delinquent loans would not have a significant impact on consolidated financial results.

The Organization had a \$750,000 bank line of credit at 8.25% interest, which matured July 31, 2008. The line of credit was used to fund construction projects. The line was collateralized by the property and improvements to the property for which the line of credit was used. The line was paid in full and not renewed.

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Year Ended December 31, 2008

(8) 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, 2008 was \$71,451. The recoverable grant is to be used to develop single family homes.

(9) Notes payable

Notes payable at December 31, 2008 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	\$ 39,181	\$ 210,819
\$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	5,202	44,798
\$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	35,835	964,165
\$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	73,285	176,715
\$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	13,099	236,901
\$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	17,292	232,708

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Year Ended December 31, 2008

(9) Notes payable (continued)

	Maturity Value	Discount	Current Note balance
\$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	\$ 21,401	\$ 228,599
\$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	29,245	220,755
\$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	31,136	218,864
\$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	66,173	433,827
\$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	28,071	221,929
\$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	79,835	170,165
\$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 the office building.	1,073,205	130,125	943,080
Total notes payable	\$ 4,873,205	\$ 569,880	\$ 4,303,325

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Year Ended December 31, 2008

(9) Notes payable (continued)

Maturities of notes payable are as follows:

Years Ending December 31,

2009	\$ 16,923
2010	1,011,282
2011	2,050,000
2012	-
2013	250,000
Thereafter	<u>1,545,000</u>
Total	<u>\$ 4,873,205</u>

(10) 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 mortgages receivable on the accompanying consolidated statement of financial position \$ 3,167,477

Providing education and resources to the Arizona Housing Counseling Collaborative, included in cash and cash equivalents on the accompanying consolidated statement of financial position 29,878

Phoenix Housing Partnership, LLC:

Development of affordable housing units included in properties held for re-sale in the accompanying consolidated statement of financial position 196,246

Total temporarily restricted net assets \$ 3,393,601

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

(11) 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 June 2008, the State of Arizona enacted a version of the Uniform Prudent Management of Institutional Funds Act ("SPMIFA"). The Board of Directors of the Organization has interpreted SPMIFA 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.

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Year Ended December 31, 2008

(11) Permanently restricted net assets (continued)

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 SPMIFA.

In August 2008, the FASB issued FSP FAS 117-1, *Endowments of Not-for-Profit Organizations: Net Asset Classification of Funds Subject to an Enacted Version of the Uniform Prudent Management of Institutional Funds Act, and Enhanced Disclosures for All Endowment Funds*. The Organization reviewed the changes to the law regarding net asset classification of endowments. The Organization had no changes to its net asset classification as a result of this law as of January 1, 2008.

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.

The changes in endowment net assets for the year ended December 31, 2008 are as follows:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Endowment net assets, January 1, 2008	\$ -	\$ -	\$ -	\$ 2,171,920
Contributions	-	-	185,000	185,000
Investment return:				
Investment income	-	23,207	-	23,207
Appropriation of endowment earnings for expenditure	23,207	(23,207)	-	-
Expenditure of endowment earnings	<u>(23,207)</u>	<u>-</u>	<u>-</u>	<u>(23,207)</u>
Endowment net assets, December 31, 2008	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 2,356,920</u>

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 SPMIFA requires the Organization to retain as a fund of perpetual duration. There were no such deficiencies as of December 31, 2008.

(12) 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.

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Year Ended December 31, 2008

(12) Commitments and other contingencies (continued)

The Organization leases equipment under a lease agreement expiring in May 2013. Minimum future rental payments under the operating lease at December 31, 2008 are as follows:

Years Ending December 31,

2009	\$	8,640
2010		8,640
2011		8,640
2012		8,640
2013		<u>3,600</u>
Total future minimum lease payments	\$	<u>38,160</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 \$11,746 for the year ended December 31, 2008.

The Organization has the following commitments under construction and predevelopment contracts at December 31, 2008 which are typically funded through operations:

Predevelopment contracts for the Isaac development	\$	58,059
Predevelopment contracts for the Target Area B development		17,493
Predevelopment contracts for infill development		<u>129,797</u>
Total commitments under construction and predevelopment contracts	\$	<u>205,349</u>

(13) 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 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 statement of financial position of Neighborhood Housing Services of Phoenix, Inc.	\$	1,997,347
Less: unacceptable assets		<u>(430)</u>
Adjusted net worth for HUD retirement programs		1,996,917
Amount required by HUD		<u>50,000</u>
Adjusted net worth above HUD requirement	\$	<u>1,946,917</u>

(14) Economic dependency

The Organization receives a significant amount, approximately 26%, of public support and revenue either directly or indirectly from the City of Phoenix and NeighborWorks America. Loss of this revenue in the future could have a materially adverse effect on the programs offered by the Organization.

(15) 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.

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Year Ended December 31, 2008

(16) 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 \$15,500 in 2008. The Organization may make a discretionary matching contribution to be determined annually by the board of directors. No matching contributions have been determined for 2008.

(17) Subsequent events

In February 2009, the Organization acquired a subdivision consisting of sixteen nearly completed homes and eighteen vacant lots with a total cost of approximately \$1.4 million. The acquisition was financed using approximately \$1.4 million of a line of credit from Neighborhood Housing Services of America - Community Development Financial Institution, a nonprofit public benefit corporation. The line of credit bears interest at 6% and interest is payable monthly. The principal and outstanding interest is payable September 29, 2010. The loan is collateralized by the acquired subdivision property.

**OMB CIRCULAR A-133
SUPPLEMENTARY REPORTS**

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

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

Year Ended December 31, 2008

Federal Grantor / Pass-Through Grantor / Program	Federal CFDA Number	Grantor's Number	Federal Expenditures
U.S. Department of Housing and Urban Development			
City of Phoenix:			
Community Development Block Grant	14.218	121992	\$ 9,050
Community Development Block Grant	14.218	124722	657
Community Development Block Grant	14.218	98421	153,414
Local Incentive Support Corporation:			
Community Development Block Grant	14.218	40904-0020	19,775
Community Development Block Grant	14.218	40904-0017	<u>2,334</u>
			185,230
Navajo Housing Authority:			
Indian Housing Block Grants	14.XXX	109-000-962	<u>114,430</u>
Total U.S. Department of Housing and Urban Development			<u>299,660</u>
U.S. Department of Treasury			
NeighborWorks America - Capital Grant - nonexpendable	21.000	None	993,750
NeighborWorks America - Operating Grant - expendable	21.000	None	<u>227,442</u>
Total U.S. Department of Treasury			<u>1,221,192</u>
Corporation for National and Community Service			
Arizona State University:			
Americorps	94.006	09-090	<u>2,000</u>
Total Corporation for National and Community Service			<u>2,000</u>
TOTAL EXPENDITURES OF FEDERAL AWARDS			<u>\$ 1,522,852</u>

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

NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

Year Ended December 31, 2008

(1) Basis of presentation

The accompanying schedule of expenditures of federal awards includes the federal grant activity of ***Neighborhood Housing Services of Phoenix, Inc. and Subsidiaries*** and is presented on the accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of *U.S. Office of Management and Budget (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 basic consolidated financial statements. ***Neighborhood Housing Services of Phoenix, Inc. and Subsidiaries*** did not provide federal awards to subrecipients during the year ended December 31, 2008.

(2) Catalog of federal domestic assistance (CFDA) numbers

The program titles and CFDA numbers were obtained from the 2008 *Catalog of Federal Domestic Assistance*.



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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 of

NEIGHBORHOOD HOUSING SERVICES OF PHOENIX, INC. AND SUBSIDIARIES

We have audited the consolidated financial statements of ***Neighborhood Housing Services of Phoenix, Inc. and Subsidiaries*** at December 31, 2008 and for the year then ended, and have issued our report thereon dated March 18, 2009. 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.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered ***Neighborhood Housing Services of Phoenix, Inc. and Subsidiaries***' internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the consolidated financial statements, but not for the purpose of expressing an opinion on the effectiveness of the ***Neighborhood Housing Services of Phoenix, Inc. and Subsidiaries***' internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of ***Neighborhood Housing Services of Phoenix, Inc. and Subsidiaries***' internal control of financial reporting.

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

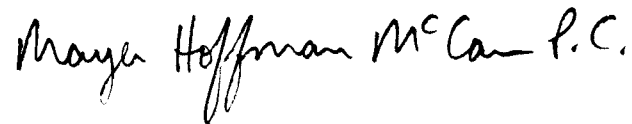
A *material weakness* is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the consolidated financial statements will not be prevented or detected by the entity's internal control.

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

Compliance and Other Matters

As part of obtaining reasonable assurance about whether **Neighborhood Housing Services of Phoenix, Inc. and Subsidiaries'** consolidated 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 consolidated financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

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

A handwritten signature in black ink that reads "Mayer Hoffman McCann P.C." in a cursive script.

Phoenix, Arizona
March 18, 2009



Mayer Hoffman McCann P.C.

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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 of

NEIGHBORHOOD HOUSING SERVICES OF PHOENIX, INC. AND SUBSIDIARIES

Compliance

We have audited the compliance of **Neighborhood Housing Services of Phoenix, Inc. and Subsidiaries** 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 December 31, 2008. **Neighborhood Housing Services of Phoenix, Inc and Subsidiaries'** major federal programs are identified in the summary of auditor's 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 their major federal programs is the responsibility of **Neighborhood Housing Services of Phoenix, Inc. and Subsidiaries'** management. Our responsibility is to express an opinion on **Neighborhood Housing Services of Phoenix, Inc. and Subsidiaries'** 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 **Neighborhood Housing Services of Phoenix, Inc. and Subsidiaries'** 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 **Neighborhood Housing Services of Phoenix, Inc. and Subsidiaries'** compliance with those requirements.

In our opinion, **Neighborhood Housing Services of Phoenix, Inc. and Subsidiaries** 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 December 31, 2008.

Internal Control Over Compliance

The management of ***Neighborhood Housing Services of Phoenix, Inc. and Subsidiaries*** 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 ***Neighborhood Housing Services of Phoenix, Inc. and Subsidiaries'*** 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 an opinion on compliance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of ***Neighborhood Housing Services of Phoenix, Inc. and Subsidiaries'*** internal control over compliance.

A *control deficiency* in an entity'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 noncompliance with a type of compliance requirement of a federal program on a timely basis. A *significant deficiency* is a control deficiency, or combination of control deficiencies, that adversely affects the entity'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 that is more than inconsequential will not be prevented or detected by the entity's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results 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 entity's internal control.

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

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

Mayer Hoffman McCann P.C.

Phoenix, Arizona
March 18, 2009

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

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

Year Ended December 31, 2008

I. SUMMARY OF INDEPENDENT AUDITORS' RESULTS

A. Type of Auditors' Report Issued on the Consolidated Financial Statements:

The Independent Auditors' Report on the basic consolidated financial statements of **Neighborhood Housing Services of Phoenix, Inc. and Subsidiaries** at and for the year ended December 31, 2008 was an unqualified opinion.

B. Significant Deficiencies in Internal Control Disclosed by the Audit of the Consolidated Financial Statements:

The audit of the basic consolidated financial statements of **Neighborhood Housing Services of Phoenix, Inc. and Subsidiaries** at and for the year ended December 31, 2008 disclosed no matters involving the internal control over financial reporting and its operations that are considered to be significant deficiencies or material weaknesses.

C. Noncompliance Material to the Consolidated Financial Statements:

The audit disclosed no instances of noncompliance material to the basic consolidated financial statements of **Neighborhood Housing Services of Phoenix, Inc. and Subsidiaries** at and for the year ended December 31, 2008.

D. Significant Deficiencies in Internal Control over Major Programs:

The audit of compliance of **Neighborhood Housing Services of Phoenix, Inc. and Subsidiaries** at and for the year ended December 31, 2008 disclosed no matters involving the internal controls over major programs that are considered to be significant deficiencies or material weaknesses.

E. Type of Auditors' Report Issued on Compliance for Major Programs:

The Independent Auditors' Report on compliance with requirements applicable to each major Federal program for the year ended December 31, 2008 was an unqualified opinion.

F. Findings Relating to Major Programs:

As indicated in Section III below, the audit disclosed no findings relating to major programs for the year ended December 31, 2008.

G. Major Programs:

<u>CFDA Number</u>	<u>Name of Federal Program</u>	<u>Amount Expended</u>
21.000	NeighborWorks America	\$ <u>1,221,192</u>

H. Threshold for Distinguishing Between Type A and Type B Programs:

The threshold for distinguishing between Type A and Type B programs was \$300,000 for the year ended December 31, 2008.

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

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

Year Ended December 31, 2008

I. SUMMARY OF INDEPENDENT AUDITORS' RESULTS (continued)

I. Qualifications of Auditee as a Low-Risk Auditee:

Neighborhood Housing Services of Phoenix, Inc. qualified as a low-risk auditee under applicable provisions of OMB Circular A-133 for the year ended December 31, 2008.

II. FINANCIAL STATEMENT AUDIT FINDINGS

None

III. FEDERAL AWARDS FINDINGS AND QUESTIONED COSTS

None

IV. STATUS OF PRIOR AUDIT FINDINGS

Item: 2007-01

Subject: Client file documentation

Condition: Twelve of the fifteen client files tested did not contain one or more pieces of required documentation. Of the twelve files with lacking documentation the number of files lacking specific documentation was as follows: five files lacked documentation specifying and referring additional community resources to assist the client, six files lacked documentation of a counseling plan, twelve files lacked client consent for the counseling plan, seven files lacked documentation of client progress, and eight files lacked documentation of the client's need to obtain housing.

Criteria: In accordance with the NeighborWorks America contract agreement, **Neighborhood Housing Services of Phoenix, Inc. and Subsidiaries** is required to maintain documentation for each counseling session regarding the following: identification of additional resources available to the client, creation of a counseling plan, client consent for the counseling plan, recommendation of additional counseling sessions, monitoring of client progress, and existence of the client's need to obtain housing.

Effect: **Neighborhood Housing Services of Phoenix, Inc. and Subsidiaries** is not in compliance with the grant requirements. As a result, funding sources could request the return of funds.

Recommendation: We recommend that **Neighborhood Housing Services of Phoenix, Inc. and Subsidiaries** thoroughly review client file documentation on a continuous basis and update information as required by the grant contract.

Current Status: **Neighborhood Housing Services of Phoenix, Inc. and Subsidiaries** implemented a new client file system to ensure all required and appropriate documentation is maintained in accordance with grant requirements. We performed a similar test in the current year and noted no issues.