

HEARTH, INC. AND AFFILIATES
COMBINING FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009
TOGETHER WITH
INDEPENDENT AUDITOR'S REPORT

HEARTH, INC. AND AFFILIATES

CONTENTS
DECEMBER 31, 2010 AND 2009

	<u>PAGES</u>
INDEPENDENT AUDITOR'S REPORT	1
COMBINING FINANCIAL STATEMENTS:	
Combining Statements of Financial Position	2 - 3
Combining Statements of Activities	4 - 5
Combining Statements of Changes in Net Assets	6
Combining Statements of Cash Flows	7
Combining Statements of Functional Expenses	8 - 9
Notes to Combining Financial Statements	10 - 25



CERTIFIED PUBLIC ACCOUNTANTS
& BUSINESS ADVISORS

Where Every Client Is A Valued Client

Alexander, Aronson, Finning & Co., P.C.

21 East Main Street, Westborough, MA 01581-1461 (508) 366-9100
Boston, MA (617) 205-9100 Wellesley, MA (781) 965-9100
www.aafcpa.com FAX (508) 366-9789 info@aafcpa.com

INDEPENDENT AUDITOR'S REPORT

To the Board of Directors of
Hearth, Inc. and Affiliates:

We have audited the accompanying combining statements of financial position of Hearth, Inc. (a Massachusetts corporation, not for profit) and Affiliates (collectively, Hearth) as of December 31, 2010 and 2009, and the related combining statements of activities, changes in net assets, cash flows, and functional expenses for the years then ended. These combining financial statements are the responsibility of Hearth's management. Our responsibility is to express an opinion on these combining financial statements based on our audits.

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

In our opinion, the combining financial statements referred to above present fairly, in all material respects, the combining financial position of Hearth, Inc. and Affiliates as of December 31, 2010 and 2009, and the changes in their net assets and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Alexander, Aronson, Finning & Co., P.C.

Wellesley, Massachusetts
April 13, 2011

HEARTH, INC. AND AFFILIATES

COMBINING STATEMENT OF FINANCIAL POSITION
DECEMBER 31, 2010

<u>ASSETS</u>	<u>OPERATING</u>	<u>RENTAL PROPERTY</u>	<u>PROPERTY MANAGE- MENT</u>	<u>REAL ESTATE DEVELOPMENT</u>	<u>ELIMI- NATIONS</u>	<u>TOTAL</u>
CURRENT ASSETS:						
Cash and cash equivalents	\$ 1,411,835	\$ 171,115	\$ -	\$ -	\$ -	\$ 1,582,950
Funds held in trust	44,933	-	-	-	-	44,933
Accounts receivable	191,138	326	-	-	-	191,464
Prepaid expenses and deposits	78,332	9,185	1,256	-	-	88,773
Current portion of due from affiliates, net	51,000	150,000	-	-	-	201,000
Total current assets	<u>1,777,238</u>	<u>330,626</u>	<u>1,256</u>	<u>-</u>	<u>-</u>	<u>2,109,120</u>
PROPERTY AND EQUIPMENT:						
Land	-	390,600	-	-	-	390,600
Buildings and improvements	173,781	3,332,133	-	-	(220,269)	3,285,645
Furniture and equipment	540,015	150,400	-	-	-	690,415
Construction in progress	-	-	-	1,296,317	(30,800)	1,265,517
	<u>713,796</u>	<u>3,873,133</u>	<u>-</u>	<u>1,296,317</u>	<u>(251,069)</u>	<u>5,632,177</u>
Less - accumulated depreciation	573,370	981,300	-	-	-	1,554,670
Net property and equipment	<u>140,426</u>	<u>2,891,833</u>	<u>-</u>	<u>1,296,317</u>	<u>(251,069)</u>	<u>4,077,507</u>
OTHER ASSETS:						
Other reserves	-	67,972	-	-	-	67,972
Investments	271,396	-	-	-	-	271,396
Due from affiliates, net of current portion	563,686	(360,776)	157,038	174,086	-	534,034
Investment in affiliate	-	-	-	240,000	-	240,000
Financing fees, net	-	58,791	-	-	-	58,791
Development fee receivable	-	-	-	53,569	(53,569)	-
Total other assets	<u>835,082</u>	<u>(234,013)</u>	<u>157,038</u>	<u>467,655</u>	<u>(53,569)</u>	<u>1,172,193</u>
Total assets	<u>\$ 2,752,746</u>	<u>\$ 2,988,446</u>	<u>\$ 158,294</u>	<u>\$ 1,763,972</u>	<u>\$ (304,638)</u>	<u>\$ 7,358,820</u>
<u>LIABILITIES AND NET ASSETS</u>						
CURRENT LIABILITIES:						
Current portion of long-term debt	\$ -	\$ 13,510	\$ -	\$ -	\$ -	\$ 13,510
Accounts payable and accrued expenses	245,272	17,460	1,674	605,686	-	870,092
Funds held in trust	44,933	-	-	-	-	44,933
Total current liabilities	<u>290,205</u>	<u>30,970</u>	<u>1,674</u>	<u>605,686</u>	<u>-</u>	<u>928,535</u>
OTHER LIABILITIES:						
Accounts payable - long-term	-	-	-	-	-	-
Long-term debt and deferred interest, net of current portion	-	702,295	-	-	(379,849)	322,446
Contingent debt	-	2,150,000	-	-	-	2,150,000
Total other liabilities	<u>-</u>	<u>2,852,295</u>	<u>-</u>	<u>-</u>	<u>(379,849)</u>	<u>2,472,446</u>
Total liabilities	<u>290,205</u>	<u>2,883,265</u>	<u>1,674</u>	<u>605,686</u>	<u>(379,849)</u>	<u>3,400,981</u>
NET ASSETS:						
Unrestricted -						
Operating	2,041,819	5,959	156,620	(9,039)	-	2,195,359
Board designated	107,351	-	-	-	-	107,351
Property and equipment	140,426	99,222	-	-	75,211	314,859
Real estate development	-	-	-	1,017,325	-	1,017,325
Total unrestricted	<u>2,289,596</u>	<u>105,181</u>	<u>156,620</u>	<u>1,008,286</u>	<u>75,211</u>	<u>3,634,894</u>
Temporarily restricted	172,945	-	-	150,000	-	322,945
Total net assets	<u>2,462,541</u>	<u>105,181</u>	<u>156,620</u>	<u>1,158,286</u>	<u>75,211</u>	<u>3,957,839</u>
Total liabilities and net assets	<u>\$ 2,752,746</u>	<u>\$ 2,988,446</u>	<u>\$ 158,294</u>	<u>\$ 1,763,972</u>	<u>\$ (304,638)</u>	<u>\$ 7,358,820</u>

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

HEARTH, INC. AND AFFILIATES

COMBINING STATEMENT OF FINANCIAL POSITION
DECEMBER 31, 2009

<u>ASSETS</u>			<u>PROPERTY</u>			
	<u>OPERATING</u>	<u>RENTAL</u>	<u>MANAGE-</u>	<u>REAL ESTATE</u>	<u>ELIMI-</u>	<u>TOTAL</u>
		<u>PROPERTY</u>	<u>MENT</u>	<u>DEVELOPMENT</u>	<u>NATIONS</u>	
CURRENT ASSETS:						
Cash and cash equivalents	\$ 970,183	\$ 110,595	\$ -	\$ -	\$ -	\$ 1,080,778
Funds held in trust	43,166	-	-	-	-	43,166
Accounts receivable	190,887	2,857	-	-	-	193,744
Prepaid expenses and deposits	87,790	9,321	1,651	-	-	98,762
Current portion of due from affiliates, net	184,844	75,818	10,165	-	-	270,827
Total current assets	<u>1,476,870</u>	<u>198,591</u>	<u>11,816</u>	<u>-</u>	<u>-</u>	<u>1,687,277</u>
PROPERTY AND EQUIPMENT:						
Land	-	390,600	-	-	-	390,600
Buildings and improvements	157,491	3,332,133	-	-	(220,269)	3,269,355
Furniture and equipment	503,537	150,400	-	-	-	653,937
Construction in progress	-	-	-	473,903	-	473,903
	<u>661,028</u>	<u>3,873,133</u>	<u>-</u>	<u>473,903</u>	<u>(220,269)</u>	<u>4,787,795</u>
Less - accumulated depreciation	539,288	868,258	-	-	-	1,407,546
Net property and equipment	<u>121,740</u>	<u>3,004,875</u>	<u>-</u>	<u>473,903</u>	<u>(220,269)</u>	<u>3,380,249</u>
OTHER ASSETS:						
Other reserves	-	67,760	-	-	-	67,760
Investments	239,214	-	-	-	-	239,214
Due from affiliates, net of current portion	755,091	(322,931)	95,150	169,843	-	697,153
Investment in affiliate	-	-	-	240,000	-	240,000
Financing fees, net	-	61,431	-	-	-	61,431
Development fee receivable	-	-	-	78,569	(53,569)	25,000
Total other assets	<u>994,305</u>	<u>(193,740)</u>	<u>95,150</u>	<u>488,412</u>	<u>(53,569)</u>	<u>1,330,558</u>
Total assets	<u>\$ 2,592,915</u>	<u>\$ 3,009,726</u>	<u>\$ 106,966</u>	<u>\$ 962,315</u>	<u>\$ (273,838)</u>	<u>\$ 6,398,084</u>
<u>LIABILITIES AND NET ASSETS</u>						
CURRENT LIABILITIES:						
Current portion of long-term debt	\$ -	\$ 12,418	\$ -	\$ -	\$ -	\$ 12,418
Accounts payable and accrued expenses	219,800	23,321	1,405	-	-	244,526
Funds held in trust	43,166	-	-	-	-	43,166
Total current liabilities	<u>262,966</u>	<u>35,739</u>	<u>1,405</u>	<u>-</u>	<u>-</u>	<u>300,110</u>
OTHER LIABILITIES:						
Accounts payable - long-term	-	-	-	119,087	-	119,087
Long-term debt and deferred interest, net of current portion	-	697,120	-	-	(361,380)	335,740
Contingent debt	-	2,047,695	-	-	-	2,047,695
Total other liabilities	<u>-</u>	<u>2,744,815</u>	<u>-</u>	<u>119,087</u>	<u>(361,380)</u>	<u>2,502,522</u>
Total liabilities	<u>262,966</u>	<u>2,780,554</u>	<u>1,405</u>	<u>119,087</u>	<u>(361,380)</u>	<u>2,802,632</u>
NET ASSETS:						
Unrestricted -						
Operating	1,992,314	(36,191)	105,561	(7,883)	-	2,053,801
Board designated	107,351	-	-	-	-	107,351
Property and equipment	121,740	265,363	-	-	87,542	474,645
Real estate development	-	-	-	781,240	-	781,240
Total unrestricted	<u>2,221,405</u>	<u>229,172</u>	<u>105,561</u>	<u>773,357</u>	<u>87,542</u>	<u>3,417,037</u>
Temporarily restricted	108,544	-	-	69,871	-	178,415
Total net assets	<u>2,329,949</u>	<u>229,172</u>	<u>105,561</u>	<u>843,228</u>	<u>87,542</u>	<u>3,595,452</u>
Total liabilities and net assets	<u>\$ 2,592,915</u>	<u>\$ 3,009,726</u>	<u>\$ 106,966</u>	<u>\$ 962,315</u>	<u>\$ (273,838)</u>	<u>\$ 6,398,084</u>

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

HEARTH, INC. AND AFFILIATES

COMBINING STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED DECEMBER 31, 2010

CHANGES IN UNRESTRICTED NET ASSETS:

OPERATING REVENUES:

Rental fees, net and program revenues	\$ 1,356,731	\$ 313,216	\$ 100,898	\$ -	\$ (63,115)	\$ 1,707,730
Government grants and other contracts	933,065	-	-	-	-	933,065
Private grants, contributions and special events, net	481,424	-	-	-	-	481,424
Management and service fees	77,260	-	21,626	-	-	98,886
Other	14,788	-	-	-	-	14,788
Investment income	11,845	127	-	-	-	11,972
Developer fee revenue	-	-	-	30,800	(30,800)	-
Net assets released from purpose restrictions	79,585	-	-	-	-	79,585
Total operating revenues	<u>2,954,698</u>	<u>313,343</u>	<u>122,524</u>	<u>30,800</u>	<u>(93,915)</u>	<u>3,327,450</u>

OPERATING EXPENSES:

Outreach	287,725	-	-	-	-	287,725
Housing and supportive services	1,949,184	306,183	-	17,586	(63,115)	2,209,838
Property management	-	-	71,465	-	-	71,465
General and administration	405,865	71,871	12,175	2,996	-	492,907
Institutional advancement	262,712	-	-	-	-	262,712
Total operating expenses before depreciation and amortization	2,905,486	378,054	83,640	20,582	(63,115)	3,324,647
Depreciation and amortization	34,082	115,682	-	-	-	149,764
Total operating expenses	<u>2,939,568</u>	<u>493,736</u>	<u>83,640</u>	<u>20,582</u>	<u>(63,115)</u>	<u>3,474,411</u>
Changes in unrestricted net assets from operations	15,130	(180,393)	38,884	10,218	(30,800)	(146,961)

OTHER REVENUES (EXPENSES):

Predevelopment and capital grants	-	3,000	-	173,227	-	176,227
Recovery of affiliate advances	73,266	-	-	-	-	73,266
Unrealized gain on investments	26,227	-	-	-	-	26,227
Interest on deferred debt	-	(18,469)	-	-	18,469	-
General partner operating expenses	-	-	-	(1,156)	-	(1,156)
Net assets released from capital restrictions	10,610	-	-	79,644	-	90,254
Total other revenues (expenses)	<u>110,103</u>	<u>(15,469)</u>	<u>-</u>	<u>251,715</u>	<u>18,469</u>	<u>364,818</u>
Changes in unrestricted net assets	125,233	(195,862)	38,884	261,933	(12,331)	217,857

CHANGES IN TEMPORARILY RESTRICTED NET ASSETS:

Grants	154,596	-	-	159,773	-	314,369
Net assets released from restrictions	(90,195)	-	-	(79,644)	-	(169,839)
Changes in temporarily restricted net assets	64,401	-	-	80,129	-	144,530
Changes in net assets	<u>\$ 189,634</u>	<u>\$ (195,862)</u>	<u>\$ 38,884</u>	<u>\$ 342,062</u>	<u>\$ (12,331)</u>	<u>\$ 362,387</u>

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

HEARTH, INC. AND AFFILIATES

COMBINING STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED DECEMBER 31, 2009

CHANGES IN UNRESTRICTED NET ASSETS:	OPERATING	RENTAL PROPERTY	PROPERTY MANAGEMENT	REAL ESTATE DEVELOPMENT	ELIMI- NATIONS	TOTAL
OPERATING REVENUES:						
Rental fees, net and program revenues and vacancies	\$ 1,376,325	\$ 321,833	\$ 108,076	\$ -	\$ (61,275)	\$ 1,744,959
Government grants and other contracts	972,994	-	-	-	-	972,994
Private grants, contributions and special events, net	630,349	2,000	-	-	-	632,349
Management and service fees	60,843	-	10,165	-	-	71,008
Investment income	6,492	374	-	-	-	6,866
Net assets released from purpose restrictions	16,180	-	-	42,131	-	58,311
Total operating revenues	<u>3,063,183</u>	<u>324,207</u>	<u>118,241</u>	<u>42,131</u>	<u>(61,275)</u>	<u>3,486,487</u>
OPERATING EXPENSES:						
Outreach	269,760	-	-	-	-	269,760
Housing and supportive services	1,889,328	300,445	-	42,131	(61,275)	2,170,629
Property management	-	-	66,123	-	-	66,123
General and administration	374,638	66,802	10,593	6,750	-	458,783
Institutional advancement	241,137	-	-	-	-	241,137
Total operating expenses before depreciation and amortization	<u>2,774,863</u>	<u>367,247</u>	<u>76,716</u>	<u>48,881</u>	<u>(61,275)</u>	<u>3,206,432</u>
Depreciation and amortization	26,773	116,538	-	-	-	143,311
Total operating expenses	<u>2,801,636</u>	<u>483,785</u>	<u>76,716</u>	<u>48,881</u>	<u>(61,275)</u>	<u>3,349,743</u>
Changes in unrestricted net assets from operations	<u>261,547</u>	<u>(159,578)</u>	<u>41,525</u>	<u>(6,750)</u>	<u>-</u>	<u>136,744</u>
OTHER REVENUES (EXPENSES):						
Predevelopment and capital grants	38,242	-	-	-	-	38,242
Recovery of affiliate advances	333,525	-	-	-	-	333,525
Unrealized gain on investments	39,130	-	-	-	-	39,130
Interest on deferred debt	-	(17,294)	-	-	17,294	-
General partner operating expenses	-	-	-	(674)	-	(674)
Net assets released from capital restrictions	-	-	-	49,106	-	49,106
Total other revenues (expenses)	<u>410,897</u>	<u>(17,294)</u>	<u>-</u>	<u>48,432</u>	<u>17,294</u>	<u>459,329</u>
Changes in unrestricted net assets	<u>672,444</u>	<u>(176,872)</u>	<u>41,525</u>	<u>41,682</u>	<u>17,294</u>	<u>596,073</u>
CHANGES IN TEMPORARILY RESTRICTED NET ASSETS:						
Grants	81,125	-	-	-	-	81,125
Net assets released from restrictions	(16,180)	-	-	(91,237)	-	(107,417)
Changes in temporarily restricted net assets	<u>64,945</u>	<u>-</u>	<u>-</u>	<u>(91,237)</u>	<u>-</u>	<u>(26,292)</u>
Changes in net assets	<u>\$ 737,389</u>	<u>\$ (176,872)</u>	<u>\$ 41,525</u>	<u>\$ (49,555)</u>	<u>\$ 17,294</u>	<u>\$ 569,781</u>

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

HEARTH, INC. AND AFFILIATES

**COMBINING STATEMENTS OF CHANGES IN NET ASSETS
FOR THE YEARS ENDED DECEMBER 31, 2010 AND 2009**

	<u>OPERATING</u>	<u>RENTAL PROPERTY</u>	<u>PROPERTY MANAGE- MENT</u>	<u>REAL ESTATE DEVELOPMENT</u>	<u>ELIMI- NATIONS</u>	<u>TOTAL</u>
NET ASSETS, December 31, 2008	\$ 1,646,705	\$ 339,242	\$ 53,443	\$ 916,033	\$ 70,248	\$ 3,025,671
Changes in net assets	737,389	(176,872)	41,525	(49,555)	17,294	569,781
Transfers	<u>(54,145)</u>	<u>66,802</u>	<u>10,593</u>	<u>(23,250)</u>	<u>-</u>	<u>-</u>
NET ASSETS, December 31, 2009	2,329,949	229,172	105,561	843,228	87,542	3,595,452
Changes in net assets	189,634	(195,862)	38,884	342,062	(12,331)	362,387
Transfers	<u>(57,042)</u>	<u>71,871</u>	<u>12,175</u>	<u>(27,004)</u>	<u>-</u>	<u>-</u>
NET ASSETS, December 31, 2010	<u>\$ 2,462,541</u>	<u>\$ 105,181</u>	<u>\$ 156,620</u>	<u>\$ 1,158,286</u>	<u>\$ 75,211</u>	<u>\$ 3,957,839</u>

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

HEARTH, INC. AND AFFILIATES

**COMBINING STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2010 AND 2009**

	<u>2010</u>	<u>2009</u>
CASH FLOWS FROM OPERATING ACTIVITIES:		
Changes in net assets	\$ 362,387	\$ 569,781
Adjustments to reconcile changes in net assets to net cash provided by operating activities:		
Depreciation and amortization	149,764	143,311
Predevelopment and capital grants	(336,000)	(38,242)
Unrealized gain on investments	(26,227)	(39,130)
Bad debt	1,487	9,774
Changes in operating assets and liabilities -		
Accounts receivable	793	182,636
Prepaid expenses and deposits	9,989	(17,511)
Due (from) to affiliates	232,946	(467,426)
Accounts payable and accrued expenses	19,880	(19,297)
Net cash provided by operating activities	415,019	323,896
CASH FLOWS FROM INVESTING ACTIVITIES:		
Deposits to and interest earned on other reserves	(212)	(10,808)
Predevelopment and capital grants received	336,000	38,242
Payments on development fee receivable	25,000	20,000
Acquisition of property and equipment	(357,783)	(70,054)
Purchases of investments	(5,955)	(6,044)
Net cash used in investing activities	(2,950)	(28,664)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from contingent debt	102,305	75,000
Payments of long-term debt	(12,202)	(11,097)
Net cash provided by financing activities	90,103	63,903
NET INCREASE IN CASH AND CASH EQUIVALENTS	502,172	359,135
CASH AND CASH EQUIVALENTS, beginning of year	1,080,778	721,643
CASH AND CASH EQUIVALENTS, end of year	\$ 1,582,950	\$ 1,080,778
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:		
Cash paid for interest	\$ 21,518	\$ 22,591
Property and equipment financed by accounts payable	\$ 486,599	\$ 27,945

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

HEARTH, INC. AND AFFILIATES
COMBINING STATEMENT OF FUNCTIONAL EXPENSES
FOR THE YEAR ENDED DECEMBER 31, 2009

	PROGRAM SERVICES				SUPPORT SERVICES				TOTAL	
	HOUSING AND SUPPORTIVE SERVICES		PROPERTY MANAGEMENT	TOTAL PROGRAM SERVICES	GENERAL AND ADMINISTRATION		TOTAL SUPPORT SERVICES	ELIMINATIONS		
	HEARTH	REAL ESTATE DEVELOPMENT			RENTAL PROPERTY	ADMINISTRATION				INSTITUTIONAL ADVANCEMENT
EXPENSES:										
Personnel and related -										
Salaries	\$ 1,397,206	\$ 28,141	\$ 34,984	\$ 1,460,331	\$ 49,232	\$ 1,704,092	\$ 351,671	\$ 179,326	\$ 530,997	\$ 2,235,089
Payroll taxes	118,253	1,967	2,811	123,031	3,606	141,284	24,891	12,645	37,536	178,320
Fringe benefits	14,006	1,334	2,290	104,666	3,803	122,475	28,116	11,894	40,010	162,485
Consultants and contracted services	6,744	10,665	-	39,313	1,731	47,788	4,875	3,535	8,410	56,198
Total personnel and related	229,926	1,645,140	42,107	1,727,341	58,372	2,015,639	409,553	207,400	616,953	2,632,592
Occupancy -										
Repairs and maintenance	413	-	53,332	61,039	29	61,481	487	58	-	62,026
Utilities	-	363	67,622	67,985	-	67,985	-	-	-	67,985
Rent	8,833	-	-	-	2,945	11,778	13,251	4,417	-	29,446
Real estate taxes	-	-	16,226	16,226	-	16,226	-	-	-	16,226
Mortgage interest	-	-	22,591	22,591	-	22,591	-	-	-	22,591
Insurance	1,520	2,729	12,848	15,577	2,047	19,144	-	1,520	-	20,664
Total occupancy	10,766	10,799	172,619	183,418	5,021	199,205	13,738	5,995	19,733	218,938
Other -										
Food and household supplies	1,741	-	1,158	94,116	-	95,857	25	-	25	95,882
Professional fees	-	-	4,881	8,002	600	8,602	36,158	3,955	-	48,715
Telephone	4,780	-	94	31,058	644	36,482	9,126	2,394	-	48,002
Printing and copying	1,554	-	2,347	2,347	369	4,270	7,925	9,727	-	21,922
Program supplies and client expenses	16,851	-	550	15,878	-	32,729	-	-	-	32,729
Miscellaneous	596	-	9,776	18,499	143	19,238	5,188	1,094	-	25,520
Insurance	-	20,441	-	20,441	-	20,441	7,563	-	-	28,004
Office expense	793	-	137	6,797	649	8,239	6,657	2,847	-	17,743
Travel and training	1,266	-	3,190	3,190	259	4,715	9,421	515	-	14,651
Postage	1,173	-	96	605	66	1,844	1,814	6,554	-	10,212
Bad debt	-	-	9,774	9,774	-	9,774	-	-	-	9,774
Fundraising expense	-	-	-	-	-	-	-	656	-	656
Recruitment	314	-	-	494	-	808	284	-	-	1,092
Management and administrative fees	-	-	61,275	61,275	-	61,275	-	-	-	(61,275)
Total other	29,068	184,711	87,741	272,476	2,730	304,274	84,161	27,742	(61,275)	354,902
Total expenses before allocations	269,760	1,840,659	42,131	2,183,235	66,123	2,519,118	507,452	241,137	(61,275)	3,206,432
DIRECT SERVICE ALLOCATION										
General and administration allocation	43,276	304,824	6,750	378,376	10,593	432,245	(470,999)	38,754	(432,245)	-
Total expenses before depreciation and amortization	313,036	2,194,152	48,881	2,610,280	76,716	3,000,032	(12,216)	279,891	(61,275)	3,206,432
DEPRECIATION AND AMORTIZATION										
Total expenses	313,406	2,207,561	48,881	2,740,227	76,716	3,130,349	-	280,669	(61,275)	3,349,743

The accompanying notes are an integral part of these combining statements

HEARTH, INC. AND AFFILIATES
NOTES TO COMBINING FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009

(1) **OPERATIONS, NONPROFIT STATUS AND SIGNIFICANT ACCOUNTING POLICIES**

OPERATIONS AND NONPROFIT STATUS

Hearth, Inc. is a nonprofit organization, which was formed in 1991 to eliminate elder homelessness in Boston, Massachusetts. Hearth, Inc. works with other agencies and Boston's homeless shelters to provide outreach, housing, and supportive services to homeless elders or elders at risk of becoming homeless.

Hearth, Inc. is exempt from Federal income taxes as an organization (not a private foundation) formed for charitable purposes under Section 501(c)(3) of the Internal Revenue Code. Hearth, Inc. is also exempt from state income taxes. Contributions made to Hearth, Inc. are deductible within the requirements of the Internal Revenue Code.

SIGNIFICANT ACCOUNTING POLICIES

Hearth, Inc. prepares its combining financial statements in accordance with generally accepted accounting standards and principles established by the Financial Accounting Standards Board (FASB). References to U.S. GAAP in these footnotes are to the FASB Accounting Standards Codification.

Principles of Combination

The combining financial statements include the net assets of Hearth, Inc. and its Affiliates (collectively, *Hearth*): *Hearth Management, Inc.* (*Hearth Mgmt.*), *Hearth Beacon, Inc.* (*Beacon*), *4 Bishop Street, Inc.* (*Bishop*), its majority-owned subsidiary, *CEEH E. Concord, Inc.* (the *General Partner*), *Hearth at Burroughs, LLC* (*Burroughs*), and *Hearth Olmsted Manager LLC* (*Olmsted, LLC*) (see Note 2).

An entity considered to be the primary beneficiary of the VIE has both (a) the power to direct activities of the VIE that most significantly impact the VIE's economic performance and (b) the obligation to absorb losses of the VIE that could potentially be significant to the VIE or the right to receive benefits from the VIE that could potentially be significant to the VIE. Under previous guidance, an entity was considered to be a primary beneficiary when it had the obligation to absorb *expected losses* rather than *potential losses*.

Under this new guidance effective for the year ended December 31, 2010, *Hearth* has determined that the activity of *East Concord Street Limited Partnership's* (the *Partnership*) and *Ruggles Assisted Living Limited Partnership* (*Ruggles*) will not be included in the accompanying combining financial statements since *Hearth* is not the primary beneficiary.

All significant balances between classes of net assets, intercompany balances and transactions have been eliminated in the accompanying combining financial statements.

Cash and Cash Equivalents

Hearth considers all short-term, highly liquid investments with an initial maturity of three months or less to be cash equivalents.

Other Reserves

Other reserves at December 31, 2010 and 2009, consist of replacement reserve accounts at *Beacon*, *Bishop*, and *Burroughs*.

HEARTH, INC. AND AFFILIATES

NOTES TO COMBINING FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009

(Continued)

(1) OPERATIONS, NONPROFIT STATUS AND SIGNIFICANT ACCOUNTING POLICIES
(Continued)

SIGNIFICANT ACCOUNTING POLICIES (Continued)

Accounts and Pledges Receivable

Pledges receivable are recorded at their net present value when unconditionally committed. The allowance for uncollectible accounts and pledges receivable is based on management's estimate of amounts that may be uncollectible, if any. There is no allowance for doubtful accounts at December 31, 2010 and 2009.

Property and Equipment, Construction in Progress and Depreciation

Property and equipment are recorded at cost, if purchased, or at fair market value at the time of the donation. Renewals and betterments are capitalized as additions to the related asset accounts, while repairs and maintenance costs are expensed as incurred. Costs of locating and analyzing potential development sites are expensed as incurred. If a site is located and eventually developed, recoverable costs are capitalized (see below).

Depreciation is provided using the straight-line method over the following estimated useful lives:

Buildings and improvements	5 – 40 years
Furniture and equipment	3 – 10 years

Buildings and improvements in the accompanying combining statements of financial position include leasehold improvements of approximately \$174,000 and \$157,000 at December 31, 2010 and 2009. Depreciation expense during 2010 and 2009 was \$147,124 and \$140,671, respectively.

During 2010 and 2009, Hearth incurred predevelopment costs of approximately \$822,000 and \$49,000, respectively, to develop up to 59 units of low-income elderly housing in Boston, Massachusetts (see page 15). These costs are included in construction in progress in the accompanying combining statements of financial position.

Hearth reviews its investment in real estate for impairment whenever events or changes in circumstances indicate that the carrying value of such property may not be recoverable. Recoverability is measured by a comparison of the carrying amount of the real estate to the future net undiscounted cash flow expected to be generated by the rental property and any estimated proceeds from the eventual disposition of the real estate. If the real estate is considered to be impaired, the impairment to be recognized is measured at the amount by which the carrying amount of the real estate exceeds the fair value of such property. There were no impairment losses recognized in 2010 or 2009.

Financing Fees and Amortization

Financing fees consist of legal and other expenses that are being amortized over the life of the related debt (fifteen and forty years) (see Notes 5 and 6). Financing fees have a cost of \$75,795 as of December 31, 2010 and 2009. Accumulated amortization of financing fees is \$17,004 and \$14,364 as of December 31, 2010 and 2009, respectively. Amortization during 2010 and 2009 was \$2,640.

HEARTH, INC. AND AFFILIATES
NOTES TO COMBINING FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009
(Continued)

(1) OPERATIONS, NONPROFIT STATUS AND SIGNIFICANT ACCOUNTING POLICIES
(Continued)

SIGNIFICANT ACCOUNTING POLICIES (Continued)

Investments

Interest and dividends are recognized when earned. Gains and losses are recognized as incurred upon sale or maturity of investments or based on market value changes during the period.

Revenue Recognition

Rental fees, program revenues, and management and service fees are recorded as services are provided and costs are incurred. Rental fees are recorded net of vacancies of \$31,824 and \$17,250 for 2010 and 2009, respectively. Government grants and other contracts are recorded over the period covered by the grant or contract as services are provided and costs are incurred. Unrestricted grants and contributions are recorded when received or unconditionally committed. Special event revenue is recorded at the time of the event. Investment and other income are recorded as earned.

Donor restricted grants and contributions designated for a specific time period or specific purpose are recognized as temporarily restricted revenue and net assets when received or unconditionally committed. When a donor stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the accompanying combining statements of activities as net assets released from restrictions. Donor restricted grants received and satisfied in the same period are included in unrestricted net assets.

Donated Goods and Services

Hearth receives goods and services from various donating organizations for use in its programs. These goods and services are reflected in private grants, contributions and special events, net and food and household supplies in the accompanying combining financial statements at fair market value. Hearth received \$203 and \$830 of donated food, materials and supplies in 2010 and 2009, respectively.

Hearth receives services of volunteers in various aspects of its programs. The value of these services is not reflected in the accompanying combining financial statements since the value assigned to these services by the donating volunteers is not ascertainable and does not meet the criteria for recognitions of U.S. GAAP.

Allocation Method

Expenses related directly to a function are distributed to that function, while other expenses are allocated based upon management's estimate of the percentage attributable to each function.

Estimates

The preparation of combining financial statements in accordance with U.S. 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 combining financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

HEARTH, INC. AND AFFILIATES
NOTES TO COMBINING FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009
(Continued)

(1) OPERATIONS, NONPROFIT STATUS AND SIGNIFICANT ACCOUNTING POLICIES
(Continued)

SIGNIFICANT ACCOUNTING POLICIES (Continued)

Income Taxes

As discussed on page 10, Hearth and its not-for-profit affiliates, Hearth Mgmt., Beacon, and Bishop (see Note 2), are exempt from income taxes under Section 501(c)(3) of the Internal Revenue Code. Hearth has a for-profit corporate subsidiary, CEEH E. Concord, Inc. (the Subsidiary) (see Note 2). At December 31, 2010, the Subsidiary has, for Federal income tax purposes, net operating loss carryforwards of approximately \$269,000 available to offset future taxable income. Also, at December 31, 2010, the Subsidiary has, for state income tax purposes, net operating loss carryforwards of approximately \$15,000 to offset future taxable income. These carryforwards expire at various dates through 2030. The tax benefit of the net operating loss carryforwards has been fully reserved as of December 31, 2010 and 2009.

Uncertainty in Income Taxes

Hearth follows the *Accounting for Uncertainty in Income Taxes* standards, which requires Hearth to report uncertain tax positions, related interest and penalties, and to adjust its combining financial statements for the impact thereof. As of December 31, 2010, Hearth determined that it had no material unrecognized tax benefits to report. Hearth does not expect a significant increase or decrease to the total amounts of unrecognized tax benefits in 2011. Hearth files tax and information returns in the United States Federal and Massachusetts state jurisdictions. These returns are generally subject to examination by tax authorities for the last three years.

Fair Value

Hearth follows the *Fair Value Measurements and Disclosure* standards. These standards define fair value, establish a framework for measuring fair value under U.S. GAAP, and expand disclosures about fair value measurements. This policy establishes a fair value hierarchy that prioritizes the inputs and assumptions used to measure fair value. Hearth values its qualifying assets and liabilities using Level I inputs. Level I inputs reflect unadjusted quoted prices in active markets for identical assets or liabilities at the measurement date. A qualifying asset or liability's level within the framework is based upon the lowest level of any input that is significant to the fair value measurement.

Subsequent Events

Subsequent events have been evaluated through April 13, 2011, which is the date the combining financial statements were available to be issued. Events that have occurred through April 13, 2011, that met the criteria for recognition and disclosure in the combining financial statements have been properly disclosed (see Note 13).

HEARTH, INC. AND AFFILIATES
 NOTES TO COMBINING FINANCIAL STATEMENTS
 DECEMBER 31, 2010 AND 2009
 (Continued)

(2) NET ASSETS AND RELATED PARTY TRANSACTIONS

NET ASSETS

Hearth's combining financial statements include the following net asset classifications and entities:

Unrestricted

Unrestricted net assets consist of the undesignated net assets of Hearth relating to program services and other operating activities that it is engaged in. Unrestricted net assets also consist of the net book value of Hearth's property and equipment, net of related debt, and Board designated net assets. Board designated net assets may be used with the approval of the Board of Directors.

Temporarily Restricted

Hearth receives grants and contributions which are designated by donors for specific purposes and designated time periods. These grants and contributions are recorded as temporarily restricted net assets until they are expended for their designated purposes or when the designated time periods expire.

Temporarily restricted net assets consist of the following at December 31:

	<u>2010</u>	<u>2009</u>
Restricted for programs	\$171,797	\$ 96,786
Restricted for predevelopment activities (see page 11)	150,000	69,871
Restricted for equipment	<u>1,148</u>	<u>11,758</u>
Total temporarily restricted	<u>\$322,945</u>	<u>\$178,415</u>

Rental Property

The Rental Property net assets consist of affiliates that operate rental properties as follows:

Beacon (a Massachusetts not-for-profit corporation, affiliated with Hearth through common Board of Director membership) operates eight units of housing for formerly homeless elders.

Bishop (a Massachusetts not-for-profit corporation, affiliated with Hearth through common Board of Director membership) operates nine units of housing for formerly homeless women.

Burroughs (a Massachusetts not-for-profit single-member LLC, affiliated with Hearth as the single member) operates fourteen units of housing for formerly homeless elders.

HEARTH, INC. AND AFFILIATES
NOTES TO COMBINING FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009
(Continued)

(2) **NET ASSETS AND RELATED PARTY TRANSACTIONS** (Continued)

NET ASSETS (Continued)

Property Management

Property Management net assets consist of the activities of Hearth Mgmt. Hearth Mgmt. is a Massachusetts not-for-profit corporation, affiliated with Hearth through common Board of Director membership. Hearth Mgmt. provides property management services to Hearth's affiliates and related parties: Beacon, Bishop, Burroughs, Ruggles (see page 18), and the Partnership (see page 16).

Real Estate Development

The Real Estate Development net assets consist of net assets of Hearth that have been designated for investments and advances relating to its subsidiary and affiliates. The Real Estate Development net assets also include the activity of the General Partner and Olmsted, LLC. The General Partner is a Massachusetts for-profit corporation, 79% owned by Hearth. The General Partner holds 1% ownership interest of the Partnership, which operates forty-one units of housing for formerly homeless elders. Olmsted, LLC is a Massachusetts limited liability company with Hearth as its sole member.

Hearth owns the controlling interest in the General Partner. The General Partner has insufficient equity at risk in the Partnership and, based on accounting standards for consolidating entities, the Partnership is deemed a variable interest entity. Under these standards, Hearth has not consolidated the Partnership into the combining financial statements, since the General Partner is not the primary beneficiary.

RELATED PARTY TRANSACTIONS

Transactions between these entities during 2010 and 2009 were as follows:

Hearth maintains the central payroll and pays the payroll and related payroll taxes and benefits for Hearth Mgmt. and the rental properties. Hearth is reimbursed for these amounts. The amounts relating to Hearth Mgmt. and the rental properties during 2010 were \$62,444 and \$43,470, respectively, and during 2009 were \$56,641 and \$40,085, respectively.

Hearth Mgmt. provides property management services to Beacon, Bishop and Burroughs. These amounts are shown as rental fees, net and program revenues in the accompanying combining financial statements and consist of the following for 2010 and 2009, respectively:

<u>2010</u>	<u>Management Services</u>	<u>Administrative Services</u>	<u>Total</u>
Burroughs	\$13,264	\$13,891	\$27,155
Beacon	8,779	9,201	17,980
Bishop	<u>8,779</u>	<u>9,201</u>	<u>17,980</u>
	<u>\$30,822</u>	<u>\$32,293</u>	<u>\$63,115</u>

HEARTH, INC. AND AFFILIATES
NOTES TO COMBINING FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009
(Continued)

(2) NET ASSETS AND RELATED PARTY TRANSACTIONS (Continued)

RELATED PARTY TRANSACTIONS (Continued)

<u>2009</u>	<u>Management Services</u>	<u>Adminis- trative Services</u>	<u>Total</u>
Burroughs	\$12,877	\$13,486	\$26,363
Beacon	8,523	8,933	17,456
Bishop	<u>8,523</u>	<u>8,933</u>	<u>17,456</u>
	<u>\$29,923</u>	<u>\$31,352</u>	<u>\$61,275</u>

Management and administrative fees are paid based upon available cash flow. Management fees have a first priority in payment from available cash flow.

Hearth has a \$166,700 development fee note receivable from Beacon for services provided during the development of the project. The note accrues interest at 6%, compounded annually. Principal and interest payments are due annually if a certain cash flow level, as defined in the agreement, is achieved. Accrued interest on this note at December 31, 2010 and 2009, is \$159,580 and \$141,111, respectively, including \$18,469 and \$17,294 of interest for 2010 and 2009, respectively. Beacon has not made any payments on the note since the cash flow level has not been achieved. In addition, Beacon does not expect to generate the level of cash flow to make future payments on this note. Hearth has reserved the interest due for 2010 and 2009.

Hearth also has a development fee agreement with Burroughs, which includes development fees and development overhead with a ceiling of \$85,000 provided there were enough funds to cover the fee. As of December 31, 2010 and 2009, \$53,569 of the development fee has been earned by Hearth. Any unpaid amounts bear no interest. The development fees earned are included in development fee receivable and long-term debt in the accompanying combining financial statements. The above development notes receivable and accrued interest have been eliminated in the accompanying combining financial statements.

Hearth and the General Partner have entered into the following transactions and agreements with the Partnership:

The Partnership rents office space to Hearth at an annual rental of \$30,329 and \$29,446 in 2010 and 2009, respectively.

Hearth Mgmt. has an agreement with the Partnership to provide property management services. The management fee is 4% of total effective income, as defined in the agreement, and either party can terminate the agreement with ninety days written notice. The Partnership also pays an administrative fee to Hearth Mgmt., as defined in the agreement. Hearth Mgmt. charged the Partnership approximately \$24,000 and \$23,600 for management and administrative staff (including payroll taxes and fringe benefits) during 2010 and 2009, respectively. Hearth Mgmt. also charged an administrative fee of approximately \$23,900 and \$23,200 during 2010 and 2009, respectively.

Hearth provides maintenance and security staff to the Partnership and charged the Partnership approximately \$181,000 and \$177,000 during 2010 and 2009, respectively, for salaries, payroll taxes and related benefits.

HEARTH, INC. AND AFFILIATES
NOTES TO COMBINING FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009
(Continued)

(2) **NET ASSETS AND RELATED PARTY TRANSACTIONS** (Continued)

RELATED PARTY TRANSACTIONS (Continued)

The Subsidiary and the Partnership have entered into an incentive management fee agreement. The fee is for 49.5% of distributable cash flow, as defined in the agreement. No fee can be paid during the low-income housing tax credit compliance period. Accordingly, there is no fee owed for 2010 or 2009. The fee is also limited to 2% of gross rents.

The Partnership owes \$134,927 and \$278,486 to Hearth and Hearth Mgmt. at December 31, 2010 and 2009, respectively, which are included in due from (to) affiliates, net in the accompanying combining statements of financial position. During 2010, the Partnership has revised its operating projections, which will enable the Partnership to repay Hearth earlier than previously expected. Under the revised projections, the Partnership expects to repay Hearth between \$17,000 and \$31,000 annually through 2016. Accordingly, Hearth has recorded a recovery of affiliate advances of \$73,266 in the accompanying combining financial statements during 2010, to reflect the change in repayment period and reversal of the allowance for uncollectible amounts. This receivable has been discounted using a 3% rate. A summary of the amount due from the Partnership at December 31, 2010, is as follows:

Gross receivable	\$134,927
Less – discount	<u>(10,689)</u>
	<u>\$124,238</u>

Hearth has contracted with the Partnership for a development fee of \$400,000 for services provided during the development of the project. Hearth collected the remaining balance of the development fee of \$25,000 in 2010.

The Partnership has granted Hearth an option to purchase the limited partner's interest in the Partnership at the end of the low-income housing tax credit compliance period (December, 2012). The purchase price will be based upon the formula defined in the Partnership agreement. Hearth's rights under this agreement are not assignable without the consent of the limited partner.

The General Partner is obligated to contribute funds to the Partnership to cover operating deficits. If there is future cash flow, contributions are repayable to the General Partner, without interest.

Hearth has guaranteed the full, timely and unconditional payment and performance of all of the General Partner's obligations under the Partnership Agreement. Hearth's guarantee of the General Partner's obligation to make operating deficit contributions is limited to \$400,000.

During the development of the Partnership's project, Hearth provided loans to the Partnership to fund development costs and also sold the building to the Partnership in exchange for notes. These notes are secured by mortgages on the land and building. Payment of these notes will be applied to accrued interest and then to principal from available cash flow. Interest on these notes compounds annually, and on one note semi-annually, at rates ranging from 6.26% to 7%. There were no payments due for 2010 or 2009, since there was no available cash flow. All unpaid principal and accrued interest are due on dates ranging from September, 2025, to July, 2026.

HEARTH, INC. AND AFFILIATES
NOTES TO COMBINING FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009
(Continued)

(2) **NET ASSETS AND RELATED PARTY TRANSACTIONS** (Continued)

RELATED PARTY TRANSACTIONS (Continued)

Hearth does not expect to receive any payments under these agreements. Accordingly, these notes and accrued interest are fully reserved. The interest income due for 2010 and 2009 was \$124,914 and \$117,013, respectively.

The notes receivable and accrued interest that have been fully reserved in the accompanying combining financial statements at December 31, 2010 and 2009, consist of the following:

	<u>2010</u>	<u>Principal</u>	<u>Accrued Interest</u>	<u>Total</u>
Linkage		\$335,213	\$ 556,992	\$ 892,205
Acquisition		320,000	488,065	808,065
Foundations		<u>99,260</u>	<u>179,536</u>	<u>278,796</u>
Total		<u>\$754,473</u>	<u>\$1,224,593</u>	<u>\$1,979,066</u>
	<u>2009</u>	<u>Principal</u>	<u>Accrued Interest</u>	<u>Total</u>
Linkage		\$335,213	\$ 498,623	\$ 833,836
Acquisition		320,000	439,759	759,759
Foundations		<u>99,260</u>	<u>161,297</u>	<u>260,557</u>
Total		<u>\$754,473</u>	<u>\$1,099,679</u>	<u>\$1,854,152</u>

Hearth needs to repay to the City of Boston any amounts received from the Partnership on the Linkage loan. Since Hearst does not anticipate any payments from the Partnership, this amount has not been recorded as a liability in the accompanying combining financial statements (see Note 7).

Investment in Affiliate

Investment in affiliate is recorded at cost and consists of the General Partner's investment in the Partnership.

Ruggles Assisted Living Limited Partnership

Hearth entered into an agreement with Ruggles to provide supportive services to the tenants of Ruggles. Ruggles operates a forty-three unit assisted living facility. Hearst was entitled to a service provider fee for its services at Ruggles. The fee was \$20,000 per year, beginning in 2001, and increased by 3% per year until cancelled by either party. This agreement was amended effective January 1, 2008, and Hearst agreed to waive charging Ruggles the service provider fee through December 31, 2011. The fee was reinstated effective April 1, 2010, subject to an annual cash flow review, and the prorated fee for 2010 was \$16,227, which is included in due from (to) affiliates in the accompanying combining statement of financial position as of December 31, 2010. This agreement expires on June 30, 2016.

HEARTH, INC. AND AFFILIATES
NOTES TO COMBINING FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009
(Continued)

(2) **NET ASSETS AND RELATED PARTY TRANSACTIONS** (Continued)

RELATED PARTY TRANSACTIONS (Continued)

Ruggles Assisted Living Limited Partnership (Continued)

Additionally, Hearth is to be reimbursed for expenses and overhead applicable to Ruggles, as approved by Ruggles' Board of Directors in the annual operating budget. Hearth billed Ruggles \$71,847 and \$70,013 during 2010 and 2009, respectively, which is included in management and service fees in the accompanying combining statements of activities. All operating expenses of Ruggles are also paid through Hearth and reimbursed monthly. In order to pay the expenses for Ruggles, Hearth has, from time-to-time, borrowed on its note payable to a bank (see Note 6). In turn, Ruggles agreed to pay accrued interest on their outstanding balance at Hearth's prevailing short-term borrowing rate, *Wall Street Journal* (WSJ) prime rates, which ranged from 7.25% to 8.25%, at the time of the borrowings. Hearth agreed to waive interest beginning January 1, 2008 through December 31, 2011.

Hearth is owed the following amount noted below from Ruggles at December 31, 2010, which is included in due from (to) affiliates, net in the accompanying combining statements of financial position. During 2010, Hearth received approximately \$194,000 of these amounts from Ruggles' 2009 available cash flow, and expects to receive approximately \$51,000 in 2011 from Ruggles 2010 available cash flow. Each year Ruggles revises its operating projections. Under the revised projections for 2010, Ruggles expects to repay Hearth between \$25,000 and \$65,000 annually through 2041. Hearth recorded a recovery of affiliate advances of \$333,525 in the accompanying combining financial statements during 2009, to reflect the change in repayment period and reversal of the allowance for uncollectible amounts. This receivable has been discounted using a 3% rate. A summary of the amount due from Ruggles at December 31, 2010, is as follows:

Gross receivable	\$ 868,578
Less – discount	<u>(257,782)</u>
	<u>\$ 610,796</u>

Hearth holds 50% of the outstanding shares of common stock in NCS Ruggles, Inc. NCS Ruggles, Inc. is a Massachusetts for-profit corporation and holds a 0.1% ownership interest in Ruggles as the general partner.

Hearth Olmsted Limited Partnership

Hearth Olmsted Limited Partnership (Olmsted, LP) was formed on November 10, 2010, as a limited partnership under the laws of the Commonwealth of Massachusetts. Olmsted, LP was created to acquire, develop, construct, own and operate fifty-nine units of housing for extremely low-income elders. Olmsted, LP is located in Mattapan, Massachusetts. Hearth, Inc. is the initial limited partner in Olmsted, LP and the general partner is Olmsted, LLC (see page 20).

HEARTH, INC. AND AFFILIATES
NOTES TO COMBINING FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009
(Continued)

(2) **NET ASSETS AND RELATED PARTY TRANSACTIONS** (Continued)

RELATED PARTY TRANSACTIONS (Continued)

Hearth Olmsted Manager LLC

Olmsted, LLC is a Massachusetts limited liability company, which was formed on November 10, 2010, with Hearth, Inc. as the sole member. This entity was formed to develop and manage Olmsted, LP (see page 19) as its general partner.

(3) **INVESTMENTS**

Investments with readily determinable fair value are reported at their fair market value.

Investments are as follows at December 31:

	<u>2010</u>	<u>Cost</u>	<u>Market Value</u>	<u>Unrealized Depreciation</u>
Fixed income		\$120,526	\$118,810	\$ (1,716)
Equities		<u>169,156</u>	<u>152,586</u>	<u>(16,570)</u>
		<u>\$289,682</u>	<u>\$271,396</u>	(18,286)
Unrealized depreciation at December, 31, 2009				<u>(44,513)</u>
Unrealized gain on investments				<u>\$ 26,227</u>
		<u>Cost</u>	<u>Market Value</u>	<u>Unrealized Depreciation</u>
	<u>2009</u>			
Fixed income		\$115,815	\$109,016	\$ (6,799)
Equities		<u>167,912</u>	<u>130,198</u>	<u>(37,714)</u>
		<u>\$283,727</u>	<u>\$239,214</u>	(44,513)
Unrealized depreciation at December 31, 2008				<u>(83,643)</u>
Unrealized gain on investments				<u>\$ 39,130</u>

Investments are reported in the accompanying combining statements of financial position as current or long-term assets based on management's intent with respect to the use of investments. Investments are not insured and are subject to ongoing market fluctuations. All of Hearth's investments are valued using Level 1 inputs (see Note 1).

HEARTH, INC. AND AFFILIATES
NOTES TO COMBINING FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009
(Continued)

(4) **LONG-TERM DEBT**

Long-term debt consists of the following at December 31:

	<u>2010</u>	<u>2009</u>
<u>Beacon</u>		
9.27% note payable to a bank, due in monthly principal and interest installments of \$1,486, through May, 2014. During June, 2014, a balloon payment of approximately \$76,000 is due. This note is secured by a first mortgage on land and a building.	\$104,408	\$112,167
<u>Bishop</u>		
1% note payable to the City of Boston, which had a balloon payment due in June, 2007. In lieu of the balloon payment, the lender proposed and the borrower is considering a modification to extend the term of the note and to modify the interest rate and repayment terms in exchange for an extension on the affordability restriction on the property. During the negotiation period, payments on the note were suspended. The note is secured by a mortgage on land and a building.	72,731	72,731
<u>Burroughs</u>		
7% note payable to a bank, payable in equal monthly principal and interest installments of \$1,320, with a maturity date of May, 2028. This note is secured by a first mortgage on land and a building.	<u>158,817</u>	<u>163,260</u>
Total long-term debt	335,956	348,158
Less - current portion	<u>13,510</u>	<u>12,418</u>
	<u>\$322,446</u>	<u>\$335,740</u>

Maturities of long-term debt over the next five years are as follows:

2011	\$13,510
2012	\$14,668
2013	\$15,992
2014	\$87,896
2015	\$ 6,438

Hearth's debt agreements contain covenants that require certain financial ratios be maintained and the combining financial statements be issued within a certain time period after year-end. Hearth was in compliance with these covenants as of December 31, 2010.

HEARTH, INC. AND AFFILIATES

**NOTES TO COMBINING FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009**

(Continued)

(5) CONTINGENT DEBT

Contingent debt consists of the following at December, 31:

	<u>2010</u>	<u>2009</u>
<u>Beacon</u>		
Non-interest bearing note payable to Community Economic Development Assistance Corporation (CEDAC). All unpaid principal is due June, 2029. This note is secured by a third mortgage on land and a building. Payments are due annually from surplus cash as defined in the agreement. There were no payments due from surplus cash as of December 31, 2010 or 2009. CEDAC may extend the maturity date of this note for one or more additional periods up to ten years provided that the property continues to be used for low-income housing.	\$ 426,000	\$ 426,000
Non-interest bearing note payable to the Town of Brookline. This note is due in June, 2039, and is secured by a second mortgage on land and a building.	<u>349,000</u>	<u>349,000</u>
Total Beacon	<u>775,000</u>	<u>775,000</u>
<u>Burroughs</u>		
Non-interest bearing note payable to CEDAC. All unpaid principal is due in August, 2038. This note is secured by a shared second mortgage on land and a building. Payments are due annually from surplus cash as defined in the agreement. There were no payments due from surplus cash as of December 31, 2010 or 2009. CEDAC may extend the maturity date of this note for one or more additional periods up to ten years provided that the property continues to be used for low-income housing.	750,000	750,000
Non-interest bearing note payable to the City of Boston. This note is due in February, 2038. This note is secured by a shared second mortgage on land and a building, an assignment in lease and rents, and interest in all assets related to the land and building.	<u>625,000</u>	<u>522,695</u>
Total Burroughs	<u>1,375,000</u>	<u>1,272,695</u>
Total contingent debt	<u>\$2,150,000</u>	<u>\$2,047,695</u>

Management's understanding is that these loans are not required to be repaid unless the projects fail to comply with other conditions in the agreements. It is the intention of the Board of Directors and the management of Hearth to maintain these properties for their intended purpose; therefore, these loans have been considered contingent and have been classified as contingent debt on the combining statement of financial position.

HEARTH, INC. AND AFFILIATES

**NOTES TO COMBINING FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009**

(Continued)

(6) NOTE PAYABLE TO A BANK

Hearth has a \$500,000 line of credit agreement with a bank, which is renewable annually. Borrowings under the agreement are due on demand, and interest is payable monthly at the bank's prime rate (3.25% at December 31, 2010 and 2009). The line of credit is secured by substantially all assets of Hearth. There is no balance outstanding as of December 31, 2010 and 2009.

(7) CONTINGENCIES

Beacon received a grant from a funding source to fund certain development costs. Beacon has received \$67,500 under this agreement in previous years. The agreement requires the residences to be occupied by low-income individuals for fifteen year periods ending on various dates through June 22, 2014. This agreement is secured by mortgages on the properties. If these conditions are not met, the total amount of the grant is due on demand. In the opinion of management, the conditions of this agreement, as defined, will be met. Accordingly, Hearth has not recorded a liability in the accompanying combining financial statements.

During 1995, Hearth received \$335,213 in Linkage funds from the City of Boston that it loaned to the Partnership (see page 18). Under the terms of the Linkage program, Hearth is required to pay to the City of Boston any amounts repaid by the Partnership. Hearth does not anticipate any payments from the Partnership and, accordingly, Hearth has not recorded a liability to the City of Boston in the accompanying combining financial statements.

(8) PENSION PLAN

Hearth operates a voluntary defined contribution retirement plan in accordance within Internal Revenue Code (IRC) Section 403(b). Employees may withhold contributions from their salaries on a tax-deferred basis within IRC limits. All employees that work at least 20 hours per week are eligible for the plan. Hearth does not make contributions to the plan.

(9) CONDITIONAL GRANTS

Hearth has received several conditional grants which are to be used for a specific project under the predevelopment program and the outreach program. As of December 31, 2010, Hearth has four grants totaling \$485,000 of which \$410,000 can be used upon the closing of public and private financing required for the project and \$75,000 can be used upon meeting certain outreach program achievements. Subsequent to December 31, 2010, the public and private financing have closed and the conditions have been met (see Note 13).

Hearth also has a \$65,000 conditional grant to be used for operations payable through 2012. Hearth received \$25,000 during 2010 and expects to receive \$40,000 through 2012, once conditions are met.

HEARTH, INC. AND AFFILIATES
NOTES TO COMBINING FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009
(Continued)

(10) **CONCENTRATIONS**

Funding

The following table reflects the two largest funding sources related to total revenue and accounts receivable:

<u>Funding Source</u>	<u>2010</u>		<u>2009</u>	
	<u>Contract Revenue</u>	<u>Accounts Receivable</u>	<u>Contract Revenue</u>	<u>Accounts Receivable</u>
A	32%	25%	32%	36%
B	22%	32%	11%	32%

These reimbursements are subject to audit by government agencies. In the opinion of management, the results of such audits, if any, will not have a material effect on the combining financial position of Hearst as of December 31, 2010 and 2009, or on the changes in their net assets for the years then ended.

Cash and Cash Equivalents

Hearth maintains its cash and cash equivalents balances in Massachusetts banks and is insured with the limits of the Federal Deposit Insurance Corporation (FDIC). At certain times during the year, cash and cash equivalents balances exceed the insured amounts. Hearst has not experienced any losses in such accounts. Hearst's management believes it is not exposed to any significant credit risk on cash and cash equivalents.

(11) **FUNDS HELD IN TRUST**

Hearth acts as a representative/payee for certain clients. The funds and corresponding liabilities related to these clients are included in funds held in trust in the accompanying combining statements of financial position.

(12) **COMMITMENTS**

In August, 2010, Hearst entered into multi-year service agreements with a cable and internet service provider, expiring in August, 2012. Future minimum payments for these agreements are as follows:

2011	\$11,640
2012	\$ 7,760

In June, 2010, Hearst also entered into multi-year service agreements with a telephone service provider. These agreements expire between June, 2012, and August, 2012, based on the dates the services began. Expenses are recorded based on total usage charges.

HEARTH, INC. AND AFFILIATES
NOTES TO COMBINING FINANCIAL STATEMENTS
DECEMBER 31, 2010 AND 2009
(Continued)

(13) SUBSEQUENT EVENTS

Hearth at Olmsted Limited Partnership

In March, 2011, Hearth syndicated Olmsted, LP (see Note 2), which finalized plans to develop a site in Mattapan in 2011 and 2012. The project is estimated to cost approximately \$16.5 million, including the funding of specific cash reserves. All predevelopment costs are recorded in construction in progress (see Note 1). Hearth will finance this project through a mix of tax credit equity, long-term debt, subordinate debt, and capital contributions.

Management Agreement

Associated with the formation of Olmsted, LP, on March 1, 2011, Hearth entered into a management agreement for the management of the project. The agreement is for three years beginning March 1, 2012. Base management fees under the management agreement will be 5% of effective gross income for bookkeeping data processing and reporting services, as defined in the agreement.