

**HEARTH, INC. AND AFFILIATES**  
**COMBINING FINANCIAL STATEMENTS**  
**DECEMBER 31, 2009 AND 2008**  
**TOGETHER WITH**  
**INDEPENDENT AUDITOR'S REPORT**

**HEARTH, INC. AND AFFILIATES**

**CONTENTS  
DECEMBER 31, 2009 AND 2008**

	<b><u>PAGES</u></b>
<b>INDEPENDENT AUDITOR'S REPORT .....</b>	<b>1</b>
<b>COMBINING FINANCIAL STATEMENTS:</b>	
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 - 24

## 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, 2009 and 2008, 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 financial position of Hearth, Inc. and Affiliates as of December 31, 2009 and 2008, 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 21, 2010

**HEARTH, INC. AND AFFILIATES**

**COMBINING STATEMENT OF FINANCIAL POSITION  
DECEMBER 31, 2009**

<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>
<b>CURRENT ASSETS:</b>						
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
Due from (to) 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>
<b>PROPERTY AND EQUIPMENT:</b>						
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>
<b>OTHER ASSETS:</b>						
Other reserves	-	67,760	-	-	-	67,760
Investments	239,214	-	-	-	-	239,214
Due from (to) affiliates, net	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>
<b><u>LIABILITIES AND NET ASSETS</u></b>						
<b>CURRENT LIABILITIES:</b>						
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>
<b>OTHER LIABILITIES:</b>						
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>
<b>NET ASSETS:</b>						
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 FINANCIAL POSITION  
DECEMBER 31, 2008**

<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>		
<b>CURRENT ASSETS:</b>							
Cash and cash equivalents	\$ 696,217	\$ 25,426	\$ -	\$ -	\$ -		\$ 721,643
Funds held in trust	45,330	-	-	-	-		45,330
Accounts and pledges receivable	364,389	21,765	-	-	-		386,154
Prepaid expenses and deposits	67,117	12,318	1,816	-	-		81,251
Due from (to) affiliates	(123,283)	(150,067)	30,594	242,756	-		-
Total current assets	<u>1,049,770</u>	<u>(90,558)</u>	<u>32,410</u>	<u>242,756</u>	<u>-</u>		<u>1,234,378</u>
<b>PROPERTY AND EQUIPMENT:</b>							
Land	-	390,600	-	-	-		390,600
Buildings and improvements	157,491	3,327,908	-	-	(220,269)		3,265,130
Furniture and equipment	461,406	147,800	-	-	-		609,206
Construction in progress	-	-	-	424,860	-		424,860
	<u>618,897</u>	<u>3,866,308</u>	<u>-</u>	<u>424,860</u>	<u>(220,269)</u>		<u>4,689,796</u>
Less - accumulated depreciation	512,514	754,361	-	-	-		1,266,875
Net property and equipment	<u>106,383</u>	<u>3,111,947</u>	<u>-</u>	<u>424,860</u>	<u>(220,269)</u>		<u>3,422,921</u>
<b>OTHER ASSETS:</b>							
Other reserves	-	56,952	-	-	-		56,952
Investments	194,040	-	-	-	-		194,040
Due from (to) affiliates, net	534,347	(56,245)	22,452	-	-		500,554
Investment in affiliate	-	-	-	240,000	-		240,000
Financing fees, net	-	64,071	-	-	-		64,071
Development fee receivable	-	-	-	98,569	(53,569)		45,000
Total other assets	<u>728,387</u>	<u>64,778</u>	<u>22,452</u>	<u>338,569</u>	<u>(53,569)</u>		<u>1,100,617</u>
Total assets	<u>\$ 1,884,540</u>	<u>\$ 3,086,167</u>	<u>\$ 54,862</u>	<u>\$ 1,006,185</u>	<u>\$ (273,838)</u>		<u>\$ 5,757,916</u>
<b><u>LIABILITIES AND NET ASSETS</u></b>							
<b>CURRENT LIABILITIES:</b>							
Current portion of long-term debt	\$ -	\$ 11,416	\$ -	\$ -	\$ -		\$ 11,416
Accounts payable and accrued expenses	192,505	70,889	1,419	-	-		264,813
Funds held in trust	45,330	-	-	-	-		45,330
Total current liabilities	<u>237,835</u>	<u>82,305</u>	<u>1,419</u>	<u>-</u>	<u>-</u>		<u>321,559</u>
<b>OTHER LIABILITIES:</b>							
Accounts payable - long-term	-	-	-	90,152	-		90,152
Long-term debt and deferred interest, net of current portion	-	691,925	-	-	(344,086)		347,839
Contingent debt	-	1,972,695	-	-	-		1,972,695
Total other liabilities	<u>-</u>	<u>2,664,620</u>	<u>-</u>	<u>90,152</u>	<u>(344,086)</u>		<u>2,410,686</u>
Total liabilities	<u>237,835</u>	<u>2,746,925</u>	<u>1,419</u>	<u>90,152</u>	<u>(344,086)</u>		<u>2,732,245</u>
<b>NET ASSETS:</b>							
Unrestricted -							
Operating	1,389,372	(55,261)	53,443	(7,209)	-		1,380,345
Board designated	107,351	-	-	-	-		107,351
Property and equipment	106,383	394,503	-	-	70,248		571,134
Real estate development	-	-	-	762,134	-		762,134
Total unrestricted	<u>1,603,106</u>	<u>339,242</u>	<u>53,443</u>	<u>754,925</u>	<u>70,248</u>		<u>2,820,964</u>
Temporarily restricted	43,599	-	-	161,108	-		204,707
Total net assets	<u>1,646,705</u>	<u>339,242</u>	<u>53,443</u>	<u>916,033</u>	<u>70,248</u>		<u>3,025,671</u>
Total liabilities and net assets	<u>\$ 1,884,540</u>	<u>\$ 3,086,167</u>	<u>\$ 54,862</u>	<u>\$ 1,006,185</u>	<u>\$ (273,838)</u>		<u>\$ 5,757,916</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

	<u>OPERATING</u>	<u>RENTAL PROPERTY</u>	<u>PROPERTY MANAGEMENT</u>	<u>REAL ESTATE DEVELOPMENT</u>	<u>ELIMI- NATIONS</u>	<u>TOTAL</u>
<b>CHANGES IN UNRESTRICTED NET ASSETS:</b>						
<b>OPERATING REVENUES:</b>						
Rental fees, net and program revenues	\$ 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 restrictions - Satisfaction of 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>
<b>OPERATING EXPENSES:</b>						
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	2,774,863	367,247	76,716	48,881	(61,275)	3,206,432
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>
<b>OTHER REVENUES (EXPENSES):</b>						
Recovery of affiliate advances	333,525	-	-	-	-	333,525
Unrealized gain on investments	39,130	-	-	-	-	39,130
Predevelopment and capital grants	38,242	-	-	-	-	38,242
General partner operating expenses	-	-	-	(674)	-	(674)
Interest on deferred debt	-	(17,294)	-	-	17,294	-
Net assets released from restrictions - Satisfaction of 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>
<b>CHANGES IN TEMPORARILY RESTRICTED NET ASSETS:</b>						
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 STATEMENT OF ACTIVITIES  
FOR THE YEAR ENDED DECEMBER 31, 2008

	<u>OPERATING</u>	<u>RENTAL PROPERTY</u>	<u>PROPERTY MANAGEMENT</u>	<u>REAL ESTATE DEVELOPMENT</u>	<u>ELIMI- NATIONS</u>	<u>TOTAL</u>
<b>CHANGES IN UNRESTRICTED NET ASSETS:</b>						
<b>OPERATING REVENUES:</b>						
Rental fees, net and program revenues	\$ 1,334,143	\$ 313,125	\$ 105,240	\$ -	\$ (59,491)	\$ 1,693,017
Government grants and other contracts	1,194,822	-	-	-	-	1,194,822
Private grants, contributions and special events, net	546,664	-	-	-	-	546,664
Management and service fees	71,321	-	-	-	-	71,321
Investment income	13,661	515	-	-	-	14,176
Other	2,140	-	-	-	-	2,140
Developer fee revenue	-	-	-	16,069	(16,069)	-
Net assets released from restrictions - Satisfaction of purpose restrictions	56,912	13,180	-	-	-	70,092
Total operating revenues	<u>3,219,663</u>	<u>326,820</u>	<u>105,240</u>	<u>16,069</u>	<u>(75,560)</u>	<u>3,592,232</u>
<b>OPERATING EXPENSES:</b>						
Outreach	258,284	-	-	-	-	258,284
Housing and Supportive Services	1,991,025	317,458	-	13,547	(59,491)	2,262,539
Property Management	-	-	82,826	-	-	82,826
General and Administration	503,148	86,699	16,834	2,753	-	609,434
Institutional Advancement	260,979	-	-	-	-	260,979
Total operating expenses before depreciation and amortization	3,013,436	404,157	99,660	16,300	(59,491)	3,474,062
Depreciation and amortization	25,717	109,114	-	-	-	134,831
Total operating expenses	<u>3,039,153</u>	<u>513,271</u>	<u>99,660</u>	<u>16,300</u>	<u>(59,491)</u>	<u>3,608,893</u>
Changes in unrestricted net assets from operations	<u>180,510</u>	<u>(186,451)</u>	<u>5,580</u>	<u>(231)</u>	<u>(16,069)</u>	<u>(16,661)</u>
<b>OTHER REVENUES (EXPENSES):</b>						
Unrealized loss on investments	(74,169)	-	-	-	-	(74,169)
Predevelopment grants	-	-	-	2,300	-	2,300
General partner operating expenses	-	-	-	(1,130)	-	(1,130)
Interest on deferred debt	-	(16,423)	-	-	16,423	-
Net assets released from restrictions - Satisfaction of capital restrictions	-	-	-	80,857	-	80,857
Total other revenues (expenses)	<u>(74,169)</u>	<u>(16,423)</u>	<u>-</u>	<u>82,027</u>	<u>16,423</u>	<u>7,858</u>
Changes in unrestricted net assets	<u>106,341</u>	<u>(202,874)</u>	<u>5,580</u>	<u>81,796</u>	<u>354</u>	<u>(8,803)</u>
<b>CHANGES IN TEMPORARILY RESTRICTED NET ASSETS:</b>						
Grants	14,721	-	-	148,700	-	163,421
Net assets released from restrictions	<u>(56,912)</u>	<u>(13,180)</u>	<u>-</u>	<u>(80,857)</u>	<u>-</u>	<u>(150,949)</u>
Changes in temporarily restricted net assets	<u>(42,191)</u>	<u>(13,180)</u>	<u>-</u>	<u>67,843</u>	<u>-</u>	<u>12,472</u>
Changes in net assets	<u>\$ 64,150</u>	<u>\$ (216,054)</u>	<u>\$ 5,580</u>	<u>\$ 149,639</u>	<u>\$ 354</u>	<u>\$ 3,669</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, 2009 AND 2008**

	<u>OPERATING</u>	<u>RENTAL PROPERTY</u>	<u>PROPERTY MANAGE- MENT</u>	<u>REAL ESTATE DEVELOPMENT</u>	<u>ELIMI- NATIONS</u>	<u>TOTAL</u>
<b>NET ASSETS</b> , December 31, 2007	\$ 1,688,841	\$ 468,597	\$ 31,029	\$ 763,641	\$ 69,894	\$ 3,022,002
Changes in net assets	64,150	(216,054)	5,580	149,639	354	3,669
Transfers	<u>(106,286)</u>	<u>86,699</u>	<u>16,834</u>	<u>2,753</u>	<u>-</u>	<u>-</u>
<b>NET ASSETS</b> , 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>
<b>NET ASSETS</b> , December 31, 2009	<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>

*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, 2009 AND 2008**

	<u>2009</u>	<u>2008</u>
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Changes in net assets	\$ 569,781	\$ 3,669
Adjustments to reconcile changes in net assets to net cash provided by (used in) operating activities:		
Depreciation and amortization	143,311	134,831
Predevelopment and capital grants	(38,242)	(151,000)
Unrealized (gain) loss on investments	(39,130)	74,169
Bad debt	9,774	1,226
Changes in operating assets and liabilities -		
Accounts and pledges receivable	182,636	(128,535)
Prepaid expenses and deposits	(17,511)	2,431
Due from affiliates	(467,426)	99,497
Accounts payable and accrued expenses	(19,297)	(43,981)
Net cash provided by (used in) operating activities	<u>323,896</u>	<u>(7,693)</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Other reserves	(10,808)	(53,825)
Predevelopment and capital grants	38,242	151,000
Payments on development fee receivable	20,000	10,000
Financing fees	-	(14,804)
Acquisition of property and equipment	(70,054)	(380,921)
Purchases of investments	(6,044)	(6,096)
Net cash used in investing activities	<u>(28,664)</u>	<u>(294,646)</u>
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Principal payments of notes payable	-	(50,000)
Proceeds from contingent debt	75,000	-
Proceeds from long-term debt	-	516,745
Payments of long-term debt	(11,097)	(8,101)
Net cash provided by financing activities	<u>63,903</u>	<u>458,644</u>
<b>NET INCREASE IN CASH AND CASH EQUIVALENTS</b>	<b>359,135</b>	<b>156,305</b>
<b>CASH AND CASH EQUIVALENTS, beginning of year</b>	<b>721,643</b>	<b>565,338</b>
<b>CASH AND CASH EQUIVALENTS, end of year</b>	<b><u>\$1,080,778</u></b>	<b><u>\$ 721,643</u></b>
<b>SUPPLEMENTAL INFORMATION:</b>		
Cash paid for interest - expensed	<u>\$ 22,591</u>	<u>\$ 20,776</u>
Property and equipment financed by accounts payable	<u>\$ 27,945</u>	<u>\$ 52,617</u>
Capitalized interest	<u>\$ -</u>	<u>\$ 14,804</u>
Refinanced notes payable	<u>\$ -</u>	<u>\$ 680,950</u>

*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

EXPENSES:	PROGRAM SERVICES						SUPPORT SERVICES					ELIMI- NATIONS	TOTAL
	OUTREACH	HOUSING AND SUPPORTIVE SERVICES			TOTAL PROGRAM SERVICES	PROPERTY MANAGEMENT	GENERAL AND ADMINIS- TRATION	INSTITUTIONAL ADVANCEMENT	TOTAL SUPPORT SERVICES				
		HEARTH	REAL ESTATE DEVELOPMENT	RENTAL PROPERTY						TOTAL			
Personnel and related -													
Salaries	\$ 194,529	\$ 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	14,647	118,253	1,967	2,811	123,031	3,606	141,284	24,891	12,645	37,536	-	178,820	
Fringe benefits	14,006	101,042	1,334	2,290	104,666	3,803	122,475	28,116	11,894	40,010	-	162,485	
Consultants and contracted services	6,744	28,648	10,665	-	39,313	1,731	47,788	4,875	3,535	8,410	-	56,198	
Total personnel and related	<u>229,926</u>	<u>1,645,149</u>	<u>42,107</u>	<u>40,085</u>	<u>1,727,341</u>	<u>58,372</u>	<u>2,015,639</u>	<u>409,553</u>	<u>207,400</u>	<u>616,953</u>	<u>-</u>	<u>2,632,592</u>	
Occupancy -													
Utilities	-	363	-	67,622	67,985	-	67,985	-	-	-	-	67,985	
Repairs and maintenance	413	7,707	-	53,332	61,039	29	61,481	487	58	545	-	62,026	
Rent	8,833	-	-	-	-	2,945	11,778	13,251	4,417	17,668	-	29,446	
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	1,520	-	20,664	
Real estate taxes	-	-	-	16,226	16,226	-	16,226	-	-	-	-	16,226	
Total occupancy	<u>10,766</u>	<u>10,799</u>	<u>-</u>	<u>172,619</u>	<u>183,418</u>	<u>5,021</u>	<u>199,205</u>	<u>13,738</u>	<u>5,995</u>	<u>19,733</u>	<u>-</u>	<u>218,938</u>	
Other -													
Food and household supplies	1,741	92,958	-	1,158	94,116	-	95,857	25	-	25	-	95,882	
Professional fees	-	3,121	-	4,881	8,002	600	8,602	36,158	3,955	40,113	-	48,715	
Telephone	4,780	30,964	-	94	31,058	644	36,482	9,126	2,394	11,520	-	48,002	
Program supplies and client expenses	16,851	15,328	-	550	15,878	-	32,729	-	-	-	-	32,729	
Insurance	-	20,441	-	-	20,441	-	20,441	7,563	-	7,563	-	28,004	
Miscellaneous	596	8,723	-	9,776	18,499	143	19,238	5,188	1,094	6,282	-	25,520	
Printing and copying	1,554	2,347	-	-	2,347	369	4,270	7,925	9,727	17,652	-	21,922	
Office expense	793	6,660	-	137	6,797	649	8,239	6,657	2,847	9,504	-	17,743	
Travel and training	1,266	3,190	-	-	3,190	259	4,715	9,421	515	9,936	-	14,651	
Postage	1,173	485	24	96	605	66	1,844	1,814	6,554	8,368	-	10,212	
Bad debt	-	-	-	9,774	9,774	-	9,774	-	-	-	-	9,774	
Recruitment	314	494	-	-	494	-	808	284	-	284	-	1,092	
Fundraising expense	-	-	-	-	-	-	-	-	656	656	-	656	
Management and administrative fees	-	-	-	61,275	61,275	-	61,275	-	-	-	(61,275)	-	
Total other	<u>29,068</u>	<u>184,711</u>	<u>24</u>	<u>87,741</u>	<u>272,476</u>	<u>2,730</u>	<u>304,274</u>	<u>84,161</u>	<u>27,742</u>	<u>111,903</u>	<u>(61,275)</u>	<u>354,902</u>	
Total expenses before allocations	269,760	1,840,659	42,131	300,445	2,183,235	66,123	2,519,118	507,452	241,137	748,589	(61,275)	3,206,432	
DIRECT SERVICE ALLOCATION	-	48,669	-	-	48,669	-	48,669	(48,669)	-	(48,669)	-	-	
GENERAL AND ADMINISTRATION ALLOCATION	43,276	304,824	6,750	66,802	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	367,247	2,610,280	76,716	3,000,032	(12,216)	279,891	267,675	(61,275)	3,206,432	
DEPRECIATION AND AMORTIZATION	370	13,409	-	116,538	129,947	-	130,317	12,216	778	12,994	-	143,311	
Total expenses	<u>\$ 313,406</u>	<u>\$ 2,207,561</u>	<u>\$ 48,881</u>	<u>\$ 483,785</u>	<u>\$ 2,740,227</u>	<u>\$ 76,716</u>	<u>\$ 3,130,349</u>	<u>\$ -</u>	<u>\$ 280,669</u>	<u>\$ 280,669</u>	<u>\$ (61,275)</u>	<u>\$ 3,349,743</u>	

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, 2008

EXPENSES:	PROGRAM SERVICES						SUPPORT SERVICES					ELIMI- NATIONS	TOTAL
	OUTREACH	HOUSING AND SUPPORTIVE SERVICES				PROPERTY MANAGEMENT	TOTAL PROGRAM SERVICES	GENERAL AND		TOTAL SUPPORT SERVICES			
		HEARTH	REAL ESTATE DEVELOPMENT	RENTAL PROPERTY	TOTAL			ADMINIS- TRATION	INSTITUTIONAL ADVANCEMENT				
Personnel and related -													
Salaries	\$ 190,424	\$ 1,412,702	\$ 10,320	\$ 32,255	\$ 1,455,277	\$ 62,485	\$ 1,708,186	\$ 430,480	\$ 192,579	\$ 623,059	\$ -	\$ 2,331,245	
Payroll taxes	15,958	146,856	588	3,343	150,787	5,356	172,101	36,564	16,712	53,276	-	225,377	
Fringe benefits	13,655	101,532	621	2,294	104,447	4,867	122,969	34,085	12,973	47,058	-	170,027	
Consultants and contracted services	5,399	22,064	-	-	22,064	1,467	28,930	53,044	3,323	56,367	-	85,297	
Total personnel and related	<u>225,436</u>	<u>1,683,154</u>	<u>11,529</u>	<u>37,892</u>	<u>1,732,575</u>	<u>74,175</u>	<u>2,032,186</u>	<u>554,173</u>	<u>225,587</u>	<u>779,760</u>	<u>-</u>	<u>2,811,946</u>	
Occupancy -													
Utilities	-	434	-	78,343	78,777	-	78,777	-	-	-	-	78,777	
Repairs and maintenance	-	4,866	-	68,570	73,436	-	73,436	52	-	52	-	73,488	
Rent	8,576	-	-	-	-	2,859	11,435	12,865	4,288	17,153	-	28,588	
Mortgage interest	-	-	-	20,776	20,776	-	20,776	-	-	-	-	20,776	
Insurance	1,685	2,651	-	12,634	15,285	2,616	19,586	-	1,685	1,685	-	21,271	
Real estate taxes	-	-	-	21,014	21,014	-	21,014	-	-	-	-	21,014	
Total occupancy	<u>10,261</u>	<u>7,951</u>	<u>-</u>	<u>201,337</u>	<u>209,288</u>	<u>5,475</u>	<u>225,024</u>	<u>12,917</u>	<u>5,973</u>	<u>18,890</u>	<u>-</u>	<u>243,914</u>	
Other -													
Food and household supplies	79	95,342	-	114	95,456	-	95,535	-	-	-	-	95,535	
Professional fees	330	44,729	-	5,762	50,491	681	51,502	39,623	3,351	42,974	-	94,476	
Telephone	3,958	29,720	356	120	30,196	854	35,008	9,276	2,070	11,346	-	46,354	
Program supplies and client expenses	11,721	16,358	-	-	16,358	-	28,079	-	-	-	-	28,079	
Insurance	-	23,110	-	-	23,110	-	23,110	8,331	-	8,331	-	31,441	
Miscellaneous	288	10,973	-	11,029	22,002	144	22,434	9,319	1,137	10,456	-	32,890	
Printing and copying	2,570	2,820	-	-	2,820	624	6,014	13,857	13,253	27,110	-	33,124	
Office expense	739	9,767	-	141	9,908	710	11,357	8,149	3,075	11,224	-	22,581	
Travel and training	1,265	3,700	1,662	123	5,485	22	6,772	10,287	130	10,417	-	17,189	
Postage	1,275	539	-	223	762	141	2,178	5,218	5,943	11,161	-	13,339	
Bad debt	-	-	-	1,226	1,226	-	1,226	-	-	-	-	1,226	
Recruitment	362	841	-	-	841	-	1,203	305	-	305	-	1,508	
Fundraising expense	-	-	-	-	-	-	-	-	460	460	-	460	
Management and administrative fees	-	-	-	59,491	59,491	-	59,491	-	-	-	(59,491)	-	
Total other	<u>22,587</u>	<u>237,899</u>	<u>2,018</u>	<u>78,229</u>	<u>318,146</u>	<u>3,176</u>	<u>343,909</u>	<u>104,365</u>	<u>29,419</u>	<u>133,784</u>	<u>(59,491)</u>	<u>418,202</u>	
Total expenses before allocations	258,284	1,929,004	13,547	317,458	2,260,009	82,826	2,601,119	671,455	260,979	932,434	(59,491)	3,474,062	
DIRECT SERVICE ALLOCATION	-	62,021	-	-	62,021	-	62,021	(62,021)	-	(62,021)	-	-	
GENERAL AND ADMINISTRATION ALLOCATION	52,649	407,507	2,753	86,699	496,959	16,834	566,442	(619,645)	53,203	(566,442)	-	-	
Total expenses before depreciation and amortization	310,933	2,398,532	16,300	404,157	2,818,989	99,660	3,229,582	(10,211)	314,182	303,971	(59,491)	3,474,062	
DEPRECIATION AND AMORTIZATION	758	13,965	-	109,114	123,079	-	123,837	10,211	783	10,994	-	134,831	
Total expenses	<u>\$ 311,691</u>	<u>\$ 2,412,497</u>	<u>\$ 16,300</u>	<u>\$ 513,271</u>	<u>\$ 2,942,068</u>	<u>\$ 99,660</u>	<u>\$ 3,353,419</u>	<u>\$ -</u>	<u>\$ 314,965</u>	<u>\$ 314,965</u>	<u>\$ (59,491)</u>	<u>\$ 3,608,893</u>	

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

**HEARTH, INC. AND AFFILIATES**  
**NOTES TO COMBINING FINANCIAL STATEMENTS**  
**DECEMBER 31, 2009 AND 2008**

(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., and Hearth at Burroughs, LLC (Burroughs) (see Note 2).

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, 2009, consist of replacement reserve accounts at Beacon, Bishop, and Burroughs.

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, 2009 and 2008.

## HEARTH, INC. AND AFFILIATES

### NOTES TO COMBINING FINANCIAL STATEMENTS DECEMBER 31, 2009 AND 2008 (Continued)

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

##### **SIGNIFICANT ACCOUNTING POLICIES** (Continued)

##### 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 \$157,000 at December 31, 2009 and 2008. Depreciation expense during 2009 and 2008 was \$140,671 and \$132,108, respectively.

During 2009 and 2008, Hearth incurred predevelopment costs of approximately \$49,000 and \$81,000, respectively, to develop up to 59 units of low-income elderly housing in Boston, Massachusetts (see page 14). 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 2009 or 2008.

##### 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). Financing fees have a cost of \$75,795 as of December 31, 2009 and 2008. Accumulated amortization of financing fees is \$14,364 and \$11,724 as of December 31, 2009 and 2008, respectively. Amortization during 2009 and 2008 was \$2,640 and \$2,723, respectively.

##### 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.

**HEARTH, INC. AND AFFILIATES**  
**NOTES TO COMBINING FINANCIAL STATEMENTS**  
**DECEMBER 31, 2009 AND 2008**  
(Continued)

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

**SIGNIFICANT ACCOUNTING POLICIES** (Continued)

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 \$17,250 and \$24,286 for 2009 and 2008, 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 income is 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 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 \$830 and \$1,342 of donated food, materials and supplies in 2009 and 2008, respectively.

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, 2009 AND 2008**  
(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, 2009, the Subsidiary has, for Federal income tax purposes, net operating loss carryforwards of approximately \$266,000 available to offset future taxable income. Also, at December 31, 2009, the Subsidiary has, for state income tax purposes, net operating loss carryforwards of approximately \$18,000 to offset future taxable income. These carryforwards expire at various dates through 2029. The Subsidiary accounts for income taxes in accordance with *Accounting Standards for Income Taxes*. The aforementioned standards do not have a material effect on the combining financial statements for the years ended December 31, 2009 and 2008, since the tax benefit of the net operating loss carryforwards have been reserved.

Uncertainty in Income Taxes

During 2009, Hearth adopted 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, 2009, 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 2010. 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 Measurements

Hearth adopted the accounting and disclosure standards pertaining to *Fair Value Measurements* for qualifying assets and liabilities. The standards define fair value, establish a framework for measuring fair value under U.S. GAAP, and expand disclosures about fair value measurements. The standards establish a fair value hierarchy that prioritizes the inputs and assumptions used to measure fair value. The three levels of the fair value framework are as follows:

- Level 1 – Inputs that reflect unadjusted quoted prices in active markets for identical assets at the measurement date.
- Level 2 – Inputs other than quoted prices in active markets that are observable for the asset either directly or indirectly, including inputs in markets that are not considered to be active.
- Level 3 – Inputs that are unobservable.

A qualifying asset or liability's level within the framework is based on the lowest level of any input that is significant to the fair value measurement. Hearth values all qualifying assets and liabilities using Level 1 inputs.

**HEARTH, INC. AND AFFILIATES**  
**NOTES TO COMBINING FINANCIAL STATEMENTS**  
**DECEMBER 31, 2009 AND 2008**  
(Continued)

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

**SIGNIFICANT ACCOUNTING POLICIES** (Continued)

Subsequent Events

The preparation of combining financial statements in accordance with U.S. GAAP requires management to disclose the date through which subsequent events have been evaluated for possible recognition or disclosure in the accompanying combining financial statements. Subsequent events are transactions or events that occur after the combining statement of financial position date, but before the combining financial statements are issued or available to be issued. The accompanying combining financial statements include the evaluation of subsequent events that have occurred through April 21, 2010, which is the date the combining financial statements were available to be issued.

(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 Hearst relating to program services and other operating activities that it is engaged in. Unrestricted net assets also consist of the net book value of Hearst's property and equipment, net of related debt, and Board designated net assets. The Board designated net assets consist of cumulative proceeds from the Journey Home Campaign. These funds 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 the designated time periods expire.

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

	<u>2009</u>	<u>2008</u>
Restricted for programs	\$ 96,786	\$ 43,599
Restricted for predevelopment activities (see page 11)	69,871	161,108
Restricted for equipment	<u>11,758</u>	<u>-</u>
Total temporarily restricted	<u>\$178,415</u>	<u>\$204,707</u>

**HEARTH, INC. AND AFFILIATES**  
**NOTES TO COMBINING FINANCIAL STATEMENTS**  
**DECEMBER 31, 2009 AND 2008**  
(Continued)

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

**NET ASSETS** (Continued)

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.

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 Assisted Living Limited Partnership (Ruggles) (see page 19) and East Concord Street Limited Partnership (the Partnership) (see page 17).

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 Subsidiary. The Subsidiary is a Massachusetts for-profit corporation, 79% owned by Hearth. The Subsidiary is the General Partner (1% ownership interest) of the Partnership, which operates forty-one units of housing for formerly homeless elders.

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 2009 and 2008 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 2009 were \$56,641 and \$40,085, respectively, and during 2008 were \$72,708 and \$37,892, respectively.

**HEARTH, INC. AND AFFILIATES**  
**NOTES TO COMBINING FINANCIAL STATEMENTS**  
**DECEMBER 31, 2009 AND 2008**  
(Continued)

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

**RELATED PARTY TRANSACTIONS** (Continued)

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 December 31:

<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>
<u>2008</u>	<u>Management Services</u>	<u>Adminis- trative Services</u>	<u>Total</u>
Burroughs	\$12,502	\$13,093	\$25,595
Beacon	8,275	8,673	16,948
Bishop	<u>8,275</u>	<u>8,673</u>	<u>16,948</u>
	<u>\$29,052</u>	<u>\$30,439</u>	<u>\$59,491</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, 2009 and 2008, is \$141,111 and \$123,817, respectively, including \$17,294 and \$16,423 of interest for 2009 and 2008, 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 2009 and 2008.

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. In 2008, the project was completed and Hearth recorded development fees earned of \$16,069. As of December 31, 2009 and 2008, \$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, INC. AND AFFILIATES**  
**NOTES TO COMBINING FINANCIAL STATEMENTS**  
**DECEMBER 31, 2009 AND 2008**  
(Continued)

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

**RELATED PARTY TRANSACTIONS** (Continued)

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

The Partnership rents office space to Hearth at an annual rental of \$29,446 and \$28,588 in 2009 and 2008, 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 \$23,600 and \$23,200 of management and administrative staff (including payroll taxes and fringe benefits) during 2009 and 2008, respectively. Hearth Mgmt. also charged an administrative fee of approximately \$23,200 and \$22,600 during 2009 and 2008, respectively.

Hearth provides maintenance and security staff to the Partnership and charged the Partnership approximately \$177,000 during 2009 and 2008, for salaries, payroll taxes and related benefits.

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 2009 or 2008. The fee is also limited to 2% of gross rents.

The Partnership owes \$278,486 and \$231,904 to Hearth and Hearth Mgmt. at December 31, 2009 and 2008, respectively, which are included in due from (to) affiliates, net in the accompanying combining statements of financial position. Hearth has reserved \$185,729 of the above amounts as of December 31, 2009 and 2008.

Hearth has contracted with the Partnership for a development fee of \$400,000 for services provided during the development of the project. Hearth expects to collect the remaining balance of the development fee of \$25,000 and \$45,000 as of December 31, 2009 and 2008, respectively, from operating cash flow. The timeframe of when these funds will be approved for release cannot be determined as of December 31, 2009 and, accordingly, the remaining balance is shown as a non-current asset in the accompanying combining statements of financial position.

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

**HEARTH, INC. AND AFFILIATES**  
**NOTES TO COMBINING FINANCIAL STATEMENTS**  
**DECEMBER 31, 2009 AND 2008**  
(Continued)

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

**RELATED PARTY TRANSACTIONS** (Continued)

Hearth has guaranteed the full, timely and unconditional payment and performance of all of the Subsidiary's obligations under the Partnership Agreement. Hearth's guarantee of the Subsidiary'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 2009 or 2008, since there was no available cash flow. All unpaid principal and accrued interest is due on dates ranging from September, 2025, to July, 2026.

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 2009 and 2008 was \$117,013 and \$109,614, respectively.

The notes receivable and accrued interest that have been fully reserved in the accompanying combining financial statements at December 31, 2009 and 2008, consist of the following:

	<b><u>2009</u></b>	<b><u>Principal</u></b>	<b><u>Accrued Interest</u></b>	<b><u>Total</u></b>
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>
	<b><u>2008</u></b>	<b><u>Principal</u></b>	<b><u>Accrued Interest</u></b>	<b><u>Total</u></b>
Linkage		\$335,213	\$ 444,073	\$ 779,286
Acquisition		320,000	394,342	714,342
Foundations		<u>99,260</u>	<u>144,251</u>	<u>243,511</u>
Total		<u>\$754,473</u>	<u>\$ 982,666</u>	<u>\$1,737,139</u>

Hearth needs to repay to the City of Boston any amounts received from the Partnership on the Linkage loan. Since Hearth 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 8).

**Investment in Affiliate**

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

## HEARTH, INC. AND AFFILIATES

### NOTES TO COMBINING FINANCIAL STATEMENTS DECEMBER 31, 2009 AND 2008

(Continued)

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

##### RELATED PARTY TRANSACTIONS (Continued)

###### Ruggles Assisted Living Limited Partnership

Hearth entered into an agreement with Ruggles Assisted Living Limited Partnership (Ruggles) to provide supportive services to the tenants of Ruggles. Ruggles operates a forty-three unit assisted living facility. Hearth 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 Hearth agreed to waive charging Ruggles the service provider fee through December 31, 2011. Due to recent operating projections, (see below) Hearth will reinstate the service provider fee beginning April, 2010. This agreement expires June 30, 2016.

Additionally, Hearth is to be reimbursed for expenses and overhead applicable to Ruggles, as approved by the Ruggles Partnership in the annual operating budget. Hearth billed Ruggles \$70,013 and \$69,999 during 2009 and 2008, 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 7). 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 from Ruggles at December 31, 2009, which is included in due from (to) affiliates, net in the accompanying combining statements of financial position. Hearth has received approximately \$86,000 of these amounts in January, 2010, and expects to receive approximately \$107,000 in 2010 from Ruggles 2009 excess cash flow. During 2009, Ruggles has revised its operating projections, which will enable Ruggles to repay Hearth earlier than previously expected. Under the revised projections, Ruggles expects to repay Hearth between \$53,000 and \$94,000 annually through 2026. Accordingly, Hearth has 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, 2009, is as follows:

Gross receivable	\$1,031,231
Less - discount	<u>(156,008)</u>
	<u>\$ 875,223</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.

#### (3) PLEDGES RECEIVABLE

Hearth has unconditional pledges from donors for operating purposes. At December 31, 2008, Hearth had \$12,750 of pledges receivable.

**HEARTH, INC. AND AFFILIATES**

**NOTES TO COMBINING FINANCIAL STATEMENTS  
DECEMBER 31, 2009 AND 2008  
(Continued)**

**(4) INVESTMENTS**

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

Investments are as follows at December 31:

	<u>2009</u>	<u>Cost</u>	<u>Market Value</u>	<u>Unrealized Depreciation</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>
	<u>2008</u>	<u>Cost</u>	<u>Market Value</u>	<u>Unrealized Depreciation</u>
Fixed income		\$111,156	\$ 92,138	\$ (19,018)
Equities		<u>166,527</u>	<u>101,902</u>	<u>(64,625)</u>
		<u>\$277,683</u>	<u>\$194,040</u>	(83,643)
Unrealized depreciation at December 31, 2007				<u>(9,474)</u>
Unrealized loss on investments				<u>\$ (74,169)</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).

**(5) LONG-TERM DEBT**

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

	<u>2009</u>	<u>2008</u>
<b><u>Beacon</u></b>		
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.	\$112,167	\$119,129

**HEARTH, INC. AND AFFILIATES**  
**NOTES TO COMBINING FINANCIAL STATEMENTS**  
**DECEMBER 31, 2009 AND 2008**  
(Continued)

(5) **LONG-TERM DEBT** (Continued)

	<u>2009</u>	<u>2008</u>
<b><u>Bishop</u></b>		
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
<b><u>Burroughs</u></b>		
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>163,260</u>	<u>167,395</u>
Total long-term debt	348,158	359,255
Less - current portion	<u>12,418</u>	<u>11,416</u>
	<u>\$335,740</u>	<u>\$347,839</u>

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

2010	\$12,418.
2011	\$13,510
2012	\$14,668
2013	\$15,992
2014	\$81,775

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, 2009.

**HEARTH, INC. AND AFFILIATES**

**NOTES TO COMBINING FINANCIAL STATEMENTS  
DECEMBER 31, 2009 AND 2008**

(Continued)

**(6) CONTINGENT DEBT**

Contingent debt consists of the following at December, 31:

	<u>2009</u>	<u>2008</u>
<b><u>Beacon</u></b>		
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. 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 June, 2039 and the note 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>
<b><u>Burroughs</u></b>		
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. 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	675,000
Non-interest bearing \$625,000 note payable to the City of Boston. This note is due February 12, 2038. This note is secured by a shared second mortgage on land and a building, an assignment in lease and rents and an interest in all assets related to the land and building.	<u>522,695</u>	<u>522,695</u>
Total Burroughs	<u>1,272,695</u>	<u>1,197,695</u>
Total contingent debt	<u>\$2,047,695</u>	<u>\$1,972,695</u>

**(7) 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, 2009 and 2008). The line of credit is secured by substantially all assets of Hearth. There is no balance outstanding as of December 31, 2009 and 2008.

**HEARTH, INC. AND AFFILIATES**

**NOTES TO COMBINING FINANCIAL STATEMENTS  
DECEMBER 31, 2009 AND 2008  
(Continued)**

**(8) CONTINGENCIES**

Beacon has 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.

**(9) 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.

**(10) CONDITIONAL GRANT**

During 2008, a Foundation awarded Hearth a multi-year grant of up to \$300,000 to be used for a specific project under the predevelopment program. Since this grant is conditional upon the closing of public and private financing required for the project, it is not reflected in the accompanying combining financial statements.

**(11) CONCENTRATIONS**

Funding

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

<u>Funding Source</u>	<u>2009</u>		<u>2008</u>	
	<u>Contract Revenue</u>	<u>Accounts Receivable</u>	<u>Contract Revenue</u>	<u>Accounts Receivable</u>
A	32%	36%	30%	30%
B	11%	32%	- %	- %
C	10%	- %	22%	40%

These reimbursements are subject to audit by the government agency. In the opinion of management, the results of such audits, if any, will not have a material effect on the combining financial position of Hearth as of December 31, 2009 and 2008, or on the changes in their net assets for the years then ended.

**HEARTH, INC. AND AFFILIATES**

**NOTES TO COMBINING FINANCIAL STATEMENTS  
DECEMBER 31, 2009 AND 2008**

(Continued)

**(11) CONCENTRATIONS** (Continued)

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. Hearth has not experienced any losses in such accounts. Hearth's management believes it is not exposed to any significant credit risk on cash and cash equivalents.

**(12) SECURITY DEPOSITS**

Tenant security deposits are collected upon move-in. The total liability was \$6,821 and \$7,313 at December 31, 2009 and 2008, respectively. Security deposit cash is included in cash and cash equivalents and accounts payable and accrued expenses in the accompanying combining statements of financial position.

**(13) 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.

**(14) RECLASSIFICATION**

Certain amounts in the 2008 combining financial statements have been reclassified to conform with the 2009 presentation.