

HEARTH, INC. AND AFFILIATES
COMBINING FINANCIAL STATEMENTS
DECEMBER 31, 2008 AND 2007
TOGETHER WITH
INDEPENDENT AUDITOR'S REPORT

HEARTH, INC. AND AFFILIATES

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DECEMBER 31, 2008 AND 2007**

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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, 2008 and 2007, 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, 2008 and 2007, 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
March 24, 2009

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>	
CURRENT ASSETS:						
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	57,469	12,318	1,816	-	-	71,603
Due from (to)	(123,283)	(150,067)	30,594	242,756	-	-
Total current assets	<u>1,040,122</u>	<u>(90,558)</u>	<u>32,410</u>	<u>242,756</u>	<u>-</u>	<u>1,224,730</u>
PROPERTY AND EQUIPMENT:						
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>
OTHER ASSETS:						
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>\$ 1,874,892</u>	<u>\$ 3,086,167</u>	<u>\$ 54,862</u>	<u>\$ 1,006,185</u>	<u>\$ (273,838)</u>	<u>\$ 5,748,268</u>
<u>LIABILITIES AND NET ASSETS</u>						
CURRENT LIABILITIES:						
Current portion of long-term debt	\$ -	\$ 15,001	\$ -	\$ -	\$ -	\$ 15,001
Accounts payable and accrued expenses	182,857	70,889	1,419	-	-	255,165
Funds held in trust	45,330	-	-	-	-	45,330
Total current liabilities	<u>228,187</u>	<u>85,890</u>	<u>1,419</u>	<u>-</u>	<u>-</u>	<u>315,496</u>
OTHER LIABILITIES:						
Accounts payable - long-term	-	-	-	90,152	-	90,152
Long-term debt and deferred interest, net of current portion	-	2,661,035	-	-	(344,086)	2,316,949
Total other liabilities	<u>-</u>	<u>2,661,035</u>	<u>-</u>	<u>90,152</u>	<u>(344,086)</u>	<u>2,407,101</u>
Total liabilities	<u>228,187</u>	<u>2,746,925</u>	<u>1,419</u>	<u>90,152</u>	<u>(344,086)</u>	<u>2,722,597</u>
NET ASSETS:						
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>\$ 1,874,892</u>	<u>\$ 3,086,167</u>	<u>\$ 54,862</u>	<u>\$ 1,006,185</u>	<u>\$ (273,838)</u>	<u>\$ 5,748,268</u>

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

HEARTH, INC. AND AFFILIATES

COMBINING STATEMENT OF FINANCIAL POSITION
DECEMBER 31, 2007

<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	\$ 562,931	\$ 2,407	\$ -	\$ -	\$ -	\$ 565,338
Funds held in trust	49,992	-	-	-	-	49,992
Accounts receivable	215,249	43,596	-	-	-	258,845
Prepaid expenses and deposits	59,943	11,693	2,398	-	-	74,034
Due from (to)	(99,505)	(83,387)	11,701	171,191	-	-
Total current assets	<u>788,610</u>	<u>(25,691)</u>	<u>14,099</u>	<u>171,191</u>	<u>-</u>	<u>948,209</u>
PROPERTY AND EQUIPMENT:						
Land	-	390,600	-	-	-	390,600
Buildings and improvements	157,491	2,984,767	-	-	(204,200)	2,938,058
Furniture and equipment	436,729	146,915	-	-	-	583,644
Construction in progress	-	-	-	343,956	-	343,956
	<u>594,220</u>	<u>3,522,282</u>	<u>-</u>	<u>343,956</u>	<u>(204,200)</u>	<u>4,256,258</u>
Less - accumulated depreciation	486,797	647,970	-	-	-	1,134,767
Net property and equipment	<u>107,423</u>	<u>2,874,312</u>	<u>-</u>	<u>343,956</u>	<u>(204,200)</u>	<u>3,121,491</u>
OTHER ASSETS:						
Other reserves	-	3,127	-	-	-	3,127
Investments	262,113	-	-	-	-	262,113
Due from (to) affiliates, net	788,556	(206,591)	18,086	-	-	600,051
Investment in affiliate	-	-	-	240,000	-	240,000
Financing fees, net	-	51,990	-	-	-	51,990
Development fee receivable	-	-	-	92,500	(37,500)	55,000
Total other assets	<u>1,050,669</u>	<u>(151,474)</u>	<u>18,086</u>	<u>332,500</u>	<u>(37,500)</u>	<u>1,212,281</u>
Total assets	<u>\$ 1,946,702</u>	<u>\$ 2,697,147</u>	<u>\$ 32,185</u>	<u>\$ 847,647</u>	<u>\$ (241,700)</u>	<u>\$ 5,281,981</u>
<u>LIABILITIES AND NET ASSETS</u>						
CURRENT LIABILITIES:						
Note payable	\$ 50,000	\$ -	\$ -	\$ -	\$ -	\$ 50,000
Current portion of long-term debt	-	9,490	-	-	-	9,490
Accounts payable and accrued expenses	157,869	93,650	1,156	1,013	-	253,688
Funds held in trust	49,992	-	-	-	-	49,992
Total current liabilities	<u>257,861</u>	<u>103,140</u>	<u>1,156</u>	<u>1,013</u>	<u>-</u>	<u>363,170</u>
OTHER LIABILITIES:						
Accounts payable - long-term	-	-	-	82,993	-	82,993
Long-term debt and deferred interest, net of current portion	-	2,125,410	-	-	(311,594)	1,813,816
Total other liabilities	<u>-</u>	<u>2,125,410</u>	<u>-</u>	<u>82,993</u>	<u>(311,594)</u>	<u>1,896,809</u>
Total liabilities	<u>257,861</u>	<u>2,228,550</u>	<u>1,156</u>	<u>84,006</u>	<u>(311,594)</u>	<u>2,259,979</u>
NET ASSETS:						
Unrestricted -						
Operating	1,388,277	(30,791)	31,029	(6,079)	-	1,382,436
Board designated	107,351	-	-	-	-	107,351
Property and equipment	107,423	486,208	-	-	69,894	663,525
Real estate development	-	-	-	676,455	-	676,455
Total unrestricted	<u>1,603,051</u>	<u>455,417</u>	<u>31,029</u>	<u>670,376</u>	<u>69,894</u>	<u>2,829,767</u>
Temporarily restricted	85,790	13,180	-	93,265	-	192,235
Total net assets	<u>1,688,841</u>	<u>468,597</u>	<u>31,029</u>	<u>763,641</u>	<u>69,894</u>	<u>3,022,002</u>
Total liabilities and net assets	<u>\$ 1,946,702</u>	<u>\$ 2,697,147</u>	<u>\$ 32,185</u>	<u>\$ 847,647</u>	<u>\$ (241,700)</u>	<u>\$ 5,281,981</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

CHANGES IN UNRESTRICTED NET ASSETS:

	OPERATING	RENTAL PROPERTY	PROPERTY MANAGEMENT	REAL ESTATE DEVELOPMENT	ELIMI- NATIONS	TOTAL
OPERATING REVENUES:						
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	6,115	515	-	-	-	6,630
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>3,212,117</u>	<u>326,820</u>	<u>105,240</u>	<u>16,069</u>	<u>(75,560)</u>	<u>3,584,686</u>
OPERATING EXPENSES:						
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	<u>3,013,436</u>	<u>404,157</u>	<u>99,660</u>	<u>16,300</u>	<u>(59,491)</u>	<u>3,474,062</u>
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>172,964</u>	<u>(186,451)</u>	<u>5,580</u>	<u>(231)</u>	<u>(16,069)</u>	<u>(24,207)</u>
OTHER REVENUES (EXPENSES):						
Interest income	7,546	-	-	-	-	7,546
Predevelopment grants	-	-	-	2,300	-	2,300
General partner operating expenses	-	-	-	(1,130)	-	(1,130)
Unrealized loss on investments	(74,169)	-	-	-	-	(74,169)
Interest on deferred debt	-	(16,423)	-	-	16,423	-
Net assets released from restrictions - Satisfaction of capital restrictions	(66,623)	(16,423)	-	80,857	-	80,857
Total other revenues (expenses)	<u>106,341</u>	<u>(202,874)</u>	<u>5,580</u>	<u>81,796</u>	<u>354</u>	<u>(8,803)</u>
Changes in temporarily restricted net assets						
Grants	14,721	-	-	148,700	-	163,421
Net assets released from restrictions	(56,912)	(13,180)	-	(80,857)	-	(150,949)
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>

CHANGES IN TEMPORARILY RESTRICTED

NET ASSETS:

Grants	14,721
Net assets released from restrictions	(56,912)
Changes in temporarily restricted net assets	(42,191)
Changes in net assets	\$ 64,150

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, 2007

CHANGES IN UNRESTRICTED NET ASSETS:

	<u>OPERATING</u>	<u>RENTAL PROPERTY</u>	<u>PROPERTY MANAGEMENT</u>	<u>REAL ESTATE DEVELOPMENT</u>	<u>ELIMI- NATIONS</u>	<u>TOTAL</u>
OPERATING REVENUES:						
Rental fees, net and program revenues	\$ 1,255,758	\$ 254,970	\$ 101,384	\$ -	\$ (57,758)	\$ 1,554,354
Government grants and other contracts	1,218,674	-	-	-	-	1,218,674
Private grants, contributions and special events, net	354,789	-	-	3,960	-	358,749
Management and service fees	69,424	-	-	-	-	69,424
Investment income	20,705	651	-	-	-	21,356
Other	4,837	-	-	-	-	4,837
Net assets released from restrictions - Satisfaction of purpose restrictions	56,977	-	-	-	-	56,977
Total operating revenues	<u>2,981,164</u>	<u>255,621</u>	<u>101,384</u>	<u>3,960</u>	<u>(57,758)</u>	<u>3,284,371</u>
OPERATING EXPENSES:						
Outreach	240,696	-	-	-	-	240,696
Housing and Supportive Services	1,888,156	279,658	-	3,960	(57,758)	2,114,016
Property Management	-	-	72,637	-	-	72,637
General and Administration	441,238	71,446	13,868	756	-	527,308
Institutional Advancement	211,691	-	-	-	-	211,691
Total operating expenses before depreciation and amortization	<u>2,781,781</u>	<u>351,104</u>	<u>86,505</u>	<u>4,716</u>	<u>(57,758)</u>	<u>3,166,348</u>
Depreciation and amortization	19,932	94,544	-	-	-	114,476
Total operating expenses	<u>2,801,713</u>	<u>445,648</u>	<u>86,505</u>	<u>4,716</u>	<u>(57,758)</u>	<u>3,280,824</u>
Changes in unrestricted net assets from operations	<u>179,451</u>	<u>(190,027)</u>	<u>14,879</u>	<u>(756)</u>	<u>-</u>	<u>3,547</u>
OTHER REVENUES (EXPENSES):						
Interest income	1,288	-	-	-	-	1,288
Predevelopment grants	-	54,320	-	35,774	-	90,094
General partner operating expenses	-	-	-	(1,130)	-	(1,130)
Unrealized loss on investments	(9,072)	-	-	-	-	(9,072)
Interest on deferred debt	-	(15,493)	-	-	15,493	-
Net assets released from restrictions - Satisfaction of capital restrictions	-	84,095	-	93,449	-	177,544
Total other revenues (expenses)	<u>(7,784)</u>	<u>122,922</u>	<u>-</u>	<u>128,093</u>	<u>15,493</u>	<u>258,724</u>
Changes in unrestricted net assets	<u>171,667</u>	<u>(67,105)</u>	<u>14,879</u>	<u>127,337</u>	<u>15,493</u>	<u>262,271</u>
CHANGES IN TEMPORARILY RESTRICTED NET ASSETS:						
Grants	83,000	13,180	-	93,265	-	189,445
Net assets released from restrictions	(56,977)	(84,095)	-	(93,449)	-	(234,521)
Changes in temporarily restricted net assets	<u>26,023</u>	<u>(70,915)</u>	<u>-</u>	<u>(184)</u>	<u>-</u>	<u>(45,076)</u>
Changes in net assets	<u>\$ 197,690</u>	<u>\$ (138,020)</u>	<u>\$ 14,879</u>	<u>\$ 127,153</u>	<u>\$ 15,493</u>	<u>\$ 217,195</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, 2008 AND 2007

	<u>OPERATING</u>	<u>RENTAL</u> <u>PROPERTY</u>	<u>PROPERTY</u> <u>MANAGE-</u> <u>MENT</u>	<u>REAL ESTATE</u> <u>DEVELOPMENT</u>	<u>ELIMI-</u> <u>NATIONS</u>	<u>TOTAL</u>
NET ASSETS, December 31, 2006	\$ 1,577,221	\$ 535,171	\$ 2,282	\$ 635,732	\$ 54,401	\$ 2,804,807
Changes in net assets	197,690	(138,020)	14,879	127,153	15,493	217,195
Transfers	<u>(86,070)</u>	<u>71,446</u>	<u>13,868</u>	<u>756</u>	<u>-</u>	<u>-</u>
NET ASSETS, 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>
NET ASSETS, December 31, 2008	<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>

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, 2008 AND 2007**

	<u>2008</u>	<u>2007</u>
CASH FLOWS FROM OPERATING ACTIVITIES:		
Changes in net assets	\$ 3,669	\$ 217,195
Adjustments to reconcile changes in net assets to net cash provided by (used in) operating activities:		
Depreciation and amortization	134,831	114,476
Predevelopment grants	(151,000)	(183,359)
Donated property and equipment	-	(3,500)
Loss on disposal of equipment	-	(736)
Unrealized loss on investments	74,169	9,072
Bad debt	1,226	5,660
Changes in operating assets and liabilities -		
Accounts and pledges receivable	(128,535)	137,515
Due from affiliates	99,497	(34,245)
Prepaid expenses and deposits	2,431	(15,053)
Accounts payable and accrued expenses	(43,981)	(185,635)
Net cash provided by (used in) operating activities	<u>(7,693)</u>	<u>61,390</u>
CASH FLOWS FROM INVESTING ACTIVITIES:		
Other reserves	(53,825)	42,141
Predevelopment grants	151,000	183,359
Payments on development fee receivable	10,000	-
Financing fees	(14,804)	(40,122)
Acquisition of property and equipment	(380,921)	(267,619)
Purchases of investments	(6,096)	(23,240)
Proceeds from sale of investments	-	69,014
Net cash used in investing activities	<u>(294,646)</u>	<u>(36,467)</u>
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds (payments) from notes payable	(50,000)	50,000
Proceeds from long-term debt	516,745	-
Payments of long-term debt	(8,101)	(13,452)
Net cash provided by financing activities	<u>458,644</u>	<u>36,548</u>
NET INCREASE IN CASH AND CASH EQUIVALENTS	156,305	61,471
CASH AND CASH EQUIVALENTS, beginning of year	<u>565,338</u>	<u>503,867</u>
CASH AND CASH EQUIVALENTS, end of year	<u>\$ 721,643</u>	<u>\$ 565,338</u>
SUPPLEMENTAL INFORMATION:		
Cash paid for interest - expensed	<u>\$ 20,776</u>	<u>\$ 13,533</u>
Capitalized interest	<u>\$ 14,804</u>	<u>\$ 43,090</u>
Refinanced notes payable	<u>\$ 680,950</u>	<u>\$ -</u>
Disposal of fully depreciated property and equipment	<u>\$ -</u>	<u>\$ 1,034</u>
Donated property and equipment	<u>\$ -</u>	<u>\$ 3,500</u>

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

HEARTH, INC. AND AFFILIATES
NOTES TO COMBINING FINANCIAL STATEMENTS
DECEMBER 31, 2008 AND 2007

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

OPERATIONS AND NONPROFIT STATUS

Hearth, Inc. (Hearth) is a nonprofit organization, which was formed in 1991 to eliminate elder homelessness in Boston, Massachusetts. Hearth 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 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 is also exempt from state income taxes. Contributions made to Hearth are deductible within the requirements of the Internal Revenue Code.

SIGNIFICANT ACCOUNTING POLICIES

Principles of Combination

The combining financial statements include the net assets of Hearth and its affiliates: 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, 2008, consist of replacement reserve accounts at Beacon, Bishop, and Burroughs. During 2007, other reserves consisted of a replacement reserve account at Bishop.

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, 2008 and 2007.

Property, 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.

HEARTH, INC. AND AFFILIATES
NOTES TO COMBINING FINANCIAL STATEMENTS
DECEMBER 31, 2008 AND 2007
(Continued)

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

SIGNIFICANT ACCOUNTING POLICIES (Continued)

Property, Equipment, Construction in Progress and Depreciation (Continued)

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, 2008 and 2007.

During 2008 and 2007, Hearth incurred predevelopment costs of approximately \$81,000 and \$129,000, respectively, to develop up to 80 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.

Depreciation expense during 2008 and 2007 was \$132,108 and \$112,709, respectively.

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 2008 or 2007.

Projects Under Development

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 above).

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 and \$60,991 as of December 31, 2008 and 2007, respectively. Accumulated amortization of financing fees is \$11,724 and \$9,001 as of December 31, 2008 and 2007, respectively. Amortization during 2008 and 2007 was \$2,723 and \$1,767, respectively.

Investments

During 2008, Hearth adopted the criteria of FASB Statement No. 157, Fair Value Measurements (FASB 157). Hearth values all its investments using level one inputs. Level one inputs are quoted prices in active markets for identical assets and liabilities. Adopting FASB 157 did not result in any change in the measurement of the carrying value of the Hearth's investments, as they have historically been recorded at market value. 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, 2008 AND 2007
(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 \$24,286 and \$23,524 for 2008 and 2007, 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.

Special Events Revenue

Special events revenue in the accompanying combining statements of activities includes private grants, contributions and special events and includes the following at December 31:

	<u>2008</u>	<u>2007</u>
Event revenue	\$15,650	\$18,950
Less - direct expenses	<u>(1,688)</u>	<u>(3,571)</u>
	13,962	15,379
Fundraising expenses	<u>(5,737)</u>	<u>(5,493)</u>
Total special events	<u>\$ 8,225</u>	<u>\$ 9,886</u>

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, determined by the donor, are as follows:

	<u>2008</u>	<u>2007</u>
Operating -		
Materials and supplies	\$1,342	\$1,058
Property and equipment	<u>-</u>	<u>3,500</u>
	<u>\$1,342</u>	<u>\$4,558</u>

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.

HEARTH, INC. AND AFFILIATES
NOTES TO COMBINING FINANCIAL STATEMENTS
DECEMBER 31, 2008 AND 2007
(Continued)

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

SIGNIFICANT ACCOUNTING POLICIES (Continued)

Estimates

The preparation of combining financial statements in accordance with accounting principles generally accepted in the United States of America 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.

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, 2008, the Subsidiary has, for Federal income tax purposes, net operating loss carryforwards of approximately \$259,000 available to offset future taxable income. Also, at December 31, 2008, the Subsidiary has, for state income tax purposes, net operating loss carryforwards of approximately \$226,000 to offset future taxable income. These carryforwards expire at various dates through 2028. The Subsidiary accounts for income taxes in accordance with Financial Accounting Standards Board Statement No. 109, "Accounting for Income Taxes" (FASB 109). FASB 109 does not have a material effect on the combining financial statements for the years ended December 31, 2008 and 2007, since the tax benefit of the net operating loss carryforwards have been reserved.

(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. 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.

HEARTH, INC. AND AFFILIATES

NOTES TO COMBINING FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007 (Continued)

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

NET ASSETS (Continued)

Temporarily Restricted (Continued)

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

	<u>2008</u>	<u>2007</u>
Restricted for predevelopment activities (see page 11)	\$161,108	\$ 93,265
Restricted for programs	<u>43,599</u>	<u>98,970</u>
Total temporarily restricted	<u>\$204,707</u>	<u>\$192,235</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.

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 (see page 18) and East Concord Street Limited Partnership (see below).

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 East Concord Street Limited Partnership (the Partnership), which operates forty-one units of housing for formerly homeless elders.

HEARTH, INC. AND AFFILIATES

**NOTES TO COMBINING FINANCIAL STATEMENTS
DECEMBER 31, 2008 AND 2007
(Continued)**

(2) NET ASSETS AND RELATED PARTY TRANSACTIONS

RELATED PARTY TRANSACTIONS

Transactions between these entities during 2008 and 2007 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 2008 were \$72,708 and \$37,892, respectively, and during 2007 were \$64,852 and \$35,237, 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 December 31:

	<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>
	<u>2007</u>	<u>Management Services</u>	<u>Adminis- trative Services</u>	<u>Total</u>
Burroughs		\$12,138	\$12,712	\$24,850
Beacon		8,034	8,420	16,454
Bishop		<u>8,034</u>	<u>8,420</u>	<u>16,454</u>
		<u>\$28,206</u>	<u>\$29,552</u>	<u>\$57,758</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, 2008 and 2007, is \$123,817 and \$107,394, respectively, including \$16,423 and \$15,493 of interest for 2008 and 2007, 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 2008 and 2007.

HEARTH, INC. AND AFFILIATES
NOTES TO COMBINING FINANCIAL STATEMENTS
DECEMBER 31, 2008 AND 2007
(Continued)

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

RELATED PARTY TRANSACTIONS (Continued)

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, 2008 and 2007, \$53,569 and \$37,500 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 Subsidiary have entered into the following transactions and agreements with the Partnership:

The Partnership rents office space to Hearth at an annual rental of \$28,588 and \$27,755 in 2008 and 2007, 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 \$23,200 and \$21,700 of management and administrative staff (including payroll taxes and fringe benefits) during 2008 and 2007, respectively. Hearth Mgmt. also charged an administrative fee of approximately \$22,600 and \$21,900 during 2008 and 2007, respectively.

Hearth provides maintenance and security staff to the Partnership and charged the Partnership approximately \$177,000 and \$175,000 during 2008 and 2007, respectively, 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 2008 or 2007. The fee is also limited to 2% of gross rents.

The Partnership owes \$231,904 and \$272,094 to Hearth and Hearth Mgmt. at December 31, 2008 and 2007, 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, 2008 and 2007.

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 \$45,000 and \$55,000 as of December 31, 2008 and 2007, respectively, from operating cash flow. The timeframe of when these funds will be approved for release cannot be determined as of December 31, 2008 and, accordingly, the remaining balance is shown as a non-current asset in the accompanying combining statements of financial position.

HEARTH, INC. AND AFFILIATES

**NOTES TO COMBINING FINANCIAL STATEMENTS
DECEMBER 31, 2008 AND 2007
(Continued)**

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

RELATED PARTY TRANSACTIONS (Continued)

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 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 2008 or 2007 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 2008 and 2007 was \$109,614 and \$102,685, respectively.

The notes receivable and accrued interest that have been fully reserved in the accompanying combining financial statements at December 31, 2008 and 2007, consist of the following:

	<u>2008</u>	<u>Principal</u>	<u>Accrued Interest</u>	<u>Total</u>
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>
	<u>2007</u>	<u>Principal</u>	<u>Accrued Interest</u>	<u>Total</u>
Linkage		\$335,213	\$393,092	\$ 728,305
Acquisition		320,000	351,639	671,639
Foundations		<u>99,260</u>	<u>128,321</u>	<u>227,581</u>
Total		<u>\$754,473</u>	<u>\$873,052</u>	<u>\$1,627,525</u>

HEARTH, INC. AND AFFILIATES

NOTES TO COMBINING FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

(Continued)

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

RELATED PARTY TRANSACTIONS (Continued)

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 Subsidiary's investment in the Partnership.

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. 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. This agreement expires June 30, 2016. Hearst charged Ruggles \$21,636 for these services in 2007. As part of renegotiating the above agreements, Hearst has fully reserved the interest and service provider fees for 2007, as they do not expect to collect these amounts.

Additionally, Hearst is to be reimbursed for expenses and overhead applicable to Ruggles, as approved by the Ruggles Partnership in the annual operating budget. Hearst billed Ruggles \$69,999 and \$67,960 during 2008 and 2007, 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 Hearst and reimbursed monthly. In order to pay the expenses for Ruggles, Hearst 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 Hearst's prevailing short-term borrowing rate. The total interest incurred for 2007 was \$77,615 at the *Wall Street Journal* (WSJ) prime interest rates ranging from 7.25% to 8.25%, at the time of the borrowings. Hearst agreed to waive interest beginning January 1, 2008 through December 31, 2011.

Hearst is owed the following amount from Ruggles at December 31, 2008 and 2007, which is included in due from (to) affiliates, net in the accompanying combining statements of financial position. Hearst expects to receive \$40,000 per year from Ruggles until the full balance is paid off. This receivable has been discounted using a 3% rate.

Gross receivable	\$ 943,912
Less - discount	(254,319)
Less - allowance for uncollectible amounts	<u>(235,214)</u>
	<u>\$ 454,379</u>

Hearst is also entitled to an incentive management fee if certain cash flow is achieved by Ruggles, at an amount defined in the agreement. As part of the renegotiating of agreements, Hearst agreed to waive this fee beginning January 1, 2008 through December 31, 2011. Ruggles did not generate adequate cash flows in 2007 in order for Hearst to earn the incentive fee.

HEARTH, INC. AND AFFILIATES
NOTES TO COMBINING FINANCIAL STATEMENTS
DECEMBER 31, 2008 AND 2007
(Continued)

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

RELATED PARTY TRANSACTIONS (Continued)

Ruggles Assisted Living Limited Partnership (Continued)

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.

(4) **INVESTMENTS**

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

Investments are as follows at December 31:

<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>
<u>2007</u>	<u>Cost</u>	<u>Market Value</u>	<u>Unrealized Appreciation (Depreciation)</u>
Fixed income	\$106,789	\$ 96,982	\$ (9,807)
Equities	<u>164,798</u>	<u>165,131</u>	<u>333</u>
	<u>\$271,587</u>	<u>\$262,113</u>	(9,474)
Unrealized depreciation at December 31, 2006			<u>(402)</u>
Unrealized loss on investments			<u>\$ (9,072)</u>

Investments are reported in the accompanying 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.

HEARTH, INC. AND AFFILIATES

**NOTES TO COMBINING FINANCIAL STATEMENTS
DECEMBER 31, 2008 AND 2007**

(Continued)

(5) LONG-TERM DEBT

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

	<u>2008</u>	<u>2007</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 \$70,000 is due. This note is secured by a first mortgage on land and a building.	\$ 119,129	\$ 125,575
Non-interest bearing note payable to the Town of Brookline. This note is due June, 2039. This note is secured by a second mortgage on land and a building.	349,000	349,000
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.	<u>426,000</u>	<u>426,000</u>
Total Beacon	<u>894,129</u>	<u>900,575</u>
<u>Bishop</u>		
1% note payable to the City of Boston, which according to the terms 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.	<u>72,731</u>	<u>72,731</u>
<u>Burroughs</u>		
A bridge loan note payable to a bank, with interest only payments of 5% of the principal due monthly, until conversion to permanent debt no later than May, 2008, when a principal payment of \$680,950 was required. This payment was made in March, 2008, with the use of loan proceeds from CEDAC and the City of Boston (page 21). The remaining balance of \$169,050 is payable in equal monthly principal and interest installments of \$1,320, and matures in May, 2028, at an interest rate of 7%. This note is secured by a first mortgage on land and a building.	167,395	850,000

HEARTH, INC. AND AFFILIATES
NOTES TO COMBINING FINANCIAL STATEMENTS
DECEMBER 31, 2008 AND 2007
(Continued)

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

	<u>2008</u>	<u>2007</u>
<u>Burroughs</u> (Continued)		
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.	522,695	-
Non-interest bearing note payable to CEDAC. All unpaid principal is due August, 2038. This note is secured by a shared second mortgage on land and a building.	<u>675,000</u>	<u>-</u>
Total Burroughs	<u>1,365,090</u>	<u>850,000</u>
Total long-term debt	2,331,950	1,823,306
Less - current portion	<u>15,001</u>	<u>9,490</u>
	<u>\$2,316,949</u>	<u>\$1,813,816</u>

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

2009	\$15,001
2010	\$16,263
2011	\$17,634
2012	\$19,063
2013	\$20,734

(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% and 7.25% at December 31, 2008 and 2007, respectively). The line of credit is secured by substantially all assets of Hearth. There is no balance outstanding as of December 31, 2008. There was a \$50,000 balance outstanding as of December 31, 2007.

(7) **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.

HEARTH, INC. AND AFFILIATES

NOTES TO COMBINING FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007 (Continued)

(7) **CONTINGENCIES** (Continued)

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 with 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.

(9) **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 by September 30, 2009, it is not reflected in the accompanying combining financial statements.

(10) **CONCENTRATIONS**

Funding

Hearth received approximately 33% and 34% of its total operating revenues, of which approximately 32% and 27% remains in accounts receivable as of December 31, 2008 and 2007, respectively, through contracts and sub-contracts from MassHealth (formerly, Massachusetts Department of Medical Assistance), and 25% and 27%, of which approximately 42% and 37% remains in accounts receivable as of December 31, 2008 and 2007, respectively, from the Massachusetts Department of Mental Health (DMH). The DMH contracts expire on June 30, 2009. DMH is currently reprocurring all contracts in the Commonwealth of Massachusetts.

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 financial position of Hearth as of December 31, 2008 and 2007, or on the changes in their net assets for the years then ended.

Cash and Cash Equivalents

Hearth maintains its cash balances in Massachusetts banks and is insured with the limits of the Federal Deposit Insurance Corporation (FDIC). At certain times during the year, cash balances exceeded the insured amounts. Hearth has not experienced any losses in such accounts. Hearth's management believes, given the updated and temporary changes made in the insurance limits by the FDIC in October, 2008, sufficiently mitigate such risks on their cash and cash equivalents.

(11) **SECURITY DEPOSITS**

Tenant security deposits are collected upon move-in. The total liability was \$7,313 and \$6,338 at December 31, 2008 and 2007, respectively. Security deposit cash is included in cash and cash equivalents and security deposit liability is included in accounts payable and accrued expenses in the accompanying combining statements of financial position.

HEARTH, INC. AND AFFILIATES
NOTES TO COMBINING FINANCIAL STATEMENTS
DECEMBER 31, 2008 AND 2007
(Continued)

(12) 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.

(13) RECLASSIFICATIONS

Certain amounts in the 2007 combining financial statements have been reclassified to conform to the 2008 presentation.