

FRONTIER HOUSING, INC.
MOREHEAD, KENTUCKY

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AUDITED COMBINED FINANCIAL STATEMENTS AND
INDEPENDENT AUDITORS' REPORT
FOR THE YEARS ENDED
MARCH 31, 2011 AND 2010



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INDEPENDENT AUDITORS' REPORT

To the Board of Directors
Frontier Housing, Inc.
Morehead, Kentucky

We have audited the accompanying combined statements of financial position of Frontier Housing, Inc. (a non-profit organization) as of March 31, 2011 and 2010, and the related combined statements of activities, changes in net assets, functional expenses, and cash flows for the years then ended. These financial statements are the responsibility of the Organization's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Frontier Housing, Inc., as of March 31, 2011 and 2010, and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated June 23, 2011, on our consideration of Frontier Housing, Inc.'s internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grants agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

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

Craft, Noble & Company, PLLC

Craft, Noble & Company, PLLC
June 23, 2011



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FRONTIER HOUSING, INC.
 COMBINED STATEMENTS OF FINANCIAL POSITION
 MARCH 31, 2011 AND 2010

	<u>2011</u>	<u>2010</u>
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	\$ 1,767,697	\$ 1,026,730
Accounts receivable	265,136	60,404
Grants receivable	200,000	-
Other assets	21,820	60,042
Cost in excess of billings on uncompleted contracts	<u>1,141,205</u>	<u>1,752,251</u>
TOTAL CURRENT ASSETS	3,395,858	2,899,427
NOTES RECEIVABLE - Less allowance for uncollectible notes of \$533,577 in 2011 and \$490,719 in 2010	8,835,965	8,959,062
APPROPRIATED FUNDS - Cash and cash equivalents	1,172,404	687,475
RENTAL PROPERTY	819,123	934,521
LAND HELD FOR DEVELOPMENT	1,292,271	839,277
PROPERTY AND EQUIPMENT		
Land	163,385	133,385
Buildings	539,495	400,329
Office equipment	253,230	247,100
Construction and shop equipment	171,176	157,726
Vehicles	<u>114,548</u>	<u>114,548</u>
TOTAL PROPERTY AND EQUIPMENT	1,241,834	1,053,088
Less accumulated depreciation	<u>(559,566)</u>	<u>(508,257)</u>
NET PROPERTY AND EQUIPMENT	682,268	544,831
OTHER ASSETS		
Intangible assets	72,968	-
Less accumulated amortization	<u>(13,375)</u>	<u>-</u>
NET OTHER ASSETS	59,593	-
TOTAL ASSETS	<u>\$ 16,257,482</u>	<u>\$ 14,864,593</u>

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

FRONTIER HOUSING, INC.
 COMBINED STATEMENTS OF FINANCIAL POSITION (CONTINUED)
 MARCH 31, 2011 AND 2010

	<u>2011</u>	<u>2010</u>
LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES		
Accounts payable	\$ 71,513	\$ 16,163
Accrued liabilities	124,715	110,286
Client advances and deposits	52,623	13,162
Rental and escrow deposits	38,030	42,975
Current portion of long-term debt	649,457	355,522
TOTAL CURRENT LIABILITIES	<u>936,338</u>	<u>538,108</u>
LONG-TERM DEBT, less current portion	<u>2,655,253</u>	<u>2,770,824</u>
TOTAL LIABILITIES	3,591,591	3,308,932
NET ASSETS		
Unrestricted	6,065,040	5,839,914
Temporarily restricted	5,674,765	5,129,531
Permanently restricted	926,086	586,216
TOTAL NET ASSETS	<u>12,665,891</u>	<u>11,555,661</u>
TOTAL LIABILITIES AND NET ASSETS	<u>\$ 16,257,482</u>	<u>\$ 14,864,593</u>

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

FRONTIER HOUSING, INC.
STATEMENTS OF ACTIVITIES
FOR THE YEARS ENDING MARCH 31, 2011 AND 2010

	2011			2010				
	Unrestricted	Temporarily Restricted	Permanently Restricted	Total	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
REVENUES								
House sales and rehabilitations	\$ 3,137,759	\$ -	\$ -	\$ 3,137,759	\$ 2,214,366	\$ -	\$ -	\$ 2,214,366
Land sales	372,367	-	-	372,367	306,177	-	-	306,177
Contributions	43,209	-	-	43,209	54,287	-	-	54,287
Rental income	3,632	-	-	3,632	2,960	-	-	2,960
Interest and fee income	75,231	-	-	75,231	77,046	-	-	77,046
Gain/(loss) on sale of assets	(47,038)	-	-	(47,038)	-	-	-	-
Developer fees	30,000	-	-	30,000	81,769	-	-	81,769
Counseling programs	2,805	-	-	2,805	597	-	-	597
Kentucky Housing Corporation(KHC)								
Affordable Housing Trust Fund	-	126,000	-	126,000	-	87,644	-	87,644
KHC/HUD Federal Grants								
HOME	-	586,950	-	586,950	-	285,460	-	285,460
RHED	-	40,599	-	40,599	-	84,725	-	84,725
CHDO Revenues	-	98,906	-	98,906	-	123,000	-	123,000
Ford Foundation	-	400,000	-	400,000	-	-	-	-
NHPL	-	29,453	-	29,453	-	18,560	-	18,560
Appalachian Regional Commission	-	25,724	-	25,724	-	5,768	-	5,768
NeighborWorks America	441,925	-	427,500	869,425	200,500	-	392,500	593,000
Department of Treasury- CDFI	750,000	-	-	750,000	-	-	-	-
Other grants	-	408,047	-	408,047	-	221,121	-	221,121
Miscellaneous income	64,997	-	-	64,997	33,974	-	-	33,974
Net assets released from restrictions:								
Satisfaction of program restrictions	1,258,075	(1,170,445)	(87,630)	-	1,388,828	(963,224)	(425,604)	-
TOTAL REVENUES AND SUPPORT	6,132,962	545,234	339,870	7,018,066	4,360,504	(136,946)	(33,104)	4,190,454
EXPENSES								
Direct cost of construction	3,219,309	-	-	3,219,309	2,288,229	-	-	2,288,229
Program services - Housing construction	2,487,765	-	-	2,487,765	1,735,851	-	-	1,735,851
General and administrative	142,515	-	-	142,515	113,357	-	-	113,357
Fundraising	58,247	-	-	58,247	56,307	-	-	56,307
TOTAL EXPENSES	5,907,836	-	-	5,907,836	4,193,744	-	-	4,193,744
CHANGE IN NET ASSETS	225,126	545,234	339,870	1,110,230	166,760	(136,946)	(33,104)	(3,290)
NET ASSETS AT BEGINNING OF YEAR	5,839,914	5,129,531	586,216	11,555,661	5,673,154	5,266,477	619,320	11,558,951
NET ASSETS AT END OF YEAR	\$ 6,065,040	\$ 5,674,765	\$ 926,086	\$ 12,665,891	\$ 5,839,914	\$ 5,129,531	\$ 586,216	\$ 11,555,661

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

FRONTIER HOUSING, INC.
 COMBINED STATEMENT OF FUNCTIONAL EXPENSES
 FOR THE YEAR ENDED MARCH 31, 2011

	Program Services & Housing Construction	General & Administrative	Fundraising	Total
Personnel and Fringe Benefits				
Salaries and wages	\$ 744,749	\$ 75,151	\$ 19,953	\$ 839,853
Payroll taxes	46,598	6,045	1,544	54,187
Retirement expense	90,764	11,233	3,065	105,062
Health and Life insurance	106,548	4,333	7,240	118,121
Total Personnel and Fringe Benefits	<u>988,659</u>	<u>96,762</u>	<u>31,802</u>	<u>1,117,223</u>
Overhead Expenses				
Legal, professional and consulting fees	313,918	15,446	4,353	333,717
Workers compensation expense	2,324	37	29	2,390
Utilities	35,371	2,492	1,145	39,008
Marketing	30,281	2,780	1,664	34,725
Insurance	25,914	1,706	1,152	28,772
Occupancy	43,082	2,182	1,326	46,590
Office supplies and postage	26,459	1,926	1,040	29,425
Grant and subsidiary expense	419,470	-	-	419,470
Inventory revaluation	200,000	-	-	200,000
Vehicle and maintenance expense	17,153	169	102	17,424
Interest expense	7,552	1,568	117	9,237
Bad debt expense	85,000	-	-	85,000
Loan servicing fee	5,865	-	-	5,865
Travel, conferences and meetings	93,824	9,845	1,179	104,848
Miscellaneous	102,901	4,120	12,990	120,011
Total Overhead Expenses	<u>1,409,114</u>	<u>42,271</u>	<u>25,097</u>	<u>1,476,482</u>
Total Expenses	<u>2,397,773</u>	<u>139,033</u>	<u>56,899</u>	<u>2,593,705</u>
Depreciation and amortization	<u>89,992</u>	<u>3,482</u>	<u>1,348</u>	<u>94,822</u>
Total Functional Expenses	<u>\$ 2,487,765</u>	<u>\$ 142,515</u>	<u>\$ 58,247</u>	<u>\$ 2,688,527</u>

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

FRONTIER HOUSING, INC.
 COMBINED STATEMENT OF FUNCTIONAL EXPENSES
 FOR THE YEAR ENDED MARCH 31, 2010

	Program Services & Housing Construction	General & Administrative	Fundraising	Total
Personnel and Fringe Benefits				
Salaries and wages	\$ 507,380	\$ 55,694	\$ 19,827	\$ 582,901
Payroll taxes	49,307	4,731	1,954	55,992
Retirement expense	85,809	8,211	3,702	97,722
Health and Life insurance	85,468	8,112	6,619	100,199
Total Personnel and Fringe Benefits	<u>727,964</u>	<u>76,748</u>	<u>32,102</u>	<u>836,814</u>
Overhead Expenses				
Legal, professional and consulting fees	175,887	5,469	4,113	185,469
Workers compensation expense	1,198	8	7	1,213
Utilities	27,388	2,190	1,458	31,036
Insurance	17,031	1,409	1,189	19,629
Marketing	37,817	3,110	2,645	43,572
Occupancy	29,959	2,246	1,820	34,025
Office supplies and postage	21,332	2,152	1,849	25,333
Vehicle and maintenance expense	32,678	330	214	33,222
Interest expense	28,529	2,093	615	31,237
Travel, conferences, and meetings	46,057	13,592	1,450	61,099
Bad debt expense	30,000	-	-	30,000
Loan servicing fee	3,516	-	-	3,516
Grants/subsidy expense	341,903	-	-	341,903
Miscellaneous	145,060	830	7,023	152,913
Total Overhead Expenses	<u>938,355</u>	<u>33,429</u>	<u>22,383</u>	<u>994,167</u>
Total Expenses	<u>1,666,319</u>	<u>110,177</u>	<u>54,485</u>	<u>1,830,981</u>
Depreciation	<u>69,532</u>	<u>3,180</u>	<u>1,822</u>	<u>74,534</u>
Total Functional Expenses	<u>\$ 1,735,851</u>	<u>\$ 113,357</u>	<u>\$ 56,307</u>	<u>\$ 1,905,515</u>

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

FRONTIER HOUSING, INC.
 COMBINED STATEMENTS OF CASH FLOWS
 FOR THE YEARS ENDING MARCH 31, 2011 AND 2010

	<u>2011</u>	<u>2010</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Changes in Net Assets	\$ 1,110,230	\$ (3,290)
Cash Provided (Used) by Operating Activities		
Depreciation and amortization	94,822	74,534
Loss on disposal of assets	47,038	-
Forgiveness of HAC SHOP 2004	(173,939)	-
Decrease (increase) in accounts receivable	(204,732)	129,319
Decrease (increase) in grants receivable	(200,000)	-
Decrease (increase) in other assets	38,222	(38,522)
Decrease (increase) in cost in excess of billings	611,046	(111,391)
Decrease (increase) in appropriated funds	(484,929)	79,297
Increase (decrease) in accounts payable	55,350	(78,852)
Increase (decrease) in accrued liabilities	14,429	8,207
Increase (decrease) in rental reserves, advances and escrows	34,516	8,348
	<u>942,053</u>	<u>67,650</u>
NET CASH PROVIDED BY OPERATING ACTIVITIES	942,053	67,650
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of property and equipment	(150,524)	(236,531)
Increase in land held for development	(452,994)	(62,331)
Increase in intangible assets	(72,968)	-
Decrease in notes receivable	123,097	483,195
	<u>(553,389)</u>	<u>184,333</u>
NET CASH PROVIDED (USED) BY INVESTING ACTIVITIES	(553,389)	184,333
CASH FLOWS FROM FINANCING ACTIVITIES		
Draws on long-term debt	722,288	626,513
Payments on long-term debt	(369,985)	(778,026)
	<u>352,303</u>	<u>(151,513)</u>
NET CASH PROVIDED (USED) BY FINANCING ACTIVITIES	352,303	(151,513)
NET INCREASE IN CASH AND CASH EQUIVALENTS	740,967	100,470
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	<u>1,026,730</u>	<u>926,260</u>
CASH AND CASH EQUIVALENTS AT END OF YEAR	<u>\$ 1,767,697</u>	<u>\$ 1,026,730</u>
Supplemental Information		
Interest paid	<u>\$ 46,172</u>	<u>\$ 54,979</u>

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

FRONTIER HOUSING, INC.
NOTES TO FINANCIAL STATEMENTS
FOR THE YEARS ENDED MARCH 31, 2011 AND 2010

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Activities

Frontier Housing, Inc.'s (the Organization) purpose is to make available fundamental housing opportunities to families living in eastern Kentucky. This is accomplished through financial education, low-interest financing, and by providing quality housing options including home ownership and rental housing. Additionally, during the year ended March 31, 2011 the Organization started operations of a wholly-owned subsidiary Next Step Network, LLC. Next Step Network, LLC is a nonprofit social enterprise whose mission is to build a national distribution system to deliver high quality, energy efficient, factory built housing at scale. This allows nonprofits to help home owners achieve wealth by growing equity, preserving assets and replacing substandard mobile homes with new ENERGY STAR homes.

Income Recognition

Revenue is recognized on construction work-in-process by the “completed contract” method. Under this method, construction costs are accumulated during the period of construction, but no revenue is recorded before the substantial completion of the work in compliance with the funding source requirements. Losses, if any, are recognized immediately when such losses can be reasonably estimated. The asset “Costs in Excess of Billings on Uncompleted Contracts” represents costs incurred on uncompleted contracts in excess of amounts billed.

Grant funds received and expended in connection with the purpose of the grants are recognized as revenues as the related expenses are incurred. Grant funds received but not expended are recorded as deferred revenues or temporarily restricted assets.

Cash and Cash Equivalents

The Organization recognizes all cash on hand, demand deposits, time deposits, and highly liquid debt instruments with a maturity of six months or less to be cash equivalents. Cash and cash equivalents for the purpose of the statement of cash flows exclude restricted cash and cash equivalents.

Property and Equipment

Property and equipment are recorded at cost or at fair market value at the time of donation if acquired by gift. Depreciation is calculated by the Organization using the straight-line method over the expected useful life of the assets with no salvage value calculated. The range of useful lives used in computing depreciation is ordinarily 2-39 years.

Notes Receivable

Notes receivable represent amounts received from individuals on real estate loans, which are ordinarily repayable over periods up to 40 years with 0-8% interest. Interest income on the notes is recognized at the stated rate in the note, net of any interest allowance the borrower has been given by the Organization.

Land Held for Development

Land held for development represents the cost of land and related site development for lots held for resale.

Federal Income Taxes

The Organization is a tax-exempt organization under section 501(c)(3) of the Internal Revenue Code. Accordingly, no provision has been made for any income tax expense.

Financial Accounting Standards Board (FASB) ASC 740-10-50, *Income Taxes* (formerly FIN 48, *Accounting for Uncertainty in Income Taxes*) requires entities to disclose known or anticipated positions of income tax uncertainty. The Organization is not aware of any unrelated business income or uncertain tax positions that may affect the financial statements as of June 23, 2011. The Organization has never been audited by the Internal Revenue Service (IRS), however, the tax years 2008 forward could be subject to examination by the IRS or other applicable tax jurisdictions.

FRONTIER HOUSING, INC.
NOTES TO FINANCIAL STATEMENTS
FOR THE YEARS ENDED MARCH 31, 2011 AND 2010

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Principles of Combination

The financial statements include the combined statements of the Organization and its subsidiary, Frontier National, LLC. Accordingly, all significant inter-company balances and transactions have been eliminated.

Donated Property, Materials and Services

Donated property, materials, and services are recorded at their estimated fair market value when received. The statement of activities for the years ended March 31, 2011 and 2010 recognized \$43,209 and \$54,287, respectively, in contributions, which include in-kind contributions made to the Organization.

Estimates

The preparation of financial statements in conformity with generally accepted accounting principles necessarily includes the use of management’s estimates. Actual results could differ from those estimates.

NOTE 2 – CASH AND CASH EQUIVALENTS

Cash and cash equivalents are on deposit in banks and are fully covered by the FDIC. Furthermore, cash and cash equivalents may be temporarily restricted by the terms of grant and loan agreements or by Board action. Restricted cash and cash equivalents are not treated as cash or cash equivalents when preparing the statement of cash flows. The following is a summary of restricted and unrestricted cash and cash equivalents at March 31:

	<u>2011</u>	<u>2010</u>
Unrestricted cash and cash equivalents	\$ 1,767,697	\$ 1,026,730
Restricted cash and cash equivalents	<u>1,172,404</u>	<u>687,475</u>
Total	<u>\$ 2,940,101</u>	<u>\$ 1,714,205</u>

NOTE 3 – TEMPORARILY RESTRICTED NET ASSETS

Any assets resulting from funds upon which the funding entity has placed restrictions on the original and/or revolving proceeds are appropriately recorded in the financial statements with an offsetting restriction to net assets. As of March 31, the following assets have been temporarily restricted:

	<u>2011</u>	<u>2010</u>
HAC Shop	\$ 203,646	\$ 199,278
HUD/Kentucky Housing Corporation	4,323,116	3,974,912
Community Development Block Grant Bath County	598,003	605,341
Next Step Network, LLC	200,000	-
Federal Home Loan Bank	<u>350,000</u>	<u>350,000</u>
Total	<u>\$ 5,674,765</u>	<u>\$ 5,129,531</u>

FRONTIER HOUSING, INC.
NOTES TO FINANCIAL STATEMENTS
FOR THE YEARS ENDED MARCH 31, 2011 AND 2010

NOTE 4 – LONG-TERM DEBT

Long-term debt as of March 31 is as follows:

	<u>2011</u>	<u>2010</u>
Non-interest bearing note payable to Kentucky Housing Corporation (KHC), due January 1, 2015. Secured by Real Property. Loan is forgivable at maturity if not in default.	\$ 286,781	\$ 286,781
1.00% note payable to KHC with principal and interest of \$12,054 payable annually under terms of Affordable Housing Trust Grant and Loan Agreement.	795,928	836,844
Line of credit payable to Federation of Appalachian Housing Enterprises, Inc. (FAHE)	550,321	207,201
1.00% unsecured note payable to KHC, due January 1, 2027 with quarterly interest payments of \$125.00.	33,333	35,000
Note payable to Housing Assistance Council (HAC) consisting of five notes due upon sale of land purchased for low-income housing units. Interest is 0% through an agreed upon due date in the notes and then is variable at HAC's prevailing rate. Furthermore, upon satisfactory completion of the condition of the note agreements, 80% of the proceeds borrowed is forgivable to Frontier Housing, Inc.	502,878	657,703
1% note payable to FAHE, under the terms of Non-Profit Housing Production and Rental Loan Programs (NHPL & NHRL):		
Due June 15, 2017, with interest paid quarterly and \$4,432 of principal paid annually.	30,606	35,452
Due June 15, 2022, with interest paid quarterly and \$4,067 of principal paid annually.	48,151	52,871
Due June 15, 2019, with interest paid quarterly and \$4,760 of principal paid annually.	42,267	47,600
Due June 15, 2018, with interest paid quarterly and \$5,421 of principal paid annually.	42,785	48,785
Due June 15, 2021, with interest paid quarterly and \$3,438 of principal due annually.	37,307	41,250
Due June 15, 2019, with interest paid quarterly and \$4,585 of principal paid annually.	45,225	50,422
Due June 15, 2024 with interest paid quarterly and \$4,567 of principal due annually.	58,571	63,932
Due July 1, 2024 with interest paid quarterly and \$4,139 of principal due annually.	57,163	61,956

FRONTIER HOUSING, INC.
NOTES TO FINANCIAL STATEMENTS
FOR THE YEARS ENDED MARCH 31, 2011 AND 2010

NOTE 4 – LONG-TERM DEBT (CONTINUED)

	<u>2011</u>	<u>2010</u>
Due June 15, 2026 with interest paid quarterly and \$3,524 of principal due annually.	\$ 52,835	\$ 56,358
Due November 1, 2030 with interest paid quarterly and \$2,500 of principal due annually.	36,300	37,139
Note payable to FAHE secured by Moores Flat property	167,757	-
Note payable to FAHE secured by Red Bud property	188,783	-
Notes payable to various corporations, interest of 0%-3.5%, varying principal payments and maturities.	69,719	349,052
Notes payable to the USDA, interest of 6%	258,000	258,000
	<u>3,304,710</u>	<u>3,126,346</u>
TOTAL NOTES PAYABLE	<u>3,304,710</u>	<u>3,126,346</u>
Less principal due within one year	<u>649,457</u>	<u>355,522</u>
TOTAL LONG-TERM DEBT	<u>\$ 2,655,253</u>	<u>\$ 2,770,824</u>

The principal repayment requirements relating to long-term debt are as follows:

	<u>2011</u>	<u>2010</u>
<u>Year Ending March 31</u>		
2011	\$ -	\$ 355,522
2012	649,457	258,482
2013	99,429	121,927
2014	481,260	97,346
2015	100,010	97,768
2016	100,298	-
Later years	1,874,257	2,197,301
TOTAL	<u>\$ 3,304,711</u>	<u>\$ 3,128,346</u>

FRONTIER HOUSING, INC.
NOTES TO FINANCIAL STATEMENTS
FOR THE YEARS ENDED MARCH 31, 2011 AND 2010

NOTE 5 – CONTINGENCIES

The Organization receives a substantial portion of its revenues from federal and state governmental agencies and other non-profit corporations. Thus, a significant reduction in the level of this support would have a negative effect on the Organization's programs and activities. Management of the Organization is aware of this dependence and does not anticipate any significant reduction, if any, in the foreseeable future. Furthermore, management has made prudent business decisions based on all revenue sources for the entity to not only continue as a going concern, but to grow its current programs and services in its five-year business plan.

NOTE 6 – SUBSEQUENT EVENTS

Management of the Organization has considered subsequent events through June 23, 2011, the date this report becomes available for issue.

NOTE 7 – RETIREMENT PLAN

The Organization is a participating employer in the County Employees' Retirement System (CERS), which is a cost sharing, multi-employer defined benefit plan. CERS provides retirement, disability and death benefits to plan members. Retirement benefits may be extended to beneficiaries of plan members under certain circumstances. Funding for the plan is provided through payroll withholding and contributions by the Organization. Non-hazardous positions are withheld at the rate of 5% of the employee's total compensation subject to contribution. The Organization contributed 16.93% and 16.16% for March 31, 2011 and 2010, respectively.

The Organization covered payroll for the years ending March 31, 2011, 2010, and 2009 was \$715,313, \$723,503 and \$649,373 respectively. The Organizations contribution requirement for CERS for the years ending March 31, 2011, 2010 and 2009 were \$102,732, \$106,804 and \$97,918, respectively. This represents 100% of the required contribution.

Benefits under the plan will vary based on final compensation, years of service and other factors as fully described in the plan documents. The CERS issues a publicly available financial report that includes financial statements and required supplementary information. That report may be obtained by writing to Kentucky Retirement Systems, 1260 Louisville Road, Frankfort, Kentucky 40601.

The Organization also participated in a section 403(b)(7) salary reduction retirement plan for eligible full-time employees during the last fiscal year. The plan provided for no employer match of employee contributions.

NOTE 8 – RELATED PARTY TRANSACTIONS

The Organization is a member of the Federation of Appalachian Housing Enterprises, Inc. (FAHE), a non-profit, tax-exempt organization. FAHE is comprised of similar organizations whose purpose is to construct and provide housing for low-income families in several states throughout the Appalachian area. As such, FAHE serves as a pass-through entity for loans and grants that are received by members. During 2011 and 2010, the Organization participated in and received pass-through loans and grants through FAHE in the ordinary course of its business.

Additionally, the Organization is a 0.51% member of Boodry Place, LLC. Boodry Place, LLC is a Kentucky limited liability company set up to provide affordable rental housing to low income families. The Organization received grants for this project that were loaned to Boodry Place, LLC. At March 31, 2011 and 2010 the Organization had loans receivable from Boodry Place, LLC of \$1,091,375 and \$1,107,908, respectively.

FRONTIER HOUSING, INC.
NOTES TO FINANCIAL STATEMENTS
FOR THE YEARS ENDED MARCH 31, 2011 AND 2010

NOTE 9 – PERMANENTLY RESTRICTED NET ASSETS

Any assets resulting from funds upon which the funding entity has placed restrictions on the original and/or revolving proceeds are appropriately recorded in the financial statements with an offsetting restriction to net assets. As of March 31, the following assets have been permanently restricted:

	<u>2011</u>	<u>2010</u>
NeighborWorks America Capital Fund	<u>\$ 926,086</u>	<u>\$ 586,216</u>
Total	<u><u>\$ 926,086</u></u>	<u><u>\$ 586,216</u></u>

NOTE 10 – NOTES RECEIVABLE

A portion of the notes receivable represents balances which are deferred until the original note is paid off, at which time, the original deferred note becomes payable over a period of agreed upon years. In certain qualifying cases, the deferred note portion is considered forgivable if specified criteria have been met throughout the life of the loan. Deferred loans at March 31, 2011 and 2010 were \$3,999,599 and \$3,877,686, respectively, of which the forgivable portion is \$387,807 and \$359,851, respectively. Additionally, at March 31 2011 and 2010 \$3,883,651 and \$4,017,039, respectively, were assigned or pledged as collateral for notes payable.

FRONTIER HOUSING, INC.
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED MARCH 31, 2011

<u>Federal Grantor/Pass-Through Grantor/Program Title</u>	<u>Program Type</u>	<u>Federal CFDA Number</u>	<u>Pass-Through Grantor's Number</u>	<u>Loan Balance or Federal Expenditures</u>
Appalachian Regional Commission:				
Pass-Through from Federation of Appalachian Housing Enterprises, Inc. (FAHE) ARC 302	B	23.005	KY07(B)1-A	25,724
U. S. Department of Housing & Urban Development:				
Rural Housing & Urban Development	B	14.250	RH-03-KY-I-0031	40,599
U.S. Department of Treasury NeighborWorks America Community Development Financial Institutions Grant	A A*	21.000 21.020		919,500 750,000
Pass Through From:				
Kentucky Housing Corporation (KHC): Home Investment Partnership Program (HOME) Housing Assistance Council (HAC) SHOP Loan and Grant	A* A A	14.239 14.247 14.247	HB08-0007-01	685,856 176,939 502,878 **
TOTAL FEDERAL AWARDS				<u>\$ 3,101,496</u>

*Major Program per Circular A-133

** Denotes Loan Balance

See accompanying notes to schedule of expenditures of federal awards.

FRONTIER HOUSING, INC.
NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED MARCH 31, 2011

NOTE A – BASIS OF PRESENTATION

The accompanying schedule of expenditures of federal awards includes the federal grant activity of Frontier Housing, Inc. and is presented on the cash basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, Audits of States, Local Governments and Non-Profit Organizations. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in, the preparation of the financial statements.

NOTE B – INSURANCE

The Organization carried insurance coverage during the entire year in amounts sufficient or in excess of required levels, including coverage for general and professional liability, real and personal property, workers compensation and fidelity bonding of employees who have access to funds.

REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING
BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN
ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

To the Board of Directors
Frontier Housing, Inc.
Morehead, Kentucky

We have audited the financial statements of Frontier Housing, Inc. (a non-profit organization) as of and for the year ended March 31, 2011, and have issued our report thereon dated June 23, 2011. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

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

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the financial statements will not be prevented, or detected, and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the following deficiency to be a significant deficiency in internal control:

Organization Structure

The size of the Organization's accounting staff precludes certain internal controls that would be preferred if the accounting staff were large enough to provide optimum segregation of duties.



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Organization Response and Corrective Action Plan

It does not appear that it would be economically feasible for our Organization to enlarge our staff to alleviate the lack of a complete segregation of duties. Thus, it is important that our Board provide oversight and independent review functions.

Compliance

As part of obtaining reasonable assurance about whether Frontier Housing, Inc.'s financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

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

Craft, Noble & Company, PLLC

Craft, Noble & Company, PLLC
June 23, 2011

INDEPENDENT AUDITORS' REPORT ON COMPLIANCE WITH REQUIREMENTS THAT COULD HAVE A
DIRECT AND MATERIAL EFFECT ON EACH MAJOR PROGRAM AND ON INTERNAL
CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133

To the Board of Directors
Frontier Housing, Inc.
Morehead, Kentucky

Compliance

We have audited the compliance of Frontier Housing, Inc. (a non-profit organization) with the types of compliance requirements described in the "U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement" that could have a direct and material effect on each of its major federal programs for the year ended March 31, 2011. Frontier Housing, Inc.'s major federal programs are identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of Frontier Housing, Inc.'s management. Our responsibility is to express an opinion on Frontier Housing, Inc.'s compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America, the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, and OMB Circular A-133, "Audits of States, Local Governments, and Non-Profit Organizations". Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about Frontier Housing, Inc.'s compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of Frontier Housing, Inc.'s compliance with those requirements.

In our opinion, Frontier Housing, Inc. complied, in all material respects, with the requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended March 31, 2011.

Internal Control Over Compliance

The management of Frontier Housing, Inc. is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered Frontier Housing, Inc.'s internal control over compliance with requirements that could have a direct and material effect on a major federal program to determine the auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the organization's internal control over compliance.



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A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A *material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis.

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

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

Craft, Noble & Company, PLLC

Craft, Noble & Company, PLLC
June 23, 2011

FRONTIER HOUSING, INC.
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED MARCH 31, 2011

SUMMARY OF AUDITORS' RESULTS

1. The auditors' report expresses an unqualified opinion on the financials statements of Frontier Housing, Inc.
2. Our report on the financial statements disclosed one significant deficiency in the internal control structure.
3. No instances of noncompliance material to the financial statements of Frontier Housing, Inc. were disclosed during our audit.
4. The auditors' report on compliance for the major federal awards program for Frontier Housing, Inc. expresses an unqualified opinion on all major federal programs.
5. Our audit report disclosed no audit finding required to be reported under Section 510(a) of OMB Circular A-133.
6. The programs tested as major programs included:

Community Development Financial Institutions CFDA #21.020 Type A.
HOME Investment Partnership CFDA #14.239 Type A
7. The threshold to determine Type A: \$300,000.
8. Frontier Housing, Inc. was determined to be a low-risk auditee.
9. In connection with tests of internal control and compliance with laws and regulations, no material weaknesses were noted in internal control, and the Organization was in substantial compliance with laws and regulations.
10. There were no questioned costs with respect to major programs selected for compliance tests.

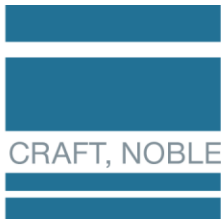
INDEPENDENT AUDITORS' REPORT
ON ADDITIONAL INFORMATION

To the Board of Directors
Frontier Housing, Inc.
Morehead, Kentucky

Our report on our audits of the basic financial statements of Frontier Housing, Inc. for the years ended March 31, 2011 and 2010 appears on page 1. We conducted our audits in accordance with auditing standards generally accepted in the United States of America for the purpose of forming an opinion on the basic financial statements taken as a whole. The Detailed Statements of Support, Revenue and Expenses, Statements of Financial Position – NeighborWorks America Capital Fund, and Statements of Activities – NeighborWorks America Capital Fund are presented for the purpose of additional analysis and are not required parts of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Craft, Noble & Company, PLLC

Craft, Noble & Company, PLLC
June 23, 2011



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FRONTIER HOUSING, INC.
 COMBINED DETAILED STATEMENTS OF SUPPORT, REVENUE AND EXPENSES
 FOR THE YEARS ENDED MARCH 31, 2011 AND 2010

	<u>2011</u>	<u>2010</u>
SUPPORT AND REVENUE (RESTRICTED AND UNRESTRICTED)		
House sales and rehabilitations	\$ 3,137,759	\$ 2,214,366
Land sales	372,367	306,177
Contributions	43,209	54,287
Rental income	3,632	2,960
Interest income	75,231	77,046
Gain/(loss) on sale of assets	(47,038)	-
Developer fees	30,000	81,769
Counseling program	2,805	597
Miscellaneous income	64,997	33,974
GRANTS AND LOANS (RESTRICTED)		
Kentucky Housing Corporation (KHC)		
Affordable Housing Trust Fund	126,000	87,644
KHC/HUD Federal grants		
HOME	586,950	285,460
RHED	40,599	84,725
CHDO revenues	98,906	123,000
Ford Foundation	400,000	-
NHPL	29,453	18,560
Appalachian Regional Commission	25,724	5,768
NeighborWorks America	869,425	593,000
Department of Treasury - CDFI Grant	750,000	-
Other grants	408,047	221,121
TOTAL SUPPORT AND REVENUE	<u>7,018,066</u>	<u>4,190,454</u>
EXPENSES		
Direct Cost of Construction	3,219,309	2,288,229
Other Indirect Costs		
Salaries and wages	839,853	582,901
Payroll taxes	54,187	55,992
Retirement expense	105,062	97,722
Health and life insurance	118,121	100,199
Legal, professional and consulting fees	333,717	185,469
Workers compensation expense	2,390	1,213
Utilities	39,008	31,036
Insurance	28,772	19,629
Marketing	34,725	43,572
Occupancy	46,590	34,025
Office supplies and postage	29,425	25,333
Grant/subsidy expense	419,470	341,903
Inventory revaluation	200,000	-
Vehicle and maintenance expense	17,424	33,222
Interest expense	9,237	31,237
Bad debt and forgivable loan expense	85,000	30,000
Loan servicing fee	5,865	3,516
Travel, conferences and meetings	104,848	61,099
Miscellaneous	120,011	152,913
Depreciation expense	94,822	74,534
Total Other Indirect Costs	<u>2,688,527</u>	<u>1,905,515</u>
TOTAL EXPENSES	<u>5,907,836</u>	<u>4,193,744</u>
EXCESS (DEFICIT) OF SUPPORT AND REVENUE OVER EXPENSES	<u>\$ 1,110,230</u>	<u>\$ (3,290)</u>

See report on additional information.

FRONTIER HOUSING, INC.
 STATEMENTS OF FINANCIAL POSITION - NEIGHBORWORKS AMERICA CAPITAL FUND
 MARCH 31, 2011 AND 2010

	<u>2011</u>	<u>2010</u>
ASSETS		
Cash and cash equivalents	\$ 432,133	\$ 156,096
Mortgages receivable	<u>493,953</u>	<u>430,120</u>
 TOTAL ASSETS	 <u>\$ 926,086</u>	 <u>\$ 586,216</u>
NET ASSETS		
Permanently restricted	<u>\$ 926,086</u>	<u>\$ 586,216</u>
 TOTAL NET ASSETS	 <u>\$ 926,086</u>	 <u>\$ 586,216</u>

See report on additional information.

FRONTIER HOUSING, INC.
STATEMENTS OF ACTIVITIES - NEIGHBORWORKS AMERICA CAPITAL FUND
FOR THE YEARS ENDED MARCH 31, 2011 AND 2010

	<u>2011</u>	<u>2010</u>
Revenues and Other Support		
Capital Grant - NeighborWorks America	\$ 427,500	\$ 392,500
Net assets released from restriction	<u>(87,630)</u>	<u>(425,604)</u>
Total Revenues and Other Support	339,870	(33,104)
CHANGE IN NET ASSETS	339,870	(33,104)
NET ASSETS AT BEGINNING OF YEAR	<u>586,216</u>	<u>619,320</u>
NET ASSETS AT END OF YEAR	<u><u>\$ 926,086</u></u>	<u><u>\$ 586,216</u></u>

See report on additional information.