

APPALACHIA SERVICE PROJECT, INC.

FINANCIAL REPORT

December 31, 2011

APPALACHIA SERVICE PROJECT, INC.

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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Appalachia Service Project, Inc.
Johnson City, Tennessee

We have audited the accompanying statements of financial position of Appalachia Service Project, Inc., (a nonprofit organization) as of December 31, 2011 and 2010, and the related statements of activities, 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 audits.

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 audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Organization's internal control over financial reporting. Accordingly we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit includes assessing the accounting principles used and the 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 Appalachia Service Project, Inc. as of December 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 May 7, 2012, on our consideration of Appalachia Service Project, Inc.'s internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Our audit was conducted for the purpose of forming an opinion on the financial statements 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 financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

Brown, Edwards & Company, S. L. P.
CERTIFIED PUBLIC ACCOUNTANTS

Bristol, Virginia
May 7, 2012

— Your Success is Our Focus —

FINANCIAL STATEMENTS

APPALACHIA SERVICE PROJECT, INC.

STATEMENTS OF FINANCIAL POSITION

December 31, 2011 and 2010

ASSETS

	<u>2011</u>	<u>2010</u>
CURRENT ASSETS		
Cash and cash equivalents:		
Undesignated	\$ 749,047	\$ 613,307
Board designated - Operating reserve	1,000,000	443,182
Board designated - Revolving loan fund	428,951	140,363
Board designated - Endowment (Note 5)	<u>162,163</u>	<u>140,363</u>
Unrestricted cash	2,340,161	1,196,852
Board designated endowment fund (Notes 3, 5 and 12)	229,539	230,277
Grant receivable	561,004	618,876
Other receivables	2,139	2,809
Employee notes receivable (due within one year)	8,450	-
Mortgages receivable current, net (Note 4)	5,845	7,596
Prepaid expenses	8,010	8,010
Inventories (Note 6)	<u>132,309</u>	<u>100,596</u>
Total current assets	3,287,457	2,165,016
RESTRICTED CASH (Note 11)	10,428	10,960
PROPERTY AND EQUIPMENT, net (Note 7)	1,820,807	1,872,516
EMPLOYEE NOTES RECEIVABLE (due after one year)	16,400	-
LONG-TERM MORTGAGES RECEIVABLE, net (Note 4)	<u>65,009</u>	<u>68,366</u>
	<u>\$ 5,200,101</u>	<u>\$ 4,116,858</u>
LIABILITIES AND NET ASSETS		
CURRENT LIABILITIES		
Accounts payable and accrued expenses	\$ 137,316	\$ 107,135
Current maturities of notes payable (Note 8)	7,055	6,965
Current portion of capital lease obligation (Note 10)	17,574	14,623
Deferred revenue	<u>560,755</u>	<u>63,284</u>
Total current liabilities	722,700	192,007
LONG-TERM LIABILITIES (net of Current Portion)		
Notes payable (Note 8)	65,000	70,694
Capital lease obligation (Note 10)	<u>14,870</u>	<u>32,445</u>
Total long-term liabilities	79,870	103,139
COMMITMENTS AND CONTINGENCIES (Note 15)	-	-
Total liabilities	<u>802,570</u>	<u>295,146</u>
NET ASSETS (Note 11)		
Unrestricted	4,387,103	3,810,752
Temporarily restricted	<u>10,428</u>	<u>10,960</u>
Total net assets	<u>4,397,531</u>	<u>3,821,712</u>
	<u>\$ 5,200,101</u>	<u>\$ 4,116,858</u>

The Notes to Financial Statements are an integral part of these statements.

APPALACHIA SERVICE PROJECT, INC.

STATEMENTS OF ACTIVITIES
For the Years Ended December 31, 2011 and 2010

	<u>2011</u>	<u>2010</u>
UNRESTRICTED NET ASSETS		
Revenues		
Donations	\$ 1,804,637	\$ 1,815,228
Grants	1,161,004	618,876
Volunteer work crews fees	4,614,646	4,482,521
Donated items	50,286	71,085
Merchandise sales	169,793	170,172
Interest and investment income	3,323	26,731
Gain on sale of assets	11,732	9,434
Miscellaneous	<u>122,377</u>	<u>42,898</u>
Total unrestricted revenues	<u>7,937,798</u>	<u>7,236,945</u>
NET ASSETS RELEASED FROM RESTRICTIONS		
Satisfaction of purpose restrictions	<u>532</u>	<u>39,799</u>
Total unrestricted revenues and net assets released from restrictions	<u>7,938,330</u>	<u>7,276,744</u>
Expenses		
Program services	<u>6,227,496</u>	<u>5,889,377</u>
Supporting services		
Office and administration	392,364	422,311
Fundraising	<u>742,119</u>	<u>723,282</u>
Total supporting services	<u>1,134,483</u>	<u>1,145,593</u>
Total expenses	<u>7,361,979</u>	<u>7,034,970</u>
Change in unrestricted net assets	<u>576,351</u>	<u>241,774</u>
Balance, beginning	<u>3,810,752</u>	<u>3,568,978</u>
Balance, ending	<u>\$ 4,387,103</u>	<u>\$ 3,810,752</u>

(Continued)

APPALACHIA SERVICE PROJECT, INC.

STATEMENTS OF ACTIVITIES
For the Years Ended December 31, 2011 and 2010

	<u>2011</u>	<u>2010</u>
TEMPORARILY RESTRICTED NET ASSETS		
Contributions	\$ -	\$ 2,598
Net assets released from restrictions	<u>(532)</u>	<u>(39,799)</u>
Change in temporarily restricted net assets	(532)	(37,201)
Balance, beginning	<u>10,960</u>	<u>48,161</u>
Balance, ending	<u>\$ 10,428</u>	<u>\$ 10,960</u>
SUMMARY OF CHANGES IN NET ASSETS		
Change in total net assets	\$ 575,819	\$ 204,573
Balance, beginning	<u>3,821,712</u>	<u>3,617,139</u>
Balance, ending	<u>\$ 4,397,531</u>	<u>\$ 3,821,712</u>

The Notes to Financial Statements are an integral part of these statements.

APPALACHIA SERVICE PROJECT, INC.

STATEMENTS OF FUNCTIONAL EXPENSES
For the Years Ended December 31, 2011 and 2010

	Program	Supporting		2011	2010
	Services	Services			
	Home Repair and Building	Office and Administration	Fundraising		
Salaries and related taxes	\$ 1,917,075	\$ 222,560	\$ 142,475	\$ 2,282,110	\$ 2,047,424
Employee benefits	420,419	57,881	24,843	503,143	466,803
Total salaries and related expenses	2,337,494	280,441	167,318	2,785,253	2,514,227
Staff expenses	117,938	10,941	13,340	142,219	108,871
Group expenses	569,515	-	-	569,515	545,471
Repair/rehabilitation/construction	1,876,617	-	-	1,876,617	1,790,791
Transportation/maintenance	118,396	2,600	7,862	128,858	110,581
Publications	76,553	-	359,649	436,202	388,373
Office expenses	393,762	35,965	17,781	447,508	410,211
Program expenses	340,944	1,195	158,038	500,177	575,965
Taxes, licenses and fees	55,526	(1,558)	1,495	55,463	42,515
Ranch and warehouse	11,802	-	-	11,802	9,024
Professional fees	37,706	55,755	14,294	107,755	230,457
Miscellaneous	277	1	1	279	426
Total expenses before depreciation	5,936,530	385,340	739,778	7,061,648	6,726,912
Depreciation	290,966	7,024	2,341	300,331	308,058
Total expenses	<u>\$ 6,227,496</u>	<u>\$ 392,364</u>	<u>\$ 742,119</u>	<u>\$ 7,361,979</u>	<u>\$ 7,034,970</u>

The Notes to Financial Statements are an integral part of these statements.

APPALACHIA SERVICE PROJECT, INC.

STATEMENTS OF CASH FLOWS
For the Years Ended December 31, 2011 and 2010

	<u>2011</u>	<u>2010</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Change in total net assets	\$ 575,819	\$ 204,573
Adjustments to reconcile change in total net assets to net cash provided by (used in) operating activities:		
Depreciation	300,331	308,058
Gain on sale of assets	(11,732)	(9,434)
In-kind donations	(50,286)	(71,085)
Loss (gain) on investments	5,057	(19,465)
Allowance for loan losses	(20,711)	(18,917)
(Increase) decrease in:		
Grant receivables	57,872	(558,630)
Mortgages receivable	25,819	25,145
Other receivables	670	97
Prepaid expenses	-	(8,010)
Inventories	13,073	56,336
Increase (decrease) in:		
Accounts payable and accrued expenses	30,181	21,139
Deferred revenue	497,471	(3,552)
	<u>1,423,564</u>	<u>(73,745)</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of property and equipment	(279,290)	(298,232)
Proceeds from sale of equipment	14,900	12,576
Payments received on employee receivables	8,150	-
Endowment dividends reinvested	(4,319)	(3,455)
	<u>(260,559)</u>	<u>(289,111)</u>
CASH FLOWS FROM FINANCING ACTIVITIES		
Payments on lease	(14,624)	(13,237)
Principal payments on notes payable	(5,604)	(5,603)
	<u>(20,228)</u>	<u>(18,840)</u>
INCREASE (DECREASE) IN CASH	1,142,777	(381,696)
CASH, beginning	<u>1,207,812</u>	<u>1,589,508</u>
CASH, ending	<u>\$ 2,350,589</u>	<u>\$ 1,207,812</u>
RECONCILIATION OF CASH TO STATEMENT OF FINANCIAL POSITION		
Cash and cash equivalents, unrestricted	\$ 2,340,161	\$ 1,196,852
Cash and cash equivalents, restricted	<u>10,428</u>	<u>10,960</u>
	<u>\$ 2,350,589</u>	<u>\$ 1,207,812</u>
SUPPLEMENTAL INFORMATION		
Interest paid	<u>\$ 10,195</u>	<u>\$ 6,086</u>

The Notes to Financial Statements are and integral part of these statements.

APPALACHIA SERVICE PROJECT, INC.

NOTES TO FINANCIAL STATEMENTS

December 31, 2011

Note 1. Significant Accounting Policies

Nature of Activities

Appalachia Service Project, Inc. (ASP) is a nonprofit corporation organized for the purpose of alleviating sub-standard housing conditions in Appalachia by utilizing volunteers to repair and renovate housing for the individuals affected by these conditions. ASP allows for the exchange of culture, hopes, talents, faith and love between volunteers and Appalachian families. The purpose of the project is to extend a helping hand to fellow human beings in the spirit of love and acceptance. ASP's programs are supported primarily by grants, donations and fees paid by volunteer work groups. ASP operates year-round centers in Johnson City, TN; Chavies, KY; Jonesville, VA; and Guyan Valley, WV.

ASP performs major remodeling and repairs to various homes. When necessary, ASP has allowed notes to be carried for the remodeling work performed. Individuals apply for assistance through grants and low or non-interest bearing mortgages. Assistance is determined based upon financial need and debt to equity ratios with a varying amount of grants and mortgages per individual.

Basis of Accounting and Presentation

The accompanying financial statements are presented on the accrual basis of accounting.

Financial statement presentation follows the recommendations of the Financial Accounting Standards Board Accounting Standards Codification 958, *Not-for-Profit Entities*. Under FASB ASC 958, ASP is required to report information regarding its financial position and activities according to three classes of net assets: unrestricted net assets, temporarily restricted net assets, and permanently restricted net assets.

ASP reports gifts of cash and other assets as temporarily restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of activities as net assets released from restrictions. All temporarily restricted contributions in which the restrictions are met in the same reporting period as the donation are reported as unrestricted.

ASP reports gifts of land, building and equipment as unrestricted support unless explicit donor stipulations specify how the donated assets must be used. Gifts of cash or other assets that must be used to acquire long-lived assets are reported as restricted support. Absent explicit donor stipulations about how long these long-lived assets must be maintained, ASP reports expirations of donor restrictions when the donated or acquired long-lived assets are placed in service.

ASP reports gifts of land, building and equipment as permanently restricted support if they are received with donor stipulations that do not expire with the passage of time and cannot be removed or fulfilled by organization actions. Permanently restricted contributions must be maintained by ASP in perpetuity.

Reclassifications

Certain reclassifications have been made to the prior years' financial statements to conform to the current year presentation. These reclassifications had no effect on previously reported results of operations or net assets.

(Continued)

APPALACHIA SERVICE PROJECT, INC.

NOTES TO FINANCIAL STATEMENTS

December 31, 2011

Note 1. Significant Accounting Policies (Continued)

Cash and Cash Equivalents

ASP considers all highly liquid investments with an original maturity of three months or less to be cash equivalents.

Funds kept in regular checking and savings accounts are secured by the Federal Deposit Insurance Corporation (FDIC). At times, these funds may be in excess of the FDIC insurance limit. ASP has not experienced any losses in such accounts.

ASP also maintains funds in registered money market funds covered by fidelity bonds and held by custodian banks.

The ASP Board of Directors has designated a cash reserve for the purpose of meeting the Organization's cash flow needs. At the end of each calendar year, this Board designation requires a cash reserve of no less than \$1,000,000, not including any cash balance in the Revolving Loan Fund, to be maintained in the General Fund. At December 31, 2011, the Organization was in compliance with the Board designated reserve.

Mortgages Receivable

Mortgages receivable are reported at their outstanding unpaid principal balances adjusted by an allowance for loan losses. ASP maintains an allowance for loan losses to absorb an estimate of losses inherent in the receivables. The allowance is reviewed periodically by management to provide assurance that an appropriate level of loan loss reserve is maintained. The allowance for loan losses is maintained at an amount management deems adequate to cover inherent losses at the balance sheet date. The Organization considers a loan to be impaired when, based upon current information and events, it believes it is probable that the Organization will be unable to collect all amounts due according to the contractual terms of the loan agreement. If an impaired loan is forgiven, loss of principal, if any, is recorded through a charge-off to the appropriate expense account.

Inventories

Inventories of resale items and purchased building materials are valued at cost. Small tools and building materials, which are donated, are valued at flea market value.

Property and Equipment

Property and equipment are capitalized at cost for purchases and at fair market value for donated items. Depreciation is computed on a straight-line basis over the estimated service lives of the assets. ASP follows the practice of capitalizing, at cost, all expenses for fixed assets in excess of \$400. Estimated useful lives are as follows:

Vehicles	3 years
Equipment	5-10 years
Furniture and fixtures	10 years
Buildings	30-39 years

Small tools and other materials are included in inventory and are not depreciated.

(Continued)

APPALACHIA SERVICE PROJECT, INC.

NOTES TO FINANCIAL STATEMENTS

December 31, 2011

Note 1. Significant Accounting Policies (Continued)

Compensated Absences

Vacation days are accrued at a rate of .83 days for the first two years of employment, 1.25 days for years 3 through 7, and 1.67 days beginning in the 8th year, for each month worked, based on the employee's anniversary date. Employees are encouraged to use their vacation time in the calendar year in which it is earned. A maximum of five days of vacation may be carried over into the first quarter of the following year. If the vacation time earned is not taken by the end of the first quarter, it is forfeited. However, ASP is liable for the amount of unused vacation time, up to the maximum allowed, for each employee as of December 31, 2011. ASP does not provide for any payment of unused sick days.

Allocation of Expenses

ASP's expenses are presented on a functional basis, showing basic program activities and support services. ASP allocates expenses to home repair and building, office and administration, and fundraising based on the organizational cost centers in which expenses are incurred. Expenses are allocated between support and program services based upon specific identification, or a defined allocation method.

Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Actual results could vary from the estimates that were used.

Deferred Revenue

Income from prepaid summer program registration fees, prepaid summer volunteer fees and conditional donations received for which the conditions have not been met is deferred and recognized in the period to which the fees and donations relate. Also, federal grant funds received but not expended are deferred and recognized in the period the grant expenditures are made.

Income Tax Status

ASP is exempt from federal income tax under Section 501(c)(3) of the Internal Revenue Code.

ASP adopted the provisions of ASC Topic 740, *Income Taxes*, relating to unrecognized tax benefits on January 1, 2009. ASP files income tax returns in the U.S. federal jurisdiction. ASP's income tax filings are subject to audit by various taxing authorities. ASP's open audit periods are 2008-2011.

Note 2. Contributed Services

A substantial number of unpaid volunteers make significant contributions of their time to work in ASP's programs. Although these services are necessary to the program, they are for the most part, not provided by volunteers with specialized skills. In addition, they probably would not be purchased if they were not donated as required by FASB ASC 958-605 Revenue Recognition to be recognized in the financial statements. Accordingly, the value of this labor has not been recorded in the financial statements. Management estimates the value of these services at \$11,475,660 and \$10,866,366 for 2011 and 2010, respectively.

APPALACHIA SERVICE PROJECT, INC.

NOTES TO FINANCIAL STATEMENTS

December 31, 2011

Note 3. Investments

Endowment investments at December 31 included the following:

	<u>2011</u>			
	<u>Cost</u>	<u>Unrealized Gains</u>	<u>Unrealized Losses</u>	<u>Fair Value</u>
Mutual funds	<u>\$ 241,161</u>	<u>\$ -</u>	<u>\$ 11,622</u>	<u>\$ 229,539</u>
	<u>2010</u>			
	<u>Cost</u>	<u>Unrealized Gains</u>	<u>Unrealized Losses</u>	<u>Fair Value</u>
Mutual funds	<u>\$ 241,161</u>	<u>\$ -</u>	<u>\$ 10,884</u>	<u>\$ 230,277</u>

Investment expenses netted against investment income in the statement of activities were \$1,871 for the year ended December 31, 2011.

Note 4. Mortgages Receivable

ASP issues non-interest and low-interest loans for construction and remodeling of homes. The mortgages result primarily from funds received from Federal and State programs. These funds have a predetermined interest rate set by the grantor agencies. For this reason, no imputed interest has been calculated.

Mortgages receivable, net totaled \$70,854 and \$75,962 at December 31, 2011 and 2010, respectively. Due to the inherent uncertainties associated with the collectability of the loans, the value of the underlying collateral, and the reputational risk associated with foreclosure, mortgages receivable, net are recorded at an amount that management believes approximates net realizable value as stated below.

	<u>2011</u>	<u>2010</u>
Mortgages receivable	\$ 349,057	\$ 374,876
Less: Allowance for loan losses	<u>(278,203)</u>	<u>(298,914)</u>
Mortgages receivable, net	70,854	75,962
Less: Mortgages receivable, current	<u>5,845</u>	<u>7,596</u>
Mortgages receivable, long-term	<u>\$ 65,009</u>	<u>\$ 68,366</u>

Note 5. Endowment

ASP's endowment funds consist of contributions received from individuals to provide the opportunity to make charitable gifts to ASP. As required by GAAP, net assets associated with endowment funds are classified and reported based on the existence or absence of donor-imposed restrictions.

(Continued)

APPALACHIA SERVICE PROJECT, INC.

NOTES TO FINANCIAL STATEMENTS

December 31, 2011

Note 5. Endowment (Continued)

Interpretation of Relevant Law

ASP's Board of Trustees has segregated a portion of unrestricted net assets as a board designated endowment to be invested to provide income for an unspecified period. The board designated endowment is classified as unrestricted net assets.

Endowment Net Asset Composition by Type of Fund
as of December 31, 2011

	<u>Unrestricted</u>	Temporarily <u>Restricted</u>	Permanently <u>Restricted</u>	<u>Total</u>
Board designated endowment funds	\$ 391,702	\$ -	\$ -	\$ 391,702

Endowment Net Asset Composition by Type of Fund
as of December 31, 2010

	<u>Unrestricted</u>	Temporarily <u>Restricted</u>	Permanently <u>Restricted</u>	<u>Total</u>
Board designated endowment funds	\$ 370,640	\$ -	\$ -	\$ 370,640

Changes in Endowment Net Assets
for the Fiscal Year Ended December 31, 2011

	<u>Unrestricted</u>	Temporarily <u>Restricted</u>	Permanently <u>Restricted</u>	<u>Total</u>
Endowment net assets, beginning of year	\$ 370,640	\$ -	\$ -	\$ 370,640
Investment return:				
Investment dividend income	4,319	-	-	4,319
Net depreciation (realized and unrealized)	<u>(5,057)</u>	<u>-</u>	<u>-</u>	<u>(5,057)</u>
Total investment loss	(738)	-	-	(738)
Contributions	21,800	-	-	21,800
Appropriation of endowment assets for expenditure	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
Endowment net assets, end of year	<u>\$ 391,702</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 391,702</u>

(Continued)

APPALACHIA SERVICE PROJECT, INC.

NOTES TO FINANCIAL STATEMENTS

December 31, 2011

Note 5. Endowment (Continued)

Changes in Endowment Net Assets
for the Fiscal Year Ended December 31, 2010

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Endowment net assets, beginning of year	\$ 266,920	\$ -	\$ -	\$ 266,920
Investment return:				
Investment dividend income	3,455	-	-	3,455
Net appreciation (realized and unrealized)	<u>19,465</u>	<u>-</u>	<u>-</u>	<u>19,465</u>
Total investment return	22,920	-	-	22,920
Contributions	80,800	-	-	80,800
Appropriation of endowment assets for expenditure	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
Endowment net assets, end of year	<u>\$ 370,640</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 370,640</u>

Description of Amounts Classified as Permanently Restricted Net Assets
Temporarily Restricted Net Assets and Unrestricted Net Assets

	<u>December 31, 2011</u>	<u>December 31, 2010</u>
<u>Unrestricted Net Assets</u>		
Board designated endowment funds	\$391,702	\$370,640

Return Objectives and Risk Parameters

ASP has adopted investment and spending policies for endowment assets that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of the endowment assets. Under this policy, as approved by the Board of Trustees, the endowment assets are invested in a manner that is intended to produce results while assuming a moderate level of investment risk. ASP expects its endowment funds, over time, to provide an average rate of return that is above the combined rate of inflation and spending rate of ASP. Actual returns in any given year may vary from this amount.

Strategies Employed for Achieving Objectives

To satisfy its long-term rate-of-return objectives, ASP relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yield (interest and dividends). ASP targets a diversified asset allocation that places a greater emphasis on equity-based investments to achieve its long-term return objectives within prudent risk constraints.

Spending Policy and How the Investment Objectives Relate to the Spending Policy

ASP has a policy of appropriating distributions only after the endowment exceeds \$500,000. Once the endowment achieves this minimum threshold, the maximum annual distribution permitted is five percent of the average of the previous three years fair market value at December 31. In establishing this policy, the Organization considered the long-term expected return on its endowment. This is consistent with the Organization's objective to maintain the purchasing power of the endowment assets held.

APPALACHIA SERVICE PROJECT, INC.

NOTES TO FINANCIAL STATEMENTS

December 31, 2011

Note 6. Inventories

Inventories consist of the following:

	<u>2011</u>	<u>2010</u>
Resale items	\$ 53,908	\$ 57,980
Small Tools	<u>78,401</u>	<u>42,616</u>
	<u>\$ 132,309</u>	<u>\$ 100,596</u>

Note 7. Property and Equipment

Property and equipment consists of the following:

	<u>2011</u>	<u>2010</u>
Vehicles	\$ 1,611,472	\$ 1,448,906
Buildings	2,162,953	2,162,953
Furniture and fixtures	25,230	26,122
Land	106,205	106,205
Equipment	<u>359,143</u>	<u>427,850</u>
	4,265,003	4,172,036
Less: accumulated depreciation	<u>(2,444,196)</u>	<u>(2,299,520)</u>
	<u>\$ 1,820,807</u>	<u>\$ 1,872,516</u>

Note 8. Notes Payable

Notes payable consist of the following:

	<u>2011</u>	<u>2010</u>
Note payable to Kentucky Housing Corporation. Annual payments of \$1,125, including interest at 1.00%. Unpaid principal is due July, 2013. Unsecured.	\$ 2,250	\$ 3,375
Note payable to Kentucky Housing Corporation. Annual payments of \$1,395, including interest at 1.00%. Unpaid principal is due December 31, 2030. Unsecured.	27,544	27,544
Notes payable to FAHE. Annual payments and quarterly interest payments to be determined by FAHE. Interest at 1.00%. Unpaid principal is due July, 2021. Unsecured.	<u>42,261</u>	<u>46,740</u>
Total notes payable	72,055	77,659
Less current maturities	<u>7,055</u>	<u>6,965</u>
Long-term debt	<u>\$ 65,000</u>	<u>\$ 70,694</u>

(Continued)

APPALACHIA SERVICE PROJECT, INC.

NOTES TO FINANCIAL STATEMENTS

December 31, 2011

Note 8. Notes Payable (Continued)

Estimated maturities of notes payable are as follows:

2012	\$ 7,055
2013	7,100
2014	6,021
2015	6,068
2016	6,115
Thereafter	<u>39,696</u>
	<u>\$ 72,055</u>

See **Note 16** for additional information.

Note 9. Lines of Credit

The Organization has the following lines of credit:

Line of credit agreement up to \$450,000 with SunTrust Bank through March 2013. Interest at the bank's prime rate plus 1% (4.25% at December 31, 2011 and 2010). Secured by property.

First Tennessee Bank, up to \$50,000, interest at 1% above the Bank's base commercial rate (4.25% at December 31, 2011 and 2010) through August 2012. This line of credit is unsecured.

Federation of Appalachian Housing Enterprises, up to \$150,000, interest at LIBOR plus 2.0% (2.80% at December 31, 2011 and 2010) through December 2012. This line of credit is unsecured.

All credit lines were unused at December 31, 2011 and 2010.

Note 10. Capital Lease

ASP has a capital lease for certain office equipment with a term of 69 months and an interest rate of 10.00% per annum. Property and equipment include the following amounts for capital leases:

	<u>2011</u>	<u>2010</u>
Equipment cost	\$ 81,400	\$ 81,400
Less: Allowance for depreciation	<u>56,980</u>	<u>40,700</u>
	<u>\$ 24,420</u>	<u>\$ 40,700</u>

Future minimum lease payments under this capital lease, including the present value of minimum lease payments, are as follows:

2012	\$ 18,672
2013	15,559
Total minimum lease payments	<u>34,231</u>
Less: amount representing interest	<u>1,787</u>
Total	32,444
Less: current installments	<u>17,574</u>
Long-term obligation	<u>\$ 14,870</u>

APPALACHIA SERVICE PROJECT, INC.

NOTES TO FINANCIAL STATEMENTS

December 31, 2011

Note 11. Restricted Net Assets

Temporarily restricted net assets and restricted cash are available for the following purposes:

	<u>2011</u>	<u>2010</u>
Collegiate Weekend fund	\$ 5,992	\$ 8,273
Purchase of vehicles	3,776	2,352
Front Porch fund	<u>660</u>	<u>335</u>
	<u>\$ 10,428</u>	<u>\$ 10,960</u>

Note 12. Fair Value of Financial Instruments

Financial Accounting Standards Board Accounting Standards Codification 820-10, *Fair Value Measurements*, establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. This hierarchy consists of three broad levels: Level 1 inputs consist of quoted prices in active markets for identical investments and have the highest priority, Level 2 inputs consist of observable inputs other than quoted prices for identical assets, and Level 3 inputs consist of unobservable inputs where there is little or no market activity. Level 3 inputs have the lowest priority.

The following are the major categories of investments measured at fair value on a recurring basis during the year ended December 31, 2011, using quoted prices in active markets for identical assets (Level 1) and significant other observable inputs (Level 2). For these investments, for which there are no quoted market prices available, a reasonable estimate of fair value was based on quoted prices for similar investments in active markets. The Organization had no Level 3 valuations at December 31, 2011.

Description	Level 2: Significant Other Observable Inputs	
	<u>2011</u>	<u>2010</u>
Mutual funds	<u>\$ 229,539</u>	<u>\$ 230,277</u>

Note 13. Pension Plan

ASP permits employees to contribute to a tax-deferred annuity program for the purchase of an annuity contract or the establishment of a custodial account as described by Internal Revenue Code Section 403(b). ASP matches the employee's contribution up to a maximum of 6% of the employee's salary. Matching funds totaled \$51,005 and \$42,160 for 2011 and 2010, respectively.

Note 14. Supplemental Cash Flow Information

During 2011 and 2010, ASP recorded the following non-cash operating and financing transactions:

In-kind donations of \$44,786 and \$68,585 in materials and \$5,500 and \$2,500 in vehicles, respectively, are recorded as support in the statement of activities.

In 2011, the Organization sold two vehicles to employees. The selling price of \$33,000 was financed through notes receivable.

APPALACHIA SERVICE PROJECT, INC.

NOTES TO FINANCIAL STATEMENTS

December 31, 2011

Note 15. Commitments and Contingencies

ASP has entered into a contractual agreement with Russ Reid Company to provide fundraising services for 2010 and 2011. Minimum monthly costs under the contract total \$8,000. The costs associated with this contract are dependent on the services performed. The contractual agreement was terminated January 31, 2011. Expenses resulting from this contractual agreement totaled \$8,000 and \$131,488 in 2011 and 2010, respectively.

As of December 31, 2011 and 2010, ASP is contingently liable as guarantor with respect to \$124,743 and \$134,459 of indebtedness for certain recipients of federal monies received for the purpose of home repair or construction. No material loss is anticipated by reason of such guarantee.

The ASP endowment program invests in various investment securities. Investment securities are exposed to various risks such as interest rate, market, and credit risks. Due to the level of risk associated with certain investment securities, it is at least reasonably possible that changes in the value of investment securities will occur in the near term and that such changes could materially affect account balances and the amounts reported in financial statements.

Note 16. Subsequent Events

In accordance with ASC 855, the Company evaluated subsequent events through May 7, 2012, the issue date of the financial statements. With the exception of those matters discussed below, there were no material subsequent events that required recognition or additional disclosures in these financial statements.

Lease Agreement

In January 2012, the Organization entered into a lease agreement for a certain parcel of commercial real estate located in Harlan County, Kentucky. The term of the lease is for ten years with payments totaling \$50,000. The entire amount of the lease payments were required to be paid in advance under the lease agreement.

Long-Term Debt

In February, 2012, the Organization satisfied all outstanding notes payable to the Kentucky Housing Corporation and the Federation of Appalachian Housing Enterprises, Inc. The loans outstanding totaled \$72,055 at December 31, 2011.

OTHER INFORMATION

APPLACHIAN SERVICE PROJECT, INC.

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
For the Year Ended December 31, 2011

<u>Federal Grantor Program Title</u>	<u>Federal CFDA Number</u>	<u>Federal Expenditures</u>
<u>U.S. Department of Housing and Urban Development:</u>		
Economic Development Initiative - Special Projects Grant B-09-SP-TN-0013	14.251	\$ 220,210
Economic Development Initiative - Special Projects Grant B-10-SP-KY-0016	14.251	225,755
Economic Development Initiative - Special Projects Grant B-10-SP-WV-0015	14.251	<u>115,039</u>
Grant Total		561,004
<u>Corporation for National and Community Service:</u>		
AmeriCorps National	94.006	<u>26,956</u>
Total Expenditures of Federal Awards		<u>\$ 587,960</u>

Note 1. Basis of Accounting

This schedule was prepared on the accrual 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.

INTERNAL CONTROL AND COMPLIANCE



**INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER
FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON
AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH
GOVERNMENT AUDITING STANDARDS**

To the Board of Directors
Appalachia Service Project, Inc.
Johnson City, Tennessee

We have audited the financial statements of Appalachia Service Project, Inc. ("ASP"), as of and for the year ended December 31, 2011, and have issued our report thereon dated May 7, 2012. 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 ASP'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 ASP's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of ASP'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 entity's 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.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether ASP'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 or other matters that are required to be reported under *Government Auditing Standards*.

We noted certain matters that we reported to management of ASP, in a separate letter dated May 7, 2012.

This report is intended solely for the information and use of ASP's management, the Board of Directors, others within the entity, and federal awarding agencies and is not intended to be and should not be used by anyone other than these specified parties.

Brown, Edwards & Company, S. L. P.
CERTIFIED PUBLIC ACCOUNTANTS

Bristol, Virginia
May 7, 2012

Your Success is Our Focus



**INDEPENDENT AUDITOR'S 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
Appalachia Service Project, Inc.
Johnson City, Tennessee

Compliance

We have audited Appalachia Service Project, Inc.'s ("ASP"), compliance with the types of compliance requirements described in the *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 December 31, 2011. ASP's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of ASP's management. Our responsibility is to express an opinion on ASP'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 ASP'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 ASP's compliance with those requirements.

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

Internal Control Over Compliance

Management of ASP 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 ASP's internal control over compliance with the 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 ASP's internal control over compliance.

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.

Your Success is Our Focus

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 solely for the information and use of ASP's management, the Board of Directors, others within the entity, and federal awarding agencies and is not intended to be and should not be used by anyone other than these specified parties.

Brown, Edwards & Company, L.L.P.

CERTIFIED PUBLIC ACCOUNTANTS

Bristol, Virginia
May 7, 2012

APPALACHIA SERVICE PROJECT
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
Year Ended December 31, 2011

A. SUMMARY OF AUDIT RESULTS

1. The auditor's report expresses an **unqualified opinion** on the financial statements of Appalachia Service Project, Inc. ("ASP").
2. **No significant deficiencies** relating to the audit of the financial statements are reported in the Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*.
3. **No instances of noncompliance** material to the financial statements of ASP, which would be required to be reported in accordance with *Government Auditing Standards*, were disclosed during the audit.
4. **No significant deficiencies** relating to the audit of the major federal award programs are reported in the 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*.
5. The auditor's report on compliance for the major federal award programs expresses an **unqualified opinion** on all major federal programs.
6. The audit disclosed **no audit findings** relating to major programs required to be reported in accordance with *Section 510(a) of OMB Circular A-133*.
7. The programs tested as major programs include:

<u>Name of Program:</u>	<u>CFDA #</u>
Economic Development Initiative – Special Projects Grant	14.251
8. The **threshold** for distinguishing Type A and B programs was \$300,000.
9. Appalachia Service Project, Inc. was **not** determined to be a **low-risk auditee**.

B. FINDINGS – FINANCIAL STATEMENT AUDIT

None.

C. FINDINGS AND QUESTIONED COSTS—MAJOR FEDERAL AWARD PROGRAMS AUDIT

None.

APPALACHIA SERVICE PROJECT
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
Year Ended June 30, 2010

2010-1 Department of Housing and Urban Development: Economic Development Initiative – Special Projects Grant – CFDA No. 14.251

Condition: Financial Status and Performance Report was not filed timely.

Criteria: A financial status and performance report is required to be filed every six months from the effective date of the grant agreement.

Cause: The deadlines for filing the reports were missed.

Current Status: Finding was not noted in current year.