

**APPALACHIA SERVICE PROJECT, INC.**

**FINANCIAL REPORT**

**December 31, 2012**

APPALACHIA SERVICE PROJECT, INC.

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## INDEPENDENT AUDITOR'S REPORT

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

### Report on the Financial Statements

We have audited the accompanying financial statements of Appalachia Service Project, Inc., (a nonprofit organization), which comprise the statements of financial position as of December 31, 2012 and 2011, and the related statements of activities, functional expenses, and cash flows for the years then ended, and the related notes to the financial statements.

### Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

### Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. 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. 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 involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Appalachian Service Project, Inc. as of December 31, 2012 and 2011, and the changes in its nets assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

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**Other Reporting Required by *Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated May 22, 2013, on our consideration of Appalachian 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 internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Appalachian Service Project, Inc.'s internal control over financial reporting and compliance.

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

CERTIFIED PUBLIC ACCOUNTANTS

Bristol, Virginia  
May 22, 2013

# FINANCIAL STATEMENTS

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APPALACHIA SERVICE PROJECT, INC.

STATEMENTS OF FINANCIAL POSITION

December 31, 2012 and 2011

| ASSETS  |    | 2012      | 2011         |
|---|----|-----------|--------------|
| CURRENT ASSETS  |    |           |              |
| Cash and cash equivalents:                            |    |           |              |
| Undesignated  | \$ | 1,147,956 | \$ 519,047   |
| Board designated - Operating reserve                  |    | 1,230,000 | 1,230,000    |
| Board designated - Revolving loan fund                |    | 32,083    | 428,951      |
| Board designated - Endowment (Note 5)                 |    | 44,510    | 162,163      |
| Unrestricted cash                                     |    | 2,454,549 | 2,340,161    |
| Board designated endowment fund (Notes 3, 5 and 12)   |    | 521,555   | 229,539      |
| Grant receivable                                      |    | 250,786   | 561,004      |
| Project income receivable                             |    | 195,534   | -            |
| Other receivables                                     |    | 2,101     | 2,139        |
| Employee notes receivable (due within one year)       |    | 8,450     | 8,450        |
| Mortgages receivable current, net (Note 4)            |    | 5,490     | 5,845        |
| Current prepaid expenses                              |    | 13,010    | 8,010        |
| Inventories (Note 6)                                  |    | 167,666   | 132,309      |
| Total current assets                                  |    | 3,619,141 | 3,287,457    |
| NONCURRENT ASSETS                                     |    |           |              |
| Restricted cash (Note 11)                             |    | 8,963     | 10,428       |
| Property and equipment, net (Note 7)                  |    | 1,852,185 | 1,820,807    |
| Employee notes receivable (due after one year)        |    | 6,825     | 16,400       |
| Long-term mortgages receivable, net (Note 4)          |    | 61,055    | 65,009       |
| Long-term prepaid expenses                            |    | 35,000    | -            |
| Total noncurrent assets                               |    | 1,964,028 | 1,912,644    |
|   | \$ | 5,583,169 | \$ 5,200,101 |
| LIABILITIES AND NET ASSETS                            |    |           |              |
| CURRENT LIABILITIES                                   |    |           |              |
| Accounts payable and accrued expenses                 | \$ | 178,811   | \$ 137,316   |
| Current maturities of notes payable (Note 8)          |    | -         | 7,055        |
| Current portion of capital lease obligation (Note 10) |    | 16,290    | 17,574       |
| Deferred revenue                                      |    | 617,191   | 560,755      |
| Total current liabilities                             |    | 812,292   | 722,700      |
| LONG-TERM LIABILITIES (net of Current Portion)        |    |           |              |
| Notes payable (Note 8)                                |    | -         | 65,000       |
| Capital lease obligation (Note 10)                    |    | -         | 14,870       |
| Total long-term liabilities                           |    | -         | 79,870       |
| Total liabilities                                     |    | 812,292   | 802,570      |
| NET ASSETS (Note 11)                                  |    |           |              |
| Unrestricted  |    | 4,761,914 | 4,387,103    |
| Temporarily restricted                                |    | 8,963     | 10,428       |
| Total net assets                                      |    | 4,770,877 | 4,397,531    |
|   | \$ | 5,583,169 | \$ 5,200,101 |

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, 2012 and 2011

|   | 2012                | 2011                |
|---|---------------------|---------------------|
| UNRESTRICTED NET ASSETS   |                     |                     |
| Revenues  |                     |                     |
| Donations   | \$ 2,212,834        | \$ 1,804,637        |
| Grants  | 250,786             | 1,161,004           |
| Volunteer work crews fees   | 4,982,453           | 4,614,646           |
| Project income  | 195,534             | -                   |
| Donated items   | 22,434              | 50,286              |
| Merchandise sales   | 158,222             | 169,793             |
| Interest and investment income  | 36,379              | 3,323               |
| Gain on sale of assets  | 11,996              | 11,732              |
| Miscellaneous   | 74,588              | 122,377             |
| Total unrestricted revenues   | <u>7,945,226</u>    | <u>7,937,798</u>    |
| NET ASSETS RELEASED FROM RESTRICTIONS                                 |                     |                     |
| Satisfaction of purpose restrictions                                  | <u>1,905</u>        | <u>532</u>          |
| Total unrestricted revenues and net assets released from restrictions | <u>7,947,131</u>    | <u>7,938,330</u>    |
| Expenses  |                     |                     |
| Program services  | <u>6,516,016</u>    | <u>6,227,496</u>    |
| Supporting services   |                     |                     |
| Office and administration   | 426,278             | 392,364             |
| Fundraising   | <u>630,026</u>      | <u>742,119</u>      |
| Total supporting services   | <u>1,056,304</u>    | <u>1,134,483</u>    |
| Total expenses  | <u>7,572,320</u>    | <u>7,361,979</u>    |
| Change in unrestricted net assets                                     | <u>374,811</u>      | <u>576,351</u>      |
| Balance, beginning  | <u>4,387,103</u>    | <u>3,810,752</u>    |
| Balance, ending   | <u>\$ 4,761,914</u> | <u>\$ 4,387,103</u> |

(Continued)

APPALACHIA SERVICE PROJECT, INC.

STATEMENTS OF ACTIVITIES  
For the Years Ended December 31, 2012 and 2011

|   | <u>2012</u>         | <u>2011</u>         |
|---|---------------------|---------------------|
| TEMPORARILY RESTRICTED NET ASSETS           |                     |                     |
| Contributions                               | \$ 440              | \$ -                |
| Net assets released from restrictions       | <u>(1,905)</u>      | <u>(532)</u>        |
| Change in temporarily restricted net assets | (1,465)             | (532)               |
| Balance, beginning                          | <u>10,428</u>       | <u>10,960</u>       |
| Balance, ending                             | <u>\$ 8,963</u>     | <u>\$ 10,428</u>    |
| SUMMARY OF CHANGES IN NET ASSETS            |                     |                     |
| Change in total net assets                  | \$ 373,346          | \$ 575,819          |
| Balance, beginning                          | <u>4,397,531</u>    | <u>3,821,712</u>    |
| Balance, ending                             | <u>\$ 4,770,877</u> | <u>\$ 4,397,531</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, 2012 and 2011

|                                     | Program<br>Services         | Supporting<br>Services       |                   |                     |                     |
|-------------------------------------|-----------------------------|------------------------------|-------------------|---------------------|---------------------|
|                                     | Home Repair<br>and Building | Office and<br>Administration | Fundraising       | 2012                | 2011                |
| Salaries and related taxes          | \$ 1,981,562                | \$ 224,954                   | \$ 135,629        | \$ 2,342,145        | \$ 2,282,110        |
| Employee benefits                   | <u>475,577</u>              | <u>68,696</u>                | <u>25,373</u>     | <u>569,646</u>      | <u>503,143</u>      |
| Total salaries and related expenses | 2,457,139                   | 293,650                      | 161,002           | 2,911,791           | 2,785,253           |
| Staff expenses                      | 86,417                      | 12,011                       | 16,355            | 114,783             | 142,219             |
| Group expenses                      | 618,876                     | -                            | -                 | 618,876             | 569,515             |
| Repair/rehabilitation/construction  | 2,019,187                   | -                            | -                 | 2,019,187           | 1,876,617           |
| Transportation/maintenance          | 138,129                     | 3,686                        | 11,718            | 153,533             | 128,858             |
| Publications                        | 47,331                      | -                            | 311,194           | 358,525             | 436,202             |
| Office expenses                     | 415,443                     | 39,131                       | 16,798            | 471,372             | 447,508             |
| Program expenses                    | 366,507                     | 3,680                        | 102,999           | 473,186             | 500,177             |
| Taxes, licenses and fees            | 46,997                      | 14,572                       | 3,154             | 64,723              | 55,463              |
| Ranch and warehouse                 | 8,020                       | -                            | -                 | 8,020               | 11,802              |
| Professional fees                   | 30,193                      | 53,528                       | 4,800             | 88,521              | 107,755             |
| Miscellaneous                       | <u>2</u>                    | <u>-</u>                     | <u>-</u>          | <u>2</u>            | <u>279</u>          |
| Total expenses before depreciation  | 6,234,241                   | 420,258                      | 628,020           | 7,282,519           | 7,061,648           |
| Depreciation                        | <u>281,775</u>              | <u>6,020</u>                 | <u>2,006</u>      | <u>289,801</u>      | <u>300,331</u>      |
| Total expenses                      | <u>\$ 6,516,016</u>         | <u>\$ 426,278</u>            | <u>\$ 630,026</u> | <u>\$ 7,572,320</u> | <u>\$ 7,361,979</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, 2012 and 2011

|   | 2012                | 2011                |
|---|---------------------|---------------------|
| CASH FLOWS FROM OPERATING ACTIVITIES  |                     |                     |
| Change in total net assets  | \$ 373,346          | \$ 575,819          |
| Adjustments to reconcile change in total net assets to net cash provided by operating activities: |                     |                     |
| Depreciation  | 289,801             | 300,331             |
| Gain on sale of assets  | (11,996)            | (11,732)            |
| In-kind donations   | (22,434)            | (50,286)            |
| Loss (gain) on investments  | (25,127)            | 5,057               |
| Loans forgiven  | 49,741              | -                   |
| Allowance for loan losses   | (68,807)            | (20,711)            |
| (Increase) decrease in:   |                     |                     |
| Grant receivables   | 310,218             | 57,872              |
| Project income receivable   | (195,534)           | -                   |
| Mortgages receivable  | 23,375              | 25,819              |
| Other receivables   | 38                  | 670                 |
| Prepaid expenses  | (40,000)            | -                   |
| Inventories   | (12,923)            | 13,073              |
| Increase (decrease) in:   |                     |                     |
| Accounts payable and accrued expenses   | 41,495              | 30,181              |
| Deferred revenue  | 56,436              | 497,471             |
| Net cash provided by operating activities   | <u>767,629</u>      | <u>1,423,564</u>    |
| CASH FLOWS FROM INVESTING ACTIVITIES  |                     |                     |
| Purchase of property and equipment  | (322,498)           | (279,290)           |
| Proceeds from sale of equipment   | 13,315              | 14,900              |
| Payments received on employee receivables   | 9,575               | 8,150               |
| Purchase of investments   | (258,955)           | -                   |
| Endowment dividends reinvested  | <u>(7,934)</u>      | <u>(4,319)</u>      |
| Net cash used in investing activities   | <u>(566,497)</u>    | <u>(260,559)</u>    |
| CASH FLOWS FROM FINANCING ACTIVITIES  |                     |                     |
| Payments on lease   | (16,154)            | (14,624)            |
| Principal payments on notes payable   | <u>(72,055)</u>     | <u>(5,604)</u>      |
| Net cash used in financing activities   | <u>(88,209)</u>     | <u>(20,228)</u>     |
| INCREASE IN CASH  | 112,923             | 1,142,777           |
| CASH, beginning   | <u>2,350,589</u>    | <u>1,207,812</u>    |
| CASH, ending  | <u>\$ 2,463,512</u> | <u>\$ 2,350,589</u> |
| RECONCILIATION OF CASH TO STATEMENT OF FINANCIAL POSITION   |                     |                     |
| Cash and cash equivalents, unrestricted   | \$ 2,454,549        | \$ 2,340,161        |
| Cash and cash equivalents, restricted   | <u>8,963</u>        | <u>10,428</u>       |
|   | <u>\$ 2,463,512</u> | <u>\$ 2,350,589</u> |
| SUPPLEMENTAL INFORMATION  |                     |                     |
| Interest paid   | <u>\$ 5,719</u>     | <u>\$ 10,195</u>    |

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

APPALACHIA SERVICE PROJECT, INC.

NOTES TO FINANCIAL STATEMENTS

December 31, 2012

**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, 2012

**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 \$1,230,000, not including any cash balance in the Revolving Loan Fund, to be maintained in the General Fund. At December 31, 2012 and 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, 2012

**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 8<sup>th</sup> 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, 2012. 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.

FASB ASC 740-10, *Accounting for Uncertainty in Income Taxes*, clarifies the accounting and recognition for income tax positions taken or expected to be taken in ASP's income tax returns. ASP files income tax returns in the U.S. federal jurisdiction. APS's income tax filings are subject to audit by various taxing authorities. ASP's open audit periods are 2009-2012.

**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 \$11,690,662 and \$11,475,660 for 2012 and 2011, respectively.

APPALACHIA SERVICE PROJECT, INC.

NOTES TO FINANCIAL STATEMENTS

December 31, 2012

**Note 3. Investments**

Endowment investments at December 31 included the following:

|              | 2012              |                  |                   |
|--------------|-------------------|------------------|-------------------|
|              | Cost              | Unrealized Gains | Unrealized Losses |
| Mutual funds | <u>\$ 500,116</u> | <u>\$ 21,439</u> | <u>\$ -</u>       |
|              |                   |                  | <u>\$ 521,555</u> |
|              | 2011              |                  |                   |
|              | Cost              | Unrealized Gains | Unrealized Losses |
| Mutual funds | <u>\$ 241,161</u> | <u>\$ -</u>      | <u>\$ 11,622</u>  |
|              |                   |                  | <u>\$ 229,539</u> |

Investment expenses netted against investment income in the statement of activities were \$3,346 for the year ended December 31, 2012.

**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 \$66,545 and \$70,854 at December 31, 2012 and 2011, 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.

|                                     | 2012             | 2011             |
|-------------------------------------|------------------|------------------|
| Mortgages receivable                | \$ 275,941       | \$ 349,057       |
| Less: Allowance for loan losses     | <u>(209,396)</u> | <u>(278,203)</u> |
| Mortgages receivable, net           | 66,545           | 70,854           |
| Less: Mortgages receivable, current | <u>5,490</u>     | <u>5,845</u>     |
| Mortgages receivable, long-term     | <u>\$ 61,055</u> | <u>\$ 65,009</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, 2012

**Note 5. Endowment (Continued)**

Interpretation of Relevant Law

ASP's Board of Directors 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, 2012

|                                  | Unrestricted | Temporarily<br>Restricted | Permanently<br>Restricted | Total      |
|----------------------------------|--------------|---------------------------|---------------------------|------------|
| Board designated endowment funds | \$ 566,065   | \$ -                      | \$ -                      | \$ 566,065 |

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

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

Changes in Endowment Net Assets  
for the Fiscal Year Ended December 31, 2012

|  | Unrestricted      | Temporarily<br>Restricted | Permanently<br>Restricted | Total             |
|--|-------------------|---------------------------|---------------------------|-------------------|
| Endowment net assets, beginning of year              | \$ 391,702        | \$ -                      | \$ -                      | \$ 391,702        |
| Investment return:                                   |                   |                           |                           |                   |
| Investment dividend income                           | 7,934             | -                         | -                         | 7,934             |
| Net appreciation (realized and unrealized)           | 25,127            | -                         | -                         | 25,127            |
| Total investment return                              | 33,061            | -                         | -                         | 33,061            |
| Contributions  | 141,302           | -                         | -                         | 141,302           |
| Appropriation of endowment<br>assets for expenditure | -                 | -                         | -                         | -                 |
| Endowment net assets, end of year                    | <u>\$ 566,065</u> | <u>\$ -</u>               | <u>\$ -</u>               | <u>\$ 566,065</u> |

APPALACHIA SERVICE PROJECT, INC.

NOTES TO FINANCIAL STATEMENTS  
December 31, 2012

**Note 5. Endowment ( Continued)**

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

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

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

|                                  | December 31, 2012 | December 31, 2011 |
|----------------------------------|-------------------|-------------------|
| <u>Unrestricted Net Assets</u>   |                   |                   |
| Board designated endowment funds | \$566,065         | \$391,702         |

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, 2012

**Note 6. Inventories**

Inventories consist of the following:

|                               | <u>2012</u>       | <u>2011</u>       |
|-------------------------------|-------------------|-------------------|
| Resale items (includes homes) | \$ 97,109         | \$ 53,908         |
| Small Tools                   | <u>70,557</u>     | <u>78,401</u>     |
|                               | <u>\$ 167,666</u> | <u>\$ 132,309</u> |

**Note 7. Property and Equipment**

Property and equipment consists of the following:

|                                | <u>2012</u>         | <u>2011</u>         |
|--------------------------------|---------------------|---------------------|
| Vehicles                       | \$ 1,647,277        | \$ 1,611,472        |
| Buildings                      | 2,385,665           | 2,162,953           |
| Furniture and fixtures         | 25,230              | 25,230              |
| Land                           | 106,205             | 106,205             |
| Equipment                      | <u>362,829</u>      | <u>359,143</u>      |
|                                | 4,527,206           | 4,265,003           |
| Less: accumulated depreciation | <u>(2,675,021)</u>  | <u>(2,444,196)</u>  |
|                                | <u>\$ 1,852,185</u> | <u>\$ 1,820,807</u> |

**Note 8. Notes Payable**

Notes payable consist of the following:

|   | <u>2012</u> | <u>2011</u>      |
|---|-------------|------------------|
| Note payable to Kentucky Housing Corporation.<br>Annual payments of \$1,125, including interest<br>at 1.00%. Unpaid principal is due July, 2013.<br>Unsecured.              | \$ -        | \$ 2,250         |
| Note payable to Kentucky Housing Corporation.<br>Annual payments of \$1,395, including interest<br>at 1.00%. Unpaid principal is due<br>December 31, 2030. Unsecured.       | -           | 27,544           |
| Notes payable to FAHE. Annual payments and<br>quarterly interest payments to be determined by<br>FAHE. Interest at 1.00%. Unpaid principal is<br>due July, 2021. Unsecured. | <u>-</u>    | <u>42,261</u>    |
| Total notes payable   | -           | 72,055           |
| Less current maturities   | <u>-</u>    | <u>7,055</u>     |
| Long-term debt  | <u>\$ -</u> | <u>\$ 65,000</u> |

(Continued)

APPALACHIA SERVICE PROJECT, INC.

NOTES TO FINANCIAL STATEMENTS  
December 31, 2012

**Note 8. Notes Payable (Continued)**

During 2012, the Organization satisfied all outstanding notes payable to the Kentucky Housing Corporation and the Federation of Appalachian Housing Enterprises, Inc.

**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 September 2013. Interest at the bank's prime rate plus 1% (4.25% at December 31, 2012 and 2011). Secured by property.

First Tennessee Bank, up to \$50,000, interest at 1% above the Bank's base commercial rate (5.50% and 4.25% at December 31, 2012 and 2011, respectively) through August 2013. This line of credit is unsecured.

Federation of Appalachian Housing Enterprises, up to \$150,000, interest at LIBOR plus 4.75%, (5.06% as of December 31, 2012) and interest at LIBOR plus 2.0% (2.80% as of December 31, 2011) through June 2013. This line of credit is unsecured.

All credit lines were unused at December 31, 2012 and 2011.

**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>2012</u>     | <u>2011</u>      |
|----------------------------------|-----------------|------------------|
| Equipment cost                   | \$ 81,400       | \$ 81,400        |
| Less: Allowance for depreciation | <u>73,260</u>   | <u>56,980</u>    |
|                                  | <u>\$ 8,140</u> | <u>\$ 24,420</u> |

All remaining lease payments totaling \$17,021 are due in 2013. Of this amount, \$731 represents interest.

**Note 11. Restricted Net Assets**

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

|                         | <u>2012</u>     | <u>2011</u>      |
|-------------------------|-----------------|------------------|
| Collegiate Weekend fund | \$ 3,826        | \$ 5,992         |
| Purchase of vehicles    | 1,020           | 3,776            |
| Front Porch fund        | <u>4,117</u>    | <u>660</u>       |
|                         | <u>\$ 8,963</u> | <u>\$ 10,428</u> |

APPALACHIA SERVICE PROJECT, INC.

NOTES TO FINANCIAL STATEMENTS  
December 31, 2012

**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 years ended December 31, 2012 and 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, 2012 and 2011.

| Description  | Level 2:<br>Significant Other Observable<br>Inputs |                   |
|--------------|--|-------------------|
|              | 2012   | 2011              |
| Mutual funds | <u>\$ 521,555</u>                                  | <u>\$ 229,539</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 \$58,562 and \$51,005 for 2012 and 2011, respectively.

**Note 14. Supplemental Cash Flow Information**

During 2012 and 2011, ASP recorded the following non-cash operating and financing transactions:

In-kind donations of \$22,434 and \$44,786 in materials, and \$0.00 and \$5,500 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.

**Note 15. Commitments and Contingencies**

As of December 31, 2012 and 2011, ASP is contingently liable as guarantor with respect to \$106,327 and \$124,743 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.

(Continued)

APPALACHIA SERVICE PROJECT, INC.

NOTES TO FINANCIAL STATEMENTS

December 31, 2012

**Note 15. Commitments and Contingencies (Continued)**

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**

Management evaluated all activity of the Organization through May 22, 2013 (the issue date of the Financial Statements) and concluded that no subsequent events have occurred that would require recognition in the Financial Statements or disclosure in the Notes to the Financial Statements.

# **INTERNAL CONTROL AND COMPLIANCE**

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**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, in accordance with the 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, the financial statements of Appalachia Service Project, Inc. ("ASP"), which comprise the statement of financial position as of December 31, 2012, and the related statements of activities, and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated May 22, 2013.

**Internal Control Over Financial Reporting**

In planning and performing our audit of the financial statements, we considered ASP's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances 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. Accordingly, we do not express an opinion on the effectiveness of ASP's internal control.

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. 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.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

**Compliance and Other Matters**

As part of obtaining reasonable assurance about whether ASP's financial statements are free from 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*.

**Purpose of this Report**

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the organization's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the organization's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

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

Bristol, Virginia  
May 22, 2013