

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION

Annual Financial Report

October 31, 2012

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
MISSION and LEADERSHIP
October 31, 2012

Rural Communities Housing Development Corporation (“RCHDC”) is a California not-for-profit corporation which was incorporated in November 1975. RCHDC’s mission is to provide decent, affordable housing to low and moderate income persons. The mission is accomplished through its self-help home ownership program and developing and managing multi-family low-income housing for the elderly and families.

BOARD OF DIRECTORS

<u>Name</u>	<u>Date Seated</u>	<u>Term Expires</u>
William Thompson, Chairperson	March 11, 2005	November 2013
Peter Klein, Vice Chairperson	July 28, 2008	November 2015
Charlotte Watkins, Secretary	October 25, 2010	November 2015
Gary Mirata, Treasurer	August 31, 2009	November 2013
Marlene Ruiz	October 26, 2009	November 2015
Raymond Hall	September 28, 2009	November 2015
Mark Rohloff	February 28, 2011	November 2013
Tom MonPere	February 27, 2012	November 2013
Aaron Lefebvre	October 30, 2012	November 2013

ADMINISTRATION

Lois Goforth – Chief Executive Officer
Chuck Lange – Fiscal Officer

ADDRESS OF CORPORATE OFFICE

499 Leslie Street
Ukiah, California 95482

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
MISSION and LEADERSHIP
October 31, 2012

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Independent Auditors' Report

To the Board of Directors of
Rural Communities Housing Development Corporation
Ukiah, California

We have audited the accompanying consolidated statement of financial position of Rural Communities Housing Development Corporation and Affiliates ("Corporation"), as of October 31, 2012 and the related consolidated statements of activities and changes in net assets and cash flows for the year then ended. These financial statements are the responsibility of the Corporation's management. 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 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 Rural Communities Housing Development Corporation's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, the evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Rural Communities Housing Development Corporation and Affiliates as of October 31, 2012, and the results of their operations and changes in net assets, and their cash flows for the year 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 a report dated April 29, 2013, on our consideration of Rural Communities Housing Development Corporation and Affiliates' internal control over financial reporting and 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.

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Rural Communities Housing Development Corporation
Independent Auditors' Report
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Our audit was conducted for the purpose of forming an opinion on the basic consolidated financial statements. The consolidating schedules of financial information on pages 41 through 49 are presented for purposes of additional analysis and are not a required part of the financial statements. The accompanying Schedule of Expenditures of Federal Awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is not a required part of the basic consolidated 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 consolidated financial statements. The information has been subjected to the auditing procedures applied in the audit of the basic consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated 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 relations to the basic consolidated financial statements as a whole.

Clark, Schaefer, Hackett & Co.

Columbus, Ohio
April 29, 2013

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
CONSOLIDATED STATEMENT of FINANCIAL POSITION
October 31, 2012

ASSETS	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Totals</u>
Current Assets:				
Cash and cash equivalents	\$ 3,691,107	\$ -	\$ 286,691	\$ 3,977,798
Net tenant accounts receivable	18,318	-	-	18,318
Tenant assistance accounts receivable	8,892	-	-	8,892
Other accounts receivable	26,296	-	-	26,296
Due from related parties	1,421,838	-	-	1,421,838
Prepaid expenses	<u>58,089</u>	<u>-</u>	<u>-</u>	<u>58,089</u>
Total Current Assets	<u>5,224,540</u>	<u>-</u>	<u>286,691</u>	<u>5,511,231</u>
Deposits:				
Tenant security deposits held in trust	177,634	-	-	177,634
Self-Help construction deposits held in trust	1,300	-	-	1,300
Tax and insurance impounds	147,093	-	-	147,093
Replacement reserves	3,124,048	-	-	3,124,048
Other required reserves	795,176	-	-	795,176
Escrow deposit for loan closing	820,000	-	-	820,000
Residual receipts reserves	576,555	-	-	576,555
Cash restricted for pension plan	13,683	-	-	13,683
Cash restricted for self-insurance plan	<u>53,098</u>	<u>-</u>	<u>-</u>	<u>53,098</u>
Total Deposits	<u>5,708,587</u>	<u>-</u>	<u>-</u>	<u>5,708,587</u>
Fixed Assets, net of Accumulated Depreciation	<u>19,237,091</u>	<u>9,782,400</u>	<u>584,000</u>	<u>29,603,491</u>
Other Assets:				
Long-term notes receivable	686,083	205,000	808,881	1,699,964
Developer notes receivable	1,063,446	-	-	1,063,446
Loan costs, net	201,633	-	-	201,633
Advances and investments in nonconsolidated affiliates	142,785	-	269,800	412,585
Land held for development	1,468,357	726,092	-	2,194,449
Development costs	<u>2,500,534</u>	<u>2,198,701</u>	<u>500,000</u>	<u>5,199,235</u>
Total Other Assets	<u>6,062,838</u>	<u>3,129,793</u>	<u>1,578,681</u>	<u>10,771,312</u>
Total Assets	<u>\$ 36,233,056</u>	<u>\$ 12,912,193</u>	<u>\$ 2,449,372</u>	<u>\$ 51,594,621</u>

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

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
CONSOLIDATED STATEMENT of FINANCIAL POSITION - Continued
October 31, 2012

LIABILITIES & NET ASSETS	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Totals</u>
Current Liabilities:				
Accounts payable and accrued liabilities	\$ 528,116	\$ -	\$ -	\$ 528,116
Accrued interest payable	53,562	-	-	53,562
Due to related parties	121,209	-	-	121,209
Current portion mortgages and notes payable	2,388,191	-	-	2,388,191
Deferred revenue	<u>29,105</u>	<u>-</u>	<u>-</u>	<u>29,105</u>
Total Current Liabilities	<u>3,120,183</u>	<u>-</u>	<u>-</u>	<u>3,120,183</u>
Long-Term Liabilities:				
Tenant security deposits	179,649	-	-	179,649
Self-Help construction deposits	1,300	-	-	1,300
Accrued interest payable	2,226,072	-	-	2,226,072
Mortgages and notes payable, net	<u>30,571,779</u>	<u>-</u>	<u>-</u>	<u>30,571,779</u>
Total Long-Term Liabilities	<u>32,978,800</u>	<u>-</u>	<u>-</u>	<u>32,978,800</u>
Total Liabilities	<u>36,098,983</u>	<u>-</u>	<u>-</u>	<u>36,098,983</u>
Net Assets	<u>134,073</u>	<u>12,912,193</u>	<u>2,449,372</u>	<u>15,495,638</u>
Total Liabilities & Net Assets	<u>\$ 36,233,056</u>	<u>\$ 12,912,193</u>	<u>\$ 2,449,372</u>	<u>\$ 51,594,621</u>

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

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
CONSOLIDATED STATEMENT of ACTIVITIES and CHANGES in NET ASSETS
Year ended October 31, 2012

REVENUES	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>Total</u>
Net tenant rents	\$ 1,948,941	\$ -	\$ -	\$ 1,948,941
Tenant assistance payments	3,461,455	-	-	3,461,455
Other rents	130,546	-	-	130,546
Grant income	209,495	-	200,000	409,495
Interest income	48,870	-	-	48,870
Management fees and reimbursements	304,700	-	-	304,700
Operational revenue	824,854	-	-	824,854
Other revenue	12,867	-	-	12,867
Gain on sale of McCarty Manor	<u>2,499,209</u>	<u>-</u>	<u>-</u>	<u>2,499,209</u>
Total Revenues	<u>9,440,937</u>	<u>-</u>	<u>200,000</u>	<u>9,640,937</u>
EXPENSES				
Administrative services	1,712,635	-	-	1,712,635
Utilities	810,589	-	-	810,589
Operating and maintenance				
Operating expenses	1,079,497	-	-	1,079,497
Replacement reserve and residual receipt expenditures	105,274	-	-	105,274
Taxes and insurance	778,432	-	-	778,432
Interest expense	1,367,138	-	-	1,367,138
Unrealized loss on land development and notes receivable	1,152,886	-	-	1,152,886
Depreciation and amortization	<u>1,223,775</u>	<u>-</u>	<u>-</u>	<u>1,223,775</u>
Total Expenses	<u>8,230,226</u>	<u>-</u>	<u>-</u>	<u>8,230,226</u>
Change in Net Assets	1,210,711	-	200,000	1,410,711
Grant liens during year	-	8,087	-	8,087
Net Asset (Deficit) at the Beginning of the Year	<u>(1,076,638)</u>	<u>12,904,106</u>	<u>2,249,372</u>	<u>14,076,840</u>
Net Assets at the End of the Year	<u>\$ 134,073</u>	<u>\$ 12,912,193</u>	<u>\$ 2,449,372</u>	<u>\$ 15,495,638</u>

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

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
CONSOLIDATED STATEMENT of CASH FLOWS
Year ended October 31, 2012

CASH FLOWS FROM OPERATING ACTIVITIES

Change in Total Net Assets from Operations	\$ 1,410,711
Adjustments to Reconcile Changes in Net Assets to Net cash Provided by (Used in) Operating Activities:	
Net present value of notes receivable	53,219
Increase in long-term accrued interest	391,024
Depreciation and amortization	1,223,775
Unrealized loss on land development and notes receivable	1,152,886
Allowance for doubtful accounts	(60,000)
Gain on sale of McCarty Manor	(2,499,209)
Decrease (Increase) in:	
Net tenant accounts receivable	18,351
Tenant assistance accounts receivable	(8,029)
Other accounts receivable	(20,462)
Prepaid expenses	(13,511)
Increase (Decrease) in:	
Accounts payable and accrued liabilities	(79,425)
Accrued interest payable	(28,786)
Deferred revenue	(40,656)
Net Cash Provided by Operating Activities	<u>1,499,888</u>

CASH FLOWS FROM INVESTING ACTIVITIES

Decrease (Increase) in:	
Tenant deposits held in trust	(7,285)
Cash restricted for loan closing	(820,000)
Tax and insurance impounds	101,791
Replacement reserve	607,069
Other reserves	528,170
Residual receipts reserve	244,396
Cash restricted for pension plan	(13)
Cash restricted for self-insurance plan	(4,979)
Purchase of fixed assets	(35,207)
Decrease in due from related parties	(12,836)
Increase in long-term notes receivable	71,986
Developer notes receivable	(444,594)
Advances to nonconsolidated affiliates	150,000
Proceeds from sale to Pine Gardens Holding 3 LLC	2,917,000
Proceeds from sale of McCarty Manor	2,714,195
Development costs	(322,780)
Net Cash Provided by Investing Activities	<u>5,686,913</u>

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

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
CONSOLIDATED STATEMENT of CASH FLOWS – Continued
Year ended October 31, 2012

CASH FLOWS FROM FINANCING ACTIVITIES

Proceeds from mortgages and notes payable	\$ 2,292
Proceeds from grant liens	8,087
Decrease in due to related parties	(319,365)
Principal payments on mortgages and notes payable	<u>(4,270,744)</u>

Net Cash Used in Financing Activities (4,579,730)

Net Increase in Cash and Cash Equivalents 2,607,071

Cash and Cash Equivalents, Beginning 1,370,727

Cash and Cash Equivalents, Ending \$ 3,977,798

SUPPLEMENTAL DISCLOSURES

Amounts Paid for Interest	<u>\$ 774,313</u>
Amounts Paid for Income Tax	<u>\$ -</u>

NON CASH INVESTING AND FINANCING ACTIVITIES

Capitalized accrued interest payable	<u>\$ 101,487</u>
Acquisition by Pine Gardens Holding 3 LLC of fixed assets with debt	<u>\$ 5,302,500</u>

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

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
NOTES to the CONSOLIDATED FINANCIAL STATEMENTS
Year ended October 31, 2012

Note 1. Organization and Summary of Significant Accounting Policies

Organization

RCHDC is a California not-for-profit corporation that was incorporated in November 1975. The primary purpose of RCHDC is to develop, own and manage low-cost housing through the use of government financing, subsidies and other available resources to alleviate housing problems affecting low and moderate income families and to promote the welfare of the elderly and handicapped.

Principles of Consolidation

The accompanying consolidated financial statements include the accounts of RCHDC and its affiliates, as described below. Significant intercompany accounts and transactions have been eliminated in consolidation, as presented in the respective consolidating schedules. Intercompany transactions include management fees, accounting fees, and receivables and payables between related parties.

These consolidated financial statements include Funds 10, 20, 21, 22, 23, 70 and 90 of RCHDC, its owned housing projects, controlled housing projects, and investments in partnerships. All but one of the controlled housing projects are owned by separate corporations or limited liability companies, which share the same board of directors as RCHDC. One of the controlled housing projects is owned by a limited partnership in which both the general partner and the limited partner are not-for-profit corporations, which share the same board of directors as RCHDC. The controlled entities, other than housing projects, are generally corporations or limited liability companies, which share the same board of directors as RCHDC. Three of these controlled entities were formed to serve as general partners in limited partnerships, which own housing projects that are not consolidated in the financial statements. RCHDC also manages other housing projects with unrelated ownership that are not consolidated in these financial statements.

Financial data used for the consolidation of CC Seabreeze, LLC and CC Seagull Villa, LLC is as of October 31, 2012. There were no events or transactions either excluded or included that would have a significant effect on the consolidated financial statements.

Nonconsolidated Interests in Partnerships

RCHDC, through its controlled entities, holds 0.01% general partner interests in five limited partnerships which operate eight low income housing projects. Based on various provisions in the partnership agreements, the general partner does not have exclusive control, therefore, the general partner interests are accounted for under the cost method of accounting. Additionally, see Note 6 for disclosures regarding potential unanticipated obligations of RCHDC or its consolidated affiliates related to these partnerships. At October 31, 2012, RCHDC's investment in the five limited partnerships totaled \$243,385 and is classified as "Advances and investment in nonconsolidated affiliates" in the consolidated statement of financial position.

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
NOTES to the CONSOLIDATED FINANCIAL STATEMENTS – Continued
Year ended October 31, 2012

Note 1. Organization and Summary of Significant Accounting Policies – (Continued)

The following summarizes the funds, owned entities and controlled entities that are included in these consolidated financial statements:

<u>RCHDC Funds</u>	<u>Fund Number</u>
Corporate Fund	Fund 10
Administrative Fund	Fund 20
Revolving Development Fund	Fund 21
Property Management	Fund 22
First Time Home Buyer	Fund 23
Self-Help Technical Assistance Grant	Fund 70
Self-Help Construction Trust Fund	Fund 90
<u>RCHDC Owned Housing Projects</u>	<u>Project Operations Included</u>
Creekside Village ***	McCarty Manor ****
Cypress Ridge	McCloud Motel Apartments
Highlands Village	Oak Hill Apartments
Holden Street	Sunshine Manor ***
Holly Heights I	Walnut Village ***
Holly Heights II	Gibson Court 4 Apartments *
<u>Controlled Entities</u>	<u>Project Operations Included</u>
Pine Gardens I, Inc. CC Seabreeze, LLC CC Seagull Villa, LLC Pine Gardens Holding 3 LLC	Creekside Village *** Sunshine Manor *** Walnut Village ***
Redwood Court Property Corporation Redwood Court Property, A California Limited Partnership ** Bevins Court Housing Corporation Clearlake Housing Corporation Gibson Court Housing Corporation Lakeview Housing, Inc. Low Gap Housing Corporation North Pine Street Senior Housing Corporation Red Bluff Senior Housing Corporation Siskiyou Gardens Inc. Washington Court Senior Housing Corporation Willits Senior Housing Corporation	Redwood Court Apartments Bevins Court Apartments North Shore Village Gibson Court Apartments * Lakeview Apartments Jack Simpson School View Apartments North Pine Street Apartments Oak Park Manor Siskiyou Garden Apartments Washington Court Apartments Lenore Street Senior Housing

*Gibson Court Housing Corporation was only able to obtain funding to support 12 of the 16 units at Gibson Court Apartments, RCHDC provided the funding for the remaining 4 units.

** Limited Partner investment interest in Redwood Court Property, A California Limited Partnership.

*** Effective August 16, 2012, RCHDC sold the owned housing project to Pine Gardens Holding 3 LLC, a related party. Subsequent to the sale date, the project is included with Controlled Entities.

**** Effective October 17, 2012, RCHDC sold the owned housing project to McCarty Manor Associates LP. Pine Gardens I, Inc. is the general partner with a .01% ownership interest. Subsequent to the date of the sale, the project is no longer included in the consolidated financial statements.

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
NOTES to the CONSOLIDATED FINANCIAL STATEMENTS – Continued
Year ended October 31, 2012

Note 1. Organization and Summary of Significant Accounting Policies – (Continued)

Description of Funds

RCHDC maintains separate funds for each low-income housing project it owns and for each federal grant it administers. In addition to these funds, RCHDC maintains corporate, administrative and trust funds. The operations of each fund are accounted for with a separate set of self-balancing accounts that comprise its assets, liabilities, fund equity, revenues and expenditures. Resources are allocated to, and accounted for, in individual funds based upon the purposes for which they are intended. The corporate, administrative, operating and trust funds are grouped into categories as follows:

Corporate Fund (Fund 10)

Assets, such as land, buildings, computer equipment and other assets, used by RCHDC to manage its housing projects and funds are recorded in Fund 10. Sources of revenue for Fund 10 include interest earned on bank accounts and other miscellaneous revenues. Fund 10 is charged with depreciation for the fixed assets discussed above.

Administrative Fund (Fund 20)

Sources of revenue for Fund 20 generally include rental income from commercial real estate owned by RCHDC, accounting fees charged to some of the housing projects where appropriate, laundry revenue from contracts with many of the housing projects managed by RCHDC, and expendable grant income where appropriate. All administrative costs of managing RCHDC and its related entities as well as costs specifically related to the production of revenue discussed above are charged to Fund 20.

Revolving Development Fund (Fund 21)

Fund 21 is used to acquire and develop land for proposed Self-Help projects and for low-income family and elderly housing projects. Revenues for Fund 21 generally include grant income designated for specific projects or developer fees associated with the completion and lease-up of new or rehabilitated low-income housing projects.

Property Management Fund (Fund 22)

Revenues for Fund 22 generally include property management fees from both affiliated and unaffiliated low-income housing projects that are managed by RCHDC. All direct costs of property management are charged to Fund 22.

First Time Home Buyer Fund (Fund 23)

All direct costs associated with the Home Ownership Center are charged to Fund 23. Revenues for Fund 23 generally include nominal charges to participants in the home ownership classes as well as grant income as appropriate.

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
NOTES to the CONSOLIDATED FINANCIAL STATEMENTS – Continued
Year ended October 31, 2012

Note 1. Organization and Summary of Significant Accounting Policies – (Continued)

Description of Funds - continued

Self-Help Technical Assistance Grant (Fund 70)

Fund 70 administers the USDA and HCD Technical Assistance grant funds to support the Self-Help families. Therefore, all costs associated with the oversight and management of the Self-Help program are charged to Fund 70.

Self-Help Construction Trust Fund (Fund 90)

Fund 90 is a trust account used to account for the Self-Help construction costs for each family. Costs incurred in excess of budget are charged to the individual family responsible for the cost overrun. Although RCHDC manages the assets and liabilities in Fund 90 on behalf of the families building their homes these assets and liabilities do not accrue to RCHDC, and therefore, are not consolidated in the financial statements.

Basis of Accounting

RCHDC uses the accrual basis of accounting. Under the accrual basis of accounting revenues are recognized when earned and expenses are recognized when incurred. Revenues are reported as increases in unrestricted net assets unless use of the related assets is limited by donor-imposed restrictions. Expenditures are reported as decreases in unrestricted net assets.

Net Asset Classifications

Unrestricted Net Assets are those currently available for use of the organization, as determined by the management and board of directors as appropriate.

Temporarily Restricted Net Assets are those received with donor stipulations that limit the use of the donated assets. Once the donor stipulations have been met, these net assets are reclassified as unrestricted net assets and reported in the statement of activities as net assets released from restrictions.

Permanently Restricted Net Assets are those contributed with donor stipulations that permanently limit the use of the donated assets for the purpose intended by the donor.

Cash and Cash Equivalents

For purposes of the statements of cash flows, RCHDC considers all highly liquid debt instruments purchased with a maturity of three months or less to be cash equivalents. There were no cash equivalents as of October 31, 2012.

Cash balances in banks are insured up to \$250,000 from October 3, 2008 through December 31, 2013 by the Federal Deposit Insurance Corporation (FDIC). As of October 31, 2012, RCHDC's Funds, Owned Projects and Controlled Entities held cash in banks in excess of amounts insured by the FDIC totaled \$4,230,303.

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
NOTES to the CONSOLIDATED FINANCIAL STATEMENTS – Continued
Year ended October 31, 2012

Note 1. Organization and Summary of Significant Accounting Policies – (Continued)

Cash and Cash Equivalents - continued

Beginning January 1, 2013, noninterest-bearing accounts will no longer be insured separately from depositors' other accounts at the same bank. Instead, noninterest-bearing transaction accounts will be added to any of a depositor's other accounts in the applicable ownership category, and the aggregate balance insured up to at least the Standard Maximum Deposit Insurance amount of \$250,000 per depositor, at each separately chartered bank.

Tenant Receivable and Bad Debt Policy

Tenant receivables are charged to bad debt expense when they are determined to be uncollectible based upon a periodic review of the accounts by management. Accounting principles generally accepted in the United States of America require that the allowance method be used to recognize bad debts; however, the effect of using the direct write-off method is not materially different from the results that would have been obtained under the allowance method. Included in expenses are bad debts of \$44,205 for the year ended October 31, 2012.

Tenant Deposits Held in Trust

Tenant security deposits are segregated and held in trust in a separate bank account in the name of the respective housing project.

Fixed Assets

Fixed assets are valued at acquisition cost. Major additions are capitalized as they are placed in service, and minor improvements, which do not extend the useful life of the asset, are expensed in the period incurred. Depreciation is provided using the straight-line method over the estimated useful lives of the related assets, which range from five to forty years.

Reserves

The low-income housing projects obtain federal, state and local funding which require certain reserves to be maintained in separate federally insured bank accounts. These accounts include tax and insurance impounds, replacement reserves, other required reserves and residual receipts reserves. Additionally, as disclosed in Note 4, Savings Bank of Mendocino County has a security interest in certain replacement and other required reserves. Use of these funds are restricted as defined in the corporate, partnership, debt and regulatory agreements and therefore, have been excluded from cash in the accompanying consolidated Statement of Financial Position and Consolidated Statement of Cash Flows.

Loan Costs

Loan costs totaling \$203,043 for mortgage financing are amortized with the straight-line method of amortization over the term of the mortgage. Accounting principles generally in the United States of America require that the effective yield method be used to amortize financing costs; however, the effect of using the straight-line method is not materially different from the results that would have been obtained under the effective yield method. As of October 31, 2012, accumulated amortization totaled \$1,410. The estimated amortization expense for each of the next five years is \$xxxxxx.

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
NOTES to the CONSOLIDATED FINANCIAL STATEMENTS – Continued
Year ended October 31, 2012

Note 1. Organization and Summary of Significant Accounting Policies – (Continued)

Grants

RCHDC receives various grants to assist with the development of specific projects and programs. Capital grants and expendable grants are received from NeighborWorks America, a sponsoring organization of RCHDC. These funds are used to assist with the development of affordable housing projects, improvements in management and planning of new programs and projects for the benefit of low-income families and seniors. The NeighborWorks America grant receipts and related expenditures are reported in Note 8 to these consolidated financial statements.

Grant Liens

RCHDC regularly receives funds from various governmental or non-profit agencies in the form of non-interest bearing mortgages secured by deeds of trust related to the development of affordable housing, subject to regulatory agreements or other restrictions that require the properties to remain affordable to low-income residents for extended periods of time. RCHDC records such advances as temporarily restricted net assets. Upon full satisfaction of the affordability restrictions and the reconveyance of the deeds of trust by the granting agencies, the face amount of these liens are reported as grant income.

Notes Receivable

As described in Note 2, RCHDC obtains funding from various external and internal sources to loan funds to individuals that qualify for self-help programs to purchase homes. The notes receivable agreements are subordinate to the first mortgage and other third party financing that has priority. The payment terms vary from 1) fully forgiven providing the buyers continue to reside in the homes for 20 to 30 years, 2) deferred for 5 or more years with payment of principal and interest 3) deferred until the first mortgage is paid in full. At October 31, 2012, RCHDC has a reserve for forgivable loans of \$466,609 and net present value reserve of \$872,553.

Additionally, as described in Note 5, RCHDC has provided seller financing in the sale of four owned projects. RCHDC also enters into developer notes receivable. Payment of the developer notes will occur as set in the development agreements.

Management reviews its note receivable balances for collectability, based on payment history and review of the underlying real estate. At October 31, 2012, no allowance for doubtful accounts is deemed necessary.

Development Costs and Revenue Recognition

Development costs are recorded on a site-specific basis. Development costs include all expenditures necessary to complete a project including but not limited to the purchase price of land, escrow and closing costs, predevelopment costs, legal and other consulting fees, architecture and engineering costs, entitlement costs, governmental fees and permits, construction and supervision costs, and interest costs during the development process. Development costs are capitalized as construction in process until the completed project is placed in service, at which time construction in process is reclassified to land and buildings subject to depreciation, for reporting purposes.

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
NOTES to the CONSOLIDATED FINANCIAL STATEMENTS – Continued
Year ended October 31, 2012

Note 1. Organization and Summary of Significant Accounting Policies – (Continued)

Development Costs and Revenue Recognition (continued)

Development costs are capitalized and proportionately allocated at sale. Developments which experience lot sales in more than one fiscal period reflect lower development costs when the first lots are sold and higher development costs as the last lots are sold.

Fixed Asset, Land Held for Development, and Development Costs Impairment

RCHDC reviews its investment in real estate for impairment whenever events or changes in circumstances indicate that the carrying value of such property may not be recoverable. Recoverability is measured by a comparison of the carrying amount of the real estate to the future net undiscounted cash flow expected to be generated by the estimated proceeds from the eventual disposition of the real estate or recent appraisals. If the real estate is considered to be impaired, the impairment to be recognized is measured at the amount by which the carrying amount of the real estate exceeds the fair value of such property. For the year ended October 31, 2012, RCHDC recorded an impairment loss of \$1,152,886. However, RCHDC may in the future sell certain real estate for less than the carrying value or determine that future events would indicate additional impairment.

Income Taxes

RCHDC and the majority of its controlled corporations are exempt from Federal and California income taxes because they are organized as a not-for-profit corporations exempt under Federal and California Code Sections 501(c)(3) and 23701(d), respectively. Redwood Court Properties, A California Limited Partnership; CC Seabreeze, LLC and CC Seagull Villa, LLC, and Pine Gardens Holding 3, LLC are pass-through entities with not-for-profit general partners and managing members, and are treated as exempt organizations for Federal and California income tax purposes per IRS ruling.

RCHDC and affiliates account for uncertainty in income taxes in accordance with Accounting Standards Codification (“ASC”) 740 Income Taxes. This interpretation prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. This interpretation also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition.

RCHDC’s previously filed income tax returns for the tax years 2008, 2009, and 2010 remain subject to examination by a taxing authority. RCHDC’s income tax returns for the tax year 2011 have not been filed and remain subject to examination by a taxing authority.

See Note 14 for tax notices received from the Internal Revenue Service (“IRS”).

Fair Value of Financial Instruments

RCHDC considers the recorded value of its financial assets and liabilities, which consist primarily of cash, accounts receivable, and account payable, to approximate the fair value of the respective assets and liabilities at October 31, 2012 based upon the short-term nature of the assets and liabilities.

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
NOTES to the CONSOLIDATED FINANCIAL STATEMENTS – Continued
Year ended October 31, 2012

Note 1. Organization and Summary of Significant Accounting Policies – (Continued)

Fair Value of Financial Instruments (continued)

Notes receivable are recorded at their net realizable value using the applicable federal rate as of the date of the note agreement and the term period.

There has been no significant change in interest rates available to RCHDC. Therefore, the fair value of mortgages and notes payable approximates book value.

Fair Value Measurements of Assets and Liabilities

The accounting guidance for “Fair Value Measurements and Disclosures” establishes a fair value hierarchy that prioritizes the inputs used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurement) and the lowest priority to unobservable inputs (Level 3 measurement). Where observable inputs are available for substantially the full term of the asset or liability, the instrument is categorized in Level 2. When quoted market prices are not available, pricing may be completed using comparable securities, dealer values, operating data and general market conditions to determine Fair value. Valuation models utilize various inputs such as commodity, interest rate and, to a lesser degree, volatility or credit that include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in inactive markets, market corroborated inputs (i.e. inputs derived principally from, or correlated to, observable market data) and other observable inputs for the asset or liability.

Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Actual results could differ from these estimates.

Subsequent Events

The consolidated financial statements and related disclosures include evaluation of events up through and including April 29, 2013, which is the date the consolidated financial statements were available to be issued.

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
NOTES to the CONSOLIDATED FINANCIAL STATEMENTS – Continued
Year ended October 31, 2012

Note 2. Notes Receivable

In assisting eligible individuals and facilitating the development or rehabilitation of low-income multifamily housing, RCHDC has provided assistance in the form of purchase money loans, which are secured by junior deeds of trust on real estate. Terms vary, but generally fall into one of the following categories:

Fund 21:

1. Loans are for a period of 30 years accruing interest at 4% per annum and do not require repayment until they mature or the homeowner sells the property.
2. Loans are for a period of 30 years accruing interest at 4% to 5% per annum. Monthly interest and principal payments are required beginning in the sixth year until the loan is fully amortized at the end of the 30 year term or prepaid in accordance with its terms.
3. Fund 21 has \$70,000 of notes receivable due from CC Seabreeze, L.P. as well as \$85,000 of notes receivable due from CC Seagull Villas, L.P. The funds were loaned to these two partnerships for the rehabilitation of three low-income housing apartments in Crescent City. The loans are secured and do not accrue interest and are due on May 31, 2066, and September 30, 2066, respectively.

Fund 10:

1. Loans with 30 year terms were made to homeowners from Fund 10. The loans bear no interest during the first ten years and accrue 3% simple interest thereafter for the next twenty years. Monthly payments of principal and interest commence in the sixteenth year such that all outstanding principal and accrued interest is fully amortized by the end of the 30 year term. The loans are secured by trust deeds on the properties.
2. Loans with 30 year terms were made to homeowners from Fund 10. The terms of these loans give RCHDC a share in the appreciation of the affordable housing that they help finance. The loans do not bear interest and require no payments unless the properties subject to the liens are sold prior to their maturity dates. The loans are secured by trust deeds on the properties. RCHDC's share of appreciation is reduced by 5% per year beginning in the eleventh year of each loan such that there shall be no amounts due to RCHDC provided the properties are held for the full 30 year terms of the loans. RCHDC's policy is to provide a valuation allowance equal to the face amount on these notes since the present value of the notes cannot be readily determined.

See note 5 for additional notes receivable from seller financing of four owned projects. Due to the long-term nature of these loans, minimal principal payments are expected during the year ended October 31, 2013.

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
 NOTES to the CONSOLIDATED FINANCIAL STATEMENTS – Continued
 Year ended October 31, 2012

Note 3. Fixed Assets

Fixed assets, net of accumulated depreciation, consists of the following at October 31, 2012:

	Beginning Balance	Additions	Deductions	Ending Balance
Fixed Assets:				
Land and Improvements	\$ 2,839,048	\$ -	\$ (190,376)	\$ 2,648,672
Building and Improvements	45,845,486	13,450	(1,626,573)	44,232,363
Office Furniture and Equipment	<u>977,296</u>	<u>21,757</u>	<u>(119,063)</u>	<u>879,990</u>
Total Fixed Assets	49,661,830	35,207	(1,936,012)	47,761,025
Accumulated Depreciation	<u>(17,934,392)</u>	<u>(1,222,365)</u>	<u>999,223</u>	<u>(18,157,534)</u>
Fixed Assets, Net	<u>\$ 31,727,438</u>	<u>\$ (1,187,158)</u>	<u>\$ (936,789)</u>	<u>\$ 29,603,491</u>

Note 4. Long-Term Debt

Long-term debt consists of the following at October 31, 2012:

FUNDS

Corporate Fund (Fund 10)

United States Department of Agriculture, Rural Development Mortgage for \$750,000 at 4.375% annual interest secured by RCHDC's principal offices on Leslie Street in Ukiah. Payments of principal and interest of \$3,315 monthly for forty years, due May 18, 2044. \$ 689,075

Revolving Development Fund (Fund 21)

Redevelopment Agency, City of Ukiah loan to be repaid when primary financing is obtained. This note is unsecured and is non-interest bearing. 18,000

Redevelopment Agency, City of Ukiah loan requiring an annual payment of \$500, payable through September 1, 2032. This note is unsecured and is non-interest bearing. 20,000

City of Ukiah loan originally due on December 31, 1999, including simple interest at 3%. This note is unsecured. This note has been extended by the City until called. As of October 31, 2012, accrued interest totaled \$69,594. 115,200

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
NOTES to the CONSOLIDATED FINANCIAL STATEMENTS – Continued
Year ended October 31, 2012

Note 4. Long-Term Debt – (Continued)

<p>Redevelopment Agency, City of Ukiah loan originally due on September 26, 1999, including simple interest at 3%. This note is unsecured. This note has been extended by the City until called. As of October 31, 2012, accrued interest totaled \$16,516.</p>	36,500
<p>Local Initiatives Support Corporation (“LISC”) advance in the amount of \$123,700 at 6% interest for RCHDC to use for Seagull Villa Apartments rehabilitation pursuant to a Line of Credit Agreement dated June 1, 2006. This advance together with accrued interest is to be repaid upon the earlier of two years from the date of the advance or upon the closing of the permanent financing for Seagull Villa Apartments. This note is unsecured. All principal and interest on the note was paid in full during 2012.</p>	-0-
<p>Savings Bank of Mendocino County loan for land development costs associated with the Lake Mendocino Drive Self-Help property in the maximum amount of \$1,500,000 at 7% interest. Interest is payable on the loan monthly in arrears and all unpaid principal and interest was originally due on or before July 21, 2009. This note is secured. This note has been extended until January 15, 2014.</p>	1,032,000
<p>California Department of Housing & Community Development note through the Joe Serna, Jr. grant program dated October 21, 2009. The note is non-interest bearing and principal payments are to be repaid upon the sale of a lot in increments of \$19,455.</p>	233,455
<p>California Department of Housing and Community Development loan of \$800,000 secured by Self-Help property on North State Street (Contract #03-PDL-34), originally due June 30, 2008, bearing interest at 3%. This note is secured by a deed of trust. The note has been extended to August 31, 2012. As of October 31, 2012, accrued interest totaled \$196,000.</p>	800,000
<p>Savings Bank of Mendocino County \$1,829,520 promissory note secured by property at Brush Street originally due October 1, 2007. Interest is fixed at 5.75% and is payable monthly. \$484,935 was paid down during the fiscal year ended October 31, 2008 from the \$500,000 Neighbor Works loan. This note has been extended to April 1, 2016 with monthly payments of principal and interest of \$9,373.</p>	1,311,149
<p>Neighborworks Capital Corporation loan in the amount of \$500,000 for Orr Creek Commons (Brush Street property) with interest at 5.5% per annum payable interest only at the end of each quarter in arrears. All unpaid principal and interest is due on or before December 31, 2015. This note is secured.</p>	500,000
<p>California Department of Housing and Community Development unsecured note dated August 11, 2008, in the amount of \$100,000 (Contract #07-PDL-69) for predevelopment costs related to Orr Creek Commons in the City of Ukiah. The note accrues simple interest of 3% and is repayable on or before August 31, 2014. As of October 31, 2012, accrued interest totaled \$12,317.</p>	100,000

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
 NOTES to the CONSOLIDATED FINANCIAL STATEMENTS – Continued
 Year ended October 31, 2012

Note 4. Long-Term Debt – (Continued)

Rural Community Assistance Corporation ("RCAC") promissory note, not to exceed \$500,000 bearing 5% interest with principal and accrued interest originally due on September 1, 2008. This note has been extended until September 1, 2016, and the interest rate has been increased to 5.5% of which 50% is paid monthly and 50% is accrued to maturity.

502,291

Redevelopment Agency, City of Ukiah loan dated April 20, 2010. The note is unsecured and non-interest bearing. Payments of principal must be made from residual receipts as required by the Agency under the terms of the Regulatory Agreement.

15,000

\$ 5,372,670

OWNED PROJECTS

Creekside Village is financed with a mortgage note of \$1,952,900 with the United States Department of Housing and Urban Development ("HUD"), under Section 202 of the National Housing Act of 1959. The mortgage note bears interest at the rate of 9.25% per annum and is being repaid in 480 equal monthly installments of principal and interest of \$15,441 payable through January 1, 2024. This note is secured. The note and accrued interest was paid in full upon the sale to Pine Gardens Holding 3 LLC, a controlled group. See Note 5 for seller financing.

\$ -0-

Cypress Ridge is financed with two mortgage notes of \$1,500,000 and \$50,000, totaling \$1,550,000, with the United States Department of Agriculture, Rural Development ("RD") under Section 515 of the National Housing Act of 1959. The mortgage note bears interest at the rate of 9.0% per annum, payable in 588 equal monthly installments (49 years) of principal and interest of \$11,780 through November 12, 2029. The mortgage note is secured by the apartment project. In addition, there is an interest subsidy from RD associated with these mortgages that reduces the effective interest rate to 7.0%. The subsidy is not recorded on the Project's books as income or expense and reduces the actual monthly payments by RCHDC to \$9,362. As of October 31, 2012, interest subsidy totaled \$18,288 and accrued interest totaled \$6,186.

1,097,232

Cypress Ridge rehabilitation is financed with a note from the City of Fort Bragg for \$225,000 that accrues interest at 3% per annum and requires repayment from residual receipts, as defined by the regulatory agreement. Principal and interest shall be due and payable on or before March 1, 2065. The note is secured by the assignments of rents and revenues. As of October 31, 2012, accrued interest totaled \$24,438.

225,000

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
 NOTES to the CONSOLIDATED FINANCIAL STATEMENTS – Continued
 Year ended October 31, 2012

Note 4. Long-Term Debt – (Continued)

<p>Cypress Ridge rehabilitation is also financed with a mortgage note from the California Department of Housing and Community Development ("HCD") under the Home Investment Partnership's ("HOME") Program, dated July 14, 2004 for a maximum amount of \$983,026 (Contract #03-HOME-0687). The note accrues simple interest of 3% per annum and requires repayment from residual receipts, as defined in the regulatory agreement, commencing the last day of the initial operating year following the completion of rehabilitation. The unpaid principal and accrued interest are due in full on or before the 55th anniversary of the note. The note is secured by a Deed of Trust against the Project. As of October 31, 2012, accrued interest totaled \$112,518.</p>	908,215
<p>Highlands Village is financed with a mortgage note of \$1,675,900 with HUD, under Section 202 of the National Housing Act of 1959. The mortgage note bears interest at the rate of 8.5% per annum and is being repaid in 480 equal monthly installments of principal and interest of \$12,285 payable through June 1, 2021. The mortgage is secured by the apartment project. As of October 31, 2012, accrued interest totaled \$6,389.</p>	902,022
<p>Holden Street is financed with a mortgage note of \$293,000 with HUD, under Section 202 of the National Housing Act of 1959. The mortgage note bears interest at the rate of 9.25% per annum and is being repaid in 454 equal monthly installments of principal and interest of \$2,334 payable through October 1, 2020. The mortgage note is secured by the apartment project. As of October 31, 2012, accrued interest totaled \$1,206.</p>	156,513
<p>Holly Heights I is financed with two mortgage notes of \$125,000 and \$670,000, totaling \$795,000, with RD under Section 515 of the National Housing Act of 1959. The mortgage notes bear interest at the rate of 8.0% per annum, payable in 468 equal monthly installments (39 years) of principal and interest of \$5,550 through October 1, 2017. In addition, there is an interest subsidy from RD associated with these mortgages that reduces the effective interest rate to 6.0%. The subsidy is not recorded on the Project's books as income or expense and reduces the actual monthly payments by the Project to \$4,405. The interest subsidy is deducted monthly by RD directly from the contract payments and is estimated at \$3,424 for the year ended October 31, 2012. As of October 31, 2012, accrued interest totaled \$813.</p>	159,223
<p>Holly Heights I received additional financing with a mortgage note of \$238,736 with HCD for new construction and rehabilitation projects under the HOME Program. The mortgage note accrues simple interest at the rate of 3% per annum. The mortgage note is secured by the apartment project. As of October 31, 2012, accrued interest totaled \$64,868.</p>	238,636

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
NOTES to the CONSOLIDATED FINANCIAL STATEMENTS – Continued
Year ended October 31, 2012

Note 4. Long-Term Debt – (Continued)

Holly Heights II is financed with two mortgage notes of \$664,632 and \$105,726, totaling \$770,358, with FmHA under Section 515 of the National Housing Act of 1959. The mortgage note contracts bear interest at the rate of 11.875% per annum, payable in 548 equal monthly installments of principal and interest of \$7,658 through November 2034. In addition, there is an interest subsidy from Rural Development ("RD") associated with these mortgages that reduces the effective interest rate to 1.0%. The subsidy is not recorded on the Project's books as income or expense and reduces the actual monthly payments by the Project to \$1,752. The interest subsidy is deducted monthly by RD directly from the contract payments and for the year ended October 31, 2012 amount to \$69,685. As of October 31, 2012, accrued interest totaled \$1,183. 716,427

Holly Heights II received additional financing with a mortgage note of \$178,928 with the Department of Housing & Community Development for new construction and rehabilitation projects under the HOME Program. The mortgage note contract bears simple interest at the rate of 3% per annum. The mortgage note is secured by the project. As of October 31, 2012, accrued interest totaled \$48,937. 178,928

McCarty Manor is financed with a mortgage note of \$1,708,500 with FmHA under Section 515 of the National Housing Act of 1959. The mortgage note contract bears interest at the rate of 10.75% per annum, payable in 588 equal monthly installments (49 years) of principal and interest of \$15,378 through October 1, 2032. The mortgage note is secured by the apartment project. In addition, there is an interest subsidy from RD associated with this mortgage that reduces the effective interest rate to 9.75%. The subsidy is not recorded on the Project's books as income or expense and reduces the actual monthly payments by the Project to \$14,010. The note and accrued interest were paid in full upon the sale to McCarty Manor Associates LP on October 17, 2012. -0-

Sunshine Manor is financed with a mortgage note of \$1,112,400 with HUD, under Section 202 of the National Housing Act of 1959, as amended. The mortgage note bears interest at the rate of 6.875% per annum and is being repaid in 480 equal monthly installments of principal and interest of \$6,812 payable through October 1, 2019. The mortgage note is secured by the apartment project. The note and accrued interest was paid in full upon the sale to Pine Gardens Holding 3 LLC on August 16, 2012. -0-

Walnut Village is financed with a mortgage note of \$1,395,100 with HUD, under Section 202 of the National Housing Act of 1959. The mortgage note bears interest at the rate of 6.875% per annum and is being repaid in 480 equal monthly installments of principal and interest of \$8,543 payable through September 1, 2019. The mortgage note is secured by the apartment project. The note and accrued interest was paid in full upon the sale to Pine Gardens Holding 3 LLC on August 16, 2012. -0-

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
 NOTES to the CONSOLIDATED FINANCIAL STATEMENTS – Continued
 Year ended October 31, 2012

Note 4. Long-Term Debt – (Continued)

McCloud Motel Apartments is financed with a promissory note from the Housing Assistance Council. The note accrues interest at 5%. The entire balance of principal and accrued interest is due and payable on December 31, 2011. The note has been extended until December 31, 2012. The note is secured by a First Deed of Trust. As of October 31, 2012, accrued interest totaled \$136,946. 799,785

Oak Hill Apartments is financed with three mortgage notes originated on October 28, 2004, in the original amounts of \$2,500,000, \$1,100,000 and \$400,000 with RD under Section 514 Labor Housing of the Title V of the Housing Act of 1949. The mortgage notes bear interest at the rate of 1% per annum and payable in monthly installments of \$13,205 of principal and interest over the over the thirty-three year term of the loans through October 28, 2037. The note is secured by the apartment project. As of October 31, 2012, accrued interest totaled \$3,025. 3,507,173

Oak Hill Apartments was also financed with a note, secured by a deed of trust, originated on June 1, 2005, in the original amount of \$3,442,000 from the Home Investment Partnerships Program ("HCD-HOME") through the California Department of Housing and Community Development. The note calls for simple interest at the rate of 3% per annum to accrue on the unpaid principal amount of the note. Payments are required pursuant to the terms of the mortgage note equal to residual receipts after the Developer Fee Note has been paid in full as well as Asset Management Fees not to exceed \$12,000 per year. Thereafter, all unpaid principal and interest are payable at the maturity date for this mortgage note on June 1, 2060. As of October 31, 2012, there were no payments made under the terms of this mortgage note. As of October 31, 2012, accrued interest totaled \$778,028. 3,442,000

\$ 12,331,154

CONTROLLED ENTITIES

Bevins Court is financed with a promissory note of \$100,000 from the County of Lake. The note matures in January 2044 and bears interest on unpaid principal of 2%. Interest is deferred from January 15, 2003, and will be repaid in 37 equal installments of \$4,236 beginning January 15, 2008. Annual payments of interest and principal shall be made from "residual receipts" as determined by HUD, or from the Project's own funds. No payments of principal are due before 2012. The promissory note is secured by the apartment project. As of October 31, 2012, accrued interest totaled \$5,718. \$ 100,000

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
NOTES to the CONSOLIDATED FINANCIAL STATEMENTS – Continued
Year ended October 31, 2012

Note 4. Long-Term Debt – (Continued)

<p>North Shore Villas is financed with a mortgage note of \$1,488,800 with HUD, under Section 202 of the National Housing Act of 1959. The mortgage note bears interest at the rate of 8.375% per annum and is being repaid in 480 equal monthly installments of principal and interest of \$10,773 payable through October 1, 2031. The mortgage note is secured by the apartment project. As of October 31, 2012, accrued interest totaled \$8,567.</p>	1,227,463
<p>Gibson Court is also financed with a promissory note from HCD. The note is for \$758,824, matures in May 2031 and bears annual interest of 3%. Annual payments of interest and principal shall be made only from "residual receipts" approved by HUD for any particular year. All other terms and conditions of the note default to the provisions of HUD Section 811. The promissory note is secured by the apartment project. As of October 31, 2012, accrued interest totaled \$148,712.</p>	758,824
<p>Lakeview Apts. is financed with a mortgage note of \$1,656,000 with HUD, under Section 202 of the National Housing Act of 1959. The mortgage note bears interest at the rate of 9.25% per annum and is being repaid in 480 equal monthly installments of principal and interest of \$13,093 payable through October 1, 2028. The mortgage note is secured by the apartment project. As of October 31, 2011, accrued interest totaled \$10,359.</p>	1,309,624
<p>Jack Simpson Apts. is financed with a mortgage note of \$1,619,200 with HUD, under Section 202 of the National Housing Act of 1959. The mortgage note bears interest at the rate of 9.0% per annum and is being repaid in 480 equal monthly installments of principal and interest of \$12,490 payable through August 1, 2032. The mortgage note is secured by the apartment project. As of October 31, 2012, accrued interest totaled \$10,380.</p>	1,384,012
<p>Siskiyou Garden Apts. is financed with a mortgage note of \$485,580 with Berkodia Mortgage Company. The mortgage note bears interest at the rate of 7% per annum and is being repaid in 190 equal monthly installments of principal and interest of \$4,007 payable through September 30, 2013. The mortgage note is secured by the apartment project. In addition, there is an interest subsidy from HUD associated with the mortgage that reduces the effective interest rate to .45%. The interest subsidy is deducted monthly by the finance company directly from the contract payments. The total interest subsidy for the year ended October 31, 2012 amounted to \$26,297.</p>	61,038

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
NOTES to the CONSOLIDATED FINANCIAL STATEMENTS – Continued
Year ended October 31, 2012

Note 4. Long-Term Debt – (Continued)

Washington Court is financed with a promissory note from HCD under the HOME Program. The original note was for \$202,720, matures in August 2031 and bears annual interest of 3%. Annual payments of interest and principal shall be made only from "residual receipts" approved by HUD for any particular year. No payments shall be required from this promissory note in the absence of residual receipts. The promissory note is secured by the apartment project. All other terms and conditions of the note default to the provisions of HUD Section 202. As of October 31, 2012, accrued interest totaled \$66,587. 202,720

Redwood Court is financed with a mortgage note of \$1,854,944, with RD under Section 515 of the National Housing Act of 1949. The mortgage note bears interest at the rate of 9.0% per annum, payable in 600 equal monthly installments (50 years) of principal and interest of \$14,072 through July 2, 2037. The mortgage note is secured by the apartment. In addition there is an interest subsidy from RD associated with this mortgage that reduces the effective interest rate to 1%. The subsidy is recorded on the Partnership's books as income and expense and reduces the actual monthly payments by the Partnership to \$4,098. The interest subsidy is deducted monthly by RD directly from the contract payments. For the year ended October 31, 2012, interest subsidy totaled \$116,807. As of October 31, 2012, accrued interest totaled \$2,371. 1,670,833

Redwood Court is also financed with a second mortgage note of \$76,923 with RD under Section 515 of the National Housing Act of 1949 on January 23, 1992 for the purpose of landscaping and installing playground equipment. The mortgage note bears interest at the rate of 8.25% and is payable in 600 equal monthly installments (50 years) of principal and interest of \$538 through February 1, 2042. The mortgage note is secured by the equipment. As of October 31, 2012, accrued interest totaled \$118. 51,576

Redwood Court is also financed with a mortgage note secured by a Deed of Trust on the apartment project from HCD under the HOME Program in the amount of \$2,987,557. The full amount of this loan funded in favor of the Partnership on September 15, 2008. The note bears interest at the rate of 3% per annum, and is repayable in 35 years. As of October 31, 2012, accrued interest totaled \$236,011. 2,987,556

Redwood Court is also financed with a mortgage note secured by a deed of trust from the Fortuna Redevelopment Agency pursuant to a Promissory Note and Loan Agreement in the amount of \$200,000. This Promissory Note bears interest at the rate of 3% per annum, simple interest, and is payable in full together with accrued and unpaid interest at its maturity on September 1, 2063. The terms of this loan include an affordability restriction on the units within the property by which the loan is secured that runs the full 55 year term of the loan. The proceeds from this loan were advanced to Pine Gardens I, Inc. so that Pine Gardens I, Inc. could acquire the limited partnership interest in the Partnership from Beech Villa Ltd. effective August 29, 2008. As of October 31, 2012, accrued interest totaled \$26,071. 200,000

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
 NOTES to the CONSOLIDATED FINANCIAL STATEMENTS – Continued
 Year ended October 31, 2012

Note 4. Long-Term Debt – (Continued)

<p>Creekside Village is financed with a mortgage note funded with tax-exempt bonds issued by the Authority and purchased by Savings Bank of Mendocino County in the amount of \$2,265,000 due August 1, 2042. The mortgage note bears interest at the rate of 5.75% per annum until August 1, 2011. Interest will increase to 6.75% on August 1, 2022 and 7.25% on August 1, 2042. This note is secured by its replacement reserve of \$448,000 and other required reserves totaling \$382,000.</p>	2,265,000
<p>Creekside Village is also financed with a promissory note from RCHDC. The note is non-interest bearing. The entire balance of principal is due and payable on August 16, 2067. The note is secured by a First Deed of Trust. See Note 5 for seller financing note payable.</p>	1,442,000
<p>Sunshine Village is financed with a mortgage note funded with tax-exempt bonds issued by the Authority and purchased by Savings Bank of Mendocino County \$1,087,500 due August 1, 2042. The mortgage note bears interest at the rate of 5.75% per annum until August 1, 2022. Interest will increase to 6.75% on August 1, 2022 and 7.25 % on August 1, 2042. This note is secured by its replacement reserve of \$248,435 and other required reserves totaling \$382,000.</p>	1,087,500
<p>Sunshine Village is also financed with a promissory note from RCHDC. The note is non-interest bearing. The entire balance of principal is due and payable on August 16, 2067. The note is secured by a First Deed of Trust. See Note 5 for seller financing note payable.</p>	830,000
<p>Walnut Village is financed with a mortgage note funded with tax-exempt bonds issued by the Authority and purchased by Savings Bank of Mendocino County of \$1,950,000 due August 1, 2042. The mortgage note bears interest at the rate of 5.75% per annum until August 1, 2022. Interest will increase to 6.75% on August 1, 2022 and 7.25 % on August 1, 2042. This note is secured by its replacement reserve of \$850,064 and other required reserves of \$190,000.</p>	1,950,000
<p>Walnut Village is also financed with a promissory note from RCHDC. The note is non-interest bearing. The entire balance of principal is due and payable on August 16, 2067. The note is secured by a First Deed of Trust. See Note 5 for seller financing note payable.</p>	<u>1,881,000</u>
	19,409,146
Less: Seller financed notes payable eliminated in consolidation	<u>(4,153,000)</u>
	<u>\$15,256,146</u>

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
NOTES to the CONSOLIDATED FINANCIAL STATEMENTS – Continued
Year ended October 31, 2012

Note 4. Long-Term Debt – (Continued)

Changes in long-term debt for the year ended October 31, 2012 is as follows:

	Beginning Balance	Additions	Reductions	Consolidating Entries	Ending Balance
Funds	\$ 5,594,315	\$ 2,292	\$ 223,937	\$ -	\$ 5,372,670
Owned Projects	16,219,039	-	3,887,885	-	12,331,154
Controlled Entities	<u>10,112,568</u>	<u>9,455,500</u>	<u>158,922</u>	<u>(4,153,000)</u>	<u>15,256,146</u>
Totals	<u>\$ 31,925,922</u>	<u>\$ 9,457,792</u>	<u>\$ 4,270,744</u>	<u>\$ 4,270,744</u>	<u>\$ 32,959,970</u>

Aggregate maturities required on the mortgages payable at October 31, 2012 is as follows:

<u>For the Year Ended October 31:</u>	<u>Funds</u>	<u>Owned</u>	<u>Controlled</u>	<u>Total</u>
2013	\$ 1,061,967	\$ 1,099,854	\$ 226,370	\$ 2,388,191
2014	1,042,725	315,353	218,868	1,576,946
2015	11,204	331,920	214,898	558,022
2016	1,051,995	314,168	231,871	1,598,034
2017	1,323,353	312,562	250,197	1,886,112
Thereafter	<u>881,426</u>	<u>9,957,297</u>	<u>14,113,942</u>	<u>24,952,665</u>
	<u>\$ 5,372,670</u>	<u>\$ 12,331,154</u>	<u>\$ 15,256,146</u>	<u>\$ 32,959,970</u>

Note 5. Seller Financing for Notes Receivable and Notes Payable

As described in Note 16, RCHDC sold three owned projects consisting of Creekside Village, Sunshine Village and Walnut Village to Pine Gardens Holding 3 LLC, a controlled entity.

RCHDC provided seller financing as follows:

Sunshine Village	\$ 830,000
Walnut Village	\$ 1,881,000
Creekside Village	\$ 1,442,000

As described in Note 4, the seller financed notes payable bear no interest, are secured by First Deeds of Trust and principal is due and payable on August 16, 2067. The notes receivable and notes payable have been eliminated in consolidation.

Additionally, RCHDC sold McCarty Manor to McCarty Manor Associates LP as described in Note 16. RCHDC provided seller financing totaling \$725,805. The note receivable bears interest of 2.63%, secured with a Deed of Trust and principal and interest are due and payable on October 1, 2067. Payments of principal and accrued interest are due beginning November 1, 2013 with annual payments totaling 75% of Residual Receipts as defined in the note receivable agreement.

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
NOTES to the CONSOLIDATED FINANCIAL STATEMENTS – Continued
Year ended October 31, 2012

Note 6. Commitments and Contingencies

As described in Note 1, RCHDC holds or maintains the General Partner (“GP”) interest in five Limited Partnerships, which own a total of eight low-income apartment developments.

These GP entities have certain ongoing obligations, with respect to the partnerships in which they are involved, as follows:

A) Pine Gardens I, Inc. has the following ongoing obligations related to Clara Court, L.P. (“Clara”):

- i) During the construction phase of Clara, Pine Gardens I, Inc. has guaranteed a September 30, 2011 completion date, is required to pay any development deficits and shall cause rental achievement to occur by June 1, 2012. Completion of Clara was delivered in December 2011 and management believes the GP will not have to pay the limited partner for any short fall in tax credit delivery.
- ii) Pine Gardens I, Inc. is required to establish a separate Operating Reserve Account in the amount of \$105,000 for Clara. This reserve has been funded.
- iii) Pine Gardens I, Inc. has pledged to lend Clara any operating loans to fund operating deficits incurred by Clara during the period commencing at rental achievement and expiring 60 months thereafter. No funds have been advanced to the Partnership pursuant to this agreement.
- iv) Pine Gardens I, Inc. is required to make capital contributions to Clara to compensate the limited partner for any ongoing shortfall in the tax credits which are hereinafter expected to accrue for the benefit of the limited partner.

Pine Gardens I, Inc. is required to make capital contributions for the portion of the Development Fee Note that remains unpaid by the thirteenth anniversary of the completion of the construction of Clara.

- vi) Pine Gardens I, Inc. is required to purchase the limited partner's interest in Clara for the total amount of capital contributions contributed by the limited partner plus any expenses incurred by the limited partner, based upon the occurrence of various specified events related to the failure of Clara to achieve the anticipated results. The management of Clara believes that it is highly unlikely that the GP will have any liability related to this obligation.

B) Pine Gardens I, Inc. has the following ongoing obligations related to Orchard River Associates, L.P. (“Orchard”) and the three apartment projects it owns:

- i) Pine Gardens I, Inc. together with RCHDC, is required to maintain an aggregate net worth of not less than \$500,000.
- ii) Pine Gardens I, Inc. is required to establish segregated Operating Reserve Accounts for each project as follows:

Orchard Manor Apts.	\$80,250
Orchard Village Apts.	\$70,500
River Gardens Apts.	\$67,000

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
 NOTES to the CONSOLIDATED FINANCIAL STATEMENTS – Continued
 Year ended October 31, 2012

Note 6. Commitments and Contingencies – (Continued)

- iii) To date these segregated Operating Reserve Accounts have not yet been established. The GP expects to fund these reserves with funds from the investor equity installments, yet to be received.
 - iv) Pine Gardens I, Inc. has guaranteed to fund the operating deficits of each project until each project has achieved a Debt Service Coverage Ratio of 1.15 to 1.00, and then for an additional sixty (60) consecutive months up to an aggregate amount of \$788,925 after the segregated Operating Reserve Accounts have been exhausted.
 - v) Pine Gardens I, Inc. is required to make capital contributions to the partnership to compensate the limited partner for any ongoing shortfall in the tax credits which are hereinafter expected to accrue for the benefit of the limited partnership.
 - vi) Pine Gardens I, Inc. is required to make a capital contribution for the portion of the Developer Fee Note for each project that remains unpaid as of the end of the twelfth year following the completion of the rehabilitation of each project.
 - vii) Pine Gardens I, Inc. is required to purchase the limited partner's interest in Orchard for the total amount of capital contributions contributed by the limited partner plus any expenses incurred by the Limited Partner, based upon the occurrence of various specified events related to the failure of the projects to achieve the anticipated results. The management of Orchard believes that it is highly unlikely that they GP will have any liability related to this obligation.
- C) CC Seabreeze, LLC (“Seabreeze”) and CC Seagull Villa, LLC (“Seagull”) have the following ongoing obligations related to the respective partnerships in which they have an interest and the related projects that these partnerships own:
- i) Seabreeze and Seagull have guaranteed to fund the operating deficits of each project until each project has achieved a Debt Service Coverage Ratio of 1.10 to 1.00, and then for an additional three (3) consecutive years up to the following total amounts:

Seabreeze Apts. and Totem Villa Apts.	\$314,594
Seagull Villa Apts.	\$154,262

These obligations are required only after the Operating Reserve Target Amounts have been exhausted.
 - ii) Seabreeze and Seagull are required to make capital contributions to the partnerships to compensate the limited partners for any ongoing shortfall in the tax credits which are hereinafter expected to accrue for the benefit of the limited partners.

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
NOTES to the CONSOLIDATED FINANCIAL STATEMENTS – Continued
Year ended October 31, 2012

Note 6. Commitments and Contingencies – (Continued)

- iii) Seabreeze and Seagull are required to make capital contributions for the portion of the Developer Fee Note for each project that remain unpaid as of the end of the twelfth year following the completion of the rehabilitation of each project.
 - iv) Seabreeze and Seagull are required to purchase the limited partners' interests in the partnerships for the total amount of capital contributions contributed by the limited partners plus \$50,000 plus any expenses incurred by the limited partners, based upon the occurrence of various specified events related to the failure of the projects to achieve the anticipated results. The management of the partnerships believe that it is highly unlikely that the GP will have any liability related to this obligation.
- D) Pine Gardens I, Inc. has the following obligations related to McCarty Manor Associates, LP (the Partnership):
- i) Pine Gardens I, Inc. together with RCHDC, is required to maintain an aggregate net worth of not less than \$500,000 and liquidity of not less than \$250,000 exclusive of any interest in the Partnership.
 - ii) Pine Gardens II, Inc., an unaffiliated entity that is funded by RCHDC has agreed to make a subordinated Permanent Loan to the Partnership in the amount of \$700,000 at the long term Applicable Federal Rate for a term of 55 years commencing with the Investor's Contribution of its third installment of equity. \$800,000 of funds have already been set aside in a separate bank account for the purpose of making this loan.
 - iii) Pine Gardens I, Inc. is required to purchase the limited partner's interest in the Partnership for the total amount of capital contributions contributed by the limited partner plus any expenses incurred by the limited partner, based upon the occurrence of various specified events related to the failure of the Partnership to achieve the anticipated results. Management believes that it is highly unlikely that Pine Gardens I, Inc. will have any liability related to this obligation.
 - iv) Pine Gardens I, Inc. is required to establish a separate Operating Reserve for the Partnership in the amount of \$200,000 out of the fourth installment of capital by the limited partner.
 - v) To the extent not otherwise funded from the Operating Reserve discussed above, Pine Gardens I, Inc. is required to make Operating Loans to the Partnership to fund any Operating Deficits throughout the Tax Credit Compliance period.
 - vi) To the extent funds are not otherwise available from other construction sources of funds for the Partnership, Pine Gardens I, Inc. shall be obligated to make Completion Loans to the Partnership for construction cost overruns through the date that the Partnership generates a 1.15 debt service coverage ratio for three consecutive months following the completion of construction.

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
 NOTES to the CONSOLIDATED FINANCIAL STATEMENTS – Continued
 Year ended October 31, 2012

Note 6. Commitments and Contingencies – (Continued)

- vii) Pine Gardens I, Inc. is required to make a capital contribution to the Partnership in an amount equal to any Developer Fee that remains unpaid as of the twelfth anniversary of the Completion Date as defined, so that the Partnership has adequate resources to pay the remainder of the Developer Fee.
- viii) Pine Gardens I, Inc. is required to make capital contributions that may be necessary to compensate the limited partner for any ongoing tax credit shortfalls that might occur over the course of the Tax Credit Compliance period.

Note 7. Functional Allocation of Expenses

Expenditures incurred in connection with RCHDC operations and expenditures made for corporate purposes have been summarized on functional basis, as administrative services, in the accompanying consolidated Statement of Activities.

Note 8. NeighborWorks America Grants

During the year ended October 31, 2012, RCHDC received grant funds from NeighborWorks America. The grants have been recognized in multiple funds and related corporations. The following provides a listing of the grants received:

<u>Grant Type</u>	<u>Amount Received</u>	<u>Unrestricted</u>	<u>Permanently Restricted</u>
Permanently Restricted	\$ 200,000	\$ -	\$ 200,000
Expendable	<u>97,000</u>	<u>97,000</u>	<u>-</u>
Total NeighborWorks America Grants Received	<u>\$ 297,000</u>	<u>\$ 97,000</u>	<u>\$ 200,000</u>

The following represents the components of permanently restricted net assets as it relates to cumulative capital grants provided to RCHDC from NeighborWorks America:

	<u>Fixed Assets</u>	<u>Notes Receivable</u>	<u>Advances to Affiliates</u>	<u>Development Costs</u>	<u>Total</u>
Beginning of the year	\$ 794,000	\$ 285,000	\$ 269,800	\$ 200,000	\$ 1,548,800
Grants	<u>-</u>	<u>100,000</u>	<u>-</u>	<u>100,000</u>	<u>200,000</u>
End of the year	<u>\$ 794,000</u>	<u>\$ 385,000</u>	<u>\$ 269,800</u>	<u>\$ 300,000</u>	<u>\$ 1,748,800</u>

Note 9. Self-Insurance

RCHDC's dental and vision insurance plans are funded through a restricted bank account established to provide medical benefits for eligible employees and their dependents. When necessary RCHDC makes a monthly contribution to the account to cover expected expenses. At October 31, 2012, RCHDC has \$53,098 in cash restricted for the self-insurance plan and accounts payable for amounts that were available to fund outstanding claims.

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
 NOTES to the CONSOLIDATED FINANCIAL STATEMENTS – Continued
 Year ended October 31, 2012

Note 10. Defined Contribution Pension Plan

RCHDC has a 403(b) defined contribution pension plan covering all employees working 20 hours per week or more. RCHDC may make a discretionary matching contribution to the plan each year, not to exceed 5% of the contributing employees' regular pay. For an employee to be eligible to receive the match, they must be employed on October 31st of the respective year. RCHDC reserves the contribution monthly and makes the deposit to the plan in the following fiscal year. Total contributions accumulated for the year ended October 31, 2012 to be deposited to the plan totaled \$13,683.

Effective January 1, 2013, RCHDC established a 401(k) plan that covers all employees who need certain eligibility requirements. RCHDC, on a discretionary basis, may choose to match at the end of the plan year.

Note 11. Temporarily Restricted Net Assets

Temporarily restricted net assets consisted of the following at October 31, 2012:

Fair market value of land of \$135,000 purchased from the County of Lake for \$1 for use by Bevins Court Housing Corporation. The land is restricted for affordable housing in Lake County for a period of 40 years from the date of grant.	\$ 135,000
Crescent City granted to RCHDC \$70,000 and \$85,000 during the years ended October 31, 2006 and 2008, respectively to be used for rehabilitation of three low income housing apartments in Crescent City, California. The housing projects must remain affordable for 55 years from the dates of the grants.	155,000
Revolving Development fund (Fund 21) grant liens	2,924,793
Owned Projects grant liens	3,300,500
Controlled Entities grant liens	6,346,900
Notes receivable with funds obtained from Redevelopment Agency of Mendocino	<u>50,000</u>
Total Temporarily Restricted Net Assets	<u>\$ 12,912,193</u>

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
 NOTES to the CONSOLIDATED FINANCIAL STATEMENTS – Continued
 Year ended October 31, 2012

Note 11. Temporarily Restricted Net Assets – (Continued)

The following is a summary of the grant liens at October 31, 2012:

REVOLVING DEVELOPMENT FUND (FUND 21)

<p>California Department of Housing and Community Development secured by deed of trust on the Lake Mendocino Drive property. The note is in the amount of \$560,000 originally due November 30, 2009. The note has been extended to November 30, 2013. The note bears interest at 3% until forgiven incrementally as individual lots are sold. RCHDC pays \$18,667 toward principal per lot sold. The note converts to a grant upon sale of lots to families. As of October 31, 2012 accrued interest totaled \$49,632.</p>	\$ 149,333
<p>California Department of Housing and Community Development, CalHOME predevelopment loans secured by deed of trust on the Lake Mendocino Drive property. The notes are in the amount of \$427,500 at 0% interest originally due February 25, 2005. The notes have been extended to lot sale dates. The notes convert to grants upon sale of lots to families.</p>	90,053
<p>Housing Assistance Council notes in the aggregate amount of \$1,493,647 on Lake Mendocino Drive Self-Help property at interest rates of 0% and 5% with a range of maturity dates. Notes are forgiven incrementally as individual lots are sold. The notes are secured by the properties. As of October 31, 2012, accrued interest totaled \$187,300.</p>	1,343,647
<p>Redevelopment Agency, County of Mendocino \$100,000 note dated January 20, 2009. Note bears interest at 1% until forgiven incrementally as individual lots are sold. This note is secured by the property.</p>	50,000
<p>County of Mendocino loan sponsored by Community Development Commission in the amount of \$496,000 which is forgiven incrementally as individual lots are sold. This note is secured by the property.</p>	217,888
<p>Lake County Redevelopment Agency note dated November 1, 2004, not to exceed \$250,000, secured by deed of trust on Collier Street property. Note balance increased by \$998,000 in 2009 to maximum balance of \$1,248,000. The note accrues simple interest at 2%. No payments or interest are due as long as the maker is not in default of an affordable housing covenant. After 10 years and each succeeding 5 years, 10% of the principal shall be reduced until the end of the 55 year term of the note. As of October 31, 2012, accrued interest totaled \$48,844.</p>	626,872
<p>Ukiah Redevelopment Agency loan of \$447,000, dated April 1, 2011. The loan is unsecured and non-interest bearing. No payments are due provided RCHDC has remained in continuous compliance with the Regulatory Agreement.</p>	<u>447,000</u>
	<u>\$ 2,924,793</u>

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
 NOTES to the CONSOLIDATED FINANCIAL STATEMENTS – Continued
 Year ended October 31, 2012

Note 11. Temporarily Restricted Net Assets – (Continued)

OWNED PROJECTS

Gibson Court 4 is financed with an Affordable Housing Program Direct Subsidy. The Agreement requires no payments or interest as long as the Project remains affordable for households with income at or below 50% of average median income. Provided the Project remains in compliance with the AHP conditions for the term of the lien, then repayment of these funds is not required. This note is secured by the apartment project. \$ 20,000

Oak Hill Apartments obtained a Grant Lien secured by a Deed of Trust which originated on January 30, 2002 in the total amount of \$2,988,000 from the Department of Housing and Community Development, Joe Serna Jr. Farmworker Housing Grant Program ("HCD-Joe Serna"). Provided that the Project remains in compliance with all of the covenants in the Grant Lien and Regulatory Agreement for the full 40 year term of the lien until January 30, 2042, no interest will accrue and no payments will be required pursuant to this Grant Lien. 2,988,000

Oak Hill Apartments obtained a Grant Lien secured by a Deed of Trust which originated on December 16, 2004 in the total amount of \$292,500 from the National Bank of the Redwoods pursuant to an Affordable Housing Program ("AHP") Award through the Federal Home Loan Bank of San Francisco ("FHLBSF"). Provided that the Project remains in compliance with FHLBSF – AHP requirements until July 26, 2022 (15 years from the date of issuance of the certificate of occupancy for the Project) no interest will accrue and no payments will ever be required pursuant to this Grant Lien. 292,500

\$ 3,300,500

CONTROLLED PROJECTS

Bevins Court is financed with a \$68,800 Affordable Housing Program Direct Subsidy. The Agreement requires no payments or interest as long as the Project remains affordable for households with income at or below 50% of average median income. The note payable is secured by the apartment project. \$ 68,800

Bevins Court is also financed with a mortgage note of \$1,104,100 from HUD, under Section 811. The mortgage note bears no interest and repayment is not required as long as the housing remains available for qualifying persons with disabilities. The note matures May 1, 2041 and may not be prepaid without prior written approval of HUD. Provided that the Project remains available and Bevins Court Housing Corporation has not defaulted on the terms of the Note, Mortgage, or Regulatory Agreement, HUD will deem the note paid in full at the maturity date. The mortgage note is secured by the apartment project. 1,104,100

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
NOTES to the CONSOLIDATED FINANCIAL STATEMENTS – Continued
Year ended October 31, 2012

Note 11. Temporarily Restricted Net Assets – (Continued)

Gibson Court is financed with a \$60,000 Affordable Housing Program Direct Subsidy. The Agreement requires no payments of principal or interest as long as the Project remains affordable for households with income at or below 50% of average median income. The note payable is secured by the apartment project. 60,000

Gibson Court is also financed with a Capital Advance Mortgage note of \$752,400 from HUD, under Section 811. The mortgage note bears no interest and repayment is not required as long as the housing remains available for qualifying persons with disabilities. The note matures May 1, 2041 and may not be prepaid without prior written approval of HUD. Provided that the Project remains available for disabled persons until the maturity date, and that Gibson Court Housing Corporation has not defaulted under the terms of the note, Mortgage, or Regulatory Agreement, HUD will deem the note paid in full at the maturity date. The mortgage note is secured by the apartment project. 752,400

North Pine St. Apts. is financed with a Capital Advance Mortgage note of \$706,000 with HUD under Section 202 of the National Housing Act of 1959, where HUD agreed to advance a maximum of \$706,000 to the project. The capital advance bears no interest and will not be repaid to HUD as long as the Project remains available to qualifying low income persons for a period of 40 years. If the Project becomes non-compliant within term, the advance becomes immediately due and payable. The note is secured by the project. 706,000

North Pine St. Apts. is also financed through a \$47,500 Affordable Housing Program Direct Subsidy. The Agreement requires no payments or interest as long as the Project remains affordable for households with income at or below 50% of average median income. The note payable is secured by the apartment project. 47,500

Oak Park Manor is financed with a mortgage note of \$1,733,300 with HUD, under Section 202 of the National Housing Act of 1959. The mortgage note bears no interest and repayment is not required as long as the housing remains available for low-income seniors. The note matures August 1, 2033 and may not be prepaid without prior written approval of the HUD. Provided that the Project remains available for low-income seniors until the maturity date, and that Red Bluff Senior Housing Corporation has not defaulted on the terms of the note, Mortgage, or Regulatory Agreement, HUD will deem the note paid in full at the maturity date. The mortgage note is secured by the apartment project. 1,733,300

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
NOTES to the CONSOLIDATED FINANCIAL STATEMENTS – Continued
Year ended October 31, 2012

Note 11. Temporarily Restricted Net Assets – (Continued)

Washington Court is financed with a \$55,000 Affordable Housing Program Direct Subsidy. The Agreement requires no payments of principal or interest as long as the Project remains affordable for households with income at or below 50% of average median income. The note payable is secured by the apartment project. 55,000

Washington Court is also financed with a Capital Advance Mortgage note in the amount of \$924,000 with HUD under Section 202 of the National Housing Act of 1959. The capital advance bears no interest and will not be repaid to HUD as long as the Project remains available to qualifying low income persons for a period of 40 years. If the Project becomes non-compliant within the term, the advance becomes immediately due and payable. The note is secured by the apartment project. 924,000

Lenore Street is financed with a \$60,000 Affordable Housing Program Direct Subsidy. The agreement requires no payments of principal or interest as long as the Project remains affordable for households with income at or below 50% of average median income. The note payable is secured by the apartment project. 60,000

Lenore Street is also financed with a Capital Advance Mortgage note of \$835,800 with HUD under Section 202 of the National Housing Act of 1959. The mortgage note bears no interest and repayment is not required as long as the housing remains available for low-income seniors. The note matures March 15, 2041 and may not be prepaid without prior written approval of HUD. Provided that the Project remains available for low-income seniors until the maturity date, and WSHC has not defaulted under the terms of the note, Mortgage or Regulatory Agreement, HUD will deem the note paid in full at the maturity date. The note payable is secured by the apartment project. 835,800

\$ 6,346,900

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
 NOTES to the CONSOLIDATED FINANCIAL STATEMENTS – Continued
 Year ended October 31, 2012

Note 12. Permanently Restricted Net Assets

Permanently restricted net assets at October 31, 2012 have been restricted for the following purpose:

Self-Help notes receivable	\$ 845,572
Notes receivable	100,000
Fixed assets	584,000
Advances to or investment in affiliates	419,800
Development costs	500,000
 Total Permanently Restricted Net Assets	 \$ 2,449,372

Note 13. Business Conditions – Oak Hill Apartments

During the year ended October 31, 2012, Oak Hill generated positive cash flow from operations and incurred a use of cash of \$2,612. The Project funded \$39,985 to the replacement reserve during the year ended October 31, 2012, but the replacement reserve remains underfunded by \$147,734. At October 31, 2012, the Project owes RCHDC a total of \$402,051. Therefore, the continued viability of this Project is dependent upon successful future operations. Effective November 1, 2011, Oak Hill received approval from RD to increase rents and received approval for the four unsubsidized units to reduce rents to market which management believes will result in reducing vacancies. However, it should be noted that as turnover continues to be higher than originally anticipated, the fact that the replacement reserves are underfunded is likely to further impact negative cash flow from operations attributable to the inability to draw upon the replacement reserves for unusual or unexpected turnover costs.

On October 29, 2012, RCHDC funded \$150,000 in a separate cash account designated as Oak Hill's replacement reserve. The balance is included in replacement reserves in the Consolidated Statement of Financial Position. As of October 31, 2012, the consolidated replacement reserve for Oak Hill exceeds the required RD funding, level, therefore, the requirement for funding the replacement reserve has been met.

Note 14. Tax Exempt Notices

Subsequent to year-end, RCHDC obtained notices for six of its controlled entities from the IRS stating that these entities had lost their tax-exempt status due to failure to file proper tax returns. These entities have been included in the consolidated tax-exempt tax return for RCHDC, which includes its funds, owned projects and certain of its controlled entities that are organized as tax-exempt entities. While these six entities were included in the consolidated return, it is the position of the IRS that the consolidated return was not properly filed in accordance with the regulations for consolidated tax-exempt returns, therefore, these entities must apply for tax-exempt status and file tax returns for certain years. RCHDC has filed the required application for retroactive reinstatement of tax-exempt status and individual tax returns and is currently working with the IRS to resolve this matter and believes that there will be no change in the tax-exempt status for these entities, therefore, no provision has been made for federal, state or local income taxes. While the ultimate outcome cannot be determined at this time, management believes that it is more likely than not that these entities will be determined to be tax-exempt organizations.

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
 NOTES to the CONSOLIDATED FINANCIAL STATEMENTS – Continued
 Year ended October 31, 2012

Note 15. Fair Value Measurements

The guidance requires that assets and liabilities carried at fair value will be classified and disclosed in one of the following three categories:

- Level 1: Quoted market prices in active markets for identical assets or liabilities.
- Level 2: Observable market based inputs or unobservable inputs that are corroborated by market data:
- Level 3: Unobservable inputs that are not corroborated by market data.

In determining the appropriate levels, RCHDC performs a detailed analysis of the assets and liabilities that are subject to fair value measurements. For the year ended October 31, 2012, the application of fair value techniques applied to similar assets and liabilities has been consistent. The following is a description of the valuation methodologies used for instruments measured at fair value.

Investment in Land Held for Development and Development Costs: The fair value of real estate is the market value of real estate based on recent appraisals, estimated future net undiscounted cash flows from the eventful disposition of the property and other real estate market condition factors.

The table below presents the balances of assets measured at fair value by level within that hierarchy at October 31, 2012:

	<u>Total</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
Land held for development and developments costs	\$ <u>7,393,684</u>	\$ <u>-</u>	\$ <u>-</u>	\$ <u>7,393,684</u>

The following summarizes the activity for Level 3 investments for the year ended October 31, 2012:

Balance, Beginning of Year	\$ 8,223,790
Total net gains (losses) included in:	
Change in Net Assets	322,780
Purchases, sales, issuances and settlements, net	<u>(1,152,886)</u>
Balance, End of Year	<u>\$ 7,393,684</u>

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
NOTES to the CONSOLIDATED FINANCIAL STATEMENTS – Continued
Year ended October 31, 2012

Note 16. Sale of Projects

Effective August 16, 2012, RCHDC sold three owned projects fixed assets for \$7,070,000 to Pine Gardens Holding 3 LLC (“PG3”), a related entity. PG3 is a single member LLC in which the sole member is Pine Gardens I, Inc., an entity with a common Board of Directors with RCHDC. The activity through August 16, 2012 is included with the Owned Housing projects Statements of Activities and Changes in Net Asset. Subsequent to the sale date, the activity is included with the Controlled Entities. The purchase was financed with \$4,153,000 in seller notes financing and bank mortgages payable totaling \$5,302,500. However, as the sale was a transaction between related parties included in these consolidated financial statements, the fixed assets are recorded in the Statement of Financial Position at the same basis just prior to the sale and any resulting gain on sale of the project is recorded in the Statement of Net Assets for the consolidating Schedule of Statement of Activities and Changes in Net Assets which will be eliminated in consolidation. Assets associated with the sale transaction and gain on sale which was transferred from Owned Projects to Controlled Projects were as follows:

	<u>Creekside Village</u>	<u>Walnut Village</u>	<u>Sunshine Manor</u>	<u>Total</u>
Sales Price	\$ 3,020,000	\$ 2,600,000	\$ 1,450,000	\$ 7,070,000
Fixed Assets	<u>732,345</u>	<u>323,555</u>	<u>277,801</u>	<u>1,333,701</u>
Gain on Sale	<u>\$ 2,287,655</u>	<u>\$ 2,276,445</u>	<u>\$ 1,172,199</u>	<u>\$ 5,736,299</u>

Effective October 17, RCHDC sold McCarty Manor, an owned project to McCarty Manor Associates LP for \$3,440,000. RCHDC provided seller financing totaling \$725,805 with terms as described in Note 5. Pine Gardens I, Inc. is the general partner. However, as the general partner does not exclusively control McCarty Manor Associates LP, the activities subsequent to October 17, 2012 are excluded from the consolidated financial statements. Assets associated with the sale transaction and gain on sale are as follows:

	<u>McCarty Manor</u>
Sales Price	\$ 3,440,000
Fixed Assets	<u>940,791</u>
Gain on Sale	<u>\$ 2,499,209</u>

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
NOTES to the CONSOLIDATED FINANCIAL STATEMENTS – Continued
Year ended October 31, 2012

Note 17. Current Concentration Due to Certain Conditions

RCHDC, through its Funds, Owned Properties and Controlled Entities, operations are concentrated in the low cost housing real estate including developing, owning and managing affordable housing which is a heavily regulated environment. The operations of the Owned Properties and Controlled Entities are subject to administrative directives, rules and regulations of federal and state regulatory agencies, including but not limited to RD, HUD, IRS and State Housing Agencies. The Funds rely on federal and state affordable housing programs to fund their purposes. Such administrative directives, rules and regulations are subject to change by an act of Congress or administrative change mandated by federal and state agencies. Such changes may occur with little notice or inadequate funding to pay for the related cost, including the additional administrative burden, to comply with a change.

SUPPLEMENTAL INFORMATION

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
CONSOLIDATING SCHEDULE of FINANCIAL POSITION
October 31, 2012

ASSETS	<u>Funds</u>	<u>Owned Projects</u>	<u>Controlled Entities</u>	<u>Consolidating Entries</u>	<u>Totals</u>
Current Assets:					
Cash and cash equivalents	\$ 3,464,191	306,708	206,899	\$ -	\$ 3,977,798
Net tenant accounts receivable	-	5,031	13,287	-	18,318
Tenant assistance accounts receivable	-	8,292	600	-	8,892
Other accounts receivable	12,061	14,235	-	-	26,296
Due from funds	-	-	15,838	(15,838)	-
Due from owned projects	440,591	-	-	(440,591)	-
Due from controlled entities	196,718	199,812	-	(396,530)	-
Due from related parties	980,923	50,305	390,610	-	1,421,838
Prepaid expenses	51,804	2,511	3,774	-	58,089
Total Current Assets	<u>5,146,288</u>	<u>586,894</u>	<u>631,008</u>	<u>(852,959)</u>	<u>5,511,231</u>
Deposits:					
Tenant deposits held in trust	-	52,941	124,693	-	177,634
Amounts held for self-help families	1,300	-	-	-	1,300
Tax and insurance impounds	-	53,475	93,618	-	147,093
Replacement reserves	150,000	570,619	2,403,429	-	3,124,048
Other required reserves	-	228,560	566,616	-	795,176
Residual receipts reserves	-	9,395	567,160	-	576,555
Escrow deposit for loan closing	820,000	-	-	-	820,000
Cash restricted for pension plan	13,683	-	-	-	13,683
Cash restricted for self-insurance plan	53,098	-	-	-	53,098
Total Deposits	<u>1,038,081</u>	<u>914,990</u>	<u>3,755,516</u>	<u>-</u>	<u>5,708,587</u>
Fixed Assets, net of Accumulated Depreciation	<u>774,119</u>	<u>14,081,732</u>	<u>14,747,640</u>	<u>-</u>	<u>29,603,491</u>
Other Assets:					
Long-term notes receivable	1,699,964	-	-	-	1,699,964
Developer notes receivable	1,063,446	-	-	-	1,063,446
Loan costs, net	-	-	201,633	-	201,633
Advances and investments in consolidated affiliates	128,000	-	332,937	(460,937)	-
Notes receivable from consolidated affiliates	4,153,000	-	-	(4,153,000)	-
Advances and investment in nonconsolidated affiliates	169,200	-	243,385	-	412,585
Land held for development	2,194,449	-	-	-	2,194,449
Development costs	5,174,032	25,203	-	-	5,199,235
Total Other Assets	<u>14,582,091</u>	<u>25,203</u>	<u>777,955</u>	<u>(4,613,937)</u>	<u>10,771,312</u>
Total Assets	<u>\$ 21,540,579</u>	<u>\$ 15,608,819</u>	<u>\$ 19,912,119</u>	<u>\$ (5,466,896)</u>	<u>\$ 51,594,621</u>

See Independent Auditors' Report.

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
CONSOLIDATING SCHEDULE of FINANCIAL POSITION – Continued
October 31, 2012

LIABILITIES & NET ASSETS (DEFICIT)	Funds	Owned Projects	Controlled Entities	Consolidating Entries	Totals
Current Liabilities:					
Accounts payable and accrued liabilities	\$ 453,825	26,433	47,858	\$ -	\$ 528,116
Accrued interest payable	-	18,802	34,760	-	53,562
Due to funds	-	492,252	127,388	(619,640)	-
Due to owned properties	52	-	69,826	(69,878)	-
Due to controlled properties	-	-	163,441	(163,441)	-
Due to related parties	-	-	121,209	-	121,209
Current portion mortgages and notes payable, net	1,061,967	1,099,854	226,370	-	2,388,191
Deferred revenue	22,587	2,047	4,471	-	29,105
Total Current Liabilities	<u>1,538,431</u>	<u>1,639,388</u>	<u>795,323</u>	<u>(852,959)</u>	<u>3,120,183</u>
Long-Term Liabilities:					
Tenant deposits held in trust	-	54,956	124,693	-	179,649
Amounts held for self-help families	1,300	-	-	-	1,300
Accrued interest payable	580,203	1,165,735	480,134	-	2,226,072
Mortgages and notes payable, net	4,310,703	11,231,300	19,182,776	(4,153,000)	30,571,779
Total Long-Term Liabilities	<u>4,892,206</u>	<u>12,451,991</u>	<u>19,787,603</u>	<u>(4,153,000)</u>	<u>32,978,800</u>
Total Liabilities	<u>6,430,637</u>	<u>14,091,379</u>	<u>20,582,926</u>	<u>(5,005,959)</u>	<u>36,098,983</u>
Net Assets (Deficit):					
Unrestricted (Deficit)	10,371,277	(2,039,560)	(7,536,707)	(460,937)	334,073
Temporarily restricted	3,129,793	3,300,500	6,481,900	-	12,912,193
Permanently restricted	1,608,872	256,500	384,000	-	2,249,372
Total Net Assets (Deficit)	<u>15,109,942</u>	<u>1,517,440</u>	<u>(670,807)</u>	<u>(460,937)</u>	<u>15,495,638</u>
Total Liabilities & Net Asset (Deficit)	<u>\$ 21,540,579</u>	<u>\$ 15,608,819</u>	<u>\$ 19,912,119</u>	<u>\$ (5,466,896)</u>	<u>\$ 51,594,621</u>

See Independent Auditors' Report.

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
CONSOLIDATING SCHEDULE of ACTIVITIES and CHANGES in NET ASSETS (DEFICIT)
Year ended October 31, 2012

REVENUES	<u>Funds</u>	<u>Owned Projects</u>	<u>Controlled Entities</u>	<u>Consolidating Entries</u>	<u>Totals</u>
Net tenant rents	\$ -	953,531	995,410	\$ -	\$ 1,948,941
Tenant assistance payments	-	2,242,604	1,218,851	-	3,461,455
Other rents	104,249	-	26,297	-	130,546
Grant income	409,495	-	-	-	409,495
Interest income	32,102	5,153	11,615	-	48,870
Management fees and reimbursements	759,141	-	76,658	(531,099)	304,700
Operational revenue	794,457	17,220	13,177	-	824,854
Other revenue	5,031	6,261	1,575	-	12,867
Gain on sale of McCarty Manor	-	2,499,209	-	-	2,499,209
Total Revenues	<u>2,104,475</u>	<u>5,723,978</u>	<u>2,343,583</u>	<u>(531,099)</u>	<u>9,640,937</u>
EXPENSES					
Administrative services	900,101	390,945	421,589	-	1,712,635
Management fees	27,492	243,008	215,646	(486,146)	-
Bookkeeping and accounting fees	-	19,130	25,823	(44,953)	-
Utilities	-	381,681	428,908	-	810,589
Operating and maintenance:					
Operating expenses	120,751	503,307	455,439	-	1,079,497
Replacement reserve & residual receipts accounts	-	105,274	-	-	105,274
Taxes and insurance	273,804	290,562	214,066	-	778,432
Interest expense	118,827	714,221	534,090	-	1,367,138
Unrealized loss on land development & notes receivable	1,152,886	-	-	-	1,152,886
Depreciation	37,509	672,154	514,112	-	1,223,775
Total Expenses	<u>2,631,370</u>	<u>3,320,282</u>	<u>2,809,673</u>	<u>(531,099)</u>	<u>8,230,226</u>
Change in Net Assets (Deficit)	(526,895)	2,403,696	(466,090)	-	1,410,711
New grant liens during year, net of forgiven grant liens for temporarily restricted net assets	8,087	-	-	-	8,087
McCarty Manor sale to third party - transfer of cash from owned to funds	1,700,410	(1,700,410)	-	-	-
McCarty Manor sale to third party - transfer of seller note receivable from owned to funds	725,805	(725,805)	-	-	-
Projects sold from owned to controlled - transfer of proceeds from sale	4,153,000	(4,153,000)	-	-	-
Transfer of notes receivable from owned to funds	2,404,223	(2,404,223)	-	-	-
Sale of owned projects to controlled entity	-	5,736,299	(5,736,299)	-	-
Net Assets (Deficit), Beginning	<u>6,645,312</u>	<u>2,360,883</u>	<u>5,531,582</u>	<u>(460,937)</u>	<u>14,076,840</u>
Net Assets (Deficit), Ending	<u>\$ 15,109,942</u>	<u>\$ 1,517,440</u>	<u>\$ (670,807)</u>	<u>\$ (460,937)</u>	<u>\$ 15,495,638</u>

See Independent Auditors' Report.

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
CONSOLIDATING SCHEDULE of CASH FLOWS
Year ended October 31, 2012

CASH FLOWS FROM OPERATING ACTIVITIES	Funds	Owned Projects	Controlled Entities	Consolidating Entries	Total
Change in Total Net Assets from Operations	\$ (526,895)	\$ 2,403,696	\$ (466,090)	\$ -	\$ 1,410,711
Adjustments to Reconcile Changes in Net Asset to Net cash Provided by Operating Activities:					
Net present value of notes receivable	53,219	-	-	-	53,219
Increase in long-term accrued interest	101,487	169,609	119,928	-	391,024
Depreciation and amortization	37,509	672,154	514,112	-	1,223,775
Forgiveness of grant liens	-	-	-	-	-
Unrealized loss on land development & notes receivable	1,152,886	-	-	-	1,152,886
Allowance for doubtful accounts	(60,000)	-	-	-	(60,000)
Gain on sale of McCarty Manor	-	(2,499,209)	-	-	(2,499,209)
Gain on sale to Pine Gardens Holding 3 LLC recorded to net assets					
Decrease (Increase) in:					
Net tenant accounts receivable	1,700	17,091	(440)	-	18,351
Tenant assistance accounts receivable	-	(7,877)	(152)	-	(8,029)
Other accounts receivable	(6,227)	(14,235)	-	-	(20,462)
Due from funds	-	52	(15,838)	15,786	-
Due from owned properties	684	-	-	(684)	-
Due from controlled entities	6,117	(199,812)	-	193,695	-
Prepaid expenses	(16,771)	2,231	1,029	-	(13,511)
Increase (Decrease) in:					
Accounts payable and accrued liabilities	(29,082)	(42,195)	(8,148)	-	(79,425)
Accrued interest payable	(2,595)	(28,665)	2,474	-	(28,786)
Due to funds	-	50,977	(75,447)	24,470	-
Due to owned properties	-	-	69,826	(69,826)	-
Due to controlled entities	-	-	163,441	(163,441)	-
Deferred revenue	(23,580)	(17,703)	627	-	(40,656)
Net Cash Provided by Operating Activities	688,452	506,114	305,322	-	1,499,888
CASH FLOWS FROM INVESTING ACTIVITIES					
Decrease (Increase) in:					
Tenant deposits held in trust	(7,293)	8	-	-	(7,285)
Cash restricted for loan closing	(820,000)	-	-	-	(820,000)
Tax and insurance impounds	-	84,905	16,886	-	101,791
Replacement reserve	(150,000)	795,297	(38,228)	-	607,069
Other reserves	-	609,513	(81,343)	-	528,170
Residual receipts reserve	-	205,920	38,476	-	244,396
Cash restricted for pension plan	(13)	-	-	-	(13)
Cash restricted for self-insurance plan	(4,979)	-	-	-	(4,979)
Purchase of fixed assets	(21,757)	(13,450)	-	-	(35,207)
Decrease (Increase) in due from related parties	(12,836)	-	-	-	(12,836)
Increase in long-term notes receivable	71,986	-	-	-	71,986
Developer notes receivable	(444,594)	-	-	-	(444,594)
Transfer of proceeds from sale of McCarty Manor	1,700,410	(1,700,410)	-	-	-
Transfer of proceeds from sale of projects from owned to controlled	2,404,223	(2,404,223)	-	-	-
Advance to nonconsolidated affiliates	150,000	-	-	-	150,000
Proceeds from sale to Pine Gardens Holding 3, Inc.	-	2,917,000	-	-	2,917,000
Proceeds from sale of McCarty Manor	-	2,714,195	-	-	2,714,195
Development costs	(322,554)	(226)	-	-	(322,780)
Net Cash Provided by (Used in) Investing Activities	2,542,593	3,208,529	(64,209)	-	5,686,913

See Independent Auditors' Report.

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
CONSOLIDATING SCHEDULE of CASH FLOWS – Continued
Year ended October 31, 2012

CASH FLOWS FROM FINANCING ACTIVITIES

	<u>Funds</u>	<u>Owned Projects</u>	<u>Controlled Entities</u>	<u>Consolidating Entries</u>	<u>Total</u>
Proceeds from mortgages and notes payable	\$ 2,292	\$ -	\$ -	\$ -	\$ 2,292
Proceeds from grant liens	8,087	-	-	-	8,087
Increase (Decrease) in due to related parties	(258,960)	(50,305)	(10,100)	-	(319,365)
Principal payments on mortgages and notes payable	<u>(223,937)</u>	<u>(3,887,885)</u>	<u>(158,922)</u>	<u>-</u>	<u>(4,270,744)</u>
Net Cash Provided by (Used in) Financing Activities	<u>(472,518)</u>	<u>(3,938,190)</u>	<u>(169,022)</u>	<u>-</u>	<u>(4,579,730)</u>
Net Increase (Decrease) in Cash and Cash Equivalents	2,758,527	(223,547)	72,091	-	2,607,071
Cash and Cash Equivalents, Beginning	<u>705,664</u>	<u>530,255</u>	<u>134,808</u>	<u>-</u>	<u>1,370,727</u>
Cash and Cash Equivalents, Ending	<u>\$ 3,464,191</u>	<u>\$ 306,708</u>	<u>\$ 206,899</u>	<u>\$ -</u>	<u>\$ 3,977,798</u>

SUPPLEMENTAL DISCLOSURES

Amounts Paid for Interest	<u>\$ 31,427</u>	<u>\$ 742,886</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 774,313</u>
Amounts Paid for Income Tax	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>

NON CASH INVESTING AND FINANCING ACTIVITIES

Capitalized accrued interest payable	<u>\$ 101,487</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 101,487</u>
McCarty Manor - transfer of note receivable to Fund 21	<u>\$ 725,805</u>	<u>\$ (725,805)</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>
Sale of three projects from owned to controlled transfer of fixed assets for notes receivable	<u>\$ 4,153,000</u>	<u>\$ (4,153,000)</u>	<u>\$ 4,153,000</u>	<u>\$ (4,153,000)</u>	<u>\$ -</u>
Sale of three projects fixed assets from owned to controlled transfer of fixed assets	<u>\$ -</u>	<u>\$ (5,736,299)</u>	<u>\$ 5,736,299</u>	<u>\$ -</u>	<u>\$ -</u>
Acquisition by Pine Gardens Holding 3 LLC of fixed assets with debt	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 5,302,500</u>	<u>\$ -</u>	<u>\$ 5,302,500</u>

See Independent Auditors' Report.

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
CONSOLIDATING FUND SCHEDULE OF FINANCIAL POSITION
October 31, 2012

ASSETS	Funds						Consolidating Entries	Totals	
	10	20	21	22	23	70			90
Current Assets:									
Cash and cash equivalents	\$ -	\$ 4,902	\$ 2,752,690	\$ 706,599	\$ -	\$ -	\$ -	\$ 3,464,191	
Other accounts receivable	-	12,061	-	-	-	-	-	12,061	
Due from funds	-	15,282	2,066,856	1,392,788	-	-	(3,474,926)	-	
Due from owned projects	20,000	33,030	378,107	378,107	-	-	-	440,591	
Due from controlled entities	48,008	111,211	31,110	6,389	-	-	-	196,718	
Due from related parties	-	32,703	930,704	17,516	-	-	-	980,923	
Prepaid expenses	10,688	21,606	3,538	1,969	-	14,003	-	51,804	
Total Current Assets	78,696	230,795	6,163,005	2,134,715	-	14,003	(3,474,926)	5,146,288	
Deposits:									
Amounts held for self-help families	-	-	-	-	-	-	1,300	1,300	
Escrow deposit for loan closing	-	-	820,000	-	-	-	-	820,000	
Replacement reserves	-	150,000	-	-	-	-	-	150,000	
Cash restricted for pension plan	13,683	-	-	-	-	-	-	13,683	
Cash restricted for self-insurance plan	53,098	-	-	-	-	-	-	53,098	
Total Deposits	66,781	150,000	820,000	-	-	-	1,300	1,038,081	
Fixed Assets, net of Accumulated Depreciation	774,119	-	-	-	-	-	-	774,119	
Other Assets:									
Long-term notes receivable	138,987	-	1,560,977	-	-	-	-	1,699,964	
Developer notes receivable	-	-	1,063,446	-	-	-	-	1,063,446	
Advance to consolidated affiliates	128,000	-	-	-	-	-	-	128,000	
Notes receivable from consolidated affiliates	-	0	4,153,000	-	-	-	-	4,153,000	
Advance to nonconsolidated affiliate	169,200	-	-	-	-	-	-	169,200	
Land held for development	-	-	2,194,449	-	-	-	-	2,194,449	
Development costs	-	-	5,174,032	-	-	-	-	5,174,032	
Total Other Assets	436,187	-	14,145,904	-	-	-	-	14,582,091	
Total Assets	\$ 1,355,783	\$ 380,795	\$ 21,128,909	\$ 2,134,715	\$ -	\$ 14,003	\$ 1,300	\$ (3,474,926)	\$ 21,540,579
LIABILITIES & NET ASSETS (DEFICIT)									
Current Liabilities:									
Accounts payable and accrued liabilities	\$ 74,414	183,915	165,452	\$ 20,048	\$ 715	\$ 9,281	\$ -	\$ 453,825	
Due to funds	49,332	2,594,833	1,451	8,451	219,091	601,458	-	(3,474,616)	
Due to owned properties	-	-	-	52	-	-	-	52	
Due to controlled entities	-	-	310	-	-	-	(310)	-	
Current portion mortgages and notes payable	10,267	-	1,051,700	-	-	-	-	1,061,967	
Deferred revenue	2,587	-	20,000	-	-	-	-	22,587	
Total Current Liabilities	136,600	2,778,748	1,238,913	28,551	219,806	610,739	-	(3,474,926)	1,538,431
Long-Term Liabilities									
Amounts held for self-help families	-	-	-	-	-	-	1,300	1,300	
Accrued interest payable	-	-	580,203	-	-	-	-	580,203	
Mortgages and notes payable	678,808	-	3,631,895	-	-	-	-	4,310,703	
Total Long-Term Liabilities	678,808	-	4,212,098	-	-	-	1,300	4,892,206	
Total Liabilities	815,408	2,778,748	5,451,011	28,551	219,806	610,739	1,300	(3,474,926)	6,430,637
Net Assets (Deficit):									
Unrestricted	345,575	(2,397,953)	11,134,033	2,106,164	(219,806)	(596,736)	-	10,371,277	
Temporarily restricted	-	-	3,129,793	-	-	-	-	3,129,793	
Permanently restricted	194,800	-	1,414,072	-	-	-	-	1,608,872	
Total Net Assets (Deficit)	540,375	(2,397,953)	15,677,898	2,106,164	(219,806)	(596,736)	-	15,109,942	
Total Liabilities & Net Assets (Deficit)	\$ 1,355,783	\$ 380,795	\$ 21,128,909	\$ 2,134,715	\$ -	\$ 14,003	\$ 1,300	\$ (3,474,926)	\$ 21,540,579

See Independent Auditors' Report.

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
CONSOLIDATING FUND SCHEDULE of ACTIVITIES and CHANGES in NET ASSETS (DEFICIT)
Year ended October 31, 2012

REVENUES	Funds						Consolidating Entries	Totals
	10	20	21	22	23	70		
Other rents	\$ -	104,249	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 104,249
Grant income	-	212,620	113,875	-	-	83,000	-	409,495
Interest income	-	19,360	12,742	-	-	-	-	32,102
Management fees and reimbursements	-	49,932	-	709,209	-	-	-	759,141
Operational revenue	-	74,954	718,813	-	690	-	-	794,457
Gain on sale of development properties	-	0	-	-	-	-	-	-
Other revenue	-	4,348	63	120	-	500	-	5,031
Total Revenues	-	465,463	845,493	709,329	690	83,500	-	2,104,475
EXPENSES								
Administrative services	-	524,697	111,126	213,056	3,296	47,926	-	900,101
Utilities	-	27,492	-	-	-	-	-	27,492
Operating & Maintenance								
Operating expenses	-	57,667	1,574	261	750	60,499	-	120,751
Taxes & Insurance	-	128,842	33,192	50,229	876	60,665	-	273,804
Interest expense	67,775	39,780	11,272	-	-	-	-	118,827
Unrealized loss on land development & notes receivable	-	-	1,152,886	-	-	-	-	1,152,886
Depreciation	37,509	-	-	-	-	-	-	37,509
Total Expenses	105,284	778,478	1,310,050	263,546	4,922	169,090	-	2,631,370
Change in Net Assets (Deficit)	(105,284)	(313,015)	(464,557)	445,783	(4,232)	(85,590)	-	(526,895)
McCarty Manor sale to third party - transfer of cash from owned to funds	-	-	1,700,410	-	-	-	-	1,700,410
McCarty Manor sale to third party - transfer of seller note receivable from owned to funds	-	-	725,805	-	-	-	-	725,805
Transfer from owned projects notes receivable from sale of projects to Pine Gardens Holding 3 LLC	-	-	4,153,000	-	-	-	-	4,153,000
Pine Gardens Holding LLC cash from sale transferred from owned to funds	-	-	2,404,223	-	-	-	-	2,404,223
New grant liens during year, net of forgiven grant liens for temporarily restricted net assets	-	-	8,087	-	-	-	-	8,087
Net Asset (Deficit), Beginning	645,659	(2,084,938)	7,150,930	1,660,381	(215,574)	(511,146)	-	6,645,312
Net Assets (Deficit), Ending	\$ 540,375	\$ (2,397,953)	\$ 15,677,898	\$ 2,106,164	\$ (219,806)	\$ (596,736)	\$ -	\$ 15,109,942

See Independent Auditors' Report.

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
CONSOLIDATING FUND SCHEDULE of CASH FLOWS
Year ended October 31, 2012

CASH FLOWS FROM OPERATING ACTIVITIES	Funds						Consolidating Entries	Totals
	10	20	21	22	23	70		
Change in Total Net Assets from Operations	\$ (105,284)	\$ (313,015)	\$ (464,557)	\$ 445,783	\$ (4,232)	\$ (85,590)	\$ -	\$ (526,895)
Adjustments to Reconcile Changes in Net Asset to Net cash Provided by (Used in) Operating Activities:								
Net present value of notes receivable	65,525	-	(12,306)	-	-	-	-	53,219
Increase in long-term accrued interest	-	-	101,487	-	-	-	-	101,487
Depreciation and amortization	37,509	-	-	-	-	-	-	37,509
Unrealized loss on land development & notes receivable	-	-	1,152,886	-	-	-	-	1,152,886
Allowance for doubtful accounts	-	-	(60,000)	-	-	-	-	(60,000)
Decrease (Increase) in:								
Net tenant accounts receivable	-	1,700	-	-	-	-	-	1,700
Other accounts receivable	-	(6,227)	-	-	-	-	-	(6,227)
Due from funds	-	958	(364,626)	11,468	-	-	352,200	-
Due from owned projects	-	1,070	-	(386)	-	-	-	684
Due from controlled entities	5,622	(13,041)	-	13,536	-	-	-	6,117
Prepaid expenses	(10,688)	(8,448)	1,108	(1,290)	60	2,487	-	(16,771)
Increase (Decrease) in:								
Accounts payable and accrued liabilities	27,389	50,869	(107,071)	(712)	20	423	-	(29,082)
Accrued interest payable	-	(2,595)	-	-	-	-	-	(2,595)
Due to funds	(179,281)	443,295	(2,534)	3,578	4,152	82,680	(351,890)	-
Due to controlled entities	-	-	310	-	-	-	(310)	-
Deferred revenue	250	-	(23,830)	-	-	-	-	(23,580)
Net Cash Provided by (Used in) Operating Activities	(158,958)	154,566	220,867	471,977	-	-	-	688,452
CASH FLOWS FROM INVESTING ACTIVITIES								
Decrease (Increase) in:								
Tenant deposits held in trust	(7,293)	-	-	-	-	-	-	(7,293)
Cash restricted for loan closing	-	-	(820,000)	-	-	-	-	(820,000)
Replacement reserves	-	(150,000)	-	-	-	-	-	(150,000)
Cash restricted for pension plan	(13)	-	-	-	-	-	-	(13)
Cash restricted for self-insurance plan	(4,979)	-	-	-	-	-	-	(4,979)
Purchase of fixed assets	(21,757)	-	-	-	-	-	-	(21,757)
Decrease (Increase) in due from related parties	-	(4,368)	-	(8,468)	-	-	-	(12,836)
Long-term notes receivable	43,000	-	28,986	-	-	-	-	71,986
Developer notes receivable	-	-	(444,594)	-	-	-	-	(444,594)
Transfer of proceeds from sale to Pine Gardens Holding 3, Inc.	-	-	1,700,410	-	-	-	-	1,700,410
Transfer of proceeds from sale of projects from owned to controlled	-	-	2,404,223	-	-	-	-	2,404,223
Advance to nonconsolidated affiliates	150,000	-	-	-	-	-	-	150,000
Development costs	-	-	(322,554)	-	-	-	-	(322,554)
Net Cash Provided by (Used in) Investing Activities	158,958	(154,368)	2,546,471	(8,468)	-	-	-	2,542,593
CASH FLOWS FROM FINANCING ACTIVITIES								
Proceeds from mortgages and notes payable	-	-	2,292	-	-	-	-	2,292
Proceeds from grant liens	-	-	8,087	-	-	-	-	8,087
Increase (Decrease) in due to related parties	-	-	(258,960)	-	-	-	-	(258,960)
Principal payments on mortgages, notes payable and grant liens	-	-	(223,937)	-	-	-	-	(223,937)
Net Cash Provided by (Used in) Financing Activities	-	-	(472,518)	-	-	-	-	(472,518)
Net Increase (Decrease) in Cash and Cash Equivalents	-	198	2,294,820	463,509	-	-	-	2,758,527
Cash and Cash Equivalents, Beginning	-	4,704	457,870	243,090	-	-	-	705,664
Cash and Cash Equivalents, Ending	\$ -	\$ 4,902	\$ 2,752,690	\$ 706,599	\$ -	\$ -	\$ -	\$ 3,464,191
SUPPLEMENTAL DISCLOSURES								
Amounts Paid for Interest	\$ -	\$ 30,371	\$ 1,056	\$ -	\$ -	\$ -	\$ -	\$ 31,427
Amounts Paid for Income Tax	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
NON CASH INVESTING AND FINANCING ACTIVITIES								
Capitalized accrued interest payable	\$ -	\$ -	\$ 101,487	\$ -	\$ -	\$ -	\$ -	\$ 101,487
McCarty Manor - transfer of note receivable to Fund 21	\$ -	\$ -	\$ 725,805	\$ -	\$ -	\$ -	\$ -	\$ 725,805

See Independent Auditors' Report.

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
SCHEDULE of EXPENDITURES of FEDERAL AWARDS
Year ended October 31, 2012

Federal Programs:		Funds	Owned Projects	Controlled Entities	Total
U.S Department of Agriculture:					
Farm Labor Housing Loans and Grants	10.405	\$ -	\$ 3,506,873	\$ -	\$ 3,506,873
Rural Rental Housing Loans (Section 515 and 521)	10.415	-	2,062,586	1,722,409	3,784,995
Rural Self-Help Housing Technical Assistance (Section 523)	10.420	23,000	-	-	23,000
Rural Rental Assistance Payments	10.427	-	305,853	5,679	311,532
Community Facilities Loans and Grants	10.766	<u>689,075</u>	<u>-</u>	<u>-</u>	<u>689,075</u>
Total U.S Department of Agriculture		<u>712,075</u>	<u>5,875,312</u>	<u>1,728,088</u>	<u>8,315,475</u>
U.S. Department of Housing and Urban Development:					
Mortgage Insurance For The Purchase or Refinancing of Existing Multifamily Housing Projects (Section 223(f)/207)	14.155	-	-	87,335	87,335
Supportive Housing For the Elderly (Section 202)	14.157	-	1,058,535	9,224,299	10,282,834
Supportive Housing for Person with Disabilities (Section 811)	14.181	-	-	752,400	752,400
Section 8 Housing Assistance Payments Program (Pass-Through Contract Administrator)	14.195	-	1,749,984	1,161,135	2,911,119
Home Investment Partnership Program (HOME) (Pass-Through California Department of Housing & Community Dev)	14.239	126,192	4,767,779	4,213,671	9,107,642
Self Help Homeownership Opportunity Program	14.247	472,888	-	-	472,888
Section 4 Capacity Building for Community Development and Affordable Housing	14.252	<u>15,620</u>	<u>-</u>	<u>-</u>	<u>15,620</u>
Total U.S. Department of Housing and Urban Development		<u>614,700</u>	<u>7,576,298</u>	<u>15,438,840</u>	<u>23,629,838</u>
NeighborWorks America:					
Expendable Grants	21.000	297,000	-	-	297,000
Capital Loan	21.000	<u>500,000</u>	<u>-</u>	<u>-</u>	<u>500,000</u>
Total NeighborWorks America		<u>797,000</u>	<u>-</u>	<u>-</u>	<u>797,000</u>
TOTAL FEDERAL AWARDS EXPENDED		<u>\$ 2,123,775</u>	<u>\$ 13,451,610</u>	<u>\$ 17,166,928</u>	<u>\$ 32,742,313</u>

Note 1. Basis of Presentation

The accompanying Schedule of Expenditures of Federal Awards includes the federal grant activity of Rural Communities Housing Development Corporation and its affiliates and is presented 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*. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of the basic consolidated financial statements.

See Independent Auditors' Report.

**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 of
Rural Communities Housing Development Corporation
Ukiah, California

We have audited the consolidated financial statements of Rural Communities Housing Development Corporation and Affiliates as of and for the year ended October 31, 2012, and have issued our report thereon dated April 29, 2013. 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 Rural Communities Housing Development Corporation and Affiliates internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the consolidated financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Corporation's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Corporation'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.

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Compliance and Other Matters

As part of obtaining reasonable assurance about whether Rural Communities Housing Development Corporation and Affiliates' consolidated 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 statements 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 an instance of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in the accompanying Schedule of Audit Findings and Questioned Costs as item 2012-1.

We noted certain other matters that we reported to management of Rural Communities Housing Development Corporation in a letter dated April 29, 2013.

Rural Communities Housing Development Corporation's response to the findings identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. We did not audit Rural Communities Housing Corporation's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of management, the board of directors, the audit committee, others within the Corporation, the United States Department of Agriculture, Rural Development, and the United States Department of Housing and Urban Development and is not intended to be and should not be used by anyone other than these specified parties.

Clark, Schaefer, Hackett & Co.

Columbus, Ohio
April 29, 2013

**Independent Auditors' Report on Compliance with Requirements that Could
Have a Direct and Material Effect on Each Major Program and on Internal
Control over Compliance in Accordance with OMB Circular A-133**

To the Board of Directors of
Rural Communities Housing Development Corporation
Ukiah, California

Compliance

We have audited Rural Communities Housing Development Corporation and Affiliates' 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 Rural Communities Housing Development Corporation and Affiliates' major federal programs for the year ended October 31, 2012. Rural Communities Housing Development Corporation's major federal programs are identified in the Summary of Audit Results section of the accompanying Schedule of Audit Findings and Questioned Costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to its major federal programs is the responsibility of the Corporation's management. Our responsibility is to express an opinion on Rural Communities Housing Development Corporation and Affiliates' 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 the 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 Rural Communities Housing Development Corporation and Affiliates' 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 on Rural Communities Housing Development Corporation and Affiliates' compliance with those requirements.

In our opinion, Rural Communities Housing Development Corporation and Affiliates 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 October 31, 2012.

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Internal Control Over Compliance

Management of Rural Communities Housing Development Corporation and Affiliates are responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered Rural Communities Housing Development Corporation and Affiliates' internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our 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 purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of Rural Communities Housing Development Corporation and Affiliates' 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.

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 that we consider to be material weaknesses, as defined above.

This report is intended solely for the information and use of management, the board of directors, the audit committee, others within the Corporation, the United States Department of Agriculture, Rural Development, and the United States Department of Housing and Urban Development and is not intended to be and should not be used by anyone other than these specified parties.

Clark, Schaefer, Hackett & Co.

Columbus, Ohio
April 29, 2013

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
 SCHEDULE OF AUDIT FINDINGS AND QUESTIONED COSTS
 Year ended October 31, 2012

SECTION I - SUMMARY OF AUDITOR'S RESULTS

Financial Statements

Type of auditor's report issued:	<u>unqualified</u>		
Internal control over financial reporting:			
Material weakness identified?	<u> </u> Yes	<u> </u> X	<u> </u> No
Control deficiency identified not considered to be material weaknesses?	<u> </u> Yes	<u> </u> X	<u> </u> None
Noncompliance material to financial statements noted?	<u> </u> Yes	<u> </u> X	<u> </u> None

Federal Awards

Type of auditor's report issued on compliance for major programs:	<u>unqualified</u>		
Internal control over financial reporting:			
Material weakness identified?	<u> </u> Yes	<u> </u> X	<u> </u> No
Control deficiency identified not considered to be material weaknesses?	<u> </u> Yes	<u> </u> X	<u> </u> None
Any audit findings disclosed that are required to be reported in accordance with Circular A-133, Section .510(a)	<u> </u> X	<u> </u> Yes	<u> </u> None

Identification of major program

<u>CFDA Number</u>	<u>Name of Federal Program or Cluster</u>
<u>10.405</u>	<u>Farm Labor Housing Loans and Grants</u>
<u>14.157</u>	<u>Supportive Housing For the Elderly</u>
<u>14.239</u>	<u>Home Investment Partnerships Program (HOME)</u>

Dollar threshold used to distinguish between Type A and Type B programs:	<u>\$982,269</u>		
Auditee qualified as low-risk auditee?	<u> </u> Yes	<u> </u> X	<u> </u> No

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
SCHEDULE OF AUDIT FINDINGS AND QUESTIONED COSTS - Continued
Year ended October 31, 2012

SECTION II - FINANCIAL STATEMENT FINDINGS

There were no findings or questioned costs relative to the financial statements.

SECTION III FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

Failure to Fund the Replacement Reserve – Redwood Court Property, a California Limited Partnership

2012-1

Condition

Redwood Court Property, a controlled entity, failed to set aside the required Reserve for Replacement for the year ended December 31, 2012.

Effect

The Replacement Reserve Bank Account was underfunded by \$17,419 pursuant to the RD Regulatory Agreement.

Cause

Due to the excessive vacancies of the Project, cash flow from operations was inadequate to set aside the required Reserve for Replacement funds during the year ended December 31, 2012.

Criteria

The Regulatory Agreement from RD, require that a predetermined amount of Reserve for Replacement be transferred from operations on a monthly basis and deposited into a properly designated Replacement Reserve Bank Account.

Recommendation

Increase monthly funding of the reserve in accordance with its workout agreement with RD.

Redwood Court Property, a California Limited Partnership Project Response and Action Plan

Although Redwood Court Property, a California Limited Partnership did not generate sufficient cash flow from operations to fully fund certain of their funding requirements to its Replacement Reserve, the Project is continuing to comply with a workout agreement with RD to restore the Replacement Reserve account to the required balance.

RURAL COMMUNITIES HOUSING DEVELOPMENT CORPORATION
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
Year ended October 31, 2012

<u>Finding / Recommendation</u>	<u>Current Status</u>	<u>Project Explanation If Not Implemented</u>
<p>Oak Hill Apartments failed to set aside the full amount of required Reserve for Replacement funds into a separate Replacement Reserve Bank Account for the fiscal year ended October 31, 2011. The Replacement Reserve Bank Account should be funded with \$145,987 as soon as possible. As a possible alternative, the Project's Owner may negotiate written waivers from Rural Development and HCD-HOME.</p>	Resolved	<p>RCHDC funded \$150,000 in a separate cash account designated as Oak Hills replacement reserve</p>
<p>Redwood Court Property failed to set aside the full amount of required Reserve for Replacement funds into a separate Replacement Reserve Bank Account for the fiscal year ended December 31, 2010. The Replacement Reserve Bank Account should be funded with \$19,336 as soon as possible. As a possible alternative, the Project's Owner may negotiate written waivers from Rural Development.</p>	Repeated	<p>See recommendation 2012-1</p>



At Clark Schaefer Hackett, we are the sum of our individuals. Each team member's training, experience and drive is well-suited to each client's needs and goals. We are committed to providing insightful and flexible service – from efficient compliance to sophisticated consulting – to help each client prosper today and plan for future success.