

**NATIONAL COMMUNITY
INVESTMENT FUND**
Chicago, Illinois

FINANCIAL STATEMENTS
December 31, 2003 and 2002

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Crowe Chizek and Company LLC
Member Horwath International

REPORT OF INDEPENDENT AUDITORS

To the Board of Trustees
National Community Investment Fund
Chicago, Illinois

We have audited the accompanying statements of financial position of National Community Investment Fund as of December 31, 2003 and 2002, and the related statements of activities and cash flows for the years then ended. These financial statements are the responsibility of the Trustees of National Community Investment Fund. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. 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 examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of National Community Investment Fund as of December 31, 2003 and 2002, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Crowe Chizek and Company LLC

Crowe Chizek and Company LLC

Chicago, Illinois
April 20, 2004

NATIONAL COMMUNITY INVESTMENT FUND
 STATEMENTS OF FINANCIAL POSITION
 December 31, 2003 and 2002

	<u>2003</u>	<u>2002</u>
ASSETS		
Current assets		
Cash and cash equivalents	\$ 2,402,726	\$ 2,565,814
Interest receivable	138,445	177,459
Accounts receivable	69,550	15,000
Unconditional promises to give (Note 9)	1,640,000	405,000
Prepaid expenses	<u>19,000</u>	<u>18,984</u>
Total current assets	4,269,721	3,182,257
Securities (Note 3)	6,996,398	4,306,891
Loans receivable (net of allowance for loan losses of \$208,043 in 2003 and \$387,032 in 2002)	7,098,059	9,284,624
Interest receivable - long-term	141,253	114,944
Equity investments in Community Development Financial Institutions (CDFIs)	<u>7,982,207</u>	<u>6,658,961</u>
	<u>\$ 26,487,638</u>	<u>\$ 23,547,677</u>
LIABILITIES AND NET ASSETS		
Current liabilities		
Accounts payable and accrued expenses	\$ 56,418	\$ 49,594
Due to fund advisor (Note 5)	<u>149,921</u>	<u>74,634</u>
Total current liabilities	206,339	124,228
Notes payable - contractual principal	22,000,000	22,000,000
Discount for below-market rates	<u>(3,606,145)</u>	<u>(4,805,065)</u>
Notes payable, net of discount (Note 4)	18,393,855	17,194,935
Accrued incentives on unrealized gains in equity investments in CDFIs	699,256	-
Net assets		
Unrestricted	(99,528)	(900,008)
Temporarily restricted	5,898,525	5,749,042
Permanently restricted	<u>1,389,191</u>	<u>1,379,480</u>
Total net assets	<u>7,188,188</u>	<u>6,228,514</u>
	<u>\$ 26,487,638</u>	<u>\$ 23,547,677</u>

See accompanying notes to financial statements.

NATIONAL COMMUNITY INVESTMENT FUND
STATEMENTS OF ACTIVITIES
Years ended December 31, 2003 and 2002

	<u>2003</u>	<u>2002</u>
Revenues		
Interest and dividend income	\$ 946,087	\$ 939,717
Conference sponsorships	33,846	18,150
Grant income	40,142	116,400
Net assets released from restrictions	<u>1,574,564</u>	<u>1,520,546</u>
Total revenues	2,594,639	2,594,813
Expenses, primarily program-related		
Advisory base fee (Note 5)	348,750	465,000
Advisory staff fees and expenses (Note 5)	589,917	566,465
Trustee's fees	22,500	31,875
Travel	62,911	95,841
Professional services	126,050	111,440
Conference sponsorships	36,492	45,096
Interest - contractual	220,556	220,556
Interest - amortization of discount	1,198,920	1,107,031
Insurance	39,828	38,284
Provision for loan losses (recovery)	(178,989)	165,646
Other	<u>40,810</u>	<u>58,864</u>
Total expenses	<u>2,507,745</u>	<u>2,906,098</u>
Change in net assets before gain on securities	86,894	(311,285)
Gains on equity CDFI investments, net of lender and advisor incentives	760,835	-
Gain (loss) on securities	<u>(47,249)</u>	<u>14,216</u>
Change in unrestricted net assets	800,480	(297,069)
Temporarily restricted net assets		
Contribution income	1,715,000	1,195,000
Interest income	9,047	2,283
Net assets released from restriction	<u>(1,574,564)</u>	<u>(1,520,546)</u>
Change in temporarily restricted net assets	149,483	(323,263)
Permanently restricted net assets		
Interest income	9,711	14,856
Gain (loss) on securities	<u>-</u>	<u>(812)</u>
Change in permanently restricted net assets	<u>9,711</u>	<u>14,044</u>
Total change in net assets	959,674	(606,288)
Net assets at beginning of year	<u>6,228,514</u>	<u>6,834,802</u>
Net assets at end of year	<u><u>\$ 7,188,188</u></u>	<u><u>\$ 6,228,514</u></u>

See accompanying notes to financial statements.

NATIONAL COMMUNITY INVESTMENT FUND
STATEMENTS OF CASH FLOWS
Years ended December 31, 2003 and 2002

	<u>2003</u>	<u>2002</u>
Cash flows from operating activities		
Change in net assets	\$ 959,674	\$ (606,288)
Adjustments to reconcile change in net assets to cash from operating activities		
Provision for loan losses (recovery)	(178,989)	165,646
Discount amortization on below market interest rate loans	1,198,920	1,107,031
Amortization of securities discounts, net of premiums	1,330	34
Net unrealized gains on securities	47,249	(13,404)
Net gain on equity investments in CDFIs	(760,835)	-
Changes in assets and liabilities		
Interest receivable	12,705	(42,997)
Accounts receivable	(54,550)	(15,000)
Prepaid expenses	(16)	(1,518)
Unconditional promises to give	(1,235,000)	(405,000)
Accounts payable and accrued expenses	(33,131)	37,674
Due to fund advisor	<u>75,287</u>	<u>(48,917)</u>
Net cash from operating activities	32,644	177,261
 Cash flows from investing activities		
Loans to CDFIs	2,365,554	(1,022,898)
Equity investments in CDFIs	176,800	(1,316,090)
Redemptions (purchases) of certificates of deposit	14,879	783,186
Purchases of securities	(4,726,887)	(2,399,140)
Proceeds from paydowns on securities	274,013	313,174
Proceeds from maturities of securities	<u>1,699,909</u>	<u>2,900,000</u>
Net cash from investing activities	<u>(195,732)</u>	<u>(741,768)</u>
 Decrease in cash and cash equivalents	(163,088)	(564,507)
 Cash and cash equivalents at beginning of year	<u>2,565,814</u>	<u>3,130,321</u>
 Cash and cash equivalents at end of year	<u>\$ 2,402,726</u>	<u>\$ 2,565,814</u>
 Supplemental disclosures of cash flow information		
Cash paid during the year for interest	\$ 220,556	\$ 220,556

See accompanying notes to financial statements.

NATIONAL COMMUNITY INVESTMENT FUND
NOTES TO FINANCIAL STATEMENTS
December 31, 2003 and 2002

NOTE 1 - ORGANIZATION

The National Community Investment Fund (referred to as "NCIF" or "the Fund"), an independent trust, was founded in December 1995. NCIF's mission is to increase the number and capacity of domestic, depository, CDFIs that are both effective agents of local community development in emerging markets and sound financial institutions.

NCIF was created through joint efforts between Bank of America and Shorebank Corporation. Bank of America provided NCIF's initial capital in the form of a \$15 million loan. NCIF raised an additional \$1,250,000 in capital in 1997 in the form of grants for its Seed Fund from the Ford and the John D. and Catherine T. MacArthur Foundations. During 1998, NCIF received a \$4 million loan from MBNA America Bank, NA. During 2000, the Fund received a \$3 million loan from Washington Mutual Community Development, Inc. To expand its geographical territory and investment activity in CDFIs, NCIF is seeking additional capital from bank and other institutional investors. NCIF has retained Shorebank Corporation to advise the Fund on market development, investment recommendations, and general administration.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Accounting: The accompanying financial statements of NCIF have been prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America.

Basis of Presentation: The Fund's net assets are classified into three classes - permanently restricted, temporarily restricted, and unrestricted - according to the existence or absence of donor-imposed restrictions. Unrestricted net assets are not subject to donor-imposed restrictions and principally include interest income, fees for service, and related expenses associated with the core activities of the Fund. Temporarily restricted net assets are subject to donor-imposed restrictions that may or will be met either by actions of the Fund or the passage of time. Permanently restricted net assets are subject to donor-imposed restrictions to be maintained permanently by the Fund; only the income generated from certain grants may be available for operations.

Contributions: Contributions received are recorded as unrestricted, temporarily restricted, or permanently restricted support depending on the existence or nature of any donor restrictions. All contributions are considered to be available for unrestricted use unless specifically restricted by the donor. Amounts received that are designated for future periods or restricted by the donor for specific purposes are reported as temporarily restricted or permanently restricted support that increases those net asset classes. When a temporary restriction expires, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of activities as net assets released from restrictions. Temporarily restricted net assets relate to NCIF's program to expand investments in CDFIs.

(Continued)

NATIONAL COMMUNITY INVESTMENT FUND
NOTES TO FINANCIAL STATEMENTS
December 31, 2003 and 2002

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Estimates: The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires the Fund Advisor to make estimates and assumptions that affect certain reported amounts and disclosures. The Fund's estimated allowance for loan losses is particularly sensitive to change in the near term. Accordingly, actual results could differ from these estimates.

Cash and Cash Equivalents: For the purpose of the statement of cash flows, NCIF considers all highly liquid investments with an initial maturity of three months or less when purchased to be cash equivalents.

Income Tax: NCIF is exempt from federal income taxes as a result of its status as a non-profit organization as described under Section 501(c)(4) of the Internal Revenue Code.

Securities: Securities consist of widely traded U.S. government obligations, U.S. government agency securities, mortgage backed securities, and corporate notes, and are carried at fair value. Changes in the fair value of securities owned at the end of the year are recorded as unrealized net gains (losses). The gains and losses on securities sold during the year are recorded as realized net gains (losses) for the year. Realized and unrealized gains or losses are combined and reflected in the statement of activities as gain (loss) on securities.

Loans: The Fund seeks to lend money to relatively high-risk, growing depository institutions that are generally under \$500 million in assets. The types of loans the Fund provides include working capital loans for expansion, acquisition of existing assets, or creation of affiliated development companies. With the exception of the Seed Fund, the minimum loan amount is \$250,000 and the maximum loan amount is \$2,000,000. Loan maturities are seven to twelve years.

The Fund also operates a Seed Fund that will lend up to \$250,000 in phased performance based credits to banks in the process of organizing or restructuring as CDFIs. Seed Fund loans are disbursed as borrowers reach performance milestones that serve as "go/no go" points for the venture.

Loans are stated at the principal amount outstanding, net of unearned discount and loan origination fees. The accrual of interest is discontinued whenever principal or interest has been in default ninety consecutive days or more, unless the loan is in process of collection as determined by the Trustees. Loan fees and direct loan origination costs are deferred and amortized over the term of the loan as a yield adjustment. However, in 2003 and 2002, these fees were recognized in revenue since they were deemed immaterial.

(Continued)

NATIONAL COMMUNITY INVESTMENT FUND
NOTES TO FINANCIAL STATEMENTS
December 31, 2003 and 2002

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Allowance for Loan Losses: An allowance for loan losses has been established to provide for those loans which may not be repaid in their entirety. The allowance is increased by provisions for loan losses charged to expense and decreased by charge-offs, net of recoveries. Although a loan is charged off by the Trustees when deemed uncollectible, collection efforts continue and future recoveries may occur.

The allowance is maintained by the Trustees at a level considered adequate to cover losses that are deemed possible based on past industry loss experience, general economic conditions, information about specific borrower situations including their financial position, and other factors and estimates which are subject to change over time. Estimating the risk of loss and amount of loss on any loan is necessarily subjective and ultimate losses may vary from current estimates. These estimates are reviewed periodically and, as adjustments become necessary, they are reported in earnings in the periods in which they become known. The Fund has experienced losses totaling \$250,000 in relation to these loans to date.

Loans considered to be impaired are reduced to the present value of expected future cash flows by allocating a portion of the allowance for loan losses to such loans.

Equity Investments in CDFIs: The Fund also makes non-controlling equity investments in CDFIs. Most of these investments are generally not readily marketable and, accordingly, are recorded at historical cost, net of any reductions for permanent declines in value. However, for those few investments which have readily available market prices and trade actively on a public exchange, the carrying cost is market value, net of any incentives payable to the lenders and the Fund Advisor.

Reclassifications: Certain prior year amounts have been reclassified to conform to the current year presentation.

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NATIONAL COMMUNITY INVESTMENT FUND
NOTES TO FINANCIAL STATEMENTS
December 31, 2003 and 2002

NOTE 3 - SECURITIES

Securities are stated at fair value. Cost is adjusted for amortized discount or premium. Cost and fair values as of December 31, 2003 and 2002 are summarized as follows:

	----- December 31, 2003-----	
	Amortized <u>Cost</u>	Fair <u>Value</u>
Mortgage backed securities	\$ 2,595,411	\$ 2,598,652
U.S. government agencies	2,969,566	2,997,451
Corporate securities	526,271	535,125
Certificates of deposit	<u>865,170</u>	<u>865,170</u>
Total	<u>\$ 6,956,418</u>	<u>\$ 6,996,398</u>
	----- December 31, 2002-----	
	Amortized <u>Cost</u>	Fair <u>Value</u>
Mortgage backed securities	\$ 440,195	\$ 465,912
U.S. government agencies	2,899,418	2,960,930
Certificates of deposit	<u>880,049</u>	<u>880,049</u>
Total	<u>\$ 4,219,662</u>	<u>\$ 4,306,891</u>

NOTE 4 - NOTES PAYABLE

Long-term debt consisted of the following:

	<u>2003</u>	<u>2002</u>
1% note, payable to Bank of America, due January 21, 2006; payments of interest only on a quarterly basis, to the extent of NCIF's available cash flow. Interest for any period which exceeds available cash flow is deferred until the next interest period.	\$ 15,000,000	\$ 15,000,000

(Continued)

NATIONAL COMMUNITY INVESTMENT FUND
 NOTES TO FINANCIAL STATEMENTS
 December 31, 2003 and 2002

NOTE 4 - NOTES PAYABLE (Continued)

	<u>2003</u>	<u>2002</u>
1% note, payable to MBNA America Bank, due January 21, 2006; payments of interest only on a quarterly basis, to the extent of NCIF's available cash flow. Interest for any period which exceeds available cash flow is deferred until the next interest period.	\$ 4,000,000	\$ 4,000,000
1% note, payable to Washington Mutual Community Development Inc., due May 1, 2010; payments of interest only on a quarterly basis, to the extent of NCIF's available cash flow. Interest for any period which exceeds available cash flow is deferred until the next interest period.	3,000,000 <u>22,000,000</u>	3,000,000 <u>22,000,000</u>
Discount for imputed interest on below market interest loans; see (1) below.	<u>(3,606,145)</u>	<u>(4,805,065)</u>
	<u>\$ 18,393,855</u>	<u>\$ 17,194,935</u>

(1) An 8% interest on below market interest loans is imputed and included in temporarily restricted contribution revenue in the year the loan is issued. The discount represents the cumulative amount of net revenue that has been recognized due to below market interest loans. Each year as the interest expense is recognized, the discount amount decreases.

NOTE 5 - TRANSACTIONS WITH FUND ADVISOR

Fees paid to fund advisor for services including advisory, investment management and consulting are as follows:

	<u>2003</u>	<u>2002</u>
Shorebank Corporation	\$ 351,125	\$ 475,188
ShoreBank	11,974	25,798
Shorebank Advisory Services	<u>459,307</u>	<u>540,667</u>
	<u>\$ 822,406</u>	<u>\$1,041,653</u>

Amounts due to fund advisor were \$149,921 and \$74,634 at December 31, 2003 and 2002.

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NATIONAL COMMUNITY INVESTMENT FUND
NOTES TO FINANCIAL STATEMENTS
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NOTE 6 - CONCENTRATION OF CREDIT RISK

NCIF maintains cash balances in excess of insurable limits at one financial institution. As of December 31, 2003 and 2002, NCIF's uninsured cash balances totaled \$2,302,726 and \$2,465,814.

NOTE 7 - COMMITMENTS

At December 31, 2003, NCIF had outstanding commitments of approximately \$15,300 to loan funds to certain CDFIs.

NOTE 8 - FUNCTIONAL EXPENSES

The statement of activities includes the following functional expense categories:

	<u>2003</u>	<u>2002</u>
Program expenses	\$ 2,333,432	\$ 2,583,127
Fundraising	31,181	17,621
General and administrative expenses	<u>322,121</u>	<u>305,350</u>
	<u>\$ 2,686,734</u>	<u>\$ 2,906,098</u>

NOTE 9 - UNCONDITIONAL PROMISES TO GIVE

Unconditional promises to give were \$1,640,000 and \$405,000 at December 31, 2003 and 2002. All unconditional promises are expected to be received within one year of December 31, 2003 and are, therefore, not discounted.

NOTE 10 - ALLOWANCE FOR LOAN LOSSES

Changes in the allowance for loan losses are as follows:

	<u>2003</u>	<u>2002</u>
Balance at beginning of year	\$ 387,032	\$ 221,386
Provision for loan losses (recovery)	<u>(178,989)</u>	<u>165,646</u>
Balance at end of year	<u>\$ 208,043</u>	<u>\$ 387,032</u>

(Continued)

NATIONAL COMMUNITY INVESTMENT FUND
NOTES TO FINANCIAL STATEMENTS
December 31, 2003 and 2002

NOTE 11 - ACCRUED INCENTIVES ON CDFI INVESTMENTS AVAILABLE FOR SALE

The Fund's lenders and advisor participate in realized gains on sale of equity investments in CDFI's. During 2003, the Fund sold certain common shares, which resulted in a realized gain of \$80,525. The lenders received additional interest expense of \$23,734 from this gain and the Fund Advisor is owed \$16,222 as its incentive.

As of December 31, 2003, there was an unrealized gain of \$1,419,522 on the Fund's equity investments in CDFIs. Since the unrealized gain has been recognized in the financial statements, the Fund accrued the total incentive of \$699,256 that would have to be paid to the lenders and Fund Advisor, had these investments been sold.