

**THE SUSTAINABLE ENERGY FUND OF
CENTRAL EASTERN PA
(A Not-for Profit Corporation)**

Financial Statements and Auditors' Report

June 30, 2003

CAMPBELL, RAPPOLD & YURASITS LLP
Certified Public Accountants
1033 SOUTH CEDAR CREST BOULEVARD
ALLENTOWN, PA 18103

**THE SUSTAINABLE ENERGY FUND OF CENTRAL EASTERN PA
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INDEPENDENT AUDITORS' REPORT

Board of Directors
The Sustainable Energy Fund Central Eastern PA
Allentown, PA

We have audited the accompanying statement of financial position of The Sustainable Energy Fund of Central Eastern PA (A Not-for-Profit Corporation) as of June 30, 2003 and 2002 and the related statements of activities and cash flows for the year then ended. These financial statements are the responsibility of the Fund'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. 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 audit provides 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 The Sustainable Energy Fund of Central Eastern PA as of June 30, 2003 and 2002, and the results of its operations and changes in net assets for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Campbell, Rappold & Yurasits LLP

Certified Public Accountants

September 8, 2004

**THE SUSTAINABLE ENERGY FUND OF CENTRAL EASTERN PA
(A Not-for Profit Corporation)**

STATEMENTS OF FINANCIAL POSITION

	June 30	
	2003	2002
<u>ASSETS:</u>		
Cash and Cash Equivalents	\$ 2,606,347	\$1,066,685
Ratepayer's Contribution Receivable	260,171	292,833
Grant Receivable	37,842	-
Royalty Receivable	-	7,094
Investments (Note 3)	8,355,053	7,160,876
Program Related Investments, Net (Note 4)	986,853	1,367,005
Office Equipment, Net (Note 5)	17,760	6,090
Prepaid Expense and Deposits	4,958	2,475
Investments - Deferred Compensation Plan (Note 8)	37,867	-
Total Assets	\$12,306,851	\$9,903,058
<u>LIABILITIES:</u>		
Accounts Payable	\$ 58,321	\$ 21,691
Accrued Employee Benefits	7,209	28,957
Deferred Compensation Liability (Note 8)	37,867	-
Total Liabilities	103,397	50,648
<u>NET ASSETS:</u>		
Unrestricted Net Assets	12,203,454	9,852,410
Total Liabilities and Net Assets	\$12,306,851	\$9,903,058

See accompanying notes to financial statements.

THE SUSTAINABLE ENERGY FUND OF CENTRAL EASTERN PA
(A Not-for Profit Corporation)

STATEMENT OF FUNCTIONAL EXPENSES

For the Year Ended June 30, 2003

With Comparative Totals for 2002

	Program Services	Management & General	<u>Total</u>	
			2003	2002
Grants Awarded	\$ 157,698	\$ —	\$ 157,698	\$ 73,999
Program Related Investments*				
Loss Allowance	<u>687,368</u>	<u>—</u>	<u>687,368</u>	<u>236,250</u>
Operating Expenses:				
Salaries and Wages	90,165	78,839	169,004	146,226
Fringe Benefits	19,808	17,862	37,670	33,610
Payroll Taxes	7,058	6,365	13,423	12,418
Contract Managers	88,454	10,424	98,878	—
Training and Recruiting	330	297	627	340
Subtotal Staff	<u>205,815</u>	<u>113,787</u>	<u>319,602</u>	<u>192,594</u>
Rent	18,474	9,040	27,514	15,755
Insurance	2,456	1,202	3,658	3,544
Depreciation	3,214	1,572	4,786	3,320
Subtotal Occupancy	<u>24,144</u>	<u>11,814</u>	<u>35,958</u>	<u>22,619</u>
Board Stipends and Expenses	19,168	19,168	38,336	23,467
Dues and Publications	—	1,538	1,538	2,075
Marketing	4,143	7,084	11,227	22,750
Office Supplies	3,052	1,493	4,545	3,022
Wind Value and Education Consulting	9,882	—	9,882	—
Audit	—	9,000	9,000	6,900
Legal	18,546	2,061	20,607	4,373
Due Diligence	17,006	—	17,006	2,635
Organization Design	—	1,602	1,602	13,684
System Support	—	11,636	11,636	16,819
Printing and Postage	2,159	1,056	3,215	4,511
Telephone	4,176	2,044	6,220	5,092
Travel	7,486	3,663	11,149	8,673
MIS Support/Web Hosting	1,786	1,786	3,572	6,328
Director and Officer Insurance	—	2,738	2,738	2,400
Workout Expenses	8,976	—	8,976	—
Miscellaneous	1,319	644	1,963	1,643
Subtotal Other	<u>97,699</u>	<u>65,513</u>	<u>163,212</u>	<u>124,372</u>
Total Operating Expenses	<u>327,658</u>	<u>191,114</u>	<u>518,772</u>	<u>339,585</u>
Totals	<u>\$1,172,724</u>	<u>\$191,114</u>	<u>\$1,363,838</u>	<u>\$ 649,834</u>

See accompanying notes to the financial statements.

**THE SUSTAINABLE ENERGY FUND OF CENTRAL EASTERN PA
(A Not-for Profit Corporation)**

STATEMENT CASH FLOWS

	<u>Year Ended June 30,</u>	
	<u>2003</u>	<u>2002</u>
<i><u>Cash Flows from Operating Activities:</u></i>		
Increase in Net Assets	\$2,351,044	\$1,944,141
Adjustments to Reconcile Change in Net Assets to Net Cash Used by Operating Activities:		
Depreciation	4,786	3,320
Loss Reserve	687,368	236,250
Net Realized and Unrealized (Gains) Losses on Investments	(45,822)	836,030
Changes in Assets and Liabilities:		
Decrease (Increase) in Accounts Receivables	1,914	(31,663)
(Increase) in Prepaid Expense and Deposits	(2,483)	(1,600)
Increase (Decrease) in Account Payable	36,630	(3,398)
Increase in Employee Benefit Liabilities	<u>16,119</u>	<u>10,706</u>
 Net Cash Provided by Operating Activities	 <u>3,049,556</u>	 <u>2,993,786</u>
<i><u>Cash Flows from Investing Activities:</u></i>		
Purchase of Office Equipment and Furniture	(16,456)	-
Net Purchase of Investments	(1,148,356)	(1,470,054)
Additions to Deferred Comp. Plan Investments	(37,867)	-
Increase in Program Related Investments	(355,000)	(1,300,000)
Return of Program Related Investments	<u>47,785</u>	<u>30,912</u>
 Net Cash Used in Investing Activities	 <u>(1,509,894)</u>	 <u>(2,739,142)</u>
 Increase in Cash and Cash Equivalents	 1,539,662	 254,644
 Cash and Cash Equivalents, Beginning of Year	 <u>1,066,685</u>	 <u>812,041</u>
 CASH AND CASH EQUIVALENTS, END OF YEAR	 <u>\$2,606,347</u>	 <u>\$1,066,685</u>

See accompanying notes to financial statements.

**THE SUSTAINABLE ENERGY FUND OF CENTRAL EASTERN PA
(A Not-for Profit Corporation)**

NOTES TO FINANCIAL STATEMENTS

June 30, 2003

1. Nature of Organization

PP&L Sustainable Energy Fund, d/b/a Sustainable Energy Fund of Central Eastern PA (the Fund) is a Pennsylvania non-profit corporation formed to promote, research and invest in clean and renewable energy technologies, energy conservation, energy efficiency and sustainable energy enterprises that provide opportunities and benefits for PP&L ratepayers.

The Fund was formed pursuant to a joint settlement agreement arising from the Pennsylvania Utility Commission (PUC) electric utility deregulation proceedings in 1998. The agreement provides, in part, a rate surcharge on electric power consumers (ratepayers) through 2004. The surcharge is collected from the ratepayers by the power distribution entity, PPL Electric Utilities for this local service area, and remitted to the Fund for investment.

The Fund is managed by an executive director who reports to a Board of Directors. The PUC also maintains oversight of the Fund.

2. Summary of Significant Accounting Policies

Basis of Accounting

The financial statements of the Fund have been prepared on the accrual basis of accounting and accordingly reflect all significant receivables, payables, and other liabilities.

Basis of Presentation

Financial statement presentation follows the recommendations of the Financial Accounting Standards Board in its Statement of Financial Accounting Standards (SFAS) No. 117, *Financial Statements of Not-for-Profit Organizations*. Under SFAS No. 117, the Fund is required to report information regarding its financial position and activities according to three classes of net assets: unrestricted net assets, temporarily restricted net assets, and permanently restricted net assets. At June 30, 2003 and 2002, all net assets are unrestricted.

Cash and Cash Equivalents

For purposes of the Statement of Cash Flows, the Fund considers all highly liquid investments with an initial maturity of three months or less to be cash equivalents.

THE SUSTAINABLE ENERGY FUND OF CENTRAL EASTERN PA
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NOTES TO FINANCIAL STATEMENTS

June 30, 2003

Concentration of Revenue

The Fund receives a substantial amount of its support from the PPL ratepayers contributions, as more fully described in Note 1, which expires December 31, 2004. Management and the Board of Directors believe that at least the current level of funding will be renewed beyond 2004.

Donated Services

No amounts have been reflected in the financial statements for donated services. The Organization generally pays for services requiring specific expertise. However, individuals volunteer their time and perform a variety of tasks that assist the Organization with specific investment programs, and various committee assignments.

Estimates

Management uses estimates and assumptions in preparing financial statements. Those estimates and assumptions affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, and the reported revenues and expenses. Actual results could differ from those estimates.

Investments in Marketable Securities

Investments in equity securities with readily determinable fair values and all investments in debt securities are measured at fair value in the statement of financial position. Investment income or loss (including gains and losses on investments, interest and dividends) is included in the statement of activities as increases or decreases in unrestricted net assets unless the income or loss is restricted by donor or law.

Program Related Investments

(a) Loans

Loans are stated at their outstanding unpaid principal balance. Interest income is recognized as revenue when received.

(b) Allowance for Loan Losses

The allowance for loan losses has been established through provisions for loan losses charged against income. Loans deemed to be uncollectible are charged against the allowance and subsequent recoveries, if any, are credited to the allowance. The allowance is maintained at a level considered adequate to provide for potential loan losses. In making this determination, management takes into consideration the results of internal review procedures, prior loan loss experience, an assessment of the effect of current and anticipated future economic conditions, the financial condition of the borrower and such other factors that, in management's judgement, deserve consideration. The determination of the adequacy of the allowance is inherently subjective, as it requires material estimates including the amounts and timing of future cash flows expected to be received on impaired loans that may be susceptible to significant change.

**THE SUSTAINABLE ENERGY FUND OF CENTRAL EASTERN PA
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NOTES TO FINANCIAL STATEMENTS

June 30, 2003

(c) **Nonmarketable Equity Securities**

Nonmarketable equity investments are holdings of less than 20% of the voting stock of investors and are carried at cost. The shares carry various conditions or restrictions on transfers and redemptions. Cost is reduced for permanent declines in value, as estimated by management, and dividends, if any, are treated as income when received. Investees are typically start-up developmental activities and as such are highly speculative. The determination of write-downs, if any, or ultimate realization of the investment is inherently subjective and as such, it requires material estimates regarding their valuation that are susceptible to significant change.

Concentration of Credit and Market Risk

Financial instruments that potentially expose the Fund to concentrations of credit and market risk consist primarily of cash equivalents and investments. The Fund places its cash at a high credit quality financial institution. From time to time, deposits at the institution exceed federal depository insurance limits. The Fund has significant investments in stocks and bonds. Though the market value of investments is subject to fluctuations, management believes the investment policy is prudent for the long-term welfare of the Fund. In addition, investments do not represent significant concentrations of market risk in as much as the Fund's investment portfolio is adequately diversified among issuers. Concentrations of credit risk with respect to program related investments are subject to the individual credit worthiness of the borrowers and investees, who are predominately located in Central Eastern Pennsylvania and associated with early stage sustainable or alternate energy endeavors. Consequently, the ability to realize the amounts may be affected by economic and political fluctuations in the power industry in this geographic region. The Fund performs ongoing credit evaluations and reserves for estimated and known uncollectibles.

Office Equipment

Office equipment acquisitions are recorded at cost. Depreciation is provided over the estimated useful lives of the assets of three to five years and computed on straight-line and accelerated methods.

Additions and betterments of \$500 or more are capitalized, while maintenance and repairs that do not improve or extend the original useful lives of the assets are expensed as incurred.

Advertising Costs

Advertising costs are expensed as incurred.

3. Investments

Investments are managed by professional investment managers. The investment managers are subject to the Fund's investment policies which contain objectives, guidelines and restrictions designed to complement the Fund's activities and mission. Investments at fair value at June 30, are comprised of the following:

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NOTES TO FINANCIAL STATEMENTS

June 30, 2003

3. Investments (continued)

	2003	2002
U.S. Government Obligations	\$2,006,910	\$1,324,330
Corporate Bonds	526,694	490,638
Equity Securities	5,648,202	5,164,458
Temporary Cash and Money Market	173,247	181,450
	\$8,355,053	\$7,160,876

Investment return is summarized as follows:

Interest and Dividend Income	\$ 199,469	\$ 162,871
Net Realized and Unrealized Gains (Losses) On Investments	45,822	(836,030)
	245,291	(673,159)
Less Investment Advisory and Custodian Fees	(48,410)	(45,521)
Total Investment Return	\$ 196,881	\$ (718,680)

4. Program Related Investments

Program related investments consist of loans to and equity investments in entities to assist them in pursuing sustainable energy opportunities.

<u>Loans</u>	2003	2002
Powerweb Technologies, Inc. - due in monthly principal repayments of \$1,042 through April 2003, \$3,125 through April 2003 and \$7,500 thereafter, due April 2008. Royalties payable at 3% of borrower's gross revenue, up to a maximum of \$650,000. Secured by assets of the borrower.	\$459,376	\$480,710

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NOTES TO FINANCIAL STATEMENTS

June 30, 2003

4. Program Related Investments (continued)

	<u>2003</u>	<u>2002</u>
<u>Loans (continued)</u>		
Energy Unlimited, Inc. - interest only due monthly at 10%, due February, 2006.	\$ 100,000	\$ 100,000
Community Energy, Inc. - due in monthly installments of \$3,042, including interest at 8%, due December 2006.	111,095	137,545
Community Energy, Inc. - \$250,000 line of credit, interest only due monthly at prime plus 1%, due June, 2004.	50,000	-
Allentown Technology Center - interest only due monthly at 6% through May, 2004, thereafter, monthly installments of \$3,207, including interest at 6%, due November, 2009.	180,000	-
Nova Cruz, Products, Inc. - due March 2007, royalties payable at 3% of net factoring sales, up to a maximum of \$487,500, secured by assets of the borrower. Foreclosed in August 2003, reduced to expected net realizable value.	104,882	325,000
	<u>1,005,353</u>	<u>1,043,255</u>
Less Loss Reserve	(268,500)	(251,250)
Total Loans, Net	<u>736,853</u>	<u>792,005</u>
<u>Nonmarketable Equity Securities</u>		
250,000 Shares Community Energy, Inc. Series A Preferred	250,000	250,000
124,521 Shares Nova Cruz Products, Inc. Series A Convertible Preferred. Foreclosed in August 2003 written down to estimated fair value	-	325,000
Total Equity Investments	<u>250,000</u>	<u>575,000</u>
Total Program Related Investments	<u>\$ 986,853</u>	<u>\$1,367,005</u>

**THE SUSTAINABLE ENERGY FUND OF CENTRAL EASTERN PA
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NOTES TO FINANCIAL STATEMENTS

June 30, 2003

5. Office Equipment

	2003	2002
Furniture	\$ 15,818	\$ 6,904
Computer and Phone Equipment	<u>12,077</u>	<u>4,535</u>
	27,895	11,439
Less Accumulated Depreciation	<u>(10,135)</u>	<u>(5,349)</u>
	<u>\$ 17,760</u>	<u>\$ 6,090</u>

6. Lease

The Fund leases its office facilities under a non-cancellable operating lease expiring September 30, 2005. The lease provides for monthly base rent of \$2,467 through September 30, 2003 and annual adjustments thereafter based on the consumer price index. The former lease required monthly rent of \$1,400 through September 2002. Future minimum lease payments are:

Years ended	<u>Amount</u>
<u>June 30:</u>	
2004	\$29,604
2005	29,604
2006	7,401

Total rents charged to expense under the leases were \$26,403 and \$15,755 for the years ended June 30, 2003 and 2002, respectively.

7. Retirement Plan

The Fund has a defined contribution retirement plan (the Plan) covering all full time employees having attained 21 years of age with three months of service. The Fund makes contribution to the Plan each year equal to 10% of all participants compensation plus 4.3% of compensation in excess of \$33,960 through December 2002 and \$35,120 effective January, 2003, being 40% of the social security taxable wage base in effect on the first day of each Plan year. Total expense was \$19,858 and \$13,720 for the years ended June 30, 2003 and 2002, respectively.

**THE SUSTAINABLE ENERGY FUND OF CENTRAL EASTERN PA
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NOTES TO FINANCIAL STATEMENTS

June 30, 2003

8. Deferred Compensation Plan

The Fund provides a key employee a non-qualified deferred compensation retirement plan. The liability is financed with contributions to Fund owned, participant directed, mutual funds. The assets are payable to the participant upon retirement. At June 30, 2003, total Fund contributions and net investment gain or loss were \$37,867.

9. Line of Credit

The Fund has a \$750,000 Line of Credit with a bank, expiring February 2004. Interest on borrowings is payable at the bank's prime rate minus .75%. There were no borrowings on the line as of or during the periods ended June 30, 2003 and 2002.

10. Related Party Transactions

The Organization awarded \$42,125 and \$43,000 of program grants in 2003 and 2002, respectively, to two organizations, each of which has a director who is a board member of the Fund.