

FINANCIAL STATEMENTS AND
INDEPENDENT AUDITORS' REPORT

ESCALLONIA LIMITED PARTNERSHIP

DECEMBER 31, 2008

Escallonia Limited Partnership

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INDEPENDENT AUDITORS' REPORT

To the Partners
Escallonia Limited Partnership

We have audited the accompanying balance sheet of Escallonia Limited Partnership as of December 31, 2008, and the related statements of operations, partners' equity (deficit) and cash flows for the year then ended. These financial statements are the responsibility of the partnership'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 Escallonia Limited Partnership as of December 31, 2008, and the results of its operations and its cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplemental information included on pages 18 and 19 are presented for purposes of additional analysis and is not a required part of basic financial statements. Such information has been subjected to the auditing procedures applied in our audits of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.



Atlanta, Georgia
March 15, 2009

Escallonia Limited Partnership

BALANCE SHEET

December 31, 2008

CURRENT ASSETS

Cash	\$ 269,494
Tenant accounts receivable	26,376
Accounts receivable - other	78,980
Prepaid expenses	<u>61,869</u>
Total current assets	<u>436,719</u>

RESTRICTED DEPOSITS AND FUNDED RESERVES

Tenant security deposits	58,962
Other reserves	<u>132,242</u>
Total restricted deposits and funded reserves	<u>191,204</u>

RENTAL PROPERTY

Building and improvements	35,353,988
Land improvements	3,152,973
Furniture and equipment	<u>594,789</u>
	39,101,750
Accumulated depreciation	<u>(4,432,939)</u>
Total rental property	<u>34,668,811</u>

OTHER ASSETS

Mortgage costs, net	280,309
Tax credit monitoring fees, net	<u>164,388</u>
Total other assets, net	<u>444,697</u>
Total assets	<u><u>\$ 35,741,431</u></u>

(continued)

Escallonia Limited Partnership
BALANCE SHEET - CONTINUED
December 31, 2008

LIABILITIES AND PARTNERS' EQUITY (DEFICIT)

CURRENT LIABILITIES	
Accounts payable	\$ 51,559
Accrued expenses	68,543
Accrued interest payable - first mortgage	4,381
Accrued interest payable - other mortgages	1,079,975
Real estate taxes payable	<u>11,739</u>
Total current liabilities	<u>1,216,197</u>
DEPOSITS AND PREPAID LIABILITY	
Tenant security deposits	58,918
Prepaid rent	<u>5,974</u>
Total deposits and prepaid liability	<u>64,892</u>
LONG-TERM LIABILITIES	
Mortgages payable - first mortgage	5,035,000
Mortgages payable - other mortgages	23,347,094
Deferred developer fee payable	867,556
Due to related parties	158,073
Other liabilities	<u>738,052</u>
Total long-term liabilities	<u>30,145,775</u>
COMMITMENTS	
Partners' equity (deficit)	<u>4,314,567</u>
Total liabilities and partners' equity (deficit)	<u><u>\$ 35,741,431</u></u>

See notes to financial statements

Escallonia Limited Partnership
STATEMENT OF OPERATIONS
Year ended December 31, 2008

Revenue	
Rental income	\$ 1,369,512
Vacancies and concessions	(16,863)
Other operating income	<u>23,272</u>
Total revenue	<u>1,375,921</u>
Operating expenses	
Salaries and employee benefits	432,835
Repairs and maintenance	206,877
Utilities	122,803
Property management fee	111,186
Real estate taxes	11,739
Property insurance	73,876
Miscellaneous operating expenses	<u>98,721</u>
Total operating expenses	<u>1,058,037</u>
Net operating income (loss)	<u>317,884</u>
Other income (expense)	
Interest income	6,642
Interest expense - first mortgage	(150,105)
Interest expense - other loans	(215,995)
Miscellaneous other income (expense)	(381)
Annual fee to affiliate of limited partner	(5,697)
Depreciation	(1,234,766)
Amortization	<u>(20,688)</u>
Total other income (expense)	<u>(1,620,990)</u>
Net loss	<u><u>\$ (1,303,106)</u></u>

See notes to financial statements

Escallonia Limited Partnership

STATEMENT OF PARTNERS' EQUITY (DEFICIT)

Year ended December 31, 2008

	General Partner	Limited Partner	Accumulated Other Comprehensive Income	Total Partners' Equity (Deficit)
	<u> </u>	<u> </u>	<u> </u>	<u> </u>
Balance, January 1, 2008	\$ (424)	\$6,356,149	\$ (312,244)	\$ 6,043,481
Net loss	(1,500,000)	196,894	-	(1,303,106)
Changes in fair value of derivative	<u>-</u>	<u>-</u>	<u>(425,808)</u>	<u>(425,808)</u>
Balance, December 31, 2008	<u>(1,500,424)</u>	<u>6,553,043</u>	<u>(738,052)</u>	<u>4,314,567</u>
Partners' percentage of partnership losses	<u>0.01%</u>	<u>99.99%</u>	<u>0.00%</u>	<u>100.00%</u>

See notes to financial statements

Escallonia Limited Partnership
STATEMENT OF CASH FLOWS
Year ended December 31, 2008

Cash flows from operating activities	
Net loss	\$ (1,303,106)
Adjustments to reconcile net loss to net cash provided by operating activities	
Depreciation	1,234,766
Amortization	20,688
Changes in:	
Tenant accounts receivable	(13,053)
Accounts receivable - other	(58,102)
Prepaid expenses	(5,521)
Accounts payable	31,019
Accrued expenses	31,402
Accrued interest payable - first mortgage	(72,086)
Accrued interest payable - other mortgages	215,995
Real estate taxes payable	11,739
Prepaid rent	<u>1,435</u>
Net cash provided by operating activities	<u>95,176</u>
Cash flows from investing activities	
Change in other reserves	<u>(39,821)</u>
Net cash used in investing activities	<u>(39,821)</u>
Cash flows from financing activities	
Principal payments on mortgage payable	(240,000)
Repayment of advances from affiliates	(89,814)
Payments on development fee	<u>(88,340)</u>
Net cash used in financing activities	<u>(418,154)</u>
Net decrease in cash	(362,799)
Cash, beginning	<u>632,293</u>
Cash, end	<u><u>\$ 269,494</u></u>
Supplemental disclosure of cash flow information	
Cash paid for interest	<u><u>\$ 222,191</u></u>

See notes to financial statements

Escallonia Limited Partnership

NOTES TO THE FINANCIAL STATEMENTS

December 31, 2008

NOTE 1 - ORGANIZATION AND NATURE OF OPERATIONS

Escallonia LP (the Partnership) was formed as a limited partnership on April 15, 2002, under the laws of the state of Washington, for the purpose of acquiring, constructing, developing and operating a low-income residential housing project. The property consists of 184 rental units located in Seattle, Washington, and operates under the name Rainier Vista Phase I (the Project).

Effective December 1, 2003, the partnership agreement was amended to admit the investor limited partner and the special limited partner and to permit the withdrawal of the original limited partner. This amendment provides for ownership and allocations of profits, losses and tax credits as follows:

General partner	.01%
Investor limited partner	99.99%
Special limited partner	0.00%
	<u>100.00%</u>

The general partner is The Housing Authority of the City of Seattle(SHA) the current investor limited partner is MMA Rainier Vista, LLC, and the current special limited partner is MMA Special Limited Partner, Inc.

The Project consists of 35 buildings which qualify for low-income housing tax credits pursuant to Internal Revenue Code Section 42 (Section 42), which regulates the use of the Project as to occupant eligibility and unit gross rent, among other requirements. Each building of the Project must meet the provisions of these regulations during each of 15 consecutive years in order to remain qualified to receive the credits. In addition, the Partnership has executed a land use restriction agreement which requires the utilization of the Project pursuant to Section 42 for a minimum of 20 years, even after disposition of the Project by the Partnership.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES

Accounts Receivable and Bad Debts

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.

Escallonia Limited Partnership

NOTES TO THE FINANCIAL STATEMENTS - CONTINUED

December 31, 2008

Investment in Real Estate

Rental property is recorded at cost. Depreciation is provided for in amounts sufficient to relate the cost of the buildings, land improvements and equipment to operations over their estimated useful lives using the straight-line method. Improvements are capitalized, while expenditures for maintenance and repairs are charged to expense as incurred.

Impairment of Long-Lived Assets

In accordance with Statement of Financial Accounting Standard No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets," the Partnership reviews its rental property for impairment whenever events or changes in circumstances indicate that the carrying value of an asset may not be recoverable. If the fair value is less than the carrying amount of the asset, an impairment loss is recognized for the difference. No asset impairment losses have been recognized during the year ended December 31, 2008.

Derivatives

Effective January 1, 2003, the Partnership adopted Statement of Financial Accounting Standards (SFAS) No. 133, "Accounting for Derivative Instruments and Hedging Activities," as amended. The Partnership uses derivatives to manage risks related to interest rate movements. Interest rate swap contracts designated and qualifying as cash flow hedges are reported at fair value. The gain or loss on the effective portion of the hedge initially is included as a component of other comprehensive income and is subsequently reclassified into earnings when interest on the related debt is paid. As part of the transaction process, the fair value of the Partnership's preexisting cash flow hedge as of the beginning of the period which is estimated to be \$738,052, is reflected in accumulated other comprehensive income.

Amortization

Mortgage costs are amortized over the terms of the related mortgage loans using the effective yield method. Tax credit monitoring fees are amortized over the compliance period using the straight-line method. Estimated amortization expense for each of the next five years through 2013 is expected to be \$20,688 annually.

Escallonia Limited Partnership

NOTES TO FINANCIAL STATEMENTS - CONTINUED

December 31, 2008

Rental Income

Rental income is recognized as rentals become due. Rental payments received in advance are deferred until earned. All leases between the Partnership and tenants of the property are operating leases.

Advertising Costs

The Partnership's policy is to expense advertising costs when incurred.

Income Taxes

No provision or benefit for income taxes has been included in these financial statements since taxable income or loss passes through to, and is reportable by, the partners individually.

In June 2006, the FASB issued FIN 48, "Accounting for Uncertainty in Income Taxes" an interpretation of FASB Statement No. 109. The effective date of FIN 48 was for fiscal years beginning after December 15, 2006. The effective date was delayed in 2007 and was delayed again in 2008 for nonpublic companies. The new effective date for FIN 48 for nonpublic companies is for fiscal years beginning after December 15, 2008. The Partnership has elected to defer application of FIN 48, as permitted by FSP FIN 48-3, "Effective Date of FASB Interpretation No. 48 for Certain Nonpublic Enterprises," until 2009. The Partnership does not anticipate that the provisions of FIN 48 will have any significant impact on its financial statements. However, additional disclosures may be required of situations, if any, where the Partnership's tax positions are considered uncertain. Currently, the FASB is deliberating the manner and extent to which pass-through entities such as the Partnership will need to apply the provisions of FIN 48.

Use of 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 the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

Escallonia Limited Partnership

NOTES TO FINANCIAL STATEMENTS - CONTINUED

December 31, 2008

NOTE 3 - RESTRICTED DEPOSITS AND FUNDED RESERVES

Operating Reserve

Under the partnership agreement, the general partner is required to fund an operating reserve in an amount equal to \$230,392. The operating reserve is required to be fully funded upon the earlier of receipt by the Partnership of the fourth installment of the investor limited partners capital contribution or January 15, 2009. As of December 31, 2008, no amounts have been funded.

Replacement Reserve Account

Under the partnership agreement, the general partner is required to fund a reserve account for capital replacements commencing with the completion date, as defined. The account shall be funded by monthly deposits equal to the product of \$3,067 times the adjustment fraction, as defined. As of December 31, 2008, \$132,242 has been funded.

Affordability Reserve

Under the partnership agreement, the general partner is required to establish an Affordability Reserve in an amount equal to \$478,000. The Affordability Reserve is required to be fully funded upon the earlier of receipt by the Partnership of the fourth installment of the investor limited partners capital contribution or January 15, 2009. As of December 31, 2008, no amounts have been funded.

NOTE 4 - RELATED PARTY TRANSACTIONS

Management Agreement

The Partnership entered into a management agreement on December 1, 2003 with Impact Property Management, an affiliate of the general partner. The management agreement provides for fees of \$25 per unit per month increasing 3 percent per annum upon commencement of operations. As of December 31, 2008, management fees of \$111,186 have been paid.

Development Services Fee

On March 3, 2003, the Partnership entered into a development services agreement with the general partner for services in connection with the development of the Project. On December 31, 2006, the Partnership amended the development services agreement with the general partners in

Escallonia Limited Partnership

NOTES TO FINANCIAL STATEMENTS - CONTINUED

December 31, 2008

connection with the development of the Project to include a \$120,000 fee increase. The development services agreement provides for a fee equal to \$2,960,000. As of December 31, 2008, \$867,556 of the development services fee has been incurred and remains payable.

Asset Management Fee

Under the partnership agreement, an annual asset management fee of \$5,000 times the adjustment fraction, as defined, is payable to the investor limited partner beginning with the completion date, as defined. Any unpaid fees will accrue to the extent cash flow, as defined, is not available to pay such fee. As of December 31, 2008, asset management fees of \$5,697 remain payable.

Advances from Affiliates

From time to time the general partner advances the Partnership funds to pay for various operating expenses. These advances do not bear interest and are due on demand. As of December 31, 2008, advances from the general partner totaled \$152,376.

NOTE 5 - MORTGAGE NOTES PAYABLE

First Mortgage - The Housing Authority of The City of Seattle

The Partnership entered into a loan agreement on October 30, 2003 with the general partner in the original amount of \$22,500,000. Under the terms of the Trust Indenture dated October 30, 2003, the loan was funded by Variable Rate Demand Revenue Bonds 2003, (Rainier Vista Project, Phase I) (the Variable Rate Bonds). The loan is secured by a deed of trust on the Partnership's property. Pursuant to the Trust Indenture, a portion of the Variable Rate Bonds can be converted into Fixed Rate Bonds. As of December 31, 2008, no conversion has occurred. Payments of interest and principal will be due in accordance with the loan agreements. The Variable Rate Bonds mature on December 1, 2036. As of December 31, 2008, \$5,035,000 is outstanding.

The loan bears interest at a variable rate. As of December 31, 2008, the variable rate was 1.00 percent. To minimize the effect of changes in interest rates, the Partnership entered into an interest rate swap agreement on \$5,275,000 of the Variable Rate Bonds under which it pays interest at a fixed rate of 4.13 percent and receives interest at a variable rate. The variable rate under the swap is based on the same notional amount as the underlying mortgage. The result is that the Partnership pays interest at a fixed effective rate. Valued separately, the interest rate

Escallonia Limited Partnership

NOTES TO FINANCIAL STATEMENTS - CONTINUED

December 31, 2008

swap agreement represents a liability as of December 31, 2008, in the amount of \$738,052. This value represents the fair value of the current difference in interest paid and received under the swap agreement over the remaining term of the agreement. Because the swap is considered to be a cash flow hedge, the value of the swap agreement is recorded in the partners' equity (deficit) as a separate component of other comprehensive income. Changes in the swap agreement's fair value are reported currently in other comprehensive income. Payments are recognized in current operating results as settlements occur under the agreement as a component of interest expense.

SHA Loan #1

The Partnership entered into a loan agreement on December 1, 2003 with the general partner in the original amount of \$13,430,695. The note was funded with proceeds provided to the general partner through HOPE VI and MTW Block grants. The loan accrues interest at 1 percent per annum. Beginning on December 22, 2003, interest only payments are due on the outstanding principal balance from available cash flow, as defined. The unpaid principal and accrued interest are due at maturity on December 21, 2058. The loan is secured by a deed of trust on the Partnership's property. At December 31, 2008, the outstanding principal and accrued interest was \$12,732,292, and \$671,535, respectively.

SHA Loan #2

The Partnership entered into an additional loan agreement on December 1, 2003 with the general partner in the original amount of \$8,168,795. The note was funded through proceeds from for sale units of the general partner. The loan accrues interest at 1 percent per annum. Beginning on December 22, 2003, interest only payments are due on the outstanding principal balance from available net cash flow, as defined. The unpaid principal and accrued interest are due at maturity on December 21, 2058. The loan is secured by a deed of trust on the Partnership's property. At December 31, 2008, the outstanding principal and accrued interest was \$10,614,802 and \$408,440, respectively.

Aggregate annual maturities of the mortgages payable over each of the next five years as of December 31, are expected to be as follows:

Escallonia Limited Partnership

NOTES TO FINANCIAL STATEMENTS - CONTINUED

December 31, 2008

	Variable Rate	SHA Loan #1	SHA Loan #2	Total
	Bonds			
2009	\$ -	\$ -	\$ -	\$ -
2010	-	-	-	-
2011	-	-	-	-
2012	-	-	-	-
2013	-	-	-	-
Thereafter	5,035,000	12,732,292	10,614,802	28,382,094
Total	<u>\$ 5,035,000</u>	<u>\$ 12,732,292</u>	<u>\$ 10,614,802</u>	28,382,094
Less current maturities				-
Net long-term portion				<u>\$ 28,382,094</u>

Standby Letter of Credit

The Partnership has a standby letter of credit with Key Bank to insure the bond holders upon any defaults by the Partnership. The letter of credit carries an interest of eight percent on any draws and matures on October, 10, 2010. As of December 31, 2008, there have been no draws on this letter of credit.

NOTE 6 - PARTNERS' CAPITAL CONTRIBUTIONS

In accordance with the First Amended and Restated Agreement of Limited Partnership, the limited partner is required to contribute \$12,387,000. As of December 31, 2008, the limited partner has contributed \$11,594,332. The remaining installments are due as follows:

1. \$792,668 shall be payable on the later of (a) the third anniversary of the due date for payment of the second installment, as defined, and (b) October 15, 2008.

In addition, the amount of the investor limited partners' capital may be reduced or increased under certain circumstances, as defined, if the final amount of low-income housing tax credits is less than or greater than \$13,319,240.

NOTE 7 - CONCENTRATION OF CREDIT RISK

The Partnership maintains its cash in deposit accounts, which, at times, may exceed federally insured limits. The Partnership has not experienced any losses in such accounts. The Partnership believes it is not exposed to any significant credit risk on such accounts.

Escallonia Limited Partnership

NOTES TO FINANCIAL STATEMENTS - CONTINUED

December 31, 2008

NOTE 8 - COMMITMENTS AND CONTINGENCIES

Tax Credit Compliance

The Project's low-income housing tax credits are contingent on its ability to maintain compliance with applicable sections of Section 42. Failure to maintain compliance with occupant eligibility, and/or unit gross rent, or to correct noncompliance within a specified time period could result in recapture of previously taken tax credits plus interest. In addition, such potential noncompliance may require an adjustment to the contributed capital by the investor limited partner.

Operating Deficit Advances

Under the partnership agreement, the general partner is required to make operating deficit advances to the Partnership in an amount not to exceed an unpaid balance of \$500,000 beginning on the admission date until the end of the compliance period, as defined. The operating deficit advances are non-interest bearing and are payable from net cash flow of the Partnership, as defined. As of December 31, 2008, no such advances have been made.

SUPPLEMENTAL INFORMATION

Escallonia Limited Partnership

SCHEDULE OF OTHER REVENUES AND CERTAIN EXPENSES

Year ended December 31, 2008

Rental income	
Rent revenue - gross potential	\$ 1,071,963
Flexible subsidy revenue	<u>297,549</u>
Total rental income	<u>\$ 1,369,512</u>
Vacancies and concessions	
Apartments vacancies	\$ 11,664
Rental concessions	<u>5,199</u>
Total vacancies and concessions	<u>\$ 16,863</u>
Other operating income	
Miscellaneous other income	<u>\$ 23,272</u>
Total other operating income	<u>\$ 23,272</u>
Salaries and employee benefits	
Salaries - administrative	\$ 170,624
Salaries - maintenance	107,161
Health insurance and other benefits	<u>155,050</u>
Total salaries and employee benefits	<u>\$ 432,835</u>
Repairs and maintenance	
Grounds	\$ 59,684
Fire protection	14,105
Security services/contract	51,303
Repairs and maintenance - other than contracts	40,453
Repairs and maintenance - contracts	22,022
Elevator	5,833
Miscellaneous maintenance expenses	<u>13,477</u>
Total repairs and maintenance	<u>\$ 206,877</u>
Utilities	
Electricity	\$ 19,131
Water	53,168
Sewer	7,069
Trash removal	43,352
Gas	<u>83</u>
Total utilities	<u>\$ 122,803</u>

Escallonia Limited Partnership

SCHEDULE OF OTHER REVENUES AND CERTAIN EXPENSES - CONTINUED

Year ended December 31, 2008

Miscellaneous operating expenses	
Office supplies and expense	\$ 10,028
Training and travel	964
Telephone and answering service	13,594
Computer supplies and expense	15,789
Bad debt expense	4,825
Miscellaneous administrative	5,196
Advertising and newspaper	13,145
Legal	290
Audit	10,850
Other professional fees	<u>24,040</u>
Total miscellaneous operating expenses	<u>\$ 98,721</u>
Interest expense - other loans	
Interest expense - second mortgage	\$ 134,307
Interest expense - third mortgage	<u>81,688</u>
Total interest expense - other loans	<u>\$ 215,995</u>
Miscellaneous other income (expense)	
Miscellaneous other expense	<u>\$ (381)</u>
Total miscellaneous other income (expense)	<u>\$ (381)</u>