

BAYBROOK PARK RETIREMENT CENTER, LTD.
FINANCIAL STATEMENTS
For the year ended December 31, 2008
with
Report of Independent Auditors

Report of Independent Auditors

To the Partners of
Baybrook Park Retirement Center, Ltd.:

We have audited the accompanying balance sheet of Baybrook Park Retirement Center, Ltd. as of December 31, 2008 and the related statements of operations, changes in partners' capital 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 Baybrook Park Retirement Center, Ltd. 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.

Novogradac & Company LLP

February 18, 2009

BAYBROOK PARK RETIREMENT CENTER, LTD.
BALANCE SHEET
December 31, 2008

ASSETS

Cash and cash equivalents	\$ 175,808
Restricted cash	103,698
Certificate of deposit	151,979
Prepaid expenses	10,391
Prepaid ground lease	559,904
Fixed assets, net of accumulated depreciation	6,630,545
Intangible assets, net of accumulated amortization	<u>132,763</u>
Total assets	<u><u>\$ 7,765,088</u></u>

LIABILITIES AND PARTNERS' CAPITAL

Liabilities	
Accounts payable	\$ 11,851
Security deposits payable	26,365
Accrued interest	155,540
Accrued expenses	7,112
Development fee payable	286,788
HOME loan payable	625,000
Mortgage loan payable	<u>3,263,808</u>
Total liabilities	4,376,464
Partners' capital	<u>3,388,624</u>
Total liabilities and partners' capital	<u><u>\$ 7,765,088</u></u>

see accompanying notes

BAYBROOK PARK RETIREMENT CENTER, LTD.
STATEMENT OF OPERATIONS
For the year ended December 31, 2008

REVENUE	
Rental revenue	\$ 706,613
Other income	<u>62,703</u>
Total revenue	769,316
OPERATING EXPENSES	
General and administrative	32,032
Payroll	120,408
Utilities	61,136
Insurance	43,111
Property management fees	36,979
Repairs and maintenance	64,184
Legal and other professional fees	17,081
Ground lease expense	10,160
Marketing and advertising	<u>5,506</u>
Total operating expenses	<u>390,597</u>
Operating income	378,719
OTHER INCOME AND (EXPENSES)	
Interest income	7,020
Interest expense	(262,273)
Depreciation and amortization	(436,404)
Other partnership expenses	<u>(7,304)</u>
Net other income and (expenses)	<u>(698,961)</u>
Net loss	<u><u>\$ (320,242)</u></u>

see accompanying notes

BAYBROOK PARK RETIREMENT CENTER, LTD.
 STATEMENT OF CHANGES IN PARTNERS' CAPITAL
 For the year ended December 31, 2008

	General Partner	Limited Partners	Total Partners' Capital
BALANCE, JANUARY 1, 2008	\$ 8	\$ 3,550,915	\$ 3,550,923
Capital contributions	-	157,943	157,943
Net loss	(32)	(320,210)	(320,242)
BALANCE, DECEMBER 31, 2008	\$ (24)	\$ 3,388,648	\$ 3,388,624

see accompanying notes

BAYBROOK PARK RETIREMENT CENTER, LTD.
STATEMENT OF CASH FLOWS
For the year ended December 31, 2008

CASH FLOWS FROM OPERATING ACTIVITIES

Net loss	\$ (320,242)
Adjustments to reconcile net loss to net cash provided by operating activities:	
Depreciation and amortization	436,404
Prepaid ground lease	10,160
Increase in restricted cash	(1,050)
Decrease in prepaid expenses	(433)
Decrease in accounts payable	(34,798)
Increase in security deposits payable	1,340
Increase in accrued interest	47,270
Decrease in accrued expenses	<u>(25,317)</u>
Net cash provided by operating activities	113,334

CASH FLOWS FROM INVESTING ACTIVITIES

Increase in restricted cash	(48,273)
Increase in certificate of deposit	<u>(151,979)</u>
Net cash used in investing activities	(200,252)

CASH FLOWS FROM FINANCING ACTIVITIES

Repayment of development fee payable	(525,000)
Repayment of mortgage loan payable	(36,192)
Capital contributions	<u>157,943</u>
Net cash used in financing activities	<u>(403,249)</u>

NET DECREASE IN CASH AND CASH EQUIVALENTS (490,167)

CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR 665,975

CASH AND CASH EQUIVALENTS AT END OF YEAR \$ 175,808

SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:

Cash paid for interest	<u><u>\$ 215,003</u></u>
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see accompanying notes

BAYBROOK PARK RETIREMENT CENTER, LTD.
NOTES TO FINANCIAL STATEMENTS
December 31, 2008

1. General

Baybrook Park Retirement Center, Ltd. (the "Partnership"), a Texas limited partnership, was formed on February 23, 2004 to acquire, construct, develop and operate a 100-unit apartment project known as Baybrook Park Retirement Center (the "Project") in Webster, Texas. The Project is rented to low-income tenants and is operated in a manner necessary to qualify for federal low-income housing tax credits as provided for in Section 42 of the Internal Revenue Code.

The general partner is HCHA Baybrook Park, LLC (the "General Partner"). The limited partners (the "Limited Partners") are Investors Affordable Housing Group V, Ltd. (the "Class A Limited Partner"), Hudson SLP, LLC (the "Special Limited Partner"), and Hudson Baybrook, LLC (the "Investment Limited Partner"). The Partnership will operate until December 31, 2079, or until its earlier dissolution or termination.

Profits, losses, and tax credits are allocated in accordance with the Amended and Restated Agreement of Limited Partnership of Baybrook Park Retirement Center, Ltd., dated June 21, 2005, and as amended (the "Partnership Agreement"). Profits and losses from operations and low-income housing tax credits are allocated 99.99% to the Limited Partners and 0.01% to the General Partner.

Pursuant to the Third Amendment to the Amended and Restated Partnership Agreement, the Investment Limited Partner is required to provide capital contributions to the Partnership totaling \$4,669,879, as adjusted for any tax credit adjustments. During 2008, the Investment Limited Partner contributed \$157,943. As of December 31, 2008, total contributions from the Investment Limited Partner were \$4,626,774. As of December 31, 2008, capital contributions had been fully funded.

2. Summary of significant accounting policies and nature of operations

Basis of accounting

The Partnership prepares its financial statements on the accrual basis of accounting consistent with accounting principles generally accepted in the United States of America.

Cash and cash equivalents

Cash and cash equivalents include all cash balances and highly liquid investments with maturities of three months or less at date of acquisition. Restricted cash is not considered cash equivalents.

Concentration of credit risk

The Partnership places its temporary cash investments with high credit quality financial institutions. At times, the account balances may exceed the institutions' federally insured limits. The Partnership has not experienced any losses in such accounts.

BAYBROOK PARK RETIREMENT CENTER, LTD.
NOTES TO FINANCIAL STATEMENTS
December 31, 2008

2. Summary of significant accounting policies and nature of operations (continued)

Income taxes

Income taxes on Partnership income are levied on the partners in their individual capacity. Accordingly, no provision for income taxes is reflected in the accompanying financial statements.

In July 2006, the Financial Accounting Standards Board (“FASB”) issued FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes – An Interpretation of FASB Statement No. 109* (“FIN 48”). FIN 48 prescribes detailed guidance for financial statement recognition, measurement and disclosure of uncertain tax positions recognized in an enterprise’s financial statements in accordance with SFAS No. 109, *Accounting for Income Taxes*. Pursuant to FSP-FIN 48-3, the effective date has been deferred for nonpublic organizations and will become effective for fiscal years beginning after December 15, 2008. The Partnership has elected to defer the application of FIN 48. Management believes that the implementation of FIN 48 will not have a material effect on the financial statements.

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 amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

Economic concentrations

The Partnership operates one property located in Webster, Texas. Future operations could be affected by changes in economic or other conditions in that geographical area or by changes in federal low-income housing subsidies or the demand for such housing.

Fixed assets

Fixed assets are recorded at cost. Residential rental buildings are depreciated over their estimated useful lives of 40 years using the straight-line method. Commercial space is depreciated over 39 years using the straight-line method. Site improvements are depreciated over 15 years using the straight-line method. Personal property is depreciated over 5 years using the straight-line method. Depreciation expense for 2008 was \$426,612.

Fixed assets consist of the following at December 31, 2008:

Buildings	\$ 5,038,127
Commercial space	74,031
Site improvements	1,556,649
Personal property	974,923
Less: accumulated depreciation	<u>(1,013,185)</u>
Fixed assets, net	<u>\$ 6,630,545</u>

BAYBROOK PARK RETIREMENT CENTER, LTD.
NOTES TO FINANCIAL STATEMENTS
December 31, 2008

2. Summary of significant accounting policies and nature of operations (continued)

Intangible assets

Intangible assets include permanent loan fees of \$102,741, and tax credit fees of \$44,144, which are amortized using the straight-line method over the life of the loan and tax credit period, respectively. Accumulated amortization at December 31, 2008 was \$14,122. Amortization expense for 2008 was \$9,792.

Impairment of long-lived assets

The Partnership reviews its long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying value may not be recoverable. Recoverability is measured by a comparison of the carrying amount to the future net undiscounted cash flow expected to be generated and any estimated proceeds from the eventual disposition. If the long-lived asset is considered to be impaired, the impairment to be recognized is measured at the amount by which the carrying amount exceeds the fair value as determined from an appraisal, discounted cash flows analysis, or other valuation technique. There was no impairment loss recognized for 2008.

Revenue recognition

Rental revenue attributable to residential leases is recorded when due from residents, generally upon the first day of each month. Leases are for periods of up to one year, with rental payments due monthly. Other income results from fees earned for late payments, cleaning, damages and laundry facilities and is recorded when earned.

Tenant receivables

An allowance for bad debts is not maintained. Accounts receivable are written off when they are determined to be uncollectible. Accounting principles generally accepted in the United States of America require that an allowance for uncollectible accounts be maintained in lieu of using the direct charge-off method; however, it has been determined that such an allowance would be immaterial with respect to the financial statements taken as a whole.

Ground lease

The Partnership accounts for its ground lease as an operating lease and records expense based on the average minimum yearly base lease accrual calculated over the term of the lease. The ground lease accrues at varying amounts over its term.

BAYBROOK PARK RETIREMENT CENTER, LTD.
NOTES TO FINANCIAL STATEMENTS
December 31, 2008

3. Restricted cash

Operating reserve

Pursuant to the Partnership Agreement, the General Partner was required to establish a \$175,000 operating reserve account in a segregated account to fund operating deficits. The funds may be released to pay operating expenses with the approval of the Special Limited Partner. A balance of \$151,979 is held in a certificate of deposit with Amegy Bank of Texas. The remaining balance of \$23,021 is in a non-segregated cash account and is included in "Restricted cash" on the accompanying balance sheet.

Security deposits

Tenant security deposits are deposited into the operating account and are generally held until termination of the lease, at which time some or all of the deposits may be returned to the lessee. As of December 31, 2008, the tenant security deposits balance was \$25,425 and was covered by funds in the operating account.

Insurance escrow

Monthly deposits are made to Amegy Mortgage Company, L.L.C. (the "Lender") for the payment of property insurance. All deposits are pledged as additional security for the Project mortgage. As of December 31, 2008, the insurance escrow balance was \$35,248.

Replacement reserve

Pursuant to the Partnership Agreement, the Partnership is required to make monthly deposits equal to an annual balance of \$250 per unit, increased annually by CPI. Monthly deposits are placed into an interest-bearing account held by the Lender for major repairs and improvements of the Project. Deposits to the replacement reserve account. All deposits in the account are pledged as additional security for the Project mortgage. As of December 31, 2008, the replacement reserve balance was \$20,004.

4. Related party transactions

Ground lease

In June 2005, the Partnership entered into a 65-year ground lease agreement (the "Ground Lease") with Harris County Housing Authority, a related party of the General Partner. The initial payment for the Ground Lease was \$595,427 and is amortized over the term of the lease. Under the terms of the Ground Lease, the Partnership is required to make annual lease payments of \$1,000 during the first 17 years. Beginning in year 18, the annual lease payment increases to \$65,000 for the remaining term of the Ground Lease, with all but \$1,000 of that waived, provided that the Project is leased to tenants in accordance with all applicable Low-Income Housing Requirements. As of December 31, 2008, the prepaid ground lease balance was \$559,904.

BAYBROOK PARK RETIREMENT CENTER, LTD.
NOTES TO FINANCIAL STATEMENTS
December 31, 2008

4. Related party transactions (continued)

Ground lease (continued)

Future minimum lease payments over the next five years and thereafter are as follows:

Year ending December 31,	
2009	\$ 1,000
2010	1,000
2011	1,000
2012	1,000
2013	1,000
Thereafter	<u>554,904</u>
Total	<u>\$ 559,904</u>

Property management fees

Pursuant to the property management agreement, Investors Management Group, LLC, a related party of the Class A Limited Partner, receives property management fees in the amount of 5% of the gross effective income collected from operations, provided that payment of 20% of the fee shall be subordinated to the payment of the Project's debt service and other operating expenses. During 2008, property management fees of \$36,979 were incurred. As of December 31, 2008, property management fees of \$3,198 were outstanding and included in "Accounts payable" on the accompanying balance sheet.

Development fee payable

Hettig Development Group XI, Ltd., a related party of the Class A Limited Partner, has earned a fee of \$961,788 for development services rendered in connection with the construction and development of the Project. The development fee payable bears interest at 6% per annum. Payments of principal and interest are to be made from Project cash flow and from additional capital contributions, which may be received from the Investment Limited Partner. As of December 31, 2008, development fee payable of \$286,788 and accrued interest of \$67,414 was outstanding.

Operating deficit guaranty

Pursuant to the Partnership Agreement, in the event that at any time during the period beginning upon the date Breakeven Operations is achieved and ending on the third anniversary of such date, the General Partner shall provide such funds to the Partnership as is necessary to pay operating deficits. The General Partner is not obligated to provide in excess of \$260,000, as defined by the Partnership Agreement. Operating Deficit Loans bear no interest. As of December 31, 2008, there were no guaranty amounts due or payable.

BAYBROOK PARK RETIREMENT CENTER, LTD.
NOTES TO FINANCIAL STATEMENTS
December 31, 2008

4. Related party transactions (continued)

Incentive partnership management fee

Pursuant to the Partnership Agreement, the General Partner and Class A Limited Partner may receive an annual, non-cumulative incentive partnership management fee equal to 11% of gross effective income and payable from net cash flow available for distribution. The Partnership did not achieve positive net cash flow during 2008, as described in the Partnership Agreement, and therefore no incentive partnership management fee was incurred.

Asset management fees

Pursuant to the Partnership Agreement and subject to the priority distributions of net cash flow as defined in the Partnership Agreement, the Special Limited Partner may receive an annual cumulative asset management fee of \$5,000, adjusted for the change in the Consumer Price Index in effect on the date of adjustment over the date in effect twelve months prior, for its services in monitoring the operations of the Partnership. During 2008, asset management fees of \$5,305 were incurred. As of December 31, 2008, asset management fees of \$429 were outstanding and are included in "Accrued expenses" in the accompanying balance sheet.

5. Mortgage loan payable

On December 14, 2007, construction financing of \$3,300,000 was converted to permanent financing for the Project from the Lender. The mortgage payable bears interest at the rate of 6.44% and is due and payable in 180 consecutive monthly installments of principle and interest, commencing in February 2008. The mortgage payable is collateralized by the Project. As of December 31, 2008, the total outstanding principal balance was \$3,263,808 and no interest was outstanding.

Future minimum principal payment requirements over each of the next five years and thereafter are as follows:

Year ending December 31,	
2009	\$ 39,034
2010	41,662
2011	44,465
2012	46,868
2013	50,611
Thereafter	<u>3,041,168</u>
Total	<u>\$ 3,263,808</u>

BAYBROOK PARK RETIREMENT CENTER, LTD.
NOTES TO FINANCIAL STATEMENTS
December 31, 2008

6. Home loan

In June 2005, the Partnership obtained a HOME loan (the "HOME loan") in the total amount of \$625,000 from Harris County Housing Authority. The HOME loan accrues interest on the outstanding balance at the applicable federal interest rate (AFR) in place on the date of the agreement, which was 4.57%. The HOME loan matures on August 31, 2027 and is collateralized by the Project and is subordinate to the mortgage. Payments of principal and unpaid interest are required at maturity. During 2008, interest of \$28,563 was incurred and no payments were made during the year. As of December 31, 2008, principal and accrued interest of \$625,000 and \$88,126, respectively, were outstanding.

7. Property exemption

In 2005, the Partnership applied for and was granted exemption from property tax by the Harris County Appraisal District, pursuant to Section 392.005 of the Texas Local Government Code. Pursuant to the code, a multifamily residential development which is owned by a housing authority is property tax exempt. The Partnership entered into an agreement for payments in lieu of taxes with Galveston appraisal district based on net lease payments.

8. Low-income housing tax credits

The Partnership expects to generate an aggregate of \$4,849,810 of low-income housing tax credits ("Tax Credits"). The Tax Credits include an annual allocation of \$445,118 from 2004 and an additional annual allocation of \$39,863 allocated in 2007. Generally, such Tax Credits are expected to become available for use by the partners pro-rata over a ten-year period that began in 2006 and 2007. In order to qualify for these Tax Credits, the Project must comply with various federal and state requirements. These requirements include, but are not limited to, renting to low-income tenants at rental rates, which do not exceed specified percentages of area median gross income for the first 15 years of operation. The Partnership has also agreed to maintain and operate the Project as low-income housing for another 15 years after that period ends. Because the Tax Credits are subject to certain compliance requirements, there can be no assurance that the aggregate amount of Tax Credits will be realized and failure to meet all such requirements may result in less Tax Credits than expected.