

Desert Palms Apartments Limited Partnership

**Financial Statements
And Supplementary Information**

Year Ended December 31, 2010

Desert Palms Apartments Limited Partnership

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Kenneth C. Boothe, P.C.

Certified Public Accountant

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INDEPENDENT AUDITOR'S REPORT

To the Partners of

Desert Palms Apartments Limited Partnership
Las Cruces, New Mexico

We have audited the accompanying balance sheet of Desert Palms Apartments Limited Partnership, as of December 31, 2010, and the related statements of operations, changes in 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 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 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 Desert Palms Apartments Limited Partnership as of December 31, 2010, and the results of its operations, changes in partners' equity, and its 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 May 2, 2011, on our consideration of Desert Palms Apartments Limited Partnership's internal control over financial reporting. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and the results of that testing and not to provide an opinion on internal control over financial reporting. In accordance with *Government Auditing Standards*, we have also issued an opinion dated May 2, 2011 on Desert Palms Apartments Limited Partnership's compliance with certain provisions of laws, regulations, contracts, and grant agreements, and other matters that could have a direct and material effect on a major HUD-assisted program. Those reports are an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The accompanying supplemental information shown on Pages 19 - 20 is presented for purposes of additional analysis and is not a required part of the basic financial statements of the Company. Such information has been subjected to the auditing procedures applied in the audit of the financial statements and, in our opinion, is fairly stated in all material respects in relation to the financial statements taken as a whole.



Kenneth C. Boothe, P.C.

May 2, 2011
Big Spring, Texas

Desert Palms Apartments Limited Partnership

Balance Sheet

December 31, 2010

ASSETS

	<u>12/31/2010</u>
Current Assets:	
Cash and Cash Equivalents	\$ 4,117
Accounts Receivable - Tenants	2,493
Prepaid Expenses	13,303
Total Current Assets	<u>19,913</u>
Restricted Deposits & Funded Reserves:	
Tenant Security Deposits	30,856
Real Estate Tax & Insurance	15,190
Other Escrows	2,075
Replacement Reserve	118,104
Operating Reserve	15,328
Total Restricted Deposits & Funded Reserves	<u>181,553</u>
Property & Equipment:	
Land	200,000
Buildings	3,336,784
Site Improvements	273,742
Furnishings	416,161
Maintenance Equipment	609
Accumulated Depreciation	(870,013)
Total Property & Equipment	<u>3,357,283</u>
Other Assets:	
Deferred Finance Cost	90,117
Amortization	(31,267)
Total Other Assets	<u>58,850</u>
Total Assets	<u>\$ 3,617,599</u>

*The accompanying notes are an integral part
of these financial statements*

Desert Palms Apartments Limited Partnership

Balance Sheet

December 31, 2010

LIABILITIES & PARTNERS' EQUITY

12/31/2010

Liabilities:

Current Liabilities:

Current Maturities of Long-Term Debt	\$ 17,323
Accounts Payable	44,607
Accrued Interest	9,210
Accrued Expenses	9,311
Accrued - Property Taxes	6,967
Notes Payable - Insurance	3,983
Total Current Liabilities	<u>91,401</u>

Deposits & Prepaid Liabilities:

Tenant Security Deposits	29,437
Prepaid Tenant Fees	3,544
Total Deposits & Prepaid Liabilities	<u>32,981</u>

Long-Term Liabilities:

Long-Term Debt (net of current maturities)	1,969,167
Long-Term Accrued Interest	56,960
Deferred Development Fees	193,939
Asset Management Fee / Return to Owner	26,650
Total Long-Term Liabilities	<u>2,246,716</u>
Total Liabilities	<u>2,371,098</u>

Partners' Equity (Deficit)

1,246,501

Total Liabilities & Partners' Equity

\$ 3,617,599

*The accompanying notes are an integral part
of these financial statements*

Desert Palms Apartments Limited Partnership

Statement of Operations

For the Year Ended December 31, 2010

	<u>12/31/2010</u>
Rental Income:	
Rental Income - Tenant Portion	\$ 411,423
Rental Income - PHA	32,277
Potential Rental Income	<u>443,700</u>
Lease Excess	13,039
Less: Vacancies	(92,287)
Less: Concessions	(2,548)
Total Rental Income	<u>361,904</u>
Other Income:	
Interest Income	741
Laundry & Vending	1,187
Tenant Charges	20,962
Miscellaneous Income	1,886
Total Other Income	<u>24,776</u>
Total Income	<u>386,680</u>
Operating Expenses:	
Administrative	93,431
Utilities	34,493
Maintenance	73,643
Taxes & Insurance	52,568
Financial Expense	133,708
Total Cost of Operations	<u>387,843</u>
Net Income/(Loss) from Operations	<u>(1,163)</u>
Non-Operating Income & (Expenses):	
Investor Service Fees	(13,140)
Depreciation Expense	(160,071)
Amortization Expense	(2,209)
Total Non-Operating Income & (Expenses)	<u>(175,420)</u>
Net Income/(Loss)	<u><u>\$ (176,583)</u></u>

*The accompanying notes are an integral part
of these financial statements*

Desert Palms Apartments Limited Partnership
Statement of Changes in Partners' Equity (Deficit)
For the Year Ended December 31, 2010

	Total	General Partner Equity	Limited Partner Equity
Partners' Equity (Deficit), December 31, 2009	\$ 1,361,395	\$ 283,877	\$ 1,077,518
Net Income/(Loss): 12/31/2010	(176,583)	(61,701)	(114,882)
Partners' Capital Contributions	61,689	61,689	0
Partners' Distributions	0	0	0
Partners' Equity (Deficit), December 31, 2010	\$ 1,246,501	\$ 283,865	\$ 962,636

*The accompanying notes are an integral part
of these financial statements*

Desert Palms Apartments Limited Partnership
Statement of Cash Flows
For the Year Ended December 31, 2010
Increase (Decrease) in Cash and Cash Equivalents

	12/31/2010
Cash Flows From Operating Activities:	
Revenue:	
Rental Receipts	\$ 338,685
Rental Income - PHA	32,277
Other Income	22,890
Miscellaneous Income	1,886
Total Receipts	395,738
Expenses:	
Administrative	(117,206)
Utilities	(39,637)
Maintenance	(78,794)
Taxes & Insurance	(57,944)
Financial Expense	(133,783)
Tenant Security Deposits	(1,419)
Total Disbursements	(428,783)
Net Cash from Operating Activities:	(33,045)
Cash Flows From Investing Activities:	
Purchase Property & Equipment	(8,353)
Real Estate Tax & Insurance	(7,544)
Other Escrows	90
Replacement Reserve	(30,659)
Operating Reserve	(81)
Net Cash from Investing Activities:	(46,547)
Cash Flows From Financing Activities:	
Principal Payments on Mortgage	(16,239)
Long-Term Accrued Interest	13,672
Accounts Receivable - Related Parties	21,679
Partners' Capital Contributions	61,689
Net Cash from Financing Activities:	80,801
Increase (Decrease) In Cash	1,209
Cash at Beginning of Period	2,908
Cash at End of Period	\$ 4,117

*The accompanying notes are an integral part
of these financial statements*

Desert Palms Apartments Limited Partnership
Statement of Cash Flows
For the Year Ended December 31, 2010
Increase (Decrease) in Cash and Cash Equivalents

	12/31/2010
Reconciliation of Net Profit (Loss) to Net Cash Provided by Operating Activities:	
Net Income (Loss)	\$ (176,583)
Adjustments to Reconcile Net Profit (Loss) to Net Cash Provided by (Used in) Operating Activities:	
Depreciation Expense	160,071
Amortization Expense	2,209
(Increase) Decrease In Assets	
Accounts Receivable - Tenants	7,044
Prepaid Expenses	531
Tenant Security Deposits	(7,198)
Increase (Decrease) In Liabilities	
Accounts Payable	(37,106)
Accrued Interest	(75)
Accrued Expenses	2,507
Accrued - Property Taxes	(5,376)
Tenant Security Deposits	5,779
Prepaid Tenant Fees	2,012
Asset Management Fee / Return to Owner	13,140
Net Cash from Operating Activities:	\$ (33,045)
<u>Supplemental Disclosures:</u>	
Interest Paid	\$ 110,952

*The accompanying notes are an integral part
of these financial statements*

Desert Palms Apartments Limited Partnership

NOTES TO FINANCIAL STATEMENTS

December 31, 2010

NOTE A - ORGANIZATION

Desert Palms Apartments Limited Partnership was organized in 2003 as a Limited Partnership to develop, construct, own, maintain, and operate a 101-unit rental housing project for mixed income tenants with both tax credit and market rate units. The Project is located in the city of Las Cruces, New Mexico, and is currently known as Desert Palms Apartments. The major activities of the Partnership are governed by the Partnership Agreement and the Internal Revenue Code Section 42.

The management of the Partnership and the ongoing management of Desert Palms Apartments are vested in the Partners. The Partnership has hired JL Gray Company to provide day to day management for the property. Compensation for such services is as determined under the Partnership Agreement and Management Agreement.

The Project is financed and constructed under Section 542(c) of the Housing and Community Development Act, as amended, and is administered by the New Mexico Mortgage Finance Authority (MFA). Under this program, the Company provides housing to low and moderate income tenants, subject to regulation by MFA and the United States Department of Housing and Urban Development (HUD), as to rental charges and operating methods. Lower rental charges to tenants are recovered by the Project through rent subsidies provided by the local Public Housing Authority (PHA).

The Partnership is reported as a component unit of the Housing Authority of the City of Las Cruces because the Housing Authority of the City of Las Cruces (HACLIC) is the General Partner of the Partnership. The Partnership has no component units.

NOTE B - SIGNIFICANT ACCOUNTING POLICIES

A summary of the Partnership's significant accounting policies consistently applied in the preparation of the accompanying financial statements are as follows:

Basis of Accounting

The Partnership utilized the accrual basis of accounting, whereby income is recognized as earned and expenses are recognized as obligations are incurred.

Cash and Cash Equivalents

Cash and cash equivalents consist of unrestricted short-term investments with an original maturity of three months or less, cash on deposit, money market funds and certificates of deposit.

Cash and Other Deposits

The Partnership maintains its cash in financial institutions insured by the Federal Deposit Insurance Corporation (FDIC). Deposit accounts, at times, may exceed federally insured limits. The Partnership has not experienced any losses in such accounts and believes it is not exposed to any significant credit risk on cash and cash equivalents.

Desert Palms Apartments Limited Partnership

NOTES TO FINANCIAL STATEMENTS

December 31, 2010

NOTE B - SIGNIFICANT ACCOUNTING POLICIES (continued)

Tenants' Security Deposits

Tenants' security deposits are held in a separate bank account. This account was funded in an amount greater than the security deposit liability as of December 31, 2010.

Tenant Receivable and Bad Debt Policy

Tenant rent charges for the current month are due on the first of the month. The Partnership does not accrue interest on the tenant receivable balances. The Partnership has not established an allowance for doubtful accounts and does not use the reserve method for recognizing bad debts. Bad debts are treated as direct write-offs in the period management determines that collection is not probable.

Rental Property

Rental property is recorded at cost. Improvements are capitalized, while expenditures for maintenance and repairs are expensed as incurred. Upon disposal of depreciable property, the appropriate property accounts are reduced by the related costs and accumulated depreciation. The resulting gains and losses are reflected in the statement of operations. Depreciation is provided for in amounts sufficient to relate the cost of depreciable assets to operations over their estimated service lives using the straight-line method.

The Partnership 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 rental property including the Low Income Housing Tax Credits and any estimated proceeds from the eventual disposition of the real estate. If the real estate is considered to be impaired, the impairment to be recognized is measured at the moment by which the carrying amount of the real estate exceeds the fair value of such property. There were no impairment losses recognized in 2010.

Income Taxes

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

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 revenues and expenses during the reporting period. Actual results could differ from those estimates.

Desert Palms Apartments Limited Partnership

NOTES TO FINANCIAL STATEMENTS

December 31, 2010

NOTE B - SIGNIFICANT ACCOUNTING POLICIES *(continued)*

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 the tenants of the property are operating leases.

NOTE C - PARTNERS' PROFIT AND LOSS ALLOCATION AND DISTRIBUTIONS

The Partners of Desert Palms Apartments Limited Partnership and their respective profit and loss percentages are as follows for the period from December 31, 2009 to January 25, 2010:

General Partner:	
<i>CAASNM, LLC</i>	0.01 %
Limited Partner:	
<i>Freddie Mac Equity Plus II, ESIC</i>	<u>99.99 %</u>
Total	<u>100.00 %</u>

The Partners of Desert Palms Apartments Limited Partnership and their respective profit and loss percentages are as follows for the period from January 25, 2010 to December 31, 2010:

General Partner:	
<i>Desert Palms Apartments LLC</i>	0.01 %
Limited Partner:	
<i>Freddie Mac Equity Plus II, ESIC</i>	<u>99.99 %</u>
Total	<u>100.00 %</u>

Desert Palms Apartments Limited Partnership

NOTES TO FINANCIAL STATEMENTS

December 31, 2010

NOTE C - PARTNERS' PROFIT AND LOSS ALLOCATION AND DISTRIBUTIONS *(continued)*

Cash Flow Distribution

Distributable cash flow is defined in the Partnership Agreement as the sum of all cash receipts less cash disbursements for operating activities and Replacement Reserve funding. Distributable cash flow is payable annually as follows:

1. To the Limited Partner an amount equal to the credit deficiency;
2. To the Limited Partner an amount sufficient to pay federal income taxes on taxable income allocated to the Limited Partner for such Fiscal Year by the Partnership, assuming the highest marginal tax rates applicable to corporations;
3. To pay the Investor Services Fee in accordance with the Investor Services Agreement;
4. To fund the Operating Reserves after the Capital Contributions of the Limited Partner has paid up to the Operating Reserve Amount;
5. To pay any Deferred Development Fee in accordance with the Development Services Agreement;
6. To pay the General Partner to repay any Operating Deficit Contributions;
7. To pay the Partnership Administration Fee in accordance with the Partnership Administration Agreement; and
8. Any remaining cash flow shall be distributed to the Partners in accordance with the following percentage, Investor Limited Partner, 99.99% to the General Partner .01%.

Distribution of proceeds from a sale or refinancing:

1. To the Limited Partner in the amount of the federal income tax liability that would be imposed on the Limited Partner and its Partners from the transaction giving rise to Sale or Refinancing Proceeds, assuming all such Persons are subject to federal income tax at a rate of thirty-five percent (35%);
2. To the Limited Partner an amount equal to the Credit Deficiency;
3. To ESIC in the amount of any unpaid Investor Services Fee;
4. To pay any unpaid Development Fee;
5. To the General Partner to repay any Operating Deficit Contribution, Credit Adjuster Advance or Additional Advance; and
6. The balance shall be distributed to the Partners in accordance with the following percentages, Investor Limited Partner, 99.99% to the General Partner .01%.

Desert Palms Apartments Limited Partnership

NOTES TO FINANCIAL STATEMENTS

December 31, 2010

NOTE C - PARTNERS' PROFIT AND LOSS ALLOCATION AND DISTRIBUTIONS (continued)

Partner Contributions

The Partnership's General Partner and Investor Limited Partner are required to make capital contributions totaling \$283,954 and \$1,891,396, respectively. In accordance with the Partnership Agreement the Limited Partner's capital contributions have been adjusted by \$21,488 which reduces the capital contributions to \$1,869,908. The Investor Limited Partner, Freddie Mac Equity Plus II, ESIC, has made capital contributions totaling \$1,794,712. The prior General Partner, CAASN, LLC, paid the capital contributions in full. They also contributed additional funds of \$61,689 for the year ended December 31, 2010. The General Partner is allocated additional loss in relation to their operating deficit contributions.

NOTE D - LONG-TERM DEBT

The Project is financed with a 35-year mortgage payable to New Mexico Mortgage Finance Authority in the original amount of \$1,705,000, with an interest rate of 6.48%. The mortgage is payable in monthly installments of \$10,277 through October 1, 2041. The accrued interest was \$8,876 as of December 31, 2010. Interest expensed on this loan was \$107,003 as of December 31, 2010.

12/31/2010

\$ 1,643,746

The Project also has a mortgage payable to City of Las Cruces in the original amount of \$342,744. Interest will accrue on the outstanding principal balance of the loan at the annual rate of 4.94% compounded annually. Accrued but unpaid interest shall bear interest at 3.94%. Monthly installments of \$285 to be paid for the first fifteen years, which represents interest only payments of 1%. After the end of year fifteen the principal and accrued interest will accrue interest at the rate of 4.94% per annum and become due and payable in 179 monthly installments of \$4,820, including principal and interest. Maturity of the loan occurs at the sale, refinance, and transfer of the property or on September 2034. The short-term accrued interest was \$333 as of December 31, 2010. The long-term accrued interest was \$56,960 as of December 31, 2010. Interest expensed on this loan was \$17,546 as of December 31, 2010.

342,744

Total
Less: Current Portion
Long-Term Notes Payable

1,986,490

17,323

\$ 1,969,167

Desert Palms Apartments Limited Partnership

NOTES TO FINANCIAL STATEMENTS

December 31, 2010

NOTE D - LONG-TERM DEBT (continued)

Aggregate maturities of the notes are approximated as follows:

	<u>Principal</u>	<u>Interest</u>
December 31, 2011	\$ 17,323	\$ 110,621
2012	18,479	109,646
2013	19,713	108,601
2014	21,029	107,482
2015	22,433	106,282
2016-2020	136,731	510,199
2021-2025	282,803	434,528
2026-2030	375,935	355,710
2031-2035	475,467	256,179
2036-2040	612,964	118,681
2041	120,870	2,988
	<u>2,103,747</u>	<u>2,220,917</u>
Total	<u>\$ 2,103,747</u>	<u>\$ 2,220,917</u>

Long-term accrued interest on the HOME loan in the amount of \$117,256 becomes principal and is amortized when principal payments begin December of 2021.

The apartment project is pledged as collateral for the mortgage. The mortgage loan is nonrecourse debt secured by deeds of trust on the related real estate.

NOTE E - RESERVE FUNDS

Replacement Reserve

In accordance with the Partnership Agreement, the Partnership shall establish a Replacement Reserve at the time of the fourth installment to fund major repairs or replacements of the Project Property. The Partnership shall make deposits into the Replacement Reserve fund of \$29,000 annually commencing with the completion of the Project. The Replacement Reserve balance was \$118,104 as of December 31, 2010.

Operating Reserve

The General Partner is required to establish and maintain an Operating Reserve on the date of the fourth capital contribution in the amount of \$75,000. The Operating Reserve should be funded from Net Cash Flow. There has not been sufficient cash flow to replenish the account. The Operating Reserve balance was \$15,328 as of December 31, 2010.

Desert Palms Apartments Limited Partnership

NOTES TO FINANCIAL STATEMENTS

December 31, 2010

NOTE F - COMMITMENTS AND CONTINGENCIES

Housing Tax Credits

As incentive for investment equity, the Partnership applied for and received an allocation certificate for Housing Tax Credits established by the Tax Reform Act of 1986. To qualify for the Tax Credits, the Partnership must meet certain requirements, including attaining a qualified basis sufficient to support the credit allocation. In addition, tenant eligibility and rental charges are restricted in accordance with Internal Revenue Code Section 42. Management has certified that each Tax Credit unit has met these qualifications to allow the credits allocated to each unit be claimed.

Compliance with these regulations must be maintained in each of the fifteen consecutive years of the compliance period. Failure to maintain compliance with occupant eligibility, unit gross rent, or to correct noncompliance within a reasonable time period could result in recapture of previously claimed Tax Credits plus interest.

HOME Investment Partnerships Program

In addition, the Partnership received funding from the HOME Investment Partnerships Program to assist with financing the development of the Project. Under the terms of the agreement, ten units shall be designated as floating HOME assisted units.

NOTE G - TRANSACTIONS WITH AFFILIATES AND RELATED PARTIES

Management Fee

In accordance with the Management Agreement, the Partnership has incurred Management Fee expenses for services rendered in connection with the leasing and operation of the Project. The current year management fee is equal to 5.5% of gross rental collections. Property Management Fees expensed were \$21,450 during 2010. The amount included in accounts payable that is due to the Management Agent related to Management Fees was \$22,519 as of December 31, 2010.

Owner Distribution - Investor Services Fee

In accordance with the Partnership Agreement, the Partnership shall pay to the Limited Partner an Investor Services Fee in the amount of \$4,000 beginning in 2004. The fee shall increase at a rate of 3% per year thereafter. The Investor Services Fee shall be payable from the available cash flows. Any unpaid fees may accrue for payment in subsequent years. Investor Services Fees of \$13,140 were recognized during 2010. The amount due to the Limited Partner related to Investor Services Fees was \$26,650 as of December 31, 2010.

Owner Distribution - Partnership Administrative Fee

In accordance with the Partnership Agreement, the Partnership shall pay to the General Partner a Partnership Administrative Fee in the annual amount of \$25,000. The fee shall increase at a rate of 3% per year thereafter. The Partnership Administration Fee shall be payable from the available cash flows. Any unpaid fees may accrue for payment in subsequent years. There were no Partnership Administrative Fees accrued during 2010.

Desert Palms Apartments Limited Partnership

NOTES TO FINANCIAL STATEMENTS

December 31, 2010

NOTE G - TRANSACTIONS WITH AFFILIATES AND RELATED PARTIES (continued)

Development Fee

The Partnership has incurred a Development Fee of \$203,230 due to JL Gray Company and CAASNM, the General Partner, rendered to the Partnership for overseeing the construction of the Project. This Development Fee has been capitalized into the basis of the building. As of December 31, 2010, \$9,290 of this fee has been paid. The amount due related to Development Fees was \$193,939 as of December 31, 2010. Of the remaining balance, \$172,260 is considered Deferred Development Fees and is payable from cash flow according to the priority of payments and distributions in Note C.

Laundry Lease

The Partnership leased space for the installation and operation of coin-operated laundry and vending machine equipment to JL Gray Company for fifty percent (50%) of the laundry room receipts after Gross Receipts Tax. This lease continues in effect until terminated by either party. The Partnership received rental income of \$1,187 for the year ended December 31, 2010.

Reimbursed Expenses

The Management Agent is reimbursed for a few expenses that are directly related to this property. Due to the nature and function of the Management Agent, some expenses are incurred for the property by the Management Agent. For example, the properties do not have access to credit cards in order to directly pay necessary items such as seminars and motels. These reimbursements qualify as eligible project expenses and do not duplicate expenses that are included in the management fee. The reimbursement is considered both reasonable and immaterial. The amount due to the Management Agent related to reimbursed expenses is considered negligible as of December 31, 2010.

Operating Deficit Loans

Pursuant to the Partnership Agreement, the General Partner has guaranteed to fund all deficits through the later of Permanent Loan Closing and achievement of a Debt Service Coverage Ratio of 1:15:1 for 90 days, as defined. Subsequent to Permanent Loan Closing or achievement of the Debt Service Coverage Ratio, funding up to an additional \$275,000 of operating deficits is guaranteed. The requirement to fund additional operating deficits will terminate on the date the following occurs:

1. The Project has operated at Break-even three consecutive calendar years following the stabilization date of the Project;
2. The Project has met the required Debt Service Coverage for three years;
3. The balance in the Operating Reserve equals or exceeds the Operating Reserve amount.

The General Partner obligations shall be Guaranteed by the Guarantor (JL Gray Company) as defined in the Guaranty Agreement.

Desert Palms Apartments Limited Partnership

NOTES TO FINANCIAL STATEMENTS

December 31, 2010

NOTE G - TRANSACTIONS WITH AFFILIATES AND RELATED PARTIES (continued)

Regulatory Agreement Provisions

On February 5, 2001, the Company executed a 542 (c) Multifamily Insurance Program Regulatory Agreement with the New Mexico Mortgage Finance Authority in order to obtain the "risk-sharing" mortgage loan. The Company is required to abide by the Regulatory Agreement provisions including, but not limited to, (1) the maintenance of certain tenant income requirements, (2) limitations on surplus cash distributions, (3) Replacement Reserve requirements, and (4) compliance with Affirmative Fair Housing marketing plans.

NOTE H - TAXABLE INCOME

A reconciliation of financial statement net income/(loss) to taxable income/(loss) of the Partnership for the year ended December 31, 2010 is as follows:

Financial statement net income/(loss)	\$(176,583)
Adjustments	0
Timing differences	<u>(17,792)</u>
Taxable income/(loss) as shown on tax return	<u><u>\$(194,375)</u></u>

NOTE I - CURRENT VULNERABILITY DUE TO CERTAIN CONCENTRATIONS

The Partnership's sole asset is Desert Palms Apartments. The Partnership's operations are concentrated in the multifamily real estate market. In addition, the Partnership operates in a heavily regulated environment. The operations of the Partnership are subject to the administrative directives, rules, and regulations of federal, state, and local regulatory agencies. Such administrative directives, rules, and regulations are subject to change 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.

NOTE J - CONTINGENT LIABILITIES

Community Action Agency of Southern New Mexico, the prior General Partner, reported a loan due by the property in prior years. Due to controversy regarding the prior General Partner entering into Loan Agreement without the consent of the Limited Partner, the liabilities were not reflected in the financial statements and prior payments made were reclassified as an accounts receivable from the prior General Partner. This receivable was offset by payments contributed by the General Partner during 2010. There was no amount due from the prior General Partner as of December 31, 2010.

NOTE K - ACCRUED LIABILITIES

The accrued liabilities on the balance sheet contain the following:

Accrued Payroll Expenses	\$ 511
Accrued Audit Fees	<u>8,800</u>
Total Accrued Liabilities	<u><u>\$ 9,311</u></u>

Desert Palms Apartments Limited Partnership

NOTES TO FINANCIAL STATEMENTS

December 31, 2010

NOTE L - SUBSEQUENT EVENTS

Subsequent events have been evaluated through May 2, 2011 which is the date the financial statements were available to be issued and there are no subsequent events requiring disclosure.

**Desert Palms Apartments Limited Partnership
Supplemental Information Required by HUD
Year Ended December 31, 2010**

Desert Palms Apartments Limited Partnership
Supplementary Information Required by HUD
Year Ending December 31, 2010

1. SCHEDULE OF RESERVE FOR REPLACEMENTS

Balance as of January 1, 2010	\$ 87,445
Deposits	30,000
Interest Earned on Reserve for Replacement Account (Net of Service Fees)	659
Balance as of December 31, 2010	\$ 118,104

Deposits Suspended or Waived Indicator No

2. SCHEDULE OF OPERATING RESERVE

Balance as of January 1, 2010	\$ 15,247
Deposits	0
Interest Earned on Operating Reserve Account (Net of Service Fees)	81
Balance as of December 31, 2010	\$ 15,328

3. SCHEDULE OF CHANGES IN FIXED ASSETS

	Balance 1/1/2010	Additions	Deductions	Balance 12/31/2010
Land	\$ 200,000	\$ 0	\$ 0	\$ 200,000
Buildings	3,336,784	0	0	3,336,784
Site Improvements/Building Equipment	273,742	0	0	273,742
Furnishings	407,807	8,354	0	416,161
Maintenance Equipment	609	0	0	609
Totals	\$ 4,218,942	\$ 8,354	\$ 0	\$ 4,227,296
Accumulated Depreciation	\$ 709,942	\$ 160,071	\$ 0	\$ 870,013
Net Book Value	\$ 3,509,000			\$ 3,357,283

Schedule of Additions to Fixed Assets:

	12/31/2010
Appliances	8,354
Totals:	\$ 8,354

Desert Palms Apartments Limited Partnership
Computation of Surplus Cash, Distributions and Residual Receipts
Year Ending December 31, 2010

		<u>12/31/2010</u>
Cash:		
	Cash	34,973
	Total Cash	<u>\$ 34,973</u>
Current Obligations:		
	Accrued Mortgage Interest Payable	9,210
	Accounts Payable - 30 Days	44,607
	Loans and Notes Payable (due w/in 30 days)	3,983
	Accrued Expenses (not escrowed)	9,311
	Prepaid Revenue	3,544
	Tenant Security Deposits Liability	29,437
	Total Current Obligations	<u>100,092</u>
	Surplus Cash (Deficiency)	<u>\$ (65,119)</u>
Required Deposit to Residual Receipts:		
	Surplus Cash	<u>\$ 0</u>

Kenneth C. Boothe, P.C.

Certified Public Accountant

1001 East Farm Road 700 • Big Spring, Texas 79720 • (432) 263-1324 • FAX (432) 263-2124

INDEPENDENT AUDITOR'S COMBINED REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING BASED ON AN AUDIT OF FINANCIAL STATEMENTS AND INTERNAL CONTROL OVER COMPLIANCE FOR HUD-ASSISTED PROGRAMS

To the Partners of
Desert Palms Apartments Limited Partnership
Las Cruces, New Mexico

We have audited the financial statements of Desert Palms Apartments Limited Partnership as of and for the year ended December 31, 2010, and have issued our report thereon dated May 2, 2011. We have also audited the Partnership's compliance with requirements applicable to major U.S. Department of Housing and Urban Development (HUD)-assisted programs and have issued our report thereon dated May 2, 2011.

We conducted our audits 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 *Consolidated Audit Guide for Audits of HUD Programs* (the "Guide"), issued by the HUD Office of the Inspector General. Those standards and the Guide require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and about whether the Partnership complied with laws and regulations, noncompliance with which would be material to a major HUD-assisted program.

The management of Desert Palms Apartments Limited Partnership is responsible for establishing and maintaining effective internal control over financial reporting and internal control over compliance. In planning and performing our audit of the financial statements and compliance, we considered the Partnership's internal control over financial reporting and its internal control over compliance with requirements that could have a direct and material effect on a major HUD-assisted program as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements and on compliance, but not for the purpose of expressing an opinion on the effectiveness of the Partnership's internal control. Accordingly, we do not express an opinion on the effectiveness of the Partnership's internal control over financial reporting and internal control over compliance.

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 (1) misstatements of the entity's financial statements, or (2) noncompliance with applicable requirements of a HUD-assisted program 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 (1) a material misstatement of the entity's financial statements or (2) material noncompliance with applicable requirements of a HUD-assisted program will not be prevented, or detected and corrected, on a timely basis.

Our consideration of internal control over financial reporting and internal control over compliance was for the limited purpose described above and would not necessarily identify all deficiencies in internal control 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 the audit committee, management, others within the entity, and HUD and is not intended to be and should not be used by anyone other than these specified parties.



Kenneth C. Boothe, P.C.

May 2, 2011
Big Spring, Texas

Kenneth C. Boothe, P.C.

Certified Public Accountant

1001 East Farm Road 700 • Big Spring, Texas 79720 • (432) 263-1324 • FAX (432) 263-2124

INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE WITH SPECIFIC REQUIREMENTS APPLICABLE TO MAJOR HUD PROGRAMS

To the Partners of
Desert Palms Apartments Limited Partnership
Las Cruces, New Mexico

We have audited Desert Palms Apartments Limited Partnership's compliance with the specific program requirements governing tenant application, eligibility, and recertification; units leased to extremely low-income families; tenant security deposits; management functions, fair housing and non-discrimination; unauthorized change of ownership/acquisition of liabilities; unauthorized transfer of beneficial interest; unauthorized loans of project funds; federal financial reports; cash receipts and disbursements; mortgage status; the replacement reserve; the residual receipts; distributions to owners; equity skimming; electronic submission verification; and excess income that are applicable to each of its major HUD-assisted programs for the year ended December 31, 2010. Compliance with those requirements is the responsibility of the Partnership's management. Our responsibility is to express an opinion on the Partnership's 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 *Consolidated Audit Guide for Audits of HUD Programs* (the "Guide"), issued by the U.S. Department of Housing and Urban Development, Office of the Inspector General. Those standards and the Guide require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the requirements referred to above that could have a direct and material effect on a major HUD-assisted program occurred. An audit includes examining, on a test basis, evidence about the Partnership's 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 of the Partnership's compliance with those requirements.

The results of our audit procedures disclosed no instances or other matters that are required to be reported under *Government Auditing Standards*.

In our opinion, Desert Palms Apartments Limited Partnership complied, in all material respects, with the requirements referred to above that are applicable to each of its major HUD-assisted programs for the year ended December 31, 2010.

This report is intended solely for the information and use of management, others within the entity, and the Department of Housing and Urban Development and is not intended to be and should not be used by anyone other than these specified parties.



Kenneth C. Boothe, P.C.

May 2, 2011
Big Spring, Texas

Kenneth C. Boothe, P.C.

Certified Public Accountant

1001 East Farm Road 700 • Big Spring, Texas 79720 • (432) 263-1324 • FAX (432) 263-2124

INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE WITH SPECIFIC REQUIREMENTS APPLICABLE TO FAIR HOUSING AND NON-DISCRIMINATION

To the Partners of
Desert Palms Apartments Limited Partnership
Las Cruces, New Mexico

We have applied procedures to test Desert Palms Apartments Limited Partnership's compliance with the Fair Housing and Non-Discrimination requirements applicable to its HUD-assisted programs for the year ended December 31, 2010.

Our procedures were limited to the applicable compliance requirement described by the *Consolidated Audit Guide for Audits of HUD Programs* (the "Guide") issued by the U.S. Department of Housing and Urban Development, Office of the Inspector General. Our procedures were substantially less in scope than an audit, the objective of which is the expression of an opinion on Desert Palms Apartments Limited Partnership's compliance with the Fair Housing and Non-Discrimination requirements. Accordingly, we do not express such an opinion.

The results of our tests disclosed no instances of noncompliance that are required to be reported herein under the Guide.

This report is intended solely for the information and use of the audit committee, management, others within the entity, and the U.S. Department of Housing and Urban Development and is not intended to be and should not be used by anyone other than these specified parties.



Kenneth C. Boothe, P.C.

May 2, 2011
Big Spring, Texas

Desert Palms Apartments Limited Partnership

Schedule of Findings and Responses

December 31, 2010

Current Year Audit Findings: December 31, 2010

None Noted

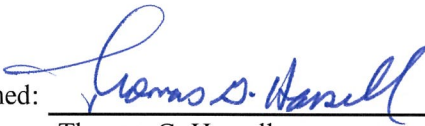
Desert Palms Apartments Limited Partnership

Mortgagor's Certification

December 31, 2010

We hereby certify that we have examined the accompanying financial statements and supplemental information of Desert Palms Apartments Limited Partnership as of December 31, 2010, and to the best of our knowledge and belief, the same are complete and accurate.

Signatories:

Signed:  Date: 5-27-11
Thomas G. Hassell
Housing Authority of the City of Las Cruces

Auditee Information:

505-325-6515
May 2, 2011
Desert Palms Apartments Limited Partnership
2405 W. Picacho
Las Cruces
New Mexico
88007
Thomas G. Hassell
Housing Authority of the City of Las Cruces

Desert Palms Apartments Limited Partnership

Management Agent's Certification

December 31, 2010

We hereby certify that we have examined the accompanying financial statements and supplemental information of Desert Palms Apartments Limited Partnership as of December 31, 2010, and to the best of our knowledge and belief, the same are complete and accurate.

Signed: _____ Date: _____

Name: Bobby Griffith

Title: CFO - Senior Executive

Management
Company: JL Gray Company

Address: 1816 East Mojave St.
Farmington, NM 87401

Federal I.D.
Number: 85-0327246

Desert Palms Apartments Limited Partnership

Information on Auditor

December 31, 2010

Auditor's Transmittal Letter

Audit Firm: Kenneth C. Boothe, P.C.
State of Texas License No. 11767
State of New Mexico License No. 10015

Lead Auditor: Kenneth C. Boothe
Certified Public Accountant

Audit Firm Address: 1001 East Farm Road 700
Big Spring, Texas 79720
Phone: 432-263-1324
Fax: 432-263-2124

Federal I.D. Number: 75-1607295

Auditor's Report Date: May 2, 2011

Contacts: kenneth@boothevassar.com

Desert Palms Apartments Limited Partnership

Exit Conference

December 31, 2010

EXIT CONFERENCE

An exit conference was held on May 2, 2011, which was attended by the following:

Housing Authority Administration

Thomas Hassell	Executive Director
Sharon Hansen	Accountant

Kenneth C. Boothe, P.C.

Kenneth Boothe	Owner
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Management Agent

Bobby Griffith	Chief Financial Officer
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Preparation of Financial Statements

The financial statements presented in this report were compiled by the auditor Kenneth C. Boothe, P.C. However, the contents of the financial statements remain the responsibility of management.