

# Desert Palms Apartments Limited Partnership

Financial Statements and Supplemental Information  
with Report of Independent Auditors

December 31, 2019 and 2018

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## Report of Independent Auditors

To the Partners of Desert Palms Apartments Limited Partnership, Las Cruces, New Mexico,  
and Brian S. Colón, New Mexico State Auditor:

### *Report on the Financial Statements*

We have audited the accompanying financial statements of Desert Palms Apartments Limited Partnership, a New Mexico limited partnership, which comprise the balance sheets as of December 31, 2019 and 2018, and the related statements of operations, changes in partners' capital, and cash flows for the years then ended, and the related notes to the financial statements.

### *Management's Responsibility for the Financial Statements*

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

### *Auditors' Responsibility*

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 in accordance with 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 from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditors consider internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### *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, 2019 and 2018, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

### *Prior Period Financial Statements*

The financial statements of Desert Palms Apartments Limited Partnership as of December 31, 2018, were audited by other auditors whose report dated April 11, 2019 expressed an unmodified opinion on those statements.

### *Changes in Accounting Principles*

As discussed in Note 2 to the financial statements, Desert Palms Apartments Limited Partnership adopted changes in accounting principles related to revenue recognition, presentation and disclosure of the statements of cash flows, and real estate sales. Our opinion is not modified with respect to those matters.

### *Other Matters*

### *Supplementary and Other Information*

Our audits were conducted for the purpose of forming an opinion on the financial statements as a whole. The accompanying supplementary information, which includes HUD-required financial data templates, is presented for purposes of additional analysis as required by the *Consolidated Audit Guide for Audits of HUD Programs* issued by the U.S. Department of Housing and Urban Development, Office of the Inspector General, and is not a required part of the financial statements.

The supplementary information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. Such information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the supplementary information is fairly stated, in all material respects, in relation to the financial statements as a whole.

The schedule of the status of prior audit findings, questioned costs, and recommendations, mortgagor's (owners) certification and managing agent's certification have not been subjected to the auditing procedures applied in the audit of the financial statements and accordingly, we do not express an opinion or provide any assurance on them.

*Other Reporting Required by Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated March 31, 2020 on our consideration of Desert Palms Apartments Limited Partnership's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Desert Palms Apartments Limited Partnership's internal control over financial reporting and compliance.

*Novogradac & Company LLP*

Austin, Texas

March 31, 2020

DESERT PALMS APARTMENTS LIMITED PARTNERSHIP  
BALANCE SHEETS  
December 31, 2019 and 2018

	ASSETS	
	2019	2018
<b>Current assets</b>		
Cash and cash equivalents	\$ 9,249	\$ 7,556
Accounts receivable	8,452	3,928
Prepaid expenses	19,259	16,550
Total current assets	36,960	28,034
<b>Restricted deposits and funded reserves</b>		
Tenant security deposits	36,310	35,180
Real estate tax and insurance	3,605	6,827
Replacement reserve	139,631	110,419
Other reserves	1,889	1,996
Total restricted deposits and funded reserves	181,435	154,422
<b>Property and equipment</b>		
Land	200,000	200,000
Buildings	3,399,062	3,399,062
Site improvements	391,753	391,753
Furnishings	515,984	515,984
	4,506,799	4,506,799
Accumulated depreciation	(2,098,908)	(1,967,414)
Net property and equipment	2,407,891	2,539,385
<b>Other assets</b>		
Tax credit fees	17,591	17,591
Accumulated amortization	(16,516)	(15,343)
Net other assets	1,075	2,248
<b>Entity assets</b>		
Operating reserve	23,231	23,228
Operating deficit reserve	15,570	15,540
Total entity assets	38,801	38,768
<b>Total assets</b>	\$ 2,666,162	\$ 2,762,857

see accompanying notes

DESERT PALMS APARTMENTS LIMITED PARTNERSHIP  
BALANCE SHEETS (CONTINUED)  
December 31, 2019 and 2018

LIABILITIES AND PARTNERS' CAPITAL

	2019	2018
<b>Current liabilities</b>		
Current maturities of long term debt	\$ 30,989	\$ 29,050
Accounts payable	100,361	72,407
Accrued interest	8,278	8,399
Accrued expenses	13,789	12,251
Accrued property taxes	8,106	8,056
Total current liabilities	161,523	130,163
<b>Deposits and prepaid liabilities</b>		
Security deposits payable	36,705	34,785
Prepaid rent	3,290	4,462
Total deposits and prepaid liabilities	39,995	39,247
<b>Long-term liabilities</b>		
Long-term debt, net of unamortized debt issuance costs	1,717,499	1,746,989
Long-term accrued interest	224,080	202,468
Development fee payable	-	143,132
Asset management fee payable	71,629	65,397
Total long-term liabilities	2,013,208	2,157,986
<b>Total liabilities</b>	2,214,726	2,327,396
<b>Partners' capital</b>	451,436	435,461
<b>Total liabilities and partners' capital</b>	\$ 2,666,162	\$ 2,762,857

see accompanying notes

DESERT PALMS APARTMENTS LIMITED PARTNERSHIP  
STATEMENTS OF OPERATIONS  
For the years ended December 31, 2019 and 2018

	2019	2018
REVENUE		
Rental income		
Potential rental income	\$ 484,575	\$ 484,560
Lease excess	15,965	26,914
Less: vacancies	(27,744)	(47,960)
Less: concessions	(12,653)	(22,011)
Net rental income	460,143	441,503
Other income		
Interest income	274	182
Tenant charges	25,361	25,035
Miscellaneous income	311	4,026
Total other income	25,946	29,243
Total revenue	486,089	470,746
OPERATING EXPENSES		
General and administrative	105,821	96,133
Utilities	31,463	33,205
Maintenance	132,170	103,911
Taxes and insurance	73,329	70,469
Financial expenses	131,564	131,950
Total operating expenses	474,347	435,668
Net operating income	11,742	35,078
OTHER EXPENSES		
Depreciation	131,494	136,300
Amortization	1,173	1,172
Investor service fee	6,232	6,050
Total other expenses	138,899	143,522
Net loss	\$ (127,157)	\$ (108,444)

see accompanying notes



DESERT PALMS APARTMENTS LIMITED PARTNERSHIP  
STATEMENT OF CHANGES IN PARTNERS' CAPITAL  
For the years ended December 31, 2019 and 2018

	General Partner	Limited Partner	Total Partners' Capital
BALANCE, JANUARY 1, 2018	\$ 283,783	\$ 209,314	\$ 493,097
Capital contributions	50,808	-	50,808
Net loss	(11)	(108,433)	(108,444)
BALANCE, DECEMBER 31, 2018	334,580	100,881	435,461
Capital contributions	143,132	-	143,132
Net loss	(13)	(127,144)	(127,157)
BALANCE, DECEMBER 31, 2019	\$ 477,699	\$ (26,263)	\$ 451,436

see accompanying notes

DESERT PALMS APARTMENTS LIMITED PARTNERSHIP

STATEMENTS OF CASH FLOWS

For the years ended December 31, 2019 and 2018

	<u>2019</u>	<u>2018</u>
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Rental receipts	\$ 454,447	\$ 443,900
Other operating receipts	25,946	29,245
Total receipts	<u>480,393</u>	<u>473,145</u>
<b>CASH PAID FOR:</b>		
Administrative expenses	(81,874)	(107,337)
Utilities expenses	(31,463)	(33,205)
Maintenance expenses	(132,170)	(103,913)
Taxes and insurance expenses	(75,988)	(69,595)
Financial expenses	(1,379)	(29,221)
Interest paid	(121,341)	(101,358)
Tenant security deposits	-	2,605
Total disbursements	<u>(444,215)</u>	<u>(442,024)</u>
Net cash provided by operating activities	36,178	31,121
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Net deposits to operating reserve	(3)	(7)
Net deposits to operating deficit reserve	(30)	(24)
Net cash used in investing activities	<u>(33)</u>	<u>(31)</u>
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Principal payments on mortgage	(29,051)	(27,232)
Long-term accrued interest	21,612	20,793
Payments on deferred developer fee	(143,132)	(50,808)
Capital contributions	143,132	50,808
Net cash used in financing activities	<u>(7,439)</u>	<u>(6,439)</u>
Net change in cash, cash equivalents and restricted cash	28,706	24,651
Cash, cash equivalents and restricted cash at beginning of year	<u>161,978</u>	<u>137,327</u>
Cash, cash equivalents and restricted cash at end of year	<u>\$ 190,684</u>	<u>\$ 161,978</u>
Cash and cash equivalents	\$ 9,249	\$ 7,556
Restricted cash	<u>181,435</u>	<u>154,422</u>
Total cash, cash equivalents and restricted cash	<u>\$ 190,684</u>	<u>\$ 161,978</u>

see accompanying notes

DESERT PALMS APARTMENTS LIMITED PARTNERSHIP  
STATEMENTS OF CASH FLOWS (CONTINUED)  
For the years ended December 31, 2019 and 2018

	2019	2018
RECONCILIATION OF NET LOSS TO NET		
CASH PROVIDED BY OPERATING ACTIVITIES		
Net loss	\$ (127,157)	\$ (108,444)
ADJUSTMENTS TO RECONCILE NET LOSS TO NET CASH		
PROVIDED BY OPERATING ACTIVITIES		
Depreciation expense	131,494	136,300
Amortization expense	1,173	1,172
Interest expense - debt issuance costs	1,500	1,501
Changes in asset and liability accounts		
Decrease (increase) in assets		
Tenant accounts receivable	(4,524)	681
Prepaid expenses	(2,709)	(4,463)
Increase (decrease) in liabilities		
Accounts payable	27,954	1,162
Accrued interest	(121)	(130)
Accrued expenses	1,538	(7,907)
Accrued property taxes	50	877
Deferred income	(1,172)	-
Tenant security deposits held in trust	1,920	2,605
Increase (decrease) in prepaid tenant fees	-	1,716
Asset management fee	6,232	6,051
Net cash provided by operating activities	\$ 36,178	\$ 31,121

see accompanying notes

DESERT PALMS APARTMENTS LIMITED PARTNERSHIP  
NOTES TO FINANCIAL STATEMENTS  
For the years ended December 31, 2019 and 2018

1. Organization

Desert Palms Apartments Limited Partnership (the “Entity”) was formed in 2003 to construct, develop and operate a 101-unit property located in Las Cruces, New Mexico known as Desert Palms Apartments (the “Property”). The Property 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 (“Section 42”).

The limited partner is Freddie Mac Equity Plus II, ESIC (the “Limited Partner”). The general partner is Mesilla Valley Public Housing Authority (the “General Partner”). Pursuant to the Amended and Restated Agreement of Limited Partnership and the subsequent amendments (“the Partnership Agreement”), profits, losses and tax credits are allocated 0.01% to the General Partner and 99.99% to the Limited Partner.

The Property 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 Entity provides housing to low- and moderate-income tenants, subject to regulation by MFA and the United States Department of Housing and Urban Development, as to rental charges and operating methods. Lower rental charges to tenants are recovered by the Property through rent subsidies provided by the local Public Housing Authority. In addition, the Entity received funding from the HOME Investment Partnerships Program to assist with financing the development of the Property. Under the terms of the agreement, eight units of the Property shall be designated as floating HOME assisted units.

On December 14, 2011, the Entity executed a 542 (c) Multifamily Insurance Program Regulatory Agreement (the “Regulatory Agreement”) with the MFA in order to obtain the “risk-sharing” mortgage loan. The Entity 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.

Pursuant to the terms of the Partnership Agreement, the Limited Partner was required to provide capital contributions subject to adjustments based on the amount of low-income housing tax credits ultimately allocated to the Property in addition to other potential occurrences as more fully explained in the Partnership Agreement. As of December 31, 2019 and 2018, all required capital contributions had been provided.

The Entity is reported as a component unit of Mesilla Valley Public Housing Authority (“MVPHA”), previously known as Housing Authority of the City of Las Cruces, because MVPHA is the General Partner of the Entity. The Entity has no component units.

Related to GASB 77, the Entity does not negotiate property tax abatements and has no tax abatement agreements as of December 31, 2019.

The Entity does not receive public money from the State of New Mexico or any local governments as defined by 6-10-1 to 6-10-63 NMSA 1978 and therefore is not subject to several state compliance regulations.

DESERT PALMS APARTMENTS LIMITED PARTNERSHIP  
NOTES TO FINANCIAL STATEMENTS  
For the years ended December 31, 2019 and 2018

2. Summary of significant accounting policies and nature of operations

Basis of accounting

The Entity prepares its financial statements on the accrual basis of accounting consistent with accounting principles generally accepted in the United States of America, whereby income is recognized as earned and expenses are recognized as obligations are incurred. The Entity is a for profit organization and prepared their financials under the Financial Accounting Standards and not the Governmental Accounting Standards generally accepted in the United States of America.

Estimates

The preparation of financial statements in accordance 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.

Cash and cash equivalents

Cash and cash equivalents include all cash balances on deposit with financial institutions and highly liquid investments with a maturity of three months or less at the date of acquisition.

Restricted cash is not considered cash and cash equivalents and includes cash held with financial institutions for funding of operating deficits, repairs and replacements to fixed assets, mortgage insurance premium payments, tenant security deposits, and annual insurance and property tax payments.

Concentration of credit risk

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

Collateralization of deposits

The Entity does not receive public money from the State of New Mexico or any local governments as defined by NMSA 1978 and therefore is not required to secure collateralization on cash deposits.

Receivables

Management considers receivables to be fully collectible. If amounts become uncollectible, they are charged to operations in the period in which that determination is made. 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.

DESERT PALMS APARTMENTS LIMITED PARTNERSHIP  
NOTES TO FINANCIAL STATEMENTS  
For the years ended December 31, 2019 and 2018

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

Fixed assets and depreciation

Fixed assets are recorded at cost. Buildings, which include building improvements, are depreciated over their estimated useful lives of 10-40 years using the straight-line method. Site improvements are depreciated over their estimated useful lives of 5-15 years using the straight-line method. Furniture and equipment are depreciated over their estimated useful lives of 3-7 years using the straight-line method. Depreciation expense for the years ended December 31, 2019 and 2018 was \$131,494 and \$136,300, respectively.

Deferred charges and amortization

Tax credit fees are amortized on a straight-line basis over the 15-year tax credit compliance period. Amortization expense for the years ended December 31, 2019 and 2018 was \$1,173 and \$1,172, respectively.

Impairment of long-lived assets

The Entity reviews its long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying value of the asset may not be recoverable. Recoverability is measured by a comparison of the carrying amount of the asset to the future net undiscounted cash flows expected to be generated and any estimated proceeds from the eventual disposition. If the long-lived assets are considered to be impaired, the impairment to be recognized is measured at the amount by which the carrying amount of the asset exceeds the fair value as determined from an appraisal, discounted cash flow analysis, or other valuation technique. There were no impairment losses recognized during 2019 or 2018.

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 revenue includes fees for late payments, cleaning, damages, laundry facilities and other charges and is recorded when earned. Advance receipts of revenue are deferred and classified as liabilities until earned.

Income taxes

Income taxes on Entity income are levied on the partners at the partner level. Accordingly, all profits and losses of the Entity are recognized by each partner on its respective tax return.

The preparation of financial statements in accordance with accounting principles generally accepted in the United States of America requires the Entity to report information regarding its exposure to various tax positions taken by the Entity. The Entity has determined whether any tax positions have met the recognition threshold and has measured the Entity's exposure to those tax positions. Management believes that the Entity has adequately addressed all relevant tax positions and that there are no unrecorded tax liabilities. Federal and state tax authorities generally have the right to examine and audit the previous three years of tax returns filed. Any interest or penalties assessed to the Entity are recorded in operating expenses. No interest or penalties from federal or state tax authorities were recorded in the accompanying financial statements.

DESERT PALMS APARTMENTS LIMITED PARTNERSHIP  
NOTES TO FINANCIAL STATEMENTS  
For the years ended December 31, 2019 and 2018

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

Economic concentrations

The Entity operates one property in Las Cruces, New Mexico. Future operations could be affected by changes in the economic or other conditions in that geographical area or by changes in federal low-income housing subsidies or the demand for such housing. In addition, the Entity operates in a heavily regulated environment. The operations of the Entity are subject to the administrative directives, rules and regulations of federal, state and local regulatory agencies, including, but not limited to, HUD. Such administrative directives, rules and regulations are subject to change by an act of Congress or an administrative change mandated by HUD. 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.

Advertising

Advertising costs are expensed as incurred. During the years ended December 31, 2019 and 2018, the Entity incurred \$10,220 and \$5,904, respectively, in advertising costs, and is included in "Administrative" on the accompanying statements of operations.

Reclassifications

Certain reclassifications have been made to the prior year financial statements to conform to the current year presentation.

Subsequent events

Subsequent events have been evaluated through May 31, 2020, which is the date the financial statements were available to be issued. The spread of a novel strain of coronavirus (COVID-19) in the first quarter of 2020 has caused significant volatility in U.S. markets. There is significant uncertainty around the breadth and duration of business disruptions related to COVID-19, as well as its impact on the U.S. economy. The extent of the impact of COVID-19 on the Partnership's operational and financial performance will depend on certain developments, including the duration and spread of the outbreak, and the impact on customers, employees and vendors, all of which are uncertain and cannot be determined at this time.

Changes in accounting principles

On January 1, 2019, the Entity adopted a new accounting standard that affects the accounting for revenue. The Entity's revenue is mainly derived from leases, which is not impacted by this standard. Adopting this standard did not have a significant impact on the financial statements.

The new revenue standard also introduced new guidance for accounting for other income, including the accounting for sales of real estate. Adopting this standard did not have a significant impact on the financial statements.

DESERT PALMS APARTMENTS LIMITED PARTNERSHIP  
NOTES TO FINANCIAL STATEMENTS  
For the years ended December 31, 2019 and 2018

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

Changes in accounting principles (continued)

On January 1, 2019, the Entity adopted new accounting standards that affect the statement of cash flows. These new standards address how certain cash receipts and payments are presented and classified in the statement of cash flows, including that debt prepayments and other debt extinguishment related payments are required to be classified as financing activities, when previously these payments were classified as an operating activity. The new standards also require the statement of cash flows to explain the change in cash, cash equivalents and restricted cash. Previously, changes in restricted cash were presented in the statement of cash flows as operating, investing or financing activities depending upon the intended purpose of the restricted funds.

The effect of the revisions to the statements of cash flows for the year ended December 31, 2018 is as follows:

	<u>As Previously Reported</u>	<u>Adjustments</u>	<u>As Revised</u>
Net cash flows from operating activities	\$28,658	\$ 2,463	\$ 31,121
Net cash flows from investing activities	(\$17,997)	\$ 17,966	\$ (31)

Change in accounting principle – not yet adopted

The Entity will adopt a new accounting standard for leases on January 1, 2021. Accounting for leases by lessors is left largely unchanged by the new standard. It is expected that the adoption of the new standard will not have a material impact on the accounting for tenant lease revenue.

3. Restricted deposits and funded reserves

Tenant security deposits

Tenant security deposits held in trust are placed into an interest-bearing account and are generally held until the termination of the lease, at which time some or all deposits may be returned to the lessee. As of December 31, 2019 and 2018, the balance was \$36,310 and \$35,180, respectively.

Real estate tax and insurance escrows

Pursuant to the Partnership Agreement, required monthly payments to the mortgagee include amounts for deposit to mortgage escrow funds. These are held by the mortgagee for future payment of property insurance and property tax. This fund is restricted in accordance with the provisions of the regulatory agreement. As of December 31, 2019 and 2018, the balance was \$3,605 and \$6,827, respectively.

Replacement reserve

Pursuant to the Partnership Agreement, annual deposits of \$30,000 are made to the replacement reserve. These deposits are held by the mortgagee until approval is obtained for use of the funds to repair or replace certain assets of the Property. As of December 31, 2019 and 2018, the balance was \$139,631 and \$110,419, respectively.



DESERT PALMS APARTMENTS LIMITED PARTNERSHIP  
NOTES TO FINANCIAL STATEMENTS  
For the years ended December 31, 2019 and 2018

3. Restricted deposits and funded reserves (continued)

Other escrows

Pursuant to loan agreements entered into by the Entity, required monthly payments to the mortgagee include amounts for mortgage insurance premiums. These are held by the mortgagee for future payment of mortgage insurance. This funds are restricted in accordance with the provisions of the regulatory agreement. As of December 31, 2019 and 2018, the balance was \$1,889 and \$1,996, respectively.

4. Entity assets

Operating and operating deficit reserve

Pursuant to the Partnership Agreement, the Entity is required to fund an operating reserve in the amount of \$75,000 and an operating deficit reserve to be held with the New Mexico Mortgage Finance Authority. Funds from the operating and operating deficit reserve are to be used for operating and debt service deficits. As of December 31, 2019 and 2018, entity assets consisted of:

	2019	2018
Operating reserve	\$ 23,231	\$ 23,228
Operating deficit reserve	15,570	15,540
Total entity assets	\$ 38,801	\$ 38,768

5. Related party transactions

Property management fee

The Entity entered into a management agreement with JL Gray Company (the “Management Agent”) for services rendered in connection with the leasing and operation of the Property. The Management Agent fee for its services is 6.0% of gross rental collections.

During 2019 and 2018, property management fees of \$28,105 and \$27,076, respectively, were incurred and are included in “Administrative” on the accompanying statements of operations. As of December 31, 2019 and 2018, property management fees of \$80,326 and \$66,659, respectively, remained payable and are included in “Accounts payable” on the accompanying balance sheets.

Employees of the Property are employed by the Management Sub-Agent and the Property reimburses the Management Sub-Agent for payroll costs, including salaries, payroll taxes, workers compensation, payroll administration fees and employee benefits.

Reimbursed expenses

The Management Agent is reimbursed for various expenditures incurred on behalf of the Entity. These reimbursed expenses are separately identifiable from the property management fee paid to the Management Agent. As of December 31, 2019 and 2018, no amounts remained outstanding.

DESERT PALMS APARTMENTS LIMITED PARTNERSHIP  
NOTES TO FINANCIAL STATEMENTS  
For the years ended December 31, 2019 and 2018

5. Related party transactions (continued)

Investor services fee

Pursuant to the Partnership Agreement, the Entity pays an investor services fee to the Limited Partner. The fee is cumulative and payable subject to available cash flow, as defined in the Partnership Agreement. The annual fee is \$4,000, increasing at a rate of 3% each year. During 2019 and 2018, investor services fees of \$6,232 and \$6,050, respectively, were incurred. As of December 31, 2019 and 2018, investor services fees of \$71,629 and \$65,397, respectively, were outstanding.

Partnership administrative fee

Pursuant to the Partnership Agreement, the Entity pays a partnership administrative fee to the General Partner. The partnership administrative fee is \$25,000, increasing 3% each year, is non-cumulative, and is payable from available cash flow as defined in the Partnership Agreement. During 2019 and 2018, no partnership administrative fees were incurred.

Development fee

Pursuant to a development services agreement (the "Development Agreement"), the Entity agreed to pay the General Partner and JL Gray Company, a total fee of \$203,230 for services relating to the development of the Property. The development fee is payable from available cash flow, as further defined in the Partnership Agreement. During 2018, the General Partner contributed \$50,808 to pay their remaining portion of the development fee in full. During 2019, JL Gray Company, through the General Partner, contributed \$143,132 to pay their portion of the development fee in full. As of December 31, 2019 and 2018, the outstanding principal balance was \$0 and \$143,132, respectively.

Operating deficit loans

Pursuant to the Partnership Agreement, the General Partner has guaranteed to fund all deficits through the later of permanent loan closing or achievement of a debt service coverage ratio of 1:15 to 1:00 for 90 days, as defined in the Partnership Agreement. Subsequent to permanent loan closing or achievement of the debt service coverage ratio, funding up to an additional \$275,000 is guaranteed. The requirement to fund additional operating deficits will terminate on the date the following occurs:

1. The Entity has operated at breakeven three consecutive calendar years following the stabilization date of the Property;
2. The Entity has met the required debt service coverage for three consecutive years;
3. The balance in the operating reserve equals or exceeds the operating reserve amount.

The General Partner obligations shall be guaranteed by JL Gray Company, the guarantor, as defined in the guaranty agreement.

DESERT PALMS APARTMENTS LIMITED PARTNERSHIP  
NOTES TO FINANCIAL STATEMENTS  
For the years ended December 31, 2019 and 2018

6. Long-term debt

The Entity has two mortgages payable to two entities. The mortgages include certain covenants and other performance requirements, for which management has reported compliance. The following are mortgages payable as of December 31, 2019 and 2018:

	2019	2018
<p>35 year mortgage from New Mexico Mortgage Finance Authority in the amount of \$1,705,000 (the "Mortgage"). The Mortgage has an interest rate of 6.48% per annum and matures on October 1, 2041. Principal and interest payments of \$10,277 are due monthly through the maturity date. The mortgage is secured by the Property. During 2019 and 2018, interest expense of \$94,122 and \$95,950, respectively, was incurred. As of December 31, 2019 and 2018, interest of \$7,771 and \$7,928, respectively, was accrued.</p>	\$ 1,439,027	\$ 1,468,078
<p>30 year second mortgage from the City of Las Cruces HOME Program in the amount of \$342,744 (the "Second Mortgage"). The Second Mortgage has an interest rate of 4.94% per annum. Interest only payments are due monthly in the amount of 1.0% of the outstanding principal plus accrued and unpaid interest for the first 15 years. After the end of year 15 the principal and accrued interest will become due and payable in 179 monthly installments of \$4,820. The Second Mortgage matures at the sale, refinance, or transfer of the Property, or on September 2034, whichever occurs first. The Second Mortgage is secured by the Property. During 2019 and 2018, interest expense of \$27,098 and \$26,071, respectively, was incurred. As of December 31, 2019 and 2018, short-term interest of \$507 and \$471, respectively, was accrued and long-term interest of \$224,080 and \$202,468, respectively, was accrued.</p>	342,744	342,744
Notes payable	\$ 1,781,771	\$ 1,810,822

Total interest expense for 2019 and 2018 was \$121,220 and \$122,021, respectively. As of December 31, 2019 and 2018, accrued interest was \$232,358 and \$210,867, respectively.

DESERT PALMS APARTMENTS LIMITED PARTNERSHIP  
NOTES TO FINANCIAL STATEMENTS  
For the years ended December 31, 2019 and 2018

6. Long-term debt (continued)

Notes payable consists of the following as of December 31,

	<u>2019</u>	<u>2018</u>
Principal balance	\$ 1,781,771	\$ 1,810,822
Less: unamortized debt issuance costs	<u>(33,283)</u>	<u>(34,783)</u>
Notes payable, net of unamortized debt issuance costs	1,748,488	1,776,039
Less: current portion	<u>(30,989)</u>	<u>(29,050)</u>
Long-term notes payable	<u>\$ 1,717,499</u>	<u>\$ 1,746,989</u>

Debt issuance costs related to the Mortgage are being amortized to interest expense over the term of the loan. For 2019 and 2018, the effective interest rate was 6.61% each year. During 2019 and 2018, amortization expense for debt issuance costs related to the Mortgage was \$1,500 and \$1,501, respectively.

Aggregate annual principal payments are due as follows:

Year ending December 31,		
2020	\$	30,990
2021		35,662
2022		51,342
2023		54,509
2024		57,873
2025 - 2029		347,707
2030 - 2034		469,830
2035 - 2039		521,211
Thereafter		<u>212,647</u>
Total	\$	<u>1,781,771</u>

7. Service contract

On March 13, 2012, the Entity entered into a Service Agreement and a Compensation Agreement with Comcast of California XIV, LLC (“Comcast”). The Service Agreement is for a term of 15 years, with an automatic biannual renewal period. Per the Compensation Agreement, Comcast agreed to pay the Entity a one-time fee of \$12,625 as consideration for the agreement. The total fee was received by the Entity upon execution of the agreements.

8. Litigation

The Entity is part of a class action lawsuit. There is not currently an estimated range of potential loss, nor has it been concluded whether there is likely to be an unfavorable outcome as of May 31, 2020.

DESERT PALMS APARTMENTS LIMITED PARTNERSHIP  
NOTES TO FINANCIAL STATEMENTS  
For the years ended December 31, 2019 and 2018

9. Commitments and contingencies

Low-income housing tax credits

As incentive for investment in equity, the Entity 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 Entity 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 the 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 to 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 tenant 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

The entity 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.

**HUD  
SUPPLEMENTARY  
INFORMATION**

DESERT PALMS APARTMENTS LIMITED PARTNERSHIP

SCHEDULES OF EXPENSES

For the years ended December 31, 2019 and 2018

	<u>2019</u>	<u>2018</u>
<b>ADMINISTRATIVE</b>		
Professional management fees	\$ 28,105	\$ 27,076
Salaries and wages	26,588	26,991
Telephone, cable, internet	5,856	3,708
Professional services	8,362	8,100
Training	2,976	3,070
Compliance and monitoring fees	4,500	4,500
Bad debt and adjustments	7,408	8,273
Technical support	1,800	1,805
Dues, fees, and subscriptions	675	675
Supplies and office expenses	3,473	2,134
Credit/criminal reports	2,780	3,529
Advertising	10,220	5,904
Equipment and furniture	140	327
Service for residents	806	-
Travel, meals, and entertainment	2,132	41
	<u>2,132</u>	<u>41</u>
 Total administrative expenses	 <u>\$ 105,821</u>	 <u>\$ 96,133</u>
 <b>UTILITIES</b>		
Utility allowance	\$ 473	\$ 550
Electricity	11,748	12,642
Water	9,822	11,108
Sewer	9,420	8,905
	<u>9,420</u>	<u>8,905</u>
 Total utility expenses	 <u>\$ 31,463</u>	 <u>\$ 33,205</u>
 <b>TAXES &amp; INSURANCE</b>		
Insurance	\$ 24,858	\$ 21,585
Property taxes	16,212	16,309
Payroll taxes	7,787	7,742
Miscellaneous taxes and insurance	24,472	24,833
	<u>24,472</u>	<u>24,833</u>
 Total taxes and insurance	 <u>\$ 73,329</u>	 <u>\$ 70,469</u>

see report of independent auditors

DESERT PALMS APARTMENTS LIMITED PARTNERSHIP  
SCHEDULES OF EXPENSES - CONTINUED  
For the years ended December 31, 2019 and 2018

	2019	2018
<b>MAINTENANCE</b>		
Maintenance payroll	\$ 32,975	\$ 31,679
Contracts	15,694	15,490
Appliance and equipment replacement	32,334	22,140
Supplies	25,484	13,864
Security	680	-
Trash removal	9,918	9,881
Painting and drywall	5,670	4,406
Landscape maintenance	1,895	1,491
Pest control	7,520	4,960
	\$ 132,170	\$ 103,911
<b>FINANCIAL EXPENSES</b>		
Interest expense	\$ 121,220	\$ 122,021
Mortgage insurance premium	7,249	7,391
Debt issuance costs	1,500	1,501
Service charges	1,595	1,037
	\$ 131,564	\$ 131,950
Total operating expenses	\$ 474,347	\$ 435,668
<b>NON-OPERATING EXPENSES</b>		
Depreciation expense	\$ 131,494	\$ 136,300
Amortization expense	1,173	1,172
Asset management fee	6,232	6,050
	\$ 138,899	\$ 143,522
Total non-operating expenses	\$ 138,899	\$ 143,522
Total expenses	\$ 613,246	\$ 579,190

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DESERT PALMS APARTMENTS LIMITED PARTNERSHIP  
SCHEDULE OF CHANGES IN RESTRICTED CASH  
For the year ended December 31, 2019

**Schedule of Reserve for Replacements**

BALANCE, JANUARY 1, 2019	\$	110,419
Monthly deposits		30,000
Interest income		240
Approved withdrawals		(1,028)
		139,631
BALANCE, DECEMBER 31, 2019	\$	139,631

**Schedule of Operating and Operating Deficit Reserves**

BALANCE, JANUARY 1, 2019	\$	38,768
Monthly deposits		-
Interest income		33
Approved withdrawals		-
		38,801
BALANCE, DECEMBER 31, 2019	\$	38,801

see report of independent auditors

DESERT PALMS APARTMENTS LIMITED PARTNERSHIP  
 COMPUTATION OF SURPLUS CASH  
 For the year ended December 31, 2019

COMPUTATION OF SURPLUS CASH, DISTRIBUTIONS, AND RESIDUAL RECEIPTS

Cash		\$ <u>9,249</u>
Total cash		9,249
Accrued mortgage (or bond) interest payable		8,278
Accounts payable (due within 30 days)		100,361
Accrued expenses (not escrowed)		21,895
Prepaid revenue		3,290
Tenant deposits held in trust		36,705
Less total current obligations		<u>170,529</u>
Surplus cash (deficiency)		<u>\$ (161,280)</u>
Amount available for distribution during next fiscal period		<u>\$ -</u>

DESERT PALMS APARTMENTS LIMITED PARTNERSHIP  
SCHEDULE OF CHANGES IN FIXED ASSETS  
For the year ended December 31, 2019

	Beginning Balance	Additions	Deductions	Ending Balance
Land	\$ 200,000	\$ -	\$ -	\$ 200,000
Buildings	3,399,062	-	-	3,399,062
Site improvements	391,753	-	-	391,753
Furnishings	515,984	-	-	515,984
	4,506,799	\$ -	\$ -	4,506,799
Accumulated depreciation	1,967,414	\$ 131,494	\$ -	2,098,908
Net book value	\$ 2,539,385			\$ 2,407,891

see report of independent auditors

REPORT OF INDEPENDENT AUDITORS ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

To the Partners of Desert Palms Apartments Limited Partnership, Las Cruces, New Mexico,  
and Brian S. Colón, New Mexico State Auditor:

We have audited, in accordance with the 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, the financial statements of Desert Palms Apartments Limited Partnership, which comprise the balance sheet as of December 31, 2019, and the related statements of operations, changes in partners' capital, and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated March 31, 2020.

*Internal Control Over Financial Reporting*

In planning and performing our audit of the financial statements, we considered Desert Palms Apartments Limited Partnership's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Desert Palms Apartments Limited Partnership's internal control. Accordingly, we do not express an opinion on the effectiveness of Desert Palms Apartments Limited Partnership's internal control.

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, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

*Compliance and Other Matters*

As part of obtaining reasonable assurance about whether Desert Palms Apartments Limited Partnership's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

*Purpose of this Report*

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

*Novogradac & Company LLP*

Austin, Texas  
March 31, 2020

REPORT OF INDEPENDENT AUDITORS ON COMPLIANCE FOR THE MAJOR HUD PROGRAM AND REPORT  
ON INTERNAL CONTROL OVER COMPLIANCE REQUIRED BY  
THE CONSOLIDATED AUDIT GUIDE FOR AUDITS OF HUD PROGRAMS

To the Partners of Desert Palms Apartments Limited Partnership, Las Cruces, New Mexico,  
and Brian S. Colón, New Mexico State Auditor:

*Report on Compliance for The Major HUD Program*

We have audited Desert Palms Apartments Limited Partnership's compliance with the compliance requirements described in the *Consolidated Audit Guide for Audits of HUD Programs* (the "Guide") that could have a direct and material effect on Desert Palms Apartments Limited Partnership's major U.S. Department of Housing and Urban Development ("HUD") program for the year ended December 31, 2019. Desert Palms Apartments Limited Partnership's major HUD program and the related direct and material compliance requirements are as follows:

**Name of Major HUD Program**

**Direct and Material Compliance Requirements**

HUD Insured Mortgage

Mortgage status, replacement reserve, distributions to owners, equity skimming, cash receipts, cash disbursements, tenant security deposits, management functions, unauthorized change of ownership/acquisition of liabilities, and unauthorized loans of project funds

*Management's Responsibility*

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to its HUD program.

*Auditor's Responsibility*

Our responsibility is to express an opinion on compliance for Desert Palms Apartments Limited Partnership's major HUD program based on our audit of the compliance requirements referred to above. 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 Guide. Those standards and the Guide require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the compliance requirements referred to above that could have a direct and material effect on a major HUD program occurred. An audit includes examining, on a test basis, evidence about Desert Palms Apartments Limited 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 on compliance for the major HUD program. However, our audit does not provide a legal determination of Desert Palms Apartments Limited Partnership's compliance.

#### *Opinion on The Major HUD Program*

In our opinion, Desert Palms Apartments Limited Partnership complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on its major HUD program for the year ended December 31, 2019.

#### *Report on Internal Control Over Compliance*

Management of Desert Palms Apartments Limited Partnership is responsible for establishing and maintaining effective internal control over compliance with the compliance requirements referred to above. In planning and performing our audit of compliance, we considered Desert Palms Apartments Limited Partnership's internal control over compliance with the requirements that could have a direct and material effect on the major HUD program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for the major HUD program and to test and report on internal control over compliance in accordance with the Guide, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of Desert Palms Apartments Limited Partnership's internal control over compliance.

*A deficiency in internal control over compliance* exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a compliance requirement of a HUD program on a timely basis. A *material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a compliance requirement of a HUD program will not be prevented, or detected and corrected, on a timely basis. A *significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a compliance requirement of a HUD program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

*Purpose of this Report*

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of the Guide. Accordingly, this report is not suitable for any other purpose.

*Novogradac & Company LLP*

Austin, Texas

March 31, 2020



DESERT PALMS APARTMENTS LIMITED PARTNERSHIP  
 SCHEDULE OF FINDINGS, QUESTIONED COSTS, AND RECOMMENDATIONS  
 December 31, 2019

Summary of Auditors' Results

*Financial statements*

Type of auditors' report issued Unmodified

Internal control over financial reporting:

- Material weakness(es) identified? \_\_\_\_\_ Yes \_\_\_\_\_ X No
- Significant deficiencies identified? \_\_\_\_\_ Yes \_\_\_\_\_ X None reported

Noncompliance material to financial statements noted? \_\_\_\_\_ Yes \_\_\_\_\_ X No

*Federal awards*

Internal control over major federal program:

- Material weakness(es) identified? \_\_\_\_\_ Yes \_\_\_\_\_ X No
- Significant deficiencies identified? \_\_\_\_\_ Yes \_\_\_\_\_ X None reported

Type of auditors' report issued on compliance for major program Unmodified

Findings – Financial Statements Audit

Our audit disclosed no findings that are required to be reported herein under the HUD Consolidated Audit Guide.

DESERT PALMS APARTMENTS LIMITED PARTNERSHIP  
SCHEDULE OF THE STATUS OF PRIOR AUDIT FINDINGS, QUESTIONED COSTS,  
AND RECOMMENDATIONS (UNAUDITED)  
December 31, 2019

Findings – Financial Statement Audit for the year ended December 31, 2018

Audit report, dated April 11, 2019, for the period ended December 31, 2018, issued by Hinkle + Landers, P.C.

There were no financial statement audit findings for the year ended December 31, 2018.

Findings from Other Audits or Studies

There were no reports issued by HUD OIG or other Federal agencies or contract administrators during the period covered by this audit.

Findings from Deficiencies Listed in Letters or Reports Issued by HUD Management


There were no letters or reports issued by HUD during the period covered by this audit.

see report of independent auditors

DESERT PALMS APARTMENTS LIMITED PARTNERSHIP  
MORTGAGOR'S (OWNERS) CERTIFICATION  
December 31, 2019

We hereby certify that we have examined the accompanying financial statements and supplemental data of Desert Palms Apartments Limited Partnership and, to the best of our knowledge and belief, the same is complete and accurate.

**DESERT PALMS APARTMENTS LIMITED PARTNERSHIP**



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March 31, 2020

Name of Signatory 1

Juan Olvera

Title of Certifying Official 1

Executive Director

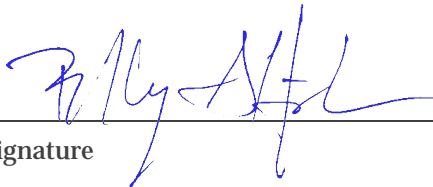
Auditee Telephone Number

505-325-6515

DESERT PALMS APARTMENTS LIMITED PARTNERSHIP  
MANAGING AGENT CERTIFICATION  
December 31, 2019

We hereby certify that we have examined the accompanying financial statements and supplemental data of Desert Palms Apartments Limited Partnership and, to the best of our knowledge and belief, the same is complete and accurate.

JL Gray Company

  
\_\_\_\_\_  
Signature

March 31, 2020  
\_\_\_\_\_  
Date

Name of Signatory \_\_\_\_\_

Managing Agent Tax Identification Number \_\_\_\_\_

Name of Property Manager JL Gray Company

DESERT PALMS APARTMENTS LIMITED PARTNERSHIP

EXIT CONFERENCE

For the Year Ended December 31, 2019

**Exit Conference**

An exit conference was held on March 31, 2020, which was attended by the following:

**Housing Authority Administration**

Juan Olvera                      Executive Director

Elizabeth Garcia              Comptroller

**Novogradac and Company, LLP**

Nick Hoehn, CPA              Audit Partner

Michael Derrickson, CPA      Audit Principal

**Management Agent**

Bobby Griffith                Chief Financial Officer

Lori Varnell                    Accountant

**Preparation of financial statements**

The auditor, Novogradac and Company, LLP, compiled the financial statements presented in this report. However, the contents of the financial statements remain the responsibility of management.