AFFORDABLE HOUSING ALLIANCE II, INC. AND SUBSIDIARIES
DBA INTEGRITY HOUSING

CONSOLIDATED FINANCIAL STATEMENTS

For the year ended December 31, 2012

with

Report of Independent Auditors

CONTENTS

NOVOGRADAC
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CERTIFIED PUBLIC ACCOUNTANTS

Report of Independent Auditors

To the Board of Directors of
Affordable Housing Alliance II, Inc. dba Integrity Housing:

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of Affordable Housing Alliance II, Inc. (a non-profit organization) and Subsidiaries dba Integrity Housing which comprise the statement of financial position as of December 31, 2012, and the related statements of activities and changes in net assets, functional expenses, and cash flows for the year 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.

Auditor's 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. 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 involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's 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 auditor considers 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.

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Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Affordable Housing Alliance II, Inc. and Subsidiaries dba Integrity Housing as of December 31, 2012 and the changes in its net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Supplementary and Other Information

Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The accompanying supplementary information on pages 23 through 25 is presented for purposes of additional analysis and is not a required part of the basic consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

San Francisco, California
October 8, 2013

AFFORDABLE HOUSING ALLIANCE II, INC. AND SUBSIDIARIES
DBA INTEGRITY HOUSING
CONSOLIDATED STATEMENT OF FINANCIAL POSITION
December 31, 2012

ASSETS		
Current assets		
Cash and cash equivalents	$	838,556
Other receivables		23,892
Managing general partner fees receivable		18,816
Tenant receivables		2,653
Security deposits		31,300
Prepaid expenses		5,762
Total current assets		920,979
Fixed assets		
Fixed assets		10,723,172
Accumulated depreciation		(2,909,479)
Net fixed assets		7,813,693
Other assets		
Restricted cash		163,567
Developer fees receivable		1,512,235
Investment in Series CC-S Bonds		1,400,000
Interest receivable on Series CC-S Bonds		20,252
Intangible assets, net		80,609
Total other assets		3,176,663
Total assets	$	11,911,335

See accompanying notes

AFFORDABLE HOUSING ALLIANCE II, INC. AND SUBSIDIARIES
DBA INTEGRITY HOUSING
CONSOLIDATED STATEMENT OF FINANCIAL POSITION (CONTINUED)
December 31, 2012

LIABILITIES AND NET ASSETS

Current liabilities		
Accounts payable and accrued expenses	$	33,305
Due to related parties - consulting fees		7,500
Security deposits payable		31,300
Prepaid rent		271
Accrued interest - notes payable		15,965
Current maturities of notes payable		94,430
Total current liabilities		182,771
Share of deficiency in assets of partnerships		599,208
Accrued interest - due to noncontrolling interests		361,636
Due to noncontrolling interests - Operating Partnerships		1,232,747
Accrued interest - notes payable		276,717
Notes payable, less current maturities		3,394,438
Total liabilities		6,047,517
Net assets		
Unrestricted net assets		
Controlling interest		3,089,528
Noncontrolling interests		2,774,290
Total net assets		5,863,818
Total liabilities and net assets	$	11,911,335

See accompanying notes

AFFORDABLE HOUSING ALLIANCE II, INC. AND SUBSIDIARIES
DBA INTEGRITY HOUSING
CONSOLIDATED STATEMENT OF ACTIVITIES AND CHANGES IN NET ASSETS
For the year ended December 31, 2012

Revenue		
Rental income	$	849,393
Managing general partner fees		12,544
Developer fee income		50,000
Other income		43,011
Interest income		145,078
Partnership flow-through loss		(508,614)
Total revenue		591,412
Expenses		
Program services		
Rental of affordable housing		1,108,132
Project expenses		724,493
Total program services		1,832,625
Supporting services		
General and administrative		138,554
Total supporting services		138,554
Total expenses		1,971,179
Change in net assets		(1,379,767)
Net assets at beginning of year		7,243,585
Net assets at end of year	$	5,863,818

See accompanying notes

AFFORDABLE HOUSING ALLIANCE II, INC. AND SUBSIDIARIES
DBA INTEGRITY HOUSING
CONSOLIDATED STATEMENT OF FUNCTIONAL EXPENSES
For the year ended December 31, 2012

	Program Services		Supporting Services	
	Rental of Affordable Housing	Project Expenses	General and Administrative	Total
Administrative	$ 29,578	$ 90,467	$ 4,765	$ 124,810
Insurance and tax	28,277	8,791	977	38,045
Interest expense	333,662	59,694	-	393,356
Legal and professional fees	38,943	26,276	-	65,219
Consulting fees	-	1,290	-	1,290
Management fees	10,565	-	-	10,565
Property management fees	56,239	-	-	56,239
Marketing	4,256	-	-	4,256
Payroll	162,744	531,251	132,812	826,807
Repairs and maintenance	98,841	-	-	98,841
Utilities	85,239	-	-	85,239
Amortization	10,176	-	-	10,176
Depreciation	249,612	6,724	-	256,336
	$ 1,108,132	$ 724,493	$ 138,554	$ 1,971,179

AFFORDABLE HOUSING ALLIANCE II, INC. AND SUBSIDIARIES
DBA INTEGRITY HOUSING
CONSOLIDATED STATEMENT OF CASH FLOWS
For the year ended December 31, 2012

Cash flows from operating activities:		
Total change in net assets	$	(1,379,767)
Adjustments to reconcile total change in net assets to net cash used in operating activities:		
Partnership flow-through loss		508,614
Depreciation and amortization		266,512
Changes in operating assets and liabilities:		
Increase in other receivables		(22,192)
Decrease in managing general partner fees receivable		2,150
Increase in interest receivable on Series CC-S Bonds		(9,644)
Increase in tenant receivable		(1,485)
Increase in prepaid expenses		(317)
Decrease in accounts payable and accrued expenses		(2,435)
Increase in due to related parties - consulting fees		7,500
Increase in prepaid rent		71
Decrease in accrued interest - notes payable		(193,718)
Decrease in due to noncontrolling interests - Operating Partnerships		(56,198)
Decrease in due from FFAH		87,000
Net cash used in operating activities		(793,909)
Cash flows from investing activities:		
Decrease in restricted cash		38,876
Purchase of fixed assets		(66,037)
Net cash provided by investing activities		(27,161)
Cash flows from financing activities:		
Payments of notes payable		(284,449)
Net cash used in financing activities		(284,449)
Net decrease in cash and cash equivalents		(1,105,519)
Cash and cash equivalents at beginning of year		1,944,075
Cash and cash equivalents at end of year	$	838,556
Supplemental disclosure of cash flow information:		
Cash paid for interest	$	587,074
Supplemental disclosure of non-cash investing and financing activities:		
Payment of note payable with CC-S Bonds	$	3,000,000

See accompanying notes

1. Organization

Affordable Housing Alliance II, Inc. dba Integrity Housing ("AHA2"), incorporated in the state of Colorado as a non-profit corporation, was established in 1993 to acquire, develop, and promote affordable senior and multi-family housing. AHA2's expressed purpose is to help ease the burden on state, county, and local housing authorities through the construction, acquisition, and operation of housing for moderate, low, and very low income individuals and families. AHA2 is dedicated to provide quality housing that serves the physical, recreational, and emotional needs of its residents.

AHA2 is responsible for project acquisition and financing involving federal and state low income tax credits and 501(c)(3) tax-exempt mortgage-backed revenue bonds, and the selection and supervision of the local professional property management company hired to handle on-site day-to-day management duties.

AHA2 builds and rehabilitates housing units for low income seniors and families. It secures construction and permanent financing, supervises architectural and general contractor selection, and manages the design and construction phases of the project, either by its director and staff or through contracting with outside consultants and service companies.

2. Summary of significant accounting policies

Principles of consolidation
AHA2 consolidates in its financial statements three limited partnerships ("Operating Partnerships") in which AHA2 is the sole general partner.

The portion of the equity of the Operating Partnerships that is not owned or controlled by AHA2 is shown as noncontrolling interests on the consolidated financial statements. All material intercompany transactions between consolidated entities have been eliminated.

The consolidated financial statements include the following Operating Partnerships:

Elizabeth Street Housing Investors, L.P.
Fort Collins Senior Housing Investors, L.P.
Claremont Villas, LLC

Share of deficiency in assets of partnerships – equity method
AHA2 uses the equity method of accounting for its investments in four entities in which AHA2 serves as a non-managing member, as AHA2 has significant influence over, but not control of the major operating and financial policies of the entities. Under this method, AHA2's share of income, losses, and distributions incurred by the entities is recognized as an increase or reduction of the carrying value of the investments. The following entities are recorded under the equity method:

2. Summary of significant accounting policies (continued)

Share of deficiency in assets of partnerships – equity method (continued)

Highlander Pointe, LLC
Maroon Creek Apartments, L.P.
Anaheim Affordable II, L.P.
Rancho Las Brisas Murrieta, L.P.

Basis of accounting

AHA2 prepares consolidated financial statements on the accrual basis of accounting consistent with accounting principles generally accepted in the United States of America. AHA2's year end for financial and tax reporting purposes is December 31.

Financial statement presentation

AHA2 reports information regarding its financial position, activities, and cash flow according to three classes of net assets: unrestricted, temporarily restricted, and permanently restricted. Donor-restricted contributions are reported as an increase in temporarily or permanently restricted net assets depending on the nature of the restrictions. When a restriction expires, temporarily restricted net assets are reclassified to unrestricted net assets. There were no permanently or temporarily restricted assets as of and for the year ended December 31, 2012. Furthermore, information is required to segregate program service expenses from management and general expenses.

Noncontrolling interests consist of the equity of unrelated partners in the Operating Partnerships.

Income taxes

AHA2 is a nonprofit corporation under Section 501(c)(3) of the Internal Revenue Code ("IRC") and Section 23701(d) of the California Revenue and Taxation Code and, therefore, is generally exempt from both federal and state income taxes. However, income from unrelated business activity not directly related to its tax-exempt purpose is subject to income tax. During the year ended December 31, 2012, AHA2 had no unrelated business income. In addition, AHA2 qualifies for the charitable contribution deduction under Section 170(b)(1)(A) and is qualified as an organization that is not a private foundation under Section 509(a)(2).

Income taxes on partnership income are levied on the partners in their individual capacity. Accordingly, all profits and losses of the Operating Partnerships are recognized by each partner on its respective tax return.

The preparation of consolidated financial statements in accordance with accounting principles generally accepted in the United States of America requires the company to report information regarding its exposure to various tax positions taken by AHA2. Management has determined whether any tax positions have met the recognition threshold and has measured the AHA2's exposure to those tax positions. Management believes that AHA2 has adequately addressed all relevant tax positions and that there are no unrecorded tax liabilities. Federal tax authorities generally have the right to examine and audit the previous three years of tax returns filed. Any interest or penalties assessed to AHA2 are recorded in operating expenses. No interest or penalties from federal or state tax authorities were recorded in the accompanying consolidated financial statements.

2. Summary of significant accounting policies (continued)

Use of estimates

The preparation of consolidated 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 reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates. Significant estimates include the collection of developer, managing general partner, management specialist service agreement, and asset/incentive management fees which in most cases is dependent on the underlying properties' cash flow.

Revenue recognition

AHA2 receives its revenue (not including public contributions or grants) from four primary sources. The first source is generated on a monthly basis from managing general partner fees (not to be confused with property management fees) for each project (which is also negotiable). The second source is asset management fees for each project. The third source consists of development fees, which are negotiated for each project and are payable in accordance with the applicable partnership or development agreement. The fourth source is from the infrequent sale of a property, the funds from which will still be subject to fulfilling the non-profit purpose of AHA2. All fees are recognized when earned.

The Operating Partnerships generate rental income from their operations. Rental income is recognized as rentals become due. Rental payments received in advance are deferred until earned. All leases between Operating Partnerships and the tenants are residential leases.

Contributions

Contributions are recognized as revenue when they are unconditionally given. Grants represent contributions if resource providers receive no value in exchange for the assets transferred. Contributions received are recorded at their fair value as unrestricted, temporarily restricted, or permanently restricted net assets depending on the absence or existence and nature of any donor-imposed restrictions as applicable. When a restriction expires (that is when a stipulated time restriction ends or purpose restriction is accomplished), temporarily restricted net assets are reclassified to unrestricted net assets and reported in the consolidated statement of activities and changes in net assets as net assets released from restrictions. If donors' restrictions are satisfied in the same period that the contribution is received or the contribution is restricted for the purchase of long-lived assets, the contribution is reported as unrestricted funds.

Contributed services are recognized in the consolidated financial statements when the services either (a) create or enhance a nonfinancial asset or (b) are specialized skills provided by entities or persons possessing those skills that would be purchased if they were not donated.

2. Summary of significant accounting policies (continued)

Economic concentrations

AHA2 receives a significant amount of revenue from the projects in which it is a general partner. These sources of funds are dependent upon the continued successful development and management of these projects.

AHA2, as a general partner, has an economic interest in the projects that are subject to business risks associated with the economy and level of unemployment in California and Colorado, which affects occupancy as well as the tenants' ability to make rental payments. In addition, these projects operate in a heavily regulated environment. The operations of these projects 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 an act of Congress or an administrative change mandated by HUD and may occur with little notice or inadequate funding to pay for the related cost, including the additional administrative burden, to comply with a change.

Concentration of credit risk

AHA2 has exposure to credit risk to the extent that its cash and cash equivalents exceed amounts covered by federal deposit insurance. AHA2 believes that its credit risk is not significant.

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 repairs or improvements to the buildings that extend their useful lives and annual insurance and property tax payments.

The carrying amounts of cash and restricted cash approximate their fair values.

Account receivables and bad debts

Accounts receivable are charged to bad debt expense when they are determined to be uncollectible based upon periodic review of the accounts by management. Accounting principles generally accepted in the United States of America require that the allowance method be used to recognize bad debts; however, the effect of using the direct write-off method is not materially different from the results that would have been obtained under the allowance method.

Fixed assets

AHA2 records all fixed assets at cost. The depreciation of the fixed assets is provided using the straight-line method over the following estimated useful lives:

Description	Life
Residential building	40 years
Land improvements	7 to 20 years
Furniture and equipment	3 to 12 years

2. Summary of significant accounting policies (continued)

Impairment of long-lived assets
AHA2 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 flow 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 for the year ended December 31, 2012.

Intangible assets and amortization
Intangible assets consist of permanent loan fees and tax credit fees. Permanent loan fees are amortized over the life of the respective loan. Tax credit fees are amortized using the straight-line method over a period of 10 or 15 years (a period that coincides with the compliance period in accordance with IRC Section 42).

Functional expenses allocation
The costs of providing program services and support services are summarized on a functional basis in the consolidated statements of activities and consolidated statements of functional expenses. The functional classifications are defined as follows:

- Program services expenses consist of costs incurred in connection with providing services and conducting programs.

- Support services consist of costs incurred in connection with the overall activities of AHA2, which are not allocable to another functional expense category.

Fair value measurements
AHA2 applies the accounting provisions related to fair value measurements. These provisions define fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, establish a hierarchy that prioritizes the information used in developing fair value estimates and require disclosure of fair value measurements by level within the fair value hierarchy. The hierarchy gives the highest priority to quoted prices in active markets (Level 1 measurements) and the lowest priority to unobservable data (Level 3 measurements), such as the reporting entity's own data. These provisions also provide valuation techniques, such as the market approach (comparable market prices), the income approach (present value of future income or cash flows) and the cost approach (cost to replace the service capacity of an asset or replacement cost).

A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement. The three levels of valuation hierarchy are defined as follows:

2. Summary of significant accounting policies (continued)

Fair value measurements (continued)

Level 1: Observable inputs such as quoted prices (unadjusted) for identical assets or liabilities in active markets.

Level 2: Inputs other than quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument.

Level 3: Unobservable inputs that reflect AHA2's own assumptions.

	December 31, 2012			
	Level I	Level II	Level III	Fair value measurements
Series CC-S Bonds	$ -	$ 1,420,252	$ -	$ 1,420,252
Restricted cash	163,567	-	-	163,567
	$ 163,567	$ 1,420,252	$ -	$ 1,583,819

AHA2's financial instruments include cash and cash equivalents, receivables, accounts payable and accrued expenses. The carrying amount of these financial instruments approximates their fair value due to their short maturities.

Subsequent events
Subsequent events have been evaluated through October 8, 2013, which is the date the financial statements were available to be issued. In 2013, management decided to put Rancho Las Brisas Murrieta, L.P. and Highlander Pointe, LLC on the market for sale in order to raise capital for new developments and to support AHA2's operations. Rancho Las Brisas Murrieta, L.P. received a satisfactory offer and has gone under contract with a potential buyer. If successful, the sale should close in mid-November. As of October 8, 2013, Highlander Pointe, LLC has not received an offer acceptable to management and management will continue the marketing process to determine if the market conditions exist for a potential disposition.

3. Restricted cash

AHA2's restricted cash is comprised of the following as of December 31, 2012:

Replacement reserve	$ 143,631
Tax and insurance escrow	19,936
Total	$ 163,567

4. Fixed assets

As of December 31, 2012, the fixed assets consist of:

	AHA2	Operating Partnerships	Total
Land	$ -	$ 1,168,441	$ 1,168,441
Buildings	-	8,980,475	8,980,475
Land improvements	-	502,106	502,106
Furniture and equipment	72,150	-	72,150
Total fixed assets	72,150	10,651,022	10,723,172
Less: accumulated depreciation	(10,807)	(2,898,672)	(2,909,479)
Net fixed assets	$ 61,343	$ 7,752,350	$ 7,813,693

Depreciation expense for the year ended December 31, 2012 was $256,336.

5. Intangible assets

As of December 31, 2012, intangible assets consist of:

	AHA2	Operating Partnerships	Total
Loan fees	$ -	$ 163,058	$ 163,058
Tax credit fees		28,060	28,060
Total intangible assets	-	191,118	191,118
Less: accumulated amortization	-	(110,509)	(110,509)
Net intangible assets	$ -	$ 80,609	$ 80,609

Amortization expense for the year ended December 31, 2012 was $10,176.

6. Share of deficiency in assets of partnerships

A summary of AHA2's investments as a non-managing member in non-consolidated entities as of December 31, 2012 is as follows:

	AHA2 Investment Balance	% of Ownership Profits/ Losses	Total Partnerships' Capital/ (Deficit)	AHA2 Share of Partnerships' Income/(Loss)
Highlander Pointe, LLC	$ (128,992)	25.00%	$ (515,967)	$ (63,744)
Maroon Creek Apartments, L.P.	(16,594)	0.51%	3,336,476	579
Anaheim Affordable II, L.P.	49	0.004%	1,329,567	49
Rancho Las Brisas Murrieta, L.P.	(453,671)	50.00%	(907,342)	(445,498)
Total	$ (599,208)		$ 3,242,734	$ (508,614)

6. Share of deficiency in assets of partnerships (continued)

Highlander Pointe, LLC
In July 2010, Highlander Pointe, LLC was formed for the purpose of owning or leasing the land and to own, construct, hold, improve, maintain, operate, develop, sell, mortgage, exchange, finance and lease a 132 unit affordable housing complex known as Highlander Pointe Apartments located in Riverside, California. AHA2 has a 25 percent interest in the limited liability company.

Maroon Creek Apartments, L.P.
In December 1994, Maroon Creek Apartments, L.P. was formed for the purpose of owning or leasing the land and to own, construct, hold, improve, maintain, operate, develop, sell, mortgage, exchange, finance and lease 42 multifamily senior rental housing units known as Maroon Creek Apartments in Aspen, Colorado. AHA2 has a 0.51 percent general partner interest in the partnership.

Rancho Las Brisas Murrieta, L.P.
In December 2011, Rancho Las Brisas Murrieta, L.P. was formed to acquire and rehabilitate and to develop, finance, rehabilitate, own, maintain, operate, and sell a rental-housing property in Murrieta, California. AHA2 has a 50 percent limited partner interest in the partnership.

Anaheim Affordable II, L.P.
In June 2012, Anaheim Affordable II, L.P. was formed to acquire, construct, own, finance, lease, and operate 135 multifamily rental housing units known as Villa Anaheim Apartments in Anaheim, California. AHA2 has a 0.004 percent general partner interest in the partnership.

7. Summaries of Operating Partnerships

Claremont Villas, LLC
In July 2009, Claremont Villas, LLC ("Claremont") was formed for the purpose of owning or leasing the land and to own, construct, hold, improve, maintain, operate, develop, sell, mortgage, exchange, finance and lease 154 units of affordable housing known as Claremont Senior Villas in Claremont, California. On December 30, 2011, Claremont sold Claremont Senior Villas.

Elizabeth Street Investors, L.P.
In August 1999, Elizabeth Street Investors, L.P. was formed for the purpose of owning or leasing the land and to own, construct, hold, improve, maintain, operate, develop, sell, mortgage, exchange, finance and lease 50 multi-family rental units known as Woodbridge Senior Apartments in Fort Collins, Colorado. AHA2 has a 0.001 percent general partner interest in the partnership.

7. Summaries of Operating Partnerships (continued)

Fort Collins Senior Housing Investors, L.P.
In November 1998, Fort Collins Senior Housing Investors, L.P. was formed for the purpose of owning or leasing the land and to own, construct, hold, improve, maintain, operate, develop, sell, mortgage, exchange, finance and lease 72 multifamily senior rental-housing units known as Reflections Senior Apartments in Fort Collins, Colorado. AHA2 has a 0.1 percent general partner interest in the partnership.

8. Investment in bonds

On December 21, 2011, California Statewide Communities Development Authority ("CSCDA") issued Variable Rate Demand Multifamily Housing Revenue Bonds Series 2011 CC in the amount of $15,500,000 and Subordinate Multifamily Housing Revenue Bonds Series 2011 CC-S in the amount of $6,400,000 (the "Subordinate Bonds"). Rancho Las Brisas Murrieta, L.P. entered into a loan agreement with CSCDA and Wells Fargo Bank Association (the "Trustee") in the amount of $15,500,000 and a subordinate loan agreement with CSCDA and the Trustee in the amount of $6,400,000. Concurrent with the creation of the notes, CSCDA entered into a trust indenture with the Trustee. Pursuant to this agreement, CSCDA assigned the Trustee all of its rights, title, and interest under the notes.

On December 21, 2011, AHA2 purchased $4,400,000 of the Subordinate Bonds. Interest on the Subordinate Bonds accrues at 8%. The Subordinate Bonds require interest only payments. The maturity date of the Subordinate Bonds is December 20, 2051. As of December 31, 2012, the investment in the Subordinate Bonds was $1,400,000 and interest receivable was $20,252. For the year ended December 31, 2012, interest income was $143,200. On January 25, 2012, AHA2 used $3,000,000 of the Subordinate Bonds to pay the outstanding debt due to Pacific Blue Investments. See Note 13.

9. Related party transactions

Managing general partner fees
AHA2 receives fees from several lower-tier properties for which it is the Managing General Partner. The amount of these fees is determined based on each property's partnership agreement. For the year ended December 31, 2012, AHA2 earned $20,228 of managing general partner fees and $7,684 was eliminated in consolidation. As of December 31, 2012, managing general partner fees receivable was $34,906 and $16,090 of managing general partner fees receivable was eliminated in consolidation.

9. Related party transactions (continued)

Incentive management fees receivable
AHA2 earned incentive management fees of $1,000 for the year ended December 31, 2012 from the Operating Partnerships that was eliminated in consolidation. As of December 31, 2012, no incentive management fees were outstanding.

Gary Ponce consulting fees
In 2011, AHA2 incurred consulting fees to Gary Ponce in the amount of $50,200 for asset management services provided for Claremont Villas, LLC. Gary Ponce is related to Anjela Ponce, director of AHA2, as husband and wife. As of December 31, 2011, consulting fees of $27,500 remained payable to Gary Ponce. As of December 31, 2012, consulting fees of $7,500 remained payable to Gary Ponce.

Developer fees
AHA2 earns developer fees from lower-tier properties, which it serves as developer. For the year ended December 31, 2012, AHA2 earned and was paid $50,000 of developer fees from Anaheim Affordable II, L.P. As of December 31, 2012, developer fees receivable from Highlander Pointe, LLC and Rancho Las Brisas Murrieta, L.P. was $254,465 and $1,257,770, respectively.

Purchase of Claremont
Pursuant to the purchase agreement between FFAH and AHA2 entered into as of February 1, 2010, FFAH agreed to sell its membership interest in Claremont for $3,215,000. Of the total sales price, AHA2 paid $3,015,000 and was to use the remaining $200,000 to fund operating expenses. Under the terms of the agreement, AHA2 purchased from FFAH its membership interest in Claremont in three phases: 49% effective February 1, 2010, 49% effective February 1, 2011 and 2% effective February 1, 2012. During 2011, the $200,000 payable to FFAH was forgiven. Claremont was liquidated and dissolved in 2012.

10. Due to noncontrolling interests - Operating Partnerships

Noncontrolling interests - fees
The Operating Partnerships incurred various accrued fees and payables to their limited partner(s) and other related parties. All fees owed to AHA2 have been eliminated. The outstanding fees are due to related parties of the Operating Partnerships other than AHA2. As of December 31, 2012, accrued fees due to noncontrolling interests were $44,589.

10. Due to noncontrolling interests - Operating Partnerships (continued)

Voluntary loans – Elizabeth Street
The investor limited partner of Elizabeth Street has advanced certain monies to the partnership. The advance is unsecured and bears interest at a rate of 7% per annum compounded annually. On December 1, 2009, the partnership entered into a note with the investor limited partner. The note will mature on December 1, 2039 and is due and payable from the distribution of cash flow in the order of priority as further detailed in the partnership agreement. During 2012, interest expense was $48,652. As of December 31, 2012, the outstanding principal balance was $482,150 and accrued interest was $238,749.

On December 1, 2009, Elizabeth Street converted the outstanding developer note and its accrued interest due to MCA Housing Partners, LLC into a voluntary loan. The note will mature on December 1, 2039, bears interest at a rate of 7% per annum compounded annually and is due and payable from the distribution of cash flow in the order of priority as further detailed in the partnership agreement. During 2012, interest expense was $40,716. As of December 31, 2012, the outstanding principal balance was $503,693 and accrued interest was $117,131.

Voluntary loan - Fort Collins
On December 1, 2011, Fort Collins converted the outstanding developer note and accrued interest into a voluntary loan. The voluntary loan matures on December 1, 2041, bears interest at a fixed rate of 2.8% compounded annually, and is due and payable from the distribution of cash flow in the order of priority as further detailed in the partnership agreement. During 2012, interest expense was $5,756. As of December 31, 2012, the outstanding principal balance and accrued interest was $202,315 and $5,756, respectively.

11. Notes payable

Notes payable consist of the following as of December 31, 2012:

	Principal	Accrued Interest
AHA2 Effective February 1, 2010, AHA2 entered into a loan agreement with Pacific Blue Investments, LLC in the amount of $3,215,000. The loan bore interest at a rate of 6% per annum. The loan and accrued interest were paid in full on January 25, 2012 using $3,000,000 in Subordinate Bonds and a cash payment of $457,729. During 2012, interest expense was $59,694.	$ -	$ -
Fort Collins Senior Housing Investors, L.P. Effective December 6, 2000, the partnership entered into a loan agreement with ARCS Commercial Mortgage Co., L.P. in the amount of $2,100,000. The loan is secured by a first deed of trust on the project and requires monthly payments of principal and interest totaling $14,914. The loan bears interest at a fixed rate of 7.66% per annum and matures on February 1, 2020. During 2012, interest expense was $138,712.	1,792,278	11,441
Effective September 27, 1999, the partnership entered into a loan agreement with the City of Fort Collins in the amount of $200,000. The loan is secured by a second deed of trust on the project. The loan will mature on September 27, 2019 and bears interest at a fixed rate of 7% per annum, compounded annually. Payment of the loan is to be made from available cash flow, as outlined in the partnership agreement. Payments will first be applied to any accrued interest, then to the principal amount. During 2012, interest expense was $31,185.	200,000	276,717

11. Notes payable (continued)

	Principal	Accrued Interest
Elizabeth Street Housing Investors, L.P Effective July 24, 2003, the partnership entered into loan agreements with the Colorado Housing Finance Authority in the amounts of $950,000 (the “First Loan”) and $350,000 (the “Second Loan”). The First Loan bears interest at a fixed rate of 6.35% per annum and is secured by a first deed of trust on the project. The Second Loan bears interest at a fixed rate of 1.00% per annum and is secured by a second deed of trust on the project. Commencing on September 1, 2003, principal and interest payments on the First Loan and Second Loan of $5,911 and $1,126, respectively, are due on the first day of the month until maturity. The unpaid principal and accrued and unpaid interest on both loans are due August 1, 2023. During 2012, interest expense was $54,891.	$ 1,067,461	$ 4,524
Effective December 14, 2001, the partnership entered into a loan agreement with the City of Fort Collins in the amount of $250,000. The note bears interest at a fixed rate of 5.5% per annum beginning on January 1, 2003. Annual interest only payments are due beginning December 14, 2003 through December 14, 2011. Beginning in year eleven until the maturity date, the partnership is required to pay equal annual payments of principal and accrued interest in an amount necessary to allow for the full repayment of the loan. The loan matures on December 15, 2021. The unpaid principal and accrued interest is due and payable in full upon the earlier of the sale of the project or the maturity date. The loan is secured by a deed of trust on the project. During 2012, interest expense was $13,750.	250,000	-
Effective May 1, 2003, the partnership entered into a loan agreement with the First National Bank of Fort Collins in the amount of $179,129, without interest. The note was made pursuant to the Federal Home Loan Bank Affordable Housing Program to help finance the construction of the project. The loan is secured by a deed of trust on the project. The loan matures on May 1, 2018.	179,129	-
Total	$ 3,488,868	$ 292,682

11. Notes payable (continued)

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

Year ending December 31,		
2013	$	94,430
2014		100,383
2015		106,756
2016		113,581
2017		120,883
Thereafter		2,952,835
Total	$	3,488,868

12. Other income

Other income is comprised of the following for the year ended December 31, 2012:

Claremont post sale income	$	10,922
Other rental related income		13,331
Miscellaneous		18,758
Total other income	$	43,011

13. Changes in consolidated unrestricted net assets

The changes in AHA2's consolidated unrestricted net assets are reconciled as follows:

	Total	Controlling Interests	Noncontrolling Interests
Balance, January 1, 2012	$ 7,243,585	$ 4,116,990	$ 3,126,595
Purchase of Claremont interest	-	131,850	(131,850)
Change in unrestricted net assets	(1,379,767)	(1,159,312)	(220,455)
Balance, December 31, 2012	$ 5,863,818	$ 3,089,528	$ 2,774,290

14. Payroll services

AHA2 has contracted with KimstaffHR to handle its payroll administration. Under this contract, all employees are employed by KimstaffHR, however they work directly for AHA2.

15. Business risk and liquidity

As indicated in the accompanying consolidated financial statements, AHA2 incurred a $1,159,312 decrease in its controlling interest of unrestricted net assets during the year ended December 31, 2012. AHA2 has in part, funded its continuing operations through development fee payments from Highlander Pointe, LLC and from Rancho Las Brisas Murrieta, L.P., which were recorded in years ended December 31, 2010 and in 2011, respectively, and carried on the books of AHA2 as receivables. Although these revenues were recognized in years ended December 31, 2010 and 2011, the process of collecting them may go on for years as the deferred portion of the fees earned are paid from cash flow of the respective properties. The collection of these deferred fees requires careful, efficient operation of the respective properties. The emphasis has to remain on the professional management of the properties. This collection of assets from affiliates creates a continuing challenge for AHA2.

Management of AHA2 has developed a plan to further reduce expenses and increase revenue through continued operational improvements. Effective November 2013, AHA2 will no longer pay for all costs of health benefits, AHA2 will pay for 75% of the lowest benefit offered and the employee will pay the difference. In addition, highly compensated employees will no longer receive a 401k match from AHA2. AHA2 has also been presented with opportunities to partner in the acquisition of existing tax credit communities as well as the development of new construction properties. Finally, the potential disposition of Rancho Las Brisas Murrieta, L.P. and Highlander Pointe, LLC will assist AHA2 to raise capital for new developments and support AHA2's operations.

SUPPLEMENTARY INFORMATION

AFFORDABLE HOUSING ALLIANCE II, INC. AND SUBSIDIARIES
DBA INTEGRITY HOUSING
CONSOLIDATING STATEMENT OF FINANCIAL POSITION
December 31, 2012

	AHA2	Subsidiaries	Pre - Consolidation	Eliminations	Consolidated Balance
ASSETS					
Current assets					
Cash and cash equivalents	$ 654,395	$ 184,161	$ 838,556	$ -	$ 838,556
Other receivables	22,192	1,700	23,892	-	23,892
Managing general partner fees receivable	34,906	-	34,906	(16,090)	18,816
Tenant receivables	-	2,653	2,653	-	2,653
Security deposits	-	31,300	31,300	-	31,300
Prepaid expenses	-	5,762	5,762	-	5,762
Total current assets	711,493	225,576	937,069	(16,090)	920,979
Fixed assets					
Fixed assets	72,150	10,651,022	10,723,172	-	10,723,172
Accumulated depreciation	(10,807)	(2,898,672)	(2,909,479)	-	(2,909,479)
Total fixed assets	61,343	7,752,350	7,813,693	-	7,813,693
Other assets					
Restricted cash	-	163,567	163,567	-	163,567
Developer fee receivable	1,512,235	-	1,512,235	-	1,512,235
Investment in Series CC-S Bonds	1,400,000	-	1,400,000	-	1,400,000
Interest receivable on Series CC-S Bonds	20,252	-	20,252	-	20,252
Intangible assets, net	-	80,609	80,609	-	80,609
Total other assets	2,932,487	244,176	3,176,663	-	3,176,663
Total assets	$ 3,705,323	$ 8,222,102	$ 11,927,425	$ (16,090)	$ 11,911,335

See report of independent auditors

AFFORDABLE HOUSING ALLIANCE II, INC. AND SUBSIDIARIES
DBA INTEGRITY HOUSING
CONSOLIDATING STATEMENT OF FINANCIAL POSITION (CONTINUED)
December 31, 2012

	AHA2	Subsidiaries	Pre - Consolidation	Eliminations	Consolidated Balance
LIABILITIES AND NET ASSETS					
Current liabilities					
Accounts payable and accrued expenses	$ 7,390	$ 25,915	$ 33,305	$ -	$ 33,305
Due to related parties - consulting fees	7,500	-	7,500	-	7,500
Security deposits payable	-	31,300	31,300	-	31,300
Prepaid income	-	271	271	-	271
Accrued interest - notes payable	-	15,965	15,965	-	15,965
Current maturities of notes payable	-	94,430	94,430	-	94,430
	14,890	167,881	182,771	-	182,771
Share of deficiency in assets of partnerships	600,905	-	600,905	(1,697)	599,208
Accrued interest - due to noncontrolling interests	-	361,636	361,636	-	361,636
Due to noncontrolling interests - Operating Partnerships	-	1,248,837	1,248,837	(16,090)	1,232,747
Accrued interest - notes payable	-	276,717	276,717	-	276,717
Notes payable, less current maturities	-	3,394,438	3,394,438	-	3,394,438
Total liabilities	615,795	5,449,509	6,065,304	(17,787)	6,047,517
Net assets					
Unrestricted net assets					
Controlling interest	3,089,528	(1,697)	3,087,831	1,697	3,089,528
Noncontrolling interest	-	2,774,290	2,774,290	-	2,774,290
Total net assets	3,089,528	2,772,593	5,862,121	1,697	5,863,818
Total liabilities and net assets	$ 3,705,323	$ 8,222,102	$ 11,927,425	$ (16,090)	$ 11,911,335

AFFORDABLE HOUSING ALLIANCE II, INC. AND SUBSIDIARIES
DBA INTEGRITY HOUSING
CONSOLIDATING STATEMENT OF ACTIVITIES
For the year ended December 31, 2012

	AHA2	Subsidiaries	Pre-Consolidation	Eliminations	Consolidated Balance
Revenue					
Rental income	$ -	$ 849,393	$ 849,393	$ -	$ 849,393
Managing general partner fee	20,228	-	20,228	(7,684)	12,544
Developer fee income	50,000	-	50,000	-	50,000
Other income	30,900	13,111	44,011	(1,000)	43,011
Interest income	144,974	104	145,078	-	145,078
Partnership flow-through loss	(542,367)	-	(542,367)	33,753	(508,614)
Total revenue	(296,265)	862,608	566,343	25,069	591,412
Expenses					
Program services					
Rental of affordable housing	-	1,116,816	1,116,816	(8,684)	1,108,132
Project expenses	724,493	-	724,493	-	724,493
Total program services	724,493	1,116,816	1,841,309	(8,684)	1,832,625
Supporting services					
General and administrative	138,554	-	138,554	-	138,554
Total expenses	863,047	1,116,816	1,979,863	(8,684)	1,971,179
CHANGE IN NET ASSETS BEFORE PURCHASES AND DISTRIBUTIONS	(1,159,312)	(254,208)	(1,413,520)	33,753	(1,379,767)
Purchase of Claremont interest	131,850	-	131,850	(131,850)	-
Distributions from subsidiaries	-	(106,116)	(106,116)	106,116	-
CHANGE IN NET ASSETS	$ (1,027,462)	$ (360,324)	$ (1,387,786)	$ 8,019	$ (1,379,767)

See report of independent auditors