

CONSOLIDATED FINANCIAL STATEMENTS

Massachusetts Housing Investment Corporation
Years Ended June 30, 2003 and 2002

Massachusetts Housing Investment Corporation

Consolidated Financial Statements

Years Ended June 30, 2003 and 2002

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Report of Independent Auditors

Board of Directors
The Massachusetts Housing Investment Corporation

We have audited the accompanying consolidated balance sheets of the Massachusetts Housing Investment Corporation (the Corporation) as of June 30, 2003 and 2002, and the related consolidated statements of activities and cash flows for the years then ended. These financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Massachusetts Housing Investment Corporation at June 30, 2003 and 2002, and the consolidated changes in its net assets and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States.

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements taken as a whole. The accompanying consolidating balance sheet and consolidating statement of activities are presented for purposes of additional analysis and are not a required part of the financial statements. Such information has been subjected to the auditing procedures applied in our audits of the consolidated financial statements and, in our opinion, is fairly stated in all material respects in relation to the consolidated financial statements taken as a whole.

As discussed in Note 1, prior year financial statements have been restated to give effect to the correction of an error.



October 24, 2003

Massachusetts Housing Investment Corporation

Consolidated Balance Sheets

	June 30	
	2003	2002
	<i>(Restated)</i>	
Assets		
Cash	\$ 1,371,527	\$ 209,041
Money market deposits at member corporations—loan fund	250,000	250,000
Notes receivable—MHEF Partnerships	13,456,377	12,893,218
Loans to affiliates	1,050,285	790,000
Due from affiliates	843,429	347,674
Amounts receivable and other assets	872,624	532,012
Furniture, equipment and leasehold improvements, net of accumulated depreciation and amortization of \$967,597 and \$874,987 in 2003 and 2002, respectively	202,758	157,824
Total assets	\$18,047,000	\$15,179,769
Liabilities and net assets		
Liabilities:		
Notes payable to member corporations	\$ 250,000	\$ 250,000
Unearned fees	13,360,369	9,732,038
Accrued interest and other liabilities	1,498,565	1,475,978
Total liabilities	15,108,934	11,458,016
Net assets:		
Unrestricted	2,770,953	3,721,753
Temporarily restricted	167,113	-
Total net assets	2,938,066	3,721,753
Total liabilities and net assets	\$18,047,000	\$15,179,769

See accompanying notes.

Massachusetts Housing Investment Corporation

Consolidated Statements of Activities

	Years Ended June 30	
	2003	2002
	<i>(Restated)</i>	
Change in unrestricted net assets:		
Revenues		
Interest revenue:		
Interest on deposits	\$ 17,331	\$ 221,373
Interest on project loans	11,496	73,619
Total interest revenue	28,827	294,992
Interest expense on notes payable	-	(77,268)
Net interest revenue	28,827	217,724
Loan program fee revenue:		
Management and advisory fees	271,770	261,811
Portfolio and servicing fees	794,518	548,758
Financing commitment fees	382,147	384,366
Origination fees	341,901	363,226
Available earnings fee	146,735	11,372
	1,937,071	1,569,533
Grant awards	468,126	-
Equity program revenue:		
Fees related to MHEF Partnerships	1,624,450	4,073,560
Other equity program fees	52,864	50,733
Total revenues	4,111,338	5,911,550
Expenditures		
Salaries and employee benefits	3,460,219	3,393,734
Occupancy, equipment and furniture	445,417	409,334
Professional services	383,931	1,129,383
Other expenditures	772,571	835,051
Total expenditures	5,062,138	5,767,502
(Decrease) increase in unrestricted net assets	(950,800)	144,048
Changes in temporarily restricted net assets:		
Grant awards	167,113	-
(Decrease) increase in net assets	(783,687)	144,048
Net assets at beginning of year	3,721,753	3,577,705
Net assets at end of year	\$2,938,066	\$3,721,753

See accompanying notes.

Massachusetts Housing Investment Corporation

Consolidated Statements of Cash Flows

	Year ended June 30	
	2003	2002
	<i>(Restated)</i>	
Operating activities		
(Decrease) increase in net assets	\$ (783,687)	\$ 144,048
Adjustments to reconcile excess of revenues over expenditures to net cash provided by (used in) operating activities:		
Depreciation and amortization expense	92,610	100,964
(Increase)/ decrease in amounts receivable and other assets	(836,367)	155,507
Decrease in unearned fees	(1,224,451)	(3,618,545)
Increase in accrued interest and other liabilities	22,587	419,214
Payments received on notes receivable—MHEF Partnerships	4,289,623	2,689,209
Net cash provided by (used in) operating activities	1,560,315	(109,603)
Investing activities		
Payments received on loans to affiliates	3,640,000	—
Funds advanced under loans to affiliates	(3,900,285)	(790,000)
Decrease in money market deposits at member corporations	—	2,123
Purchases of furniture, equipment and leasehold improvements	(137,544)	(130,733)
Net cash used in investing activities	(397,829)	(918,610)
Net increase (decrease) in cash	1,162,486	(1,028,213)
Cash at beginning of year	209,041	1,237,254
Cash at end of year	\$ 1,371,527	\$ 209,041
Supplemental information:		
Unearned fees recorded in exchange for notes receivable	\$ 4,852,782	\$ 7,195,711
Cash paid for interest on notes payable	—	\$ 77,267

See accompanying notes.

Massachusetts Housing Investment Corporation

Notes to Consolidated Financial Statements

June 30, 2003 and 2002

1. Background and Accounting Policies

Purpose

On July 1, 1990, the Massachusetts Housing Investment Corporation (MHIC) was formally established as a Massachusetts-chartered, Chapter 180, not-for-profit corporation. MHIC's mission is to pool the resources of Massachusetts' lenders and investors to improve and expand the financing of affordable housing throughout the state. MHIC has established two main financing programs to carry out its mission:

Loan Program

The loan program focuses on providing debt financing to developers of affordable housing. From its inception in 1990 through December 2000, MHIC utilized a loan pool structure to extend this financing. The loan-pool was funded with the proceeds from below market rate loans (member loans) made to MHIC from participating member corporations. In January 2001, MHIC converted the loan pool to a limited liability company structure. As a result, the member loans were converted to equity interests in a new entity, MHIC, LLC (the LLC). In addition, the various project loans, deposit accounts and reserves owned by MHIC were transferred to the LLC in exchange for extinguishing the member loans. MHIC is the manager of the LLC (See Note 2, Loan Program Conversion).

Equity Program

The equity program provides tax credit equity financing to developers of affordable housing. The initial role of the program was to assist member corporations in underwriting low-income housing tax credit investments. The program, through its wholly-owned subsidiary Massachusetts Housing Equity Fund, Inc. (MHEF), is now a full-service syndicator of limited partnerships (the Partnerships) structured for investment in low-income housing projects (Operating Partnerships) in Massachusetts. MHEF was formed in June 1993 and is currently the General Partner of nine Operating Partnerships.

Basis of Presentation

Net assets and revenues, gains and losses are classified based on the existence of donor-imposed restrictions. Accordingly, net assets and changes therein are classified as follows:

Permanently restricted net assets—Net assets subject to donor-imposed stipulations that they be maintained in perpetuity by MHIC.

Massachusetts Housing Investment Corporation

Notes to Consolidated Financial Statements (continued)

1. Background and Accounting Policies (continued)

Temporarily restricted net assets—Net assets subject to donor-imposed stipulations that may or will be met by actions of MHIC and/or the passage of time.

Unrestricted net assets—Net assets not subject to donor-imposed stipulations.

Contributions of cash and other assets are reported as temporarily restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor 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 statement of activities as net assets released from restrictions.

Temporarily restricted net assets at June 30, 2003 reflect grant funds that will be awarded to beneficiaries not yet specified for Chapter 40B technical assistance.

Principles of Consolidation

The consolidated financial statements include the accounts of MHIC and its wholly-owned subsidiary, MHEF. All significant intercompany transactions and balances have been eliminated in consolidation.

Furniture, Equipment and Leasehold Improvements

Furniture, equipment and leasehold improvements are stated at cost, less accumulated depreciation and amortization. Depreciation is computed by the straight-line method using rates based on estimated useful lives.

Revenue Recognition

Loan program fee revenue reflects fees earned on a contractual basis for services provided to the LLC (see Note 2).

Equity program revenue reflects fees for services that include organization, syndication, underwriting, long-term asset management and partnership administration. The fees for syndicating and organizing the Partnerships are recognized when syndication is substantially

Massachusetts Housing Investment Corporation

Notes to Consolidated Financial Statements (continued)

1. Background and Accounting Policies (continued)

complete. Fees for underwriting investments are recognized at the time the underlying properties are acquired. As of June 30, 2003, MHIC had substantially completed the acquisition of six properties for which closings had not yet occurred. These closings resulted in the recognition of \$1,133,130 of revenues subsequent to June 30. The fees for asset management and partnership administration are recognized evenly over the life of the Partnerships (estimated to be approximately 15 years). Certain refundable fees are deferred until the potential obligation lapses.

During 2003, MHIC concluded that certain revenues which it had previously deferred should have been recognized in earlier periods. In addition, additional losses associated with two of the Partnerships should have been recognized. Consequently, net assets as of June 30, 2001 were increased by the net amount of \$591,755 and net assets were increased by \$78,815 for the year ended June 30, 2002 to give effect to the correction of these errors.

Grants are recognized as revenue in the period in which the conditions, if any, of the grant are satisfied.

Income Tax Status

In February 1993, MHIC was granted tax-exempt status as a 501(c)(3) corporation under federal tax law. MHEF is a for-profit corporation and therefore is subject to federal and state income taxes.

Use of Estimates

Financial statements prepared in accordance with accounting principles generally accepted in the United States require the use of significant management estimates that affect the amounts and disclosures recorded in the consolidated financial statements. Actual results may differ from those estimates.

2. Loan Program Conversion

In January 2001, MHIC converted its loan-pool to an LLC structure. The initial capitalization of the LLC was effected by a Contribution Agreement whereby member corporations contributed loans made to MHIC under the former loan pool structure (member loans) to the LLC in exchange for LLC membership interests. In addition, MHIC and the LLC entered into a Participation Agreement that provided for the LLC to purchase an undivided 100% interest in the project loans, bank accounts and reserves owned by MHIC (associated with the former loan pool) in exchange for the discharge of the member loans.

Massachusetts Housing Investment Corporation

Notes to Consolidated Financial Statements (continued)

2. Loan Program Conversion (continued)

The proceeds of member loans for member corporations that have elected to remain in the loan pool (and not convert to the LLC structure) are held in deposit accounts at those institutions. The terms of the member loans are pursuant to a Master Member Agreement and accrue interest at 1% less than the annual interest rate earned on the interest-bearing deposit accounts (see Note 4).

MHIC earns advisory fees for managing the affairs of the LLC pursuant to the term of an Advisory Agreement. The scope of services under the Advisory Agreement includes managing the orderly underwriting, approval and origination of loans and acquisition of investments, servicing loans and investments, establishing loan and investment policies, supervising and managing the requisition and disbursement of funds for loans, investing idle funds, business development and various other services that may be required by the Company in the ordinary course of its business.

Under the terms of the Advisory Agreement, fees to MHIC are provided for as follows:

- ❑ A management and advisory fee equal to an annual percentage rate of 0.75% of the average value of the aggregate capital commitments of all Investor Members of the LLC during such payment period;
- ❑ A portfolio and servicing fee equal to an annual percentage rate of 1.50% of the average amount of Real Estate Investments outstanding during a given payment period;
- ❑ A financing commitment fee equal to an annual percentage rate of 0.50% of the average amount of funded and unfunded commitments for Real Estate Investments existing during a given payment period.

In addition, MHIC is entitled to an available earnings fee, based upon the degree to which the LLC achieves certain performance hurdles. MHIC shall receive the amounts described below in the following priority.

- ❑ First, after payment of a 4% return to the members of the LLC, MHIC shall receive 10% of all remaining available earnings until the members have received a return equal to the federal funds rate.
- ❑ Second, MHIC shall receive 40% of all remaining available earnings until members have received a return equal to the federal funds rate plus 2%.
- ❑ Third, MHIC shall receive 60% of all remaining available earnings until members have received a return equal to the federal funds rate plus 4%.
- ❑ Fourth, MHIC shall receive 75% of all remaining available earnings.

Massachusetts Housing Investment Corporation

Notes to Consolidated Financial Statements (continued)

2. Loan Program Conversion (continued)

Under the terms of the Advisory Agreement, MHIC earned available earnings fees of \$146,735 and \$45,488 in 2003 and 2002, respectively. For the year ended June 30, 2003, the full amount of the available earnings fee was recognized. For the year ended June 30, 2002, the Board of Directors ratified a one-time modification to the available earnings fee by calculating the available earnings fee at the first performance hurdle rate of 10% instead of the second performance hurdle rate of 40%, resulting in a modified fee of \$11,732.

3. Massachusetts Housing Equity Fund, Inc. (MHEF)

As of June 30, 2003 and 2002, MHIC's investment in MHEF amounted to \$2,878,606 and \$2,883,900, respectively. MHEF, as general partner of the aforementioned Partnerships, has a .01% in their respective profits, losses and distributions. MHEF accounts for its investment in the Partnerships using the equity method. Under the equity method, the investments are carried at cost and adjusted for MHEF's share of income or loss from the Partnerships, additional investments and cash distributions.

The Partnerships, as limited partners in the various Operating Partnerships, are subject to risks inherent in the ownership of property which is beyond their control, such as fluctuations in occupancy rates and operating expenses, variations in rental schedules, proper maintenance of facilities and continued eligibility of tax credits. If the cost of operating a property exceeds the rental income earned thereon, the Partnership, or MHEF acting independently as an investor, may deem it in its best interest to voluntarily provide funds in order to protect its investment.

At June 30, 2003 and 2002, the Partnerships have combined total assets of \$192 million and \$192 million, respectively, and combined cumulative deficits of approximately \$96 million and \$96 million, respectively.

4. Notes Payable to Member Corporations

Prior to the conversion, MHIC funded a loan pool through unsecured notes issued to member corporations pursuant to a Master Membership Agreement. Under this agreement, all note proceeds not currently used to fund projects are deposited in interest-bearing deposit accounts at their respective lending institutions. Note proceeds that are not used to fund projects accrue interest at 1% less than the annual interest rate earned on the interest-bearing deposit accounts. All proceeds that are lent to projects earn interest at the prime rate less 1%. For the years ended June 30, 2003 and 2002, interest expense paid to member corporations totaled approximately \$0

Massachusetts Housing Investment Corporation

Notes to Consolidated Financial Statements (continued)

4. Notes Payable to Member Corporations (continued)

and \$317, respectively, and is reflected in interest expense on notes payable in the accompanying consolidated statements of revenues and expenditures. These notes are renewable annually (applicable only to members that elected not to convert to the LLC). If the notes are not renewed, they require no principal amortization for five years and then amortize over a subsequent five-year period at an amount equal to the stated amount of the note less the member's pro-rata share of unfunded losses. At June 30, 2003 and 2002, outstanding borrowings under these agreements totaled \$250,000.

5. MHEF Notes Receivable and Unearned Fees

Notes receivable represent the present value (using effective interest rates that range from 8% to 9%) of future cash payments that will be received by MHIC from the MHEF Partnerships for asset management and other services it will provide to the Partnerships, as specified in the Partnership Agreements. At June 30, 2003 and 2002, notes receivable included accrued interest of \$411,102 and \$544,871, respectively.

Unearned equity fees reflect MHIC's obligation to provide future services to the Partnerships as consideration for the aforementioned notes receivable. These services include underwriting investments, long-term asset management and partnership administration. This obligation is reduced as services are provided, according to the revenue recognition methodology associated with the particular service (see Note 1). At June 30, 2003 and 2002, unearned fees were \$14,407,762 and \$10,755,119, respectively. Other unearned fees include development monitoring and loan commitment fees.

6. Leases

MHIC leases its facilities and certain furniture and equipment under operating leases that expire over future periods and require various minimum rental payments. Future minimum payments, by year and in aggregate, under these noncancelable operating leases consist of the following at June 30, 2003:

2004	\$ 347,268
2005	345,651
2006	340,800
2007	340,800
2008	88,530
Thereafter	<u>1,110</u>
Total	<u>\$1,464,159</u>

Massachusetts Housing Investment Corporation

Notes to Consolidated Financial Statements (continued)

6. Leases (continued)

MHIC incurred lease expenses associated with office space and equipment of \$329,227 and \$280,001 for the years ended June 30, 2003 and 2002, respectively.

7. Employee Benefit Plan

As a tax-exempt 501(c)(3) corporation, MHIC established a noncontributory, defined contribution plan under Section 401(a) of the Internal Revenue Code covering all full-time employees. The employer contribution is based upon a percentage of employee salary. In July 1999, MHIC amended the Plan to include a 100% match of employee contributions up to 3% of a given employee's salary. MHIC contributed and charged to expense approximately \$166,000 and \$148,000 for the years ended June 30, 2003 and 2002, respectively. These amounts are reflected in salaries and employee benefits in the accompanying consolidated statements of revenues and expenditures.

8. Grant Awards

In 1999, MHIC applied for and received designation as a Community Development Finance Institution (CDFI). MHIC also applied for and received a grant award of \$1,000,000 from the CDFI Fund. The purpose of the grant is to add to MHIC's capacity to pursue its mission and grow. The proceeds from the grant can be used to expand existing programs, develop new ones or support its operations. In April 2001, \$684,761 of that grant was received and recorded as income. In June 2003, MHIC secured matching funds to be eligible for the remaining \$315,239 of the grant, and recorded that amount as grant award income. As a condition to the funding of the grant, MHIC and the CDFI Fund executed an Assistance Agreement, which established target goals for MHIC to achieve and specific measurement criteria to be used in evaluating progress. The goals are merely guidelines to evaluate progress and achieving specific results are not a condition to retaining the grant award. The grant is revocable if MHIC substantially changes its mission or ceases to be a CDFI prior to June 30, 2004.

In June 2003 MHIC received a \$320,000 grant from the Massachusetts Housing Partnership Fund Board to provide grants in support of technical assistance to local communities confronting Chapter 40 B developments.

Other Financial Information

Massachusetts Housing Investment Corporation

Other Financial Information

Consolidating Balance Sheet

June 30, 2003

	MHIC	MHEF	Elimination	Consolidated
Assets				
Cash	\$ 1,257,501	\$ 114,026	\$ —	\$ 1,371,527
Money market deposits at member corporations—loan fund	250,000	—	—	250,000
Investment in MHEF Partnerships	2,878,606	—	(2,878,606)	—
Notes receivable—MHEF Partnerships	13,456,377	—	—	13,456,377
Loans to affiliates	1,050,285	—	—	1,050,285
Amounts receivable and other assets	1,656,324	59,729	—	1,716,053
Due from parent	—	2,704,881	(2,704,881)	—
Furniture, equipment and leasehold improvements, net of accumulated depreciation and amortization of \$967,597	202,758	—	—	202,758
Total assets	\$20,751,851	\$2,878,636	\$(5,583,487)	\$18,047,000
Liabilities and net assets				
Liabilities:				
Notes payable to member corporations	\$ 250,000	\$ —	\$ —	\$ 250,000
Due to subsidiary	2,704,881	—	(2,704,881)	—
Unearned fees	13,360,369	—	—	13,360,369
Accrued interest and other liabilities	1,498,535	30	—	1,498,565
Total liabilities	17,813,785	30	(2,704,881)	15,108,934
Net assets:				
Unrestricted	2,770,953	2,878,606	(2,878,606)	2,770,953
Temporarily restricted	167,113	—	—	167,113
Total net assets	2,938,066	2,878,606	(2,878,606)	2,938,066
Total liabilities and net assets	\$20,751,851	\$2,878,636	\$(5,583,487)	\$18,047,000

See accompanying notes.

Massachusetts Housing Investment Corporation

Other Financial Information

Consolidating Statement of Activities

For the year ended June 30, 2003

	MHIC	MHEF	Elimination	Consolidated
Change in unrestricted net assets:				
Revenues				
Interest revenue:				
Interest on bank deposits	\$ 16,405	\$ 926	\$ -	\$ 17,331
Interest on project loans	11,496	-	-	11,496
Total interest revenue	27,901	926	-	28,827
Interest expense on notes payable	-	-	-	-
Net interest revenue	27,901	926	-	28,827
Loan program fee revenue:				
Management and advisory fees	271,770	-	-	271,770
Portfolio and servicing fees	794,518	-	-	794,518
Financing commitment fees	382,147	-	-	382,147
Origination fees	341,901	-	-	341,901
Available earnings fee	146,735	-	-	146,735
Grant awards	468,126	-	-	468,126
Equity program revenue:				
Fees related to MHEF Partnerships	1,624,450	-	-	1,624,450
Other equity program fees	52,894	(30)	-	52,864
Income from investment in MHEF	(5,294)	-	5,294	-
Total revenues	4,105,148	896	5,294	4,111,338
Expenditures				
Salaries and employee benefits	3,460,219	-	-	3,460,219
Occupancy, equipment and furniture	445,417	-	-	445,417
Professional services	383,931	-	-	383,931
Other expenditures	766,381	6,190	-	772,571
Total expenditures	5,055,948	6,190	-	5,062,138
Decrease in unrestricted net assets	(950,800)	(5,294)	5,294	(950,800)
Change in temporarily restricted net assets:				
Grant awards	167,113	-	-	167,113
Decrease in net assets	(783,687)	-	-	(783,687)
Net assets at beginning of year	3,721,753	2,883,900	(2,883,900)	3,721,753
Net assets at end of year	\$2,938,066	\$2,878,606	\$(2,878,606)	\$2,938,066

See accompanying notes.

CONSOLIDATED FINANCIAL STATEMENTS

Massachusetts Housing Investment Corporation
As of December 31, 2003 and June 30, 2003 and
for the six-months Ended December 31, 2003 and
the year Ended June 30, 2003

Massachusetts Housing Investment Corporation

Consolidated Financial Statements

As of December 31, 2003 and June 30, 2003 and
for the six-months Ended December 31, 2003 and
the year Ended June 30, 2003

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Report of Independent Auditors

Board of Directors
The Massachusetts Housing Investment Corporation

We have audited the accompanying consolidated balance sheets of the Massachusetts Housing Investment Corporation (the Corporation) as of December 31, 2003 and June 30, 2003, and the related consolidated statements of activities and changes in net assets and cash flows for the six-months ended December 31, 2003 and for the year ended June 30, 2003. These financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Massachusetts Housing Investment Corporation at December 31, 2003 and June 30, 2003, and the consolidated results of its operations and its cash flows for the six-months ended December 31, 2003 and for the year ended June 30, 2003, in conformity with accounting principles generally accepted in the United States.

Our audits were conducted for the purpose of forming an opinion on the basic consolidated financial statements taken as a whole. The accompanying consolidating balance sheet and consolidating statement of activities are presented for purposes of additional analysis and are not a required part of the basic consolidated financial statements. Such information has been subjected to the auditing procedures applied in our audits of the consolidated financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic consolidated financial statements taken as a whole.

Ernst & Young LLP

May 27, 2004

Massachusetts Housing Investment Corporation

Consolidated Balance Sheets

	December 31	June 30
	2003	2003
Assets		
Cash	\$ 2,017,996	\$ 1,371,527
Money market deposits at member corporations—loan fund	250,000	250,000
Notes receivable—MHEF Partnerships	10,912,502	13,456,377
Loans to affiliates	2,223,028	1,050,285
Due from affiliates	525,808	843,429
Amounts receivable and other assets	392,226	872,624
Furniture, equipment and leasehold improvements, net of accumulated depreciation and amortization of \$1,012,737 and \$967,597 in 2003 and 2002, respectively	<u>162,851</u>	<u>202,758</u>
Total assets	<u>\$16,484,411</u>	<u>\$18,047,000</u>
Liabilities and net assets		
Liabilities:		
Notes payable to member corporations	\$ 250,000	\$ 250,000
Unearned fees	11,249,212	13,360,369
Accrued interest and other liabilities	<u>1,672,675</u>	<u>1,498,565</u>
Total liabilities	13,171,887	15,108,934
Net assets:		
Unrestricted	3,145,411	2,770,953
Temporarily restricted	<u>167,113</u>	<u>167,113</u>
Total net assets	<u>3,312,524</u>	<u>2,938,066</u>
Total liabilities and net assets	<u>\$16,484,411</u>	<u>\$18,047,000</u>

See accompanying notes.

Massachusetts Housing Investment Corporation

Consolidated Statements of Activities and Changes in Net Assets

	Six-months Ended December 31 2003	Year Ended June 30 2003
Change in unrestricted net assets:		
Revenues		
Interest revenue:		
Interest on deposits	\$ 14,253	\$ 17,331
Interest on loans to affiliates	25,718	11,496
Total interest revenue	<u>39,971</u>	<u>28,827</u>
Loan program fee revenue:		
Management and advisory fees	139,500	271,770
Portfolio and servicing fees	350,035	794,518
Financing commitment fees	182,722	382,147
Origination fees	165,165	341,901
Available earnings fee	189,119	146,735
	<u>1,026,541</u>	<u>1,937,071</u>
Grant awards	-	468,126
Equity program revenue:		
Fees related to Partnerships	2,284,317	1,624,450
Other equity program fees	23,046	52,864
Total revenues	<u>3,373,875</u>	<u>4,111,338</u>
Expenditures:		
Salaries and employee benefits	1,958,177	3,460,219
Occupancy, equipment and furniture	227,960	445,417
Professional services	535,409	383,931
Other expenditures	277,871	772,571
Total expenditures	<u>2,999,417</u>	<u>5,062,138</u>
Increase (decrease) in unrestricted net assets	374,458	(950,800)
Changes in temporarily restricted net assets:		
Grant awards	-	167,113
Increase (decrease) in net assets	<u>374,458</u>	<u>(783,687)</u>
Net assets at beginning of period	<u>2,938,066</u>	<u>3,721,753</u>
Net assets at end of period	<u><u>\$3,312,524</u></u>	<u><u>\$2,938,066</u></u>

See accompanying notes.

Massachusetts Housing Investment Corporation

Consolidated Statements of Cash Flows

	Six-months Ended December 31 2003	Year Ended June 30 2003
Operating activities		
Increase (decrease) in net assets	\$ 374,458	\$ (783,687)
Adjustments to reconcile (decrease) increase in net assets to net cash provided by operating activities:		
Depreciation and amortization expense	45,140	92,610
Decrease/ (increase) in amounts receivable and other assets	798,019	(836,367)
Decrease in unearned fees	(1,654,317)	(1,224,451)
Increase in accrued interest and other liabilities	174,110	22,587
Payments received on notes receivable—MHEF Partnerships	2,087,035	4,289,623
Net cash provided by operating activities	1,824,445	1,560,315
Investing activities		
Payments received on loans to affiliates	1,721,609	3,640,000
Funds advanced under loans to affiliates	(2,894,352)	(3,900,285)
Purchases of furniture, equipment and leasehold improvements	(5,233)	(137,544)
Net cash used in investing activities	(1,177,976)	(397,829)
Net increase in cash	646,469	1,162,486
Cash at beginning of period	1,371,527	209,041
Cash at end of period	\$ 2,017,996	\$ 1,371,527
Supplemental information:		
Unearned fees recorded in exchange for notes receivable	\$ 600,000	\$ 4,852,782

See accompanying notes.

Massachusetts Housing Investment Corporation

Notes to Consolidated Financial Statements

December 31, 2003

1. Background and Accounting Policies

Purpose

On July 1, 1990, the Massachusetts Housing Investment Corporation (MHIC) was formally established as a Massachusetts-chartered, Chapter 180, not-for-profit corporation. MHIC's mission is to pool the resources of Massachusetts' lenders and investors to improve and expand the financing of affordable housing throughout the state. MHIC has established two main financing programs to carry out its mission:

Loan Program

The loan program focuses on providing debt financing to developers of affordable housing. From its inception in 1990 through December 2000, MHIC utilized a loan pool structure to extend this financing. The loan-pool was funded with the proceeds from below market rate loans (member loans) made to MHIC from participating member corporations. In January 2001, MHIC converted the loan pool to a limited liability company structure. As a result, the member loans were converted to equity interests in a new entity, MHIC, LLC (the LLC). In addition, the various project loans, deposit accounts and reserves owned by MHIC were transferred to the LLC in exchange for extinguishing the member loans. MHIC is the manager of the LLC (see Note 2, Loan Program).

Equity Program

The equity program provides tax credit equity financing to developers of affordable housing. The initial role of the program was to assist member corporations in underwriting low-income housing tax credit investments. The program, through MHIC's wholly-owned subsidiary Massachusetts Housing Equity Fund, Inc. (MHEF), is now a full-service syndicator of limited partnerships (the Partnerships) structured for investment in low-income housing projects (Operating Partnerships) in Massachusetts. MHEF was formed in June 1993 and is currently the General Partner of nine Partnerships.

Basis of Presentation

Net assets and revenues, gains and losses are classified based on the existence of donor-imposed restrictions. Accordingly, net assets and changes therein are classified as follows:

Permanently restricted net assets—Net assets subject to donor-imposed stipulations that they be maintained in perpetuity by MHIC.

Massachusetts Housing Investment Corporation

Notes to Consolidated Financial Statements (continued)

1. Background and Accounting Policies (continued)

Temporarily restricted net assets—Net assets subject to donor-imposed stipulations that may or will be met by actions of MHIC and/or the passage of time.

Unrestricted net assets—Net assets not subject to donor-imposed stipulations.

Contributions of cash and other assets are reported as temporarily restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor 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 as net assets released from restrictions.

Temporarily restricted net assets at December 31, 2003 and June 30, 2003 reflect grant funds that will be awarded to beneficiaries not yet specified for Chapter 40B technical assistance.

Principles of Consolidation

The consolidated financial statements include the accounts of MHIC and its wholly-owned subsidiary, MHEF. All significant intercompany transactions and balances have been eliminated in consolidation.

Furniture, Equipment and Leasehold Improvements

Furniture, equipment and leasehold improvements are stated at cost, less accumulated depreciation and amortization. Depreciation is computed by the straight-line method using rates based on estimated useful lives that range from 3 to 5 years.

Revenue Recognition

Loan program fee revenue reflects fees earned on a contractual basis for services provided to the LLC (see Note 2).

Equity program revenue reflects fees for services that include organization, syndication, underwriting, long-term asset management and Partnership administration. The fees for syndicating and organizing the Partnerships are recognized when syndication is complete. Fees for underwriting investments are recognized at the time the underlying properties are acquired. The fees for asset management and Partnership administration are recognized evenly over the life of the Partnerships (estimated to be approximately 15 years). Certain refundable fees are deferred until the potential obligation lapses.

Massachusetts Housing Investment Corporation

Notes to Consolidated Financial Statements (continued)

1. Background and Accounting Policies (continued)

Grants are recognized as revenue in the period in which the conditions, if any, of the grant are satisfied.

Income Tax Status

In February 1993, MHIC was granted tax-exempt status as a 501(c)(3) corporation under federal tax law. MHEF is a for-profit corporation and therefore is subject to federal and state income taxes.

Use of Estimates

Financial statements prepared in accordance with accounting principles generally accepted in the United States require the use of significant management estimates that affect the amounts and disclosures recorded in the consolidated financial statements. Actual results may differ from those estimates.

Change in Fiscal Year-End

During 2003, MHIC changed its fiscal year-end from June 30 to December 31. As a result, the statement of operations and statement of cash flows present a six-month stub-period due to this transition.

2. Loan Program

The loan program utilizes a structure whereby investors invest in a limited liability company (MHIC, LLC), which in turn provides financing to low-income housing and community development projects. The interest on this financing is passed-through to investors to provide a "reasonable" return on investment. The initial capitalization of the LLC was effected by a Contribution Agreement whereby member corporations contributed loans made to MHIC under the former loan pool structure (member loans) to the LLC in exchange for LLC membership interests. In addition, MHIC and the LLC entered into a Participation Agreement that provided for the LLC to purchase an undivided 100% interest in the project loans, bank accounts and reserves owned by MHIC (associated with the former loan pool) in exchange for the discharge of the member loans.

The proceeds of member loans for member corporations that have elected to remain in the loan pool (and not convert to the LLC structure) are held in deposit accounts at those institutions. The terms of the member loans are pursuant to a Master Member Agreement and accrue interest at 1% less than the annual interest rate earned on the interest-bearing deposit accounts (see Note 4).

Massachusetts Housing Investment Corporation

Notes to Consolidated Financial Statements (continued)

MHIC earns advisory fees for managing the affairs of the LLC pursuant to the term of an Advisory Agreement. The scope of services under the Advisory Agreement includes managing the orderly underwriting, approval and origination of loans and acquisition of investments, servicing loans and investments, establishing loan and investment policies, supervising and managing the requisition and disbursement of funds for loans, investing idle funds, business development and various other services that may be required by the Company in the ordinary course of its business.

Under the terms of the Advisory Agreement, fees to MHIC are provided for as follows:

- ❑ A management and advisory fee equal to an annual percentage rate of 0.75% of the average value of the aggregate capital commitments of all Investor Members of the LLC during such payment period;
- ❑ A portfolio and servicing fee equal to an annual percentage rate of 1.50% of the average amount of real estate investments outstanding during a given payment period;
- ❑ A financing commitment fee equal to an annual percentage rate of 0.50% of the average amount of funded and unfunded commitments for Real Estate Investments existing during a given payment period.
- ❑ An origination fee, payable by borrowers, that typically range from .5% to 1% of a given loan amount. The origination fees are typically paid to the LLC and subsequently passed-through to MHIC.

In addition, MHIC is entitled to an available earnings fee, based upon the degree to which the LLC achieves certain performance hurdles. MHIC shall receive the amounts described below in the following priority.

- ❑ First, after payment of a 4% return to the members of the LLC, MHIC shall receive 10% of all remaining available earnings until the members have received a return equal to the federal funds rate.
- ❑ Second, MHIC shall receive 40% of all remaining available earnings until members have received a return equal to the federal funds rate plus 2%.
- ❑ Third, MHIC shall receive 60% of all remaining available earnings until members have received a return equal to the federal funds rate plus 4%.
- ❑ Fourth, MHIC shall receive 75% of all remaining available earnings.

Massachusetts Housing Investment Corporation

Notes to Consolidated Financial Statements (continued)

2. Loan Program (continued)

Under the terms of the Advisory Agreement, MHIC earned available earnings fees of \$189,119 and \$146,735 for the six months ended December 31, 2003 and the year ended June 30, 2003, respectively.

3. Massachusetts Housing Equity Fund, Inc. (MHEF)

As of December 31, 2003 and June 30, 2003, MHIC's investment in MHEF amounted to \$2,875,184 and \$2,878,606, respectively. MHEF, as general partner of the aforementioned Partnerships, has a .01% interest in their respective profits, losses and distributions. MHEF accounts for its investment in the Partnerships using the equity method. Under the equity method, the investments are carried at cost and adjusted for MHEF's share of income or loss from the Partnerships, additional investments and cash distributions.

The Partnerships, as limited partners in the various Operating Partnerships, are subject to risks inherent in the ownership of property which is beyond their control, such as fluctuations in occupancy rates and operating expenses, variations in rental schedules, proper maintenance of facilities and continued eligibility of tax credits. If the cost of operating a property exceeds the rental income earned thereon, the Partnership, or MHEF acting independently as an investor, may deem it in its best interest to voluntarily provide funds in order to protect its investment.

At December 31, 2003 and June 30, 2003, the Partnerships have combined total assets of \$224 million and \$194 million, respectively, and combined cumulative deficits of approximately \$122 million and \$114 million, respectively.

4. Notes Payable to Member Corporations

Prior to the conversion as discussed in Note 1, MHIC funded a loan pool through unsecured notes issued to member corporations pursuant to a Master Membership Agreement. Under this agreement, all note proceeds not currently used to fund projects are deposited in interest-bearing deposit accounts at their respective lending institutions. Note proceeds that are not used to fund projects accrue interest at 1% less than the annual interest rate earned on the interest-bearing deposit accounts. All proceeds that are lent to projects earn interest at the prime rate less 1%. For the period ended December 31, 2003 and June 30, 2003, MHIC did not incur or pay any interest expense to member corporations since the interest rate on the note payable was less than 0%. These notes are renewable annually (applicable only to members that elected not to convert to the LLC). If the notes are not renewed, they require no principal amortization for five years and then amortize over a subsequent five-year period at an amount equal to the stated amount of the note less the member's pro-rata share of unfunded losses. At December 31, 2003 and June 30, 2003, outstanding borrowings under these agreements totaled \$250,000.

Other Financial Information

Massachusetts Housing Investment Corporation

Other Financial Information

Consolidating Balance Sheet

December 31, 2003

	MHIC	MHEF	Elimination	Consolidated
Assets				
Cash	\$ 1,904,092	\$ 113,904	\$ -	\$ 2,017,996
Money market deposits at member corporations—loan fund	250,000	-	-	250,000
Investment in MHEF Partnerships	2,875,184	-	(2,875,184)	-
Notes receivable—MHEF Partnerships	10,912,502	-	-	10,912,502
Loans to affiliates	2,223,028	-	-	2,223,028
Due to affiliates	525,808	-	-	525,808
Amounts receivable and other assets	332,497	59,729	-	392,226
Due from parent	-	2,704,881	(2,704,881)	-
Furniture, equipment and leasehold improvements, net of accumulated depreciation and amortization of \$1,012,737	162,851	-	-	162,851
Total assets	\$19,185,962	\$2,878,514	\$(5,580,065)	\$16,484,411
Liabilities and net assets				
Liabilities:				
Notes payable to member corporations	\$ 250,000	\$ -	\$ -	\$ 250,000
Due to subsidiary	2,704,881	-	(2,704,881)	-
Unearned fees	11,249,212	-	-	11,249,212
Accrued interest and other liabilities	1,669,345	3,330	-	1,672,675
Total liabilities	15,873,438	3,330	(2,704,881)	13,171,887
Net assets:				
Unrestricted	3,145,411	2,875,184	(2,875,184)	3,145,411
Temporarily restricted	167,113	-	-	167,113
Total net assets	3,312,524	2,875,184	(2,875,184)	3,312,524
Total liabilities and net assets	\$19,185,962	\$2,878,514	\$(5,580,065)	\$16,484,411

See accompanying notes.

Massachusetts Housing Investment Corporation

Other Financial Information

Consolidating Statement of Activities and Changes in Net Assets

For the six-months ended December 31, 2003

	MHIC	MHEF	Elimination	Consolidated
Change in unrestricted net assets:				
Revenues				
Interest revenue:				
Interest on bank deposits	\$ 13,920	\$ 333	\$ -	\$ 14,253
Interest on project loans	25,718	-	-	25,718
Total interest revenue	39,638	333	-	39,971
Loan program fee revenue:				
Management and advisory fees	139,500	-	-	139,500
Portfolio and servicing fees	350,035	-	-	350,035
Financing commitment fees	182,722	-	-	182,722
Origination fees	165,165	-	-	165,165
Available earnings fee	189,119	-	-	189,119
Equity program revenue:				
Fees related to Partnerships	2,284,317	-	-	2,284,317
Other equity program fees	23,046	-	-	23,046
Income from investment in MHEF	(3,422)	-	3,422	-
Total revenues	3,370,120	333	3,422	3,373,875
Expenditures				
Salaries and employee benefits	1,958,177	-	-	1,958,177
Occupancy, equipment and furniture	227,960	-	-	227,960
Professional services	535,409	-	-	535,409
Other expenditures	274,116	3,755	-	277,871
Total expenditures	2,995,662	3,755	-	2,999,417
Increase (decrease) in unrestricted net assets	374,458	(3,422)	3,422	374,458
Net assets at beginning of period	2,938,066	2,878,606	(2,878,606)	2,938,066
Net assets at end of period	\$3,312,524	\$2,875,184	\$(2,875,184)	\$3,312,524

See accompanying notes.