



Financial Statements
December 31, 2018 and 2017
Josephine Commons, LLC

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Independent Auditor's Report

To the Members
Josephine Commons, LLC
Boulder, Colorado

Report on the Financial Statements

We have audited the accompanying financial statements of Josephine Commons, LLC, which comprise the balance sheets as of December 31, 2018 and 2017, and the related statements of operations and members' equity, and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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 of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the 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.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Josephine Commons, LLC as of December 31, 2018 and 2017, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Report on Supplementary Information

Our audits were conducted for the purpose of forming an opinion on the financial statements as a whole. The Schedules of Maintenance and Operating, Utilities, Administrative, Taxes and Insurance, and Interest Expenses are presented for purposes of additional analysis and are not a required part of the 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 financial statements. The information has been subjected to the auditing procedures applied in the audits of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

A handwritten signature in black ink that reads "Eide Bailly LLP". The signature is written in a cursive, flowing style.

Fargo, North Dakota
March 6, 2019

Josephine Commons, LLC

Balance Sheets

December 31, 2018 and 2017

	<u>2018</u>	<u>2017</u>
Assets		
Cash	\$ 613,373	\$ 578,758
Accounts receivable	2,610	2,658
Tenant security deposits	21,676	21,670
Prepaid expenses	37,360	-
Restricted deposits and funded reserves	604,019	622,925
Property and equipment, at cost, less accumulated depreciation	12,695,705	13,156,407
Tax credit fees, at cost, net of accumulated amortization of \$38,148 in 2018 and \$32,125 in 2017	52,202	58,225
	<u>\$ 14,026,945</u>	<u>\$ 14,440,643</u>
Liabilities and Members' Equity		
Liabilities		
Accounts payable	\$ 9,354	\$ 6,763
Due to related party	15,197	11,380
Prepaid rent	3,747	2,529
Accrued expenses	398,951	335,130
Tenant security deposits payable	20,700	21,000
Developer fee payable	-	34,507
Long-term debt, net of unamortized debt issuance costs	4,466,604	4,488,592
	<u>4,914,553</u>	<u>4,899,901</u>
Total liabilities	4,914,553	4,899,901
Members' Equity	<u>9,112,392</u>	<u>9,540,742</u>
	<u>\$ 14,026,945</u>	<u>\$ 14,440,643</u>

Josephine Commons, LLC
Statements of Operations and Members' Equity
Years Ended December 31, 2018 and 2017

	2018	2017	
Operations			
Revenue			
Tenant rent	\$ 621,422	\$ 616,444	
Rental assistance payments	124,255	114,797	
Less vacancies and concessions	(12,479)	(6,493)	
Net rental income	733,198	724,748	
Tenant charges	2,246	1,241	
Interest income	113	86	
Other income	33	458	
Total revenue	735,590	726,533	
Expenses			
Maintenance and operating	194,341	181,323	
Utilities	57,930	58,690	
Administrative	101,705	92,306	
Taxes and insurance	36,118	35,154	
Interest	274,505	275,073	
Depreciation and amortization	467,426	467,273	
Total expenses	1,132,025	1,109,819	
Loss before Company Fees and Gain on Involuntary Conversion of Equipment	(396,435)	(383,286)	
Company Fees			
Asset management fee	6,150	5,970	
Incentive management fee	22,902	-	
Gain on Involuntary Conversion of Equipment	-	(4,308)	
Net Loss	\$ (425,487)	\$ (384,948)	
Members' Equity			
	Managing Member	Investor and Special Members	Total
Balance, December 31, 2016	\$ 86,334	\$ 9,839,356	\$ 9,925,690
Net loss	(35)	(384,913)	(384,948)
Balance, December 31, 2017	86,299	9,454,443	9,540,742
Distributions	-	(2,863)	(2,863)
Net loss	(38)	(425,449)	(425,487)
Balance, December 31, 2018	\$ 86,261	\$ 9,026,131	\$ 9,112,392

Josephine Commons, LLC
Statements of Cash Flows
Years Ended December 31, 2018 and 2017

	2018	2017
Operating Activities		
Net loss	\$ (425,487)	\$ (384,948)
Adjustments to reconcile net loss to net cash from operating activities		
Depreciation	461,402	461,250
Amortization	6,023	6,024
Gain on involuntary conversion of equipment	-	(4,308)
Interest expense attributable to amortization of debt issuance costs	5,302	5,302
Accrued interest - long-term	63,642	65,233
Changes in operating assets and liabilities		
Accounts receivable	48	5,143
Tenant security deposits	(6)	(7)
Prepaid expenses	(37,360)	3,011
Accounts payable	2,591	(2,334)
Prepaid rent	1,218	(396)
Accrued expenses	179	174
Tenant security deposits payable	(300)	(250)
	77,252	153,894
Net Cash from Operating Activities		
Investing Activities		
Net withdrawals from (deposits to) from restricted deposits and funded reserves	18,906	(66,292)
Purchase of property and equipment	(700)	(36,632)
Insurance proceeds received	-	35,198
	18,206	(67,726)
Net Cash from (used for) Investing Activities		
Financing Activities		
Principal payments on long-term debt	(27,290)	(25,451)
Payment on developer fee payable	(34,507)	(136,476)
Advances from (payment to) related party	3,817	(828)
Member distributions	(2,863)	-
	(60,843)	(162,755)
Net Cash used for Financing Activities		
Net Change in Cash	34,615	(76,587)
Cash, Beginning of Year	578,758	655,345
Cash, End of Year	\$ 613,373	\$ 578,758
Supplemental Disclosure of Cash Flow Information		
Cash payments for interest	\$ 205,561	\$ 204,538

Note 1 - Principal Activity and Significant Accounting Policies

Principal Activity, Risks, and Uncertainty

Josephine Commons, LLC (Company) was formed May 5, 2011, as a limited liability company under the laws of the State of Colorado and shall continue in perpetual existence, unless dissolved or terminated at an earlier date. The Company was formed for the purpose to acquire, own, develop, construct and lease, manage and operate a building in Lafayette, Colorado consisting of 74 units of affordable rental housing for low-income and elderly residents. The project began operations in September 2012. Substantially all of the Company's income is derived from the rental of its apartment units.

The project has qualified and been allocated low-income housing tax credits pursuant to the Internal Revenue Code Section 42, which regulates the use of the complex as to occupant eligibility and unit gross rent, among other requirements. The project must meet the provisions of these regulations during each of 15 consecutive years in order to continue to qualify to receive the tax credits. Failure to comply with occupant eligibility and/or unit gross rent or to correct noncompliance within a specified time period could result in recapture of the previously taken low-income housing tax credits plus interest. Such potential noncompliance may require an adjustment to the contributed capital by the investor member. All residential units within this project are subject to the contract restrictions regarding rental charges and other operating policies under the Low-Income Housing Tax Credit Program.

Concentrations of Credit Risk

The Company maintains its cash accounts in various deposit accounts, the balances of which are periodically in excess of federally insured limits.

Property and Equipment

Property and equipment is recorded at cost. Expenditures for renewals and improvements that significantly add to the productive capacity or extend the useful life of an asset are capitalized. Expenditures for maintenance and repairs are charged to expense. When equipment is retired or sold, the cost and related accumulated depreciation are eliminated from the accounts and the resultant gain or loss is reflected in income.

Depreciation is computed principally by the straight-line method over the following estimated useful lives:

Land improvements	20 years
Buildings and improvements	40 years
Equipment and furnishings	10 years

The Company reviews the carrying value of property and equipment for impairment whenever events and circumstances indicate that the carrying value of an asset may not be recoverable from the estimated future cash flows expected to result from its use and eventual disposition. In cases where undiscounted expected future cash flows are less than the carrying value, an impairment loss is recognized equal to an amount by which the carrying value exceeds the fair value of assets. The factors considered by management in performing this assessment include current operating results, trends and prospects, the manner in which the property is used, and the effects of obsolescence, demand, competition, and other economic factors. Based on this assessment there was no impairment at December 31, 2018 and 2017.

Tax Credit Fees

Tax credit fees are being amortized over a 15-year life using the straight-line method of amortization. Amortization expense for each of the next 5 years will be approximately \$6,020.

Debt Issuance Costs

Debt issuance costs are amortized over the period the related obligation is outstanding using the straight-line method, which is a reasonable estimate of the effective interest method. Debt issuance costs are included within long-term debt on the balance sheet. Amortization of debt issuance costs is included in interest expense in the accompanying financial statements.

Income Taxes

As a limited liability company, the Company's taxable income or loss is allocated to members in accordance with the operating agreement. Therefore, no provision for income taxes has been included in the financial statements.

The Company evaluates its tax positions that have been taken or are expected to be taken on income tax returns to determine if an accrual is necessary for uncertain tax positions. As of December 31, 2018 and 2017, the unrecognized tax benefit accrual was zero. The Company will recognize future accrued interest and penalties related to unrecognized tax benefits in income tax expense if incurred.

Rental Income

Housing units are rented under operating lease agreements with terms of one year or less. Rent income from tenants and rental assistance payments is recognized in the month in which it is earned rather than received. Any rent received prior to the month of occupancy is reported as prepaid rent. Tenant rent represents gross rent for all units in the project. Vacancy loss is recorded for any unrented units and concessions are recorded for discounts to units to arrive at net tenant rent.

Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

Subsequent Events

The Company has evaluated subsequent events through March 6, 2019, the date which the financial statements were available to be issued.

Note 2 - Restricted Deposits and Funded Reserves

	2018	2017
Replacement reserve	\$ 275,042	\$ 245,550
Insurance reserve	32,593	80,991
Operating reserve	296,384	296,384
	\$ 604,019	\$ 622,925

Replacement Reserve

Pursuant to the operating agreement, the Company is to establish a replacement reserve to provide for working capital needs, improvements and replacements relating to the project, commencing upon final closing. The Company is to deposit \$300 per unit, per year, increasing at a rate of three percent each year.

Replacement reserve activity for the years ended December 31, 2018 and 2017, is as follows:

	2018	2017
Balance, January 1	\$ 245,550	\$ 219,754
Deposits	31,612	25,737
Withdrawals	(2,188)	-
Bank fees	(27)	(20)
Interest	95	79
Balance, December 31	\$ 275,042	\$ 245,550

Insurance Reserve

The Company has established and maintains a reserve with the mortgage company, used to pay insurance expenses. The account is to receive monthly deposits equal to one-twelfth of the annual payment, which is paid annually from the account.

Operating Reserve

Pursuant to the operating agreement, the Company is to establish and maintain an operating reserve to meet operating expenses and debt service of the Company which exceed operating revenues. The reserve is to be funded in the amount of \$288,984. The managing member may make withdrawals subject to the special member's approval.

Note 3 - Property and Equipment

Property and equipment at December 31, 2018 and 2017 consist of the following:

	2018	2017
Land and improvements	\$ 1,620,859	\$ 1,620,859
Buildings and improvements	13,527,192	13,527,192
Equipment and furnishings	465,050	465,050
Construction in progress	700	-
	15,613,801	15,613,101
Accumulated depreciation	(2,918,096)	(2,456,694)
	\$ 12,695,705	\$ 13,156,407

Construction in progress consists of costs incurred in relation to design work for a future deck remodel, of which the total expected cost is currently unknown.

Note 4 - Accrued Expenses

Accrued expenses at December 31, 2018 and 2017 consist of the following:

	2018	2017
Interest (Note 5)	\$ 392,802	\$ 329,160
Asset management fees (Note 7)	6,149	5,970
	\$ 398,951	\$ 335,130

Note 5 - Long-Term Debt

Long-term debt as of December 31, 2018 and 2017 consists of:

	2018	2017
7.0% mortgage note payable to Berkadia Commercial Mortgage, Inc. due in monthly principal and interest payments of \$19,166 through November 2029, secured by a deed of trust and assignment of rents	\$ 2,880,748	\$ 2,908,038
Unamortized debt issuance costs, based on effective interest rate of 7.35%	(57,437)	(62,739)
	2,823,311	2,845,299

Josephine Commons, LLC
Notes to Financial Statements
December 31, 2018 and 2017

	2018	2017
4.3% mortgage note payable to Boulder County Housing Authority (BCHA), payments due from cash flow, remaining principal and interest due August 2061, secured by a second mortgage	\$ 550,000	\$ 550,000
4.3% mortgage note payable to BCHA, payments due from cash flow, remaining principal and interest due August 2061, secured by a third mortgage	250,000	250,000
4.3% mortgage note payable to BCHA, entire principal balance will be forgiven after a term of 99 years unless canceled earlier, secured by a fourth mortgage	200,000	200,000
4.3% mortgage note payable to BCHA, entire principal balance will be forgiven after a term of 99 years unless canceled earlier, secured by a fifth mortgage	200,000	200,000
0.50% note payable to BCHA, due from cash flow, remaining principal and interest due August 2061, unsecured	443,293	443,293
Total notes payable to BCHA due from cash flow	1,643,293	1,643,293
Total long-term debt, net of unamortized debt issuance costs	\$ 4,466,604	\$ 4,488,592

Future maturities of long-term debt are as follows:

Year Ended December 31,	Amount
2019	\$ 29,434
2020	31,561
2021	33,843
2022	36,289
2023	38,913
Thereafter	4,354,001
Unamortized debt issuance costs	(57,437)
	\$ 4,466,604

A summary of accrued interest as of December 31, 2018 and 2017 is as follows:

	2018	2017
Berkadia Commercial Mortgage, Inc.	\$ 16,804	\$ 16,964
BCHA 4.3% (HOME)	172,754	141,091
BCHA 4.3% loan (AHP)	73,595	62,998
BCHA 4.3% loan (Worthycause I)	57,711	48,078
BCHA 4.3% (Worthycause II)	57,711	48,078
BCHA 0.5% loan	14,227	11,951
	375,998	312,196
	\$ 392,802	\$ 329,160

Note 6 - Property Taxes

The Company is exempt from property taxes under C.R.S 29-4-507 through Josephine Commons Manager, LLC. Currently there is no expiration date on the property tax exemption for so long as Josephine Commons Manager, LLC owns interest in the Company.

Note 7 - Related Party Transactions

Developer Fees

The Company has entered into a development agreement with Boulder County Housing Authority (BCHA), the sole member of the managing member, for the services provided in connection with the development and construction of the project. Developer fees of \$1,351,067 have been capitalized as part of the building. During 2018 and 2017, the Company paid developer fees of \$34,507 and \$136,476, respectively, to BCHA. As of December 31, 2018 and 2017, the Company owes BCHA \$0 and \$34,507, respectively, for developer fees.

Mortgage Notes Payable

The Company has entered into multiple loan agreements with BCHA (Note 5). During 2018 and 2017, the Company incurred interest expense of \$66,664 and \$65,381, respectively in relation to these mortgage notes payable. As of December 31, 2018 and 2017, the Company owes BCHA \$375,998 and \$312,196, respectively for accrued interest (Note 5).

Due to Related Party

As of December 31, 2018 and 2017, the Company owed BCHA \$15,197 and \$11,380, respectively, for costs related to operations.

Management Fees

The Company has entered into a management agreement with BCHA, to provide management services for the project. Under the terms of the agreement, the Company is to pay management fees equal to the lesser of \$466 per unit or 5.5% of effective gross income. During 2018 and 2017, the Company incurred management fees of \$34,484.

Reimbursement of Expenses

During 2018 and 2017, the Company reimbursed BCHA approximately \$153,000 and \$136,100, respectively, for payroll and other expenses.

Asset Management Fee

Pursuant to the operating agreement, the Company is to pay Red Stone Equity Manager, LLC, the special member, a cumulative fee equal to \$5,000 annually, commencing in 2012, for the review of the operations of the Company. The fee is to increase by 3% annually. During 2018 and 2017, the Company incurred \$6,150 and \$5,970, respectively, for asset management fees. As of December 31, 2018 and 2017, the Company owed the special member \$6,149 and \$5,970, respectively, for these fees.

Incentive Management Fee

Pursuant to the operating agreement, the Company is to pay the managing member for their services in managing the business of the Company, a non-cumulative fee equal to 80% of cash flow remaining after other required payments. At no time is the fee to exceed 10% of gross revenues in any year. During 2018 and 2017, the Company paid \$22,902 and \$0, respectively.

Distributions

During 2018 and 2017, the Company paid distributions to the investor member in the amount of \$2,863 and \$0, respectively. Distributions are paid based on available cash flow, as outlined in the operating agreement.

Operating Deficit Guaranty

Pursuant to the operating agreement, the managing manager is required to fund operating deficits during the period beginning upon the date that stabilized operations is achieved and for five years thereafter as defined in the agreement. The managing manager shall be obligated to provide funds in the form of a loan, not to exceed \$350,000, shall bear no interest and shall be repayable solely from net cash flow as allowed in the operating agreement.

Note 8 - Members' Equity

<u>Members</u>	<u>Ownership Percentages</u>
Managing Josephine Commons Manager, LLC	0.009%
Investor Red Stone Josephine, LLC	99.990%
Special Red Stone Equity Manager 2, LLC	<u>0.001%</u>
	<u><u>100.000%</u></u>

Profit or loss will be allocated as allocated in the partnership agreement.

The partners have certain rights and obligations as outlined in the partnership agreement.



Supplementary Information
December 31, 2018 and 2017

Josephine Commons, LLC

Josephine Commons, LLC

Schedules of Maintenance and Operating, Utilities, Administrative, Taxes and Insurance, and Interest Expenses
Years Ended December 31, 2018 and 2017

	<u>2018</u>	<u>2017</u>
Maintenance and Operating		
Reimbursed salaries and benefits	\$ 80,939	\$ 90,870
Contracted services	59,450	46,745
Grounds	27,312	11,010
Supplies	15,192	11,029
Trash removal	11,448	8,883
Other maintenance and operating	-	12,786
	<u>\$ 194,341</u>	<u>\$ 181,323</u>
Utilities		
Electricity	\$ 28,715	\$ 28,606
Water and sewer	27,916	28,950
Other utilities	1,299	1,134
	<u>\$ 57,930</u>	<u>\$ 58,690</u>
Administrative		
Reimbursed salaries and benefits	\$ 49,800	\$ 39,553
Management fees	34,484	34,484
Audit and accounting	6,470	6,291
Telephone	10,744	10,434
Legal and compliance fees	10	10
Other administrative	197	1,534
	<u>\$ 101,705</u>	<u>\$ 92,306</u>
Taxes and Insurance		
Insurance	\$ 36,091	\$ 35,134
Other taxes, licenses, and permits	27	20
	<u>\$ 36,118</u>	<u>\$ 35,154</u>
Interest		
Berkadia Commercial Mortgage Inc.	\$ 207,841	\$ 209,692
BCHA	66,664	65,381
	<u>\$ 274,505</u>	<u>\$ 275,073</u>