

***CAPITOL HILL HOUSING
IMPROVEMENT PROGRAM***

Financial Statements With
Independent Auditors' Report

For The Year Ended
December 31, 2006

Table Of Contents

	<i>Page</i>
Independent Auditors' Report	1
Management Discussion and Analysis	2 - 5
Financial Statements:	
Balance Sheet	6
Statement Of Revenues, Expenses and Changes in Net Assets	7
Statement Of Cash Flows	8 - 9
Notes To Financial Statements	10 - 29
Supplemental Information:	
Schedule Of Departmental Operations	30
Schedule Of Property Operations	31 – 33

Independent Auditors' Report

*Board of Directors
Capitol Hill Housing Improvement Program
Seattle, Washington*

We have audited the accompanying financial statements of the business-type activities and the aggregate discretely presented component units of Capitol Hill Housing Improvement Program ("CHHIP") as of and for the year ended December 31, 2006, as listed in the table of contents. These financial statements are the responsibility of CHHIP's management. Our responsibility is to express an opinion on these financial statements based on our audits. We did not audit the financial statements of the tax credit limited partnerships and LLCs identified in Note 6, except for Larned Apartments Limited Partnership, which represent all of the assets, net assets, and revenues of the aggregate discretely presented component units of CHHIP. Those financial statements were audited by other auditors whose reports have been furnished to us, and our opinion, insofar as it relates to the amounts included for the aggregate discretely presented component units, is based solely on the reports of the other auditors.

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 includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, based on our audit and the reports of other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities and the aggregate discretely presented component units of CHHIP, as of December 31, 2006, and the respective changes in financial position and cash flows thereof for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 12 to the financial statements, CHHIP changed its accounting and reporting for component units in 2006.

The management's discussion and analysis on pages 2 through 5 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was made for the purpose of forming an opinion on the financial statements of CHHIP taken as a whole. The supplemental information on pages 30 to 33 is presented for additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audits of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Clark Nuber P.S.

Certified Public Accountants
May 23, 2007

CAPITOL HILL HOUSING IMPROVEMENT PROGRAM

Management Discussion And Analysis For The Year Ended December 31, 2006

As management of Capitol Hill Housing Improvement Program (“CHHIP”), we offer readers of the CHHIP financial statements this narrative overview and analysis of the financial activities of CHHIP for the year ended December 31, 2006.

FINANCIAL HIGHLIGHTS

- Assets exceeded liabilities (net assets) at the close of 2006 by nearly \$5 million.
- Cash and cash equivalents at December 31, 2006 increased over the previous year by \$261,628.
- Significant development accomplishments during 2006 included:
 - Rent up of Pantages Apartments after completion of construction in late 2005
 - Completion and sale of the commercial portion of the Broadway & Pine Mixed Use Project while the residential portion neared completion
 - Rehabilitation of Silvan Apartments with tenants in place.
 - Purchase of land and beginning of permit and design process for Woodland Park Project
- CHHIP’s debt increased due to the beginning of the Woodland Park Project.
- CHHIP received \$370,492 in general contributions and grants and \$148,500 in grants for property development during 2006.

OVERVIEW OF THE FINANCIAL STATEMENTS

CHHIP’s financial statements consist of three parts - management’s discussion and analysis (this section), financial statements required by Governmental Accounting Standards Board (GASB), and supplemental schedules.

CHHIP financial statements provide information about CHHIP’s overall financial position and results of operations. The financial statements report information about CHHIP as a whole using accounting methods similar to those used by private sector companies. These statements, which are presented on the accrual basis, consist of the Balance Sheet, Statement of Revenues, Expenses and Changes in Net Assets, and the Statement of Cash Flows. The Balance Sheet includes all of CHHIP’s assets and liabilities. All of the current year’s revenues and expenses are accounted for in the Statement of Revenues, Expenses and Changes in Net Assets regardless of when cash is received or paid.

The financial statements include not only the activities of CHHIP but also 12 legally separate tax credit partnerships for which CHHIP is financially accountable as the sole general partner or managing member and three related non-profit entities. Financial information for the tax credit partnerships is reported separately from the financial information presented for CHHIP. Included this year as part of CHHIP are three nonprofits, Elizabeth James Senior Housing, Central City Affordable Housing and CH Development Association. Although legally separate, they were formed to further the mission of CHHIP. Since CHHIP board members comprise all or a majority of the nonprofit boards’ members, they are considered instrumentalities of CHHIP and are included in CHHIP’s financial statements. The inclusion of the affiliate financial statements and the inclusion of the nonprofits in the CHHIP financial statements is a change in accounting presentation effective for 2006.

CAPITOL HILL HOUSING IMPROVEMENT PROGRAM

Management Discussion And Analysis For The Year Ended December 31, 2006

The financial statements also include a "Notes to Financial Statements" section that provides additional information that is essential to a full understanding of the data provided in the financial statements.

The supplemental schedule provides a breakdown of CHHIP property operations from program management and administration. Audited financial statements are available for eleven of the twelve component units and may be requested from CHHIP.

Consistent with the note on presentation format above, please note the following when comparing 2005 and 2006. Near year end 2005 CHHIP transferred one building from CHHIP ownership to an affiliate consistent with its development plan and financing strategy. One building developed through an affiliate began operations in 2006.

OVERVIEW OF THE CHHIP-WIDE FINANCIAL POSITION AND OPERATIONS

	<i>December 31,</i>	<u>2006</u>	<u>2005</u>
Current assets		\$ 1,797,770	\$ 1,868,470
Non-current assets:			
Capital assets, net		32,795,716	33,012,675
Other		<u>8,176,485</u>	<u>7,403,807</u>
Total Assets		<u>\$ 42,769,971</u>	<u>\$ 42,284,952</u>
Current liabilities		\$ 1,284,416	\$ 1,080,618
Non-current liabilities		<u>36,498,174</u>	<u>36,397,665</u>
Total Liabilities		<u>\$ 37,782,590</u>	<u>\$ 37,478,283</u>
Net assets:			
Invested in capital assets, net of related debt		\$ (1,278,638)	\$ (804,988)
Restricted		3,891,940	2,647,029
Unrestricted		<u>2,374,079</u>	<u>2,964,628</u>
Total Net Assets		<u>\$ 4,987,381</u>	<u>\$ 4,806,669</u>

The assets of CHHIP consist primarily of capital assets, its buildings and building improvements. This is consistent with CHHIP's mission to develop and operate affordable housing for low income residents on Capitol Hill and other Seattle neighborhoods. Capital assets are shown net of depreciation. Other assets include cash reserves for repairs and replacements and debt service as required by our lenders.

The liabilities are predominantly long term debt that was used to purchase, develop and rehabilitate our apartment buildings. Many of these loans, provided by governmental entities, have below market interest rates and do not require annual debt service. See Note 5 for a more complete discussion.

CAPITOL HILL HOUSING IMPROVEMENT PROGRAM

Management Discussion And Analysis For The Year Ended December 31, 2006

The difference between total assets and total liabilities, net assets, is one indicator of financial health. Net assets increased by \$180,712 during 2006, an increase of 3.8%.

The results of operations for CHHIP are presented below:

	<i>For the Year Ended December 31,</i>	<u>2006</u>	<u>2005</u>
Operating Revenues:			
Tenant revenues	\$	3,634,501	\$ 3,827,005
Fees for service		667,494	390,274
Contributions and grants		370,492	368,181
Project development fees		875,497	702,651
Other		353,471	478,960
Nonoperating Revenues:			
Interest income		166,285	119,804
Grants for developing property		148,500	
Other			209,019
		<hr/>	<hr/>
Total Revenues		6,216,240	6,095,894
Operating Expenses:			
Salaries, benefits, and payroll taxes		2,429,629	2,236,532
Repairs and maintenance		505,814	567,442
Other operating expenses		1,267,207	1,405,309
Depreciation and amortization		913,503	996,111
Nonoperating Expenses:			
Interest expense		919,375	1,273,341
		<hr/>	<hr/>
Total Expenses		6,035,528	6,478,735
		<hr/>	<hr/>
Change in Net Assets	\$	180,712	\$ (382,841)
		<hr/> <hr/>	<hr/> <hr/>

Results of Operations - Operating revenues are generated principally from rental income and HUD subsidies of rental income, as well as property management and other fees paid by affiliates or component units. CHHIP earns development fees for its management role in the development of new properties. Operating expenses, as they relate to operating revenues, have continued to decline as a percentage of operating revenue from 2002 through 2006.

Interest expense, primarily from the long term financing of the properties, continues to be a significant expense. Typically each property acquired has both amortizing and non-amortizing debt from commercial and governmental sources, respectively. A portion of the interest expense, under the terms of the financing, is deferred and will eventually be forgiven as long as the properties are managed in compliance with the loan agreements.

CAPITOL HILL HOUSING IMPROVEMENT PROGRAM

Management Discussion And Analysis For The Year Ended December 31, 2006

Grants for developing property are inherently less predictable and can cause revenues to vary substantially from year to year. Other revenues such as the sale of transferable development rights are infrequent and do not regularly occur.

Supplemental Schedule - The supplemental Schedule of Departmental Operations provides additional insight into the financial operations of CHHIP. CHHIP budgets and manages financial performance based on its lines of business including its buildings (Property Operations) and organizational and off site activities (Program Management and Administration). Taken together operating revenues exceeded operating expenses by \$627,504.

Property Operations, which includes all building based revenues and expense, shows expenses plus scheduled reserve deposits exceeded revenues by \$258,034. Vacancies and repairs and maintenance were higher than budgeted across the portfolio. During the second half of 2006 the Property Management department was reorganized and vacancies decreased. As the buildings age, repair and maintenance expenses continue to increase. Higher vacancies also meant more maintenance and repairs as units turned over. CHHIP has included in the 2007 budget an Asset Manager position to specifically address the capital needs of its diverse portfolio over the long term.

Non-property operations did better than projected. Salaries and related expenses grew due to growth and general cost increases while other expenses declined leaving overall non-property expenses stable. Revenues from property management fees increased with the growth in units under management and due to increasing the maintenance services staff which in turn increased revenues. Development fees, from the development of new projects, were higher in both 2006 and 2005 than a typical year. Partnership income included a final distribution from an unaffiliated limited partnership that was not budgeted and will not recur.

ECONOMIC FACTORS AFFECTING CHHIP'S FUTURE

CHHIP is at risk from political and governmental decisions beyond its control such as changes to the federal and local rental subsidy programs or changes in priorities for capital subsidies to develop new properties. Inflation may cause overall operating expenses to increase faster than it is desirable to raise rents for existing unit occupants which may generate higher turnover or vacancy. Certain operating expenses such as insurance or utilities may increase due to external events outside of the control of CHHIP. The local economy continues to grow and the region continues to experience in migration which means continued demand for affordable housing. The strong economy also creates an extremely competitive market rate real estate market which means fewer or more expensive opportunities for developers of affordable housing. Loss of development fee revenue would adversely affect CHHIP's operating budget.

CONTACTING CHHIP'S FINANCIAL MANAGEMENT

The financial report is designed to provide a general overview of CHHIP's finances for all those with an interest. Questions concerning any of the information provided in this report or requests for additional information should be addressed to Executive Director, Capitol Hill Housing Improvement Program, 1406 10th Avenue, Seattle, WA 98122.

CAPITOL HILL HOUSING IMPROVEMENT PROGRAM

Balance Sheet
December 31, 2006

	<u>CHHIP</u>	<u>Discrete Component Units</u>
Assets		
Current Assets:		
Cash and cash equivalents	\$ 566,228	\$ 697,190
Accounts receivables, net	1,109,702	73,949
Prepaid expenses and other current assets	98,220	806
Current portion of lease receivable	23,620	
Total Current Assets	1,797,770	771,945
Restricted cash and cash equivalents	3,891,940	3,022,331
Lease receivable, net of current portion	977,073	
Notes and interest receivable	2,948,820	
Land, buildings, and equipment, net	32,795,716	48,344,159
Investment in limited partnerships and LLCs	282,562	
Unamortized financing costs, net	76,090	828,653
Total Assets	\$ 42,769,971	\$ 52,967,088
Liabilities And Net Assets		
Current Liabilities:		
Accounts payable and accrued liabilities	\$ 484,501	\$ 1,087,015
Construction payables		653,690
Security deposits	115,398	96,456
Current portion of notes payable	684,517	4,472,665
Total Current Liabilities	1,284,416	6,309,826
Notes payable, net of current portion	34,391,807	35,661,271
Accrued interest payable	2,106,367	806,891
Total Liabilities	37,782,590	42,777,988
Net Assets:		
Restricted for building improvements	3,777,875	1,380,712
Restricted for other purposes	114,065	1,641,619
Total restricted	3,891,940	3,022,331
Invested in capital assets, net of related debt	(1,278,638)	8,210,223
Unrestricted	2,374,079	(1,043,454)
Total Net Assets	4,987,381	10,189,100
Total Liabilities and Net Assets	\$ 42,769,971	\$ 52,967,088

The accompanying notes are an integral part of the financial statements

CAPITOL HILL HOUSING IMPROVEMENT PROGRAM

**Statement Of Revenues, Expenses, And Changes In Net Assets
For The Year Ended December 31, 2006**

	<u>CHHIP</u>	<u>Discrete Component Units</u>
Operating Revenues:		
Gross rent potential	\$ 3,771,078	\$ 3,272,611
Vacancy loss	(263,065)	(178,474)
Laundry, parking, and other tenant income	126,488	106,166
Fees for services	667,494	
Contributions and grants	370,492	31,556
Project development fees	875,497	
Partnership income	353,471	
	<u>5,901,455</u>	<u>3,231,859</u>
Operating Expenses:		
Salaries, benefits, and payroll taxes	2,429,629	545,120
Utilities	469,093	309,103
Professional fees	126,084	87,586
Administrative	323,085	385,332
Taxes and Insurance	221,077	229,554
Repairs and maintenance	505,814	396,076
Bad debt expense	98,811	40,265
Other	29,057	5,496
Depreciation and amortization	913,503	1,548,423
	<u>5,116,153</u>	<u>3,546,955</u>
Operating Income (Loss)	785,302	(315,096)
Nonoperating Revenues (Expenses):		
Interest income	166,285	20,867
Grants for developing property	148,500	
Gain on sale of asset		3,106
Interest expense	(919,375)	(1,123,058)
	<u>(604,590)</u>	<u>(1,099,085)</u>
Total Nonoperating Revenues (Expenses)	(604,590)	(1,099,085)
Change in Net Assets	180,712	(1,414,181)
Net Assets:		
Beginning of year	4,806,669	5,625,990
Capital contributions		5,977,291
	<u>4,806,669</u>	<u>5,625,990</u>
End of Year	\$ 4,987,381	\$ 10,189,100

The accompanying notes are an integral part of the financial statements

CAPITOL HILL HOUSING IMPROVEMENT PROGRAM

Statement Of Cash Flows

For The Year Ended December 31, 2006

	<u>CHHIP</u>	<u>Discrete Component Units</u>
Cash Flows from Operating Activities:		
Receipts from tenants, customers, contributors, and for operating subsidies	\$ 6,186,587	\$ 3,254,298
Payments to employees and for payroll taxes and benefits	(2,387,793)	(761,567)
Payments to suppliers	(1,626,225)	(922,994)
Net Cash Provided by Operating Activities	2,172,569	1,569,737
Cash Flows from Capital and Related Financing Activities:		
Acquisition of land, building, and equipment	(696,544)	(13,525,781)
Proceeds from sale of asset		3,752,903
Grants for developing property	148,500	
Proceeds from notes payable	594,989	11,881,039
Principal payments on notes payable	(538,991)	(8,115,520)
Interest paid on notes payable	(761,506)	(1,006,538)
Financing costs paid		(166,665)
Proceeds from lease receivable	22,266	
Net issuance and repayment of notes receivable	1,456	
Capital contributions		5,977,291
Net Cash Used by Capital and Related Financing Activities	(1,229,830)	(1,203,271)
Cash Flows from Investing Activities:		
Net change in restricted cash	(708,703)	(1,070,017)
Interest receipts	123,592	20,867
Investment in LLCs	(96,000)	
Net Cash Used by Investing Activities	(681,111)	(1,049,150)
Net Change in Cash and Cash Equivalents	261,628	(682,684)
Cash and Cash Equivalents:		
Beginning of year	304,600	1,379,874
End of Year	\$ 566,228	\$ 697,190

- Continued -

The accompanying notes are an integral part of the financial statements

CAPITOL HILL HOUSING IMPROVEMENT PROGRAM

Statement Of Cash Flows

For The Year Ended December 31, 2006

	<u>CHHIP</u>	<u>Discrete Component Units</u>
Reconciliation of Operating Income (Loss) to Net Cash Provided by Operating Activities		
Operating income (loss)	\$ 785,302	\$ (315,096)
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation and amortization	913,503	1,548,423
Changes in assets and liabilities:		
Accounts receivables	371,402	4,519
Notes receivable for developer fees	46,863	
Other assets	(34,941)	(3,697)
Accounts payable and accrued liabilities	94,862	317,668
Security deposits	(4,422)	17,920
Net Cash Provided by Operating Activities	<u>\$ 2,172,569</u>	<u>\$ 1,569,737</u>

The accompanying notes are an integral part of the financial statements

CAPITOL HILL HOUSING IMPROVEMENT PROGRAM

Notes To Financial Statements For The Year Ended December 31, 2006

Note 1 - Nature Of Operations And Summary Of Significant Accounting Policies

Organization - Capitol Hill Housing Improvement Program ("CHHIP") is a public corporation chartered in 1975 under Washington State and municipal law as a public development authority. CHHIP has broad powers to assist residents and property owners in preserving and improving housing and the neighborhood and to undertake activities in support of those goals.

These financial statements include the accounts of CHHIP and CHHIP's blended component units, CH Development Association, Elizabeth James Senior Housing, Central City Affordable Housing, and Woodland Park Avenue Apartments LLC. CH Development Association, Elizabeth James Senior Housing and Central City Affordable Housing are non-profit corporations that CHHIP controls through assignment of the board of directors of these non-profit corporations. Woodland Park Avenue Apartments LLC is wholly-owned by CHHIP. All inter-organization balances and transactions have been eliminated for presentation in CHHIP's financial statements.

Discrete Component Units – CHHIP serves as the general partner or managing member in several limited partnerships and LLCs (see Note 6). These limited partnerships and LLCs constitute discrete component units of CHHIP as defined by GASB Statement 14, *The Financial Reporting Entity*, because they are separate legal entities and subject to CHHIP's will. As general partner or managing member, CHHIP is financially accountable for and oversees the day-to-day operation of these properties. The data for these limited partnerships and LLCs is combined and discretely presented in a separate column on the face of CHHIP's financial statements. Each limited partnership and LLC, except for Larned Apartments Limited Partnership, is audited separately. Copies of these financial statements can be obtained by contacting CHHIP.

Basis of Accounting - The financial statements of CHHIP have been prepared in conformity with accounting principles generally accepted in the United States of America as applied to governmental units. These financials have been prepared using the economic resources measurement focus and the accrual basis of accounting. The Governmental Accounting Standards Board ("GASB") is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. CHHIP, in accordance with GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, elected not to apply all statements of the Financial Accounting Standards Board ("FASB") issued subsequent to November 30, 1989.

Cash and Cash Equivalents - CHHIP considers all highly liquid temporary investments purchased with a maturity of three months or less at the acquisition date to be cash equivalents. Portions of CHHIP's cash and cash equivalents are restricted by lenders or governmental agencies for specific uses.

CHHIP's deposits and certificates of deposit are entirely covered by federal depository insurance (FDIC) or by collateral held in a multiple financial institution collateral pool administered by the Washington Public Deposit Protection Commission. The FDIC insures the first \$100,000 of CHHIP's deposits at each financial institution. Deposit balances over \$100,000 are insured by the collateral pool. As of December 31, 2006, the carrying amount of CHHIP's demand deposits was \$2,139,091 and was not materially different from the bank balances. At December 31, 2006 CHHIP had \$2,319,077 in Washington State's Local Government Investment Pool (LGIP). The amounts invested in the pool represent the fair value equal to the value of the pool shares.

CAPITOL HILL HOUSING IMPROVEMENT PROGRAM

Notes To Financial Statements For The Year Ended December 31, 2006

Note 1 - Continued

The LGIP is operated in a manner consistent with Rule 2a-7 money market funds, as recognized by the Securities and Exchange Commission. Rule 2a-7 funds are limited to high quality obligations with limited maximum and average maturities in order to minimize both market and credit risk. The LGIP is audited annually by the Office of the State Auditor and by an outside independent auditor. Financial reports are available at the State Treasures Office.

Certain cash balances are restricted for building improvements and other specific uses in accordance with debt and other agreements.

Accounts Receivable - Accounts receivable consist primarily of rents due from tenants, grants due from grantors, and amounts due from the limited partnerships and LLCs described in Note 6. Annually, tenant receivables are analyzed and the allowance for doubtful accounts is adjusted. Other receivable allowances are established for uncertain collectibles.

Notes Receivable and Notes Payable - Many of the notes carry below market interest rates and/or contain provisions for deferral or forgiveness of interest or principal. Such notes and related interest amounts are recorded in the financial statements according to the terms of the notes. No adjustment to market rates has been made due to the interest rates being set by governmental entities and the compliance requirements that must be met for forgiveness or deferral to occur. Forgiveness of debt and related accrued interest for notes payable will be recorded as income when all terms of the agreement have been completed.

Land, Buildings and Equipment - CHHIP capitalizes assets with a cost greater than \$1,000 and an estimated useful life of one or more years. Land, buildings, and equipment are recorded at cost or estimated fair market value at the date of donation. Depreciation of buildings and equipment is recorded on a straight-line basis over their estimated useful lives of five to 40 years.

Investment in Limited Partnerships - CHHIP is the sole general partner and owns 1% or less interest in nine limited partnerships and is the managing member and owns .01% in four limited liability companies as of December 31, 2006. CHHIP records its investment in these partnerships using the equity method of accounting as it is the general partner or managing member and possesses significant influence in the operating and financial policies of the investees.

Revenue Recognition - Gross rent potential reflects gross rental revenue at 100% occupancy. CHHIP deducts vacancy loss from gross rent potential to reflect actual occupancy. Rental revenue is recognized monthly as earned. Development fee revenue is recognized over the development period using the percentage-of-completion method.

CAPITOL HILL HOUSING IMPROVEMENT PROGRAM

Notes To Financial Statements For The Year Ended December 31, 2006

Note 1 - Continued

Operating Revenues and Expenses - Operating revenues include fees and charges from providing services in connection with the operations and development of providing low-income housing. Operating revenues also include operating subsidies and grants provided by the U.S. Department of Housing and Urban Development ("HUD"). Operating expenses are those expenses that are directly incurred while in the operation of providing low-income housing. All other revenues and expenses are considered non-operating.

Restricted Net Assets – Net assets have been reported as restricted for building improvements and other purposes due to constraints that are either externally imposed by creditors, grantors, contributors, or laws or regulations of other governments, or imposed by law through constitutional provisions or enabling legislation. CHHIP's policy is to first apply restricted resources when an expense is incurred for purposes for which both restricted and unrestricted net assets are available.

Federal Income Tax - CHHIP has been notified by the Internal Revenue Service that it is exempt from federal income taxes as an entity described in Section 115 of the Internal Revenue Code. CH Development Association, Elizabeth James Senior Housing, and Central City Affordable Housing have been notified by the Internal Revenue Service that they are exempt from federal income taxes as an entity described in Section 501(c)(3) of the Internal Revenue Code. Woodland Park Avenue Apartments LLC has no provision or benefit for income taxes included in these financial statements since taxable income or loss passes through to, and is reportable by, each member individually.

Concentrations of Credit Risk - All of CHHIP's properties are located in Seattle, Washington (the "City"). As such, CHHIP's operations are directly linked to the economic conditions in the City.

Use of Estimates - The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions. These affect the reported amounts of assets, liabilities, revenues, and expenses, as well as the disclosure of contingent assets and liabilities. Actual results could differ from these estimates.

CAPITOL HILL HOUSING IMPROVEMENT PROGRAM

Notes To Financial Statements For The Year Ended December 31, 2006

Note 2 - Notes And Interest Receivable

Notes and interest receivable consisted of the following amounts due primarily from affiliated limited partnerships and LLCs (Note 6) as of December 31, 2006:

1214 Boylston Avenue Limited Partnership:

Developer fee note, interest at 7%, principal and accrued interest due at maturity on May 1, 2012 \$ 180,023

Broadway & Pine LLC:

Note receivable, interest at 5%, annual payments from cash flow starting June 2007 through maturity on June 1, 2057 180,000

Byron/Wetmore Limited Partnership:

Note receivable, interest at 5%, monthly payments of \$72 until maturity, which occurs upon sale of the property or dissolution of the partnership 10,000

Note receivable, interest at 6.25%, monthly payments of \$265 until maturity in December 2008 3,957

Firestation Seven Associates:

Note receivable from unrelated organization, interest at 9%, monthly payments of \$306 until maturity in September 2017 24,135

Fleming Apartments Limited Partnership:

Note receivable, interest at 1%, payments from operating income, principal and accrued interest due at maturity on December 31, 2049 436,170

Developer fee note receivable, interest at 4.67%, payments from operating income, principal and accrued interest due at maturity on June 1, 2014 163,163

Note receivable, interest at 0.00%, annual payments from cash flow, principal due at maturity on April 08, 2043 339,579

Helen V LLC:

Developer fee note receivable, interest at 1.00%, monthly payments of \$1,163 until maturity on December 31, 2015 102,338

Oleta Apartments Limited Partnership:

Note receivable, interest at 0.00%, annual payments from cash flow starting June 2003 through maturity on June 30, 2053 909,000

CAPITOL HILL HOUSING IMPROVEMENT PROGRAM

**Notes To Financial Statements
For The Year Ended December 31, 2006**

Note 2 - Continued

Pantages Apartments LLC:

Note receivable, interest at 6%, annual payments from cash flow starting February 2006 through maturity on February 1, 2056 220,000

Deferred developer fee note receivable, interest at 0.00%, annual payments from cash flow starting in 2006 through maturity on March 31, 2015 111,394

Villa Apartments Limited Partnership:

Deferred developer fee note receivable from, interest at 7%, principal and accrued interest due at maturity on November 1, 2011 127,067

Total principal 2,806,826
Accrued interest on the above notes 141,994

Total \$ 2,948,820

Note 3 - Land, Buildings And Equipment

Land, buildings and equipment activity consisted of the following:

	<u>December 31, 2005</u>	<u>Additions</u>	<u>Disposals</u>	<u>December 31, 2006</u>
Land	\$ 8,924,894	\$ 337,503	\$ -	\$ 9,262,397
Buildings and facilities	32,895,905	341,084		33,236,989
Equipment and vehicles	<u>988,562</u>	<u>17,957</u>	<u>(5,867)</u>	<u>1,000,652</u>
	42,809,361	696,544	(5,867)	43,500,038
Less accumulated depreciation	<u>(9,796,686)</u>	<u>(913,503)</u>	<u>5,867</u>	<u>(10,704,322)</u>
Total	<u>\$ 33,012,675</u>	<u>(216,959)</u>	<u>\$ -</u>	<u>\$ 32,795,716</u>

CAPITOL HILL HOUSING IMPROVEMENT PROGRAM

Notes To Financial Statements For The Year Ended December 31, 2006

Note 4 - Leases

Operating Lease - CHHIP, as lessee, leases administrative office space. Subsequent to December 31, 2006, the administrative office lease was extended to March 2010. Rental expense under this lease totaled \$70,206 for 2006. Minimum lease payments under the lease are as follows:

<i>Years Ending December 31,</i>	
2007	\$ 73,230
2008	76,521
2009	81,267
2010	<u>20,643</u>
	<u>\$ 251,661</u>

CHHIP, as lessor, leases apartments and commercial space under noncancellable terms of less than one year.

Ground Lease - CHHIP as lessor has entered into a ground lease with Harrison Family Housing Limited Partnership (see Note 6) through 2074. Lease payments started at \$12,000 per year with a 3% annual increase. Payments are made subject to available cash flow, as defined or from proceeds of a sale or refinance. Minimum lease payments under the lease are as follows:

<i>Years Ending December 31,</i>	
2007	\$ 14,239
2008	14,758
2009	15,201
2010	15,657
2011	16,127
Thereafter	<u>3,010,938</u>
	<u>\$ 3,086,920</u>

CAPITOL HILL HOUSING IMPROVEMENT PROGRAM

Notes To Financial Statements For The Year Ended December 31, 2006

Note 4 - Continued

Financing Lease - During 1999, CHHIP entered into a finance lease agreement, leasing real property to the Fleming Apartments Limited Partnership. CHHIP has recorded this lease as a direct financing lease expiring on December 31, 2097. The lessee has the right to extend the term of this agreement for a period of time equal to the remaining useful life of the capital improvements to the property as of December 31, 2097.

The lease payments due to CHHIP are made in the form of principal and interest payments (\$6,853 monthly) directly to the bank on the related note payable CHHIP holds, which totaled \$1,000,693 for December 31, 2006 (See Note 6) plus annual rent of \$12. Accordingly, an amount equal to the note payable is also presented in the financial statements as a corresponding lease receivable. Additionally, the lease agreement requires the lessee to pay, to the bank as owner of the note payable, on behalf of CHHIP, rent in an amount sufficient to pay in full all of the principal, premium, and interest on the note payable when due, whether at maturity or upon earlier redemption or acceleration. Such rent shall be allocated to principal, premium, and interest in proportion to the payment due on the note payable to be paid. The lessee has the option to buy the property at the end of the lease for \$1. Minimum lease payments to be received under this lease are as follows:

<i>Years Ending December 31,</i>	
2007	\$ 82,227
2008	82,227
2009	82,227
2010	82,227
2011	82,227
Thereafter	<u>1,363,603</u>
	1,774,738
Less: amounts representing interest	(774,045)
Less: current portion	<u>(23,620)</u>
Noncurrent Portion	<u>\$ 977,073</u>

CAPITOL HILL HOUSING IMPROVEMENT PROGRAM

Notes To Financial Statements For The Year Ended December 31, 2006

Note 5 - Notes Payable And Accrued Interest

Notes payable consist of the following at December 31:

410 - 11th East Apartments:

Note payable to individual, original principal balance of \$83,802, interest at 8%, monthly payments of \$500 until maturity on July 10, 2014

\$ 31,952

Note payable to City of Seattle, original principal balance of \$266,169, interest accrues at 1%, principal and accrued interest due at maturity in September 2034

270,117

Berneva Apartments:

Note payable to City of Seattle, original principal balance of \$661,078, interest at 1%, principal and accrued interest due at maturity in October 2032

661,078

Note payable to bank, original principal balance of \$260,000, interest at 6.625%, monthly payments of \$1,665 until maturity in October 2007 when remaining outstanding balance is due

191,951

Boylston/Howell Apartments:

Note payable to State of Washington, original principal balance of \$1,830,000, interest at 2%, annual payments of \$57,928 until maturity in January 2046

1,595,214

Note payable to City of Seattle, original principal balance of \$1,619,193, interest at 1%, principal and accrued interest due at maturity in January 2035

1,584,858

Bremer Apartments:

Note payable to City of Seattle, original principal balance of \$101,264, no interest, principal and accrued interest due at maturity in December 2006; subsequent to December 31, 2006 City of Seattle agreed to extend the term of the note consistent with the second note described below

101,264

Note payable to City of Seattle, original principal balance of \$914,296, interest accrues at 1% upon advance of funds, principal and accrued interest due at maturity in August 2031

914,002

Note payable to bank, original principal balance of \$925,308, interest at 8.63%, monthly payments of \$7,200 until maturity in October 2030

872,234

CAPITOL HILL HOUSING IMPROVEMENT PROGRAM

Notes To Financial Statements For The Year Ended December 31, 2006

Note 5 - Continued

Brewster Apartments:

Note payable to bank, original principal balance of \$386,212, interest at 7.5%, monthly payments of \$3,111 until maturity in August 2014 217,187

Note payable to City of Seattle, original principal balance of \$1,166,363, interest at 1%, principal and accrued interest due at maturity in October 2034 1,166,363

Note payable to State of Washington, original principal balance of \$1,050,000, interest at 1%, annual payments of \$26,789 until maturity in August 2044 843,415

Broadway Apartments:

Note payable to bank, original principal balance of \$102,511, interest at 6.898%, monthly payments of \$675 until maturity in October 2030 94,632

Burke Gilman Gardens Apartments:

Note payable to State of Washington, original principal balance of \$1,150,833, no interest, annual payments of \$23,017 until maturity in February 2048 966,700

Note payable to City of Seattle, original principal balance of \$971,320, interest at 1%, principal and accrued interest due at maturity in January 2037 968,165

Casa di Cinque Apartments:

Note payable to City of Seattle, original principal balance of \$25,000, interest at 1%, monthly payments of \$304 until maturity in June 2007 1,820

Centennial Apartments:

Note payable to State of Washington, original principal balance of \$300,000, no interest, annual payments of \$16,625 and interest at 1% beginning February 2029 until maturity in February 2048 300,000

Note payable to U.S. Bank, original principal balance of \$1,500,322, interest at 6.42%, monthly payments of \$9,404 until maturity on March 1, 2029 1,348,532

Note payable to City of Seattle, original principal balance of \$761,677, interest at 1%, principal and interest due at maturity on January 1, 2039 761,677

CAPITOL HILL HOUSING IMPROVEMENT PROGRAM

***Notes To Financial Statements
For The Year Ended December 31, 2006***

Note 5 - Continued

Central City Affordable Housing:

Note payable to Federal National Mortgage Association, interest at 8.5%, monthly payments of \$1,840 until maturity at October 1, 2011. The monthly payments are offset by a federal interest subsidy credit which reduces the effective interest rate on the mortgage to 1%. The mortgage is insured by HUD under Section 236

86,458

Note payable to Local Initiatives Support Corporation, original Principle balance of \$124,710, interest at 8%, quarterly payments of \$3,811, remaining principle and interest due September 2011

89,094

Note payable to City of Seattle, original principle balance of \$652,896, interest at 1%, principle balance due at maturity in February 2034

640,702

Devonshire Apartments:

Note payable to City of Seattle, original principal balance of \$616,019, interest at 1%, principal and accrued interest due at maturity in February 2033

612,126

Note payable to Washington State Department of Community Development, original principal balance of \$454,500, no interest, annual payments of \$9,080 until maturity in February 2043

335,960

Note payable to bank, original principal balance of \$950,000, interest at 5.8%, monthly payments of \$7,914 until maturity in March 2008

114,249

Eighteenth Avenue:

Note payable to City of Seattle, original principal balance of \$449,573, interest at 1%, principal and accrued interest due at maturity on July 1, 2052

449,573

Note payable to State of Washington, original principal balance of \$230,000, interest at 2%, annual payments of \$7,319 until maturity on October 1, 2051

202,768

Note payable to U.S. Bank, original principal balance of \$344,000, interest at 7.88%, monthly payment of \$2,945 until maturity on July 1, 2032

330,888

Elizabeth Dean Wells Apartments:

Note payable to City of Seattle, original principal balance of \$116,125, interest at 1%, monthly payments of \$60 through September 2003, principal and accrued interest due at maturity in June 2012

108,414

CAPITOL HILL HOUSING IMPROVEMENT PROGRAM

Notes To Financial Statements For The Year Ended December 31, 2006

Note 5 - Continued

Note payable to bank, original principal balance of \$75,154, interest at 6.898%, monthly payments of \$500 until maturity in October 2030	68,905
Elizabeth James Senior Housing: Mortgage payable to Aetna Life Insurance Company, due in monthly installments of \$3,400 including interest at 6% per annum, the mortgage is insured by HUD under Section 221(d)(3), matures in 2009	88,624
Second mortgage payable to GMAC Commercial Mortgage, due in monthly installments of \$13,394 including interest at 7.42% per annum, matures in 2035	1,899,722
Fleming Apartments: Note payable to bank, original principal balance of \$1,152,772, interest at 5.92%, monthly payments of \$6,853 until June 2028 when the note can be extended upon meeting certain conditions	1,000,693
Fredonia Apartments: Note payable to City of Seattle, original principal balance of \$409,760, interest at 1%, monthly payments of \$275 until March 2008, then balloon payment	409,760
Note payable to bank, original principal balance of \$821,302, interest at 6.898%, monthly payments of \$5,408 until maturity in October 2030	758,174
Gale Place Apartments: Note payable to City of Seattle, original principal balance of \$1,034,400, no interest, no payments until maturity in April 2028 unless extended at CHHIP's option for five years at five-year intervals	766,400
Note payable to bank, original principal balance of \$455,604, interest at 6.898%, monthly payments of \$3,000 until maturity in October 2030	419,508
Harrison Apartments Note payable to City of Seattle, original principal balance of \$825,000, interest at 1%, principal and accrued interest due at maturity in July 2039	808,211

CAPITOL HILL HOUSING IMPROVEMENT PROGRAM

**Notes To Financial Statements
For The Year Ended December 31, 2006**

Note 5 - Continued

Hazel Plaza I Apartments:

Mortgage payable to KeyCorp Mortgage, due in monthly installments of \$1,701 including interest of 8.5% per annum and maturing November 1, 2011. The monthly payments are offset by a federal interest subsidy credit which reduces the effective interest rate on the mortgage to 0%. This credit amounted to \$13,741 for the year ended December 31, 2006. The mortgage is insured by HUD under section 236 and is secured by the land and building subject to the mortgage.

80,659

Note payable to State of Washington, original principal balance of \$15,571, no interest, principal to be forgiven upon maturity in September 2020 if units are rented as stipulated in loan agreement

15,571

Note payable to City of Seattle, original principal balance of \$475,242, interest accrues at 1% upon advance of funds, principal and accrued interest due upon maturity in December 2031

475,091

Holden Vista Apartments:

Note payable to State of Washington, original principal balance of \$544,843, interest at 3%, annual payments of \$21,051 until maturity in April 2046

487,958

Note payable to Federal National Mortgage Association, original principal balance of \$169,812, interest at 8.5%, monthly payments of \$1,629 until maturity in August 2010. The monthly payments are offset by a federal interest subsidy credit which reduces the effective interest rate to 0%. The Mortgage is insured by HUD under section 236.

60,184

John Carney Apartments:

Note payable to City of Seattle, original principal balance of \$744,681, interest accrues at 1%, principal and accrued interest due at maturity in July 2031

744,681

Note payable to bank, original principal balance of \$451,807, interest at 6.898%, monthly payments of \$2,975 until maturity in October 2030

417,079

Lincoln Court:

Note payable to State of Washington, original principal balance of \$1,000,000, interest at 1.00%, quarterly interest only payments of \$2,500, accrued interest and principle due at maturity on June 30, 2045

1,000,000

CAPITOL HILL HOUSING IMPROVEMENT PROGRAM

Notes To Financial Statements For The Year Ended December 31, 2006

Note 5 - Continued

Note payable to City of Seattle, original principal balance of \$1,400,512, interest at 1.00%, annual principal and interest payments of \$35,731 from available cash flow, as defined, until maturity in November 2053.	1,400,512
Note payable to bank, original principal balance of \$1,250,000, interest at 5.527%, Monthly principal and interest payments of \$7,119 until maturity on December 1, 2033	1,196,831
Mary Ruth Manor Apartments: Note payable to City of Seattle, original principal balance of \$759,646, interest at 1%, principal and accrued interest due at maturity in September 2034	745,347
Note payable to bank, original principle balance of \$557,600, interest at 8%, monthly payments of \$4,091 until maturity in October 2024.	465,660
Note payable to bank, original principal balance of \$263,339, interest at 8.5%, monthly payments of \$2,424 until maturity in January 2012. The monthly payments are offset by a federal Interest subsidy credit which reduces the effective interest rate to 0%. The mortgage is insured by HUD under section 236.	119,760
Maxwell Apartments: Note payable to City of Seattle, original principal balance of \$190,109, interest at 1%, principal and accrued interest due at maturity in June 2029	189,706
Note payable to bank, original principal balance of \$58,773, interest at 6.898%, monthly payments of \$387 until maturity in October 2030	54,181
Melrose Apartments: Note payable to City of Seattle, original principal balance of \$725,000, interest at 1%, principal and accrued interest due at maturity in August 2029	725,000
Note payable to bank, original principal balance of \$413,688, interest at 6.898%, monthly payments of \$2,724 until maturity in October 2030	381,890
Miller Park Apartments: Note payable to City of Seattle, original principal balance of \$647,875, interest at 1%, principal and accrued interest due at maturity in April 2036	647,875

CAPITOL HILL HOUSING IMPROVEMENT PROGRAM

**Notes To Financial Statements
For The Year Ended December 31, 2006**

Note 5 - Continued

Note payable to State of Washington, original principal balance of \$707,420, no interest, annual payments of \$35,371 beginning April 2027 until maturity in April 2046	707,420
Note payable to bank, original principal balance of \$242,600, interest at 8.5%, monthly payments of \$1,865 until maturity in March 2028	220,119
Park Hill Apartments:	
Note payable to City of Seattle, original principal balance of \$383,640, interest at 1%, principal and accrued interest due upon maturity in March 2013	330,000
Note payable to City of Seattle, original principal balance of \$25,000, interest at 3%, principal and accrued interest due at maturity in March 2013	25,000
Note payable to bank, original principal balance of \$681,128, interest at 6.898%, monthly payments of \$4,485 until maturity in October 2030	628,774
Tiltsonian Apartments:	
Note payable to bank, original principal balance of \$106,308, interest at 6.898%, monthly payments of \$700 until maturity in October 2030	98,137
Villa Apartments:	
Note payable to City of Seattle, original principal balance of \$1,182,510, interest at 1%, principal and accrued interest due at maturity in August 2037	1,182,510
Woodland Park:	
Note payable to City of Seattle, maximum principal balance of \$1,777,000 available, \$594,989 drawn to date, interest at 1%, principal and accrued interest due at May 1, 2058.	<u>594,989</u>
	35,076,324
Less current portion	<u>(684,517)</u>
Noncurrent Portion	<u>\$ 34,391,807</u>

CAPITOL HILL HOUSING IMPROVEMENT PROGRAM

**Notes To Financial Statements
For The Year Ended December 31, 2006**

Note 5 - Continued

Debt service payments due on these notes are as follows:

<i>Years Ending December 31,</i>	<u>Principal</u>	<u>Interest</u>
2007	\$ 684,517	\$ 1,044,905
2008	852,720	1,005,227
2009	415,874	977,771
2010	420,815	952,804
2011	427,713	927,481
2012-2016	3,101,408	4,166,434
2017-2021	2,490,003	3,430,607
2022-2026	3,211,783	2,590,162
2027-2031	7,212,105	1,542,790
2032-2036	7,191,650	715,044
2037-2041	4,612,790	308,131
2042-2046	1,871,680	180,616
2047-2051	138,534	123,179
2052 -2056	1,850,085	53,005
2057-2061	<u>594,647</u>	<u>8,925</u>
Total	<u>\$ 35,076,324</u>	<u>\$ 18,027,081</u>

Accrued interest payable on the above notes payable totaled \$2,106,367 at December 31, 2006, and is presented separate from the above total for notes payable on the balance sheet. Interest expense on the above notes payable aggregated \$919,375 for 2006 and included the deferred interest on certain non-amortizing loans.

Substantially all notes payable are secured by deeds of trust on the related buildings. The notes payable to the City of Seattle require rental of the apartment units to low or moderate income tenants at stipulated base rents with certain allowable increases, compliance with certain federal regulations as to discrimination, and establishment of certain reserves for repairs and maintenance.

Certain material City and State interest and principal are forgivable when and with the passage of time and if CHHIP meets certain continuing management obligations. Such notes have been included in notes payable, and interest expense has been accrued in accordance with the terms of the loans.

Long-term liability activity consisted of the following during 2006:

	<u>December 31, 2005</u>	<u>Increases</u>	<u>Decreases</u>	<u>December 31, 2006</u>	<u>Due Within One Year</u>
Notes payable	\$ 35,020,326	\$ 594,989	\$ (538,991)	\$ 35,076,324	\$ 684,517
Accrued interest payable	<u>1,948,498</u>	<u>919,375</u>	<u>(761,506)</u>	<u>2,106,367</u>	
Total	<u>\$ 36,968,824</u>	<u>\$ 1,506,998</u>	<u>\$ (1,293,131)</u>	<u>\$ 37,182,691</u>	<u>\$ 684,517</u>

CAPITOL HILL HOUSING IMPROVEMENT PROGRAM

Notes To Financial Statements For The Year Ended December 31, 2006

Note 5 - Continued

Line of Credit - During 2006, CHHIP obtained a predevelopment line of credit at 6% with a maximum of \$250,000 from Impact Capital. No funds have been drawn at December 31, 2006.

Note 6 - Investments In Limited Partnerships And LLCs

CHHIP is the sole general partner and owns a 1% or less interest in nine limited partnerships and is the managing member and owns a .01% interest in four limited liability companies. The remaining ownership interests in these entities are owned by unrelated third parties.

During 2006, CHHIP earned property management fees of \$212,380 and limited partnership and LLC management fees of \$96,282 from these entities. Additionally, CHHIP earned development fees of \$875,497 in 2006 from four of these LLCs.

The following is a summary of selected financial information from the separate financial statements of the limited partnerships and LLCs described above:

	<i>December 31, 2006</i>		
	<u><i>Assets</i></u>	<u><i>Liabilities</i></u>	<u><i>Equity</i></u>
1214 Boylston Avenue Limited Partnership	\$ 2,622,575	\$ 1,032,145	\$ 1,590,430
Broadway & Pine LLC (under development)	9,274,108	9,185,002	89,106
Byron Wetmore Limited Partnership	677,668	665,844	11,824
El Nor Limited Partnership	3,787,029	2,208,325	1,578,704
Fleming Apartments Limited Partnership	2,409,505	2,653,333	(243,828)
Gilman Court Limited Partnership	2,704,818	2,066,282	638,536
Harrison Family Housing Limited Partnership	3,132,353	2,801,619	330,734
Helen V Apartments LLC	4,106,824	3,616,196	490,628
Larned Apartments Limited Partnership	1,680,366	1,780,865	(100,499)
Oleta Apartments Limited Partnership	2,639,766	2,505,635	134,131
Pantages Apartments LLC	10,514,820	5,900,202	4,614,618
Silvian Apartments LLC	3,920,719	3,115,598	805,121
Villa Apartments Limited Partnership	5,496,537	5,246,942	249,595
	<u>\$ 52,967,088</u>	<u>\$ 42,777,988</u>	<u>\$ 10,189,100</u>

CAPITOL HILL HOUSING IMPROVEMENT PROGRAM

**Notes To Financial Statements
For The Year Ended December 31, 2006**

Note 6 - Continued

	<i>Year Ended December 31, 2006</i>	
	<u>Revenues</u>	<u>Net Income (Loss)</u>
1214 Boylston Avenue Limited Partnership	\$ 239,832	\$ (58,270)
Broadway & Pine LLC (under development)		3,106
Byron Wetmore Limited Partnership	74,558	(71,181)
El Nor Limited Partnership	449,114	(34,775)
Fleming Apartments Limited Partnership	205,170	(86,832)
Gilman Court Limited Partnership	167,939	(143,778)
Harrison Family Housing Limited Partnership	253,069	(91,924)
Helen V Apartments LLC	311,614	(91,545)
Larned Apartments Limited Partnership	145,664	(98,614)
Oleta Apartments Limited Partnership	201,483	(114,312)
Pantages Apartments LLC	373,546	(455,407)
Silvian Apartments LLC	311,250	13,995
Villa Apartments Limited Partnership	<u>498,620</u>	<u>(184,644)</u>
	<u>\$ 3,231,859</u>	<u>\$ (1,414,181)</u>

In addition to the notes receivable described in Note 2, CHHIP has recorded accounts receivable from the limited partnerships and LLCs described above with a net balance of \$941,619 at December 31, 2006. The accounts receivable balance at December 31, 2006 is reported net of an allowance for doubtful accounts totaling \$385,922.

CHHIP also holds a special limited partner interest in a limited partnership not listed above. The ownership interest was donated to CHHIP in a previous year. During the year ended December 31, 2006, CHHIP received a liquidating distribution of \$313,213 from this partnership and recorded it as partnership income on the statement of revenues, expenses, and changes in net assets. No further distributions are anticipated from this limited partnership.

CAPITOL HILL HOUSING IMPROVEMENT PROGRAM

Notes To Financial Statements For The Year Ended December 31, 2006

Note 7 - Grants And Contributions

During 2006, CHHIP received grants and contributions from the following sources:

- Washington Mutual
- Impact Capital
- Paul G Allen Family Foundation
- Plymouth Housing Group
- The Seattle Foundation
- Raynier Institute and Foundation
- Enterprise Community Fund
- Foster Pepper
- GeoTech Consultants
- MarPac Construction
- Buchanan Construction
- Russell Matching Gifts Program
- Starbucks Coffee Company
- Abrahams Architects
- Bailey Coy Books
- Infusion
- Kingfish Café
- Regan & Associates
- Tango Restaurant
- Kovalenko Hale Architects
- The Longbrake Family Foundation
- City of Seattle
- KeyBank Foundation
- U.S. Bank
- National Equity Fund
- Bill & Martha Longbrake
- Walsh Construction
- GGLO Architect
- SMR Architects
- Kantor Taylor McCarthy
- Windermere Real Estate – Capitol Hill
- RAFN Construction
- Housing Development Consortium from a number of combined charities campaigns
- Dunn & Hobbes
- Microsoft Corporation
- Members of the CHHIP Board of Directors and the general community

CAPITOL HILL HOUSING IMPROVEMENT PROGRAM

Notes To Financial Statements For The Year Ended December 31, 2006

Note 8 - Employee Benefits

CHHIP contributes to a Simplified Employee Pension Plan (SEP), a defined contribution benefit plan, on behalf of all eligible employees. The SEP was established to provide a "public retirement system" in lieu of participation in social security. CHHIP's contributions range from 7.5% to 15% of gross wages annually with the rate of contribution decreasing as compensation increases. The amount of CHHIP's contributions in 2006 was \$142,809.

Note 9 - Net Assets

"Net Assets - Investment in Capital Assets, Net of Related Debt" is calculated by subtracting total debt and depreciation from the cost of CHHIP's properties. The negative amount in this category illustrates the unique position CHHIP is in as a Public Development Authority involved in low-income housing development. Several factors contribute to this calculation resulting in a negative number.

First, consistent with public lender policies, the amount of private debt from banks (subject to conventional lending requirements for debt coverage ratio maintenance) is usually maximized to minimize public subsidy levels. These bank loans are then combined with loans from the City, State, and other public sources to finance properties. As a result, CHHIP typically finances over 99% of a project's cost from public and private sources.

Secondly, a significant portion of CHHIP's debt is with the City of Seattle. This debt does not follow a typical schedule for amortization of principal and interest. Principal repayment is deferred for forty years (and may be extended thereafter) and interest accrues but is also deferred for twenty years. If certain conditions are met, the principal and interest are forgiven in year seventy-five and years twenty through forty respectively. However, during much of the term the overall amount of debt (principal and accrued interest) is growing rather than reducing through amortization. Similarly, loans from the State of Washington, the second largest public source, amortize over 50 years, instead of the typical 30 years, resulting in a slower decline of total debt. In addition some State debt has deferred payment terms. Lastly, in some years CHHIP initially acquires properties using "bridge financing," paying interest only when it needs to acquire the site prior to having access to all the permanent financing. This results in a high amount of debt in a particular period.

Taken together the normal increase in total depreciation expense over time combined with the extraordinarily low equity CHHIP subsequently contributes in the normal course of developing its properties and the fact that some of its debt builds over the first twenty years, as long as CHHIP continues to acquire new properties, it is reasonable for CHHIP to have negative "Net Assets - Investment in Capital Assets, Net of Related Debt."

CAPITOL HILL HOUSING IMPROVEMENT PROGRAM

Notes To Financial Statements For The Year Ended December 31, 2006

Note 10 - Acquisitions And Development

During 2006 CHHIP was engaged in the following acquisition and development projects:

Broadway & Pine Apartments – During 2005, CHHIP created Broadway & Pine Apartments LLC (see Note 6), the LLC purchased property, and CHHIP began managing the construction of low-income housing which was ongoing at December 31, 2006. Construction was completed and the property was placed in service in March 2007.

Fremont Project – During 2006, CHHIP created Woodland Park Avenue Apartments LLC (see Note 1), the LLC purchased property, and is in the permitting and design phase as of December 31, 2006. The project has a development budget of \$4.9 million, which will be financed with bond and other debt and tax credit investor funding.

Note 11 – Subsequent Event

Larned Apartments Limited Partnership - Effective January 1, 2007, CH Development Association (a blended component unit of CHHIP) purchased the limited partnership interest of Larned Apartments Limited Partnership from the unrelated third party owner for \$25,000.

Note 12 – Change in Reporting Entity

Blended Component Units - During 2006, CHHIP reviewed its control over Elizabeth James Senior Housing, Central City Affordable Housing, CH Development Association and determined that these organizations should be presented as blended component units in CHHIP's financial statements. This change in reporting entity was made by restating CHHIP's previously reported balance sheet as of December 31, 2005 and resulted in increases to total assets of \$3,225,443, total liabilities of \$2,982,747, and total net assets of \$242,696 as of that date.

Discrete Component Units - During 2006, CHHIP also reviewed its control over the limited partnerships and LLCs described in Note 6 and determined that these organizations should be presented as discrete component units in CHHIP's financial statements. This change in reporting entity was made by combining and discretely presenting these limited partnerships and LLCs in a separate column on the face of CHHIP's financial statements.

SUPPLEMENTAL INFORMATION

CAPITOL HILL HOUSING IMPROVEMENT PROGRAM

***Schedule Of Departmental Operations
For The Year Ended December 31, 2006***

	<i>Property Operations</i>	<i>Program Management & Administration</i>	<i>Total</i>
Receipts:			
Rents	\$ 3,771,078	\$ -	\$ 3,771,078
Vacancy loss	(263,064)		(263,064)
Development fees		875,497	875,497
Consulting, management, and service fees		1,365,129	1,365,129
Grants and contracts		518,992	518,992
Partnership income		367,382	367,382
Other income	129,764	67,531	197,295
Total Receipts	3,637,778	3,194,531	6,832,309
Expenditures:			
On-site management expense	696,060		696,060
Office salaries, benefits, and payroll taxes		1,878,518	1,878,518
Utilities	445,567		445,567
Professional fees	54,026	106,102	160,128
Insurance	178,585	10,114	188,699
Property management	342,971		342,971
Repairs and maintenance	406,516	77,644	484,160
Maintenance services	180,961		180,961
Debt service	1,218,515		1,218,515
Office lease and triple net costs		85,950	85,950
Reserves	194,456		194,456
Other	176,314	150,665	326,979
Total Expenditures	3,893,971	2,308,993	6,202,964
Operating Income (Loss)	(256,193)	885,538	629,345
Reconciliation to Statement of Revenues, Expenses, and Changes in Net Assets:			
Depreciation	(890,546)	(22,954)	(913,500)
Reserves additions	194,456		194,456
Interest income - restricted	80,527	14,951	95,478
Interest expense	(897,500)	(21,872)	(919,372)
Property lease expense	(3,750)		(3,750)
Expenses paid from reserves	(120,460)		(120,460)
Debt service payments	1,218,515		1,218,515
Front-line charges	187,299	(187,299)	
Management fees	342,971	(342,971)	
Maintenance service adjustments	180,961	(180,961)	
Change in Net Assets	\$ 36,280	\$ 144,432	\$ 180,712

See independent auditors' report.

CAPITOL HILL HOUSING IMPROVEMENT PROGRAM

*Schedule Of Property Operations
For The Year Ended December 31, 2006*

	<i>Berneva</i>	<i>Boylston/ Howell</i>	<i>Bremer</i>	<i>Brewster</i>	<i>Broadway</i>	<i>Burke Gilman Gardens</i>	<i>Casa di Cinque</i>	<i>Centennial</i>	<i>Devonshire</i>
Receipts:									
Rents	\$ 74,458	\$ 198,492	\$ 254,615	\$ 205,302	\$ 31,380	\$ 90,300	\$ 24,528	\$ 216,157	\$ 347,767
Vacancy loss		(1,526)	(15,744)	(14,136)		(2,729)	(1,181)	(13,851)	(11,243)
Other income	1,341	9,014	8,305	4,150	850	4,616	830	11,505	19,959
Total Receipts	75,799	205,980	247,176	195,316	32,230	92,187	24,177	213,811	356,483
Expenditures:									
On-site management expense	16,929	44,391	40,107	36,225	1,526	11,254	1,490	35,660	65,119
Utilities	12,090	29,084	30,275	23,581	2,882	1,626	5,430	16,831	63,558
Professional fees	930	2,292	3,754	2,676	228	1,146	228	2,292	4,737
Insurance	4,802	13,761	13,896	10,630	1,641	4,990	458	9,734	13,459
Property management	8,846	11,522	31,731	20,304	6,915	11,504	6,915	14,975	43,019
Repairs and maintenance	6,307	21,150	33,407	27,455	2,060	18,036	2,192	17,542	15,205
Maintenance services	4,530	6,065	14,348	8,708	408	6,093	253	8,456	10,212
Debt service	19,978	57,928	86,403	64,125	10,248	23,017	3,498	112,851	104,052
Reserves	2,256	10,000	6,348	8,400		8,000	540	8,503	11,500
Other	592	3,833	3,776	6,158	374	2,007	5,382	4,539	6,753
Total Expenditures	77,260	200,026	264,045	208,262	26,282	87,673	26,386	231,383	337,614
Operating Income (Loss)	(1,461)	5,954	(16,869)	(12,946)	5,948	4,514	(2,209)	(17,572)	18,869
Reconciliation to Statement of Revenues, Expenses, and Changes in Net Assets:									
Depreciation	(21,868)	(72,631)	(50,473)	(55,850)	(12,635)	(69,480)	(553)	(54,133)	(49,698)
Reserves additions	2,256	10,000	6,348	8,400		8,000	540	8,503	11,500
Interest income - restricted	881	3,951	3,535	5,836	566	6,014	741	773	16,834
Interest expense	(19,552)	(48,011)	(85,853)	(37,003)	(7,501)	(9,682)		(96,958)	(15,048)
Property lease expense							(3,750)		
Expenses paid from reserves		(4,159)			(557)	(11,175)		(1,117)	
Debt service payments	19,978	57,928	86,403	64,125	10,248	23,017	3,498	112,851	104,052
Front-line and bookkeeping charges	3,593	8,975	14,619	10,444	228	4,475	228	8,950	18,497
Management fees	8,846	11,522	31,731	20,304	6,915	11,504	6,915	14,975	43,019
Maintenance service adjustments	4,530	6,065	14,348	8,708	408	6,093	253	8,456	10,212
Change in Net Assets	\$ (2,797)	\$ (20,406)	\$ 3,789	\$ 12,018	\$ 3,620	\$ (26,720)	\$ 5,663	\$ (15,272)	\$ 158,237

See independent auditors' report.

- Continued -

CAPITOL HILL HOUSING IMPROVEMENT PROGRAM

*Schedule Of Property Operations - Continued
For The Year Ended December 31, 2006*

	<i>Elizabeth</i>								
	<i>Eighteenth Avenue</i>	<i>Dean Wells</i>	<i>410-11th East</i>	<i>Fredonia</i>	<i>Gale Place</i>	<i>Hazel Plaza I</i>	<i>Holden Vista</i>	<i>John Carney</i>	<i>Lincoln Court</i>
Receipts:									
Rents	\$ 97,320	\$ 35,640	\$ 27,456	\$ 153,578	\$ 163,860	\$ 107,936	\$ 127,368	\$ 137,140	\$ 206,021
Vacancy loss	(7,081)	(2,427)	(2,175)	(3,636)	(19,007)	(8,156)	(23,586)	(7,772)	(16,551)
Other income	817	1,531	2,087	3,918	6,059	2,527	10,439	5,210	6,901
Total Receipts	91,056	34,744	27,368	153,860	150,912	102,307	114,221	134,578	196,371
Expenditures:									
On-site management expense	14,974	5,801	1,988	6,073	21,227	35,794	38,931	21,179	28,343
Utilities	6,958	5,651	3,494	15,143	18,703	9,650	13,278	18,035	31,004
Professional fees	2,498	382	114	1,133	1,836	2,982	3,549	2,064	2,220
Insurance	2,937	2,050	1,909	4,612	7,748	5,543	5,158	7,158	8,561
Property management	4,573	4,402	8,298	20,714	15,453	6,604	5,341	16,722	12,527
Repairs and maintenance	9,021	10,750	2,178	4,654	32,825	14,988	29,710	6,447	21,865
Maintenance services	5,859	1,745	1,640	1,204	16,777	4,295	22,815	4,333	4,527
Debt service	37,264	6,000	6,000	68,196	36,000	6,735	27,902	35,700	95,423
Reserves	6,601	1,256	4,062	1,440	7,120	10,946	6,960	5,808	17,400
Other	4,986	511	379	14,657	2,000	10,716	9,862	4,081	2,412
Total Expenditures	95,671	38,548	30,062	137,826	159,689	108,253	163,506	121,527	224,282
Operating Income (Loss)	(4,615)	(3,804)	(2,694)	16,034	(8,777)	(5,946)	(49,285)	13,051	(27,911)
Reconciliation to Statement of Revenues, Expenses, and Changes in Net Assets:									
Depreciation	(18,772)	(5,289)	(8,451)	(29,826)	(45,770)	(20,678)	(16,347)	(38,346)	(70,411)
Reserves additions	6,601	1,256	4,062	1,440	7,120	10,946	6,960	5,808	17,400
Interest income - restricted	216	356	960	5,818	323	636	400	2,822	7,887
Interest expense	(35,070)	(5,876)	(5,363)	(60,085)	(29,156)	1,684	(6,390)	(36,431)	(90,633)
Property lease expense									
Expenses paid from reserves	(8,131)		(915)		(1,761)	(10,635)	(42,727)		(3,844)
Debt service payments	37,264	6,000	6,000	68,196	36,000	6,735	27,902	35,700	95,423
Front-line and bookkeeping charges	3,697	1,492	114	546	7,162	6,572	6,572	8,056	8,681
Management fees	4,573	4,402	8,298	20,714	15,453	6,604	5,341	16,722	12,527
Maintenance service adjustments	5,859	1,745	1,640	1,204	16,777	4,295	22,815	4,333	4,527
Change in Net Assets	\$ (8,378)	\$ 282	\$ 3,651	\$ 24,041	\$ (2,629)	\$ 213	\$ (44,759)	\$ 11,715	\$ (46,354)

See independent auditors' report.

CAPITOL HILL HOUSING IMPROVEMENT PROGRAM

*Schedule Of Property Operations - Continued
For The Year Ended December 31, 2006*

	<i>Mary Ruth Manor</i>	<i>Maxwell</i>	<i>Melrose</i>	<i>Miller Park</i>	<i>Park Hill</i>	<i>Elizabeth James Senior Housing</i>	<i>Central City Affordable Housing</i>	<i>Tiltsonian</i>	<i>Total</i>
Receipts:									
Rents	\$ 168,576	\$ 21,996	\$ 146,886	\$ 84,888	\$ 202,914	\$ 501,960	113,208	\$ 31,332	\$ 3,771,078
Vacancy loss	(24,230)		(11,225)	(1,846)	(8,272)	(47,598)	(19,092)		(263,064)
Other income	3,907	296	4,918	3,569	6,046	7,027	2,150	1,792	129,764
Total Receipts	148,253	22,292	140,579	86,611	200,688	461,389	96,266	33,124	3,637,778
Expenditures:									
On-site management expense	41,195	1,303	29,294	17,829	42,384	95,408	40,063	1,573	696,060
Utilities	18,062	3,550	26,196	9,833	21,929	41,572	13,849	3,303	445,567
Professional fees	3,150	178	2,994	915	2,609	5,650	3,241	228	54,026
Insurance	3,694	1,465	7,468	4,815	11,176	24,936	4,168	1,816	178,585
Property management	7,947	5,532	13,168	4,890	25,250	23,718	5,186	6,915	342,971
Repairs and maintenance	18,731	2,509	14,417	8,315	20,299	45,922	18,547	1,984	406,516
Maintenance services	14,834	915	6,531	2,448	5,624	21,093	7,106	142	180,961
Debt service	62,558	4,644	32,688	22,385	53,820	204,936	27,764	8,400	1,218,515
Reserves	9,996	1,440	5,600	10,456	12,000	30,024	7,800		194,456
Other	29,868	953	6,745	974	3,092	42,122	8,936	606	176,314
Total Expenditures	210,035	22,489	145,101	82,860	198,183	535,381	136,660	24,967	3,893,971
Operating Income (Loss)	(61,782)	(197)	(4,522)	3,751	2,505	(73,992)	(40,394)	8,157	(256,193)
Reconciliation to Statement of Revenues, Expenses, and Changes in Net Assets:									
Depreciation	(36,331)	(5,980)	(32,087)	(35,560)	(37,356)	(56,647)	(37,857)	(7,517)	(890,546)
Reserves additions	9,996	1,440	5,600	10,456	12,000	30,024	7,800		194,456
Interest income - restricted	244	519	1,748	2,791	3,578	11,083	723	1,292	80,527
Interest expense	(36,093)	(5,593)	(33,789)	(25,328)	(47,745)	(148,359)	(6,845)	(6,820)	(897,500)
Property lease expense									(3,750)
Expenses paid from reserves	(10,483)	(1,254)	(1,219)	(1,731)		(10,014)	(9,455)	(1,283)	(120,460)
Debt service payments	62,558	4,644	32,688	22,385	53,820	204,936	27,764	8,400	1,218,515
Front-line and bookkeeping charges	8,461	178	8,975	3,578	8,950	36,819	7,209	228	187,299
Management fees	7,947	5,532	13,168	4,890	25,250	23,718	5,186	6,915	342,971
Maintenance service adjustments	14,834	915	6,531	2,448	5,624	21,093	7,106	142	180,961
Change in Net Assets	\$ (40,649)	\$ 204	\$ (2,907)	\$ (12,320)	\$ 26,626	\$ 38,661	\$ (38,763)	\$ 9,514	\$ 36,280

See independent auditors' report.