

**INDEPENDENCE**  
**TAX CREDIT PLUS II**

**QUARTERLY**  
**REPORT**

**Ended**  
**September 30, 2009**



November 2009

Message to Our BACsholders:

We would like to take this opportunity to present the Quarterly Report for Independence Tax Credit Plus LP II (the "Partnership") for the quarter ended September 30, 2009.

Currently, the Partnership has not sold any of its interests or assets in the Partnership. There remain 15 assets in the Partnership's portfolio. The General Partner continues to research liquidation opportunities. We anticipate full liquidation to occur within the next two-four years. We will, of course, keep you apprised of any sales in future reports. For more detailed information on the Partnership's overall performance please read the Management's Discussion and Analysis of Financial Condition and Results of Operations and Notes section of this report.

The Schedule K-1 forms for 2009 will be mailed during the first quarter of 2010 and simultaneously will be accessible via our website. Please go to [www.centerline.com](http://www.centerline.com) and click on "K-1 Tax Information for Investors", then click on the Partnership in which you are an investor. You will be asked to provide your taxpayer identification number and your six-digit investor number. If you do not know your six-digit investor number, have recently changed your mailing address or have questions concerning your investment, please contact Denise Bernstein of the Partnership's Investor relations Department at 1-800-600-6422, ext. 6451.

Very truly yours,



Robert L. Levy  
Chief Financial Officer  
Related Independence Associates Inc.

## Consolidated Balance Sheets

	September 30, 2009	March 31, 2009
	(Unaudited)	(Audited)
<b>ASSETS</b>		
Property and equipment at cost, net of accumulated depreciation of \$46,890,457 and \$45,187,290, respectively	\$ 60,724,612	\$ 62,427,780
Cash and cash equivalents	1,311,643	1,300,092
Cash held in escrow	3,306,590	2,970,379
Deferred costs, net of accumulated amortization of \$209,015 and \$193,544, respectively	197,990	213,461
Other assets	<u>465,144</u>	<u>397,259</u>
Total assets	<u>\$ 66,005,979</u>	<u>\$ 67,308,971</u>
<b>LIABILITIES AND PARTNERS' DEFICIT</b>		
Liabilities:		
Mortgage notes payable	\$ 56,616,560	\$ 56,945,695
Accounts payable	883,204	747,108
Security deposit payable	458,961	457,037
Accrued interest	23,131,876	22,239,687
Due to local general partners and affiliates	2,477,278	2,545,330
Due to general partner and affiliates	<u>6,468,464</u>	<u>6,108,050</u>
Total liabilities	<u>90,036,343</u>	<u>89,042,907</u>
Commitments and contingencies (Note 4)		
Partners' deficit:		
Limited partners (58,928 BACs issued and outstanding)	(21,397,101)	(19,369,227)
General partner	<u>(744,890)</u>	<u>(724,890)</u>
Independence Tax Credit Plus L.P. II total	<u>(22,141,991)</u>	<u>(20,094,117)</u>
Noncontrolling interests	<u>(1,888,373)</u>	<u>(1,639,819)</u>
Total partners' deficit	<u>(24,030,364)</u>	<u>(21,733,936)</u>
Total liabilities and partners' deficit	<u>\$ 66,005,979</u>	<u>\$ 67,308,971</u>

See accompanying notes to consolidated financial statements.

## Consolidated Statements of Operations

(Unaudited)

	Three Months Ended September 30,		Six Months Ended September 30,	
	2009	2008	2009	2008
Revenues				
Rental income	\$ 2,840,173	\$ 2,674,817	\$ 5,694,910	\$ 5,355,631
Other income	<u>73,782</u>	<u>99,573</u>	<u>145,946</u>	<u>182,941</u>
Total revenues	<u>2,913,955</u>	<u>2,774,390</u>	<u>5,840,856</u>	<u>5,538,572</u>
Expenses				
General and administrative	636,730	614,803	1,438,198	1,331,393
General and administrative- related parties (Note 2)	275,137	261,634	551,119	525,512
Repairs and maintenance	679,748	738,121	1,370,026	1,453,535
Operating	335,177	382,528	756,671	817,110
Taxes	192,350	191,482	386,994	392,121
Insurance	167,482	167,329	328,266	339,675
Financial	680,356	676,890	1,354,738	1,362,341
Depreciation and amortization	<u>863,376</u>	<u>841,867</u>	<u>1,718,638</u>	<u>1,671,309</u>
Total expenses	<u>3,830,356</u>	<u>3,874,654</u>	<u>7,904,650</u>	<u>7,892,996</u>
Net loss	(916,401)	(1,100,264)	(2,063,794)	(2,354,424)
Net loss attributable to noncontrolling interests	<u>6,790</u>	<u>2,616</u>	<u>15,920</u>	<u>6,054</u>
Net loss attributable to Independence Tax Credit Plus L.P. II	<u>\$ (909,611)</u>	<u>\$ (1,097,648)</u>	<u>\$ (2,047,874)</u>	<u>\$ (2,348,370)</u>
Net loss-limited partners (BACs holders)	<u>\$ (900,515)</u>	<u>\$ (1,086,672)</u>	<u>\$ (2,027,395)</u>	<u>\$ (2,324,886)</u>
Number of BACs outstanding	<u>58,928</u>	<u>58,928</u>	<u>58,928</u>	<u>58,928</u>
Net loss per weighted average BAC	<u>\$ (15.28)</u>	<u>\$ (18.44)</u>	<u>\$ (34.40)</u>	<u>\$ (39.45)</u>

See accompanying notes to consolidated financial statements.

**Consolidated Statement of Changes in Partners' Deficit**  
*(Unaudited)*

	<u>Total</u>	<u>Limited Partners</u>	<u>General Partner</u>	<u>Non- controlling Interests</u>
Partners' deficit – April 1, 2009	\$ (21,733,936)	\$ (19,369,227)	\$ (724,890)	\$ (1,639,819)
Net loss	(2,063,794)	(2,027,874)	(20,000)	(15,920)
Distributions	<u>(232,634)</u>	<u>-</u>	<u>-</u>	<u>(232,634)</u>
Partners' deficit – September 30, 2009	<u>\$ (24,030,364)</u>	<u>\$ (21,397,101)</u>	<u>\$ (744,890)</u>	<u>\$ (1,888,373)</u>

See accompanying notes to consolidated financial statements.

**Consolidated Statements of Cash Flows**  
*(Unaudited)*

	Six Months Ended September 30,	
	<u>2009</u>	<u>2008*</u>
Cash flows from operating activities:		
Net loss	\$ <u>(2,063,794)</u>	\$ <u>(2,354,424)</u>
Adjustments to reconcile net loss to net cash provided by operating activities:		
Depreciation and amortization	1,718,638	1,671,309
Increase in accounts payable	136,096	28,098
Increase in security deposit payable	1,924	11,561
Increase in accrued interest	892,189	988,898
Increase in cash held in escrow	(215,843)	(233,940)
Increase in other assets	(67,885)	(29,795)
Increase in due to local general partners and affiliates	1,106	31,433
Decrease in due to local general partners and affiliates	(54,366)	(9,639)
Increase in due to general partner and affiliates	<u>360,414</u>	<u>262,272</u>
Total adjustments	<u>2,772,273</u>	<u>2,720,197</u>
Net cash provided by operating activities	<u>708,479</u>	<u>365,773</u>
Cash flows from investing activities:		
Improvements to property and equipment	-	(35,745)
Increase in cash held in escrow	(120,368)	(120,196)
Increase in due to local general partners and affiliates	<u>-</u>	<u>47,695</u>
Net cash used in investing activities	<u>(120,368)</u>	<u>(108,246)</u>

See accompanying notes to consolidated financial statements.

**Consolidated Statements of Cash Flows** *(continued)*  
*(Unaudited)*

	Six Months Ended September 30,	
	<u>2009</u>	<u>2008*</u>
Cash flows from financing activities:		
Principal payments of mortgage notes	(329,135)	(303,098)
(Decrease) increase in due to local general partners and affiliates	(14,791)	1,813
Decrease in capitalization of consolidated subsidiaries attributable to noncontrolling interests	<u>(232,634)</u>	<u>(32,046)</u>
Net cash used in financing activities	<u>(576,560)</u>	<u>(331,331)</u>
Net increase (decrease) in cash and cash equivalents	11,551	(75,804)
Cash and cash equivalents at beginning of period	<u>1,300,092</u>	<u>1,085,780</u>
Cash and cash equivalents at end of period	<u>\$ 1,311,643</u>	<u>\$ 1,009,976</u>

\* Reclassified for comparative purposes.

See accompanying notes to consolidated financial statements.

## **Notes to Consolidated Financial Statements**

### **September 30, 2009 (Unaudited)**

#### Note 1 - General

The consolidated financial statements include the accounts of Independence Tax Credit Plus L.P. II (the "Partnership") and fifteen other limited partnerships ("subsidiary partnerships", "subsidiaries" or "Local Partnerships") owning leveraged apartment complexes that are eligible for the low-income housing tax credit. The general partner of the Partnership is Related Independence Associates L.P., a Delaware limited partnership (the "General Partner"). Through the rights of the Partnership and/or an affiliate of the General Partner, which affiliate has a contractual obligation to act on behalf of the Partnership, to remove the general partner of the subsidiary partnerships (each a "Local General Partner") and to approve certain major operating and financial decisions, the Partnership has a controlling financial interest in the subsidiary partnerships.

For financial reporting purposes, the Partnership's fiscal quarter ends September 30. The Partnership's fiscal quarter ends September 30, in order to allow adequate time for the subsidiary partnerships' financial statements to be prepared and consolidated. All subsidiaries have fiscal quarters ending June 30. Accounts of the subsidiary partnerships have been adjusted for intercompany transactions from April 1 through September 30.

All intercompany accounts and transactions with the subsidiary partnerships have been eliminated in consolidation.

The Partnership has adopted FASB ASC 810, Noncontrolling Interests in Consolidated Financial Statements, which is effective for fiscal year ends beginning after December 15, 2008. In accordance with FASB ASC 810, losses attributable to noncontrolling interests amounted to approximately \$7,000 and \$16,000 for the three and six months ended September 30, 2009. Prior to the adoption of this ASC, losses attributable to noncontrolling interests which exceeded the noncontrolling interests' investment in a subsidiary partnership were charged to the Partnership. Such losses aggregated approximately \$7,000 and \$14,000 for the three and six months ended September 30, 2008. Increases (decreases) in the capitalization of consolidated subsidiaries attributable to noncontrolling interest arise from cash contributions from and cash distributions to the noncontrolling interest partners. The Partnership's investment in each subsidiary is equal to the respective subsidiary's partners' equity less noncontrolling interest capital, if any.

## **Notes to Consolidated Financial Statements** *(continued)* **September 30, 2009** (Unaudited)

Certain information and note disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”) have been omitted or condensed. These condensed financial statements should be read in conjunction with the financial statements and notes thereto included in the Partnership’s Annual Report on Form 10-K for the year ended March 31, 2009.

The books and records of the Partnership are maintained on the accrual basis of accounting in accordance with GAAP. In the opinion of the General Partner of the Partnership, the accompanying unaudited financial statements contain all adjustments (consisting only of normal recurring adjustments) necessary to present fairly the financial position of the Partnership as of September 30, 2009, the results of operations for the three and six months ended September 30, 2009 and 2008 and its cash flows for the six months ended September 30, 2009 and 2008, respectively. However, the operating results for the three and six months ended September 30, 2009 may not be indicative of the results for the year.

### Recent Accounting Pronouncements

In June 2009, the FASB issued ASC 105-10 (formerly SFAS No. 168), “The FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles”. The objective of this statement is to replace SFAS No. 162 and to establish the FASB Accounting Standards Codification as the source of the authoritative accounting principles recognized by the FASB to be applied by nongovernmental entities in the preparation of financial statements in conformity with GAAP. Rules and interpretive releases of the SEC under authority of federal securities laws are also sources of authoritative GAAP for SEC registrants. This ASC was effective for financial statements issued for interim and annual periods ending after September 15, 2009 and was adopted by the Partnership for its second quarter reporting. The adoption did not have a significant impact on the reporting of our financial position, results of operations or cash flows.

**Notes to Consolidated Financial Statements** (continued)  
**September 30, 2009** (Unaudited)

NOTE 2 – Related Party Transactions

An affiliate of the General Partner has a 0.01% interest as a special limited partner in each of the Local Partnerships.

The costs incurred to related parties for the three and six months ended September 30, 2009 and 2008 were as follows:

	Three Months Ended September 30,		Six Months Ended September 30,	
	2009	2008	2009	2008
Partnership management fees (a)	\$ 136,500	\$ 136,500	\$ 273,000	\$ 273,000
Expense reimbursement (b)	40,269	32,029	80,539	64,057
Local administrative fee (c)	10,875	10,500	21,750	21,000
Total general and administrative-General Partner	<u>187,644</u>	<u>179,029</u>	<u>375,289</u>	<u>358,057</u>
Property management fees incurred to affiliates of the subsidiary partnerships' general partners	<u>87,493</u>	<u>82,605</u>	<u>175,830</u>	<u>167,455</u>
Total general and administrative-related parties	<u>\$ 275,137</u>	<u>\$ 261,634</u>	<u>\$ 551,119</u>	<u>\$ 525,512</u>

- (a) The General Partner is entitled to receive a partnership management fee, after payment of all Partnership expenses, which together with the annual local administrative fees will not exceed a maximum of 0.5% per annum of invested assets (as defined in the Partnership's agreement of limited partnership (the "Partnership Agreement")), for administering the affairs of the Partnership. Subject to the foregoing limitation, the partnership management fee will be determined by the General Partner in its sole discretion based upon its review of the Partnership's investments. Unpaid partnership management fees for any year have been accrued without interest and will be payable from working capital reserves or to the extent of available funds after the Partnership has made distributions to the limited partners of sale or refinancing proceeds equal to their original capital contributions plus a 10% priority return thereon (to the extent not theretofore paid out of cash flow). Partnership management fees owed to the General Partner amounting to approximately \$5,666,000 and \$5,393,000 were accrued and unpaid as of September 30, 2009 and March 31, 2009, respectively. Without the General Partner's advances and continued accrual without payment of certain fees and expense reimbursements, the Partnership would not be in a position to meet its obligations.

**Notes to Consolidated Financial Statements** (continued)  
**September 30, 2009** (Unaudited)

- (b) The Partnership reimburses the General Partner and its affiliates for actual Partnership operating expenses incurred by the General Partner and its affiliates on the Partnership's behalf. The amount of reimbursement from the Partnership is limited by the provisions of the Partnership Agreement. Another affiliate of the General Partner performs asset monitoring for the Partnership. These services include site visits and evaluations of the subsidiary partnerships' performance.
- (c) Independence SLP L.P., a special limited partner of the subsidiary partnerships, is entitled to receive a local administrative fee of up to \$5,000 per year from each subsidiary partnership.

**NOTE 3 – Fair Value of Financial Instruments**

The following methods and assumptions were used to estimate the fair value of each class of financial instruments (all of which are held for nontrading purposes) for which it is practicable to estimate that value:

Cash and Cash Equivalents, Investments Available-for-Sale and Cash Held in Escrow

The carrying amount approximates fair value.

Mortgage Notes Payable

The Partnership adopted FASB ASC 820 – “Fair Value Measurements” for financial assets and liabilities. ASC 820 defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. ASC 820 applies to reported balances that are required or permitted to be measured at fair value under existing accounting pronouncements; accordingly, the standard does not require any new fair value measurements of reported balances.

As permitted, we chose not to elect the fair value option as prescribed by FASB SFAS No. 159, “The Fair Value Option for Financial Assets and Financial Liabilities” – Including an Amendment of FASB Statement No. 115, for our financial assets and liabilities that had not been previously carried at fair value. Therefore, we did not elect to fair value any additional items under SFAS No. 159.

The estimated fair value of financial instruments has been determined using available market information or other appropriate valuation metho-

**Notes to Consolidated Financial Statements** *(continued)*  
**September 30, 2009** (Unaudited)

dologies. However, considerable judgment is required in interpreting market data to develop estimates of fair value. Consequently, the estimates are not necessarily indicative of the amounts that could be realized or would be paid in a current market exchange. The following are financial instruments for which the Partnership's estimate of fair value differs from the carrying amounts:

	At September 30, 2009		At March 31, 2009	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
LIABILITIES:				
Mortgage notes	\$ 56,616,560	\$ 41,074,174	\$ 56,945,695	\$ 39,563,316

For the mortgage notes, fair value is calculated using present value cash flow models based on a discount rate. It was determined that the Tender Option Bond market, through which these bonds have been securitized in the past, continued to see a dramatic slowdown with limited liquidity and significantly reduced transaction levels. To assist in valuing these notes, the Partnership held separate discussions with various third party investment banks who are leaders in the municipal bond business. The discussions produced assumptions that were based on market conditions as well as the credit quality of the underlying property partnerships, which held the mortgage notes, to determine what discount rates to utilize.

NOTE 4 – Commitments and Contingencies

a) Subsidiary Partnerships – Going Concern

Creative Choice Homes VI Ltd. (“Creative Choice”)

The Local General Partner funded approximately \$142,000 to cover operating costs during the year ended 2008, and Creative Choice is in default of one of its subordinate notes. These factors create an uncertainty about Creative Choice's ability to continue as a going concern. The ability of Creative Choice to continue as a going concern is dependent on the Local General Partner's ability and willingness to continue funding operating losses.

During the year ended December 31, 2005, the property incurred hurricane damage. The total cost to bring the units back into service was approximately \$1,800,000. Creative Choice contracted with Naimisha Construction, a related party, for \$1,600,000 to complete the repairs and

**Notes to Consolidated Financial Statements** *(continued)*  
**September 30, 2009** (Unaudited)

renovations of the buildings damaged. During 2005, emergency insurance proceeds had been received by Creative Choice to offset the cost of immediate repair work. In 2006, Washington Mutual, the mortgage holder, received the remaining balance of the insurance proceeds which were subsequently reimbursed to Creative Choice in the amount of \$1,433,817. As of September 30, 2009, all hurricane repairs and renovations had been completed and a balance of approximately \$634,500 remains payable to Naimisha Construction.

Creative Choice also suffered fire damage on June 20, 2006 affecting nine of its units. As of September 30, 2009, \$567,370 of its insurance proceeds had been received to cover the cost of immediate repair work and securing the location. Naimisha Construction, a related party, has been contracted to complete the repairs for \$673,889 and \$206,519 remains payable as of September 30, 2009 to Naimisha Construction.

The above circumstances called into question the recoverability of the carrying amounts of the building. As a result, during the year ended December 31, 2006, pursuant to ASC 360, an impairment loss of \$603,733 was recognized on the building and improvements.

The Partnership's investment in Creative Choice at September 30, 2009 and March 31, 2009 was reduced to zero as a result of prior years' losses and the noncontrolling interest balance was \$0 at each date. Creative Choice's net income (loss) after noncontrolling interests amounted to approximately \$300 and (\$124,000) for the six months ended September 30, 2009 and 2008, respectively.

b) **Subsidiary Partnerships – Other**

Mansion Court Associates (“Mansion Court”)

Mansion Court had a net loss of \$48,366 for the six months ended September 30, 2009. In prior years and in 2009, Mansion Court has sustained operating losses and has not generated sufficient cash flow from operations to meet its obligations, primarily payable to related parties. The Local General Partner has provided funding in the past years; however there is no obligation to do so. The property also has experienced a high number of vacancies due to deteriorating conditions in the area. As of September 30, 2009, the project had 22 vacant units. In addition, Mansion Court's physical inspection by the Pennsylvania Housing Finance Agency (“PHFA”) noted 15 units for poor physical condition which would not meet a level of living standard. Although the Local General Partner could make the necessary repairs to improve the units to

**Notes to Consolidated Financial Statements** *(continued)*  
**September 30, 2009** (Unaudited)

a living standard, vacancies continue to increase due to declining conditions in the surrounding neighborhood, and the expenditure of funds at this time to make improvements would not benefit the project. The Local General Partner is exploring options to mitigate increased crime and deteriorating neighborhood conditions. The options include assistance from the local government housing agencies and possible transfer of ownership.

During the year ended March 31, 2009, in accordance with ASC 360, *Property, Plant and Equipment*, the Partnership deemed the building of Mansion Court further impaired and in addition to an earlier writedown of approximately \$1,342,000, wrote it down to its new reduced fair value of approximately \$338,000, which resulted in a further loss on impairment of approximately \$463,000. Fair value was obtained from an assessment made by the management after indications that the carrying value of the assets were not recoverable, evidenced by a history of net operating losses over the past few years as discussed above. In addition, at September 30, 2009, Mansion Court was contingently liable in an open letter of credit issued in favor of the PHFA in the amount of \$24,000.

The Partnership's investment in Mansion Court at September 30, 2009 and March 31, 2009 was zero as a result of prior years' losses and the noncontrolling interests balance was (\$1,989) and (\$1,500) at each date, respectively. Mansion Court's net loss after noncontrolling interests amounted to approximately \$48,000 and \$63,000 for the six months ended September 30, 2009 and 2008, respectively.

c) Uninsured Cash and Cash Equivalents

The Partnership maintains its cash and cash equivalents in various banks. The accounts at each bank are guaranteed by the Federal Deposit Insurance Corporation up to \$250,000.

d) Cash Distributions

Cash distributions from the Local Partnerships to the Partnership are restricted by the provisions of the respective agreements of limited partnership of the Local Partnerships and/or the U.S. Department of Housing and Urban Development.

**Notes to Consolidated Financial Statements** *(continued)*  
**September 30, 2009** (Unaudited)

e) Property Management Fees

Property management fees incurred by the Local Partnerships amounted to \$200,521 and \$186,406 and \$398,915 and \$376,144 for the three and six months ended September 30, 2009 and 2008, respectively.

f) Other

The Partnership and Beneficial Assignment Certificates (“BACs”) holders began to recognize the low-income housing credit (“Tax Credit”) with respect to an apartment complex (“Property”) when the periods of the Partnership’s entitlement to claim Tax Credits for such Property commenced (for each Property, generally ten years from the date of investment or, if later, the date the Property is placed in service) (“Credit Period”). Because of the time required for the acquisition, completion and rent-up of Properties, the amount of Tax Credits per BAC gradually increased over the first three years of the Partnership’s existence. Tax Credits not recognized in the first three years will be recognized in the 11th through 13th years. Once a Local Partnership has become eligible to recognize Tax Credits, it may lose such eligibility and suffer an event of “recapture” if its Property fails to remain in compliance with the Tax Credit requirements during the 15-year period commencing at the beginning of the Credit Period (“Compliance Period”). None of the Local Partnerships in which the Partnership has acquired an interest has suffered an event of recapture. As of December 31, 2007, all the Local Partnerships had completed their Credit Periods, and the Partnership had met its primary objective of generating Tax Credits for qualified BACs holders. However, each Local Partnership must continue to comply with the Tax Credit requirements until the end of the Compliance Period in order to avoid recapture of the Tax Credits. The Compliance Periods will continue through December 31, 2012 with respect to the Properties depending upon when the Compliance Period commenced.

g) Subsequent Events

We evaluated all subsequent events from the date of the balance sheet through November 4, 2009, which represents the issuance date of these financial statements. There were no events or transactions occurring during this subsequent event reporting period which require recognition or disclosure in the financial statements.

## **Management's Discussion and Analysis of Financial Condition and Results of Operations**

*(Summarized from form 10-Q as filed with the Securities and Exchange Commission. A copy is available upon written request.)*

### Liquidity and Capital Resources

As of September 30, 2009, the Partnership has invested all of its net proceeds in fifteen Local Partnerships. Approximately \$282,000 of the purchase price remains to be paid to the Local Partnerships (including approximately \$24,000 being held in escrow at the Partnership level).

### Short-Term

The Partnership's primary sources of funds include working capital reserves, interest earned on working capital reserves and distributions received from the Local Partnerships. However, none of these sources provides a material amount of funds.

For the six months ended September 30, 2009, cash and cash equivalents of the Partnership and its fifteen consolidated Local Partnerships increased approximately \$12,000. This increase was provided by operating activities (\$708,000), which exceeded principal payments of mortgage notes (\$329,000), a decrease in capitalization of consolidated subsidiaries attributable to minority interest (\$233,000), an increase in cash held in escrow relating to investing activities \$(120,000) and a net decrease due to local general partners and affiliates relating to financing activities (\$15,000). Included in the adjustments to reconcile the net loss to net cash provided by operating activities is depreciation and amortization (\$1,719,000).

At September 30, 2009, there was approximately \$314,000 in the working capital reserves at the Partnership level. For the six months ended September 30, 2009, the Partnership received approximately \$103,000 in distributions from the Local Partnerships. Management anticipates receiving additional distributions in the future, although not to a level sufficient to return to the limited partners their original investments. These distributions, if any, as well as the working capital reserves referred to above and the deferral of fees by the General Partner referred to below, will be used to meet the operating expenses of the Partnership.

Total expenses for the three and six months ended September 30, 2009 and 2008, excluding depreciation and amortization, interest and general and administrative-related parties, totaled \$2,011,487 and \$2,094,263 and \$4,280,155 and \$4,333,834, respectively.

## **Management's Discussion and Analysis of Financial Condition and Results of Operations** *(continued)*

Accounts payable as of September 30, 2009 and March 31, 2009 were \$883,204 and \$747,108, respectively. Accounts payable are short term liabilities which are expected to be paid from operating cash flows, working capital balances at the Local Partnership level, Local General Partner advances and, in certain circumstances, advances from the Partnership. The Partnership believes it (and the applicable Local Partnerships) has sufficient liquidity and ability to generate cash and to meet existing and known or reasonably likely future cash requirements over both the short and long term.

Security deposits payable are offset by cash held in security deposits, which are included in "Cash held in escrow" on the financial statements.

Accrued interest payable as of September 30, 2009 and March 31, 2009 was \$23,131,876 and \$22,239,687, respectively. Accrued interest payable represents the accrued interest on all mortgage loans, which include primary and secondary loans. Certain secondary loans have provisions such that interest is accrued but not payable until a future date. The Partnership anticipates the payment of accrued interest on the secondary loans (which make up the majority of the accrued interest payable amount which has been accumulating since the Partnership's investment in the respective Local Partnership) will be made from future refinancing or sales proceeds of the respective Local Partnerships. In addition, each Local Partnership's mortgage notes are collateralized by the land and buildings of the respective Local Partnership, and are without further recourse to the Partnership.

### Long-Term

Partnership management fees owed to the General Partner amounting to approximately \$5,666,000 and \$5,393,000 were accrued and unpaid as of September 30, 2009 and March 31, 2009, respectively. Without the General Partner's advances and continued accrual without payment of certain fees and expense reimbursements, the Partnership will not be in a position to meet its obligations.

For a discussion of contingencies affecting certain Local Partnerships, see Item 1, Note 4. Since the maximum loss the Partnership would be liable for is its net investment in the respective Local Partnerships, the resolution of the existing contingencies is not anticipated to impact future results of operations, liquidity or financial condition in a material way. However, the Partnership's loss of its investment in a Local Partnership will eliminate the ability to generate future Tax Credits from such Local

## **Management's Discussion and Analysis of Financial Condition and Results of Operations** *(continued)*

Partnership and may also result in recapture of Tax Credits, if the investment is lost before the expiration of the 15-year period commencing at the beginning of the Credit Period ("Compliance Period").

The Local Partnerships are impacted by inflation in several ways. Inflation allows for increases in rental rates generally to reflect the impact of higher operating and replacement costs. Furthermore, inflation generally does not impact the fixed long-term financing under which real property investments were purchased. Inflation also affects the Local Partnerships adversely by increasing operating costs, such as fuel, utilities, and labor.

Management is not aware of any trends or events, commitments or uncertainties which have not otherwise been disclosed that will or are likely to impact liquidity in a material way. Management believes the only impact would be from laws that have not yet been adopted. The portfolio is diversified by the location of the Properties around the United States so that if one area of the country is experiencing downturns in the economy, the remaining Properties in the portfolio may be experiencing upswings. However, the geographic diversification of the portfolio may not protect against a general downturn in the national economy. The Partnership has fully invested the proceeds of its offering in fifteen Local Partnerships, all of which have fully utilized their Tax Credits. As of December 31, 2007, all the Local Partnerships had completed their tax credit periods, and the Partnership had met its primary objective of generating Tax Credits for qualified BACs holders. However, each Local Partnership must continue to comply with the Tax Credit requirements until the end of the Compliance Period in order to avoid recapture of the Tax Credits. The Compliance Periods will continue through December 31, 2012 with respect to the Properties depending upon when the Compliance Period commenced.

### Off-Balance Sheet Arrangements

The Partnership has no off-balance sheet arrangements.

### Tabular Disclosure of Contractual Obligations

The Partnership discloses in Item 7 of the Partnership's Annual Report on Form 10-K for the year ended March 31, 2009, the Partnership's commitments to make future payments under its debt agreements and other contractual obligations. There are no material changes to such disclosure or amounts as of September 30, 2009.

## Management's Discussion and Analysis of Financial Condition and Results of Operations *(continued)*

### Fair Value Measurements

The following methods and assumptions were used to estimate the fair value of each class of financial instruments (all of which are held for nontrading purposes) for which it is practicable to estimate that value:

#### Cash and Cash Equivalents, Investments Available-for-Sale and Cash Held in Escrow

The carrying amount approximates fair value.

#### Mortgage Notes Payable

The Partnership adopted FASB ASC 820 – “*Fair Value Measurements*” for financial assets and liabilities. ASC 820 defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. ASC 820 applies to reported balances that are required or permitted to be measured at fair value under existing accounting pronouncements; accordingly, the standard does not require any new fair value measurements of reported balances.

As permitted, we chose not to elect the fair value option as prescribed by FASB SFAS No. 159, “*The Fair Value Option for Financial Assets and Financial Liabilities*” – Including an Amendment of FASB Statement No. 115, for our financial assets and liabilities that had not been previously carried at fair value. Therefore, we did not elect to fair value any additional items under SFAS No. 159.

The estimated fair value of financial instruments has been determined using available market information or other appropriate valuation methodologies. However, considerable judgment is required in interpreting market data to develop estimates of fair value. Consequently, the estimates are not necessarily indicative of the amounts that could be realized or would be paid in a current market exchange. The following are financial instruments for which the Partnership’s estimate of fair value differs from the carrying amounts:

	<u>At September 30, 2009</u>		<u>At March 31, 2009</u>	
	<u>Carrying Amount</u>	<u>Fair Value</u>	<u>Carrying Amount</u>	<u>Fair Value</u>
LIABILITIES:				
Mortgage notes	\$ 56,616,560	\$ 41,074,174	\$ 56,945,695	\$ 39,563,316

## **Management's Discussion and Analysis of Financial Condition and Results of Operations** *(continued)*

For the mortgage notes, fair value is calculated using present value cash flow models based on a discount rate. It was determined that the Tender Option Bond market, through which these bonds have been securitized in the past, continued to see a dramatic slowdown with limited liquidity and significantly reduced transaction levels. To assist in valuing these notes, the Partnership held separate discussions with various third party investment banks who are leaders in the municipal bond business. The discussions produced assumptions that were based on market conditions as well as the credit quality of the underlying property partnerships, which held the mortgage notes, to determine what discount rates to utilize.

### Critical Accounting Policies and Estimates

The preparation of consolidated financial statements requires management to make estimates and assumptions. These estimates and assumptions affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates. The following is a summary of certain accounting estimates considered critical by the Partnership. The summary should be read in conjunction with the more complete discussion of the Partnership's accounting policies included in Item 8, Note 2 to the consolidated financial statements in the Partnership's Annual Report on Form 10-K for the year ended March 31, 2009.

### Property and Equipment

Property and equipment to be held and used are carried at cost which includes the purchase price, acquisition fees and expenses, construction period interest and any other costs incurred in acquiring the Properties. The cost of property and equipment is depreciated over their estimated useful lives using accelerated and straight-line methods. Expenditures for repairs and maintenance are charged to expense as incurred; major renewals and betterments are capitalized. At the time property and equipment are retired or otherwise disposed of, the cost and accumulated depreciation are eliminated from the assets and accumulated depreciation accounts and the profit or loss on such disposition is reflected in earnings. The Partnership complies with ASC 360, *Property, Plant and Equipment*. A loss on impairment of assets is recorded when management estimates amounts recoverable through future operations and sale of the Property on an undiscounted basis are below depreciated cost. At that time, Prop-

## **Management's Discussion and Analysis of Financial Condition and Results of Operations** *(continued)*

erty investments themselves are reduced to estimated fair value (generally using discounted cash flows).

Through September 30, 2009, the Partnership has recorded approximately \$6,334,000 as an aggregate loss on impairment of assets.

### Revenue Recognition

Rental income is earned primarily under standard residential operating leases and is typically due the first day of each month, but can vary by Property due to the terms of the tenant leases. Rental income is recognized when earned and charged to tenants' accounts receivable if not received by the due date. Rental payments received in advance of the due date are deferred until earned. Rental subsidies are recognized as rental income during the month in which it is earned.

Other revenues are recorded when earned and consist of the following items: interest income earned on cash and cash equivalent balances and cash held in escrow balances, income from forfeited security deposits, late charges, laundry and vending income and other rental related items.

### Income Taxes

The Partnership is not required to provide for, or pay, any federal income taxes. Net income or loss generated by the Partnership is passed through to the partners and is required to be reported by them. The Partnership may be subject to state and local taxes in jurisdictions in which it operates. For income tax purposes, the Partnership has a fiscal year ending December 31.

### Results of Operations

The Partnership's results of operations for the three and six months ended September 30, 2009 and 2008 consisted primarily of the results of the Partnership's investment in fifteen consolidated Local Partnerships. The majority of Local Partnership income continues to be in the form of rental income with the corresponding expenses being divided among operations, depreciation and mortgage interest.

Rental income increased approximately 6% for the three and six months ended September 30, 2009 as compared to the corresponding periods in 2008, primarily due to decreases in vacancies at six Local Partnerships,

## **Management's Discussion and Analysis of Financial Condition and Results of Operations** *(continued)*

an increase in Section 8 rental subsidy income at two Local Partnerships and increases in rental rates at several Local Partnerships.

Other income decreased approximately \$26,000 and \$37,000 for the three and six months ended September 30, 2009 as compared to the corresponding periods in 2008, primarily due to an insurance refund received in the prior year at one Local Partnership and decreases in laundry, legal, miscellaneous and interest income at a second Local Partnership.

Operating expenses decreased approximately \$(47,000) and \$(60,000) for the three and six months ended September 30, 2009 as compared to the corresponding periods in 2008, primarily due to a decrease in the purchase of gasoline in bulk at one Local Partnership and a decrease in trash removal expense at a second Local Partnership.

### **Item 3. Quantitative and Qualitative Disclosures about Market Risk**

The Partnership has mortgage notes that are payable in aggregate monthly installments including principal and interest at rates varying from 0% to 9.05% per annum. The Partnership does not believe there is a material risk associated with the various interest rates associated with the mortgage notes as the majority of the Local Partnership mortgage notes have fixed rates. The Partnership disclosed in Item 8, Note 3 to the consolidated financial statements in the Partnership's Annual Report on Form 10-K for the year ended March 31, 2009, as well as in Item 2, the fair value of the mortgage notes payable. There are no material changes to such disclosure or amounts as of September 30, 2009.

The Partnership does not have any other market risk sensitive instruments.

### **Item 4T. Controls and Procedures**

(a) *Evaluation of Disclosure Controls and Procedures.* The Chief Executive Officer and Chief Financial Officer of Related Independence Associates, L.P., the general partner of the Partnership, have evaluated the effectiveness of the Partnership's disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended ("Exchange Act") as of the end of the period covered by this report. Based on such evaluation, such officers have concluded that, as of the end of such period, the Partnership's disclosure controls and procedures are effective.

## **Management's Discussion and Analysis of Financial Condition and Results of Operations** *(continued)*

(b) *Management's Annual Report on Internal Control over Financial Reporting.* Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Exchange Act Rules 13a-15(f) and 15d-15(f). In evaluating the Partnership's internal control over financial reporting, management has adopted the framework in Internal Control-Integrated Framework issued by the Committee of Sponsoring organizations of the Treadway Commission (the "COSO Framework"). Under the supervision and with the participation of our management, including the Chief Executive Officer and Chief Financial Officer of the General Partner, the Partnership conducted an evaluation of the effectiveness of its internal control over financial reporting as of March 31, 2009. The Partnership's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external reporting purposes in accordance with generally accepted accounting principles. Internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the Partnership; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the Partnership are being made only in accordance with authorizations of management and directors of the Partnership; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the Partnership's assets that could have a material effect on the financial statements. However, because of inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Based on management's evaluation under the COSO Framework, it has concluded that the Partnership's internal control over financial reporting, was, as of March 31, 2009, (1) effective at the Partnership level, in that they provide reasonable assurance that information required to be disclosed by the Partnership in the reports it files or submits under the Securities Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms and (2) ineffective at the subsidiary level due to certain deficiencies noted in the audit reports for such subsidiaries. Management will attempt to cause the Local General Partner's to remedy such deficiencies; however, the Gen-

## **Management's Discussion and Analysis of Financial Condition and Results of Operations** *(continued)*

eral Partner does not have control over the internal controls at the subsidiary level. Management believes they have sufficient controls at the Partnership level to mitigate these deficiencies, and such deficiencies do not have a material impact on the consolidated financial statements.

The Partnership's Annual Report on Form 10-K did not include an attestation report of the Partnership's registered public accounting firm regarding internal control over financial reporting. The Partnership's internal control over financial reporting was not subject to attestation by the Partnership's registered public accounting firm pursuant to temporary rules of the Securities and Exchange Commission that permit the Partnership to provide only this report.

(c) *Changes in Internal Controls over Financial Reporting.* Except as noted in (b) above, during the period ended September 30, 2009, there were no changes in the Partnership's internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, the Partnership's internal control over financial reporting.





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