# HOLLY MORTGAGE TRUST

2007 ANNUAL REPORT

**TO OUR SHAREHOLDERS:**

We are pleased to report that Holly Mortgage Trust ("Holly") had a very successful year in 2007. As reflected in the financial statements audited by Melton & Melton, L.L.P. appearing at the end of this report, gross revenues, net income and net income per share all significantly improved over the prior year.

| | 2007 | 2006 | Percentage Change |
|---|---|---|---|
| **Gross Revenue** | $609,959 | $279,823 | 117% |
| **Net Income** | $384,154 | $97,347 | 293% |
| **Net Income per Share** | $0.27 | $0.07 | 385% |

An important part of revenues for both 2007 and 2006 years is the recovery of amounts previously written off related to Holly's investments in the Wilco Building, a twenty-two story office building in Midland, Texas. Holly in 1999 purchased all of the stock of A.R. Goldrick Company, Inc. (Goldrick), the general partner of Wilco Building Partners, Ltd. (Wilco), the owner the Wilco Building. During the years 2003 through 2005, all amounts invested in Goldrick were deemed to be impaired and were written off Holly's books. During 2004, Goldrick sold a major portion of its partnership interest in Wilco for $100,000 plus a $500,000 installment note maturing over the next five years. Collections on this installment note have resulted in income from a recovery of the earlier impairment losses.

Another major contributor to revenues in 2007 was the sale of Holly's interest in the remaining acreage in a residential development in Franklin and Marion Counties, Tennessee.

## LOANS

The following tabulation summarizes all of the mortgage loans outstanding at December 31, 2007, either wholly or partially funded by Holly.

| Principal Amount Outstanding | Maturity | Interest Provision | Property Securing Loan |
|---|---|---|---|
| $105,980 | Demand | 0.7824 of Prime | Office Building in Midland, TX |
| $150,000 | 2008 | 12% | Residential Development in El Paso, TX |
| $920,000 | 2008 | 18% | Real Estate in Tampa, FL |
| $113,640 | 2009 | 12% | Office Building in Midland, TX |
| $48,017 | 2010 | 10% | Real Estate in El Paso, TX |
| $197,403 | 2010 | 11% | Apartment Complex in Pasadena, CA |
| $1,535,040 | | | |

Management plans to include in its proxy statement for the 2008 annual meeting of shareholders a proposal to change Holly from a Massachusetts business trust to a Texas real estate investment trust. The Texas laws that would apply to Holly would, in management's judgment, be an improvement over the non-statutory provisions under which Holly now operates. There would be no change in the capitalization of Holly and each share of Holly, both the common and preferential, would continue as shares of the new REIT.

Holly maintains a website www.hollymortgage.com that contains additional information about the Trust. Additional copies of this and earlier annual reports are posted on the website along with notices of dividend declarations.

Robert W. Scharar
President

Robert A. Burns
Vice President & Treasurer

April 30, 2008

# HOLLY MORTGAGE TRUST

## FINANCIAL STATEMENTS

**December 31, 2007 and 2006**

## HOLLY MORTGAGE TRUST

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MELTON & MELTON, L.L.P.
CERTIFIED PUBLIC ACCOUNTANTS

**REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS**

March 11, 2008

To the Board of Trustees of
**Holly Mortgage Trust**

We have audited the accompanying balance sheet of Holly Mortgage Trust (the "Trust") as of December 31, 2007 and 2006, and the related statements of operations, changes in shareholders' equity, and cash flows for the years then ended. These financial statements are the responsibility of the Trust's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States 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 audits provide a reasonable basis for our opinion.

As more fully discussed in Note 8 to the financial statements, The Trust reports its investment in A. R. Goldrick Company, Inc. ("A. R. Goldrick"), its wholly owned subsidiary, under the cost method of accounting. In our opinion, accounting principles generally accepted in the United States of America require that this investment be accounted for as a consolidated subsidiary. The effects of this departure from accounting principles generally accepted in the United States of America cannot be reasonably estimated.

In our opinion, except for the effects on the financial statements of the matter discussed in the preceding paragraph, the financial statements referred to in the first paragraph present fairly, in all material respects, the financial position of Holly Mortgage Trust as of December 31, 2007 and 2006, and the results of its operations and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 9 to the financial statements, distributions on the Trust's mandatorily redeemable shares of beneficial interest were recorded as dividends instead of interest expense. Accordingly, the 2006 financial statements have been restated to correct the error.

Melton & Melton, L.L.P.

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# HOLLY MORTGAGE TRUST
# BALANCE SHEET
# December 31, 2007 and 2006

| | 2007 | 2006 |
|---|---|---|
| **ASSETS** | | |
| **Mortgage Notes Receivable:** | | |
| Mortgage notes receivable | $ 5,507,459 | $ 1,355,717 |
| Mortgage participations | (4,086,060) | (457,435) |
| Loan discounts | - | (11,816) |
| Allowance for losses | - | (189,675) |
| | 1,421,399 | 696,791 |
| Cash and cash equivalents | 18,032 | 58,539 |
| Restricted certificate of deposit | - | 403,264 |
| Accrued interest receivable, net of participated interest payable of $898 and allowance of $627,612 at December 31, 2006 | - | 11,963 |
| Advances to affiliate | 113,640 | 137,000 |
| Investment in affiliates | 192,677 | 402,677 |
| Prepaid expenses | - | 7,922 |
| | **$ 1,745,748** | **$ 1,718,156** |
| **LIABILITIES AND SHAREHOLDERS' EQUITY** | | |
| **Liabilities:** | | |
| Accounts payable and accrued expenses | $ 23,409 | $ 63,154 |
| Participation in excess of mortgage notes receivable | - | 405,499 |
| Participated interest payable, net of accrued interest receivable of $893,332 and allowance of $676,604 at December 31, 2007 | 17,480 | - |
| Notes payable | 98,469 | 27,267 |
| Preferential 9% cumulative mandatorily redeemable shares of beneficial interest | 950,000 | 950,000 |
| | 1,089,358 | 1,445,920 |
| **Shareholders' Equity:** | | |
| Shares of beneficial interest, no par value, unlimited shares authorized, 1,404,232 shares issued and outstanding at December 31, 2007 and 2006 | 1,336,119 | 1,336,119 |
| Accumulated deficit | (679,729) | (1,063,883) |
| | 656,390 | 272,236 |
| | **$ 1,745,748** | **$ 1,718,156** |

(See Notes to Financial Statements)

# HOLLY MORTGAGE TRUST
## STATEMENT OF OPERATIONS
### For the Years Ended December 31, 2007 and 2006

| | 2007 | 2006 |
|---|---|---|
| **Revenue:** | | |
| Interest income | $ 411,775 | $ 93,062 |
| Other income | 198,184 | 186,761 |
| | 609,959 | 279,823 |
| **Costs and Expenses:** | | |
| General and administrative | 120,718 | 94,807 |
| Interest expense | 105,087 | 87,669 |
| | 225,805 | 182,476 |
| Net income | **$ 384,154** | **$ 97,347** |
| Weighted average shares outstanding | **1,404,232** | **1,404,232** |
| Net income per share, basic and diluted | **$ 0.27** | **$ 0.07** |

(See Notes to Financial Statements)

**HOLLY MORTGAGE TRUST**
**STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY**
**For the Years Ended December 31, 2007 and 2006**

| | Shares of Beneficial Interest | | Accumulated | Shareholders' |
|---|---|---|---|---|
| | **Number** | **Amount** | **Deficit** | **Equity** |
| **Balance,** December 31, 2005 | 1,404,232 | $ 1,336,119 | $ (1,161,230) | $ 174,889 |
| Net income | - | - | 97,347 | 97,347 |
| **Balance,** December 31, 2006 | 1,404,232 | 1,336,119 | (1,063,883) | 272,236 |
| Net income | - | - | 384,154 | 384,154 |
| **Balance,** December 31, 2007 | **1,404,232** | **$ 1,336,119** | **$ (679,729)** | **$ 656,390** |

(See Notes to Financial Statements)

# HOLLY MORTGAGE TRUST
# STATEMENT OF CASH FLOWS
## For the Years Ended December 31, 2007 and 2006

| | 2007 | 2006 |
|---|---|---|
| **Cash Flows from Operating Activities:** | | |
| Net income | $ 384,154 | $ 97,347 |
| Adjustments to reconcile net income to net cash used in operating activities: | | |
| Amortization of loan discounts | (11,816) | (12,217) |
| Accrued investment income | - | (149,199) |
| Bad debt recovery | (189,675) | - |
| Changes in operating assets and liabilities: | | |
| Accrued interest receivable | (356,057) | (2,133) |
| Prepaid expenses | 7,922 | (7,922) |
| Accounts payable and accrued expenses | (39,745) | 29,343 |
| Total adjustments | (589,371) | (142,128) |
| Net cash used in operating activities | (205,217) | (44,781) |
| **Cash Flows from Investing Activities:** | | |
| Mortgage notes originated | (4,400,000) | (525,000) |
| Mortgage note participations sold | 3,465,500 | 350,000 |
| Principal collected on mortgage notes receivable, net of participation | 391,384 | 372,969 |
| Advance to affiliate | - | (97,000) |
| Collection on advance to affiliate | 23,360 | - |
| Investment in affiliate | - | (200,000) |
| Return of investment in affiliate | 210,000 | - |
| Purchase of certificate of deposit | - | (4,652) |
| Redemption of certificate of deposit | 403,264 | - |
| Net cash provided by (used in) investing activities | 93,508 | (103,683) |
| **Cash Flows from Financing Activities:** | | |
| Stock escrow advance | - | 13,606 |
| Proceeds from note payable | 530,000 | 36,000 |
| Payments on note payable | (458,798) | (61,000) |
| Net cash provided by (used in) financing activities | 71,202 | (11,394) |
| Decrease in cash and cash equivalents | (40,507) | (159,858) |
| **Cash and Cash Equivalents**, beginning of year | 58,539 | 218,397 |
| **Cash and Cash Equivalents**, end of year | **$ 18,032** | **$ 58,539** |

(See Notes to Financial Statements)

**HOLLY MORTGAGE TRUST**
**STATEMENT OF CASH FLOWS (CONTINUED)**
**For the Years Ended December 31, 2007 and 2006**

| | 2007 | 2006 |
|---|---|---|
| **Supplemental Information:** | | |
| Cash paid for interest | **$ 105,087** | **$ 87,669** |
| **Non-Cash Investing and Financing Activities:** | | |
| Mortgage note received as payment for accrued interest | **$ 385,500** | |

(See Notes to Financial Statements)

**HOLLY MORTGAGE TRUST**
**NOTES TO FINANCIAL STATEMENTS**
**December 31, 2007**

## NOTE 1 - ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES

### Nature of Organization

Holly Mortgage Trust (the "Trust") was organized as a Massachusetts business trust on January 2, 1998, with a termination date of January 2, 2013. The Trust is engaged primarily in the business of investing in second mortgages and equity participation mortgages. First Commonwealth Holdings Corporation ("FCHC"), whose principal shareholder is a trustee and shareholder of the Trust, is the Trust's compensated manager.

### Cash and Cash Equivalents

The Trust considers all highly liquid investments with an original maturity of three months or less to be cash equivalents.

### Mortgage Notes Receivable

Mortgage notes receivable are carried at unpaid principal balances since generally it is management's intention to hold mortgage notes to maturity. Commitment and origination fees collected from prospective borrowers are deferred and recognized as income using a method approximating the interest method over the life of those loans.

A loan is considered impaired when it is probable that the scheduled principal or interest will not be collected when due. Impaired loans are measured based on the present value of expected future cash flows discounted at the loan's effective interest rate, or collateral fair value, if the loan is collateral dependent. If the measure of the impaired loan is less than the recorded investment in the loan, an impairment loss is recognized through a valuation allowance and a corresponding charge to income.

### Allowance for Losses

The allowance for losses is based on management's estimate of the amount required to maintain an allowance adequate to reflect the risks inherent in the loan portfolio after giving consideration to existing economic conditions, loss experience in relation to outstanding loans, changes in the loan portfolio, borrowers' performance in reducing loan principal, adequacy of loan collateral, and other relevant factors.

### Interest Income

Interest income on loans is accrued based upon the principal amount outstanding. If a loan is placed on nonaccrual status, interest previously recognized but uncollected is reversed and charged against current income. Subsequent interest collected on such a loan is credited to principal if, in the opinion of management, collectibility of principal is doubtful; otherwise, the interest collected is recognized as revenue.

## NOTE 1 - ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

### Concentrations of Credit Risk

The Trust's primary business activity is investing in loans collateralized by mortgages on real estate. These loans are principally collateralized by real estate in Florida and California.

The Trust maintains cash balances in a bank that at times, exceeds federal insured limits. The Trust monitors the financial condition of the bank and has experienced no losses associated with this account.

### Net Income Per Share

Net income per share is calculated by dividing net income by the weighted average number of shares of beneficial interest outstanding during the year. Earnings per share, both basic and diluted, are the same.

### Management 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 that affect the reported amounts of assets and 1iabilities at the dates of the financial statements and the reported amounts of revenues and expenses during the reporting period. Such estimates include the value of collateral and, therefore, the resulting allowance for losses. Actual results could differ from those estimates. Management believes that these estimates and assumptions provide a reasonable basis for the fair presentation of the financial statements.

## NOTE 2 - MORTGAGE NOTES RECEIVABLE AND COMMITMENTS

Notes receivable from funding mortgage loans are principally collateralized by second mortgage loans on commercial or residential property and are due at various dates, with the latest maturity due in October 2010. Notes receivable bear interest at rates generally ranging from prime (7.25% at December 31, 2007) to 18%.

There were no commitments to lend additional funds at December 31, 2007.

## NOTE 3 - NOTES PAYABLE

Notes payable at December 31, 2007 and 2006 consist of the following:

| | 2007 | 2006 |
|---|---|---|
| Unsecured note payable to an individual, bearing interest at 8%, principal and interest due monthly. Maturity in September 2007 | $ - | $27,267 |

**NOTE 3 - NOTES PAYABLE (CONTINUED)**

| | 2007 | 2006 |
|---|---|---|
| Unsecured note payable to an individual, bearing interest at 8%, principal and interest due monthly. Maturity in December 2008 | $48,469 | $ - |
| Unsecured note payable to an individual, bearing interest at 8%, interest due monthly. Due on demand or at maturity in January 2010 | 50,000 | - |
| | $98,469 | $27,267 |

**NOTE 4 - FEDERAL INCOME TAXES**

The Trust operates in such a manner to qualify as a "real estate investment trust" under Sections 856 through 860 of the Internal Revenue Code of 1986, as amended, and the Treasury Regulations promulgated thereunder. Under those sections, the Trust will not be taxed on that portion of its qualifying income distributed to shareholders so long as at least 90% of the Trust's otherwise taxable income is distributed to shareholders each year and other requirements of a qualified real estate investment trust are met. The Trust satisfied the income distribution requirements for the years ending December 31, 2007 and 2006. Management believes that all other requirements of a qualified real estate investment trust have been met. For tax purposes, interest on the mandatorily redeemable shares of beneficial interest is treated as dividends.

The tax status of per-share dividend distributions declared attributable to the years presented is as follows:

| | 2007 | 2006 |
|---|---|---|
| Ordinary income | $0.09 | $0.09 |

**NOTE 5 - SHAREHOLDERS' EQUITY**

Except for the rights and preferences in payment of dividends and in liquidations, the Preferential Shares of Beneficial Interest ("Preferential Shares") have the same voting and other rights as the Shares of Beneficial Interest ("Common Shares"). The Preferential Shares are entitled to receive cumulative preferential dividends at the annual rate of nine cents ($0.09) per share before any dividends are paid on the Common Shares.

In the event of liquidation of the Trust, the assets available for distribution will be distributed first to the holders of the Preferential Shares up to one dollar ($1) per share plus any deferred dividends, then second to the holders of Common Shares up to one dollar ($1) per share and then equally on all of the shares of Preferential and Common Shares.

The Preferential Shares are subject to redemption at any time after January 1, 2009 upon not less than thirty days' prior written notice, in whole or in part, at the election of the Trust at the redemption price of one dollar ($1) per share plus all unpaid dividends accrued to the redemption date. Any Preferential Shares outstanding on September 30, 2014 will be redeemed on that date.

**NOTE 5 - SHAREHOLDERS' EQUITY (CONTINUED)**

During 2003, the Financial Accounting Standards Board ("FASB") issued FASB Statement No. 150 ("FAS 150"), *Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity*. This statement establishes standards for how an issuer classifies and measures certain financial instruments with characteristics of both liabilities and equity. This statement requires an issuer to classify a financial instrument issued in the form of shares that is mandatorily redeemable and embodies an unconditional obligation to redeem it by transferring its assets at a specified or determinable date or upon an event that is certain to occur as liabilities. The Trust has adopted these provisions in their financial statements and has included mandatorily redeemable preferred stock in liabilities on the accompanying balance sheet and dividends on the mandatorily redeemable preferred stock as interest expense in the accompanying statement of operations.

**NOTE 6 - MANAGEMENT AGREEMENT AND RELATED PARTY TRANSACTIONS**

The Trust is managed by FCHC, whose principal shareholder is a trustee and shareholder of the Trust. Effective January 1, 2007, a management fee is incurred based on the greater of $50,000 or 1.4% of the book value of the assets of the Trust at the end of each fiscal year. Prior to 2007, a management fee was incurred on approximately 1% of the book value of the assets of the Trust at the end of each fiscal year. The management fees for the years ended December 31, 2007 and 2006 were approximately $50,000 and $20,000, respectively.

At December 31, 2007 and 2006, the Trust had advanced $113,640 and $137,000, respectively, to Wilco Building Partners, Ltd. (See Note 8.)

At December 31, 2007, the Trust also had a mortgage note receivable due from Wilco Building Partners, Ltd. of $105,980, which is included in mortgage notes receivable on the balance sheet.

During the year 2007, the Trust engaged in three mortgage participation payables with an affiliated business trust. At December 31, 2007, the Trust had two outstanding mortgage participation payables that totaled $735,500 and is included in mortgage notes receivable, net on the balance sheet. The participations incur interest at rates ranging from 8% to 11% and maturity dates ranging from January 30, 2008 to July 31, 2010. Interest on such participations paid to the affiliates amounted to approximately $28,000 for the year ended December 31, 2007.

During the year 2006, the Trust engaged in two mortgage participation payables with an affiliated business trust. At December 31, 2006, the Trust had one outstanding mortgage participation payable that totaled $350,000 and is included in mortgage notes receivable, net on the balance sheet. The participation incurs interest at 11%, with a maturity date of September 30, 2007. Interest on such participations paid to the affiliates amounted to approximately $32,000 for the year ended December 31, 2006.

## NOTE 7 - MAJOR LOANS

At December 31, 2007, one mortgage note receivable represented approximately 71% of total mortgage notes receivable and related participations payable represented approximately 75% of total participations payable. Interest related to this note and one other note was approximately 74% of total interest income for the year ended December 31, 2007.

At December 31, 2006, three mortgage notes receivable represented approximately 81% of total mortgage notes receivable and related participations payable represented 100% of total participations payable. Interest related to these notes was approximately 76% of total interest income for the year ended December 31, 2006.

## NOTE 8 - INVESTMENT IN AFFILIATES

The Trust owns 100% of the common stock of A. R. Goldrick Company, Inc. (a C corporation) (A. R. Goldrick). A. R. Goldrick is the general partner of Wilco Building Partners, Ltd., a limited partnership which owns and operates an office building in Midland, Texas. The financial statements of A. R. Goldrick have not been consolidated with those of the Trust. The investment in A. R. Goldrick was deemed by the Trust's management to be impaired and the investment's carrying value was $0 at December 31, 2005. In 2006, the Trust recognized approximately $149,000 in income from A. R. Goldrick which is included in other income. In addition, the Trust made a capital contribution in 2006 of $200,000 to A. R. Goldrick. In 2007, the Trust received a return of capital of $210,000 from A. R. Goldrick. The investment at December 31, 2007 is secured by notes receivable totaling $290,000.

The Trust owns 50 partnership units of Global REIT, L.P. The Trust accounts for this investment using the cost method of accounting. The cost of this investment was $53,478 at December 31, 2007 and 2006.

## NOTE 9 - CORRECTION OF AN ERROR

The 2006 financial statements have been restated for the accounting of dividends on the mandatorily redeemable shares of beneficial interest. Prior to 2007, the distributions on the mandatorily redeemable shares of beneficial interest were recorded as dividends. In accordance with FAS 150, these dividends should have been recorded as interest expense. As a result, $85,500 of dividends in 2006 has been reclassed as interest expense. Net income for 2006 decreased by $85,500. The change in accounting had no effect on accumulated deficit at December 31, 2005.

**TRANSFER AGENT**

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