400 Sibley Street | Suite 300 | Saint Paul, MN 55101-1998 | 651.296.7608
800.657.3769 | fax: 651.296.8139 | tty: 651.297.2361 | www.mnhousing.gov
Equal Opportunity Housing and Equal Opportunity Employment

DATE: August 23, 2012

TO: Minnesota Housing Board Members

FROM: Mary Tingerthal
Commissioner

SUBJECT: **AUDIT COMMITTEE MEETING**

A meeting of the **Audit Committee** has been scheduled for **11:30 a.m.,** on **Thursday, August 30** at the offices of Minnesota Housing, 400 Sibley Street, Suite 300, St. Paul, MN in the **State Street Conference Room on the first floor**.

The topic for discussion at this meeting is:

A. Discussion, Presentation of Annual Financial Report, Annual Financial Audit and Federal Single Audit.
B. Discussion, Post Sale Report for Homeownership Finance Bonds 2012 Series A.
C. Discussion, Funding Options for Single Family First Mortgage Production.
D. Approval, Fiscal 2012 Interfund Transfers.

All members are invited to attend.

If you have questions, please call Becky Schack at (651) 296-2172.

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AGENDA ITEM: 6.A
MINNESOTA HOUSING BOARD MEETING
August 30, 2012

ITEM: Fiscal Year 2012 Financial Results, Financial Audit, and Federal Program Single Audit

CONTACT:
Jim Cegla, 651-297-3126
Jim.Cegla@state.mn.us

Terry Schwartz, 651-296-2404
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Bill Kapphahn, 651-215-5972
William.Kapphahn@state.mn.us

Don Wyszynski, 651-296-8207
Don.Wyszynski@state.mn.us

REQUEST:

☐ Approval ☑ Discussion ☐ Information

TYPE(S):

☑ Administrative ☐ Commitment(s) ☐ Modification/Change ☐ Policy ☐ Selection(s) ☐ Waiver(s)

☐ Other: _____

ACTION:

☐ Motion ☐ Resolution ☑ No Action Required

SUMMARY REQUEST:
Staff will present and discuss fiscal year 2012 financial results. CliftonLarsonAllen, the Agency's external auditors, will present and discuss the results of their fiscal year 2012 financial statement audit, federal program single audit, and information technology review.

FISCAL IMPACT:
None.

MEETING AGENCY PRIORITIES:

☐ Promote and support successful homeownership ☐ Preserve federally-subsidized rental housing

☐ Address specific and critical needs in rental housing markets

☐ Prevent and end homelessness ☐ Prevent foreclosures and support community recovery

ATTACHMENT(S):
None. All materials will be distributed at the Audit Committee meeting on August 30, 2012.

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AGENDA ITEM: 6.B.
MINNESOTA HOUSING AUDIT COMMITTEE
August 30, 2012

ITEM: Post-Sale Report, Homeownership Finance Bonds, 2012 Series A

CONTACT: Don Wyszynski, 651-296-8207
don.wyszynski@state.mn.us

REQUEST:

☐ Approval ☑ Discussion ☐ Information

TYPE(S):

☐ Administrative ☐ Commitment(s) ☐ Modification/Change ☐ Policy ☐ Selection(s) ☐ Waiver(s)

☑ Other: Finance

ACTION:

☐ Motion ☐ Resolution ☑ No Action Required

SUMMARY REQUEST:
The Agency sold $50,000,000 of Homeownership Finance Bonds on July 31, 2012 to provide financing for its single family mortgage program. Pursuant to Debt Management Policy, the attached post-sale report is provided by the Agency's financial advisor, CSG Advisors, as an information item at the Board Meeting. This is an information item and does not require approval.

FISCAL IMPACT:
None.

MEETING AGENCY PRIORITIES:

☑ Promote and support successful homeownership ☐ Preserve federally-subsidized rental housing

☐ Address specific and critical needs in rental housing markets

☐ Prevent and end homelessness ☐ Prevent foreclosures and support community recovery

ATTACHMENT(S):
Post-Sale Report

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$50,000,000
Minnesota Housing Finance Agency
Homeownership Finance Bonds
2012 Series A
(GNMA Pass-Through Program)

POST-SALE ANALYSIS

KEY RESULTS FOR MHFA

Purpose. This transaction was a nationally innovative approach to issue single-family tax-exempt bonds at a low enough yield for MHFA to finance its loans at approximately full spread.

Without the New Issue Bond Program, no housing finance agency had been able to achieve this on an all new money issue in recent years. Conventional mortgage rates have dropped to historic low levels as global investors purchase federally guaranteed mortgage-backed securities. Interest rates on long-term tax-exempt housing bonds have not dropped nearly as much, resulting in loan rates far above the level at which an HFA can compete with conventional rates.

Until Series A, the only way MHFA or other HFAs could offer competitive rates had been by combining new tax-exempt bonds with zero participations from prior issues or with savings from refunding old bonds.

As such, Series A was designed to:

- Finance $50 million of single-family loans in MHFA's pipeline that have an average interest rate of 3.7%, and
- Earn full spread while minimizing the use of MHFA's $18 million of existing zero participations, so they can be used on future transactions, and
- Test out a new approach to selling and structuring bonds to make this possible, by designing them to be very similar to taxable GNMA securities.

Accomplishments. Each of these objectives was very successfully achieved.

1. **Finance New Loans at Full Spread Without Using Existing Zero Participations.** Series A financed $50 million of pipeline loans, did not require any zero participations, and even generated a modest additional $250,000 of new zero participations. This *preserves the amount of subsidy available for future bond issues.*

2. **Provide a New, Very Successful Way of Selling Single Family Bonds.** MHFA was able to publicly sell its tax-exempt bonds at a yield of 2.60%. This is approximately 80 to 90 basis points below where MHFA or any other AAA single-family issuer has been able to achieve on other transactions.

Bond Results. Following are key highlights.

1. **Approach.** Based on feedback from RBC's customers, there was potentially extraordinary interest by investors who normally buy taxable mortgage-backed securities – if MHFA could

structure a financing that looked very similar to those securities. MHFA therefore designed the issue so that:

- the bonds would exactly equal the same amount of new GNMA securities;
- at bond closing, the investor would know the specific GNMA securities backing the bonds, and would then be able to track the payments and prepayments on those specific securities just as if they were buying individual taxable securities;
- interest and principal is paid monthly (rather than semi-annually on almost all other housing bonds);
- all principal received each month on those GNMA securities – both regularly scheduled loan payments and loan prepayments – would be passed through to the investor on the 1st of the following month;
- the minimum denomination is $0.01 rather than $5,000, so bonds can be redeemed from exactly all principal received;
- the Trustee does not have to give 30 days notice of redemption, but simply passes through the principal actually received without a formal notice requirement;
- each investor would thus receive monthly its pro rata share of the interest and principal on those specific GNMA securities, very much as if they had simply purchased a participation in taxable securities.

In order to structure bonds in this way, MHFA issued the bonds under its newer Homeownership Finance Bonds (NIBP) Indenture rather than its Residential Housing Finance Bond (RHFB) indenture. This also avoided any concerns investors might have had about the variable rate debt in the RHFB indenture.

2. **Benefits to Investors.** The approach outlined thus allows an investor to purchase a housing bond that is very similar to buying taxable securities. MHFA provided two benefits, however, that were not available on taxable securities:

   - MHFA's bonds were sold at par, whereas to buy new GNMA securities with similar underlying loans an investor would normally have to pay a very large up-front premium in today's market, often 6 to 8 points. The investor thus avoids the risk of early prepayments wiping out the value of its premium.
   - MHFA's bonds are, of course, tax-exempt. For corporate or bank investors in a marginal 35% tax bracket, the 2.6% yield is equivalent to a 4% yield on taxable securities, far higher than they can achieve in the taxable markets.

3. **Timing.** MHFA's timing turned out to be excellent. The bonds were sold on July 31st, when 10 year Treasury yields and taxable mortgage-backed security yields were within a few basis points of the lowest yields ever achieved.

4. **Successful Sale.** The sale proved very favorable, allowing MHFA to lower yields significantly from its initial expected level of 2.75%, to price bonds at 2.625%. There was a very high level of interest, with 14 investors providing approximately $195 million of orders. The bond yield was then lowered to 2.60%. A typical tax-exempt bond structure in the same market would have had a bond yield of approximately 3.50%.

Measuring Transaction Benefits to MHFA. MHFA's key objective was to permanently finance loans already in its pipeline at the lowest cost possible, achieve full spread and minimize the use of zero participations.

1. **Zero Participations.** The Agency earned full spread on the $50 million of new loans and slightly increased its zero participations (extra interest rate spread above the maximum spread allowed of 1.125% under the tax code) for future issues by $250,000. This leaves MHFA with approximately $18 million of zeroes, offering financing flexibility in structuring future issues and reducing interest rate risk on future production.

2. **All of the Agency's New Issue Guidelines Were Exceeded**:

Criteria	Execution
Better than 1.00% spread for the Agency	Full allowable spread of 1.125% (plus generating $250,000 of new zero participations)
No more than 40% variable rate	None
Expected swap life less than 26 years	No swap
Manage unhedged bond risk	None
Manage liquidity risk	None
Provides mortgage rate which meets Agency needs	Funds loans already in pipeline or to be reserved at a full spread

FEATURES OF THIS ISSUE

Structure. The bond structure most closely resembles monthly pass-through single-family bonds that were sold to Fannie Mae about 15 years ago by a few state and local HFAs.

1. **Non-AMT Bonds.** All bonds were Non-AMT.

2. **Single Maturity.** All bonds mature in 2042 (e.g., 30 years after closing). There were no serial bonds, PAC bonds or any of the other structures normally found in housing bond issues, to try to allocate tranches to investors based on maturity or prepayment speed. Instead, each investor owns and receives a pro rata share of all principal and interest.

Pricing. Because this was a single maturity of monthly pass-through bonds, there was no retail order period or priority, but rather a single institutional order period. Pricing took place after several weeks of intense pre-marketing by RBC to identify and approach potential investors who might be interested in this new product.

1. **Strong Institutional Demand.** MHFA attracted strong support from institutional investors and was oversubscribed by 3.9 times.

UNDERWRITING

Underwriting Fees. Takedowns were established at lower levels than industry standards or MHFA precedent on long-term tax-exempt bond sales. Management fees were appropriate, consistent with industry standards, and in the same range as fees reported for other housing issues of similar size and structure.

Comparable Transactions. Single-family transactions in the prior month included Virginia, SONYMA (only very short maturities), Montana and Tennessee. Of these, the only one which financed new loans with 30 year bonds was Virginia. Virginia generally trades extremely tight to MMD; it was sold the same week as Minnesota, on a competitive basis, and resulted in a bond yield approximately 80 basis points higher than Minnesota's.

Performance. All orders were taken by RBC for the benefit of the group of 3 managers (RBC, Morgan Stanley and Piper Jaffray). Because there were no retail orders, a rotating co-manager was not needed or utilized on this issue.

IMPLICATIONS

Future Issues. The significant institutional interest in this product provides an excellent precedent for MHFA to seek to continue to use this structure in the future. The constraints on future issues are from supply rather than demand. On this issue, MHFA needed to be able to identify all GNMAs to be included in the issue that was closing approximately 30 days after pricing. MHFA was thus limited to GNMAs about to be formed or those already existing before pricing. In the future, it should be possible to extend the time from pricing to closing to approximately 60 days. If this is possible, MHFA should routinely be able to finance about 2 months of GNMA production (or about $50 - $60 million) every two months.

This structure provides an alternative to GNMA taxable market sales. A new single-family strategy will determine how best to use such taxable market sales (such as for loans which do not meet tax-exempt requirements) alongside this type of bond structure. Naturally, since the structure is new, the ultimate level of continuing demand cannot be known, nor how long this level of demand for such bonds (and for taxable mortgage backed securities) will continue at these levels.

Thus, there is no assurance that this structure can be repeated in the future. But it offers, for the first time in several years, at least one viable alternative that MHFA can use – alongside taxable market sales – to continue to finance its loan production in an efficient and profitable manner.

ISSUE DETAILS

Key Dates: 2012 A Bond Pricing:

Institutional Order Period:	Tuesday morning, July 31, 2012
Closing Date:	August 28, 2012

Use of Proceeds. The bond issue provides $50 million to purchase GNMA mortgage-backed securities. The average rate on the loans is expected to be approximately 3.70%.

Market Conditions

Treasuries. Long term treasury bond yields dropped to record low levels in 2011 and early 2012 reflecting ongoing bank and sovereign debt crises in Europe, weak economic recovery in the U.S., the paradoxical impact of S&P's downgrade of the U.S. government, and the announcement of the Federal Reserve's policy of maintaining near-zero short-term rates through 2014. U.S. Treasury bond yields increased slightly in March with signs of economic recovery but then have dropped to record low levels due to global worries over euro zone credit, first Greece, then Spain.

This extended flight to safety brought 10 year treasuries from 2.30% on April 3 to 1.51% at pricing, far below the starting level for the year of 1.97%. (The all-time low was 1.43% on July 25). Similarly, 30 year Treasuries dropped from 3.41% on April 3 to 2.56% at pricing, far below the starting level for the year of 2.98%. The year starting levels of approximately 2% and 3% seemed like expected floors for the year, but the Eurozone crisis continues to dramatically increase demand for treasuries.

Municipals. Municipal yields have generally followed Treasury yields but more moderately. Other factors include:

- Volume of new issuance continues at low levels, although supply has increased somewhat over the last few months, including from refunding opportunities.
- Despite the absolute low level of rates, buyers have adjusted and there has been ongoing and renewed retail and institutional interest.
- Despite the low absolute level of rates, credit spreads continue to be relatively wide with a spread of approximately [100] basis points between the AAA 30-year G.O. MMD index and A-rated G.O.s.
- As a result of the extraordinary rally in treasuries, municipal bonds have again become very cheap to treasuries. While the 10 year Treasury yield went down by 69 basis points since 2012 ABCD in March, 10 year MMD dropped by less than half as much, 31 basis points. MMD is back to approximately 110% of Treasury (a very high historic level).

Issue	Date	10-Year Treasury	10-Year MMD	MMD/ Treasury Ratio	30-Year Treasury	30-Year MMD	MMD/ Treasury Ratio
2010 A*	9/15/10	2.67%	2.39%	89.5%	3.79%	3.72%	98.2%
2011 A/B*	3/22/11	3.34%	3.27%	97.9%	4.44%	4.85%	109.2%
2011 C/D*	6/7/11	3.01%	2.63%	87.4%	4.27%	4.23%	99.1%
2011 E*	8/24/11	2.29%	2.26%	98.7%	3.63%	3.89%	107.2%
2011 F/G*	11/22/11	1.94%	2.18%	112.4%	2.91%	3.83%	131.6%
2012 ABCD**	3/27/12	2.20%	1.97%	89.5%	3.29%	3.34%	101.5%
2012 A*	7/31/12	1.51%	1.66%	109.9%	2.56%	2.84%	110.9%
Change from 2012 ABCD to 2012 A		**- 69 bps**	**- 31 bps**	**+ 20.4%**	**- 73 bps**	**- 50 bps**	**+ 9.4%**

- Homeownership Finance Revenue Bond Indenture

** Residential Housing Finance Bond Indenture (RHFB)

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Minnesota Housing Finance Agency
Homeownership Program Bonds, 2012 Series A
Final Pricing Comparables (Non-AMT)

SALE DATE	July 31, 2012		July 26, 2012		July 25, 2012		July 24, 2012		July 11, 2012	
ISSUER	Minnesota HFA		Washington State HFC		NYS HFA		Virginia H.D.A.		SONYMA	
AMOUNT	$50,000,000		$11,100,000		$45,500,000		$39,075,000		$120,000,000	
SERIES	2012 Series A		Desert Villa Apts		2012 Series B		2012 Series B		Series 173 and 174	
PROGRAM	Single Family / Negotiated		**Multifamily** / Negotiated		**Multifamily** / Negotiated		**Multifamily** / **Competitive**		Single Family / Negotiated	
RATING(S)	Aaa / - / -		- / AA+ / -		Aa2 / - / -		Aa1 / - / -		Aa1 / - / -	
TAX STATUS	**Non-AMT**		**Non-AMT**		**Non-AMT**		**Non-AMT**		**Non-AMT**	
MATURITY	Coupon or Yield	Spread to MMD	Coupon or Yield	Spread to MMD	Coupon or Yield	Spread to MMD	Coupon or Yield	Spread to MMD	Coupon or Yield	Spread to MMD
2012					0.25	+5			0.19	-1
2013			0.70	+51	0.30 / 0.45	+10			0.23	+3
2014			0.85	+56	0.65 / 0.75	+34	0.45	+14		
2015			1.05	+67	0.90 / 1.00	+49	0.75	+34		
2016			1.30	+82	1.10 / 1.20	+59	0.90	+39		
2017			1.50	+87	1.40 / 1.50	+75	1.125	+48		
2018			1.75	+90	1.75 / 1.85	+88	1.50	+62		
2019			2.00	+92	1.95	+86	1.75	+65		
2020			2.25	+96	2.15 / 2.20	+85	2.00	+69		
2021			2.45	+97	2.40	+91	2.25	+75		
2022			2.60	+100	2.65	+104	2.375	+76		
2023					2.80	+106	2.625	+88		
2024					2.85 / 2.90	+102	2.75	+90		
2025					2.95 / 3.00	+103	2.875	+94		
2026			3.10	+109	3.05	+104				
2027					3.10	+101	3.00	+89		
2028										
2029										
2030			3.35	+105						
2031							3.25	+86		
2032					3.45	+101				
2033										
2034										
2035										
2036										
2037					3.75	+101	3.50	+75		
2038										
2039										
2040										
2040										
2041										
2042	2.60	+115*			3.85	+106	3.625	+83		
2043										
2045										
2046										
2048										
2051										
2053 / 2054										
	* Structure is a GNMA Monthly-Pass Through structure. Market for structure is still developing, but the +115 spread listed is to the 8.63 yr A/L assuming 150% PSA.						TIC of 3.388694%.			
MKT INDEX	BBI / RBI	3.61% / 4.44%	BBI / RBI	3.61% / 4.44%	BBI / RBI	3.75% / 4.51%	BBI / RBI	3.75% / 4.51%	BBI / RBI	3.94% / 4.65%
SEN MGR	RBC Capital Markets		Citigroup		JP Morgan		Raymond James Morgan		Morgan Stanley	

CSG | advisors

Minnesota Housing Finance Agency
Homeownership Program Bonds, 2012 Series A
Final Pricing Comparables (Non-AMT)

SALE DATE	July 31, 2012		July 11, 2012		July 11, 2012		July 2, 2012		June 27, 2012	
ISSUER	Minnesota HFA		Maryland Dept of HCD		Montana Board of Housing		Colorado HFA		Tennessee H.D.A.	
AMOUNT	$50,000,000		$9,340,000		$20,065,000		$10,500,000		$105,825,000	
SERIES	2012 Series A		2012 Series A		2012A-1		2012 Series A		2012-1BC	
PROGRAM	Single Family / Negotiated		**Multifamily** / Negotiated		Single Family / Negotiated		**Multifamily** / Negotiated		Single Family / Negotiated	
RATING(S)	Aaa / - / -		Aa2 / AA+ / -		Aa3 / - / -		Aaa / AAA / -		Aa1 / AA+ / -	
TAX STATUS	**Non-AMT**		**Non-AMT**		**Non-AMT**		**Non-AMT**		**Non-AMT**	
MATURITY	Coupon or Yield	Spread to MMD	Coupon or Yield	Spread to MMD	Coupon or Yield	Spread to MMD	Coupon or Yield	Spread to MMD	Coupon or Yield	Spread to MMD
2012					0.375	+18				
2013										
2014			0.40 / 0.50	+8						
2015			0.75 / 0.85	+31						
2016			1.00 / 1.10	+46						
2017			1.35 / 1.50	+61						
2018			1.70 / 1.85	+70					1.90 / 1.95	+85
2019			2.05 / 2.10	+83					.2.15 / 2.20	+87
2020			2.35	+91					2.45	+93
2021			2.50	+87	2.70	+107			2.65	+93
2022			2.70	+93	2.85	+108	2.75	+90	2.80	+94
2023			2.85	+94	3.00	+109			3.00	+98
2024			2.95	+90	3.125	+108				
2025										
2026										
2027			3.40	+107	3.40	+107			3.50	+103
2028										
2029									3.65	+103
2030					3.60	+105				
2031										
2032			3.75	+106			3.90	+107		
2033										
2034										
2035										
2036										
2037			4.00	+103					PPAC 2.40*	+161
2038										
2039										
2040										
2040										
2041										
2042	2.60	+115*	4.05	+103			4.20	+104		
2043										
2045										
2046										
2048										
2051							4.50	+134		
2053 / 2054			4.375	+136						
	* Structure is a GNMA Monthly-Pass Through structure. Market for structure is still developing, but the +115 spread listed is to the 8.63 yr A/L assuming 150% PSA.								* Premium PAC yielding 2.40% with 5.00 yr A/L from 75% - 400% PSA. 4.50% coupon, $109.689 price.	
MKT INDEX	BBI / RBI	3.61% / 4.44%	BBI / RBI	3.94% / 4.65%	BBI / RBI	3.94% / 4.65%	BBI / RBI	3.95% / 4.69%	BBI / RBI	3.95% / 4.72%
SEN MGR	RBC Capital Markets		JP Morgan		RBC Capital Markets		RBC Capital Markets		Citi	

AGENDA ITEM: 6.C.
MINNESOTA HOUSING AUDIT COMMITTEE
August 30, 2012

ITEM: Financing Mechanisms for Single Family First Mortgage Production

CONTACT: Don Wyszynski, 651-296-8207
don.wyszynski@state.mn.us

REQUEST:

☐ Approval ☑ Discussion ☐ Information

TYPE(S):

☐ Administrative ☐ Commitment(s) ☐ Modification/Change ☐ Policy ☐ Selection(s) ☐ Waiver(s)

☑ Other: Finance

ACTION:

☐ Motion ☐ Resolution ☑ No Action Required

SUMMARY REQUEST:
Staff and representatives from CSG Advisors will discuss alternative financing mechanisms to support the Agency's single family first mortgage production.

FISCAL IMPACT:
The single family first mortgage lending programs have historically been major contributors of net revenue to the Agency. The discussion will focus on the ways the Agency can adapt to changing capital markets dynamics that will allow the Agency to maintain or increase production levels and agency profitability.

MEETING AGENCY PRIORITIES:

☑ Promote and support successful homeownership ☐ Preserve federally-subsidized rental housing

☐ Address specific and critical needs in rental housing markets

☐ Prevent and end homelessness ☐ Prevent foreclosures and support community recovery

ATTACHMENT(S):
Presentation Outline

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Financing Mechanisms for MHFA Single Family Production

Board Meeting Presentation

CSG | advisors

August 30, 2012

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Table of Contents

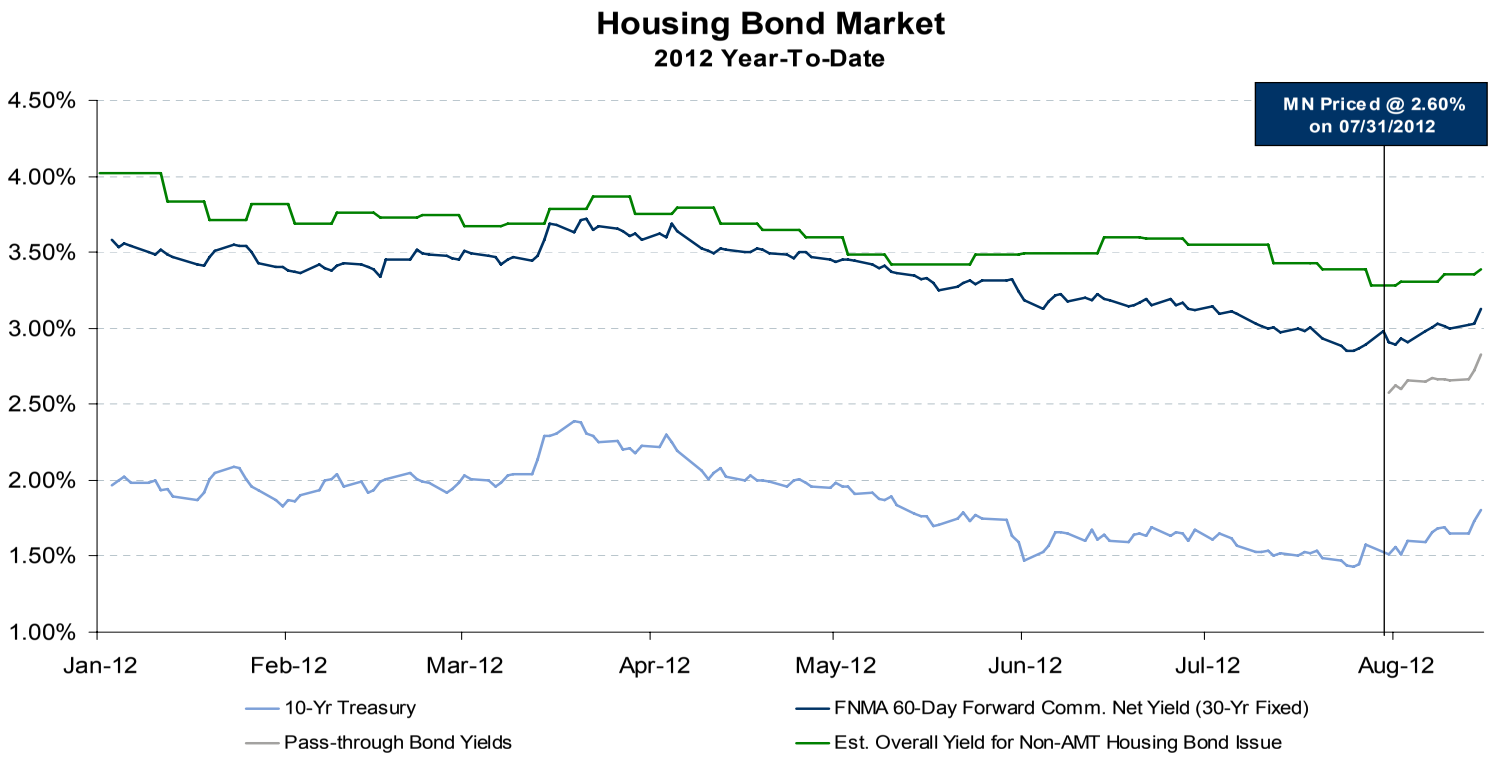
1. Changes in HFA Single Family Approaches
2. Selling Mortgage-Backed Securities
3. Interest Rate and Risk Management
4. MHFA Resources and Options
    a. Tax-exempt eligible borrowers
    b. Other borrowers
5. Potential MHFA Criteria

1. Changes in Financing Options

A. Highly competitive market for HFAs

- End of New Issue Bond Program
- Very low conventional mortgage rates
- Tax-exempt bonds above GNMAs and Fannie Maes
- How do HFAs remain useful, relevant and profitable?

1. Changes in Financing Options



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RBC Capital Markets®

1. Changes in Financing Options

HFA Approaches

HFA Sells	Creates an Attractive Rate	Minnesota Example
1. Tax-exempt bonds with – Savings from refunding old bonds – Zero participations	Subsidize tax-exempt bonds with (limited) resources that can only be used with bonds	2012 Series ABCD
2. Tax-exempt pass-through bonds	Structure tax-exempt bonds that look and perform like MBS	2012 Series A
3. Mortgage Backed Securities (MBS) in taxable market	Use same market as conventional mortgages	In planning

2. Selling Mortgage-Backed Securities

A. Range of HFA Activity

Status	Control Interest Rate Risk	Examples
Beginning to explore MBS rather than whole loans	Not yet started	New York, North Carolina
Pipeline and sell individual MBS	NIBP or cash invested long-term	Missouri
Large pipeline based on MBS sales	Hedges some or all production	Massachusetts, Colorado, Pennsylvania, Idaho, Utah

2. Selling Mortgage-Backed Securities

B. Keys to Successful Production (despite low conventional rates):

1. HFA lender network
2. Downpayment assistance
3. Fannie Mae preferred risk sharing
4. Potential to serve non-first time homebuyers (since taxable financing)
5. Different interest rates for different loan types

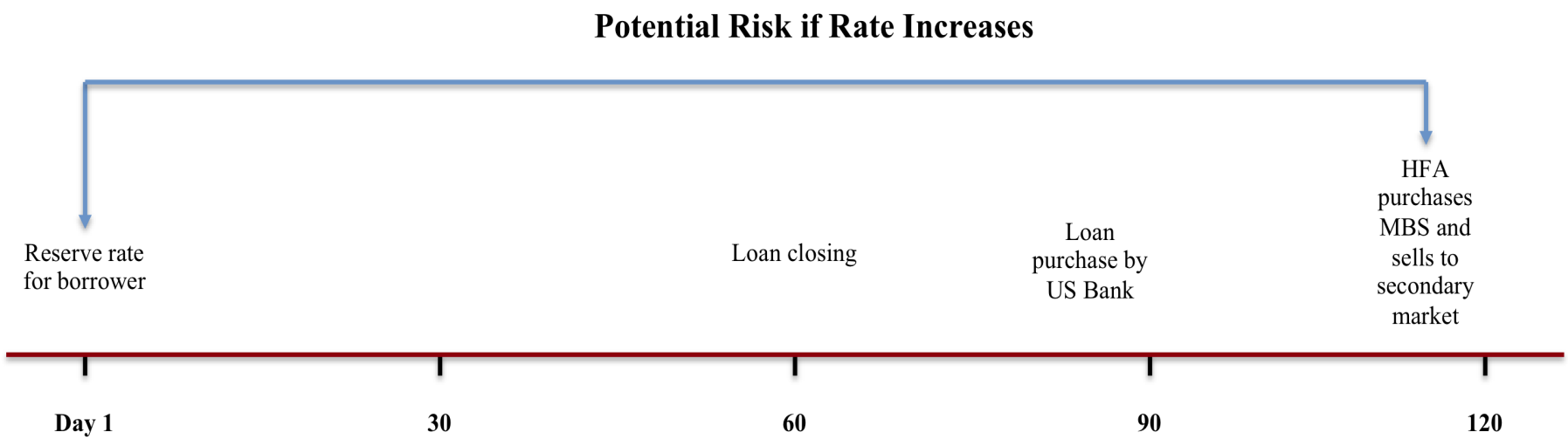
2. Selling Mortgage-Backed Securities

C. Market Will Change

1. Extremely attractive now for MBS sales
2. Opportunities will keep changing
3. MBS sales are one tool together with others for financing an ongoing program

3. Interest Rate and Risk Management

A. Timing: from reservation to MBS sale creates possible interest rate risk

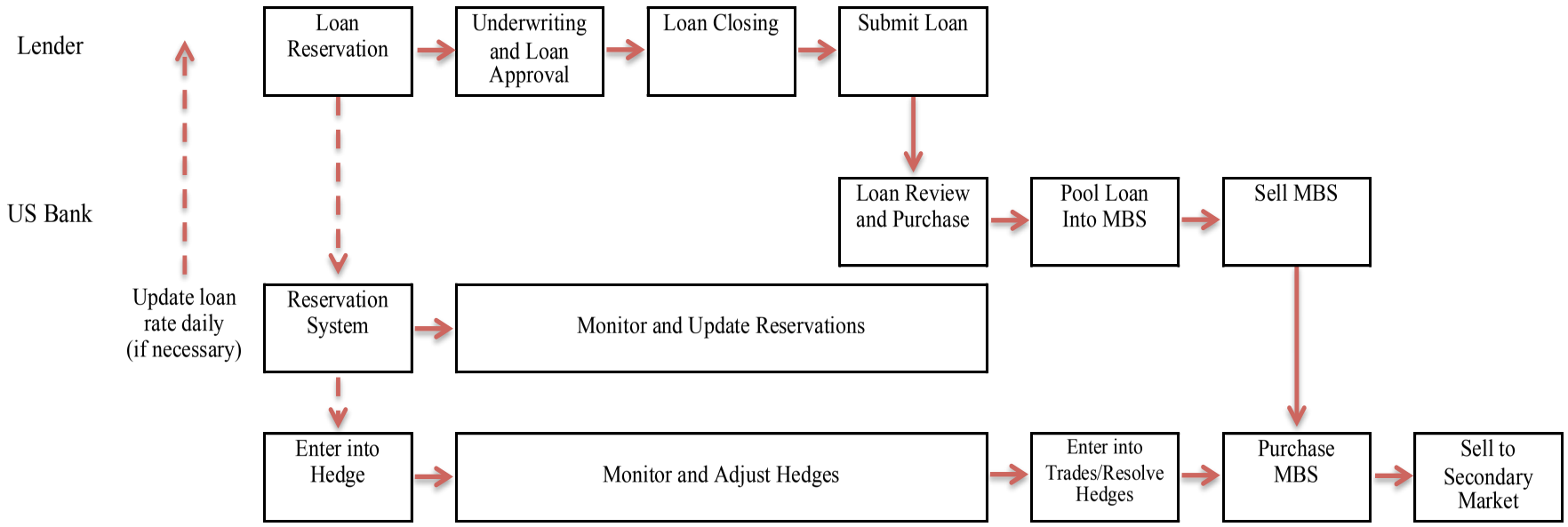


3. Interest Rate and Risk Management

B. Key Tools to Hedge Loan Pipeline

1. Frequently establish rates for new reservations
2. Hedge reserved loans
   - "To Be Announced" Market, the largest and most active global financial market
   - Assure price now for future delivery
3. Keep track of and adjust hedges
4. Execution choices at sale
5. Faster delivery of MBS
6. Systematic monitoring of portfolio
   - loan drop-out rate
7. Individual focused on this process daily with appropriate software
8. Risk controls

3. Interest Rate and Risk Management



3. Interest Rate and Risk Management

C. How MHFA Is Establishing These Capabilities

1. Independent consultant's analysis
2. Software evaluation and selection
3. Defining data needs and systems
4. Revising procedures and timelines for lenders and master servicer
5. Recruiting secondary market professional

4. MHFA Resources and Options

A. MHFA Has Very Valuable Resources for Financing Ongoing Single-Family Program

For Tax-Exempt Borrowers

For First Mortgage

Resource	Approx. $16 million of zero participations Pass-through bonds
Need to purchase hedges	No
Execution choice	Pass-through bonds or MBS sale (if more favorable)

For Entry Cost Assistance

Lower income	State appropriations and HOME $
Moderate income	Pool 2 cash, to be recovered from premium on: - pass-through bonds or - MBS sale

4. MHFA Resources and Options

For Non-Tax-Exempt Borrowers

For First Mortgage

Resource	Can purchase and hold MBS as investment of money market fund cash
Need to purchase hedges	On most but not all of pipeline (since MHFA can hold some long-term)
Execution choice	MBS sale or MHFA long-term investment

For Entry Cost Assistance

All borrowers	Pool 2 cash to be recovered from sale of MBS at premium

5. Potential MHFA Criteria

Criteria for Financing MHFA's Ongoing Single Family Program

A. Provide Long-Term Financing for:

1. New, expanded, simplified First Mortgage Program, including
   - Loans for both tax-exempt and non-tax-exempt borrowers
   - GNMA, Fannie Mae Preferred, and Fannie Mae Preferred Risk-Share
2. Entry Cost Assistance for as many borrowers as require it
   - Beyond the $ available and income limits of State Appropriations and HOME

5. Potential MHFA Criteria

B. Enable MHFA to Offer Attractive Financing:

1. For a larger potential volume of total lending
2. For non-tax-exempt borrowers
3. On an ongoing basis, despite markets changes, using widest range of execution choices

5. Potential MHFA Criteria

C. Be Financially Sustainable

Enable MHFA to continue to finance single-family program on ongoing basis, by:

1. Efficiently accessing the secondary mortgage markets
2. Providing ongoing funding to recover costs of MHFA Entry Cost Assistance without constraining either
   - total amount of Entry Cost Assistance or
   - MHFA's liquidity

5. Potential MHFA Criteria

3. Establishing lending rates at levels which provide MHFA the resources to:
   - Cover all risks and costs generated by the Program,
   - Fully recover any MHFA investment of its own funds in Entry Cost Assistance,
   - Maintain Agency liquidity*,
   - Enable Agency net worth to remain stable or increase*,
   - Provide adequate net revenues for funding Agency operations and contributing to Pool 3, and
   - Provide such net revenues in a way that supports future as well as current operations

*Under both expected and rating agency stress scenarios

5. Potential MHFA Criteria

D. Manage and Limit MHFA Risks by:

1. Establishing clear rate-setting and risk management guidelines which:
   a. Limit maximum risk exposure so that even under very conservative stress assumptions, the program:
      - is still significantly net profitable on an annual basis, and
      - increases total Agency net worth
   b. Are monitored and managed on a daily basis to assure compliance
   c. Provide for oversight by a secondary marketing staff committee, including Finance, Single-Family and Risk Management
2. Providing periodic reports to the Board on:
   - Program performance
   - Compliance with risk guidelines, and
   - Impacts on MHFA financial sustainability

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AGENDA ITEM: 6.D.
MINNESOTA HOUSING AUDIT COMMITTEE
August 30, 2012

ITEM: Fiscal 2012 Interfund Transfers

CONTACT: Bill Kapphahn, 651-215-5972
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REQUEST:

☑ Approval ☐ Discussion ☐ Information

TYPE(S):

☑ Administrative ☐ Commitment(s) ☐ Modification/Change ☐ Policy ☑ Selection(s) ☐ Waiver(s)

☐ Other: _____

ACTION:

☑ Motion ☐ Resolution ☐ No Action Required

SUMMARY REQUEST:
During the course of the fiscal year, various transfers occur in the normal course of executing approved Agency transactions. Annually these transfers are summarized to provide the Board an occasion for final review and approval.

FISCAL IMPACT:
See attached.

MEETING AGENCY PRIORITIES:

☑ Promote and support successful homeownership ☑ Preserve federally-subsidized rental housing

☑ Address specific and critical needs in rental housing markets

☑ Prevent and end homelessness ☑ Prevent foreclosures and support community recovery

ATTACHMENT(S):

- Background
- Interfund transfers: administrative reimbursements, to maintain Pool 1 required balance, and other transfers not previously approved by the Board, fiscal year 2012

The following categories of transfers of assets between Agency funds occur in the normal course of Agency business.

1. **Transfers of administrative fees from bond funds**: Most of the administrative expenses associated with managing Agency programs and the related assets that are accumulated there are paid from the General Reserve fund while most of the Agency's earning assets are held in the bond funds. An administrative fee is assessed monthly by the General Reserve and transferred in accordance with bond resolution provisions, if applicable, from funds holding assets under management.

2. **Transfers of administrative fees from appropriated funds**: Administrative expenses associated with managing programs funded from state and federally appropriated monies are recoverable to a certain extent. For programs funded with state appropriations, documentable overhead expenses can be recovered by transferring interest earned from undisbursed state appropriations. Expense recoveries are limited to interest earnings. For programs funded with federally appropriated monies, overhead expenses may be recovered according to a federally approved indirect cost recovery rate. Overhead recoveries for state and federal programs are made monthly by transfers to the General Reserve fund.

3. **Transfers to maintain Pool 1 required balance**: Pool 1 is a liquidity reserve maintained within the General Reserve fund per the Board's investment guidelines. The liquidity reserve requirement is 1% of all loans pledged in support of the Agency's credit ratings. Since the Agency shifted away in 2009 from acquiring single family whole loans to acquiring mortgage-backed securities, principal repayments of whole loans have steadily reduced the Pool 1 required balance. Excess Pool 1 balances are transferred by Board policy to Pool 2.

4. **Contributions to Pool 3**: Annually, as the Agency's final net earnings are confirmed, management determines whether some or all of those earnings are available for contribution to Pool 3. Pool 3 is the Agency's most flexible source of capital to address the most challenging housing needs. Other than an incidental amount of investment earnings, Pool 3 is funded almost solely from periodic transfers of Agency earnings that are in excess of the Board's investment guidelines. Board investment guidelines require that the combined net asset balances of General Reserve and the bond funds be maintained at no less than the combined net asset balances for the same funds for the immediately prior fiscal year end before any consideration of a transfer to Pool 3 is made.

5. **Bond sale contributions:** Each time bonds are issued additional collateralization may need to be contributed to the applicable bond resolution to achieve the parity of assets to liabilities necessary to meet ratings tests and to permit the transfer of monthly administrative fees. Bond sale contributions are an investment of Agency funds or other assets and are funded from Pool 2.

6. **Debt service and other debt related expenses:** Certain debt issues are structured from the outset to draw upon the Agency's general obligation to support the debt service and related expenses such as trustee fees. Examples include the short-term debt issued to preserve tax-exempt bonding authority, expenses related to the Treasury-sponsored New Issue Bond Program, and home improvement bonds issued in 2002.

Minnesota Housing Finance Agency
Interfund Transfers: Administrative Reimbursements, to Maintain Required Pool 1 Balance, and Other Transfers not Previously Approved by the Board
Fiscal Year 2012

Amount	Transfer from	Transfer to	Category	Description
$ 13,547,000	Residential Housing Finance bond resolution	General Reserve	1	Administrative fees to the General Reserve from the bond resolution in accordance with the bond resolution provisions.
$ 1,584,000	Rental Housing bond resolution	General Reserve	1	Administrative fees to the General Reserve from the bond resolution in accordance with the bond resolution provisions.
$ 979,000	Single Family bond resolution	General Reserve	1	Administrative fees to the General Reserve from the bond resolution in accordance with the bond resolution provisions.
$ 2,776,000	Homeownership Finance bond resolution	General Reserve	1	Administrative fees to the General Reserve from the bond resolution in accordance with the bond resolution provisions.
$ 97,000	Multifamily Housing bond resolution	General Reserve	1	Administrative fees to the General Reserve from the bond resolution in accordance with the bond resolution provisions.
$ 789,000	State Appropriated fund	General Reserve	2	Reimbursement to General Reserve for a portion of the administrative overhead expense attributable to state appropriation-funded programs.
$ 1,774,000	Federal Appropriated fund	General Reserve	2	Reimbursement to General Reserve for the administrative overhead expense attributable to federal appropriation-funded programs.
$ 9,659,000	General Reserve - Pool 1	Residential Housing Finance bond resolution- Pool 2	3	Transfer of excess funds to maintain the Pool 1 balance in accordance with Board investment guidelines.
$ 17,000,000	Residential Housing Finance Bond resolution- Pool 2	Residential Housing Finance bond resolution- Pool 3	4	Pool 2 contribution to Pool 3 for use in mission-intensive housing programs.
$ 8,612,000	Residential Housing Finance Bond resolution- Pool 2	Homeownership Finance bond resolution	5	Bond sale contributions to HFB 09A-3/11CD, HFB 09A-4/11E and HFB 09A-5/11FG.
$ 443,000	Residential Housing Finance Bond resolution- Pool 2	Rental Housing bond resolution	5	Bond sale contribution to RH 2012A1A2.
$ 13,959,587	Single Family Bond resolution	Residential Housing Finance Bond resolution- Bonds	5	Bond sale contribution to RHFB 2012ABCD.
$ 18,690,000	Residential Housing Finance Bond resolution- Pool 2	Residential Housing Finance Bond resolution- 04EFG, 07CDE, 07HIJ	5	To provide funds for 7-1-2012 bond calls.
$ 58,510,413	Single Family Bond resolution	Residential Housing Finance bond resolution- Bonds and Pool 2	7	Transfer net assets and liabilities remaining in the Single Family Bond resolution after all outstanding bonds were defeased in May, 2012.
$ 113,000	Residential Housing Finance Bond resolution- Pool 2	Residential Housing Finance bond resolution- Limited Obligation Notes	6	To provide funds to pay interest and various expenses on the limited obligation notes.
$ 10,000	Residential Housing Finance Bond resolution- Bonds	Homeownership Finance bond resolution	7	Contribution to Homeownership Finance bond resolution of certain unamortized premium on mortgage-backed securities resulting from the creation of a zero participation pool.
$ 493,000	Residential Housing Finance Bond resolution- Pool 2	Residential Housing Finance bond resolution- bonds	6	To provide funds for debt service on the RHFB 2002H bonds which were issued to provide funds for home improvement loans which reside in Pool 2.
$ 30,000	Residential Housing Finance Bond resolution- Pool 2	Homeownership Finance bond resolution	6	To provide funds to pay various bond related expenses.

Categories

1	Transfers of administrative fees from bond funds
2	Transfers of administrative fees from appropriated funds
3	Transfers to maintain Pool 1 required balance
4	Contributions to Pool 3
5	Bond sale contributions
6	Debt service and other debt-related expenses
7	Other non-recurring or minor transactions

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