BOARD OF DIRECTORS

California Housing Finance Agency
Board of Directors

July 8, 2014

California State Teacher's Retirement System ("CalSTRS")
100 Waterfront Place
Board Room
West Sacramento, California
(916) 414-4008
and
CalHFA Culver City Office
100 Corporate Pointe, Suite 250
Culver City, California
(310) 342-1250

10:00 a.m.

Bd.Table:#261435v1
BdMtg:07-08-14

7. Closed Session under Government Code Section 11126€(1) to confer with and receive advice from counsel regarding litigation in connection with MortgageFlex Systems, Inc., v. California Housing Finance Agency, Sacramento Superior Court Case No. 34-2014-00164768.

8. Discussion of other Board matters.

9. Public testimony: Discussion only of other matters to be brought to the Board's attention.

10. Adjournment

11. Handouts

NOTES**

CALSTRS PARKING: The parking facility is open to the public. You may park on any level, or in the surface lot. DO NOT park in any space that is especially marked, i.e. – "LEV Parking", "Member Visitor", etc. The parking fee is $1.00 per 20 minutes with a maximum of $15.00 per day. You will need to pull a ticket to raise the gate to enter the parking facility. Payment is to be made when exiting by placing a credit or debit card into the pay booth.
(*MACHINES DO NOT ACCEPT CASH PAYMENTS)

FUTURE MEETING DATE: Next CalHFA Board of Directors Meeting will be September 16, 2014, at the Holiday Inn Capitol Plaza, Sacramento, California.

STATE OF CALIFORNIA

CALIFORNIA HOUSING FINANCE AGENCY

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BOARD OF DIRECTORS

PUBLIC MEETING

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California Public Employees' Retirement System ("CalPERS")
CalPERS Auditorium
Lincoln Plaza North
400 Q Street
Sacramento, California

Tuesday, May 13, 2014
10:03 a.m. to 12:37 p.m.

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Reported By: YVONNE K. FENNER, CSR #10909, RPR

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A P P E A R A N C E S

Board of Directors Present:

MATTHEW JACOBS, Chairperson
Co-Managing Partner
Bulldog Partners, LLC

KEN ALEX
Director
Office of Planning & Research
State of California

ANNA CABALLERO
Secretary
Business, Consumer Services & Housing Agency
State of California

CLAUDIA CAPPIO
Executive Director
California Housing Finance Agency
State of California

KATIE CARROLL
for Bill Lockyer
State Treasurer
State of California

JANET FALK
Retired, formerly Vice President
Real Estate Development
Mercy Housing

THERESA GUNN
Deputy Secretary, Farm and Home Loan Division
CalVet Home Loans
State of California

MICHAEL GUNNING
Vice President
Personal Insurance Federation of California

JONATHAN HUNTER
Managing Director, Region 2
Corporation for Supportive Housing

PRESTON PRINCE
CEO & Executive Director
Fresno Housing Authority

A P P E A R A N C E S

Board of Directors Present (continued):

DALILA SOTELO
Principal
The Sotelo Group

LAURA WHITTALL-SCHERFEE
for Randall Deems, Acting Director
Department of Housing and Community Development
State of California

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Participating CalHFA Staff:

SHERYL ANGST
Housing Finance Specialist

THOMAS O. FREEBURGER
Assistant General Counsel

KENNETH H. GIEBEL
Director of Marketing

TIM HSU
Director of Financing

VICTOR J. JAMES
General Counsel

JOJO OJIMA
Office of the General Counsel
Legal Division

RICK OKIKAWA
Programs Administrator

JACKLYNNE M. RILEY
Director
Administration Division

ANTHONY SERTICH
Manager
Financing Risk Division

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BE IT REMEMBERED that on Tuesday, May 13, 2014, commencing at the hour of 10:03 a.m., at the California Public Employees' Retirement System ("CalPERS"), CalPERS Auditorium, Lincoln Plaza North, 400 Q Street, Sacramento,, California, before me, YVONNE K. FENNER, CSR #10909, RPR, the following proceedings were held:

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CHAIRPERSON JACOBS: I'm going to call to order today's meeting of the California Housing Finance Agency.

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Item 1. Roll Call.

CHAIRPERSON JACOBS: JoJo, do you want to start with the roll call?

MS. OJIMA: Thank you.

Ms. Caballero.

CHAIRPERSON JACOBS: She's outside taking her photo.

MS. OJIMA: Ms. Whittall-Scherfee for Mr. Deems.

MS. WHITTALL-SCHERFEE: Here.

MS. OJIMA: Thank you.

Ms. Falk.

MS. FALK: Present.

MS. OJIMA: Ms. Gunn for Mr. Gravett.

MS. GUNN: Here.

MS. OJIMA: Thank you.
Mr. Gunning.
MR. GUNNING: Here.
MS. OJIMA: Thank you.
Mr. Hunter.
MR. HUNTER: Here.
MS. OJIMA: Ms. Carroll for Mr. Lockyer.
MS. CARROLL: Here.
MS. OJIMA: Thank you.
Ms. Patterson.
(No audible response.)
MS. OJIMA: Mr. Prince.
MR. PRINCE: Here.
MS. OJIMA: Ms. Sotelo.
MS. SOTELO: Here.
MS. OJIMA: Mr. Alex.
MR. ALEX: Here.
MS. OJIMA: Mr. Cohen.
(No audible response.)
MS. OJIMA: Ms. Cappio.
MS. CAPPIO: Here.
MS. OJIMA: Mr. Jacobs.
CHAIRPERSON JACOBS: Here.
MS. OJIMA: We have a quorum.
CHAIRPERSON JACOBS: Great.

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Item 2. Approval of the minutes of the March 17, 2014 Board of Directors meeting.

CHAIRPERSON JACOBS: Let's go to the minutes from the last meeting. Did anyone have comments or adjustments to the minutes?

Does anyone want to move to approve the minutes?

MR. HUNTER: I'll move adoption of the minutes.

CHAIRPERSON JACOBS: Great. Second, anyone?

MS. SOTELO: I'll second.

MS. OJIMA: I'm sorry, who's second?

MS. SOTELO: Dalila.

MS. OJIMA: Thank you.

Mr. Chair? Should we acknowledge Ms. Caballero?

CHAIRPERSON JACOBS: I'm sorry. I should do more than just nod my head.

MS. OJIMA: Ms. Caballero is present.

CHAIRPERSON JACOBS: Oh, yes, welcome. You were taking your photo outside, and so I want to acknowledge you just walked into the room.

MS. OJIMA: Thank you.

All right. Ms. Caballero.

MS. CABALLERO: Here.

MS. OJIMA: To approve the minutes.

CHAIRPERSON JACOBS: We're voting on the

minutes.

MS. CABALLERO: Oh.

CHAIRPERSON JACOBS: You just happened to be outside when we did the roll.

MS. CABALLERO: Then it's an aye.

MS. OJIMA: Thank you.

MS. CABALLERO: I'll make it easier if I --

MS. OJIMA: Yes, both, thank you.

Ms. Whittall-Scherfee.

MS. WHITTALL-SCHERFEE: Abstain.

MS. OJIMA: Thank you.

Ms. Falk.

MS. FALK: Abstain.

MS. OJIMA: Ms. Gunn.

MS. GUNN: Aye.

MS. OJIMA: Mr. Gunning.

MR. GUNNING: Abstain.

MS. OJIMA: Mr. Hunter.

MR. HUNTER: Aye.

MS. OJIMA: Ms. Carroll.

MS. CARROLL: Aye.

MS. OJIMA: Mr. Prince.

MR. PRINCE: Aye.

MS. OJIMA: Ms. Sotelo.

MS. SOTELO: Aye.

MS. OJIMA: Mr. Jacobs.

CHAIRPERSON JACOBS: Aye.

MS. OJIMA: We have a quorum -- it has passed.

CHAIRPERSON JACOBS: Great. Thanks, JoJo.

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Item 3. Chairman/Executive Director comments.

CHAIRPERSON JACOBS: Today we've got a fairly important agenda with the financials and the business plan for the Agency, and so I'd like this to be a discussion, and please speak up and let's actually discuss how we're going to move forward here.

Claudia, do you have any remarks before we jump in?

MS. CAPPIO: Just in terms of the agenda, the report of the Audit Committee, do you want to save that?

CHAIRPERSON JACOBS: Yeah.

MS. CAPPIO: Okay. So you want to go right into the business plan.

CHAIRPERSON JACOBS: Well, I guess -- let's talk -- we can go to the Audit Committee.

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Item 4. Report of the Chair of the Audit Committee.

CHAIRPERSON JACOBS: Michael Gunning, chair of the Audit Committee, you want to -- we have CliftonLarsonAllen here.

Nancy Jones and Mandy Heagy, are you both here still? There you are.

(Off the record discussion where it was discovered that only a limited number of microphones can be on at one time.)

MR. GUNNING: There it is. Now we can talk.

Thank you, Mr. Chairman, members.

The Audit Committee met this morning. As I said in the committee, it's always good to have a straightforward audit. There were no audit findings or management letter for the loan insurance fund. However, there were a couple adjustments. The corrections were made during the audit, but we turned out okay.

Lori and the team this year, we did lose Mike, but we've got Nancy with us now, who's just as capable and look forward to working with her.

We're good. Any questions?

One other thing, they did -- we had some duties and our charter, which was done back in 2006, so at the November meeting we're going to take a look at that and evaluate that again, so that will be on the agenda for November when the committee meets again to look at the Agency's fund.

That's it, Mr. Chairman.

CHAIRPERSON JACOBS: Thank you, Mr. Gunning.

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Item 5. Discussion, recommendation and possible action regarding the adoption of a resolution approving the Agency's Strategic Business Plan for Fiscal Year 2014/2015. (Resolution 14-05)

CHAIRPERSON JACOBS: Okay. So, Claudia, let's jump into the strategic plan. And, again, if people have questions, just let us know and we'll discuss.

MS. CAPPIO: Good morning. The item here before you is the Agency's forthcoming strategic business plan, and this is the third year in this format whereby senior staff began work in January and worked steadily to provide you with specific goals, strategies and actions for the coming year, in this case for the '14/15 budget year.

We have reviewed accomplishments with you in January, based on the current year business plan, and we provided a work in progress to you in March for your review and comment. And we received comments from the Board. Specifically we responded by linking overarching goals at the top of each page with specific strategies that apply to that goal, and we refined strategies based on further research work and internal discussion.

Some of the highlights are that we changed up single-family servicing priorities, and we have specific target lending volume requirements for both single family and multiple family to link our revenue estimates with our operational expenses. This work is essentially grounded in improving programs and financial resources for affordable housing in California, and that includes coordination of programs and greater collaboration among those agencies and services throughout the state government that do affordable housing, expansion and diversification of revenue streams, looking at operational efficiencies where we can find them, and continue to aggressively pursue foreclosure prevention during the next two to three years with our Keep Your Home California funds.

So how to proceed today? First, I would like Tim Hsu, our financial officer, to provide information and projections on Agency income and cash flow versus operational expenses -- again, this is directly in line with what you were concerned about in the March meeting -- then request that the Board review the draft business plan and discuss questions and comments. Upon conclusion, the Board can choose to adopt the resolution approving the plan, or you can pause action and go to item 6, which is the budget for next year and look at those as one, as long as at the end of the day we request that you provide action, affirmative action, to us on both resolutions, adopting the strategic business plan and adopting a budget for the next year.

I'll be glad to take any questions or comments.

So we should proceed with Tim.

CHAIRPERSON JACOBS: Okay.

MS. CAPPIO: Your show.

MR. HSU: Good morning, Mr. Chairman, and good morning, Members of the Board. With your indulgence, I'd like to try something different today. No sports analogy or metaphors. And you know that I can mix analogies with the best of them, so no fourth quarter home runs. And I'm going to assume that everybody today prefers to deal with the turbulent times and prefers to be a human being than a dog. And all of this is predicated on something I read recently. Someone shared an article with me which had a profound influence on me, and I'd like to use a quote from this article to frame my presentation today. And the quote is: "All fear and hope arises from looking backward and forward. It is only in the present moment, free from hope and fear, do we receive the gift of clarity and resolve."

Alas, I will spend quite a bit of time today talking about the past, and I will also spend some time talking about the future, but it's my aspiration that at the end of the presentation, that we will come back to the present with some clarity and resolve and have some clarity on what is it today that we ought to be doing.

So when we talk about the budget, when we talk about the Agency's ability to pay for its own operations -- and as a reminder, the Agency does not -- the Agency is not a burden on the State's general obligation fund. The Agency pays for its own operations. And when we think about the budget, we think about where do we get the money to pay for our operations. What should we be looking for and what we should be looking at is sometimes the more important question, because I know that we just had a presentation regarding the audit of the insurance fund. When you look at the various entities of the Agency and look at our financial statements, it is a lot to consume. But what should you be looking at?

So this is on page 3. This is a 15,000-foot view of CalHFA. So at that level, you will see in the orange box our single-family indenture and in the yellow box our multifamily indenture. You might recall recently that we've managed to decouple the rating of the yellow box from the blue box. You'll notice this general obligation, which is in blue. And today what we're going to focus on is this green box. This green box is the non-bond assets that the Agency has.

So you will notice that in this box today, I'm showing that we have $186 million of cash and securities. What we also have in the green box is another $175 million of loans receivables. Okay. We'll come back to the importance of that in a little bit.

So this green box, how did money or the assets get into this green box? When things were doing better, perhaps more than five years ago, these orange boxes and these yellow boxes used to feed cash and assets into the green box, because the Agency, in effect, if these indentures were to be completely paid off and there's any assets, any equity left, the Agency takes possession of those equities.

So this green box, why is this green box important? Because this green box pays for that roughly $40 million of operating expenses that we will spend some time talking about today. And that box is the -- the -- sort of the main character or the -- I don't want to say point guard, but it's the main character to look at today. And that's the -- that's the entity that we're going to focus on as we think about the Agency's wherewithal, our ability to sustain paying for its operations.

So I'm chagrined that every time I present this chart, the person who asked for this chart initially is never here, and that's Tia. We -- we started creating this chart last year when Tia had asked the question about, well, how did we do in this past nine months or 12 months? Prior to that, we were more forward looking, and we will have charts later on more forward looking and stuff.

So what this chart is really doing is showing you how that green box fared in the first nine months of the fiscal year. So let me just walk you -- this chart warrants a little bit of walking through in detail. So if you look at July 2013, what you'll see is that in July 2013, in the columns what I'm doing is I'm stacking the income items that comes into the green box. So there's roughly about $1.5 million of interest on mortgages and securities.

As I mentioned, this -- this green box owns about $175 million of loans receivables plus MBSs, so we got about $1.5 million in July 2013, and then we got another half a million dollars in various fee incomes, which I won't go into in great detail for now. And we also got about a million dollars of income from loan servicing. So what we're doing is month by month we're stacking the amount of income, different income items, that comes into that green box month to month.

And in red we're showing the operating expenses spent by the Agency, also by month to month. These are discrete observations, although they are connected. So you can see roughly we spent about $3 million on the average. There are some months we spent more; there are some months we spent less, but on the average we spend about $3 million a month.

Now, if you add up all these columns and you add up all the lines and you figure out all the income items collected in the first nine months of the fiscal year and all the expenses, you go to the upper right-hand corner of this chart, you'll see that we collected in income $26.8 million and then we collect -- or we spent in expenses $28 million, so we had a net deficit of 1.2 million.

CHAIRPERSON JACOBS: Tim, how does this compare with our forecasted income for this period? I mean, where were we short? Where did we exceed?

MR. HSU: In terms of income, we generally are very close to what we project. And where we're not as accurate, if you will, is the next chart, which I'll come to in a second, which is on the prepayment and repayment of loans. But on income items, we tend to be fairly steady.

So on the income to expenses basis, we do have a small deficit of $1.2 million, which is -- which can be alarming.

So if you go to the next page, this is page 5. What this chart is attempting to do now is instead of just looking at all income items or items that can be construed as being income items, what we're going to look at now is everything that is coming into that green box in terms of cash. Okay. So I'm stacking, once again, all these items again. So on the bottom of these column stacks are the same things, carryovers from the previous page, page 4, but what's stacking on top here are two items. They're, again, back to July 2013, we received -- this microphone is really tricky. We received $3.2 million of loan repayments in July 2013. So in addition to all those income items that we show on page 4, we now have another $3 million that comes in because we got some prepayments.

So then the other item that added on here is I do look at October 2013. We also had received about half a million dollars of reserves that the Agency had set aside for earthquake insurance at some point. I won't go into that in great detail, but that cash is also being released from the reserves as these -- the earthquake insurance that was set aside for condos, as the condo loans pay off or they refinance, the balance goes down, and we release that reserve into this green box.

So when those two items stack on top of the income items, what you now see is that if you add up all these cash and also release of reserves, they amount to -- migrating over to the box on the right-hand side, these additional cash items amount to $33.7 million, which makes it -- which makes the first nine months of the fiscal year, though short on an income basis of about $1.2 million, but when you look at just the cash basis, we are actually -- we actually have a surplus of $32 million.

MS. FALK: This may be sort of a technical question, but why isn't this other cash coming in considered income?

MR. HSU: Because these are -- these are -- you mean the reserves or are you talking about --

MS. FALK: I'm talking about the -- well, I guess the prepayments are not -- the repayments are not the revenue into the Agency.

MR. HSU: Yes, they're certainly revenue, but I think that the distinction we're making is that suppose that we run out of these loans. Right? Because -- and that's a point we will come back to later on, Janet, is that it's true that in large part these repayments are helping us meet from a revenue to expenses basis, but part of the issue here is that when I mention that this green box does have about $175 million of loans receivable, they're all very, very seasoned loans that are paying off relatively quickly. So as they repay and prepay and as they enter sort of the final stages of their existence in terms of the loans receivable, if they -- and, again, we have a chart about this later on when we sort of bring together the past and the future together, it's not sustainable to rely on that revenue source that's out five to ten years.

MS. FALK: Okay. I understood that, but on a given year basis, you could project something about what's likely to come in only in the next year, right?

MR. HSU: We actually have later on charts that goes out like two and a half fiscal years.

MS. FALK: Okay. Even though -- I mean, I understand that the income might be much more steady, but that these other sources are going to fluctuate, but they're still somewhat predictable.

MR. HSU: That's correct.

MS. FALK: Okay.

MR. HSU: So then from a projection basis, we assume that the loans amortize as expected and they mature when -- they pay off and mature on the expiration date of the loans.

CHAIRPERSON JACOBS: One question. The repayments and the prepayments. I guess what's the vintage of the loans, and, two, are they getting recapped with our loans or, you know, with extended affordability and new facilities from us, or how are they getting paid back?

MR. HSU: Sometimes. Sometimes they are capitalized, recapitalized, with loans from multifamily programs. So this past -- back in November, you might recall the Board passed three multifamily projects, and all three of those were prepayments that led to new loans that the program folks here made. Actually, I'm sorry. I don't want to say all of them. I think one out of three of them was. The other two were new. And so that happens sometimes.

MS. SOTELO: Tim, I just had another question. The income from loan servicing is only showing in July and December. Is there a reason that it's only in those two periods, at the beginning and mid-term?

MR. HSU: There's -- this is really just an operational practice. It's certainly true that the loan servicing collects fees every month. We sort of let it accumulate, and then we'll transfer this accumulated servicing from the servicing account to this green box once every six months or so, when it kind of exceeds a certain dollar amount.

And that's why it's important to mention a couple things. This particular analysis is really only on a cash basis and then they are on an audited basis because, as you -- as you know, the auditors are usually looking back at things that happened, but because this particular exercise warrants that we look forward, this is unaudited. Plus this is all on a cash basis, so said another way on Dalila's question, is to say that I'm showing that the loan servicing I believe -- I think you all know I'm color blind. I believe that the last time we received income from loan servicing is in December. So in theory -- three months have gone by, so in theory if we were doing accrual accounting, we would have three months of loan servicing accrues in here. Here I'm just worrying about everything on a cash basis.

So this chart, the punchline here I think is that we have generated, as what -- I think what Janet is saying is that if we are worried about just simply revenues to expenses, this chart would really say that, well, we generate plenty of revenues versus expenses, and as a matter of fact, we have a surplus of $32 million. So you might conclude that, jeez, that must mean that our cash position in this green box is actually growing over time.

As it turns out, I think that over the last 18 months I have at various times presented to the Board using -- that we have been using this cash in a very strategic fashion to target our balance sheet and to leverage our balance sheet using our cash to call out these VRDOs which are backed by U.S. Treasury's Temporary Credit Liquidity Program, TCLP. And in so doing, these targeted redemptions have bolstered our credit ratings.

Page 8. On page 8 is a summary of how much of this we have done over the last 15 months or so. We have used about $165 million of our unencumbered cash to redeem our VRDOs, and this is simply a breakdown of how much we've done in every six month increments.

And on page 9, as I mentioned, most of these redemptions were targeting VRDOs, which are backed by this letter of credit by U.S. Treasury, which by the way expires at the end of next year, so it's imperative that we either take them all out completely or we find a way to replace them.

So this targeted redemption has primarily been targeting this multifamily indenture, back on page 3, I believe -- 2 or 3, that's the yellow box. So you can see that this kind of targeted behavior has actually led to a tremendous lift in this multifamily indenture's rating. So you can see on page 9 here that we have gotten a four-notch upgrade from S&P last year, and we have also gotten a two-notch upgrade from Moody's earlier this year.

So this has -- this behavior of using some of our unencumbered cash has -- both helps us to leverage our balance sheet, but also giving us a lift on our credit ratings. And this -- this targeted behavior has, again, not focused as much on the orange box, which is our single-family indenture, which we have only done that to the tune of $10 million in the last 15 months or so, and you can see that we have gotten a two-notch upgrade from S&P, and it has been somewhat steady in terms of Moody's. And the blue box, of course, is the entity that's giving up the $165 million, and its rating has been fairly steady over the last couple years.

On page 10 -- and I know that this is just so that I pause. What I'm trying to do is give some sense of the past, and the takeaway before we go into this more is that I don't want us to dwell on this. As much as I'm spending the time to talk about this, I think that what we really need to do is, as I said in the opening, that -- not let the past inject fear in us, is really the main message here.

So on page 10, as I mentioned that we have been using some of our cash to target these VRDOs. So as it turns out, our cash position actually has been declining. It has declined from $306 million from February of last year to $186 million on April 1st of this year.

And on page 11 for the -- for the accountant in you, what I thought was to show the line item and number for how we have gotten from $306 million as of 2/1 of last year to $186 million on 4/1 of this year. So if you focus on, for example, the 7/1/13, that second column, you'll see a $60.6 million. That cash inflow number, that's a number that I showed you on page 5 but in graphical terms. You'll see that same number of 28 on page 5 in graphical terms, and that 32.6 in graphical terms on page 5.

And also, I mentioned earlier that we spend $165 million of cash to redeem our VRDOs. You'll see that at -- sort of at the very bottom right-hand corner, right above the yellow box. So this is, again, sort of a much more detailed reconciliation of how we got to that -- got from that $306 million to $186 million. You can see that we've been generating a balance cash surplus, but our cash position has gone down because we've been employing it to leverage our balance sheet.

On page 12, the other justification, of course, that I've brought to the Board over the last 15 months of why it's okay -- of why is it that it's okay for us to have a lower cash balance? It is because our requirement, our need, to set aside for cash so that we can deal with this collateral posting risk has declined tremendously over the last I would say two to two and a half years.

So what you can see here is that on February of last year, we suggested that about 150 to 160 million dollars of our cash was actually set aside to deal with that collateral posting risk. And if you look -- so if you look further back -- and I guess I do want to do that. Because part of my message here is that there's no point to dwell on things that happened two and a half and three years ago, but if you did look beyond that, this time frame here, we set aside more than $200 million to deal with this risk.

So you can see that as of 4/30 this -- our -- the way that we set aside for this risk is at a hundred million dollars. So our need to hold onto cash has also declined because this risk was receded.

On page 13, this is -- this is, again, a way to justify or a way to rationalize the amount of cash that we have is adequate, the amount of cash that we have is sufficient, to deal with all the things that we need to do at that green box level.

So what you can see is that the $186 million of cash that we have on hand, the way we're setting aside as collateral posting risk is that we say, well, how much money do we need if we were to -- how much money do we need if we were to be downgraded by one notch. And of course that risk of being downgraded by one notch has receded tremendously over the last two years, but continuing that tradition of setting aside that reserve, assuming we were to get downgraded, we suggest that that reserve would be just a hair under a hundred million dollars.

So that's why I suggest that we have about $88 million in cash that we can use for -- one of the things that we talked about last year is that it's useful to have some internal line of credit for warehousing to support our programs. So, for example, three multifamily loans that we did, they closed -- some of them closed in December, some of them closed in March, but we didn't do the bond transaction until April, so the ability to be able to warehouse loans after closing but before bond sale is extremely useful. So we have $27 million, for example, set aside for that.

We also have a $3 million line of credit set up internally to support single-family lending. So that cash is being set aside in sort of this stacked column on the right-hand side. You can see about $98 million has been set aside for this collateral posting risk and a year operating expense that we set aside.

And this is another point that is worth dwelling on, that last year we had shown this particular set-aside to be two years. But we have always known that this is something that we're simply doing out of -- as the lawyers would say, out of an abundance of caution in the sense that we don't use this money to pay for operations because I show on page 5 we generate enough current year cash to pay for operations, and later on I'm going to also show you that we generate enough for future current year cash to continue operations.

CHAIRPERSON JACOBS: Tim, one question on the legacy loan prepayments, is there a sensitivity that we ran where if the rate environment changes dramatically and those stop coming in early, what does that do to all this?

MR. HSU: In large part the unencumbered loan receivables that we have in our green box are multifamily loans, so it's my impression that the multifamily loans are at least the loans that we have in that green box. So keep in mind, as I mentioned earlier, that the stuff, the loans that we have inside our green box tend to be very seasoned loans. They're -- again, this is my impression. They are less driven, in my mind, by rate sensitivity versus the tremendous equity that the developers have in these projects.

Because again, these are not projects that came on line three years ago, four years ago. These are projects that probably got originated 15, 20, in some cases 25 years ago. There's tremendous equity that's trapped in these deals, and they want to prepay and recapitalize. And that is a stronger force than the rate sensitivity. And as you and I know, we all made New Year resolutions this year that we would allocate less of our own personal assets to fixing that because rates were going to go up. But you and I also know that in the first quarter, fixed income kicked butt. It was the best performing asset class.

So to me, guessing where rates are going to go is a fool's errand. What is really key to these projects, these loans, that are inside the green box is what the developers know that they have tremendous equity trapped inside, and they want to get it out. So that's what, to me, is driving the prepayments more than rate sensitivity.

MS. SOTELO: Tim, I think that's a really good point, talking with developers around that. I guess my question goes back to your boxes. And where in these boxes -- maybe I'm just missing it. Where in these boxes do you put money that's available to do programs, to do loan product, to do, you know, the work of the Agency? Where does that all fit, and how much is that?

MR. HSU: So let me make sure I understand. So are you saying that if a new project were to -- if we had someone who wanted to do a preservation program, how does that flow through the system?

MS. SOTELO: Oh, no. No, no. Two separate points. So I really do see developers wanting to recapitalize their projects and the repayments increasing as a result of that desire. That's one point.

The second point is just understanding the cash from the Agency's -- you know, we've got the operating expenses. We've got the warehousing line of credit. Where is the new money, or where is the money to do programs?

MR. HSU: So let's take the example -- let's go back to page 3. So I'm going to use this deal that we just closed in April as an example. So I mentioned earlier that we did three projects, and one out of three of them was -- was where's that loan before we made the new loan to the developer. So when that -- when that old loan pays off, it paid off inside this yellow box. So then we used that prepayment to call the bond that had funded it I believe about ten years ago. Then we issued a new set of bonds under the yellow box, and we got bond proceeds to fund the new loans. So this yellow box is sort of the entity that's flowing -- that's receiving the prepayments and also creating new proceeds to fund new loans.

MS. SOTELO: I guess my question is if you're setting aside cash that's coming in for the VRDO obligation, then how much money does that leave beyond, you know, setting aside 40 million for operations and for, you know, everything else that you're talking about? How much money does that leave to do programs or to do projects?

MR. HSU: I think I'm -- sorry, I'm a little bit dense. I think that the actual funding of the loan to come from bond proceeds, but it is possible there are times in which we take, let's say, Agency -- some money from the green box, too, to facilitate the bond sale, and that does happen. And I think that that dollar amount, we don't have a particular set-aside.

Said a different way, suppose that instead of -- suppose that we were dealing with, instead of the three projects that we did this past April, last month, if we had 30 projects, for example, we would figure out some way to fund the bond reserves as necessary to make that bond deal work. In my mind -- in my mind, there's really -- at least in my mind, I hope Claudia agrees. In my mind, if we are lending and the lending activities themselves requires capital from the standpoint of well, we need to fund reserves in order to make that project work, I don't think there is a limit, meaning that we could figure out some way to fund those lending activities and figure out -- there's -- there's a will to do that, then we will create a reserve for it.

MS. CAPPIO: And I do agree, just officially, and let us have that problem coming up. It's a good problem.

MR. HSU: Yeah. And then one way to think about that, if we are focused on, for example, the boxes on page 13 is that you can think of -- you can think of what I've done on the right-hand column here as having a lot of dollars, but I wouldn't want to suggest they're idle because risks, as we know as they are, needs to be dealt with. But at the moment, the amount of collateral we're actually posting is 50 million, so that we've set aside nearly a hundred million. Right? And then also this $40 million set aside for operating expenses, I sort of have made the case that we don't actually use that money. We actually generate enough cash in the current year to pay for operations.

So that alone, you can argue that we have about 40 plus 50 million dollars of cash that, if need be, just need to be used to support lending, which is not to -- not to reveal my hand here, is what we need to do.

MS. SOTELO: Okay. That's the question I was getting to. How much of that, of this cash, would be unencumbered or, you know, unbudgeted to be able to -- to increase our production on the program side? So that answers the question.

CHAIRPERSON JACOBS: I think, Tim, what's challenging for me and probably some other folks is just, you know, it's an expense budget here and then the table shows the revenues, but it would great to see like almost even a five-year plan of, you know, where we think the revenue is going to be coming from and just --

MR. HSU: We have that.

CHAIRPERSON JACOBS: -- together with --

MR. HSU: We have that. You just have to live through the past first, and we'll get to the punchline at the end. I'm sorry. We'll get there. We're going to get there. We're going to get there.

Okay. Okay. So if no more questions, we have slayed the dragon that is our past, and I'm going to go into the future.

MR. HUNTER: I just have one more question.

MR. HSU: Yes.

MR. HUNTER: The Mental Health Services Act housing program, so the counties transferred funds to CalHFA to administer on their behalf. Did it end up in one of these colored boxes, those funds?

MR. HSU: So let's go back to page 3. So the money that's received for the MHSA, is our acronym, goes into this box on the very right-hand side that we call contract administration. So the actual get back I believe was $400 million. That cash would go in here, sort of -- it goes in there as a conduit to fund the loans, but after we make the loans, the loan generates a small up-front fee for the Agency, along with an annuity, then that would flow into when you go and look at page 4, part of that -- part of that fee income.

MR. HUNTER: Right. Okay.

MR. HSU: Okay? But the actual cash that got generated by MHSA, we never count that as part of our own cash because that's the State's cash to run a very specific program. But the small fee that we're generating by being the administrator for the program does show up as projected income.

MR. HUNTER: Thank you.

MS. CABALLERO: I just want to make a comment. I really like the graphs. My mind works better when you show me the graphs than the numbers, but I really like the way that you've laid it out, so I appreciate it. I just wanted you to know that.

MR. HSU: Thank you so much. I actually spent an inordinate amount of time preparing for this, so anyway, so I appreciate that.

MS. FALK: Just to give the opposite viewpoint, I really like the numbers as the way they're presented on page 11. It's much easier for me to see, understand, what's going on when you do it that way.

MS. CAPPIO: So that means both, Tim. We'll just do it both ways.

MS. FALK: It's -- and I really appreciate all the time you spent on the past, but maybe now going forward we can just start focusing on present and future.

MR. HSU: We will. So starting on page 14, let's talk about the future next, because, again, it's the past and the future that gives us fear.

So what we're going to talk about -- and I think that I'm just going to talk about this at a high level. If you guys have detailed questions about the actual programs that are inside the business plan, it's better I think for my colleagues to answer those questions.

So on page 15, what you're looking at is that when we went through the business planning process, what we asked the program folks to do was to create three different scenarios on their projected lending activities and the amount of revenues they will generate.

So what you'll see is under the fiscal '14 and '15 on the single-family program, they're expecting what we're going to do is that we're going to focus on the central case, which is the latter case. What you see is that -- I'm on page 15, that for the fiscal year '14 and '15, they're expecting to generate 927 loans in the moderate case, and in so doing, they're projecting they will generate $2.5 million of fee income in that fiscal year.

One of the things that we want to also do is give you some historical context -- more on the past, I'm sorry -- on what that $927 million -- 927 loans represent in terms of how it compares to the past. So you can see that at some point in the early 2000s we used to do about five to six thousand loans per fiscal year. So that 900 loans is well within reach, and I think it's certainly attainable. There's some certain timing issues that I think Ken and Sheryl can address later.

And then moving on to the following fiscal year, you can see that that central case does increase slightly, so instead of 927 loans, they're thinking that now they can do about 1200 loans, and the income generated from that fiscal year would be closer to about $3 million.

MS. FALK: I have a question. So we're going to go from 39 loans in this fiscal year to 927 loans next year; is that correct?

MR. HSU: That's correct.

MS. FALK: Okay. And we have the capacity to do that?

MS. CAPPIO: We've planned accordingly in the budget for both the high, medium and low case.

MR. HSU: Moving on to page 16. The other thing that is worth thinking about is that it's true that the single-family program is generating a current year income to the tune of the $2.5 million we see on page 15, but it's also going to generate loans receivable in the form of a subordinate loan that would get paid off if the homeowner were to refinance or pay off the loan in, let's say, five or ten years. So that's the loan that we sort of affectionately refer to as ZIP. This is the downpayment assistance loan that we're making from the premium generator from this TBA program.

So what you see on page 16 is the combination of the current fee being received, plus the present value adjusted for some expectation of losses of this subordinate downpayment assistance loan. So you can see roughly that in the fiscal year '14/15, that that loans receivable is worth almost as -- is actually worth more than the income that we receive. So instead $2.5 million, we're now looking at about $5.8 million. And likewise for 2015 and '16, that the loans receivable increases the value of what they're doing by about 130 percent.

Again, I'm sure there are a lot of questions, and I think that I'm just looking at the numbers and how they look in terms of revenue generation. So if you look at page 17, what page 17 is now talking about is the multifamily side of the equation. So multifamily on the moderate case would suggest that we would generate about 20 loans that we think of as lender issuer. These are -- this is sort of the scenario in which we're making a loan and at the same time issuing the bonds to pay for the loans, so this is really sort of the main business line of the multifamily side. So this -- and again, this is the three loans that we just closed last month.

And the fee that we would generate from the multifamily program in the current year is actually comparatively less than the single-family side, to the tune of $1.5 million. But if you look at page 18, you'll see that the multifamily program, however, is generating a much bigger loans receivable, and that's because these loans tend to have a healthier spread and also they tend to last longer than the single-family side. So a very typical multifamily loan could last 15 to 20 years or so, whereas if you look at any single-family MBS, the average life is probably closer to about I want to say eight to 12 years or so.

So on page 17 again, you could also get a little bit of historical context of how the moderate case of 20 loans compares to what we've done in the past. And that gives you a sense that this is something we think we can attain.

So on page 19, so what I'm going to attempt to do here is bring the past and the future together to see if we can shed some light on today, for what we ought to focus on today. This is the -- this is the finale, I guess, the information that Matt and Janet have been yearning for.

So what I did here is I brought together the past. And what is the past in this chart? The past is the -- if you see the green here -- I got color coordinated with my wife this morning -- the green columns here, these are the income generations from loans that are sitting inside our green boxes. So if we look at page 5 and then looking at the first nine months of the fiscal year thinking about income generation, now I'm looking at that green box, and I'm thinking about income generation for the next three fiscal years. Okay.

So you can see that on balance, as we talked about earlier, it's somewhat steady but declining. And then in the gray is -- again, that green box has loans receivable, and what we assume here is that simply they will pay off when due. They pay off on maturity dates. And you can see that that too is also substantial but it is also declining.

So that's the past. On this chart those two things really in large part represent what the past is able to gift us today.

So what you're seeing in the future, which is what's in the yellow box. Okay. So I have four charts which shows the income generation from single family and multifamily. The first chart of each program shows the income received in a year. So what I did was I added all the single-family income received in that year. Again, I'm ignoring the loans receivable, this downpayment assistance loan. If it were to pay off, it could pay off much further down the line.

So I added the current income generated from single family, the current income generated from multifamily, and there's also in here $200,000 of new things that asset management is doing, I also put in there. They altogether add up to this $4.3 million in the next fiscal year in yellow, so comes in as being sort of of what we would generate in the near future.

One other thing to point out here is that in these dashed yellow, which is coming across each of the columns, what I'm also showing is the operating expenses today. So this number that you see here is slightly lower than the number that will be presented to you later, and that's because we have a certain number of vacancies. And as it turns out, we're working on filling about half of those vacancies, and the other half of the vacancies are to be determined. So my number here is slightly lower, as I explain in this text box here, because I have taken out half of the vacancies because we're not sure if we're going to fill them.

I did not inflate these numbers either, as far as the operating expenses. You can tell that they stay steady across the years. That's because there's just a lot of unknowns. Perhaps there will be raises. Perhaps there will be attrition. I just don't know enough to -- to worry about that at the moment.

Now, what does this do in the sense that now that brought the past and the future together? What does this have to do with now? And the reason, in my mind, is that if you look at this chart and you say that if we're having this meeting a year from now and these yellow that you're seeing, these yellow boxes are substantially lower than what they are today, what I'm showing you today, what does that mean? Because as you can see that -- as you're going further along the fiscal years, you can see that the past is becoming less generous over time. And we really are starting to become more and more dependent on what the yellow will do for us three years from now and four years from now.

And that's why I say that if you bring these two pieces together, the past and the future, you get some clarity that, jeez, what you really have to do today is making sure that these yellow boxes show up tomorrow, and you really need to get back into thinking how to generate that income. Now, since I'm a dollars and cents guy, I won't make any statements about what kind of lending we ought to be doing, but I agree, as some people said at the last meeting, that we should be a lender with a purpose.

But having said that, we need to also be overlaying that idea, in my mind -- this is a little bit me speaking now, so that a year from now we should be able to look back and say, well, how did we do on that yellow box, because, again, we are starting to become more and more dependent on that yellow box and that past, the generosity of the past, is -- it is working slowly lower and lower.

So that's my presentation. I'll take any comments.

The last couple pages, which I won't go into, these couple pages arise from a couple questions that Dalila had. They deal with mostly about sort of our recent history. And I heard some questions about the past. Some people do want to think about the past, and I think I won't go over them, but it is at your leisure if you'll look at them, you'll see that we have also done a lot in the past four years.

CHAIRPERSON JACOBS: The edits you made to this thing I guess this week are immensely helpful. It answers a lot of my questions.

MR. GUNNING: I guess the question I have, Tim, is we have to examine what our lending activity is if the boxes trend downwards. And that's the question.

MS. CAPPIO: I, through the Chair, I think that's right. What we'll be doing over the next year is the market is really different. Credit is tight. Interest rates are low. We have to fit in somewhere, or we still fulfill our purpose and yet make sure that we're still sustainable. And it's a new order. It's a new order of things that we're -- there's a lot of unknowns.

MS. FALK: Well, first I'd like to commend you, Tim, for putting this in a way that, you know, really gives us a historical perspective and we can really see, you know, what we have to focus on.

I would like to make a request, however, and I don't know if we're moving into the budget yet, but in order for me to feel comfortable approving a budget, I need to see the revenue on the same page with the expenditures, because I don't think you can have one without the other. And in the same way that you have budgeted and actuals for the last year and then the projection for the future year, I'd like to see the same thing with -- with the revenue.

And that way, when we get to next year -- and I promise I'll be here for that, requesting this -- we get to next year, we can see, oh, here's what our projections were for our revenue for '14/15, and then we can see how we've done against it. Because it's kind of hard to evaluate it without knowing what we adopted or what we were even projecting, because all the charts don't get adopted as part of an official budget, I don't believe. You know, it helps us to understand it, but I would really like to see it as part of the, you know -- we've got ten pages of broken-down expenses, but I would really like to see some broken-down revenue, too, to go along with it.

MR. HSU: Okay. I can certainly work on that. I think that --

MS. FALK: I think you've got it all here, you just need to put it into this format. Yeah.

MR. HSU: Okay. I think some of these numbers that we have that drives page 20 has some of that. But since you revealed your propensity for page 16, I think I know what to do.

MS. FALK: Page 11.

MR. HSU: Eleven, okay, sorry. Page 11. Yeah, I think that we have information to be able to show you what you -- it's all here, like I said.

MS. FALK: Is it also -- you know, I'm used to looking at budgets where you see income and expense statement, then you also see a balance sheet, which is really what you're talking about as your cash position. Is it possible to generate that for the Agency, or is that really complicated?

MR. HSU: We can try. We can try. I think one of the things that we struggle with, which is part of the reason why we show page 3, is that that entity that we think of as the green box is a loosely -- it's like a loose federation in the way that it's not a separately audited entity. So then what we have to do sometimes is to pull together various pieces to make that green entity.

MS. FALK: Yeah, okay. Then maybe we can just -- instead of a whole balance sheet, because I know that that would be really complicated with all of the different bonds that are outstanding -- I'm looking for the page where you had the cash position and what was in it -- and just translate those into numbers instead of a -- well, it was -- you had one where it showed what your cash -- the cash balances were, kind of pages 12 and 13. Just put those in numbers on a page that becomes again part of the budget statement, that that's -- so we can see a statement of our cash position each year and kind of know where it is.

CHAIRPERSON JACOBS: And also just setting targets for lending activities, for new lending activities. I mean we're fortunate that we have the legacy stuff, but I think -- and again, budgets, it's a goal. And we need not think of it so much as the way government budgeting is done, where we know exactly what we're going to spend on these things, but let's target the revenues and set some goals for ourselves.

MS. SOTELO: So as part of the budget discussion, Claudia, I'm wondering -- you know, there's a tremendous increase in the single-family activity from 39 loans up to 927 loans, which then supports the yellow box that you have on page 20. So that's a -- that's a huge increase. And then on the multifamily side, you're going programmatically from three issuer and two conduit loans to 20 and six. Right? So programmatically and operationally, that's a huge leap between, you know, last year and this year.

So in our budget discussion -- and this is just a precursor, I guess, but in our budget discussion, can we talk about what happens operationally, what that means in terms of the number of staff people that will support that activity, and, you know, what controls will you have during the fiscal year to check in to see how we're doing in terms of that volume?

MS. CAPPIO: Sure. And I guess this -- we'll hold that, if we can, because right now, we're in the middle of the strategic business plan. If you want to move to the budget, we would have not discussed the strategic business plan, so I'm just thinking --

CHAIRPERSON JACOBS: I think we can run them concurrently.

MS. CAPPIO: Okay. So do you want the budget presentation right now and then you discuss them together?

CHAIRPERSON JACOBS: Yeah, I think it makes sense to do it altogether. And frankly, on approving the budget, I almost think we ought to approve the budget and the business plan together and it may be that we do it at the next meeting with -- you know, with the goals set out in a numeric table. If that makes -- I mean unless --

MS. CAPPIO: We operate a June 30 --

CHAIRPERSON JACOBS: We have to have it done by then.

MS. CAPPIO: Well, we could have a special meeting.

CHAIRPERSON JACOBS: Well, we could approve subject to seeing that table in there. I think that might be --

MS. SOTELO: Why don't we have a joint discussion and see where we are at the end of that discussion to see whether -- how many outstanding items there are.

CHAIRPERSON JACOBS: It's really goal setting on both sides, and I think certainly on the expense side we understand it, and I think it would be good for us to put those tables into a fixed set of goals, if you will.

MS. CAPPIO: Okay. So right now, we're on item 5, and I think the Board wants to have the presentation on item 6, which is the draft budget, and then we pull them altogether. I will note to you, even if you want to -- if you do choose to adopt them, we do have two separate resolutions that we --

CHAIRPERSON JACOBS: Correct.

MS. CAPPIO: Okay. I just wanted to be sure.

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Item 6. Discussion, recommendation and possible action regarding the adoption of a resolution approving the Fiscal Year 2014/2015 CalHFA Operating Budget. (Resolution 14-06)

MS. CAPPIO: So I'll introduce item 6, which is the proposed budget for fiscal year '14/15. And Jackie Riley will make the presentation, since you've all already reviewed it.

MS. RILEY: Good morning.

I had sent last week this budgeted versus actuals as we've been taking a little bit of a historic look back on some of our expenditures and numbers of loans and all of that. So with this, you can see we put in the OPOB, which is the other postoperative benefits, and it is shown as a projection. It's not budgeted for. It's not expensed out. So it's in there, and then it's taken out.

So our projected actuals for the year, we project that we're coming in at 37 to 38 million. It's a little bit more than last year, and I'll show you the next chart here, the little bar graph that last year was a good year as far as expenses. This year we've had some benefit increases, and we've also had a 3 percent increase for those employees who were at the top of their salary range. And since we have a lot of seasoned employees, that was another half million dollars that was not budgeted for last year but has been absorbed. That's generally why the cost we believe will come in a little bit higher this year.

The next chart, I thought -- we decided -- you know, we've been slicing and dicing and looking at everything in the Agency for the last several months, and so we decided to come up with this chart to show kind of where the projected expenses are by program. And we decided even though portfolio management isn't a program -- it is all that back office legacy stuff, but it still takes a lot of resources. And so this is kind of -- this is the Agency's entire projected budget with all of the business operations included, you know, that support each of these program units.

So it's kind of an interesting look. You know, you're looking to see what's eating up the most resources, and in some ways, you know, there's no one that's -- they're all sort of in some ways equal. So I thought I would present that so you can see that. I don't know that you have a copy of that. That was something we just kind of came up with at the end of last week to just kind of look at what those business units or program units were costing us.

CHAIRPERSON JACOBS: This is very helpful. I think again, you know, going forward, it would be helpful to have this match with, you know, what are the revenues generated by these --

MS. CAPPIO: Right. Exactly. We get that.

MS. RILEY: So that's -- these are my little slides. The projected budget this year, which is -- is the 42.8, which is a little bit higher than we had wanted to come in at, but we went through every unit very closely, and we do have a little bit of contingency money in there. We have started out -- the last couple of years we've had an estimated 40 vacancies a year. We eliminated 13 of those. We have come up with 27 vacancies. We're actively recruiting right now for probably about ten to 12 of those vacancies. Beyond that, they've been spoken for, but we're not really sure that they're going to be utilized, because this year we started in on doing sort of a wholistic look at the organization.

And I guess before I get into that I also want to say that the Governor, of course, his May Revise was announced this morning, and there is going to be a 2-percent increase for a lot of our employees. So we did not build that into that 42 million because we weren't sure if it was going to happen or not. And we also have an increase in our CalPERS, the employer's share of CalPERS, that will go into effect in January, and we're not sure what that number is.

So we built in, you know, a little additional money in here through our vacancies. And please always remember that if we don't fill positions, if we don't spend money, it's ours. It just reverts back and goes towards next year's budget, so it isn't lost. It isn't -- it doesn't go away.

So with that, we began to take what I kind of consider a wholistic look at, you know, our business operations, and we've kind of determined that those business operations are really based on our old model of doing business, and we really need to restructure and redefine and retool, though, how we're doing business and how we're allocating positions and resources and all of that. So this is the first time that we've really looked at it so intensely.

And with that, when you get to the people side, which if you look at the budget, the people side of things is really the place, you know, that kind of makes or breaks you as far as saving money. And so we are going at this from a position of looking at our performance management.

I know, Dalila, you had mentioned that, that you were hoping that whatever our strategic things, you know, filtered down to performance management. And we're looking at workload standards for all the units. We've gotten some information from the private sector, also from other HFAs, and trying to figure out, you know, where we're off a little bit; what can we do better; what are they doing differently than we're doing; is it technology; is it something else? So some of the units we know a little bit more about than others. That's why some of the positions may or may not ever get filled if we can determine, okay, they're doing something different and what if we can do it that way too?

So we're also looking at managing our talent, you know, how do we grow talent, and how do we recognize it, and how do we train it? That leads to succession planning. A couple of the positions, two or three, that are in that budget are really for succession planning. We begin to look at units, and you can see there's lot of good people, a lot of hard-working people, but you need to add something right here. You know, they're missing this little piece or that knowledge base or something.

So we're going to be doing a few strategic hires that will hopefully, you know, ensure the long run and the smooth transition as people retire. So we're looking at attrition. There are several positions that we know people will be retiring from, and they will not be refilled.

We're also -- you know, we have office space in Culver City and in Sacramento and in a West Sacramento location. And last year at this time we were really hopeful of using the extra space for PBCIA, but that has not materialized, and we're not really sure we can ever count on that, so we're looking at subletting some of our space.

The other thing that we've been doing just internally is looking at how we manage our records, how do we do that more efficiently, how can we save time but also -- so we, you know, are implementing a scanning facility that we hope will keep our records current but also maybe take some of our records from storage and get them out of storage, where they're more accessible, because we have a lot of paper records from legacy, years past. So we're looking and trying to come up with ways of doing things more efficiently with less.

And I guess lastly I'll say on the balance sheet of the Agency we have a lot of accrued vacation that came about as a result of furloughs and all that, and so it shows up on the balance sheet as a liability, so we're going to this month be sending out for those people who are over the maximum of 640 hours a year, making them come up with some vacation plans to start reducing that amount. The Governor also authorized up to 20 hours of vacation buy-back for managers and supervisors for Unit 9 employees, of which we have a few. And most people that are eligible are taking advantage of cashing out that little 20 hours. So that helps -- you know, if you start, you got to start somewhere, so if you start with that just to, you know, start getting your balance sheet a little bit more in order and start getting rid of some of those liabilities when people retire.

If you have any questions, I can answer them. A lot of the budget is really tied into the strategic plan, so I guess if you have questions I'd be glad to answer anything. I did send you copies of org charts so you can see how we're organized.

CHAIRPERSON JACOBS: Thanks, Jackie.

Does anyone have any questions on the budget?

Jonathan.

MR. HUNTER: Yeah. Is this the time to ask questions on budget detail?

MS. RILEY: Sure.

MR. HUNTER: So I'm looking at page 137 and, you know, the REO disposition. And if I -- that was where I also started really thinking about this, and I wanted to make sure my assumptions are correct. So the -- you're going from one housing finance associate to 12 under disposition and from 14 down to six under administration. I'm assuming this is shifting people from --

MS. RILEY: Actually, during midyear, portfolio management took over some of what had been done in loan servicing, so there are now 13 what are called SPOCs that are -- that are required by HOBAR, single point of contact for loans that are in default that maybe you can do loan modifications for. So our REOs -- our REOs are going down. Our short sales are going down. But right now, we have 13 positions that are doing loss mitigation and really loan mods. And we have, you know, KYHC and all that, so that was transferred from the servicing over. And that happened around the beginning of the year.

MR. HUNTER: Yeah, I guess my question is more I'm assuming that some of the shifting is the reassignment of responsibilities. That doesn't mean we're laying off six people and hiring 12.

MS. RILEY: Oh, no. No, no, no. We have hired no new employees in that area.

MR. HUNTER: Okay.

MS. RILEY: And it really is reallocating people. And what we're hoping for -- because obviously the legacy issues in portfolio management are getting smaller and smaller, which is a good thing, but we're hoping our lending program in single family picks up so those people can matriculate and transition back to lending, which is where most of them are from. Because in days past, we did a lot of lending and very little back office, and now we've been doing more back office than the lending.

MR. HUNTER: Thank you.

MS. SOTELO: Just to be clear on that item, you're going from 27 field positions to 33 authorized positions and 36 proposed positions?

MS. RILEY: Where are we looking at?

MS. SOTELO: The total column under portfolio management on 137 -- 35, I'm sorry, those positions. So you are going to be hiring eight people?

MS. RILEY: Portfolio management shows 33 --

MS. SOTELO: Total portfolio management 27, 33 and 35.

MS. RILEY: I believe those numbers actually, we have -- of the positions that were originally allocated last year for the portfolio management, we -- like I said, we moved over from loan servicing, so the number has gone up, but loan servicing's number has gone down, so they balance themselves out. And actually there are probably less positions between the two units than there were last year.

MS. SOTELO: Yeah, your servicing number is 84 and a half filled and 90 proposed.

MS. RILEY: No. Servicing is --

MS. SOTELO: For all servicing.

MS. RILEY: For -- oh, for -- that's all -- if you look at that 90 --

MS. SOTELO: That's total servicing.

MS. RILEY: -- that's single family.

MS. SOTELO: Right. Okay. So total servicing is 35, 47 and then 30.

MS. RILEY: Right. So you can see that the number from loan servicing went down considerably, by 17. And some of those are the vacant positions that went away. Because we only increased portfolio by two over last year by transitioning that over.

CHAIRPERSON JACOBS: But the overall numbers, I think, still -- the trend is to the -- 2014/15 down to, what is it, 300 employees more or less?

MS. RILEY: Are you talking overall?

CHAIRPERSON JACOBS: Overall.

MS. RILEY: Overall we have been, you know, over 300. This year it's 285 permanent positions. And we're hoping to come in next year at less than that.

MS. SOTELO: So this goes back to, I guess, my question back to the, you know, 900, increasing the production on the single-family side and increasing the production on multifamily.

MS. CAPPIO: Sure. So as Jackie has just relayed, there's a big connection between portfolio management and loan lending. The modifications that we've had to do in our portfolio have a lot of similar skill sets to loan origination and underwriting, both strong underwriting skills. So as the loan -- the portfolio management requirements and demands have decreased, those people will be redeployed to lending, back to lending, and we have a plan to do that, depending on the demand that we see in single-family lending.

As for multiple family, I will note a lot of our current activity in the last couple years has been via the Mental Health Services Act, the lending we did on the permanent supportive housing. And that is winding down. So again, the timing is serendipitous in terms redeploying those people for the lending that we would like to do, that we aspire to do.

So we think this fiscal year with the employees that we've got, we can make those transitions as we need to during the year to accommodate increased lending activity for both single family and multiple family.

MS. FALK: And come out with a net zero for hiring new employees.

MS. SOTELO: That's very creative. That's -- that's really good. I commend you for doing that.

MS. CAPPIO: Timing is everything, as they say.

MS. SOTELO: Yeah. So in terms of keeping track of the volume, right, and checking in, is there a plan to check in to find out whether you're on track to increase production by that 927?

MS. CAPPIO: Check in with the Board or --

MS. SOTELO: Or just what is your management plan or operational plan to see that you're on track?

MS. CAPPIO: Sure. We -- the strategic plan that we -- that you all hopefully will adopt today is a living document that we use as senior staff quite frequently, and at least once a quarter we check in with regard to the dates, the status of the program and the fulfillment of the actions. And so it's a very live kind of an effort throughout the year.

And I will note that it's been our practice to check in with the Board about how we're doing on those at midyear, which is January of '15. If the Board wants to do that prior, I will be glad to do that.

MS. RILEY: The other thing that I have noted is about monthly there are some status reports on how many loans, how many new -- people are really -- the program areas are really keeping track of what they're doing. And they know when the -- you know, on single family, how many loans are falling out, why they're falling out, so we're getting some really good statistics that are helping manage and manage, you know, from the budget standpoint, you know, from the people standpoint and, you know, are you going to need somebody. You know, are you going to -- Ken has numbers that will show up in the strategic plan and if there's this many loans, here's how many people he needs.

MS. SOTELO: I've been very impressed with the team and Ken in particular in terms of saying, you know, in order to achieve 927, we need to do 20 loans a week, and, you know, they have implications for how that happens. And so it's good to see that you're tying that goal to the operating budget.

CHAIRPERSON JACOBS: My question is do you have anything from us that you need in order to be flexible enough to adapt?

MS. RILEY: With this budget, if this budget is approved, yes. I think that, like I said, we have some contingency in there. I'm hoping that next year at this time we'll be seeing that we didn't expense all that we had because our goal is really how do we do things more efficiently for less? And we want to use all the resources we have. And we do have some attrition -- because a lot of our employees have been there a long time -- we don't really plan on filling. We plan on reassigning or, you know, moving people around. So that's our goal.

CHAIRPERSON JACOBS: Any further questions from the Board?

Does anyone want to move to approve the budget? Subject to us getting our little table.

MS. FALK: I make a motion to approve the budget, which I assume is the pages --

MS. CAPPIO: I want to know what you're exactly --

CHAIRPERSON JACOBS: Item 6, which is --

MS. FALK: Page 129.

CHAIRPERSON JACOBS: 129.

MS. FALK: Subject to taking the information in Tim's charts, particularly page -- what's on page 20, maybe. Is that the right page? And then putting that into number form and putting in the revenue side.

MS. CAPPIO: So that revenues and expenses appear on one summary sheet for '14/15.

MS. FALK: That's what we're approving. So we're not just approving this list of expenses, we're also approving the revenue that is to be generated.

CHAIRPERSON JACOBS: Understanding full well that some, you know, loan prepayments we can't really predict.

MS. FALK: Right. Exactly.

MR. JAMES: I'm sorry, Mr. Chair, may I ask a question for clarification? Would it be the Board's pleasure to adopt the budget but then ask that the staff return with the information that you asked for, at which point you could modify the budget?

MS. FALK: Yeah, I want to make it clear that we're approving the revenue as well the expenses; we're not just approving the expenditures.

MR. JAMES: Okay.

MS. SOTELO: We have a -- don't we have a resolution on page 143, which is the resolution that we're adopting?

CHAIRPERSON JACOBS: Yes.

MS. SOTELO: Why don't we turn to that and take a look at that to see whether we need to amend that or adopt as resolved.

CHAIRPERSON JACOBS: I think the resolution is fine, but.

MR. JAMES: Yeah, I think that the resolutions accomplish the Board's goals. I think what I'm hearing from Ms. Falk is that -- and other members of the Board is that you want information presented in a different way having to do with revenues and expenses. So I guess my only question is did you want to review it in that revised format and have the budget -- assuming you approve it today, but have it come back to you for review and --

MS. FALK: Well, it would be nice to see it again, but I think since you need to have it approved, I guess part of the problem for me is that I don't think of a budget as just the expenditure side, and that the real important thing is the relationship between the income and the expenditures, not just the expenditures. So that's why I really feel it's really important to see both and to see what the bottom line is. So in adopting -- the resolution just says the operating budget attached, which is these pages here, which --

MS. CAPPIO: Does not contain --

MS. FALK: -- does not contain the revenue side.

CHAIRPERSON JACOBS: The content, we're well aware, that it exists and is --

MS. FALK: And it's the content that's in those charts. It just needs to be translated into this format.

MR. HSU: So my proposed compromise, I can run back to the office real fast to produce the chart and bring it back, so you just all talk slowly for the next 30 minutes.

MS. FALK: I don't -- I hate to have you do that. Is there some way we can approve it that we can, like, send it around and just everybody says okay? I mean, we've got the information pretty much attached.

CHAIRPERSON JACOBS: Let’s move to approve the budget and then confirm the additional exhibit at our next meeting.

MS. FALK: Okay.

MS. SOTELO: An operating budget is an operating budget, and, you know, if we're comfortable with the staff levels and the operating budget as it's presented, that's one action that we can take. In terms of the revenues, there's nothing to -- I mean, we can have it presented, but there’s really nothing to approve on the revenues because it's projected. It's not actuals.

CHAIRPERSON JACOBS: Correct. It's a matter of goal setting and just how we look towards as a business plan setting some numbers to the business plan so we'll work towards those goals. I think that's really -- I think we've all reviewed the business plan, too, and this is to further the business plan along, I think is the intent here.

MS. FALK: Well, I just want to clarify one thing, though. If Tim's projections had shown that we were going to be in a big deficit gap this year, then I wouldn't approve the operating budget as it is, and you probably wouldn't want us to do that, so that's why I think they have to go together.

CHAIRPERSON JACOBS: Does anyone want to make a motion?

MS. FALK: I'll make to motion to approve it.

CHAIRPERSON JACOBS: Do we have a second?

John's microphone isn't on.

MS. SOTELO: My microphone is on. I'll second.

MR. HUNTER: I just wanted to see if I could state this a little different way in terms of how I understand the basic question that Janet is raising. It's that we're being presented with an operating budget, and that operating budget is clearly based on some revenue assumptions. And it would just be helpful -- I mean, we've walked through all those revenue assumptions with all those boxes and charts, but it would helpful to see them in numerical format alongside.

And then I think it's important to recognize that we're not necessarily approving the revenue assumptions as an operating revenue, but we are saying that that is clearly the goal and the assumptions. As reports come in during the year, if we see that we're not meeting our assumptions, we know we have to adjust what we're doing on the expenditure side. So that's -- I think that's what we're trying to get at.

CHAIRPERSON JACOBS: Elegantly stated.

MS. RILEY: We know we need to adjust, too, on our side.

CHAIRPERSON JACOBS: So we have a motion on the table to approve the operating budget.

MR. HUNTER: And I'll second that motion.

CHAIRPERSON JACOBS: And then at the next meeting we'll have the exhibit.

JoJo, call the roll.

MS. OJIMA: Thank you.

Ms. Caballero.

MS. CABALLERO: Aye.

MS. OJIMA: Ms. Whittall-Scherfee.

MS. WHITTALL-SCHERFEE: Aye.

MS. OJIMA: Ms. Falk.

MS. FALK: Aye.

MS. OJIMA: Ms. Gunn.

MS. GUNN: Aye.

MS. OJIMA: Mr. Gunning.

MR. GUNNING: Aye.

MS. OJIMA: Mr. Hunter.

MR. HUNTER: Aye.

MS. OJIMA: Ms. Carroll.

MS. CARROLL: Aye.

MS. OJIMA: Mr. Prince.

MR. PRINCE: Aye.

MS. OJIMA: Ms. Sotelo.

MS. SOTELO: Aye.

MS. OJIMA: Mr. Jacobs.

CHAIRPERSON JACOBS: Aye.

MS. OJIMA: Resolution 14-06 has been approved.

MS. RILEY: Thank you very much.

CHAIRPERSON JACOBS: So let's jump back then to the strategic plan, too, because I believe we are approving the plan as well. So I think -- does anyone have additional comments on the plan, other than the fact that we should be, again, tying into specific goal setting?

I guess I have one comment on this before we jump into it. It's really I guess the elusive question of what is our permanent source for funding for affordable housing in this state and our quest to find that?

MS. CAPPIO: That's a good question.

CHAIRPERSON JACOBS: I know we have some additional informational items on the recent discussion in the Legislature, but -- would you want to address that now, or --

MS. CAPPIO: I can. I mean, I think we have to first reflect on the fact that this Agency would not be necessarily a direct beneficiary of that funding, that we have always relied on independent sources of revenues through the sale of tax-exempt instruments. And so we have contracted and entered into interagency agreements for certain aspects of additional funding. Prop 1C, we administered the downpayment assistance program. There are various proposals out there. There's a bill in the Legislature, SB 391, that would create a fee on recordation of documents pertaining to -- well, on anything, actually, other than the sale of single-family homes. And that is paused at this point.

The administration has not taken a position on any permanent source of funding or revenue stream, although I think there's acknowledgment that it's an important piece of the puzzle.

So we are going to get to the cap and trade proposals. It does remain a big issue.

CHAIRPERSON JACOBS: Does anyone have any questions or comments about the business plan?

MR. HUNTER: I had a comment and -- I think it's a comment. I don't think it's a question, but it kind of goes back again to how we're seeing the numbers presented. I was glad to see in the business plan that there are specific targets for generating revenue that we've just been talking about. So if I'm looking at -- in the plan, strategy No. 7, revenue targets for first mortgage loans and for DPA loans. And the thing that was -- that I found a little -- I realize it's hard to, you know -- we're kind of looking at the numbers in different ways, so when we saw the report earlier, we looked at the number of loans, and then we saw some estimate of what the fee would be generated. And I just -- I was glad to see that the revenue -- that the goal for the staff is to hit a revenue number and not a loan number, because it may be that we get five loans that raise the whole revenue, as opposed to getting 20 loans to raise the whole revenue.

But at some point it just, you know, would be interesting to see kind of what that -- how the averages go over time in terms of what's the average size of loan that we're actually doing. I would be interested in seeing that. So just a report going forward, it would be interesting to see -- I would be interested in seeing that. I just would say, again, that I was glad to see the actual revenue targets in the -- in the plan.

CHAIRPERSON JACOBS: Janet.

MS. FALK: I'm going back to what Tim presented to get us -- to help us understand the picture that these legacy fees and things are going down, and we're really going to have to generate some more revenue, and I really appreciate that items 6 and 7 in the business plan talk about those things. However, I think the most -- it looks to me like they're mostly looking at things that kind of sort of really currently exist or sort of are out there, we're just not taking advantage of them.

But I'd almost like to see a new item of thinking outside the box. What other areas can we go to in the future? They may not -- it may not happen in this next year, but to start really thinking about, you know, creating a multiyear plan of where -- what are some other opportunities? What can we do in a creative way? Because that revenue that we have to generate is really key. And, you know, playing around the edges where we currently are may not get us to where we need to be.

MS. SOTELO: Yeah, I would totally support that, adding that as a goal for the organization, to look at diversifying our income or our program income and making that maybe an operational goal, that staff spends time and, you know, gets acknowledgment for spending that time to look at it and reports back to us as part of the plan. So I like that. I like -- you know, if staff is open to it, I think it would be a nice goal to add.

CHAIRPERSON JACOBS: So it's a slight restatement of our goals, but I think it --

MS. CAPPIO: Yeah, I think we can incorporate that. It's understood.

CHAIRPERSON JACOBS: Any other comments about the plan?

MR. PRINCE: Yes, I'm sorry. So if I heard you correctly, Tim, the $40 million of operating -- one-year operating is pretty substantial, as well as the collateral is about $50 million, so there's $90 million -- I don't know, I'm a developer -- at all times. It sure seems like that's a great opportunity to -- yes, it's very safe the way it is, but maybe there's a higher purpose to be using those dollars in a thoughtful way. So I would support also looking at new initiatives, new investments, to generate revenue but also take advantage of the funds that the Agency has. I think that's a new strategic line item for you, Claudia, isn't it?

MS. CAPPIO: Yeah. I'm just looking about where to put it in the best way. Yeah. We have for the one in six, we have the C. Six C, is to create a multiyear plan to identify the use of certain funds that we have to look at how we can add value to the lending that we do do, by the use of sort of outside-the-box thinking about the use of these funds that we've got. We can either add a D or modify C.

And similarly with seven, we have some specific things that we're going to do, as you requested, for instance, mortgage products to non-first-time homebuyers, the CalVet, working more closely with CalVet. But we can easily add, I guess, I, review other programs and lending products, you know, that we could use in the future. We could modify that accordingly.

MS. SOTELO: How about doing it as part of the goal, right? So the way this is organized is there’s the goal for the organization and you have four goals, so if you add it as a fifth goal, and then the key strategies, like you were trying to do right now, just fit it into different key strategies. But the goal itself is an affirmative goal of diversifying, you know -- think creatively about diversifying income. I mean, we can -- we can come up with a phrase, phraseology for it.

MS. CAPPIO: Sure. That would be acceptable as well. That's an overarching --

MS. SOTELO: That's an overarching goal that's manifested through key strategies in the different areas.

CHAIRPERSON JACOBS: Does anyone want to move for approval of this subject to the addition of the new goal?

MR. GUNNING: So moved.

CHAIRPERSON JACOBS: Do we have a second?

MR. PRINCE: I'll second.

CHAIRPERSON JACOBS: JoJo.

MS. OJIMA: Thank you.

Ms. Caballero.

MS. CABALLERO: Yes.

MS. OJIMA: Ms. Whittall-Scherfee.

MS. WHITTALL-SCHERFEE: Yes.

MS. OJIMA: Ms. Falk.

MS. FALK: Yes.

MS. OJIMA: Ms. Gunn.

MS. GUNN: Yes.

MS. OJIMA: Mr. Gunning.

MR. GUNNING: Yes.

MS. OJIMA: Mr. Hunter.

MR. HUNTER: Yes.

MS. OJIMA: Ms. Carroll.

MS. CARROLL: Yes.

MS. OJIMA: Mr. Prince.

MR. PRINCE: Yes.

MS. OJIMA: Ms. Sotelo.

MS. SOTELO: Aye.

MS. OJIMA: Mr. Jacobs.

CHAIRPERSON JACOBS: Aye.

MS. OJIMA: Resolution 14-05 has been approved.

CHAIRPERSON JACOBS: And let's take a five-minute recess, if we will, and let's try to keep it to five minutes even though the restrooms in this end of the building are closed.

(Recess taken.)

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Item 7. Discussion of CalHFA's authority to lend directly to homebuyers in the Single Family program.

CHAIRPERSON JACOBS: Great. Let's move on to item 7, the single-family direct lending. We've got Rick here.

MR. OKIKAWA: Good morning -- we can just make it as good morning, anyway -- Mr. Chairman, members of the Board.

Last meeting, there was an open discussion about direct lending and the benefits of direct lending. Part of the discussion included discussion about cutting out the middleman and some of those benefits that could be had from cutting out the middleman and to pass those on to the borrower and the Agency. However, the issue came up about direct lending itself, and that's why Tom Freeburger, our assistant general counsel, has written this memo to the board. And he'd like to go over briefly what that memo is and answer any questions that you might have.

MR. FREEBURGER: Good morning. Just in case you might not have had an opportunity to look at it, I'll just quickly go through. And the main point is we are currently statutorily prohibited from direct lending. There are a couple of exceptions, which don't really -- have never come into play. And we have some limited exceptions for some downpayment assistance which, fortunately, we have not had to use.

This came about when we were first created. The savings and loans basically fought our doing that, and the compromise was we could buy loans they originated, but we couldn't originate them ourselves. Whether that will continue on with the current industry, I wouldn't know. At least I suspect that perhaps.

There are also substantial risks to the Agency were we to engage in this. Basically, one would be real estate risks because when we sold those loans to a master servicer to be securitized, we would have a repurchase obligation for any failure on warranties or many other things that might go wrong with the loan. And there's been a lot of press lately about Fannie, Freddie and other securitizers going back against loan originators to repurchase billions of dollars worth of loans.

And then there's also regulatory risk because there are many, many rules governing these, which then theoretically could expose us to sanctions from the appropriate government entity.

And lastly, there are other very significant considerations here, IT among them, and also staffing to handle the work that would go with being loan officers and originating loans and the very substantial issue of staffing for compliance, which for those of you who read anything about Frank -- Dodd-Frank or FHA, there are so many, so many, regulations to be dealt with now that it's an up and coming source of jobs, is just compliance officers and compliance attorneys. Expensive, hard to find and even if we farmed it out, it would be very expensive.

So I'd be glad to answer any questions you have or expand on something, but at the moment we're not allowed to. And if we wanted to look at it at some time in the future, those are the type of issues that would have to be considered and addressed.

MR. GUNNING: Mr. Chairman?

Tom, in the public finance business, we used to categorize lawyers in two buckets: Ones that said, no, you can't do the deal and, two, that said, yes, you can do the deal. You seem to be in the first bucket here. Is there a way to do it? I mean, what if you think about it differently? And I know all the cautions you provided --

MR. FREEBURGER: The first way to do it is we have to go to the Legislature and get their permission, and that's why I alluded whether or not lenders now would care whether we did that or would see us as a source of competition that they'd rather not have, I could only surmise. But we would have to go to the Legislature. It would be some work. Di would be much better able to address what the possibilities of that might be --

MR. GUNNING: We know Di can get it done.

MR. FREEBURGER: -- but that would be the first step. Pardon me?

MR. GUNNING: We know Di can get it done. She can work miracles in that building.

MS. FALK: Well, if we were going to be exploring this at all, I'd rather see it be part of the business plan and part of the new revenue and, you know, look at this versus other kinds of things, if that's -- I mean, I personally don't want to go in that direction, but if that's what people are interested in. I'd rather see it be taken a look at and studied before we go any further.

CHAIRPERSON JACOBS: Agreed.

MR. FREEBURGER: I might mention, you know, things change. This is not a question that's come up for the first time since I've been here. It comes up regularly every couple of years if we have a new director of lending or something, but the big objection was, years back, brick and mortar. Well, that's not the same consideration now. You don't have to have 500 loan offices across the state. But now there's other reasons that we'd have to think about. That one's gone. Times do change. And in the future perhaps it should be looked at again, but right now, with the constraints and the risks that we're currently addressing, I'd caution to be careful about that going into it and look at all the things that I have mentioned.

CHAIRPERSON JACOBS: Thank you, Tom.

Any other questions on this item?

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Item 8. Discussion to expand CalHFA's mortgage products to include low or moderate income non-first-time homebuyers who are not in targeted areas.

CHAIRPERSON JACOBS: Let's move on to No. 8, non-first-time homebuyers.

MR. GIEBEL: Good morning. Thanks for the chance to talk about single-family lending. It seems to be a hot topic. Sheryl Angst is our secondary marketing chief.

Just something that was mentioned earlier, before I get into this, we do track every loan, every day from reservation to purchase, and that would include CHDAPs, downpayment assistance, first mortgages. Right now it's the FHAs and our MCCs and our Extra Credit Teacher Program. So we can tell you on any given day how many have been purchased and how many reservations we have. For example, I think the number was 38 that we've actually purchased, first mortgages. We have 90 in the queue. Just to let you know, our dropout rate is about 20 percent. So we'd be happy to share those numbers with you.

What we're about to present to you is a discussion about expanding our capabilities on lending to another target audience. Right now we are focused, except in targeted areas, on first-time homebuyers. We started that way with our FHA product. Monday we are going to announce our 97-percent conventional product, along with our energy efficient program. That will go out to the marketplace on Monday.

And this discussion is to expand the target audience -- and I'll take you through this -- to non-first-time homebuyers across the state. Low to moderate income, same requirements, and -- as we have for the first-time homebuyers, but it's just another target market. So Sheryl will -- Sheryl and I will take you through the presentation, and please ask any questions as we go through.

Just to let you know, CalHFA statutes permit lending to non-first-time homebuyers. It's not a statute issue. Two, the TBA market does not have a first-time homebuyer requirement. It's not a mortgage revenue bond requirement, as we had in the past. That was federal with the tax exemption. It was -- the target was first-time homebuyers, as the MCC is, for example. Many of the HFAs over the last three years have expanded across the country in their states to non-first-time homebuyers because there's a need, and we'll talk about that in a minute.

Just quickly, some of the benefits that we have identified is, again, as you've seen in all the publications, renting continues to be more expensive than purchasing a home -- particularly in the eight counties, which I'll show you in a minute, than a purchase of a home at our interest rates today. Today our FHA first is 3.75, and our Cal Plus FHA product is 4 and a quarter. So we have very good interest rates, and they can save a considerable amount of money if they can qualify to purchase.

Two, a lot of people in low to moderate income areas have the ability to move up now that their houses are no longer under water, and this product, our products, would give them opportunity to move up based on family needs, and it's, again, within our income and sales price limits.

Distressed homeowners, which we know there's a significant number of distressed homeowners still in the state, this would also help those people, for example, people who have gone through a divorce and they are on a deed and wouldn't qualify as a first-time homebuyer. Two, people who have gone through short sales and -- in the last three years, they can get back in the market with this product and have across the states. And other people who have run into other issues would have the ability to buy that were homebuyers in the last three years.

Sheryl, why don't you talk about what FHA permits on the people who have -- in the last two or three years have gone through the short sale process and that type of thing.

MS. ANGST: In general, the industry does have a three-year requirement for anybody who's had a foreclosure, bankruptcy, et cetera. FHA has -- under extenuating circumstances does allow people after two years, if they can prove that the extenuating circumstances happened, they have recovered from it and they have reestablished credit, to now purchase a home after two years.

MR. GIEBEL: So FHA does permit this in their -- in the process.

The last thing with our conventional product is we have -- Fannie permits you -- this was a Fannie preferred product only for housing finance agencies across the country. They permit 140-percent average AMI, area medium income. They permit that.

In the outlying areas where housing is -- you see increases, we think this -- our conventional product will be helpful to this particular segment of the market, but there is one caveat with this. The sales price limit is $417,000. So regardless of what the income is, with Fannie, Freddie, and also FHA, you're at 417, and that will be the law of the land as of the first of the year.

And the last area is it's an additional area for us to generate some revenue. It's a little bit larger market.

MS. ANGST: The homeowner requirements for this are going to be very similar to what we're doing now. They're going to be low and moderate income borrowers.

They cannot have an ownership interest in any other property at the time of loan closing. We're going to go ahead and mirror the Fannie Mae guidelines, which does not allow them to own a second home, a rental or a manufactured house at all.

They have to meet all the existing CalHFA and partner underwriting guidelines as far as DTA, the cash into the transaction, the homebuyer education and the home warranty. And they have to meet the Fannie Mae and FHA limits of 417.

MR. GIEBEL: Just, we looked - again, I talked about our target markets. We have eight. We do around 75 to 80 percent of our loans in these markets on the CHDAP side, downpayment assistance. And I know as you've read before, you can see what the challenge is here. If you look at listings, 417 and below, there's just not a whole lot of inventory there. That's why in our large number that you saw, our goal of the 900 and the 1200 number, if we get a one percent to a one and half percent share of this business in those target markets where we're already providing downpayment assistance, you can see that's 250 to 360 loans of our -- just this particular segment of the market.

We will probably pick up some loans in the East Bay, in the Bay Area, San Diego, Orange County, but we haven't counted those in our forecast. Okay? Just to let you know the size of the market that we're looking at.

I think it's very interesting if you look at the county of Los Angeles, there's only 5600 listings of 417 and below. That's why first-time homebuyer numbers are dropping from the usual third of the marketplace to the low 20s, because it's not only the restrictions on underwriting with FICOs and DTIs, it's also becoming a matter of inventory across the state.

MS. CABALLERO: I have one question.

MR. GIEBEL: Sure.

MS. CABALLERO: How were the targeted counties identified? What were the criteria that you used?

MR. GIEBEL: Our criteria is we have -- we will do about -- over 4,000 CHDAP loans this year, and they provide the 3 percent downpayment assistance. So every six months, we look at where those loans are going, because you have -- they're -- they're targeted to first-time homebuyers and low to moderate. In fact, they're pretty low income, compared to conventional loans. So we look at where those loans are done. And they're not all -- all our firsts have CHDAPs, but all the CHDAPs basically meet the income limits, so we use that as our base of where those properties are being sold, marketed.

MS. CABALLERO: So is there a possibility of identifying other counties? The reason I say that is because I think the understanding that in L.A. trying to get -- trying to identify properties that sell under $400,000 is important, yet if you take a look at the Central Valley starting in Stanislaus County all the way down to Madera, you probably could find, I'm guessing, ten times the amount of housing stock, mostly because those were the commuter communities that were expanded into during the rapid growth of the housing market. And those -- that housing stock, with the collapse, means that they're significantly under the 400,000. I'm just --

MR. GIEBEL: Well, if you just look at this quickly, Secretary, you'll see in the county of Fresno, there's a much higher percentage of 417. These are just listings. We picked these up from Trulia. This was what was on the market four weeks ago. And if you look at San Bernardino, you can see the vast majority, over 50 percent, is with -- below 417. So those are our targets and filling in behind that.

The conventional product is going to be a little bit different because it's a 97. Nobody else has it. So we are projecting that in the outlying areas in the higher cost counties we will get additional business. But these, we target all our marketing and outreach to these markets.

MS. CABALLERO: I guess I'm just trying to figure out if we can -- from our perspective, if we can impact that in a way that might be substantive in terms of this actually working really well in certain markets. That's the reason for the question. I appreciate that, thank you.

CHAIRPERSON JACOBS: Is the 417 limit the same for duplex or triplex properties?

MS. ANGST: No, it will actually go up with the amount of residents, units.

CHAIRPERSON JACOBS: Okay, thanks.

MS. ANGST: This is just a snapshot of what we are currently offering to our first-time homebuyer programs. As you see, we have the five first mortgage --

MR. GIEBEL: As of Monday.

MS. ANGST: As of Monday we have the five first mortgage products, and they are TBA financed and allow subordinate financing, the ZIP, the CHDAP or the Extra Credit Teacher Program and the MCC. When we flip over to the next page, this is what our non-first-time homebuyers lending program would be. So we still have our five first-time -- first mortgage loan programs, but the CHDAP, the Extra Credit Teacher Program and the MCC go away because those are bond financed, and they're not allowed.

MR. GIEBEL: So this is just another piece of the puzzle to get to our volume goals while serving our mission of -- to low to moderate homebuyers in the state of California and addressing needs. Because this product that's up here, there isn't another product on the market like it.

MS. SOTELO: Ken, how would you define success and when you measure that success of this program that you're launching on Monday? Can you kind of give us --

MR. GIEBEL: We will -- we will probably need six months to take a look at it. I think I mentioned this the other day. Our big challenge right now, as is almost everybody's in the lending business, is to get our lenders -- not the loan officers, but to get our lenders to put these products on their lending platforms.

We have over 90 CalHFA-approved lenders. We have slightly over 50, it might be 55 now, that are approved by U.S. Bank, our master servicer, to do these loans. We have slightly less than that that are approved by Fannie Mae, but we can cover those through the U.S. master servicer's approval by Fannie. We have as of last Friday about 28 lenders of that 50 that have actually submitted a reservation. Our challenge -- and we are spending all our time on getting them to load the product because we can't spend a dime on letting borrowers or doing outreach per se -- not training, but outreach -- until we get enough lenders to get us to those goal numbers we need. That's our challenge.

MS. SOTELO: So again, just so that we're all on the same page, what are your goal numbers and when -- I mean, how -- how often will you -- can you report back to the Board in terms of --

MR. GIEBEL: We can -- we can report monthly. I mean, as you meet, we can report every Board meeting.

MS. CAPPIO: We can add it to the reports on the back of the agenda that we don't necessarily talk about at the meeting but are provided to the Board.

MS. SOTELO: Yeah, because I think it would be important to look at the targeted counties and to see how you're performing in each of those targeted counties. And if the performance is less than you anticipate, to then readjust and target other counties that may have better play for us on the market side.

MR. GIEBEL: It takes us at least 60 to 90 days to get the loan officers trained once they load the --

trained and then you start seeing the volume. Just to let you know on the FHA product that we've been -- had out there since the 26th of August, over the last six weeks we have almost -- or eight weeks, we have half of the volume I mentioned to you. So it's taken that long to get them loaded, and we probably have added a dozen in the last 40 days, lenders, to put it on their platform.

Okay? Thank you.

MR. GUNNING: And I had a follow-up question to that, and I guess it goes to last year this time, I don't remember what the product was, but the number of projections you made for that product, how many you've actually done and where do you plan to be at fiscal year end?

MR. GIEBEL: We -- we had projected last year 600 on the FHA only product. Okay. Needless to say, we didn't -- I don't know if you would say we were naive -- and that was based on what other FHAs had done -- states of Washington, Texas -- with the same products. We just couldn't get people to put it on their platforms, Michael. It took us till the first of the year to get a dozen lenders to put the FHA product on their platform.

MR. GUNNING: So the numbers --

MR. GIEBEL: Oh, one of the reasons why that

January number is, is because of Dodd-Frank. They weren't loading anything. They had to do -- load all their requirements for FHA and for Fannie and, you know, the basic lending industry.

MS. FALK: So I have a follow-up question to that, which is how many -- if we do this, how many new loans are you projecting either in terms of number of loans or volume, total dollar amount? How much is it going to add?

MR. GIEBEL: Well, the numbers -- the goals, the numbers you saw earlier that go from July to June '14/15 the 900 and the 1200 number, the higher one, those are our goals.

MS. FALK: But that's -- that includes this and other things. How much is this new --

MR. GIEBEL: We are projecting --

MS. FALK: -- program going to add?

MR. GIEBEL: We projected as we have on the conventional and the FHA, when we've gone back and done the numbers, a one and a half percent share. So out of those numbers you saw, the 24 percent, it's about 360 loans from the non-first-time homebuyer market.

MS. FALK: So that 927, 300-plus is going to come from this.

MR. GIEBEL: Yes.

MS. FALK: Okay, great.

MR. GIEBEL: It's in here.

MS. FALK: Yeah.

MR. GIEBEL: That's how we built those numbers.

MS. FALK: It's good to see those kinds of numbers when we see the program because then we have a sense of what it's going to do.

MR. GIEBEL: We've gone through the waterfall of each program and how many loans we anticipate and what the range is. And then the revenue fees that go along with that, that's in the number you saw for revenues.

CHAIRPERSON JACOBS: Thank you.

MR. GIEBEL: Thanks.

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Item 9. Discussion, recommendation and possible action regarding the adoption of a resolution to authorize hedging loan commitments as a financing strategy. (Resolution 14-07)

CHAIRPERSON JACOBS: Next we've got a discussion of our master hedge policy. Tony, hi.

MR. SERTICH: Yes, good afternoon.

We've had many discussions on our hedge policy and our hopes to do future hedging. Last meeting I think Mr. Jacobs had requested that we --

(Court reporter interrupts for clarification of the record.)

MR. SERTICH: So last meeting Mr. Jacobs had proposed that maybe we come with a resolution this time to finally talk about moving forward with this. So what we're doing today is we are asking for permission for two things. One is to do hedges, two different type of hedges. One is single-family loan commitment hedges. The resolutions asks for permission to do $200 million worth of single-family loan commitment hedges under the Agency's TBA program, as Ken and Sheryl talked about, through early next year. We could come back with a resolution every year, along with the financing resolutions that we did last -- we came to you last Board meeting with. And $40 million of multifamily loan commitment hedges. These numbers tie to the goals in the business plan, so we would -- we're not asking to do hedges in excess of anything that's in the business plan right now.

Second thing in the resolution is adoption of the master hedge policy. The master hedge policy provides a framework within which we will do all of these hedges. It is the -- last meeting we talked a lot about the hedge policy and what's in it. There's been a couple of changes that have been made since last meeting. One was we put more clear limits on market exposure we'll take on the hedges. And then the rest of the changes are just clarifying changes, some language changes, but nothing too significant.

And then the -- but both the red-line version and the original version were presented as part of the Board package, I believe. And, again, the master hedge policy will be presented next year when we come back with another resolution, along with the financing resolutions, if we have any changes that need to be made to that or earlier if there’s -- if the program is not working as we planned.

MS. CAPPIO: We had just a question through the chair.

CHAIRPERSON JACOBS: Yes.

MS. CAPPIO: That the one handed out this morning is the clean version of the red line.

MR. SERTICH: Correct.

MS. CAPPIO: Okay. I just wanted to double-check.

MR. SERTICH: It should be the final version that's in there.

CHAIRPERSON JACOBS: Did everyone get a chance to read the red-line version with just those changes that are proposed? Okay. Great.

MS. CAPPIO: Thank you.

MR. SERTICH: So if there's any questions about this, I'm available for questions.

CHAIRPERSON JACOBS: Does anyone have questions on the edits? I think the edits addressed the concerns that we had. Anyone have a question?

Madame Secretary.

MS. CABALLERO: It actually isn't a question. It's just an observation. I think you've done a really good job of kind of walking us through this so that I feel real comfortable with it, but it would be good at -- maybe in October or thereabouts to kind of give us -- maybe December, the December meeting, an overview of how has this worked, what have been the challenges, that kind of thing. Because March doesn't -- March is -- doesn't line up with the budget in terms of when we'd be looking at the budget for the next year. And so it would be good to have a preview of kind of lessons learned or things we found out doing this, and so that it informs us when we come back in March, we'll be making a decision that's separate from the budget because we won't have the budget at that time. Otherwise I appreciate all the work that's gone into this, because I feel much more comfortable about it.

MR. SERTICH: The only thing I'd like to add is there's no immediate plans for us to do this right away, but it could happen. So we will definitely update you as we move forward with this.

CHAIRPERSON JACOBS: Yeah, I think just as one of the reported items that we may not even discuss at meetings just to -- every time we have meetings, are we using the facility; if so, how much, how's it going.

MR. SERTICH: Yes. I think that would be very doable.

CHAIRPERSON JACOBS: Anyone want to -- we have a resolution here. Does anyone want to bring this up?

MR. HUNTER: I'll be so bold. And also just to say it was really helpful having the red-line and clean edition side by side. Thank you for that.

And with that, I will move approval of Resolution 14-07.

MS. FALK: I'll second.

MR. PRINCE: And I'll provide a hedge to that second just in case -- no.

CHAIRPERSON JACOBS: Let's do the roll.

MS. OJIMA: Ms. Caballero.

MS. CABALLERO: Yes.

MS. OJIMA: Ms. Whittall-Scherfee.

MS. WHITTALL-SCHERFEE: Yes.

MS. OJIMA: Ms. Falk.

MS. FALK: Yes.

MS. OJIMA: Ms. Gunn.

MS. GUNN: Yes.

MS. OJIMA: Mr. Gunning.

MR. GUNNING: Yes.

MS. OJIMA: Mr. Hunter.

MR. HUNTER: Yes.

MS. OJIMA: Ms. Carroll.

MS. CARROLL: Yes.

MS. OJIMA: Mr. Prince.

MR. PRINCE: Yes.

MS. OJIMA: Ms. Sotelo.

MS. SOTELO: Yes.

MS. OJIMA: Mr. Jacobs.

CHAIRPERSON JACOBS: Yes.

MS. OJIMA: Resolution 14-07 had been approved.

CHAIRPERSON JACOBS: Thank you. And thanks for the hard work on that, guys.

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Item 10. Review and Discussion of Two Proposals for Using Greenhouse Gas Reduction Funds (via the Cap and Trade Program in the California Global Warming Solutions Act of 2006) to further sustainable communities and affordable housing.

CHAIRPERSON JACOBS: Let's see. The discussion of these, I guess the cap and trade proposals that have come around, we have a memo from Claudia. Do you have anything to add to that?

MS. CAPPIO: This was at the request of a Board member. There are two proposals, one from the Administration and one from Senator Steinberg. They're both included in your packets.

Just as a brief overview, the sustainable communities implementation initiative is an interagency effort to come to some overarching principles within which to spend the money that would conceivably be allocated to that effort, and there are other expenditures proposed as well -- the high speed rail, the agricultural land preservation, Cal Fire efforts -- all in the -- with the focus of decreasing greenhouse gas. So for us, the initial discussion in our interagency group has been the development of housing and fixtures around transit stations, obviously thus reducing vehicle miles traveled. So it's just information, if you'd like to address any questions.

MS. FALK: I just have a question. What is the Sustainable Growth Council, and who's -- who are its members?

MS. CAPPIO: I will defer to Ken Alex on that, actually.

MR. ALEX: Hi. So I'm the director of the

Governor's Office of Planning and Research and the chair of the Strategic Growth Council. I'll probably get this wrong since we just added three members, but the Strategic Growth Council includes Secretary Caballero, the Secretary of Resources, the Secretary of CalEPA, the Secretary of Transportation -- let's see -- there's one public member.

MS. CAPPIO: Secretary Dooley.

MR. ALEX: Secretary Dooley, Health and Human Services. I'm probably missing one there. Oh, now we've just added Food and Ag, the Secretary of Food and Ag as well. So that's pretty much the group.

And so, as you can tell, with -- the Administration proposal is for $100 million in this coming year out of cap and trade revenues with many mouths to feed and with things like housing and transportation as part of the mix. In addition, because the Williamson Act payments have ended, the $100 million is also intended to cover potentially some issues around agricultural land that would otherwise be developed to keep it in agriculture production. So $100 million is a fairly limited amount of money for all of this, so we're hoping to figure out in the next few months the best possible way to make the 100 million be meaningful for greenhouse gas reduction.

CHAIRPERSON JACOBS: Thanks for answering those questions, actually.

If you would just keep us apprised of this as it progresses.

MS. CAPPIO: And I guess you noted, just for the record, that there's a substantial difference between the Administration's proposal and Senator Steinberg's, so perhaps somewhere in the middle of that is where we'll end up.

MR. ALEX: If I can comment on that, just real quickly, there's some suggestion that the Steinberg proposal is not about this year, and so we need to figure -- there may be in future years, because after this year, the cap and trade revenue will also include money from fuels. So right now -- and that may increase the dollars available quite significantly. So that may be part of the difference between the two proposals.

MS. FALK: One additional question. So in the Steinberg write-up in the back of here, it says that the illustration was for 5 billion, and it says in your memo that the current amount is 850 million, and there's a pretty big gap there. Is it really expected to get to 5 billion?

MS. CAPPIO: I guess I'll note that's projected versus actual.

MR. ALEX: We can hedge a bit, but just to clarify, when fuels come under the cap, it will change the revenue projections pretty significantly. The cap also declines over time. That's the purpose of the cap. And that will also increase the value of -- the credits will conceivably increase the dollar amount as well, so what those dollars are actually, of course you can imagine that we're being fairly conservative.

MR. HUNTER: So I have sort of a -- well, to me, interesting question. It may not be interesting to everybody else. Does CalHFA as an entity advocate or advise various parts of the state government on issues related to the housing needs of low and moderate income Californians? So in other words, as this conversation moves forward, is CalHFA -- is there any way in which CalHFA as a board or as an entity is participating in those conversations as an advocate for the population that we're to serve?

MS. CAPPIO: CalHFA has been an integral part of the sustainable communities group, the interagency group, that has come together for part of the -- for the trailer bill that has been proposed by the Administration. I also provide technical assistance and information. I actually need to stop short of advocacy. That's not been our role, and I think if I may call on my general counsel, I think there's a prohibition against that.

MR. JAMES: Well, yes, it's -- well, advocacy is different from providing technical advice. And because you are a governmental agency, our role is to -- statutorily to provide technical information or advice to the Legislature and, of course, to the Administration where appropriate.

This is an independent board. It can sort of state a position with regards to what its interests are, but as an entity, it cannot advocate in any active way by virtue of our status as a governmental entity.

MS. CAPPIO: So the short answer is I ride a fine line.

MS. FALK: Can the Board take a position on things?

MR. JAMES: Let me get back to you on it. That's an important point, and let me get back to the Board on it.

CHAIRPERSON JACOBS: Okay. I'm sure we'll see this coming back and around as it moves through. All right. Thanks.

MR. HUNTER: I just would say that the reason that I raised that question is that I've been concerned about the trends in transit line development that's actually being built not adequately addressing the needs of low and very low income Californians.

MS. CAPPIO: Thank you.

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Item 11. Reports.

CHAIRPERSON JACOBS: Let's see. We've got a series of reports. Did anyone have specific -- I mean, are these mostly information items?

MS. CAPPIO: That's correct. We normally don't present them, but if there are any questions or you need additional information, we're happy to address that.

MR. HUNTER: Well, I guess I would just say as a part of my sidebar conversation during the break, I do think that as one of the old-timers on the Board, it is so heartening to see the reduction in the delinquent loan trends but also as apropos of our former conversation about the legacy revenues and costs. And it's sort of like as this problem decreases, it does create an interesting corresponding future problem, which is what is the future source of revenue? But I -- it is -- I am pleased to see that the delinquent loan trend continues to be on a downward arch. But also it would be really nice to see future lending activity also correspondingly increasing.

CHAIRPERSON JACOBS: Well said, actually.

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Item 12. Discussion of other Board matters.

CHAIRPERSON JACOBS: Are there any other Board matters? Anybody else have any new items?

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Item 13. Public testimony.

CHAIRPERSON JACOBS: Are there any members of the public who wish to speak?

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Item 14. Adjournment.

CHAIRPERSON JACOBS: All right. Seeing none, I'd like to thank everyone. Good questions, good discussion today. Good work by staff. And we'll adjourn.

(The meeting concluded at 12:37 p.m.)

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REPORTER'S CERTIFICATE

I hereby certify the foregoing proceedings were reported by me at the time and place therein named; that the proceedings were reported by me, a duly certified shorthand reporter and a disinterested person, and was thereafter transcribed into typewriting by computer.

In witness whereof, I have hereunto set my hand this 2nd day of June 2014.

____

Yvonne K. Fenner
Certified Shorthand Reporter
License No. 10909, RPR

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State of California

M E M O R A N D U M

To: Board of Directors **Date:** July 8, 2014

Tim Hsu, Director of Financing
From: **CALIFORNIA HOUSING FINANCE AGENCY**

Subject: CalHFA Fiscal 2014-2015 Projected Revenues and Expenses

At the May 13, 2014 Board meeting we presented to the Board the Agency's projected revenues and expenses for fiscal year 2014-2015. The Board approved the Agency's budget; however, the board requested that we provide a more detailed report of the Agency's projected cash inflows for fiscal year 2014-2015.

Attached for your information is the requested report.

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California Housing Finance Agency
Fiscal 2014-2015
Projected Revenues and Budget
(in millions)

		7/1/14 to 6/30/15	
Projected Cash Inflows			
from "legacy" activities			
Income from single-family loan servicing	$	3.00	
Release of earthquake insurance	$	0.94	
Mortgage repayments and maturities:			
- HELP loans (maturities)	$	11.60	
- Unencumbered multifamily loans (repayments)	$	8.14	
Fee income:			
- Administrative fees from bond indentures	$	4.90	
- HAP administration fees	$	1.06	
- Multifamily servicing fees (MHSA and Citi)	$	1.00	
Interest on mortgages/securities/cash:			
- HELP loans	$	3.66	
- Unencumbered multifamily loans	$	7.84	
- Unencumbered MBS	$	2.72	
- Float Earnings (invested in State's SMIF)	$	0.56	
	$	45.43	
from new activities (Moderate Scenario)			*# of loans*
Single-family Program:			
- Fee income from sale of MBS	$	1.20	*927*
- Fee income from origination of CHDAP	$	1.34	*4,040*
- Fee income from origination of MCC	$	0.05	*720*
Multifamily Program (all HUD Risk-share insured):			
- Loan fees from acq-rehab financings:			
- fully amortizing permanent loans	$	0.38	*5*
- 30-35 year amortizing but due in 17+ years	$	0.75	*10*
- Loan fee from permanent-only financings:			
- fully amortizing permanent loans	$	0.28	*5*
- Conduit financings:	$	0.15	*6*
Multifamily Asset Management:			
- HUD 811	$	0.10	
- HCD's Tenant Based Rental Assistance	$	0.10	
	$	4.34	
Total Inflows	$	49.77	
Projected Cash Outflows			
FY2014-2015 Total Budget Requested			
Payroll expense (salaries and benefits)	$	(29.86)	
Rent (Agency) expense	$	(3.08)	
Prorata expense & General Expenses	$	(2.31)	
General operating expenses	$	(7.21)	
Total Outflows	$	(42.46)	
Projected Net Cashflow	$	7.31	

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State of California

MEMORANDUM

To: Board of Directors **Date:** June 25, 2014

From: James S.L. Morgan, Housing Finance Chief
Multifamily Programs
California Housing Finance Agency ("CalHFA")

Subject: Agenda Item 5: Update regarding HUD's approval allowing balloon loans for loans financed under CalHFA's Risk Share/Preservation Loan Program.

Background:

Section 542(c) of the Housing and Community Development Act of 1992 enables the U.S. Department of Housing and Urban Development (HUD) and State and local housing finance agencies (HFAs) to provide risk-sharing arrangements to help HFAs provide more insurance and credit enhancements for multifamily loans. On April 26, 1994, CalHFA entered into a Risk-Sharing Agreement with HUD (the "Risk Share Agreement") pursuant to which HUD agreed to provide full mortgage insurance through the Federal Housing Administration (FHA) for CalHFA loans made to affordable multifamily housing projects (the "HUD Risk Share Program"). Pursuant to the HUD Risk Share Agreement, CalHFA and HUD each agreed to assume 50 percent of the risk of loss on mortgages issued by CalHFA under the HUD Risk Share Program.

On July 4, 1994, the Board of Directors adopted Resolution 94-11 amending CalHFA's business plan to include the HUD Risk Share Program.

CalHFA's Strategy to Reduce Bond Costs while Obtaining FHA Loan Insurance

HUD regulations require that mortgages insured under section 542(c) be regularly amortizing over the 30 to 40 year period of the insured loan. Recent changes in the capital markets have adversely impacted the cost of tax exempt financing since the HUD Risk Share Program was implemented over 20 years ago. In addition, the current tax credit and bond marketplace offers favorable non-fully amortizing loan products that have shorter loan terms for affordable multifamily housing projects.

In light of the challenges associated with the cost of issuing 30 to 40 year bonds that require full loan amortization over the term of the mortgage, CalHFA sought and obtained a waiver (discussed in more detail below) of the full amortization regulatory requirement, so that CalHFA could issue shorter term bonds and make loans with amortization periods of up to 35 years that mature in 17 to 25 years.

The cost savings associated with the shorter loan term will allow CalHFA to offer a lower interest rate which will help CalHFA fulfill its mission of both creating new, and preserving existing, affordable multifamily housing by providing improved financing opportunities for new projects as well as recapitalization of existing CalHFA projects.

HUD's Approval of Risk Share Loans with a Minimum Loan Term of 17 Years:

On May 27, 2014, HUD approved a 2-year regulatory waiver, effective from July 1, 2014 to June 30, 2016 (the "2014 Waiver"), a copy of which is attached hereto. The 2014 Waiver allows CalHFA to make loans to affordable multifamily housing projects with amortization periods of up to 35 years, but terms as short as 17 years. In other words, the 2014 Waiver allows CalHFA to make loans that require a balloon payment upon maturity. HUD understands the challenges that CalHFA and other housing financing agencies face under the current HUD risk sharing regulations. In fact, HUD has told CalHFA that it plans to pursue a regulation change that allows balloon payment loans under Section 542(c) nationwide.

HUD and CalHFA understand that the 2014 Waiver is limited to 20 loans per year or a total of 40 loans during the waiver period. In addition, the 2014 Waiver is conditioned on (among other things) HUD's review and approval of CalHFA's proposed underwriting standards and requirements prior to CalHFA's closing its first loan under the 2014 Waiver. In general, HUD wants to understand CalHFA's approach to risk analysis and mitigation, and the criteria CalHFA applies when evaluating each borrower's exit strategy at the balloon term.

Staff will provide the Board with a general overview of proposed underwriting criteria to analyze and mitigate balloon payment risk at the July 8 meeting.

Attachment

State of California

M E M O R A N D U M

To: Board of Directors **Date:** June 19, 2014

Tim Hsu, Director of Financing

From: **CALIFORNIA HOUSING FINANCE AGENCY**

Subject: Homeownership Loan Portfolio Update as of April 30, 2014

Attached for your information is a report summarizing the Agency's Homeownership loan portfolio:

- Delinquencies as of April 30, 2014 by insurance type,
- Delinquencies as of April 30, 2014 by product (loan) type,
- Delinquencies as of April 30, 2014 by loan servicer,
- Delinquencies as of April 30, 2014 by county,
- A chart of the number of CalHFA's FHA Delinquent Loan Trend for 30-90 Day and 120 Day (for the period of December 2011 thru April 2014)
- A chart of the number of CalHFA's Conventional Delinquent Loan Trend for 30-90 Day and 120 Day (for the period of December 2011 thru April 2014)
- A graph of CalHFA's 90-day+ ratios for FHA and Conventional loans (for the period of April 2009 through April 2014),
- A graph of 90-day+ ratios for CalHFA's three Conventional loan (products) types, for the period of April 2012 through April 2014,
- Real Estate Owned (REO) at April 30, 2014,
- Accumulated Uninsured Losses from January 1, 2008 through April 30, 2014,
- Disposition of 1st Trust Deed Gain/(Loss) for January 1, 2014 through April 30, 2014, and
- Write-Offs of subordinate loans for January 1, 2014 through April 30, 2014

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HOMEOWNERSHIP LOAN PORTFOLIO

DELINQUENCY, REO, SHORT SALE and LOSS REPORT – April 30, 2014

Reconciled Loan Delinquency Summary
All Active Loans By Insurance Type
As of April 30, 2014

				DELINQUENCY RATIOS - % of Loan Count							
	Loan Count	Balance	% of Balance	Loan Count	30-Day	Loan Count	60-Day	Loan Count	90(+) Day	Totals Count	Totals %
Federal Guaranty											
FHA	7,388	$ 782,988,962	30.01%	346	4.68%	104	1.41%	378	5.12%	828	11.21%
VA	169	17,498,665	0.67%	8	4.73%	1	0.59%	9	5.33%	18	10.65%
RHS	76	13,311,780	0.51%	3	3.95%	1	1.32%	9	11.84%	13	17.11%
Conventional loans											
with MI											
CalHFA MI Fund	3,390	846,614,607	32.45%	110	3.24%	51	1.50%	260	7.67%	421	12.42%
without MI											
Orig with no MI	3,845	687,919,392	26.37%	86	2.24%	24	0.62%	153	3.98%	263	6.84%
MI Cancelled*	1,594	260,499,458	9.99%	29	1.82%	3	0.19%	39	2.45%	71	4.45%
Total CalHFA	16,462	$ 2,608,832,864	100.00%	582	3.54%	184	1.12%	848	5.15%	1,614	9.80%

*Cancelled per Federal Homeowner Protection Act of 1998, which grants the option to cancel the MI with 20% equity.

Note: In accordance with CalHFA's policy, *no trustee sale is permitted between December 15 and January 5 of any year without CalHFA's prior written approval.*

Reconciled Loan Delinquency Summary
All Active Loans By Loan Type
As of April 30, 2014

				DELINQUENCY RATIOS - % of Loan Count							
	Loan Count	Balance	% of Balance	Loan Count	30-Day	Loan Count	60-Day	Loan Count	90(+) Day	Totals Count	Totals %
30-yr level amort											
FHA	7,388	$ 782,988,962	30.01%	346	4.68%	104	1.41%	378	5.12%	828	11.21%
VA	169	17,498,665	0.67%	8	4.73%	1	0.59%	9	5.33%	18	10.65%
RHS	76	13,311,780	0.51%	3	3.95%	1	1.32%	9	11.84%	13	17.11%
Conventional - with MI	1,666	366,828,922	14.06%	46	2.76%	29	1.74%	103	6.18%	178	10.68%
Conventional - w/o MI	4,853	816,995,236	31.32%	87	1.79%	21	0.43%	152	3.13%	260	5.36%
40-yr level amort											
Conventional - with MI	310	84,069,284	3.22%	12	3.87%	3	0.97%	28	9.03%	43	13.87%
Conventional - w/o MI	165	31,377,702	1.20%	9	5.45%	1	0.61%	7	4.24%	17	10.30%
***5-yr IOP, 30-yr amort**											
Conventional - with MI	1,414	395,716,401	15.17%	52	3.68%	19	1.34%	129	9.12%	200	14.14%
Conventional - w/o MI	421	100,045,912	3.83%	19	4.51%	5	1.19%	33	7.84%	57	13.54%
Total CalHFA	16,462	$ 2,608,832,864	100.00%	582	3.54%	184	1.12%	848	5.15%	1,614	9.80%
	Weighted average of conventional loans:			225	2.55%	78	0.88%	452	5.12%	755	8.55%

*As of December 1, 2013 all IOP loans (except 82 loans which were modified) were converted to fixed (amortizing) loans.

Cal HFA California Housing Finance Agency

Reconciled Loan Delinquency Summary
All Active Loans By Servicer
As of April 30, 2014

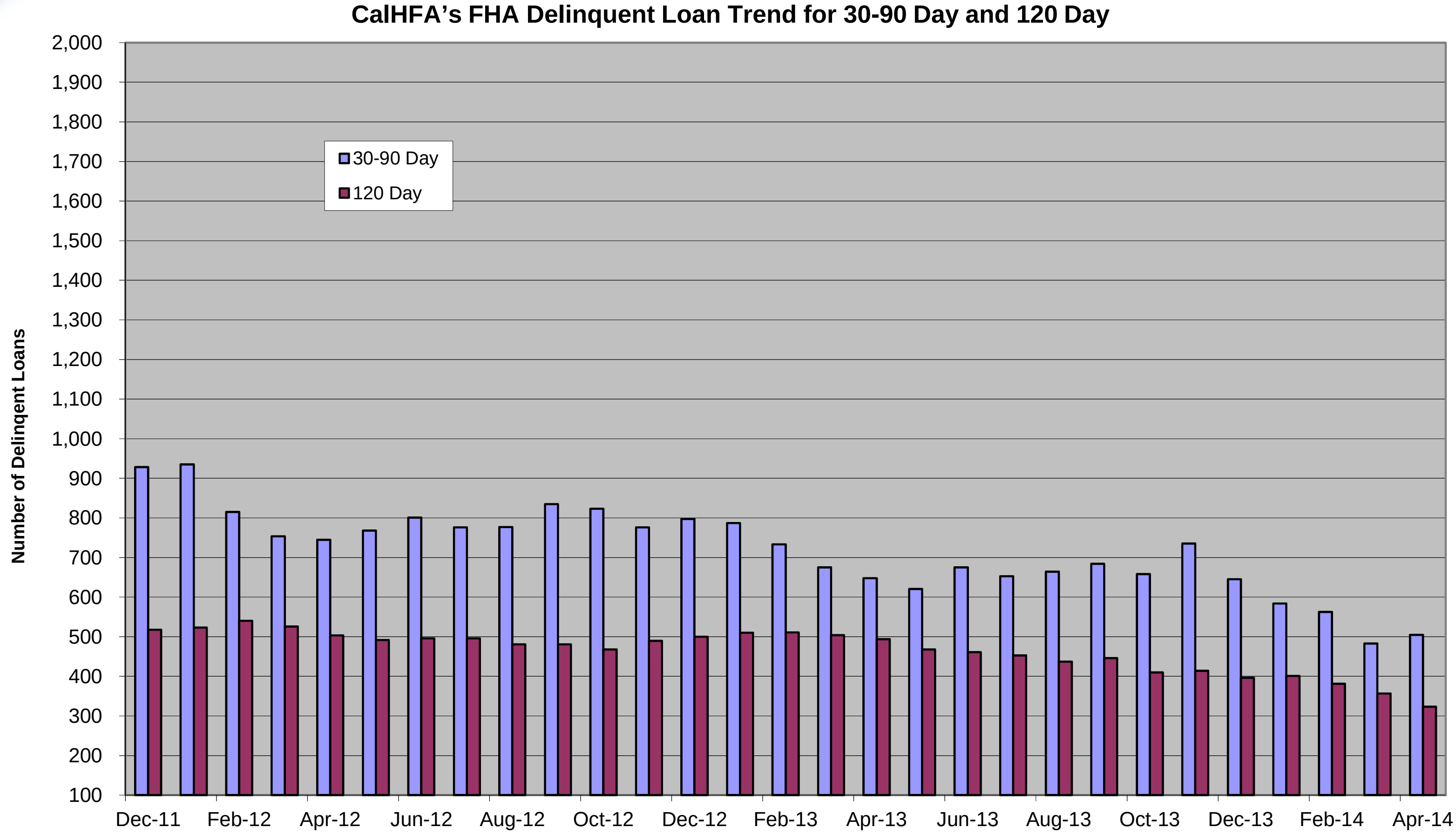
	Loan Count	Balance	% of Balance	Loan Count	30-Day	Loan Count	60-Day	Loan Count	90(+) Day	Totals Count	Totals %
				DELINQUENCY RATIOS - % of Loan Count							
CALHFA - LOAN SERVICING	6,121	$ 1,236,182,295	47.38%	152	2.48%	51	0.83%	309	5.05%	512	8.36%
GUILD MORTGAGE	3,875	577,087,466	22.12%	175	4.52%	53	1.37%	125	3.23%	353	9.11%
WELLS FARGO HOME MORTGAGE	1,743	173,476,743	6.65%	56	3.21%	24	1.38%	90	5.16%	170	9.75%
EVERHOME MORTGAGE COMPANY	1,626	136,908,526	5.25%	92	5.66%	16	0.98%	40	2.46%	148	9.10%
CALHFA - LOAN SERVICING - BAC HOME LOANS	1,625 *	262,203,905	10.05%	63	3.88%	13	0.80%	174	10.71%	250	15.38%
GMAC MORTGAGE CORP	721	86,593,700	3.32%	29	4.02%	19	2.64%	58	8.04%	106	14.70%
FIRST MORTGAGE CORP	565	101,448,044	3.89%	12	2.12%	6	1.06%	29	5.13%	47	8.32%
JPMORGAN CHASE BANK, N.A.	112	24,409,258	0.94%	0	0.00%	2	1.79%	13	11.61%	15	13.39%
CITIMORTGAGE, INC.	37	7,942,746	0.30%	1	2.70%	0	0.00%	6	16.22%	7	18.92%
DOVENMUEHLE MORTGAGE, INC.	30	887,865	0.03%	1	3.33%	0	0.00%	0	0.00%	1	3.33%
BAC HOME LOANS SERVICING, LP	5	1,209,131	0.05%	1	20.00%	0	0.00%	4	80.00%	5	100.00%
WESCOM CREDIT UNION	2	483,185	0.02%	0	0.00%	0	0.00%	0	0.00%	0	0.00%
Total CalHFA	16,462	$ 2,608,832,864	100.00%	582	3.54%	184	1.12%	848	5.15%	1,614	9.80%

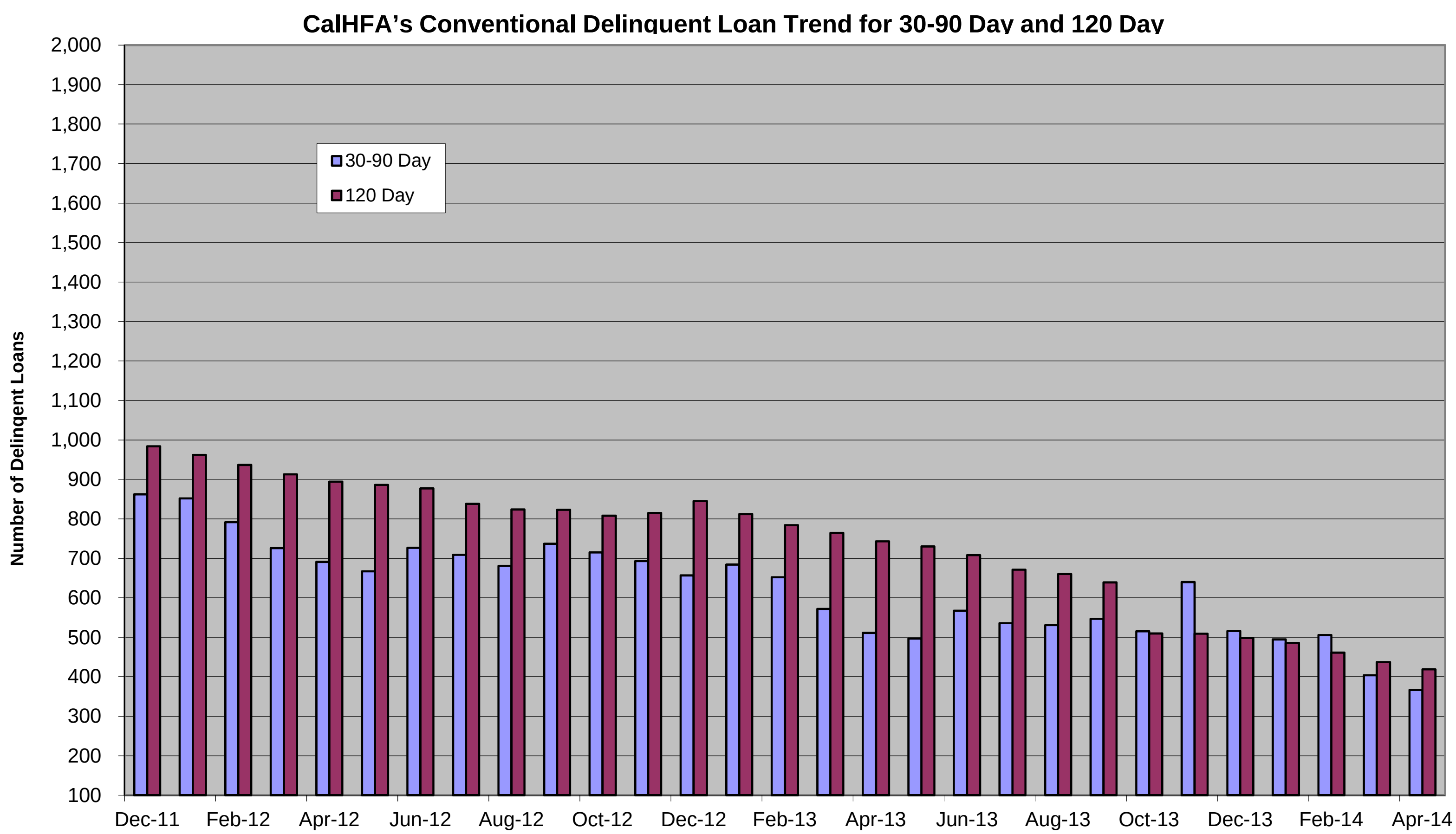
*These BAC Home Loans were transferred to CalHFA Loan Servicing in November 2013 and February 2014.

Reconciled Loan Delinquency Summary
All Active Loans By County
As of April 30, 2014

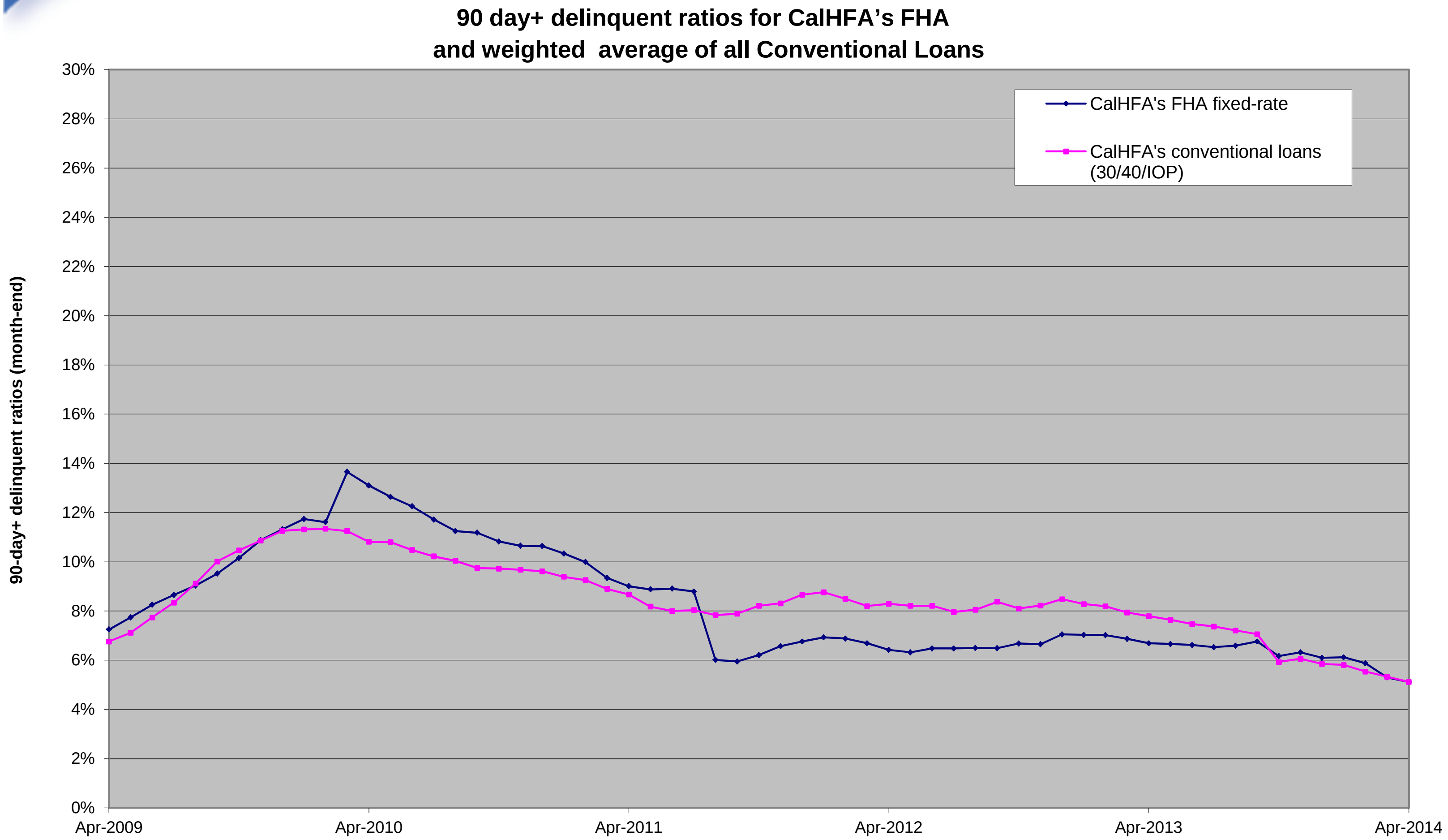
	Loan Count	Balance	% of Balance	Loan Count	30-Day	Loan Count	60-Day	Loan Count	90-Day+	Total Count	Total %
				DELINQUENCY RATIOS - % of Loan Count							
LOS ANGELES	2,732	$ 518,785,530	19.89%	87	3.18%	32	1.17%	143	5.23%	262	9.59%
SAN DIEGO	1,332	259,210,055	9.94%	45	3.38%	8	0.60%	77	5.78%	130	9.76%
KERN	1,100	102,405,969	3.93%	44	4.00%	22	2.00%	72	6.55%	138	12.55%
SANTA CLARA	1,032	244,177,323	9.36%	25	2.42%	6	0.58%	26	2.52%	57	5.52%
FRESNO	930	73,628,285	2.82%	47	5.05%	10	1.08%	37	3.98%	94	10.11%
TULARE	912	73,087,974	2.80%	48	5.26%	9	0.99%	41	4.50%	98	10.75%
SAN BERNARDINO	734	108,039,439	4.14%	36	4.90%	7	0.95%	61	8.31%	104	14.17%
RIVERSIDE	731	102,189,941	3.92%	43	5.88%	17	2.33%	65	8.89%	125	17.10%
SACRAMENTO	728	116,021,778	4.45%	22	3.02%	9	1.24%	55	7.55%	86	11.81%
ORANGE	727	148,724,937	5.70%	16	2.20%	4	0.55%	32	4.40%	52	7.15%
ALAMEDA	711	155,316,373	5.95%	6	0.84%	3	0.42%	25	3.52%	34	4.78%
CONTRA COSTA	579	115,263,127	4.42%	20	3.45%	12	2.07%	27	4.66%	59	10.19%
IMPERIAL	444	40,352,798	1.55%	21	4.73%	10	2.25%	14	3.15%	45	10.14%
VENTURA	400	95,411,694	3.66%	9	2.25%	3	0.75%	12	3.00%	24	6.00%
SONOMA	349	65,114,708	2.50%	7	2.01%	4	1.15%	9	2.58%	20	5.73%
OTHER COUNTIES	3,021	391,102,932	14.99%	106	3.51%	28	0.93%	152	5.03%	286	9.47%
Total CalHFA	16,462	$ 2,608,832,864	100.00%	582	3.54%	184	1.12%	848	5.15%	1,614	9.80%

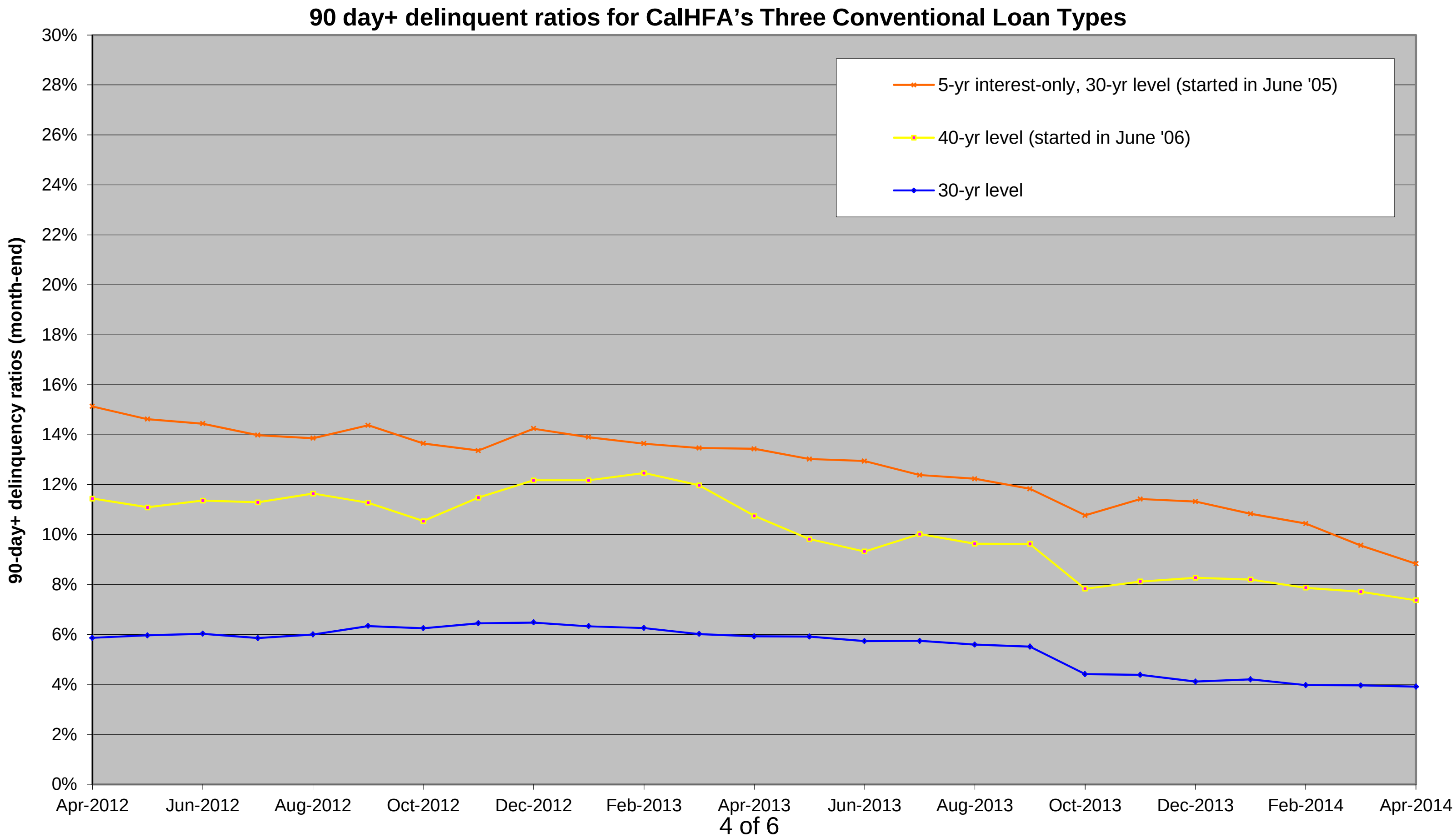
Cal HFA California Housing Finance Agency





Cal HFA California Housing Finance Agency





Real Estate Owned

Calendar Year 2014 (As of April 30, 2014)												
			**Trustee Sales			Disposition of REO(s)						
Loan Type	Beginning Balance # of Loans	Prior Calendar Adj.	Reverted to CalHFA Jan-Mar	Reverted to CalHFA April	Total Trustee Sales	Repurchased by Lender Jan-Mar	Market Sale(s) Jan-Mar	Repurchased by Lender April	Market Sale(s) April	Total Disposition of REO(s)	Ending Balance # of Loans	UPB of REO's Owned
FHA/RHS/VA	12	0	23	11	34	17		13		30	16	$ 2,562,560
Conventional	91	0	38	8	46		47		20	67	70	14,155,027
Total	103	0	61	19	80	17	47	13	20	97	86	$ 16,717,587

Calendar Year 2013							
			*Trustee Sales	Disposition of REO(s)			
Loan Type	Beginning Balance # of Loans	Prior Calendar Adj.	Reverted to CalHFA 2013	Repurchased by Lender 2013	Market Sale(s) 2013	Ending Balance # of Loans	UPB of REO's Owned
FHA/RHS/VA	45	(1)	111	143		12	$ 1,686,151
Conventional	161	1	249		320	91	19,379,399
Total	206	0	360	143	320	103	$ 21,065,550

Calendar Year 2012							
			*Trustee Sales	Disposition of REO(s)			
Loan Type	Beginning Balance # of Loans	Prior Calendar Adj.	Reverted to CalHFA 2012	Repurchased by Lender 2012	Market Sale(s) 2012	Ending Balance # of Loans	UPB of REO's Owned
FHA/RHS/VA	124	(18)	312	373		45	$ 7,884,581
Conventional	565	3	786		1,193	161	40,029,375
Total	689	(15)	1,098	373	1,193	206	$ 47,913,957

Calendar Year 2011						
		*Trustee Sales	Disposition of REO(s)			
Loan Type	Beginning Balance # of Loans	Reverted to CalHFA 2011	Repurchased by Lender 2011	Market Sale(s) 2011	Ending Balance # of Loans	UPB of REO's Owned
FHA/RHS/VA	198	496	570		124	$ 22,948,976
Conventional	1084	1311		1830	565	123,482,821
Total	1282	1807	570	1830	689	$ 146,431,797

**3rd party trustee sales are not shown in the tables (tltle to these loans were never transferred to CalHFA). There were eight (8) 3rd party sales in calendar year 2008, eighteen (18) 3rd party sales year 2009, thirty-nine (39) 3rd party sales year 2010, twenty two (22) 3rd party sales in calendar year 2011, forty one (41) 3rd party sales in calendar year 2012, fifty nine (59) 3rd party sales in calendar year 2013, and there are eighteen (18) 3rd party sales to date 2014.*

Accumulated Uninsured Losses as of April 30, 2014						
Conventional Loans	# of Properties Sold	Principal Write-Offs (1)	# of GAP Claims	Actual GAP(2) Claim Payments	# of Subordinate Loans	Subordinate Write-Offs (3) & (4)
REOs Sold	5,085	$ (185,216,214)	2,601	$ (117,367,774)		
Short Sales	1,417	(61,885,182)	395	(17,461,359)	2,341	$ (20,803,292)
3rd Party Sales	87	(196,576)	4	(170,867)	87	(826,196)
Write-offs resulting from foreclosures					8,119	(74,538,335)
Subordinate loan without CalHFA 1st					2,006	(14,164,210)
Total:	6,589	$ (247,297,973)	3,000	$ (135,000,000)	12,553	$ (110,332,033)

(1) Principal loan write-offs from January 1, 2008. Does not include allowance for loan losses or loan loss reserves.

(2) The California Housing Loan Insurance Fund (the MI Fund") provided GAP insurance to meet HMRB bond indenture requirements that all loans held within that indenture have 50% of the unpaid principal balance insured by a mortgage insurance policy for the life of the loan. The insurance may be provided by any combination of government insurance, private mortgage insurance, or a policy from the MI fund. The Agency agreed, pursuant to an internal interfund agreement, to indemnify the MI Fund for claims paid for principal losses under the GAP insurance policy, up to a cumulative maximum amount of $135 million, this maximum amount was reached in August 2011. The indemnification is payable solely from available funds held in a sub account within the California Housing Finance Fund.

(3) Includes both FHA/Conventional Loans.

(4) Does not include FNMA and CalSTRS subordinates (non-agency loans serviced by in house loan servicing)

2014 Year to Date Composition of 1st Trust Deed Loss
(As of April 30, 2014)

Loan Type	Disposition				Principal Write-Offs
	Repurchased by Lender	Market Sales	Short Sales	Loan Balance at Sales	
FHA/RHS/VA	30		15	$ 8,209,985	
Conventional		67	62	31,979,252	$ (4,163,515)
	30	67	77	$ 40,189,237	$ (4,163,515)

2014 Year to Date Composition of Subordinate Write-Offs by Loan Type(1)
(As of April 30, 2014)

Loan Type	Active Loans		Write-Offs with CalHFA 1st		Write-Offs w/o CalHFA 1st		Total Write-Offs	
	Active Loans	Dollar Amount	Number of Write-Offs	Dollar Amount	Number of Write-Offs	Dollar Amount	Number of Write-Offs	Dollar Amount
CHAP/HHPA (HiCAP)	6,526	$68,850,756	60	$ 519,908	4	$ 25,500	64	$545,408
CHDAP / ECTP (THPA) / HiRAP	27,686	191,578,551	70	522,161	49	270,813	119	792,975
Other (2)	199	2,655,038	0	0	1	3,510	1	3,510
	34,411	$263,084,346	130	$1,042,069	54	$299,823	184	$1,341,892

(1) Does not include FNMA and CalSTRS subordinates (non-agency loans serviced by in house loan servicing)

(2) Includes HPA, MDP, OHPA, and SSLP.

State of California

M E M O R A N D U M

To: Board of Directors **Date:** June 24, 2014

Timothy Hsu, Director of Financing

From: **CALIFORNIA HOUSING FINANCE AGENCY**

Subject: AGENCY BONDS, INTEREST RATE SWAPS, AND FINANCING RISK FACTORS REPORT

The following report describes our bond and interest rate swap positions as well as the related risks associated with variable rate and swap strategies. The report is divided into sections as follows:

1) Outstanding Bonds
2) Variable Rate Debt
    a) Variable Rate Debt Exposure
    b) Types of Variable Rate Debt
    c) Liquidity Providers
    d) Interest Rate Swaps
3) Financing Risk Factors
    a) Unhedged Variable Rate Risk
    b) Basis Risk
    c) Amortization Risk
    d) Termination Risk
    a) Collateral Posting Risk

1) OUTSTANDING BONDS

Below is the Agency's outstanding debt position. This table does not include any pass-thru or conduit financings which makes up an additional $410 million

BONDS OUTSTANDING
As of July 1, 2014
($ in millions)

	Fixed Rate	Variable Rate	Totals
Single Family	$,1,626	$1,251	$2,877
Multifamily	388	257	645
TOTALS	$2,014	$1,508	$3,522

2) VARIABLE RATE DEBT

a) VARIABLE RATE DEBT EXPOSURE

Over the years the Agency has integrated the use of variable rate debt as a primary issuance strategy in providing capital to support its programmatic goals. Most of our interest rate exposure from variable rate debt is hedged in the swap market.

This section describes the variable rate bonds of CalHFA and is organized programmatically by indenture as follows: HMRB (Home Mortgage Revenue Bonds--CalHFA's largest single family indenture), MHRB (Multifamily Housing Revenue Bonds III--CalHFA's largest multifamily indenture), and HPB (Housing Program Bonds--CalHFA's multipurpose indenture, used to finance a variety of loans including the Agency's downpayment assistance loans). The total amount of CalHFA variable rate debt is $1.5 billion, 38% of our $3.9 billion of total indebtedness as of July 1, 2014.

VARIABLE RATE DEBT
($ in millions)

	Swapped to Fixed Rate	Not Swapped or Tied to Variable Rate Assets	Total Variable Rate Debt
HMRB (SF)	$522	$729	$1,251
MHRB (MF)	184	73	257
Total	$706	$802	$1,508

b) Types of Variable Rate Debt

The following table shows our variable rate debt sorted by type, i.e., whether auction rate, indexed rate, or variable rate demand obligations (VRDOs). Auction and indexed rate securities cannot be "put" back to us or to a third party by investors; hence they typically bear higher rates of interest than do "put-able" bonds such as VRDOs.

Types of Variable Rate Debt
($ in millions)

	Auction Rate & Similar Securities	Indexed Rate Bonds	Variable Rate Demand Obligations	Total Variable Rate Debt
HMRB	$0	$506	$745	$1,251
MHRB	99	0	158	257
Total	$99	$506	$903	$1,508

c) Liquidity Providers

On October 19, 2009, the United States Treasury (Treasury) announced a new initiative for state and local housing finance agencies (HFAs) to provide a new bond purchase program to support new lending by HFAs and to provide a temporary credit and liquidity program (TCLP) to improve access of HFAs to liquidity for outstanding HFA bonds. On December 23, 2009, the Agency closed eight TCLP transactions with Treasury to replace the liquidity for $3.5 billion of variable rate bonds. The new liquidity became effective in January 2010 on the mandatory tender dates of the bonds with an initial expiration date of December 23, 2012. However, the Agency successfully negotiated with Treasury to extend the deadline for the TCLP to December 23, 2015.

The table below shows the government-sponsored enterprises (GSE) which are providing liquidity in the form of standby bond purchase agreements for our VRDOs.

Liquidity Providers
As of 7/1/2014
($ in millions)

Financial Institution	$ Amount of Bonds
Freddie Mac	$ 451
Fannie Mae	451
Total	$ 902

d) <u>INTEREST RATE SWAP</u>

Currently, we have a total of 79 “fixed-payer” swaps with eleven different counterparties for a combined notional amount of $1.5 billion. All of these fixed-payer swaps are intended to establish synthetic fixed rate debt by converting our variable rate payment obligations to fixed rates. The table below provides a summary of our swap notional amounts.

FIXED PAYER INTEREST RATE SWAPS
(notional amounts)
($ in millions)

	Tax-Exempt	Taxable	Totals
HMRB	$907	$117	$1,024
MHRB	492	0	492
TOTALS	$1,399	$117	$1,516

SWAPS
($ in millions)

	Hedging Bonds	Not Hedging Bonds	Totals
HMRB	$529	$495	$1,024
MHRB	272	220	492
TOTALS	$801	$715	$1,516

For all of our fixed-payer swaps, we receive floating rate payments from our counterparties in exchange for a fixed-rate obligation on our part. In today’s market, the net periodic payment owed under these swap agreements is from us to our counterparties. As an example, on our February 1, 2014 semiannual debt service payment date we made a total of $33 million of net payments to our counterparties. Conversely, if short-term rates were to rise above the fixed rates of our swap agreements, then the net payment would run in the opposite direction, and we would be on the receiving end.

The table on the following page shows the diversification of our fixed payer swaps among the thirteen firms acting as our swap counterparties.

SWAP COUNTERPARTIES

Swap Guarantor	Credit Ratings Moody's	S & P	Notional Amounts Swapped as of 7/1/2014 ($ in millions)	Number of Swaps
Merrill Lynch Derivative Products	Aa3	A+	$ 499	33
JPMorgan Chase Bank, N.A.	Aa3	A+	335	15
Goldman Sachs Mitsui Marine Derivative Products, , L.P.	Aa2	AAA	192	7
Deutsche Bank AG	A2	A	149	10
AIG Financial Products, Corp. [2]	Baa1	A-	91	3
Citigroup Financial Products, Inc.	Baa2	A-	83	4
Morgan Stanley Capital Services, Inc.	Baa2	A-	82	2
BNP Paribas	A1	A+	40	2
Bank of New York Mellon	Aa2	AA-	25	1
UBS AG	A2	A	12	1
Dexia Credit Local New York Agency [2]	Baa2	BBB	10	1
			$ 1,517 [1]	79

[1] *Basis Swaps not included in totals*

[2] *Swap counterparty's rating has triggered Additional Termination Event (ATE); Agency has right to terminate the associated swaps; additionally, the rating agencies no longer consider these swaps to be effective hedges see "Termination Risk" section of report*

3) FINANCING RISK FACTORS

a) Unhedged Variable Rate Risk

As shown in Sec. 2(a), the Variable Rate Debt table, our "net" variable rate exposure is $802 million, 20% of our indebtedness. The net amount of variable rate bonds is the amount that is neither swapped to fixed rates nor directly backed by complementary variable rate loans or investments. The $802 million of net variable rate exposure ($417 million taxable and $385 million tax-exempt) is offset by the Agency's variable rate investments and excess swap positions. The Agency's balance sheet has: i) $386 million (six month average balance) of non-bond indenture related funds invested in the State Treasurer's investment pool (SMIF) earning a variable rate of interest; and, ii) $687 million notional amount of interest rate swaps in excess of the hedged bonds.

From a risk management perspective, these two positions serve as a balance sheet hedge for the $802 million of net variable rate exposure.

In order to estimate the “true” unhedged position to the Agency, first, the overhedged swaps were used to offset the unhedged bonds. Then, the remaining tax-exempt unhedged bonds were converted into their equivalent taxable basis. Using this conversion method, the $802 million of net variable rate exposure translates to $171 million of net variable rate exposure. This $171 million is further reduced by the $386 million of funds invested in SMIF. Thus the “true” net variable rate debt is -$242 million which, from the Agency’s balance sheet perspective, means there is no net unhedged position.

In addition, taking unhedged variable rate exposure mitigates the amortization risk without the added cost of purchasing swap optionality. Our unhedged variable rate bonds are callable on any date and allow for bond redemption or loan recycling without the cost of par termination rights or special bond redemption provisions. In addition, taking unhedged variable rate exposure diversifies our interest rate risks by providing benefits when short-term interest rates rise slower than the market consensus. In a liability portfolio that is predominately hedged using long-dated swaps, the unhedged exposure balances the interest rate profile of the Agency’s outstanding debt.

b) BASIS RISK

Almost all of our swaps contain an element of what is referred to as “basis risk” – the risk that the floating rate component of the swap will not match the floating rate of the underlying bonds. This risk arises because our swap floating rates are based on indices, which consist of market-wide averages, while our bond floating rates are specific to our individual bond issues. The only exception is where our taxable floating rate bonds are index-based, as is the case of the taxable floaters we have sold to the Federal Home Loan Banks.

The relationship between the two floating rates changes as market conditions change. Some of the conditions that contributed to our extreme basis mismatch in 2009 and early 2010 were the collapse of the auction rate securities market, the impact of bond insurer downgrades, the funding of bank bonds at higher rates, and SIFMA/LIBOR ratio at historically high levels over 100% We responded to the market disruption by refunding, converting, or otherwise modifying many of the under performing auction rate securities and insured VRDOs, and we eliminated bank bonds by taking advantage of the Temporary Credit and Liquidity Program offered by the federal government.

The new Temporary Credit and Liquidity Program from the federal government and the GSEs has significantly reduced basis mismatch. As part of this process, all bond insurance was removed from VRDOs and the federal government now provides direct credit support on all CalHFA VRDOs. This has allowed CalHFA VRDOs to reset with little or no spread to SIFMA. Since January 2010, our VRDOs have reset at an average of 10 basis points or 0.10% below SIFMA, whereas in 2009, our VRDOs were resetting at an average of 106 basis points or 1.06% above SIFMA. The main risk that exists is that the SIFMA/LIBOR ratio continues to be high and as market rates rise our basis mismatch may remain higher than expected due to general market conditions.

The floating formulas of Agency swaps are usually indexed to LIBOR or SIFMA. LIBOR is the London Interbank Offered Rate index which is used to benchmark taxable floating rate debt, and SIFMA is the Securities Industry and Financial markets Association Index to benchmark tax-exempt variable rates. When the SIFMA/LIBOR ratio is very high, the swap payment we receive falls short of our bond payment, and the all-in rate we experience is somewhat higher. The converse is true when the percentage is low. We continually monitored the SIFMA/LIBOR relationship and the performance of our swap formulas and made certain adjustments to the formula. The following table displays the SIFMA/LIBOR ratio for the past eight calendar years.

Average SIFMA/LIBOR Ratio			
2007	69%	2011	79%
2008	84%	2012	69%
2009	123%	2013	49%
2010	96%	2014 to date	38%

The table below shows the diversification of variable rate formulas used for determining the payments received from our interest rate swap counterparties.

BASIS FOR VARIABLE RATE PAYMENTS
RECEIVED FROM SWAP COUNTERPARTIES
(notional amounts)
($ in millions)

	Tax-Exempt	Taxable	Totals
% of LIBOR (+ spread)	$857	$0	$857
SIFMA (+ spread)	364	0	364
Stepped % of LIBOR [1]	168	0	168
3 mo. LIBOR (+ spread)	0	72	72
% of SIFMA	18	0	18
1 mo. LIBOR	0	27	27
3 mo. LIBOR	0	8	8
6 mo. LIBOR	0	2	2
TOTALS	$1, 407	$109	$1,516

[1] Stepped % of LIBOR – This formula has seven incremental steps where at the low end of the spectrum the swap counterparty would pay us 85% of LIBOR if rates should fall below 1.25% and at the high end it would pay 60% of LIBOR if rates are greater than 6.75%.

c) **<u>AMORTIZATION RISK</u>**

Our bonds are generally paid down (redeemed or paid at maturity) as our loans are prepaid. Our interest rate swaps amortize over their lives based on assumptions about the receipt of prepayments, and the single family transactions which include swapped bonds have generally been designed to accommodate prepayment rates between two and three times the "normal" rate. Our interest rate swaps generally have had fixed amortization schedules that can be met under a sufficiently wide ranges of prepayment speeds. In addition, swaps that were entered into after 2003 had swap termination options which allowed the Agency to terminate all or portions of the swap at par (no cost to terminate). The table below shows the par terminations that the Agency has exercised to date.

	Swap Par Options Exercised ($ in thousands)
2004	$12,145
2005	35,435
2006	20,845
2007	28,120
2008	18,470
2009	370,490
2010	186,465
2011	288,700
2012	361,975
2013	243,855
2014	142,110
	$1,708,610

The table below shows the speed at which the Agency's single family first mortgage loans have been prepaying for the past five years.

SEMI-ANUAL PREPAYMENT SPEED
FOR PAST FIVE YEARS

6-mo Period Ending:	PSA
Dec-2008	58%
Jun-2009	89%
Dec-2009	128%
Jun-2010	165%
Dec-2010	236%
Jun-2011	255%
Dec-2011	299%
Jun-2012	278%
Dec-2012	257%
Jun-2013	308%
Dec-2013	335%

Of interest is a $715 million overswap mismatch between the notional amount of certain of our swaps and the outstanding amount of the related bonds. This mismatch has occurred for two reasons: 1) as a result of the interplay between loan prepayments and the "10-year rule" of federal tax law and 2) the strategic debt management of the Agency to redeem bonds that were hedged but were associated with troubled or problematic financial partners. While some of our bonds are "over-swapped", there are significantly more than enough unswapped variable rate bonds to compensate for the mismatch. To mitigate our overswapped position, we continually monitor the termination value of our "excess swap" position looking for opportunities to unwind these positions when market terminations would be at minimal cost or a positive value to us and by exercising the par swap options as they become available.

d) TERMINATION RISK

Termination risk is the risk that, for some reason, our interest rate swaps must be terminated prior to their scheduled maturity. Our swaps have a market value that is determined based on current interest rates. When current fixed rates are higher than the fixed rate of the swap, our swaps have a positive value to us (assuming, as is the case on all of our swaps today, that we are the payer of the fixed swap rate), and termination would result in a payment from the provider of the swap (our swap "counterparty") to us. Conversely, when current fixed rates are lower than the fixed rate of the swap, our swaps have a negative value to us, and termination would result in a payment from us to our counterparty.

Our swap documents allow for a number of termination "events," i.e., circumstances under which our swaps may be terminated early, or "unwound". One circumstance that would cause termination would be a payment default on the part of either counterparty. Another circumstance would be a sharp drop in either counterparty's credit ratings and, with it, an inability (or failure) of the troubled counterparty to post sufficient collateral to offset its credit problem. It should be noted that, if termination is required under the swap documents, the market determines the amount of the termination payment and who owes it to whom. Depending on the market, it may be that the party who has caused the termination is owed the termination payment.

TERMINATION VALUE HISTORY

Date	Termination Value ($ in millions)
9/30/12	($330)
12/31/12	($294)
3/31/13	($294)
6/30/13	($248)
9/30/13	($203)
12/31/13	($176)
3/31/14	($183)

** As reported in the Financial Statements*

e) <u>COLLATERAL POSTING RISK</u>

Some ISDA agreements that we have entered into with the swap counterparties have collateral posting requirements. These postings are a function of the mark-to-market, ratings, threshold amounts, independent amounts and any collateral already posted. Our trades are valued weekly, and our collateral position is adjusted weekly based on those valuations. Failure to post the required collateral can result in a termination event.

The table below shows the required collateral amounts currently posted to swap counterparties. In the past months, falling interest rates have caused the swaps to have a negative value to the Agency thereby increasing the amount of collateral being posted to the counterparties.

Swap Collateral Posting
as of 6/11/2014
($ in millions)

	JPMorgan	Goldman Sachs	BofA	BofA / Merrill Lynch	Deutsche	Total
Marked-to-Market	42.34	24.3	43.38	24.71	24.5	
Credit Support Amount	23	10.55	6.25	12.35	0	52.15