STATE OF CALIFORNIA

CALIFORNIA HOUSING FINANCE AGENCY

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BOARD OF DIRECTORS

PUBLIC MEETING

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Burbank Airport Marriott & Convention Center
2500 Hollywood Way, Pasadena Room
Burbank, California

Thursday, March 7, 2013
10:00 a.m. to 12:31 p.m.

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Minutes approved by the Board of Directors at its meeting held:
MAY 9, 2013

Attest:

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:

WAYNE BELL
for BRIAN KELLY, Acting Undersecretary
Business, Transportation & 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 of Real Estate Development
Mercy Housing

MICHAEL A. GUNNING
Vice President
Personal Insurance Federation of California

JONATHAN HUNTER
Managing Director, Region 2
Corporation for Supportive Housing

MATTHEW JACOBS
Co-Managing Partner
Bulldog Partners, LLC

JACK SHINE
Chairman
American Beauty Development Co.

RUBEN A. SMITH
Partner
AlvaradoSmith
Professional Corporation

LAURA WHITTALL-SCHERFEE
Deputy Director of Financial Assistance

Department of Housing and Community Development
State of California

A P P E A R A N C E S

Participating CalHFA Staff:

TIM HSU
Director of Financing

VICTOR J. JAMES
General Counsel

JAMES S.L. MORGAN
Loan Officer
Acting Chief of Multifamily Programs

JOJO OJIMA
Office of the General Counsel

RICK OKIKAWA
Interim Programs Administrator

TONY SERTICH
Financing Officer

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Public Testimony:

MARCUS ALLEN FRISHMAN
Former FTB member and BOE Dept. board member

LEA OSBORNE

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BE IT REMEMBERED that on Thursday, March 7, 2013, commencing at the hour of 10:00 a.m., at the Burbank Airport Marriott Hotel & Convention Center, 2500 Hollywood Way, Pasadena Room, Burbank, California, before me, YVONNE K. FENNER, CSR #10909, RPR, the following proceedings were held:

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ACTING CHAIRPERSON GUNNING: Why don't we get started. Why don't we start with roll call.

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Item 1. Roll Call.

MS. OJIMA: Thank you.
Ms. Falk.
MS. FALK: Present.
MS. OJIMA: Mr. Carey.
(No audible response.)
MS. OJIMA: Mr. Hunter.
(No audible response.)
MS. OJIMA: Mr. Jacobs.
MR. JACOBS: Here.
MS. OJIMA: Mr. Bell for Mr. Kelly.
MR. BELL: Present.
MS. OJIMA: Ms. Carroll for Mr. Lockyer.
MS. CARROLL: Here.

MS. OJIMA: Ms. Patterson.

(No audible response.)

MS. OJIMA: Mr. Shine.

MR. SHINE: Here.

MS. OJIMA: Mr. Smith.

(No audible response.)

MS. CAPPIO: I know he's here.

MS. OJIMA: He's here.

Ms. Whitall-Scherfee for the Department of Housing and Community Development.

MS. WHITTALL-SCHERFEE: Here.

MS. OJIMA: Mr. Alex.

(No audible response.)

MS. OJIMA: Ms. Matosantos.

(No audible response.)

MS. OJIMA: Ms. Cappio.

MS. CAPPIO: Here.

MS. OJIMA: Mr. Gunning.

ACTING CHAIRPERSON GUNNING: Present.

MS. OJIMA: We have a quorum.

ACTING CHAIRPERSON GUNNING: It's a good thing.

Well, our industrious leader Mr. Carey was stuck in Washington and couldn't get out, and I'm glad to hopefully fill in in his shoes, with a lot of coaching and help. I always thought I was a coachable player, so between JoJo and Victor and Claudia, maybe we'll get through this thing.

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Item 2. Approval of the minutes of the November 13, 2012 Board of Directors meeting.

ACTING CHAIRPERSON GUNNING: Let's move on to agenda item No. 2, approving the minutes, so a motion to approve the minutes from November.

MR. BELL: I'll move --

MR. SHINE: Go ahead.

MR. BELL: I'll move the minutes.

ACTING CHAIRPERSON GUNNING: Okay. So moved. Is there a second?

MR. SHINE: I'll second that.

MS. OJIMA: Thank you.

Ms. Falk.

MS. FALK: Abstain.

MS. OJIMA: Thank you.

Mr. Jacobs.

MR. JACOBS: Abstain.

MS. OJIMA: We're in trouble already.

Mr. Bell.

MR. BELL: Abstain.

MS. OJIMA: Ms. Carroll.

MS. CARROLL: Aye.

MS. OJIMA: Thank you.

Mr. Shine.

MR. SHINE: Aye.

MS. OJIMA: Mr. Smith? Where is he?

ACTING CHAIRPERSON GUNNING: We need that vote.

MS. OJIMA: Ms. Whittall-Scherfee.

MS. WHITTALL-SCHERFEE: Abstain.

MS. OJIMA: Mr. Gunning.

ACTING CHAIRPERSON GUNNING: Aye.

MS. OJIMA: We do not have a quorum.

MS. CAPPIO: Even with Mr. Ruben?

MS. OJIMA: Even with Mr. Ruben.

MS. CAPPIO: Okay. Well, we'll get them next time.

ACTING CHAIRPERSON GUNNING: We'll put it over again.

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Item 3. Approval of the minutes of the January 17, 2013 Board of Directors meeting.

ACTING CHAIRPERSON GUNNING: Well, let's try with the minutes from January then. Is there a motion?

MS. FALK: Move approval.

ACTING CHAIRPERSON GUNNING: There's a motion.

MR. JACOBS: Second.

ACTING CHAIRPERSON GUNNING: And a second.

MS. OJIMA: Ms. Falk.

MS. FALK: Aye.

MS. OJIMA: Mr. Jacobs.

MR. JACOBS: Aye.

MS. OJIMA: Mr. Bell.

MR. BELL: Aye.

MS. OJIMA: Ms. Carroll.

MS. CARROLL: Aye.

MS. OJIMA: Mr. Shine.

MR. SHINE: Aye.

MS. OJIMA: Mr. Smith.

MR. SMITH: I have to pass.

MS. OJIMA: Ms. Whittall-Scherfee.

MS. WHITTALL-SCHERFEE: Aye.

MS. OJIMA: Mr. Gunning.

ACTING CHAIRPERSON GUNNING: Abstain.

MS. OJIMA: Thank you.

We just made it. Under the gun.

ACTING CHAIRPERSON GUNNING: Perfect. So at least we got one set of minutes done, right?

MS. OJIMA: Yes.

ACTING CHAIRPERSON GUNNING: Awesome.

MS. OJIMA: The November is still --

ACTING CHAIRPERSON GUNNING: Still hanging out there.

MS. OJIMA: -- hanging.

ACTING CHAIRPERSON GUNNING: Two meetings.

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Item 14. Public testimony.

ACTING CHAIRPERSON GUNNING: Most of you know the agenda. We do have typically public comment towards the end of the meeting, but reading the -- the minutes from last meeting, I know we have a pretty aggressive agenda and a lot of things to talk about as a board, so if you'd indulge me, there's a couple members of the audience who would like to make brief comments to the Board, so -- typically it's the last thing, but let's bring them up for this thing.

So I believe there's a Ms. Osborne, Lea Osborne. Hi. If you'd approach -- yes.

MS. OSBORNE: Okay.

ACTING CHAIRPERSON GUNNING: We have -- in consideration of --

MS. OSBORNE: Sit here?

ACTING CHAIRPERSON GUNNING: Yes, please. We'll give you five minutes to --

MS. OSBORNE: Okay.

ACTING CHAIRPERSON GUNNING: -- share your thoughts with the Board.

MS. OSBORNE: I had a personal issue that seems to be resolved, but since I'm here I thought I would bring in -- because I'm sure there are others who have a similar issue. And this is regarding the rental policy. I would like you to revisit it and perhaps change it.

You're probably aware that when someone gets a CalHFA loan, they have to keep the -- that residence until they sell it, otherwise CalHFA will foreclose. I mean, they cannot rent it out. Either they have a -- if they have to move for a job change, they have to sell it or CalHFA will foreclose on them.

And I'm not a public speaker, so I may not -- so 48 other states don't have the same policy as California. So I just wanted for you all to revisit it. I know it only affects maybe 200 people, so you guys have a lot of bigger things to worry about. But for those people, it's a very important issue.

You have two legal bond counsels: Orrick, Herrington & Sutcliff and Hawkins Delafield & Wood. Hawkins Delafield & Wood says as long as the initial intent was to occupy it as a residence, if at some point -- hey, you can say five years, six years, eight years, put a time limit on it or something. If you've occupied it that long, then if you, for some reason, you know, a personal life change, whatever, you can rent it.

Of course, this came to a head because of what's happening right now in the real estate where everything is under. I mean not everything, but so many people bought a home and they don't -- maybe they had a child, they can't -- the home's too small. They need to -- to move. They're 500 -- 50,000, a hundred thousand under. They can't afford to sell it. It will mess up their credit.

They were -- I was told by your staff in Sacramento that if we foreclose on you, it's -- it's going to be a foreclosure. There's not even going to be an asterisk to say you were paying your bills and we foreclosed on you for a reason. So that, a foreclosure like that, goes with you for seven years and still is taken off your credit.

So I just -- with everything else you have to do, perhaps you could revisit this issue at some point. You know, like I say, CalHFA must meet its obligations to their bondholders, yes, but are they meeting their obligations by foreclosing on properties? And when you foreclose on a property, apart from it being sold for so much less, it costs CalHFA an extra $50,000 per foreclosure, based on what I've read.

So that's my issue. And just a request for you to -- and there are, you know -- they -- right now, as you probably know, there are -- they -- there are exceptions they work with you, but it seems, you know, this is something constantly hanging over your head.

Not only that, I read that these -- I can't think of the word. These cannot exceed 5 percent of the total loans that CalHFA puts out. So if your issue -- if you request the approval to rent at the beginning of the year, let's say, you're okay, but at the end of the year, let's say they've exceeded those 5 percent, you're out. You're going to be foreclosed upon.

So thank you for listening. That's my -- my issue.

ACTING CHAIRPERSON GUNNING: Thank you very much. Appreciate your testimony. I know this has been an issue, and I think staff has looked at this. And I understand we've worked it out with you, but --

MS. OSBORNE: Yeah. Yeah. I'm -- I'm -- on my personal. But I thought since I was here, you know, maybe somebody didn't think to come and try to work it out.

ACTING CHAIRPERSON GUNNING: Thank you for your testimony.

MS. OSBORNE: Okay? Okay.

ACTING CHAIRPERSON GUNNING: We have one more. Mr. Frishman?

MR. FRISHMAN: Yes.

ACTING CHAIRPERSON GUNNING: Marcus Allen.

MR. FRISHMAN: Hi, thank you. I'm Marcus Frishman. Thank you for allowing me to speak at the beginning of your meeting today.

I'm here to speak on the broad public policy issue as well as asking for your intervention in my personal matter, in my personal case. I'm here to talk about the Keep Your Home California Principal Reduction Program.

There's a list of summary guidelines to the Principal Reduction Program, and No. 7 of the guidelines is program exclusions. There's several listings of items that would exclude you from a principal reduction. One of the items is the loan to value ratio, and they've decided the number will be 105 percent to 140 percent. I won't bore you with how the formula works, but there's only so much money available, so they've decided that if you're too deep underwater, you don't get a principal reduction modification. If you're slightly underwater, you don't get a principal modification. You have to fit within this range.

I made it to 147, off by seven points on the principal reduction modification, because the proprietary system that determines the value of your home is flawed, and I want to explain why. It's pretty good, actually, because it does eliminate all those subjective elements such as I have a better countertop than you. I've got the custom doorknobs. You've neutralized that, so it's good in that regard, but it is including short sales.

In the inclusion of short sales, particularly in the Hardest Hit Fund, is the hardest hit neighborhoods. They are endemic with short sales. In my particular case, it's pretty simple because I don't live in a custom home. I live in a simple gated community, condominiums, with the builder selling homes on-site. The homes are fixed price. They're not discounted. And it's pretty easy to determine the value of unit No. 4. A lot of them, hundreds of them, are sold at X number of dollars without discount.

They evaluated me, and they determined I was a certain value, and that value was deficient by $70,000, by the way. $70,000 more dollars, the real value of my home, would have put me into the program to allow for principal reduction. But because they included a vast number of short sales, it reduced my value and excluded me.

No one uses short sales. The California Real Estate Brokers Association has reported to me, the National Brokers Association reported to me, the California Bankers Association has reported to me when they do property evaluations -- long ago, when short sales turned into an epidemic problem, they had them coded, and they were excluded automatically from determining market value across the board by anyone that determines market value -- except this program.

The law, I've studied, doesn't require the inclusion of short sales. The policy that has been established to in fact implement this says something to the effect property value will be determined by all sales comps. The staff has determined that means short sales, so it skews -- it skews the value to a fake number that's not in fact market value, not accurate, and it needs to be fixed badly.

It needs to be fixed for all Californians because what has happened? Here's your result: You're actually granting principal reduction modifications to people that are falling below your own threshold number, 105. Remember 105 to 140? You've lowered the standard, and it shouldn't be that way. It should be 105 to 140 based on market value as defined by everyone else in the world -- or at least in the United States except this program.

So I've written something. I'd like to pass it out, give it to you -- where is it? Oh, here it is -- for consideration. It's asking for personal intervention on my matter. And by the way, I've been told just day before yesterday, I will have a loan modification. I've been approved. My package is on to the -- to the -- what do you call it -- the investor to decide. But let me just assure you, the investor would really like this principal reduction modification program but in fact it allocates at least a hundred thousand dollars in real cash to the bank. That gets the investor's attention.

You're likely -- there's a 50 or 60 percent denial rate on people that don't get this program. They'll never get modified, even though they're qualified.

So please fix this so that you're doing what you say you want to do and not doing what a technical glitch in the proprietary value system -- they call it the Proprietary Market Value System -- has created this problem, that -- that no one can correct.

And I'll end with this on a personal note: The program analyst that handled my account wanted to correct this. She tried. She saw the problem, particularly in my neighborhood where you don't have custom home disputes of value. You have unit 4 being sold in volume right next door to me. It had to be completely ignored because of short sale prices, which in my neighborhood are on average of $120,000 under the real market value. So that's the problem I'm here to explain.

Thank you for allowing me to speak ahead of time. That's very kind of you, considering you have a public agenda item at the end.

ACTING CHAIRPERSON GUNNING: Appreciate your comments.

MR. FRISHMAN: A whole new concept for public meetings.

ACTING CHAIRPERSON GUNNING: We do appreciate your comments, sir, thank you.

MR. FRISHMAN: Thank you. Have a nice day.

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Item 4. Chairman/Executive Direct comments.

ACTING CHAIRPERSON GUNNING: All right. Why don't we move on with item No. 4, chairman/executive director comments.

And I cede my time to you, Claudia.

MS. CAPPIO: Thank you. Thank you, Mr. Chair.

I have two items to talk with you about.

We recently completed some strategic planning for next year, for this year, '13 and '14. And we -- as part of that review, we reviewed our record and outcomes for last year, and you have them in front of you. It's Review of Outcomes of California Business Plan for last year. And I just wanted to make sure that the Board noted, since you did approve this plan, that we had some very big successes.

We were able to reduce variable-rate debt and notional swap balance over 1.2 billion, and we also were able to complete an extension agreement with the U.S. Treasury about temporary liquidity. I would want to note that Tim Hsu and his staff were very diligent in that, and we are actually ahead of the game, relatively speaking, in our -- in our plan with U.S. Treasury, so we are much more stable and better off.

We had the re-initiation of the preservation program for multiple family, the risk preservation program, and Jim Morgan and his staff did an excellent job. Over $70 million in loans were made for seven projects, and we hope -- we'll be discussing that program again this morning to get your sign-off on -- on the next year. Some -- those are the sort of really key ones.

We -- we looked at certain operational -- operational instances where we needed to look at procedures and policies a little more closely, revise them. We did some housekeeping, and we also are in the midst of some reorganization matters with the Governor and Housing and Community Development and CalHFA. And although we pursued a plan, we're now in another plan, but I'll keep you posted on that.

So I just wanted to make sure you knew, and we will be back to you in May with a revised plan for -- business plan for next year.

With regard to the reorganization, I can only say that discussions are ongoing. We are taking it very seriously and meeting together in both organizations, particularly the leadership team of both organizations, to see where the opportunities lie and the most chances of success.

We are looking at some shared objectives that really could elevate the conversation about housing with regard to infrastructure, sustainable growth, greenhouse gas emissions, and also to coordinate on our end of the game. HCD and CalHFA can coordinate better with our sister agencies, CDLAC and TCAC, to really make sure that we deliver those services, funding and programs that we can do in this state most efficiently.

We also have to look at new revenue streams and new financial structures because those that have served us well before are now -- now need to be supplemented. So we're working together well. At this point I can say that we are looking at a unified leadership structure for both agencies so that we share management, a common management, set of policies, procedures and -- and communications and therefore will flow directly down to both of our programs and divisions. I will be back to you hopefully in May or later with a more definitive set of changes, but at this point, that's what I can say.

And that ends my report. Be glad to take any questions.

ACTING CHAIRPERSON GUNNING: Questions? Comments?

Excellent. Thank you, Claudia, I know it's a Herculean task you have there and --

MS. CAPPIO: I've begun weightlifting.

ACTING CHAIRPERSON GUNNING: You can tell. We can see.

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Item 5. Report of the Audit Committee Chairman.

ACTING CHAIRPERSON GUNNING: All right. We're going to move to the report of the Audit Committee.

MR. SMITH: Okay.

ACTING CHAIRPERSON GUNNING: Item No. 5.

MR. SMITH: Yes. The Audit Committee met this morning and really was in response to the audit that was previously done. And a number of items were addressed, probably the most important of which was the timely disbursement of federal funds received from HUD, which previously we had not complied with. And I'm happy to tell you that under the new procedures, we're now under compliance. So congratulations to the staff for moving mountains to make that happen.

Secondly, there was a series of recommendations in the audit from the last time that the staff has now responded to in terms of being better run, and so I can -- you can look at the report for those. It's a fairly -- you know, not a long list, but it's a small list. And we've basically satisfied that requirement by responding to that, and that was a voluntary response, in addition to restructuring our financial statement to make it a little bit more -- better to understand and to read.

So that's the report of the Audit Committee. If there's any -- any questions, I'll be glad to entertain those.

ACTING CHAIRPERSON GUNNING: No questions? Thank you, Ruben.

MR. SMITH: Thank you.

ACTING CHAIRPERSON GUNNING: Appreciate the work of the staff on that as well.

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Item 6. Update and discussion regarding Multifamily Portfolio Preservation Program.

ACTING CHAIRPERSON GUNNING: The next agenda item is 6, update and discussion regarding the Multi-Family Portfolio Preservation Program.

MS. CAPPIO: Tim, if you could just present an overview, because I think we're taking a number of items --

MR. HSU: Yeah --

MS. CAPPIO: -- together.

MR. HSU: -- I'm going to do that.

MS. CAPPIO: Yeah.

MR. HSU: Good morning, Mr. Chairman, and good morning, Members of the Board. I will give you a -- with your indulgence, I'm going to give you a road map of how we're going to present this in a second, but I'd like to make an attempt to connect what we're going to do here with what we did at the last Board meeting. And I promised Claudia that I would have another analogy today.

Mr. -- our president recently made a major faux pas when he mixed two metaphors. He said that he -- he wished that he could do a Jedi mind meld with John Boehner so they can get a federal budget deal done. And as a Star Wars fan, I was very offended by this idea that he forgot that was actually the Jedi mind trick and the Vulcan mind meld. But what these two story lines, however, have in common is that they are both very complex and compelling stories and in which the viewers at the end of an episode is wishing for more, and that level of engagement and also anticipation helps to drive the success of the story line.

And at the end of the last Board meeting, I really sensed that engagement and anticipation from the Board. And after all, CalHFA is a compelling story. The melding of our mission, of our successes, of our travails and of our future is -- is -- is a very compelling story. It's -- it's, to be sure, no Star Wars, but it is a compelling story.

And some of the examples of this engagement that I sense from the Board, some of them were more direct. There were questions from Katie, for example, about the impact of lending to our capital base, and also Tia's question about capital allocation. Some of them were more subtle. There was Janet's question after the Board meeting about the risks involved in the TBA model. And I left the Board meeting with Matt, and as we were departing, he also said to himself that next time we're going to talk about swaps.

So these were sort of my -- these -- these were, from my vantage point, some of the things I picked up in the engagement from the Board, which I think bodes well for the future of the Agency.

One of the things I do want to emphasize is that the Board should know that the staff is actively listening to your concerns and your lines of questioning. And we have done a mind meld with these concerns, and they are reflected in the day-to-day management of the Agency, and they're important to us.

As I mentioned, with your indulgence, I'd like to take the liberty of sort switching the agenda items a little bit here. At the end of the day we would ask the Board to vote on a set of financing resolutions which does give staff the ability to do primarily three things: One is to manage our current balance sheet and to leverage whenever possible, and two is to manage our financial contracts, and three is to issue new bonds to finance new lending activities.

But before -- but because there's this piece about financing new lending activities, we thought that it would be also a great time to continue the dialogue to update you on what we're doing on the program side. But we thought that, well, before we talk about lending, we should also probably tie in together some of these questions that was brought up last time like, as I mentioned, from Katie such as, well, what's -- what's the impact on our balance sheet if we were to go into lending? And there were also a couple other questions. One of the more direct questions from Matt, too, was he mentioned something about burn rate.

So I took the liberty to turn that question about burn rate into what are the resources, what are some of the sources that support our operating expenses over the next couple years? And I also want to also tie in at the -- at the end of my presentation at the last Board meeting, I mentioned that, yes, we can and -- we can lend. I'd like to turn that idea and evolve the idea a little bit more into, indeed we shall -- we need to go back into the lending space. It's not so much that we can lend, but we really need to go back into the lending space. And that question is tied to the question about how we're paying for our operating expenses over the next couple years.

And since I'm insistent that we need to go into the lending space, can I actually on my side be putting up capital to support lending? These are the kind of questions I'm hoping that we'll address as part of the capital allocation question that we'll talk about, and it will go towards directly answering Tia's question from the last Board meeting about capital allocation.

One of the key components of the capital allocation question is this swap collateral risk that we have that we talked to the Board about. And so the first thing that we thought we should do is to step back a little bit and give the Board a sense of what this risk is and -- and why staff thinks that this risk today is more -- is better contained then ever.

So first, I'm -- I went back in my records on whether or not I presented this chart to the Board in the last couple years, and I'm chagrined that I haven't shown this chart for quite some time. I think we've been flying very high level on this collateral posting risk, but I thought it might be instructive to step back a little bit and -- and talk about why we have these swaps in the first place.

The swaps were intended to hedge the floating interest rate risk of variable-rate financing from the years in which we did this. And it was believed at the time that these variable financings would give us a lower cost of fund over a long period of time. That has proven to be untrue, and I'm not here to discuss why that's not -- that didn't work out for now, but I'm here to talk about our efforts in dealing with this legacy risk. And if there's interest in that, we can talk about that at a different Board meeting.

But in general, the swap was put in place so that we would receive a floating rate from the counterparties. And you can see that the floating rate is passing through to the bondholders, which have a variable-rate bond. And since we have a fixed-rate asset in our mortgages, the fixed rate is able to debt service the fixed rate that pay to the counterparties.

And why is it that we talk about the swaps as having a need to post collateral? Over time it's becoming a real risk that we're dealing with. As the rates have declined over the last couple years -- because we pay a fixed rate and receive a floating rate, as rates declined, these mark -- the mark to market on these swaps became more and more negative to us.

The other way to think about that is that since we're paying them a fixed rate that was determined many years ago, as rates continue to come down, that value of that cash flow we pay them becomes more and more valuable over time. And you can see this inverse relationship on this chart. You can see that as rates plummet by this -- what this chart is showing on the left-hand side is a scale of interest rates. On the right-hand side is the scale for our mark to market. And in red is the sort of declining of the interest rates.

So you can see as rates start to plummet over here, the mark to market on our swaps is going up. And you can see they're almost sort of like a mirror image of each other. As interest rates are going up, our mark to market actually goes down. So it's -- so there's this inverse relationship between rates. As rates go down, our mark to market goes up.

But there's a couple other phenomenon to keep in mind here. One is that you can see, too, that when you have these dotted lines, these are periods -- these are actually periods in which we're actually making a payment to the counterparties. So every six months we make a net payment to the counterparties. When we do make a net payment to the counterparties, you can see that mark to market goes down.

It may seem very straightforward, but when you owe someone money, when you pay them money, what you owe them goes down. And then we also take those occasions when we make the payment to them to also lower the notional amount of what we need to pay on these swaps over time, as we have those opportunities. So you can see that between 2/1 and 8/1, we actually lowered the notional on these swaps by $200 million, from $2.3 billion and $2.1 billion.

So these periods when we make the payments, not only do we make a payment, which makes the swap valuation go lower, we also take those occasions to -- to lower the amount of what we need to pay them going forward. So you see that in these periods, the mark to market has been driven down. It happens here.

It happens here to a lesser extent. You can see this is quite dramatic. And it happened most recently a couple weeks ago.

There is a lot going on on this chart. This is one of the charts that kind of will bend your mind a little bit, but I'm going to try to explain why -- using this chart that this idea that the mark to market, the highest mark to market is behind us. What this chart is that -- this is a histogram, which for the Star Trekkies in you, is a distribution of certain observations. So I'm going to focus on the right-hand side of this chart for now.

So what this chart is showing is that how many times our -- how many times our mark to market fell into a certain bucket. So what this is showing here is that, for example, there are about 34 weeks -- these are weekly observations over the last two years. Okay? There were 34 weeks in which our mark to market was in between $320 million and $335 million. So that was -- this is sort of the peak observation. We have a lot of weeks in which we fell in this bucket.

And there was about two weeks in which our mark to market was as high as $380 million to 395. And there was about one week in which our mark to market was between 215 to 230. Where we are now is right here in this bucket of 275 and 290. So you can see that where we are now is well on the lower half of this distribution of our observations over the last two years or so. Again, these are weekly observations.

So one of the things that I know that people worry about is that these observations are very dependent on rates, like I've been showing the last couple charts. So what we did was we said that, well, even if we were to lower the current rate by 50 basis points -- and in the previous chart we've been using the six-year LIBOR as a key rate -- the key rate around now for six-year LIBOR is 1.25 percent. So even if we were to lower that on the average from 1.25 by 50 basis points down to 75 basis points, our mark to market would jump up out of these two categories to about 305 to 320, but certainly it's still well in the lower half of this distribution.

And this is one of the reasons why I'm asserting that this risk, that the mark to market is going to cause a very high collateral posting, is -- the worst of that is definitely behind us. And then the reasons are, as I mentioned in the last slide, we've been making these payments when the payment comes due, and we've been driving down the notionals when we have the opportunity.

So this is -- this is the view from the mark to market point of view.

On the left-hand side of this chart -- this is the view from the collateral point of view, but you can see the pattern is very similar. So you can see that there was about nine weeks in which we were posting between $125 million to 140 million. And its peak, the peak -- the peak posting amount, if you will, of about 46 weeks is in this 95-million-to-110-million-dollar category. And there was about ten weeks in which we were posting only 20 to $35 million. And where we are now is about in this range, 65 to 80. I think we're posting about 69.

And you can see if we were to shock it by 50 basis points, our plot would go up to this category. I think it goes up to about $91 million. It wouldn't -- it wouldn't be -- it doesn't spill into these categories over here, which is on the higher path, if you will, of that distribution. This idea that we're now in the lower half of the distribution is -- is the main reason why I'm thinking that this risk is better contained than it has been over the last two years.

And this is just another way to show that -- why I believe that this risk is better contained today than it has been over the last two years. What you can see here is that the highest collateral amount we've ever posted was back in January of last year. And at that time, we posted $132 million.

And the six-year LIBOR, which is, again, sort of a proxy that we're using for interest rate, interest rate curve in general, the six-year LIBOR at the time was just a hair above 1.25 percent. It was probably about 1.3, 1.4 percent. You can see that despite the fact that that LIBOR rate actually declined a little bit -- it declined a little bit until about today.

So as it declined, you would expect our mark to be higher and our collateral to be higher, but on the contrary what's happening is our collateral, right? But on the contrary, what's happening is that our collateral is actually lower. And, again, the same point's that we're making: The reason why they're lower is that we've been making these payments on these value dates and the fact that we've lowered our notionals from $2.3 billion down to $1.9 billion.

Tony is our new financing risk manager. He's going to present the next couple slides.

MR. SERTICH: I'll give Tim a break from his workout jumping around over there. I'll walk through the next few slides, still on the swaps and the collateral posting.

You know, a general question you may get after these last few slides that Tim has shown is why do we have to post collateral? And the collateral, as you noticed from a couple of the charts, is directly related to the market value of the swaps. What we have to do is we -- the counterparties require us to post collateral on market values over specific thresholds with each counterparty.

The chart -- the table on the bottom of this slide here shows a sample counterparty and how much thresh -- how much -- what the threshold is that we do not have to post collateral on the market value. So it's dependent on the rating of CalHFA, CalHFA's general obligation.

So in this case, when we started issuing these swaps, the rating of CalHFA was AA minus. And at that rating level, we never had to post collateral to the counterparties. They trusted that we would be able to pay the obligations going forward on the swaps, and they weren't worried about it. As we got downgraded, they said, well, we'll give you some amount of leeway on your market value, but if you cross that threshold, then you have to post the extra amount as collateral.

So currently we're rated A minus/A3 by the two different rating agencies. So we -- we would -- on the original agreements we made with them, anything in excess of $14 million of market value we would have to post as collateral. However, over the last three years, three, four years, we've restructured these agreements with a few counterparties to give us a little more wiggle room in terms of the threshold.

The first time we restructured, we increased the A level thresholds up significantly, especially the A minus went from 14 million to $40 million, so that saved us $26 million in collateral we'd have to post to a specific counterparty. And then we also did a second restructuring where we increased a BBB plus threshold if -- if CalHFA ever was downgraded to that level, which thankfully so far we have not.

And another point Tim was getting at was how aggressively we're reducing the swap notional amount, which is the amount that the -- sort of like the par amount of the swaps. And in 2009, early 2009, the notional amount on all of our swaps exceeded $4.5 billion. And if we had let the swaps just run off and passively let them go their way, today the notional would have been reduced by about a billion dollars to about $3.6 billion. However, because we aggressively managed these swaps and exercised all the par options we had available to us, we have decreased the amount below $2 billion, which is, you know, slightly over half of what it would have been if we had only passively managed these swaps.

And along with that is the projected swap valuations going forward. We continue to expect them to decline for the same reasons Tim gave before. Every time we make a payment, we owe less in future payments to the counterparties. And, also, we expect the notional amounts to decrease over time as the swaps peel off and as we exercise the par options. So we expect the -- currently the swap market value is about $275 million. In three years' time, we expect it to be closer to a hundred million dollars, well under half of what we have today.

And that -- that holds true for the amount that we're posting in collateral as well. Currently, like Tim said, we're posting around $70 million in collateral, and we expect that to decrease over the next three years to well under $50 million as the -- as the market value deceases.

And so, you know, Tim -- the larger point we wanted to make today is that we think we have a much better handle on the collateral posting. If we get downgraded, we will be able to manage that. And if rates go down, we will be able to manage that. And that's what we wanted -- that's our main point from this presentation.

MR. HSU: Though this risk is better contained, it still plays a large part of our capital allocation, which we're going to talk about in a second, but I thought that it would be good for us to first establish to the Board that, yes, this risk is there, but compared to what we've been through over the last couple years, this is much better.

ACTING CHAIRPERSON GUNNING: Tim, excuse me, can I just interrupt you?

MR. HSU: Yeah.

ACTING CHAIRPERSON GUNNING: What's your sense of when we'll be done then with the swaps and all that variable-rate stuff? Prediction when it's all paid or a sense of how far out?

MR. HSU: My -- my sense is that if you look at this chart -- so what we're showing on this chart here is history, is how we got to where we are today since the financial crisis, which is probably defined to be the latter part of 2008. And this chart here shows how we expect to take down these swaps over the next couple years. And part of the reason why we have been ending some of these charts on 2015 is that that is also the expiration date for TCLP.

So my sense of it is that this idea that we have to post collateral and it being a risk, it will probably not ever go away -- and by that I mean five years, say, or ten years -- to the degree that our rating is still under some pressure. But you can see, if you look at this chart, that at some point -- and I think that this is something we talked about with -- amongst the staff all the time is that many of the things that we do here inherently has risks, meaning real estate lending and also selling bonds. It -- inherently there are dimensions of risks that we deal with in our business. The question is how manageable are these risks?

So if I could have your indulgence and turn your question into not that when they go away completely, but when is it -- when is the day going to come in which the amount of capital we allocate for this risk is, let's say, something that is not going to be alarming. And you might -- you might suggest that, later on when we show you how much capital we're setting aside for this risk, it's a lot of money. But what is it, for example, when we only set aside let's say 20 or 30 or $40 million for this risk?

I would say by 2015 or so, our -- in that range and about, you can see that the notional amount of our swap is going to be even lower than where we are today. So what this chart is showing is -- in the blue here, it's showing the passive management of these swap notionals over time. So you can see that even if we do nothing, these swaps will amortize, so nearly $1.9 billion down to about $1.5 billion. But with active management we think we can bring that down too -- that's in blue. And in red here is our active management. With our active management, we can probably bring it down closer to about $1.2 billion.

The combination of the lower notional at that time and the general expectation that by that time rates will be slightly higher than where they are now will probably drive the need to post collateral to an amount that would be so manageable that it wouldn't be -- later on you'll see how much money we're actually setting aside for this risk, and you'll see that while at the moment I'm contending that it's -- well, it's a better-controlled risk than it has been in the last couple years, we're still setting aside a tremendous amount of capital for this.

Oh, yeah. And this chart that Tony's pointing out, what this chart is showing is -- is -- is the -- the geeky way to look at this question, since we're on a Star Trek theme. So what we're -- what we did here is we said that we can look at the projected interest rate curve in the marketplace to project our future mark to market. So at any given point in time, the marketplace has a projection of what rates are going to be tomorrow. And what this is trying to do is simply piggyback on that projection to project our future mark to markets.

So what this is saying is that the future mark to market, what we're expecting is that -- let's say by 2015, for example -- by 2015 instead of today's mark to market of about $270 million or so, we're expecting that our mark to market will be close to about $130 million. And with a $130 million mark to market, we're only expecting a collateral posting of about $20 million or so or $30 million or so with our current rating. And even if we were to be downgraded, that collateral would only be about $50 million or so.

ACTING CHAIRPERSON GUNNING: That's good.

MR. JACOBS: Tim, how does this look if there are, you know, sensitivity analyses on a couple shocks to the system? I mean, is it still under control even with an unexpected rate environment?

MR. HSU: So what we did -- which I didn't bring here, but, for example, in the -- when we're doing this -- when we're doing this, for example, we are shocking the interest rate by 50 basis points. So we had a chart that looks very much like the last chart you saw with 50 basis point lower curve than they are today. But what you do see, though, is that generally, though -- I'm sorry. Going the wrong way, sorry.

You'll see that with the 50 basis point lower projection on the far curve, that we will have a mark to market line or step, if you will, that are probably $50 million -- again, if I had known you were going to ask that, I should have brought it -- about $50 million higher than these steps.

But what's -- what's important to -- to focus on, while that's true and -- is that there will -- despite the fact that we will be $50 million higher, it will exhibit the same pattern of the step. Again, we're making the payments and we're driving down notionals when we have the opportunity. And we're going to talk a little bit more about that later on when we talk about setting aside capital for that.

MR. SERTICH: In general, though, time is on our side with this. The longer we make it out, the lower it's going to be, even with these stresses on it.

MR. HSU: So marching on to capital allocation. Before we talk about the actual allocation itself, this is a chart I showed to the Board last Board meeting. I wanted to establish a little bit of high level what our balance sheet looks like again and then show you where to keep your -- where to focus on for this particular exercise of capital allocation.

So at a high level, the Agency has three entities. There's on the very right-hand side contract administration. And the reason why that's important is that this is a lot of money that the Agency receives from the State to administer, so they don't count as part of the Agency's equity, but by running the program, we do generate annuity -- a fee-based annuity out of running these programs.

And on the left-hand side in orange is the single-family indenture, which -- which I won't spend too much time talking about for now today. But in blue this is, if you will, sort of the parent company. This is where we keep the lights on and pay people's salary. Where I want you to keep your eye on for today is that I think -- this doesn't look blue to you, does it? Or does it?

MR. SHINE: No, it's green.

ACTING CHAIRPERSON GUNNING: Green.

MR. HSU: It looks green, right, but I think on your page it's actually blue, right?

MS. CAPPIO: It's blue.

MR. HSU: Okay, good.

MR. SHINE: Bluish.

MR. HSU: It think you guys all know I'm color blind, so I was a little bit surprised to see that I could see it's actually green.

But what I wanted to actually -- what I want you to focus on for today, for this particular capital allocation exercise, is the pot of money that's sitting in here under blue, what I refer to as non-bond assets, that $435 million of unencumbered assets. And that is the money that we can use to support lending or to do various things that -- that we need to do to keep -- keep the Agency healthy.

And this is also a chart I showed last time to talk with the four high level risks that we confront. I won't go over them again, but what I want to focus on again is the fact that this blue, this -- this sort of a -- this sort of archipelago of blues that you see here are all under the umbrella of our Agency's general obligation. And it primarily has three big things that it does. It guarantees the real estate risk of this multi-family indenture, which is where we make all our multi-family -- which is where we make a lot of our multi-family loans prior to the financial crisis. You can see that this indenture does have some of these TCLP-backed VRDOs in them.

And it also backs the real estate risk of this indenture called HPB. And this is an indenture that currently has a lot of our multi-family tail loans, and also it has a lot of our single-family downpayment assistance loans that we finance to support some of the production in the peak years of our single-family program.

The key thing to remember is that the Multi-Family III indenture, it does benefit from the guarantee for the real estate risk for that indenture, but that indenture houses very well-performing multi-family loans that are doing very well, so it can cash flow on its own. It doesn't need cash infusion from anywhere else to actually meet its obligations.

This HPB indenture, however, because it does house a lot of these single-family downpayment assistance loans is unable to cash flow on its own, so it needs cash infusions periodically in order to pay its debt service.

And then last but not least is this idea -- it's -- it's green again -- this idea that out of this non-bond asset bucket, we do have some very liquid assets and cash and securities that we can use to post as collateral to our counterparties when we need to. So the idea of keeping a lot of cash around to meet that collateral posting risk is also being -- being embedded in the obligations of this blue box.

The key thing to remember here is that when times were good -- when times were good and this orange box was actually performing well, periodically it would actually send cash, release out of the lien of the indenture, it would actually pay cash into this box over here, and it would be used to help pay for the operating expenses of the Agency. And this indenture here did the same thing. It used to send cash over here so we can pay for the operating expenses of the Agency or do whatever else we would desire to do.

But today because the orange box is dealing with a lot of single-family losses, in large part the cash that it would otherwise distribute up into the blue is needed in order to help it survive these losses.

And the Multi-Family III indenture, while it does have the capability to distribute cash into the non-bond asset bucket, a lot of the cash that it does generate -- again, that indenture is doing very well, so it's generating quite a bit of profit -- we are trapping that cash in that indenture because we also want to deal with the idea that we need to get rid of these variable-rate bonds sooner rather than later, possibly before 2015.

So one of the questions that Matt asked out of the last Board meeting is this idea of a burn rate. And as I said, that's the last time I'm going to use that phrase. I'm going to turn it into how do we -- where are the sources in which we -- where are the sources that pay for the Agency's operating expenses over the next couple years. Okay?

Since the orange box and that multi-family indenture are very busy taking care of themselves and they're not distributing cash into the parent company, if you will, then the question arises that -- and how have we been paying for operations?

Well, a lot of the sources for paid operations over the next couple years come from these unencumbered assets that we have. So this chart is a breakdown of the -- this chart is a breakdown of the unencumbered assets that we have. So you can see that we have about $298 million of cash and securities, and we also have about $137 million of unencumbered loans.

So some of these loans are HELP loans that we made throughout the years to the cities and locals.

And multi-family loans, these are sort of -- multi-family loans, these are the LIHTC deals that we have that are very seasoned. And many of these actually need recapitalization, so some of these will actually be recapitalized and prepaid over the next couple years.

And these single-family loans of about $60 million that we have, these are the single-family downpayment assistance loans that we have.

So in large part, these assets over here could generate an annuity. Moving on to the next page, 17. Those unencumbered assets can generate an annuity, which is represented by the lighter green on the bottom of this chart. So you can see that for the next couple years it generates roughly about $30 million a year.

And on the top over here, on the darker green, what you're seeing is that -- as I mentioned, out of that contract administration box, we are administering programs for the State, and we're generating fees. But the top green over there represents the fees that we generate for running state programs and also the flow earnings that we're getting from holding cash and holding securities.

One of the things I want to emphasize -- because I'm sure that this chart will generate a lot of discussion. One of the things I want to emphasize is that this, in many sense, is the baseline revenue for the Agency over the next three years. In other words, we have not put in what the benefits would be if we were to do lending this year, next year, or the year after this year. In some sense, this is sort of -- in a way I almost think of it as a safety net. This is the baseline projection. Okay?

And so in red what we have is our projected operating expenses over the next couple of years. Now, while I'm sort of emphasizing the point that this is not -- this is -- this does not include the revenues that we might generate over the next couple years, this compression, if you will, between here and here is unmistakable. We can't deny the fact that we seem to have less room for error over there than over here.

But the key thing I want to -- one of the other things I want to emphasize is that this additional buffer that we have here this year, at the end of the year, this will actually be added onto the cash you saw on the last page. Okay?

So to answer the question in a different way, it would seem that based on this projection, we are actually not -- we actually have enough cash flow that comes in on a yearly basis to meet our operating expenses for -- for the year. And we can do that for the next three years.

But, again, that compression of the room that we have is certainly unmistakable, and what we really need to do -- and this is part of the reason why I emphasized in the early part of the presentation we need to emphasis that not only do we -- not only can we lend, we really need to get back into the lending space because we do need to generate the revenues so that this baseline here could be -- we could be adding on more revenues on top of the baseline so we can clear this hurdle better than what we're doing here a couple years out.

MS. FALK: Tim?

MR. HSU: Yes.

MS. FALK: I have a question. So the top part of the boxes, the darker green, is that primarily from contract administration?

MR. HSU: Yes. It's primarily -- I think that about three -- three quarter of that top box is from contract administration and about one quarter is from flow earnings.

MS. FALK: How long are those contracts? Are these ongoing or are they -- is there risk that they might stop at some point?

MR. HSU: I do think that a lot of those annuities are -- are longer term. So if we take this project out longer, what is actually more volatile is not the top, but the bottom.

MS. FALK: Oh, okay.

MR. HSU: Because of the -- some of the revenues you see here on the bottom do represent that in the previous chart where I'm showing you these assets that we have, like for example here and here, these over here. These are very seasoned multi-family loans that we have. They could be 30-year loans that have seasoned for about 25 years, so they're at the tail-end of their amortization schedules. They're amortizing really fast.

So much of what you're actually seeing here could actually potentially not be revenue, if you will, because this is merely a cash flow exercise, right, that will actually represent the repayments at maturity of some of these loans. So what's more volatile is not the top piece, but it's actually the bottom piece.

MR. SHINE: So you want to carry that out further than three years to get more comfortable.

MR. HSU: What I'm hoping to do is that once we establish a better -- a better sense of what we can do on the revenue side, to do those things together. Because I think at the moment if I take this out for ten years and thinking that we're going to be passive in terms of our revenues, it will -- it will appear as if this compression will continue to compress and at some point it will flip over. But I think that to assume that we're going to be passive about generating revenue is probably not fair going out that long.

For -- for some of the Board members who have been with us for a long time, our cash position today is much better than it has been in the past. And not only is the idea that the absolute dollar amount is higher, what's more important to me is that some of the variables -- some of the variables that could cause the volatility in the cash position has also been eliminated. We have fewer variables than before, and we also have a better cash position than before.

So I mentioned that what we would do is talk about how much of our capital is actually set aside for this collateral posting risk. So what you see on this chart is that currently out of that $298 million the counterparties hold $69 million and we hold $229 million. And if we were to be downgraded by one notch, they would actually hold $158 million and we would hold $140 million.

What we propose as a possible -- on page 19. What we propose as a possible way to allocate our liquid capital is to assume that we would maintain an A-minus rating but be prepared for a one-notch downgrade. So we will hope for the best but prepare for the worst.

So what you see on the left-hand side of the chart is that out of that $298 million, we would actually set aside $158 million to prepare for this collateral posting risk. Over the years we've also had this rule of thumb that roughly speaking we should have an amount of cash in the bank that's equal to about two years of operating expenses.

Now, this is very, very conservative. Because if you think about it relative to the chart, we presented on the fact that we could actually generate cash on the current year basis to offset the expenses for the current year, that we don't really -- this is money that's just being parked there. We're actually not spending this money. We have money that comes in that we can spend right away. So parking on two years' operating is arguably conservative, but it's a rule of thumb that we've been living with.

So that means that out of that $298 million, arguably we could think that about $60 million of money is available for us to be supporting lending or possibly be used for debt management. So on the right-hand side of this chart, what you're seeing is that out of that $60 million is one of -- one of the many possibilities of this allocation but one that we're proposing in which $30 million would be dedicated to our debt management and $27 million would be used to warehouse multi-family loans and $3 million would be used for warehousing single-family loans.

MS. CARROLL: Tim, can I ask a quick question?

MR. HSU: Go ahead.

MS. CARROLL: On the chart where you're showing rating shock, does that also have interest rate shock in it, or is that just rating shock?

MR. HSU: This is just the rating shock. And for the double whammy, I'll show you that in a couple slides.

MS. CARROLL: Okay. Thank you.

MR. HSU: So what -- what made us pick some of these numbers that we're showing you on the last slide? So we have a nine to one ratio between what we're dedicating to multi-family warehousing and single-family warehousing, $27 million versus $3 million.

That ratio, we believe, does reflect the Board's concern about the single-family lending space, and it also represents, in many sense, the difference in what's being contemplated in the different programs. So in the multi-family world, we're still contemplating being a lender, an issuer. And I think at the last Board meeting we talked about being a lender is more capital intensive than -- than not.

In the single-family world, we're contemplating being a part of a TBA funding model in which we're not the lender. There are different risks associated with that, which Tony and Rick will talk about later, but in large part we have designed that so that they're minimizing the risk that the Agency would take.

And -- and that's, in many sense, a good example of this mind meld I talked about earlier, that the discussion that we are having here with the Board does translate into some of the decisions that we make in the back end on the program side.

Why is this warehousing idea a big deal? I think that at the last Board meeting we talked about that it's actually impossible for you to lend if you don't borrow. Well, it's actually really hard to lend, too, if you don't have any kind of warehouse line. And I think at this -- at that Board meeting a year ago, I mentioned to the Board that we actually paid off our line of credit from the State, the PMI line. And almost a year ago prior to that we paid off our line of credit from B of A. So for about a year now we basically have no line of credit. So this is, to me, a significant event for us to suggest that we could take some of our own liquidity to be warehousing lines to support lending.

What would some of these money dollars be used for? On the multi-family side, that $27 million, that money, could be used to facilitate loan closings and bond closings, and to the degree that one day we do the construction program again, it could also be used to facilitate a funding of the construction draws.

On the single-family side, that could be used to advance the funding of downpayment assistance loans. And I think that's something that Tony and Rick are going to talk about later. But I think that it's important to mention to the Board that at the last Board meeting, we didn't really talk about the single-family program needing any capital, but the evolution of things, there's now a small amount that needs to be set aside to warehouse some of these downpayment assistance loans.

And there is a one-to-one allocation percentage between the program warehousing supporting lending and also the idea that some of our cash would be set aside for debt management. So we're setting aside $30 million for debt management, and we're setting aside $30 million to support lending. And that represents sort of our -- our dual mandate, if you will, of trying to fix the legacy issues and also at the same time needing to launch into a lending space again.

MR. BELL: Tim, the suggestion you're making is that the Board should focus on the finances of the Agency under a lower rating? And I'm asking that because the proposed allocation of liquid capital is based on the Baa1/BBB plus.

MR. HSU: Um-hmm.

MR. BELL: And I assume if we were to look at the current rating, we'd have a lot more cash to spend. Am I right?

MR. HSU: That's correct.

MR. BELL: And the operating expenses seem to be the same under every model, 80 million a year?

MR. HSU: 40.

MS. CAPPIO: 40.

MR. BELL: It's 40. 40, okay. And I see -- I see -- I see you have --

MR. HSU: Keep reading, Claudia. Keep reading.

MR. BELL: -- set aside for two years of operating expenses. So but I'm just trying to -- I'm just trying to follow this. So if -- if we took the proposed allocation of liquid capital and we applied the current rating, the available cash would be 149 million as opposed to 60? Because I'm looking at the 229 and I'm subtracting out 80?

MR. HSU: I think --

MR. BELL: Is that --

MR. HSU: I think if we were setting aside capital using the current rating.

MR. BELL: Um-hmm.

MR. HSU: So what we have is that we would have 60 plus the difference between 158 and 69. So what is that, Tony?

MR. SERTICH: It's 169.

MR. HSU: It's 169.

MR. BELL: Okay.

MR. HSU: So then --

MR. BELL: Okay.

MR. HSU: So then it's true. If we decided that -- that's a much more aggressive approach, and it would go in the polar opposite direction of her question about shocking both rating and interest rate.

MR. BELL: But as far as -- as the Board's consideration of how much money is available for lending, are you suggesting that the -- the more conservative model with the shock of a lower rating for the Agency should be used?

MR. HSU: Yes, I am. In terms of supporting -- in terms of supporting lending, we are suggesting that we ought to be prepared for one notch downgrade so we have the cash to meet those obligations. Yes, we are.

MR. BELL: Thank you.

MS. CAPPIO: We're not expecting it, but we have to be prepared for it.

MR. HSU: That's right.

MS. CAPPIO: Because Fortune shines on those who are prepared.

MS. FALK: What's the average size of the multi-family loans that we do?

MR. MORGAN: Well, the ones we did last year were 10 million. So we did seven loans, 70 million.

MS. FALK: So --

MR. MORGAN: But for the acq. rehab, probably anywhere from five to ten, $12 million.

MS. FALK: So the $27 million doesn't do very many loans.

MR. HSU: Well, it's true, but I think keep in mind that oftentimes just because of the way the approval process works in terms of CDLAC and TCAC, there is a natural grouping of the projects as they come into the funding mode. So what that $27 million would do, it wouldn't warehouse every project we do, but if for whatever reason we have someone who is not part of some bigger cohort, we could potentially warehouse that.

And -- and it's true. I mean, I think the questions from Wayne and from Janet are -- are suggesting this is not a large amount. And I -- I know it's not a large amount. But -- but I think -- I do think it's significant, though, that we're getting these flexibilities because up until this point we haven't had any flexibility.

Whether or not this dollar amount can grow next year, I'm confident that this number will grow next year because of my entire presentation about that collateral posting risk will be lower next year than it is now. So that number will probably only have potential to grow, but it's a small step.

But wait until we talk about Katie's concern. You'll see why I'm trying to -- I am trying to strike a conservative pose here, but it's because what we're doing here in some sense is static because rates move all the time and things happen. So as such, we need to be conservative in how we allocate capital.

So let's talk about Katie's double whammy, if you will. So what we did and I think we've shown -- we're now on page 21. What we've shown in a couple of the previous slides, on the collateral posting risks and swaps, is that we did the collateral -- we did take our mark to market and shock it by 50 basis points. So what you see on this chart is that we're doing a two -- a two variable test, assuming both of them happen to the worst. So we're saying what happens if we get downgraded and in addition what happens if interest rates go 50 basis points lower than where they are now.

So if they do go lower but we don't get downgraded, what we would post is $91 million, and we would have $270 million of cash left. But if we do get downgraded and rates do also go lower at the same time, you know, thus the double whammy, the collateral posting will go all the way up to $196 million, and we would only have $102 left. So our counterparties would hold two out of every three dollars that we have.

If we allocate capital the way that we've been talking about, which is to allocate assuming that we can sustain a one notch downgrade, this is what it would look like if we did deal with the double whammy. So what you'll see on the left-hand side is how I -- how we proposed to allocate capital a couple of slides ago. You'll see that we allocate $158 million for this collateral posting risk, and we have this $80 million buffer that we set aside for operating expenses.

If we were to post 196, what would happen is that our buffer for operating will go down to 42, and what will happen is that when I mentioned that we -- we're allocating capital assuming that we have an A-minus rating but be prepared for one notch downgrade, but once we are -- suppose hypothetically we are indeed downgraded. Our par share at the time will also change so what would happen is that these lines of credits that we have extended to the lending side, these warehouse lines, these are not subsidies. These are not grants. We would very quickly try to unwind these warehouses to build back up our more liquid cash position.

So the sum of those two is $30 million. So over three- or six-month time frame as these warehousing needs unwind, then we can replenish up to $72 million, 30 plus 42, $72 million of our sort of target set-aside for operating.

So if we do set aside for one notch downgrade, we can, in my opinion, still deal with a downgrade coupled with a rate -- a lower interest rate with -- with -- with no problem.

ACTING CHAIRPERSON GUNNING: Tim, just one question. The ratio nine to one, is that what the Board thought about or -- it seems to work, but, what, eight to one, ten to one? Is that your doing?

MR. HSU: I said proposed. And I think that what Tia wanted from the last Board meeting was a very clear discussion with the Board on what the allocation would be. And I think that she, along with few other Board members, articulated more of an emphasis on multi-family versus single family. I think that -- I think --

ACTING CHAIRPERSON GUNNING: It seems like you hit a sweet spot. That's the point.

MS. CAPPIO: If I may, I also think that the multiple-family need is a lot clearer, and at this point our position in the single-family market is still -- we're still trying to figure out that -- where the new world order lies and where our position is, so that's the other reason. We -- Jim keeps pounding us, "Money. Come on. Let me lend. Let me lend," because the need is so demonstrated. And it's not clear at this point given the market where we fit into the single family, although we want to pursue it.

MR. HSU: So, okay. I think that the idea that we need to go into the lending space needs to acquire some sense of urgency because, as I've been saying, it is tied to this idea that those lines you see, that compression you see, in terms of our baseline revenues and also our expenses, we need to create more revenues to offset those out years.

But having said that, I do agree that $30 million in the grand scheme of things does not seem like a lot of money, but I'm hoping that number will grow over the years. I'm confident that next year it will be higher, but it's a small step.

I think that we're going to now have updates on the single-family program and get back on the agenda, starting with agenda item 7. And Rick and Tony are going to cover this.

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Item 7. Update, discussion and possible action regarding Single Family Lending Program.

MR. OKIKAWA: Thank you, Board Members. Good morning. My name is Rick Okikawa, and I'm the interim program administrator. It's O-k-i- -- this is like a deposition, you have to spell it out, so O-k-i-k-a-w-a.

So listening to Tim's presentation about the capital allocation, that's clearly what we're here for, is to fit in what our single-family plans are. And as Claudia said, it's not exactly certain right now, but what we'd like to do is kind of lay out as what we did in the last Board meeting where we provided that TBA model in -- in joint conjunction with the two products. And those products were the CHAP and CHDAP products.

But in this situation, what we're looking at today is we're focusing more on the risk. And that's what Tony is going to go into as we go on. But in conjunction with what Tim was saying, we're looking at that blue box and protecting the blue box. And so any of the -- the allocations that were allowed for warehousing, the $3 million, that goes in context with what we're going to present today in terms of the downpayment assistance.

And also, yes, we are listening to all the Board members. And in terms of the mind meld, I guess the analogy used before, clearly, like last meeting, Matt, you had mentioned what happens when, say, for example, a water heater or a roof, which is a common cause, what happens then when there's no capital and what -- what situation -- what are the things we are doing? So what we're trying to do is -- is form products and -- along with this TBA model so that we can address some of those issues and come out with some kind of presentation for the next meeting.

So the direction of this is -- where we're headed is the next meeting after we go through the risk analysis today on the TBA model, we're looking to get approval of the TBA model as well as presenting certain products, existing products, that already exist, like our CHAP, CHDAPs and discussing certain general parameters. Because obviously in today's market we need to be very flexible in terms of how fast things change. For example, with the FHA lending and the requirements of FHA lending, you know, soon it will probably be 5 percent down, which right now is 3 and half percent. Things may change, and we need to be flexible in order to lend.

And as Tim says, yes, we -- you know, it would be good to be able to lend again. And even though we're in a -- kind of a growing stage in terms of single-family lending, it would be nice to be able to get back out there again.

Other comments I noticed last meeting,

Ms. Falk, you were talking about, you know, what are the -- where are most of our defaults? And -- and, you know, we need to figure out where those -- what causes those defaults and how to address them and clearly make sure that we address those issues instead of going around trying to solve -- make a solution without knowing what the problem is.

And, Mr. Bell, you had talked clearly about this TBA model that's been used in other areas and what -- what other states. And it sounds like you were more concerned about the risks. And those are the kind of things we'd like to go over today.

Ms. Patterson, who's not here, she was talking clearly about our limited resources and how those limited resources could be best allocated through focus groups and finding out where the best needs are for the state and -- and what -- what areas we need to cover.

So that is the -- that's the direction we're headed. And as I said, for next meeting we need to be looking at a lot of these things, and we're looking at our current programs and would like to next meeting talk more about approving this TBA model and as well as other -- in conjunction with other products.

One other thing, I believe the funding of the DPA loans in terms of what risk, since what we're talking about today is risk, funding the DPA model oftentimes with our CHAP loans, we require some for warehousing, without use of a better term, where we would initially fund -- sometime after closing purchase the CHAP loan and then at that point until the MBSs are sold under this TBA model, that we wouldn't be reimbursed until then, so it's kind of like a short warehouse period.

And so I'll let Tony talk about the risks. Thank you.

MR. SERTICH: Thanks, Rick.

The first thing that I wanted to go over just to -- as a little refresher is what is this TBA model that we keep talking about. And really what it is, it's a -- it's a -- it's a basic MBS sale transaction. So TBA stands for to be announced, as it does in many different areas. And it's -- and it's a transaction where a price, volume and a future date are decided upon up-front when the reservation of the loan is taken. So it's really a hedge in a lot of ways, where an agreed-upon sales price is -- is determined at the date the reservation is taken for that loan and for that MBS.

The -- there are many other HFAs, several other HFAs, that are using this model in different ways. Most of them use it with some sort of -- some form of downpayment assistance. Some use it with only FHA loans. Some also include conventional loans. So they're all different, a little different. And what we're trying to figure out is where we can fit into the California market using this MBS TBA model.

So a little more detail about how this works and where the risks lie in the TBA model. Like I said, the first thing that happens is a lender will take down a commitment. And then somebody will have -- will make a commitment -- in this case it would be CalHFA -- to deliver this loan into a Ginnie Mae security at a future date. This -- this slide that we're showing assumes a two-month future delivery on that loan. And a -- and a fixed coupon and price are determined at the -- at the date of commitment. So in this case we're assuming a 4-percent coupon on the -- on the loan and that we'll sell it for a hundred percent of the par value of the loan in two months.

If there's a successful delivery of the loan, the loan closes correctly and there's -- there's no issues within it and it becomes a security, a Ginnie Mae security, the Agency will receive a hundred million -- I mean a million dollars to fund the million dollars of loans that have been committed.

However, if there's a failed delivery, borrowers -- just the loans don't close, the borrowers pull out for whatever reason, then the risk is there that someone has to make up the difference in the commitment, the price of the market value. If the market value of that commitment changes over those two months, then the Agency would have to make up the difference in that price. However, in the model that we're presenting, a hedging facilitator is taking all of these risks. They're taking all the interest rate risk associated with interest rate as well as the failed delivery risks. And on the next page I'll get into that a little more.

So failed delivery, what it does is exposes the lender to the interest rate risk in terms of trade settling in the future. If we agree to a million -- a million dollar future MBS two months down the road but we only have a $600,000 MBS, then the market value of that $400,000 that doesn't settle will have to be made up by the lender. However, like I said, we're passing that on to the hedging facilitator to take that risk so that risk does not lie with the Agency anymore.

The only risk that will remain to the Agency is the risk that the hedging facilitator does not -- does not commit -- or does not follow through on their obligations.

MR. BELL: Can I ask --

MR. SERTICH: Yes.

MR. BELL: Can I ask you a question? Is the Agency going to be paying the hedging facilitator a fee for the hedge as in total amount, or are you going to be paying them on a per loan basis or --

MR. SERTICH: It's --

MR. BELL: -- there no payment?

MR. SERTICH: It's -- it's part of the price of the MBS. So -- so if -- if -- to be honest, I don't know what the -- what that costs, but it's all included. We're not paying on a per-loan basis. We're not paying on a dollar-amount basis. It's included in the settlement price of the --

MR. BELL: And then the other question I have: Is 4 percent a negotiated percentage? So is this just one that you've chosen for purposes of --

MR. SERTICH: On this -- on this slide it's just an example.

MR. BELL: Okay.

MR. SERTICH: But what -- what we would do, and I'll get into it in the next slide, there's -- it's all based on -- this is very liquid securities. There's a very liquid market for this, so it's all determined by the general marketplace in terms of what the price and -- and, you know -- the interplay between the price and the interest. The coupon on the loan will be dependent on how the Agency -- what sort of premium the Agency wants to make on that.

MR. BELL: Thank you.

MR. JACOBS: Are we scaled to do this efficiently? I mean, it just seems to me that the size of capital may not be sufficient to compete.

MR. SERTICH: In terms of the $3 million set aside?

MR. JACOBS: Yeah.

MR. SERTICH: Well --

MR. OKIKAWA: It depends, because clearly a lot of our loans, downpayment assistance loans, aren't necessarily going to be pulling from the capital. For example, CHAP, that's Prop 46 moneys coming through us, so we're not really using that as a warehouse. So really this pretty much pertains, I think, just to CHAPs.

MR. SERTICH: Yeah, the warehouse is not being used for the first loan at all. It's only being used for the second loan, so it's a very -- when we're talking about million dollar MBSs, we're not saying we can do three of those transactions. We'll get to that.

So -- so the one risk that remains, like I said, is the counterparty risk to the hedging facilitator, but we work with highly rated facilitators to make sure that that risk is mitigated.

ACTING CHAIRPERSON GUNNING: Tony, could you share who would be some sample lenders you would work with?

MR. SERTICH: The lenders we would work with would be the same lenders that we have worked with in the past.

MR. OKIKAWA: Our current -- current qualified mortgage lenders. Gild.

ACTING CHAIRPERSON GUNNING: Okay.

MR. OKIKAWA: Wells.

MR. SERTICH: So the lenders would be very similar to our --

MR. OKIKAWA: Right.

MR. SERTICH: And then we would -- we would also have to find a master servicer who would assume the loan underwriting servicing risk upon the close of the loan. So those risks would be pushed off as well.

So the next -- the next slide has a little model of how this -- how this -- what we're calling a premium TBA structure would work. Really this gets back into Wayne's question about how the rate and the -- and the price would be set. What -- what a lot of other HFAs have done and what we're looking into is selling the MBS at a premium and using that premium to fund a downpayment assistance loan. And that's what the warehouse would be used for, would be to warehouse the downpayment assistance loan between loan closing and the sale of the MBS.

When we get that premium, the premium would go through to fund, to reimburse, the warehouse for the downpayment assistance funding at loan closing. And also out of that premium would go to pay for Agency fees, transactional fees, which is pretty standard in the MBS market.

So this is -- this is sort of -- what we're trying to rule out here is that the risks to the Agency are very minimal, and it's really just to the hedging facilitator. And -- and then ultimately when we get deeper into developing a specific program, we'll present that again.

Are there any other questions regarding this program?

Okay. I think next Tim and Jim Morgan are going to present the multi-family lending program that we have.

MR. MORGAN: Good morning.

For our multi-family, we have a new CalHFA preservation loan program. Basically what we want to do is not only focus on the existing CalHFA portfolio, but bring in deals that are non-CalHFA deals and -- to add as not only business development, but add to the -- add assets to our portfolio, start generating deals. We've -- we've received inquiries from -- from folks to see where we would be competitively as far as our interest rates are concerned, and we're getting -- we're generating a lot of buzz with regards to our own existing portfolio, and this will give us the opportunity to grow it.

The loan -- the preservation loan program would be administered with the -- CalHFA's existing 50/50 FHA risk share agreement with HUD. We are experienced with that. It was -- last year we -- first time in over ten years that we had utilized HUD risk share, since 2002. And we were able to do seven deals for $70 million, representing about 700 units.

We've participated with HUD risk share since 1994. The majority of those deals that we've done with HUD risk share were between '95 and 2002. Currently we have about 90 projects representing 8500 units for our current HUD risk share program.

The loan program, this preservation loan program, will provide the capital and -- for rehabilitation of existing developments and also preserve and extend affordability for existing tenants and also extend the economic life. Given the new energy efficiency and sustainable building requirements, it also provides an opportunity to upgrade existing projects with energy efficiency appliances, materials.

For our existing CalHFA portfolio projects, the loans must have met or exceeded their 15-year tax credit compliance period and are subject to a prepayment fee associated with that loan. So currently in that bucket we have about 119 projects representing about $205 million of existing debt with a huge opportunity to recapitalize. We have projects that weren't able to make our time line last year, in 2012, and those projects, right now we have six projects ranging from Red Bluff, California, to -- to -- to Los Angeles and with about $50 million worth of the deals queued up and ready to go.

And, again, available for nonprofit, for-profit, public agency sponsors.

MS. FALK: Jim? One question?

MR. MORGAN: Sure.

MS. FALK: Just of these projects that you have and you've seen coming through, are most of them using -- utilizing tax credits again?

MR. MORGAN: Yes.

MS. FALK: Okay.

MR. MORGAN: Yes.

MS. FALK: And so they're already being -- are you requiring them to continue the affordability that they originally had?

MR. MORGAN: We're -- we're -- that's what --

MS. FALK: At least --

MR. MORGAN: We're looking at their proposals, the existing deals is -- the existing deals received on those six, they want to maintain the current affordability restrictions. We're -- we're looking at our -- in our term sheet on how we determine what we want to do as far as affordability restrictions. We'll meet our 20 percent at 50 or 10 percent at 50 and 30 and 60 as minimums. It's a -- we're looking at if we want to see if we want those at 80, 120. It will depend, deal by deal. But we'll have -- we'll have a minimum that meets our CalHFA requirements.

Mine was a very accelerated presentation. I know that there may be a question about the rate stack on this. And we in -- with research with Finance and what we can come out of the gate would be sub 5 percent, so we feel we're pretty aggressive. Looking at some recent deals that have happened with Citi and Chase and Prudential, we can be very competitive. So that's a big bonus with our existing portfolio and also to be competitive outside of the portfolio.

ACTING CHAIRPERSON GUNNING: Yeah, why don't we take a pause for the cause, as it were, and take a ten-minute break there.

(Recess taken.)

ACTING CHAIRPERSON GUNNING: Why don't we get back together here and get to the fun part.

I can't start without JoJo sitting next to me.

Okay, Tim, go ahead.

MR. HSU: *Apparently I had a Lifesaver I* forgot to use. Do you see that?

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Item 8. Discussion, recommendation and possible action regarding the adoption of a resolution authorizing the Agency's single family bond indentures, the issuance of single family bonds, short term credit facilities for homeownership purposes, and related financial agreements and contracts for services. (Resolution 13-02)

MR. HSU: I'm hoping this will be the easy part of the -- of our discussion today. What we're asking the Board to do is to vote on a set of resolutions which give the staff the ability to do three high-level things: One is to manage our balance sheet so -- we have a lot of legacy debt -- and to manage that balance sheet liability and to leverage where we can; to also issue new bonds, financing new lending activities. And to tie to some of the lending program questions, in large part these lending -- these new bonds to be issued for new lending is more focused on our multi-family side. On the single-family side it is not a bond execution at this point. And the third thing is that it gives us the authority to manage many of the financial contracts that we have with a lot of financial institutions, the counterparties out there.

Those are sort of high-level summaries of these resolutions. What I've highlighted here in the slides are the key changes, the key deltas, to last year's resolution. So the one high-level thing we're doing is that the staff is doing strategic planning in the January and February time frame, and some of those discussions sometimes have -- they have an impact on the substance of these resolutions, so we felt that going forward it might just be better for us to -- to -- to delay our customary January schedule for the financing resolutions to March.

So the first large change that we're making -- and we're making this change both on the single side and the multi side -- is to suggest that the financing resolutions would be in effect until 60 days after the first Board meeting after March 1st of next year in which we have a quorum. So we would be -- said another way, we would be passing financing resolutions in that second Board meeting of the year instead of the first Board meeting of every year.

And the other change that we made on the single-family side is last year we inserted this idea that if we were to do a refunding on the single-family side -- and for this it's probably just easiest if I return to page 15. Gosh, I wish there was an easier way to do this.

MR. SERTICH: It's a good review.

MR. HSU: Okay. So what we're suggesting here is that there's a need to give leverage to the balance sheet here. So what we did last year was that we did a $456 million refunding of the variable-rate bonds in here. But because these assets, the pass-through bonds, are -- as we talked about, have a lot of issues with them, to say the least, this box here actually had to contribute some money to make the refunding happen. So as it turns out on that transaction, the contributions that we made were about 10 points, meaning 10 percent of the refunded amount.

So what we're suggesting here is to extend

Claudia's authority to be able to use some of the money from here to facilitate a refunding of the leveraging of the bonds in the orange box if we see there's an opportunity to do that. And I think that she does have to certify that that contribution will not hurt the blue box, and she has an amount of $50 million as a limit.

What we added this year is this idea that in addition to this collar of the $50 million max for the year is the idea that it would also not exceed more than 10 percent of the bonds to be refunded. That's the -- that's the thing that we added for this year.

And you might say, well, why do we add that? Arguably the higher that percentage is, you might start questioning the value of doing that refunding because we're getting the leverage ratio of the contribution versus the amount of the leveraging we're doing. We want that ratio to be very high in terms of a dollar put up refunding more bonds than a dollar put up refunding less bonds.

Some of the other changes we had made were that for new money issuance -- and as I mentioned, at the moment what's being contemplated by the program folks is not a bond execution. But having said that, things could change from now until March or April of next year, and what we're asking the Board is to reintroduce this idea that we could create indentures that -- in very similar forms than the ones that the Board has previously approved.

And reason why that could be a very useful flexibility is that the bond financings of the transactions that are done in this space are undergoing certain, I would say, innovations or changes. And the ability to be able to create an indenture that are stand-alone, they are sort of apart from everything else, to do a bond financing, that will be sort of valuable going forward.

But having said that, having sort of reintroduced this flexibility to create indentures that are similar in form to what we have now, we will restrict ourselves to not issuing variable-rate bonds. So they must be all fixed-rate bonds, and we won't use any swaps or derivatives in these transactions.

And then the last but not least is that we wouldn't be issuing whole loans, so everything would be securitized in the MBA space like what Tony and Rick were talking about earlier.

That concludes my remarks for this resolution.

MR. BELL: I have one question. The resolution creates wide latitude to go up to the $50 million. Do you have a guestimate now as to what the amount will likely be?

MR. HSU: Honestly, I think it will be zero for the year. I think that the refunding opportunity that we had last year was very unique because we did that refunding as part of the NIBP authority that we had. So in short, the NIBP -- Treasury allows a certain amount of the NIBP amount to be refunding bonds. So we basically maximized our refunding potential out of these bonds that Treasury was willing to buy from us.

I would like to say that some of that amount could be used this year in order to do some refundings, but I think the fact of the matter is that we really do need that orange box to continue to stabilize more so that the performance of loans get better. And I think that this year it might be zero, but next year I think that that might be a much -- much -- a higher possibility, once we see that there's a longer period of stabilization out of the loan performance.

ACTING CHAIRPERSON GUNNING: Are there any additional questions from the Board members?

Here's the opportunity for anyone from the public to comment. Are there any public comments?

All right. I know the first time I did this, it seemed, okay, just here it is, go for it, but I know that staff -- you know, we've been briefed very well, and I think these resolutions help them operate. We have a lot of trust in them. They're very competent.

So is there a motion to accept the resolution for the single-family financing?

MR. HUNTER: I'll move adoption of Resolution 13-02.

ACTING CHAIRPERSON GUNNING: Is there a second?

MR. BELL: Second.

ACTING CHAIRPERSON GUNNING: Moved and seconded.

JoJo.

MS. OJIMA: Thank you.

Ms. Falk.

MS. FALK: Aye.

MS. OJIMA: Mr. Hunter.

MR. HUNTER: Aye.

MS. OJIMA: Mr. Jacobs.

MR. JACOBS: Aye.

MS. OJIMA: Mr. Bell.

MR. BELL: Aye.

MS. OJIMA: Ms. Carroll.

MS. CARROLL: Aye.

MS. OJIMA: Mr. Shine.

MR. SHINE: Aye.

MS. OJIMA: Mr. Smith.

MR. SMITH: Aye.

MS. OJIMA: Ms. Whittall-Scherfee.

MS. WHITTALL-SCHERFEE: Aye.

MS. OJIMA: Mr. Gunning.

ACTING CHAIRPERSON GUNNING: Aye.

MS. OJIMA: Resolution 13-02 has been approved.

MR. HSU: Thank you.

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Item 9. Discussion, recommendation and possible action regarding the adoption of a resolution authorizing the Agency's multifamily bond indentures, the issuance of multifamily bonds, short term credit facilities for multifamily purposes, and

related financial agreements and contracts for services. (Resolution 13-03)

MR. HSU: On Resolution 13-03, this is a mirror image of the resolution on the single-family side except this is on the financing of the multi-family lending activities. We are making a similar change here in terms of delaying the regular presentation of these resolutions to the Board instead of January to March.

And we are also doing something similar here as we -- what you saw on the single-family side that to the degree that we do non-conduit issues, so these are actually bonds that we're issuing under our own credit to the degree that we do financings of some of the projects that Jim was talking about earlier, we will not issue variable-rate bonds. We will issue only fixed-rate bonds. We will not use any swaps or derivatives.

And furthermore, we would at least get FHA risk share insurance on these loans or something comparable to that level of security on the loan side of the equation.

Wayne, do you -- I sense a question.

MR. BELL: This -- this is in a sense a

successor to the 2012 resolution that we just continued out at the last Board meeting; am I right?

MR. HSU: That's correct. So I think that what -- at the last Board meeting what the Board did was that the Board extended the authority we had from 2012. And this one here is meant to replace the authority that we received from the Board from the 2012 and the extension from last Board meeting.

MR. BELL: Right. And -- and because it goes out to March 2014, it would obviate the need to have an extension at a January meeting the following year.

MR. HSU: That's correct. So what we're intending now is that coming to the Board every March to present the financing resolutions instead of January.

MR. BELL: Okay.

ACTING CHAIRPERSON GUNNING: And, Tim, the practice, though, is an annual resolution --

MR. HSU: This is an annual resolution.

ACTING CHAIRPERSON GUNNING: -- not an extension.

MR. HSU: Yes, this is an annual authority that staff requests from the Board.

So I think that in general one of the things that has come up in the midst of the financial crisis was some concerns, for example, about some of the loan products that we launched in the past. And this come up too with the BSA. It's important to realize that these financing resolutions are only dealing with the bond side of this whole enterprise we've been talking about. This only deals with the issuance of bonds or the borrowing to financing -- to financing the lending activities. The idea of what we do on the lending side is not really part of what you -- we're asking you to vote on here.

So -- so Jim's presentation of risk share, I think he mentioned to you that we have received a separate and prior authorization from the Board to approve risk share and lending of risk share. And what we might do in terms of lending on the single-family side, that in itself might deserve another authority from the Board.

This is not in any way authorizing what we might do in the TBA space or any single-family products that we might launch. This is really only having to do with how we borrow money and managing our contracts.

MR. JAMES: May I make one comment, please?

ACTING CHAIRPERSON GUNNING: Of course.

MR. JAMES: The -- the point that Tim makes, sort of reiterated the point, is that the Board has instructed us in 2011 that we had to come to the Board to get authorization for new loan products, and that's what he's referring to.

Of course our risk share program is a long-existing or long-standing program going back to the -- '94, so we have numerous of those projects in our portfolio. It's not a new loan product. So I'm not of the mind that we have to or -- that -- that at least at this point that the direction of the Board is that we have to come back for authorization to issue loans on our multi-family side under the risk share program that Jim was referring to. I think he mentioned some five or seven or nine or so that -- maybe I'm going too high. It's five?

MR. MORGAN: Six.

MR. JAMES: Six. I'm optimistic.

So that's just -- just to be clear on that point with regard to what you are resolving. Tim's of course correct as well with the authorization, is to authorize issuance of bonds to finance the loans that we hope to make on the multi-family side.

ACTING CHAIRPERSON GUNNING: Thank you, Victor.

Any questions from the Board?

Once again --

MS. CARROLL: I'm sorry. If we've already authorized risk share -- I think done a very long time ago -- how does that fit in with the limits that you're proposing that are going to be getting voted on in May as to how much risk we will take in the multi-family space? Like are we going -- do we approve each project?

MR. HSU: The approval of the projects would be subject to some of the previous resolutions that we have passed. So I think that we are required to bring back to the Board for projects that are greater than $4 million.

MS. CARROLL: Okay.

MR. HSU: But in terms of capital allocation again, in general we don't think that -- and we have never been told by the rating agencies -- that we're capital constrained. That --

MS. CARROLL: Okay.

MR. HSU: -- it's really about liquidity constrained. So I think at the last Board meeting we talked about looking back at the deal that we did in December. So as it turns out, that deal had about a seven-point capital set-aside and a three-point funding need. So the three-point funding needed cash. That -- that seven point doesn't really worry us. It's really the three points or having to fund the three points of cash and make the deal work.

And arguably if we decide to do a bond execution to fund the loans that Jim is talking about on risk share, we would have to suggest that some of that $27 million warehousing, we would have to take some of that to make the bond deal work.

MS. CARROLL: Okay. Thank you.

ACTING CHAIRPERSON GUNNING: This is, again, time for public comment. Anyone from the public?

Seeing none, is there a motion to authorize the multi-family financing resolution?

MR. SHINE: I'll move it.

ACTING CHAIRPERSON GUNNING: Mr. Shine has moved. Is there a second?

MR. SMITH: I'll second.

ACTING CHAIRPERSON GUNNING: Mr. Smith, second.

Roll call.

MS. OJIMA: Thank you.

Ms. Falk.

MS. FALK: Aye.

MS. OJIMA: Mr. Hunter.

MR. HUNTER: Aye.

MS. OJIMA: Mr. Jacobs.

MR. JACOBS: Aye.

MS. OJIMA: Mr. Bell.

MR. BELL: Aye.

MS. OJIMA: Ms. Carroll.

MS. CARROLL: Aye.

MS. OJIMA: Mr. Shine.

MR. SHINE: Aye.

MS. OJIMA: Mr. Smith.

MR. SMITH: Aye.

MS. OJIMA: Ms. Whittall-Scherfee.

MS. WHITTALL-SCHERFEE: Aye.

MS. OJIMA: Mr. Gunning.

ACTING CHAIRPERSON GUNNING: Aye.

MS. OJIMA: Resolution 13-03 has been approved.

MR. HSU: I'm now doing better than the minutes. I got two out of two.

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Item 10. Discussion, recommendation and possible action regarding the adoption of a resolution authorizing applications to the California Debt Limit Allocation Committee for private activity bond allocations for the Agency's homeownership and multifamily programs. (Resolution 13-04)

MR. HSU: On the CDLAC application, Resolution 12-04 --

ACTING CHAIRPERSON GUNNING: 13.

MS. WHITTALL-SCHERFEE: 13-04.

MR. HSU: 13-04, I'm sorry.

MS. CAPPIO: I think we have to bring it back, sorry.

ACTING CHAIRPERSON GUNNING: Next meeting. You don't get it this time.

MR. HSU: We could do that, if that's the pleasure of the Board. But I'd like to correct that, what's on the board there.

What we're asking the Board here is to vote on authority to give the staff, Agency staff, to apply for a certain dollar amount of volume cap, of private activity volume cap, from CDLAC. So on the single-family side, we're requesting the authority to apply for up to $200 million from CDLAC. On the multi-family side we're requesting for authority up to $400 million from CDLAC.

These numbers, especially on the single family side, given that we have been talking about not doing a bond financing -- bond financing to finance some of those MBS activities for now, these numbers are probably going to be on the high side.

That concludes my remarks.

ACTING CHAIRPERSON GUNNING: Any questions from the Board?

Once again, this is time for public comment. Anyone from the public?

Seeing none, is there a motion to authorize Resolution 13-04?

MS. FALK: So moved.

ACTING CHAIRPERSON GUNNING: Moved by Janet. A second?

MR. BELL: I'll second it.

ACTING CHAIRPERSON GUNNING: Mr. Bell. Moved and seconded.

Roll call.

MS. OJIMA: Thank you.

Ms. Falk.

MS. FALK: Aye.

MS. OJIMA: Mr. Hunter.

MR. HUNTER: Aye.

MS. OJIMA: Mr. Jacobs.

MR. JACOBS: Aye.

MS. OJIMA: Mr. Bell.

MR. BELL: Aye.

MS. OJIMA: Ms. Carroll.

MS. CARROLL: Aye.

MS. OJIMA: Mr. Shine.

MR. SHINE: Aye.

MS. OJIMA: Mr. Smith.

MR. SMITH: Aye.

MS. OJIMA: Ms. Whittall-Scherfee.

MS. WHITTALL-SCHERFEE: Aye.

MS. OJIMA: Mr. Gunning.

ACTING CHAIRPERSON GUNNING: Aye.

MS. OJIMA: Resolution 13-04 has been approved.

ACTING CHAIRPERSON GUNNING: Excellent.

Tim, I have some additional slides here, but I think the agenda item is informational workshop. Are we going to do this or?

MR. HSU: It's true. This is -- this is

something that we could do after you, if you -- if you want.

MR. JAMES: Go ahead.

MR. HSU: Okay. We'll try to make it fast.

Tony's going to give you an update on our investment policy that we adopted last year.

MR. SERTICH: I'll be very quick.

So last year the Board adopted a new Agency investment policy, and the policy set up an Investment Oversight Committee made up of six CalHFA staff members, including the executive director, the director of financing, the financing risk manager, the general counsel, the comptroller. And the committee's task is to review any -- any -- review the policy annually and periodically and approve any new investment counterparties or investment vehicles.

There was a new investment vehicle that was added to the investment policy. It was a U.S. Bank commercial paper vehicle to replace U.S. Bank open repurchase agreement, which is no longer going to be an available investment next week. So the -- a copy of that approval has been included in the Board handouts.

It's -- there's no new counterparty risk there. They're still both backed by U.S. Bank, so there's no new credit risk the Agency is taking.

Also in the -- in the past few months, the Agency terminated a GIC that was with a counterparty that had been downgraded. The agency redeemed all of the bonds that were tied to that GIC, so there was no issue with terminating the GIC. It automatically terminates if the bonds are gone. That's a guaranteed investment contract.

So that's the investment update.

MR. HSU: And the very last thing, Tia asked last Board meeting about the cure rate of loans we modified. And I think I went on record saying about -- we have a cure rate of about 60 percent. I was a little bit off. Our overall cure rate is about 64 percent.

But this is actually a really interesting chart. We -- I had a really hard time trying to make this pretty, but it's actually very interesting. What you see here is that overall we have a cure rate of 64 percent, but we broke it out between loans that we modified with assistance from KYHC and loans that have been modified without KYHC.

So what you can see is that generally speaking the loans that we modified with KYHC, we have a much higher cure rate with those because you're starting to deal with principal reduction, you're starting to deal with -- you're sort of -- you're starting to address people's willingness to pay, rather than just capacity to pay, is one sure way of thinking about it. So you can see that the cure rate with the assistance of KYHC is 84 percent, and the cure rate without KYHC is much lower at 58 percent.

But these points here are also very interesting. So what we're plotting is the cure rate for loans that were modified within a certain range. So what you can see is that loans that are modified the first half of 2011, the cure rate for loans that are modified with KYHC and the cure rate for loans that are modified without KYHC. So you can see that KYHC takes about -- is doing much better with that.

That is true for three quarters. You can see that here. You can see that here. You can see that here. But then you can see it starts narrowing, and it kind of flips over. And we have to do more work on this but we think that part of the reason for that is probably some sort of selection bias that's happening, meaning that the loans that are most needy or the loans that are most -- or the borrower that is most distressed, they're actually being channeled over to KYHC, and what we're modifying, the population that we're modifying, is actually slightly better off than the population that we're sending over to KYHC, meaning that there is a change in the underlying demographics of the population that are going in either direction.

MS. WHITTALL-SCHERFEE: Tim, when you talk about cure rate, you just -- are you just saying they now are making their payments under this new modified plan? Is that how we define cure?

MR. SERTICH: And they haven't re-defaulted.

MS. WHITTALL-SCHERFEE: Okay.

MR. HSU: I think that the categories are they're current or that they're actually paid off. So if they're any -- so if they're delinquent at all, even 30 days, for this exercise we're not counting them.

And that's all we have. Thank you, Board.

ACTING CHAIRPERSON GUNNING: Thank you very much, Tim and Tony.

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Item 11. Informational workshop discussing Board

governance.

MR. JAMES: We've now evolved to afternoon. Good afternoon, Board, Members of the Board.

Is this the button? Okay.

I wanted to take a few minutes with the Board this afternoon to present on a high level general matters having to do generally with Board governance and specifically -- by -- this is in a handout that you received this morning as opposed to it being in the binder.

The four points that I'd like to go over with you are going to be the CalHFA structure generally, statutory role of the Board to administer the Agency, open meeting law requirements and your fiduciary duties to the Agency as members of the Board.

Page 2 of the handout, the structure of the CalHFA Agency. The Agency is administered by the Board, as you all know. There are eight appointed members, six are ex officio, for a total of 11 voting members. Six of those voting members are needed for a quorum.

We also have two advisory committees on -- two standing advisory committees for the Board, one being the Audit Committee, which you heard from earlier this morning from Mr. Smith, and the Compensation Committee, which is scheduled to -- will immediately follow this meeting.

The executive director is responsible for the day-to-day operations of the Agency. We have four lines of business, generally speaking, again on a high level: Single-family lending; multi-family lending, including special-needs-type lending; contract-administered programs that Tim mentioned to you earlier in support of some of our revenue -- those are the kinds of programs like MHSA, CHDAP, Props 46 and 1C -- and our mortgage insurance program, which is currently in pause, though it is -- it is paying claims.

CalHFA is financial and operationally independent of the State with the exception of our personnel administration. And for employees of the Agency, we are part of the state civil service system, either as civil service employees or exempt from -- exempt employees within state service and thus subject to the civil service rules. But beyond that personnel administration or personnel management oversight, we are generally independent of the operations of the State of California.

We have our own general obligation credit rating, which is independent of the State. Our funds are continuously appropriated and not subject to annual appropriation of the Legislature. And while Cal MAC, which was formed as a nonprofit, is a separate entity from CalHFA, it adheres to the values of transparency like those of CalHFA.

The Board is responsible for the overall supervision and control of the Agency's operations. It sets policy. You approve all bond indentures, sales of debt obligations. You authorize issuance of securities. You authorize major contractual obligations. And by regulation the Board has deemed major contractual obligations to be those which exceed $1 million in a fiscal year. If it is $1 million or below in any fiscal year, you've delegated that to the executive director by way of regulation.

Final commitments -- and Ms. Carroll was referring or asking the question of Tim and Tim mentioned that matters having to do with our multi-family program that are in excess of $4 million come to the Board for approval. And by resolution the Board has delegated the authority to approve loans which are $4 million or less to the executive director.

The Board also approves the Agency's operating budget, which you will receive in our next -- our upcoming meeting in May. You also set salaries of key exempt managers. And those key exempt managers are listed there for your convenience. You supervise the executive director, who, as I mentioned before, administers and directs the day-to-day operations of the state agency -- of CalHFA.

As you know, meetings of the Board must be in open session and properly noticed, absent it being an executive session, which still must be noticed but will allow the Board to retire to executive session for matters which it otherwise should -- for policy reasons could not be heard by the public, but there are specific statutory provisions for that. As a practical matter, our executive sessions typically happen during -- for matters involving personnel, typically the evaluation of the executive director, and matters having to do with litigation. Beyond that, all meetings are -- are held in open session and must be properly noticed.

The hallmark of the open meeting law is governance in the public and with the fundamental idea of allowing the public to fully participate and hear the deliberations and the rationale for what it is the Board is doing. A meeting is any congregation of a majority of Board members to discuss matters having to do with items that are within the jurisdiction of CalHFA. Meetings must be held in open session in public.

As I just said, a meeting is -- is -- is any congregation of a majority of the Board members -- that's six or more -- who choose to discuss items that have to do with the jurisdiction of CalHFA. Those discussions, those conversations, with Board -- amongst and between Board members are not limited to matters having to do with reaching consensus. The Court views that very broadly to say that it almost encompasses matters having to do with exploratory fact-finding, questions, answers that you might have of each other. If there are -- if it constitutes a majority, then those meetings must be held in open session and properly noticed.

So it begs the question if there are five or less members having those conversations, is that a violation of the open meetings law, and the answer to that is no, but I implore extreme caution with five or more members having conversations outside of the Board for two reasons: One is this notion of serial meetings, which is a huge issue and very easy -- it's a big pitfall for all governmental agencies or public entities subject to the open meeting laws because anytime that breach, whether it's in a collective meeting in person or if in serial, that is one meeting after another, the collective results in six or more individuals having discussed matters involving the Board, that constitutes a meeting, and so it would be a violation of law.

The same with the use of intermediaries. There the classic example is a case out of Stockton, the lawyer who -- the city attorney contacted the members of the board, polled them to see if they were supporting a real estate transaction. It was deemed to be unlawful because he was canvassing and trying to get a consensus, and it amounted to deliberation of matters having to do with, of course, an issue pending before the board that should have been properly vetted and discussed and decided in open session. Even the -- the preliminary polling of the information was an inappropriate meeting of the members.

Advisory committees under the law, because we have three or more members, it's also subject to the open meetings laws. Our advisory (sic) committee is that, as is our Compensation Committee, so those, both of those committees, need to be properly noticed and agendized and open to the public. If the -- if there were ever a committee delegated authority to act on behalf of the Board, typically known as an executive committee, that committee, no matter how small, as long it consists of two or more individuals, would be subject to the open meeting laws.

The penalties for violating the open meeting laws are it typically voids the action and can result in attorney's fees and costs if that individual has to petition the court to ask the board to set it aside. If there is -- if members are -- there's a potential misdemeanor violation for members who attend a meeting with the intent to deprive the public of information. That's an intentional act, of course, but nonetheless it's a misdemeanor.

The other practical side, of course, that -- that is -- is something that the Board also is concerned with is while it might be okay to have conversation outside of these proceedings, the public perception is one that all of us need to be mindful of to ensure that, you know, all matters having to do with Board affairs are fully vetted in public and so the public understands, then, that they have the opportunity to participate in the matter before decisions are made.

Your duty, your fiduciary duty, is to be informed, to be prudent, to exercise independent judgment, and act in good faith while carrying out the duties of the Agency.

As you know, the Agency's bond issuances must comply with SEC disclosure requirements. And in January of last year, our bond counsel explained that the Agency's robust disclosure process, which is done internally by staff, that results in the issuance of the official statements, complies with those disclosure requirements and does not impose any obligation upon the Board to -- any disclosure obligation. It doesn't impose any disclosure obligation onto the Board, absent, of course, the Board -- a Board member knowing about -- actually knowing about something that needs to be disclosed associated with the bond issuance. And if that's the case, then, of course, you should contact staff.

This -- you may not participate in a decision that may affect your financial interests. If there is a matter before the Board that does affect your financial interest, you must disclose that interest on the record and not participate or otherwise influence the outcome.

This is an acknowledgment, as I set forth in romanette iii, an acknowledgment of the Legislature that it is encouraging the diverse interests of members of this Board, and members of this Board could very likely have financial interest in holdings in matters that would come before it. But the trade-off is, of course, the benefit of the specialized expertise that each of the members have to offer, so it's permitted but you must disclose and recuse yourself.

This prohibition under section D recognizes that you may be passionate about a project and you may advocate for it, but you may not be compensated for it. Okay?

And finally, the Government Claims Act is an acknowledgment that your responsibility and stewardship in providing guidance and oversight to the -- to the Agency entitles you to a defense of indemnification and defense costs in civil proceedings.

Any questions?

Okay. Thank you.

ACTING CHAIRPERSON GUNNING: Thank you, Victor.

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Item 12. Reports.

ACTING CHAIRPERSON GUNNING: Item No. 12 is reports that are included in your packet. Have you had a chance to look at those, or any questions from the Board on the regular reports?

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Item 13. Discussion of other Board matters.

ACTING CHAIRPERSON GUNNING: Seeing none, are there any other matters to come before the Board?

You guys are --

MS. CAPPIO: Full of charts.

ACTING CHAIRPERSON GUNNING: -- full of charts, I know.

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Item 14. Public testimony.

ACTING CHAIRPERSON GUNNING: This is the moment -- I know we had public comment earlier, but we do want to offer the public an opportunity to make any comments before the body before we adjourn. Anyone want to make public comments?

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Item 12.D. Update on Keep Your Home California Program.

MR. HSU: Do you want to talk about KYHC?

ACTING CHAIRPERSON GUNNING: Absolutely. I think it's included, the Keep Your Home Program. There's a -- it was one of the attachments underneath --

MS. CAPPIO: Yeah, it's one of the reports.

MR. HSU: As you know, Di's not here today because she got trapped in D.C., so I'm the Padawan in training on KYHC. I think there's a lot of good stuff happening in KYHC, and I feel almost bad making this presentation instead of Di because I'm just a cheerleader. I'm that guy who's dancing in the end zone when someone else scores.

I think that it could be summarized in two words: Mario Lopez. We are going to get Mario to do a public announcement for the program. And he's going to do it in Spanish, and he's going to do it in English. So our outreach program, no different than when we started doing mailings with EDD, I think our outreach program is going to gain -- you know, we're going to be -- this is going to kick up a couple notches in terms of the outreach, in terms of the marketing, in terms of the visibility for the program.

And on the first slide here you can just -- I mean, I think that there's so much good stuff happening here. We're -- we've helped 23,000 homeowners. We signed up more than a hundred servicers now and more than half of them are doing the Principal Reduction Program. We're going to do a new mailing with EDD. Our UMA program really took off last year because of the legitimacy of someone who was getting an unemployment check and see that there's a mailing from KYHC, all that are sort of like great stuff that's just going to be happening over the next, you know, six months or so.

We put together this chart recently, Di and I, to also show you that while we've been telling you that this program has gained a lot of traction, well, this chart to me is worth a thousand words. Because if you look at this chart, you'll see that at the end of fourth quarter 2011, we put out $39 million. And you look at how much money we've put out by the end of last year, we've increased that dollar amount by more than fivefold.

And the reservations that we have, too, here are not insubstantial. We have a pipeline now that's twice as large as we had, what, a year -- you know, at the end of the year prior. And the traction that we're getting on some of these programs, such as the Principal Reduction Program and the Recasts program out of the Principal Reduction Program, it's so significant that I think -- I believe -- I hope I'm not putting words in Di's mouth. I think for the very first time we are actually showing a projection that we will be using all these program dollars before the program sunsets in 2017.

So this particular -- that's -- this particular projection here is showing that we'll use all those dollars by the end of 2016. We will update this probably on a quarterly basis for the Board so that we can all be focused on not only what we have done looking backwards, but what we expect going forward.

Because I think that, as the Board has heard before, there are -- there a lot of ideas out there for how people could help -- how people could be helped and how this money can be used. And they look very different when you know whether or not these program dollars would be used under the existing programs that are in place. The -- the -- the mind-set of the folks who are running the program is that these dollars will be used under the current programs that are in place.

There's a lot of good stuff after these slides, but I think between Mario and this slide, I think that this program is doing really well. And I think that that's all that needs to be said.

ACTING CHAIRPERSON GUNNING: Tim, just for my benefit because I know -- and when Di's here, we can commend her -- but 1.7 is the amount we were given by the federal government and to date we've spent how much, committed?

MR. HSU: So -- so by the end of last year we had spent --

ACTING CHAIRPERSON GUNNING: Right.

MR. HSU: -- we had actually disbursed $245 million. And we have -- we have disbursed $245 million, and we have $218 million of loans that are -- or program dollars that are reserved.

So one of the things that you'll notice is that -- in this chart here you'll notice that in white here we're showing the reservation dollars. And you can see that in the outer years as we do expect that the program dollars will be all spent, we need to start sort of dialing down the programs so that as the reservations sort of declines, that we're also -- you know, we're finishing the program and not going over the program dollar amounts.

ACTING CHAIRPERSON GUNNING: Right. Awesome. Thanks for stepping in, Tim, you Padawan. The Star Trek analogies --

MR. HSU: I don't just try, I do.

ACTING CHAIRPERSON GUNNING: I do. There you go.

All right. Any other business before this illustrious group?

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Item 15. Adjournment.

ACTING CHAIRPERSON GUNNING: Then I think we can adjourn.

(The meeting concluded at 12:31 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 27th day of March 2013.

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