Holiday Inn Capitol Plaza
300 J Street
Sacramento, California

Wednesday, February 6, 2008
10:42 a.m. to 2:55 p.m.

Minutes approved by the Board of Directors at its meeting held:
03/19/2008

Attest: 

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

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Minutes approved by the Board of Directors of the meeting held: 

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Attent:

ORIGINAL
STATE OF CALIFORNIA
CALIFORNIA HOUSING FINANCE AGENCY

BOARD OF DIRECTORS
BOARD TRAINING AND WORKSHOP

Holiday Inn Capitol Plaza
300 J Street
Sacramento, California

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Board Training and Workshop - February 6, 2008

**APPEARANCES**

**Directors Present:**

JOHN A. COURSON, Chairperson  
President  
Central Pacific Mortgage

PETER N. CAREY  
President/CEO  
Self-Help Enterprises

JEFF DAVI  
for Dale E. Bonner  
Secretary  
Business, Transportation and Housing Agency

CAROL GALANTE  
President  
BRIDGE Housing Corporation

LYNN L. JACOBS  
Director  
Housing and Community Development

CARLA I. JAVITS  
President  
REDF  
(formerly Roberts Enterprise Development Fund)

THERESA A. PARKER  
Executive Director  
California Housing Finance Agency

WILLIAM J. PAVAO  
for Bill Lockyer  
State Treasurer

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Board Training and Workshop - February 6, 2008

**CalHFA Staff Present:**

THOMAS C. HUGHES  
General Counsel

JOJO OJIMA  
Office of the General Counsel

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**Speakers from the Public:**

NICK FLUEHR  
CitiGroup

MIKE KOESSEL  
CitiGroup

WAGNER  
Kutak, Rock, LLP

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BE IT REMEMBERED that on Wednesday, February 6, 2008, commencing at the hour of 10:42 a.m., at the Holiday Inn Capitol Plaza, JQ Board Room, 16th Floor, 300 J Street, Sacramento, California, before me, YVONNE K. FENNER, CSR #10909, RPR, the following proceedings were held:

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Item 1. Roll Call

MR. COURSON: I'll call the meeting to order, and we will call the roll.

MS. OJIMA: Thank you.

Mr. Davi for Mr. Bonner.

(No response.)

MS. OJIMA: Mr. Carey.

MR. CAREY: Here.

MS. OJIMA: Ms. Galante.

MS. GALANTE: Here.

MS. OJIMA: Ms. Jacobs.

MS. JACOBS: Yes, here.

MR. COURSON: Ms. Javits.

(No response.)

MS. OJIMA: Mr. Pavao for Mr. Lockyer.

(No response.)

MS. OJIMA: Mr. Morris.

(No response.)

MS. OJIMA: Mr. Shine.

(No response.)
MS. OJIMA: Ms. Bryant.
(No response.)
MS. OJIMA: Mr. Genest.
(No response.)
MS. OJIMA: Ms. Parker.
MS. PARKER: Here.
MS. OJIMA: Mr. Courson.
MR. COURSON: Here.
MS. OJIMA: We do not have a quorum.
MR. COURSON: And we have no action items on the agenda, so that is going to work out very well.

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Item 2. Board Chairman/Executive Director Comments

MR. COURSON: I'd just make a couple of comments -- obviously we're going to have some other folks joining us through the day -- and take the opportunity that we've talked about. This is a chance for us to really do a couple of things. One this morning is to listen to John Wagner, who I've had the privilege of listening to twice, actually, talk a little bit about board governance. And John has a really good handle on what happens in other HFAs and policies and relationships and board dealings and so on. And I think we'll enjoy not only his presentation but with the group and the way we're set up certainly interactive to be
able to chat back and forth as he introduces us to some of his thoughts.

We'll do that. That will -- then after John finishes, we're going to take a break for lunch. And then as you know this afternoon, we're going to be joined by two individuals from CitiGroup, who I'll talk about at that time, why they're here.

In our book, John -- and I think we also sent out to everybody via e-mail, but I've also reproduced in our book the materials for John's presentation. John does a lot of work for HFAs all over the country. He's with Kutak, Rock.

And, John, we appreciate you traveling out here to California to join us.

MR. WAGNER: Okay, thank you. Do I need to move this up or anything?

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Item 3. Educational and development workshop regarding Board governance issues entitled "Boardsmanship Basics," presented by John Wagner, Kutak, Rock LLP Board

MR. WAGNER: It's a pleasure being here. For what it's worth, I've been a bond lawyer, like some of the gentlemen in the audience, for 35 years. I've worked with state agencies 32 of those 35 years, and it's been fun, because agencies do a lot of good in this
And interestingly enough, if you look back in your records, and I now realize that you keep verbatim minutes of all your meetings, if you go to some of your early meetings, you'll find that we probably show up because we actually were involved in some of your very early finances in the late 70s and early 80s. So at that time, you guys were a very baby agency, and now you're one of the biggest in the country, so it's kind of interesting to see how you've grown over the years and where you've come to.

What I'm going to do today is just talk about what I call boardsmanship basics, the basics of being a board member and the roles and responsibilities and how to deal with some of the pressures and the things that you have to deal with as a board member. I'm going to talk a little bit about the nature of the HFA because you have to understand what an HFA is before you can talk about governing it.

Then I'm going to talk about the role of the board and board interaction with other board members, with the executive director, the other staff and then with your professional team. I'm going to talk a little bit about just Board operations, that is, the roles of your officers, of the use of committees, meetings and
how they should be conducted, and then I'll close, if
you want to, talking a little bit about the legal duties
and liabilities of board members, because that always
seems to have some interest when I start talking to
board members. Fortunately Tom's here to correct me if
I say that you're going to be liable and you won't be
liable and that kind of stuff.

Right?

MR. HUGHES: Hopefully.

MR. WAGNER: One of the things that's happened
in governance in the last ten years is the influence of
the Sarbanes-Oxley law, which is a law that was passed
in 2002 by the federal government. It was in response
to the Enron and other fiascos.

But the thing that's important about it is that
for about a month, the feds held hearings, and they had
all kinds of professionals come in and talk about
governance and the way that organizations should be
governed and the role of the directors. Because in the
Enron fiasco and some of those others, everybody said
where was the board? What should the board have been
doing, and why didn't it do its job? So we had all
these experts. We had experts from Stanford come in and
Cal Berkeley and every other place in the country. So
there's a lot of things that were developed as a result
of that.

The Sarbanes-Oxley law which was passed actually
doesn't technically affect you guys, except in two minor
instances. But what happened is that the underlying
principles have gradually pervaded other kinds of
institutions than just SEC registered companies. In
fact, the courts -- the recent court cases have
basically said that the rules of governance that apply
to nonprofits and even governmental organizations have
changed. And that paradigm shift is because of the
Sarbanes-Oxley law.

The best example I can think of is a year ago,
an elected member of a school board in Colorado, the
school board had gotten into some -- had come under some
criticism because there had been embezzlements. And a
school board member said, "Gee, I didn't attend the
meetings and I didn't read all the stuff and therefore
I'm really not responsible."

And the Court said, "No, those rules don't apply
anymore. They may have applied 15 years ago, but the
principles of Sarbanes-Oxley we're going apply to you as
an elected member of a political subdivision."

So the rules that we see that were developed
there are expanding, and that's -- underlies some of the
stuff I'm going to be talking about.
One of the things that was made real clear in those hearings was that you need to understand the kind of organization that you're governing. And I'm going to talk a little bit about the nature of HFAs, and you all can -- Tom can correct me if I misstate some of the things that apply to you guys, because it's important for you to understand what you're governing because you're unique.

HFAs really generally have no counterpart in state governments. You are usually a combination of a political subdivision that you're supposed to be run kind of like a private company, and that's a very difficult thing to do because there's no great guidelines like you have in the private sector. You don't have shareholders that you're supposed to be catering to. The State creates you. The State tells you what your powers are. The State tells you what your purposes are. But within those purposes, you're supposed to refine and define your mission, and then you're supposed to carry out your mission within the parameters that were created by the Legislature.

Now, you guys are like most state agencies. The Legislature usually gives you little or no money to operate on. You started basically on a shoestring a long time ago, as did everybody else, so you're supposed
to be self-supporting. You're supposed to create and carry out programs where they're subsidizing people, but nobody is giving you any money, so one of the things you have to do is manage yourself very well when it comes to finances.

The two things that you are given by both the State and the feds are two tax breaks, and really what you're doing with all your operations is you're doing -- is you are leveraging the two tax breaks that you have as an organization.

The first tax break is that you can borrow money generally at a cheaper rate because the people who loan money to you, your bondholders, do not have to pay interest on the money that they loan to you. That's your tax-exempt bonds. Of course, the feds put limits on what that can do, but that gives you the ability to leverage your borrowings effectively.

The other tax break that you have, which a lot of people don't think about, is the fact that you don't have to pay any taxes on the money that you make, and you probably have exemption from state real property and state sales taxes, which help you a fair amount, too. But the big thing that you're leveraging, really, is the tax exemption and the ability to borrow on a tax-exempt basis. So you have -- as a board member
you have to keep in mind that those are the real only
two powers and authority that you have. And I would
tell you that even though you are today a
$5-billion-asset organization with a network of probably
about a billion dollars, that when you started out, you
had much more favorable tax laws than you do today. The
Feds substantially restricted what you can do in the
80s, and you've really made a lot of money off tax rules
that are not in place today.

What that means to you as a board member is that
if you would decide to basically spend out all your net
equity, you no longer have the ability to rebuild that
net equity the way that you did 25 years ago because the
tax rules are not as favorable for you as they were
then. So that's one of the kinds of things that you
have to keep in mind as a board member is that the rules
have changed a little bit in terms of what you can do
and how you operate.

As a board member, I would suggest to you that
you should make sure you understand the lines of
business in your organization, whether it's single
family or whether it's multifamily or other things, PMI
insurance, you should understand where your revenues
come from because you have to pay your staff, you have
to repay your bondholders, and you have to generate
enough money to carry out new programs as well as carry
out your existing programs. So as a board member, you
can't just rely on the staff to understand all that
stuff. You should have a basic understanding of where
your revenues come from and where your expenses go.

You have multiple overseers and multiple
stakeholders, and you need to keep all these people in
mind as you go about your role of governing the
organization. The overseers that you have are obviously
the Governor and the Legislature. They created you.
They can change your powers. They can basically shut
you down, other than paying off your obligations, if
they want to.

You have some other overseers that you may not
always think about. To the extent you carry out HUD
programs, HUD has oversight over how you carry out their
programs. The IRS is always overseeing what you're
doing because you're borrowing on a tax-exempt basis.
And if you haven't been told, and I'm sure you have, but
the IRS about eight or nine years ago started a random
audit program where they're auditing bond issues.

They focused on single-family issues beginning
about a year ago. You guys are one of the biggest
issuers of tax-exempt single-family bonds in the
country. It would be stunning if you were not sooner or
later selected for one or more audits. It's just out there. You need to understand that as a board member.

You also need to understand that the IRS, if they think you're good guys, will go easy on you. If they think you're trying to do something that's shady or inconsistent with what you're supposed to do, will come down hard on you.

MR. COURSON: And, John, what's the thrust of those audits? Is it that the securities we issue are in accordance with the code?

MR. WAGNER: Generally what they're doing, there are two kinds of audits. One is just a regular random audit. All they're doing there is making sure that you're kind of following the general rules in the single-family area. They want to make sure that you have proper form documents or the proper tax provisions and that kind of stuff.

If it's a targeted audit, that means that you have somehow fallen into a group where they think something is amiss and doesn't necessarily mean that you're the bad guy. For example, some years ago there was a particular underwriter that the IRS seemed to be targeting, and they, on a target basis, audited every bond issue that that underwriter underwrote for state housing agencies. They didn't find any improprieties.
within the state agency stuff, but sometimes you get caught up in that stuff.

Right now there's a lot audit stuff going on in the GIC area for any GICs that were written since the mid-1990s, and the next target area is the swaps. And you guys will sure as heck be caught up in the swap stuff because you're just so involved in that market. It doesn't mean you did anything wrong, but the IRS is concerned about that stuff.

Another party that oversees what you do on a regular basis is the SEC. You don't think about it that much. Fortunately it hasn't affected you that much, but the director or the chairman of the board of the SEC is not very happy with the municipal business. He was a legislator when Orange County had its problems. He knows about San Diego. It's his home area.

And then when he was chairman, Miami had its problems and Phoenix had its problems, and he basically thinks that many of the large municipal borrowers don't follow good practices and that they aren't telling the public about what's really going on with their finances. So he is not happy with municipal business generally.

He has proposed a selected basic recision of some of the exemptions that you enjoy. But the thing that's most interesting and so far fortunately hasn't
gotten any traction, he actually, back in May of last year, told the Senate that he thinks he should be given the authority to define the roles of directors of all municipal issues in the country.

In other words, he would get to define what your roles would be as a member of the board of CalHFA. And rest assured, he would define it probably a lot differently than you would define them and your state defines them right now, and it would be to impose a lot more responsibility than you probably have on you right now. So you need to be aware that that's out there.

Your trade group obviously is hopefully on top of this from a legislative standpoint and will make sure that it doesn't happen, but you just need to know that one of the guys who oversees what you do doesn't like the municipal business generally because he thinks that they're not doing a good job, and he's proposing to try to get himself more power.

MR. COURSON: Has there been -- there's not legislation yet to introduce to that extent?

MR. WAGNER: There's been -- I don't know if they actually introduced legislation. He had the SEC staff draft legislation, and it was discussed at a committee hearing, but I don't know if it's actually been proposed. Of course, even though it's been
proposed, it doesn't necessarily mean it's going to be enacted, by any means.

Another overseer that you have are the rating agencies because they're the guys who rate your bonds, and your bondholders are purchasing bonds largely still based upon those ratings. So the rating agencies have major oversight responsibility with respect to the finance stuff.

Of course, you got the capital markets generally looking at what's going on. And right now with the subprime meltdown and mess, there's a lot of scrutiny, particularly of state agencies, the question being whether you're really financing subprime loans and all that stuff. You'll hear about that this afternoon when the bankers will come in and they'll have lots of charts and lots of information, and then they'll ultimately tell you that they don't know for sure what's going to happen either. That's just a preview because I heard it last week.

Another overseer that you have are the press, and usually you won't see the press until they have something negative to write, so you need to always keep in mind that the press is out there. And anytime you discuss something, you make a decision, you need to take into account the spin that the press could put on it,
because they will spin it if it would sell another newspaper for them. It's just the nature of their business. You need to know that.

The stakeholders that you have, first of all, of course, the low and moderate income people that you're here to serve, may have a major stake. They may not always have a major voice, but that's the reason you're here. That's the mission of your organization.

Your bondholders obviously have a major stake, right now about a $5-billion stake, probably, or $4-billion stake in your operation and how you manage things, so they care a lot.

You also have a lot of financial counterparties, swap counterparties, standby bond purchase agreement people, in some cases your GICs or other guarantors. They care a lot about how you're running this place, so they have a major stake.

The other major stakeholder party are private industry partners that you have, the lenders, the people who are originating the loans, the people who are servicing the loans, the real estate agents who are able to sell a house and make a living because you guys are effectively providing financing, developers in the multifamily side and all the panoply of people that go with that.
So there's a lot of people who have a major stake in what you're doing and care that you do a good job of governing the organization.

If you have any questions as we go through this, please feel free --

MR. COURSON: You mentioned when HFAs, obviously with the legislation that created them in different states and so on -- is there -- is there any wide variance as to powers that you see of other housing finance agencies from one state to another because of provisions in the laws that created them or a change in those laws later or are they all pretty much the same?

MR. WAGNER: Most state agencies have largely the same powers. There's some diversions on the edges. There are some state agencies, for example, who don't have the technical authority to make grants. So they will make zero-rate-interest loans. Then they will forgive the loan in five or ten years, and they won't call that a grant, but it really is.

No. What happened actually in the evolution is the old state agencies, and it's not you, they had very specific powers. This tended to be in the Northeast, agencies in Illinois and Wisconsin. Theirs were so restrictive that over the years they've had to amend their legislation a lot of times.
You're one of the newer agencies, and your legislation tends to be broader and basically much easier to work with than the old state agencies. But they all largely end up with the same powers.

MS. PARKER: Tom is rolling his eyes.

MR. WAGNER: Well, you guys are a legislative happy state. Let's put it that way. So he probably has to deal with all that stuff.

MR. HUGHES: I'll resist comment.

MR. WAGNER: Since this is being recorded, I won't say any more.

Does that answer your question, John?

MR. COURSON: Yeah, it does. Thanks.

MR. WAGNER: Okay. Then I'm going to talk some about the role of the board both generally and more specifically.

Obviously the role of the board is to govern the organization. That means you make big policy decisions, but also means you have to make sure that you have proper processes or procedures in place as part of your governance. So it's really kind of a two-part thing. Clearly one of your jobs is to set policies.

Now, for what it's worth, bylaws, if you've adopted bylaws, that's not what we're talking about. We're talking about a policy. Policies generally
address things which the law does not already address. What it does is it provides guidance to people about how to act, of course, provides guidance to other board members, provides guidance to the rest of the world. It can clarify ambiguities.

One of the nice things it can do is it can create political and sometimes even legal foxholes for board members, and that's why I happen to like policies. If you have policies that address ambiguities as a board member and then something later on comes up, you can say, well, the board when it wasn't under pressure thought this through and adopted the policy and we're just following the policy. It's really nice when you're under criticism on the political side.

There are two kinds of policies. One more relates to programs. This has to do with the public purposes, the mission of your organization, which you've obviously defined in how you carry out these missions. It may also relate to other things like will you issue conduit bonds without a rate, which is one of the hot things a lot of agencies have to deal with. Those all fit in the program side.

Then there are operational policies which have to do with things like travel reimbursement, ethics. I assume you all have a state ethics law. You have laws
on everything. But a lot of times you find that ethics
laws that are written for general purposes don't always
fit real well with state agencies, so there may be
things that are ambiguous that you can address in a
policy which kind of fills out an ethics law that's
already in place.

The types of things we see often addressed are
can a board member buy into a bond issued by the agency.
That's one that always seems to come up. Some agencies
basically have a policy against it because they're
afraid of insider trading and things like that. Other
agencies have rules that favor it because they think
it's a real good signal to the capital markets that the
board's willing to buy bonds from the agency. But some
of those are the kinds of things that you ought to have
on the operational side.

Now, interestingly, the Sarbanes-Oxley law,
excuse me, addresses policies. And they think it's so
important at the federal level that if a corporation
does not have an ethics policy, they have to highlight
it in the prospectus when they sell securities. That's
how important the Feds think the adoption of policies
are at the board level. So it's a little thing to keep
in mind when you go about your own operations.

Two other operational policies that you should
have, and I bet you have in place, that the Feds put into law, one is that you cannot retaliate against any whistle-blowers that raise questions about federal law violations. And if you do, it's a crime. That means you go to jail and pay money. It's a bad thing.

The other thing is that you have to have a good record retention policy because if you destroy any records that would ever pertain to an investigation by a federal supervising agency, that's a federal crime. Well, you've got federal supervising agencies all over. Every one of your tax-exempt bond deals is supervised theoretically by the IRS. Every one of your HUD programs is supervised by HUD.

So you've got lots of supervision at the federal level, so you got to make sure you keep records. I'm sure that Tom's been through all this stuff and that you have a wonderful record retention policy.

Right, Tom?

MR. HUGHES: We have retained many records.

MR. WAGNER: This is being recorded.

MR. HUGHES: Managing them is another issue.

MS. PARKER: Tom, aren't there Public Records Act requirements?

MR. HUGHES: The public records law in California is really geared towards making all of our
documents publicly available. It doesn't discuss some of the hot issues that we have right now about records retention.

But I would draw a distinction between what I think John is talking about, which is our transactional records of our deals, everything to document what we've done over the years, versus our run-of-the-mill e-mails and correspondence and things like that, although maybe I'm incorrectly drawing that distinction. I don't know.

But certainly we have -- we saved probably way too much over the years and run into management issues with all that information.

MR. WAGNER: I didn't mean to put you on the spot, Tom.

MR. HUGHES: No, that is a hot issue. And one of the really good points, I think, that comes from what you just said, John, is that other state agencies and the State and other types of entities have come forth with lots of policies about records retention, but they don't necessarily have to deal with the issues that you just mentioned, which is the documentation of our transactions from a federal oversight point of view. So we have to balance what others may do or may want us to do with what we need to do inherent with those responsibilities.
MR. COURSON: And in terms of ethics, I guess, we rely on, do we -- for our ethics as opposed to a specific policy, we're really relying on some of the statutes?

MR. HUGHES: There are multiple things.

MR. COURSON: I know we talk about this all the time in terms of recusing and conflicts.

MR. HUGHES: Yeah, and each one of the Board members, as well as the staff members, is a public official, and there's a series of California laws, both the FPPC, Fair Political Practices Commission, and other general state laws that relate to ethics. Each California agency is required to adopt its own conflict of interest code, which we have, and we've amended -- this Board has amended from time to time. And those are the, basically, conflict of interest rules. You know, there's just a broader sense of ethics, maybe, that aren't covered in minute detail in the statutes that we also need to be aware of.

MR. CAREY: Is there a broad policy about record retention at this point, for instance, the more mundane things like e-mail?

MR. HUGHES: Well, the Agency is in the midst of a number of strategic projects, one of which is a document management system, and the -- that project, the
oversight committee of that project is delving into a number of issues related to that, one of which is document retention.

It is a major issue in litigation these days because of the discovery of electronic documents. And many of our sister state agencies have come up with record retention mostly directed at e-mails, things like that, that actually purge them after a very short time.

But it's critical that you have a litigation hold kind of process to prevent destruction so that if there's an investigation or litigation, that you're able to retrieve those. And that's particularly with an agency like ourselves that's 30 years old and has a lot of old records, it's a very big task to manage that document flow and especially the back file of documents.

MR. CAREY: In some cases it's almost desirable to create a policy that destroys things that no longer need to be kept.

MR. HUGHES: The other thing that we've found out, and we certainly found this out in connection with the audit committee review that this Board was involved in, is that it is unbelievably expensive to retrieve all of these documents. And if we do that on a regular basis, you know, it's a major expense item.
So I think that process of a document retention policy is ongoing, but we have to balance the inconvenience and expense on one hand with the need to be transparent and maintain the required documents on the other. And, again, we're actually still working on that.

MS. PARKER: I think we have a tendency to err on the side of keeping everything, and there have been a number of situations where either having those documents and/or, for example, our verbatim Board minutes have really served the Agency well in being able to demonstrate through documentation a variety of actions that have helped us in litigation and audits and a number of different situations.

MS. GALANTE: Can I just --

MR. WAGNER: Sure.

MS. GALANTE: I just want to ask a broader question about policies because I know we have a number of these policies that you're referring to, but I don't know that we have them all as, quote, Board policies in some --

MR. WAGNER: A nice little book, three-ring binder, that you give to a new Board member, are you talking about?

MS. GALANTE: Right. And I'm thinking -- I'm
trying to remember my little orientation binder, and I know there's certainly the ethics stuff in there. I can kind of visualize a number of things, but, you know, this conversation is making me wonder whether, you know, there ought to be a place where these policies exist. Because, you know, when you come in as a new Board member, you don't necessarily know what policies have been adopted two years ago. Just a thought.

MR. COURSON: I think that's a good -- gathering them, whistle-blower, I know we've done a whistle-blower policy. We've had some conversations about that. But putting them all in one spot. And I guess when you do that, too, you'd look at it and maybe some of the things we don't have policies on or at least not formal policies would be more --

MS. PARKER: Would jump out.

MR. COURSON: -- would jump out at us.

MR. WAGNER: The other thing that it would help you do, which we also would encourage you to do, or the Agency, is to periodically look at the policies. Because sometimes those policies are really old. Technically they're still there, and you may find that, in fact, you've been violating them on a routine basis because the nature of business has simply changed. It's just like your bylaws and other procedural type things.
You should periodically review those and make sure that, you know, if changes need to be made, they should be made.

MR. COURSON: Good suggestion.

MR. WAGNER: But for what it's worth on the record retention thing, a hot topic with the IRS right now is that under the IRS tax rules in the single-family arena you basically could never get rid of old information about mortgages that were financed because we continually are refunding bond issues. And the IRS is very much aware of the fact that there are agencies like you guys who probably have maybe hundreds of thousands of mortgage files, some of which may be 20 or 25 years old that you to have pay fees to warehouse because right now the IRS rules don't permit you to destroy them.

And our friends at the IRS tell us that you guys are probably more affected by their record retention rules than any other sector in the municipal business. It doesn't mean they're going to solve anything for you, but they recognize the issue.

Another thing that the Board obviously needs and does is you govern and monitor, but on the other hand you have to be careful not to micromanage. This is always a source of discussion. There's a lot of state
housing agency executive directors when I talk to their boards like this they will come to me and say, "Please tell my Board not to micromanage."

And invariably there will be a few Board members who will come and say, "You know, our executive director is just getting a little too far out, and we're trying to -- we've got to rein them in." There is some tension --

MS. PARKER: John, for the record, I didn't say anything.

MR. WAGNER: No, Terri said nothing.

But it's a natural tension. It's a tension that you see in any organization between the policy and governing Board and the CEO who on a day-to-day basis is managing. So don't get all uptight about it. It's natural. But you have to be aware of it.

So the question then becomes for a board, well, how do you govern, how do you monitor what's going on? And there are several things that I would suggest that you ought to be doing and looking at.

First of all, I assume you're getting regular internal reports from the staff about operations. I would be stunned if you weren't getting that. It should be covering things like the single-family program, what are your delinquencies, what are your defaults, really
basic things like that.

I assume you're also getting financials on a regular basis. Whether or not you have them prepared in accordance with GAP or on a real cash basis is kind of up to you. A lot of people feel like GAP accounting is so misleading that it's better to look at things on a true cash basis.

I assume you're getting periodic reports about the status of your lenders, whether they're in good shape, and your counterparties and your swaps and all that kind of stuff.

But you as a Board need to make sure that you've thought about the kind of reports that you want from the staff, and then you should tell the staff that you want these kinds of reports.

You should also be careful, and I'm sure your staff would never do it here, but in other state agencies I know a few executive directors who err the other way, and what they do is they dump lots of paper on the Board. There's one state agency whose executive director routinely every month will give his Board about two inches of paper and reports.

And I keep telling that Board, "You need to tell this guy to quit doing that, because if it's given to you, there's an expectation that you're going to look at..."
"So you should be getting what you want. When an executive director is dumping lots of paper on you, what they're really doing is they're ducking their own responsibilities to report and synthesize things to you, and instead they're trying to make you do their job for them.

So you ought to think about the reports that you want. Make sure that you're getting what you want and that you're not getting a whole bunch more than you're asking for.

So you should be getting internal reports.

Another thing you should be making sure you do, and I'm sure you do it, is when your auditors go through your financials, you know, they're going to produce your financials. You should understand your financials kind of because, again, including how good -- how much they really tell you.

But your auditors will give you a management report, and you should make sure you go through the management report carefully and you should talk to the auditors about the reports that they have prepared and the review they have done on your internal controls.

Auditors are really uptight these days about internal controls. It's the big deal that's going on in the corporate SEC area. In fact, the SEC issued a..."
release back in August on the difference between a material weakness and a significant deficiency, because one has to be reported in the prospectus and the other doesn't, and it's a huge deal. The accountants are really splitting hairs in this area. But it does mean that they're paying a lot of attention and putting a lot of time in on it.

You ought to piggyback on all that work they're doing for you guys and make sure that you're getting feedback from them about internal controls, because that's part of your responsibility as a board, to make sure that there are adequate internal controls. These guys are experts and you're paying them lots of dollars to do it. Talk to them about it. So they're people you should talk to.

The rating agencies, every time you do a bond issue, and usually on an annual basis, they issue reports. And they're -- you know, they're always somewhat flattering to management because they know that management are the guys who really select which rating agency you're going to go to.

On the other hand, they're not going to out and out lie. And they will generally -- if you read between the lines, you can kind of tell what they say are your strengths, because the things that they don't mention as
strengths often are weaknesses in your operation, and
they sometimes won't say that. But if you read between
the lines, you can figure that out.

So you ought to read the reports that you get
from the rating agencies because these guys are experts
on the creditworthiness of your obligations and how well
you're running the programs. And they will tell you a
lot. Again, it's somebody you're paying lots of money
to do this, take advantage of it. So you've got outside
experts that could help you a lot.

Also, I assume that at least once a year Tom
sits down and gives you some kind of a legal review of
how things are going with the organization. Maybe Tom
doesn't. A lot of agencies do that.

MR. HUGHES: It's on an as-needed basis, I
think.

MR. WAGNER: A lot of agencies have -- they will
have a little bit at the end of each Board meeting, but
they usually also have as part of their annual meeting a
good overview of all the legal things that are going on
with the agency, all the lawsuits that are in place and
where they stand and all that kind of stuff. So you
ought to make sure that you get those kinds of reports.

Tom's your expert and he should be able to tell you and
synthesize those things for you.
MR. HUGHES: This is one of those areas that
John and I actually talked about a little bit before the
meeting in which California law creates some unique
challenges in that area because other than in pending or
threatened litigation, I have no capacity to counsel the
Board in closed session. And it is sometimes very
difficult to advise a client on legal matters in a
verbatim transcribed public meeting. That creates many
challenges. But over the years, of course, we have held
a fair number of closed sessions to discuss pending
litigation.

And I've also pointed out to the Board that I do
have the capacity to provide a one-way legal advice memo
to the Board outside of a Board meeting, but I can't
discuss that with the majority of Board members except
in an open session in a public meeting if the litigation
exception to the Bagley-Keene Act doesn't apply.

So California law creates some unique challenges
to practices that might be more routine in other states.
So we try to select -- we try to keep the Board apprised
of major issues, but, you know, within that -- those
working constraints.

MS. PARKER: I'm wondering, you are required --
it's an internal document which we supply to colleagues
within the executive branch information on a monthly
basis of litigation. We have not typically included that report, and I'm wondering whether or not that would be something we should look at putting in the binder like Bruce's reports.

   MR. HUGHES: I don't think we can do that. Again, the document you're referring to, it's called the SMR, significant matter report, that's reporting from a state agency up the chain to the Governor's Legal Affairs secretary, clearly attorney-client privileged. And it is something that is not a public document.

   And again because of our laws, I don't have any capacity to make those documents private if I have to reveal them in a public meeting. So it creates some real conundrums. That's viewed as a strictly privileged matter with the administration, so very little I can do about that.

   MR. WAGNER: Back, you know, in terms of the micromanagement versus overall governing, the best analogy I can give is one of my clients just hired a new executive director, and he used to be the chairman of board of a different state housing agency, so he's now been on both sides of the fence. And he said that when you're a board member, what you want is the view from 40,000 feet. When you're the executive director, your view is supposed to be from the ground. So it's kind of
a neat way to think about how you should be viewing things. If you're a board member, it should be an overall strategic view, and if you're the executive director, it's on the ground.

Another obligation of the Board generally is to make sure that you're developing and maintaining the programs that carry out the purposes and the mission of the organization. That doesn't mean that Board members themselves should be creating programs. Normally the staff creates the programs. The staff is supposed to know what's going on on a day-to-day basis in the real world. They should come to you with ideas, but it's your job to make sure that you're generally carrying out the purposes that the Legislature has declared for the agency.

You should also make sure that you're involved in planning. Boards, Board planning, is an important thing. This generally means long-range planning, typically one to five year plans and that type of thing, although it seems to be more and more difficult to see five years out because things change so much. But that planning should be in terms of staffing, in terms of programs, things like technology, which is a huge area that seems to change so fast.

But you ought to plan for the future. You ought
to have measurable yardsticks as part of the planning. So often you see great plans but there's no way to tell whether or not you succeeded in the plans because all they are is kind of hopes and wishes. You should have measurable yardsticks because that helps the staff figure out how to implement the plans because it gives them something more objective to look at. You should be involved in planning. It should be strategic planning.

So those are kind of the principle roles that we see for the Board. I'd be happy to talk about any other roles that you think are out there.

If not, we'll move on to working together. Boards are productive when they work together and they work together as a team. No board member, individually, really has any legal authority. What you have as a board member is a platform from which you can convince other people or build a consensus on various issues. And if you get a majority to vote with you, then you have some power. But unless you do that, unless you develop a consensus, you really have no power as a board member.

So consensus building is a very big deal for boards. To build consensus, that means you normally need to be open and honest about where you're at and
what you're worried about. You should listen to other people and not talk all the time. Because if you don't know what other people's concerns are and sensitivities, you're not going to be able to build a consensus.

You need to be able to compromise, and that's an important part of building a consensus. You should not personalize things. If you personalize things, you're going to make enemies and nobody is going to want to be on your side. You need to be informed because part of building a consensus is being able to convince other people of the correctness of your position, and you can only do that if you're informed.

You should not be political. People don't like to hear that, but usually politics on a board is not a good thing because it means that people aren't keeping in mind the mission of the organization is to help low and moderate income people get into housing or get affordable housing. Politics generally is not written into your state law as a consideration for any actions that you take. So I would strongly suggest that politics not -- should not be an important part, should not even show up, hopefully, at the board level. It doesn't mean it doesn't, but it's not a good thing when it does.

A healthy board is a board that has a high level
of trust and candor amongst each other and you have
strong relationship dynamics. The best example I can
think of is about a year ago somebody was talking about
what's the difference between a good board and a bad
board, what's an analogy? And I said a good board is
like a symphony orchestra. You've got the basses,
you've got the strings, you've got the various wind
instruments, but together they produce a wonderful
product. The opposite is like the ultimate fight night
where everybody is in it for themselves and nothing good
comes out except one person maybe wins.

A good example of what you don't want a board to
be comes right out here in your own backyard 18 months
ago. Don't be a board like HP had a year and a half ago.
If you don't know about it, I'm sure if you read The
Wall Street Journal, it went on and on and on and they
had board members who didn't get along. They weren't
getting along with the chair. They weren't getting
along with the president. The chair of the board hired
a reporter to go out and try to find which board member
was leaking information to the largest shareholder
because the largest shareholder was trying to assert
control. That's exactly what you don't want.

I can tell you in the governance magazines as
well as in The Wall Street Journal people roundly
criticized all of those board members. Some of the board members just simply stepped back and would not participate. They didn't take any actions to stop what was going on. Others were the antagonists. Nobody came out looking good in that, which turned out to be a huge mess. So if you want an example of what not to do, don't be an HP board from 18 months ago.

If you're going to build a consensus, I would suggest to you that you should get to know the other board members and what their cares and concerns are, because that way when you build a consensus, you can cater to or take into consideration their concerns.

I would also suggest that the Executive Director should be considered a key part of your board team. Some boards like to meet or try to exclude the Executive Director. Well, the Executive Director is your CEO. She's the person who is carrying out things on a day-to-day basis. It is stupid to try to exclude the Executive Director. They should know more about the organization than any individual board member, so they are an important source of information as well as operational information.

Recently Jack Welch -- and I assume you all know who Jack Welch was, the old GE chair who is really into governance -- had an article -- he has one at the end of
the Business Week magazine each month. But he in October listed the five dysfunctional board member types that he saw in his many years in the corporate sector, and they're kind of interesting.

The first and the easiest to deal with is the do nothing board member, the board member who shows up and does nothing. They may think it's more of a ceremonial position. Jack's only complaint about that is that if you've got ten board members and one of them is nonfunctioning, you've lost 10 percent of the intellectual firepower that is supposed to be at the table, and so it's really a disservice to the others. But he said as a CEO at least they're not causing problems because they don't do anything.

He said the second dysfunctional type is the white flag person. That's the director who's willing to have an opinion until you have to make a tough decision, then they run away from the tough decisions. Part of your job as a board member is to make the difficult decisions.

The third and sometimes the biggest problem is what he calls the cabalist. This is the board member who doesn't speak up that much at board meetings, but then outside the boardroom will put together little cliques and try to influence things that way and will
complain about things that go on and will not bring these types of things up at the board meeting. He thinks that the cabalist is one of the most problem board members that you can have because they take time away from the board when the board should be focusing on productive things.

The fourth is what he calls the meddler, you would call the micromanager. That's the person who knows a lot about some very narrow technical areas so they get very involved in some minor technical thing that really belongs within the purview of the staff, and they waste everybody's time focusing on that.

And the fifth dysfunctional board member, which sometimes we see more with folks who are elected officials, is the pontificator. They like to use the board position as an opportunity to sit and preach to other people or to push some kind of a political message.

So I thought it was interesting that Jack talked about those five types of dysfunctional board members because they really do fit, unfortunately, sometimes into state agency board structures too.

MR. COURSON: When was that? What was the article? It was in Newsweek?

MR. WAGNER: It was in Business Week. It was --
MR. COURSON: Business Week.

MR. WAGNER: -- I think October 29th or something like that. It's the second to the last page, is where he always writes his article about business stuff. And it's always kind of fascinating because a lot of times it has to do with governance.

And remember, he was on both sides of both the board and the CEO side. He tends to err toward the CEO side.

So if there are no more questions about working with each other as a team, let's talk a little bit about the relationship that you have with your Executive Director, because that's a very important relationship.

The Executive Director is the CEO of your organization. Terri has all the day-to-day management responsibility. Her job is to make sure that your wishes and your policies and your directions are carried out by the staff. Another way to describe it is that the Executive Director recommends things usually, and the board approves things.

Trust is a very important part of this relationship. If you don't trust the Executive Director, you're going to waste a lot of time as a board basically micromanaging her job.
She's got lots of responsibilities I assume you're all aware of, but just to list a few, and this is -- just touches on them, she is -- her first job is to implement your policies. She represents you probably in negotiations and at public events. She usually maintains legislative liaisons. Probably has responsibility for hiring, supervising, educating, evaluating, disciplining and firing staff.

It's her job to make sure an annual budget is properly prepared. She probably has bond oversight, bond issuance responsibilities. She should make sure the finances of the agency are properly managed, that the programs are properly run. She should plan annual operations. She should stay abreast of industry developments and keep the board up-to-date on industry developments. She should be on the inside of all the stuff that's going on, and she should be telling you about it.

She should keep you up-to-date on appropriate management changes if she thinks that they're appropriate. And she also is actually responsible technically for monitoring compliance with all the laws that apply to you.

Of course what she does is she goes and hires staff to do all this kind of stuff, but ultimately it's
still primarily her bailiwick to make sure that all that stuff gets done. And you should be able to look toward her -- to her to make sure all that gets done. So it's a -- there's a lot of responsibilities that go with the job.

The board also needs to tell the Executive Director what kind of information and reports it wants to monitor things, as we talked about earlier. So make sure you communicate and tell her what you need to properly run this organization.

Now, the flip side of this is that you need to have an understanding with Terri about what her job is. I don't know if you have a job description. Many agencies have job descriptions.

The other thing you ought to do is take that job description and you ought to at least annually evaluate that job that Terri is doing. And the job description is helpful because the evaluation should be in response to the job description. If you want other things, you need to change the job description.

Do you know that like one third of the Executive Directors in this country never get evaluated because the board just doesn't want to bring up things that might cause a dysfunction between the two, and it's really unfair almost to the Executive Director because
if they don't have a job description, if they don't get evaluated, they don't know if they're doing a good job. You need some kind of institutional mechanism to give her feedback about the job she's doing.

And then you need to be honest about the evaluation. Don't do what they do in the military where everybody gets the highest grade because it makes the commander look like he's doing a better job. You need to be honest about the evaluation.

MR. COURSON: I want to follow up on your institutional evaluation issue. What do you -- in the two thirds that do do an evaluation, what are the different kinds of, I guess, processes or procedures that you see boards utilize to evaluate an executive director?

MR. WAGNER: Most of the time what happens is they will have every board member fill out some kind of evaluation, a written evaluation. And then they will have either the chairman or a committee, it's usually better if it's the chairman, sit down and read through them all, sometimes they'll actually circulate them amongst each other, synthesize the evaluation results and then sit down with the Executive Director and talk about the results, the synthesized results. Usually it's done on an anonymous basis like most evaluations.
Some agencies also talk to the senior staff people underneath the CEO. This is the famous 360 evaluation stuff so that you get feedback from the people who are subject to the Executive Director's direction. You just have to be careful when you do that kind of stuff, because you got to make sure that you don't have people who have an axe to grind, because that does happen too.

But as a general rule, you get an evaluation filled out by every board member. And then you have, you, the chair, or a small group synthesize and then give it to the executive director.

And then, of course, the question for Tom is do you have to keep all that kind of paper?

MR. HUGHES: And I think from the Agency, the only -- it's only been since SB357 that the Board has had that -- at least a portion of that role because prior -- again, we have an unusual situation in that the executive director of CalHFA has a term. The Board doesn't hire or fire or until SB257 had no control over working conditions, compensation or anything and now has direct authority to set salary, so the landscape has changed a little bit.

MR. WAGNER: Yeah. And there are some other
agencies who have a similar setup, but that shouldn't --
that doesn't mean that the board still should not
evaluate the Executive Director with feedback.

MR. COURSON: I'd be interested in knowing -- I
know we have two members of our audit committee here who
are going to be meeting, and we have a series through
outside counsel has made a number of issues regarding
compensation for the audit committee. We've assigned it
to the Audit Committee. It will come back to the Board
to consider how we want to handle performance reviews,
evaluations and compensation. And there's a number
of -- there's four or five sort of broad issues that are
issues for further consideration that they're going to
be taking a look at.

Other boards that you look at, do they -- do
they -- I guess, A, do have they compensation
committees? If they do, how do they function? Or, B, if
they don't, do they deal with these issues as a
committee of the whole, or what do you see in other
HFAs?

MR. WAGNER: There seems to be a growing trend
toward having a committee. Whether it's called HR or
compensation or whatever, it seems to handle a lot of
these kinds of things because it's certainly a growing
legal area.
Some agencies try to do it with a committee as a whole. And often committees of a whole don't work very well, because there are just too many people to get the type of intense focus and decision-making process that you can get with a three-person or four-person committee. But more and more agencies are going to that kind of review, and they're going to some kind of a committee to make those decisions.

But it's an area that's discussed a lot right now because a lot of agencies feel like we shouldn't have to have all that kind of stuff. It's when we've got 25 or 50 people or something like that. The problem is that the law simply -- this is not -- does not in that direction. I mean there's a huge growth area in HR and all the stuff that goes with it, and there's more and more federal laws on a regular basis, and you need to have somebody who becomes more and more specialized in that.

MS. PARKER: I'm wondering the diversity of HFAs is everything from it being very much a typical state agency --

MR. WAGNER: That's right.

MS. PARKER: -- like HCD, not how CalHFA is in California, to some of the HFAs in Florida and Connecticut that are completely outside --
MR. WAGNER: Separate authorities.

MS. PARKER: -- separate authorities.

MR. WAGNER: Yeah.

MS. PARKER: And some of them they're civil service, some of them not, kind of a mixture of everything. John, I wonder, given your experience, if you are aware of some states that might be closer to how we are structured that maybe we could get information for the Board of how they are, you know, doing compensation that might be more relevant for them to look at to see if there are some policies that they might want to adopt. I mean can you or do you know of --

MR. WAGNER: I'd have to think about that a little bit because I'm familiar with about 30 agencies and how they work, and there are some that are similar to you, you're right. I mean there's Maryland and Oregon, for example, are actually part of state government, so they're totally controlled by that. It's irrelevant. In fact, they don't even have boards except advisory boards.

MS. PARKER: Well, Maryland, though, the agency is a member of the cabinet --

MR. WAGNER: Yeah.

MS. PARKER: -- which is very different from
here.

MR. WAGNER: That's right.

MS. PARKER: You're right. It ranges all over.

MR. COURSON: It's really -- it has taken up a huge amount of our board time over the last year, and we just -- and it all came about, just as some background for John which might help him make some additional comments, is we just got -- gathered authority through legislation a year ago for the Board to set salaries of senior management and undertook that through a compensation committee and compensation studies and that whole thing. And it was quite a process. And it really, frankly, was difficult.

And I think we made it -- we made it through and then stepped back and said, whoa, wait a minute. Before we do this again, let's figure out what's -- what are the -- is there a better way, what are the ways to do it, how do we do this, what's the authority and so on, and that's where these items for further consideration came out of this outside counsel's report.

MR. WAGNER: So you're looking for guidelines kind of on how other -- what other states look at when they set the salaries or --

MS. PARKER: I think what we are looking for is what the policies are. Policies and procedures maybe
kind of thing.

MS. GALANTE: And I was going to say and procedures. The big question is is it a decision of the full -- is the full board going through all of the mechanics of how to do a compensation survey, what should be in the compensation survey, and then actually doing the analysis of what the salary should be versus, you know, delegating some or all of that.

And I think actually it could be a combination, too, a compensation committee that then recommends to the board. And I think one of the things, you know, that's got to be decided there is give a broad enough compensation committee or, you know, is there enough trust in that compensation committee that then when things come to the full board, you know, you don't necessarily want the full board then undoing everything a committee did. And if that's what's going to happen, then why have a committee?

MR. WAGNER: That's right.

MS. GALANTE: So I think, you know, just looking at policies that other entities follow around that would be helpful.

MR. WAGNER: Okay. I made a note of that, if you'd let me get back to you on that.

MR. COURSON: Even if you can think of people
that are similar to our situation --

MS. PARKER: Yeah, we can --

MR. COURSON: -- we can do the legwork on --

MS. PARKER: I can contact my colleagues in those particular states. I just -- you know, I think it was more from the standpoint of you're knowing --

MR. WAGNER: Offhand? See, and what I'd have to do is I'd have to mentally go through, okay, how does Alaska do it, how does Washington do it, how does Montana, Hawaii, Vermont --

MS. PARKER: No, not right here, but if you could think of it and share that with me --

MR. WAGNER: Sure.

MS. PARKER: -- I could make -- but I think that would help, perhaps, the Board from the standpoint of, you know, giving them some comfort of whatever we are doing as policies and procedures are things that have been tried in some of the agencies that have been --

MR. WAGNER: Okay.

MS. PARKER: -- around and doing it longer. And we went through the first -- like the baby step of trying to get stuff done, establish it, and then trying to now be in a mode where we'd like to help the Board improve it.

MR. WAGNER: Okay.
MR. COURSON: And it's particularly timely because we've -- this really has sort of been malingering and at the last Board meeting in January, we've instructed the Audit Committee to look at these areas of further consideration and come up with some or none, but action items for our March meeting so we can put this behind us and get on with the rest of it.

MR. WAGNER: Okay.

MR. COURSON: So the timing is particularly important.

MR. WAGNER: Okay.

Then I'd like to talk just for a minute about the relationship between the Board and other staff people, not the Executive Director, keeping in mind that in a classic structure, Executive Director is at the top of the chain of command structure. And normally the Board should try to always communicate through the Executive Director, although a lot of times the Board will actually -- or will want to talk to specific senior staff people who have specialties, whether it's finance or law or whatever.

The only thing the Board needs to do is to keep in mind that the Executive Director is supposed to have an overall perspective of everything that is going on. If you talk to people who are specialists, whether it's
the lawyers or the finance guys or whomever, they're really good at their specialty, but they may not appreciate a lot of the other kinds of sensitivities that are out there, and so you may be getting a very slanted view or slanted piece of information.

For example, if you're talking to the finance guys or particularly if they're a CPA, they will want to always protect the bottom line. So a lot of times their focus will be on doing whatever results in saving the most money for the agency or costing the least, whereas if you're talking to program people, they often don't pay nearly as much attention to the cost of things because they're trying to carry out the programs, so their slant will be more towards let's spend the money because we're doing a good thing.

So you have to realize when you talk to the people that are below the executive director level, that you may get some slant. You also have to be careful if you do that too much, you will tend to undercut the executive director, and that's not a good thing.

The other thing that I would point out, I'm sure it doesn't occur out here, is that there seem to be -- there are occasions that fortunately are less and less that occur where board members will inadvertently kind of abuse the staff by asking them to make political or
charitable contributions or support charitable causes. It's very interesting because this is a concern even at the corporate level. The SEC in its governance stuff is now making a big deal out of the fact that it's considered improper for board members to solicit charitable support or contributions from management of corporations. So if that's the rule on the corporate side, rest assured that's probably a good kind of rule that you ought to keep in mind here.

Again, I'm sure it doesn't happen in your state, but there are states where it happens on a regular basis. There's politics. Usually there's a law that controls that kind of stuff, but apparently the abuse that's occurring is more in the corporate giving area these days. So I just pass that along.

The Board also has relationships with a professional team. You hire lots of professionals. You need to make sure you understand the differences amongst the relationships.

I'll start with the lawyers, since I am one. You've got Tom here. Your lawyers, your General Counsel and your bond counsel have a legal obligation to you. It's controlled by ethics laws. And they basically can't talk to anybody, disclose things. So theirs is a very defined set of rules that make them keep their
mouth shut, basically.

But the other professionals have different sets of rules. The investment bankers that you work with don't have any kind of legal obligation to you except for the contracts that they sign. There's always been talk about, well, gee, they have some kind of fiduciary advisory relationship or role or responsibility to you, but there was a case out of New York about a year ago where somebody was unhappy with the services provided by, I believe it was, Goldman Sachs in that case.

And Goldman was the underwriter, and they sued Goldman because they said these bonds weren't properly priced. And the Court said the underwriter has a contractual relationship. They do not have a legal obligation to give you the best deal.

So your bankers always -- they want you to trust them, and it's not to say they're not trustworthy, but you need to understand they don't have a legal obligation to do some of those things that you might think they do.

MR. HUGHES: John, I just throw in that this exact issue came up within CalHFA over the past year in a slightly different context, though, in terms of complying with various ethics laws and disclosures and contracting issues. And the question was asked why the
investment bankers aren't signed on to these processes.

And the answer is exactly what John just said. They're actually a party in a transaction. We looked at this. We also ran it through bond counsel and got precisely the same answer. They're not our fiduciary. They're not our consultant. We, on the -- operationally and practically we have a close relationship and rely on a lot of what they say, but legally that is not the structure. So that's exactly what we concluded as well.

MR. WAGNER: Another party that you deal with on a regular basis is your accountants. After Sarbanes-Oxley, I can assure you the accountants will tell you that they have to be independent. You will sign all kinds of pieces of paper saying that, and they will tell you that. They will tell you that their relationship is -- and their obligations are to the Board.

There's -- it's a big deal about being independent of management. And it's -- they have probably overreacted in part, but if you got sued for billions of dollars in 2001 and 2002, you'd probably overreact too. So the accountants' obligation is to be independent, give independent financial opinions to potential investors.
Your bond trustee is technically a fiduciary for the bondholder. Although they may be your agent for a lot of things, their technical first obligation runs to the bondholder. It doesn't mean that their job is to make sure that the bondholder gets the best deal or anything like that. Their job is to make sure that the trust instruments that you sign are carried out properly and that you carry out your promises.

The last party that you may have, and I don't know if you have them, are financial advisers of various sorts. And if you do, those guys' job is to give you financial advice, but again, they're not fiduciaries for you.

You should make sure that your professional team works well with your management team, because if they don't, you will not get the best product that you can possibly get. I also would suggest to you that you should periodically review your professional team. And I think guys do that on a regular basis. I know you review your underwriters. Usually the parties are reviewed every two or three years.

Accountants, there's always been -- there's been a big deal the last few years about whether or not you should change your accountants. On the corporate side, they say you should change them every three years, and
then they found out that got really expensive because you always were reeducating people, and it takes about three years to figure out what in the heck's going on.

So now the rule on the accounting side generally is that the partner in charge of the account should change every three years, but you can keep the same people on the account. And I would suggest to you it's probably a good rule to follow in your business too. The other thing you'll probably find with respect to your accounts is that most of the time they don't understand what you're doing anyway, so you wonder how much value it has. By the way, their job is to follow technical artificial rules, and they're really very good at doing that.

And the others to look at, if you want to, would be the bond trustee. There are actually one or two state agencies that actually review their bond trustees. They have contracts that permit them to terminate them every two or three years without reviewing them. I would suggest it's better just to review them, not go through an RFP process because it's really painful and expensive to change bond trustees, so you only do it if you've really got a problem.

And the same rule generally applies to your lawyers.
Then we'll talk a little about board officers, but not very much. Then we'll talk a little about committees and board meetings.

MR. COURSON: Let me ask a question. Do we need to take just a --

MR. WAGNER: Want to take a break?

MR. COURSON: Okay. Let's just take about a maybe five-, ten-minute break so she can catch up. We have to respect our reporter here.

MR. WAGNER: I'm sure we do.

(Recess taken.)

MR. COURSON: Let me just talk logistically. Obviously we'll continue on with John, and when we finish, then we are having some lunch brought in. And we'll see what our timing is as to make a decision whether to eat while we continue to work and enjoy the presentation by the representatives of CitiGroup or take a little break. So we'll see what the timing is as we do that.

MS. PARKER: Yeah, I might just add that the staff, you know, if you folks want to go out and get lunch, so you --

FROM AUDIENCE: That's why I asked if you were working through lunch, just if we were going to -- don't want to miss any of this, it's so good.
MR. WAGNER: The lawyers don't think this is good because we get this in law school.

MR. COURSON: Okay, John. Thank you.

MR. WAGNER: Okay. Let's talk just for a little bit about the Board officers, particularly about the role of the Chair. The Chair is the key Board officer, and the Chair really sets the tone for the Board. The Chair needs to be a team builder. The Chair should liaison with the Executive Director and plan the meeting agendas and facilitate the meetings and appoint committees, if you're going to have them. So the Chair really is an important -- very important position. And I assume John is doing an excellent job, so I'll just skip the rest of that.

I'm going to talk a little about Board committees. I understand that you guys are not great fans of Board committees. Board committees are usually used by a board when they think that the full board is just too large a group to address a particular subject.

A lot of agencies have standing committees for audits, in particular, sometimes for budgets, sometimes for personnel or human resources stuff. And a lot of times boards will commit -- create ad hoc or temporary committees to address particular issues that come up and
then once the issue is addressed, they disband the committee.

But, again, the idea is primarily that you can get three or four people to really sit down and spend a lot of time and really focus on a particular single subject where it's hard to get a full board to do that.

The most common standing committee is an audit committee, which I understand you guys have talked about or maybe are doing.

MR. COURSON: We have one.

MR. WAGNER: The accountants love it because the accounting professions, they're really pushed to make sure there at least is one person on the committee who understands finance and audits. And sometimes with state housing agencies it's not easy to find a person who does have that kind of background and who really understands that kind of stuff.

Ideally the audit committee would actually sit down with the auditors for two or three or four hours and go over all the stuff that the auditors want to talk about, and then they would report to the board on that so the whole board wouldn't have to spend their time doing that.

My experience is that many agencies end up doing this as a committee of the whole, that a lot of the
board members don't really care about it, so they sit there and start to yawn and get fidgety and the whole process takes about half an hour and nothing really gets done. It drives the auditors nuts, and that's not the best way to do things, and that's why the committee sometimes is a better way to do it.

But I'm sure -- I keep seeing shaking of the heads like, yeah, we know.

MR. CAREY: John, I should just, from my own perspective, add to something you said about the committees aren't really in favor. I think there's two issues, one of which is that committee meetings are constrained by the same public meeting laws as the board meetings, and that makes it challenging to find a meeting time when a committee can get together. It's just difficult.

But I, for one, think that committees are a very effective way to get detailed work done and would not want to see us steer away from using them whenever we can. I think that it comes back to the commitment of the board members and being willing to come to committee meetings as well as board meetings.

MR. WAGNER: That's right. And a lot of times you can find two or three members who are willing to be on a committee and do have the time and will sit down
and make the commitment to put in the time that's necessary. So it's a good -- I happen to think it's a good way to address certain types of issues, and that kind of work is important.

Another thing you should also keep in mind, and this is something that is particular to audit committees sometimes or even other committees is that sometimes if you want to you can add to the committee people who are not board members. So that if you lack expertise in a particular area, it's okay to have somebody who is not a board member be part of the committee.

We do see this once in a while, in particularly the audit area. If you've got nobody on the board who really knows anything about audits, they will authorize the committee to go out and hire or bring in as another committee member an accountant or a lawyer with a lot of finance background who can help the committee go through its -- the process and procedures that it needs to go through.

MS. PARKER: How can you do that?

MR. WAGNER: Because --

MS. PARKER: Is it from the sense --

MR. WAGNER: You've got to be careful not to act like a lawyer.

MS. PARKER: No, but is the board -- is the
board hiring a consultant? Because I don't know how you can -- how you could add somebody who had any status to a committee that it has appointment statutory authority for.

MR. WAGNER: It's a concept that's foreign to most people, but it is something that can be done. You can either hire that person or it may be somebody who is just willing to volunteer their time, if they're a retired CPA or something, they're willing to act as a member of a committee, a nonvoting member of a committee to provide the expertise.

Now, you may have particular state laws that create issues for you in that regard, obviously.

MR. HUGHES: Well, when we've created committees, most notably the Audit Committee, the resolution, the charter that's adopted by the Board by resolution specifies that various types of people can effectively be staffed, including going out and hiring someone, and that's how we do it.

And I think what you're getting at, Terri, is that that person wouldn't have the capacity that a board member would, but they could be -- they could work with the Board on a consultant, paying basis basically.

MR. WAGNER: Yeah. They don't have to be voting members. The voting part is not the key. The key thing
is --

MS. PARKER: I mean I don't want to dissuade --

I mean I actually -- you know, I think this is a good
thing for the Board to be aware of, but I guess I see
that it could be effected fairly easily by the -- you
know, much the same as we've talked about -- maybe the
analogy is for the Compensation Committee, the Board,
you know, hiring the firm that essentially acts as the
expertise to the committee to get the work done.

MR. COURSON: Well, when we started our

Compensation Committee, we did that.

MR. HUGHES: Exactly.

MR. COURSON: We talked with Watts and Wyatt and

we retained them, and they came to every meeting that

the Compensation Committee had and advised us and helped

us and gave us forms and formats and policies that we

could use, but ultimately the -- any decision that was

made was made by the Board members --

MR. WAGNER: Right.

MR. COURSON: -- that were on the committee, but

they clearly were there for all the sessions.

MR. HUGHES: And the Audit Committee did that,
too, retained outside counsel.

MR. COURSON: Yeah, that's exactly right.

MR. WAGNER: Okay. So that's about it for
committees.

I was going to talk to you a little bit about Board meetings, because Board meetings are where the real work of the Board is largely done. So if you're a Board member, you ought to attend the meetings. I guess I shouldn't underscore that. Obviously the people here believe that. Because if you don't attend the meetings, you're not going to have any input, and the intellectual firepower you're supposed to bring to the table is gone and wasted.

You should prepare for the meeting by reading the packet that's sent to you ahead of time. A lot of times you see Board members who are reading -- sitting at a meeting reading it, and they can't certainly give much thought to what they're reading as they're sitting there reading it at the meeting. Plus, if they're making everybody wait, they're kind of imposing on other people a waste of their time.

So you ought to prepare for the meeting by reading the packet in advance, think about the issue. And if you need input on particular issues, normally you should call the Executive Director or whoever is appropriate to try to get input so you're not wasting the Board's time asking questions that are easily answered ahead of time.
You should take part in discussions. You were appointed to the Board because you're supposed to add to the Board, so you shouldn't just sit there quietly. You should learn to compromise and cooperate.

You should understand the basic rules of parliamentary procedure, just because that's the way boards operate and that's the rules that they follow. On the other hand, I would suggest to you that it's inappropriate to use parliamentary procedure rules to try to drive your position through so as to stop other people from being able to discuss their position.

You see people do that on the floor of the Legislature and some other places, and it may be it's acceptable there, but the idea up here is that you've got a lot of people who are intelligent who have particular expertise and you want all of their input so you can make an informed decision. And if you use parliamentary rules to stop that process, you're doing a disservice to the organization. So they should not be used as an offensive weapon. They should be used as a guide to direct things, and that's all they should be used for.

You should make sure you know the applicable open meeting rules because, again, sometimes if you violate those you go to jail.
You should learn the traditional board meeting practices because that's the way you most effectively will be able to get things done, and that's, again, your job as board member.

Meetings should be conducted in a businesslike, on-time manner. You shouldn't be wasting people's time because if you do, pretty soon people won't want to attend or won't want to participate. Just pretty simple basic stuff.

You should have an agenda, and you should follow the agenda. By and large your state law probably requires that, which is a good thing.

And I would suggest to you -- we talked -- I was talking to Tom a little bit about this. One of the things that the Sarbanes-Oxley law did suggest and the SEC really pushes is that a board member at board meetings, you should talk about substantive matters. You should not focus on routine reports. And it was very interesting. The SEC actually came out and endorsed this as a proper governance method.

You get routine reports, like in your case reports about delinquencies and defaults and routine kind of stuff, their position on a governance standpoint is that you should not be wasting your time talking about routine reports. Unless there's something that
really sticks out that needs to be discussed, you should be spending your time on the big issues, not the little things.

And there are a lot of agencies who have gone to having a consent agenda or something like that where they just list all those reports, and they just say, "Does anybody have a problem with anything?" Nobody has a problem, they go on. It takes 30 seconds, and they're done with all that kind of stuff.

There are other agencies who spend 15 or 20 minutes talking about the same old thing, and nobody ever has any questions because they got the reports ahead of time. It's just a waste of time. So that's kind of it on board meetings.

The last thing that I was going to talk a little bit about, and I'm sure Tom will chime in here, is the legal duties of board members and then the results of liability that you may have if you don't carry out your legal duties.

The law basically says you have three primary duties. The first is what we call a duty of due care, which means that you have to exercise ordinary and reasonable care that any other board member would. This means that you should do things like if your legislation says that you are required to do things, like submit an
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annual report maybe to the Legislature or those kinds of things, those are called ministerial, you should do those. It's a bad thing. Courts don't like it if you fail to do the things that you're told to do.

The second kind of thing that you should do is make sure you adopt appropriate programmatic policies, but this is discretionary. You have lots of leeway generally about how you will do this and what the policies will say, but you should still have those kinds of things.

As a general rule you're supposed to make sure you employ competent staff. I'm sure that's not a problem in the state of California. There are a few other states where sometimes the staff may not rise to the level of being competent, but I'm sure that's not an issue here.

You should supervise and monitor the HFA's operations. Make sure you've adopted appropriate management policies. Exercise independent judgment, which means that you're not doing things to help yourself or somebody else. You should protect confidential information that's given to you.

And you should become and stay informed. There's a famous case out in New Jersey about ten years ago where they had actually a nonprofit had a director
and the nonprofit was sued, and the director's defense was I didn't come to the meetings, I didn't read the materials, therefore I can't be responsible, and the court, the New Jersey court in that case said there's no defense called a dummy director defense. It's a good way to put it.

So those are the kinds of things that the duty of due care says that you should be doing as a director.

The second duty that you have as a director is what they call a duty of loyalty, which means that you have to be loyal to the organization. What that means is when you sit at this table as a Board member, your loyalty is to this organization. I don't care if you're a director or the president of another company, if you're an elected politician to another position, when you sit here as a Board member, your job is to be loyal to this organization. And if you have a problem with that, you should talk to somebody about the conflicts that you may have. But that's what the law says your job is.

It also means you should avoid situations that give rise to litigation against the HFA. The best example I can give of that is another HFA in the Southeast had a problem a long -- for a long time
because they allocated tax credits, and they had some board members who always didn't agree with the allocations. And the board members would talk to the unhappy developers afterwards, and this agency had at one time 35 lawsuits against it. And in every case, the first piece of evidence was the board member talking outside the board meeting to a developer about, well, gee, you know, you really should have got it, but these other guys didn't agree with me. So you should not be doing that kind of stuff.

The third -- oh, and by the way, a part of that and something we're seeing nowadays that the SEC is focusing on, interestingly, the corporate side, is that you should not take personal advantage of HFA opportunities. And this, right now, the problem that they're dealing with is what they call steering, where you have board members will say to management, gee, my friend does so and so. It would really be nice if you would hire them to do this. It's not a directive, but it's called steering business.

And on the corporate side at least now, the SEC is requiring that those kinds of relationship, if they occur, be disclosed because it's considered an improper thing for a board member to do. And we do see that a fair amount. So you need -- so it's okay to say, gee,
if you're thinking of hiring people, my experience with this person was good, that's one thing.

   It's a very different thing to say, gee, you're going to be hiring people, you ought to go hire this guy because he's really good. There's a difference between the two statements. You need to appreciate that difference.

   The third duty is one that arises under the federal securities laws, so your state law can't give you any protection really with respect to it, and that's when you sell securities in the open market, the agency has an obligation to disclose any material information.

   And you, as a director, if you have particular information that nobody else has, you have an obligation to tell the agency staff about it so that they can decide whether or not it needs to be disclosed.

   You know, this is kind of what the Orange County thing was partly about. In the case of an agency, sometimes you find a director who knows that a lender, for example, has particular financial problems and may be on the verge of shutting down, a situation you can easily understand today, and nobody else knows about it.

   If you have that situation, you, as a director, should be telling the staff, hey, these guys are in financial trouble. You ought to look at it. Because that may be
a material item that needs to be disclosed to your investors.

If you don't do that, you make yourself potentially personally liable for violating the federal securities laws. So you ought to just keep that in mind, that if you know particular information, you may need to tell that to the staff. And these days for some board members sometimes that becomes a real issue.

MS. GALANTE: I'm not clear about when you -- when and how you would know that you might know something that staff needs to know.

MR. WAGNER: Well, hopefully as a board member you have some idea what the programs are.

MS. GALANTE: Yeah.

MR. WAGNER: So the question is would what you know adversely impact the program or your financial situation. And if it is, you probably ought to at least tell the staff about it so they can assess whether or not it's material.

MS. PARKER: In our case --

MR. WAGNER: It's not easy sometimes.

MS. PARKER: We have legal requirements in our state for every board member to go through, you know, FPPC training twice a year -- every two years, excuse me. And they go through, you know, huge numbers of
examples.

And I think my sense is, Carol, that that really is meant to try to prompt us with what might be the kinds of things to look for that the board might be proceeding on and might be more specific than what John is saying more generally.

MR. HUGHES: I think it's worth taking a moment to just kind of backtrack. I mean I agree with everything John said on this, but I think it's worth taking a moment to sort of break out different types of responsibilities and consequences.

Back in 2001 when I first joined the Agency, I know during that year we had extensive discussions with the Board about liability issues. That's the last time we've done it because it was in the context of getting a commercial liability policy, but we haven't revisited that in quite some time as a board.

There are differences between personal liability under state tort law and other kinds of liabilities that board members may incur. Because board members are public officials, your personal liability for state tort law issues is limited. There is potential liability, but it is limited by the Tort Claims Act and various other limitations. That does not mean that a violation of duties might not have profound implications for the
agency as a whole against to one's personal liability.

Beyond that, I think what John was referring to
is that basically under federal law, under securities
law, all of us have a duty to make sure that we're not
misleading investors or omitting things that might be
misleading if they were disclosed. And so the mechanics
of how that work -- would work are quite complicated
because generally you're getting the information from
the staff.

But I think the point is that if you know of
something that is not being disclosed that should be,
that the board members do have that responsibility,
which goes to a point we've discussed at the staff
level, too, that the board members are really part of
this whole financing mechanism and need to take the time
to know enough about it to fulfill those duties, because
there is responsibility there.

And then there are generally, apart from state
tort law considerations or federal securities laws,
there is a general -- all the fiduciary duties that John
has talked about do apply. And regardless of whether
you're going to be personally sued for them or get a
defense, those are very important things to recognize,
because they have broader consequences than just being
named as a defendant in a lawsuit.
MR. WAGNER: Did that answer it? No, it doesn't.

MS. GALANTE: It's fine.

MR. HUGHES: Carol, I don't know that there's a lot of practical situations that we've had here where a board member would be in a position to know or not know something that is a material disclosure in an official statement. I can't think of one off the top of my head.

MS. GALANTE: Well, I guess what I was getting at is --

MR. HUGHES: But the general point still remains.

MS. GALANTE: We're not reading the official statements of these things, so how would we know?

MR. WAGNER: When I'm saying -- what I'm talking about more is if you happen to, for example, be a personal friend of the president of Countrywide. And maybe you're at a cocktail party and he says, oh, by the way, tomorrow morning, you know, dump your stock or something because tomorrow morning we're going to file. You would want to in a -- if the agency is about to issue bonds, I don't know if Countrywide is a big player, but I assume they are. You would want to tell the staff, hey, you know, this is about to happen.

MS. GALANTE: Okay.
MR. WAGNER: That's the kind of -- I mean by and large it would be pretty unusual that these kinds of situations arise.

MR. HUGHES: I think another way to just make the point is, again, in my prior life in the law firm, we represented various public entities and did bond law work for them. And I think it's fair to say that -- I guess how should I put this -- in some public entities the -- the city councils, the supervisors, whatever the governing body might be, might have a very limited understanding of the actual finances and pretty much sign off on things, you know, without a lot of question.

In the HFA world, and I think CalHFA, our finances are complicated enough and not dependent on tax revenue that, just as a general statement, the board of directors needs to understand that it is an integral part of that and should -- should make an effort to understand those finances, because you're all part of that chain of responsibility.

MR. WAGNER: That's a good segue to talking a little bit more about board member liability. As a general rule, I don't know if I've ever seen a board member actually held personally liable for anything, accept maybe in Texas, because if you do your job, you
pay attention at meetings, you follow the policies and
basically use common sense, you're usually going to be
okay. If you have questions, you should always talk to
your general counsel.

Tom talked a little bit about D&N or E&O
policies. I don't know what you guys do. As a general
rule, most people think they are largely worthless
because the carriers don't like to pay and they've
gotten very, very expensive.

MR. HUGHES: Right. And that's what I was
alluding to. Back in 2001, part of the issue that the
Board had us look at was whether a directors and
officers type of policy was worthwhile expending the
money for, and we did an extensive review of it and
concluded exactly what John said, that between the
limitations on personal liability under state law and
the cost of it, there was very little value in doing
that. There were some certainly hypothetical situations
in which board members would be responsible, but
generally those are matters outside the course, the
scope of ones duties as a board member and questionable
whether you should be covered.

So we do not have directors and officers
coverage. We do have general liability coverage for
various things.
MR. WAGNER: Do you have an indemnification policy or is that permitted under state law? Because the one thing that we do encourage is that every agency have an indemnification policy because if you do get sued, usually the cost is not the settlement amount, the cost is hiring the darn attorneys and paying all those things.

MR. HUGHES: Right.

MR. WAGNER: And with your balance sheet, quite honestly, you're probably financially better off than a whole heck of a lot of insurers that would be providing you with E&O and D&O insurance anyway.

MR. HUGHES: Right. And I think by policy, you're referring to a procedural policy as opposed to --

MR. WAGNER: That's right.

MR. HUGHES: -- insurance policy.

MR. WAGNER: Yes.

MR. HUGHES: And, yes, this is -- this is one of the interesting things really that runs through your entire talk, John, is that much of what we would consider to be our policies are really state statutes which govern how we need to operate, and in that case the California Tort Claims Act does have -- and various state statutes have extensive provisions on when the agency has to protect and indemnify and provide a legal
defense for any public official.

MS. PARKER: We went through this, whether or not given the cost and what the coverage was, that the Agency was better off sort of self --

MR. WAGNER: Doing it itself.

MS. PARKER: Self-indemnify, yeah.

MR. HUGHES: But it is correct as a general statement, there's some -- always some devil in the details, but generally the Agency will have an obligation to provide a defense for board members or staff members, for that matter, that are sued within -- you know, acting in good faith within the scope of their duties.

MR. COURSON: Is that part of the law?

MR. HUGHES: Yes.

MR. WAGNER: Yeah, because that's really worth more than any of this other stuff.

MS. PARKER: Right. I mean particularly for our profession, the Board, it's kind of like the least we could do. We had a situation where this came up, members of our board who had substantial personal wealth and, you know, rightly so, I don't think any of them should be personally --

MR. WAGNER: Right.

MR. HUGHES: Where the board discussion took a
lot of time in 2001 was with respect to liability for punitive damages. And it's a very complex analysis under state law because it's very circular, but there are even circumstances in which the State might be required to satisfy any judgment based on punitive damages. It's not unlimited. There's a variety of hoops that need to be jumped through, but that is always a possibility.

MR. WAGNER: Okay. Well, that pretty much sums up certainly the liability discussion.

And I guess from a closing standpoint, the bottom line is you guys have a cool agency. You do a good job. And we're really jealous of you guys being board members because there's a hell of a lot of us who would like to sit out here and -- who would like to be in your shoes at some point in time because it is -- what you do is fun. You do a good thing. You run a good set of programs. You're helping your state, and that's what you should continue to focus on.

And that's it.

MR. COURSON: John, I really thank you for your time. That was very good.

MS. JACOBS: That was good.

MR. COURSON: It helps us focus really sort of outside the pressure of a board meeting and so on on
some of the things. I've got a lot of ideas, I'm sure others do, that, you know, we can pursue and follow through and will make us even better than we are.

MR. CAREY: Can I ask one question?

MR. COURSON: Please.

MR. CAREY: As we sit here and talk about the functioning of the board as board members and our responsibility to the agency, we all end up -- we all get on the board through a variety of different channels or whatever, and I've heard it argued that -- that some might argue that the primary responsibility of a board member is to the public, not to the agency. And how would you speak to that?

MR. WAGNER: Well, first, the Legislature created you, and the Legislature said here are the purposes of this agency. So when you're appointed to the board, your primary responsibility is to make sure that the purposes specified by the Legislature are carried out. And that's what -- so in that way, I guess, that's how you're representing the public, so to speak. But your primary obligation is to carry out the purposes of the agency and therefore further the agency.

MR. CAREY: Because a board member who -- I think with a board, you have the understanding that once the board decides something, that is the board's
decision. Right?

MR. WAGNER: Right.

MR. CAREY: But you could have a situation where somebody felt that was the wrong decision.

MR. WAGNER: Oh, and that's going to happen a lot of times.

MR. CAREY: And would feel that they had a responsibility to take that elsewhere. How do you speak to that?

MR. WAGNER: That becomes a problem because once the board has decided something, it's the job and responsibility of every board member to support the decision, even though they may not agree with it. Supposed to disagree during the discussion process, but if the vote is against them, they should not be going out and undermining the decision that was made. That's one of the aspects of the responsibilities of being board members. You support the board's decisions as a whole.

MR. HUGHES: And I do think that was the point that you were making, John, when covering the various director's duties, the director -- the duty, excuse me, of loyalty. It's not -- it's not partial loyalty, it's a duty not to -- not to damage the agency.

MR. WAGNER: Not to undercut the agency, that's
right.

    MR. COURSON: Lynn.

    MS. JACOBS: Even though this is not an official quorum meeting, are we going to get the minutes from this?

    MR. COURSON: Yeah. Oh, sure.

    MS. PARKER: Absolutely.

    MR. HUGHES: The meeting is being handled exactly as a regular meeting.

    MR. COURSON: They'll be sent to all board members.

    MS. JACOBS: That's terrific.

    MR. COURSON: Okay?

    John, thank you very much. We really appreciate you coming out.

    MR. WAGNER: Happy to do this.

    MR. COURSON: It was very enlightening. You've given us some things to work on going forward and very helpful.

    MS. PARKER: I would mention to the board members that for all intents and purposes we're just barely covering John's expenses, so he's really come and done this, from the standpoint of his time, on a pro bono basis.

    MR. WAGNER: Lawyers are not all avaricious
people.

   MR. COURSON: We really appreciate that. Thank you very much.

   MS. PARKER: I think he was in this case very pleased to be able to come and talk to this group.

   MR. COURSON: Thank you.

   We're going to recess for about 30 minutes and -- actually, can we go to 1:15?

   MS. PARKER: Sure. One of the things that I was thinking about, and I don't know whether or not you are willing to let me do this is I know there's a couple of board members who are going to be leaving about 3:00, and I wanted to just give an update on this mortgage counseling program. So can I do that ahead of -- maybe while people are eating or something?

   MR. COURSON: Yeah, let's recess until 1:00 o'clock, and then we'll come back. Terri, you can do that. We can finish eating if we're still eating and then go right into the CitiGroup. Okay. So we'll recess till 1:00.

   (Lunch recess taken.)

   MR. COURSON: We'll reconvene our meeting. And I think for the record, let's recognize that Mr. Pavao and Mr. Davi and Ms. Javits have joined us for our afternoon session.
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Item 5. Update on CalHFA participation in mortgage foreclosure counseling program

MR. COURSON: And before we move into our presentation this afternoon, we're going to go to item 5 on our agenda. As you know, at our last board meeting, we asked Terri to give us an update on where we stand on our foreclosure counseling program and our application and bid.

So Terry, why don't you do that before we start.

MS. PARKER: Thank you. And then we'll introduce our afternoon guests.

I just want to give you a progress report on where we are on the project to try to bring in these federal appropriated dollars for a foreclosure counseling program. We had introduced at the last board meeting, Stan Keasling from RCAC, but I wanted to say what it stood for -- Rural Community Assistance Corporation, and also Alan Fisher from the California Reinvestment Coalition. We handed out a little document that sort of said this is how we think this relationship might work, and then we told you disregard it because it's totally going to change.

But here's what's happened to date: The applications are due to NeighborWorks by the close of
business Friday, February 8th. And we are well on our way of getting our application for California done. We plan to have a structure whereby the CalHFA is the applicant as we have authority to be under the federal legislation. We have hired Rich Friedman, I believe you all know him, former General Counsel for HCD and manager of Multifamily Programs.

MS. JACOBS: Financial assistant.

MS. PARKER: Thank you. I didn't want to dis him on what his title was.

But Rich Friedman has agreed to come in and on a consultant basis be the project manager for CalHFA, in that sense for the Board, manage our -- make sure to address our concerns separate from what the concerns might be of the subcontractor, who will be RCAC, who will be subcontracting to be the contract manager of the programs.

They have done a survey of HUD qualified counseling entities throughout California, and the response back was from 24 entities, 19 of which have requested $10.7 million in counseling funds. Three of those 19 have requested $6.4 million alone. That includes L.A. Neighbor Housing for 3.4 million, Operation Hope for a million-eight and Acorn for a million-two.
Five of the entities have not yet applied for any specific dollars, partly because they do not meet the criteria at the moment of being -- for application because they haven't done recent counseling, but RCAC is working with them, and the expectation is that by its second round, they will probably be qualified. So we would intend to obviously include that group in a request for funds further along.

Application is due, as I said, Friday. We expect to get the document from RCAC by the end of the day today so that we at CalHFA have an opportunity for a day and a half to review it before we turn it in on Friday.

We are going to have it be accompanied by a letter that Tom has written that's very specific to NeighborWorks explaining what we at CalHFA's role are and what we believe we have our authority and how we are meeting the criteria in the legislation through our subcontractor.

The awards are supposed to be the 24th of February. And once we receive that, the dollar or flow of funds are supposed to be out to the coordinating counselors by the first part of March.

So we think at the moment we've got a good team together. We've actually had very good interest, but
there will be a lot of work to be done and work to be
done at the federal level because I think there's
expectation of all these dollars going out by the end of
the year. Whether that is realistic, I think we can
probably already say that we're probably going to be
encouraging that any dollars that are not expended are
able to be rolled into 2009.

MR. COURSON: Is that a requirement of the
program, that the 180, full 180 has to be expended by
the end of the year?

MR. CAREY: It's statutory.

MS. PARKER: Happy to answer questions.

MS. GALANTE: How much is CalHFA's/California in
toto applying for?

MS. PARKER: The expectation or my understanding
at the moment, Carol, is that I believe -- I'm not --
people who can apply are either the HFA for the state or
a nationally HUD certified counseling entity. I don't
know if there are any of them --

MS. GALANTE: Separate from this.

MS. PARKER: -- separate from us that are
applying for funds to serve California.

MR. PAVAO: There are?

MR. CAREY: There are.

MS. PARKER: Peter? Do you --
MR. CAREY: Yeah.

MS. PARKER: Who?

MR. CAREY: The National Credit Counseling Network, the National Council of La Raza, are two that I'm aware of that will be going in as intermediaries that will then pass some funds through local affiliates in California. Plus the NeighborWorks organizations themselves --

MS. PARKER: Right.

MR. CAREY: -- are --

MS. PARKER: NeighborWorks, there are -- there's 15 percent set aside for them, and their applicants flow through that. And, you know, maybe we'll find some more. I have no idea of those groups how much they have requested that would be California based.

The application requires the -- it to be very specific about the entity and -- that's going to be providing and how much, whether it be Level I, Level II or Level III type of counseling of services are going to be provided. And that's how we build essentially the estimate that you're requesting for.

So at the moment, the expectation of these 19 of 24 entities is 10.7 million. And obviously it will be, once it goes out, reviewed, you know, whether its performance is -- there's performance goals before
subsequent releases of funds can be made.

MS. GALANTE: Thank you.

MR. COURSON: Bill.

MR. PAVAO: Did I hear you refer to a subsequent round, or are these funds available in rounds?

MS. PARKER: Well, from what I understand of the $180 million, that they are required to get $50 million out like immediately. So I don't think -- we don't know whether they would give us what we would expect for, you know, our full application or they'd say here's your portion of the first 50.

But, again, I mean, I -- Peter, do you know anything more than that?

I think the expectation is that there will be -- I don't think they're going to allocate everything, and so we'll keep going back if we can essentially justify that we need more money.

MR. CAREY: I think there's an assumption too that funds -- even if a high level of funding is allocated, that there will be places in the country where they're unable to implement it effectively and there will be some passback.

MR. COURSON: Okay. Other questions?

Can you let the Board know after the bid date whether we are successful or not? I mean we don't meet
till the third week of March and so we'll know by the end of February. Right?

MS. PARKER: Sure. I'll send out an e-mail about what the award was to California.

MR. COURSON: Right. Yeah.

MS. PARKER: Right.

MR. COURSON: Just so everybody knows.

MS. PARKER: That would be great, yeah. I think -- and, you know, we can try to plan to do some kind of an update at the Board meeting and see if we can get Stan and particularly Rich to come and do a little presentation.

MR. COURSON: If we're successful, we should make sure we put that on the agenda for the meeting.

Any other questions on the counseling?

If not, do you want to do the honors?

MS. PARKER: Yes.

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Item 4. Presentation on issues and events relating to the current subprime lending crisis, presented by Nick Fluehr and Mike Koessel of CitiGroup

MS. PARKER: Maybe I should have been more formal in bringing in the glowing background of the two colleagues from Citi who are joining us this morning, Nick Fluehr and Mike Koessel. Nick is the managing
director of the housing unit for Citi -- did I do that?
And Mike is his colleague. Mike has the distinction of
also having a Ph.D. in -- what is it, Mike?

MR. KOESSEL: Philosophy.

MS. PARKER: That really helps out a lot in
dealing with HFAs.

We've asked specifically to have Nick and Mike
come out. They did this presentation for a group of
HFAs in New York the last part of January, and we
thought -- John went and Bruce and I went, and we
thought it was so good that we thought it would be
really helpful.

And as you all know, I've been saying this for
the last six or eight months, that Citi has been very
helpful to the Agency in providing us information on
subprime activities, specifically subprime activities in
California. And that's been the basis of the
information that we've come back in giving you in Board
meetings, shared with staff, done some briefings for
legislative staff, so that people are more educated at
least in what's happening in California for us to see if
there are some kind of solutions that we could put
together a role that the HFA may play or any other
activity in the State of California to help, given the
dramatic impact that California has disproportionate to
the rest of the nation on the subprime issue.

So Nick and Mike sort of tweaked their presentation that they did in New York to make it even more California specific. And I know that their presentation will be very informal, so if there are any questions, I think they would probably say, you know, interactive is the best. And if there are some questions from some of the members of the public, that we try to provide a forum so that we can make this as informative to everyone as possible.

So with that, Nick, I will turn it over to you.

MR. FLUEHR: Thanks.

I mentioned this morning that we were in the kind of in the unenviable position of being experts on the subprime, given that Citi has written off, I don't know, untold billions of exposure to subprimes and CDOs, and obviously it's taken its toll throughout the finance industry.

But I do think, you know, this issue is fascinating just when you see the ripple effect that it has had on the financial markets really worldwide. I mean it has impacted the municipal market, obviously real estate, everything. And you can, you know, hopefully get a sense of that.

I mean the problem is so enormous. There are
all kinds of directions you can go off in tangents, but
I think what we've tried to do here and what we did in
January was going distill sort of rationale as to how
we -- you know, how we got to this problem, why did it
start, what has occurred, how big is it, who are the
lenders, what's impacted and then sort of, again as
Terri said, happy to respond to questions and everybody
has different ideas and different input, which is part
of what's been valuable to us.

Just going back, you know, it's interesting if
you compare how quickly the financial markets have
changed. We take a look, you know, back until really
mid-2007, we had relative calm in the financial markets.
You know, liquidity, cash was plentiful.

Buyers -- because risk premiums, or sort of the
reward for risk, were so low, buyers were coming to us
saying I want high-yield securities. How can I get
more, you know, higher yield? How can I leverage what I
have to -- it was really a search for yield.

You recall that the Fed had risen rates, that
rates had risen on the short-term side. Really on the
long-term side we hadn't seen -- you know, rates were
pretty stubborn. They didn't move a whole lot. So for
investors it was, you know, at the bottom bullet here --
it was really do they achieve yield in this low
volatility, low risk yield. And that's what sort of characterized our financial markets.

MR. KÖESSEL: Nick's kind of specified what the key characteristics of the market were six months ago, a year ago. And there was a kind of a -- Terri's let the cat out of the bag. I have a philosophy background.

There's kind of a theoretical underpinning that was going on a year ago, too, which was there was the general view, and the term that's used -- that's applied to it comes from Ben Bernanke, the chairman of the Fed, and the term is the Great Moderation. There was a general view that the Fed fiscal policymakers both in the United States and globally had gotten very good at managing economies.

In the last 25 years, we've seen two rather shallow and rather short-lived recessions. And to a large extent, that success is attributed to the Fed, those policies of gradually moving interest rates to fight inflation predominantly.

And in addition, it's attributed to a certain set of financial innovations including some of the innovations that we're going to talk about in the course of the next half hour, hour that have undone the real estate market and are largely at fault with respect to the credit crunch and the crisis in the financial
markets.

But the backdrop here was that the economy was something that could be managed, and it was pretty much riskfree. There wasn't a great sense that, you know, the stakes in the economy couldn't be managed, couldn't be controlled.

At the bottom here there's a quotation which is taken from an economist, a guy named Dalinsky (phonetic) who's talked a lot about this, says that the great paradox here is that greater stability actually breeds instability. Nothing is so destabilizing as stability.

The basic idea there is that when you strip away the sense that we live in a risky economy, it actually encourages high-risk behavior. And that's what we're going to be talking about to a large extent.

MR. FLUEHR: When we looked specifically, drilled down to the HFA marketplace, to the tax-exempt markets, there was relative calm there as well until last summer. The fact is that you guys issued generally tax-exempt bonds, that's your funding advantage versus the conventional market, and what we call the ratio of tax exempts to taxables, and that ratio does move around, but ratios were very, very attractive.

In other words, your selling just vanilla bonds, what we call cash market bonds, was very advantageous.
You didn't have to go out to the swap markets. You didn't have to pursue a lot of, you know, riskier structures, per se, in that the cash market was very favorable.

When you talk about MMD ratios, MMD, that's municipal market data. That's sort of our perfect AAA curve for a GO obligation. We'll talk a little bit more those MMD ratios later on.

The other thing in the middle there you can see that credit enhancement and liquidity were all very cheap. The fact is you could go out and get liquidity for variable rate bonds, lines of credit, letters of credit.

Insurance policies. Monoline insurance policies were very inexpensive. In fact, those entities thought that, jeez, we've sort of nailed this municipal market down so perhaps we should diversify and get into other esoteric mortgage backed securities and talk about insuring those, so we'll have that -- more on that later obviously.

MR. KOESSEL: So that takes us up to where we are today. And basically you take everything we've said so far and just flip it on its head, just turn it upside down.

Nick talked about a surplus of cash and
liquidity in the marketplace. To a large extent that's largely been absent in the course of the last six months. There's been a real crisis with respect to cash and the availability of credit in the market.

Volatility. Volatility has gone from very low and being perceived as being very low to being very, very high. Risk premiums have gone from being very low to being very, very high.

All of this basically is part and parcel of a general flight to quality. What people have done is they have gotten nervous about lending money. They have gotten nervous about the markets, nervous about what might happen to their money if they lend it, and they put it in what they perceive as being the safest possible investments, which are government insured Treasuries.

There's been a flight to Treasuries, a rally in that market. As Nick pointed out a few minutes ago, the relationship between municipals and Treasuries has changed dramatically, and that's because people are chasing Treasuries. They're chasing security. And they're running away from anything that's perceived as being risky. And anything with the word "housing" attached is perceived as being risky, but lots of other things as well out there.
But these points are made graphically on the next couple of pages. You can just see beginning in about August, late July, early August, you see credit spreads starting to widen. Credit spreads are basically the differences between a high credit security and a lower credit security. That's highlighted on page 5. Those are the differences there between AA credits and lower rated credits.

One of the most -- if you flip the page, one more, one of the places where spreads have widened out most dramatically is in the short-term LIBOR market. LIBOR has to do with banks lending to each other.

And when the Fed -- typically those short-term LIBOR funds track the Fed funds rate. When the Feds started to cut -- actually before the Fed actually started to cut, when people got concerned, you get concerned about what kind of -- what kind of assets other banks may have on their books, these spreads started to widen. They started widening last August.

And as the Fed continued to cut, they would narrow a little bit, and then they'd widen out. The Fed has now introduced enough liquidity into the marketplace that three-month LIBOR seems to be on top of the Fed funds rate, which is where we would expect it to be in the current rate environment. We'll see if that lasts.
It may or may not. This is again indicative of the fact that banks are much, much more comfortable with something like a Treasury security than they were even in lending to each other.

MR. FLUEHR: One thing I would like to point out, you look at these credit spreads that Mike talked about, and obviously we can see here that, you know, sort of credit spreads appeared to be and in fact were a lot wider obviously in the sort of 2000 year than they are right here. But as I'll talk about, I mean you've seen the widening again in August. It was interesting.

I remember in August in the municipal market we were bringing an issue to market, and the market essentially shut down for municipals.

And that was really due to the fact that three European money market funds stopped redemptions on their portfolios because they were unable to value assets, the underlying assets, the, you know, CDOs and MBSs that they had in there. There was no -- they couldn't get a value, so they shut them down. That caused a crisis in confidence that rippled through every market, including our own, which is why you saw this spike up here. It happened, you know, basically and it's only grown.

The interesting thing is I talked a little bit about MMD, and while those spreads look very, very
tight, the fact is that the MMD curve, which, again --
this is the perfect municipal GO issue, if you will.
The fact is that tax-exempt curve right now is very
cheap or, you know, very high yielding versus the
taxable market.

The two graphs at the top here, you see this is
five-year MMD versus Treasuries. And you can see that
basically five-year municipals are yielding about a
hundred percent of five-year Treasuries.

Same thing at the long end. In other words, you
know, in a perfect world, remember, if you were in the,
say, 35-percent tax bracket and you were buying two
equivalent AAA securities, you'd say -- ordinarily you'd
say, well, what kind of return would I want? Well, I'd
be happy to get 65-percent return on my tax-exempt
investment versus the hundred-percent return that I
would get on my taxable reinvestment. I'd be different
in those cash flows at the end of the day after you pay
taxes.

So the fact is that we're yielding a hundred
percent of Treasuries in our tax-except market right now
obviously doesn't bode very well for tax-exempt
issuance. It's problematic. That is, again, an effect
of the fact that people -- there's a flight to quality.

They don't even trust highly rated municipal bonds
right now.

The -- let me -- one other thing on this last page. The housing bonds, obviously we're not the perfect AAA GO issuance that MMD is, so housing bonds, CalHFA bonds, typically trade as a spread -- at a spread to MMD. That spread generally widens the further out you go.

You can see here that this line tracks those spreads to MMD for 30-year AMT housing bonds. You can see that that spread has gone up dramatically, you know, more than doubled basically. You know, let's call it 50 basis points, 60 basis points here, to 120 basis points at the long end.

So not only have we had this adverse relationship versus the taxable market, but housing bonds, again, are getting penalized sort of doubly, causing a problem which is, you know, depicted in this chart here. This shows again ten-year Treasury is this dark line at the top versus 30-year AMT housing cost of funds.

You can see that generally the lines were on top of each other. Your cost of funds approximated ten-year Treasury bonds. And since the conventional market uses the ten-year Treasury to price their mortgages off of, generally you're, you know, in good territory here.
When these lines diverge, and we've seen that with this flight to quality, the fact is your cost of funds has stayed relatively constant. This dark line represents the spread between those lines. So obviously the bigger this line is, the worse off you are. So right now, we're finding it exceedingly problematic to fund ourselves in the tax-exempt market and to produce a viable cost of funds because of these market disruptions.

We talk a lot about, you know, the -- we have used the snowball at the edge of the hill analogy and maybe we'll return to that, but, you know, there's kind of a cycle here. Obviously if you have deteriorating financial markets, you have deteriorating interest rates. You have real estate prices dropping.

There's a snowball effect, if you will, where people -- more inventory gets put on the market on the housing side, you know, that's going to depress prices. Depressed prices are going to cause more people, you know -- and it's sort of a self-fulfilling prophecy.

The interesting thing is, you know, not -- you know, less than a year ago, there was talk in the markets that we're in a new paradigm, you know. And anytime you hear that, you know, the warning bells should go off. It should be like -- because we're in a
new market. Risk is -- everybody is willing to accept risk, looking for, in fact, to take on risk in order to boost yield. And because of that, quote, new paradigm, the -- I think the important thing down here is this last bullet talking about complexity.

Basically Wall Street, more and more complex to answer this investor desire for different financial instruments that would basically augment yield, in turn taking more risk. And as those instruments, as we'll talk about, as they got more complex, the -- it was harder and harder to evaluate how they might perform if we deviated from the assumptions under which these securities were sold, so.

MR. COURSON: Nick, what -- obviously with the Fed cutting rates and the resulting now rates in the mortgage market, the applications -- application index is growing dramatically, particularly on the refinance side. Everybody is now afraid. If they're in or out of the money with their adjustable rate mortgage, they're running for a fixed rate, which if you look at some of the numbers, if the -- the percentage of pulled through for loans being actually funded versus that application rate, we're going to have a substantial increase in product seeking securitization, seeking a home. Does that just exacerbate the problem for the tax exempts?
MR. FLUEHR: You know, I don't -- I don't know that it hurts the tax exempts. There's a whole subset of the tax-exempt market, you know, monolines. And there's the fact that -- and we'll talk about this a little later, but it's really -- the tax-exempt markets, it's a buyer problem. The buyers that we have traditionally looked to, which a lot of times are what they call these arb investors, the tender option bond programs and the hedge funds that we're looking to sort of leverage returns, they have stopped buying. In fact, they're often liquidating securities.

So all of a sudden we've gone from, you know, this big piece of pie that we have sort of all these buyers before, now we're back to this, basically, insurance companies and even Fannie Mae and Freddie Mac are not being big buyers.

MR. KOESSEL: John, arguably it's good for HFAs for the simple reason that -- if I'm understanding your question right, which is that you've got pull back of investors willing to buy MBSs. Obviously the CDO -- we'll come back to this in a second.

CDOs are out the window. We aren't doing those anymore. We're back to old-fashioned MBSs. Presumably that world is contracting.

To the extent you have less investor interest in
housing project, the spread of a conventional product to the underlying cost of funds has widened. We don't have that chart in here. Those spreads are widening, and that benefits you guys because even the Treasuries are rallying and HFA cost of funds are not keeping pace with that. The spread of a conventional cost of funds to the conventional product is widening out because of this lack of investor demand for housing paper.

So that's actually worked reasonably well. I mean one of the things that we saw early on with our HFA clients was that as ten-years started to rally, they were doing more business than ever because there was no other investor there serving their community.

MR. COURSON: Right.

MR. KOESSEL: And these spreads were widening out. Initially, at least, mortgage rates in the conventional market were not tracking down with Treasuries. Now Treasuries have dropped 180 basis points. As you know, they're probably 550, 560 right now for conventional loans.

MR. FLUEHR: So just stepping back here, we're going to talk a little bit just about how mortgages are typically funded. You'll recall back when the mortgage industry started, you generally had savings and loan companies who were funding mortgages from -- with their
deposits, so they were making longer-term loans with short-term deposits, which obviously caused a -- excuse me -- caused a little bit of a hiccup in the S and L crisis as you recall 20 years ago.

MS. GALANTE: Did you do that on purpose?

MR. FLUEHR: There was -- yeah.

There -- some bright guys at one of our predecessor companies, Solomon Brothers, actually, had a great idea in that they thought, well, jeez, why don't we buy these mortgages, pool them, cut up the cash flows so that we can rather than having a 30-year asset that is unbelievable volatile -- I mean obviously a mortgage can prepay tomorrow. It can go out for its life -- but instead we'll cut up these cash flows and tranche these securities, so that was really the start of the securitization market.

And there was all kinds of arbitrage opportunities where people made fantastic sums of money where they would buy these mortgages and cut up the cash flows and basically sell the parts for a lot more than the whole under which they bought it. And that was kind of how securitization started.

Today obviously we've got governmental sponsored enterprises -- Ginnie Mae, Fannie Mae, Freddie Mac -- who are active in the securitization market, guaranteed
pools of mortgages. Just to give you a flavor, Ginnie Mae makes up about 4 percent of the securitized product in '06; Fannie Mae, Freddie Mac 40 percent; the remaining 56 percent are what we call private label MBSs or companies that are actually securitizing their own mortgages. And those are largely where you see most of the subprime, Alt-A, the sort of sketchier product.

Again, the theory on securitization is that by cutting up these cash flows we seemingly have cut risk. We're giving investors shorter -- you know, if they want a shorter tranche, they can buy a shorter tranche. If they want a longer average life with arguably more risk, they can buy that as well.

I think, you guys, we don't need to spend a lot of time here. You can see that it's interesting that in mortgage backed security space, this dark area here, sort of subprime component of mortgage backed bonds, you can see that that component has grown very significantly -- or grew very significantly in the '04, '05, '06 time frame.

And, again, just -- you know, just to talk a little bit, you know, in the securitized market, let's just say you had a thousand hundred-thousand-dollar mortgage loans. You would pull those into a mortgage backed security that might be -- that would be a hundred
million dollars, if I did my math right. Let's just say all those mortgages had a 6-and-a-half-percent rate to the holder. They would pool those, securitize those, they'd cut out -- take off 50 basis points for servicing and the guarantee would be, the pass-through would be 6 percent. Cut up that hundred million dollars into bonds blocks of say $10,000, and you, me, institutions could buy those securities for those -- sorry.

MR. KOESSEL: The key point here is if you look at the box at the top there, you'll see the number of participants there. At one time it would have been very simple. The homeowner takes out a loan from the bank. The bank has depositors, and that's his ultimate refinancing that loan, those people putting their money in savings accounts.

We've added quite a number of parties to this. In the process we've added a lot of complexity. And those two features are key here. We've moved the loan from the person originating the loan. The loan is being passed along to the MBS, and ultimately the investor may be several times removed from the MBS in very, very complicated CDO structures. And that's a second key point, is the complexity of it. The complexity, the removal, have at some level facilitated the crisis, and we'll come back to that.
MS. GALANTE: Are you going to talk about --
given that complexity of that box, I don't know where
all this is going, so -- talk about the potential to
help borrowers and given this complexity how you reach
in and actually make an impact on that situation?

MR. FLUEHR: We can.

MR. KOESSEL: We sort of --

MR. FLUEHR: Yes. At the end we kind of --
obviously that's the $64,000 question is how do you
address this, and that is the last section of this book.

MR. KOESSEL: We have a few things to say on
that subject. We don't have a magic bullet. I think
that term is in there.

MS. PARKER: The only thing -- I'm sure, just to
say this for Carol -- I want to make sure you guys get
to there before she needs to leave.

MR. FLUEHR: Okay.

MS. PARKER: So keep it -- you know.

MR. KOESSEL: What time do you need to leave?

MS. GALANTE: 3:00 o'clock.

MR. FLUEHR: We talked a little bit about --
and, again, you know, we use -- I know as bankers a lot
of times we use these buzzwords that we have used for
years, and they -- it sounds like we're talking Greek to
other people, so stop us if we do.
I thought it would be interesting just given that everybody sees and hears the terms CDOs or collateralized debt obligations. You see it on the cover of the Journal. I mean that's largely where Citi has written off, you know, billions of dollars because of CDO exposure. So the question is what are CDOs, why were they there.

I talked a little bit about that arbitrage opportunity or the earnings opportunity in the early days of the mortgage market where people could buy mortgages from banks. They could securitize them and cut them up into pieces and sell them at a profit. Well, obviously markets are very efficient, so that search for those mortgages, that -- the balloon went off. That rose very, very quickly.

So those arbitrage opportunities essentially evaporated. Today everybody is -- I shouldn't say everybody, but price versus the Fannie Mae index, you know exactly what your take-out price is and there's very little arbitrage opportunity there.

CDOs were really created to cut up the cash flows further from these mortgage backed securities, arguably to -- you know, the thought was, hey, we can diversify risk. And, again, by pooling different types of assets, we can sell different rated tranches.
So we can have a highly rated tranche, which would get the first cash flows from this underlying pool of assets. And you can see at the top here we have mezzanine tranches that got the second, third, fourth, and you kind of had a waterfall effect as to how all these bonds would receive payments.

The CDOs tended to be a very efficient mechanism to digest sort of these mortgage backed securities and even, and more importantly, to digest the lower rated tranches of prior CDOs. So what you had is, you know, these -- CDOs were sometimes CDO squares. They were buying -- you can see that quote in the box there, right there: "The majority of subprime asset backed securities was bought by another securitization vehicle that issued further bonds."

So you were having CDOs, you know, basically backed by prior CDOs. As a consequence, you were leveraging up this -- this ugly tranche, the mezzanine and those sort of the equity tranches. And as we'll talk about further, the rating agencies kind of went along with this thought in that there was very little history on the underlying subprime assets.

We were in a rising rate environment. These subprime borrowers were performing very well. They were making payments. They were refinancing their prior
mortgages. Everything actually looked pretty rosy. Their FICO scores were improving. And as you can see, the CDO issuance ramped up to sort of digest these pieces, and investors were happy to buy these. It was again that search for yield.

The other thing that occurred throughout this period is that because again investors were willing to take more risk, very low interest rates, housing costs were appreciating, in order to get people into houses, we had different new mortgage products that came out to address sort of that need as how do we get people into these homes. The same question that you guys face all the time. It's like how do we do that?

Well, one thing was to extend the term. Forty-year mortgage loans. We had hybrid mortgage loans. You know, the bulk of these subprime loans are what they call 2/28s where they'd have a two-year teaser rate that would subsequently adjust up to a higher rate. ARM was very popular.

Interest-only loans where there would be an interest-only period that would -- then these loans would subsequently start to pay principal at a later date in time. Really all of these latter products, though, subject to payment shock, in other words, you know, there would be a ramp-up in the payment at the
time that they came due.

The other interesting phenomenon, you know, we have a graph later on here that looks at homeownership rates. And the fact is that homeownership rates have ramped up, have increased. I think, you know, one argument was, hey, the subprime -- these subprime loans helped people get into homes that ordinarily couldn't have gotten into a home.

The reality is -- is that something like only 15 percent of the subprime loans were actually applied to get people, new people, into homes. The 85-percent remainder was really for cash out refis.

I told a story this morning. Connecticut HFA actually came to us two and a half, three years ago and said, Nick, Mike, we'd like you to create a subprime mortgage program for us because we feel that people are taking advantage of our population in our state and, you know, we'd like to offer something. We don't think the credit risk is as severe as the market is assessing or charging these subprime borrowers. They're being taken advantage of.

We went to one of our subsidiary companies, CitiMortgage, and said, look, give us a brain dump on subprime loans. How do you -- how do you price them. And the really telling and interesting thing that they
said is those subprime loans -- the subprime loans that we have, their average life is one and a quarter years, that -- and the instant that these borrowers develop any equity in their home, they're out of that loan and they're financing to pull that additional equity out.

So these are really just tools to, you know -- for borrowers to get more money, to cash out.

MR. PAVAO: So is that the expectation when these loans were originated, was these are just going to be held very short-term?

MR. FLUEHR: I think the expectation was that they would refi these, yes.

MR. PAVAO: So there was no expectation that their incomes are going to go up and they're going to be able to afford that bump up in year three or year four?

MR. KOESSEL: I don't think there was any realistic expectation.

MR. FLUEHR: That was the argument, perhaps but as far as expectation --

MR. KOESSEL: There was the expectation that interest rates would stay low and that home prices would go up. There was that expectation. Because there was the expectation that there would be a continual refinancing of these. And that's one of the things that's come to a stop.
There wasn't the expectation that you would -- there wasn't the expectation that you were making a loan that was going to go bust. There was the expectation you were making a loan that would turn into another loan that would turn into another loan.

MR. FLUEHR: As a consequence, CitiMortgage told us, look, we don't even bother to securitize these loans. We hold them in portfolio. They're basically a bridge financing. I mean it was very interesting.

MR. KOESSEL: Nick has talked about the securitization process, and he's talked about the appetite for risk, both at the investor level and also at the origination level, the level of originating loans.

Let's add one more dimension of risk on top of that. It's a risk that you're all familiar with. It's a risk to a poor credit, a credit challenged borrower, i.e., a subprime loan or an Alt-A loan. That's really where the crisis began. It's -- apart from the credit crunch crisis is the subprime crisis that we're all familiar with.

Just to get clear on our definitions, a subprime loan is a loan that is made, in theory, to someone with a FICO score of 620 or below. Recent evidence has shown that a lot of those loans were actually made to people
who are eligible because of their FICO scores for lower rate prime product. They were put into an improper loan.

But a subprime loan, in theory, is a loan that's made to a poor credit, 620 or below, and it carries a higher interest rate because of that. And frequently also, there's a premium paid to the originator for originating a high-rate loan. In fact, one of the quotes here is, "At its simplest, subprime lending can be described as high-cost lending." It's high-cost lending. It's high cost to the borrower.

Alt-A loans are a slight deviation from that. An Alt-A loan is typically a person who doesn't have a historical credit problem. They may have no -- or a limited credit record at all, but they don't have an obvious credit problem, but there's something else lacking in the application process that puts them in something subpar not -- excuse me, subprime, nonprime. Typically what that -- what's lacking is full documentation of their income. It's a stated income very frequently. Not always, not a hundred percent, but very frequently.

And the other thing that can be said about each of these two loans is that in both cases in 2005, in 2006, 70 percent of each of these two categories were
hybrid loans. They were loans that had an initial
teer rate for a period of two, three, in the case of
Alt-A loans, five years, and then reset at a variable
rate mode, and the expectation was that they would reset
higher.

MS. JAVITS: Is this why you hear so much that
the vast majority of people who got subprime loans could
have gotten -- not gotten subprime loans, but they did
because they couldn't provide income verification or
something? Is that -- is that the source for that?

MR. KOESSEL: That's -- that's more typical in
the case of the Alt-A loan is that they chose, for
whatever reason, to take out a higher cost loan because
they didn't either have documentation or didn't want to
provide it. Those loans are sometimes colloquially
referred to as liar loans because there's increasing
evidence not only that people were put in the wrong
loans but also that people sometimes lied about their
income in the process.

MS. JAVITS: So is it the case that most of the
people who ended up with subprime and Alt-A loans could
have qualified for --

MR. FLUEHR: I don't know if I'd say most, but
there's evidence that a significant number.

MS. PARKER: Mike, I thought it was more true of
subprime as opposed to Alt-A, the groupings.

MR. KOESSEL: Right.

MS. PARKER: So Carla, I think that there were people, from what we've heard, that got subprime loans that could have gotten prime loans, but the Alt-A group is a different group. And we don't talk so much about the Alt-A group because we spent so much talking about subprime.

MR. KOESSEL: One of the reasons we don't talk about the Alt-A group is because the crisis there hasn't quite hit yet. People -- for the first time in the last month or so you hear the head of the FDIC talking about, hey, behind this there's another crisis about to hit us. It's the Alt-A crisis. Most Alt-A loans are 5/25 loans. Their rate resets haven't hit yet. We'll come back to that in just a second.

MS. GALANTE: I just want -- along the same lines, one of the pieces of lore that you hear is that one of the reasons that people took these loans is because this is what the mortgage companies were pushing and that the rate structure was such that they, you know, got more money to make these loans than to make other loans, so that they didn't educate people -- they weren't incentivized to educate people about alternatives. Is that --
MR. KOESSEL: That seems fair. One of the criticisms you hear is actually that they were paid more to originate a high priced loan, a subprime loan.

MR. FLUEHR: You know, there's a chart that we'll come to later on. The fact is that there's blame --

MS. GALANTE: All the way around.

MR. FLUEHR: -- many different -- borrowers were looking to take equity out. Appraisers -- I mean we'll get to that chart, but there's no one party, I think, who warrants all --

MR. KOESSEL: Fitch did a report. Fitch is a rating agency, and they did a report in November. And they decided to go back and ask how could they have been so wrong about this stuff. And they went back and they inspected 42 loans. And they found evidence of fraud either on the borrower's part or on the lender's part in all 42.

MS. GALANTE: Wow.

MR. KOESSEL: Flipping the page, so we're not only making -- we're not only making riskier loans, IO loans, loans that have payment shock, as they put it, loans that have variable -- you know, the interest rate and the payment may go up in subsequent years, very, very low down payment loans, loans that are taking out
equity positions and constantly keeping the loan to value ratio at or just under a hundred, sometimes above a hundred. Some people are taking out more than actually the house is worth because there's the expectation that prices will continue to go up.

But in addition, we're making loans to less and less creditworthy people. As the -- as the -- as 2005 became 2006, we'll come back to this, increasing loans are being made to people who not only couldn't make the payment once the loan reset, they were having a hard time making the loan a month or two after it was originated while they were still in that initial teaser rate.

If you flip the page here, you can see at the subprime level, the risk profiles on subprimes. So you're making loans to people with bad credit, by and large, not universally. You're increasingly making IO loans. That's the upper right-hand graph. It's interest-only loans which have their own set of risks associated with those.

You're making higher and higher LTV loans. Go back to 1998 to CLT of about 78, and it's ramped up to -- higher up into the 80s a few years later. More and more piggyback loans, loans that have got a second, contributing -- an additional loan to contribute the
equity, as opposed to coming out of the borrower's pocket.

And then down here in the lower right-hand corner, low documentation loans. And I think one of the most telling statistics is percentage of income that's going to pay the loan. It used to be the case that percentage of income was somewhere in the 35-, 36-, 37-percent range. Increasingly it's 42 percent. And that's the average.

That means that you're probably seeing loans increasingly where they're taking 50 percent of one's disposable income, and this may well be a loan that when it ramps up and the payment ramps up is going to take more. You can't expect that borrowers are going to be able to sustain those loans for a very long time.

The upside of all of this, flipping the page here, is it increased homeownership. For about 35 years, homeownership really didn't change much. It stayed at about the 64-percent level until about 1994. It actually, interestingly enough, corresponds with the beginning of use of a lot of these higher risk, more innovative or, pick your term, exotic loan products. And it ramped up in '05 to about 69-plus percent of the American population was now a homeowner. That was an important political emphasis, and most people thought it
was a very, very good thing.

As Nick pointed out, however, very little of that probably ultimately had to do with the subprime. A lot of the subprime itself had to do with the equity takeouts and accessing the value of the house.

Today's crisis with respect to the subprimes is largely a product of the fact that in 2005, 2006, there was this incredibly expanded use of subprime products to originate mortgages. It rose from about 13 percent of the overall mortgage market in 2001 to about 30 percent of the mortgage market in 2006, 2007. And 70 percent of these Alt-A subprime loans were the hybrid loans facing resets.

Now what's happening and what's started beginning with last year is we've commenced on these loan resetting. People see their payments going up. They're experiencing payment shock. And they can't -- they can't stay in that loan. They have a choice, a choice between selling the house and taking the loan out, refinancing the house, if they have equity. That was always the expectation is that that would be the case. Or if interest rates had stayed low, then conceivably they might have been able to make the payment.

None of that to date has been the case, though
some of that may be changing. What may be changing is interest rates may be falling. It doesn't look like home prices are going to continue to go up. It's quite clear that that's a trend which seems to be on the rise.

If you flip the page here, additional product here with taking out your prior position, that is refinancing your loan, is that so many lenders have pulled back in their credit criteria. They've just pulled out of the business entirely. It's harder and harder, especially for subprime borrowers, people who have had credit problems, to actually get a loan.

Interest rates until just recently have been up. They started to fall back. Home prices are way down. All of that -- all of that is a problem. And that's what's feeding into the current crisis. We'll come back to that in just a moment.

MR. FLUEHR: So now we're going to get into some of the specifics with respect to California, some hard data on California.

Obviously, there is not, I think, a good description of the market dynamics that facilitated this whole thing. You know, the fact is that low interest rates, I think, contributed a great deal. You can see this top bullet, it's interesting that a rate reduction of 300 basis points, say, from 9 to 6 percent, allows
the home price to be 33-percent higher.

So the fact is that if you look at kind of this bottom graph of the ten-year Treasury, the fact that we had generally falling rates throughout, you know, from the early 80s through today, that has facilitated both an increase in homeownership that we saw before, people being able to buy more house, but it's also caused, as you can see in the graph here, a ramp-up in -- a significant ramp-up in home prices.

That has occurred, you know -- it dramatically outpaced population growth. We can see here that building cost index is actually building cost for the most part declined.

You know, the other factor that was going on here is sort of the whole irrational exuberance if you will, the bubble notion. As you can see here, there's a -- we show this graph GDP versus housing valuations. You can see that there's a very tight, very good correlation dating back to 1960 really until we saw those rates starting to -- that fall off in interest rates in 2000. There you start to see these housing valuations diverging dramatically from GDP.

And you take Florida, for example, I mean you go down there and you have college students saying, you know, I'm not going to get a job. I'm just going to
put -- you know, option out a condo. I'm going to go in
on three condos, and I'm going to flip them in a year,
and that's how I'm going to make my money. And a lot of
people for a number of years did very well doing that.
But obviously, it's, again -- it's all about timing, and
there's a lot of people in Florida now wishing that they
had nothing to do with the condo market.

MS. PARKER: I was telling Nick and Mike this
last night because I heard it when I was in Washington
last week, in Pensacola, Florida, there is 80 months of
condo supply in the market in Pensacola, Florida. So if
you're trying to sell a condo, think about your window
of getting that sold. Five-plus years. Eighty months.

MR. FLUEHR: And, again, it's all about, you
know, sort of opportunity cost of your money. What do
you want to do with your money? As you can see, the
middle part here, you can see that analyzed rents
roughly fluctuate between 5 and 5 and a quarter percent
of home prices.

That, you know, dropped here to, you know, third
quarter of 2007 to 3 and a half percent, a decline that
obviously homeowners are generally better off renting.
They'd have more free cash flow to do things with by
renting. And so obviously the prediction here is until
we see that those rental rates climb back up, until the
inventory is digested, we're probably going to have a problem with property values.

The next graph looks at home price appreciation. Obviously you guys here in California, as you can see from the colors in this graph, obviously the orange, red and yellow are sort of above average home price appreciation. The green areas are sort of static, if not low price, low price appreciation.

So we've seen dramatic increases in home prices on the -- on the Pacific Coast here. Arizona. Obviously big problem in Nevada, one of the other states that has big subprime issues. Florida as well. And up in the East Coast as well.

But, you know, the fact is where the auto industry had problems, the Midwest, the centralized United States, they haven't enjoyed anywhere near the price appreciation that you guys have, although, as we'll talk about in a minute, they certainly have their share of subprime issues as well.

This kind of just takes a look at California. This compares national average home price appreciation for California. In the upper right-hand box here you can see that obviously you have outpaced virtually every other state in the nation. Down here you can see one of the other high growth, high price increased states,
Florida. Their increase wasn't anywhere near what yours was.

You take a state like Ohio, where again they're having horrible economic effects because of the auto industry carnage, you can say that they have actually had dramatic price decreases while you enjoyed these price increases.

I apologize for those of you out there who don't have the books, but this takes a look at subprime volume. And we sorted this by different -- by different measures. These are really the statistics that Terri talked about where we have been sending them to you guys to give you an approximate -- sort of see how you compare versus other states, looking at various zip codes, how you compare various different areas of the state. You can see, unfortunately, and, you know, I guess not, kind of logically, you guys do have the largest volume of subprime loans, just under 200 billion of subprime volume. You're the number one state in the nation in terms of subprime volume.

The next --

MR. COURSON: Nick, are subprime loans defined the same way you previously defined them in the book?

MR. KOESSEL: They're defined as high-rate loans. They're defined as loans with -- that are two or
three -- at the point of origination had a yield of two to three points higher than prime.

MR. COURSON: So not credit.

MR. KOESSEL: It's not credit rates.

MR. COURSON: It's FICO based.

MR. KOESSEL: It's FICO based.

MR. FLUEHR: And the other thing, John, just on the -- this data we get on performance, this only represents -- this is securitized loans, and it's only about 85 percent. So it actually, if anything, understates the volume by about 50 percent.

MR. KOESSEL: You state somewhere else that the total volume of -- outstanding volume of subprime loans in the United States is about 1.4 trillion out of the $10-trillion market -- you know, $10-trillion mortgage market, overall mortgage market. So this represents a pretty sizable share of the overall. It's a good sample space.

MR. FLUEHR: The next page here we just look at -- this is sorted by subprime per capita. You can see that fortunately you fell off the No. 1 ranking. You're No. 2 ranked here. Nevada actually has the highest subprime loans on a per capita basis. This we sort by seriously delinquent. Here you're ranked as the fifth sort of highest state in
seriously delinquent. We're defining seriously
delinquent as 90-plus days or more of delinquency or in
REO/foreclosure status. And you can see that the
interesting, worrisome number here is that, you know,
20 percent of those subprime loans are seriously
delinquent right now. So it's an enormous number when
you think of the billions of dollars that we have --
that you have in subprime.

Another arguably worrisome number is the change
of month to month. This just looks at the change in
seriously delinquent loans from November to December.
You can see that California ranks No. 6 on this chart.
You had a 12-percent increase in seriously delinquent
loans just in a one-month period of time.

The other, I think, take-away here is you look
down this column, obviously not a single state in the
nation has actually improved. Everybody has gotten --
delinquencies have only gotten worse in every single
state in the nation.

MR. KOESSEL: If you were to extrapolate out
that number, you'd have at this time next year over 50
percent of your subprimes would be seriously delinquent.
If you were to extrapolate out those numbers, you'd
have over 50 percent of your subprimes seriously
delinquent a year from now, which is pretty significant.
Obviously at some point it starts to taper off and we've already begun to see California begin to taper off. Still, the problem is enormous.

MR. DAVI: I have a question. I have a question for you. You said if you forecast it out. Are you predicting it will reach that 50 percent?

MR. KOESSEL: No.

MR. DAVI: It won't. Okay.

MR. KOESSEL: No, I'm just saying --

MR. DAVI: If you did interpret --

MR. KOESSEL: -- if the rate is increasing 12 percent a month --

MR. DAVI: Yes.

MR. KOESSEL: -- you're going to see it more than double.

MR. DAVI: I understand.

MR. KOESSEL: And by the way, it has gone from about 12-percent seriously delinquent in August to a 20-percent in December. So in the course of four months, it has come close to doubling. I don't expect it to continue to rise at that level.

MR. DAVI: Okay.

MR. KOESSEL: Nick pointed out that we had a bubble. You would have thought just looking at the line
going up exponentially after it had moved in a linear
fashion for so long for so many years that that would
have foretold a bubble, but we're seeing it now. We're
seeing the aftereffects of the bubble. One is
increasing inventory, increasing months supply.

Right here we're seeing -- this is slightly
dated, maybe a month or two old -- nationally a month's
supply of mortgages is approximately ten months. John,
you may have a better feel for it. My guess is it's a
little bit higher than that.

MR. COURSON: I think it is.

MR. KOESSEL: At this point probably 12, 13,
something like that. We expect that to continue to
rise. One of the things -- one of the features of a
credit crunch, of a lack of liquidity, is a huge
separation between bid/ask prices. And that's true, not
just of the credit crunch generally, but there's a huge
discrepancy between what people think a CDO or an MBS is
worth and what people are willing to pay for it.

This is also very much true in the housing
market. There's a huge discrepancy between what sellers
think their house is worth based on prior market
experience and what buyers think their house is worth
based on the trend lines that are now tending down and
the expectation that we are in crisis mode and that
prices are going to fall dramatically.

Speaking of that, you see over on the right-hand corner, you see the decline in prices year over year. I think December decline on prices over the prior December average price was about 10 percent.

A little bit back, a month or so ago, Moody's Economy.com predicted that the overall decline in prices would be about 12 percent. If the 10 percent is already in place and they're only expecting a 12 percent, we should see near the -- we should see the bottom at some point in the near future. At the moment, no one is seeing the bottom. No one is predicting that we're that close, and people have started revising the numbers with respect to how far prices might fall. Currently I think the current wisdom is more like 25 percent on the national level.

MR. COURSON: And that -- don't you -- is it your opinion that that bottom certainly will be different based on geographic?

MR. KOESSEL: Absolutely.

MR. COURSON: Go back to your red, yellow, green, and you've got to believe that the reds are -- their bottom is further away and deeper than the --

MR. KOESSEL: I think the general sense is that places like California and Florida will see more than
25 percent from the highs a year or two ago, that	hey'll see a more significant price decline.

I think also just because of the particular
economic -- their economies, places like Michigan and
Ohio will also probably see very, very high levels fall,
even though they're not coming off of highs. The
interesting question really becomes -- this we'll come
back to -- if we are entering recession, how deep is it,
how long will it last and what kind of multiplier effect
will that have on home prices. This is the snowball now
rolling down the other side of the hill or something,
but it's that sort of snowball effect.

The next page kinds of shows you a rough way of
how we go about calculating what the losses might be.
And one very simple mechanism is to try to forecast what
your foreclosure rate may be and what the loss is likely
to be on a house. Based on a foreclosure rate of
25 percent, and you saw that I think the national
average back there -- I can't remember what it was a few
pages back -- was 16, 17 percent, something like that.
California is already close to 20 or above 20. Some
places are above 25.

If you do have a foreclosure rate of 25 percent
and you have 40-percent loss, then the real losses on
these mortgages will total something like $140 billion.
We're just talking subprimes here, not any kind of ripple or carryover effect in the prime market.

There are more difficult, more strenuous stress scenarios that forecast higher foreclosure levels, greater losses. Both of those are really unknown variables, but obviously that's a significant amount of money that's just going -- that's just evaporating.

At this point I think the question we're trying to at least help people understand is what this all means from a broader perspective. This overaggressive lending -- and I mean that in the broadest sense possible -- overaggressive lending in the housing market, it's now carried over into the financial markets and it's having all sorts of financial implications, as per our first few slides where we said that the financial world has been turned upside down.

This all sort of started last spring when you started seeing lenders who had originated -- been very aggressive in the subprime market in '05 and '06, they saw their last vintage, their latest vintage loans starting to go into default within months of having been originated. The buyers of those loans could put those loans back to the investors -- excuse me, to the originators, and they started to do that.

That hurt a lot of originators. They didn't
have the cash to buy these loans back. They needed to place them, and they couldn't place them because these loans were so -- such poor credits. That was the first indication that there was something seriously wrong.

In the course of the last nine months, that's rippled through the economy in a number of ways. Nick mentioned the hedge funds. In early August they couldn't price certain CDOs. That had a huge impact on the markets, scared the market enormously. And since that time, there have been a number of other ripple effects.

You can see it in the behavior of the Fed. It's not very hard to see there. You can see it in what's -- what are called the monoline insurance companies. These are the insurers who have typically devoted most of their resources to insuring municipal paper in the housing market and outside of the housing market. But a few years ago they started insuring elsewhere, and we'll come back to that, and they're starting to see -- take capital hits.

And obviously anybody holding any of this paper like CitiGroup, like a number of other banks, are also taking capital hits. They're starting to reevaluate the value of their portfolio based on the sort of numbers that we saw in the prior page, doing those sort of
analytics and others as well.

If you flip the page here, the real crisis began when the highest rated AAA tranches and CDOs fell off the shelf. If you look at the upper right-hand corner, there's something Nick mentioned earlier. With respect to the lowest rated tranches, you expect to see some losses there. You expect them to be gradual. You know that a subprime product is going to see a higher rate of foreclosure. You know you're going to see some losses.

But when the highest reaches, the AAA, started to see problems and they started to see them very, very, very early on, within months of their origination, that's when they knew there was a problem. And that's what happened last summer, and that's what precipitated initially the credit crunch last summer, and it's carried on since then.

If you flip the page, one of the ways in which the markets try to get a handle on the housing world is by looking at an index, just the way you try to get a handle on the stock market by looking at where the Dow is on a given day. It's an index. It's an indicator of where the stock market is. There's something called the ABX index, and that's an indicator where the housing market is, and you see those -- that fall-off there.
There are two things that are key here. One is the degree to which it's fallen off in a very, very short period of time. And second is the dark blue lines represent that part of the ABX index which is concerned with the most recently securitized mortgages, mortgages from the second half of 2006. And those have seen the greatest price declines.

It's just verification that this increasingly risky lending behavior on everyone's part, this greater interest in risk, greater interest in risk premiums, with less concern with what this might all mean, that that accelerated to the end of '06 and that stuff is now -- as you can see here, that's now showing significant declines because of that.

I'm not going to spend a lot of time on the next two pages. They're interesting, but this is the -- the tentacles of this crisis have been extended further, and they're now wrapped around the so-called monolines. And we're seeing a lot of disruption in the municipal markets because of this.

Basically the monoline insurers decided a few years ago that one way to get into something a little more profitable, lucrative, I'll use the word "sexy," a little more sexy than municipal insuring was to get involved in credit default swaps, and they started
taking risks there.

You don't need to know a lot about credit default swaps. It's basically a form of insurance that they were offering. Bottom line there is that they got in over their heads. They wrote -- they wrote swap policies out -- on credit default swaps that have now jeopardized their core business. A business that was very stable, they were well capitalized for, they've undermined their capital position.

And what this means for a lot of municipal issuers, and it has broad implications throughout the market because of the size of the municipal market and the number of places that hold municipal bonds, especially short-term debt is the kind of vehicle for cash, is that it's freezing up or seizing that market. It's creating an enormous amount of discomfort in that world because of that.

Fitch has downgraded a couple of the monoline insurers from the AAA level to the AA level and MBIA -- the two that they've downgraded so far are AMBAC and FGIC, and MBIA is on watch.

MR. FLUEHR: I think this is -- you know, when we talk about the globalization and the fact that these monolines, again, were really municipal players predominantly until recently, and we talked -- I
mentioned this whole search for risk or reward, the fact that we have hedge funds very active in the markets these days, they look back at these monoline credit default swap rates here in the early June, and he said, jeez, we think that these are really undervalued. In other words, nobody thought the MBIA, AMBAC, FGIC, any of these guys would default, but, you know, a lot of the hedge funds said, jeez, we can't buy credit default swap, this form of insurance. These kind of low basically negligible premiums, we want to make a bet that it -- you know, the credit markets are going the way we think they are, we're going to buy -- we're going to buy up some of this exposure here at these levels.

And obviously you can see that those bets proved to be very, you know, lucrative in the long term. Those spreads have widened. People have, you know, made 20 times their investment on the credit default swap market. They're also, obviously, trying to -- they want this to occur, so in the stock market they may be shorting MBIA and AMBAC's stock, putting pressure on dumping shares, trying to create, you know, this sort of market uncertainty.

So I mean it's all interrelated, and, you know, it's so -- it's -- you know, there are people out there who are trying to cause these. I mean they are
profiting from these declines.

MS. PARKER: It's important just for the Board members to know this. We've been looking at this because we do have some of our financial instruments involved, and there's an irrationality by investors in the marketplace. So these aren't even logical actions. They're irrational actions. And in that sense, it's just not a matter of looking forward, but managing the investments that the Agency has for the past bonds. It's a very active, involved in the time from the standpoint of looking how this portends for us and business going toward.

MR. KOESSEL: Speculation obviously drove the irrational exuberance of the housing market on the way up, and what we're seeing here is that a degree of speculation in a very large global market, the credit default swap market, is largely -- well, not largely, but it is playing a significant role in driving prices down and driving a downward spiral.

We started out talking a little bit about what the losses might come to. If you look at the losses, the potential losses in housing from the standpoint of the ABX indexes, they would be significantly higher than the ones that we highlighted, 40-percent loss or -- $200 million with a 40-percent foreclosure rate, meaning
40-percent loss of houses. These ABX indexes have literally dropped so dramatically that when we start looking at them from that perspective, the consequences are dire. They probably overshot. I don't know if that's helpful.

MR. FLUEHR: And I think just the only point on this page, we talked about these credit default swap market. Mike, as he mentioned earlier on an earlier slide, the total value of residential real estate in the United States is $20 trillion. Roughly 10 trillion of that is mortgaged. It has loans associated with it.

If you look at the size of the credit default swap market, which obviously people write credit default swaps on anything, you know, the euro, the Japanese yen, companies, but it's $45 trillion is the size of the credit default swap market. So that's just an enormous, enormous number.

The fact is that you had some of these monoline players on the previous page, we talked -- there was a bullet that said that ACA has been downgraded to CCC. You can see here ACA wrote $60 billion of credit default swaps. I believe their capitalization is like $2 billion.

So my worry is that you've got 45 trillion of those credit default swaps outstanding. You've got
hedge funds that are playing and trying to profit from
market disruptions. And you've got players that
arguably took on more exposure than they should have.

And that's why we're seeing the kind of market
disruptions that we are these days, where people have
made arguably irrational decisions. I mean they're
saying I don't want to have -- we traded some long-term
bonds the other day where basically it's identical
credit bond, same issuer, the one had AMBAC insurance,
the other didn't. So it was only just an add-on to have
the AMBAC insurance. And the one with the AMBAC
insurance traded 30 basis points cheaper than without
AMBAC insurance. You know, it just doesn't make a whole
lot of sense.

MR. KOESSEL: The question people always ask is,
you know, how does this compare with the prior crisis?
And just speaking anecdotally, Nick and I were talking
earlier, and, you know, I'm relatively new to the
financial industry. Nick has been in it 20 years. But
it doesn't compare with anything we've seen before.

One point -- two points of comparison are the
dotcom boom and bust of the late 90s early 2000s and the
other is the S and L crisis. Both of those were
sizeable in terms of the losses. I think that when we
look at the $200-million loss number that some people
have assessed on just the subprimes themselves, I think -- I think I'm very conservative -- excuse me, not conservative numbers. I think they're somewhat dated.

That corresponds roughly with the S and L crisis. The S and L crisis was a little bit bigger. It was spread out over a longer period of time.

The dotcom bust lost about $6 billion -- trillion in market value in a relatively short period, about two years. We're not talking about that sort of loss on the home real estate market. The big difference here is that most people borrow their homes, so this is a heavily leveraged market.

And what that means in this market is that the assumption has generally been in the past that people don't walk away from their homes unless they really can't afford them anymore. Then they walk away.

However, if you've taken out a loan on a home and you find that loan is under water, that is, you're paying more on that loan than your home is worth, there's a reasonable likelihood that you're just going to close the doors and walk away from that. There's no point. You're paying more on that loan to live in that house than you would pay rent or to go live somewhere else given that homes prices have fallen. And that's the real danger in this kind of prolonged and
significant crisis with respect to housing itself.

MR. FLUEHR: I guess the sort of final question of this section is where do we go from here? What does the future portend? I mean obviously we have seen the Fed take some very dramatic action, unprecedented action, in lowering their discount rate by, you know, one and a quarter percent in just a week's time.

That said, we've seen some, you know, continued negative news, unemployment, you know, business inventory, consumer spending decreasing, fuel costs increasing, household wealth declining, et cetera. So if we have a recession, the question is, you know, what does that do to our models? Is it going to get even worse than sort of the projections that we've seen here?

You know, and the other question is how long will it go on for?

You know, again, the numbers are pretty staggering. The question is what do you do about this, which is really the next question.

I don't know if this is funny or not funny.

On the question of what is to be done, when we were up at our Armand (phonetic) sort of corporate facility, we were talking about this with HFAs around the nation. We talked a little bit about having the subset of borrowers in the subprime space specifically
and how there's really -- you can't generalize with respect to the borrowers.

I talked about at the beginning sort of assessing blame. You can see here that, you know, really a lot of people were to blame for this crisis. And you can see everything from, you know -- you can point fingers all around. The fact is we're in this situation now, and the question is how do we deal with it?

Going back to my pie analogy, you're going to have borrowers who are arguably prime borrowers who were put into subprime loans who probably do have the wherewithal to get out of those subprime loans and refinance into a prime product. So, you know, they're at the kind of easy to figure out sort of side of the equation.

The intermediate side are those question -- are those people who can't afford the resets. The rate is going to reset, probably very soon given the graphs that we saw on how many loans are coming up for reset here. And that is really the pool that I think for the most part some of the initiatives that we've seen on the federal side and even with the state HFA side have been addressing.

And then finally at the, you know, far end of
the spectrum are the borrowers who, you know, as Mike pointed out, were having problems from the day they were put into this loan. They arguably should have never been given a loan in the first place. They shouldn't -- you know, they should have been renters. They should have not been homeowners. And really there's nothing that we can do to help those people.

So the -- I think, you know, again, at our Armand meeting, we talked about the filters that you apply to essentially screen those borrowers down to the ones that you want to serve. And I think that's actually the tough sort of policy question is to -- you know, arguably you don't want to necessarily help that person who bought the big flat-screen TV and bought a boat and refinanced their house three times and is in trouble now. You want to help the person that, you know, is having problems.

MR. KOESSEL: We talked a little bit here -- do you want to flip back to those filters. We talked a little bit here about some of the government initiatives. We talked basically about two of the major initiatives. One is fed regulations that would include money practices somewhat akin to selling someone a security. You would exercise greater caution to make sure that you're putting them into the right product.
That's certainly one alternative, and it certainly has its virtues. We're not here to endorse it or criticize it so much as to just state that there's a real initiative. Some people felt that the Fed was just too lax in its oversight responsibilities with respect to lending.

Second is a plan that probably most people in the room have heard of, it's been on the front page of the paper a lot, which is the New Hope Alliance (sic), or sometimes people refer to it as the Paulson plan, which for a certain segment of borrowers who are facing rate resets beginning right now and going on, I believe, for the next three years, it's a relatively small set of borrowers, but for that class of borrowers their rates would be frozen at their prior so-called initial teaser rate.

So assuming that they could afford their payment before and they can afford it going forward and that they meet certain other parameters, no more than a certain amount of equity in their home, they have FICO scores that have to meet a certain level, they would qualify for this so-called fast track rate freeze. That's a second -- second class of solutions.

And there are many, many more having to do with bankruptcy law. It's really kind of hard to keep up...
with everything going on, but one of the things that
we've actually worked most closely with Terri and Bruce
and Steve and folks here in trying to think through, if
CalHFA, like other HFAs in the country, were to use some
of its volume to try to do anything, how would it target
the program? That's a gigantic if because the magnitude
the problem that you're seeing is just enormous in
California.

But in trying to think about these things, we
put together a little chart on page 48. And this is the
simple chart. This is the idea that you go in there and
you ask yourself the question. Well, we've got good and
bad borrowers and we've got good and bad loans. And you
certainly want to help the good borrower who was put in
the bad loan. They certainly seem to be deserving of
assistance.

MR. PAVAO: Well, is this a pretty tough
analysis to figure out which box they go in, or is it
actually pretty simple when you've got a case-by-case
basis?

MR. KOESSEL: I think it's rather hard. I think
it's really hard.

MS. PARKER: I think if you ask the question
given this model of the HFAs that are doing this, I
think they would tell you it's extremely difficult.
MR. KOESSEL: But a lot of HFAs, the first thing, you know, the population is going to ask you is why are you helping that person? Well, nobody helped me with my loan. So you almost kind of have to have some justification of having gone through this thought process.

The bottom line of this frankly is I think it is very, very hard to discern. And, frankly, in many cases, it's just impossible to discern, number one, and number two, the bigger thing is that this -- the magnitude of the problem is so enormous and it has so many -- if you don't help borrowers, the social cost is just enormous, and that's really what the next page is --

MS. PARKER: Maybe it's a preface. You know, I think we have said to you over the last six months, we've looked at this. We've tried to come up with good ideas. I didn't -- you know, I tried to say I don't know how good they are, and I think some of these questions may be evidence of that, why we haven't been able to come back. So the thing that's maybe kind of the bad thing is that even our best ideas, we have said to you, we don't think they're viable in this environment.

MR. PAVAO: I guess my question was getting at if this is a pretty good lens through which to view this
problem and there's maybe a strategic way for us to intervene, my question was just technically how difficult is that, even if you think strategically there's this slice of the borrower population that we want to help, technically how difficult is it to identify that population and sort this out? It sounds like technically it's difficult.

MR. KOESSEL: I think it's very hard. I think it's very, very hard. I think you do have a second -- there's another question there, rebounds, which is -- well, flip the page to page 49.

Declining home prices and rising rates of foreclosure are going to impact lots and lots of people. Whether or not they were good or bad borrowers, whether or not they took out a loan at all, people are going to be impacted. Whole communities are going to be impacted.

This just lays out a few statistics, but I mean obviously when homes are foreclosed upon and sit there empty, that affects everybody's home value, whether you took out a good loan or a bad loan, whether you were a participant in this whole equity take-out hype of the last few years or not.

You know, it hits tax rolls. It hits communities. It impacts crime rates. There's one study
that indicated 1-percent increase in foreclosures increases violent crime by over 2 percent. And the quote here that mentions Sacramento: "Reports from Cleveland, Atlanta and the sprawl around Los Angeles and Sacramento from low income city neighborhoods to middle class suburbs all tell a similar story: When vacancies appear, so do looters, vagrants, prostitutes and drug dealers."

So it's almost like you can focus in on whether or not this borrower is deserving or not, but the problem is so enormous and it's so difficult to ask that question. I mean, for example, was -- you'd have to filter through. What about the person who encountered healthcare problems and they started borrowing against their home and they ran into problems like that, and they took out more and more equity out of their home and they developed credit problems and they turned to a subprime loan and now they're going to lose their house. They clearly were taking out equity, but you have to distinguish them from the person who bought a big-screen TV with their equity take-out.

It's a very, very difficult thing to do. It's very expensive because each transaction has to be assessed and the history of it has to be assessed.

MS. PARKER: You know, I think I told you at one
of our meetings that, again, Massachusetts has put a program together that's done very few, if any, loans, but very -- probably, I think, one of the most thoughtful, the work that's been done. And they've been working on -- they're actually in Phase II of the program.

And they hired counselors to essentially go through and interview. And one of their criteria, at least at the beginning besides credit and other kinds of things, was whether or not -- did the borrower know, that they were consciously aware of it as being a subprime loan and everything that that meant, because they were -- that was a -- if you checked that box, then you were not eligible, because you knew what you were doing and you're responsible.

And they found that in that particular case, that that pretty much wiped out most of anybody who would have -- that they would have had further discussions with. So, you know, you start going through these screens and -- and I think that's trying to deal with the existing people in these houses.

But aside from all that, at the end of the day from an economic standpoint, we're going to be sitting here with this huge inventory of houses, loss of property tax, impact on the state budgets, schools, et
MR. PAVAO: And do those two dynamics warrant at least two different strategies as in we're talking about a strategy of sort of a -- for lack of better phrasing, sort of a homeowner rescue strategy, but then there's got to be a separate almost community development strategy around vacant, flighting, housing stock, what do you do about that. And maybe the answer to that is homeownership, and maybe it isn't.

MS. PARKER: Well, I think we would all say there are so many levels of need that anything that might work in this environment.

MR. FLUEHR: The one take-away I thought from -- and again, we had a whole session with CitiMortgage and the subprime servicing segment. They talked for a while about what they were doing to try and address this problem. Because the reality is that even with a loan modification, when you look at what you lose in the foreclosure process, they're better off -- they would rather modify the loan and lose that future income and keep the loan than have to go through the foreclosure process and not to mention the ripple effect if this -- again, if the snowball starts rolling.

MR. PAVAO: I'm sorry, this was the note holder speaking now?
MR. FLUEHR: This was, yeah, our servicers, yeah, exactly.

The take-away that I got from our -- what was successful on the HFA side was sort of the initiatives that you talked about right before we talked of outreach to these borrowers, because a lot of them just -- you know, it's like deer in the headlights, but they -- you know, they see the car coming, but they just -- it's like I don't know what to do and they don't even know that they have any options. A lot of times they are -- you know, they're out of options if they've reached the point where they hit the reset, they don't have the money, and it's too late at that point.

So I think both the HFAs that have -- like Massachusetts, they've partnered with a lot of the local not-for-profits to counsel borrowers, to outreach to borrowers. That seemed to be true of a lot of your peer agencies that have done that, getting the information out there and partnering even with the for-profit entities and saying, hey, you know -- I mean I had a call last week where I got SONY Mae, State of New York Mortgage Agency, together with our counselors. And SONY Mae wanted us to send out sort of SONY Mae sort of flyers and advocating their subprime loan program, which, again, has done really nothing.
MS. PARKER: Two, maybe.

MR. FLUEHR: But they feel like they need to be doing something.

MR. CAREY: And I think I heard that Connecticut has done zero.

MS. PARKER: Well, yeah, and the only thing is, you know, in some defense of my colleague in Connecticut, they only started their -- they're one of the last states to start it, so their program is only a month or six weeks old. So compared to New York and Ohio and Massachusetts and Michigan, they are the most recent states to enter this.

MS. GALANTE: I'm trying to -- back to my question earlier because I'm trying to understand this. Even if you can understand who is a borrower that might benefit from a modified loan, is there -- you know, is there somebody at the other end for them to actually --

MR. KOESSEL: Speak with.

MS. GALANTE: -- speak with?

MR. KOESSEL: Increasingly that seems to be the case. Somebody asked earlier is there any bright side to what we have to say at all, and I thought of one. Home prices fall enough, and it's in everybody's interest it to leave that person in their house regardless, whatever you have to do to that loan. So
there's a bright side here. Home prices just fall a little bit and you have to raise the question, well, is the investor -- do you have to make the investor whole? Do you have to pick the person out, dispose of the house and pay off the investor?

They fall enough and that's a no-brainer. The investor doesn't want that property. The home price has fallen so much that they want the person to stay in that house and take care of it.

Increasingly with home prices already declining 10 percent, some places significantly more, the holder of that property, the person who really owns that property doesn't want that property. They want the person who's living in it taking care of it now to continue to live in it and take care of it.

So the question stands is there someone to speak to, but increasingly I think the answer is yes.

MS. JACOBS: I have a question, though. Aren't there some of these securitized products where there's insurance, and when you get the insurance paid out -- I think there's some of the securitized products, I've been told. I don't -- I haven't seen one personally -- that have insurance, and the only way the investor can collect on the insurance is if they go through the foreclosure process. So isn't there a part of the
market where there's that pressure?

MR. KOESSEL: That will drive a lot of insurers out of business.

MS. JACOBS: Well, no, I mean I understand that, but isn't that --

MS. GALANTE: Part of the problem?

MS. JACOBS: -- one segment of the market?

MR. KOESSEL: That makes sense.

MS. JACOBS: I don't know how big that segment is.

MR. COURSON: Are you talking about mortgage insurance?

MS. JACOBS: No, I'm talking about insurance on the security.

MR. FLUEHR: Oh, I assumed you were talking mortgage.

MR. COURSON: Mortgage insurance is the default of the security, not the individual loans in that security.

MS. JACOBS: But there are no conditions to get to that default?

MR. COURSON: Well, no, there are conditions what a servicer can do to modify loans in that security. That's a contractual arrangement on each of them as to how many they can modify, but the insurance, the
monoline insurance that Nick's talking about is just
insurance against a default of the security.

Now, the loans that are in that security may
have private mortgage insurance on them. And there
could -- and they're -- you can file a claim.

MS. JACOBS: And they have to --

MR. COURSON: Well, but also -- and Chuck
McManus knows better than I do, but the mortgage
insurers are also part of this workout solution too
because clearly rather than pay the full claim, they're
a part of the workout to work with the lender and the
borrower to try to find some --

MR. KOESSEL: Maybe what you're thinking of is
there are credit default swaps people who have taken a
speculative position and they would like to see home
prices fall because they benefit from it.

MS. PARKER: That's back to those people who
especially have this perverse incentive in the market.

MS. JACOBS: Yeah. It's just the different
types of insurance make it more complicated. I mean
obviously there's not one solution, but.

MR. KOESSEL: We were told by the -- in our
market we were told by the people working on this at
Citi, and this may sound self-serving, but we were told
by them that we don't -- Citi doesn't want to hold that
property. Basically if that person wants to stay in that home and they have an income stream and they reach out to us early enough, we can usually work something out, whether it's extending the loan, writing off a portion of it, lowering the rate, maintaining/freezing the current rate, whatever. There are ways of modifying the loan, assuming the person has income and assuming they want to stay in that home and assuming they do reach out.

MS. GALANTE: You know, in all of this you haven't talked home equity loans and how that plays in here. My understanding is a lot of these subprime loans also have, you know, a second, which is a home equity loan. Is that right?

MR. FLUEHR: Yeah.

MS. GALANTE: So that compounds all of this.

MR. FLUEHR: It's another lien on the property, and it's typically a second lien, obviously, behind the first lien, but, yeah.

MR. COURSON: The other problem is -- which hopefully one of the brighter lights is 50 percent of the loans that are foreclosed, the borrower never talks to the lender or servicer. And that -- there's so many more products now and initiatives over the last four, five, three, two months going on, modifications and so
on, that there are a lot of tools that are innovative things happening.

The key is getting to the borrowers and letting them know. And then normally borrowers when they get a call or a letter from their servicer and they're behind on their payments, obviously the thought process is going be adversarial, they want my house, and that's what all this counseling and everything is trying to change, is get them in someplace where they know what these tools are. And if you can get that 50-percent figure down notably, you'll be able to save more houses.

MR. CAREY: I think in all honesty it's been very difficult to talk to the lenders if they want to. The service departments are overwhelmed, and you get nonlanguage speakers, you get 800 numbers that get no place, and so I think that's another piece of the bridge.

I think the other thing in the Central Valley is going to be -- there's going to be a huge amount of houses people walk from. If you have a hundred-percent LTV and your house drops 15 percent in value, it doesn't take a lot of math to say why am I paying --

MS. PARKER: I will tell you all that that's what we're looking at with our own portfolio. Our delinquency rate most recent now is up to 5.9. We're
projecting 20 REOs a month going forward. We're going to be talking to you about this next month when we come back as part of our business plan development. The focus will really be shifting about, you know, irrespective of outside, but our own internal portfolio for REOs for -- on our single-family side.

MR. CAREY: And there's going to be a world of people out there that are no longer first-time home buyers that need homeownership opportunity.

MS. JAVITS: So I guess -- I mean I wanted to ask about that. So I mean if -- if in a sense you can divide up the world into individual people in homes now who are going to lose their homes or keep their homes and so there's a kind of cluster of things you try to do around that -- and at least for now, this HFA is looking at counseling to attempt to connect as many of those people as possible to whatever opportunities are available, period, to keep them -- okay. So there's that.

Then on the other side, and it seems like this is -- I mean in some ways I guess I'm trying to take from what you said there's these sort of externalities in a sense that are almost worse for the overall economy. The individual homeowner losing their home is horrible to them, but what -- so the bad things for the
overall economy certainly are if you have whole
eighborhoods where everybody's property values go into
the tank and the neighborhood goes under, I mean, trying
to come out from that.

So I guess I'm just trying to wrap my mind
around what -- yeah, and I think what you had been
talking about at our last meeting, Terri, was this
interest in HFAs really focusing on our core mission,
which is making it possible for people to get into the
market. And we do that both on the multifamily side and
on the single-family side. I'm just trying to
understand this. Maybe you can shed some light on it.

So -- and meanwhile kind of what the market is
doing is bringing these prices down. Pricing has been a
terrible thing in certain ways for people who want to
get into the market in California. So those prices are
going down. Presumably some people have a job and
can -- but I understand you're saying there's a little
problem between, you know, demand and supply.
Supposedly the pricing begins to bring that more into
equilibrium, and then we have certain tools we can use
to even further bring that into equilibrium by helping
people get into --

MR. KOESSEL: It sounds like what you're saying
kind of that there are two issues here. One is people
in homes who can no longer afford their homes, that they want to stay in those homes, counseling, if you can get them to a lender that says, look, I'm better off with this person staying in this home than owning this --

MS. JAVITS: Right. These larger federal initiatives.

MR. KOESSEL: We can conceivably help those people. Then there's another class of problems populated by people who don't want to stay in that house. They don't want to stay in that house because, you know, it's not worthwhile to them, or whole communities that are just emptied out, all the houses. You've now got empty housing stock.

It's my understanding that the legislation that has to do with private activity volume cap as it's evolved in recent weeks has basically said to HFAs, we need you as a vehicle for home possession, homeownership. It doesn't -- if you want to focus on first-time home buyer, then that may be what you focus on with respect to these empty properties. Or if you want to focus on refis with this additional bond cap, you can make that decision yourself.

Is that consistent with the direction you've seen it go, John?

MR. COURSON: Right.
MR. KOESSEL: You're much more aware of the legislation.

MR. COURSON: Well, that's the form of the legislation that's now in the Senate Finance Committee's amendment they're trying to hook on at 5:45 tonight to the House bill which will either crash and be gone and there will be a second tax bill coming up within a couple of weeks.

MR. PAVAO: Just to keep up with you here, so that second piece is trying to get perhaps new home buyers into that inventory of vacant stock.

MR. COURSON: Well, it does two things. The first thing is we have the right now, through our tax-exempt regular program, if values and housing prices fall enough, there are first-time homebuyers now presumably, as Carla says, that do have jobs and so on who will on the affordability index be able to afford that house. We can make them loans.

Now, we all know that bond cap is dear to us, so depending on how much additional volume there is is our ability to do that with tax-exempt versus taxable funds. That's one piece. So that additional cap over the next three years would help that.

In addition to that, if we can create or use an FHA program authority to refinance borrowers, not
first-time homebuyers, but refinance borrowers who are facing default, we have that tool. So those are the two things that are --

MS. PARKER: To add to that -- to add to that, the thing that's really interesting in going back and that's why we really wanted to have Nick and Mike give you a sense of what's happening in the capital market because irrespective of kind of what we're doing, there's relationships with the liquidity providers who buy bonds who -- you know, who really have to depend on getting the capital to borrow.

And as I mentioned to you the other day, I was back in Washington last week for our negotiations with Fannie Mae for the partnership that we developed with them almost two years ago, and right now Fannie has essentially put additional fees on any loans. One, they've got an adverse market fee, and then on top of that in declining markets, which California is the poster child, they will not do any loan to value greater than 95 percent.

My discussions with them was how can you ban California when there might be some affordability for the first time in almost decades, but that's the perfect storm that keeps happening is that you've got now affordability, but do you have lendable resources and
you have partners and, you know.

MR. COURSON: And do you also have shareholders?

MS. PARKER: Yes.

MS. GALANTE: Can I? You know, this is just a
grain of an idea that I've been working on with a number
of different -- anybody I can talk to, actually. And I
think trying to see whether CalHFA can play a role here
is taking this 200 billion in California, right, and
looking at that more on a neighborhood basis. I mean
obviously there’s some concentration of this. And even
looking at picking, you know, two demonstration places,
one north, Stockton, and -- isn’t Stockton the --

MR. CAREY: Yes.

MS. GALANTE: -- foreclosure capital of the
world?

MR. COURSON: Yes.

MS. GALANTE: And I don’t know where and which
neighborhoods in Stockton, but if you could look at it
as a neighborhood strategy where you are, you know,
maybe going to add some public resources into the mix,
redevelopment agency dollars or something, where you can
create some silent seconds, you know, some shared
appreciation mortgages, something that will add to the
fact that the capital markets aren’t quite ready to
totally flow back into, you know, repossessing these
houses.

MS. PARKER: Carol --

MS. GALANTE: Charitable donations --

MS. PARKER: Carol, I think the reason why we wanted so much to do this today is it essentially sets the stage for next month. When we come back on the 19th, we're going to tell you, you know, what we have as far as those resources that we could do down payment assistance or do special programs with. And, you know, particularly what Bruce is going to tell you about, what's happening with our own portfolio and our need to essentially protect our AA rating.

You know, we don't have the resources that we had last year, so we -- in my discussion with you all, we're going to have to really decide and focus, and I'll give you the preview now, but I think there's going to be some programs we're going to be recommending to you not to be doing that we have done in the past so that we can more, with what resources we have, hone in and try to deal with really what's the highest priority and we think we can get the most public benefit for.

MR. PAVAO: And is some of that thinking geographically based, as in is what Carol's mentioning, distressed neighborhoods with large volumes of these kinds of --
MS. PARKER: Well --

MR. PAVAO: -- properties?

MS. PARKER: -- we're thinking everything.

MR. COURSON: It could be. I mean you could make a decision whether it's really whether sort of throw it up and -- or do you target it and where is the better effect?

MR. PAVAO: It seems like lots of good public benefits could come from some geographic targeting.

MS. PARKER: Well, we --

MR. COURSON: There is likely going to be -- and it's unusual, but I've been told that what -- depending on what does or does not get into the stimulus bill from the Senate side, oddly, you wouldn't think this will happen, that there may well be a second tax bill coming rather quickly through Ways and Means. And normally that doesn't ever happen.

And one of the things that's in there -- well, this initiative would be in the stimulus bill. And the other things they're talking about are things in a funding bill such as CDBG funds to come in and try to save neighborhoods and use CDBG funds to come into the neighborhoods and do the infrastructure type -- not infrastructure, but the demographic type things you have to do in these neighborhoods to --
MR. KOESSEL: Dollars I assume --

MR. COURSON: Correct, exactly.

MR. KOESSEL: Probably money for those programs --

MR. COURSON: Correct. And if you're never going to get it, now is the time to get it. The climate is right.

MR. KOESSEL: Next year a recession.

MR. COURSON: All of a sudden the pay-go becomes less of an issue as how important is pay-go as opposed to the recession and the economic benefits or the impact on our economy. So I think there will be another bill. Those kinds of things go right hand in glove --

MS. JAVITS: Can we -- I mean so there's 763,501 loans outstanding, loans at risk, subprime loans in California.

MR. COURSON: Just total subprime loans.

MS. JAVITS: Total subprime loans. And then --

MS. PARKER: Twenty percent.

MR. DAVI: Twenty percent.

MS. JAVITS: -- 21 percent are now seriously delinquent.

MR. COURSON: And about --

MS. JAVITS: Right?

MR. COURSON: If you believe the numbers,
about -- excuse me, but 25 percent of that $700,000 number are non-owner-occupied properties.

MS. GALANTE: Investor.

MR. PAVAO: Say that again.

MS. JAVITS: I see.

MR. COURSON: About 25 percent of the subprime loans in California are non-owner occupied. They're second homes or investor owned.

MS. JAVITS: So is there any way -- does the data exist now so that we could look at it on a map just trying to understand this community by community -- any of this data, that looks community by community, so we can see the total number or the percentage of those that really --

MS. PARKER: Well, yeah, I mean that's --

MS. JAVITS: -- we're concerned about?

MS. PARKER: That's exactly the data that they've been provided by zip code. And you can look at the concentration of these loans --

MS. JAVITS: So that will help.

MS. PARKER: So the data that we have, the concentration of these loans by zip code. Now, we don't -- we can't tell you in that zip code what is the concentration of all housing units in it. We don't know. That part we don't know, but we can give you a
sense of the concentration of the number of loans in
that geographic area.

MS. JAVITS: And the numbers that are seriously
delinquent?

MS. PARKER: Yeah, that's -- that's right.

MS. JAVITS: And the percentage that are not?

MR. COURSON: In fact, they did --

MR. FLUEHR: All this data --

MR. COURSON: They did --

MR. FLUEHR: -- is available.

MS. JAVITS: All right.

MR. COURSON: What they did is they took the
data that Citi graciously provided and mapped -- it's
almost like your property value map -- into hot red,
red, lighter red and pink as where the concentration of
these loans are in the state of California. So we've
got maps that we could show to the Board that shows
exactly where it is. Then you can drill down to the --

MR. CAREY: Does that include rural data as well
as --

MS. PARKER: By zip code.

MR. COURSON: Our reporter is going to need to
take a break, but I don't -- if there are just a couple
more questions or things? I mean these fellows will be
around a little bit. They've got a plane to catch in
San Francisco so we've got to get them on their way back to the City, too.

MS. GALANTE: It was fabulous, thank you.

MS. JAVITS: It was a terrific presentation.

MR. COURSON: And anything that, you know, comes up in the meantime or in our board meeting I know that they'll be a great resource for us. And Mike and Nick have been very helpful to us.

MS. JAVITS: If we can get those geographic breakdowns --

MS. JACOBS: On the 19th, that would be very helpful.

MR. COURSON: We've got them.

MS. PARKER: In fact, what we can give you -- it's really been great, is that we can give you percent change so you can see over a period of time what areas have gotten hotter and what areas have gotten cooler, so.

MR. COURSON: All right. Thank you very much. We really appreciate it. Thank you for taking the effort to come out. And they're on their way back late, late tonight to New York.

--o0o--

Item 6. Public testimony

MR. COURSON: And I guess I should ask if
there's any public testimony.

And seeing none, then the meeting will stand

adjourned.

(The meeting concluded at 2:55 p.m.)
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 13th day of February 2008.

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

This is a Final Commitment request for a $4,730,000 construction loan. Security for the loan will be a first deed of trust on a proposed 33 unit senior residential community to be constructed at 1447 Herbert Avenue, South Lake Tahoe (El Dorado County), California. Tahoe Senior Housing II L.P., ("TSH II") a California limited partnership will own the property. The managing general partner will be Carmel Senior Housing, Inc, a California nonprofit public benefit corporation.

Tahoe Senior Plaza II is a proposed 2-story elevator apartment structure containing 32 rental units and one manager's unit, and situated on a 3.19 acre parcel. The project will be restricted to seniors age 62 and older, with rents restricted at 50% of Area Median Income ("AMI").

LOAN TERMS

Construction

<table>
<thead>
<tr>
<th>First Mortgage</th>
<th>$4,730,000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Interest Rate</td>
<td>1 month SIFMA +150 bps, adjusted monthly</td>
</tr>
<tr>
<td>Term</td>
<td>18 months (interest only)</td>
</tr>
<tr>
<td>Financing</td>
<td>Tax-exempt mortgage revenue bonds</td>
</tr>
</tbody>
</table>

OTHER FINANCING

The primary sources of construction financing will be proceeds from the South Lake Tahoe HOME loan, as well as the California Housing Finance Agency ("CalHFA") construction loan:

<table>
<thead>
<tr>
<th>Other Construction Financing</th>
<th>Type</th>
<th>Loan Amount</th>
<th>Term</th>
<th>Interest Rate</th>
<th>Repayment</th>
</tr>
</thead>
<tbody>
<tr>
<td>South Lake Tahoe HOME funds</td>
<td>Loan</td>
<td>$2,707,500</td>
<td>55 yrs</td>
<td>3%</td>
<td>Residual Receipts</td>
</tr>
</tbody>
</table>

February 27, 2008
The following table identifies sources of funds for permanent financing and repayment in full of the CalHFA construction loan:

<table>
<thead>
<tr>
<th>Source</th>
<th>Type</th>
<th>Amount</th>
<th>Term</th>
<th>Interest Rate</th>
<th>Repayment</th>
</tr>
</thead>
<tbody>
<tr>
<td>South Lake Tahoe HOME funds (Includes construction loan funds)</td>
<td>Loan</td>
<td>$3,412,500</td>
<td>55 yrs</td>
<td>3%</td>
<td>Residual Receipts</td>
</tr>
<tr>
<td>South Tahoe Redevelopment Agency</td>
<td>Loan</td>
<td>$906,722</td>
<td>55 yrs</td>
<td>3%</td>
<td>Residual Receipts</td>
</tr>
<tr>
<td>Project Sponsor Loan</td>
<td>Loan</td>
<td>$376,702</td>
<td>55 yrs</td>
<td>0%</td>
<td>Residual Receipts</td>
</tr>
<tr>
<td>Tax Credit Equity</td>
<td>Equity</td>
<td>$3,235,000</td>
<td>N/a</td>
<td>N/a</td>
<td>N/a</td>
</tr>
</tbody>
</table>

Regulatory Constraints

The CalHFA Regulatory Agreement shall regulate 20% or 7 units at 50% AMI for a period of at least the qualified project period. The CalHFA Regulatory Agreement shall be recorded in a priority position to all other recorded loan documentation and regulatory constraints.

The South Lake Tahoe HOME and South Tahoe Redevelopment Agency regulatory agreements shall each regulate 32 units at 50% AMI for a period of fifty-five (55) years.

CONDITIONS PRECEDENT TO CONSTRUCTION LOAN CLOSING

Prior to construction loan closing all sources of construction period and permanent loan financing, including grants, developers equity and other financing and subsidy sources must be fully committed and enforceable upon terms acceptable to CalHFA. A condition of the HOME and RDA loans is that construction commence on or before May 1, 2008.

PROJECT DESCRIPTION

Project Location

- The project is located at the corner intersection of Herbert Avenue and Pioneer Trail Road in the city of South Lake Tahoe. The site is on the north side of Herbert Avenue with frontage along Pioneer Trail Road to the east. Pioneer Trail Road is an arterial road connecting north and south areas of the city. It is situated in the Lake Tahoe Basin and is located approximately 6,000 feet south of Lake Tahoe. Surrounding uses are single-family residences or vacant parcels. The site is within 1.5 – 2.5 miles of supermarkets and restaurants, financial and automotive services; 2-5 miles of medical services and hospital; 1-2.5 miles of emergency and governmental services; and 1-2 miles from park and recreational areas, including Lake Tahoe.
Site

- The site of the proposed development is a triangular sloping lot containing approximately 3.19 acres. The site is undeveloped and exists in a native condition with Jeffrey and Ponderosa pines and native shrubs. All utilities are available to the site. The property is properly zoned for its intended use.

Improvements

- The project will consist of one (1) two-story, elevator, garden style apartment building of wood frame with hardi-plank exterior siding. Building elevations are designed to emulate the tradition of “rustic Alpine” style hotels and resorts that are prevalent in the area.
- The unit mix will consist of thirty (30) one-bedroom units and three (3) two-bedroom units. One of the two-bedroom units will be the managers unit.
- Common area features and amenities will include security access to the building, a centrally located entrance vestibule with mailboxes located adjacent to the elevator, with visible control from the project office and lounge/library located on the ground floor.
- There will be a multi-use room for arts and crafts and a computer learning center with a small kitchenette for activities, meetings or outside educational programs provided to the residents.
- A small private office provided for special usages such as social service providers or occasional private care service persons or visiting nurses.
- Common area laundry facilities and public restrooms will be located on the ground floor, near the elevator for ease of accessibility.
- There will be maintenance workspace and management/office space.
- On site surface parking will be provided for thirty-five (35) vehicles.
- A public transit bus stop will be constructed on the front of the site along Pioneer Trail Road.

Construction

- The total development cost is estimated at $8,500,000 or $258,000 per unit.
- Construction is scheduled for 12 months and will commence on or before May 1, 2008.
- CalHFA will monitor the project during course of construction.

Relocation

- The site is vacant and requires no relocation.

SERVICES

Resident services will include the following:

- A Computer learning center with computer lessons
- Planned activities such as bingo, book clubs, and cultural workshops. Films and slide shows; bridge, billiards and other table games
- Commitment from the ABHOW Foundation to provide a nine passenger para-transit bus with a wheel-chair hydraulic lift. This bus will be used for resident doctor appointments, trips to the pharmacy, supermarket and recreational areas.

February 27, 2008
Coordination with the nearby South Tahoe Senior Center for the meals on Wheels program that delivers meals to residents on Mondays through Fridays

- Arts and Crafts
- Cultural programs
- Gardening
- Chartered bus tours and special outings
- Teas, picnics, and special social and resident celebrations
- Video and book library
- Blood pressure screening

MARKET

Market Overview

- There is only one existing senior development in South Lake Tahoe, Tahoe Senior Plaza, 45 units. Currently there are 81 seniors on the waiting list. Although there are other affordable housing projects in the City, the comparable affordable housing developments examined all have almost no vacancies and have waiting lists as well.
- There are 337 existing affordable units in South Lake Tahoe located in six (6) projects. Only one of these projects Tahoe Senior Plaza, which is owned by the project sponsor, American Baptist Homes of the West, offers units specifically for seniors.
- There is one affordable project currently under construction that will increase the supply of affordable rental housing in South Lake Tahoe. Sky Forest Acres is an 18-unit Section 811 project for persons with disabilities. This project, which is scheduled to open in mid 2008, along with the proposed Tahoe Senior Plaza II, will bring the total number of affordable units in South Lake Tahoe to 387. There are no other affordable rental projects underway or in planning process in the city.
- The additional senior rental housing planned at Tahoe Senior Plaza II is not expected to have a negative impact on other affordable housing developments in South Lake Tahoe. There is high demand for affordable senior housing as evidenced by the waiting list at Tahoe Senior Plaza (81 seniors on the waiting list).

PROJECT FEASIBILITY

Estimated Lease-up Period

According to the market study the project is expected to be at 95% occupancy within nine months of completion.

ENVIRONMENTAL

- An updated Phase I Environmental Site Assessment is pending. A Phase I Environmental Assessment report was completed in June 2004 for the American Baptist Homes of the West. No adverse environmental conditions warranting further investigation or remedial action were identified in the report.

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DEVELOPMENT TEAM

Borrower/Developer

Tahoe Senior Housing II L.P., a California limited partnership.

The managing general partner is Carmel Senior Housing, Inc, a California nonprofit public benefit corporation, and a wholly controlled affiliate of American Baptist Homes of the West ("ABHOW").

American Baptist Homes of the West's original vision was to provide quality housing and health care for retired American Baptist ministers and missionaries. Today, its communities welcome all people, regardless of occupation or religious affiliation. Its first community, Pilgrim Haven, opened in 1949 in Los Altos, CA. Nearly 4,500 residents currently live in 30 communities located in four Western states. ABHOW is known for pioneering leadership in the concept of continuing care and for recent innovations in memory support care. Nine of its communities are accredited by the Continuing Care Accreditation Commission.

Management Agent

American Baptist Homes of the West

American Baptist Homes of the West ("ABHOW") currently owns and manages 19 HUD assisted elderly apartment communities and 10 continuing care retirement communities. The total number of elders served in the continuing care facilities is approximately 2,511 and approximately 1,588 seniors and disabled people are served in the affordable rental complexes.

All facilities are under central management of ABHOW's main office in Pleasanton, California. Every project is individually staffed with administrative, clerical, maintenance and grounds, and in many cases supportive services staff.

Architect

Borges Architectural Planning Group.

Founded in 1986, Borges Architectural Group, and its predecessor groups, have specialized in master planning and commercial design for office, retail, senior housing institutional and industrial properties in both the public and private sector.

Contractor

Broward Brothers, Inc.

Broward Brothers, Inc, a California General Building and engineering contractor was founded in 1990 and employs 175 people. Since it's founding they have constructed over 1,000 units of affordable/special needs housing.

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## PROJECT SUMMARY

**Project:** Tahoe Senior Plaza II  
**Location:** 1447 Herbert Avenue  
**City:** South Lake Tahoe  
**County:** El Dorado  
**Zip Code:** 96150  
**Developer:** ABHOW  
**Partner:** 0  
**Investor:** Merritt Community Capital  

<table>
<thead>
<tr>
<th>Project Type</th>
<th>Occupancy</th>
<th>Total Units</th>
<th>Style Units</th>
<th>Elevators</th>
<th>Total Parking</th>
</tr>
</thead>
<tbody>
<tr>
<td>New Construction</td>
<td>Senior</td>
<td>33</td>
<td>Flats</td>
<td>Yes</td>
<td>35</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>No. of Buildings</th>
<th>No. of Stories</th>
<th>Residential Space</th>
<th>Commercial Space</th>
<th>Gross Area</th>
<th>Land Area</th>
<th>Units per acre</th>
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</thead>
<tbody>
<tr>
<td>1</td>
<td>2</td>
<td>18,950 sq. ft.</td>
<td>0 sq. ft.</td>
<td>27,060 sq. ft.</td>
<td>138,956 sq. ft.</td>
<td>10</td>
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### CalHFA Construction Financing

<table>
<thead>
<tr>
<th>Source of Funds</th>
<th>Amount</th>
<th>Rate</th>
<th>Term (Mths)</th>
</tr>
</thead>
<tbody>
<tr>
<td>CalHFA Construction Financing (variable rate)</td>
<td>$4,730,000</td>
<td>4.77%</td>
<td>18</td>
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</table>

### Permanent Sources of Funds

<table>
<thead>
<tr>
<th>Source of Funds</th>
<th>Amount</th>
<th>Rate</th>
<th>Years</th>
</tr>
</thead>
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<tr>
<td>CalHFA First Mortgage</td>
<td>$0</td>
<td>0.00%</td>
<td>0</td>
</tr>
<tr>
<td>CalHFA Bridge Loan</td>
<td>$0</td>
<td>0.00%</td>
<td>0</td>
</tr>
<tr>
<td>CalHFA Second Mortgage</td>
<td>$0</td>
<td>0.00%</td>
<td>0</td>
</tr>
<tr>
<td>So Lake Tahoe HOME</td>
<td>$3,412,500</td>
<td>3.00%</td>
<td>55</td>
</tr>
<tr>
<td>South Lake Tahoe RDA</td>
<td>$906,722</td>
<td>3.00%</td>
<td>55</td>
</tr>
<tr>
<td>0</td>
<td>$0</td>
<td>0.00%</td>
<td>0</td>
</tr>
<tr>
<td>Source 7</td>
<td>$0</td>
<td>0.00%</td>
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<tr>
<td>Source 8</td>
<td>$0</td>
<td>0.00%</td>
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<td>Source 9</td>
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<td>0.00%</td>
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<tr>
<td>Source 10</td>
<td>$0</td>
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<tr>
<td>Source 11</td>
<td>$0</td>
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<tr>
<td>Source 12</td>
<td>$0</td>
<td>0.00%</td>
<td>0</td>
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<tr>
<td>Sponsor Loan</td>
<td>$376,702</td>
<td>0.00%</td>
<td>55</td>
</tr>
<tr>
<td>Developer Contribution</td>
<td>$485,000</td>
<td>0.00%</td>
<td></td>
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<tr>
<td>Deferred Dev. Fee</td>
<td>$158,000</td>
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<tr>
<td>Tax Credit Equity</td>
<td>$3,235,000</td>
<td>0.00%</td>
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### Construction Valuation

<table>
<thead>
<tr>
<th>Investment Value</th>
<th>$7,650,000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Loan / Cost</td>
<td>62%</td>
</tr>
<tr>
<td>Loan / Value</td>
<td>62%</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Appraisal Value Upon Completion</th>
</tr>
</thead>
<tbody>
<tr>
<td>Appraisal Date: Pending</td>
</tr>
<tr>
<td>Cap Rate: Restricted Value</td>
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<tr>
<td>Perm. Loan / Value</td>
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</tbody>
</table>

### CalHFA Fees and Reserve Requirements

#### CalHFA Loan Fees

<table>
<thead>
<tr>
<th>Amount</th>
<th>Required Reserves</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>CalHFA Construction Loan Fee</td>
<td>$35,475</td>
<td>Rent Subsidy Reserve</td>
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<tr>
<td>CalHFA Permanent Loan Fees</td>
<td>$0</td>
<td>Replacement Resv. Initial Deposit</td>
</tr>
<tr>
<td>Other Fee</td>
<td>$0</td>
<td>Repl. Reserve - Per Unit/ Per Yr</td>
</tr>
</tbody>
</table>

#### Construction Loan - Guarantees and Fees

<table>
<thead>
<tr>
<th>Amount</th>
<th>CalHFA Operating Expense Reserve-below</th>
<th>$0</th>
</tr>
</thead>
<tbody>
<tr>
<td>Completion Guarantee Fee</td>
<td>$5,192,000</td>
<td>Rent Up Reserve</td>
</tr>
<tr>
<td>Contractors Payment Bond</td>
<td>$5,192,000</td>
<td>Operating Expense Reserve</td>
</tr>
<tr>
<td>Contractors Performance Bond</td>
<td>$5,192,000</td>
<td></td>
</tr>
</tbody>
</table>

### Date

| Date: 3/19/2008 | Senior Staff Date: 2/27/2008 |
## UNIT MIX AND RENT SUMMARY

### Tahoe Senior Plaza II

#### Total Unit Mix

<table>
<thead>
<tr>
<th># of Units</th>
<th>Unit Type</th>
<th># of Baths</th>
<th>Average Sq. Ft.</th>
</tr>
</thead>
<tbody>
<tr>
<td>30</td>
<td>1 Bedroom Flat</td>
<td>1</td>
<td>540</td>
</tr>
<tr>
<td>2</td>
<td>2 Bedroom Flat</td>
<td>1</td>
<td>720</td>
</tr>
<tr>
<td>1</td>
<td>1 Bedroom Flat (managers)</td>
<td>1</td>
<td>720</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
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</tr>
<tr>
<td></td>
<td><strong>Total</strong></td>
<td></td>
<td><strong>33</strong></td>
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</tbody>
</table>

#### Number of Regulated Units By Agency

<table>
<thead>
<tr>
<th>Agency</th>
<th>35%</th>
<th>45%</th>
<th>50%</th>
<th>60%</th>
<th>80%</th>
<th>Unrestricted</th>
<th>Total</th>
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<tbody>
<tr>
<td>CalHFA</td>
<td></td>
<td></td>
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<tr>
<td>Tax Credits</td>
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<tr>
<td>Locality HOME</td>
<td></td>
<td></td>
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<tr>
<td>Locality RDA</td>
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<tr>
<td>Zoning</td>
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<td>Other</td>
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</table>

#### Restricted Rents Compared to Average Market Rents

<table>
<thead>
<tr>
<th>Median Income Rent Levels</th>
<th>Units Restricted</th>
<th>Restricted Rents</th>
<th>Avg. Market Rate Rents</th>
<th>Dollars Difference</th>
<th>% of Market</th>
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<tbody>
<tr>
<td>One Bedroom</td>
<td></td>
<td></td>
<td>$848</td>
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<tr>
<td>30%</td>
<td>0</td>
<td>$0</td>
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</tr>
<tr>
<td>50%</td>
<td>7</td>
<td>$515</td>
<td>$333</td>
<td>61%</td>
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<tr>
<td>50%</td>
<td>23</td>
<td>$515</td>
<td>$333</td>
<td>61%</td>
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<tr>
<td>60%</td>
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<td>$0</td>
<td>0%</td>
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</tr>
<tr>
<td>80%</td>
<td>0</td>
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<td>$0</td>
<td>0%</td>
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</tr>
<tr>
<td>Two Bedroom</td>
<td></td>
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<tr>
<td>30%</td>
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</tr>
<tr>
<td>50%</td>
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<tr>
<td>50%</td>
<td>2</td>
<td>$611</td>
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<tr>
<td>80%</td>
<td>0</td>
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<td>$0</td>
<td>0%</td>
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<tr>
<td>Three Bedroom</td>
<td></td>
<td><strong>$1</strong></td>
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<tr>
<td>30%</td>
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<tr>
<td>50%</td>
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</tr>
<tr>
<td>80%</td>
<td>0</td>
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<td>$0</td>
<td>0%</td>
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<tr>
<td>Four Bedroom</td>
<td></td>
<td><strong>$1</strong></td>
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<tr>
<td>30%</td>
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<td>$0</td>
<td>$0</td>
<td>0%</td>
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<tr>
<td>50%</td>
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<tr>
<td>50%</td>
<td>0</td>
<td>$0</td>
<td>$0</td>
<td>0%</td>
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</tr>
<tr>
<td>60%</td>
<td>0</td>
<td>$0</td>
<td>$0</td>
<td>0%</td>
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<tr>
<td>80%</td>
<td>0</td>
<td>$0</td>
<td>$0</td>
<td>0%</td>
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</table>
## Sources and Uses of Funds

### SOURCES OF FUNDS:

<table>
<thead>
<tr>
<th>Funds in during Construction ($)</th>
<th>Funds in at Permanent ($)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>CalHFA Construction Financing (variable rate)</strong></td>
<td>4,730,000</td>
</tr>
<tr>
<td>Construction Only Source 2</td>
<td>-</td>
</tr>
<tr>
<td>Construction Only Source 3</td>
<td>-</td>
</tr>
<tr>
<td><strong>CalHFA First Mortgage</strong></td>
<td>-</td>
</tr>
<tr>
<td><strong>CalHFA Second Mortgage</strong></td>
<td>0</td>
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<tr>
<td><strong>So Lake Tahoe HOME</strong></td>
<td>2,707,500</td>
</tr>
<tr>
<td><strong>South Lake Tahoe RDA</strong></td>
<td>-</td>
</tr>
<tr>
<td><strong>Source 7</strong></td>
<td>-</td>
</tr>
<tr>
<td><strong>Source 8</strong></td>
<td>-</td>
</tr>
<tr>
<td><strong>Source 9</strong></td>
<td>-</td>
</tr>
<tr>
<td><strong>Source 10</strong></td>
<td>-</td>
</tr>
<tr>
<td><strong>Source 11</strong></td>
<td>-</td>
</tr>
<tr>
<td><strong>Source 12</strong></td>
<td>-</td>
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<tr>
<td><strong>Deferred Interest Costs</strong></td>
<td>42,704</td>
</tr>
<tr>
<td><strong>Sponsor Loan</strong></td>
<td>108,000</td>
</tr>
<tr>
<td><strong>Developer Contribution</strong></td>
<td>-</td>
</tr>
<tr>
<td><strong>Deferred Developer's Fee</strong></td>
<td>-</td>
</tr>
<tr>
<td><strong>Tax Credit Equity</strong></td>
<td>10,000</td>
</tr>
<tr>
<td><strong>Total Sources of Funds</strong></td>
<td>7,596,204</td>
</tr>
<tr>
<td><strong>Total Sources of Funds per Unit</strong></td>
<td>5,748,424</td>
</tr>
<tr>
<td><strong>(Gap)/Surplus (rounding)</strong></td>
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</table>

### USES OF FUNDS:

#### LOAN PAYOFFS & ROLLOVERS

<table>
<thead>
<tr>
<th>Construction ($)</th>
<th>Permanent ($)</th>
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<tbody>
<tr>
<td><strong>Construction Loan payoffs</strong></td>
<td>$4,730,000</td>
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<tr>
<td><strong>Lesser of Land Cost or Value</strong></td>
<td>685,000</td>
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<tr>
<td><strong>Demolition</strong></td>
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<tr>
<td><strong>Legal / Acquisition Related Fees/Charges</strong></td>
<td>27,500</td>
</tr>
<tr>
<td><strong>Subtotal - Land Cost / Value</strong></td>
<td>712,500</td>
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<tr>
<td><strong>Existing Improvements Value</strong></td>
<td>-</td>
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<tr>
<td><strong>Off-Site Improvements</strong></td>
<td>65,000</td>
</tr>
<tr>
<td><strong>Other</strong></td>
<td>-</td>
</tr>
<tr>
<td><strong>Total Acquisition</strong></td>
<td>777,500</td>
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#### REHABILITATION

<table>
<thead>
<tr>
<th>Construction ($)</th>
<th>Permanent ($)</th>
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<tr>
<td><strong>Site Work</strong></td>
<td>-</td>
</tr>
<tr>
<td><strong>Rehab to Structures</strong></td>
<td>-</td>
</tr>
<tr>
<td><strong>General Requirements</strong></td>
<td>-</td>
</tr>
<tr>
<td><strong>Contractors Overhead</strong></td>
<td>-</td>
</tr>
<tr>
<td><strong>Contractors Profit</strong></td>
<td>-</td>
</tr>
<tr>
<td><strong>Contractor's Bond</strong></td>
<td>-</td>
</tr>
<tr>
<td><strong>General Liability Insurance</strong></td>
<td>-</td>
</tr>
<tr>
<td><strong>Environmental Mitigation Expense</strong></td>
<td>-</td>
</tr>
<tr>
<td><strong>Other</strong></td>
<td>-</td>
</tr>
<tr>
<td><strong>Total Rehabilitation</strong></td>
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</table>

#### RELOCATION EXPENSES

<table>
<thead>
<tr>
<th>Construction ($)</th>
<th>Permanent ($)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Relocation Expense</strong></td>
<td>-</td>
</tr>
<tr>
<td><strong>Relocation Compliance Monitoring</strong></td>
<td>-</td>
</tr>
<tr>
<td><strong>Total Relocation</strong></td>
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</tbody>
</table>

### Total Development Sources

<table>
<thead>
<tr>
<th>Total Sources of Funds ($)</th>
<th>Sources per Unit</th>
</tr>
</thead>
<tbody>
<tr>
<td>7,596,204</td>
<td>5,748,424</td>
</tr>
</tbody>
</table>

### Total Development Costs

<table>
<thead>
<tr>
<th>Total Uses of Funds ($)</th>
<th>Cost per Unit</th>
<th>%</th>
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</thead>
<tbody>
<tr>
<td>777,500</td>
<td>23,561</td>
<td>9%</td>
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</table>

(Continued on Next 2 Pages)
### USES OF FUNDS (Cont’d):

<table>
<thead>
<tr>
<th>Category</th>
<th>Construction ($)</th>
<th>Permanent ($)</th>
<th>Total Development Costs</th>
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<tr>
<td><strong>NEW CONSTRUCTION</strong></td>
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<tr>
<td>Site Work</td>
<td>349,433</td>
<td>-</td>
<td>349,433</td>
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<tr>
<td>Structures (Hard Costs)</td>
<td>3,694,216</td>
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<td>3,694,216</td>
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<tr>
<td>General Requirements</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Contractors Overhead/Profit/General Conditions</td>
<td>835,518</td>
<td>-</td>
<td>835,518</td>
</tr>
<tr>
<td>Contractors Profit</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Contractor's Perf. &amp; Pynt Bond</td>
<td>42,064</td>
<td>-</td>
<td>42,064</td>
</tr>
<tr>
<td>General Liability Insurance</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Personal Property in const contract</td>
<td>218,769</td>
<td>-</td>
<td>218,769</td>
</tr>
<tr>
<td>Personal Property not in const contract</td>
<td>52,000</td>
<td>-</td>
<td>52,000</td>
</tr>
<tr>
<td><strong>Total New Construction</strong></td>
<td>5,192,000</td>
<td>-</td>
<td>5,192,000</td>
</tr>
</tbody>
</table>

| **ARCHITECTURAL & ENGINEERING**               |                  |               |                         |
| Architectural Design/Reimbursements/landscape | 432,500          | -             | 432,500                 |
| Architect’s Supv during Construction          | -                | -             | -                       |
| **Total Architectural**                       | 432,500          | -             | 432,500                 |

| **CONSTRUCTION LOAN COSTS**                   |                  |               |                         |
| Construction Loan Interest                    | 241,169          | 241,169       | 7,308                   |
| Deferred HOME interest during const           | 42,704           | 42,704        | 1,075                   |
| CalHFA Construction Loan Fee                  | 35,475           | 35,475        | 1,061                   |
| Predevelopment Loan Interest                  | -                | -             | -                       |
| Other Construction Loan Fees                  | 17,510           | 17,510        | 531                     |
| CalHFA Outside Legal Counsel Fees (see legal below) | -          | -             | -                       |
| Other Lender Req’d Legal Fees                 | -                | -             | -                       |
| Title and Recording fees                      | 27,000           | 27,000        | 818                     |
| CalHFA Req’d Inspection Fees                  | 27,000           | 27,000        | 818                     |
| Other Req’d Inspection Fees                   | -                | -             | -                       |
| Prevailing Wage Monitoring Expense            | -                | -             | -                       |
| Taxes during construction                      | 3,500            | 3,500         | 106                     |
| Insurance during construction                 | 35,000           | 35,000        | 1,061                   |
| Cost for Completion Guarantee                  | -                | -             | -                       |
| Other                                         | -                | -             | -                       |
| **Total Construction Loan Expense**           | 429,358          | -             | 429,358                 |

| **PERMANENT LOAN COSTS**                      |                  |               |                         |
| CalHFA Perm Loan Fees                         | -                | -             | -                       |
| CalHFA Bridge Loan Fees                       | -                | -             | -                       |
| CalHFA Loan Application Fee                   | 500              | 500           | 15                      |
| Other Lender Perm. Loan Fees                  | -                | -             | -                       |
| Title and Recording                           | 10,000           | 10,000        | 303                     |
| Perm. Bridge Loan Interest Expense            | -                | -             | -                       |
| Bond Origination Guarantee Fee                | -                | -             | -                       |
| Tax Exempt Bond Allocation Fee                | -                | -             | -                       |
| Other -Perm. financing costs??                | -                | -             | -                       |
| **Total Permanent Loan Expense**              | 10,500           | -             | 10,500                  |

| **LEGAL FEES**                                |                  |               |                         |
| Lender legal                                  | -                | -             | -                       |
| Borrower Legal Fee                            | 40,000           | -             | 40,000                  |
| Legal Organizational                          | 4,000            | -             | 4,000                   |
| Legal syndication                             | 40,000           | -             | 40,000                  |
| Tax Legal                                     | -                | -             | -                       |
| **Total Attorney Expense**                    | 84,000           | -             | 84,000                  |
### USES OF FUNDS (Cont'd):

<table>
<thead>
<tr>
<th>CONTRACT / REPORT COSTS</th>
<th>Construction ($)</th>
<th>Permanent ($)</th>
<th>Total Development Costs</th>
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<tbody>
<tr>
<td><strong>Appraisal</strong></td>
<td>9,000</td>
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<tr>
<td><strong>Market Study</strong></td>
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<td>12,000</td>
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<tr>
<td><strong>Physical Needs Assessment</strong></td>
<td>-</td>
<td>-</td>
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<tr>
<td><strong>HUD Risk Share Environ. Review</strong></td>
<td>-</td>
<td>-</td>
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<tr>
<td><strong>CalHFA EQ Waiver Seismic Review Fee</strong></td>
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<tr>
<td><strong>Environmental Phase I / II Reports</strong></td>
<td>-</td>
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<tr>
<td><strong>Soils / Geotech Reports</strong></td>
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<tr>
<td><strong>Asbestos / Lead-based Paint Report</strong></td>
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<tr>
<td><strong>Noise/Acoustical/Traffic Study Report</strong></td>
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<tr>
<td><strong>Other</strong></td>
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<tr>
<td><strong>Total Contract Costs</strong></td>
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<table>
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<th>Construction ($)</th>
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<td><strong>Hard Cost Contingency</strong></td>
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<td><strong>Soft Cost Contingency</strong></td>
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<table>
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<th>Construction ($)</th>
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<th>Total Development Costs</th>
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<tbody>
<tr>
<td><strong>CalHFA Operating Expense Reserve-below</strong></td>
<td>-</td>
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<tr>
<td><strong>Construction Defects Reserve</strong></td>
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</tr>
<tr>
<td><strong>Rent-Up Reserve</strong></td>
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<tr>
<td><strong>Capitalized Operating Reserve-Other</strong></td>
<td>36,200</td>
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<tr>
<td><strong>Rent Subsidy Reserve</strong></td>
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<td><strong>Total Reserves</strong></td>
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<tr>
<th><strong>OTHER</strong></th>
<th>Construction ($)</th>
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<th>Total Development Costs</th>
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</thead>
<tbody>
<tr>
<td><strong>CTCAC App/Alloc/Monitor Fees</strong></td>
<td>18,446</td>
<td>18,446</td>
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<tr>
<td><strong>Local Permit Fees</strong></td>
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<tr>
<td><strong>Local Development Impact Fees</strong></td>
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<tr>
<td><strong>Other Local Fees</strong></td>
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<tr>
<td><strong>Advertising &amp; Marketing Expenses</strong></td>
<td>22,000</td>
<td>22,000</td>
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<tr>
<td><strong>1st Year Taxes &amp; Insurance</strong></td>
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<td>-</td>
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<tr>
<td><strong>Furnishings</strong></td>
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<tr>
<td><strong>Final Cost Audit Expense</strong></td>
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<tr>
<td><strong>Miscellaneous Admin Fees</strong></td>
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<tr>
<td><strong>Other</strong></td>
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<td>-</td>
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</tr>
<tr>
<td><strong>Other</strong></td>
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<tr>
<td><strong>Total Other Expenses</strong></td>
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<th>Construction ($)</th>
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<th>Total Development Costs</th>
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<tbody>
<tr>
<td></td>
<td>7,558,204</td>
<td>4,781,200</td>
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<table>
<thead>
<tr>
<th><strong>DEVELOPER COSTS</strong></th>
<th>Construction ($)</th>
<th>Permanent ($)</th>
<th>Total Development Costs</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Developer Overhead/Profit (5% Acq.)</strong></td>
<td>967,224</td>
<td>967,224</td>
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<tr>
<td><strong>Developer Profit payable from Operations</strong></td>
<td>-</td>
<td>-</td>
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<tr>
<td><strong>Developer Overhead/Profit (NC/Rehab)</strong></td>
<td>40,000</td>
<td>40,000</td>
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</tr>
<tr>
<td><strong>Consultant / Processing Agent</strong></td>
<td>-</td>
<td>-</td>
<td></td>
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<tr>
<td><strong>Project Administration</strong></td>
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<td>-</td>
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<tr>
<td><strong>Broker Fees to a related party</strong></td>
<td>-</td>
<td>-</td>
<td></td>
</tr>
<tr>
<td><strong>Construction Mgmt. Oversight</strong></td>
<td>-</td>
<td>-</td>
<td></td>
</tr>
<tr>
<td><strong>Other</strong></td>
<td>-</td>
<td>-</td>
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<tr>
<td><strong>Total Developer Fee / Costs</strong></td>
<td>40,000</td>
<td>967,224</td>
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<table>
<thead>
<tr>
<th><strong>Total Costs</strong></th>
<th>Construction ($)</th>
<th>Permanent ($)</th>
<th>Total Development Costs</th>
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<tbody>
<tr>
<td></td>
<td>7,598,204</td>
<td>5,748,424</td>
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</table>

<table>
<thead>
<tr>
<th><strong>Per Unit</strong></th>
<th>Permanent of Funds ($)</th>
<th>Per Unit</th>
<th>%</th>
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<tr>
<td></td>
<td></td>
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<tr>
<td><strong>362</strong></td>
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### Annual Operating Budget

**Tahoe Senior Plaza II**

**Final Commitment**

#### INCOME:

<table>
<thead>
<tr>
<th>Description</th>
<th>$ Amount</th>
<th>Per Unit</th>
<th>% of Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Rental Income</td>
<td>$200,064</td>
<td>$6,063</td>
<td>99.40%</td>
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<tr>
<td>Laundry</td>
<td>$1,200</td>
<td>$36</td>
<td>0.60%</td>
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<tr>
<td>Other Income</td>
<td>$0</td>
<td>$0</td>
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<tr>
<td><strong>Gross Potential Income (GPI)</strong></td>
<td><strong>$201,264</strong></td>
<td><strong>$6,099</strong></td>
<td><strong>100.00%</strong></td>
</tr>
</tbody>
</table>

#### Less:

<table>
<thead>
<tr>
<th>Description</th>
<th>$ Amount</th>
<th>Per Unit</th>
<th>% of Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Vacancy Loss</td>
<td>$10,063</td>
<td>$305</td>
<td>5.26%</td>
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<tr>
<td><strong>Effective Gross Income</strong></td>
<td><strong>$191,201</strong></td>
<td><strong>$5,794</strong></td>
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</table>

#### EXPENSES:

<table>
<thead>
<tr>
<th>Description</th>
<th>Total Cost</th>
<th>Per Unit</th>
<th>% of Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Payroll</td>
<td>$38,556</td>
<td>$1,168</td>
<td>26.65%</td>
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<tr>
<td>Administrative</td>
<td>$16,440</td>
<td>$498</td>
<td>11.36%</td>
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<tr>
<td>Management fee</td>
<td>$18,585</td>
<td>$563</td>
<td>12.85%</td>
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<td>Utilities</td>
<td>$33,155</td>
<td>$1,005</td>
<td>22.92%</td>
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<tr>
<td>Operating and Maintenance</td>
<td>$22,650</td>
<td>$686</td>
<td>15.65%</td>
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<tr>
<td>Insurance and Business Taxes</td>
<td>$15,098</td>
<td>$458</td>
<td>10.44%</td>
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<td>Locality Compliance Monitoring Fee</td>
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<td>Other</td>
<td>$0</td>
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<tr>
<td><strong>Subtotal Expenses</strong></td>
<td><strong>$144,484</strong></td>
<td><strong>$4,378</strong></td>
<td><strong>99.86%</strong></td>
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<td>Replacement Reserves</td>
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<tr>
<td>Operating Reserves II Deposit (HCD)</td>
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<td>$0</td>
<td>0.00%</td>
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<tr>
<td>Taxes &amp; Assessments</td>
<td>$200</td>
<td>$6</td>
<td>0.14%</td>
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<tr>
<td><strong>Total Expenses</strong></td>
<td><strong>$144,684</strong></td>
<td><strong>$4,384</strong></td>
<td><strong>100.00%</strong></td>
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#### Financial Expenses

<table>
<thead>
<tr>
<th>Description</th>
<th>$ Amount</th>
<th>Per Unit</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>CalHFA First Mortgage</td>
<td>$0</td>
<td>$0</td>
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<tr>
<td>CalHFA Second Mortgage</td>
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<tr>
<td>Other Required Debt Service</td>
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**NET OPERATING INCOME** | **$46,517** | **$1,410** |
### Cash Flow

<table>
<thead>
<tr>
<th></th>
<th>Year 1</th>
<th>Year 2</th>
<th>Year 3</th>
<th>Year 4</th>
<th>Year 5</th>
<th>Year 6</th>
<th>Year 7</th>
<th>Year 8</th>
<th>Year 9</th>
<th>Year 10</th>
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<tbody>
<tr>
<td><strong>RENTAL INCOME</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>Affordable Rents</td>
<td>200,064</td>
<td>204,065</td>
<td>208,147</td>
<td>212,310</td>
<td>216,556</td>
<td>220,887</td>
<td>225,305</td>
<td>229,511</td>
<td>234,407</td>
<td>239,095</td>
</tr>
<tr>
<td>Affordable Rent Inc.</td>
<td>2.00%</td>
<td>2.00%</td>
<td>2.00%</td>
<td>2.00%</td>
<td>2.00%</td>
<td>2.00%</td>
<td>2.00%</td>
<td>2.00%</td>
<td>2.00%</td>
<td>2.00%</td>
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<tr>
<td>Rental Subsidies</td>
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<td>0</td>
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<tr>
<td>Rental Subsid Inc.</td>
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<td>0</td>
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<td>0</td>
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<td>0</td>
<td>0</td>
<td>0</td>
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<tr>
<td><strong>TOTAL RENTAL INCOME</strong></td>
<td>200,064</td>
<td>204,065</td>
<td>208,147</td>
<td>212,310</td>
<td>216,556</td>
<td>220,887</td>
<td>225,305</td>
<td>229,511</td>
<td>234,407</td>
<td>239,095</td>
</tr>
<tr>
<td><strong>OTHER INCOME</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Laundry</td>
<td>1,200</td>
<td>1,224</td>
<td>1,248</td>
<td>1,273</td>
<td>1,299</td>
<td>1,325</td>
<td>1,351</td>
<td>1,378</td>
<td>1,406</td>
<td>1,434</td>
</tr>
<tr>
<td>Other Income</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
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</tr>
<tr>
<td>Other In. Inc.</td>
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<td>2.00%</td>
<td>2.00%</td>
<td>2.00%</td>
<td>2.00%</td>
<td>2.00%</td>
<td>2.00%</td>
<td>2.00%</td>
<td>2.00%</td>
<td>2.00%</td>
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<tr>
<td><strong>TOTAL OTHER INCOME</strong></td>
<td>1,200</td>
<td>1,224</td>
<td>1,248</td>
<td>1,273</td>
<td>1,299</td>
<td>1,325</td>
<td>1,351</td>
<td>1,378</td>
<td>1,406</td>
<td>1,434</td>
</tr>
<tr>
<td><strong>GROSS POTENTIAL INCOME</strong></td>
<td>201,264</td>
<td>205,289</td>
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<td>217,855</td>
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<td>226,656</td>
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<td>240,529</td>
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<td><strong>VACANCY ASSUMPTIONS</strong></td>
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<tr>
<td>Affordable (Blended Average)</td>
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<td>5.00%</td>
<td>5.00%</td>
<td>5.00%</td>
<td>5.00%</td>
<td>5.00%</td>
<td>5.00%</td>
<td>5.00%</td>
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<td>Unrestricted Units / Market Rate Units</td>
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<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Laundry &amp; Other Inc.</td>
<td>5.00%</td>
<td>5.00%</td>
<td>5.00%</td>
<td>5.00%</td>
<td>5.00%</td>
<td>5.00%</td>
<td>5.00%</td>
<td>5.00%</td>
<td>5.00%</td>
<td>5.00%</td>
</tr>
<tr>
<td><strong>LESS: VACANCY LOSS</strong></td>
<td>10,063</td>
<td>10,264</td>
<td>10,470</td>
<td>10,679</td>
<td>10,883</td>
<td>11,091</td>
<td>11,299</td>
<td>11,507</td>
<td>11,715</td>
<td>11,923</td>
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<td><strong>EFFECTIVE GROSS INCOME</strong></td>
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<td>195,025</td>
<td>198,925</td>
<td>202,904</td>
<td>206,962</td>
<td>211,101</td>
<td>215,323</td>
<td>219,630</td>
<td>224,022</td>
<td>228,503</td>
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<td><strong>OPERATING EXPENSES</strong></td>
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<td></td>
<td></td>
<td></td>
<td></td>
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</tr>
<tr>
<td>Expenses</td>
<td>144,484</td>
<td>148,819</td>
<td>153,283</td>
<td>157,682</td>
<td>162,618</td>
<td>167,497</td>
<td>172,621</td>
<td>177,697</td>
<td>183,028</td>
<td>188,519</td>
</tr>
<tr>
<td>Annual Expense Inc.</td>
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<td>3.00%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.00%</td>
<td>3.00%</td>
</tr>
<tr>
<td>Taxes and Assessments</td>
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<td>208</td>
<td>212</td>
<td>216</td>
<td>221</td>
<td>225</td>
<td>230</td>
<td>234</td>
<td>239</td>
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<td>Annual Tax Inc.</td>
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<td>2.00%</td>
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<td>2.00%</td>
<td>2.00%</td>
<td>2.00%</td>
<td>2.00%</td>
<td>2.00%</td>
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</tr>
<tr>
<td>Replacement Reserve</td>
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<td>0</td>
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<tr>
<td>Percentage Increase Yearly</td>
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<td>0.00%</td>
<td>0.00%</td>
<td>0.00%</td>
<td>0.00%</td>
<td>0.00%</td>
<td>0.00%</td>
<td>0.00%</td>
<td>0.00%</td>
<td>0.00%</td>
</tr>
<tr>
<td><strong>TOTAL EXPENSES</strong></td>
<td>144,484</td>
<td>148,819</td>
<td>153,283</td>
<td>157,682</td>
<td>162,618</td>
<td>167,497</td>
<td>172,621</td>
<td>177,697</td>
<td>183,028</td>
<td>188,519</td>
</tr>
<tr>
<td><strong>NET OPERATING INCOME</strong></td>
<td>46,517</td>
<td>46,002</td>
<td>45,434</td>
<td>44,810</td>
<td>44,127</td>
<td>43,384</td>
<td>42,576</td>
<td>41,703</td>
<td>40,760</td>
<td>39,745</td>
</tr>
<tr>
<td><strong>DEBT SERVICE</strong></td>
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<td></td>
<td></td>
<td></td>
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<td></td>
</tr>
<tr>
<td>CalHFA - 1st Mortgage</td>
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<td>0</td>
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<td>0</td>
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<td>CalHFA - Bridge Loan</td>
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<td>CalHFA - 2nd Mortgage</td>
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<td>0</td>
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<td>0</td>
<td>0</td>
<td>0</td>
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<tr>
<td><strong>Sum of all req'd debt service</strong></td>
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<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Cash flow after CalHFA debt service</td>
<td>46,517</td>
<td>46,002</td>
<td>45,434</td>
<td>44,810</td>
<td>44,127</td>
<td>43,384</td>
<td>42,576</td>
<td>41,703</td>
<td>40,760</td>
<td>39,745</td>
</tr>
<tr>
<td>DCR for just CalHFA loans</td>
<td>46,517</td>
<td>46,002</td>
<td>45,434</td>
<td>44,810</td>
<td>44,127</td>
<td>43,384</td>
<td>42,576</td>
<td>41,703</td>
<td>40,760</td>
<td>39,745</td>
</tr>
<tr>
<td>CASH FLOW after all debt service</td>
<td>46,517</td>
<td>46,002</td>
<td>45,434</td>
<td>44,810</td>
<td>44,127</td>
<td>43,384</td>
<td>42,576</td>
<td>41,703</td>
<td>40,760</td>
<td>39,745</td>
</tr>
<tr>
<td><strong>DEBT COVERAGE RATIO</strong></td>
<td>0.00%</td>
<td>0.00%</td>
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<td>0.00%</td>
<td>0.00%</td>
<td>0.00%</td>
<td>0.00%</td>
<td>0.00%</td>
<td>0.00%</td>
<td>0.00%</td>
</tr>
</tbody>
</table>
RESOLUTION 08-06

RESOLUTION AUTHORIZING A FINAL LOAN COMMITMENT

WHEREAS, the California Housing Finance Agency (the "Agency") has received a loan application on behalf of Tahoe Senior Plaza II, L.P., a California limited partnership (the "Borrower"), seeking a loan commitment, the proceeds of which are to be used to provide financing for a multifamily housing development located in South Lake Tahoe, El Dorado County, California, to be known as Tahoe Senior Plaza II (the "Development"); and

WHEREAS, the loan application has been reviewed by Agency staff which prepared a report presented to the Board on the meeting date recited below (the "Staff Report"), recommending Board approval subject to certain recommended terms and conditions; and

WHEREAS, Section 1.150-2 of the Treasury Regulations requires the Agency, as the issuer of tax-exempt bonds, to declare its reasonable official intent to reimburse prior expenditures for the Development with proceeds of a subsequent borrowing; and

WHEREAS, on January 22, 2008, the Executive Director exercised the authority delegated to her under Resolution 94-10 to declare the official intent of the Agency to reimburse such prior expenditures for the Development; and

WHEREAS, based upon the recommendation of staff and due deliberation by the Board, the Board has determined that a final loan commitment be made for the Development;

1. The Executive Director, or in his/her absence, either the Chief Deputy Director or the Director of Multifamily Programs of the Agency is hereby authorized to execute and deliver a final commitment letter, in a form acceptable to the Agency, and subject to recommended terms and conditions set forth in the Staff Report, in relation to the Development described above and as follows:

<table>
<thead>
<tr>
<th>PROJECT NUMBER</th>
<th>DEVELOPMENT NAME/LOCALITY</th>
<th>MORTGAGE AMOUNT</th>
</tr>
</thead>
<tbody>
<tr>
<td>07-028-C</td>
<td>Tahoe Senior Plaza II</td>
<td>$4,730,000.00 Const. 1st Mortgage</td>
</tr>
<tr>
<td></td>
<td>South Lake Tahoe</td>
<td></td>
</tr>
<tr>
<td></td>
<td>El Dorado County, California</td>
<td></td>
</tr>
</tbody>
</table>
2. The Executive Director may modify the terms and conditions of the loans or
loans as described in the Staff Report, provided that major modifications, as defined below,
must be submitted to this Board for approval. "Major modifications" as used herein means
modifications which either (i) increase the total aggregate amount of any loans made pursuant to
the Resolution by more than 7%; or (ii) modifications which in the judgment of the Executive
Director, or in his/her absence, either the Chief Deputy Director or the Director of Multifamily
Programs of the Agency, adversely change the financial or public purpose aspects of the final
commitment in a substantial way.

I hereby certify that this is a true and correct copy of Resolution 08-06 adopted at a duly
constituted meeting of the Board of the Agency held on March 19, 2008, at Sacramento,
California.

ATTEST: _____________________________
Secretary
SUMMARY

This is a Final Commitment request for acquisition, construction and permanent loan financing. Security will be a 109-unit senior apartment complex known as Bay Avenue Senior Apartments, located at 750 Bay Avenue, Capitola, California. Bay Avenue Senior Housing L.P., ("Borrower") whose general partner is First Community Housing, a California nonprofit corporation will own the property.

Bay Avenue Senior Apartments was constructed in 1971 and is presently a 96-unit project consisting of 30 one-bedroom and 66 two-bedroom units in 6 two-story walk-up buildings. Upon completion, the project will have a total of 109 units with 64 one-bedroom units and 45 two-bedroom units. Thirty-five percent of the units will be limited to a tenant population defined as chronically ill and at risk of homelessness.

LOAN TERMS

Acquisition/Construction Period

<table>
<thead>
<tr>
<th>First Mortgage</th>
<th>$22,470,000</th>
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</thead>
<tbody>
<tr>
<td>Interest Rate</td>
<td>5%, fixed for term</td>
</tr>
<tr>
<td>Term</td>
<td>24 Months, interest only</td>
</tr>
<tr>
<td>Financing</td>
<td>$21,580,000 Tax-Exempt Bonds</td>
</tr>
<tr>
<td></td>
<td>$890,000 Taxable Bonds</td>
</tr>
</tbody>
</table>

Permanent Loan Period

<table>
<thead>
<tr>
<th>First Mortgage</th>
<th>$6,600,000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Interest Rate</td>
<td>3%</td>
</tr>
<tr>
<td>Term</td>
<td>35 year fixed, fully amortized, pre-payable after 15 years with 120 day notice to Agency</td>
</tr>
<tr>
<td>Financing</td>
<td>Tax-Exempt</td>
</tr>
</tbody>
</table>

Agency financing is subject to the assignment by the borrower of tax credit equity and all rights under non-Agency financing commitments.

The CalHFA Regulatory Agreement is to remain in place for the latter of the 15 year qualified project period of payment of the loan.

February 27, 2008
SPECIAL NEEDS LOAN TERMS

The interest rate on the permanent loan will be reduced by the Agency from 5% to 3% using HAT funds to subsidize the rate. The Agency will require that all of CalHFA's requirements for Special Needs financing be satisfied prior to construction loan closing.

OTHER FINANCING

<table>
<thead>
<tr>
<th>Source</th>
<th>Type</th>
<th>Loan Amount</th>
<th>Term</th>
<th>Interest Rate</th>
<th>Repayment</th>
</tr>
</thead>
<tbody>
<tr>
<td>MHP</td>
<td>Loan</td>
<td>$6,879,000</td>
<td>55</td>
<td>3.00%</td>
<td>Residual Receipts</td>
</tr>
<tr>
<td>City Capitola HOME</td>
<td>Loan</td>
<td>$1,900,000</td>
<td>55</td>
<td>3.00%</td>
<td>Residual Receipts</td>
</tr>
<tr>
<td>City of Capitola RDA</td>
<td>Loan</td>
<td>$765,000</td>
<td>55</td>
<td>3%</td>
<td>Residual Receipts</td>
</tr>
<tr>
<td>Income from Operations</td>
<td>Income</td>
<td>$550,000</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Tax Credit Equity</td>
<td>Equity</td>
<td>$10,913,616</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
</tbody>
</table>

The HCD MHP loan will specify that thirty-five percent of the units (39) are for use by tenants at risk of homelessness and include at least one tenant with a chronic illness. The HCD definition of at risk of homelessness is households with incomes at or below 20% of Area Median Income (AMI) or tenants at 30% of AMI who face eviction, overcrowded conditions, reside in substandard housing or pay over 50% of their income towards rent. The HCD definition of chronic illness is a chronic condition requiring assistance with daily activities. HCD rent restrictions require that 46% of the units are rented at 30% AMI and 49% of the units are rented at 50% AMI.

The Agency will require that all of HCD's supportive housing requirements be satisfied at time of construction loan closing.

The City of Capitola RDA and HOME funds will be available at construction loan closing and will stay in at permanent loan closing.

The CalHFA Regulatory Agreement shall be recorded in a priority position to all other recorded loan documentation and regulatory constraints. The Regulatory Agreement shall regulate 20% or 22 units at 50% AMI for a period of at least the qualified project period.

PURCHASE AND SALE OF PROPERTY

The borrower will purchase the property from the owner, The Salvation Army, for $6,100,000 in an all cash sales transaction scheduled to close in May.

PROJECT DESCRIPTION

Project Location

- The subject development is located in a residential area in the City of Capitola in Santa Cruz County. It is 4 miles from downtown Santa Cruz and 25 miles south of San Jose. Capitola is a bedroom community for Santa Cruz and the South Bay Area.
The project is located in a predominately older residential area in central Capitola and is less than .15 miles from a major grocery store and drug store and .5 miles from the Capitola Wharf, which is a major tourist attraction.

The site is accessible from Bay Avenue, north of Capitola Avenue and less than .6 miles from the ocean. Highway 1 is ¼ mile away and is accessed via Bay Avenue.

A senior center is .10 miles from the site, a major hospital is 1.6 miles away and all levels of social services are between 1-5 miles away.

Public transportation is available less than 500 feet from the property with routes providing transportation throughout the county.

Site

- The site is an irregularly-shaped 4.62 acre parcel.
- The site is zoned RM-M multifamily residential, medium density and the planned use is legally conforming.

Improvements

- The project is currently a 96-unit apartment complex built in 1971 consisting of six 2-story walk up buildings with 30 one-bedroom units and 66 two-bedroom units.
- Common areas currently consist of a single-story office/recreation building, in-ground swimming pool and landscaping.
- The buildings are conventional wood-frame structures and slab on grade foundations. Exteriors are finished with plywood siding and asphalt built-up roof.
- Current parking allows for 128 cars with 88 carports and 40 open spaces.
- Rehabilitation will consist of building systems upgrades including installation of fire sprinklers, replacement of all wet and dry utilities and installation of copper piping and replacement of the central boiler/heating system with individual through-wall HVAC units.
- Site improvement will also include demolition of carports and the new parking area will provide 81 open parking spaces. The pool will be removed, the site will be re-graded, fencing and walkways will be replaced and new landscaping and irrigation will be installed.
- Exterior building renovations will include stair, balcony and patio replacement, pitching flat roof areas and re-roofing all buildings, re-siding all exteriors, structural upgrades to buildings and window replacement.
- Unit renovations will include replacement of cabinets and appliances on an as-needed basis, replacement of all window coversings and retrofitting all first floor units to be ADA accessible.
- Rehab costs are estimated to be $5,076,90, which is $46,577 per unit.
- New construction will consist of replacement of a building containing 16 units and the office/recreation building. The new building will be three-stories with 33 one-bedroom units serviced by an elevator, with a community room, recreation and management spaces.
- The cost of new construction is estimated to be $6,573,146, excluding site work.
- The cost of the site improvements is estimated to be $1,785,301.
- Construction and rehab is scheduled to commence in June 2008 and is projected to be completed within 24 months.
- Prevailing wages will be paid on this project.

February 27, 2008
Relocation

- As a result of the proposed rehabilitation, during the course of construction, all of the households will be temporarily displaced on site.
- There are presently 16 units held vacant and available for relocation purposes. The first phase of construction and relocation includes moving tenants into the 16 vacant units, demolishing the vacant building and constructing a 33-unit building in its place.
- The second phase will consist of moving into the newly-completed building and renovating 2 existing buildings.
- The third phase of construction similarly will include relocation of tenants in two buildings and renovation of these buildings.
- There is approximately $200,000 in relocation expense allocated for this project. The budget will pay for reasonable out-of-pocket moving expenses for the temporarily displaced tenants.
- The relocation consultant, Overland, Pacific and Cutler Inc., will be responsible for administering the relocation plan.
- The Borrower will conduct tenant orientation meetings prior to commencement of construction and during the rehabilitation period regarding the scope of work and timelines and to address any tenant issue or concerns regarding the project.
- Prior to closing the acquisition/construction loan the relocation budget and final plan are to be approved by HCD.

SPECIAL NEEDS SERVICES

- Thirty-five percent of the units (39 units) will serve senior households where one member is at risk of homeless and include at least one resident with a chronic illness.
- Tenant qualification will be determined through an independent needs assessment from the County of Santa Cruz Human Resources Agency and Adult & Long Term Care Division.
- Comprehensive services will be provided by partnerships with Senior Network Services for counseling, assessment and training; Central Coast Center for Independent Living for educational and peer support for tenants with physical disabilities. In-Home Supportive Services will provide a program for care-giving funded by the County of Santa Cruz Human Resources Agency, Division of Adult and Long Term Care.
- Other services include recreational and social service opportunities, exercise, nutrition and wellness classes.
- A part-time service provider will assist in the coordination of the services and providers and will be paid from the operating budget.

CalHFA's approval of the supportive services plan is required prior to closing the construction loan.
HOUSING SUPPLY AND DEMAND

- The market study defines the Primary Market Area (PMA) as areas including Capitola, Santa Cruz, Aptos, Soquel and Rio Del Mar. The Secondary Market Area (SMA) includes all of Santa Cruz County.
- The rental housing stock in the PMA is primarily comprised of market rate single family homes and apartments (1960's-1990's) in average to good condition.
- The market study found a strong need for affordable senior apartments in the PMA, citing the 98% to 100% occupancy rates of comparable market and affordable housing projects. None of the properties surveyed offered the level of services similar to the subject properties level of services.
- There are over 1,075 seniors in the PMA that have some level of disability and are chronically ill and the market study concluded that there is a very strong demand for senior housing with supportive services included.
- The properties' rents at the 50% AMI level are 38% to 39% below comparable market rents.
- The market study assumed 70% of the tenants would remain during rehabilitation and based on absorption rates of 20 units per month, it would take one month to achieve 100% occupancy of Supportive Housing units and units for the general senior population.

ENVIRONMENTAL

A Phase I Environmental Assessment was completed on June 12, 2006 by Confidential Compliance Consultants. The report recommended additional testing for Lead Based Paint and Asbestos Containing Materials due to the age of the property and the level of rehabilitation. Results of the additional testing will be incorporated into a remediation plan and environmental clearances are required prior to conversion to the permanent loan.

SEISMIC

The borrower has requested an earthquake insurance waiver and a review of this request is underway. If the waiver is denied, the loan amount may decrease so the earthquake insurance premium can be paid.

DEVELOPMENT TEAM

Borrower

Bay Avenue Senior Housing, L.P.

The project is to be owned by Bay Avenue Senior Housing, L.P. a California limited partnership. Bay Avenue Senior Housing, LLC will be the general partner. The sponsor, First Community Housing Corporation, a California nonprofit public benefit corporation (FCH) will be the sole member of Bay Avenue Senior Housing LLC and the general partner. FCH was founded in 1986 and has completed 15 projects containing over 900 units. Currently three projects with 212 units are in various stages of construction. CalHFA has financed loans for FCH on three
properties, Murphy Ranch Phase I and Phase II, Gish Apartments and Villa Montgomery, all of which have been completed and converted to permanent loans.

Management Agent

The John Stewart Company

The John Stewart Company was formed in 1978. They are a full service housing management, development and consulting company with over 1,000 employees. They manage over 200 properties totaling about 20,000 units, including several properties financed by CalHFA. They are the third largest manager of multifamily rental housing in California. They have significant experience managing special needs and supportive housing projects.

Architect

OJK Architects, Inc. (formerly the Office of Jerome King)

OJK Architects, Inc. was formed in 1981. The firm has extensive experience in historic restoration and adaptive reuse, commercial development, and affordable housing. They have designed eight affordable housing complexes, including Gish Apartments, Craig Gardens and Betty Ann Gardens, for First Community Housing. Craig Gardens, a senior project, won a "Best in Seniors Housing" award from the National Association of Home Builders and Betty Ann Gardens which was featured in a case study on best-practices on green-building by the Green Affordable Housing Coalition. Gish Apartments was recently awarded the "Gold" award by LEED for environmentally sustainable building practices.

Contractor

Branagh Construction

Branagh Construction has been in business since 1920, with projects ranging from educational facilities to churches, high-density residential, commercial, hotels and offices. Branagh is based in Oakland and its projects are primarily in the Bay Area. Branagh has built 4 projects developed by FCH totaling 265 units of high-density residential construction. They recently completed Villa Montgomery and Gish Apartments on time and on budget.
# PROJECT SUMMARY

**Project:** Bay Avenue Senior Apartments  
**Location:** 750 Bay Avenue  
**City:** Capitola  
**County:** Santa Cruz  
**Zip Code:** 95010  
**Project Type:** 33 units new construction, 76 units rehab.  
**Occupancy:** Senior  
**Total Units:** 109  
**Style Units:** Flats  
**Elevators:** Yes  
**Total Parking:** 81  
**Covered:** 0  
**Developer:** First Community Housing  
**Partner:** Bay Avenue Senior Housing LLC, GP  
**Investor:** Unknown  
**No. of Buildings:** 6  
**No. of Stories:** 5 two-story walk-up, 1 three story  
**Residential Space:** 86,687 sq. ft.  
**Office Space:** 3,080 sq. ft.  
**Commercial Space:** 0 sq. ft.  
**Gross Area:** 89,767 sq. ft.  
**Land Area:** 201,062 sq. ft.  
**Units per acre:** 24  

<table>
<thead>
<tr>
<th>CalHFA Construction Financing</th>
<th>Amount</th>
<th>Rate</th>
<th>Term (Mths)</th>
</tr>
</thead>
<tbody>
<tr>
<td>CalHFA Construction Financing - Taxable</td>
<td>$890,000</td>
<td>5.00%</td>
<td>24</td>
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</table>

<table>
<thead>
<tr>
<th>Permanent Sources of Funds</th>
<th>Amount</th>
<th>Rate</th>
<th>Years</th>
</tr>
</thead>
<tbody>
<tr>
<td>CalHFA First Mortgage</td>
<td>$6,600,000</td>
<td>3.00%</td>
<td>35</td>
</tr>
<tr>
<td>CalHFA Bridge Loan</td>
<td>$0</td>
<td>0.00%</td>
<td>0</td>
</tr>
<tr>
<td>CalHFA Gap Loan-Second Mortgage</td>
<td>$0</td>
<td>3.00%</td>
<td>30</td>
</tr>
<tr>
<td>MHP</td>
<td>$6,879,000</td>
<td>3.00%</td>
<td>55</td>
</tr>
<tr>
<td>City of Capitola-HOME</td>
<td>$1,900,000</td>
<td>3.00%</td>
<td>55</td>
</tr>
<tr>
<td>City of Capitola-RDA</td>
<td>$765,000</td>
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<td>55</td>
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<tr>
<td>AHP</td>
<td>$0</td>
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<td>30</td>
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<tr>
<td>Source 8</td>
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<tr>
<td>Source 9</td>
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<td>0.00%</td>
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<tr>
<td>Source 10</td>
<td>$0</td>
<td>0.00%</td>
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<tr>
<td>Income from Operations</td>
<td>$550,000</td>
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<td></td>
</tr>
<tr>
<td>Developer Contribution - city grant</td>
<td>$114,000</td>
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<td></td>
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<tr>
<td>Deferred Dev. Fee</td>
<td>$535,497</td>
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<tr>
<td>GP Equity</td>
<td>$854,139</td>
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<tr>
<td>Tax Credit Equity</td>
<td>$10,913,616</td>
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</table>

<table>
<thead>
<tr>
<th>Construction Valuation</th>
<th>Appraisal</th>
<th>Value Upon Completion</th>
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<tbody>
<tr>
<td>Investment Value</td>
<td>$25,460,000</td>
<td>Restricted Value $7,326,000</td>
</tr>
<tr>
<td>Loan / Cost</td>
<td>82%</td>
<td>Per. Loan / Cost 23%</td>
</tr>
<tr>
<td>Loan / Value</td>
<td>85%</td>
<td>Per. Loan / Value 90%</td>
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<table>
<thead>
<tr>
<th>CalHFA Fees and Reserve Requirements</th>
<th>Amount</th>
<th>Required Reserves</th>
<th>Amount</th>
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<tbody>
<tr>
<td>CalHFA Construction Loan Fee</td>
<td>$107,900</td>
<td>Operating Expense Reserve</td>
<td>$80,782</td>
</tr>
<tr>
<td>CalHFA Permanent Loan Fees</td>
<td>$16,500</td>
<td>Replacement Resv. Initial Deposit</td>
<td>$218,000</td>
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<tr>
<td>Other Fee</td>
<td>$0</td>
<td>Repl. Reserve - Per unit/per year</td>
<td>$400</td>
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<tr>
<td>Completion Guarantee Fee</td>
<td>$14,633,069</td>
<td>Capitalized Investor Reserve</td>
<td>$109,541</td>
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<tr>
<td>Contractors Payment Bond</td>
<td>$14,633,069</td>
<td>Rent-Up Reserve</td>
<td>$100,000</td>
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<tr>
<td>Contractors Performance Bond</td>
<td>$14,633,069</td>
<td></td>
<td></td>
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</tbody>
</table>

**Date:** 3/19/2008  
**Senior Staff Date:** 2/27/2008
### UNIT MIX AND RENT SUMMARY

**Bay Avenue Senior Apartments**

#### Total Unit Mix

<table>
<thead>
<tr>
<th># of Units</th>
<th>Unit Type</th>
<th># of Baths</th>
<th>Average Sq. Ft.</th>
</tr>
</thead>
<tbody>
<tr>
<td>64</td>
<td>1 Bedroom Flat</td>
<td>1</td>
<td>682</td>
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<tr>
<td>45</td>
<td>2 Bedroom Flat</td>
<td>1</td>
<td>815</td>
</tr>
<tr>
<td></td>
<td>2 Bedroom Townhome</td>
<td>1.5</td>
<td></td>
</tr>
<tr>
<td></td>
<td>2 Bedroom Townhome</td>
<td>2</td>
<td></td>
</tr>
<tr>
<td></td>
<td>3 Bedroom Townhome</td>
<td>2</td>
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<tr>
<td></td>
<td>4 Bedroom Townhome</td>
<td>2.5</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>109</td>
</tr>
</tbody>
</table>

#### Number of Regulated Units By Agency

<table>
<thead>
<tr>
<th>Agency</th>
<th>25%</th>
<th>30%</th>
<th>50%</th>
<th>55%</th>
<th>60%</th>
<th>Unrestricted</th>
<th>Total</th>
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</thead>
<tbody>
<tr>
<td>CalHFA</td>
<td></td>
<td></td>
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<td></td>
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<td>22</td>
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<tr>
<td>Tax Credits</td>
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<td></td>
<td></td>
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<td>106</td>
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<tr>
<td>Locality</td>
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<td></td>
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<td>HCD</td>
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<tr>
<td>HOME</td>
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<td>53</td>
<td>0</td>
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<td>109</td>
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<tr>
<td>City RDA</td>
<td>0</td>
<td>50</td>
<td>53</td>
<td>0</td>
<td>5</td>
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#### Restricted Rents Compared to Average Market Rents

<table>
<thead>
<tr>
<th>Median Income Rent Levels</th>
<th>Units Restricted</th>
<th>Restricted Rents</th>
<th>Avg. Market Rate Rents</th>
<th>Dollars Difference</th>
<th>% of Market</th>
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</thead>
<tbody>
<tr>
<td>One Bedroom</td>
<td></td>
<td></td>
<td>$1,100</td>
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<tr>
<td>25%</td>
<td>0</td>
<td>$0</td>
<td>$0</td>
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</tr>
<tr>
<td>30%</td>
<td>31</td>
<td>$424</td>
<td>$676</td>
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<tr>
<td>50%</td>
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<td>$728</td>
<td>$372</td>
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</tr>
<tr>
<td>60%</td>
<td>1</td>
<td>$728</td>
<td>$372</td>
<td>66%</td>
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<tr>
<td>Two Bedroom</td>
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<tr>
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</tr>
<tr>
<td>30%</td>
<td>19</td>
<td>$507</td>
<td>$793</td>
<td>39%</td>
<td></td>
</tr>
<tr>
<td>50%</td>
<td>21</td>
<td>$873</td>
<td>$427</td>
<td>67%</td>
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<tr>
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<td>$0</td>
<td>$427</td>
<td>67%</td>
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<td>60%</td>
<td>4</td>
<td>$873</td>
<td>$427</td>
<td>67%</td>
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<tr>
<td>Three Bedroom</td>
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<td></td>
</tr>
<tr>
<td>25%</td>
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<td>$0</td>
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</tr>
<tr>
<td>30%</td>
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</tr>
<tr>
<td>60%</td>
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<td>Four Bedroom</td>
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</tr>
<tr>
<td>25%</td>
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<tr>
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</tr>
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<td>60%</td>
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### Sources and Uses of Funds

#### Sources of Funds

<table>
<thead>
<tr>
<th>Source</th>
<th>Construction ($)</th>
<th>Permanent ($)</th>
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<tbody>
<tr>
<td>CalHFA Construction Financing - Taxable</td>
<td>22,470,000</td>
<td>6,600,000</td>
</tr>
<tr>
<td>CalHFA Construction Financing - Taxable</td>
<td>890,000</td>
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</tr>
<tr>
<td>Construction Only Source 3</td>
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<td>6,600,000</td>
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<td>CalHFA First Mortgage</td>
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<tr>
<td>CalHFA Gap Loan-Second Mortgage</td>
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<td>0</td>
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<tr>
<td>MHP</td>
<td></td>
<td>0</td>
</tr>
<tr>
<td>City of Capitola-HOME</td>
<td>1,900,000</td>
<td>0</td>
</tr>
<tr>
<td>City of Capitola-RDA</td>
<td>765,000</td>
<td>0</td>
</tr>
<tr>
<td>AHP</td>
<td></td>
<td>0</td>
</tr>
<tr>
<td>Source 8</td>
<td></td>
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</tr>
<tr>
<td>Source 9</td>
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</tr>
<tr>
<td>Source 10</td>
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<td>0</td>
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<tr>
<td>Source 11</td>
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</tr>
<tr>
<td>Source 12</td>
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<td>0</td>
</tr>
<tr>
<td>City of Capitola-HOME</td>
<td></td>
<td>0</td>
</tr>
<tr>
<td>City of Capitola-RDA</td>
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</tr>
<tr>
<td>AHP</td>
<td></td>
<td>0</td>
</tr>
<tr>
<td>Source 8</td>
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<tr>
<td>Source 9</td>
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<td>0</td>
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<tr>
<td>Source 10</td>
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<td>0</td>
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<tr>
<td>Source 11</td>
<td></td>
<td>0</td>
</tr>
<tr>
<td>Source 12</td>
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<td>0</td>
</tr>
<tr>
<td>Income from Operations</td>
<td>550,000</td>
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<td>Developer Contribution - City Grant</td>
<td>114,000</td>
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<td>Deferred Developer Fee</td>
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<td>535,497</td>
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<tr>
<td>GP Equity</td>
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<td>854,139</td>
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<tr>
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<td><strong>Total Sources</strong></td>
<td>27,234,000</td>
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<td><strong>Gap/ Surplus</strong></td>
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<td>4,450</td>
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<tr>
<td><strong>Total Development Sources</strong></td>
<td>29,111,252</td>
<td>267,076</td>
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<tr>
<td><strong>% of Total Sources</strong></td>
<td>100%</td>
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#### Uses of Funds

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<thead>
<tr>
<th>Category</th>
<th>Construction ($)</th>
<th>Permanent ($)</th>
</tr>
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<tbody>
<tr>
<td><strong>Loan Payoffs &amp; Rollovers</strong></td>
<td>23,360,000</td>
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<tr>
<td><strong>Acquisition</strong></td>
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<tr>
<td>Lesser of Land Cost or Value</td>
<td>2,200,000</td>
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<tr>
<td>Demolition</td>
<td>155,284</td>
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<tr>
<td>Legal - Acquisition Related Fees</td>
<td>10,000</td>
<td></td>
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<tr>
<td><strong>Subtotal - Land Cost / Value</strong></td>
<td>2,365,284</td>
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<tr>
<td>Existing Improvements Value</td>
<td>3,900,000</td>
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<tr>
<td>Off-Site Improvements</td>
<td>0</td>
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<tr>
<td><strong>Total Acquisition</strong></td>
<td>6,265,284</td>
<td></td>
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<tr>
<td><strong>Rehabilitation</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Site Work</td>
<td>494,068</td>
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<tr>
<td>Rehab to Structures</td>
<td>5,076,900</td>
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<tr>
<td>General Requirements</td>
<td>255,345</td>
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<tr>
<td>Contractors Overhead</td>
<td>426,431</td>
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<tr>
<td>Contractors Profit</td>
<td>201,152</td>
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<tr>
<td>Contractor's Bond</td>
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<tr>
<td>General Liability Insurance</td>
<td>0</td>
<td></td>
</tr>
<tr>
<td>Environmental Mitigation Expense</td>
<td>314,794</td>
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<tr>
<td><strong>Total Rehabilitation</strong></td>
<td>6,768,690</td>
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<tr>
<td><strong>Relocation Expenses</strong></td>
<td>200,000</td>
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<tr>
<td>Relocation Expense</td>
<td>200,000</td>
<td></td>
</tr>
<tr>
<td>Relocation Compliance Monitoring</td>
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<tr>
<td><strong>Total Relocation</strong></td>
<td>200,000</td>
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</table>

(Continued on Next 2 Pages)
# USES OF FUNDS (Cont’d):

<table>
<thead>
<tr>
<th>Costs</th>
<th>Construction ($)</th>
<th>Permanent ($)</th>
<th>Total Development Costs</th>
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</thead>
<tbody>
<tr>
<td><strong>NEW CONSTRUCTION</strong></td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>Site Work</td>
<td>1,291,233</td>
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<td>1,291,233</td>
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<tr>
<td>Structures (Hard Costs)</td>
<td>5,545,727</td>
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<tr>
<td>General Requirements</td>
<td>278,924</td>
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<td>278,924</td>
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<tr>
<td>Contractors Overhead</td>
<td>465,809</td>
<td>0</td>
<td>465,809</td>
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<tr>
<td>Contractors Profit</td>
<td>219,727</td>
<td>0</td>
<td>219,727</td>
</tr>
<tr>
<td>Contractor's Perf. &amp; Pymt Bond</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>General Liability Insurance</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Environmental Remediation</td>
<td>62,959</td>
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<td>62,959</td>
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<tr>
<td><strong>Total Construction Contract</strong></td>
<td>7,864,379</td>
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<td>7,864,379</td>
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<tr>
<td>Joint Trench/Utility Work</td>
<td>50,000</td>
<td>0</td>
<td>50,000</td>
</tr>
<tr>
<td><strong>Total New Construction</strong></td>
<td>7,914,379</td>
<td>0</td>
<td>7,914,379</td>
</tr>
</tbody>
</table>

| **ARCHITECTURAL & ENGINEERING** | | | |
| Architectural Design | 550,000 | 0 | 550,000 | 5,046 | 2% |
| Architect's Supv during Construction | 100,000 | 0 | 100,000 | 917 | 0% |
| **Total Architectural** | 650,000 | 0 | 650,000 | 5,963 | 2% |
| Engineering Expense | 25,000 | 0 | 25,000 | 229 | 0% |
| Engineers Supv. during Construction | 0 | 0 | 0 | 0% |
| ALTA Survey | 10,000 | 0 | 10,000 | 92 | 0% |
| **Total Engineering & Survey** | 35,000 | 0 | 35,000 | 321 | 0% |

| **CONSTRUCTION LOAN COSTS** | | | |
| Construction Loan Interest | 1,517,111 | 0 | 1,517,111 | 13,918 | 5% |
| CalHFA Construction Loan Fee | 107,900 | 0 | 107,900 | 990 | 0% |
| Other Construction Loan Fees | 0 | 0 | 0 | 0% |
| CalHFA Legal Counsel Fees | 0 | 0 | 0 | 0% |
| Other Lender Req'd Legal Fees | 0 | 0 | 0 | 0% |
| Title and Recording fees | 15,000 | 0 | 15,000 | 138 | 0% |
| CalHFA Req'd Inspection Fees | 15,000 | 0 | 15,000 | 138 | 0% |
| Other Req'd Inspection Fees | 0 | 0 | 0 | 0% |
| Prevailing Wage Monitoring Expense | 0 | 0 | 0 | 0% |
| Taxes, Insurance,bonds during construction | 310,000 | 0 | 310,000 | 2,844 | 1% |
| Predevelopment Interest | 0 | 0 | 0 | 0% |
| **Total Construction Loan Expense** | 1,965,011 | 0 | 1,965,011 | 18,028 | 7% |

| **PERMANENT LOAN COSTS** | | | |
| CalHFA Perm Loan Fees | 16,500 | 0 | 16,500 | 151 | 0% |
| CalHFA Bridge Loan Fees | 0 | 0 | 0 | 0% |
| CalHFA Loan Application Fee | 500 | 0 | 500 | 5 | 0% |
| Other Lender Perm. Loan Fees | 0 | 0 | 0 | 0% |
| Title and Recording | 0 | 20,000 | 20,000 | 183 | 0% |
| Perm. Bridge Loan Interest Expense | 0 | 0 | 0 | 0% |
| Bond Origination Guarantee Fee | 0 | 0 | 0 | 0% |
| Tax Exempt Bond Allocation Fee | 600 | 0 | 600 | 6 | 0% |
| Other | 0 | 0 | 0 | 0% |
| **Total Permanent Loan Expense** | 17,600 | 20,000 | 37,600 | 345 | 0% |

<p>| <strong>LEGAL FEES</strong> | | | |
| Borrower Legal Fee | 25,000 | 10,000 | 35,000 | 321 | 0% |
| Syndication Legal | 35,000 | 0 | 35,000 | 321 | 0% |
| <strong>Total Attorney Expense</strong> | 60,000 | 10,000 | 70,000 | 642 | 0% |</p>
<table>
<thead>
<tr>
<th>USES OF FUNDS (Cont'd):</th>
<th>Construction ($)</th>
<th>Permanent ($)</th>
<th>Total Development Costs</th>
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<tbody>
<tr>
<td><strong>CONTRACT / REPORT COSTS</strong></td>
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<tr>
<td>Appraisal</td>
<td>10,000</td>
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<tr>
<td>Market Study</td>
<td>10,000</td>
<td>0</td>
<td>10,000</td>
</tr>
<tr>
<td>Physical Needs Assessment</td>
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<td>0</td>
<td>10,000</td>
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<td>HUD Risk Share Environ. Review</td>
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<td>CalHFA EQ Waiver Seismic Review Fee</td>
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<td>12,000</td>
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<td>Environmental Phase I / II Reports</td>
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<td>Soils / Geotech Reports</td>
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<tr>
<td>Asbestos / Lead-based Paint Report</td>
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<td>10,000</td>
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<tr>
<td>Noise/Acoustical/Traffic Study Report</td>
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<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Other</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Other</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td><strong>Total Contract Costs</strong></td>
<td>52,000</td>
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<td>52,000</td>
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<tr>
<td><strong>CONTINGENCY</strong></td>
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<tr>
<td>Hard Cost Contingency</td>
<td>1,282,825</td>
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<td>1,282,825</td>
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<tr>
<td>Soft Cost Contingency</td>
<td>171,000</td>
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<td>171,000</td>
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<tr>
<td><strong>Total Contingency</strong></td>
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<td>1,453,825</td>
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<td><strong>RESERVES</strong></td>
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<td>CalHFA Operating Expense Reserve</td>
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<td>80,782</td>
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<tr>
<td>Construction Defects Reserve</td>
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<tr>
<td>Rent-Up Reserve</td>
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<td>100,000</td>
<td>100,000</td>
</tr>
<tr>
<td>Capitalized Investor Req'd Reserve</td>
<td>0</td>
<td>109,541</td>
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<tr>
<td>Capitalized Replacement Reserve</td>
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<td>218,000</td>
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<tr>
<td><strong>Total Reserves</strong></td>
<td>0</td>
<td>508,323</td>
<td>508,323</td>
</tr>
<tr>
<td><strong>OTHER</strong></td>
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<td></td>
<td></td>
</tr>
<tr>
<td>CTCAC App/Alloc/Monitor Fees</td>
<td>46,690</td>
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<td>46,690</td>
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<td>Local Permit Fees</td>
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<tr>
<td>Local Development Impact Fees</td>
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<tr>
<td>Other Local Fees</td>
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<td>0</td>
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<tr>
<td>Advertising &amp; Marketing Expenses</td>
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<tr>
<td>1st Year Taxes &amp; Insurance</td>
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<tr>
<td>Furnishings</td>
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<tr>
<td>Final Cost Audit Expense</td>
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<tr>
<td>Miscellaneous Admin Fees</td>
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<tr>
<td><strong>Total Other Expenses</strong></td>
<td>601,690</td>
<td>30,000</td>
<td>631,690</td>
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<tr>
<td><strong>SUBTOTAL PROJECT COSTS</strong></td>
<td>25,983,479</td>
<td>23,928,323</td>
<td>26,551,802</td>
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<tr>
<td><strong>DEVELOPER COSTS</strong></td>
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<tr>
<td>Developer Overhead/Profit (5% Acq.)</td>
<td>301,071</td>
<td>2,198,929</td>
<td>2,500,000</td>
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<tr>
<td>Developer Overhead/Profit (NC/Rehab)</td>
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<td>0</td>
<td>0</td>
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<tr>
<td>Consultant / Processing Agent</td>
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<tr>
<td>Project Administration</td>
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<td>0</td>
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<tr>
<td>Broker Fees to a related party</td>
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<td>0</td>
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<tr>
<td>Construction Mgmt/Testing</td>
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<tr>
<td><strong>Total Developer Fee / Costs</strong></td>
<td>356,871</td>
<td>2,198,929</td>
<td>2,555,000</td>
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<td><strong>Total Costs</strong></td>
<td>26,339,550</td>
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<td>29,106,802</td>
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## Annual Operating Budget

### Bay Avenue Senior Apartments

#### Final Commitment

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<tr>
<th>INCOME:</th>
<th>$ Amount</th>
<th>Per Unit</th>
<th>% of Total</th>
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<tr>
<td>Total Rental Income</td>
<td>$833,892</td>
<td>$7,650</td>
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<tr>
<td>Laundry</td>
<td>$12,016</td>
<td>$110</td>
<td>1.42%</td>
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<tr>
<td>Other Income</td>
<td>$0</td>
<td>$0</td>
<td>0.00%</td>
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<tr>
<td><strong>Gross Potential Income (GPI)</strong></td>
<td><strong>$845,908</strong></td>
<td><strong>$7,761</strong></td>
<td><strong>100.00%</strong></td>
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<table>
<thead>
<tr>
<th>Less:</th>
<th>$ Amount</th>
<th>Per Unit</th>
<th>% of Total</th>
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<tbody>
<tr>
<td>Vacancy Loss</td>
<td>$38,084</td>
<td>$349</td>
<td>4.71%</td>
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<tr>
<td><strong>Effective Gross Income</strong></td>
<td><strong>$807,824</strong></td>
<td><strong>$7,411</strong></td>
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</table>

<table>
<thead>
<tr>
<th>EXPENSES:</th>
<th>Total Cost</th>
<th>Per Unit</th>
<th>% of Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Payroll</td>
<td>$172,101</td>
<td>$1,579</td>
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<tr>
<td>Administrative</td>
<td>$45,915</td>
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<td>10.58%</td>
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<tr>
<td>Management fee</td>
<td>$43,600</td>
<td>$400</td>
<td>10.05%</td>
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<tr>
<td>Utilities</td>
<td>$67,730</td>
<td>$621</td>
<td>15.61%</td>
</tr>
<tr>
<td>Operating and Maintenance</td>
<td>$63,029</td>
<td>$578</td>
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<tr>
<td>Insurance and Business Taxes</td>
<td>$33,050</td>
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<td>Locality Compliance Monitoring Fee</td>
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<td>0.00%</td>
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<tr>
<td><strong>Subtotal Expenses</strong></td>
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<td><strong>$3,903</strong></td>
<td><strong>98.06%</strong></td>
</tr>
<tr>
<td>Replacement Reserves</td>
<td>$0</td>
<td>$0</td>
<td>0.00%</td>
</tr>
<tr>
<td>Taxes, Assessments, Other</td>
<td>$8,430</td>
<td>$77</td>
<td>1.94%</td>
</tr>
<tr>
<td><strong>Total Expenses</strong></td>
<td><strong>$433,855</strong></td>
<td><strong>$3,980</strong></td>
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#### Financial Expenses

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**NET OPERATING INCOME**

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<tr>
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<tr>
<td><strong>RENTAL INCOME</strong></td>
<td>Year 1</td>
<td>Year 2</td>
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<td>0%</td>
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<td>854,739</td>
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<tr>
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<tr>
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<tr>
<td><strong>TOTAL OTHER INCOME</strong></td>
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<td>12,316</td>
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<td>867,056</td>
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<td>Unrestricted Units / Market Rate Units</td>
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<td>Annual Tax Increase</td>
<td>0.00%</td>
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<td>Replacement Reserve</td>
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<tr>
<td>Percentage Increase Yearly</td>
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### Cash Flow

**CalHFA Project Number:** 08-002  
**Bay Avenue Senior Apartments**

<table>
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<tr>
<th>RENTAL INCOME</th>
<th>Year 11</th>
<th>Year 12</th>
<th>Year 13</th>
<th>Year 14</th>
<th>Year 15</th>
<th>Year 16</th>
<th>Year 17</th>
<th>Year 18</th>
<th>Year 19</th>
<th>Year 20</th>
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<tbody>
<tr>
<td>Affordable Rents</td>
<td>1,054,165</td>
<td>1,080,519</td>
<td>1,107,532</td>
<td>1,135,220</td>
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<td>1,192,691</td>
<td>1,222,508</td>
<td>1,253,071</td>
<td>1,284,396</td>
<td>1,316,508</td>
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<td>2.50%</td>
<td>2.50%</td>
<td>2.50%</td>
<td>2.50%</td>
<td>2.50%</td>
<td>2.50%</td>
<td>2.50%</td>
<td>2.50%</td>
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<tr>
<td>Rental Subsidies</td>
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<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
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<tr>
<td>Rental Subsidy Increases</td>
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<td>0%</td>
<td>0%</td>
<td>0%</td>
<td>0%</td>
<td>0%</td>
<td>0%</td>
<td>0%</td>
<td>0%</td>
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<tr>
<td>Market Rate Units</td>
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<td>13,619</td>
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<td>15,409</td>
<td>15,794</td>
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<td>16,594</td>
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<td>2.50%</td>
<td>2.50%</td>
<td>2.50%</td>
<td>2.50%</td>
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<td>1,237,917</td>
<td>1,268,865</td>
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<table>
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<th>Year 16</th>
<th>Year 17</th>
<th>Year 18</th>
<th>Year 19</th>
<th>Year 20</th>
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</thead>
<tbody>
<tr>
<td>Laundry</td>
<td>15,381</td>
<td>15,768</td>
<td>16,160</td>
<td>16,564</td>
<td>16,978</td>
<td>17,403</td>
<td>17,838</td>
<td>18,284</td>
<td>18,741</td>
<td>19,209</td>
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<tr>
<td>Other Income</td>
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<td>2.50%</td>
<td>2.50%</td>
<td>2.50%</td>
<td>2.50%</td>
<td>2.50%</td>
<td>2.50%</td>
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<td>0</td>
<td>0</td>
<td>0</td>
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<tr>
<td><strong>TOTAL OTHER INCOME</strong></td>
<td>15,381</td>
<td>15,768</td>
<td>16,160</td>
<td>16,564</td>
<td>16,978</td>
<td>17,403</td>
<td>17,838</td>
<td>18,284</td>
<td>18,741</td>
<td>19,209</td>
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<table>
<thead>
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<th>Year 14</th>
<th>Year 15</th>
<th>Year 16</th>
<th>Year 17</th>
<th>Year 18</th>
<th>Year 19</th>
<th>Year 20</th>
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</thead>
<tbody>
<tr>
<td>Affordable (Blended Average)</td>
<td>4.50%</td>
<td>4.50%</td>
<td>4.50%</td>
<td>4.50%</td>
<td>4.50%</td>
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<td>4.50%</td>
<td>4.50%</td>
<td>4.50%</td>
<td>4.50%</td>
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<tr>
<td>Rental Subsidy Income</td>
<td>0%</td>
<td>0%</td>
<td>0%</td>
<td>0%</td>
<td>0%</td>
<td>0%</td>
<td>0%</td>
<td>0%</td>
<td>0%</td>
<td>0%</td>
</tr>
<tr>
<td>Unrestricted Units / Market Rate Units</td>
<td>5.00%</td>
<td>5.00%</td>
<td>5.00%</td>
<td>5.00%</td>
<td>5.00%</td>
<td>5.00%</td>
<td>5.00%</td>
<td>5.00%</td>
<td>5.00%</td>
<td>5.00%</td>
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<tr>
<td>Laundry &amp; Other Income</td>
<td>5.00%</td>
<td>5.00%</td>
<td>5.00%</td>
<td>5.00%</td>
<td>5.00%</td>
<td>5.00%</td>
<td>5.00%</td>
<td>5.00%</td>
<td>5.00%</td>
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<td>49,970</td>
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<th>Year 18</th>
<th>Year 19</th>
<th>Year 20</th>
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<td>771,782</td>
<td>798,794</td>
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<td>3.50%</td>
<td>3.50%</td>
<td>3.50%</td>
<td>3.50%</td>
<td>3.50%</td>
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<tr>
<td>Annual Expense Increase</td>
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<td>2.00%</td>
<td>2.00%</td>
<td>2.00%</td>
<td>2.00%</td>
<td>2.00%</td>
<td>2.00%</td>
<td>2.00%</td>
<td>2.00%</td>
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<tr>
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<td>2.00%</td>
<td>2.00%</td>
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<td>2.00%</td>
<td>2.00%</td>
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<tr>
<td>Replacement Reserve</td>
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<td>0.00%</td>
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<td>0.00%</td>
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<th>Year 12</th>
<th>Year 13</th>
<th>Year 14</th>
<th>Year 15</th>
<th>Year 16</th>
<th>Year 17</th>
<th>Year 18</th>
<th>Year 19</th>
<th>Year 20</th>
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<tr>
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<td>407,618</td>
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</table>

| DEBT COVERAGE RATIO | 1.13 | 1.14 | 1.16 | 1.17 | 1.18 | 1.19 | 1.20 | 1.21 | 1.22 | 1.23 |
### Cash Flow

#### CALIFORNIA HOMELAND FUNDING ASSISTANCE (CALHFA)

**CalHFA Project Number: 08-002**

**Bay Avenue Senior Apartments**

<table>
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<th>Year</th>
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<th>Year 22</th>
<th>Year 23</th>
<th>Year 24</th>
<th>Year 25</th>
<th>Year 26</th>
<th>Year 27</th>
<th>Year 28</th>
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<td>1624285</td>
<td>1664861</td>
<td>1706483</td>
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</tbody>
</table>

#### OTHER INCOME

- **Laundry:** 19690, 20182, 20686, 21204, 21734, 22277, 22834, 23405, 23990, 24590
- **Other Income Increase:** 0, 0, 0, 0, 0, 0, 0, 0, 0, 0

#### NET RENTAL INCOME

- **Total Other Income:** 19690, 20182, 20686, 21204, 21734, 22277, 22834, 23405, 23990, 24590

#### GROSS POTENTIAL INCOME

- **Vacancy Assumptions:**
  - Affordable Blended Average: 4.50%
  - Rental Subsidy Income: 0%
  - Unrestricted Units / Market Rate Units: 5.00%
  - Laundry & Other Income: 5.00%

#### EFFECTIVE GROSS INCOME

- **Total:** 62405, 63965, 65564, 67204, 68884, 70606, 72371, 74180, 76035, 77935

#### OPERATING EXPENSES

- **Expenses:**
  - Annual Expense Increase: 85688, 885637, 916635, 948717, 981922, 1016289, 1051860, 1088675, 1126778, 1166215
  - Taxes and Assessments: 3.50%

#### TOTAL EXPENSES

- **Total:** 911830, 941892, 973005, 1005205, 1038351, 1075544, 1111240, 1148182, 1186416, 1225986

#### NET OPERATING INCOME

- **Total:** 411884, 414914, 417721, 420289, 422601, 422118, 423862, 425297, 426400, 427151

#### DEBT SERVICE

- **CalHFA - 1st Mortgage:** 304801, 304801, 304801, 304801, 304801, 304801, 304801, 304801, 304801, 304801
- **CalHFA - Bridge Loan:** 0, 0, 0, 0, 0, 0, 0, 0, 0, 0
- **CalHFA - 2nd Mortgage:** 28892, 28892, 28892, 28892, 28892, 28892, 28892, 28892, 28892, 28892
- **MHP:** 0, 0, 0, 0, 0, 0, 0, 0, 0, 0
- **None:** 0, 0, 0, 0, 0, 0, 0, 0, 0, 0

#### DEBT COVERAGE RATIO

- **Total:** 1.23, 1.24, 1.25, 1.26, 1.27, 1.26, 1.27, 1.27, 1.28, 1.28
<table>
<thead>
<tr>
<th>Cash Flow</th>
<th>CalHFA Project Number: 08-002</th>
<th>Bay Avenue Senior Apartments</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>RENTAL INCOME</strong></td>
<td>Year 31</td>
<td>Year 32</td>
</tr>
<tr>
<td>Affordable Rents</td>
<td>1,727,372</td>
<td>1,770,556</td>
</tr>
<tr>
<td>Affordable Rent Increase</td>
<td>2.50%</td>
<td>2.50%</td>
</tr>
<tr>
<td>Rental Subsidies</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Rental Subsidy Increase</td>
<td>0%</td>
<td>0%</td>
</tr>
<tr>
<td>Market Rate Units</td>
<td>21,773</td>
<td>22,317</td>
</tr>
<tr>
<td>unrestricted/Market Unit Increases</td>
<td>2.50%</td>
<td>2.50%</td>
</tr>
<tr>
<td><strong>TOTAL RENTAL INCOME</strong></td>
<td>1,749,145</td>
<td>1,792,873</td>
</tr>
<tr>
<td><strong>OTHER INCOME</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Laundry</td>
<td>25,204</td>
<td>25,834</td>
</tr>
<tr>
<td>Other Income</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Other Income Increase</td>
<td>2.50%</td>
<td>2.50%</td>
</tr>
<tr>
<td><strong>TOTAL OTHER INCOME</strong></td>
<td>25,204</td>
<td>25,834</td>
</tr>
<tr>
<td><strong>GROSS POTENTIAL INCOME</strong></td>
<td>1,774,349</td>
<td>1,818,708</td>
</tr>
<tr>
<td><strong>VACANCY ASSUMPTIONS</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Affordable (Blerded Average)</td>
<td>4.50%</td>
<td>4.50%</td>
</tr>
<tr>
<td>Rental Subsidy Income</td>
<td>0%</td>
<td>0%</td>
</tr>
<tr>
<td>Unrestricted Units / Market Rate Units</td>
<td>5.00%</td>
<td>5.00%</td>
</tr>
<tr>
<td>Laundry &amp; Other Income</td>
<td>5.00%</td>
<td>5.00%</td>
</tr>
<tr>
<td><strong>LESS: VACANCY LOSS</strong></td>
<td>79,884</td>
<td>81,881</td>
</tr>
<tr>
<td><strong>EFFECTIVE GROSS INCOME</strong></td>
<td>1,694,465</td>
<td>1,736,827</td>
</tr>
<tr>
<td><strong>OPERATING EXPENSES</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Expenses</td>
<td>1,207,033</td>
<td>1,249,279</td>
</tr>
<tr>
<td>Annual Expense Increase</td>
<td>3.50%</td>
<td>3.50%</td>
</tr>
<tr>
<td>Taxes and Assessments</td>
<td>6,910</td>
<td>7,049</td>
</tr>
<tr>
<td>Annual Tax Increase</td>
<td>2.00%</td>
<td>2.00%</td>
</tr>
<tr>
<td>Replacement Reserve</td>
<td>52,996</td>
<td>55,646</td>
</tr>
<tr>
<td>Percentage Increase Yearly</td>
<td>5.00%</td>
<td>0.00%</td>
</tr>
<tr>
<td><strong>TOTAL EXPENSES</strong></td>
<td>1,266,939</td>
<td>1,311,974</td>
</tr>
<tr>
<td><strong>NET OPERATING INCOME</strong></td>
<td>427,526</td>
<td>424,853</td>
</tr>
<tr>
<td><strong>DEBT SERVICE</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>CalHFA - 1st Mortgage</td>
<td>304,801</td>
<td>304,801</td>
</tr>
<tr>
<td>CalHFA - Bridge Loan</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>MHP</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>None</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td><strong>DEBT COVERAGE RATIO</strong></td>
<td>1.28</td>
<td>1.27</td>
</tr>
</tbody>
</table>
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RESOLUTION 08-07

RESOLUTION AUTHORIZING A FINAL LOAN COMMITMENT

WHEREAS, the California Housing Finance Agency (the "Agency") has received a loan application on behalf of Bay Avenue Senior Housing, L.P., a California limited partnership (the "Borrower"), seeking a loan commitment, the proceeds of which are to be used to provide financing for a multifamily housing development located in Capitola, Santa Cruz County, California, to be known as Bay Avenue Senior Apartments (the "Development"); and

WHEREAS, the loan application has been reviewed by Agency staff which prepared a report presented to the Board on the meeting date recited below (the "Staff Report"), recommending Board approval subject to certain recommended terms and conditions; and

WHEREAS, Section 1.150-2 of the Treasury Regulations requires the Agency, as the issuer of tax-exempt bonds, to declare its reasonable official intent to reimburse prior expenditures for the Development with proceeds of a subsequent borrowing; and

WHEREAS, on January 18, 2008, the Executive Director exercised the authority delegated to her under Resolution 94-10 to declare the official intent of the Agency to reimburse such prior expenditures for the Development; and

WHEREAS, based upon the recommendation of staff and due deliberation by the Board, the Board has determined that a final loan commitment be made for the Development;

1. The Executive Director, or in his/her absence, either the Chief Deputy Director or the Director of Multifamily Programs of the Agency is hereby authorized to execute and deliver a final commitment letter, in a form acceptable to the Agency, and subject to recommended terms and conditions set forth in the Staff Report, in relation to the Development described above and as follows:

<table>
<thead>
<tr>
<th>PROJECT NUMBER</th>
<th>DEVELOPMENT NAME/LOCALITY</th>
<th>MORTGAGE AMOUNT</th>
</tr>
</thead>
<tbody>
<tr>
<td>08-002-C/N</td>
<td>Bay Avenue Senior Apartments Capitola, Santa Cruz County California</td>
<td>$21,580,000 Acq/Const. Tax-Exempt 1st Mortgage</td>
</tr>
<tr>
<td></td>
<td></td>
<td>$ 890,000 Acq/Const. Taxable 1st Mortgage</td>
</tr>
<tr>
<td></td>
<td></td>
<td>$ 6,600,000 Permanent Tax-Exempt 1st Mortgage</td>
</tr>
</tbody>
</table>
2. The Executive Director may modify the terms and conditions of the loans or loans as described in the Staff Report, provided that major modifications, as defined below, must be submitted to this Board for approval. "Major modifications" as used herein means modifications which either (i) increase the total aggregate amount of any loans made pursuant to the Resolution by more than 7%; or (ii) modifications which in the judgment of the Executive Director, or in his/her absence, either the Chief Deputy Director or the Director of Multifamily Programs of the Agency, adversely change the financial or public purpose aspects of the final commitment in a substantial way.

I hereby certify that this is a true and correct copy of Resolution 08-07 adopted at a duly constituted meeting of the Board of the Agency held on March 19, 2008, at Sacramento, California.

ATTEST: ____________________________
Secretary
State of California

MEMORANDUM

To: Board of Directors

Date: March 6, 2008

Bruce D. Gilbertson, Director of Financing

From: CALIFORNIA HOUSING FINANCE AGENCY

Subject: RESOLUTION 08-08 AMENDING AND RESTATING BOARD RESOLUTION 08-04 TO PERMIT THE USE OF ADDITIONAL FORMS OF BOND INDENTURES TO FINANCE MULTIFAMILY HOUSING PROJECTS

Attached for the Board’s consideration is Resolution 08-08 that amends and restates Resolution 08-04 (the Prior Resolution) to include a new form of bond indenture to be used for financing subordinate multifamily loans.

The Prior Resolution, as approved by the board of directors at its January 17, 2008 meeting, authorizes the issuance of bonds from a list of twenty prior bond indentures to provide financing to developers of affordable rental housing. Resolution 08-08 would amend Section 3 of the Prior Resolution to authorize the issuance of bonds under one additional new form of bond indenture; the Multifamily Housing Revenue Bonds Subordinate Loan Indenture (MHRSL Indenture). The MHRSL Indenture will be a limited obligation, conduit revenue bond indenture used to provide capital to finance subordinate loans for multifamily properties that utilize Agency bond programs to provide the primary financing of an affordable housing project. The Agency will not take any credit risk with respect to subordinate loans funded under the MHRSL Indenture.

The Agency currently intends to issue bonds under the MHRSL Indenture to finance a second mortgage in regards to Grand Plaza Apartments, which the final loan commitment to the borrower was approved by the board at the January 17, 2008 board meeting.

Bonds issued under the MHRSL Indenture will be unrated securities privately placed to sophisticated investors secured by a promissory note and a deed of trust. No additional credit enhancement, from the Agency or otherwise, will be provided to investors of the MHRSL bonds.

Attachment
RESOLUTION NO. 08-08

AMENDING AND RESTATING RESOLUTION NO. 08-04

AMENDED AND RESTATED RESOLUTION OF THE CALIFORNIA HOUSING FINANCE AGENCY 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

WHEREAS, the California Housing Finance Agency (the “Agency”) has determined that there exists a need in California for the financing of mortgage loans for the construction or development of multi-unit rental housing developments for the purpose of providing housing for persons and families of low or moderate income (the “Developments”);

WHEREAS, the Agency has determined that it is in the public interest for the Agency to provide such financial assistance by means of an ongoing program (the “Program”) to make or acquire, or to make loans to lenders to make or acquire, mortgage loans for the purpose of financing such Developments (the “Loans”);

WHEREAS, pursuant to Parts 1 through 4 of Division 31 of the Health and Safety Code of the State of California (the “Act”), the Agency has the authority to issue bonds to provide sufficient funds to finance the Program, including the making of Loans, the payment of capitalized interest on the bonds, the establishment of reserves to secure the bonds, the payment of other costs of the Agency incident to, and necessary or convenient to, the issuance of the bonds, and for the other purposes provided by Sections 51065.5 and 51365 of the Act; and

WHEREAS, pursuant to the Act, the Agency has the authority to enter into short-term credit facilities for the purpose of financing the Program, including the making of Loans and the payment of other costs of the Agency incident to, and necessary or convenient to, the issuance of the bonds;

WHEREAS, the Agency wishes to add a new form of bond indenture (the Multifamily Housing Revenue Bonds Subordinate Loan Indenture);

NOW, THEREFORE, BE IT RESOLVED, by the California Housing Finance Agency as follows:

Section 1. Determination of Need and Amount. The Agency is of the opinion and hereby determines that the offer, sale and issuance of one or more series of multifamily housing revenue bonds (the “Bonds”) in an aggregate amount not to exceed the sum of the following amounts is necessary to provide sufficient funds for the Program:

(a) the aggregate amount of prior multifamily bonds of the Agency (or of other issuers to the extent permitted by law) to be redeemed or maturing in connection with such issuance;
the aggregate amount of private activity bond allocations under federal tax law heretofore or hereafter made available to the Agency for such purpose;

if and to the extent the Bonds are “qualified 501(c)(3) bonds” under federal tax law, are not “private activity bonds” under federal tax law, or are determined by the Executive Director of the Agency (the “Executive Director”) to be intended not to be tax-exempt for federal income tax purposes, $800,000,000; and

if and to the extent the Bonds are issued for the purpose of financing or refinancing the acquisition of existing Loans that finance existing Developments, or for the purpose of refinancing such Developments, $300,000,000.

Section 2. Authorization and Timing. The Bonds are hereby authorized to be issued at such time or times on or before the day 30 days after the date on which is held the first meeting in the year 2008 of the Board of Directors of the Agency at which a quorum is present, as the Executive Director deems appropriate, upon consultation with the Treasurer of the State of California (the “Treasurer”) as to the timing of each such issuance; provided, however, that if the Bonds are sold at a time on or before the day 30 days after the date on which is held such meeting, pursuant to a forward purchase or drawdown agreement providing for the issuance of such Bonds on a later date on or before August 1, 2010, upon specified terms and conditions, such Bonds may be issued on such later date; and provided, further, that Bonds being issued to refund Bonds of the type described in Section 1(d) of this resolution or to refinance Developments financed by Bonds of the type described in such Section 1(d) may be issued at any time prior to the original maturity date of the original Loans financed by such Bonds.

Section 3. Approval of Indentures, Supplemental Indentures and Certain Other Financing Documents. (a) The Executive Director and the Secretary of the Board of Directors of the Agency (the “Secretary”) are hereby authorized and directed, for and on behalf and in the name of the Agency in connection with the issuance of Bonds, to execute and acknowledge and to deliver to a duly qualified bank or trust company selected by the Executive Director to act, with the approval of the Treasurer, as trustee (the “Trustee”), one or more new indentures (the “New Indentures”), in one or more forms similar to one or more of the following (collectively, the “Prior Indentures”):

1. the Multi-Family Revenue Bonds (Federally Insured Loans) Indenture, dated as of April 17, 1979;
2. the Multi-Unit Rental Housing Revenue Bonds Indenture, dated as of July 12, 1979;
3. the Rental Housing Revenue Bonds (FHA Insured Loans) Indenture, dated as of June 1, 1982;
4. the Multi-Unit Rental Housing Revenue Bonds II Indenture, dated as of September 1, 1982;
5. the Multifamily Rehabilitation Revenue Bonds, 1983 Issue A Indenture, dated as of December 1, 1983;
the Multifamily Housing Revenue Bond (Insured Letter of Credit 1984-I) Indenture, dated as of March 1, 1984;

(7) the Housing Revenue Bond Indenture, dated as of July 1, 1984;

(8) the Multifamily Rehabilitation Revenue Bond, 1985 Issue A, Indenture, dated as of March 1, 1985;

(9) the form of indenture approved by the Board of Directors of the Agency at its May 11, 1989 meeting for the Financial Guaranty Insurance Company program;

(10) the Housing Revenue Bond II Indenture, dated as of July 1, 1992;

(11) the Multifamily Housing Revenue Refunding Bond Indentures, dated as of July 1, 1993 (including as originally delivered and as amended and restated);

(12) the Multifamily Housing Revenue Bond (Tara Village Apartments), 1994 Series A, Indenture, dated as of November 1, 1994;

(13) the Multifamily Housing Revenue Bond (FHA Insured Mortgage Loans) Indenture, dated February 1, 1995;

(14) the Multifamily Housing Revenue Bond II Indenture, dated as of October 1, 1995;

(15) the Multifamily Housing Revenue Bond III Indenture, dated as of March 1, 1997;

(16) the form of commercial paper note indenture presented to the May 11, 2000 meeting of the Agency;

(17) the Multifamily Loan Purchase Bond Indenture, dated as of July 1, 2000;

(18) the form of draw down bond indenture approved by Resolution No. 01-05, as amended by Resolution No. 01-39, adopted November 8, 2001;

(19) the form of bond indenture approved by Resolution No. 02-02, as amended by Resolution 02-17, adopted June 6, 2002;

(20) the Housing Program Bond Indenture, dated as of November 1, 2004; or

(21) the Multifamily Housing Revenue Bonds Subordinate Loan Indenture, the form of which is attached hereto.

Each such New Indenture may be executed, acknowledged and delivered with such changes therein as the officers executing the same approve upon consultation with the Agency's legal counsel, such approval to be conclusively evidenced by the execution and delivery thereof.

(b) For each series of Bonds, the Executive Director and the Secretary are hereby authorized and directed, for and on behalf and in the name of the Agency, if appropriate, to
execute and acknowledge and to deliver with respect to each series of Bonds, a supplemental indenture (a “Supplemental Indenture”) under either one of the Prior Indentures or a New Indenture and in substantially the form of any supplemental indenture or series indenture executed or approved in connection with any of the Prior Indentures, in each case, with such changes therein as the officers executing the same approve upon consultation with the Agency’s legal counsel, such approval to be conclusively evidenced by the execution and delivery thereof.

The Executive Director is hereby expressly authorized and directed, for and on behalf and in the name of the Agency, to determine in furtherance of the objectives of the Program those matters required to be determined under the applicable Prior Indenture or the New Indentures, as appropriate, in connection with the issuance of each such series.

(c) For each series of Bonds, the Executive Director is hereby authorized and directed to execute, and the Secretary is hereby authorized to attest, for and in the name and on behalf of the Agency and under its seal, if and to the extent appropriate, a reimbursement agreement, a letter of credit agreement or any other arrangement with respect to credit enhancement or liquidity support in substantially the forms of the reimbursement agreements, letter of credit agreements or other such arrangements contemplated under the Prior Indentures or New Indentures or used in connection with the bonds issued under one or more of the Prior Indentures.

(d) Any New Indenture, Supplemental Indenture, reimbursement agreement, letter of credit agreement or other such arrangement as finally executed may include such modifications as the Executive Director may deem necessary or desirable in furtherance of the objectives of the Program, including, but not limited to, one or more of the following provisions:

(1) for the Agency’s insured or uninsured, limited or general, obligation to pay any debt secured thereby,

(2) for a pledge of an amount of the Supplementary Bond Security Account to the extent necessary to obtain an appropriate credit rating or appropriate credit enhancement,

(3) for a pledge of additional revenues which may be released periodically to the Agency from the lien of one or more indentures heretofore entered into by the Agency, including but not limited to one or more of the following:

(A) the Prior Indentures,

(B) the Home Mortgage Revenue Bond Indenture, dated as of September 1, 1982, as amended, and

(C) the indentures under which are issued the Single Family Mortgage Bonds,

(4) for a deposit of such other available assets of the Agency in an appropriate amount in furtherance of the Program,
for risk sharing provisions dividing between the Agency and any credit provider
and/or FHA, in such manner as the Executive Director may deem necessary or
desirable in furtherance of the objectives of the Program, the credit and financing
risks relating to the Bonds and the Developments financed by the Bonds,

(6) for liquidity support,

(7) for contingent or deferred interest, or

(8) for the use or application of payments or receipts under any arrangement entered
into under Section 9 of this resolution.

Section 4. Approval of Forms and Terms of Bonds. The Bonds shall be in
such denominations, have such registration provisions, be executed in such manner, be payable
in such medium of payment at such place or places within or without California, be subject to
such terms of redemption (including from such sinking fund installments as may be provided for)
and contain such terms and conditions as each Indenture as finally approved shall provide. The
Bonds shall have the maturity or maturities and shall bear interest at the fixed, adjustable or
variable rate or rates deemed appropriate by the Executive Director in furtherance of the
objectives of the Program; provided, however, that no Bond shall have a term in excess of fifty
years or bear interest at a stated rate in excess of fifteen percent (15%) per annum, or in the case
of variable rate bonds, a maximum floating interest rate of twenty-five percent (25%) per annum.
Commercial paper shall be treated for these purposes as variable rate bonds. Any of the Bonds
and the Supplemental Indenture(s) may contain such provisions as may be necessary to
accommodate an option to put such Bonds prior to maturity for purchase by or on behalf of the
Agency or a person other than the Agency, to accommodate the requirements of any provider of
bond insurance or other credit enhancement or liquidity support or to accommodate the
requirements of purchasers of Dutch auction bonds or indexed floaters.

Section 5. Authorization of Disclosure. The Executive Director is hereby
authorized to circulate one or more preliminary official statements relating to the Bonds and,
after the sale of the Bonds, to execute and circulate one or more official statements relating to the
Bonds, and the circulation of such preliminary official statement and such official statement to
prospective and actual purchasers of the Bonds is hereby approved. The Executive Director is
further authorized to hold information meetings concerning the Bonds and to distribute other
information and material relating to the Bonds.

Section 6. Authorization of Sale of Bonds. The Bonds are hereby authorized to
be sold at negotiated or competitive sale or sales. The Executive Director is hereby authorized
and directed, for and in the name and on behalf of the Agency, to execute and deliver one or
more agreements, by and among the Agency, the Treasurer and such purchasers or underwriters
as the Executive Director may select (the "Purchasers"), relating to the sale of the Bonds, in such
form as the Executive Director may select (the "Purchasers"), relating to the sale of the Bonds, in such
form as the Executive Director may approve upon consultation with the Agency’s legal counsel,
such approval to be evidenced conclusively by the execution and delivery of said agreements by
the Executive Director.
The Treasurer is hereby authorized and requested, without further action of this Board and unless instructed otherwise by this Board, to sell the Bonds pursuant to the terms and conditions set forth in each such agreement as finally executed on behalf of the Agency. The Treasurer is hereby further authorized and requested to deposit the proceeds of any good faith deposit to be received by the Treasurer under the terms of such agreement in a special trust account for the benefit of the Agency, and the amount of such deposit shall be retained by the Agency, applied at the time of delivery of the applicable Bonds as part of the purchase price thereof, or returned to the Purchasers, as provided in such agreement.

Section 7. Authorization of Execution of Bonds. The Executive Director is hereby authorized and directed to execute, and the Secretary of this Board is hereby authorized and directed to attest, for and on behalf and in the name of the Agency and under its seal, the Bonds, in an aggregate amount not to exceed the amount authorized hereby, in accordance with each New Indenture or Supplemental Indenture in one or more of the forms set forth in such New Indenture or Supplemental Indenture.

Section 8. Authorization of Delivery of Bonds. The Bonds when so executed, shall be delivered to the Trustee to be authenticated by or caused to be authenticated by the Trustee. The Trustee is hereby requested and directed to authenticate, or cause to be authenticated, the Bonds by the execution of the certificate of authentication and registration appearing thereon, and to deliver or cause to be delivered the Bonds when duly executed and authenticated to the Purchasers in accordance with written instructions executed on behalf of the Agency by the Executive Director, which instructions said officer is hereby authorized and directed, for and on behalf and in the name of the Agency, to execute and deliver to the Trustee. Such instructions shall provide for the delivery of the Bonds to the Purchasers, upon payment of the purchase price thereof.

Section 9. Authorization of Related Financial Agreements. The Executive Director and the other officers of the Agency are hereby authorized to enter into, for and in the name and on behalf of the Agency, any and all agreements and documents designed (i) to reduce or hedge the amount or duration of any payment, interest rate, spread or similar risk, (ii) to result in a lower cost of borrowing when used in combination with the issuance or carrying of bonds or investments, or (iii) to enhance the relationship between risk and return with respect to the Program or any portion thereof. To the extent authorized by law, including Government Code Section 5922, such agreements or other documents may include (a) interest rate swap agreements, (b) forward payment conversion agreements, (c) futures or other contracts providing for payments based on levels of, or changes in, interest rates or other indices, (d) contracts to exchange cash flows for a series of payments, or (e) contracts, including, without limitation, interest rate floors or caps, options, puts or calls to hedge payment, interest rate, spread or similar exposure, and in each such case may be entered into in anticipation of the issuance of bonds at such times as may be determined by such officers. Such agreements and other documents are authorized to be entered into with parties selected by the Executive Director, after giving due consideration for the creditworthiness of the counterparties, where applicable, or any other criteria in furtherance of the objectives of the Program.

Section 10. Authorization of Program Documents. The Executive Director and the other officers of the Agency are hereby authorized and directed to execute all documents
they deem necessary or appropriate in connection with the Program, including, but not limited to, regulatory agreements, loan agreements, origination and servicing agreements (or other loan-to-lender documents), servicing agreements, developer agreements, financing agreements, investment agreements, agreements to enter into escrow and forward purchase agreements, escrow and forward purchase agreements, refunding agreements and continuing disclosure agreements, in each case with such other parties as the Executive Director may select in furtherance of the objectives of the Program.

The Executive Director and the other officers of the Agency are hereby authorized to enter into, for and in the name and on behalf of the Agency, one or more mortgage sale agreements with such purchasers as the Executive Director may select in accordance with the objectives of the Program. Any such sale of Loans may be on either a current or a forward purchase basis.

The Executive Director and the other officers of the Agency are hereby authorized to enter into, for and in the name and on behalf of the Agency, contracts to conduct foreclosures of mortgages owned or serviced by the Agency with such attorneys or foreclosure companies as the Executive Director may select in accordance with the objectives of the Program.

The Executive Director and the other officers of the Agency are hereby authorized to enter into, for and in the name and on behalf of the Agency, contracts for the sale of foreclosed properties with such purchasers as the Executive Director may select in accordance with the objectives of the Program. Any such sale of foreclosed properties may be on an all cash basis or may include financing by the Agency. The Executive Director and the other officers of the Agency are also authorized to enter into any other agreements, including but not limited to real estate brokerage agreements and construction contracts, necessary or convenient for the rehabilitation, listing and sale of such foreclosed properties.

Section 11. Authorization of Short-Term Credit Facilities. In addition, the Executive Director and the other officers of the Agency are hereby authorized to enter into, for and in the name and on behalf of the Agency, one or more short-term credit facilities for the purposes of (i) financing the purchase of Loans on an interim basis, prior to the financing of such Loans with Bonds, whether issued or to be issued, and (ii) financing expenditures of the Agency incident to, and necessary or convenient to, the issuance of Bonds, including, but not limited to, Agency expenditures to pay costs of issuance, capitalized interest, redemption price of prior bonds of the Agency, costs relating to credit enhancement or liquidity support, costs relating to investment products, or net payments and expenses relating to interest rate hedges and other financial products. Any such short-term credit facility may be from any appropriate source, including, but not limited to, the Pooled Money Investment Account pursuant to Government Code Section 16312; provided, however, that the aggregate outstanding principal amount of short-term credit facilities authorized under this resolution, Resolution No. 08-03 (the single family financing resolution adopted at the same meeting), or Resolution No. 06-06 (the Bay Area Housing Plan resolution), as amended from time to time, may not at any time exceed $500,000,000 (separate and apart from the amount of Bonds authorized by Section 1 of this resolution).
The Executive Director and the other officers of the Agency are hereby authorized to use available Agency moneys (other than and in addition to the proceeds of bonds) to make or purchase loans to be financed by bonds (including bonds authorized by prior resolutions of this Board) in anticipation of draws on a credit facility, the issuance of Bonds or the availability of Bond proceeds for such purposes.

Section 12. Ratification of Prior Actions. All actions previously taken by the officers of the Agency in connection with the implementation of the Program, the issuance of the Bonds, the issuance of any prior bonds (the "Prior Bonds"), the execution and delivery of related financial agreements and related program agreements and the implementation of any credit facilities as described above are hereby approved and ratified.

Section 13. Authorization of Related Actions and Agreements. The Treasurer, the Executive Director and the officers of the Agency, or the duly authorized deputies thereof, are hereby authorized and directed, jointly and severally, to do any and all things and to execute and deliver any and all agreements and documents which they deem necessary or advisable in order to consummate the issuance, sale, delivery, remarketing, conversion and administration of Bonds and Prior Bonds and otherwise to effectuate the purposes of this resolution, including declaring the official intent of the Agency for purposes of U.S. Treasury Regulations Section 1.150-2, and including executing and delivering any amendment or supplement to any agreement or document relating to Bonds or Prior Bonds in any manner that would be authorized under this resolution if such agreement or document related to Bonds authorized by this resolution. Such agreements may include, but are not limited to, remarketing agreements, tender agreements or similar agreements regarding any put option for Bonds or Prior Bonds, broker-dealer agreements, market agent agreements, auction agent agreements or other agreements necessary or desirable in connection with the issuance of Bonds in, or the conversion of Bonds or Prior Bonds to, an auction rate mode or an indexed rate mode, agreements for the investment of moneys relating to the Bonds or Prior Bonds, reimbursement agreements relating to any credit enhancement or liquidity support or put option provided for the Bonds or the Prior Bonds, continuing disclosure agreements and agreements for necessary services provided in the course of the issuance of the bonds, including but not limited to, agreements with bond underwriters and placement agents, bond trustees, bond counsel and financial advisors and contracts for consulting services or information services relating to the financial management of the Agency, including advisors or consultants on interest rate swaps, cash flow management, and similar matters, and contracts for financial printing and similar services. The Agency's reimbursement obligation under any such reimbursement agreement may be a special, limited obligation or a general obligation and may, subject to the rights of the Bondholders, be secured by a pledge of the same revenues and assets that may be pledged to secure Bonds or by a pledge of other revenues and assets.

This resolution shall constitute full, separate, complete and additional authority for the execution and delivery of all agreements and instruments described in this resolution, without regard to any limitation in the Agency's regulations and without regard to any other resolution of the Board that does not expressly amend and limit this resolution.
Section 14. **Additional Delegation.** All actions by the Executive Director approved or authorized by this resolution may be taken by the Chief Deputy Director of the Agency, the Director of Financing of the Agency, the Comptroller of the Agency or any other person specifically authorized in writing by the Executive Director.
SECRETARY'S CERTIFICATE

I, Thomas C. Hughes, Secretary of the Board of Directors of the California Housing Finance Agency, hereby certify that the foregoing is a full, true, and correct copy of Amended and Restated Resolution No. 08-08 duly adopted at a regular meeting of the Board of Directors of the California Housing Finance Agency duly called and held on the 19th day of March, 2008, of which meeting all said directors had due notice; and that at said meeting said resolution was adopted by the following vote:

AYES:

NOES:

ABSTENTIONS:

ABSENT:

IN WITNESS WHEREOF, I have executed this certificate and affixed the seal of the Board of Directors of the California Housing Finance Agency hereto this ___ day of ___, 2008.

[SEAL]

Thomas C. Hughes
Secretary of the Board of Directors of the California Housing Finance Agency
SECRETARY'S CERTIFICATE

I, Thomas C. Hughes, Secretary of the Board of Directors of the California Housing Finance Agency, hereby certify that the foregoing is a full, true, and correct copy of the Amended And Restated Resolution No. 08-08 duly adopted at a regular meeting of the Board of Directors of the California Housing Finance Agency duly called and held on the 19th day of March, 2008, of which meeting all said directors had due notice; and that at said meeting said resolution was adopted by the following vote:

AYES:

NOES:

ABSTENTIONS:

ABSENT:

I further certify that I have carefully compared the foregoing copy with the original minutes of said meeting on file and of record in my office; that said copy is a full, true, and correct copy of the original resolution adopted at said meeting and entered in said minutes; and that said resolution has not been amended, modified, or rescinded in any manner since the date of its adoption, and the same is now in full force and effect.

IN WITNESS WHEREOF, I have executed this certificate and affixed the seal of the Board of Directors of the California Housing Finance Agency hereto this ___ day of ____________, ____.

[SEAL]

Thomas C. Hughes
Secretary of the Board of Directors of the California Housing Finance Agency
TRUST INDENTURE

By and Between

CALIFORNIA HOUSING FINANCE AGENCY

and

[TRUSTEE],
as Trustee

Dated as of [AS OF DATE]

Securing

California Housing Finance Agency
Multifamily Housing Revenue Bonds
Subordinate Loan Indenture
20__ Series __ ([PROJECT] Project)
TRUST INDENTURE

THIS TRUST INDENTURE is made and entered into as of [AS OF DATE], by and between the
CALIFORNIA HOUSING FINANCE AGENCY, a public instrumentality and a political subdivision
of the State of California (together with its successors and assigns, “Agency”), and [TRUSTEE], a [trustee
corporate form] duly authorized to accept and execute trusts of the character herein set forth, as trustee
(the “Trustee”).

WITNESSETH:

WHEREAS, the Agency has been created by the Zenovich-Moscone-Chacon Housing and Home
Finance Act (constituting Division 31 of the Health and Safety Code of the State of California), as
amended (Parts 1 through 4 of which are herein called the “Act”);

WHEREAS, the Agency has determined to issue bonds for the purpose of making loans to
finance or refinance the acquisition, construction, rehabilitation and development of multifamily rental
housing and to that end has duly authorized the issuance of its bonds hereunder, and to secure the
payment of the principal thereof and of the interest and premium (if any) thereon, and the observance of
the covenants and conditions herein contained, has authorized the execution and delivery of this Trust
Indenture (this “Indenture”);

WHEREAS, said bonds are to be issued hereunder and designated the “California Housing
Finance Agency Multifamily Housing Revenue Bonds, Subordinate Loan Indenture, 20__ Series __
([PROJECT] Project) (herein called the “Bonds”), in the aggregate principal amount of $[PAR
AMOUNT];

WHEREAS, [BORROWER], [Borrower corporate form] (the “Borrower”), has requested that
the Agency issue the Bonds and use the proceeds thereof to fund a loan to the Borrower (the “Loan”) to
finance a portion of the cost of acquiring, constructing, rehabilitating and developing a multifamily rental
housing development known as [PROJECT] and located in [LOCATION], California (the “Project”);

WHEREAS, the Loan and all other obligations securing the Bonds will be subordinate in right of
payment to the prior payment in full of the indebtedness evidenced by the mortgage loan made by the
Agency to the Borrower in the amount of $________ for the acquisition, construction, rehabilitation
and development of the Project (as further described herein, the “Senior Loan”), which Senior Loan will
be funded from proceeds of the Agency’s [SENIOR BONDS];

WHEREAS, by resolution adopted in accordance with Section 51352 of the Act, the Agency has
determined that the Bonds will not be general obligations of the Agency but will be repayable solely from
payments of principal and interest on account of the loan funded thereby, which shall be used for no other
purpose than to pay the principal of and interest on the Bonds, except as may be otherwise expressly
authorized in this Indenture;

WHEREAS, the Bonds will be privately placed with a single holder in minimum authorized
denominations as set forth herein and will be subject to transfer restrictions as set forth herein; and

WHEREAS, all things necessary to make the Bonds, when authenticated by the Trustee and
issued as provided in this Indenture, the valid, binding and legal obligations of the Agency according to
the import thereof, and to constitute this Indenture a valid assignment and pledge of the Trust Estate for
payment of the principal of, premium, if any, and interest on the Bonds, in such priority as provided
herein, have been done and performed, and the creation, execution and delivery of this Indenture, and the
creation, execution and issuance of the Bonds, subject to the terms hereof, have in all respects been duly authorized;

GRANTING CLAUSES

NOW, THEREFORE, the Agency, in consideration of the premises and the acceptance by the Trustee of the trusts hereby created and of the purchase and acceptance of the Bonds by the Owners thereof, and for other good and valuable consideration, the receipt and sufficiency of which is hereby acknowledged, in order to secure the payment of the principal of, premium, if any, and interest on the Bonds according to their tenor, priority and effect, and to secure the performance and observance by the Agency of all the covenants expressed or implied herein and in the Bonds, does hereby bargain, sell, convey, mortgage, assign, pledge and grant, a security interest in the Trust Estate to the Trustee, and its successors in trust and assigns forever, for the securing of the performance of the obligations of the Agency hereinafter set forth, including all of the Agency's right, title and interest in and to the following property:

GRANTING CLAUSE FIRST

The Loan Agreement and the Mortgage, including all extensions and renewals of the terms thereof, if any (except for the Reserved Rights of the Agency, as defined herein), including, but not limited to, the present and continuing right to make claim for, collect, receive and receipt for any of the sums, amounts, income, revenues, issues and profits and any other sums of money payable or receivable under the Loan Agreement and the Mortgage, to bring actions and proceedings thereunder or for the enforcement thereof, and to do any and all things that the Agency is or may become entitled to do under the Loan Agreement and the Mortgage;

GRANTING CLAUSE SECOND

All moneys and securities from time to time held by the Trustee under the terms of this Indenture (except amounts on deposit in the Rebate Fund and except that moneys and securities on deposit in the Funds and Accounts established with respect to the Bonds shall be held solely for the Owners of the Bonds); and

GRANTING CLAUSE THIRD

Any and all other property rights and interests of every kind and nature from time to time hereafter by delivery or by writing of any kind granted, bargained, sold, alienated, demised, released, conveyed, assigned, transferred, mortgaged, pledged, hypothecated or otherwise subjected hereto, as and for additional security herewith, by the Agency or any other person on its behalf or with its written consent, and the Trustee is hereby authorized to receive any and all such property at any and all times and to hold and apply the same subject to the terms hereof;

TO HAVE AND TO HOLD all and singular the Trust Estate, whether now owned or hereafter acquired, to the Trustee and its respective successors in trust and assigns forever;

IN TRUST NEVERTHELESS, upon the terms and trusts herein set forth, for the equal and proportionate benefit, security and protection of all present and future owners of the Bonds on a pro rata and parity basis;

PROVIDED, HOWEVER, that if the Agency, its successors or assigns, shall well and truly pay, or cause to be paid, the principal of, premium, if any, and interest on the Bonds due or to become due
thereon, at the times and in the manner mentioned in the Bonds and as provided in Article VII hereof according to the true intent and meaning thereof, and shall cause the payments to be made as required under Article IV hereof, or shall provide, as permitted hereby, for the payment thereof in accordance with Article VII hereof, and shall well and truly keep, perform and observe all the covenants and conditions pursuant to the terms of this Indenture to be kept, performed and observed by it, and shall disburse or cause to be disbursed to the Trustee all sums of money due or to become due in accordance with the terms and provisions hereof, then upon such final payments or deposits as provided in Article VII hereof, this Indenture and the rights hereby granted shall cease, terminate and be void and the Trustee shall thereupon cancel and discharge this Indenture and execute and deliver to the Agency such instruments in writing as shall be requisite to evidence the discharge hereof.

THIS TRUST INDENTURE FURTHER WITNESSETH, and it is expressly declared, that all Bonds issued and secured hereunder are to be issued, authenticated and delivered and all of the Trust Estate is to be dealt with and disposed of, under, upon and subject to the terms, conditions, stipulations, covenants, agreements, trusts, uses and purposes hereinafter expressed, and the Agency has agreed and covenanted, and does hereby agree and covenant, with the Trustee and with the respective Owners, from time to time, of the Bonds, or any part thereof, as follows:

ARTICLE I

DEFINITIONS AND INTERPRETATION

Section 1.1. Definitions. Unless the context otherwise requires, the following words and phrases shall, for all purposes of this Indenture and of the Loan Agreement and of any supplement or amendment hereto or thereto, have the following meanings:

“Act” means Parts 1 through 4 of Division 31 of the Health and Safety Code of the State, and all laws supplementary thereto and amendatory thereof.

“Agency” means the California Housing Finance Agency, a public instrumentality and a political subdivision of the State of California, and its successors and assigns.

“Agency Representative” means the Chairperson, the Executive Director, the Deputy Director or the Director of Financing, or any other person authorized by resolution of the Agency to act as an Agency Representative hereunder.

“Authorized Denomination” means the entire outstanding principal amount of the Bonds from time to time, or such lesser amount as the Agency may otherwise approve in writing to the Trustee.


“Bond Counsel” means any counsel of nationally recognized standing in matters pertaining to the validity of, and exclusion from gross income for federal income tax purposes of interest on, obligations issued by states and political subdivisions, familiar with the transactions contemplated under this Indenture, and acceptable to the Agency.

“Bond Documents” means this Indenture and the Borrower Documents.
“Bond Fund” means the trust fund by that name created with respect to the Bonds pursuant to Section 5.1 hereof.

“Bond Obligation” means the outstanding principal amount of the Bonds.

“Bond Payment Date” means, with respect to the Bonds, any Interest Payment Date, any Principal Payment Date and any other date on which the principal of, premium, if any, or interest on the Bonds is to be paid to the Owners thereof, whether upon redemption, at maturity or upon acceleration of maturity of the Bonds.

“Bond Rate” means an interest rate of ____% per annum.

“Borrower” means [BORROWER], [Borrower corporate form], organized and existing under the laws of the State of California, and its successors and assigns under the Loan Agreement.

“Borrower Documents” means the Loan Agreement, any promissory note, the Mortgage, the Tax Certificate and any regulatory agreement, together with all other documents or instruments executed by the Borrower which evidence or secure the Borrower’s indebtedness under the Loan Agreement, all as amended or supplemented from time to time.

“Borrower Representative” means each person at the time designated to act on behalf of the Borrower by written certificate furnished to the Agency and the Trustee containing the specimen signature of such person and signed by a general partner of the Borrower. Such certificate may designate an alternate or alternates.

“Business Day” means a day on which banks in the States of New York and California are not required or authorized by law to remain closed and on which The New York Stock Exchange is not closed.

“Closing Date” means the date of issuance and delivery of the Bonds to the initial purchasers thereof.

“Code” means the Internal Revenue Code of 1986. Each reference to the Code herein shall be deemed to include the United States Treasury Regulations promulgated thereunder or otherwise applicable thereto.

“Condemnation Award” means the total condemnation proceeds paid by the condemnor as a result of condemnation or eminent domain proceedings with respect to all or any part of the Mortgaged Property or of any settlement or compromise of such proceedings that remains after the application of such proceeds pursuant to the terms of the Senior Loan Documents.

“Debt Service Requirement” means, for the Loan or the Senior Loan, as the case may be, for a specified period:

(i) amounts needed to pay scheduled payments of principal of such Loan or Senior Loan during such period, including payments for mandatory sinking fund redemption;

(ii) amounts needed to pay interest on such Loan or Senior Loan payable during such period; and
(iii) amounts needed to pay the ordinary fees and expenses of the Trustee and the Agency during such period.

“Event of Default” means any occurrence or event specified in Section 8.1 hereof.

“Excess Project Revenues” means for any period, __% of all cash operating and nonoperating revenues of the Project, less (i) Operating Expenses and any extraordinary and nonrecurring items (including any real property tax refunds), (ii) Debt Service Requirements for the Senior Loan, (iii) income derived from the sale of assets not in the ordinary course of business, which is permitted under the Bond Documents, (iv) security, cleaning or similar deposits of tenants until applied or forfeited, and (v) Net Proceeds of Insurance Proceeds or Condemnation Awards; but including as Excess Project Revenues (1) any such Net Proceeds resulting from business interruption insurance or other insurance or condemnation proceeds retained by the Borrower, and (2) amounts received by the Borrower or the Trustee pursuant to any payment guaranty, operating guaranty or similar agreement with respect to the Project.

“Government Obligations” means direct obligations of, or obligations the principal of and interest on which are unconditionally guaranteed by, the United States of America.

“Indenture” means this Trust Indenture, executed and delivered by the Agency and the Trustee and agreed to and acknowledged by the Borrower, as amended or supplemented from time to time.

“Insurance Proceeds” means the total proceeds of insurance paid by an insurance company under the policies of insurance required to be procured by the Borrower pursuant to the Mortgage remaining after the application of such proceeds pursuant to the terms of the Senior Loan Documents.

“Interest Account” means each trust account by that name in the Bond Fund created pursuant to Section 5.1 hereof.

“Interest Payment Date” means with respect to the Bonds the first Business Day of each month, commencing __________, 20__, until the redemption or final Principal Payment Date.

“Interest Requirement” means an amount equal to the interest that would be due and payable on such Bonds on the Interest Payment Date next succeeding the date of determination (assuming that no principal of Bonds is paid or redeemed between such date and the next succeeding Interest Payment Date).

“Investment Securities” means any of the following obligations or securities, to the extent permitted by applicable law:

(i) Government Obligations;

(ii) Bank demand deposits (whether or not interest bearing), deposit accounts and interest bearing bank time deposits evidenced by certificates of deposit issued by any bank (which may include the Trustee and its affiliates), trust company, or savings and loan association whose long-term debt obligations are rated not less than “AA” or its equivalent by Moody’s or S&P;

(iii) Obligations of, or participation certificates guaranteed by Federal Intermediate Credit Banks, Federal Home Loan Banks, the Federal National Mortgage Association (excluding stripped securities), the Export-Import Bank of the United States, the Federal Land Bank, the Federal Home Loan Mortgage Corporation, the Government National Mortgage Association and the Federal Financing Bank,
or any other instrumentality of the United States of America backed by the full faith and credit of the
United States and approved in writing by the Borrower;

(iv) Obligations rated not less than “AA” or its equivalent by S&P or Moody’s, issued by any
state of the United States of America or the District of Columbia, or any political subdivision, agency or
instrumentality of one of such states;

(v) Any repurchase agreement or reverse repurchase agreement relating to Investment
Securities described in (i) or (iii) above with any bank having general unsecured debt which at the time of
investment is rated F-1+, or its equivalent by Moody’s or S&P and which is a member of the Federal
Deposit Insurance Corporation;

(vi) Any obligation or debt security of any corporation, whether organized under the laws of
the United States of America or of any state thereof or the laws of any foreign country, which, at the time
of investment therein by the Borrower, shall be rated not less favorably than “AA” or its equivalent by
Moody’s or S&P;

(vii) Money market mutual funds (including those of an affiliate of the Trustee or for which
the Trustee or any of its affiliates provides management advisory or other services) which invest solely in
Government Obligations rated “AAAm-G” or its equivalent by Moody’s or S&P;

(viii) Obligations which in the opinion of Bond Counsel are tax-exempt obligations (as defined
in Section 150(a) (6) of the Code and are not “investment property” as defined in Section 148(b)(2) of the
Code), and which are rated “A-1+,” “SP-1+,” or “AAA” or its equivalent by Moody’s or S&P;

(ix) Investment contracts with, or guaranteed by, banks or other financial institutions whose
long-term unsecured debt or claims-paying ability is rated at the time of the investment in one of the two
highest rating categories by Moody’s and S&P; provided that if either such rating of such bank or other
financial institution at any time during the holding of such investment contract shall be terminated or
suspended or shall be reduced to less than “A3” by Moody’s or to less than “A-” by S&P, then within five
Business Days, at the option of the provider thereof, either such contract shall be collateralized by United
States Treasury securities maintaining a value on a daily mark-to-market basis of not less than 102% of
the par value of such investment contract, the manner of such collateralization to be satisfactory to the
Borrower, or such contract shall be terminated and the full amount thereof plus accrued interest paid to
the Trustee; and

(x) Any other investments approved in writing by the Agency and Owners of all of the
Bonds.

“Investor Letter” means an investor letter in substantially the form attached to this Indenture as
Exhibit B.

“Issuer Fee” means the Agency’s annual fee in an amount equal to ___% of the principal
amount of Bonds issued hereunder on the Closing Date, payable by the Borrower pursuant to the Loan
Agreement, which shall be paid to the Trustee (for remittance to the Agency) in equal monthly
installments on each Interest Payment Date.

“Loan” means the loan of the proceeds of the Bonds made by the Agency to the Borrower
pursuant to the terms of the Loan Agreement.
“Loan Agreement” means [LOAN AGREEMENT], as amended or supplemented from time to time.

“Moody’s” means Moody’s Investors Service, its successors and their assigns, and if such corporation shall be dissolved or liquidated or shall no longer perform the functions of a securities rating agency, “Moody’s” shall be deemed to refer to any other nationally recognized securities rating agency designated by the Agency by notice to the Trustee, if such an agency shall exist.

“Mortgage” means the Deed of Trust, Security Agreement, Assignment of Rents and Fixture Filing of even date herewith, from the Borrower [for the benefit of the Trustee] [for the benefit of the Agency [and assigned to the Trustee]] securing the Loan, as amended and supplemented from time to time.

“Mortgaged Property” means all property subject to the lien of the Mortgage and this Indenture.

“Net Proceeds,” when used with respect to any Insurance Proceeds or Condemnation Award, means the gross proceeds from such Insurance Proceeds or Condemnation Award remaining after the application of such proceeds pursuant to the terms of the Senior Loan Documents, less all expenses (including reasonable attorneys’ fees of the Borrower or the Trustee and any extraordinary fees and expenses of the Trustee) incurred in the realization thereof.

“Operating Expenses” means for any period, expenses paid or budgeted to be paid in connection with the operation and maintenance of the Project (determined on a cash basis) during such period, including fees and expenses of the manager of the Project and payments into operational (but not capital) reserves for liabilities, but excluding (i) the Debt Service Requirement for the Loan and the Senior Loan, (ii) any loss or expense resulting from or related to any extraordinary and nonrecurring items, (iii) any losses or expenses related to the sale of assets, the proceeds of which sale are not included in Excess Project Revenues pursuant to clause (iii) of the definition thereof, and (iv) expenses paid from operational reserves.

“Outstanding” or “outstanding” means, as of any given date, all Bonds that have been authenticated and delivered by the Trustee under this Indenture, except:

(a) Bonds cancelled at or prior to such date or delivered to or acquired by the Trustee on or prior to such date for cancellation;
(b) Bonds deemed to be paid in accordance with Article VII of this Indenture; and
(c) Bonds in lieu of which other Bonds have been authenticated under Section 2.9 or 2.10 hereof.

“Owner,” “Bondowner,” “Bondholder” or “holder” means the person or persons in whose name any Bond is registered on the registration books of the Agency maintained by the Trustee.

“Person” or “person” means an individual, a corporation, a partnership, an association, a joint stock company, a trust, any unincorporated organization, a governmental body, any other political subdivision, municipality or authority or any other group or entity.

“Principal Account” means the trust account by that name within the Bond Fund created pursuant to Section 5.1 hereof.
“Principal Payment Date” means the maturity date of the Bonds and any date for mandatory sinking fund redemption of such Bonds.

“Principal Requirement” means an amount equal to the regularly scheduled principal that is due and payable on such Bonds on the Bond Payment Date next succeeding the date of determination, whether by maturity or by mandatory sinking fund redemption.

“Project” means the [UNITS]-unit multifamily rental housing facility located in [LOCATION] and known as [PROJECT] including the site on which such facility is located and all related support facilities including all buildings, structures and improvements now or hereafter constructed thereon, and all fixtures, machinery, equipment, furniture, furnishings and other personal property hereafter attached to, located in, or used in connection with any such structures, buildings or improvements, and all additions, substitutions and replacements thereto, whether now owned or hereafter acquired.

“Project Fund” means the trust fund by that name created pursuant to Section 5.1 hereof.

“Rebate Fund” means the trust fund by that name created pursuant to Section 5.1 hereof.

“Record Date” means the fifth day (whether or not a Business Day) of the calendar month preceding any applicable Interest Payment Date.

“Reserved Rights” of the Agency means (a) the right of the Agency to payment of the Issuer Fee and other fees and expenses payable to it pursuant to the Loan Agreement, (b) all rights that the Agency or its officers, officials, agents or employees may have under this Indenture and the Borrower Documents to indemnification by the Borrower and by any other persons and to payments for expenses incurred by the Agency itself, or its officers, officials, agents or employees; (c) the right of the Agency to receive notices, reports or other information, make determinations and grant approvals hereunder and under the other Bond Documents; (d) all rights of the Agency to enforce the representations, warranties, covenants and agreements of the Borrower pertaining in any manner or way, directly or indirectly, to the requirements of the Act or of the Agency, and set forth in any of the Bond Documents or in the Tax Certificate or in any other certificate or agreement executed by the Borrower; and (e) all rights of the Agency in connection with any amendment to or modification of the Bond Documents.

“Responsible Officer” means any corporate trust officer or assistant corporate trust officer or any other officer of the Trustee within its corporate trust department with responsibility for matters related to this Indenture.

“Revenue Fund” means the trust fund by that name created pursuant to Section 5.1 hereof.

“S&P” means Standard & Poor’s Ratings Group, its successors and their assigns, and, if such corporation shall be dissolved or liquidated or shall no longer perform the functions of a securities rating agency, “S&P” shall be deemed to refer to any other nationally recognized securities rating agency designated by the Borrower by notice to the Trustee, if such an agency shall exist.

“Senior Bonds” means [SENIOR BONDS].

“Senior Lender” means the Agency in its capacity as lender under the Senior Loan.

“Senior Loan” means the mortgage loan made by the Agency from proceeds of the Agency’s Senior Bonds to the Borrower for the acquisition, construction, rehabilitation and development of the
Project, at any time outstanding and any debt incurred to refund or refinance such loan, together with any sums due and owing under the Senior Loan Documents.

"Senior Loan Documents" means the indenture securing the Senior Bonds, the loan and security documents providing for the funding of and securing the Senior Loan, and all other documents related to the Senior Loan.

"State" means the State of California.

"Supplemental Indenture" means any amendment to this Indenture entered into in accordance with Article X hereof.

"Tax Certificate" means the Tax Certificate and Agreement dated the Closing Date, between the Agency and the Borrower, and any amendment or supplement thereto.

"Trust Estate" means the property conveyed to the Trustee hereunder, including all of the Agency’s right, title, and interest in and to the property described in the Granting Clauses hereof.

"Trustee" means [TRUSTEE], or any successors and assigns hereunder.

"Trustee Fee" means the Trustee's annual fee in an amount equal to $__, payable by the Borrower pursuant to the Loan Agreement, which shall be paid to the Trustee (for remittance to the Agency) [annually] [semi-annually] [in equal monthly installments on each Interest Payment Date] [in advance/in arrears].

Section 1.2. Rules of Construction.

The singular form of any word used herein, including the terms defined in Section 1.1, shall include the plural, and vice versa, unless the context otherwise requires. The use herein of a pronoun of any gender shall include correlative words of the other genders.

All references herein to "Articles," "Sections" and other subdivisions hereof are to the corresponding Articles, Sections or subdivisions of this Indenture as originally executed; and the words "herein," "hereof," "hereunder" and other words of similar import refer to this Indenture as a whole and not to any particular Article, Section or subdivision hereof.

The headings or titles of the several Articles and Sections hereof, and any table of contents appended to copies hereof, shall be solely for convenience of reference and shall not affect the meaning, construction or effect of this Indenture.

Section 1.3. Content of Certificates and Opinions. Every certificate or opinion with respect to compliance with a condition or covenant provided for in this Indenture or the Loan Agreement shall include (a) a statement that the person or persons making or giving such certificate or opinion have read such covenant or condition and the definitions herein relating thereto; (b) a brief statement as to the nature and scope of the examination or investigation upon which the statements or opinions contained in such certificate or opinion are based; (c) a statement that, in the opinion of the signers, they have made or caused to be made such examination or investigation as is necessary to enable them to express an informed opinion as to whether or not such covenant or condition has been complied with; and (d) a statement as to whether, in the opinion of the signers, such condition or covenant has been complied with.
Any such certificate or opinion made or given by an officer of the Agency may be based, insofar as it relates to legal matters, upon a certificate or opinion of or representations by counsel, unless such officer knows that the certificate or opinion or representations with respect to the matters upon which his or her certificate or opinion may be based as aforesaid are erroneous, or in the exercise of reasonable care should have known that the same were erroneous. Any such certificate or opinion made or given by counsel may be based, insofar as it relates to factual matters (with respect to which information is in the possession of the Agency), upon the certificate or opinion of or representations by an officer of the Agency, unless such counsel knows that the certificate or opinion or representations with respect to the matters upon which his or her opinion may be based as aforesaid are erroneous, or in the exercise of reasonable care should have known that the same were erroneous.

ARTICLE II

THE BONDS

Section 2.1. Authority for and Issuance of Bonds. Bonds in an aggregate principal amount not to exceed $[PAR AMOUNT] are hereby authorized under this Indenture. The Bonds shall be designated “California Housing Finance Agency Multifamily Housing Revenue Bonds, Subordinate Loan Indenture, 20__ Series __ ([PROJECT] Project).” The total principal amount of Bonds that may be issued and Outstanding hereunder is expressly limited to the amount set forth above. The Bonds shall be dated the Closing Date, shall bear interest at the Bond Rate and shall mature on __________, 20__.

The Bonds shall be issuable only as fully registered Bonds without coupons, in Authorized Denominations. The Bonds shall be lettered “R” and shall be numbered separately from 1 consecutively upward. The Bonds shall bear interest from the Interest Payment Date preceding the date of authentication thereof, unless the date of such authentication shall be an Interest Payment Date, in which case they shall bear interest from such Interest Payment Date, or, if the Bonds are authenticated prior to the first Interest Payment Date, they shall bear interest from their dated date; provided that if, as shown by the records of the Trustee, interest on the Bonds shall be in default, Bonds shall bear interest from the date to which interest has been paid in full on the Bonds, or if no interest has been paid on the Bonds, from their date. Interest shall be computed on the basis of a 360-day year of twelve 30-day months.

The principal of and premium, if any, on the Bonds shall be payable, when due, in lawful money of the United States of America at the principal corporate trust office of the Trustee upon presentation and surrender of the Bonds. Payment of interest on the Bonds shall be made on each Interest Payment Date to the Owner thereof as of the Record Date, by check mailed first class by the Trustee on such Interest Payment Date to the Owner at its address as it appears on the registration books maintained by or on behalf of the Agency. Payment of interest on the Bonds shall, upon written notice to the Trustee of any Owner of Bonds be transmitted by wire transfer of immediately available funds on the Interest Payment Date to such Owner to the bank account number at a bank located within the United States on file with the Trustee as of the Record Date. Any such wire transfer request shall continue in force until revoked in writing by such Owner to the Trustee, and to be effective as to any interest payment such revocation must be received by the Trustee prior to the applicable Record Date.

No Bonds may be issued under the provisions of this Indenture except in accordance with this Article.

Section 2.2. Execution. The Bonds shall be executed in the name of the Agency by the manual or facsimile signature of an Agency Representative, and its corporate seal (or a facsimile thereof) shall be thereunto affixed, imprinted, impressed, engraved or otherwise reproduced and attested by the manual or facsimile signature of another Agency Representative of the Agency, or in such other manner
as may be required by law. In case any one or more of the Agency Representatives who shall have
signed, sealed or attested any of the Bonds or whose signature appears on any of the Bonds shall cease to
be such Agency Representatives before the Bonds so signed and sealed shall have been actually
authenticated by the Trustee or delivered or caused to be delivered by the Trustee or issued by the
Agency, such Bonds may, nevertheless, be authenticated and issued and, upon such authentication,
delivery and issue, shall be as binding upon the Agency as if the persons who signed or sealed such
Bonds or whose signatures appear on any of the Bonds had not ceased to hold such offices or be so
employed until such delivery. Any Bond may be signed and sealed on behalf of the Agency by such
persons as at the actual time of the execution of such Bond shall be duly authorized or hold the proper
office in or employment by the Agency, although at the issue date of such Bond such persons may not
have been so authorized or have held such office or employment.

The Bonds shall bear thereon a certificate of authentication executed by the Trustee. Only
such Bonds as shall bear thereon such certificate of authentication shall be entitled to any right or
benefit under the Indenture, and no Bond shall be valid for any purpose under the Indenture until
such certificate of authentication shall have been duly executed by the Trustee. Such certificate of
authentication upon any Bond shall be conclusive evidence that the Bond so authenticated has been
duly issued under the Indenture and that the holder thereof is entitled to the benefits of the Indenture.

Section 2.3. Limited Obligations. The Bonds shall not be general obligations of the Agency
but shall be repayable solely from payments of principal and interest on account of the Loan funded
thereby, which shall be used for no other purpose than to pay the principal of and interest on the Bonds,
except as may be otherwise expressly authorized in this Indenture. EACH AND EVERY COVENANT
MADE HEREIN BY THE AGENCY IS PREDICATED UPON THE CONDITION THAT THE
AGENCY WILL IN NO EVENT BE LIABLE FOR THE PAYMENT OF THE PRINCIPAL OF,
PREMIUM, IF ANY, OR INTEREST ON THE BONDS, OR OTHER FEES AND EXPENSES
PROVIDED HEREUNDER OR THE PERFORMANCE OF ANY PLEDGE, SECURITY
AGREEMENT, OBLIGATION OR AGREEMENT CREATED BY OR ARISING UNDER THIS
INDENTURE OR THE BONDS FROM ANY PROPERTY OTHER THAN THE TRUST ESTATE,
AND THAT NEITHER THE BONDS NOR ANY SUCH OBLIGATION OR AGREEMENT OF THE
AGENCY WILL BE CONSTRUED TO CONSTITUTE AN INDEBTEDNESS OF THE AGENCY
WITHIN THE MEANING OF ANY CONSTITUTIONAL OR STATUTORY PROVISION
WHATSOEVER, OR AS A PLEDGE OF THE GENERAL CREDIT, FAITH OR ANY TAXING
POWER OF THE AGENCY, THE STATE OF CALIFORNIA OR ANY POLITICAL SUBDIVISION
THEREOF. THE AGENCY HAS NO TAXING POWER. Neither the members of the board of the
Agency nor the officers of the Agency nor any person executing the Bonds shall be personally liable on
the Bonds or be subject to any personal liability or accountability by reason of the issuance thereof.

Section 2.4. Authentication. The Bonds shall bear thereon a certificate of authentication
executed by the Trustee. Only such Bonds as shall bear thereon such certificate of authentication shall be
entitled to any right or benefit under the Indenture, and no Bond shall be valid for any purpose under the
Indenture until such certificate of authentication shall have been duly executed by the Trustee. Such
certificate of authentication upon any Bond shall be conclusive evidence that the Bond so authenticated
has been duly issued under the Indenture and that the holder thereof is entitled to the benefits of the
Indenture.

Section 2.5. Form of Bonds. The Bonds shall be substantially in the form set forth in
Exhibit A hereto, with such variations, omissions and insertions as are permitted or required by this
Indenture. If appropriate, any portion of the text of any Bond as shown on Exhibit A may be printed on
the back of such Bond, and in such case there shall be inserted in place of such text a legend referring
thereto to the following effect: "Reference is hereby made to the further provisions of this Bond set forth
on the back hereof, and such further provisions are hereby incorporated by this reference as if set forth here in full.” Definitive bonds may be typewritten, printed, engraved, lithographed or otherwise produced.

**Section 2.6. Delivery of Bonds; Physical Delivery.** Upon the execution and delivery of this Indenture, the Agency shall execute and deliver the Bonds to the Trustee, and the Trustee shall authenticate the Bonds and shall deliver them to the original purchaser thereof as directed by the Agency in the request described in (c) below. The Bonds shall be issued and delivered only as physical certificates and may not be issued as book-entry bonds under any book-entry system or through any securities depository.

**Section 2.7. Mutilated, Lost, Stolen or Destroyed Bonds.** In the event any Bond is mutilated, lost, stolen or destroyed, the Agency may execute and the Trustee may authenticate and deliver a new Bond of like date, maturity and denomination as the Bond mutilated, lost, stolen or destroyed; provided that, in the case of any mutilated Bond, such mutilated Bond shall first be surrendered to the Trustee, and, in the case of any lost, stolen or destroyed Bond, there shall be first furnished to the Trustee evidence of such loss, theft or destruction satisfactory to the Trustee, together with indemnity to the Agency and the Trustee satisfactory to them. In the event any such Bond shall be about to mature or have matured or been called for redemption, instead of issuing a duplicate Bond, the Agency may pay the same without surrender thereof. The Agency and the Trustee may charge the Owner of such Bond their reasonable fees and expenses incurred pursuant to this Section.

All duplicate Bonds issued and authenticated pursuant to this Section 2.7 shall constitute original, contractual obligations of the Agency to the extent provided in this Indenture (whether or not lost, stolen or destroyed Bonds be at any time found by anyone) and shall be entitled to equal and proportionate rights and benefits hereunder as all other Outstanding Bonds issued hereunder.

**Section 2.8. Registration and Transfer of Bonds; Persons Treated as Owners.** The Agency shall cause books for the registration and for the transfer of the Bonds as provided in this Indenture to be kept by the Trustee.

Bonds may only be sold, resold and transferred (1) only in Authorized Denominations, (2) only with the written consent of the Agency, and (3) only to (i) the Borrower or an affiliate thereof, (ii) “qualified institutional buyers” as defined in Rule 144A of the Securities Act of 1933, as amended or (iii) “accredited investors” as defined under Regulation D of the Securities Act of 1933, as amended; and the Bonds shall contain a legend to that effect as set forth in Exhibit A hereto. The Trustee shall not authenticate any Bond until the Trustee has received an Investor Letter in the form attached as Exhibit B.

Promptly following surrender for transfer of any Bond at its principal corporate trust office, the Trustee shall enter the name and address of the transferee upon the registration books of the Agency and shall deliver to the transferee a new fully authenticated and registered Bond or Bonds in the name of the transferee, such new Bond or Bonds, of Authorized Denominations and of the same maturity and for the aggregate principal amount which the new Owner is entitled to receive. In addition, promptly following surrender of any Bond at the principal corporate trust office of the Trustee, duly endorsed in blank, such Bond may at the option of the Owner thereof, be exchanged for a Bond or Bonds in an equal aggregate principal amount of the Authorized Denominations and of the same form and tenor of the Bond being exchanged.

All Bonds presented for transfer, exchange, redemption or payment shall (if so required by the Agency or the Trustee) be accompanied by a written instrument or instruments of transfer, in form and
with guaranty of signature as set forth in the form of Bond or as may be satisfactory to the Trustee, duly executed by the Owner or by its duly authorized attorney.

The Trustee also may require payment from the Owner of a sum sufficient to cover any tax or other governmental fee or charge that may be imposed in relation thereto. Such taxes, fees and charges shall be paid before any such new Bond shall be delivered. The cost of printing Bonds and any services rendered or expenses incurred by the Trustee in connection with any transfer shall be paid by the Borrower.

The Agency and the Trustee shall not be required (a) to issue or register the transfer of any Bonds during any period beginning on a Record Date with respect thereto and ending at the close of business on the Business Day preceding the next Interest Payment Date or (b) to transfer any Bonds selected, called or being called for redemption in whole or in part.

Bonds delivered upon any transfer as provided herein, or as provided in Section 2.7 hereof, shall be valid limited obligations of the Agency, evidencing the same debt as the Bonds surrendered, shall be secured by this Indenture and shall be entitled to all of the security and benefits hereof to the same extent as the Bonds surrendered.

The Agency, the Borrower, and the Trustee may treat the person in whose name a Bond is registered on the registration books of the Agency maintained by the Trustee as the absolute owner thereof for all purposes, whether or not such Bond shall be overdue, and shall not be bound by any notice to the contrary.

Section 2.9. Cancellation of Bonds. Whenever any Outstanding Bond shall be delivered to the Trustee for cancellation pursuant to this Indenture, upon payment of the principal amount thereof and interest thereon, for replacement pursuant to Section 2.7 hereof, for transfer or exchange pursuant to Section 2.8 hereof or otherwise, such Bond shall be cancelled and destroyed by the Trustee and, upon written request of the Agency, counterparts of a certificate of destruction evidencing such destruction shall be furnished by the Trustee to the Agency.

Section 2.10. Temporary Bonds. Pending preparation of definitive Bonds, there may be executed, and upon request of the Agency, the Trustee shall authenticate and deliver, in lieu of definitive Bonds and subject to the same limitations and conditions, temporary typewritten, printed, engraved or lithographed bonds, in the form of registered Bonds without coupons in Authorized Denominations, substantially in the form of Exhibit A hereto and with such appropriate omissions, insertions and variations as may be required with respect to such temporary Bonds.

If temporary Bonds shall be issued, the Agency shall cause the definitive Bonds to be prepared and to be executed, authenticated and delivered to the Trustee not later than fourteen (14) days following the delivery of such temporary Bonds, and the Trustee, upon presentation to it at its principal corporate trust office of any temporary Bond, shall cancel the same and deliver in exchange therefor at the place designated by the Owner, without charge to the Owner, a definitive Bond or Bonds in an equal aggregate principal amount, of the same maturity and bearing interest at the same rate or rates as the temporary Bond surrendered. Until so exchanged, the temporary Bonds shall in all respects be entitled to the benefit and security of this Indenture as the definitive Bonds to be issued and authenticated hereunder.

Section 2.11. Termination. Upon the occurrence of an event of default under any of the Senior Loan Documents that results in a foreclosure or deed in lieu of foreclosure with respect to the deed of trust securing the Senior Loan, the Trustee shall promptly thereafter deliver any moneys then remaining in the Trust Estate first to pay any fees and expenses owed to the Trustee and the Agency.
payable with respect to the Bonds and then to the Bondholders, whereupon the lien of this Indenture shall automatically be deemed to be discharged, this Indenture, the Loan Agreement and the Mortgage shall automatically be deemed to be terminated and the Bonds and all obligations owed under the Bond Documents shall be deemed paid and satisfied.

Section 2.12. Bonds and Loan Payable to Extent of Excess Project Revenues. The Bonds are limited obligations of the Agency and are payable on any Bond Payment Date only to the extent the Trustee has received sufficient payment under the Loan for such purpose. The Loan is repayable in accordance with the Loan Agreement on any Loan payment date only to the extent the Borrower has available sufficient Excess Project Revenues for such purpose. Pursuant to Section 8.1, failure to make a payment on the Bonds shall not result in a default hereunder so long as the Trustee pays all principal and interest received from the Borrower under the Loan. Amounts due but unpaid on the Bonds (whether or not failure to pay such amounts constitutes a default hereunder) shall continue to accrue interest at the Bond Rate compounded on each Interest Payment Date.

Section 2.13. Subordination. The obligation securing the Bonds is and shall be subordinate in right of payment to the prior payment in full of the indebtedness evidenced by the Senior Loan. This Indenture is and shall be subject and subordinate in all respects to the liens, terms, covenants and conditions of the Senior Loan Documents.

ARTICLE III
REDEMPTION OR PURCHASE OF BONDS

Section 3.1. Mandatory Redemption of Bonds. The Bonds shall be subject to redemption at a price equal to the principal amount of Bonds redeemed plus interest accrued thereon to the date fixed for redemption, without premium, on the earliest practicable date for which notice of redemption can be given pursuant to Section 3.5 hereof (1) in the event the Project or any portion thereof is damaged or destroyed or taken in a condemnation proceeding and Net Proceeds resulting therefrom are required to be used to redeem Bonds pursuant to the Loan Agreement; and (2) at the written direction of the Agency following the occurrence of an event of default under the Loan Agreement.

If called for redemption at any time pursuant to the paragraph above, the Bonds to be redeemed shall be subject to redemption in whole at the earliest practicable date at a redemption price equal to 100% of the principal amount thereof plus accrued interest to the redemption date, without premium

Section 3.2. Optional Redemption of Bonds. The Bonds are subject to optional redemption in whole or in part on any Interest Payment Date, upon optional prepayment of the Loan in accordance with the Loan Agreement, at a redemption price equal to 100% of the principal amount of the Bonds called for redemption, plus accrued interest, if any, to the redemption date, without premium.

Section 3.3. Mandatory Sinking Fund Redemption of Bonds. The Bonds are subject to mandatory sinking fund redemption at a redemption price equal to 100% of the principal amount thereof, without premium, on each Principal Payment Date and in the principal amounts shown in Exhibit C of this Indenture. The amounts set forth in such Exhibit shall be reduced pro rata in the event of any partial redemption of Bonds in part pursuant to Section 3.1 or 3.2.

Section 3.4. Selection of Bonds to Be Redeemed. Bonds may be redeemed in whole or in part in any amount. If less than all of the Bonds are being redeemed, the principal amount of the Bonds to be redeemed shall be designated by the Borrower in writing to the Trustee. If it is determined that less
than all of the principal amount represented by any Bond is to be called for redemption, then, following notice of intention to redeem such principal amount, the Owner thereof shall surrender such Bond to the Trustee on or before the applicable redemption date for (a) payment on the redemption date to such Owner of the redemption price of the amount called for redemption and (b) delivery to such Owner of a new Bond or Bonds in the aggregate principal amount of the unredeemed balance of the principal amount of such Bond, which shall be an Authorized Denomination. A new Bond representing the unredeemed balance of such Bond shall be issued to the Owner thereof, without charge therefor. If the Owner of any Bond or integral multiple of the Authorized Denomination selected for redemption shall fail to present such Bond to the Trustee for payment and exchange as aforesaid, such Bond shall, nevertheless, become due and payable on the date fixed for redemption to the extent of the amount called for redemption (and to that extent only), and interest shall cease to accrue from the date fixed for redemption.

Section 3.5. Notice of Redemption.

In the event any of the Bonds are called for redemption pursuant to Section 3.2, the Trustee shall give written notice of the redemption of such Bonds, which notice shall (i) specify the Bonds to be redeemed, the redemption date, the redemption price and the place or places where amounts due upon such redemption will be payable (which shall be the principal corporate trust office of the Trustee) and, if less than all of the Bonds are to be redeemed, the numbers of the Bonds to be so redeemed, (ii) state any condition to such redemption and (iii) state that on the redemption date, and upon the satisfaction of any such condition, the Bonds to be redeemed shall cease to bear interest. Such notice may set forth any additional information relating to such redemption. Such notice shall be given by first-class mail to the Owners of the Bonds to be redeemed, at least one hundred twenty (120) days but no more than one hundred fifty (150) days prior to the date fixed for redemption.

No notice shall be required for redemption of Bonds pursuant to Section 3.1 or 3.3.

Any Bonds which have been duly selected for redemption and which are deemed to be paid in accordance with Article VII hereof shall cease to bear interest on the specified redemption date.

Section 3.6. Payment of Redemption Price. For the redemption of any of the Bonds pursuant to Section 3.1 or 3.2, the Agency shall cause to be deposited in the Redemption Account of the Bond Fund an amount sufficient to pay the principal of, premium, if any, and interest to become due on the date fixed for such redemption. The obligation of the Agency to cause any such deposit to be made hereunder shall be reduced by the amount of moneys in such Redemption Account available for and used on such redemption date for payment of the principal of, premium, if any, and accrued interest on the Bonds to be redeemed.

ARTICLE IV
GENERAL COVENANTS

Section 4.1. Payment of Bonds; Limited Obligations.

The Agency covenants that it will promptly pay the principal of, premium, if any, and interest on every Bond issued under this Indenture at the place, on the dates and in the manner provided herein and in the Bonds, provided that the principal, premium, if any, and interest on the Bonds are payable by the Agency solely from the Trust Estate in such priority as set forth herein, and nothing in the Bonds or this Indenture shall be considered as assigning or pledging any other funds or assets of the Agency other than the Trust Estate.
Each and every covenant made herein by the Agency is predicated upon the condition that neither the Agency, the State, nor any political subdivision of the State shall in any event be liable for the payment of the principal of, premium, if any, or interest on any of the Bonds or for the performance of any pledge, obligation or agreement undertaken by the Agency except to the extent that moneys pledged herein are sufficient therefor.

Section 4.2. Performance of Covenants; Authority; Due Execution. The Agency covenants that it will faithfully perform or cause to be performed at all times any and all covenants, undertakings, stipulations and provisions to be performed by the Agency contained in this Indenture and the other Bond Documents to which it is a party, in any and every Bond executed, authenticated and delivered hereunder and in all of its proceedings pertaining hereto. The Agency covenants that it is duly authorized under the laws of the State, including particularly the Act, to issue the Bonds, to execute this Indenture and to pledge the amounts hereby pledged in the manner and to the extent herein set forth. The Agency further covenants that all action on its part for the issuance of the Bonds and the execution and delivery of the Bond Documents to which it is a party have been duly and effectively taken, and that the Bonds in the hands of the Owners thereof are and will be valid and enforceable obligations of the Agency according to the terms thereof and hereof.

Section 4.3. Instruments of Further Assurance. The Agency covenants that it will do, execute, acknowledge and deliver, or cause to be done, executed, acknowledged and delivered, such indentures supplemental hereto and such further acts, instruments and transfers as the Trustee may reasonably require for the better assuring, transferring, pledging, assigning and confirming to the Trustee all and singular the rights assigned hereby and the amounts pledged hereby to the payment of the principal of, premium, if any, and interest on the Bonds. The Agency covenants and agrees that, except as herein and in the Mortgage provided, neither it nor the Borrower will sell, convey, assign, pledge, encumber or otherwise dispose of any part of the Trust Estate.

Section 4.4. Recording and Filing; Further Instruments. The Trustee will cooperate with the Agency and the Borrower so that the Agency or the Borrower shall cause to be recorded or filed, at the Agency’s or the Borrower’s request and expense, all necessary financing statements, including continuation statements, related to this Indenture and the Mortgage and all supplements hereto and thereto, and such other documents as may be necessary to be kept and filed in such manner and in such places as may be required by law in order to perfect, preserve and protect fully the security of the Owners and the rights of the Trustee hereunder.

Section 4.5. Tax Covenants. The Agency shall not use or permit the use of any proceeds of Bonds or any other funds of the Agency, directly or indirectly, to acquire any securities or obligations, and shall not use or permit the use of any Excess Project Revenues in any manner, and shall not take or permit to be taken any other action or actions, which would cause any Bond to be an “arbitrage bond” within the meaning of Section 148 of the Code, or which would otherwise affect the exclusion of interest on the Bonds from gross income of the recipients thereof for federal income tax purposes.

The Agency shall at all times do and perform all acts and things permitted by law and necessary or desirable in order to assure that interest paid by the Agency on the Bonds shall, for federal income tax purposes, be excluded from the gross income of the recipients thereof. In furtherance of this covenant, the Agency and the Borrower shall execute, deliver and perform the Tax Certificate, which is by this reference incorporated herein and made a part hereof as if set forth herein in full, and by its acceptance of this Indenture the Trustee acknowledges receipt of the Tax Certificate and acknowledges its incorporation herein by reference.
Notwithstanding any provision of this Indenture, any regulatory agreement or the Loan Agreement to the contrary, unless otherwise specifically agreed in the Tax Certificate or in a separate written agreement, the Trustee shall not be liable or responsible for any calculation or determination which may be required in connection with, or for the purpose of complying with, Section 148 of the Code, or any successor statute or any regulation, ruling or other judicial or administrative interpretation thereof, including, without limitation, the calculation of amounts required to be paid to the United States of America or the determination of the maximum amount which may be invested in nonpurpose obligations having a yield higher than the yield on the Bonds, and the Trustee shall not be liable or responsible for monitoring the compliance by the Borrower or the Agency with any of the requirements of Section 148 of the Code or any applicable regulation, ruling or other judicial or administrative interpretation thereof except as specifically provided in the Tax Certificate.

Section 4.6. No Disposition of Trust Estate or Project. Except as permitted by this Indenture, the Agency shall not sell, lease, pledge, assign or otherwise encumber or dispose of its interest in the Trust Estate and will promptly pay or cause to be discharged, or make adequate provision in the judgment of the Trustee to discharge, any lien or charge on any part thereof not permitted hereby. Except as described in the Loan Agreement and the Mortgage, the Agency will not, and will not permit the Borrower to, sell, lease, pledge, assign or otherwise encumber or dispose of the Project.

Section 4.7. Access to Books. All books and documents in the possession of the Agency or the Trustee relating to the Project and the Trust Estate shall at all reasonable times be open to inspection by the Trustee, the Agency, the Borrower, and the Owners all of the Outstanding Bonds.

Section 4.8. Trustee to Retain Information. So long as any of the Bonds shall be outstanding, the Trustee shall retain all certificates, requisitions, financial statements and other written information furnished to it by or on behalf of the Borrower or any other person under the Loan Agreement and any other agreement or instrument pertaining to the Bonds and shall make such documentation available to the Agency, the Borrower or any Owner for review after reasonable notice during regular business hours at the principal corporate trust office of the Trustee. The Trustee shall permit such reviewers to take copies of all or any part of such documentation, subject to their payment of such reasonable copying and handling charges as the Trustee may impose.

ARTICLE V
DEPOSIT OF BOND PROCEEDS; FUNDS AND ACCOUNTS; REVENUES

Section 5.1. Creation of Funds and Accounts. There are hereby created and established the following Funds and Accounts to be held by the Trustee:

(a) a Bond Fund and, within such Fund, a Principal Account, an Interest Account and a Redemption Account;

(b) a Revenue Fund; and

(c) a Rebate Fund.

Section 5.2. Application of Proceeds; Funding of Loan. Upon execution and delivery of the Bonds on the Closing Date, all of the proceeds of the Bonds in the amount of $________ shall be delivered to the Trustee and deposited into the Loan Fund, which is hereby established. All proceeds of the Loan Fund shall be immediately transferred on the Closing Date to the Borrower to fund the Loan.
Section 5.3. Revenue Fund.

(a) There shall be deposited in the Revenue Fund (i) all amounts paid to the Trustee as repayment of the Loan under the Loan Agreement, (ii) all other amounts required to be so deposited pursuant to the terms hereof or of the Tax Certificate, including investment earnings to the extent provided in Article VI, (iii) any amounts derived from the Loan Agreement or the Mortgage to be applied to payment of amounts intended to be paid from the Revenue Fund, and (iv) such other moneys as are delivered to the Trustee by or on behalf of the Agency or the Borrower with directions for deposit of such moneys in the Revenue Fund.

(b) Moneys on deposit in the Revenue Fund shall be transferred on or before the final Business Day of each month, first, to the Rebate Fund, to the extent of any deposit required to be made thereto pursuant to the Tax Certificate and which is not made directly pursuant to the Loan Agreement; then, in the following order of priority:

(i) To the Interest Account, the Interest Requirement for the Bonds for the previous calendar month, together with an amount equal to any unfunded Interest Requirement for any prior month; and

(ii) To the Principal Account, an amount equal to the Principal Requirement for the Bonds, together with an amount equal to any unfunded Principal Requirement; and

Amounts remaining in the Revenue Fund shall be retained therein and applied as provided in subsection (c) of this Section.

(c) On each Interest Payment Date, moneys on deposit in the Revenue Fund shall be disbursed in the following order:

(i) To the Interest Account and the Principal Account, in that order, in each case to the extent necessary to cause the amount in each such Account to be sufficient to pay all amounts due as principal, redemption price for redemption pursuant to Section 3.3, and interest on such Bonds on such Interest Payment Date; and

(ii) To the Trustee, (i) an amount equal to the Trustee Fee, plus its reasonable fees and expenses in connection with any redemption of Bonds; and an amount equal to any reasonable fees and expenses for extraordinary services incurred by the Trustee; and (ii) an amount equal to the Issuer Fee then due and payable, which shall be remitted by the Trustee to the Agency; and

Any amount remaining in the Revenue Fund shall be retained in such Fund and applied to costs and expenses as otherwise required under this Indenture.

Section 5.3. Deposits into the Bond Fund; Use of Moneys in the Bond Fund.

(a) There shall be deposited into the Interest Account of the Bond Fund (i) moneys transferred to such Interest Account from the Revenue Fund pursuant to Section 5.2 hereof, and (ii) any other amounts deposited with the Trustee with directions to deposit the same in such Interest Account of the Bond Fund.

(b) There shall be deposited into the applicable Principal Account of the Bond Fund (i) moneys transferred to such Principal Account from the Revenue Fund pursuant to Section 5.2 hereof,
and (ii) any other amounts deposited with the Trustee with directions to deposit the same in such Principal Account of the Bond Fund.

(c) There shall be deposited in the Redemption Account of the Bond Fund all payments made by the Borrower with respect to the redemption of Bonds (or portion thereof) pursuant to Sections 3.1 or 3.2 hereof, including but not limited to Net Proceeds in the event the Project or any portion thereof is damaged or destroyed or taken in a condemnation proceeding and such amounts are required to redeem Bonds. Amounts on deposit in such Redemption Account shall be used to pay the redemption price of such Bonds being redeemed.

(d) Except as otherwise provided herein, moneys in the Principal Account shall be used solely for the payment of principal of the Bonds as the same shall become due and payable on any Principal Payment Date with respect to such Bonds; and moneys in an Interest Account shall be used solely for the payment of interest on the Bonds as the same becomes due and payable on any Bond Payment Date.

Section 5.4. Rebate Fund. Amounts shall be deposited in the Rebate Fund and shall be applied as provided in the Tax Certificate. Within thirty (30) days after the end of every fifth bond year (as defined in the Tax Certificate), and within fifty-five (55) days after the date on which no Bonds are outstanding, the Agency shall, at the Borrower’s expense, deliver or cause to be delivered to the Trustee a certificate stating whether any rebate payment is required to be made and the amount of any such rebate payment to be made, as set forth in the Tax Certificate, and cause the Borrower to deliver to the Trustee any amount so required to be paid. The Trustee shall have no obligation with respect to the Rebate Fund other than to make the deposits requested by the Borrower or the Agency and make payments to the U.S. Government in accordance with instructions of the Borrower or the Agency.

Section 5.5. Bonds Not Presented for Payment. In the event any Bonds shall not be presented for payment when the principal thereof becomes due on any Bond Payment Date, if moneys sufficient to pay such Bonds are held by the Trustee, the Trustee shall segregate and hold such moneys in trust, without liability for interest thereon, for the benefit of Owners of such Bonds who shall, except as provided in the following paragraph, thereafter be restricted exclusively to such funds for the satisfaction of any claim of whatever nature on their part under this Indenture or relating to said Bonds.

All moneys deposited with the Trustee for the payment of principal of, premium, if any, or interest on the Bonds and not claimed for two years after they become payable or distributable shall be paid by the Trustee to the Agency. In such event, the Trustee shall be relieved of all liability with respect to such moneys and payment for such Bonds and the Owner of such Bonds shall look solely to the Agency for such payment.

Section 5.6. Moneys Held in Trust. All moneys required to be deposited with or paid to the Trustee for deposit into any Fund or Account (other than the Rebate Fund) and all moneys withdrawn from the Bond Fund and held by the Trustee shall be held by the Trustee in trust, and such moneys (other than moneys held pursuant to Section 5.8 hereof) shall, while so held, constitute part of the Trust Estate and be subject to the lien hereof. Moneys held in the Bond Fund shall constitute a separate trust fund for the Owners, as applicable, and shall not constitute property of the Agency or the Borrower.

Section 5.7. Payment to the Borrower. After the right, title and interest of the Trustee in and to the Trust Estate and all covenants, agreements and other obligations of the Agency to the Owners shall have ceased, terminated and become void and shall have been satisfied and discharged in accordance with Article VII hereof, all fees, expenses and other amounts payable to the Trustee and the Agency pursuant to any provision hereof shall have been paid in full, any moneys remaining in the Funds and
Accounts hereunder shall be paid or transferred to the Borrower upon its written request; provided that amounts on deposit in the Rebate Fund shall be retained therein to the extent required by the Tax Certificate.

ARTICLE VI

INVESTMENTS

Section 6.1. Investments. Moneys in all Funds and Accounts established hereunder shall, at the written direction of the Borrower, with the consent of the Agency, at least two Business Days before the making of such investment, be invested and reinvested by the Trustee in Investment Securities. If no such instructions are provided, the Trustee shall invest such moneys in Investment Securities described in clause (vii) of the definition thereof until instructions regarding investments are received. Subject to the further provisions of this Article, such investments shall be made by the Trustee as directed and designated by the Borrower in a certificate of, or telephonic advice promptly confirmed by a written certificate of, a Borrower Representative. As long as no Event of Default shall have occurred and be continuing, the Borrower shall have the right to designate the investments to be sold and otherwise to direct the Trustee in the sale or conversion to cash of the investments made with the moneys in any Fund or Account. The Borrower will not direct that any investment be made of any funds that would violate the covenants set forth in Section 4.5 hereof. Unless otherwise confirmed in writing, an account statement delivered by the Trustee to the Borrower shall be deemed written confirmation by the Borrower that the investment transactions identified therein accurately reflect the investment directions given to the Trustee by the Borrower, unless the Borrower notifies the Trustee in writing to the contrary within 30 days after the date of such statement.

Moneys in any fund or account shall be invested in Investment Securities with respect to which payments of principal thereof and interest thereon are scheduled to be paid or are otherwise payable (including Investment Securities payable at the option of the holder) not later than the earlier of (i) the date on which it is estimated that such moneys will be required by the Trustee, or (ii) six (6) months after the date of acquisition thereof by the Trustee.

The Trustee may make any and all such investments through its own banking department or the banking department of any affiliate. All income attributable to moneys deposited in any Fund or Account created hereunder shall be credited to the Revenue Fund, except that income on moneys in the Project Fund shall be credited to the Project Fund and moneys in the Rebate Fund shall be credited to the Rebate Fund. Any net loss realized and resulting from any such investment shall be charged to the particular fund or account for whose account such investment was made. The Trustee is authorized and directed to sell and reduce to cash funds a sufficient amount of such investments whenever the cash balance in any fund or account is insufficient to make any withdrawal therefrom as required under this Indenture. The Trustee shall not be liable for any depreciation of the value of any investment made pursuant to this Article VI or for any loss resulting from any such investment on the redemption, sale and maturity thereof. Investment Securities that are registerable securities shall be registered in the name of the Trustee.

The Trustee shall at all times maintain accurate records of deposits into each Fund and Account and the sources of such deposits.

The Agency (and the Borrower by its execution of the Loan Agreement) acknowledges that to the extent regulations of the Comptroller of the Currency or other applicable regulatory entity grant the Agency or the Borrower the right to receive brokerage confirmations of securities transactions as they occur, the Agency and the Borrower specifically waive receipt of such confirmations to the extent
permitted by law. The Trustee will furnish the Agency and the Borrower periodic cash transaction statements that include detail for all investment transactions made by the Trustee hereunder.

ARTICLE VII

RELEASE OF INDENTURE

Section 7.1. Release of Indenture. If the Agency shall pay or cause to be paid to the Owner of any Bond the principal of, premium, if any, and interest due and payable, and thereafter to become due and payable, upon such Bond, or any portion of such Bond in any Authorized Denomination thereof, such Bond or portion thereof shall cease to be entitled to any lien, benefit or security under this Indenture. If the Agency shall pay or cause to be paid the principal of, premium, if any, and interest due and payable on all Outstanding Bonds, and thereafter to become due and payable thereon, and shall pay or cause to be paid all other sums payable hereunder by the Agency, including all fees, compensation and expenses of the Trustee, then the right, title and interest of the Trustee in and to the Trust Estate shall thereupon cease, terminate and become void and the Trustee shall release or cause to be released the Trust Estate, the Mortgage and any other documents securing the Bonds or execute such documents so as to permit the Trust Estate, the Mortgage and such other documents to be released.

Any Bond shall be deemed to be paid within the meaning of this Article and for all purposes of this Indenture when (a) payment of the principal of and premium, if any, on such Bond, plus interest thereon to the due date thereof (whether such due date is by reason of maturity or upon redemption as provided herein) shall have been made or caused to be made in accordance with the terms thereof and (b) all fees, compensation and expenses of the Trustee pertaining to the Bond with respect to which such deposit is made accrued and to accrue until final payment of the Bonds, whether at maturity or upon redemption, shall have been paid or the payment thereof provided for to the satisfaction of the Trustee. At such times as a Bond shall be deemed to be paid hereunder, as aforesaid, such Bond shall no longer be secured by or entitled to the benefits of this Indenture.

ARTICLE VIII

DEFAULTS AND REMEDIES

Section 8.1. Events of Default. Each of the following events shall constitute an “Event of Default” hereunder with respect to the Bonds:

(a) payment of any interest on a Bond shall not be made when the same becomes due and payable, provided sufficient Excess Project Revenues have been deposited in the Bond Fund for such payment;

(b) payment of the principal of or the Redemption Price a Bond shall not be made when the same shall become due and payable, either at maturity or by proceedings for redemption or otherwise, provided sufficient Excess Project Revenues have been deposited in the Bond Fund for such payments; or

(c) failure in the performance or observance of any of the other agreements or conditions on the part of the Agency (other than as referred to in (A) and (B) above) herein or in the Bonds contained and the continuance of such failure for a period of 60 days after receipt of notice given by the Trustee thereof to the Agency or the Borrower; provided, however, that if such failure is such that it can be corrected but not within such 60 day period, it shall not constitute an Event of Default if corrective action capable of remedying such default is instituted by the Agency or the Borrower within such 60 day period and diligently pursued until such failure is corrected but in any event not more than 90 days without the
written consent of all Bondholders.

Notwithstanding any other provision hereof to the contrary, failure to make a payment on the Bonds shall not result in a default hereunder so long as the Trustee applies to the payment of principal and interest on the Bonds all principal and interest received from the Borrower under the Loan.

Notice of an Event of Default hereunder shall be promptly provided by the Trustee to the Agency and to the trustee for the Senior Bonds. An Event of Default hereunder shall not, in and of itself, constitute an event of default with respect to the Senior Loan or the Senior Bonds.

Section 8.2. Acceleration; Other Remedies.

Upon the occurrence and continuance of an Event of Default, the Trustee, may, with the written consent of the Senior Lender, and at the written request of the Senior Lender, or the Owners of a majority of the Bond Obligation, with the consent of the Senior Lender, shall, by written notice to the Agency and the Borrower, declare the Bonds to be immediately due and payable, whereupon such Bonds shall, without further action, become and be immediately due and payable, anything in this Indenture or in the Bonds to the contrary notwithstanding, and the Trustee shall give notice thereof to the Agency and the Senior Lender, and shall give notice thereof by first-class mail to Owners of the Bonds.

The provisions of the preceding paragraph are subject to the condition that if, after the principal of the Bonds shall have been so declared to be due and payable, and before any judgment or decree for the payment of the moneys due shall have been obtained or entered as hereinafter provided, (i) a sum sufficient to pay all matured installments of interest on all Bonds and the principal of any and all Bonds that have become due otherwise than by reason of such declaration shall have been deposited with the Trustee and such amount as shall be sufficient to cover reasonable compensation and reimbursement of fees and expenses (including reasonable attorneys fees and expenses) payable to the Trustee, and (ii) all Events of Default hereunder other than nonpayment of the principal of the Bonds that shall have become due by said declaration shall have been remedied, then, in every such case, upon the written consent of the Owners of not less than a majority of the Bond Obligation Outstanding, such Event of Default shall be deemed waived and such declaration and its consequences rescinded and annulled, and the Trustee shall promptly give written notice of such waiver, rescission or annulment to the Agency and the Trustee, and shall give notice thereof by first-class mail to all Owners of Bonds; but no such waiver, rescission and annulment shall extend to or affect any subsequent Event of Default or impair any right or remedy consequent thereon.

Upon the occurrence and continuance of any Event of Default, then and in every such case the Trustee in its discretion may, with the written consent of the Senior Lender, and upon the written direction of the Owners of not less than a majority of the Bond Obligation Outstanding, and receipt of indemnity to its reasonable satisfaction shall, in its own name and as the Trustee of an express trust:

(i) by mandamus, or other suit, action or proceeding at law or in equity, enforce all rights of the Owners under this Indenture or the Bonds, including without limitation requiring the Agency or the Borrower to carry out any agreements with or for the benefit of the Owners and to perform its or their duties under the Act, the Loan Agreement, the Mortgage and this Indenture, provided that any such remedy may be taken only to the extent permitted under the applicable provisions of the Loan Agreement, the Mortgage or this Indenture, as the case may be;

(ii) bring suit upon the Bonds;
(iii) by action or suit in equity require the Agency to account as if it were the trustee of an express trust for the Owners of the Bonds;

(iv) by action or suit in equity enjoin any acts or things which may be unlawful or in violation of the rights of the Owners of the Bonds hereunder;

(v) file proofs of claim in any bankruptcy or insolvency proceedings related to the Agency, the Borrower or the Project, necessary or appropriate to protect the interests of the Trustee or the Owners of the Bonds; or

(vi) exercise any rights available to it hereunder or under the Borrower Documents.

Notwithstanding anything herein to the contrary, neither the Owners of the Bonds nor the Trustee acting on behalf of the Owners of the Bonds shall have any right, and hereby waive any right, to institute a proceeding under the Bankruptcy Code seeking to adjudge the Agency insolvent or a bankrupt or seeking a reorganization of the Agency.

Section 8.3. Restoration to Former Position. In the event that any proceeding taken by the Trustee to enforce any rights under this Indenture shall have been discontinued or abandoned for any reason, or shall have been determined adversely to the Trustee, then the Agency, the Trustee and the Owners shall be restored to their former positions and rights hereunder, respectively, and all rights, remedies and powers of the Trustee shall continue as though no such proceeding had been taken.

Section 8.4. Cure by Owners. Any Owner of Bonds may, but shall not be obligated to, cure an Event of Default under this Indenture, including the advancing of funds to the Trustee for payments required under this Indenture, or to indemnify the Trustee under Section 9.4 hereof. Any funds so advanced are to be applied by the Trustee in accordance with the instructions of the Owner providing the same.

Section 8.5. Owners' Right to Direct Proceedings. Anything in this Indenture to the contrary notwithstanding, the Owners of at least a majority of the Bond Obligation shall have the right, by an instrument in writing executed and delivered to the Trustee, consented to in writing by the Senior Lender, to direct the time, method and place of conducting all remedial proceedings available to the Trustee under this Indenture or exercising any trust or power conferred on the Trustee by this Indenture; provided that the Trustee may decline to follow any direction that would favor one or more Bondholders over the remaining Bondholders.

Section 8.6. Limitation on Owners' Right to Institute Proceedings. No Owner shall have any right to institute any suit, action or proceeding in equity or at law for the execution of any trust or power hereunder, or any other remedy hereunder or on the Bonds, unless such Owner previously shall have given to the Trustee written notice of an Event of Default as hereinabove provided and unless also the Owners of not less than a majority of the Bond Obligation shall have made written request of the Trustee to do so, consented to in writing by the Senior Lender, after the right to institute said suit, action or proceeding under Section 8.2 hereof shall have accrued, and shall have afforded the Trustee a reasonable opportunity to proceed to institute the same in either its or their name, and the Trustee shall not have complied with such request within a reasonable time. No one or more of the Owners of the Bonds shall have any right in any manner whatever by its or their action to affect, disturb or prejudice the security of this Indenture, or to enforce any right hereunder or under the Bonds, except in the manner herein provided, and all suits, actions and proceedings at law or in equity shall be instituted, had and maintained in the manner herein provided and for the equal benefit of all Owners of Bonds.
Notwithstanding anything to the contrary, the furnishing of indemnity to the Trustee as provided in Section 9.6 hereof is hereby declared in every such case, at the option of the Trustee, to be a condition precedent to the institution of said suit, action or proceeding by the Trustee.

**Section 8.7. No Impairment of Right to Enforce Payment.** Notwithstanding any other provision in this Indenture, the right of any Owner of a Bond to receive payment of the principal of and interest on such Bond, on or after the respective due dates expressed therein, or to institute suit for the enforcement of any such payment on or after such respective date, shall not be impaired or affected without the consent of such Owner.

**Section 8.8. Proceedings by Trustee Without Possession of Bonds.** All rights of action under this Indenture or under any of the Bonds secured hereby which are enforceable by the Trustee may be enforced by it without the possession of any of the Bonds, or the production thereof at the trial or other proceedings relative thereto, and any such suit, action or proceeding instituted by the Trustee shall be brought in its name for the equal and ratable benefit of the Owners of all of the Bonds, subject to the provisions of this Indenture.

**Section 8.9. No Remedy Exclusive.** No remedy herein conferred upon or reserved to the Trustee or to Owners is intended to be exclusive of any other remedy or remedies, and each and every such remedy shall be cumulative, and shall be in addition to every other remedy given hereunder, or now or hereafter existing at law or in equity or by statute; provided, however, that any conditions set forth herein to the taking of any remedy to enforce the provisions of this Indenture or the Bonds shall also be conditions to seeking any remedies under any of the foregoing pursuant to this Section.

**Section 8.10. No Waiver of Remedies.** No delay or omission of the Trustee or of any Owner to exercise any right or power accruing upon any default shall impair any such right or power or shall be construed to be a waiver of any such default, or an acquiescence therein; and every power and remedy given by this Article to the Trustee and to the Owners, respectively, may be exercised from time to time and as often as may be deemed expedient.

**Section 8.11. Application of Moneys.**

If an Event of Default exists, any moneys held in any Fund or Account hereunder (excluding the Rebate Fund) or received by the Trustee, by any receiver or by any Owner pursuant to any right given or action taken under the provisions of this Article, after payment of (i) the costs and expenses of the proceedings resulting in the collection of such moneys, and (ii) the fees, expenses, liabilities or advances payable to or incurred or made by the Trustee or any Owner, shall be deposited in the Revenue Fund; and all moneys so deposited in the Revenue Fund during the continuance of an Event of Default (other than moneys for the payment of Bonds that had matured or otherwise become payable prior to such Event of Default or for the payment of interest due prior to such Event of Default) shall be applied as follows:

Unless the principal of all the Bonds shall have been declared due and payable, all such moneys shall be applied (A) first, to the payment to the persons entitled thereto of all installments of interest then due on the Bonds, in the order of maturity of the installments of such interest and, if the amount available shall not be sufficient to pay in full any particular installment of interest, then to the payment ratably, according to the amounts due on such installment; and (B) second, to the payment to the persons entitled thereto of the unpaid principal of any of the Bonds that shall have become due (other than Bonds called for redemption for the payment of which money is held pursuant to the provisions of this Indenture) and, if the amount available shall not be sufficient to pay in full the Bonds due on any particular date, together with such interest, then to the payment ratably, according to the amount of principal and interest due on such date, in each case to the persons entitled thereto, without any discrimination or privilege.
If the principal of all the Bonds shall have been declared due and payable, all such moneys shall be applied to the payment of the principal and interest then due and unpaid upon the Bonds, without preference or priority of principal over interest or interest over principal, or of any installment of interest over any other installment of interest, or of any Bond over any other Bond, ratably, according to the amounts due respectively for principal and interest, to the persons entitled thereto without any discrimination or privilege.

Whenever moneys are to be applied pursuant to the provisions of this Section, such moneys shall be applied at such times, and from time to time, as the Trustee shall determine, having due regard to the amount of such moneys available for application and the likelihood of additional moneys becoming available for such application in the future. Whenever the Trustee shall apply such funds, it shall fix the date (which shall be an Interest Payment Date unless it shall deem another date more suitable) upon which such application is to be made and upon such date interest on the amounts of principal and interest to be paid on such date shall cease to accrue. The Trustee shall give notice of the deposit with it of any such moneys and of the fixing of any such date by first-class mail to all Owners of the Bonds and shall not be required to make payment to any Owner of a Bond until such Bond shall be presented to the Trustee for appropriate endorsement or for cancellation if fully paid.

Section 8.12. Severability of Remedies. It is the purpose and intention of this Article to provide rights and remedies to the Trustee and the Owners that may be lawfully granted under the provisions of the Act, but should any right or remedy herein granted be held to be unlawful, the Trustee and the Owners shall be entitled, as above set forth, to every other right and remedy provided in this Indenture and by law.

Section 8.13. Notice of Event of Default. If an Event of Default occurs and continues for five (5) Business Days after the Trustee has notice of the same as provided in Section 9.5 hereof, then the Trustee shall give notice thereof by first-class mail to the Owners, the Borrower and the Agency.

Section 8.14. No Interference or Impairment of Senior Loan. Notwithstanding anything herein to the contrary, as long as the Senior Loan is outstanding, neither the Agency, the Trustee nor any other person shall:

(a) initiate or take any action which may have the effect, directly or indirectly, of impairing the ability of the Borrower to timely pay the principal of, interest on, or other amounts due and payable under, the Senior Loan;

(b) interfere with or attempt to interfere with or influence the exercise by the Senior Lender of any of its rights under the Senior Loan, including, without limitation, any remedial rights of the Senior Lender under the Senior Loan upon the occurrence of an event of default by the Borrower under the Mortgage; or

(c) upon the occurrence of an event of default under the Loan or the Senior Loan, take any action to accelerate or otherwise enforce payment or seek other remedies with respect to the Senior Loan,

it being understood and agreed that neither the Agency nor the Trustee may, without the prior written consent of the Senior Lender, on account of any default under this Indenture, cause the Senior Loan to become due and payable or to declare the principal of the Senior Loan and the interest accrued on the Senior Loan to be immediately due and payable, or cause the trustee to foreclosure or take any other action under the Senior Loan Documents or any other documents to obtain such performance or observance.
No person other than the Senior Lender shall have the right to declare the principal balance of the deed of trust securing the Senior Loan to be immediately due and payable.

The foregoing prohibitions and limitations shall not limit the rights of the Agency or the Trustee to specifically enforce this Indenture in order to provide for the operation of the Project in accordance with the requirements of the Code and the Act, and shall not be construed to limit the rights of the Agency to enforce its rights against the Borrower under the indemnification provisions of this Indenture so long as it does not cause the Borrower to file a petition seeking reorganization, arrangement, adjustment or composition of or in respect of the Borrower under any applicable liquidation, insolvency, bankruptcy, rehabilitation, composition, reorganization, conservation or other similar law in effect now or in the future.

Notwithstanding anything in this Indenture to the contrary, any right of the Agency or the Trustee to take any action at law or in equity to enforce the obligations, covenants and agreements of the Borrower under this Indenture which includes any claim for indemnification, damages or any other monetary obligation sought to be enforced shall be subject and subordinate in all respects to the repayment in full of all amounts due to the Senior Lender from the Borrower under the Senior Loan Documents.

All obligations of the Borrower under this Indenture for the payment of money, including claims for indemnification and damages shall not be secured by or in any manner constitute a lien on the Project, and neither the Agency nor the Trustee shall have the right to enforce such obligations other than directly against the Borrower.

No subsequent Borrower of the Project shall be liable or obligated for the breach or default of any obligation of any prior Borrower unless specifically assumed in writing by a subsequent Borrower, including, but not limited to, any payment or indemnification obligation. Such obligations shall be personal to the person who was the Borrower at the time the default or breach was alleged to have occurred and such person shall remain liable for any and all damages occasioned by the default or breach even after person ceases to be the Borrower of the Project.

Promptly upon determining that a violation of this Indenture has occurred, the Agency or the Trustee shall, by notice in writing to the Senior Lender, inform the Senior Lender that such violation has occurred, the nature of the violation and that the violation has been cured or has not been cured, but is curable within a reasonable period of time, or is incurable; notwithstanding the occurrence of such violation, neither the Agency nor the Trustee shall have, and each of them acknowledge that they shall not have, any right to cause or direct acceleration of the Senior Loan, to enforce the Senior Loan documents or to foreclosure on deed of trust securing the Senior Loan.

ARTICLE IX

TRUSTEE

Section 9.1. Acceptance of Trusts. The Trustee hereby accepts the trusts imposed upon it by this Indenture, and agrees to perform said trusts, but only upon and subject to the following express terms and conditions set forth in this Article IX:

(a) The Trustee, before the occurrence of an Event of Default and after the curing of all Events of Default that may have occurred, undertakes to perform such duties and only such duties as are specifically set forth in this Indenture. In case an Event of Default has occurred (which has not been
cured or waived), the Trustee shall exercise such of the rights and powers vested in it by this Indenture, and use the same degree of care and skill in their exercise, as a prudent person would exercise or use under the circumstances in the conduct of his or her own affairs.

(b) The Trustee shall not be accountable for the use of any Bonds authenticated or delivered hereunder. The Trustee may buy, sell, own and deal in any of the Bonds secured hereby with the same rights, which it would have were it, not the Trustee.

(c) The Trustee shall not withhold unreasonably its consent, approval or action to any reasonable request of the Agency, provided that any such consent, approval or action is permitted by this Indenture. Any action taken by the Trustee pursuant to this Indenture upon the request or authority or consent of any person who at the time of making such request or giving such authority or consent is the owner of any Bond shall be conclusive and binding upon all future owners of the same Bond and upon Bonds issued in exchange therefor or in place thereof.

(d) As to the existence or nonexistence of any fact or as to the sufficiency or validity of any instrument, paper or proceeding, the Trustee shall be entitled to rely upon a certificate signed by an Agency Representative or a Borrower Representative as sufficient evidence of the facts therein contained, and before the occurrence of a default of which the Trustee has notice as provided in Section 9.5 hereof, or of which by said Section it is deemed to have notice, shall also be at liberty to accept a similar certificate to the effect that any particular dealing, transaction or action is necessary or expedient, but may, at its discretion, secure such further evidence reasonably deemed necessary or advisable, but shall not be bound to secure the same. The Trustee may accept a certificate of the Secretary of the Agency to the effect that a resolution in the form therein set forth has been adopted by the Agency as conclusive evidence that such resolution has been duly adopted, and is in full force and effect.

(e) The permissive right of the Trustee to do things enumerated in this Indenture shall not be construed as a duty, and it shall not be answerable for other than its negligence or willful misconduct.

(f) At any and all reasonable times the Trustee, and its duly authorized agents, attorneys, experts, engineers, accountants and representatives, shall have the right (but not any duty) fully to inspect any and all of the property herein conveyed, including all books, papers and records of the Agency or the Borrower pertaining to the revenues and receipts relating to the Project or the Bonds, and to take such memoranda from and in regard thereto as may be desired.

(g) The Trustee shall not be required to give any bond or surety in respect of the execution of the trusts and powers hereunder or otherwise in respect of the premises.

(h) The Trustee shall not be under any duty or obligation to perform any act that would cause it to incur any expense or liability or to institute or defend any suit in respect of this Indenture or to advance any of its own moneys.

(i) The Trustee shall not be required to enter, take possession of or take any other action with respect to the Project unless it shall have first received assurances satisfactory to it that the Trustee will not be subject to liability for the existence of, or contamination by environmentally hazardous substances or other discharges, emissions or releases with respect to the Project.

(j) The Trustee shall have no responsibility, opinion or liability with respect to any information, statements or recitals in any offering memorandum or other disclosure material prepared or distributed with respect to the issuance of the Bonds.
(k) The Trustee's rights to immunities and protection from liability hereunder and its rights to payment of its fees and expenses shall survive its resignation or removal and final payment or defeasance of the Bonds.

(l) The Trustee shall not be under any obligation to effect or maintain insurance or to renew any policies of insurance or to inquire as to the sufficiency of any policies of insurance carried by the Borrower, or to report, or make or file claims or proof of loss for, any loss or damage insured against or which may occur.

(m) All moneys received by the Trustee need not be segregated except to the extent required by law.

(n) The Trustee shall not be liable for any action taken or not taken by it in accordance with the direction of a majority (or other percentage provided for herein) in aggregate principal amount of Bonds outstanding relating to the exercise of any right, power or remedy available to the Trustee.

Section 9.2. No Responsibility for Recitals. The recitals, statements and representations contained in this Indenture or in the Bonds, save only the Trustee's authentication upon the Bonds, shall be taken and construed as made by and on the part of the Agency, and not by the Trustee, and the Trustee does not assume, and shall not have, any responsibility or obligation for the correctness of any thereof.

Section 9.3. Limitations on Liability. The Trustee may execute any of the trusts or powers hereof and perform the duties required of it hereunder by or through attorneys, agents, receivers or employees selected by it, and shall be entitled to advice of counsel concerning all matters of trust and its duty hereunder and to obtain the opinion of counsel prior to taking action hereunder, and may in all cases pay such reasonable compensation to all such attorneys, agents, receivers or employees as is reasonable in connection with the performance of the Trustee's duties under this Indenture, and the Trustee shall not be answerable for the default or misconduct of any such attorney, agent or employee selected by it with reasonable care. The Trustee may act upon the advice of any attorney approved by the Trustee in the exercise of reasonable care, and the Trustee shall not be responsible for any loss or damage resulting from any action or nonaction in good faith reliance upon such opinion or advice. The Trustee shall not be answerable for the exercise of any discretion or power under this Indenture or for anything whatsoever in connection with the trust created hereby, except only for its own negligence or willful misconduct.

Section 9.4. Compensation, Expenses and Advances. The Trustee shall be entitled to reasonable compensation for its services rendered hereunder (not limited by any provision of law in regard to the compensation of the trustee of an express trust) and to reimbursement for its actual out-of-pocket expenses (including reasonable counsel fees and expenses and any fees, expenses, payments, indemnification reserves or other security which may be incurred in connection with the appointment or designation of a separate trustee for all or part of the Bonds) reasonably incurred in connection therewith, except as a result of its negligence or willful misconduct. The Agency agrees that it will, but solely from the Trust Estate as provided herein, or will require the Borrower to, pay to the Trustee such compensation and reimbursement of expenses and advances, but the Agency may, without creating a default hereunder, contest in good faith the reasonableness of any such services, expenses and advances but only after the payment thereof.

Section 9.5. Notice of Events of Default. The Trustee shall not be required to take notice, or be deemed to have notice, of any default or Event of Default under this Indenture, other than an Event of Default under clause (a) or (b) of Section 8.1 hereof, unless a Responsible Officer of the Trustee shall have received actual knowledge or shall have been specifically notified in writing of such default or Event.
of Default by the Agency, the Borrower, or the Owners of at least 25% of the Bond Obligation. The 
Trustee may, however, at any time, in its discretion, and shall, upon the request of at least 25% of the 
Bond Obligation, require of the Borrower full information and advice as to the performance of any of the 
covenants, conditions and agreements contained herein.

Section 9.6.  Action by Trustee. The Trustee shall be under no obligation to take any action 
in respect of any default or Event of Default hereunder or toward the execution or enforcement of any of 
the trusts hereby created, or to institute, appear in or defend any suit or other proceeding in connection 
therewith, and if in its opinion such action may tend to involve it in expense or liability, unless furnished, 
from time to time as often as it may require, with security and indemnity reasonably satisfactory to it; but 
the foregoing provisions are intended only for the protection of the Trustee, and shall not affect any 
discretion or power given by any provisions of this Indenture to the Owners or to the Trustee to take 
action in respect of any default or Event of Default without such notice or request from the Owners, or 
without such security or indemnity.

Section 9.7.  Good Faith Reliance. The Trustee shall be protected and shall incur no liability 
in acting or proceeding in good faith, reasonably exercised, upon any resolution, notice, telex or facsimile 
transmission, request, consent, waiver, certificate, statement, affidavit, voucher, bond, requisition or other 
paper or document which it shall in good faith believe to be genuine and to have been passed or signed by 
the proper board, body or person or to have been prepared and furnished pursuant to any of the provisions 
of this Indenture or the other Bond Documents, or upon the written opinion of any attorney, engineer, 
accountant or other expert reasonably believed by the Trustee to be qualified in relation to the subject 
matter, and the Trustee shall be under no duty to make any investigation or inquiry as to the qualification 
of such person or any statements contained or matters referred to in any such instrument, but may accept 
and rely upon the same as conclusive evidence of the truth and accuracy of such statements.

Section 9.8.  Dealings in Bonds or with the Agency or the Borrower. The Trustee, in its 
individual capacity, may in good faith, reasonably exercised, buy, sell, own, hold and deal in any of the 
Bonds issued hereunder, and may join in any action which any Owner may be entitled to take with like 
effect as if it did not act in any capacity hereunder. The Trustee, in its individual capacity, either as 
principal or agent, may also engage in or be interested in any financial or other transaction with the 
Agency or the Borrower, and may act as depository, trustee or agent for any committee or body of 
Owners secured hereby or other obligations of the Agency or the Borrower as freely as if it did not act in 
any capacity hereunder.

Section 9.9.  Resignation of Trustee. The Trustee may resign and be discharged of the trusts 
created by this Indenture by executing an instrument in writing resigning such trust and specifying the 
date when such resignation shall take effect, and filing the same with the Agency and the Borrower, and 
by giving notice of such resignation by first-class mail, not less than fifteen (15) days prior to such 
resignation date, to all Owners. Such resignation shall only take effect on the day a successor Trustee 
shall have been appointed as hereinafter provided.

Section 9.10.  Removal of Trustee. The Trustee may be removed at any time by the Agency or 
by filing with the Trustee so removed and with the Agency an instrument or instruments in writing 
appointing a successor, executed by an Agency Representative; provided that the Agency may not remove 
the Trustee if an Event of Default has occurred and is continuing hereunder.

Section 9.11.  Appointment of Successor Trustee. If at any time the Trustee shall be 
removed, or be dissolved, or if its property or affairs shall be taken under the control of any state or 
federal court or administrative body because of insolvency or bankruptcy, or for any other reason, then a
vacancy shall forthwith and ipso facto exist in the office of Trustee and a successor may be appointed, and if at any time the Trustee shall resign, then a successor may be appointed, by the Agency.

Section 9.12. Qualifications of Trustee. The Trustee and every successor Trustee, if any, (a) shall be a bank or trust company duly organized under the laws of the United States or any state thereof authorized by law to perform all the duties imposed upon it by this Indenture, (b) shall at the time of appointment have (or in the case of a corporation or trust company included in a bank holding company system, the related bank holding company shall have) trust assets under management of at least $50,000,000, and (c) shall be permitted under the Act to perform the duties of Trustee.

Section 9.13. Judicial Appointment of Successor Trustee. If at any time the Trustee shall resign and no appointment of a successor Trustee shall be made pursuant to the foregoing provisions of this Article prior to the date specified in the notice of resignation as the date when such resignation is to take effect, the resigning Trustee may forthwith apply to a court of competent jurisdiction for the appointment of a successor Trustee. If no appointment of a successor Trustee shall be made pursuant to the foregoing provisions of this Article within six (6) months after a vacancy shall have occurred in the office of Trustee, any Owner may apply to any court of competent jurisdiction to appoint a successor Trustee. Such court may thereupon, after such notice, if any, as it may deem proper and prescribe, appoint a successor Trustee.

Section 9.14. Acceptance of Trusts by Successor Trustee. Any successor Trustee appointed hereunder shall execute, acknowledge and deliver to the Agency an instrument accepting such appointment hereunder, and thereupon such successor Trustee, without any further act, deed or conveyance, shall become duly vested with all the estates, property, rights, powers, trusts, duties and obligations of its predecessor in the trust hereunder, with like effect as if originally named Trustee herein. Upon request of such Trustee and the payment of the predecessor Trustee's fees and expenses hereunder, such predecessor Trustee and the Agency shall execute and deliver an instrument transferring to such successor Trustee all the estates, property, rights, powers and trusts hereunder of such predecessor trustee and, subject to the provisions of Section 9.4 hereof, such predecessor Trustee shall pay over to the successor Trustee all moneys and other assets at the time held by it hereunder, and such predecessor Trustee shall assign its beneficial interest in the Mortgage, if any, to the successor Trustee and record said assignment in the same manner as the Mortgage was recorded.

Section 9.15. Successor by Merger or Consolidation. Any corporation into which the Trustee may be merged or converted or with which it may be consolidated, or any corporation resulting from any merger, conversion or consolidation to which the Trustee shall be a party, or any corporation succeeding to the business of the Trustee, or any company to which the Trustee may sell or transfer all or substantially all of its corporate trust business, provided such corporation meets the qualifications contained in Sections 9.12 hereof, as appropriate, shall be the successor Trustee under this Indenture, without the execution or filing of any paper or any further act on the part of the parties hereto, anything in this Indenture to the contrary notwithstanding.

ARTICLE X

MODIFICATION OF BOND DOCUMENTS

Section 10.1. Limitations. No Bond Document shall be amended in any respect subsequent to the first delivery of fully executed and authenticated Bonds except as provided in and in accordance with and subject to the provisions of this Article. Notwithstanding any provisions of this Article, the Tax Certificate and any regulatory agreement may be amended pursuant to the provisions thereof, and shall be amended to the extent required by such documents.
Section 10.2. Supplemental Indentures Without Owner Consent. With the written consent of the Senior Lender, the Agency and the Trustee may (and in the case of clause (g) shall), from time to time and at any time, without the consent of but with prompt notice to the Owners, enter into Supplemental Indentures as follows:

(a) to cure any formal defect, omission, inconsistency or ambiguity in this Indenture;

(b) to add to the covenants and agreements of the Agency in this Indenture other covenants and agreements, or to surrender any right or power reserved or conferred upon the Agency if such surrender shall not, materially adversely affect the interests of the Owners, the Trustee being authorized to rely on an opinion of counsel with respect thereto;

(c) to confirm, as further assurance, any pledge of or lien on the Loan Agreement or of any other moneys, securities or funds subject to the lien of this Indenture;

(d) to preserve the exclusion of interest on the Bonds from gross income for federal income tax purposes, as set forth in an opinion of Bond Counsel; or

(e) to provide for any amendment specifically authorized or required by any provision of this Indenture.

Section 10.3. Supplemental Indentures Requiring Owners' Consent. No Supplemental Indenture may be entered into without the written consent of the Senior Lender and, except for any Supplemental Indenture entered into pursuant to Section 10.2 hereof, no Supplemental Indenture may be entered into without the consent of the Owners of not less than a majority of the Bond Obligation affected thereby; provided, however, that, unless approved in writing by all Owners of Bonds affected thereby, nothing herein contained shall permit, or be construed as permitting, (i) a change in the times, amounts or currency of payment of the principal of or interest on any Outstanding Bond or a reduction in the principal amount or redemption price of any Outstanding Bond or the rate of interest thereon, or (ii) the creation of a claim or lien upon, or a pledge of, the Trust Estate ranking prior to or on a parity with the claim, lien or pledge created by this Indenture, or (iii) a reduction in the aggregate Bond Obligation the consent of the Owners of which is required for any such Supplemental Indenture or which is required, under Section 10.5 hereof, for any modification, alteration, amendment or supplement to any Borrower Documents.

Section 10.4. Amendment of Borrower Documents Without Owner Consent. With the written consent of the Senior Lender and without the consent of but with notice to the Owners, the Trustee may (and in the case of clause (e) shall) consent to any amendment of any Borrower Document from time to time as follows:

(a) to cure any formal defect, omission, inconsistency or ambiguity in such Borrower Document;

(b) to add to the covenants and agreements of the Agency or the Borrower in such document other covenants and agreements;

(c) to confirm, as further assurance, any lien or pledge of the Project or the revenues therefrom or of any other property, moneys, securities or funds subject to the Mortgage or any other security for the Loan Agreement; or
(d) to preserve the exclusion of interest on the Bonds from gross income for federal income tax purposes, as set forth in an opinion of Bond Counsel.

Section 10.5. Amendment of Borrower Documents Requiring Owner Consent. No Borrower document may be amended without the written consent of the Senior Lender and, except in the case of amendments referred to in Sections 10.1 and 10.4 hereof, the Agency shall not enter into, and the Trustee shall not consent to, any amendment of any Borrower Document without the written approval or consent of the Owners of not less than a majority of the Bond Obligation, given and procured as provided in Section 10.6 hereof; provided, however, that, unless approved in writing by all the Owners of the Bonds affected thereby, nothing herein contained shall permit, or be construed as permitting, an amendment which has any of the effects described in clauses (i) through (iii) of Section 10.3.

Section 10.6. Procedures for Amendments. If at any time the Trustee shall be requested to enter into any Supplemental Indenture pursuant to Section 10.2 or to consent to any amendment pursuant to Section 10.5, the Trustee shall cause notice of the proposed Supplemental Indenture or other amendment to be given by first-class mail to all Owners. Such notice shall briefly set forth the nature of the proposed Supplemental Indenture or other amendment and shall state that a copy thereof is on file at the office of the Trustee for inspection by all Owners. Within two (2) years after the date of the first giving of such notice, the Agency and the Trustee may enter into such Supplemental Indenture or the Trustee may consent to such amendment in substantially the form described in such notice, but only if there shall have first been delivered to the Trustee (i) the required consents, in writing, of Owners and (ii) the opinion of Bond Counsel required by Section 10.7 hereof.

If Owners of not less than the amount of Bond Obligation required by Section 10.2 or 10.5, as applicable, shall have consented to and approved the execution and delivery thereof as herein provided, no Owner shall have any right to object to the execution and delivery of such Supplemental Indenture or other amendment, or to object to any of the terms and provisions contained therein or the operation thereof, or in any manner to question the propriety of the execution and delivery thereof, or to enjoin or restrain the Agency or the Trustee from executing and delivering or consenting to the same or from taking or permitting any action pursuant to the provisions thereof.

Section 10.7. Opinions; Certificate. The Trustee shall not enter into or consent to any amendment of any provision of any Bond Document except with the written consent of the Agency and upon delivery to the Agency and the Agency of an opinion of Bond Counsel stating that such amendment will not adversely affect the exclusion of interest on the Bonds from the gross income of the recipients thereof for federal income tax purposes. In addition, the Trustee shall be furnished, and shall be protected in relying on, an opinion of counsel to the effect that such amendment is authorized or permitted by this Indenture and complies with the terms hereof.

Section 10.8. Effect of Amendments. Upon the execution and delivery of any Supplemental Indenture or any amendment to a Borrower Document pursuant to the provisions of this Article, this Indenture or such Borrower Document shall be, and be deemed to be, modified and amended in accordance therewith, and the respective rights, duties and obligations under the Bond Documents of the Agency, the Trustee, the Borrower and all Owners shall thereafter be determined, exercised and enforced under the Bond Documents subject in all respects to such modifications and amendments.
ARTICLE XI
MISCELLANEOUS

Section 11.1. Successors of the Agency. In the event of the dissolution or transfer of functions of the Agency, all the covenants, stipulations, promises and agreements in this Indenture contained, by or on behalf of, or for the benefit of, the Agency, shall bind or inure to the benefit of the successors of the Agency from time to time and any entity, officer, board, commission, agency or instrumentality to whom or to which any power or duty of the Agency shall be transferred.

Section 11.2. Parties in Interest. Except as herein otherwise specifically provided, nothing in this Indenture expressed or implied is intended or shall be construed to confer upon any person, firm or corporation other than the Agency, the Borrower, the Trustee and the Owners any right, remedy or claim under or by reason of this Indenture, this Indenture being intended to be for the sole and exclusive benefit of the Agency, the Borrower, the Trustee and the Owners.

Section 11.3. Severability. In case any one or more of the provisions of this Indenture or of any Borrower Document or of the Bonds shall, for any reason, be held to be illegal or invalid, such illegality or invalidity shall not affect any other provisions of this Indenture, such Borrower Document or such Bonds, and this Indenture, the Borrower Documents and the Bonds shall be construed and enforced as if such illegal or invalid provisions had not been contained herein or therein.

Section 11.4. No Personal Liability. No covenant or agreement contained in the Bonds or in this Indenture shall be deemed to be the covenant or agreement of any official, director, officer, agent or employee of the Agency or the Trustee in his or her individual capacity, and neither the members of the Agency or the Trustee nor any official executing the Bonds shall be liable personally on the Bonds or be subject to any personal liability or accountability by reason of the issuance thereof.

Section 11.5. Counterparts. This Indenture may be executed in any number of counterparts, each of which, when so executed and delivered, shall be an original; but such counterparts shall together constitute but one and the same Indenture.

Section 11.6. Governing Law. The laws of the State shall govern the construction and enforcement of this Indenture and of all the Bonds issued hereunder.

Section 11.7. Notices. Except as otherwise provided in this Indenture, all notices, certificates, requests, requisitions or other communications by the Agency, the Trustee or the Trustee pursuant to this Indenture shall be in writing and shall be sufficiently given and shall be deemed given when mailed by registered mail, postage prepaid, addressed as follows:

To the Issuer: California Housing Finance Agency
1415 L Street, Suite 500
Sacramento CA 95814

To the Trustee: [TRUSTEE]

To the Borrower: [BORROWER]
Any of the foregoing may, by notice given hereunder to each of the others, designate any further or different addresses to which subsequent notices, certificates, requests or other communications shall be sent hereunder or under the Loan Agreement.

Section 11.8. Holidays. If the date for making any payment or the last date for performance of any act or the exercising of any right, as provided in this Indenture, shall not be a Business Day, such payment may, unless otherwise provided in this Indenture, be made or act performed or right exercised on the next succeeding Business Day with the same force and effect as if done on the nominal date provided in this Indenture, and no interest shall accrue for the period from and after such nominal date.

(Remainder of page intentionally left blank.)
IN WITNESS WHEREOF, the California Housing Finance Agency has caused this Indenture to be signed in its name by its Director of Financing and its corporate seal to be affixed hereto and attested by the Secretary of its Board of Directors, and [TRUSTEE], in token of its acceptance of the trusts created hereunder, has caused this Indenture to be signed in its corporate name by one of its authorized signatories, all as of the day and year first above written.

CALIFORNIA HOUSING FINANCE AGENCY

By: ______________________________
   Director of Financing

[Seal]

Attest:____________________________
   Secretary of the Board of Directors

[TRUSTEE], as Trustee

By: ______________________________
   Agency Representative

Agreed to and Acknowledged by:

[BORROWER]

By: ______________________________
   Authorized Officer
EXHIBIT A
[FORM OF BOND]

No.- __________ $ _______

THIS BOND MAY TRANSFERRED ONLY WITH THE CONSENT OF THE ISSUER HEREOF AND MAY
BE OWNED ONLY BY A QUALIFIED INSTITUTIONAL BUYER OR AN ACCREDITED
INSTITUTIONAL INVESTOR (AS DEFINED UNDER THE SECURITIES ACT OF 1933, AS AMENDED)
AND THE HOLDER HEREOF REPRESENTS THAT IT IS SUCH AN ACCREDITED INSTITUTIONAL
INVESTOR.

CALIFORNIA HOUSING FINANCE AGENCY
MULTIFAMILY HOUSING REVENUE BOND
SUBORDINATE LOAN INDENTURE
20__ SERIES __ ([PROJECT] PROJECT)

INTEREST RATE DATED DATE MATURITY DATE CUSIP NO.

REGISTERED OWNER:

PRINCIPAL AMOUNT: ___________________________ AND NO/100 DOLLARS

The CALIFORNIA HOUSING FINANCE AGENCY (the “Agency”), a public instrumentality
and a political subdivision of the State of California (the “State”), for value received, promises to pay,
subject to the provisions hereof and of the Indenture, to the Registered Owner named above on the
Maturity Date specified above, or upon earlier redemption as described herein, the Principal Amount
shown above and to pay interest on the unpaid principal amount hereof at the Interest Rate specified
above until payment of the principal or redemption price hereof has been made. Interest on this Bond is
payable on each the first Business Day of each month, commencing ______ 20, 20__ (each such date
being hereinafter referred to as an “Interest Payment Date”) and on any other date on which payment of
principal of this Bond is due. Interest hereon will be computed on the basis of a 360-day year of twelve
30-day months. This Bond is payable in lawful money of the United States of America. Interest on this
Bond will be paid by check mailed on each Interest Payment Date by [TRUSTEE] (together with its
successors and assigns in such capacity, the “Trustee”) to the Registered Owner of this Bond as of the
Record Date at such Owner’s address as it appears on the registration books maintained by or on behalf of
the Agency or at such other address as is furnished to the Trustee in writing by such Registered Owner
prior to such Record Date. “Record Date” means the first day (whether or not a Business Day) of the
calendar month of an Interest Payment Date. At the option of a Registered Owner of Bonds, as
hereinafter defined, interest on this Bond may be transmitted by wire transfer on the Interest Payment
Date to such Registered Owner to the bank account number at a bank located within the United States on
file with the Trustee as of the Record Date. The principal of and premium, if any, on this Bond is payable
at the principal corporate trust office of the Trustee, upon presentation and surrender of this Bond.

This Bond is one of a duly authorized issue of revenue bonds of the Agency, aggregating
$______ in principal amount, designated as “California Housing Finance Agency Multifamily Housing
Revenue Bonds, Subordinate Loan Indenture, 20__ Series __ ([PROJECT] Project) (the “Bonds”). The
Bonds are issued under and pursuant to the laws of the State, particularly the Act, and a Trust Indenture
dated as of [AS OF DATE] (as amended and supplemented from time to time, the "Indenture"), between the Agency and the Trustee.

Reference is hereby made to the Indenture for a description of the rights, duties and obligations of the Agency, the Trustee and the owners of the Bonds, the terms upon which the Bonds are issued, a description of the property and interests pledged for the payment of the Bonds, the relative claims of the Bonds and the Senior Loan (defined herein) against such property and interests, the terms upon which such property and interest are pledged and the terms and conditions upon which the Bonds will be deemed to be paid, at or prior to maturity or redemption of the Bonds, if any, upon the making of provision for the payment thereof in the manner set forth in the Indenture. The terms and provisions contained in the Indenture are hereby incorporated herein by reference and the owner of this Bond, by purchase hereof, assents to all of such terms and provisions. All capitalized, undefined terms used herein will have the meanings ascribed to them in the Indenture. In the event of any inconsistency between the provisions of this Bond and the provisions of the Indenture, the provisions of the Indenture shall control.

The Bonds are being issued for the purpose of providing a portion of the financing for the acquisition, construction, rehabilitation and development of a rental housing development known as [PROJECT] (the "Project"). The proceeds of the Bonds are being used by the Agency to make a loan (the "Loan") to [BORROWER], [Borrower corporate form] (the "Borrower"), pursuant to a Subordinate Loan Agreement dated as of [AS OF DATE] (as amended and supplemented from time to time, the "Loan Agreement") among the Agency, the Trustee and the Borrower. Pursuant to the Loan Agreement, the Borrower is obligated, to the extent it receives sufficient Excess Project Revenues to do so, to make payments sufficient to pay principal of, premium, if any, and interest on the Bonds. The liability of the Borrower under the Loan Agreement is limited as provided therein. Under the Indenture, the Agency has pledged all amounts on deposit in the funds and accounts (except for the Rebate Fund) established with respect to the Bonds to the payment of the Bonds. The Loan is made on a basis that is subordinate to the mortgage loan made by the Agency to the Borrower in the amount of $ for the acquisition, construction, rehabilitation and development of the Project (as further described herein, the "Senior Loan"), which Senior Loan will be funded from proceeds of the Agency's [SENIOR BONDS].

The Loan is secured by a subordinate mortgage lien on and security interest in the Project, granted pursuant to a deed of trust with respect to the Project (the "Mortgage"). The obligations securing this Bond are and shall be subordinate in right of payment to the prior payment in full of the Senior Loan. The Indenture securing this Bond is and shall be subject and subordinate in all respects to the liens, terms, covenants and conditions of the Senior Loan Documents.

The Bonds are subject to optional, extraordinary and mandatory sinking fund redemption at the times, in the amounts, at the redemption prices and in the manner set forth in the Indenture and upon notice as set forth in the Indenture.

The Bonds are issuable in the form of registered Bonds in Authorized Denominations. This Bond will be registered on the books of the Agency to be kept for that purpose by the Trustee, who will act as bond registrar with respect to the Bonds, at its principal corporate trust office. Upon surrender for transfer of this Bond at its principal corporate trust office, the Trustee will enter the name or names and address of the transferee upon the registration books of the Agency and will deliver such Bond to the transferee, or, upon request of the transferee, will deliver a new fully authenticated and registered Bond or Bonds in the name or names of the transferee, such new Bond or Bonds, of authorized denominations and of the same maturity and for the aggregate principal amount which the Registered Owner is entitled to receive. In addition, this Bond, upon surrender hereof at the principal corporate trust office of the Trustee, duly endorsed in blank, may at the option of the registered owner be exchanged for an equal aggregate principal amount of Bonds of authorized denominations and of the same form and tenor of this
All Bonds presented for transfer, exchange, redemption or payment (if so required by the Agency or the Trustee), must be accompanied by a written instrument or instruments of transfer, in form and with guaranty of signature as set forth hereon or as may be satisfactory to the Trustee, duly executed by the Registered Owner or by its duly authorized attorney. The Trustee may require payment from the Owner of a sum sufficient to cover any tax or other governmental fee or charge that may be imposed in relation thereto. Such taxes, fees and charges must be paid before any such new Bond will be delivered.

The Agency and the Trustee are not required (a) to issue or register the transfer of any Bonds during any period beginning on a Record Date with respect thereto and ending at the close of business on the Business Day preceding the next Interest Payment Date or (b) to transfer any Bonds selected, called or being called for redemption in whole or in part.

The Agency and the Trustee may deem and treat the person in whose name this Bond is registered on the registration books of the Agency maintained by the Trustee as the absolute owner hereof for all purposes, whether or not this Bond is overdue; and neither the Agency nor the Trustee will be affected by any notice to the contrary.

The stated maturity of this Bond and the stated dates for the payment of interest may be accelerated upon the occurrence of certain “Events of Default” as defined in the Indenture. The Registered Owner of this Bond has no right to enforce the provisions of the Indenture, or to institute action to enforce the covenants therein, or to take any action with respect to any default under the Indenture, or to institute, appear in or defend any suit or other proceeding with respect thereto, except as provided in the Indenture.

The Bonds are not general obligations of the Agency but are repayable solely from payments of principal and interest on account of the Loan funded thereby, which shall be used for no other purpose than to pay the principal of and interest on the Bonds, except as may be otherwise expressly authorized in the Indenture. EACH AND EVERY COVENANT MADE THEREIN BY THE AGENCY IS PREDICATED UPON THE CONDITION THAT THE AGENCY WILL IN NO EVENT BE LIABLE FOR THE PAYMENT OF THE PRINCIPAL OF, PREMIUM, IF ANY, OR INTEREST ON THE BONDS, OR OTHER FEES AND EXPENSES PROVIDED THEREUNDER OR THE PERFORMANCE OF ANY PLEDGE, SECURITY AGREEMENT, OBLIGATION OR AGREEMENT CREATED BY OR ARISING UNDER THE INDENTURE OR THE BONDS FROM ANY PROPERTY OTHER THAN THE TRUST ESTATE, AND THAT NEITHER THE BONDS NOR ANY SUCH OBLIGATION OR AGREEMENT OF THE AGENCY WILL BE CONSTRUED TO CONSTITUTE AN INDEBTEDNESS OF THE AGENCY WITHIN THE MEANING OF ANY CONSTITUTIONAL OR STATUTORY PROVISION WHATSOEVER, OR AS A PLEDGE OF THE GENERAL CREDIT, FAITH OR ANY TAXING POWER OF THE AGENCY, THE STATE OF CALIFORNIA OR ANY POLITICAL SUBDIVISION THEREOF. THE AGENCY HAS NO TAXING POWER.

Neither the members of the Agency nor any person executing this Bond shall be personally liable on this Bond or be subject to any personal liability or accountability by reason of the issuance of this Bond.

This Bond will not be entitled to any security or benefit under the Indenture, or be valid or become obligatory for any purpose, until the Trustee has authenticated this Bond by the execution of the Certificate of Authentication inscribed hereon.
IN WITNESS WHEREOF, the California Housing Finance Agency has caused this Bond to be executed on its behalf by the facsimile signature of its Executive Director, and its seal to be reproduced hereon and attested by the facsimile signature of the Secretary of its Board of Directors, all as of the Issue Date set forth above.

CALIFORNIA HOUSING FINANCE AGENCY

By: ____________________________________
       Executive Director

[SEAL]

Attest:

_______________________________________
Secretary of the Board of Directors
[FORM OF CERTIFICATE OF AUTHENTICATION]

This Bond is one of the Bonds described in the Indenture referred to herein. Date of Authentication: 

[TRUSTEE], as Trustee

By: 

Agency Representative

OHS West:260384513.3
40024-2 J78/J78

A-5
[FORM OF ASSIGNMENT]

FOR VALUE RECEIVED the undersigned hereby sells, assigns and transfers the within Bond and all rights thereunder, and hereby irrevocably constitutes and appoints unto Attorney to register the transfer of the within Bond on the books kept for registration thereof, with full power of substitution in the premises.

(Please print or typewrite Name and Address, including Zip Code, and Federal Taxpayer Identification or Social Security Number of Assignee)

Dated: __________

Signature guaranteed by: _______________________________________

NOTICE: Signature must be guaranteed by a qualified guarantor institution.

NOTICE: The signature to this Assignment must correspond with the name as it appears on the face of the within Bond in every particular, without alteration or enlargement or any change whatsoever.
EXHIBIT B
FORM OF INVESTOR LETTER

California Housing Finance Agency
Sacramento, California

[TRUSTEE]

Re: $[amount] Multifamily Housing Revenue Bonds
Subordinate Loan Indenture
20__ Series __ ([PROJECT] Project)

Ladies and Gentlemen:

Reference is made to the Trust Indenture, dated as of [AS OF DATE] (as amended to the date hereof, the “Indenture”), by and between the California Housing Finance Agency (the “Agency”) and [TRUSTEE], as trustee thereunder (the “Trustee”). Capitalized terms defined in the Indenture but not defined herein shall have the same meanings given to them in the Indenture unless the context shall clearly otherwise require.

In connection with its purchase of the above-captioned bonds (the “Bonds”) on the date hereof, the undersigned does hereby certify as follows:

(a) The undersigned is a “qualified institutional buyers” as defined in Rule 144A of the Securities Act of 1933, as amended (the “Securities Act”) or an “accredited investors” as defined under Regulation D of the Securities Act.

(b) The undersigned acknowledges that the Bonds have not been and will not be registered under the Securities Act and agrees that it will not knowingly make any future offer, resale, pledge or other transfer of the Bonds or any part thereof (except any offer, resale, pledge or other transfer of the Bonds or any part thereof to an affiliate of the undersigned) except in accordance with the restrictions on transfer set forth in the Indenture.

(c) The undersigned acknowledges that the bond certificates evidencing the Bonds will bear a legend setting forth the applicable restrictions for transfer, including the restriction that the Bonds may only be transferred with the written consent of the Agency.

(d) The undersigned acknowledges that the Bonds are special and limited obligations of the Agency payable solely from the revenues and receipts pledged under the Indenture, and that the Bonds and interest thereon shall never constitute a debt or indebtedness or multiple fiscal year obligation of the Agency within the meaning of any provision or limitation of the Constitution or statutes of the State of California, and shall never constitute or give rise to a pecuniary liability of the Agency.

(e) The undersigned has received information from the [BORROWER], [Borrower corporate form] (the “Developer”), relating to: (i) the sources of repayment of the Bonds, (ii) the Project, (iii) the developer, if different from the Borrower (including financial and operating data) and (iv) such other
material matters relating to the Bonds as the undersigned has deemed relevant. The undersigned has had
the opportunity to ask questions of, and request additional information from, the Borrower regarding the
information provided to it and any other matters that the undersigned considered to be relevant to the
undersigned's decision to purchase the Bonds. The undersigned understands, acknowledges and agrees
that neither the Agency nor any of its commission members, officials, officers, employees, or agents have
any responsibility for the accuracy or completeness of the information supplied to it or any other
information that the undersigned has received or relied upon in making its decision to invest in the Bonds.
The undersigned has received copies of the bond and loan documents relating to the Bonds and has
reviewed them and understands their terms.

(f) The undersigned has reviewed and has made its decision to invest in the Bonds based
solely on its review of the information provided by the Borrower. The undersigned understands and
acknowledges that the Bonds are a speculative investment; that there is a high degree of risk in investing
in the Bonds; and that the undersigned is capable of suffering a loss of the entirety of its investment,
which is represented by the Bonds. The undersigned can bear the economic risk associated with a
purchase of high risk securities such as the Bonds and has such knowledge and experience in business and
financial matters, including the analysis of a participation in the purchase of similar investments, so as to
be capable of evaluating the merits and risks of an investment in the Bonds on the basis of the information
and review described herein.

(g) The undersigned is duly and legally authorized to purchase obligations such as the Bonds.

(h) The undersigned acknowledges that there may be no secondary market for the Bonds and
that no credit rating has been sought or obtained with respect to the Bonds.

This letter and the statements contained herein are made for your benefit.

By ___________________________
EXHIBIT C

MANDATORY SINKING FUND SCHEDULE
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MEMORANDUM

To: Board of Directors

From: Tom Hughes, General Counsel

Subject: Pending Audit Committee Issues

At the request of Board Chair John Courson and Audit Committee Chair Jack Shine, staff is providing the Board with a list of the issues related to the Manatt report that have been pending before the Audit Committee. The first seven items are taken verbatim from an email from Audit Committee Chair Jack Shine to me dated September 18, 2007. Item 8 is an issue raised in the Manatt report but not addressed in the September 18, 2007 email from Mr. Shine. Item 9 was raised by John Morris.

The issues considered by the Committee were:

1. Should the board of directors need to approve any major contractual agreement for the use of independent outside advisors to conduct salary surveys or other items of concern except for the contracts dealing with the daily finances that are on a regular basis.

2. Should we keep the compensation committee, (whether or not we change members) so that we can have a viable committee to whom we can make recommendations for their consideration and presentation to the board.

3. Should the compensation committee be given the task of conducting an independent review prior to presentation to the board of directors for approval -- any agreement relating to compensation to key exempt management and any scope of work documents.

4. Should the compensation committee recommend to the board of directors any work or instructions to be given to survey contractors prior to the commencement of a salary survey.

5. Should key exempt management who are beneficiaries of a compensation determination, be advised to avoid any direct involvement with any entity hired by the agency to conduct salary surveys, --- and should a policy regarding independent third parties be created so that necessary tasks be done by this independent party would be reported only to the compensation committee.

6. Should the authority of the executive director to sign contracts on behalf of the agency be delegated exclusively to the chair of the compensation committee or other designees --- and should any member tasked with overseeing this responsibility to establish key exempt
management compensation - be allowed to be a person or someone who has business dealings with Cal HFA.

7. Should all members of the board be required to provide a statement annually setting forth the level of business they are involved with directly or indirectly, (if applicable) with the agency so that all board members are aware of this situation.”

8. Should the Agency adopt a statement of principles that it treats Board members who do business with the Agency the same as any other person; and

9. Should a Board member with business dealings with the Agency be permitted to vote on compensation issues?

At the November 15, 2007 meeting of the Committee, the members considered each of these issues and formed some preliminary consensus. The Committee decided it would review the minutes at its next meeting, and would formalize those recommendations for presentation to the Board. A copy of the minutes is attached.
STATE OF CALIFORNIA
CALIFORNIA HOUSING FINANCE AGENCY

AUDIT COMMITTEE
PUBLIC MEETING

Burbank Airport Marriott Hotel & Convention Center
2500 Hollywood Way
Burbank, California

Thursday, November 15, 2007
9:13 a.m. to 10:33 a.m.

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

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Audit Committee Meeting - November 15, 2007

APPEARANCES

Committee Members Present:

JACK SHINE, Chairperson
Chairman
American Beauty Development Co.

PETER N. CAREY
President/CEO
Self-Help Enterprises

CAROL GALANTE
President
BRIDGE Housing Corporation

JOHN G. MORRIS
President
John Morris, Inc.

CalHFA Staff Present:

SUSAN GOODISON
AccountingAdmin III

THOMAS C. HUGHES
General Counsel

DENNIS MEIDINGER
Comptroller

JOJO OJIMA
Office of the General Counsel

THERESA A. PARKER
Executive Director

Speakers from the Public:

TIM STENVICK
Deloitte
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--o0o--
BE IT REMEMBERED that on Thursday, November 15, 2007, commencing at the hour of 9:13 a.m., at the Burbank Airport Marriott Hotel and Convention Center, Academy One Conference Room, 2500 Hollywood Way, Burbank, California, before me, YVONNE K. FENNER, CSR #10909, RPR, the following proceedings were held:

--o0o--

CHAIRMAN SHINE: It is 13 minutes after 9:00. I'm calling the meeting to order of the Audit Committee of the Board of Directors of California Housing Finance Agency. First we have a roll call.

--o0o--

Item 1. Roll Call

MS. OJIMA: Thank you.

Mr. Carey.

MR. CAREY: Here.

MS. OJIMA: Ms. Galante.

MS. GALANTE: Here.

MS. OJIMA: Mr. Morris.

MR. MORRIS: Here.

MS. OJIMA: Mr. Shine.

CHAIRMAN SHINE: Here.

MS. OJIMA: All members are present.

CHAIRMAN SHINE: Thank you.

--o0o--
Item 2. Chairman comments

CHAIRMAN SHINE: Beside the discussion of some recommendations that we've received from counsel, which we're going to discuss this -- again, on our agenda this morning are the issues of the recommendations made by counsel in connection with the investigation that we held, which we're going to discuss in a moment, and then the Housing and Emergency Shelter Trust Fund and the financials. Let's follow the agenda exactly.

--o0o--

Item 3. Discussion and possible recommendation to the Board of Directors regarding dissolution of the Compensation Committee

CHAIRMAN SHINE: And I'd like to open the discussion to all of you members of this committee as to some of the issues here which, first of one -- the first of which has to do with should there be a compensation committee or should the Board fill that role. We -- as you recall, we talked about this before and decided to postpone the discussion of this item until after we had discussed the recommendations of Manat Phelps in our -- in the letter we got. And maybe, unless you object, we should put that to the side for the moment and get through those items, which might lead us to the conclusion as to whether we want to recommend or not.
that there be a Compensation Committee specially on its own.

---

Item 4. Discussion and possible recommendation to the Board of Directors regarding proposed changes to the compensation process made by outside counsel and Board members

CHAIRMAN SHINE: So if that's okay, the first issue we want to talk about is should the Board of Directors need to approve any major contractual agreement for the use of independent outside advisers to conduct salary surveys or other items of concern with the exception of contracts dealing with daily finances and daily operations.

I'm open for comments. Peter, do you want to start, and we'll just come down the aisle here?

MR. CAREY: Well, I think I said this at the last meeting, that I would not be opposed to going back and reviewing specifically the guidelines that we've established for signing contracts. I do not want to see us do anything that hampers the operation of the Agency.

At the same time, I think whether it's policy or simply practicality, there are certain contracts where it's probably best to have buy-in from the Board, which is going to rely on that information. So whether it's
policy or simply practicality, there are certainly some selections that are worthwhile bringing to the Board, I think.

I can't sit here today and say, yes, we ought to change it in this way or that way because I really think we ought to review what the existing status is.

CHAIRMAN SHINE: So what action item could we take then to move that along, in your opinion?

MR. CAREY: I think we could specifically review the current policy.

CHAIRMAN SHINE: Is that policy in a manual or in a book of documents somewhere that we can see? I don't know how the policy is set forth or how it's kept or how it's memorialized.

MR. CAREY: We approved it, but I don't recall it word for word, to be honest.

CHAIRMAN SHINE: Tom? Mr. Hughes, how could we accomplish that task of taking a look at the policies that we have to see which, if any, of them we think need to be addressed again to deal with this issue?

MR. HUGHES: The Agency has a regulation. The Board approved a regulation, I believe, back in 2005, which defines major contractual obligations because that phrase essentially comes out of the CalHFA statutes, and that governs all contracts. There is not a specific
policy for contracts dealing with people that conduct salary surveys. If you want to recommend an internal policy, that would be your prerogative.

CHAIRMAN SHINE: The issue that we're discussing now doesn't only have to do with the salary thing that we dealt with before. It has to do with any major contractual agreements that we have, which, I guess, would extend outside of the normal day-to-day running of the business of the Agency.

MR. HUGHES: Well, again, that is set by statute, that CalHFA -- the Health and Safety Code says the Board of Directors approves major contractual obligations. And then the Agency, the Board, has enacted regulation which defines "major contractual obligations."

CHAIRMAN SHINE: Is that definition somewhere in writing?

MR. HUGHES: It's in the regulations that the Board approved in 2005. It's published in the California Code of Administrative Regulations. That was -- unless I'm missing what you're getting at, that is the -- that is what controls the -- what contracts go to the Board.

CHAIRMAN SHINE: Mr. Carey, am I incorrect or am I correct in saying what you would like to do is see
something that you could read that would bring it to focus.

MR. CAREY: You're right. I recognize I could look that up, I just don't think --

MR. HUGHES: I may have a copy of it.

CHAIRMAN SHINE: Without reading it here, if we could just get the written document that contains the language that we're discussing here and have a chance to look at it.

MR. HUGHES: I have a copy there. We can go make photocopies of it if you want to read it here.

MS. GALANTE: Can I just say something?

CHAIRMAN SHINE: Ms. Galante.

MS. GALANTE: We have a lot of items to go through on this list, and I don't think that I would be prepared today to have a whole conversation on reviewing all of how we do our contracting. If we want to have a separate conversation on that to review it, you know, I'm open to it.

I think what I was going to say on this first point is the law firm was specifically recommending that perhaps the salary survey consultant for compensation, whether they're reporting to the full Board or the Compensation Committee, it was their recommendation that that contract in particular probably ought to be done by
a Compensation Committee or by the Board as opposed to just staff. And I would say that, you know, I think agree with that.

So that's a subcomponent of the overall -- you know, looking at our overall contracting policy. I'm not opposed to looking at our overall contracting policy, but I feel for that one specific recommendation I would be willing to recommend to the Board that we make that particular change.

CHAIRMAN SHINE: All right. We'll do that.

Mr. Morris.

MR. MORRIS: I think if we go back -- and, you know, clearly that this, what we're discussing, really falls under the category of the general contracting that is provided in the statute, and that is something that, you know, clearly -- I think the easiest way to do it is to say kind of what is the big picture of what we're looking for, and then let CalHFA go back and say, okay, you know, if, for example, you want to state that, you know -- you know, a contract with an outside consultant in excess of X amount of dollars, you know, must be approved by the Board, I mean these are the kinds of things that can go back and you can deal with the general counsel on.

I think that the issue today as it relates to
what we're talking about, the Compensation Committee and what contracts need to be approved, it gets back to the point that, you know, we had a problem before where a firm was hired without Board approval, a salary survey was done without Board's input prior to -- or without the Compensation Committee's input prior to the survey being conducted, and that's what kind of started the problem.

What I would recommend -- we don't have any salary -- we're not doing any salary surveys in the near future; is that correct, Terri? I mean within the next few months? We're not -- we're not -- in the next few months, we're not adjusting any salaries, doing any salary surveys?

MS. PARKER: I have no intention to do so.

MR. MORRIS: Okay. So if that's the case, then I think what we should do at our next Audit Committee meeting is -- or prior to that, review the language. But then maybe today what we can do is say, you know, what types of things, in a kind of a big picture way, do we think should be approved by the Board as it relates to contracts. So, you know -- and I think that -- and I don't know what that list would be. We'd have to review it.

But clearly hiring a consulting firm to conduct
a -- in this case a salary survey where we're making
major adjustments to various positions should clearly be
something that the Board should be aware of and should
approve. And there are other types of contracts. To be
honest with you, I'd like to look at maybe some other
agencies and the types of contracts that the Board gets
approval of. I have been on a couple different state
boards and agencies, and they have been different,
but -- they've been quite a bit different than CalHFA.

So it's kind of a long way of saying that, yes,
I do believe that a contract such as the one that we had
with Watts and Wyatt, should have gone to the Board for
approval, and I do believe the Compensation Committee
should have had more input into the process.

CHAIRMAN SHINE: Thank you, Mr. Morris.

Having said that, the action that needs to be
taken, I think, would be for you, if you'd be so kind to
send us or you can leave it with us before we leave
today a copy of the language that talks about this issue
in general. And then if any of us want to go to other
agencies and ask the questions or find out from people
we know who are serving on other boards, we can do that
and reconvene either at our next regular scheduled
meeting or if we could put it together at an in-between
interim meeting to discuss and focus on the issue of
contractual agreements.

Yes?

MR. CAREY: It sounds as if we would be prepared to say, yes, we believe that outside compensation review contracts should come to the Board.

CHAIRMAN SHINE: I think on that single issue, I don't hear anybody saying otherwise, but I think this, even though this was initiated for one purpose, has increased the size of the umbrella over the whole issue in general of contracting and how we handle it and what staff can do on a daily basis, which they're doing, and what we think ought to go to the Board and what we're going to recommend.

So having said that, would you do that, Tom?

MR. HUGHES: Yes. I'll send each of the members of the committee both the Health and Safety Code section, and also it's the section at issue is Title 25 of the California Code of Regulations section 13302.

As a heads-up procedurally, though, there are two ways that the Committee and the Board can handle this, and you can do one or both of these. To the extent that you want to amend section 13302, we need to draft regulation. It needs to be approved by the full Board. It has to go to the Office of Administrative Law. It has to go through a process. It's probably at
least a six-month process or more. And then it has to be codified.

The other thing that you can do -- and you can do both of these if you want -- is to simply request that the staff bring you those contracts, maybe as an interim measure, I don't know. But the actual changing of the rule is a rulemaking process that needs to go through.

CHAIRMAN SHINE: And I don't think that the thrust of the comments that were made here just now was that we want to change all the rules, rather we want to see the document from which it started and review the policy that we've been following to see if we want to change it at all, and if so how.

MR. HUGHES: Right. I will see to that.

CHAIRMAN SHINE: The idea is to keep this as simple as possible and still be able to accomplish our objective.

MR. HUGHES: Right. I simply want to point out that if you wanted to change this actual rule, there's a process that needs to be followed.

CHAIRMAN SHINE: It wasn't even in my mind just yet, but thank you very much.

Okay. I'm going skip down here. There's a question here should the Compensation Committee be given
the task of conducting an independent review prior to presentation to the Board of Directors of any agreement relating to the compensation of key management and so on and so forth.

Who would like to pick up on that? Mr. Morris.

MR. MORRIS: Well, I don't think --

MS. GALANTE: Is this not -- a point of information. I think this is referring to essentially information that would be coming from this kind of salary survey from an independent entity. And the question -- I mean the way I'm reading the question is should we be as a -- or should the Compensation Committee be reviewing that information prior to it going to the full Board. Is that --

CHAIRMAN SHINE: That's essentially the question. And understand, in whatever form the Compensation Committee ends up, whether it stays as is or it gets changed, some group is going to be designated as the group that deals with this issue of compensation. And the question is should they be given the task of doing an independent review.

MR. MORRIS: Well --

CHAIRMAN SHINE: Who wants to take that?

MS. GALANTE: I guess my personal opinion is if we're doing an independent salary survey and that
independent salary was contracted for by the Compensation Committee or by the Board, that I wouldn't want the Compensation Committee to have to feel obligated to do something beyond that, if that's what this is suggesting. It's not clear to me that's what it's suggesting, but.

CHAIRMAN SHINE: I think it's suggesting that before you -- before an agreement is submitted for our approval to hire a firm to do that, that the Compensation Committee should do an independent review or -- whether that's the bidding process or an independent investigation into the background of the company or whatever, what it's doing is giving the Compensation Committee a mandate to review and discuss --

MS. GALANTE: The scope of the actual salary --

CHAIRMAN SHINE: -- and investigate before they actually take a contract proposal and present it to the Board for approval.

Mr. Morris.

MR. MORRIS: What I think that -- if I understand the question, what we're really talking about is do we want to give some entity, I don't know whether it's the Compensation Committee or some members of the Board, the ability to -- I wouldn't call it an
independent review because you're not going to sit there -- but independently interview, maybe, several different firms and then along with staff make a recommendation as it relates to which consulting firm you'd want to use. Is that what you're talking about?

CHAIRMAN SHINE: This is Steve Nissen's recommendation from Manat Phelps.

MR. MORRIS: Right. I'm just trying to clarify it. Is that the way you'd understand it?

CHAIRMAN SHINE: Yeah. It says it's an independent review --

MR. MORRIS: But I don't understand. My question is what is the definition of independent review, I mean to what extent. So what I'm saying is I think -- I think what they are saying here, and I think -- I know what I'm trying to say is in the future if we're going to pick someone like a Watts and Wyatt, that whatever -- I don't know whether it's the Compensation Committee or whether it's the Board, but that staff would go to whatever this group is and say, okay, here are several firms that we are contemplating using and here's the firm we recommend and here's why, and if you want to talk to these other people and have them make their presentation, fine. So in other words, it just isn't thrown on the Board saying, okay, we've
picked Watts and Wyatt and here they are.

CHAIRMAN SHINE: It's called due diligence.

MR. MORRIS: Right.

MR. CAREY: These questions, if I'm not mistaken, were paraphrasing our own questions from a committee meeting sometime back; right?

MR. HUGHES: Each one of these numbered comments is verbatim Mr. Shine's summary of the issues.

MR. CAREY: Right. Okay. To help us recall.

To me, the scope of it is that the Compensation Committee or the Board, however functions, wants to be involved in approving the contract, reviewing the selection of the contractor and establishing the scope of the work. Isn't that sort of the simple terms, rather than getting constrained by these particular statements here?

CHAIRMAN SHINE: And I understand, in putting this together, the genesis of it came from the recommendations contained in the report of counsel that we hired, and it's almost word for word with slight changes, thank you. And what he's saying is there should be a committee. They should exercise due diligence in preparing this thing before they present it to somebody and ask for their permission to sign the contract. Does that make it clearer?
Are we -- how do we feel about that? Yes?
Okay. So we're saying on that recommendation, that is
the -- that's going to be the recommendation of this
committee to the Board as it becomes a matter of policy.
Okay. The next one falls in the same category.
I don't think we need to discuss it. It's part of the
due diligence.
There's another issue here that talks about key
exempt management and this compensation issue. And let
me just read it for the record. It says should key
exempt management who are beneficiaries of a
compensation determination be advised to avoid any
direct involvement with any entity hired by the Agency
to conduct salary surveys and should a policy regarding
independent third parties be created so that necessary
tasks be done by this independent party and they would
be reported only to the Compensation Committee. It's
just a matter of crystallizing how it's done. That is
the issue that was raised, and the question before us is
do we agree? If we do, should we also make that a
recommendation?

MS. GALANTE: I'll take a stab at this. My
feeling is that this would be very difficult to
implement with respect to the executive director and
senior management personnel.
I mean I, as a CEO of a company, if there's going to be a salary survey done, for example, on -- for my senior management team, I'm going to want to understand and have some input based on my knowledge of where, you know, what appropriate kinds of comparables might be. And so I think it could be impractical to separate that.

You know, with respect to, for example, the executive director's own salary, I guess I'm a little more ambivalent about that one. And again, I will say in our own company when we're doing compensation surveys, I have a compensation committee, but I'm involved as the CEO in the structuring of the compensation conversation with the compensation committee. And so I -- you know, just giving you my personal experience, I'm a little uncomfortable as to how you could totally exclude the executive director of the Agency from these -- from the compensation process.

Now, you know, there are some nuances there that I think, you know, get a little more complicated.

CHAIRMAN SHINE: And this is very specific because it says will be reported only to the Compensation Committee. What I hear you saying is --

MS. GALANTE: I have a little problem with that.

CHAIRMAN SHINE: Right. I hear you saying,
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well, yes, it should be taken up with Compensation Committee, but the executive director or whoever should be also at the table, if you will, to participate in it because obviously that person has an interest in it.

So we're not going to recommend solely that it be given directly to the Compensation Committee without any staff input at all. Is that correct?

MR. MORRIS: I mean, I don't see this really as an issue as long as whatever this, whether it's the Compensation Committee or the Board is involved in the beginning of the process. It will take care of itself, because obviously they're going to be involved in the process of selecting the firm and the process in which a survey would be conducted, which obviously would include these types of activities. So I don't see it as an issue as long as we approve these, the previous.

CHAIRMAN SHINE: So are you saying that as long as we have a compensation committee or entity of some kind --

MR. MORRIS: Some kind, yeah. It could be the Board, I mean maybe just the Board, but as long as they're involved in the process, I don't see that -- I think that's kind of micromanaging the process. I don't have a problem with the executive director --

CHAIRMAN SHINE: We did this in the last survey.
There was a third party, if I recall correctly, that was brought in to move things along. It was someone who worked for the Agency some time ago, if I recall.

MR. MORRIS: Right. Where we got into the problem before was because that was done prior to the first Compensation Committee.

CHAIRMAN SHINE: So the first time around, there were a lot of things happening which created --

MR. MORRIS: No, I understand. So I don't see it as an issue.

CHAIRMAN SHINE: So what you're saying is that if something is brought up, it should be brought up to the compensation entity which should or, you could say, may include the executive director as appropriate.

MR. MORRIS: Right.

MR. CAREY: I think I sort of hear that we're simply saying that No. 5 is not an issue, that we simply don't need to deal with it.

CHAIRMAN SHINE: All right, then. There we go. The next issue has to do with the question should the authority of the executive director to sign contracts on behalf of the Agency be delegated exclusively to the --

MS. GALANTE: Chair.

CHAIRMAN SHINE: I got it -- to the chair of the
Compensation Committee or other designees and should any member tasked with overseeing this responsibility to establish key exempt management compensation be allowed to be a person or someone who has business dealings with CalHFA?

So there's two issues here. One is should anybody involved in the process -- excuse me, should anybody who has business dealings with CalHFA be also involved in that process. Let's take that one first.

Mr. Morris.

MR. MORRIS: I think what -- there are a couple things. First of all, I think that any Board member that has any business dealings at all with CalHFA should disclose that with the general counsel and discuss it with the general counsel and make a determination as to whether or not they may have the conflict.

And they also have to be careful that it's not even if they technically have a conflict, it may be perceived that they have a conflict, and that could also create problems. And I think it also should be disclosed not only to the general counsel, but also to the other Board members. I'm not saying that just because somebody has business dealings with CalHFA that they shouldn't be involved in the process, but, No. 1, I'd like to know about it and, No. 2, I'd like to know
if there is a conflict in the technical nature or in the spirit of the act.

CHAIRMAN SHINE: That's item 7 on the agenda, which we haven't come to yet. But let's go into that. And does anybody disagree that -- how do we feel about the requirement and need or desire, as the case may be, to disclose to counsel and to the Board the business relationship Board members have with the Agency?

MS. GALANTE: Well, my feeling is that we have that obligation now. We've always had it. The way it, I think, has been generally interpreted -- and Mr. Hughes can correct me if I'm wrong -- is talking about, you know, a specific action that maybe come before the Board that you have a specific conflict on. CalHFA is making a loan to my company, you know, it's a specific conflict that, you know, or it may be a conflict that needs to be disclosed.

I think when I remember reading the Manat Phelps report, I think I was concerned that their recommendation was that simply by the fact that -- for example, my company does overall business with CalHFA, that -- and Peter's does -- and, for example, that would be excluded from -- or the recommendation appeared to me to be to exclude those Board members from compensation committee type responsibilities, whether
that's with the full Board or on the Compensation Committee.

And I, you know, am not an expert in conflict of interest law by any stretch, but I think that, you know, that is not a direct conflict and it's so key a part of being a Board member, that I would have a pretty big problem with that.

CHAIRMAN SHINE: Someone just said, though, that it's not only disclosing to Mr. Hughes the nature of whatever business dealings might be, but whether there was as a result of that a conflict of interest. It may be if you are involved and have one take-out loan to a homebuyer, then you're doing business with CalHFA, but that doesn't mean as a Board member you necessarily have a conflict of interest in deciding a compensation issue or some other relevant issue.

And I think it would be up to counsel to advise us, as many, as I've done it, and others have done it, explain the situation and let him tell you yes or no. What do you think, what is the opinion as to the real or maybe even perceived conflict. So, Carol, I think that your comment points out that, yes, a lot of people have dealings, but my point is that doesn't necessarily mean that it's a conflict.

Peter.
MR. CAREY: A couple thoughts. First of all, in terms of conflict of interest, and the FPPC 700 forms are public information; right?

CHAIRMAN SHINE: Correct.

MR. CAREY: So certainly they could be shared. I share John's perspective that daylight is best on all issues of interest.

I don't -- I don't see us going beyond state law and trying to define what is a conflict of interest because that's a matter of law and complex law. But perhaps we should share the 700s among the Board. That would be a starting point because those are the forms we all fill out and they are a starting point for information. Beyond that, the spirit is important.

But CalHFA is different than many other boards. We don't directly award, aside from approving recommended multifamily loans, and we are advised and continue to be scrupulous in disclosing potential conflicts, but this Board is meant to be an involved Board. It's meant to be a Board that has direct experience in the work of the Agency, and I think the Agency benefits from that. And the Agency has a significant substantial professional staff that manages the Agency on a day-to-day basis, which keeps us out of those day-to-day situations where there are greatest
potential for appearances of conflict.

So I agree with the idea of sort of a principle of openness, but I don't see any way that we could exclude anyone with business dealings from participation in decisions because that would be -- that would hamstring the Board. It would lead to a Board where no one had any direct experience in the business of the organization.

CHAIRMAN SHINE: All right. Item 6 and 7 really are three issues, one of which I think we've all agreed, yes, there should be disclosure, the second of which has to do with, having said that, should anybody with business dealings at all be allowed to be a person dealing in these issues. And I -- my perception is that we're saying, well, that's a matter for counsel to tell us as long we don't have a conflict of interest and we disclose it, and the Board is made aware of it annually or whatever we decide, then that ought not to be something that we're going to worry about.

And third is in that -- actually in that comment, is the question of the executive director's authority to sign contracts and whether it should be delegated exclusively to the chair of the Compensation Committee. And I'm sure this focuses on contracts dealing with compensation. So the question is, to put
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it in different words, should a contract with someone in
the area of dealing with compensation be the kind of
thing that the chair of the Compensation Committee,
rather than the executive director, finally signs.

Mr. Morris.

MR. MORRIS: I mean, I don't see that as an
issue either. I mean I think that it's who executes the
contract. I mean the executive director can execute the
contract as long as it's been approved by whatever this
committee, whatever this body is that evolves from this
process.

CHAIRMAN SHINE: So the answer is, in your
opinion, no?

MR. MORRIS: No. The executive director can
sign.

MS. GALANTE: I agree with that.

MR. CAREY: I agree.

CHAIRMAN SHINE: All right. So what we're not
going to recommend is the part that talks about the
signing, the executive director's ability to sign
contracts for compensations so long as they're subject
to and have been approved by, I guess, the Compensation
Committee and the Board.

MS. GALANTE: Or the Board, I think, depending
on where -- where the role ends up.
CHAIRMAN SHINE: Okay. All right. Well, good.

There's another issue here asking should we adopt a statement of principles saying that we treat Board members who do business with the Agency the same as any other person. Do we need to do that? Is that -- isn't that kind of a nonissue, you think, if we're going to do all these other things?

MR. CAREY: It should be assumed.

CHAIRMAN SHINE: Well, the question is do we want to recommend that a policy be made, or do we want to just follow through on all these other items and think that that will keep things transparent sufficiently?

MS. GALANTE: I'd prefer the latter, which is to not -- let's not make work in terms of creating policies and statements if we don't need to, and I think given everything else we're talking about, we don't need to do this. I don't think we need to do this, creating a statement of principles that Board members who do business with the Agency be treated the same as other people. I think everything else we're talking about makes that implicit and explicit in other ways.

CHAIRMAN SHINE: Okay. So then to go back for a moment to item 4, the question there is should the Compensation Committee recommend to the Board of
Directors any work or instructions to be given contractors, in other words, should the criteria of the Compensation Committee, unless it actually ends up being the Board anyway, when they create the criteria for instructions, should they go to the Board first to get approval and then let the contract, or not? Anybody want to take that on?

MR. CAREY: I'll just say that approving the scope of work would be appropriate. I think "any instructions" would be a little bit narrow.

MS. GALANTE: Having the Board approve the scope of work?

MR. MORRIS: Once, again, it depends if we say the Board or the Compensation Committee, but I think that having the Compensation Committee or whatever it is approve the scope of work of a contractor is -- it should be done. That's part of their responsibility.

Now, the question is, I mean, as far as I'm concerned, absolutely, that would be not only involved in the selection, but reviewing the scope of work and approving the scope of work. What I hate to do is to get a situation like we had before where you have a contractor go ahead and basically complete most of the job and then find out -- then the Board find out what the scope of work was and go, gee, we would have done
that differently.

CHAIRMAN SHINE: We all agree that that wasn't right, and that's why we're here today.

MR. MORRIS: That's why we're here, and that's my point. So that, yes, I would recommend that the Board, the Compensation Committee, or whatever it is that is formed to review this in the future, that they be involved in the selection of the consulting firm, No. 1, and, No. 2, that there is an approval of the scope of work before they start.

CHAIRMAN SHINE: What it now says is should the Compensation Committee recommend to the Board the scope of work to be given to contractor before the commencement of a salary survey? What you're saying is the Compensation Committee or the Board should review the scope of work before that contract is -- before we go out for request for proposals.

MR. MORRIS: No. Before -- before they -- before they start the work. In other words, we picked Watts and Wyatt. Watts and Wyatt was basically selected.

CHAIRMAN SHINE: Well, but when you select somebody and you tell them you want them to do a certain work, you got to tell them what the work is they're going to do so they'll know how to bid the contract.
MR. MORRIS: But obviously that's going to be part of the process of what we want them to do. But the actual -- actual task of the scope of work is more narrowly defined in the contract, and that is something that obviously we're going to want --

CHAIRMAN SHINE: Okay. I'm not --

MR. MORRIS: I think -- I don't think -- I think as long as the Board -- as long as the Compensation Committee or the Board is involved in the selection of the contractor, okay, and they have approval of the scope of work, you don't have a problem.

MR. CAREY: Isn't the goal, simply stated, so that when the results come to the Compensation Committee or the Board, that the process already has integrity and confidence for the Board so that the Board can deal with the information presented and not process at that point. It's easier to deal with the process up front.

CHAIRMAN SHINE: So am I clear that in the process of selection, the determination of the scope of the work for which we're looking for people to make proposals to do work for us should be approved by the Compensation Committee or the Board, as the case may be.

We'll go back to the minutes and pick all this up and reformat it in a way that we can all agree is what we said here. But I think I understand what you're
saying, and that's fine.

Okay. That takes care of No. 4.

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Item 3. Discussion and possible recommendation to the
Board of Directors regarding dissolution of the
Compensation Committee

CHAIRMAN SHINE: Now, let's go back up to the
issue of the Compensation Committee itself. Given
everything that we've talked about, do we want to
recommend that a Compensation Committee continue to
operate as a separate committee or do we want to close
the Compensation Committee as a committee and give to
the Board that task of being involved in the
compensation with no Compensation Committee?

MR. MORRIS: Well, I mean, I personally don't
think -- I mean, I was the one that originally thought
we needed to have a Compensation Committee for a number
of reasons, because I thought we were going to be
involved in the selection and the process and things of
that nature. But I think I have a different feeling
now.

My feeling is that given what's occurred and
given the size of our Board, that there really isn't a
need for it. I think that all the Board members should
be involved in the process and that this -- you know,
this -- as these issues come up in the future, it should be something that's on the agenda, and it's going to be something that's going to be addressed to the full Board. There may be Board members that may be more interested in the issue than others, so be it. And -- but I don't think -- and I think that once we get to the phase in another couple years or next year or whatever where you're actually setting salaries, you go into closed, you meet with the Board, and you do it.

I mean, we had three people do it this year. I mean, how many Board members do we typically get at a meeting anyway? Seven? So I think it doesn't -- I don't think you need a separate meeting for that in the future. I think I'd just put it -- I don't think there's a need for it now as long as we know for sure that the types of things that we've discussed will be presented to the Board.

CHAIRMAN SHINE: Mr. Carey.

MR. CAREY: Just looking from a practical point of view, would you see the Board interviewing potential survey consultants or simply seeing -- I'm concerned about the practicality of quorums. And I don't disagree about the whole Board having buy-in. I'm just concerned about the practicality of the process of getting to a recommendation to the Board and whether you think there
would be the ability for us to have a quorum to get through all those steps on the way.

MR. MORRIS: Well, you know, the problem is we have a fair amount of Board meetings but they're usually not very long. If you do add this, you're going to add once a year or every 18 months, you know, a significant amount of time. I mean, I would say we met -- the Compensation Committee met, I mean John's got the notes. I mean, I don't know, we probably met half a dozen times, maybe for a couple hours apiece, and we probably spent ten, 12 hours. So it would be on an annual basis, probably an extra, you know, probably ten hours of Board time. I mean you're not going to do a survey every year, but you're probably talking about adding to each -- you know, towards the -- whenever that is done, you know, probably a half a day.

MS. GALANTE: If I could just state my preference, I do agree in reading the Phelps analysis that this was the first time through for having done this. I think there were some bumps along the way. I think there are some improvements to the process that certainly could be made. And I think if we got our arms around this, the Compensation Committee being involved in the process more deeply, being involved in, you know, hiring the compensation consultant and looking at, you
know, what information -- what the scope is, I -- my instinct is that a smaller committee doing that work would be ultimately more beneficial than trying to have the full Board involved in that whole process.

And I -- you know, just as a matter if we were sitting here discussing these kind of issues with seven people or more, I don't know how many our full Board is, but I just think it would get very cumbersome. And so my preference, I think, really would be, if we make these other adjustments, to keep the concept of the Compensation Committee for, I think, some of the practicality reasons that I hear Peter suggesting. So it's just my instinct that that would flow better, and that we would, you know, solve a lot of problems that we had this first time around.

MR. CAREY: We would be, I think, virtually locked into the six meetings a year. I think about the difficulty of trying to schedule just the four of us, that if perhaps -- if the end result is a Compensation Committee does the work but recommends to the Board and the Board approves, I think maybe that meets my need for full openness while allowing the work to get done.

CHAIRMAN SHINE: So am I then to understand that the consensus here is that some kind of a committee like or maybe slightly different from what we have now, but
nonetheless a Compensation Committee be kept and
utilized for all the preliminary work until it has its
recommendations to the Board for the Board to approve
the scope of work and other important items to be
contained in a proposal to go out for people to bid on
contracts that we will let for the purpose of
compensation or other major items --

MR. MORRIS: I would --

CHAIRMAN SHINE: -- relating to compensation.

MR. MORRIS: I would agree with it with just one
condition that when you do create the -- keep the
Compensation Committee, that existing -- that Board
members that want to serve on the committee be permitted
to do so. You might have three people that want to do
it, but there might be someone that wants to do it, and
there have been instances. That's not my point.

CHAIRMAN SHINE: I understand. I think as a
matter of courtesy from Board member to Board member
that probably is going to happen anyway, but we can
include that as our suggestion.

If that is the consensus, which I said in a not
very brief way just now, then, again, we'll refer to the
minutes to come up with the proper language and maybe
approve this at our next Board meeting. Or in the
alternative, we can take a few minutes, Mr. Hughes, and
go through this, and we'll present it to the Board meeting which is going to occur next. What do you think?

MR. HUGHES: I think it's up to the committee how they -- you need to bring it to the full Board, clearly. The only question is whether we can articulate the total substance of this meeting well enough for the Board meeting. We could try or we could get the minutes and you can do it the next time. I think it's up to you.

CHAIRMAN SHINE: Sounds to me like what I'm hearing, reading between the lines, is we better get it done and present it in a proper way to the Board, which means we should probably do it next time and have time in between, as you suggested, to really properly memorialize in writing these various action items that we're going to recommend. Did I get that right?

MR. HUGHES: I think it's easier when you review the minutes, but certainly we could sit here and try and do that. I think, again, that's up to you.

CHAIRMAN SHINE: Then I'm going to suggest that we do this after we've had a chance to see the minutes, which we will ask be expedited so that we can get them as early as possible and agree on a look at the language to be used and will present it at the next Board meeting.
as our series of recommendations. Does that capture the
spirit of what we're talking about?

MR. MORRIS: Nothing is going to happen between
now and the next Board meeting anyway, so we have plenty
of time. There's no urgency. So I think that's a good
idea.

CHAIRMAN SHINE: Okay. Then that's what we'll
do. We'll come back to the Board with those
recommendations at our next meeting.

Are there any other comments from the committee?

Anyone else?

Our esteemed chairman.

MR. COURSON: Mr. Chairman, if I can -- I would
never allow this to happen at a Board meeting, but I'm
going to ask you while we are on this topic -- you're
going to move on to another agenda item? -- I have one
thing that Terri and I would like to have you consider
as a recommendation as part of this compensation
process, if I may.

CHAIRMAN SHINE: Well, of course.

MR. COURSON: Terri has some information for
you. Let me just set the stage for this and the need
for talking about this process, a change in the process.

Everybody knows in January that the Board, as
you well know, went through this process and ultimately
did approve a change in the salary structure for key personnel at CalHFA. And what happened shortly after that Board meeting and frankly unbeknownst to myself or the executive director until -- since our last Board meeting of CalHFA, was the fact that the Department of Personnel, if you'll recall -- and it was well reported in the papers. There were a number of what they termed significant salary increases for employees of other state agencies and state employees.

And as part of that, what the Department did was issue a recommendation, if you will, a policy that those salaries that would be put in place would be, what I'm going to use the word, PERSable over an extended period of time. And, in other words, the normal process in putting salaries in place -- and Terri and Tom can correct me -- is when a new salary is adjusted, then it goes in for retirement purposes in calculating retirements through PERS at that salary level.

What this recommendation was and what this policy was from DPA was to implement or have the new salary increase calculated over a three-year period. So it would be PERSable over three years rather than over the immediate year, obviously I can't speak for DPA, but my own intuition tells me so that there's not this pension spiking. And so also, in fact, obviously it is
so somebody doesn't get a salary increase and leave the
next year and have the pension over that one year. It
has to be phased in over a three-year period. So --

CHAIRMAN SHINE: So are you saying that under
the current rules, pre what we're going to talk about
here, that the level of salary was automatic a hundred
percent vesting, and criteria to be used was that new
salary immediately.

MR. COURSON: Yes, for PERS purposes.

CHAIRMAN SHINE: Now you're talking about a
three-year phase-in to vest?

MR. COURSON: That's correct.

So let me go back and if you'll --

CHAIRMAN SHINE: Isn't that going backwards from
what --

MR. COURSON: Well, yeah, but this came in after
our approval of the salaries in January.

And also, you'll recall in our March meeting the
executive director and we recommended and we approved
moving her approved -- previously approved salary back
by $25,000 to address this issue of pension spiking.
You'll recall that. So after all of that and when these
other, what the State has called, substantial salary
increases came in, is when this PERS issue arose.

So having said that, as part of our process
here, we know that at our last -- I think our last Board meeting we were told by outside counsel discussion about changing previous actions taken by the Board in terms of compensation.

So to -- in the spirit of complying with DPA, we're asking and I'm asking you to -- as part of the process that I'd like to take to the Board today a recommendation that the salaries that were approved previously based upon the agreement of those who got those salaries -- they have agreed and you'll see, I think you have a letter in front of you signed by them -- that they would agree to accept the three-year PERS phase-in of the -- of the salaries we approved. And the executive director, given the fact that she dropped her salary by 25,000, would be phased in over a two-year period.

And so to comply with what the Governor's Office and DPA has asked us to do, I would like to have you recommend to the Board -- I'm going to ask the Board to consider approving this process, if you would, to go back and accept the PERS of three years for these six people and two years for our executive director.

CHAIRMAN SHINE: When did you see the commencement date of the vesting period occur? Does it go all the way back to January?
MR. COURSON: Yes.

CHAIRMAN SHINE: So what you're saying is that everybody who was dealt with in that salary adjustment would be, as of January '07, beginning a three-year phase-in vesting by I guess a third, a third, a third?

MR. COURSON: Yes. That's correct.

CHAIRMAN SHINE: And Terri, the executive director --

MR. COURSON: Two and two.

CHAIRMAN SHINE: -- would be given a two-year phase-in.

MR. COURSON: Two and two.

CHAIRMAN SHINE: So on the second anniversary, then the executive director will be fully vested.

MR. COURSON: Correct.

MS. PARKER: Mr. Chairman, I'd like to add to this.

As Mr. Courson said, this is an issue that, with respect to phasing in -- I don't know whether this is on (indicating).

With respect to phasing in our retirement benefits, the current practice under PERS is that for any salary for any state employee is vested after a 12-month period. Twelve consecutive months, the salary, it becomes the base for calculation of their retirement.
purposes for their retirement base.

There was a lot of discussion about this and has been for the last six or 12 months. The discussion, the major discussion, of this came out after the Board took action in January, but so much has come out of it that when I talked with my senior managers after we received the October letter from the Department of Personnel Administration -- the Department of Personnel Administration has not raised this issue to us prior to this letter being received.

We went back -- I went back with my managers and looked at it. And essentially we said, and what we have proposed to you, is if this is an important item, that we essentially think is from a management standpoint -- SB257 called for the recruitment and retention of senior managers -- then we should recommend and abide by a policy that essentially uses the adjustment to our retirement base as a tool to promote longevity among our senior managers.

So I have asked, just because there have been pay letters that have been signed and pay letters that have not been signed, that all of the senior managers of CalHFA be affected and rise and fall together. Because if it is an important tool and important management consideration, then it should be applied to all of the
managers equally.

This letter is signed by all of those people that are impacted. They have all agreed. And the reason why they have signed it is because for some of the people on this list, given that it is November, for all intents and purposes, they have vested. But we are all asking you as a group to essentially -- you have the authority -- for all other state employees that this has been done to, department directors and agency secretaries, the director of DPA has the authority.

The director of DPA does not have the authority to do it for the CalHFA senior managers. The Board has the authority to set salary compensation.

So we have asked -- we have agreed and we are asking you to essentially concur in this so that this can be essentially given to the Department of Personnel Administration in their contract with CalPERS to have that salary calculation for PERS contribution essentially changed on a go-forward basis.

CHAIRMAN SHINE: Two things. No. 1, you're saying that vesting occurs on the 13th-month anniversary of the change in salary, not on the day it's given? It's 12 consecutive months of a particular salary, then vesting at the new level; is that correct? Or is it --

MS. PARKER: No. For purposes of the
calculation of your PERS retirement, it is the single highest 12 months.

CHAIRMAN SHINE: Twelve months. That's my question. So it's a 12-month issue.

And am I clear then that if the management has agreed to take a step back, in a matter of speaking --

MS. PARKER: That is correct.

CHAIRMAN SHINE: -- in vesting, that the first year of the three years is already in practice anyway, because you have to have 12 months. So they're actually taking a two year -- a two-year longer period --

MS. PARKER: Correct.

CHAIRMAN SHINE: -- to be vested.

MS. PARKER: Correct.

CHAIRMAN SHINE: And in your case a year.

MS. PARKER: Correct.

CHAIRMAN SHINE: And everybody is going backward?

MR. COURSON: I would suggest they're not going forward as quickly.

CHAIRMAN SHINE: I now understand what you're saying. And the bottom line is you're asking us to approve something to some degree that's less than what we thought we had before for all the people that are involved in this letter.
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MS. PARKER: That's correct.

CHAIRMAN SHINE: Any comments from the committee?

Thank you very much.

MR. COURSON: Mr. Chairman?

CHAIRMAN SHINE: Yes.

MR. COURSON: It would be -- I think since it is part of your agenda on part of the compensation process going back, that perhaps as part of your report, depending on what the -- how the committee would decide, you might want to suggest to the Board your recommendation that we -- I think that the Board take action to approve the contents of this letter that was received by me, and I'll then deliver it to DPA for processing.

CHAIRMAN SHINE: Are we -- you have a comment, Mr. Morris?

MR. MORRIS: Yeah. I haven't had a chance to review this issue. This is something that, you know -- it would be nice to get this information before meetings so we could discuss it. To get something and say we've got five minutes to decide whether you want to approve is not the way I would do it.

But let me go back so I understand what it is, what this letter says, because I'm not familiar with how
the vesting works. When we adjusted salaries earlier in
the year, what you're saying is after -- after a year,
these exempt employees would be fully vested in their
PERS contribution.

MS. PARKER: That is true of those employees and
every employee in state government.

MR. MORRIS: These exempt positions.

MS. PARKER: That's -- it's all employees.

MR. MORRIS: Along with the other employees of
CalHFA, it's all the same. So every other --

MS. PARKER: Correct.

MR. MORRIS: -- employee of CalHFA, the -- after
one year, after a year, they've fully vested in their
pension.

MS. PARKER: Correct.

MR. MORRIS: Can you explain to me now the
reason that you are going back and saying how will this
affect -- the other CalHFA employees will not be
affected at all. They will continue to fully vest after
one year.

MS. PARKER: What DPA, when they started this
discussion and had it apply to certain high-level state
managers that had not received pay increases for in
excess of six years, those salary increases then became
under their definition a significant percentage
increase. For example, agency secretaries got a 30-percent increase.

So what the policy or the thinking of DPA was for its significant salary increases for incumbents, that rather than have them receive that increase and after 12 months then be vested and leave, that they wanted to essentially say let us phase this in because we want to use this as a retention tool to keep those people around for a couple of years, given this now -- this new salary increase.

So I -- my sense is that this is consistent with what the Board has talked about. It's consistent with what we talked about in SB257 as a recruitment and retention. And that was why I had essentially talked to the Board at the very beginning that we needed to include in the salary compensation those incumbents that we had. We couldn't just deal with new people. We had to deal with existing ones, because we needed to make sure that we retained them.

So by now going back, because there are many people on this list, by them agreeing to this, they essentially pretty much are signing up that they won't get the full benefit of this salary increase, and in some cases it is over 30 percent, unless they stay a full 36 months.
MR. MORRIS: Why is yours 24 months versus 36 months?

MS. PARKER: Mine is 24 months because the Board originally proposed a $200,000 salary. I came in in March and asked the Board to take my salary down 25,000 because Senator Lowenthal was concerned about the issue of pension spiking. And he was concerned about wanting a phase-in.

I went back to the Board at that point in time and said I -- I don't want this to be about any particular individual. If it makes people more comfortable to have the salary of the executive director phased in, then I will commit to go back to the 25th percentile for the salary survey of my colleagues and use that as a way to phase in my salary.

If I had been remained at $200,000 and had my salary phased in over a three-year period, at the end of the second year, my base would be 179. So in this case, by essentially taking 200,000 down to 175, after two years my vesting will be 175. So if I was subjected to a three-year period, it would be disproportionate to how this had been done for every other individual.

MR. MORRIS: When does your term expire?

MS. PARKER: My term expires at the end of next year.
MR. MORRIS: The calendar year?

MS. PARKER: Correct.

MR. MORRIS: Okay. So you got -- you have 14 months left, basically? Okay.

I mean my comment would be I understand when you came back you had been approved to 200,000 and came back to 175. I've heard different stories on how that occurred and --

MS. PARKER: Well, the story from me is --

MR. MORRIS: No, I understand. I understand what you said.

MS. PARKER: -- the --

MR. MORRIS: I understand what you said. But I find it -- I mean, during the next 14 months, is there going to be any salary adjustments made to your salary?

MS. PARKER: That would be up to the Board.

MR. COURSON: I don't think -- let me respond to that.

I think that's a Board decision, and I don't think that decision has been made, so that will be made -- you talked about a compensation process, and it will be made --

MR. MORRIS: Okay.

MR. COURSON: -- as a part of that.

MR. MORRIS: Okay. I've heard different stories
MR. COURSON: Would you share with us what those different stories are, Mr. Morris?

MR. MORRIS: It's not -- this really isn't the forum to do it. If we want to go into closed, we can go into closed and do it.

But I personally would not approve it based upon your phasing in in two years versus three years, saying that you took a reduction of 25,000, because I've heard a different process. But I think that, you know, I'm only one vote, so we'll see what everybody says.

MR. COURSON: Let me -- Mr. Chairman, may I respond to that?

I have to say in all due respect, I think it's a little disingenuous to sit here and not support something based on information that a Board member has and then unwillingness to share it with this committee or the Board. I just -- I just don't think that is the way we should make informed decisions. Anything that is worthy of a Board member to bring in their own mind that causes them not to support something that is before them and then not to be willing to discuss the reasons for that, I just think is -- is not the proper way we ought to be doing our Board business.

MR. MORRIS: Well, I don't need a lecture on the
proper way to do Board business, but I'll tell you right 
now some things should be done in private and some 
things should be in public. And some things have been 
told to me in confidence from people in various agencies 
and in the administration which I will not share in 
public.

MR. COURSON: Okay.

MS. PARKER: Mr. Morris, I just want to also add 
you were not here at the Board meeting. Your three 
other colleagues were.

I just want to say to the three colleagues who 
were here, I essentially explained my rationale to you. 
I did not lie when I essentially said that this was an 
agreement between Senator Lowenthal and myself, because 
he is the one person who had talked about a concern 
about pension spiking and talked about the need to do 
something about it. And I came in and asked the Board 
to do it. And that, for the record, is the story.

MR. COURSON: I would like to respond to one 
other comment talking about getting information earlier. 
This -- this all, this discussion we're having, results 
from a communication that I received at the end of last 
week. So this is not like it's something that's been 
laying around for consideration by CalHFA, brought to my 
attention at the end of last week.
And obviously for this Board to do anything, it took the voluntary action of meeting with this senior group and obtaining their consent to roll these back, because obviously they needed to make their own voluntary move, as Terri's described, backwards. So this is something that that was finally achieved yesterday after meetings the first couple of days of the week that they had. So this is not something that we've had information for any period of time.

MS. GALANTE: Can I?

CHAIRMAN SHINE: Please.

MS. GALANTE: I'd like to make a comment and then a motion.

I just want to say I very clearly remember Terri coming in and asking for her salary to be rolled back, and I think if you look at the minutes, I remember it because I voted against it. I think I was the only one who voted against it, and I've taken a little bit of heat for that vote. But I felt like we had gone through a compensation process, we had established salaries, and I just really didn't want to accept, frankly, the executive director's request.

You know, so having said that, I -- I think it's admirable that staff has all agreed to do this, quote, rollback, for lack of a better term, on the pension
side. And, you know, when I read the letter from the DPA, I can see that this is a policy that's been established for other state agencies.

And as the executive director mentioned, the CalHFA employees aren't subject to that DPA, so we're the only body that can try to make some consistency with the DPA recommendation for CalHFA employees -- or the Board, not us as the Audit Committee.

But I -- so I'm willing to make a motion that we accept the recommendation in the letter from the employees dated November 14th and recommend that we do that.

CHAIRMAN SHINE: Is there a second?

MR. CAREY: In seconding that, I'd like to concur with everything that Ms. Galante had to say.

CHAIRMAN SHINE: Any comments from anybody?

All in favor of the motion? Mr. Carey.

MR. CAREY: Aye.

CHAIRMAN SHINE: Ms. Galante.

MR. CAREY: Yes.

CHAIRMAN SHINE: Mr. Morris.

MR. MORRIS: No.

CHAIRMAN SHINE: I vote yes.

MR. COURSON: Thank you, Mr. Chairman.

MS. PARKER: Thank you.
CHAIRMAN SHINE: So we have an issue to report to the Board, Mr. Hughes, that we just discussed. That can be taken up by the Board today.

MR. HUGHES: Correct.

CHAIRMAN SHINE: And the putting together of the items we discussed before that for us to review and come back with can be put before the Board at the next Board meeting. I don't know whether we will or will not need another Audit Committee meeting in the interim, we may just to review the results of our own work, given what it takes to try and get together between meetings.

MR. HUGHES: Mr. Chair, I'll ask -- I've asked Yvonne to expedite.

CHAIRMAN SHINE: I'm sorry?

MR. HUGHES: I've asked the court reporter to expedite the transcript. And what I will do is I will get the transcript to each one of the committee members, and we will use that as a basis to have the committee prepare its recommendations.

CHAIRMAN SHINE: Is there any further business from members of the committee?

Any comments from the public?

MR. CAREY: On this issue?

CHAIRMAN SHINE: I'm talking about the meeting. I'm getting ready to adjourn here. But I want to close
Mr. Carey: You're just talking about this one issue?

Chairman Shine: Yes.
Okay. Then we're done with that issue.
Let's move on, because there's two other things on the agenda here. One is a review of the trust fund audit by the Bureau of State Audits. Who is going to deal with that issue?

Ms. Galante: I just need to say for the record I did read this report and I read the audit report. Unfortunately, I had e-mailed Terri Parker last week that I had an urgent matter come up and I'm not going to be able to stay for the balance of the Board meeting, so I am going to leave in a few minutes and I didn't want to just interrupt the flow once things got started.

Chairman Shine: Any further?
All right. So let's get started now with this report.

Item 5. Review and discussion of Housing and Emergency Shelter Trust Fund (Prop. 46) audit by the Bureau of State Audits

Mr. Meidinger: Good morning, Mr. Chairman. My name is Dennis Meidinger, comptroller of the Agency. To
my right is Susan Goodison, our accounting administrator. And I also do have Tim Stenvick from Deloitte.

Items No. 5 and 6 are to go over a summary of the two audits that we've just completed, and then I'll ask Tim to go over the results that -- that he found.

The first audit, I burdened you with all of the audit reports and all the information there, but to summarize it very quickly, the first audit that we had during the summer was from the Bureau of State Audits over two voter-approved propositions of funds, named the Housing and Emergency Shelter Trust Fund Acts of 2002 and 2006.

Now, these funds are all -- it's voter approved in two -- in the form of two different propositions, and they are appropriated to Department of Housing and Community Development. However, our piece in it is that we contract with HCD to administer some of the programs.

During the summer when they came in, the Bureau selected five different programs to look at, four of them resided at HCD and really only one of them resided with the California Housing Finance Agency, which was the California Homebuyers Downpayment Assistance Program.

The results were that the Bureau found that
CalHFA had been timely and consistent with law and that our timing and amounts of awards had approximated or exceeded the Agency's projected estimates.

CHAIRMAN SHINE: Excuse me. We have a terrible sound system here this morning or it's not turned up, one or the other. You'd have to speak almost right into it to get your voice over here.

MR. MEIDINGER: Sorry.

So further, the Bureau found that the California Housing Finance Agency had established and adhered to policies intended to ensure that only eligible applicants received the funds, and as such there were no recommendations or findings by the Bureau.

So are there any questions about that audit?

CHAIRMAN SHINE: So the comment on the cover sheet of this that the monitoring of the use of funds has been inconsistent didn't apply to what we're doing; is that correct?

MR. MEIDINGER: Right.

CHAIRMAN SHINE: Good. I have no questions.

MR. CAREY: Mr. Chair, I'd just say that as someone who's very concerned with the integrity of the bond process and worked hard for Prop 46 and Prop 1C, I'm thrilled to see the very positive results for the Agency and actually the Department also.
Item 6. Review and discussion of the audited Housing Finance Fund financials for 6/30/07, including a discussion with auditors from Deloitte and Touche LLP

MR. MEIDINGER: Next I'll go over a quick summary of our Housing Finance Fund financials. This is the fund that the Agency accounts for all of our loan and bond programs, as well as the Agency's operating account.

Taking a look at the balance sheet first, you'll notice that on our assets, which we have $9.7 billion of assets now, 99 percent of them consist of cash and investments and program loans receivable.

As you can see, during the year comparison with 2007 versus '06, we reduced our cash and investment by 989 thousand -- million dollars. And what we did is we put them into program loans receivable. So our program loans receivable, as you can see in the next line, increased by $1.2 billion. So our total assets compared to last year increased, as you can see, by $249 million.

Taking a look at our liabilities, our bonds payable increased by $134 million net, and other liabilities decreased by $10 million as we completed all
calculations that we owed to the IRS for arbitrage. And so liabilities increased by 124 million. So our bottom line is that 125 million was increased to our fund equity, so we now stand at $1.4 billion of equity.

Taking a look at our income statement, in 2007 we had generated 375 million of interest income from program loans, that compares with 314 million last year, for a $61-million increase. Included in this was a sale that we had to Fannie Mae of 6,000 subordinate loans.

Our interest income from investments decreased by 17 million, as we -- it's logical that we had reduced our cash and investments to put into new mortgages. And if you take a look at our other loans and commitment fees, they had increased by $6 million as a larger loan portfolio resulted in more loan servicing fees for our loan servicing group.

Other revenues increased by 18 million over last year as the Agency sold all of its remaining multifamily REOs, so over last year, we had earned $67 million more.

Taking a look at the expense side, as interest rates increased, we had to pay more for our bonds, bond interest, and so that increased by 20 million. The amount that we paid to our mortgage servicers increased by 3 million because we had a larger portfolio. Our operating expenses only increased by a million dollars,
which was about 3 -- a little more than 3 percent, which was about the standard increase in overall state employees in salaries. And our other expenses decreased by 5 million from the prior year as last year we had recognized some deferred loss on bond refundings.

So taking a look at our increase in income versus the expenses, we had earned $48 million more than last year. However, we did have those two extraordinary sales. One was the Fannie Mae, and also the other was the multifamily REOs. And so had we not had those, our income instead of 85 million this year would have been closer to 52 million, for at least a $15-million increase.

Are there any questions?

CHAIRMAN SHINE: Any questions from anybody?

Comments?

MR. MEIDINGER: I'd like to ask Tim Stenvick from Deloitte to go over results that they found.

MR. STENVICK: Thanks, Dennis.

Mr. Chair, and Committee Member, my name is Tim Stenvick. I'm an auditor partner with the firm of Deloitte and Touche. We are your independent auditors, and we not only audit the financials, but also help you in fulfilling some of your other audit obligations for the federal government as well as the State Controller's
Office and the Department of Finance, each of which has sort of separate and unique rules.

We have provided to you -- or I should say that staff has provided to you a letter that we issued that summarizes the result of our audit. It's a letter that's very typical to be provided to Audit Committee members as a result of an audit. In the interest of your time and schedule, I won't go through that. But I will just tell you that the audit went very well this year. There were no audit adjustments proposed by us. Management takes a high level of responsibility for your financial statements, and in my view you have a very effective and highly functioning finance function. And really, there's nothing notable.

I will say that in the past and over the past few years, we have given you what we term a management letter containing some observations about internal control and other matters. This year we have no such letter to discuss with you, because we didn't prepare one. And as part of our normal audit procedures, we looked at the attention that the Agency had given to the matters that we had brought to their attention in the past and had found it to be satisfactory.

So in the interest of time, I'll just tell you that the audit went well and that I believe the
financials fairly present the results of operations of
the Agency or the Fund.

Thank you.

CHAIRMAN SHINE: Thank you very much.

Comments or anything from the public? If not,
thank you very much for your report. I appreciate it.
Very well done.

MR. CAREY: If I could ask just one question.

Just to clarify, so you're saying that no management
issue was issued because there were no issues that would
rise to that level.

MR. STENVICK: Correct.

---00---

Item 7. Public testimony

CHAIRMAN SHINE: Okay. Is there any testimony
or comments from the public at this time?

Seeing none, the meeting is adjourned.

(Whereupon the meeting concluded at 10:33 a.m.)

---00---
Audit Committee Meeting - November 15, 2007

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 26th day of November 2007.

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

Yvonne K. Fenner & Associates  916.531.3422
Fiscal Years 2008/09 to 2012/13
Five-Year Business Plan

Concept Proposal

March 19, 2008
CalHFA Business Plan
Fiscal Year 2008/09

- Overview of Special Programs Loan Initiatives

- Production Goals:
  - Homeownership
  - Mortgage Insurance
  - Multifamily Rental
  - Special Lending
  - Asset Management

- Other Considerations
  - Strategic Initiatives
  - California Housing Market
  - Capital Markets
## CalHFA Business Plan FY 2008/09
### Special Programs Loans Initiatives
### Production Levels

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<th>GO BOND PROGRAMS</th>
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Proposed Homeownership Business Plan FY 2008/09

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|                  |          |       |      | $58.4 M |

| REO (FICO >680)  | 100% LTV 1st |       |      | $200 M  |
| All conventional |           |       |      |         |
| CHDAP            |           |       |      | $6 M    |
| CHAP/HICAP       |           |       |      | $5.5 M  |
| TOTAL            |           |       |      | $1.2 B  |

| SHBAP            | SELF-HELP | CONST/ | DEVELOPMENT | $1.5M |

- $1.0 Billion standard 1<sup>st</sup> Mortgage Production
- $200 M New REO Program
  - 100% 30-yr fixed rate
- Increase FHA volume
- Underwriting changes
  - FICO scores
  - 95% LTV Conventional Loan
- HAT Funded DAP scaled back (CHAP/HICAP)
- HELP and Habitat for Humanities reallocated to fund DAP
- RDLP to maintain CHDAP funding
- Continuing LOS Project
Proposed Mortgage Insurance Business Plan FY 2008/09

- $500 Million Mortgage Insurance Production
  - $300 Million New ≤ 95% LTV
  - $200 Million 100% LTV REO Program
- $100 Million of ≤ 80% LTV (Gap Insured)
- Underwrite 1,600 CHDAP Stand Alone 1st Mortgages
- Increase Over 95% LTV Minimum Credit Score to 680
- Reduce Maximum LTV for Non-REO Program Loans to 95% LTV and Minimum 620 Credit Score
- Develop Program to Promote DAPs on ≤ 95% LTV and under loans to reduce share of 100% LTV loans
Proposal Multifamily Business Plan FY 2008/09

- Production Goal: $250 Million Annual +
  - Includes both Construction and Permanent Financing
- Multifamily Competitiveness
  - Interest rates, loan fees and processing
  - MHSA Homelessness Initiative
  - Partnership with Fannie Mae
  - Acquisition Program
  - Low Floater Program
Asset Management Market Conditions

- Rental market & occupancy rates remain strong
- Increasing operating costs putting squeeze on bottom line
- Portfolio aging:
  - Loan terms are expiring
  - Projects need rehabilitation, recapitalization
- Owners are aging:
  - Want exit strategy
  - Want equity take out
- Pressure to allow prepayment
Resources for Managing Assets

- Identify and convince owners to sell through Preservation Sales program through Multifamily Programs
- $8M HAT funds dedicated for preservation & rehabilitation of existing portfolio
- $50M earned surplus funds for rehabilitation of HUD properties
- SB 707 - Extension of RHCP program 7-1-2008
- Watchlist - Identified most troubled properties and give greater agency attention and resources
- Report card project to evaluate how we are doing from loan close to 5 years out
- Continue efforts to create an in-house refinance program
Business Plan – Other Considerations

- Strategic Initiatives
  - Major Agency resource commitment;
  - Homeownership, Fiscal Services & Doc Management
  - Sacramento Office Consolidation Update

- California Housing Markets
  - Declining Values -- Good News (Affordability) – Bad News (Loss of Collateral Value)

- Capital Markets
  - Update on the capital markets challenges
Strategic Initiatives

- Homeownership
  - Loan Origination System
- Fiscal Services Re-Platforming – Phase 1
  - Phase 2 – Other FS Business Processes
  - Phase 3 – Cost Accounting
- Enterprise Content Management
  - Agency-wide Implementation of WorkSite
  - Imaging Promissory Notes
- Debt Management
- Sacramento Office Consolidation Update
# Implementation Roadmap

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**Legend:**
- Development and Deployment
- Maintenance and Warranty Period

**Note:** The roadmap outlines the implementation timeline for various projects and initiatives, with dates and key milestones for each fiscal year from 2007/2008 to 2012/2013.
Business Plan – Other Considerations

- Strategic Initiatives
  - Major Agency resource commitment;
  - Homeownership, Fiscal Services & Doc Management
  - Sacramento Office Consolidation Update

- California Housing Markets
  - Declining Values -- Good News (Affordability) – Bad News (Loss of Collateral Value)

- Capital Markets
  - Update on the capital markets challenges
Review of California Housing Finance Agency Mortgage Insurance Rates
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CalHFA Mortgage Insurance

BOARD PRESENTATION
MARCH 19, 2008

Charles K. McManus
Director of Mortgage Insurance
Review of California Housing Finance Agency
Mortgage Insurance Rates

- Mortgage Insurance Fund (California Housing Loan Insurance Fund) formed to credit enhance low down payment mortgage loans for low and moderate income California residents

- Mortgage Insurance Fund historically provided below market premium rates

- Housing market in California currently experiencing falling prices in many markets

- Low down payment lending increasingly risky
Review of California Housing Finance Agency
Mortgage Insurance Rates (continued)

- Private Mortgage Insurance companies have withdrawn from the 100% LTV market; severely limited the 97% LTV lending or withdrawn from lending over 95% LTV

- CalHFA needs to increase mortgage insurance premium rates to current market rates

- CalHFA will continue to review housing market conditions; would plan on returning to current or similar premium rates when home prices have stabilized
### Chart 1. CalHFA 35% Coverage Rates

<table>
<thead>
<tr>
<th>LTV</th>
<th>Coverage</th>
<th>Exposure</th>
<th>Standard Mortgage Insurance Rates</th>
<th>Stable &amp; Rising Market Alternative Rates</th>
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<tr>
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<tr>
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<td>0.62% 0.51%</td>
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### Chart 2. New CalHFA Rates

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<th>Stable &amp; Rising Market Alternative Rates</th>
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<td>35%</td>
<td>65%</td>
<td>&gt;25 Yr 0.96%</td>
<td>≤ 25 Yr 0.85%</td>
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<tr>
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<td>65%</td>
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<td>≤ 25 Yr 0.85%</td>
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<td>75%</td>
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<td>≤ 25 Yr 0.21%</td>
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## Chart 3. New CalHFA MBS Coverage Rates

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<th>Standard Mortgage Insurance Rates</th>
<th>Stable &amp; Rising Market Alternative Rates</th>
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</thead>
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<tr>
<td>100% - 97.01%</td>
<td>28%</td>
<td>75%</td>
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<td>0.67%</td>
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<tr>
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<td>25%</td>
<td>75%</td>
<td>0.71% 0.60%</td>
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<tr>
<td>95% - 90.01%</td>
<td>22%</td>
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<tr>
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<td>12%</td>
<td>75%</td>
<td>0.32% 0.21%</td>
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Chart 4. New CalHFA Minimum GSE Charter Rates

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<th>Stable &amp; Rising Market Alternative Rates</th>
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<td>≤ 25 Yr 0.23%</td>
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<tr>
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<td>&gt;25 Yr 0.23%</td>
<td>≤ 25 Yr 0.12%</td>
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The CalHFA Mortgage Insurance Fund (California Housing Loan Insurance Fund or CaHLIF) was formed to provide credit enhancement to low-down payment mortgage loans for low- and moderate-income California residents. CaHLIF has historically provided the uninterrupted availability of mortgage insurance to support CalHFA affordable housing finance programs and to help first-time home buyers qualify for and afford a home.

The housing market in California is currently experiencing falling prices in many markets throughout the state, making low-down payment lending increasingly risky. Private Mortgage Insurance companies have withdrawn from the 100% LTV market and either severely limited the insuring of 97% LTV lending or withdrawn from insuring over 95% LTV loans. CalHFA has revised its mortgage insurance premium rates up to current market rates in order to continue to offer mortgage insurance coverage on all loans in this market and has added additional credit rating requirements for borrowers seeking 97% LTV and 100% LTV loans.

The attached table list the rates CalHFA Mortgage Insurance Fund will begin charging as standard rates as well as those that may be charged in the future under circumstances where the housing market is stable and economic situations allow for such an adjustment. CalHFA will continue to review the housing market conditions in California and would plan on revisiting its mortgage insurance premium rates some time in the future when home prices have stabilized or started to rise again.
<table>
<thead>
<tr>
<th>LTV</th>
<th>Coverage Exposure</th>
<th>Standard Mortgage Insurance Rates</th>
<th>Stable &amp; Rising Market Alternative Rates</th>
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California Housing Finance Agency 3/5/2008
### Standard Mortgage Insurance Rates

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