



**VERMONT HOUSING FINANCE AGENCY**

Financial Statements and  
Required Supplementary Information

June 30, 2006

(With Independent Auditors' Report Thereon)

# VERMONT HOUSING FINANCE AGENCY

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**Independent Auditors' Report**

To the Honorable Randolph D. Brock  
State Auditor of the  
State of Vermont and  
The Commissioners  
Vermont Housing Finance Agency:

We have audited the accompanying financial statements of the business-type activities and each major fund of the Vermont Housing Finance Agency as of and for the year ended June 30, 2006, as listed in the table of contents. These financial statements are the responsibility of the Agency's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Agency's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities and each major fund of the Vermont Housing Finance Agency as of June 30, 2006, and the respective changes in financial position and cash flows for the year then ended in conformity with U.S. generally accepted accounting principles.

The Management's Discussion and Analysis on pages 2 to 6 is not a required part of the financial statements but is supplementary information required by U.S. generally accepted accounting principles. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

**KPMG LLP**

September 14, 2006

# VERMONT HOUSING FINANCE AGENCY

## Management's Discussion and Analysis

June 30, 2006

**(Unaudited)**

This section of the Vermont Housing Finance Agency's (the Agency) annual Financial Report presents management's discussion and analysis of its financial performance and significant changes in financial position for fiscal year ended June 30, 2006. Readers are encouraged to consider the information presented in conjunction with the financial statements as a whole.

### **Overview of the Agency**

The Agency was created in 1974 by an Act of the General Assembly of the State of Vermont. The purpose of the Agency is to promote the expansion of the supply of funds available for mortgages on residential housing and to encourage an adequate supply of safe and decent housing at reasonable costs. The Agency is authorized to issue bonds and other obligations to fulfill its corporate purposes up to a total outstanding amount of \$900 million. Obligations of the Agency do not constitute debt of the State of Vermont and are payable solely from the revenues or assets of the Agency.

The majority of the Agency's funding has been provided from the proceeds of sales of tax-exempt and taxable bonds and notes, advances from lending institutions, and from the administration of federal programs. Since September 1974, the Agency has issued \$2.3 billion aggregate principal amount of bonds, notes and line of credit borrowings, of which \$640.8 million was outstanding as of June 30, 2006, to finance its various programs. The proceeds of the debt have been or will be used to make mortgage loans to sponsors of multi-family residential housing units for persons and families of low and moderate income in the State, to purchase mortgage loans on single family residential housing units for persons and families of low and moderate income in the state, to make loans to mortgage lenders to finance such single family housing, and to make loans to finance certain other multi-family housing developments. The bonds are secured pursuant to the terms of the resolutions under which they were issued.

### **Overview of the Financial Statements**

The Agency's financial statements consist of three parts – Management's Discussion and Analysis, the basic financial statements and the notes to the financial statements. The basic financial statements include the Statement of Net Assets, Statement of Revenues, Expenses and Changes in Net Assets and the Statement of Cash Flows. The notes to the basic financial statements are intended to provide additional information that is essential to a full understanding of the data provided in the basic financial statements.

### **Summary of Net Assets**

The Agency's Statement of Net Assets consists primarily of single family and multi-family mortgage loans, cash and investments, and related bonds and notes payable. It also includes a portfolio of mortgage loans financed through its Operating Fund, as well as a variety of other assets such as property and equipment, other receivables, and deferred charges.

Cash and investments are used to fund loan purchases, bond debt service, and reserve funds, and are typically held in guaranteed investment contracts or other investment vehicles, as authorized in accordance with the Agency's investment policy.

**VERMONT HOUSING FINANCE AGENCY**

Management's Discussion and Analysis

June 30, 2006

**(Unaudited)**

The following table summarizes the net assets of the Agency as of June 30, 2006 with comparative data from the prior fiscal year.

	<u>2006</u>	<u>2005</u>	<u>Percentage Change 2006-2005</u>
<b>Assets</b>			
Cash and investments	\$ 182,245,067	219,070,095	(16.8)
Loans receivable, net	529,001,950	465,703,753	13.6
Other assets	17,002,028	16,804,699	1.2
Total assets	<u>728,249,045</u>	<u>701,578,547</u>	<u>3.8</u>
<b>Liabilities</b>			
Bonds and notes payable	640,810,463	615,216,124	4.2
Other liabilities	8,855,993	9,971,242	(11.2)
Total liabilities	<u>649,666,456</u>	<u>625,187,366</u>	<u>3.9</u>
<b>Net Assets</b>			
Invested in capital assets	1,690,221	1,771,187	(4.6)
Restricted:			
Bond and other requirements	61,297,505	60,073,671	2.0
Excess yield loans	8,349,379	8,094,406	3.1
Unrestricted	7,245,484	6,451,917	12.3
Total net assets	<u>\$ 78,582,589</u>	<u>76,391,181</u>	<u>2.9</u>

Total assets increased by \$26.6 million or 3.8% for the year ended June 30, 2006 when compared to the year ended June 30, 2005, primarily as a result of:

- Cash and investments decreased by \$36.8 million, or 16.8%. This represents bond proceeds held in acquisition funds at year end awaiting the purchase of mortgages, and the decrease in fair value of investments.
- Total Mortgage and Construction Loans Receivable increased by \$63.3 million, or 13.6%. Loan originations increased by \$30.2 million, or 26.8% over the prior fiscal year. In fiscal year 2006 there was a slowdown in the level of prepayments, with the amount of principal collections decreasing by \$9.5 million, or 10.8% from the prior year.
- Included in restricted net assets is approximately \$8.3 million of Multi-Family mortgages (net of \$1.5 million of loan loss reserves) which were funded by excess interest income received (excess yield) from mortgages related to the Agency's 1995 and 1999 Multi-Family bond issues. The excess yield represents mortgage interest earned in excess of that permitted by federal tax laws. To be in compliance with such tax laws, the Agency estimates that it may be required to forgive or restructure up to \$9.8 million of its loans, prior to the final maturity of bonds in these series.

**VERMONT HOUSING FINANCE AGENCY**

Management's Discussion and Analysis

June 30, 2006

**(Unaudited)**

The following table summarizes the change in mortgage loans receivable for the year ended June 30, 2006, with comparative data from the prior fiscal year:

	<u>2006</u>	<u>2005</u>	<b>Percentage Change 2006-2005</b>
Beginning balance	\$ 465,703,753	445,322,983	4.6
Mortgage loan originations	142,604,540	112,439,021	26.8
Principal collections	(78,460,206)	(88,001,075)	(10.8)
Loans transferred to REO status	(931,632)	(866,246)	7.5
Loan loss provision	85,495	(3,190,930)	(102.7)
Ending balance	<u>\$ 529,001,950</u>	<u>465,703,753</u>	<u>13.6</u>

Total liabilities of the Agency increased by \$24.3 million, or 3.9% for the year ended June 30, 2006 when compared to the year ended June 30, 2005, primarily as a net result of:

- Two new bond series of Single Family Housing Bonds were issued totaling \$104.4 million in bonds and \$30 million in notes. These proceeds were used to finance single family mortgage purchases and to refund \$5.5 million in Housing Program Series 5 and \$11.1 million of Series 6 bonds.
- An additional \$46.3 million of Single Family Housing Bonds were redeemed prior to maturity as a result of mortgage loan prepayments received.
- Fourteen Multi-Family loan program construction projects totaling \$13.6 million were financed with notes payable from lending institutions.
- All bond issues are rated by Moody's Investors Service and Standard and Poor's with a minimum stand alone rating of A. Many Agency bond issues carry bond insurance, which upgrades the bond rating to AAA.

**Summary of Revenues, Expenses and Changes in Net Assets**

The Agency's operating revenues consist primarily of interest income on mortgage and construction loans, investment income, and miscellaneous fee income. Operating expenses consist of bond interest expense and other debt financing costs, operational expenses, and mortgage servicing fees.

**VERMONT HOUSING FINANCE AGENCY**

Management's Discussion and Analysis

June 30, 2006

**(Unaudited)**

The following summarizes the changes for the year ended June 30, 2006 with comparative data from the prior fiscal year.

	<u>2006</u>	<u>2005</u>	<b>Percentage Change 2006-2005</b>
<b>Operating Revenues</b>			
Interest on loans	\$ 31,413,101	29,288,490	7.3
Interest on investments	8,772,556	8,330,204	5.3
Fee income	765,665	601,441	27.3
Other revenue	61,823	71,036	(13.0)
Total operating revenues	<u>41,013,145</u>	<u>38,291,171</u>	<u>7.1</u>
<b>Operating Expenses</b>			
Financing costs	32,469,627	31,426,098	3.3
Operational expenses	4,192,544	3,955,248	6.0
Mortgage servicing	973,310	910,963	6.8
Loan loss provision	(101,943)	3,199,607	(103.2)
Loss on bond redemptions	169,833	716,710	(76.3)
Total operating expenses	<u>37,703,371</u>	<u>40,208,626</u>	<u>(6.2)</u>
Operating income (loss)	<u>3,309,774</u>	<u>(1,917,455)</u>	<u>(272.6)</u>
<b>Non-Operating Revenues</b>			
Net appreciation (depreciation) in fair value of investments:			
Unrealized gain (loss) on investments	(1,118,366)	1,036,206	(207.9)
Realized gain (loss) on sale of investments	—	(65,681)	(100.0)
Net appreciation (depreciation) in fair value of investments	<u>(1,118,366)</u>	<u>970,525</u>	<u>(215.2)</u>
Increase (decrease) in net assets	2,191,408	(946,930)	(331.4)
Net assets at beginning of year	<u>76,391,181</u>	<u>77,338,111</u>	<u>(1.2)</u>
Net assets at end of year	<u>\$ 78,582,589</u>	<u>76,391,181</u>	<u>2.9</u>

## VERMONT HOUSING FINANCE AGENCY

### Management's Discussion and Analysis

June 30, 2006

**(Unaudited)**

For the year ended June 30, 2006 net assets increased \$2,191,408, compared to a decrease of \$946,930 for the prior year. The \$3,138,368 change in net assets when comparing 2006 to 2005, was primarily the result of the following:

- Total operating revenues increased \$2.7 million or 7.1% in fiscal year 2006, due to the effects of a mortgage loan portfolio shifting to slightly higher rates following years of decreasing interest rates.
- There were no changes to the provision for operating or multi-family loan loss reserves in fiscal year 2006 compared with provisions of \$2.0 million and \$1.5 million, respectively, in fiscal year 2005. The provision for loan loss reserves has been reviewed by management and the Audit/Risk Committee of the Agency's Board of Commissioners and deemed to be adequate.
- The loss on bond redemptions reduced net assets by \$170 thousand in fiscal year 2006 compared to \$717 thousand in the prior year.
- Net depreciation in the fair value of investments accounted for a decrease in net assets of \$1.1 million in fiscal year 2006, compared to net appreciation of \$1.0 million in the prior year.

The Agency budgets its day-to-day operating costs and related income (net of deferred loan origination costs and fees) in its Operating Fund. The operating budget is prepared by staff and reviewed and approved prior to the start of each fiscal year by the Agency's Board of Commissioners.

For fiscal year 2006, the Agency projected an Operating Fund budget surplus of \$103 thousand and achieved an actual budget surplus of \$595 thousand as a result of positive income and expense variances of \$402 thousand and \$90 thousand, respectively.

The addition of net deferred loan origination costs and fees of \$118 thousand in fiscal year 2006 to the actual budget surplus of \$592 thousand results in an increase in Operating Fund net assets for fiscal year 2006 of \$712 thousand compared with the prior period.

#### **Contacting the Agency's Financial Management**

This financial report is designed to provide a general overview of the Agency's operations and insight into the financial statements. If you have questions about this report or need additional financial information, please contact the Chief Financial Officer at Vermont Housing Finance Agency, 164 St. Paul Street, Burlington, VT 05401 or visit our website at [www.vhfa.org](http://www.vhfa.org).

**VERMONT HOUSING FINANCE AGENCY**

Statement of Net Assets

June 30, 2006

<b>Assets</b>	<b>Operating Fund</b>	<b>Single Family Mortgage Program Fund</b>	<b>Multi-Family Mortgage Program Fund</b>	<b>Total</b>
Cash and cash equivalents	\$ 7,519,011	—	—	7,519,011
Investments	100,000	—	—	100,000
Accrued interest receivable:				
Mortgage and notes	1,199,763	1,517,287	524,478	3,241,528
Investments	21,379	1,170,745	519,849	1,711,973
Current portion of mortgage loans receivable	260,855	7,459,443	15,673,216	23,393,514
Current costs of bond issuance expense	—	90,831	64,746	155,577
Current receivables and prepaid expenses	323,038	1,125,077	53,264	1,501,379
Interfund receivables (payables)	(660,091)	2,963,284	(2,303,193)	—
<b>Total current assets</b>	<b>8,763,955</b>	<b>14,326,667</b>	<b>14,532,360</b>	<b>37,622,982</b>
Noncurrent assets:				
Restricted cash and cash equivalents	—	98,901,758	27,818,552	126,720,310
Restricted investments	—	40,124,082	7,781,664	47,905,746
Noncurrent portion of mortgage loans receivable, net	12,610,445	377,419,466	115,578,525	505,608,436
Deferred costs of bond issuance, net	—	2,452,804	1,058,444	3,511,248
Deferred mortgage origination fees, net	—	1,942,863	—	1,942,863
Noncurrent receivables and prepaid expenses:	5,605	3,039,901	—	3,045,506
Land	775,000	—	—	775,000
Building (less accumulated depreciation of \$287,740)	713,094	—	—	713,094
Office furniture and fixtures (less accumulated depreciation of \$1,196,495)	202,127	—	—	202,127
Other assets and real estate owned	—	201,733	—	201,733
<b>Total noncurrent assets</b>	<b>14,306,271</b>	<b>524,082,607</b>	<b>152,237,185</b>	<b>690,626,063</b>
<b>Total assets</b>	<b>\$ 23,070,226</b>	<b>538,409,274</b>	<b>166,769,545</b>	<b>728,249,045</b>
<b>Liabilities and Fund Balances</b>				
Liabilities:				
Current liabilities:				
Current notes payable and lines of credit	\$ 3,846,690	15,000,000	11,073,582	29,920,272
Current bonds payable	8,320	8,555,000	5,734,009	14,297,329
Current unamortized bond and note premium (discount), net	—	(45,786)	(127,018)	(172,804)
Current deferred loan origination fees	191,155	—	—	191,155
Accounts payable	472,732	956,620	48,339	1,477,691
Escrowed cash deposits	2,556,333	—	—	2,556,333
Accrued interest payable	67,597	3,916,626	2,463,668	6,447,891
<b>Total current liabilities</b>	<b>7,142,827</b>	<b>28,382,460</b>	<b>19,192,580</b>	<b>54,717,867</b>
Noncurrent liabilities:				
Noncurrent notes payable	6,105,011	30,000,000	—	36,105,011
Noncurrent bonds payable	563,082	438,650,000	121,274,769	560,487,851
Unamortized bond and note premium (discount), net	—	(595,707)	(1,442,661)	(2,038,368)
Arbitrage rebate payable	—	70,494	—	70,494
Noncurrent deferred mortgage loan origination fees:	323,601	—	—	323,601
<b>Total noncurrent liabilities</b>	<b>6,991,694</b>	<b>468,124,787</b>	<b>119,832,108</b>	<b>594,948,589</b>
<b>Total liabilities</b>	<b>14,134,521</b>	<b>496,507,247</b>	<b>139,024,688</b>	<b>649,666,456</b>
Net assets:				
Invested in capital assets	1,690,221	—	—	1,690,221
Restricted	—	41,902,027	27,744,857	69,646,884
Unrestricted	7,245,484	—	—	7,245,484
<b>Total net assets</b>	<b>8,935,705</b>	<b>41,902,027</b>	<b>27,744,857</b>	<b>78,582,589</b>
<b>Total liabilities and net assets</b>	<b>\$ 23,070,226</b>	<b>538,409,274</b>	<b>166,769,545</b>	<b>728,249,045</b>

See accompanying notes to financial statements.

**VERMONT HOUSING FINANCE AGENCY**

Statement of Revenues, Expenses and Changes in Net Assets

Year ended June 30, 2006

	<u>Operating Fund</u>	<u>Single Family Mortgage Program Fund</u>	<u>Multi-Family Mortgage Program Fund</u>	<u>Total</u>
Operating revenues:				
Interest income:				
Mortgage and construction loans	\$ 842,230	21,943,683	8,627,188	31,413,101
Investments	155,215	6,837,920	1,779,421	8,772,556
Fee income:				
Multi-Family Mortgage Programs	697,349	—	45,008	742,357
Single Family Mortgage Programs	20,026	3,282	—	23,308
Miscellaneous income	61,823	—	—	61,823
Total operating revenues	<u>1,776,643</u>	<u>28,784,885</u>	<u>10,451,617</u>	<u>41,013,145</u>
Operating expenses:				
Financing costs, including interest and amortization of premium, discount and costs of issuance, net	762,336	24,065,554	7,641,737	32,469,627
Mortgage service and contract administration fees	—	973,310	—	973,310
Salaries and benefits	2,811,238	—	—	2,811,238
Operating expenses	1,070,899	—	—	1,070,899
Professional fees	120,987	—	—	120,987
Trustee and assignee fees	189,420	—	—	189,420
Loss on bond redemptions	—	169,833	—	169,833
Property disposition and loan loss recoveries	—	(101,943)	—	(101,943)
Total operating expenses	<u>4,954,880</u>	<u>25,106,754</u>	<u>7,641,737</u>	<u>37,703,371</u>
Operating income (loss)	(3,178,237)	3,678,131	2,809,880	3,309,774
Non-operating revenues:				
Net depreciation in fair value of investments	—	(1,036,774)	(81,592)	(1,118,366)
Income (loss) before transfers	(3,178,237)	2,641,357	2,728,288	2,191,408
Net transfers to (from) operating fund	3,890,838	(3,107,588)	(783,250)	—
Increase (decrease) in net assets	712,601	(466,231)	1,945,038	2,191,408
Net assets at beginning of year	8,223,104	42,368,258	25,799,819	76,391,181
Net assets at end of year	\$ <u>8,935,705</u>	<u>41,902,027</u>	<u>27,744,857</u>	<u>78,582,589</u>

See accompanying notes to financial statements.

**VERMONT HOUSING FINANCE AGENCY**

Statement of Cash Flows

Year ended June 30, 2006

	<b>Operating Fund</b>	<b>Single Family Mortgage Program Fund</b>	<b>Multi-Family Mortgage Program Fund</b>	<b>Total</b>
Cash flows from operating activities:				
Interest collections on mortgages	\$ 824,246	21,955,686	8,529,143	31,309,075
Principal collections on mortgages	8,088,282	46,008,937	24,362,987	78,460,206
Purchases of mortgages	(5,476,875)	(100,132,801)	(36,994,864)	(142,604,540)
Purchases of down payment assist mortgages	—	(539,972)	—	(539,972)
Fee income and other receipts	779,198	3,282	108,764	891,244
Salaries and benefits payments	(2,811,238)	—	—	(2,811,238)
Operating expense payments	(1,256,943)	—	—	(1,256,943)
Mortgage service fee payments	—	(971,566)	—	(971,566)
Payment on prepaid origination fees	—	(1,513,758)	—	(1,513,758)
Service fee and other payments	—	—	(63,756)	(63,756)
Net cash provided by (used for) operating activities	<u>146,670</u>	<u>(35,190,192)</u>	<u>(4,057,726)</u>	<u>(39,101,248)</u>
Cash flows from investing activities:				
Purchases of investments	—	(3,408,905)	—	(3,408,905)
Proceeds from sales and maturities investments	—	43,085,000	—	43,085,000
Interest received on investments	141,771	6,592,535	1,733,080	8,467,386
Increase (decrease) in escrowed cash deposits	(462,495)	(4,968)	—	(467,463)
Cost of real estate owned	—	(431,208)	—	(431,208)
Proceeds from sales of real estate owned	—	1,429,462	—	1,429,462
Payment to IRS to rebate excess earnings	—	(329,538)	—	(329,538)
Net cash provided by (used for) investing activities	<u>(320,724)</u>	<u>46,932,378</u>	<u>1,733,080</u>	<u>48,344,734</u>
Cash flows from noncapital financing activities:				
Net proceeds from issuance of bonds payable	—	100,450,036	3,700,000	104,150,036
Principal payments on bonds	(7,776)	(74,190,000)	(4,853,118)	(79,050,894)
Interest payments on bonds and notes payable	(724,740)	(21,929,524)	(7,422,319)	(30,076,583)
Proceeds from issuance of notes payable	400,000	30,000,000	14,399,645	44,799,645
Repayment of notes payable	(6,268,348)	(35,000,000)	(3,326,062)	(44,594,410)
Payments to bond insurers	—	(418,414)	(19,588)	(438,002)
Payments for cost of issuance	378,289	(150,911)	(219,410)	7,968
Transfers from (to) other funds	7,113,541	(3,112,195)	(4,001,346)	—
Net cash provided by (used for) noncapital financing activities	<u>890,966</u>	<u>(4,351,008)</u>	<u>(1,742,198)</u>	<u>(5,202,240)</u>
Cash flows from capital related financing activities:				
Purchase of office furniture and fixtures	(71,812)	—	—	(71,812)
Net cash used for capital related financing activities	<u>(71,812)</u>	<u>—</u>	<u>—</u>	<u>(71,812)</u>
Net increase (decrease) in cash and cash equivalents	645,100	7,391,178	(4,066,844)	3,969,434
Cash and cash equivalents at beginning of year	6,873,911	91,510,580	31,885,396	130,269,887
Cash and cash equivalents at end of year	<u>\$ 7,519,011</u>	<u>98,901,758</u>	<u>27,818,552</u>	<u>134,239,321</u>

**VERMONT HOUSING FINANCE AGENCY**

Statement of Cash Flows

Year ended June 30, 2006

	<u>Operating Fund</u>	<u>Single Family Mortgage Program Fund</u>	<u>Multi-Family Mortgage Program Fund</u>	<u>Total</u>
Reconciliation of cash flows from operating activities:				
Operating income (loss)	\$ (3,178,237)	3,678,131	2,809,880	3,309,774
Adjustments to reconcile operating income (loss) to net cash provided by (used for) operating activities:				
Depreciation	152,778	—	—	152,778
Amortization of (premiums) discounts on bonds and notes payable, net	—	49,847	127,016	176,863
Amortization of costs of bond issuance and other fees	—	896,792	66,044	962,836
Gain on loans and real estate owned	—	(26,030)	—	(26,030)
Provision for loan losses	—	(85,495)	—	(85,495)
Loss on bond redemptions	—	169,833	—	169,833
Investment interest income	(155,215)	(6,837,920)	(1,779,421)	(8,772,556)
Bond and note interest expense	716,848	22,321,145	7,429,072	30,467,065
Bond insurance expense	—	422,690	19,604	442,294
Prepaid cost of issuance	(378,289)	—	—	(378,289)
Changes in assets and liabilities:				
Decrease (increase) in mortgage loans receivable	2,611,408	(54,209,361)	(12,631,876)	(64,229,829)
Decrease (increase) in other assets	—	25,454	(23,413)	2,041
Increase in accrued interest receivable	(18,893)	(232,192)	(41,381)	(292,466)
Decrease (increase) in other receivables and prepaid expenses	363,143	(723,608)	878,882	518,417
Decrease in escrow cash deposits	—	—	(912,133)	(912,133)
Increase (decrease) in deferred mortgage origination fees, net	97,985	(262,121)	—	(164,136)
Decrease in accounts payable	(64,858)	(377,357)	—	(442,215)
Net cash provided by (used for) operating activities	\$ <u>146,670</u>	<u>(35,190,192)</u>	<u>(4,057,726)</u>	<u>(39,101,248)</u>
Supplemental noncash operating/investing activities:				
Mortgage loans receivable converted to real estate owned amounted to \$931,630 in fiscal year 2006.				
Supplemental noncash financing activities:				
The fair value of investments decreased \$1,118,366 in fiscal year 2006.				

See accompanying notes to financial statements.

# VERMONT HOUSING FINANCE AGENCY

## Notes to Financial Statements

June 30, 2006

### (1) Authorizing Legislation and Nature of Funds

#### (a) *Authorizing Legislation*

Vermont Housing Finance Agency (the Agency) was created as a body politic and corporate of the State of Vermont by an Act of the General Assembly approved on April 11, 1974 (the Act). The purpose of the Agency is to promote the expansion of the supply of funds available for mortgages on residential housing and to encourage an adequate supply of safe and decent housing at reasonable costs. The Agency is not a component unit of the State of Vermont, but is classified as a related organization of the State of Vermont. The State of Vermont appoints a majority of the Agency's board of commissioners but the State of Vermont is not financially accountable for the Agency.

The Agency is empowered by the Act and subsequent amendments to issue bonds and notes in an amount not to exceed \$900 million outstanding at any one time. Instruments so issued do not constitute a debt or obligation of the State of Vermont and are payable solely from revenues or assets of the Agency.

The State of Vermont has pledged and agreed with the holders of bonds and notes of the Agency not to impair in any way the rights and remedies of such holders.

#### (b) *Basis of Presentation and Nature of Funds*

The financial statements are presented on a program basis, combining the various restricted accounts required by each bond resolution into groups that account for the various bonds issued, related costs of issuance and debt service activity and the investment and related earnings of the bond proceeds in mortgages or loans and temporary investments and the maintenance of certain reserve fund requirements – all under the specific requirements of each resolution.

These accounts are in turn grouped by major fund as described below for the Single Family Mortgage Program fund, the Multi-family Mortgage Program fund, and the unrestricted Operating fund of the Agency.

##### (i) **Operating Fund**

This fund derives its revenue principally from fees, mortgage interest and investment income. Operating expenses of the Agency are paid from this fund.

Transfers from program funds to the Operating Fund represent amounts allowed to be transferred pursuant to the terms of the Agency's bond resolutions.

##### (ii) **Single Family Mortgage Program Fund**

This fund has been established under the Single Family Insured Mortgage Bond Resolution adopted in September 1976, the Single Family Mortgage Purchase Bond Resolution adopted in June 1978, the Home Mortgage Purchase Bond Resolution adopted in July 1983 and the Single Family Housing Bond Resolution adopted in September 1990. Monies from these programs have been used by the Agency to purchase, mortgage loans on single family residential housing units for persons and families of low and moderate income in Vermont.

## VERMONT HOUSING FINANCE AGENCY

### Notes to Financial Statements

June 30, 2006

#### (iii) Multi-Family Mortgage Program Fund

This fund has been established under the Multi-Family Mortgage Bond Resolution adopted in February 1977, the Multi-Family Housing Bond Resolution adopted in September 1981, and various individualized taxable and tax exempt bond resolutions adopted between December 1985 and September 2003. Monies from these programs are used by the Agency to make and finance mortgage loans to sponsors of multi-family residential housing units for persons and families of low and moderate income within the State of Vermont.

#### (iv) Reserve Requirements

Under various bond resolutions of the Agency, certain amounts from bond proceeds are required to be set aside and maintained for potential debt service requirements in trusteed accounts. As of June 30, 2006, reserve requirements totaled \$16,164,857 for the Single Family Mortgage Programs and \$10,692,388 for the Multi-Family Mortgage Programs. Amounts held in reserve accounts as of June 30, 2006 exceeded the required balances in all cases.

### (2) Summary of Significant Accounting Policies

#### (a) Basis of Accounting

The Agency's financial statements have been prepared on the accrual basis of accounting using the economic resource management focus. Accordingly, the Agency recognizes revenue in the period earned and expenses in the period incurred.

As permitted under Governmental Accounting Standards Board (GASB) Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that Use Proprietary Fund Accounting*, the Agency has elected not to apply Statements of Financial Accounting Standards issued after November 30, 1989.

#### (b) Net Assets

In accordance with GASB Statement No. 34, *Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments*, the Agency's net assets have been classified for external financial reporting purposes into the following three net asset categories:

- **Invested in Capital Assets:** Capital assets, net of accumulated depreciation, and cost of construction or improvement of those assets.
- **Restricted:** Net assets subject to externally imposed stipulations, including those for excess yield loans.
- **Unrestricted:** Net assets that are not subject to externally imposed stipulations. Unrestricted net assets may be designated for specific purposes by action of management or the Board of Commissioners or may otherwise be limited by contractual agreements with outside parties.

## VERMONT HOUSING FINANCE AGENCY

### Notes to Financial Statements

June 30, 2006

(c) ***Cash Equivalents***

The Agency considers all highly liquid investments, including investment agreements with insurance companies, with original maturities of three months or less to be cash equivalents for purposes of the statement of cash flows. Cash equivalents also includes mortgage payments which are in transit to the trustee to be invested in collateralized repurchase agreements.

(d) ***Mortgage Loans Receivable***

Mortgage loans receivable are carried at their uncollected principal balances less an allowance for loan losses on mortgages. The loan loss allowances are established based on historical loss experience. Future additions to the allowance may be necessary based on changes in economic conditions. At June 30, 2006, the allowance for loan losses totaled \$96,882, relating to Single Family mortgage loans, \$1,500,000 for Multi-Family mortgage loans and \$2,669,756 for operating fund mortgage loans.

Included in Multi-Family mortgage loans receivable is approximately \$9.8 million of mortgages funded by excess yield. The Agency estimates that it may be required to forgive or restructure up to this amount of its loans prior to the final maturity of the related 1995 and 1999 bond issues, in order to be in compliance with Federal tax laws.

(e) ***Investments***

Investments are comprised of short-term investments other than cash equivalents that mature in one year or less, and long-term investments with maturities in excess of one year. The Agency follows the provisions of GASB No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*. GASB No. 31 requires investments to be reported at fair value in the statement of net assets. The net decrease in the fair value of investments, including both realized and unrealized gains and losses, is recognized in the statement of revenues, expenses, and changes in net assets. Fair values of guaranteed investment contracts (GICs) are recorded at contract value. Fair values of all other investments are based upon quoted market prices.

(f) ***Depreciation***

The Agency records purchases of its capital assets at cost and depreciates that cost over the estimated useful lives of the assets, which are forty years for the building and three to five years for furniture and fixtures, using the straight-line method.

(g) ***Amortization***

Costs of bond issuance, which represents underwriters' fees and legal costs are deferred and amortized over the lives of the respective issues using the straight-line method. Bond discounts and premiums are amortized using the effective interest method over the life of the bonds.

The difference between the reacquisition price and net carrying amount of defeased bonds is deducted from, or added to the refunding debt liability and amortized on the straight-line method over the shorter of the maturity of the new debt or the defeased debt.

## VERMONT HOUSING FINANCE AGENCY

### Notes to Financial Statements

June 30, 2006

**(h) *Income Tax Status***

The Agency is exempt from Federal and state income taxes.

**(i) *Deferred Loan Origination Fees and Costs***

In accordance with SFAS No. 91, *Accounting for Nonrefundable Fees and Cost Associated with Origination or Acquiring Loans and Initial Direct Costs of Leases*, loan origination fees and certain related costs are deferred and amortized over the estimated lives of the respective loans.

**(j) *Arbitrage to be Rebated***

Bonds issued by the Agency are subject to a variety of Internal Revenue Service (IRS) regulations which limit the amount of income which may be earned with nonmortgage investments to an amount not greater than that amount which would have been earned had the funds been invested at the yield on the bonds as defined by the IRS. Excess earnings must be rebated every five years.

**(k) *Operating and Nonoperating Revenues and Expenses***

The Agency records all revenues and expenses related to its Single Family and Multi-Family loan programs as operating revenues and expenses since they are generated from the Agency's daily operations needed to carry out its statutory purposes. Investment income is recorded as operating revenue in all funds.

**(l) *Use of Estimates***

The preparation of the financial statements in conformity with U.S. generally accepted accounting principles requires estimates and assumptions that affect the reported amount of the assets and liabilities and contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Significant items subject to estimates and assumptions include the provision for loan losses and the valuation of investments.

**(3) *Cash, Cash Equivalents and Investments***

For mortgage program investments, bond resolution requirements mandate specific classes of investment vehicles. Qualified investments are: direct obligations of the United States of America; obligations unconditionally guaranteed by the United States of America; indebtedness issued by certain Federal agencies; bank time deposits evidenced by certificates of deposits insured by the Federal Depository Insurance Corporation (FDIC) and, if in excess of insured limits, collateralized in full by the aforementioned Federal government investments; obligations of the State of Vermont, and/or Federal or state insured mortgages; collateralized repurchase agreements secured by obligations of the Federal government; GICs with the collateral held by or at the direction of the appropriate trustee; and, investment agreements with banks or bank holding companies rated in the top categories by nationally recognized rating agencies.

The Agency has an investment policy with an overriding goal of providing optimum coverage of risk exposure and maintaining liquidity necessary for future cash needs while maximizing the return on investments. All investment agreements with banks or bank holding companies, insurance companies or

## VERMONT HOUSING FINANCE AGENCY

### Notes to Financial Statements

June 30, 2006

other financial institutions must be rated at least “A” by nationally recognized credit rating agencies. All bonds are issued by U.S. Government agencies such as FNMA, FHLMC and FHLB, and have implied credit ratings of AAA.

**(a) Custodial Credit Risk – Deposits**

The custodial credit risk for deposits is the risk that in the event of a bank failure, the Agency’s deposits may not be recovered. The deposits in the bank in excess of the insured amount are uninsured and uncollateralized. The deposits (including certificates of deposit) at June 30, 2006, were \$4.5 million. Of these, \$2.6 million were exposed to custodial credit risk as uninsured and uncollateralized.

**(b) Investments**

The Agency’s investments at June 30, 2006 are presented below.

**Investments by Type**

June 30, 2006

(Expressed in thousands)

Investment type	Fair value	Investment maturities (in years)			
		Less than 1	1-5	6-10	More than 10
Certificate of deposit	\$ 100	100	—	—	—
Guaranteed investment contracts	34,706	15,000	—	2,303	17,403
U.S. Treasury securities	6,213	—	—	1,019	5,194
Government agency securities	5,611	—	546	3,845	1,220
Common stock	1,376	—	—	—	—
	\$ 48,006				

**(c) Concentration of Credit Risk**

Concentration of credit risk is the risk of loss attributable to the magnitude of the Agency’s investment in a single issuer. More than 5% of the Agency’s investments are invested in guaranteed investment contracts; Trinity Plus, AIG, Transamerica, Bayern LB, and CDC Funding. These investments are 31.3%, 9.4%, 7.0%, 5.8%, and 5.5%, respectively, of the Agency’s total investments. The Agency does not have a formal investment policy that limits the amount invested in a single issue.

**(d) Interest Rate Risk – Investments**

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The Agency does not have a formal policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

**VERMONT HOUSING FINANCE AGENCY**

Notes to Financial Statements

June 30, 2006

**(4) Mortgage and Construction Loans Receivable**

**(a) *Single Family Mortgage Loans Receivable***

Single Family mortgage loans earn interest at annual rates ranging predominantly from 5.30% to 10.5%. Mortgage payments are received monthly by the Agency from which a service fee is generally retained by servicing lenders and the subservicer.

At June 30, 2006, approximately 75% of the Single Family mortgage portfolios consist of primary insured mortgages.

Conventional mortgage loans, not requiring primary insurance, are limited to 75% of the appraised value of the property.

**(b) *Multi-Family Mortgage Loans and Construction Loans Receivable***

Multi-Family mortgage loans receivable earn interest at annual rates ranging predominantly from 4.5% to 14%, and are collateralized by first mortgage liens on all real and personal property of the mortgaged premises. As of June 30, 2006, \$188,480 of the Multi-Family mortgage loans receivable under the Multi-Family Housing Program were financed from funds transferred from the Agency's Operating Fund.

**(5) Real Estate Owned**

Real estate owned at June 30, 2006 consists of properties held pending sale as a result of foreclosure by the Agency. Real estate owned is carried at the lower of cost or fair value less estimated costs to sell. A valuation allowance has been established to account for the reduction in value of properties held. At June 30, 2006, the valuation allowance totaled \$63,962.

**(6) Escrowed Cash Deposits**

Escrowed cash deposits are received primarily from multi-family housing developers at the time the Agency makes permanent mortgage loans. Escrowed deposits are governed by agreements, and released upon satisfactory compliance with their terms.

**(7) Bonds Payable**

All bonds payable are general or special obligations of the Agency and are collateralized by the operating revenues, loans, funds and investments pledged pursuant to the respective bond resolutions. Interest is payable semi-annually. All bonds are subject to redemption after various dates at prices ranging from 100% to 103% of par value.

**VERMONT HOUSING FINANCE AGENCY**

Notes to Financial Statements

June 30, 2006

Outstanding bonds payable at June 30, 2006 are as follows (in thousands):

A.	Single Family Mortgage Program Fund:		
	Home Mortgage Purchase Program:		
	1989 Series B, maturing 2006 to 2009, interest at 7.45%	\$	<u>2,390,000</u>
	Housing Program:		
	Series 7, maturing 2006 to 2031, interest at 5.5% to 6.3%		12,005,000
	Series 8, maturing in 2031, interest at 6.05%		5,890,000
	Series 9, maturing 2006 to 2037, interest at 4.35% to 5.4%		19,025,000
	Series 10, maturing 2006 to 2030, interest at 4.15% to 5.25%		11,100,000
	Series 11, maturing 2006 to 2030, interest at 4.85% to 5.95%		4,840,000
	Series 12, maturing 2006 to 2031, interest at 5.2% to 6.4%		5,260,000
	Series 13, maturing 2006 to 2031, interest at 4.85% to 5.97%		10,995,000
	Series 14, maturing 2007 to 2032, interest at 4.2% to 6.05%		14,395,000
	Series 15, maturing 2006 to 2032, interest at 3.85% to 5.7%		18,510,000
	Series 16, maturing 2007 to 2033, interest at 4.2% to 5.6%		42,630,000
	Series 17, maturing 2007 to 2034, interest at 2.7% to 5.1%		26,020,000
	Series 18, maturing 2007 to 2034, interest at 2.25% to 4.95%		28,145,000
	Series 19, maturing 2006 to 2035, interest at 1.8% to 5.0%		29,275,000
	Series 20, maturing 2006 to 2035, interest at 2.65% to 5.5%		29,945,000
	Series 21, maturing 2006 to 2035, interest at 1.9% to 5.0%		44,495,000
	Series 22, maturing 2006 to 2035, interest at 2.95% to 5.0%		41,915,000
	Series 23, maturing 2006 to 2035, interest at 2.95% to 5.0%		58,410,000
	Series 24, maturing 2007 to 2036, interest at 3.6% to 5.0%		<u>41,960,000</u>
	Total Housing Program		<u>444,815,000</u>
	Total Single Family Mortgage Program Fund		<u>447,205,000</u>
B.	Multi-Family Mortgage Program Fund:		
	Mortgage Program:		
	1999 Series A, maturing 2007 to 2020, interest at 4.35% to 5.125%		3,915,000
	1999 Series B, maturing 2007 to 2030, interest at 5.0% to 6.0%		3,775,000
	1999 Series C and D, maturing 2007 to 2021, interest at 4.9% to 5.8%		25,525,000
	2000 Series A, maturing in 2039, interest at 5.9%		5,080,000
	2000 Series B, C, and D, maturing 2014 to 2031, interest at 5.65% to 6.7%		2,815,000
	2001 Series A, B, C, and D, maturing 2031 to 2032, interest at 5.4% to 7.27%		5,355,000
	2002 Series A and B, maturing 2006 to 2039, interest at 3.8% to 7.2%		11,865,000
	2003 Series A, maturing 2023 to 2043, interest at 5.05% to 5.25%		4,280,000
	2003 Series C, maturing 2007 to 2034, interest at 2.4% to 5.1%		10,715,000
	2004 Series A, B, and C, maturing 2006 to 2046, interest at 2.6% to 6.3%		14,650,000
	2004 Series D, maturing 2024 to 2039, interest at 4.65% to 4.9%		2,780,000
	2005 Series A, B, C, and D, maturing 2015 to 2035, interest at 4.4% to 5.75%		<u>4,450,000</u>
	Total Mortgage Program		<u>95,205,000</u>

**VERMONT HOUSING FINANCE AGENCY**

Notes to Financial Statements

June 30, 2006

Housing Program:	
1995 Series A, maturing 2007 to 2014, interest at 5.65% to 6.15%	\$ 12,565,000
1997 Series A, maturing 2007 to 2029, interest at 4.9% to 5.75%	<u>5,395,000</u>
Total	<u>17,960,000</u>
Direct Placement Program:	
Northgate Housing Program:	
Eleven series of bonds, issued December 1989, maturing 2006 to 2031, interest at 7.085% to 9.23%	6,728,797
Highgate Housing Program:	
Two series of bonds, issued May 1991, maturing 2006 to 2031, interest at 6.45% to 7.741%	1,503,991
Pine Meadow Development Bond:	
Taxable bond, issued July 1991, maturing 2007 to 2016, interest at 6%	370,500
Whitney Hill Housing Development Bond:	
Taxable bond, issued January 1992, maturing 2006 to 2007, interest at 9%	1,056,800
Kilbourn Mobile Home Park Bond:	
Taxable bond, issued May 1996, maturing 2006 to 2016, interest at 7.5%	210,400
Black River Overlook Housing Project Bond:	
Taxable bond, issued September 1998, maturing 2006 to 2018, interest at 8%	273,290
T.D. Banknorth Borrowing – Chittenden Housing Corp. Bond:	
Issued June 2006, maturing 2006 to 2012, interest at 5.41%	<u>3,700,000</u>
Total Direct Placement Programs	<u>13,843,778</u>
Total Multi-Family Mortgage Program Fund	<u>127,008,778</u>
C. Operating Fund:	
Northgate Housing Site Acquisition, issued December 1989, maturing 2006 to 2031, interest at 7%	<u>571,402</u>
Total bonds payable	<u>\$ 574,785,180</u>

\* All calendar year 2006 maturities on bonds payable occur after June 30, 2006.

In 2006, the Agency issued Single Family Housing Series 23 and Series 24 bonds for a total of \$104.4 million. The proceeds were used to finance Single Family Mortgage loans and refund \$5.5 million in Single Family Housing Series 5 and \$11.1 million of Single Family Housing Series 6 bonds. The current refunding resulted in a difference between the reacquisition price and the net carrying amount of the old debt of approximately \$331,000. This difference is being charged to operations through the year 2031, using the effective interest method. The bonds were refunded to reduce total debt service payments over the next thirty years by approximately \$6.3 million and to obtain an economic gain of approximately \$1.5 million.

**VERMONT HOUSING FINANCE AGENCY**

Notes to Financial Statements

June 30, 2006

Future maturities on bonds payable as of June 30, 2006 are as follows (in thousands):

	Multi-Family Mortgage Programs					
	Mortgage Program		Housing Program		Direct Placement Programs	
	Principal	Interest	Principal	Interest	Principal	Interest
Year ending June 30:						
2007	\$ 2,600	5,155	1,630	1,068	1,504	951
2008	2,785	5,030	1,730	976	478	823
2009	2,915	4,894	1,845	871	518	786
2010	3,060	4,749	1,960	759	475	749
2011	3,230	4,592	2,085	640	461	712
2012-2016	17,290	20,239	4,825	1,677	4,586	2,610
2017-2021	20,450	15,040	1,155	989	2,181	1,652
2022-2026	10,510	10,585	1,555	617	1,415	1,089
2027-2031	13,345	7,345	1,175	138	2,014	485
2032-2036	12,930	3,576	—	—	212	6
2037-2041	5,175	880	—	—	—	—
2042-2046	840	128	—	—	—	—
2047	75	2	—	—	—	—
Total	\$ 95,205	82,215	17,960	7,735	13,844	9,863

	Single Family Mortgage Programs							
	Home Mortgage Purchase Program		Housing Program		Operating Fund		Agency Totals	
	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest
Year ending June 30:								
2007	\$ 620	167	7,935	21,129	8	40	14,297	28,510
2008	665	120	9,465	20,770	9	39	15,132	27,758
2009	725	69	10,175	20,398	10	39	16,188	27,057
2010	380	14	10,270	19,981	10	38	16,155	26,290
2011	—	—	10,630	92,551	63	179	16,469	98,674
2012-2016	—	—	61,435	77,099	88	154	88,224	101,779
2017-2021	—	—	78,030	57,433	123	118	101,939	75,232
2022-2026	—	—	86,690	35,383	173	69	100,343	47,743
2027-2031	—	—	98,245	11,736	87	9	114,866	19,713
2032-2036	—	—	70,325	284	—	—	83,467	3,866
2037-2041	—	—	1,615	—	—	—	6,790	880
2042-2046	—	—	—	—	—	—	840	128
2047	—	—	—	—	—	—	75	2
Total	\$ 2,390	370	444,815	356,764	571	685	574,785	457,632

A summary of bonds payable, discount on bonds, and premium on bonds and arbitrage rebate payable activity for the year ended June 30, 2006 is as follows (in thousands):

	Balance at June 30, 2005	Increases	Decreases	Balance at June 30, 2006	Amounts due within one year	Amounts due thereafter
Bonds payable	\$ 549,396	104,440	(79,051)	574,785	14,297	560,488
Discount on bonds	(5,442)	(782)	643	(5,581)	(297)	(5,284)
Premium on bonds	2,852	1,032	(514)	3,370	124	3,246
Arbitrage rebate payable	182	218	(330)	70	—	70

**VERMONT HOUSING FINANCE AGENCY**

Notes to Financial Statements

June 30, 2006

The Agency has entered into interest rate swap agreements with counterparties in connection with the Single Family Housing Bonds Variable Rate Demand Bonds (VRDB) and Auction Rate Certificates (ARC) in order to obtain a synthetic fixed interest rate at a cost expected to be less than that associated with variable rate debt. Under the swap agreement, the swap provider pays the Agency an amount based on the London InterBank Offered Rate (LIBOR) or the Bond Market Association Index (BMA), and the Agency pays the swap provider an amount at a fixed rate of interest.

A summary of the agreements follows:

<u>Issue</u>		<u>Effective date</u>	<u>Face amount</u>	<u>Termination date</u>	<u>Termination option date</u>	<u>Fixed swap payment rate</u>	<u>Variable receivable rate</u>	<u>Fair value at June 30, 2006</u>
Series 17	VRDB	5/1/2004	\$ 7,590,000	5/1/2019	—	3.182%	70% of LIBOR	\$ 244,509
Series 19	ARC	4/8/2004	7,850,000	11/1/2027	—	3.492%	70% of LIBOR	259,571
Series 20	ARC	8/12/2004	7,900,000	5/1/2028	11/1/2014	4.166%	70% of LIBOR	(7,356)
Series 21	VRDB	11/30/2004	11,500,000	5/1/2029	—	3.682%	BMA + .10% (if LIBOR ≤ 3.00%) 68% of LIBOR (if LIBOR > 3.00%)	176,772
Series 22	VRDB	6/8/2005	13,800,000	11/1/2034	5/1/2012	3.731%	65% of LIBOR	466,449
Series 23	VRDB	10/26/2005	14,500,000	11/1/2034	11/1/2014	3.569%	65% of LIBOR + 0.28%	587,002
Series 24	VRDB	4/19/2006	10,440,000	11/1/2036	5/1/2015	3.973%	65% of LIBOR + .28%	82,214
								<u>\$ 1,809,161</u>

By using derivative financial instruments to hedge exposures to changes in interest rates, the Agency exposes itself to credit and market risk. Credit risk is the failure of the counter-party to perform under the terms of the derivative contract. When the fair value of a derivative contract is positive, the counter-party owes the Agency, which creates credit risk for the Agency. When the fair value of a derivative contract is negative, the Agency owes the counter-party and, therefore, it does not possess credit risk. The Agency minimizes its credit risk in derivative instruments by entering into transactions with high-quality counter-parties whose credit rating is higher than Aa. Market risk is the adverse effect on the value of a financial instrument that results from a change in interest rates. The market risk associated with interest rates is managed by establishing and monitoring parameters that limit the types and degree of market risk that may be undertaken.

**(8) Notes Payable**

The Agency may borrow from the Federal Home Loan Bank (FHLB) in an amount not to exceed assets pledged to the FHLB. As of June 30, 2006, the Agency had outstanding borrowings totaling \$6,256,701 which are secured by investments and mortgage loans with a carrying value of \$7,433,203. These borrowings have interest rates ranging from 6.32% to 7.66% and mature through November 2018.

**VERMONT HOUSING FINANCE AGENCY**

Notes to Financial Statements

June 30, 2006

The Agency is operating under unsecured variable rate lines of credit that total \$57,500,000 with lending institutions expiring in 2007. At June 30, 2006, there was a \$14,268,583 balance outstanding at 4.61% to 6.275%. The lines of credit were entered into in order to fund working capital, and to be used for specific construction projects financed by the Agency.

The Agency has a \$500,000 note payable to the Vermont Community Foundation at a rate of 4%, maturing in November 2006.

As of June 30, 2006, the Agency had \$45,000,000 of notes payable in the Single Family Housing Program fund. These notes have interest rates ranging from 3.35% to 3.80% and mature between April 2007 and November 2007. The proceeds of these notes are invested in guaranteed investment contracts.

Future maturities on notes payable and line of credit borrowings as of June 30, 2006 are as follows (in thousands):

	<b>Operating Fund</b>		<b>Single Family Housing Program</b>		<b>Multi Family Direct Placement Program</b>		<b>Agency totals</b>	
	<b>Principal</b>	<b>Interest</b>	<b>Principal</b>	<b>Interest</b>	<b>Principal</b>	<b>Interest</b>	<b>Principal</b>	<b>Interest</b>
Year ending June 30:								
2007	\$ 3,847	528	15,000	1,675	11,073	292	29,920	2,495
2008	163	427	30,000	570	—	—	30,163	997
2009	175	415	—	—	—	—	175	415
2010	313	401	—	—	—	—	313	401
2011	195	387	—	—	—	—	195	387
2012-2016	1,289	1,616	—	—	—	—	1,289	1,616
2017-2020	3,970	317	—	—	—	—	3,970	317
Total	\$ 9,952	4,091	45,000	2,245	11,073	292	66,025	6,628

A summary of line of credit borrowings and notes payable activity for the year ended June 30, 2006 is as follows (in thousands):

	<b>Balance at June 30, 2005</b>	<b>Increases</b>	<b>Decreases</b>	<b>Balance at June 30, 2006</b>	<b>Amounts due within one year</b>	<b>Amounts due thereafter</b>
Line of credit borrowings	\$ 9,328	13,546	(8,606)	14,268	14,268	—
Notes payable	56,492	30,400	(35,135)	51,757	15,652	36,105
	\$ 65,820	43,946	(43,741)	66,025	29,920	36,105

**(9) Asset Restrictions**

Pursuant to the Act and agreements with bondholders and other parties, the Agency's assets are pledged to secure specific obligations or are otherwise restricted.

Programs which are financed by the issuance of bonds are accounted for separately in accordance with each of the general bond resolutions. Program assets and revenues are pledged to bondholders. Revenues in excess of required amounts are available to be transferred to the Operating Fund.

## VERMONT HOUSING FINANCE AGENCY

### Notes to Financial Statements

June 30, 2006

Amounts transferred to the Operating Fund from the bond resolutions are free and clear of any lien or pledge created by the bond resolutions, and may be used for any lawful purpose under the Act, including payments to various accounts within the bond resolutions. All of the outstanding bonds, except for the Single Family Housing Bonds, are general obligations of the Agency. For general obligation bonds, the Agency covenants that it will restore deficiencies to the bond programs, as defined by the bond resolutions, from the Operating Fund.

The Operating Fund is also the primary source to pay administrative expenses in connection with current and future housing programs, and to provide collateral for credit agreements.

#### **(10) Pension Plan**

Upon meeting certain eligibility requirements, the Agency's employees are eligible to participate in the Vermont Housing Finance Agency 401(k) Plan, a noncontributory defined contribution pension plan, in accordance with the provisions of the Employee Retirement Income Security Act of 1974. For the year ended June 30, 2006, the Agency had a total payroll of \$2,043,225, of which \$2,016,920 was covered by the pension plan. The Agency's contribution to the Plan is 10% of the covered payroll. Employees vest in benefits under the Plan at 20% per year of service and are fully vested after five years. Forfeitures of nonvested benefits by terminated employees reduce the Agency's contribution. The cost of the plan was \$201,692 for the year ended June 30, 2006, and is included in salaries and benefits expense.

#### **(11) Loss on Bond Redemptions**

During the year ended June 30, 2006, the Agency redeemed \$51,705,000 of its Single-Family Housing Program Bonds. Loss on bond redemptions of \$169,833 was recognized which represents the unamortized balance of bond discount and cost of issuance expenses associated with the bonds retired.

**VERMONT HOUSING FINANCE AGENCY**

Notes to Financial Statements

June 30, 2006

The following is a summary of the redeemed bonds (in thousands):

	<b>Single Family Housing Program</b>
Series 5	\$ 2,010,000
Series 6	4,320,000
Series 7	2,450,000
Series 8	2,110,000
Series 9	5,625,000
Series 10	3,635,000
Series 11	1,715,000
Series 12	2,185,000
Series 13	2,460,000
Series 14	3,980,000
Series 15	2,360,000
Series 16	7,880,000
Series 17	2,940,000
Series 18	2,295,000
Series 19	1,915,000
Series 20	1,630,000
Series 21	1,780,000
Series 22	45,000
Series 23	370,000
	<hr/>
	\$ 51,705,000

**(12) Commitments and Contingencies**

At June 30, 2006, the Agency had outstanding commitments in the amount of \$20,230,353 to purchase or finance mortgage loans pursuant to its normal funding from bond proceeds. In addition, there were commitments of \$17,700,000 for general loans or future program subsidy purposes.

Under the Single Family Mortgage Programs, the Agency has obtained surety bonds in the amount of \$25,442,078 expiring between 2025 and 2037, which satisfy the requirements of certain bond resolutions.

**(13) Risk Management**

The Agency is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; errors; and omissions; injuries to employees; employees' health; and natural disasters. The Agency manages these risks through a combination of participating in the State self-insurance program and purchasing commercial insurance packages in the name of the Agency. The Agency has not experienced settled claims resulting from these risks which have exceeded its insurance coverage. In addition, the Agency's bylaws provide for the indemnification of Agency commissioners and officers by the Agency. This indemnification requirement is supported by various statutes related to claims against employees and entities of the State and the Agency's authorizing legislation which includes the benefit of sovereign immunity.

**VERMONT HOUSING FINANCE AGENCY**

Notes to Financial Statements

June 30, 2006

**(14) Subsequent Event**

In July 2006, the Agency issued \$51,780,000 of bonds and \$20,000,000 of notes under the Single Family Housing Bonds, Series 25A and 25B. The bond proceeds will be used to purchase single family mortgages, while the note proceeds will be invested in guaranteed investment contracts.