VERMONT HOUSING FINANCE AGENCY

(A Component Unit of the State of Vermont)

Financial Statements and
Required Supplementary Information

June 30, 2016

(With Independent Auditor's Report Thereon)

COHN REZNICK

ACCOUNTING • TAX • ADVISORY

VERMONT HOUSING FINANCE AGENCY
(A Component Unit of the State of Vermont)

Table of Contents

Independent Auditor's Report

The Honorable Douglas R. Hoffer
State Auditor of the State of Vermont
and
The Commissioners
Vermont Housing Finance Agency

Report on the Financial Statements

We have audited the accompanying financial statements of the business-type activities of the Vermont Housing Finance Agency (the Agency), component unit of the State of Vermont, as of and for the year ended June 30, 2016, and the related notes to the financial statements, which collectively comprise the Agency's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

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 and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Agency, as of June 30, 2016, the changes in financial position and cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 2 to the financial statements, Vermont Housing Finance implemented GASB No. 72, *Fair Value Measurement and Application.*

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3 through 9 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated September 30, 2016 on our consideration of the Agency's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Agency's internal control over financial reporting and compliance.

CohnReznick LLP

Baltimore, Maryland
September 30, 2016

VERMONT HOUSING FINANCE AGENCY
(A Component Unit of the State of Vermont)

Management's Discussion and Analysis
(Unaudited)

June 30, 2016

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 the fiscal year ended June 30, 2016. 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. 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, and advances from lending institutions. Since September 1974, the Agency has issued approximately $3.4 billion of bonds and notes, of which $447.0 million was outstanding as of June 30, 2016, 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 backed securities (MBS) or mortgage loans on Single Family residential housing units for persons and families of low and moderate income in the State, and to make loans to finance 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 Position, Statement of Revenues, Expenses and Changes in Net Position 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 Position

The Agency's Statement of Net Position consists primarily of Single Family and Multi-Family mortgage loans, mortgage backed securities (MBS), cash and investments, and related bonds and notes payable. It also includes a portfolio of mortgage and construction loans financed through its Operating Fund, as well as a variety of other assets such as capital assets, other receivables, and real estate owned.

Cash and investments are used to fund loan and MBS 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.

The following table summarizes the Net Position of the Agency as of June 30, 2016 with comparative data from the prior fiscal year (in thousands)

	2016	2015	Percentage change
Assets:			
Cash and investments	$ 73,894	76,755	(3.7)%
Loans receivable, net	289,799	309,976	(6.5)
Mortgage backed securities	173,485	151,422	14.6
Other assets	6,388	8,062	(20.8)
Total assets	543,566	546,215	(0.5)
Deferred Outflows of Resources:			
Interest rate swap agreements	3,375	5,332	(36.7)
Liabilities:			
Bond and notes payable	447,007	458,114	(2.4)
Other liabilities	11,100	12,790	(13.2)
Total liabilities	458,107	470,904	(2.7)
Net position:			
Invested in capital assets	632	712	(11.2)
Restricted for bond resolutions	82,278	75,833	8.5
Restricted for down payment assistance	592	—	—
Unrestricted	5,332	4,098	30.1
Total net position	$ 88,834	80,643	10.2%

Total assets decreased by $2.65 million or 0.5% for the fiscal year ended June 30, 2016 when compared to the year ended June 30, 2015. The change in assets is primarily the net result of:

- Overall cash and investments decreased by $2.86 million or 3.7% from June 30, 2015. The overall decrease in cash and investments is mostly related to a higher level of redemptions of Multiple Purpose and Mortgage Revenue bonds in FY 2016. There was a lower balance of unexpended proceeds from bonds issued in FY 2016 vs. FY 2015. Another factor is the timing of collections from outstanding mortgages.

- Mortgage loans receivable decreased a net of $20.18 million or 6.5% due mainly to the collection of outstanding mortgages. Because almost all Single Family mortgages are now being securitized as mortgage backed securities or sold, as existing mortgages pay down they will not be backfilled with new loans. However, the balance in mortgage backed securities will increase. Total loan originations in the fiscal year were $95.59 million (compared to $68.81 million the previous year), which includes $33.44 million of loans originated using MBS and $22.8 million using the To-Be-Announced (TBA) securities market program.

- Mortgage backed securities increased by $22.06 million due mainly to the increase in the production of securitized Single Family loans.

- A net increase in loans receivable and mortgage backed securities of $1.89 million, due primarily to an increase in new Multi-Family loan activity.

The following table summarizes the change in net mortgage loans receivable for the years ended June 30, 2016 and 2015 (dollars in thousands):

	2016	2015	Percentage change
Beginning balance	$ 309,976	334,755	(7.4)%
Whole loan originations	38,882	26,294	47.9
Down Payment Assistance loans	475	—	—
Principal collections	(57,507)	(48,002)	19.8
Loans transferred to REO status	(2,200)	(3,108)	(29.2)
Loan loss provision	173	37	367.6
Ending balance	$ 289,799	309,976	(6.5)%

The following table summarizes the change in mortgage backed securities for the year ended June 30, 2016 (in thousands):

	2016
Beginning balance	$ 151,422
MBS Purchases	33,439
Premium on MBS Purchases	229
MBS Principal Paydowns	(16,052)
TBA Purchases	22,795
Premium on TBA Purchases	269
TBA Sold	(23,374)
Gain on TBA Sold	310
Amortization of discount	23
Appreciation in fair value	4,424
Ending balance	$ 173,485

Total liabilities of the Agency decreased by $12.80 million or 2.72% for the fiscal year ended June 30, 2016 when compared to the year ended June 30, 2015, primarily the net result of the following:

- In September 2015, the Agency issued $25.9 million of Multiple Purpose Bonds. The proceeds of the Multiple Purpose Series 2015 F and G sale were used to purchase approximately $15.1 million in mortgage backed securities and to refund $10.6 million in Single Family Housing Bonds Series 25.

- In February 2016, the Agency issued $29.6 million of Multiple Purpose Bonds. The proceeds of the Multiple Purpose Series 2016 A and B sale will be used to purchase approximately $15.1 million in mortgage backed securities and to refund $14.3 million in Single Family Housing Bonds Series 26.

- Total principal payments on bonds were $86.7 million:

  - Bonds redeemed prior to maturity as a result of mortgage loan prepayments were $50.8 million including $9.8 million Single Family Housing Bonds, $31.6 million in Multiple Purpose Bonds, $8.9 million Mortgage Revenue Bonds and $0.5 million in Multi-Family Mortgage Bonds.

  - Single Family Housing Bonds redeemed as a result of refunding were $24.9 million.

  - Bonds redeemed as result of scheduled maturities were $11.0 million.

- The Agency saw a significant increase in notes payable due to a spike in multi-family construction loan activity, which are financed by lines of credit at local banks. The net increase in notes payable was $19.4 million.

Discussion of Changes in Statement of Revenues, Expenses and Changes in Net Position

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.

The following summarizes the changes for the fiscal year ended June 30, 2016 with comparative data from the prior fiscal year (in thousands):

	2016	2015	Percentage change
Operating revenues:			
Interest on investments	$ 1,188	1,446	(17.8)%
Interest on mortgage loans	16,728	18,636	(10.2)
Interest on mortgage backed securities	5,168	5,063	2.1
Fee income	987	840	17.5
Sales of state tax credits	594	—	—
Gain on sales of loans and securities	310	404	(23.3)
Gain on bond redemptions	501	324	54.6
Other revenue, net	16	103	(84.5)
Total operating revenues	25,492	26,816	(4.9)
Operating expenses:			
Financing costs	16,508	18,580	(11.2)
Mortgage servicing expenses	342	397	(13.9)
Operational expenses	4,482	4,270	5.0
Loan loss expenses, net	804	1,065	(24.5)
Total operating expenses	22,136	24,312	(9.0)
Operating income	3,356	2,504	34.0
Nonoperating revenues (expenses):			
Net appreciation in fair value of investments	4,080	1,006	305.6
Other nonoperating revenue	755	—	—
Federal programs:			
Program revenue	2,854	3,583	(20.3)
Program expenses	(2,795)	(3,476)	(19.6)
Administration and period costs	(59)	(107)	(44.9)
Total nonoperating revenues	4,835	1,006	380.6
Increase in net position	$ 8,191	3,510	133.4%

The Agency's net operating income was $3.36 million for the fiscal year ended June 30, 2016, compared to a net operating income of $2.5 million for the fiscal year ended June 30, 2015. When net non-operating revenues are included, the overall increase in net position for the fiscal year ended June 30, 2016 was $8.19 million compared with a net increase in net position in the previous fiscal year of $3.51 million (due mainly to the difference in net appreciation in fair value of investments).

Income and expense highlights include:

- Interest income on loans and mortgage backed securities decreased by $1.8 million (7.6%) reflecting the effect of net portfolio runoff and the reduced spread on the whole loans converted to MBS.

- Interest income on investments decreased by $258 thousand (17.8%). A contributor to this decrease was the termination of older high-interest guaranteed investments contracts (GIC's) that could not be replaced in the current low interest rate market. The Agency also converted some Cash Reserves to Certificates of Deposit and used other Cash Reserves to pay down bonds.

- Fee income increased $147 thousand due primarily to an increase in loan origination fees and loan prepayment fees.

- Gain on sale of loans and securities dropped by 23.3% and includes $310 thousand from the gain on sale of securities under the TBA program. The TBA program was not used as much in FY 2016 because the Agency was able to issue bonds.

- Financing costs decreased $2.07 million (11.2%) relative to the prior year due to the net reduction in outstanding bonds and notes payable of $11.11 million and the reduction of interest rates and remarketing fees paid on a smaller variable rate debt portfolio due to economic bond refundings. Financing Costs include significant one-time expenses incurred and recorded at the time of bond closings, a change implemented with the adoption of GASB 65 in FY 2015. Under GASB 65 bond closing costs now have to be expensed, rather than capitalized and amortized as in the past. In FY 2016 the bond closing costs expensed were $712.25 thousand related to the closing of Multiple Purpose 2015 FG and Multiple Purpose 2016 AB. In FY 2015, the bond closing costs expensed were $959.77 thousand related to the closing of Multiple Purpose 2014 ABC and Multiple Purpose 2015 ABCD. The total net decrease in one-time closing expenses from FY 2015 to FY 2016 was $247 thousand.

- Operational expenses were reported at $4.48 million, up $212 thousand (5%) from fiscal year ended 2015. The entire increase is in the Salary and benefits expense category which makes up more than 70% of the operating expenses and is attributable to a small increase in headcount and related expenses.

- Mortgage servicing fees were lower in 2016 by $55 thousand (13.9%) as the Single Family loan portfolio continues to pay down over time. Because of the migration to the mortgage backed securities strategy, loans are now being securitized into MBS's. Therefore, the Single Family whole loan portfolio is not being replenished as older loans are being paid off.

- The Agency saw a decrease in Single Family and Multi-Family loan losses and loss provisions from $1.07 million in FY 2015 to $804 thousand in FY 2016, reflecting an overall improvement in the health of the loan portfolio. The Agency has worked aggressively to mitigate loan losses and continues to take a more conservative approach to reserving for future losses.

Budgetary Information

The Agency prepares an annual budget of income, expenses, and fund transfers for its Operating Fund. The operating budget is prepared by staff, and reviewed and approved prior to the start of the fiscal year by the Agency's Board of Commissioners.

The Agency relies on fund transfers from bond programs and Operating Fund cash-on-hand to bridge the gap between annual operating expenses and operating income.

For fiscal year 2016, the Agency budgeted $1.58 million in operating revenues and $4.87 million in operating expenses. Actual operating revenues of $2.39 million were over budget by $810 thousand, mainly due to revenue booked as the result of tax credits issued by the State of Vermont to be used for a new Down Payment Assistance Program ($594 thousand). Actual operating expenses of $4.73 million were under budget by $140 thousand.

Federal grant revenues and expenses related to the Agency's participation in programs under the American Recovery and Reinvestment Act of 2009 (ARRA) and the Federal Housing and Economic Recovery Act of 2008 (HERA) are reported in the Operating Fund, but are not part of the Agency's operating budget.

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 information, please contact the Chief Financial Officer at VHFA, 164 St. Paul St., Burlington, VT 05401 or visit our website at www.vhfa.org.

VERMONT HOUSING FINANCE AGENCY

(A Component Unit of the State of Vermont)

Statement of Net Position

June 30, 2016

(dollars in thousands)

Assets	Operating Fund	Single Family Mortgage Program Fund	Multiple Purpose Bond Fund	Multi-Family Mortgage Program Fund	Total
Current assets:					
Cash and cash equivalents					
Unrestricted	$ 248	—	—	—	248
Restricted	4,398	15,655	30,785	11,170	62,008
Accrued interest receivable:					
Investments	—	37	82	9	128
Mortgage loans	53	102	2,066	335	2,556
Mortgage backed securities	—	228	224	—	452
Investments maturing within one year	100	395	5,186	1,586	7,267
Current portion of mortgage loans receivable	3,660	512	5,469	22,166	31,807
Current portion of mortgage backed securities	—	1,941	2,023	—	3,964
Other receivables and prepaid expenses	840	30	243	26	1,139
Due from other funds	351	—	4	—	355
Total current assets	9,650	18,900	46,082	35,292	109,924
Noncurrent assets:					
Investments	—	753	910	2,708	4,371
Mortgage loans receivable, net	8,440	16,135	146,477	86,940	257,992
Mortgage backed securities	—	81,514	88,007	—	169,521
Capital assets	632	—	—	—	632
Real estate owned	80	329	717	—	1,126
Total noncurrent assets	9,152	98,731	236,111	89,648	433,642
Total assets	18,802	117,631	282,193	124,940	543,566
Deferred Outflows of Resources					
Accumulated decrease in fair value of hedging derivatives - Interest rate swaps	—	496	1,775	1,104	3,375
Liabilities					
Current liabilities:					
Notes payable	1,768	—	—	2,915	4,683
Current portion of bonds payable	—	2,860	7,412	2,017	12,289
Accrued interest payable	29	1,048	1,496	855	3,428
Other payables	346	7	75	—	428
Funds held on behalf of mortgagors	2,561	—	—	—	2,561
Due to other funds	—	—	—	355	355
Total current liabilities	4,704	3,915	8,983	6,142	23,744
Noncurrent liabilities:					
Notes payable	7,233	—	—	27,519	34,752
Bonds payable, net of current portion	—	94,933	223,570	76,780	395,283
Fair value of derivative instrument - interest rate swaps	—	496	1,775	1,104	3,375
Other liabilities	309	—	—	644	953
Total noncurrent liabilities	7,542	95,429	225,345	106,047	434,363
Total liabilities	12,246	99,344	234,328	112,189	458,107
Net Position					
Invested in capital assets	632	—	—	—	632
Restricted for bond resolutions	—	18,783	49,640	13,855	82,278
Restricted for down payment assistance	592	—	—	—	592
Unrestricted	5,332	—	—	—	5,332
Total net position	$ 6,556	18,783	49,640	13,855	88,834

See accompanying notes to financial statements.

VERMONT HOUSING FINANCE AGENCY
(A Component Unit of the State of Vermont)

Statement of Revenues, Expenses and Changes in Net Position

Year ended June 30, 2016

(dollars in thousands)

	Operating Fund	Single Family Mortgage Program Fund	Multiple Purpose Bond Fund	Multi-Family Mortgage Program Fund	Total
Operating revenues:					
Interest income:					
Investments	$ 2	546	570	70	1,188
Mortgage loans	663	2,166	8,631	5,268	16,728
Mortgage backed securities	—	2,949	2,219	—	5,168
Fee income	808	—	152	27	987
Sales of state tax credits	594	—	—	—	594
Gain on sales of loans and securities	310	—	—	—	310
Gain on bond redemptions, net	—	45	456	—	501
Other revenue	16	—	—	—	16
Total operating revenues	2,393	5,706	12,028	5,365	25,492
Operating expenses:					
Financing costs, including interest expense and amortization of bond premium and discount, net	373	4,022	8,804	3,309	16,508
Mortgage service and contract administration fees	1	73	268	—	342
Salaries and benefits	3,385	—	—	—	3,385
Operating expenses	750	8	4	28	790
Professional fees	90	51	27	18	186
Trustee and assignee fees	121	—	—	—	121
Provision for losses on loans and real estate owned	7	122	542	133	804
Total operating expenses	4,727	4,276	9,645	3,488	22,136
Operating income (loss)	(2,334)	1,430	2,383	1,877	3,356
Nonoperating revenues (expenses):					
Net appreciation (depreciation) in fair value of investments	—	2,462	1,631	(13)	4,080
Other nonoperating revenue	755	—	—	—	755
Federal programs:					
Program revenue	2,854	—	—	—	2,854
Program expenses	(2,795)	—	—	—	(2,795)
Administration and period costs	(59)	—	—	—	(59)
Total nonoperating revenues (expenses)	755	2,462	1,631	(13)	4,835
Income (loss) before transfers	(1,579)	3,892	4,014	1,864	8,191
Net transfers from (to) other funds	3,325	(4,650)	2,737	(1,412)	—
Increase (decrease) in net position	1,746	(758)	6,751	452	8,191
Net position:					
Net position at beginning of year	4,810	19,541	42,889	13,403	80,643
Net position at end of year	$ 6,556	18,783	49,640	13,855	88,834

See accompanying notes to financial statements.

VERMONT HOUSING FINANCE AGENCY
(A Component Unit of the State of Vermont)

Statement of Cash Flows

Year ended June 30, 2016

(dollars in thousands)

	Operating Fund	Single Family Mortgage Program Fund	Multiple Purpose Program Fund	Multi-Family Mortgage Program Fund	Total
Cash flows from operating activities:					
Mortgage loans interest receipts	$ 680	2,358	8,673	5,236	16,947
Mortgage backed securities interest receipts	—	2,984	2,153	—	5,137
Mortgage loans principal collections	8,740	6,486	28,030	14,251	57,507
Mortgage backed securities sales and paydowns	—	11,153	4,899	—	16,052
Mortgage loan originations	(7,773)	—	—	(31,584)	(39,357)
Mortgage backed securities purchases	—	67	(33,758)	—	(33,691)
Fee income and other receipts	1,003	—	152	656	1,811
Salaries and benefits payments	(3,342)	—	—	—	(3,342)
Operating expense payments	(1,063)	(61)	(41)	(34)	(1,199)
Service fee and other payments	(1)	(73)	(268)	—	(342)
Other nonoperating revenue	755	—	—	—	755
Federal program receipts	2,919	—	—	—	2,919
Federal program expenditures	(2,854)	—	—	—	(2,854)
Operating transfers from (to) other funds	(464)	25,105	(26,613)	1,972	—
Net cash (used in) provided by operating activities	(1,400)	48,019	(16,773)	(9,503)	20,343
Cash flows from investing activities:					
Investment sales	—	2,162	—	(1,777)	385
Investment interest receipts	2	557	560	120	1,239
Decrease in funds held on behalf of mortgagors	73	—	—	—	73
Sales of distressed properties	10	1,715	2,419	—	4,144
Distressed property expenditures	(7)	(321)	(1,175)	—	(1,503)
Payment to IRS to rebate excess earnings	—	(24)	—	—	(24)
Net cash provided by (used in) investing activities	78	4,089	1,804	(1,657)	4,314
Cash flows from noncapital financing activities:					
Bond and note interest payments	(285)	(4,295)	(7,748)	(3,275)	(15,603)
Bond principal payments	—	(47,195)	(36,584)	(2,463)	(86,242)
Repayment of notes	(4,426)	—	—	(9,600)	(14,026)
Bond issue proceeds	—	(86)	56,310	4	56,228
Increase in notes payable	4,000	—	—	29,434	33,434
Bond insurance payments	—	—	—	—	—
Financing costs other than interest	(83)	(100)	(843)	(53)	(1,079)
Noncapital financing transfers from (to) other funds	3,557	(4,647)	2,723	(1,633)	—
Net cash provided by (used in) noncapital financing activities	2,763	(56,323)	13,858	12,414	(27,288)
Cash flows from capital related financing activities:					
Net cash provided by (used in) capital related financing activities	—	—	—	—	—
Net increase (decrease) in cash and cash equivalents	1,441	(4,215)	(1,111)	1,254	(2,631)
Cash and cash equivalents at beginning of year	3,205	19,870	31,896	9,916	64,887
Cash and cash equivalents at end of year	$ 4,646	15,655	30,785	11,170	62,256

(Continued)

VERMONT HOUSING FINANCE AGENCY
(A Component Unit of the State of Vermont)

Statement of Cash Flows - Continued

Year ended June 30, 2016

(dollars in thousands)

	Operating Fund	Single Family Mortgage Program Fund	Multiple Purpose Program Fund	Multi-Family Mortgage Program Fund	Total
Reconciliation of cash flows from operating activities:					
Operating income (loss)	$ (2,334)	1,430	2,383	1,877	3,356
Adjustments to reconcile operating income (loss) to net cash provided by (used for) operating activities:					
Depreciation	80	—	—	—	80
Financing costs other than interest	83	70	820	53	1,026
Investment interest income	(2)	(546)	(570)	(70)	(1,188)
Sales of distressed properties	(10)	(1,715)	(2,419)	—	(4,144)
Distressed property expenditures	28	1,135	1,759	—	2,922
Arbitrage rebate	—	(4)	—	—	(4)
Bond and note interest expense	289	3,924	7,960	3,257	15,430
Gain on bond redemptions	—	(45)	(456)	—	(501)
Bond insurance expense	—	30	23	—	53
Appreciation in fair value of investments	—	2,489	1,936	—	4,425
Changes in assets and liabilities:					
Decrease (increase) in accrued interest receivable	17	229	(24)	(32)	190
Decrease (increase) in mortgage loans receivable	493	32,292	2,619	(15,228)	20,176
(Increase) decrease in mortgage backed securities	—	8,731	(30,794)	—	(22,063)
(Increase) decrease in other receivables and prepaid	(46)	5	2	(1)	(40)
(Decrease) increase in other liabilities	(659)	—	—	644	(15)
Increase (decrease) in other payables	661	(6)	(12)	(3)	640
Net cash (used in) provided by operating activities	$ (1,400)	48,019	(16,773)	(9,503)	20,343

Supplemental noncash operating/investing activities:
Mortgage loans receivable converted to real estate owned amounted to $2,200 in 2016

See accompanying notes to financial statements.

(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 a component unit of the State of Vermont and the State of Vermont appoints a majority of the Agency's board of commissioners.

The Agency is empowered by the Act and subsequent amendments to issue bonds and notes. 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 Multiple Purpose 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.

Federal grant revenues and expenses related to the Agency's participation in programs under the American Recovery and Reinvestment Act of 2009 (ARRA) and the Federal Housing and Economic Recovery Act of 2008 (HERA) are reported in the Operating 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, the Single Family Housing Bond Resolution adopted in September 1990, and the Mortgage Revenue Bond (Mortgage Backed Securities Program) indenture adopted in December 2009 under the federal New Issue Bond Program (NIBP). Monies from these programs have been used by the Agency to purchase mortgage backed securities or mortgage loans on single family residential housing units for persons and families of low and moderate income in Vermont.

(iii) Multiple Purpose Program Fund

This fund has been established under the Multiple Purpose Bond Indenture adopted in July 2007. Monies from these programs have been used by the Agency to finance mortgage loans on single family residential housing units and multi-family residential housing units for persons and families of low and moderate income in Vermont.

(iv) 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, the Multi-Family HFA initiative adopted in December 2009 under the federal NIBP, and various individualized taxable and tax exempt bond resolutions adopted between December 1985 and June 2007. 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 in Vermont.

(v) 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, 2016, reserve requirements totaled $34 thousand for Operating Fund, $717 thousand for the Single Family Mortgage Programs, $5.3 million for the Multiple Purpose Programs and $4.2 million for the Multi-Family Mortgage Programs. Amounts held in reserve accounts as of June 30, 2016 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.

The Agency implemented the provisions of Governmental Accounting Standards Board VHFA (GASB) Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November, 1989 FASB and AICPA Pronouncements.* Prior to the adoption of this standard, the Agency elected to adopt all Financial Accounting Standards Board (FASB) statements issued after November, 1989 that did not conflict with GASB standards. With the adoption of Statement No. 62, the Agency no longer adopts or applies FASB statements.

(b) Net Position

Net Position has been classified for external financial reporting purposes into the following three net position categories:

- *Invested in Capital Assets* – Capital assets, net of accumulated depreciation, and cost of construction or improvement of those assets.
- *Restricted* – Net Position subject to externally imposed stipulations, including those for excess yield loans.
- *Unrestricted* – Net Position that is not subject to externally imposed stipulations. Unrestricted Net Position 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.

(c) Cash Equivalents

The Agency considers all highly liquid investments with original maturities of three months or less to be cash equivalents for purposes of the Statement of Cash Flows. Cash equivalents also include mortgage payments which are held in trust by loan servicers in depository accounts or amounts in transit to trustees to be invested in collateralized repurchase agreements.

(d) Mortgage Loans Receivable

Mortgage loans receivable are carried at their uncollected principal balances less allowances for loan losses on mortgages and reserves for federally funded loans that are pass-through in nature.

The allowance for the single family loan portfolio is based on the ages of the loans receivable, current economic conditions and prior loss experience. The allowance for the multi-family loan portfolio is based on a review of each loan and considers the operating cash flows of the respective projects and fair values of the properties. The multi-family loan portfolio also includes an allowance for loans that may be forgiven in order to be in compliance with federal tax laws related to excess yield. At June 30, 2016, the allowances for loan losses totaled $7.810 million, broken out as follows: $1.280 million for the Operating Fund, $149 thousand for the Single Family Fund, $5.016 million for the Multiple Purpose Fund and $1.365 million for the Multi-Family Fund.

The reserve for federally funded mortgage loans made under Section 1602 and the Tax Credit Assistance Program (TCAP) held in the Operating Fund is $19.579 million.

(e) Mortgage Backed Securities

Mortgage backed securities consist of Federal National Mortgage Association (FNMA), Federal Home Loan Mortgage Corporation (FHLMC), and Government National Mortgage Association (GNMA) certificates. Mortgage backed securities are reported at fair value on the Statement of Net Position, and the net appreciation (depreciation) in the fair value is recognized in the Statement of Revenues, Expenses, and Changes in Net Position.

(f) 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. Investments are reported at fair value in the Statement of Net Position. The net appreciation (depreciation) 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 Position. Fair values of guaranteed investment contracts (GICs) are recorded at contract value. Fair values of all other investments are based upon quoted market prices.

(g) 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, five to ten years for building improvements, and three to five years for furniture and fixtures and computer equipment, using the straight-line method.

(h) Real Estate Owned

Real estate owned (REO) consists of properties acquired through foreclosure or repossession and are carried at the lower of cost or net realizable value (estimated market value less costs to sell).

(i) Hedging Derivatives – Interest Rate Swaps

The Agency has entered into interest rate swap agreements with counterparties with the intention to achieve a lower overall cost of funds for certain bond issuances. In accordance with GASB Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*, the interest rate swap instruments are reported at fair value on the Statement of Net Position.

All of the Agency's interest rate swaps are deemed to be effective cash flow hedges and therefore the fair value adjustment is reported as a deferred outflow on the Statement of Net Position.

(j) Amortization

Bond premiums and discounts are deferred and amortized over the lives of the respective issues using the straight-line method. Scheduled amortization of net bond premiums are $192,000; $189,000; $186,000; $183,000 and $179,000 for the five years ending June 30, 2017 through 2021, respectively.

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.

(k) Income Tax Status

The Agency is generally not subject to federal and Vermont income taxes under Section 115 of the Internal Revenue Code (IRC) and applicable state laws. The Agency qualifies as a tax-exempt organization under Section 501(c)(3) of the IRC.

(l) 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 non-mortgage 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.

(m) Operating and Non-operating Revenues and Expenses

The Agency records all revenues and expenses related to its 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. Net appreciation and depreciation in the fair value of investments and federal grant revenues and expenses are recorded as non-operating revenues and expenses. Gains and losses on bond redemption are recorded in operating results, as they are a part of the normal operations of the Agency's activities.

Grants received from federal, state and local governments are recognized as non-operating revenue as the related expenditures are incurred.

(n) 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.

(o) New accounting principles

During fiscal year 2016, the Agency implemented GASB Statement No. 72, Fair Value Measurement and Application, which applied GASB account concepts of fair value measurement to the Authority's valuation. The statement requires additional analysis of fair value if the volume or level of activity for an asset or liability has significantly decreased. It also requires identification of transactions that are not orderly. The statement establishes a hierarchy of inputs to valuation techniques used to measure fair value with three levels. Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities. Level 2 inputs are inputs-other than quoted prices-included within Level 1 that are observable for the asset or liability, either directly or indirectly.

Finally, Level 3 inputs are unobservable inputs, such as management's assumption of the default rate among underlying mortgages of a mortgage-backed security. The implementation of this standard does not have a material effect on the Agency's reporting as the fair value measurement is already maintained by the authority. See Note 3 for discussion of fair value measurements.

(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 Deposit 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; Guaranteed Investment Contracts (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 other financial institutions must be rated at least "A" by nationally recognized credit rating agencies or have posted adequate collateral to minimize the Agency's risk. All bonds are issued by U.S. Treasury or U.S. government agencies such as FNMA, FHLMC and FHLB, and had implied credit ratings of AAA at the time of purchase and continued to hold those ratings at June 30, 2016. In August of 2011, Standard & Poors (S&P) downgraded the long-term debt rating of the U.S. Government from AAA to AA+. S&P subsequently lowered its credit rating on both Fannie Mae (FNMA) and Freddie Mac (FHLMC) one level from AAA to AA+, noting that the two companies were directly reliant on the U.S. government and have been under U.S. government conservatorship since 2008. The debt of the U.S. Government, FNMA and FHLMC continue to be rated Aaa by Moody's Investment Services.

(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. Bank deposits in excess of the insured amounts are uninsured and uncollateralized. Deposits in bank accounts at June 30, 2016 totaled $5.445 million. Of this amount, $3.690 million was exposed to custodial credit risk as uninsured and uncollateralized.

(b) Cash and Investments

The Agency's cash and investments at June 30, 2016 are presented below (in thousands).

		Investment maturities (in years)			
	Total	**Less than 1**	**1 – 5**	**6 – 10**	**More than 10**
Cash	$ 5,470	5,470	—	—	—
Money market accounts	39,128	39,128	—	—	—
Certificates of deposit	4,206	1,686	2,520	—	—
Guaranteed investment contracts	18,596	17,658	—	—	938
U.S. Treasury securities	5,581	5,581	—	—	—
Government agency securities	913	—	—	3	910
Mortgage backed securities	173,485	3,964	282	279	168,960
Total cash and investments	$ 247,379	73,487	2,802	282	170,808

The following table provides information on the credit ratings associated with the Agency's cash and investments at June 30, 2016 (in thousands):

	Total	**AAA**	**AA**	**A**	**NR**
Cash	$ 5,470	—	—	—	5,470
Money market accounts	39,128	—	—	—	39,128
Certificates of deposit	4,206	—	—	—	4,206
Guaranteed investment contracts	18,596	—	1,523	17,073	—
U.S. Treasury securities	5,581	5,581	—	—	—
Government agency securities	913	913	—	—	—
Mortgage backed securities	173,485	173,485	—	—	—
Total cash and investments	$ 247,379	179,979	1,523	17,073	48,804

(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. Approximately 8% of the Agency's cash and investments are invested in guaranteed investment contracts. Bayerische, PNC, Transamerica, Credit Agricole, AIG, and Natixis are 65%, 18%, 8%, 4%, 4%, and 1%, respectively, of the Agency's total guaranteed investment contracts (GICs). The Agency's investment policy does not limit 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's policy does not limit investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

(e) Fair Value of Investments

VHFA has adopted GASB No. 72, *Fair Value Measurement and Application*. This statement establishes a hierarchy of inputs to valuation techniques used to measure fair value:

- Level 1 – quoted market prices in active markets

- Level 2 – inputs other than quoted market prices that are observable either directly or indirectly
- Level 3 – unobservable inputs

The following table presents the investments that the Agency measured at fair value:

	Total	Level 1	Level 2	Level 3
Certificates of deposit	$ 4,206	—	4,206	—
Guaranteed investment contracts	18,596	—	18,596	—
U.S. Treasury securities	5,581	5,581	—	—
Government agency securities	913	913	—	—
Mortgage backed securities	173,485	—	173,485	—
Total investments and MBS	$ 202,781	6,494	196,287	—

(4) Mortgage and Construction Loans Receivable

(a) Single Family Mortgage Loans Receivable

Single Family mortgage loans earn interest at annual rates ranging from 0% to 9.05%. Mortgage payments are received monthly by the Agency from which service fees are generally retained by servicing lenders or sub-servicers.

At June 30, 2016, approximately 38% of the Single Family mortgage portfolios consisted of primary insured mortgages.

Mortgage loans, not requiring primary insurance, are limited to 80% of the appraised value of the property.

(b) Multi-Family Mortgage Loans Receivable

Multi-Family mortgage loans receivable earn interest at annual rates ranging predominantly from 0% to 8.5%, and are collateralized by first mortgage liens on all real and personal property of the mortgaged premises.

(5) Capital Assets

	Beginning balance	Additions	Ending balance
Capital assets not being depreciated:			
Land	$ 50	—	50
Capital assets being depreciated:			
Building	1,001	—	1,001
Building improvements	795	—	795
Computer equipment	1,161	—	1,161
Furniture and fixtures	213	—	213
Total capital assets being depreciated	3,170	—	3,170
Less accumulated depreciation for:			
Building	(513)	(25)	(538)
Building improvements	(707)	(13)	(720)
Computer equipment	(1,084)	(39)	(1,123)
Furniture and fixtures	(204)	(3)	(207)
Total accumulated depreciation	(2,508)	(80)	(2,588)
Total capital assets being depreciated, net	662	(80)	582
Capital assets, net	$ 712	(80)	632

(6) Real Estate Owned

Real estate owned (REO) at June 30, 2016 consists of properties held pending sale as a result of foreclosure or repossession by the Agency. REO is carried at the lower of cost or net realizable value. At June 30, 2016 the net realizable value of REO properties held by the Agency totals $1.126 million, of which $80 thousand is related to the Operating Fund, $329 thousand to the Single Family Fund and $717 thousand to the Multiple Purpose Fund.

(7) Funds Held on Behalf of Mortgagors

Funds held on behalf of mortgagors are received primarily from Multi-Family housing developers at the time the Agency makes permanent mortgage loans. Funds held are governed by agreements, and released upon satisfactory compliance with their terms.

(8) 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. In most cases, interest is payable semi-annually. All bonds are subject to redemption after various dates at par value.

Outstanding bonds payable at June 30, 2016 are as follows (in thousands):

A. Single Family Mortgage Program Fund:	
Housing Program:	
Series 17, maturing 2016 to 2033, interest at 3.182%	$ 925
Series 19, maturing 2016 to 2035, interest at 3.492% to 4.750%	4,645
Series 27, maturing 2016 to 2038, interest at 4.350% to 4.900%	11,750
Total Housing Program	17,320
Mortgage Revenue Bonds (Mortgage Backed Securities Program):	
Series 2009A, Subseries A-1 and Series 2010 A, maturing 2016 to 2041, interest at 2.25% to 4.50%	18,175
Series 2009A, Subseries A-2 and Series 2011 A, maturing 2016 to 2041, interest at 2.00% to 4.50%	21,120
Series 2009A, Subseries A-3, maturing 2016 to 2041, interest at 2.49%	40,980
Total Mortgage Revenue Bond Program	80,275
Total Single Family Mortgage Program Fund	97,595
B. Multiple Purpose Bond Program Fund:	
Multiple Purpose Bonds:	
2007 Series A and B, maturing 2017 to 2037, interest at 4.197% to 4.197%	12,800
2007 Series C, maturing 2017 to 2037, interest at 3.99% to 3.99%	16,500
2008 Series C, maturing 2016 to 2040, interest at 3.167% to 5.35%	9,165
2012 Series A, B and C, maturing 2016 to 2042, interest at 1.9% to 4.125%	39,290
2013 Series A, B and C, maturing 2016 to 2043, interest at 1.8% to 4.875%	20,455
2014 Series A and B, maturing 2016 to 2044, interest at 0.75% to 4.25%	39,780
2015 Series A, B, C, D and E, maturing 2016 to 2045, interest at 1.15% to 4.78%	33,990
2015 Series F and G, maturing 2016 to 2045, interest at 0.85% to 4.0%	25,890
2016 Series A and B, maturing 2017 to 2046, interest at 0.75% to 4.0%	29,615
Total Multiple Purpose Bonds	227,485

C. Multi-Family Mortgage Program Fund:	
Mortgage Program:	
2000 Series A, maturing 2017 to 2039, interest at 5.9%	2,280
2003 Series A, B, maturing 2016 to 2043, interest at 5.05% to 5.25%	3,590
2012 Series A, B and C, maturing 2016 to 2052, interest at 1.587% to 4.629%	24,670
2014 Series A, B and C, maturing 2016 to 2045, interest at 1.2% to 6.0%	14,575
Total Mortgage Program	45,115
Direct Placement Program:	
Variable Rate Demand Revenue Bonds, Series 1, maturing 2017 to 2038, interest at 4.18% to 5.49%	3,605
Variable Rate Demand Revenue Bonds, Series 2, maturing 2017 to 2038, interest at 3.756% to 4.61%	2,230
Total Direct Placement Programs	5,835
HFA Initiative Multifamily Bonds:	
2009 Series B, maturing 2016 to 2041, interest at 3.61%	6,110
2009 Series C and 2011 Series A, maturing 2016 to 2051, interest at 1.75% to 3.2%	18,975
2012 Series A, maturing 2016 to 2043, interest at 5.25%	2,855
Total HFA Initiative Bonds	27,940
Total Multi-Family Mortgage Program Fund	78,890
Total bonds payable	403,970
Plus Unamortized Bond Premium (Discount), net	3,602
	$ 407,572

All calendar year 2016 maturities on bonds payable occur after June 30, 2016.

Future maturities on bonds payable as of June 30, 2016 are as follows (in thousands):

Year ending	Single Family		Multiple Purpose		Multi-Family		Total	
June 30:	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest
2017	$ 2,825	2,977	7,250	8,050	2,021	2,954	12,096	13,981
2018	2,865	2,894	8,610	7,920	2,068	2,909	13,543	13,723
2019	2,940	2,806	8,700	7,733	2,087	2,859	13,727	13,398
2020	2,990	2,714	8,810	7,519	1,885	2,802	13,685	13,035
2021	3,085	2,619	9,010	7,281	1,748	2,743	13,843	12,643
2022-2026	16,720	11,475	47,590	32,075	11,084	12,702	75,394	56,252
2027-2031	19,965	8,478	50,800	23,208	15,444	10,229	86,209	41,915
2032-2036	22,740	5,232	49,875	12,983	16,618	6,947	89,233	25,162
2037-2041	21,605	1,913	23,225	5,022	14,988	3,617	59,818	10,552
2042-2046	1,860	47	13,300	1,479	8,232	1,083	23,392	2,609
2047-2051	—	—	315	13	2,595	211	2,910	224
2052-2056	—	—	—	—	120	6	120	6
Total	$ 97,595	41,155	227,485	113,283	78,890	49,062	403,970	203,500

A summary of bonds payable, discount on bonds, and premium on bonds and arbitrage rebate payable activity for the year ended June 30, 2016 is as follows (in thousands):

	Beginning balance	Increases	Decreases	Ending balance	Due within one year	Due thereafter
Bonds payable	$ 435,209	55,505	(86,744)	403,970	12,096	391,874
Discount on bonds	(244)	—	30	(214)	(16)	(198)
Premium on bonds	3,122	1,410	(716)	3,816	209	3,607
Arbitrage rebate payable	(27)	—	27	—	—	—

The Agency has entered into interest rate swap agreements with counterparties in connection with the Variable Rate Demand Bonds (VRDB). Under the swap agreement, the swap provider pays the Agency an amount based on the London InterBank Offered Rate (LIBOR) or the Securities Industry and Financial Markets Association (SIFMA), and the Agency pays the swap provider an amount at a fixed rate of interest.

Using rates as of June 30, 2016, debt service requirements of the variable rate bonds and net swap payments, assuming current interest rates remain constant, are as follows (in thousands):

	Variable rate		Interest rate	
Year ending June 30:	**Principal**	**Interest**	**swaps, net**	**Total**
2017	$ 1,355	224	1,669	3,248
2018	1,855	217	1,613	3,685
2019	1,860	209	1,551	3,620
2020	1,860	200	1,488	3,548
2021	1,920	192	1,424	3,536
2022-2026	13,720	724	5,388	19,832
2027-2031	8,875	499	3,722	13,096
2032-2036	10,505	280	2,065	12,850
2037-2040	6,960	49	341	7,350
Total	$ 48,910	2,594	19,261	70,765

A summary of the swap agreement is as follows (in thousands):

Issue	Counter-Party	Ratings (Moody's/S &P)	Effective date	Notional amount	Termination date	Fixed swap payment rate	Variable receivable rate	Fair Value at 6/30/2016
Series 17	BNY Mellon	Aa2/AA-	4/23/2003	$ 925	5/1/2019	3.18%	70% 1mo LIBOR	$ (36)
Series 19	BNY Mellon	Aa2/AA-	4/8/2004	3,450	11/1/2027	3.49%	70% 1mo LIBOR	(460)
MPB 2007A*	BNY Mellon	Aa2/AA-	7/24/2007	12,800	5/1/2037	4.20%	65% 1mo LIBOR + 0.28%	(383)
MPB 2007C*	BNY Mellon	Aa2/AA-	9/12/2007	16,500	11/1/2037	3.99%	65% 1mo LIBOR + 0.28%	(466)
MPB 2008C	Wells Fargo	Aa2/AA-	9/24/2008	4,300	5/1/2040	3.17%	SIFMA + 0.05%	(261)
MPB 2013A	BNY Mellon	Aa2/AA-	11/30/2004	5,100	5/1/2029	3.68%	SIFMA + 0.10%	(665)
MF Series 1A	KeyBank NA	Aa3/A-	1/25/2007	570	1/1/2022	4.24%	SIFMA + 0.15%	(97)
MF Series 1B	KeyBank NA	Aa3/A-	1/25/2007	1,550	1/1/2022	4.18%	SIFMA + 0.10%	(260)
MF Series 1C	KeyBank NA	Aa3/A-	1/25/2007	1,485	1/1/2022	5.49%	1mo LIBOR + 0.05%	(343)
MF Series 2A	KeyBank NA	Aa3/A-	1/24/2008	1,115	1/5/2023	3.80%	SIFMA + 0.15%	(182)
MF Series 2B	KeyBank NA	Aa3/A-	1/24/2008	235	1/5/2023	3.76%	SIFMA + 0.10%	(39)
MF Series 2C	KeyBank NA	Aa3/A-	1/24/2008	880	1/5/2023	4.61%	1mo LIBOR + 0.05%	(183)
Total				$ 48,910				$ (3,375)

*Optional termination date - 5/1/2017

By using derivative financial instruments to hedge exposures to changes in interest rates, the Agency exposes itself to credit, market risk and basis 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 ratings are higher than A. 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. Basis risk is the risk that variable rate payments to bondholders will not equal variable rate receipts from the counterparty.

(9) 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, 2016, the Agency had outstanding borrowings totaling $2.158 million which are secured by mortgage loans with a carrying value of $2.68 million. These borrowings have interest rates ranging from 6.32% to 7.66% and mature from September 2016 through February 2018.

The Agency has an $850,000 note payable to the Vermont Community Foundation at a rate of 1.5%, maturing in March, 2019. The note is uncollateralized.

The Agency has a $2.0 million note payable to the MacArthur Foundation at a rate of 1.0%, maturing October 2017 through October 2019. The proceeds of this note are used to provide low cost pre-development, energy, and equity bridge loans to multi-family housing projects.

The Agency has a $2.8 million note payable to the State of Vermont at a rate of 2.76%, maturing February 2024. The proceeds of this note are to provide financing for energy efficiency projects described in Act No. 97 of the Acts of 2013.

The Agency has a $3.993 million 40-year amortizing note payable to the Federal Financing Bank at a rate of 3.011%, maturing in April 2056. The proceeds of this note were used to finance an FHA Risk-Sharing Insured Mortgage Loan.

The Agency is operating under unsecured lines of credit that total $71.06 million with lending institutions expiring in 2017. At June 30, 2016, there was a $27.634 million Multi-Family balance outstanding at interest rates of .935% to 1.438%. 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.

Future notes payable maturities as of June 30, 2016 are as follows (in thousands):

	Operating		Multi-Family		Total	
	Principal	Interest	Principal	Interest	Principal	Interest
Year ending June 30:						
2017	$ 1,768	218	2,915	377	4,683	595
2018	974	166	24,718	214	25,692	380
2019	1,395	138	255	75	1,650	213
2020	1,047	118	295	67	1,342	185
2021	48	114	540	53	588	167
2022 - 2056	3,770	2,430	1,710	66	5,480	2,496
Total	$ 9,002	3,184	30,433	852	39,435	4,036

A summary of notes payable activity for the year ended June 30, 2016 is as follows (in thousands):

	Beginning balance	Increases	Decreases	Ending balance	Current	Non-current
Line of credit borrowings	$ 11,450	29,434	(13,250)	27,634	2,915	24,719
Notes payable	8,577	4,000	(776)	11,801	1,768	10,033
Total	$ 20,027	33,434	(14,026)	39,435	4,683	34,752

(10) 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.

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.

Net Position derived from purpose restricted resources provided under contractual agreements with federal agencies are restricted to the underlying purpose.

(11) Retirement Plan

Upon meeting certain eligibility requirements, the Agency's employees are eligible to participate in the Vermont Housing Finance Agency 403(b) Plan, a defined contribution retirement plan. The Agency's contribution to the Plan is 10% of the covered payroll. Employees are 30% vested in benefits under the plan upon participation, and vest in the remaining 70% on a pro-rata basis over five years of service. Forfeitures on non-vested benefits by terminated employees reduce the Agency's contribution. The cost of the plan was $253 thousand for the year ended June 30, 2016, and is included in salaries and benefits expense.

(12) Gain on Bond Redemptions

During the year ended June 30, 2016, the Agency redeemed $43.6 million of its Single Family Bonds, $31.6 million of its Multiple Purpose Bonds, and $500 thousand of its Multi-Family Bonds prior to scheduled maturity dates. Net gain on bond redemptions was $501 thousand and represents the net unamortized bond premium and discount balances at the time the bonds were retired.

(13) Federal Programs

In fiscal year 2016, the Agency participated in the following federal funding programs under the American Recovery and Reinvestment Act of 2009 (ARRA) and Federal Housing and Economic Recovery Act of 2008 (HERA):

- On July 1, 2009, VHFA entered into an agreement with the United States Department of Housing and Urban Development (HUD) to administer $5.4 million of funding available to eligible Vermont housing development under Federal Tax Credit Assistance Program (TCAP). The TCAP program, authorized by the American Recovery and Reinvestment Act pays for capital items in developments that receive Internal Revenue Code Section 42 Housing Credits. As of June 30, 2016, the Agency had distributed the full $5.4 million from this program.

- On August 26, 2009, VHFA made its first distribution under Section 1602 of the American Recovery and Reinvestment Act of 2009 which authorized the United States Department of the Treasury to issue grants to State housing credit agencies in lieu of low-income housing credits. The program allows states to exchange up to 100% of returned and unused pre-2009 ceiling credits and 40% of 2009 per capita and national pool credits for cash. VHFA administered the distribution of

the cash to eligible housing developments to pay for capital items. As of June 30, 2016, VHFA had exchanged approximately $1.7 million of credits for $14.2 million in awarded funds, the full amount of which has been disbursed.

- On June 15, 2009, VHFA signed a memorandum of agreement with the State of Vermont to administer $7.0 million out of $19.6 million of Neighborhood Stabilization Program (NSP) funds allocated to the State under the Federal Housing and Economic Recovery Act of 2008. VHFA's portion to administer is called the Homeownership Acquisition and Rehabilitation Program (HARP). The NSP-HARP funds were used to purchase Single Family homes that have been foreclosed upon, rehabilitate each home with a focus on energy efficiency, and resell the homes to income eligible homebuyers. In addition to the initial $7.0 million, sales proceeds have been and will continue to be recycled until all program funding and income from sales has been invested in homes, including provisions for homebuyer subsidies. As of June 30, 2016, VHFA had incurred program expenses of $15.3 million, funded by the $7.0 million NSP award and $8.3 million from the sale of rehabilitated houses.

- On May 11, 2011, VHFA signed a memorandum of agreement with the State of Vermont to administer $2.9 million out of $5.0 million of Neighborhood Stabilization Program (NSP-3) funds allocated to the State under the Federal Housing and Economic Recovery Act of 2008. NSP-HARP III, is administered as a separate and distinct pool of funds, but serves as an extension of the activities in the NSP-HARP I Program noted above. As in NSP-HARP I, sales proceeds are recycled to leverage the original $2.9 million until all funding and program income have been invested. As of June 30, 2016, VHFA had incurred program expenses of $6.2 million, funded by the $2.9 million NSP award and $3.3 million from the sale of rehabilitated houses.

- During fiscal year 2016, the Agency administered the "Section 8 Housing Assistance Payment Program" (HAP) under Annual Contribution Contracts (ACC) with the Department of Housing and Urban Development (HUD) for 13 housing developments (318 units). Under the ACC, VHFA receives funds from HUD with which to make housing assistance payments to an owner of assisted housing pursuant to Housing Assistance Payment Contracts entered into by HUD with the owners. Under the Section 8 program, the owner must determine the portion of the gross rent to be paid by tenants in accordance with HUD schedules and criteria, typically 30% of the tenant's adjusted income (as defined by HUD). The balance of the monthly contract rent is paid by VHFA in the form of monthly housing assistance payments. The Agency distributed $2.6 million in HAP payments under this program during the year ended June 30, 2016.

(14) Commitments and Contingencies

At June 30, 2016, the Agency had outstanding commitments in the amount of $11.3 million to purchase mortgage loans or mortgage backed securities pursuant to its normal funding from bond proceeds. The Agency also had $17.7 million of outstanding commitments to purchase securities under the TBA model. In addition, there were commitments of $18.8 million for general loans.

Under the Single Family Mortgage Programs, the Agency has obtained surety bonds in the amount of $4.7 million expiring between 2034 and 2038, which satisfy the requirements of certain bond resolutions.

(15) 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.

(16) Subsequent Events

The events that occur after the date of the Statement of Net Position but before the financial statements were available to be issued must be evaluated for recognition or disclosure. The effects of subsequent events that provide evidence about conditions that existed at the date of the Statement of Net Position are recognized in the accompanying financial statements. Subsequent events which provide evidence about conditions that existed after the date of the Statement of Net Position require disclosure in the accompanying notes. Management evaluated the activity of VHFA through September 30, 2016 (the date the financial statements were available to be issued) and concluded that the following subsequent events require recognition in the Financial Statements or disclosure in the Notes to the Financial Statements.

On August 24, 2016, the Agency issued $10,140,000 of 2016 Series C (AMT) and $20,000,000 of 2016 Series D (non AMT) Multiple Purpose Bonds out of which $10,140,000 of the principal amount along with excess funds in the refunded Series will be used to refund Single Family Housing Bonds Series 27 on November 1, 2016.

COHN REZNICK

ACCOUNTING • TAX • ADVISORY

Independent Member of Nexia International

cohnreznick.com