

Massachusetts Housing Investment Corporation

Consolidated Financial Statements

For the years ended June 30, 1999 and 1998

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## Report of Independent Auditors

Board of Directors  
The Massachusetts Housing Investment Corporation

We have audited the accompanying consolidated balance sheets of the Massachusetts Housing Investment Corporation (the Corporation) as of June 30, 1999 and 1998, and the related consolidated statements of revenues and expenditures, and cash flows for the years then ended. These financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. 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 examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Massachusetts Housing Investment Corporation at June 30, 1999 and 1998, and the consolidated results of its operations and its cash flows for the years then ended, in conformity with generally accepted accounting principles.

Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements taken as a whole. The accompanying consolidating balance sheets and statements of revenues and expenditures are presented for purposes of additional analysis and are not a required part of the financial statements. Such information has been subjected to the auditing procedures applied in our audits of the financial statements and, in our opinion, is fairly stated in all material respects in relation to the consolidated financial statements taken as a whole.

*Ernst & Young LLP*

Boston, Massachusetts  
September 30, 1999

Massachusetts Housing Investment Corporation

Consolidated Balance Sheets

	June 30	
	1999	1998
<b>Assets</b>		
Cash	\$ 446,192	\$ 366,900
Loan fund:		
Project loans, net of allowance for loan losses of \$275,000 and \$250,000 in 1999 and 1998, respectively	15,616,672	5,883,630
Money market deposits at member corporations	36,383,328	47,341,370
Total loan fund	<u>52,000,000</u>	<u>53,225,000</u>
Loan guarantee fund:		
Loan guarantee funds on deposit	79,214	30,101
Loan guarantee loans	6,167,195	4,813,611
Total loan guarantee fund	<u>6,246,409</u>	<u>4,843,712</u>
Notes receivable	7,612,332	6,911,012
Amounts receivable and other assets	865,383	1,015,218
Furniture, equipment and leasehold improvements, net of accumulated depreciation and amortization of \$510,391 and \$378,434 in 1999 and 1998, respectively	263,695	320,300
<b>Total assets</b>	<u>\$ 67,434,011</u>	<u>\$ 66,682,142</u>
<b>Liabilities and net assets</b>		
Liabilities:		
Notes payable to member corporations	\$ 52,275,000	\$ 53,475,000
Notes payable – loan guarantee program	6,051,173	4,839,562
Unearned fees	6,629,015	6,531,991
Accrued interest and other liabilities	636,667	645,433
<b>Total liabilities</b>	<u>65,591,855</u>	<u>65,491,986</u>
<b>Net assets</b>	<u>1,842,156</u>	<u>1,190,156</u>
<b>Total liabilities and net assets</b>	<u>\$ 67,434,011</u>	<u>\$ 66,682,142</u>

*See accompanying notes to consolidated financial statements.*

Massachusetts Housing Investment Corporation

Consolidated Statements of Revenues and Expenditures

For the years ended June 30, 1999 and 1998

	<b>Year ended June 30,</b>	
	<b>1999</b>	<b>1998</b>
<b>Revenues</b>		
Interest Revenue:		
Interest on deposits	\$ 1,403,507	\$ 1,473,303
Interest on project loans	1,472,492	1,458,405
Total interest revenue	<u>2,875,999</u>	<u>2,931,708</u>
Interest expense on notes payable	(1,938,724)	(2,139,673)
Net interest revenue before provision for loan losses	<u>937,275</u>	<u>792,035</u>
Provision for loan losses	(25,000)	(25,000)
Net interest revenue after provision for loan losses	<u>912,275</u>	<u>767,035</u>
Equity program revenue:		
Fees related to MHEF limited partnerships	3,043,928	3,212,152
Other equity program fees	44,778	42,979
<b>Total revenues</b>	<u>4,000,981</u>	<u>4,022,166</u>
<b>Expenditures</b>		
Salaries and employee benefits	2,164,170	1,907,993
Occupancy, equipment and furniture	383,899	350,318
Professional services	468,379	483,335
Other expenditures	647,533	595,759
<b>Total expenditures</b>	<u>3,663,981</u>	<u>3,337,405</u>
<b>Excess of revenues over expenditures before     extraordinary item</b>	<u>337,000</u>	<u>684,761</u>
<b>Extraordinary item</b>		
Gain on extinguishing of debt	315,000	
<b>Excess of revenues over expenditures</b>	<u>652,000</u>	<u>684,761</u>
Net assets at beginning of year	1,190,156	505,395
<b>Net assets at end of year</b>	<u>\$ 1,842,156</u>	<u>\$ 1,190,156</u>

*See accompanying notes to consolidated financial statements.*

Massachusetts Housing Investment Corporation

Consolidated Statements of Cash Flows

	Year ended June 30	
	1999	1998
<b>Operating activities</b>		
Excess of revenues over expenditures	\$ 652,000	\$ 684,761
Adjustments to reconcile excess of revenues over expenditures to net cash provided by (used for) operating activities:		
Extraordinary gain on extinguishing of debt	(315,000)	
Provision for loan losses	25,000	25,000
Depreciation and amortization expense	131,957	87,945
Decrease (increase) in amounts receivable and other assets	149,835	(72,356)
Increase (decrease) in unearned fees	(1,338,965)	(1,336,208)
(Decrease) increase in accrued interest and other liabilities	(8,766)	191,943
Total adjustments	(1,355,939)	(1,103,676)
<b>Net cash provided by (used for) operating activities</b>	<b>(703,939)</b>	<b>(418,915)</b>
<b>Investing activities</b>		
Project loan advances	(25,922,980)	(23,892,446)
Project loan repayments	16,164,938	27,244,609
(Increase) decrease to loan guarantee funds on deposit	(49,113)	5,163,373
Decrease (increase) in money market deposits at member corporations	10,958,042	(3,402,163)
Loan guarantee advances	(1,842,750)	(6,950,615)
Loan guarantee repayments	489,166	2,137,004
Payments received on notes receivable	734,669	1,020,613
Purchases of furniture, equipment and leasehold improvements	(75,352)	(302,228)
<b>Net cash (used for) provided by investing activities</b>	<b>456,620</b>	<b>1,018,147</b>
<b>Financing activities</b>		
Proceeds from notes payable to member corporations		250,000
Amortization of notes payable to member corporations	(885,000)	(200,000)
Proceeds from notes payable to loan guarantee lenders	1,370,813	1,295,000
Payments of notes payable to loan guarantee lenders	(159,202)	(1,648,912)
<b>Net cash provided by (used for) financing activities</b>	<b>326,611</b>	<b>(303,912)</b>
<b>Net increase in cash</b>	<b>79,292</b>	<b>295,320</b>
Cash at beginning of year	366,900	71,580
<b>Cash at end of year</b>	<b>\$ 446,192</b>	<b>\$ 366,900</b>
<b>Supplemental information:</b>		
Unearned fees recorded in exchange for notes receivable	\$ 823,200	\$ 2,200,458
Cash paid for interest	\$ 1,890,646	\$ 1,624,149

See accompanying notes to consolidated financial statements.

# Massachusetts Housing Investment Corporation

## Notes to Consolidated Financial Statements

June 30, 1999 and 1998

### 1. Background and Accounting Policies

#### Purpose

On July 1, 1990, the Massachusetts Housing Investment Corporation (MHIC) was formally established as a Massachusetts-chartered, Chapter 180, not-for-profit corporation. MHIC's mission is to pool the resources of Massachusetts lenders and investors to improve and expand the financing of affordable housing throughout the state. In 1990, MHIC established a loan pool which provides loans for affordable housing on a statewide basis to not-for-profit as well as for-profit developers. Prior to January 1994, MHIC also managed a program that provided assistance to member corporations in underwriting low-income housing tax credit investments. In June 1993, MHIC established a wholly owned subsidiary, Massachusetts Housing Equity Fund, Inc. (MHEF), which is the General Partner of five limited partnerships (the Partnerships) structured for investment in low-income housing projects (Operating Partnerships) in Massachusetts.

#### Principles of Consolidation

The consolidated financial statements include the accounts of MHIC and its wholly owned subsidiary, MHEF. All significant inter-company transactions and balances have been eliminated in consolidation.

#### MHEF

MHIC has capitalized MHEF in the amount of \$2,187,044. MHEF, as general partner of the aforementioned Partnerships, has an interest (that ranges between .01% and 1% for a given Partnership) in their respective profits, losses, and distributions. MHEF accounts for its investment in the Partnerships using the equity method. Under the equity method, the investments are carried at cost and adjusted for MHEF's share of income or loss from the Partnerships, additional investments, and cash distributions.

Pursuant to the terms of the Partnership Agreements, the Partnerships, as limited partners in the various Operating Partnerships, have no obligation to the fund liabilities of the Operating Partnerships beyond its investment, including committed investment amounts. Consequently, MHEF does not include its share of cumulative losses from the Operating Partnerships if it results in its investment in a given Partnership being carried below zero. To the extent that equity losses are incurred when a Partnerships' respective asset values have been reduced to a zero balance, the losses will be suspended to be offset against future income.

# Massachusetts Housing Investment Corporation

## Notes to Consolidated Financial Statements (continued)

### **1. Background and Accounting Policies (continued)**

The Partnerships, as limited partners in the various Operating Partnerships, are subject to risks inherent in the ownership of property which are beyond its control, such as fluctuations in occupancy rates and operating expenses, variations in rental schedules, proper maintenance of facilities and continued eligibility of tax credits. If the cost of operating a property exceeds the rental income earned thereon, the Partnership, or MHEF acting independently as an investor, may deem it in its best interest to voluntarily provide funds in order to protect its investment.

At June 30, 1999 and 1998, the Partnerships have combined total assets of \$103,838,520 and \$85,127,208, respectively, and combined cumulative deficits of \$28,973,453 and \$15,870,456, respectively.

#### **Accrual Basis**

The consolidated financial statements of MHIC have been prepared on an accrual basis.

#### **Project Loans and Allowance for Possible Project Loan Losses**

Loans are stated at the amount of unpaid principal, net of the allowance for loan losses. Interest on project loans is recognized as income by applying the interest rates to the principal amount outstanding. An allowance for project loan losses is maintained based upon the evaluation of the risks associated with the outstanding loan pool. Any losses or recoveries subsequently realized are charged or credited to the allowance.

#### **Furniture, Equipment and Leasehold Improvements**

Furniture, equipment and leasehold improvements are stated at cost, less accumulated depreciation and amortization. Depreciation is computed by the straight-line method using rates based on estimated useful lives.

#### **Revenue Recognition for Fees Related to MHEF Limited Partnerships**

The Partnerships have contracted with MHIC to provide broad services that include organization, syndication, underwriting, long-term asset management and partnership administration. The fees for syndicating and organizing the Partnerships are recognized when syndication is substantially complete. The fees for underwriting investments are recognized according to the percentage of

# Massachusetts Housing Investment Corporation

## Notes to Consolidated Financial Statements (continued)

### 1. Background and Accounting Policies (continued)

work complete. The fees for asset management and partnership administration are recognized evenly over the life of the Partnerships (estimated to be approximately 15 years). In addition, MHIC monitors the construction process for the project investments in the various Partnerships. The fee for this service is paid by the project's sponsor and is recognized over the estimated construction period. During 1999 and 1998, MHIC recognized fees of approximately \$3,044,000 and \$3,212,000, respectively, for services provided and costs incurred in connection with the formation and operations of the Partnerships.

#### Income Tax Status

In February 1993 MHIC was granted tax-exempt status as a 501(c)(3) corporation under federal tax law. MHEF is a for-profit corporation and therefore is subject to federal and state income taxes.

#### Use of Estimates

Financial statements prepared in accordance with generally accepted accounting principles require the use of significant management estimates which affect the amounts and disclosures recorded in the financial statements. Actual results may differ from those estimates.

### 2. Project Loans

MHIC provides loans for the development of affordable housing throughout Massachusetts.

Project loan activity was as follows:

	<u>1999</u>	<u>1998</u>
Beginning balance	\$ 6,133,630	\$ 9,485,793
Loan disbursements	25,922,980	23,892,446
Loan repayments	(16,164,938)	(27,244,609)
Project loans outstanding	<u>15,891,672</u>	<u>6,133,630</u>
Allowance for loan losses	(275,000)	(250,000)
Project loans, net	<u>\$ 15,616,672</u>	<u>\$ 5,883,630</u>



# Massachusetts Housing Investment Corporation

## Notes to Consolidated Financial Statements (continued)

### 2. Project Loans (continued)

Project loans earn a variable rate (that ranges from 8.25% to 12%) of interest pursuant to MHIC's established loan policy and are secured by the underlying real estate. In certain instances, the primary repayment of these loans will be received from the equity syndication payments provided to the project by the MHEF limited partnerships tax credit equity investment program. At June 30, 1999 and 1998, MHIC had no delinquent or non-performing project loans and there have been no charge-offs recorded to date.

### 3. Loan Guarantee Program

Under the loan guarantee program, MHIC utilizes its loan pool as collateral to provide guarantees for loans made by other parties or to obtain fixed-rate funding for loans that it directly originates. MHIC offers two products under the program. The first product (the "Third Party" product") is a project loan guarantee, whereby MHIC administers construction loans for third parties, and assumes the construction period risk by guaranteeing repayment of the loan. Such transactions are treated as off-balance sheet liabilities and therefore not presented in the body of the financial statements. The second product (the "Direct" product) consists of direct loans made by MHIC, where its loan pool is used as collateral to secure funding, which is then advanced to borrowers. The corresponding borrowing to fund such loans are invested in short-term government backed securities until the funds are advanced.

Loan guarantee program activity was as follows:

	1999			1998		
	Third Party	Direct	Total	Third Party	Direct	Total
Beginning balance – loans	\$ 0	\$ 4,813,611	\$ 4,813,611	\$ 3,965,721	\$ 0	\$ 3,965,721
Loan disbursements	0	1,842,750	1,842,750	0	6,950,615	6,950,615
Loan repayments	0	(489,166)	(489,166)	(3,965,721)	(2,137,004)	(6,102,725)
Ending balance - loans	\$ 0	\$ 6,167,195	\$ 6,167,195	\$ 0	\$ 4,813,611	\$ 4,813,611

### 4. Notes Payable to Member Corporations

MHIC funds a loan pool through unsecured notes issued to member corporations pursuant to a Master Membership Agreement. Under this agreement, all note proceeds not currently being used to fund projects are to be deposited in interest-bearing deposit accounts at their respective lending institutions. Note proceeds not currently being used to fund projects accrue interest at

# Massachusetts Housing Investment Corporation

## Notes to Consolidated Financial Statements (continued)

### 4. Notes Payable to Member Corporations (continued)

1% less than the annual interest rate earned on the interest-bearing deposit accounts. All proceeds lent to projects bear interest at the prime rate less 1%. At June 30, 1999 and 1998, the average rate paid by MHIC for proceeds lent to projects was 6.75% and 7.5%, respectively. For the years ended June 30, 1999 and 1998, interest expense paid to member corporations totaled approximately \$1,686,000 and \$1,864,000, respectively. These notes are renewable annually. If the notes are not renewed, they require no principal amortization for five years and then amortize over a subsequent five-year period at an amount equal to the stated amount of the note less the member's pro rata share of unfunded losses. At June 30, 1999 and 1998, outstanding borrowings under these agreements totaled \$52,275,000 and \$53,475,000, respectively.

### 5. Notes Payable - Loan Guarantee Program

MHIC obtained a discretionary revolving line of credit of \$2,500,000 that it utilizes as a source of fixed-rate funding. A separate note evidences each advance under this line of credit and accrues interest at a rate of 70 basis points above the 5-year treasury note in effect at the time of the advance. At June 30, 1999 and 1998, borrowings under the line totaled \$2,099,929 and \$791,934, respectively. In addition, MHIC has borrowed \$3,951,244 and \$4,047,627 at June 30, 1999 and 1998, respectively. These borrowings have been used to fund the loan guarantee program (*see note 6, loan guarantee program*).

### 6. Notes Receivable and Unearned Fees

Notes receivable represent the present value (using effective interest rates that range from 8% to 9%) of future cash payments that will be received by MHIC from the MHEF Partnerships for asset management and other services it will provide to the Partnerships, as specified in the Partnership Agreements. At June 30, 1999 and 1998, notes receivable included accrued interest of \$447,814 and \$245,376, respectively.

Unearned equity fees reflect MHIC's obligation to provide future services to the Partnerships as consideration for the aforementioned notes receivable. These services include underwriting investments, long-term asset management and partnership administration. This obligation is reduced as services are provided, according to the revenue recognition methodology associated with the particular service (*see note 1, revenue recognition*). At June 30, 1999 and 1998, unearned equity fees were \$6,305,144 and \$5,844,320, respectively.

# Massachusetts Housing Investment Corporation

## Notes to Consolidated Financial Statements (continued)

### 7. Commitments

At June 30, 1999 and 1998, MHIC had unfunded commitments to originate loans of \$8,633,689 and \$21,983,842, respectively. These commitments have been established pursuant to MHIC's loan policy.

### 8. Leases

MHIC leases its facilities and certain furniture and equipment under operating leases which expire over future periods and require various minimum rental payments. Future minimum payments, by year and in aggregate, under these non-cancelable operating leases consist of the following at June 30, 1999:

2000	\$ 240,889
2001	249,758
2002	252,711
2003	64,963
<b>TOTAL</b>	<b><u>\$ 808,321</u></b>

MHIC incurred lease expenses associated with office space and equipment of \$255,076 and \$239,722 in 1999 and 1998, respectively.

### 9. Employee Benefit Plan

As a tax-exempt 501(c)(3) corporation, MHIC established a noncontributory, defined contribution plan under Section 401(a) of the Internal Revenue Code covering all full-time employees. The only source of contributions under the Plan is the annual employer contribution. The employer contribution is based upon a percentage of employee salary. MHIC contributed and charged to expense approximately \$87,000 and \$80,000 in 1999 and 1998, respectively.

### 10. Gain on extinguishing of debt

Workingman's Cooperative Bank, a member corporation in MHIC's loan fund, filed for bankruptcy in 1993. MHIC negotiated the repayment of the loan fund proceeds with the Federal Deposit Insurance Corporation (FDIC). The original note between Workingman's Cooperative Bank and MHIC was for \$1,000,000. During 1999, MHIC paid \$685,000 to the FDIC in full settlement to extinguish the debt while recognizing a \$315,000 extraordinary gain. The transaction resulted in a \$1,000,000 reduction in the loan fund.

# Massachusetts Housing Investment Corporation

## Notes to Consolidated Financial Statements (continued)

### **11. Impact of Year 2000 (unaudited)**

In general, without particular reference to MHIC, certain older computer programs were written using two digits rather than four to define the applicable year. As a result, those computer programs have time-sensitive functions that recognize a date using "00" instead of the year 2000 (the "Year 2000 Issue"). This could result in a system failure or miscalculations that led to disruption of operations, including, among other things, a temporary inability to process transactions or engage in other normal business activities.

MHIC has completed an initial assessment of the Year 2000 Issue and will modify or replace portions of its software so that its computer systems will function properly with respect to dates in the year 2000 and thereafter. MHIC believes that these modifications to existing software and conversions to new software will be sufficient, and that the Year 2000 Issue will not pose significant operational problems for its computer systems. This assessment is based on MHIC's best estimates, and actual results could differ materially from those anticipated. In addition, there is no guarantee that the systems of other companies on which MHIC's systems rely will be converted timely and would not have an adverse effect on the company.

## **Other Financial Information**

Massachusetts Housing Investment Corporation

Other Financial Information

Consolidating Balance Sheets

June 30, 1999

	MHIC	MHEF	Elimination	Consolidated
<b>Assets</b>				
Cash	\$ 297,769	\$ 148,423	\$	\$ 446,192
Loan fund:				
Project loans, net of allowance for loan losses of \$275,000	15,616,672			15,616,672
Money market deposits at member corporations	36,383,328			36,383,328
Total loan fund	52,000,000			52,000,000
Loan guarantee fund:				
Loan guarantee funds on deposit	79,214			79,214
Loan guarantee loans	6,167,195			6,167,195
Total loan guarantee fund	6,246,409			6,246,409
Investment in MHEF	2,223,603		(2,223,603)	
Investment in Partnerships				
Notes receivable	7,612,332			7,612,332
Amounts receivable and other assets	865,084	299		865,383
Due from parent		2,074,881	(2,074,881)	
Furniture, equipment and leasehold improvements, net of accumulated depreciation and amortization of \$510,391	263,695			263,695
<b>Total assets</b>	<b>\$ 69,508,892</b>	<b>\$ 2,223,603</b>	<b>\$ (4,298,484)</b>	<b>\$ 67,434,011</b>
<b>Liabilities and net assets</b>				
<b>Liabilities:</b>				
Notes payable to member corporations	\$ 52,275,000	\$	\$	\$ 52,275,000
Notes payable - loan guarantee program	6,051,173			6,051,173
Due to subsidiary	2,074,881		(2,074,881)	
Unearned fees	6,629,015			6,629,015
Accrued interest and other liabilities	636,667			636,667
<b>Total Liabilities</b>	<b>67,666,736</b>		<b>(2,074,881)</b>	<b>65,591,855</b>
<b>Net assets</b>	<b>1,842,156</b>	<b>2,223,603</b>	<b>(2,223,603)</b>	<b>1,842,156</b>
<b>Total Liabilities and net assets</b>	<b>\$ 69,508,892</b>	<b>\$ 2,223,603</b>	<b>\$ (4,298,484)</b>	<b>\$ 67,434,011</b>

*See accompanying notes to consolidated financial statements.*

Massachusetts Housing Investment Corporation

Other Financial Information

Consolidating Statements of Revenues and Expenditures

For the years ended June 30, 1999

	MHIC	MHEF	Elimination	Consolidated
<b>Revenues</b>				
Interest Revenue:				
Interest on bank deposits	\$ 1,403,507	\$	\$	\$ 1,403,507
Interest on project loans	1,455,252	17,240		1,472,492
Total interest revenue	2,858,729	17,240		2,875,999
Interest expense on notes payable	(1,938,724)			(1,938,724)
Net interest revenue before provision for loan losses	920,035	17,240		937,275
Provision for loan losses	(25,000)			(25,000)
Net interest revenue after provision for loan losses	895,035	17,240		912,275
Equity program revenue:				
Fees related to MHEF limited partnerships	3,043,928			3,043,928
Other equity program fees	44,778			44,778
Income from investment in MHEF	14,400		(14,400)	
<b>Total revenues</b>	<b>3,998,141</b>	<b>17,240</b>	<b>(14,400)</b>	<b>4,000,981</b>
<b>Expenditures</b>				
Salaries and employee benefits	2,164,170			2,164,170
Occupancy, equipment and furniture	383,899			383,899
Professional services	468,379			468,379
Other expenditures	644,693	2,840		647,533
<b>Total expenditures</b>	<b>3,661,141</b>	<b>2,840</b>		<b>3,663,981</b>
<b>Excess of revenues over expenditures before extraordinary item</b>	<b>337,000</b>	<b>14,400</b>	<b>(14,400)</b>	<b>337,000</b>
<b>Extraordinary item</b>				
Gain on extinguishing of debt	315,000			315,000
<b>Excess of revenues over expenditures</b>	<b>652,000</b>	<b>14,400</b>	<b>(14,400)</b>	<b>652,000</b>
Additional capitalization of MHEF		140,000	(140,000)	
Net assets at beginning of year	1,190,156	2,069,203	(2,069,203)	1,190,156
<b>Net assets at end of year</b>	<b>\$ 1,842,156</b>	<b>\$ 2,223,603</b>	<b>\$ (2,223,603)</b>	<b>\$ 1,842,156</b>

*See accompanying notes to consolidated financial statements.*