Pennsylvania Housing Finance Agency

Annual Report November 1973

Contents

Statement from the Chairman

As we review the history of the Pennsylvania Housing Finance Agency, we find ourselves in the unique position of having cleared the last obstacle, a test of the constitutionality of the enabling legislation, at a point in time when the agency will be able to have a significant impact on solving the problems of housing for the citizens of Pennsylvania.

The mission of the Pennsylvania Housing Finance Agency is impressed on us almost daily by headlines in our newspapers. The growing list of housing problems facing the entire population of our country has become front page news. These problems are most acute for those citizens with low and moderate incomes. We are now able to move into a program of action aimed at alleviating the problems of housing within Pennsylvania.

PHFA is already applying fiscally sound and prudent housing finance programs which in the coming year will provide an increasing supply of new housing for Pennsylvanians.

Richard J. Fox
Chairman

Statement from the Former Chairman

For those of us involved in the establishment of the Pennsylvania Housing Finance Agency, the past year will stand as one of the most exciting—and rewarding—in our respective careers.

The mission was twofold: to create a viable entity to meet the shelter needs of the Commonwealth's people; and at the same time, to build a sound business-like foundation for a long-range program of assistance in providing adequate housing.

The creation of a quasi-governmental agency with the power to issue tax-exempt notes and bonds, make loans and charge operating fees involved the surmounting of many technical obstacles. Our final and most important test on the viability of the PHFA concept was overcome when the Pennsylvania Supreme Court upheld the constitutionality of the Agency.

It was a difficult and, at many times, a frustrating year. But, with the passage of new legislation, and the employment of highly competent professional staff, the Pennsylvania Housing Finance Agency today stands ready and well-equipped to fulfill its purpose of assisting in the creation of quality housing at prices low-and moderate-income families can afford.

John Chatley, Jr.
Former Chairman

Statement from the Executive Director

In many ways, the Pennsylvania Housing Finance Agency is similar to the buildings we just now are beginning to finance. A good deal of research must take place before construction begins. The next step is to establish a stable and solid foundation, followed by the building of the basic framework of the unit. Finally, the mechanisms are installed which enable the building to do what it was designed to do: serve people.

An organization chart, legislation authorizing the creation of a new agency, even a suite of offices—these are not what PHFA really is, any more than plans and specifications are buildings. PHFA is people working together to deal effectively with one of Pennsylvania's most pressing problems: the lack of high quality, affordable housing. The best plans of state government, like the architect's drawings, are only as good as the people chosen to execute those plans.

Our Agency is fortunate in having a nucleus of staff members with ability equal to the challenge ahead—young people with the solid experience necessary to make fresh, bold ideas work. The concept behind PHFA is sound, the mechanisms for performing its functions are well-planned and efficient. Add to this the expertise and innovation of an exceptional group of staff members, and the Agency's programs have every reason to succeed.

John McCoy
Executive Director

Agency Members, Counsel and Underwriters

Agency members from the left are Richard Fox, Chairman; James Lineberger; Leon Hickman; Eugene R. Eisman, Treasurer; John O'Brien; Robert Lavelle; William Wilcox, Secretary, Department of Community Affairs, and John Chatley Jr.

Senior Managing Underwriter:
Salomon Brothers

Co-Managing Underwriters:
Paine, Webber, Jackson & Curtis
Mellon Bank, N.A.
Philadelphia National Bank

Independent Certified Public Accountants:
Peat, Marwick, Mitchell & Company

Bond Counsels:
Mudge, Rose, Guthrie & Alexander
Schnader, Harrison, Segal & Lewis

General Counsel:
McNees, Wallace & Nurick

Staff

The Pennsylvania Housing Agency staff, shown below, uses private and public sector experiences to fund housing in Pennsylvania.

Operations

Purpose & History

The Pennsylvania Housing Finance Agency is an independent institution created by the General Assembly to finance the construction of low-and moderate-income housing in the Commonwealth of Pennsylvania. It was conceived to promote the construction of new housing at a time when experts were beginning to discuss the housing shortage in Pennsylvania in terms of a crisis.

The housing shortage began to take shape in the Commonwealth during the 1960s. In that decade, housing starts for Pennsylvania averaged only 3.5 homes per 1,000 residents, while the national average was more than seven homes built for every 1,000

persons. Few or no increases in housing were registered in 44 of Pennsylvania's 67 counties during that period.

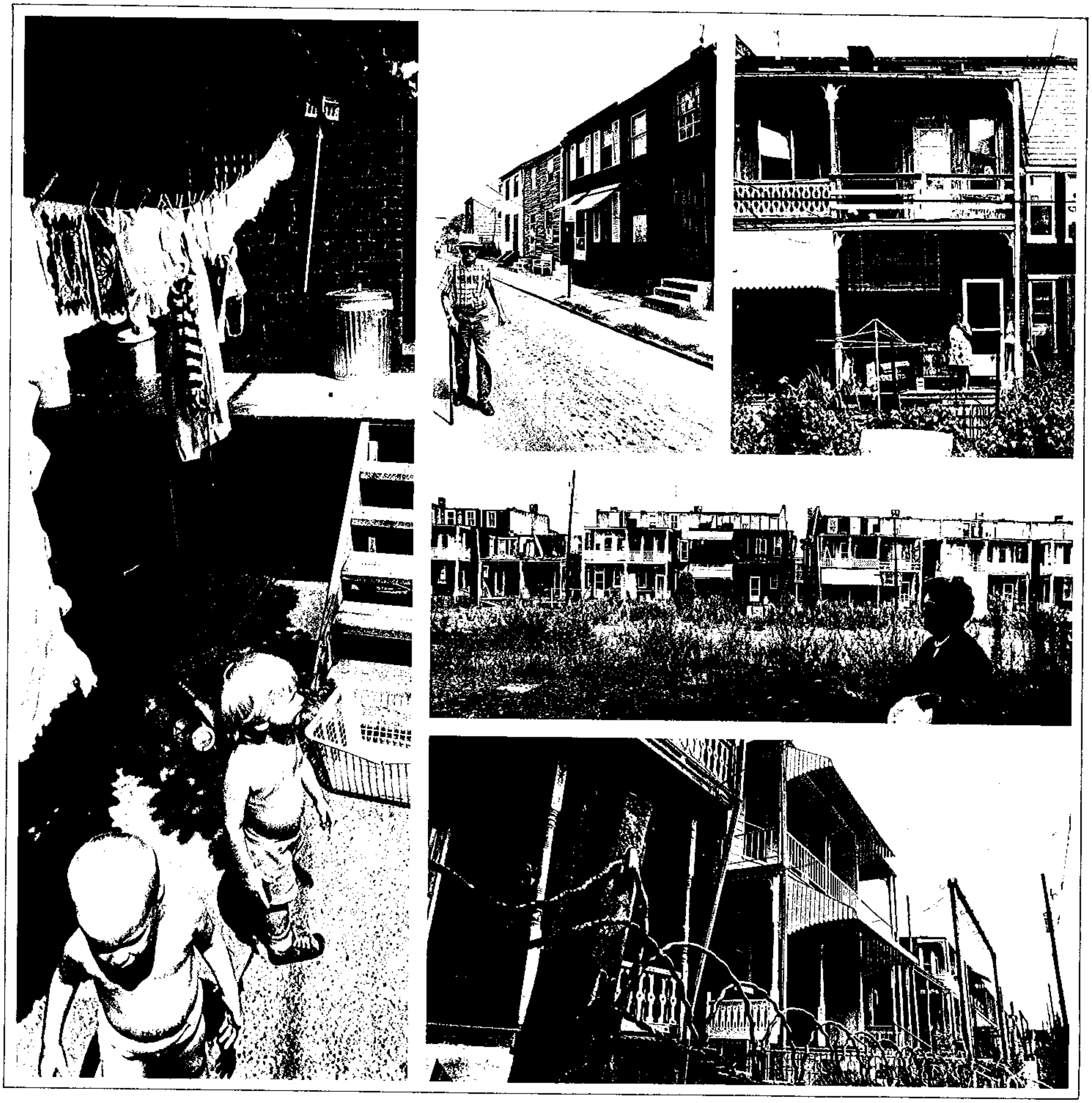
There were several reasons for the virtual halt in homebuilding — skyrocketing materials, construction and land costs; high taxes; restrictive zoning practices; dwindling capital; and a moratorium on many Federal Housing Administration programs. Added to this negative climate was tropical storm Agnes which struck the State in June 1972. Agnes cut a swath of destruction through Pennsylvania, leaving in her wake thousands of flood-damaged homes, many totally uninhabitable.

Out of the tragedy of Agnes and the simultaneous collapse of the existing housing supply, the Pennsylvania Housing Finance Agency was established as an action agency. The PHFA's immediate predecessor, the Pennsylvania Housing Agency, had been legislated into existence in 1959. While it had operated in relative obscurity with little mandate for action, the PHA had helped with flood relief during the aftermath of Agnes.

With the signing of the Housing Finance Agency Law in December 1972, Governor Milton J. Shapp and the Commonwealth's lawmakers formally acknowledged a responsibility to assist in providing moderate income families with suitable housing at affordable prices. The legislation also eliminated the conditions which traditionally prevent private industry from providing that housing.

With its mission outlined, the PHFA began developing the mechanisms for making construction loans and long-term mortgages to developers without dipping into Commonwealth tax revenues or adding to the state debt. The Pennsylvania Supreme Court recently upheld the purpose of the Agency, paving the way for negotiations on the first of the loans, expected to be closed shortly.

All of the units financed by the Agency are privately owned, and



managed by private management firms. They pay normal real estate taxes to the municipality in which they are located.

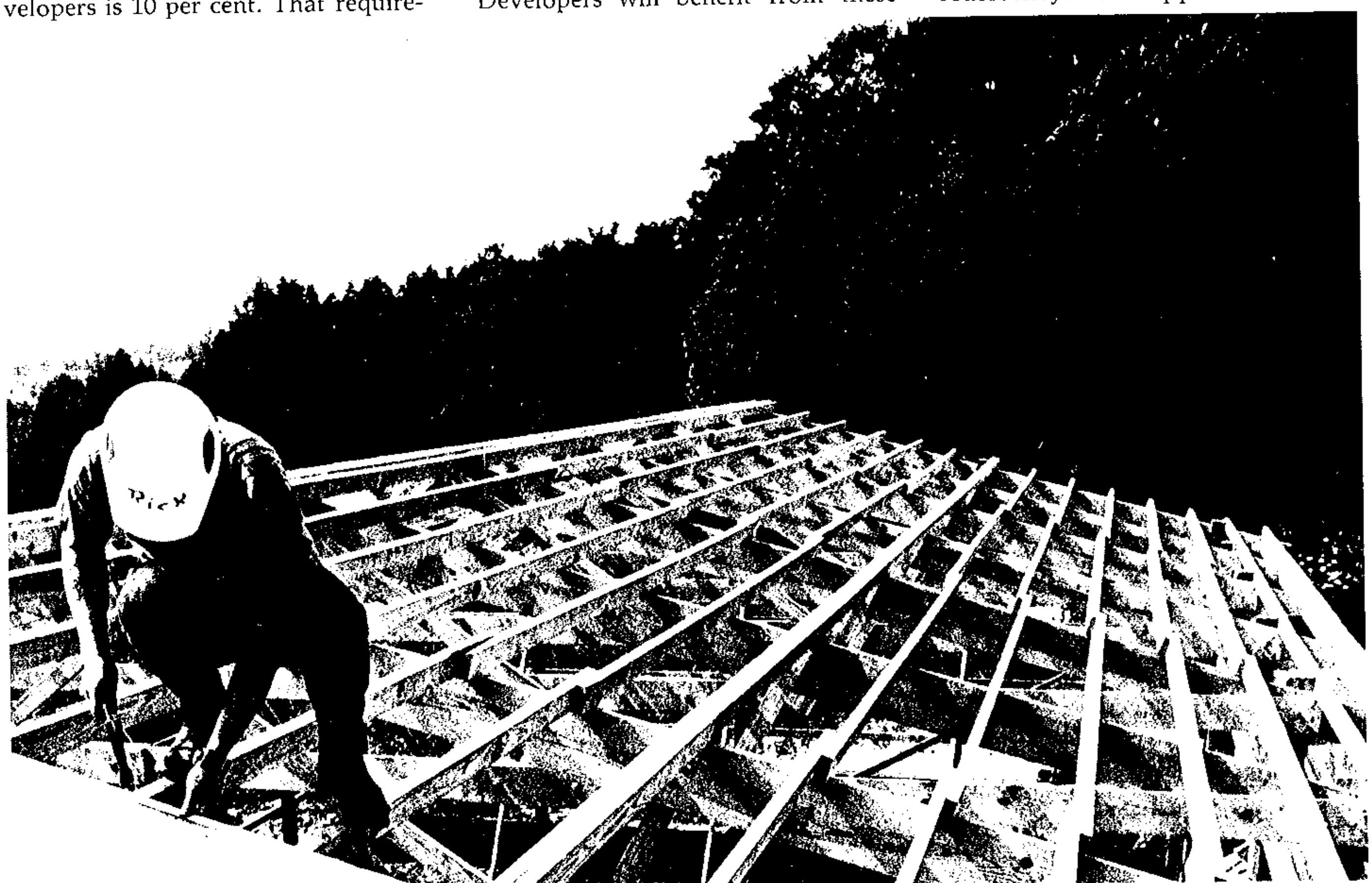
The Agency was created to insure an attractive investment climate for developers. It also offers builders a number of incentives for using its services over those of traditional lending institutions. And the entire mechanism, from attracting developers to management of the completed residences, is designed to include the safeguards inherent in business-oriented operations.

First, the equity requirement for developers is 10 per cent. That requirement is enhanced further by the fact that the current market value of the land for the project...no matter what the acquisition cost...may be used as part of that equity.

There is also a profit incentive for developers. If a project operates at a profit, the developer may earn as much as an eight per cent return on equity while at the same time benefiting from the tax benefits of accelerated depreciation. The sponsor also may collect a management fee if he elects to take on that responsibility.

Construction will be financed through the issuance of notes and bonds. Developers will benefit from these lower interest rates; allowing them to create housing with rental charges below those of the current market. Given the present interest squeeze, the Agency stands almost alone in providing loans at interest rates that will permit the development of housing for families with moderate incomes at costs they can afford.

PHFA will examine proposals carefully and make decisions with a minimum of red tape, thus assuring developers of prompt notifications on projects. The Agency screening procedure will include analyses of community needs and development feasibility. Each application is re-



viewed to assure the proposal is sound physically and economically and will generate sufficient income from rents to pay all operating costs plus principal and interest. Before final approval of a project, studies also are conducted on the background of the developer, site selection, construction costs, and the possibility of obtaining Federal subsidies. The Agency has received more than fifty applications for loans for the construction of multi-unit rental structures. That volume of inquiries is encouraging since the applications indicated a willingness on the part of many prominent developers to make initial cash outlays even before the court case was completed. We believe that the elimination of this last obstacle to Agency financing and this, our first real public relations effort, will greatly increase the number of developers entering our program.

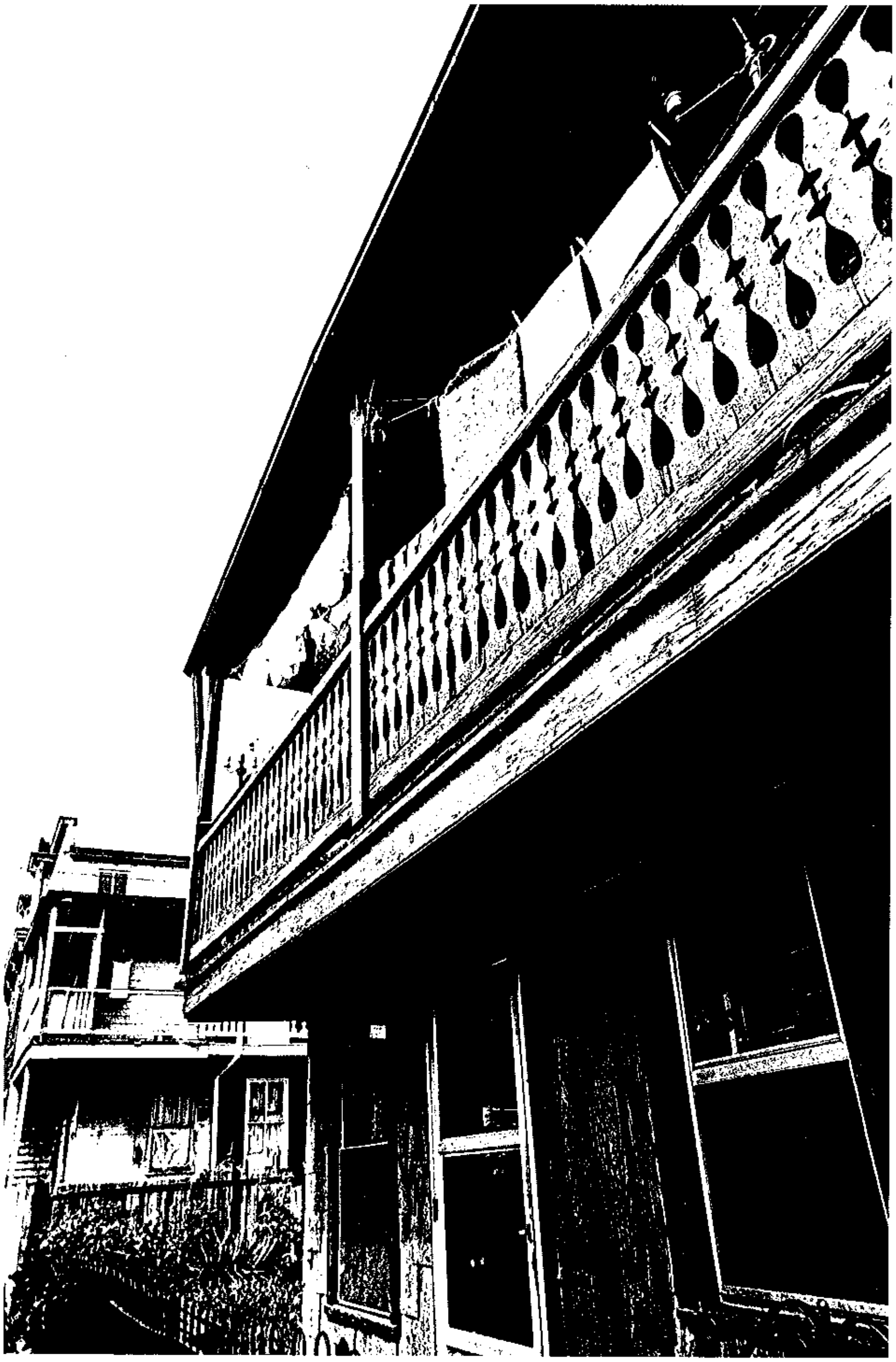
PHFA anticipates financing 3,000 units at a total cost of $40 to $60 million in fiscal 1974. The Agency expects to participate in the development of $100 million worth of construction during fiscal 1975.

The Agency is self-supporting with operating expenses and staff salaries covered by fees paid to the Agency by developers. The PHFA charges a fee of two per cent of the mortgage, payable at the initial closing for expenses incurred in issuing notes and bonds and preliminary project reviews. For administering outstanding notes and bonds, servicing the loans and supervising management of the development, the Agency will charge an annual fee of one-half per cent of the initial face amount of the mortgage.

Under the Housing Finance Agency Law, PHFA may lend funds to qualified developers for the construction, reconstruction or rehabilitation of rental and single-or multi-family units. The bonds and notes issued for housing construction will be payable out of Agency revenues, including the proceeds of its mortgage loans. The

bonds and notes are, under the law, not debts of the Commonwealth or any of its subdivisions.

The Agency is required to maintain a capital reserve fund with monies equal to the entire principal and interest payment due on its bonds and notes during the calendar year. If it anticipates any deficiencies in the fund or defaults in the payment of interest



and principal during the year, the Agency must submit an estimate of the needed funds to the Governor and General Assembly. The Governor then must place the amount of the deficiency in the State budget.

Loans for construction may not exceed 90 per cent of the approved project cost in the case of profit motivated developers. Individual loans may not exceed 98 per cent of the first $20,000 of the cost, or 95 per cent of the excess above $20,000.

The review of mortgage applications will be made according to conventional lending standards. The cost of development and construction must be covered by the loan plus equity. Income from rents and other charges must service the debt and pay for management, maintenance and taxes.

The Agency will first concern itself with the financing of rental projects and later single-family dwellings. The development of homes and condominimums, whose traditionally lower default rate will provide another layer of security, is unique for housing finance agencies. Condominium and house purchases will be limited to those families with adjusted incomes of less than $15,000 annually. Those persons wishing to rent must have annual income not exceeding seven times the yearly rental rate.

Staff

The Agency currently is carrying out its work with a staff of eight: an Executive Director, a Finance Director, two Housing Development Officers, a Technical Services Director, two Secretaries and an Administrative Assistant. When its programs are fully operational, the Agency will have a staff of between 40 and 50, including a number of field representatives.

The agency staff already has outgrown its present headquarters and will be moving to new and larger facilities in the near future.

The man responsible for coordinating the operation of the PHFA is John McCoy, the Executive Director. Mr. McCoy came to the Agency from Illinois, where he had been Development Administrator of that state's Housing Development Authority. He has had previous experience with the New Jersey Housing Finance Agency and five years with the Real Estate Investment Department of the Prudential Insurance Company of America.

The Director of Finance, Marc S. Moonin, is a certified public accountant with considerable experience in both the public and private sector. His duties at PHFA include supervision of all accounting functions as well as investment decisions.

The Director of Housing Development will evaluate development sites and make recommendations for changes in program where necessary. He has primary responsibility for insuring that development proposals are economically sound. Mr. McCoy currently holds the position in addition to his duties as Executive Director. It is his job to supervise the Housing Development Officers.

Carl Payne and Samuel W. Smith Jr., the Housing Development Officers, will be responsible for making market studies, determining the economic feasibility of developments and investigating the possibilities for Federal subsidies.

Mr. Payne, a graduate of Indiana University of Pennsylvania, joined the Agency after two years as Director of the Program Planning and Neighbor-

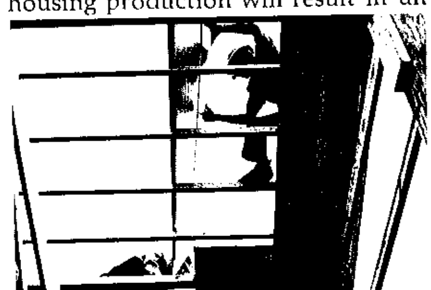
hood Operations Division of the Pittsburgh Urban Redevelopment Authority. His background includes housing-related work in public and private sector organizations. He earned a Master's Degree in Urban and Regional Planning at the University of Pittsburgh.

Mr. Smith, who holds a Bachelor's Degree from the University of North Carolina, has had three years' experience in community and housing development with the Pennsylvania Department of Community Affairs. He had housing and redevelopment program responsibility for a 24-county service region for the Commonwealth.

The Director of Technical Services, Merle Easton, is responsible for the architectural review of each proposed development. A registered architect, Ms. Easton is a graduate of the University of Washington. She has served as staff and project architect for three architectural firms before joining the Agency.

Complementing the staff are professional firms with expertise in the important financing area. Senior managing underwriter is Salomon Brothers. Co-managers are Paine, Webber, Jackson & Curtis; Mellon Bank, N.A.; and the Philadelphia National Bank. Peat, Marwick, Mitchell & Co. is the Agency's auditor and the firms of Mudge, Rose, Guthrie & Alexander and Schnader, Harrison, Segal & Lewis are co-bond counsels. General counsel is McNees, Wallace & Nurick.

In addition to providing urgently needed housing, the work of the Agency will have an important effect on Pennsylvania's economy. When in full swing, the Agency's investment in housing production will result in un-



counted new jobs, generate sales tax revenue to the State, and increase the local real estate tax base.

The PHFA is taking a business-like approach to solving the housing shortage in Pennsylvania. Through built-in incentives, it is helping qualified developers speed up the rate of new construction. The overall effect of the Agency's operation is to ease the financial burdens of both developers and home buyers and renters while at the same time meeting the housing needs of the Commonwealth of Pennsylvania.

Summary of Significant Accounting Policies
June 30, 1973

Authorizing Legislation

The Pennsylvania Housing Finance Agency is a body corporate and politic created by the Housing Finance Agency Law, December 3, 1959, P.L.1688, as amended. The Act became effective March 27, 1961 when the Governor declared by proclamation that sufficient funds were available for its administration. The Agency was activated July 11, 1970 upon the signing of a grant contract funded by appropriations of the Legislature in its 1970 session.

Pursuant to the Act, the Agency is authorized and empowered to finance the construction and rehabilitation of housing units for sale or rent to low and moderate income persons or families or the elderly. Bonds and bond anticipation notes issued under the provisions of the Act shall not be deemed to constitute a debt liability of the Commonwealth of Pennsylvania or any subdivision thereof.

General Fund Balance

The Agency's General fund was established for the purpose of receiving all monies which may be made available to the Agency from any source, other than the proceeds from the issuance and sale of notes or bonds by the Agency. The fund is used for the payment of all expenses for organization, development and operations as the Agency shall deem necessary to carry out the provisions of the Housing Finance Agency Law.

Capital Reserve Fund Balance

The Capital Reserve fund is designated for any monies appropriated and made available by the Commonwealth of Pennsylvania for the purpose of such fund and any proceeds from the sale of notes or bonds to the extent provided in the resolution of the Agency authorizing issuance thereof.

The Agency has the power to invest any funds not required for immediate disbursement. All other monies in the Capital Reserve fund are restricted to the following types of payments applicable to the Agency's bonds and notes:

a. principal at maturity
b. interest
c. redemption premium
d. repurchase of bonds
e. sinking fund established for the amortization of term bonds

Any interest or income earned by the Capital Reserve fund due to investments may be transferred to the General fund or any other fund of the Agency to the extent it does not reduce the fund below the maximum principal and interest maturing and becoming due on all bonds or other amounts earmarked for the Capital Reserve fund by grant contracts and provisions of appropriation laws.

Operations

Mortgage loans are carried at face value as of the date of purchase with the related discount amortized over the term of the mortgage. Income on investment on all funds is accrued as it is earned.

Operating expenses include salaries and related benefits of employes, legal fees, professional and contracted services, and general and administrative expenses. Such costs and expenses are charged to operations in the General fund when the services or materials are received.

The Agency follows the accrual basis of accounting except that furnishings, fixtures and equipment are charged to operations when purchased and, accordingly, no depreciation is recorded in the statement of revenues and operating expenses, and statement of changes in fund balances. However, these assets are reported in the General fund assets and fund balance at cost.

Statement of Assets, Liabilities and Fund Balances
June 30, 1973

Assets	General fund	Capital Reserve fund	Combined total
Cash	$ 15,079	8,535	23,614
Temporary investments	694,466	569,352	1,263,818
Accrued interest receivable	3,185	18,066	21,251
Mortgage loans receivable, less unamortized discounts of $24,813 (note 1)	–	1,364,047	1,364,047
Other receivables	3,124	–	3,124
Furnishings, fixtures and equipment	9,943	–	9,943
	$ 725,797	1,960,000	2,685,797

Liabilities and Fund Balances	General fund	Capital Reserve fund	Combined total
Accounts payable	$ 25,583	–	25,583
Total liabilities	25,583	–	25,583
Unrestricted	690,271	–	690,271
Investment in fixed assets	9,943	–	9,943
Restricted	–	1,960,000	1,960,000
Total fund balances	700,214	1,960,000	2,660,214
	$ 725,797	1,960,000	2,685,797

See accompanying statement of significant accounting policies and notes to financial statements.

Statement of Revenues and Operating Expenses
Year ended June 30, 1973

Revenues	General fund	Capital Reserve fund	Combined total
Interest income:			
Investments	$ 32,528	34,541	67,069
Mortgages, net (note 1)	—	64,704	64,704
Reimbursement from Federal government for flood loss (note 6)	12,097	—	12,097
Total Revenues	44,625	99,245	143,870
Operating expenses			
Salaries and related benefits	39,908	—	39,908
Legal fees	41,981	—	41,981
Professional and contracted services	13,900	—	13,900
Furnishings, fixtures and equipment	9,943	—	9,943
General administrative	21,098	—	21,098
Total operating expenses	126,830	—	126,830
Excess (deficiency) of revenues over operating expenses	$ (82,205)	99,245	17,040

Statement of Changes in Fund Balances
Year ended June 30, 1973

	General fund			Capital Reserve fund	Combined total
	Unrestricted	Investment in fixed assets	Total		
Fund balances at beginning of year	$ 519,715	—	519,715	2,103,244	2,622,959
Prior period adjustment (note 5)	—	—	—	10,272	10,272
Fund balances at beginning of year, as restated	519,715	—	519,715	2,113,516	2,633,231
Excess (deficiency) of revenues over operating expenses	(82,205)	—	(82,205)	99,245	17,040
Purchase of fixed assets		9,943	9,943		9,943
Transfer to General fund	252,761	—	252,761	(252,761)	—
Fund balances at end of year	$ 690,271	9,943	700,214	1,960,000	2,660,214

See accompanying statement of significant accounting policies and notes to financial statements.

1. Mortgage Loans

Mortgage loans are secured by first mortgage liens on single-family homes located within Pennsylvania. All are insured by the Federal Housing Administration (FHA) and mature between November 1990 and November 2002. The mortgages bear a 7% interest rate; however, the Agency has provided an interest reduction rider to reduce rates to as low as 5% per annum. The interest reduction rider provides for graduated interest rate increases when the mortgagor's income exceeds limits as established in the rider.

All such loans were purchased from FHA approved mortgage companies and these companies service the mortgages. During the current year, service fees amounted to $4,710 which has been netted against mortgage interest income.

All mortgages were purchased at a discount from face value. These discounts are being amortized over the remaining terms of the mortgages on a straight-line basis.

2. Pension and Retirement Plan

Employes of the Agency are covered by the State Employes' Retirement Board of the Commonwealth of Pennsylvania. Retirement plan payments, based on 7% of gross wages, amounted to $2,791 for the period ended June 30, 1973. Effective July 1, 1973, the contribution rate was increased to 8% of gross wages.

3. Lease Agreements

The Agency's office premises are occupied under the terms of a lease agreement which expires on December 31, 1973. The lease provides for payments in the amount of $2,604 during the six months ended December 31, 1973.

4. Litigation

A taxpayer's action was filed in the Supreme Court of Pennsylvania on February 7, 1973 to determine the constitutionality of the Housing Finance Agency Law as enacted by the General Assembly of the Commonwealth of Pennsylvania.

In the opinion of counsel and management of the Agency, the constitutionality of the Agency and its enabling legislation will be upheld.

5. Adjustment of Provision for Mortgage Losses

Under the terms of the mortgage sale and servicing agreements between the Agency and the servicing companies, the Agency purchases only mortgages insured by Federal Housing Administration. Furthermore, under the servicing agreement, all obligations of the Agency are discharged as mortgagee by the servicing company as set forth in the contract of insurance with the Federal Housing Commissioner; therefore, the Agency is not subject to loss on approved mortgage purchases. Therefore, in the opinion of the Agency, the provision for mortgage loan losses as reported on the prior financial statement is not deemed necessary. Accordingly, the beginning Capital Reserve fund balance has been restated in the amount of $10,272 to reflect the restoration of the provision in a previous year for mortgage losses.

6. Federal Reimbursement for Flood Loss

The Agency received a grant from the Federal government for losses sustained during the flood of 1972. The grant provided reimbursement for the following expenses:

Salaries and related benefits	$ 375
Professional and contracted services	2,468
Furnishings, fixtures and equipment	5,748
General administrative	3,506
	$12,097

At June 30, 1973, the Agency had a balance due from the Federal government under the grant in the amount of $3,024. Such amount is to be received from the government upon completion of a final audit by the Office of Emergency Preparedness.

7. Other Matters

On April 24, 1972 the Auditor General of the Commonwealth of Pennsylvania recommended that estimated surplus funds of $824,825 be returned to the General fund of the Commonwealth until such time as they are required by the Agency, and estimated earned surplus interest of $125,175 be returned permanently. On advice of counsel, the Agency is of the opinion that the Housing Finance Agency Law does not require the return of such funds. In addition, it is the contention of management that the passage of the Housing Finance Agency amendment, Act 282, 1972, further strengthens the Agency's position that these funds are required for the purposes of the Agency and need not be returned to the Commonwealth.

Statement of Cash Receipts and Disbursements (Schedule 1)
Year ended June 30, 1973

	General fund	Capital Reserve fund	Combined total
Cash balances at beginning of year	$ 150,538	25,926	176,464
Receipts:			
Proceeds from temporary investments	—	250,250	250,250
Interest income:			
Investments	33,281	28,721	62,002
Mortgages, net of service fees	—	61,991	61,991
Reimbursement from Federal government for flood loss	9,073	—	9,073
	42,354	340,962	383.316
Disbursements:			
Purchase of temporary investments	65,595	—	65,595
Purchase of mortgage loans	—	358,353	358,353
Operating expenses	112,218	—	112,218
	177,813	358,353	536,166
Cash balances at end of year	$ 15,079	8,535	23,614

Report of Independent Certified Public Accountants

To the Members of the Pennsylvania Housing Finance Agency:

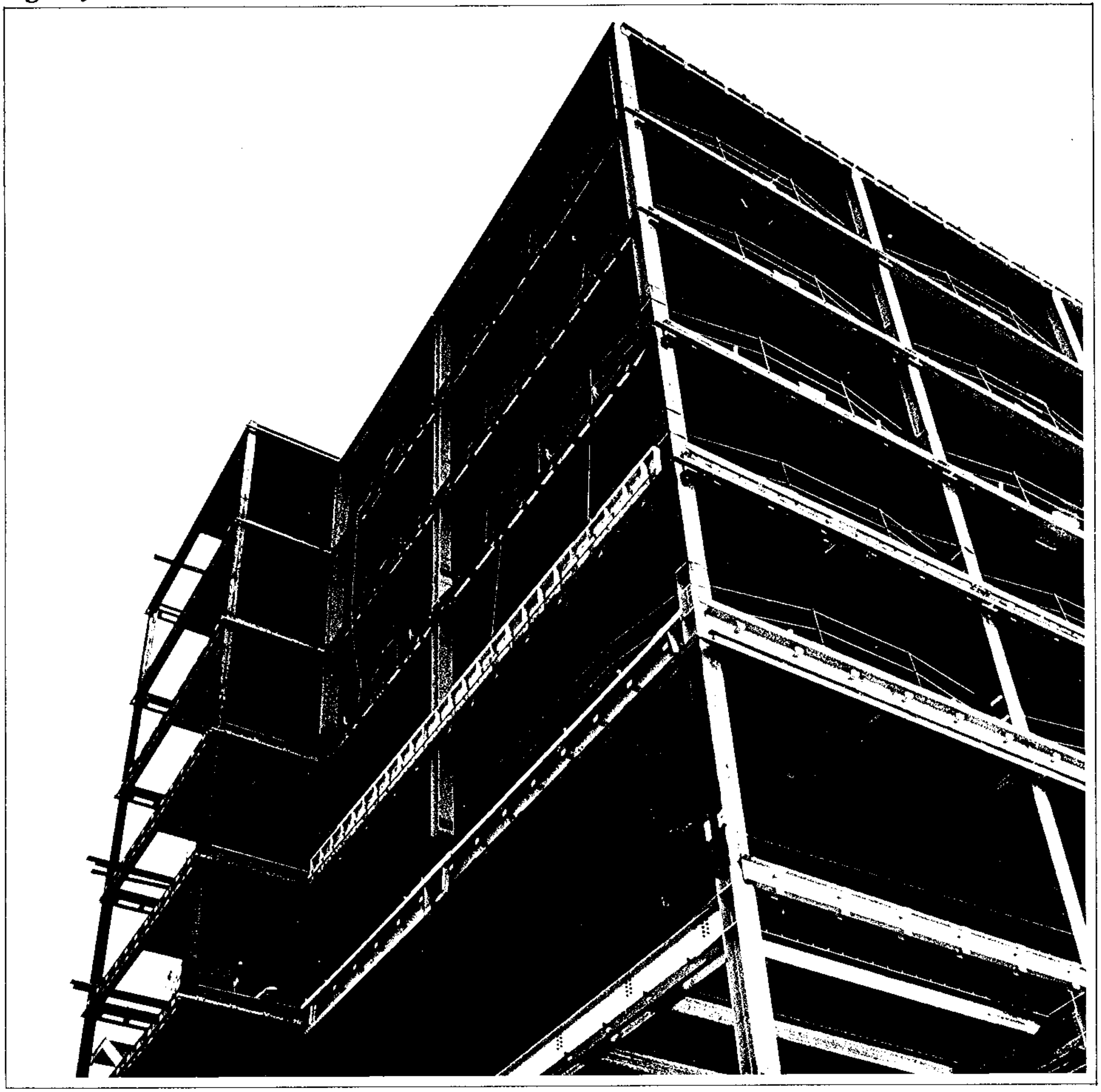
We have examined the statement of assets, liabilities and fund balances of the Pennsylvania Housing Finance Agency as of June 30, 1973, and the related statements of revenues and operating expenses and changes in fund balances for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, such financial statements present fairly the assets, liabilities, and fund balances of Pennsylvania Housing Finance Agency at June 30, 1973 and the revenues and operating expenses and changes in fund balances for the year then ended, in conformity with generally accepted accounting principles applied on a basis consistent with that of the preceding year. The current year's supplementary data included in schedule 1 has been subjected to the same auditing procedures and, in our opinion, is stated fairly in all material respects when considered in conjunction with the basic financial statements taken as a whole.

Peat, Marwick, Mitchell & Co.

August 6, 1973

Pennsylvania
Housing
Finance
Agency



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