The Housing Authority of the City of Mission Viejo

Treasurer's Annual Report

Fiscal Year Ended

June 30, 2018

Treasurer's Annual Report

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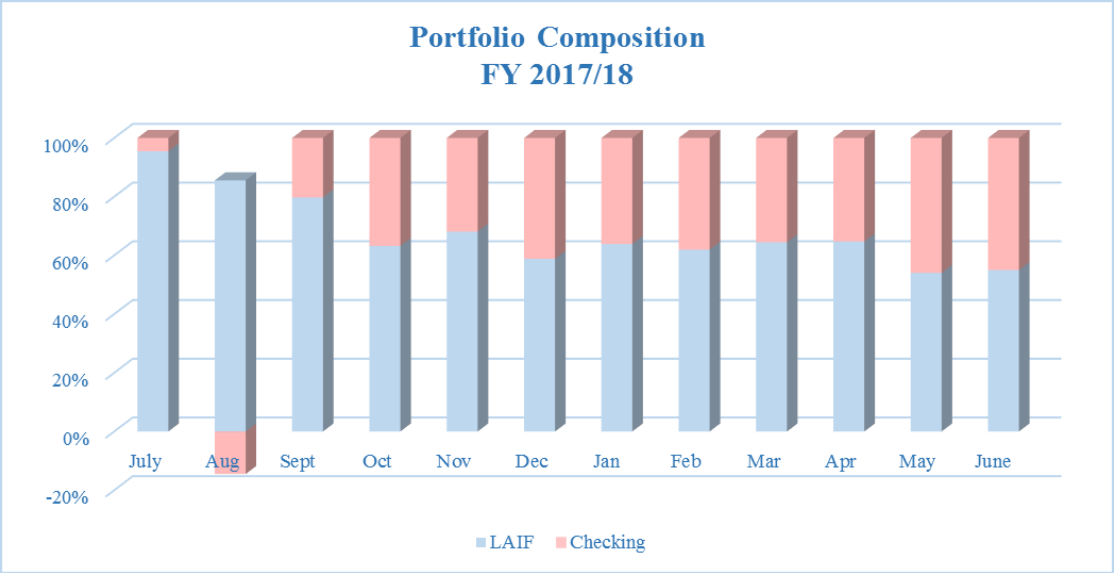
INTRODUCTION

The Mission Viejo Housing Authority (MVHA) was formed in February 2011 in anticipation of redevelopment dissolution. Upon dissolution of the City's former redevelopment agency on February 1, 2012, the MVHA became the "Housing Successor" of the former redevelopment agency's Low and Moderate Income Housing Assets. The purpose of the MVHA is to facilitate development and rehabilitation of affordable housing and programs and services that support the city's affordable housing goals. After the formation of the MVHA and prior to the end of fiscal year June 30, 2011, $5.7 million in assets were transferred from the former redevelopment agency to MVHA in anticipation of subsidies for affordable housing as required by a Settlement Agreement and Judgement dated July 14, 2008. During fiscal year 2011/12 and at redevelopment dissolution, the balance of cash and investments held in the former redevelopment agency's Low and Moderate Income Housing Fund, in the amount of $1.478, were transferred to MVHA as the Housing Successor.

PORTFOLIO COMPOSITION

The portfolio of the MVHA has consisted of funds on deposit at the State of California Local Agency Investment Fund (LAIF). The following chart illustrates the composition of the portfolio between LAIF and the MVHA's checking account during fiscal year 2017/18. The checking account had a negative balance at the end of August due to checks issued at the end of the month, but released and funded the following month. At June 2018, cash and investments totaled $119,222 and consisted of $65,596 invested in LAIF.



PERMITTED INVESTMENTS

The MVHA Investment Policy's three major objectives are, in order of priority:

1) Safety of principal, in compliance with applicable laws
2) Maintain sufficient liquidity to meet cash flow needs
3) Attain a market average rate of return consistent with the primary objectives of safety and liquidity

Fiscal year 2017/18 investment activity was continuously focused on these objectives, in that order.

The investment policy list of permitted investments includes U.S. Treasury securities, securities issued by U.S. Government agencies, banker's acceptances, federally insured and collateralized time deposits, negotiable certificates of deposit, repurchase agreements, state and local government investment pools, and government money market funds. Generally, the investment policy would restrict the maximum investment in a specific investment pool; however, due to the low cash and investment balance, the MVHA investment policy allows that 100% of the MVHA cash and investment balance may be invested in LAIF while the total portfolio balance is smaller than $5 million. The advantages offered by LAIF include its safety, liquidity, favorable short term interest rates, and a streamlined administrative process. Funds on deposit at LAIF also have same day availability. The MVHA portfolio only included those investments allowed in the Investment Policy during the fiscal year 2017/18.

The Investment Policy requires annual disclosure to the Board of investment practices of investment pools and government money market funds in which the MVHA participates, which differ from the MVHA's own policies.

LAIF

The MVHA may not invest directly in reverse repurchase agreements, however it should be noted that the State Treasurer's Statement on Portfolio Management Goals, Objectives and Policies allows reverse repurchase agreements up to ten percent of the State's total portfolio of approximately $88.8 billion. The Local Agency Investment Fund (LAIF) program constitutes approximately 26.6% of that portfolio. All reverses in the State's portfolio are cash matched either to the maturity of the re-investment or an adequately positive cash flow date which is approximate to the maturity of the reinvestment. In addition, only securities already held in the portfolio and unencumbered may be reversed. No item purchased against a reverse will be used as a reversible security while the original reverse is outstanding. As of June 2018 the State's total portfolio did not include any reverse repurchase agreements.

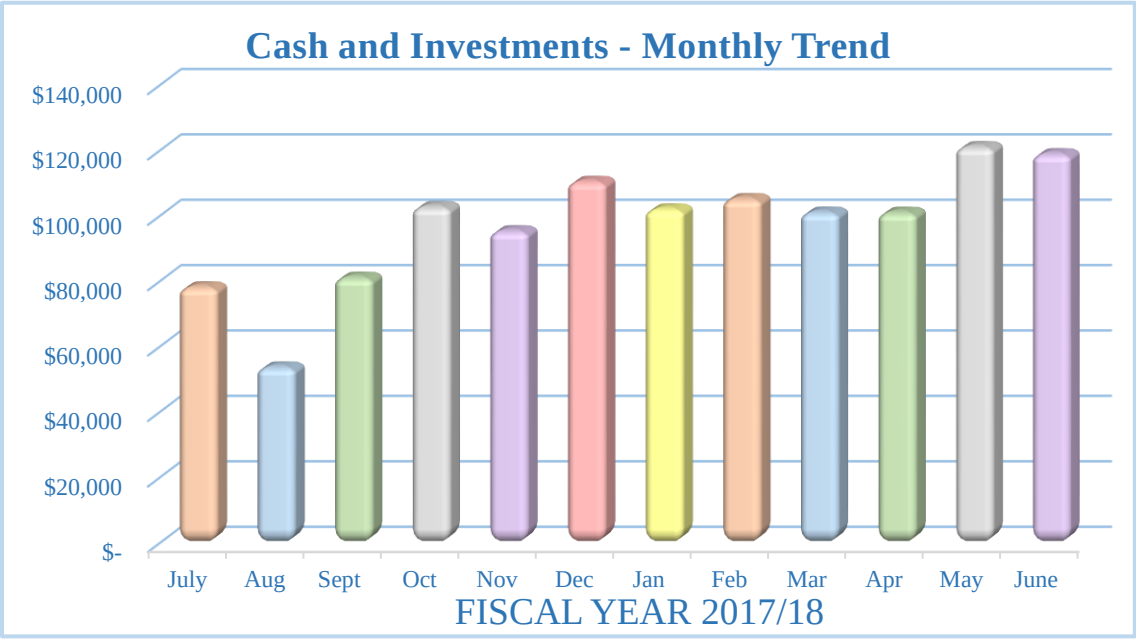
The State pool also allows investment in Bank Notes, Corporate Bonds, Structured Notes, Asset-Backed Securities, Pooled Loans and Strips, investment vehicles not permitted in the City's 2017/18 investment policy. Bank Notes are senior, unsecured promissory notes issued in the United States on either an underwritten or continuously-offered basis by domestic commercial banks. The Notes represent senior debt of the bank and have a maximum maturity of one year.

Bank Notes are not deposits and are not insured by the Federal Deposit Insurance Corporation (FDIC) or any other insurer. The State had $900 million in Bank Notes in their portfolio, 1.01% of total portfolio holdings. The State's investment in Corporate Bonds is limited to "blue chip" companies with credit ratings within the top three ratings of a nationally recognized rating service, nothing lower than an "A" rated company. There is no limit on what percent of its portfolio may be invested in these instruments. There is no maximum maturity either; however, the State's practice is to keep the maturities at five years or less. As of June 2018, the State did not own any Corporate Bonds. Structured notes are debt securities whose cash flow characteristics (coupon rate, redemption amount, or stated maturity) depend upon one or more indices and/or that have embedded forwards or options. They are issued by corporations and by government-sponsored enterprises or an international agency such as the World Bank. As of June, 2018, the State held $825 million in structured notes, 0.93% of total portfolio. Asset-backed securities entitle the purchaser to receive a share of the cash flows from a pool of assets such as principal and interest repayments from a pool of mortgages, small business loans, or credit card receivables. As of June 2018, the State held $1.55 million (1.74% of portfolio) of asset-backed securities. Pooled Loans represent interim financing to State agencies with pending, publicly approved bond issues. These loans have a maximum maturity of one year. As of June 2018, the State had $734 million, or 0.83% of portfolio, outstanding in Pooled Loans. U.S. Treasury STRIPS (Separate Trading of Registered Interest and Principal of Securities) are issued by the Treasury as zero-coupon bonds and represent the principal or interest coupon payments from selected Treasury notes and bonds. The value of STRIPs is based on the interest rate market and is not based on the value of the underlying securities. As of June 30, the State did not own any STRIPs.

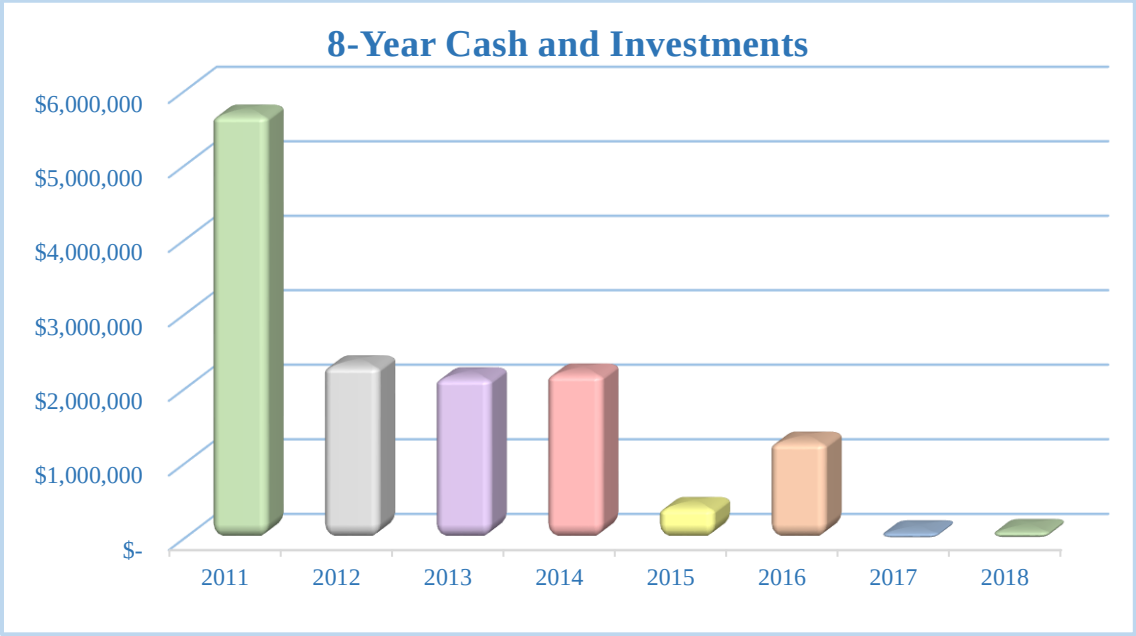
LAIF reports a factor representing the Agency's participation in market value changes in the LAIF pool. The reporting of balances on deposit with LAIF reflects this factor. On June 30, 2018 LAIF market value was 99.8127% of the amortized cost. As previously stated, LAIF funds now represent 26.6% of the State's portfolio. During this fiscal year, the State portfolio has increased in size from $77.6 billion at June 30, 2017 to $88.8 billion at June 30, 2018. LAIF membership has decreased from 2,439 participants at July 2017 to 2,409 participants at June 2018. LAIF balances have decreased from $22.8 to $22.5 billion during that time frame.

PORTFOLIO SIZE AND TRENDS

The size of the portfolio averaged about $97,900 during the fiscal year. There is minimal activity in the portfolio. Increases and decreases are typically due to quarterly expense reimbursements or loan repayments. Cash and investments decreased from July to August by approximately $25,000 due to legal services and a reimbursement to the City for payroll costs incurred during the last quarter of the previous fiscal year. In September and October there were increases to the portfolio because of a reimbursement from the Successor Agency for payroll costs and a housing rehab loan repayment. The City received a second housing rehab loan repayment in May causing the balance to increase again in that month.



The cash and investment balance has declined significantly since MVHA formation as shown in the following graph.



Significant transactions causing this decline include:

As stated in the Introduction section, the MVHA was established during fiscal year 2010/11 and was initially funded with $5.7 million in assets from the former redevelopment agency. Of this amount, $4.8 was obligated under an affordable housing agreement for apartments that were to be built adjacent to the Mission Viejo Golf and Country Club along Oso Parkway. These funds were disbursed in January 2012 and is reflected in the sharp decline in assets between 2011 and 2012. Following redevelopment dissolution, a due diligence review was performed by an independent auditor under redevelopment Dissolution Law to assist the Department of Finance (DOF) in determining how the assets of the former redevelopment agency should be disbursed. The DOF determined that of the $5.7 million initial deposit to MVHA, $4.8 million was disallowed; therefore during fiscal year 2012/13 the housing agreement was voided and the $4.8 million was remitted to the County or Orange Auditor-Controller.

The graph shows a second significant decrease in cash and investment balance from 2014 to 2015 as a result of the acquisition of land, commonly referred to as Site C, by the MVHA for future affordable housing development. At the time of acquisition in May 2015, the MVHA made an initial down payment on the property of $2.6 million, with the balance owed under an executed promissory note between the MVHA and the City. Additional information regarding the promissory note is discussed further in this report.

The increase reflected in 2016 is due to the repayment of the Heritage Villas affordable housing agreement loan. Total loan repayment in September 2015 was $1.8 million, of which $1.14 million was due to the MVHA.

The decline that occurred in 2017 is a result of Site C loan payments to the City in the amount of $1,780,000. Additional resources available to make this payment were the receipt of the balance of a loan between the MVHA and the Successor Agency, under Dissolution Law, in the amount of $454,920 in July 2016.

SIGNIFICANT HOUSING AUTHORITY ASSETS

ARROYO VISTA AFFORDABLE HOUSING LOAN AGREEMENT

In October 1994, the Mission Viejo Community Development Agency (now the Successor Agency) loaned $401,000 to a developer in accordance with an affordable housing agreement executed by the Agency and the Developer on July 1, 1994. The note bore no interest during the first two years after the date of the note, and bears simple interest at the rate of 3% per annum thereafter until the note is paid in full. No payments were required to be made on the note during the first five years. Thereafter, annual payments of principal and interest amortized over a thirty year period are due. Loan repayments have been used to fund annual operating expenses of the MVHA. As of June 30, 2018, the outstanding balance is $222,530 which includes unpaid accrued interest of $23,511. Unless paid off in advance, this loan is expected to mature in October 2029.

HOUSING REHABILITATION LOAN PROGRAM

The objective of the housing rehabilitation program is to maintain the quality of housing in neighborhoods for low and very low income households by providing deferred loans to owner occupants who meet low and very low income thresholds. There are 14 outstanding loans totaling $260,911 with an average loan balance of $18,600. Loan repayments have been used to fund annual operating expenses and payments on the Site C loan balance.

LENNAR HOMEBUYER LOAN AGREEMENTS

The former redevelopment agency entered into an agreement with Lennar Homes to provide housing subsidies for 22 low and moderate income housing units in The Ridge housing development. Upon dissolution, the MVHA became the successor to this agreement under redevelopment Dissolution Law. At the time of purchase of each unit by a qualified buyer, a homebuyer loan agreement was executed between MVHA and the homebuyer. If one of these 22 units is sold to an unqualified buyer, some balance of the housing loan is required to be paid back to the MVHA. To date, there have been 2 units sold to unqualified buyers (one during fiscal year 2014/15 and one in 2016/17), resulting in repayments to MVHA in the amount of $410,351. It is not the expectation of the MVHA that these loan be paid off, but forgiven over a forty year covenant period. However, as was the case with 2 units previously noted, future repayments may occur. Any future repayments will be used toward Site C loan payments.

SIGNIFICANT HOUSING AUTHORITY LIABILITIES

SITE C PROMISSORY NOTE

In May 2015, the MVHA acquired City of Mission Viejo owned property for the purpose of facilitating the development of affordable housing on a site referred to as Site C. The initial purchase price of $6.9 million was based on current appraised value. At the time of acquisition, the MVHA paid $2.6 million from available MVHA funds as a down payment. A promissory note between the MVHA and the City of Mission Viejo was executed for the balance of $4.3 million. Loan payments are scheduled as resources become available. Resources include loan repayments from the Arroyo Vista loan, housing rehabilitation loan repayments and Lennar homebuyer loan repayments. The table below shows historical Site C promissory note activity. The last payment against the promissory note was in July 2017 for $123,000. The balance of the note is $2,125,000 at June 30, 2018.

Site C Loan Repayment Schedule

Date	Payments	Balance
6/26/15		$4,300,000
8/3/15	272,000	4,028,000
8/2/16	1,600,000	2,248,000
6/14/17	180,000	3,848,000
7/31/17	123,000	2,125,000

Based on the cash and investment balance at June 30, 2018 of $119,222 and projected budget activity for the next fiscal year as presented under Anticipated Cash and Investment Activity later in this report, no payments against the Site C promissory note are planned for fiscal year 2018/19.

RETURN ON INVESTMENT

Close of the accounting records for fiscal year 2017/18 is in progress. The estimated interest earnings for fiscal year 2017/18 is projected to be $7,771 compared to $10,424 in fiscal year 2016/17, a projected decrease of $2,653. Interest earned from LAIF for the fiscal year totaled $956 compared to $2,602 last fiscal year. Also, earnings include interest received pursuant to the existing Arroyo Vista affordable housing loan agreement which decrease annually until the loan is paid off. The Arroyo Vista loan to the developer is discussed on page 8 of the report.

ANTICIPATED CASH AND INVESTMENT ACTIVITY

The cash flow projection for fiscal year 2018/19 is based on the adopted budget, and prior year historical cash flows. The projection shows that the portfolio balance will decrease by $34,145 during fiscal year 2018/19. Arroyo Vista loan interest and principal payments are projected to generate $22,355 and general interest earnings are projected in the amount of $1,000. Budgeted expenditures for the fiscal year include administrative costs, and legal, professional, and auditing services. Staff anticipates available resources will remain well below $5 million in the coming fiscal year; therefore 100% of excess funds not needed for operating expenditures will remain on deposit at LAIF.

Cash Flow Forecast

Fiscal Year 2018-19

	Inflows	Outlflows	Change to Portfolio	
		Cash & Investments @ 6/30/18		$ 119,223
July	$ 12,355	$ 39,482	$ (27,127)	92,095
August	-	7,471	(7,471)	84,624
September	3,146	337	2,810	87,434
October	2,777	1,092	1,685	89,119
November	-	2,255	(2,255)	86,865
December	2,463	2,210	253	87,118
January	22	2,634	(2,612)	84,506
February	351	3	348	84,854
March	-	1,258	(1,258)	83,596
April	26	90	(64)	83,531
May	2,214	3	2,211	85,742
June	-	664	(664)	85,078
Total	**23,355**	**57,500**	**(34,145)**	

INVESTMENT POLICY COMPLIANCE

As the Finance Officer of the Housing Authority of the City of Mission Viejo, I certify that I have complied with the annual Investment Policy adopted by the City Council effective September 12, 2017.

8/22/18

Cheryl Dyas
Director of Administrative Services/
City Treasurer

Date