

FINANCIAL STATEMENTS AND  
INDEPENDENT AUDITORS' REPORT

**COMMUNITY DEVELOPMENT ADMINISTRATION  
LOCAL GOVERNMENT INFRASTRUCTURE BONDS  
(AMBAC INSURED)**

JUNE 30, 2004 AND 2003

Community Development Administration  
Local Government Infrastructure Bonds (Ambac Insured)

TABLE OF CONTENTS

	PAGE
INDEPENDENT AUDITORS' REPORT	3
FINANCIAL STATEMENTS	
STATEMENTS OF NET ASSETS	4
STATEMENTS OF REVENUE, EXPENSES AND CHANGES IN NET ASSETS	5
STATEMENTS OF CASH FLOWS	6
NOTES TO FINANCIAL STATEMENTS	7

## INDEPENDENT AUDITORS' REPORT

Office of the Secretary  
Department of Housing and Community Development

We have audited the accompanying financial statements of the Community Development Administration Local Government Infrastructure Bonds (Ambac Insured) (the Fund) of the Department of Housing and Community Development of the State of Maryland as of and for the years ended June 30, 2004 and 2003 as listed in the table of contents. These financial statements are the responsibility of the Fund's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes 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.

As discussed in Note A, the financial statements present only the Community Development Administration Local Government Infrastructure Bonds (Ambac Insured) and do not purport to, and do not, present fairly the financial position of the Department of Housing and Community Development of the State of Maryland as of June 30, 2004 and 2003, and the changes in its net assets and cash flows, where applicable, thereof for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to in the first paragraph present fairly, in all material respects, the financial position of the Community Development Administration Local Government Infrastructure Bonds (Ambac Insured) of the Department of Housing and Community Development of the State of Maryland as of June 30, 2004 and 2003, and the changes in its net assets and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.



Baltimore, Maryland  
September 28, 2004

Community Development Administration  
Local Government Infrastructure Bonds (Ambac Insured)

STATEMENTS OF NET ASSETS  
(in thousands)

June 30, 2004 and 2003

	2004	2003
<b>RESTRICTED ASSETS</b>		
Restricted current assets		
Cash and cash equivalents on deposit with trustee	\$ 21,051	\$ 17,301
Community facilities loans	1,825	1,050
Accrued interest receivable	215	99
	23,091	18,450
Restricted long-term assets		
Community facilities loans, net of current portion	43,015	28,465
	\$ 66,106	\$ 46,915
<b>LIABILITIES AND NET ASSETS</b>		
Current liabilities		
Bonds payable	\$ 1,825	\$ 1,050
Accrued interest payable	208	94
Due to local governments	20,889	17,258
Accounts payable	118	-
	23,040	18,402
Long-term liabilities		
Bonds payable, net of current portion	43,015	28,465
Advance trustee fees	5	5
	43,020	28,470
Total liabilities	66,060	46,872
<b>NET ASSETS</b>		
Restricted	46	43
Total liabilities and net assets	\$ 66,106	\$ 46,915

See notes to financial statements

Community Development Administration  
Local Government Infrastructure Bonds (Ambac Insured)

STATEMENTS OF REVENUE, EXPENSES AND  
CHANGES IN NET ASSETS  
(in thousands)

Years ended June 30, 2004 and 2003

	<u>2004</u>	<u>2003</u>
Operating revenue		
Interest on community facilities loans	\$ 1,242	\$ 741
Interest income on cash equivalents	4	1
	<u>1,246</u>	<u>742</u>
Operating expenses		
Interest expense on bonds	<u>1,243</u>	<u>742</u>
Operating income	<u>3</u>	<u>-</u>
CHANGES IN NET ASSETS	3	-
Net assets at beginning of year	<u>43</u>	<u>43</u>
Net assets at end of year	<u><u>\$ 46</u></u>	<u><u>\$ 43</u></u>

See notes to financial statements

Community Development Administration  
Local Government Infrastructure Bonds (Ambac Insured)

STATEMENTS OF CASH FLOWS  
(in thousands)

Years ended June 30, 2004 and 2003

	2004	2003
Cash flows from operating activities		
Principal and interest received on community facilities loans	\$ 2,177	\$ 1,081
Origination of community facilities loans	(12,627)	(11,428)
Advance trustee fees received	12	10
Trustee fees paid	(12)	(6)
	(10,450)	(10,343)
Cash flows from investing activities		
Interest received on cash equivalents	4	1
	4	1
Cash flows from noncapital financing activities		
Proceeds from sale of bonds	16,375	18,115
Payments on bond principal	(1,050)	(390)
Interest on bonds	(1,129)	(689)
	14,196	17,036
NET INCREASE IN CASH AND CASH EQUIVALENTS ON DEPOSIT WITH TRUSTEE	3,750	6,694
Cash and cash equivalents on deposit with trustee at beginning of year	17,301	10,607
Cash and cash equivalents on deposit with trustee at end of year	\$ 21,051	\$ 17,301
Reconciliation of operating income to net cash used in operating activities		
Operating income	\$ 3	\$ -
Adjustments to reconcile operating income to net cash used in operating activities		
Increase in community facilities loans	(15,325)	(17,725)
Increase in accrued interest receivable	(116)	(50)
Increase in accrued interest payable	114	53
Increase in accounts payable	118	-
Increase in other liabilities	3,631	6,691
Interest received on cash equivalents	(4)	(1)
Interest on bonds	1,129	689
	\$ (10,450)	\$ (10,343)

See notes to financial statements

Community Development Administration  
Local Government Infrastructure Bonds (Ambac Insured)

NOTES TO FINANCIAL STATEMENTS  
(in thousands)

June 30, 2004 and 2003

NOTE A - AUTHORIZING LEGISLATION AND PROGRAM DESCRIPTION

The Community Development Administration (CDA) is authorized to issue Local Government Infrastructure Bonds (Ambac Insured) pursuant to Sections 2-201 through 2-208 of Article 83B of the Annotated Code of Maryland to provide a mechanism for financing the infrastructure needs of local governments. CDA is in the Division of Development Finance in the Department of Housing and Community Development (DHCD) of the State of Maryland.

The accompanying financial statements only include CDA's Local Government Infrastructure Bonds (Ambac Insured) (the Fund). CDA's other Funds are not included.

The Fund was established to issue bonds to provide funds for construction and permanent financing to local governments for public facilities.

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

The Fund is set up in accordance with CDA's enabling legislation and the Resolution providing for the issuance of Local Government Infrastructure Bonds (Ambac Insured) (the Resolution). The Fund is an enterprise fund of the State of Maryland and uses the accrual basis of accounting.

Generally Accepted Accounting Principles

CDA reports its financial activities by applying Standards of Governmental Accounting and Financial Reporting as promulgated by the Governmental Accounting Standards Board (GASB). CDA has adopted GASB Statement No. 20 *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that Use Proprietary Fund Accounting*. Consequently, CDA applies all applicable GASB pronouncements as well as Financial Accounting Standards Board (FASB) Statements and Interpretations, APB Opinions, and ARBS of the Committee on Accounting Procedure issued on or prior to November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements.

Community Development Administration  
Local Government Infrastructure Bonds (Ambac Insured)

NOTES TO FINANCIAL STATEMENTS - CONTINUED  
(in thousands)

June 30, 2004 and 2003

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

CDA has adopted GASB Statement No. 34 *Basic Financial Statements and Management's Discussion and Analysis*. Under GASB Statement No. 34, net assets should be reported as restricted when constraints placed on net asset use are either: externally imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments; or are imposed by law through constitutional provisions or enabling legislation. Accordingly, all net assets of the Fund are restricted as to their use as all net assets are pledged to bondholders.

The Annual Financial Report may include a Management's Discussion and Analysis. Since CDA is an enterprise fund included in the State of Maryland's Comprehensive Annual Financial Report, a separate Management's Discussion and Analysis is not required in these financial statements. CDA prepares a Management's Discussion and Analysis for the General Accounting Division of the State of Maryland that is not part of these financial statements.

Cash and Cash Equivalents on Deposit with Trustee

Cash equivalents may include commercial paper, money market funds, repurchase agreements, investment agreements and any other investments, primarily U.S. Treasury and agencies, which have maturities of 90 or less days at the time of purchase. As of June 30, 2004 and 2003, all of CDA's cash equivalents are invested in a money market mutual fund that is more fully described in Note C.

Community Facilities Loans

Community facilities loans are carried at their unpaid principal balances. See Note D for additional information on community facilities loans.

Allowance for Loan Losses

Community facilities loans are secured by the full faith and credit of the applicable local governments. Therefore, CDA has determined that no allowance for loan losses was necessary as of June 30, 2004 and 2003.

Community Development Administration  
Local Government Infrastructure Bonds (Ambac Insured)

NOTES TO FINANCIAL STATEMENTS - CONTINUED  
(in thousands)

June 30, 2004 and 2003

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Accrued Interest Receivable

Accrued interest includes both income on cash deposits and interest on loans. As of June 30, 2004 and 2003, all loans were current. Therefore, all accrued interest on loans was recorded during the period.

Bonds Payable

Bonds payable are carried at their unpaid principal balances. There are no premiums or discounts to amortize. See Notes E, F, G and I for additional information.

Administrative Support

In addition to expenses incurred directly by the Fund, CDA receives certain support services from other divisions of DHCD. Support services and the operating expenses of CDA have been allocated to CDA's General Bond Reserve Fund and are reported in the financial statements of CDA's Revenue Obligation Funds. The General Bond Reserve Fund records these expenses as invoiced by DHCD for the fiscal year.

The employees of CDA are covered by the Maryland State Retirement and Pension System (the System) and the costs of employees' retirement benefits are included in the salaries and related costs charged to CDA's General Bond Reserve Fund. See Note J for additional information.

Revenue and Expenses

The Fund distinguishes operating revenue and expenses from nonoperating items in conformity with GASB Statement No. 34. Operating revenue and expenses are identified as those activities that are directly related to financing public facilities for local governments. All of the Fund's activities are considered to be operating.

Community Development Administration  
Local Government Infrastructure Bonds (Ambac Insured)

NOTES TO FINANCIAL STATEMENTS - CONTINUED  
(in thousands)

June 30, 2004 and 2003

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions. These estimates and assumptions affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue, expenses, gains and losses during the reporting periods. Actual results could differ from these estimates.

Due to Local Governments

CDA records the total loan amount when the loan closes and collects interest from the local government on this full loan amount from the date of closing. Due to local governments represents the undrawn loan amount which is held by CDA as an escrow until the funds are needed by the local government.

Reclassifications

Certain 2003 amounts have been reclassified to conform to 2004 financial statement presentation.

NOTE C - CASH AND CASH EQUIVALENTS ON DEPOSIT WITH TRUSTEE

Proceeds from bonds are invested in authorized investments as defined in the respective indentures until required for financing projects, redeeming outstanding bonds and notes, and funding program expenses. Authorized investments include obligations of the U.S. Treasury, U.S. Government agencies, political subdivisions in the United States, bankers' acceptances, repurchase agreements, corporate debt securities and certificates of deposit with foreign or domestic banks. All CDA accounts held in trust by the trustee are kept separate from the assets of the bank and from other trust accounts.

Community Development Administration  
Local Government Infrastructure Bonds (Ambac Insured)

NOTES TO FINANCIAL STATEMENTS - CONTINUED  
(in thousands)

June 30, 2004 and 2003

NOTE C - CASH AND CASH EQUIVALENTS ON DEPOSIT WITH TRUSTEE (Continued)

As of June 30, 2004 and 2003, the Fund had \$21,051 and \$17,301, respectively, invested in money market mutual funds (Federated Treasury Obligations Fund and ARK U.S. Government Cash Management Corporate II Class Fund, respectively) which are classified as cash and cash equivalents. The Federated Treasury Obligations Fund invests exclusively in U.S. Treasuries and in repurchase agreements collateralized by Treasury securities and is rated AAAM by Standard & Poor's and Aaa by Moody's Investors Services. As of June 30, 2003, the ARK U.S. Government Cash Management Corporate II Class Fund invested exclusively in obligations of the U.S. Government and its agencies and instrumentalities and in repurchase agreements. It was rated AAA by Standard & Poor's and Aaa by Moody's Investors Services.

As of June 30, 2004 and 2003, the cost of the money market mutual funds approximates fair value.

The money market mutual funds are not categorized by credit risk because they are not evidenced by securities that exist in physical or book entry form.

NOTE D - COMMUNITY FACILITIES LOANS

Community facilities loans are secured by the full faith and credit of the applicable local government. As such, no allowance for loan losses was necessary as of June 30, 2004 and 2003. Interest rates on such loans range from 2.73% to 4.87% and 3.574% to 4.87% with remaining loan terms ranging from approximately 7 years to 30 years and 9 years to 29 years as of June 30, 2004 and 2003, respectively.

NOTE E - BONDS PAYABLE

The bonds issued by CDA are special obligations of CDA and are payable from the revenue and special funds of the applicable indentures. These bonds do not constitute debt and are not guaranteed by the State of Maryland or any other program of the State of Maryland or any political subdivision. The provisions of the Resolution require or allow for the redemption of bonds through the use of unexpended bond proceeds and excess funds accumulated primarily through prepayment of community facilities loans. All outstanding bonds are subject to redemption at the option of CDA, in whole or in part at any time, after certain dates, as specified in the respective series resolutions. All bonds have fixed interest rates and all are tax-exempt.

Community Development Administration  
Local Government Infrastructure Bonds (Ambac Insured)

NOTES TO FINANCIAL STATEMENTS - CONTINUED  
(in thousands)

June 30, 2004 and 2003

NOTE E - BONDS PAYABLE (Continued)

The following is a summary of the bond activity for the year ended June 30, 2004 and the bonds payable as of June 30, 2004:

	Issue Dated	Range of Interest Rates	Range of maturities	Bonds Payable at 6/30/2003	Bond Activity		Bonds Payable at 6/30/2004
					New bonds issued	Scheduled maturity payments	
Local Government Infrastructure Bonds (Ambac Insured)							
2002 Series A	3/1/2002	3.00% - 5.00%	2004 - 2032	\$ 11,470	\$ -	\$ (330)	\$ 11,140
2002 Series B	10/1/2002	2.25% - 4.375%	2004 - 2022	3,485	-	(140)	3,345
2003 Series A	3/1/2003	2.00% - 4.50%	2004 - 2023	14,560	-	(580)	13,980
2004 Series A	4/22/2004	2.00% - 4.875%	2005 - 2034	-	16,375	-	16,375
Total				<u>\$29,515</u>	<u>\$16,375</u>	<u>\$ (1,050)</u>	<u>\$ 44,840</u>

The following is a summary of the bond activity for the year ended June 30, 2003 and the bonds payable as of June 30, 2003:

	Issue Dated	Range of Interest Rates	Range of maturities	Bonds Payable at 6/30/2002	Bond Activity		Bonds Payable at 6/30/2003
					New bonds issued	Scheduled maturity payments	
Local Government Infrastructure Bonds (Ambac Insured)							
2002 Series A	3/1/2002	3.00% - 5.00%	2003 - 2032	\$ 11,790	\$ -	\$ (320)	\$ 11,470
2002 Series B	10/1/2002	2.25% - 4.375%	2003 - 2022	-	3,555	(70)	3,485
2003 Series A	3/1/2003	2.00% - 4.50%	2004 - 2023	-	14,560	-	14,560
Total				<u>\$11,790</u>	<u>\$18,115</u>	<u>\$ (390)</u>	<u>\$ 29,515</u>

Community Development Administration  
Local Government Infrastructure Bonds (Ambac Insured)

NOTES TO FINANCIAL STATEMENTS - CONTINUED  
(in thousands)

June 30, 2004 and 2003

NOTE F - DEBT SERVICE REQUIREMENTS

As of June 30, 2004, the required principal payments for bonds (including mandatory sinking fund payments) and interest payments for each of the next five years and in five-year increments thereafter, are as follows:

<u>Years ended June 30,</u>	<u>Interest</u>	<u>Principal</u>
2005	\$ 1,774	\$ 1,825
2006	1,668	1,870
2007	1,626	1,910
2008	1,581	1,960
2009	1,527	2,015
2010 - 2014	6,614	10,885
2015 - 2019	4,500	11,240
2020 - 2024	2,087	9,265
2025 - 2029	763	2,020
2030 - 2034	233	1,850
Total	<u>\$ 22,373</u>	<u>\$ 44,840</u>

As of June 30, 2003, the required principal payments for bonds (including mandatory sinking fund payments) and interest payments for each of the next five years and in five-year increments thereafter, are as follows:

<u>Years ended June 30,</u>	<u>Interest</u>	<u>Principal</u>
2004	\$ 1,129	\$ 1,050
2005	1,104	1,070
2006	1,079	1,105
2007	1,052	1,125
2008	1,023	1,160
2009 - 2013	4,531	6,395
2014 - 2018	3,259	7,600
2019 - 2023	1,606	7,550
2024 - 2028	497	1,235
2029 - 2033	157	1,225
Total	<u>\$ 15,437</u>	<u>\$ 29,515</u>

Community Development Administration  
Local Government Infrastructure Bonds (Ambac Insured)

NOTES TO FINANCIAL STATEMENTS - CONTINUED  
(in thousands)

June 30, 2004 and 2003

NOTE G - BOND REFUNDINGS

For current refundings of debt in an optional redemption, CDA replaces previously issued bonds with lower cost debt. For the year ending June 30, 2004, CDA issued Local Government Infrastructure Bonds (Ambac Insured) 2004 Series A in the amount of \$16,375. Part of the proceeds of this issue refunded Infrastructure Financing Bonds (AMBAC Insured) 1992 Series A and 1994 Series A in the amounts of \$550 and \$1,720, respectively. This refunding did not result in any economic gain to CDA because the reduction in bond debt service is passed along to the local governments in lower loan payments.

In accordance with GASB No. 23 *Accounting and Financial Reporting for Refunding of Debt Reported by Proprietary Activities*, a deferral of the difference between the reacquisition price and the net carrying amount of the old debt should be offset to the new bonds on the accompanying Statements of Net Assets. Because there were no deferred bond issuance costs or premiums on the refunded bonds, the offset to the refunding bonds was zero.

NOTE H - LONG-TERM OBLIGATIONS

Changes in long-term obligations for the year ended June 30, 2004, were as follows:

	<u>Beginning balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Due within one year</u>	<u>Ending balance</u>
Long-term bonds payable	\$ 28,465	\$ 16,375	\$ -	\$ (1,825)	\$ 43,015
Advance trustee fees	<u>5</u>	<u>12</u>	<u>-</u>	<u>(12)</u>	<u>5</u>
Total long-term liabilities	<u>\$ 28,470</u>	<u>\$ 16,387</u>	<u>\$ -</u>	<u>\$ (1,837)</u>	<u>\$ 43,020</u>

Community Development Administration  
Local Government Infrastructure Bonds (Ambac Insured)

NOTES TO FINANCIAL STATEMENTS - CONTINUED  
(in thousands)

June 30, 2004 and 2003

NOTE H - LONG-TERM OBLIGATIONS (Continued)

Changes in long-term obligations for the year ended June 30, 2003, were as follows:

	<u>Beginning balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Due within one year</u>	<u>Ending balance</u>
Long-term bonds payable	\$ 11,470	\$ 18,115	\$ (70)	\$ (1,050)	\$ 28,465
Advance trustee fees	<u>1</u>	<u>10</u>	<u>(6)</u>	<u>-</u>	<u>5</u>
Total long-term liabilities	<u>\$ 11,471</u>	<u>\$ 18,125</u>	<u>\$ (76)</u>	<u>\$ (1,050)</u>	<u>\$ 28,470</u>

NOTE I - BOND INSURANCE

All bonds of the Fund are insured by Ambac Assurance Corporation. The provisions of the policy require the insurer to pay that portion of the principal and interest on the bonds which become due for payment but are not paid by CDA. The insurance generally extends for the term of the bonds and cannot be cancelled by the insurer.

NOTE J - PENSION AND OTHER POST-RETIREMENT BENEFITS

Eligible employees of CDA and employees of the State of Maryland are covered under the retirement plans of the State Retirement and Pension System of Maryland (System) and are also entitled to certain healthcare benefits upon retirement. CDA's only liability for retirement and post-employment benefits is its required annual contribution, which was paid in full by CDA to the State of Maryland prior to year end. The System prepares a separate audited Comprehensive Annual Financial Report which can be obtained from the State Retirement and Pension System of Maryland, 120 East Baltimore Street, Baltimore, Maryland 21202 or by visiting the website at [www.sra.state.md.us](http://www.sra.state.md.us).