

MUNICIPAL GUARANTEE BOARD
ANNUAL REPORT 2007

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Information about the Annual Report

Funding guaranteed by the Municipal Guarantee Board is channelled in the form of loans for upgrading the operations and infrastructure of municipalities and for housing production on social grounds.

Municipal Guarantee Board

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Managing Director's Review

During the past year, 2007, the Municipal Guarantee Board carried out the changes in its operations required by the new Act on the Municipal Guarantee Board (MGB), which had been passed by Parliament in the previous year.

The new act gives municipalities outside the MGB the opportunity to become member organizations of the MGB, an opportunity that was taken up by Hankasalmi, Koski TI, Perniö, Pihtipudas, Ruokolahti and Ypäjä. At the end of 2007 there were only five municipalities with a total population of around 12,000 that were not member organizations of the MGB. Receiving new member organizations indicates strong support for the joint funding system.

In the past year, the reporting of the financial responsibilities of the MGB's member organizations was clarified. The clarification was given by the Municipal Section of the Finnish Accounting Board at the request of the MGB's Board of Directors. The purpose of the clarification was to unify the reporting practises for every member organization.

The MGB can only grant guarantees against sufficient security. Until last year the custody of securities was administered under Finnish law. Because of the expanding operations and the development in the supply of custody services abroad, the custody of securities was transferred to the London-based Northern Trust Corporation, which operates under English law.

The year under review, 2007, was the best for the municipalities' joint funding system so far in terms of market share and profitability. At the same time the margins of the municipalities' borrowing still remained at a historically low level. Successful operations are based on motivated personnel and advanced business methods. The system's funding was dominated by structured financial products, as in previous years.

During the past year the development of the system was characterized by close cooperation with decision-makers in the new member municipalities, and with the Department for Municipal Affairs at the Ministry of Interior, credit rating agencies, municipality representatives and the media. I would like to express my gratitude to all those with whom we have cooperated for the MGB's good financial performance and I look forward to further shared success in the years to come.



Heikki Niemeläinen
Managing Director

REPORT ON OPERATIONS 2007

During 2007 the Municipal Guarantee Board carried out the changes in its operations required by the new Act on the Municipal Guarantee Board (MGB), which had been passed by Parliament in the previous year.

The new act gives municipalities outside the MGB the opportunity to become member organizations of the MGB, an opportunity that was taken up by Hankasalmi, Koski TI, Perniö, Pihtipudas, Ruokolahti and Ypäjä. At the end of 2007 the number of municipalities that were not members of the MGB had thus fallen to five. At the end of the year under review, 395 municipalities were member organizations of the MGB, their combined population representing about 99.8 percent of the Finnish population. Because of municipal mergers, the number of member organizations fell by eight municipalities compared to 2006. The municipalities of the Åland Islands cannot be member organizations of the MGB because of the autonomy of Åland.

At its spring meeting the MGB's Council approved new Standing Orders, which replaced the earlier Regulations. At its autumn meeting, the Council also augmented the MGB's strategy by expressing its opinion on the growth of the MGB's fund. The Council stated that the MGB's liquidity will be safeguarded both by the fund, which relationship to the outstanding guarantees will be made stable, and with sufficient stand-by credit facilities.

In the past year, the reporting of the financial responsibilities of the MGB's member organizations was clarified. The clarification was given by the Municipal Section of the Finnish Accounting Board at the request of the MGB's Board of Directors. The purpose of the clarification was to unify the reporting practises for every member organization.

The MGB can only grant guarantees against sufficient security. Until last year the custody of securities was administered under Finnish law. Because of the expanding operations and the development in the supply of custody services abroad, the custody of securities was transferred to the London-based Northern Trust Corporation, which operates under English law. This reconciliation caused the MGB a great deal of unforeseen preparatory work.

The year under review, 2007, was the best for the Municipal Guarantee Board and Municipality Finance Plc so far in terms of market share and profitability. At the same time the margins of the municipalities' borrowing still remained at a historically low level. Successful operations are based on motivated personnel and advanced business methods. The system's funding was dominated by structured financial products, as in previous years.

Municipal Guarantee Board Legislation

The Act on the Municipal Guarantee Board (487/1996) was passed by Parliament on 18 June 1996 and entered into force on 1 July 1996. The Act states that the purpose of the Guarantee Board is to safeguard and develop the joint funding of Finnish municipalities. In order to fulfil this purpose, the Guarantee Board can grant guarantees for such funding by credit institutions directly or indirectly owned or controlled by municipalities that will be used for lending to municipalities and municipal federations, and to corporations wholly owned by municipalities or under their control. In 2007, the only credit institution to meet the criteria set out in the Act was Municipality Finance Plc.

An amendment to the Act, passed by the Finnish Parliament on 25 April 1997, entered into force on 1 May 1997. As a result of the amendment, MGB has been able to grant guarantees for such funding of a credit institution as will be used for lending to corporations designated by government authorities and engaged in renting or producing and maintaining housing on social grounds or corporations controlled by them.

Parliament made considerable changes to the Act on the Municipal Guarantee Board when an Amendment on the Act on the Municipal Guarantee Board was passed by Parliament on 18 October 2006

The Amendment specified the range of receivables for which a guarantee granted by the Guarantee Board can be used as security. The Amendment opened up an opportunity for remaining non-member municipalities to join the MGB. With the Amendment, the Regulations controlling the operations of the MGB and confirmed by the Ministry of the Interior were abandoned and replaced by the Standing Orders.

Some of the legal provisions included in the Regulations were transferred to the Act, for instance the requirements to granting of guarantees in accordance with European Community State aid rules, the investment and use of the MGB's fund and the powers of the Guarantee Board Auditor.

Since the amendment to the Act, the MGB's fund and stand-by credit facilities may be used to grant interim funding to a credit institution, the funding of which is guaranteed by the MGB.

The auditing corporation of the MGB's administration and accounts, and the Guarantee Board Auditor, can be appointed for a minimum of one year and for a maximum of four years.

The latest amendment to the Act was issued by Parliament on 9 November 2007 (1005/2007). According to the Act, the MGB will be transferred from the Ministry of the Interior to the Ministry of Finance from 1 January 2008.

Administration and Personnel

Under the Act, the Municipal Guarantee Board has a Council of 15 members, each of whom has a personal deputy. On 30 August 2005, the Ministry of the Interior appointed a Council for the MGB for a term of office lasting from 1 October 2005 to 30 September 2009. Mr Jari Blom, Executive Director (Jyväskylä) acted as Chairperson, and Mr Mika Munkki, Agrologist (Vehmaa) and Ms Raija Rönkä-Nieminen, Administration Manager (Lohja), as Deputy Chairpersons. The Council convened twice during the year under review.

Under the Act the MGB has a Board of Directors of 5-7 members who are responsible for MGB's administration, the granting of guarantees, and the preparation and execution of the decisions of the Council. The members of the Board of Directors in 2006 were as follows:

Mr Pekka Alanen, Director, Helsinki

Ms Maija-Liisa Havia, Permanent Undersecretary, Jyväskylä

Ms Sari Innanen, Lecturer, Kokkola

Ms Pirkko Janhunen, Finance Manager, Varkaus

Mr Janne Laine, City Manager, Savonlinna

Mr Markku Pietarila, Director of Town Structure, Kemi

Mr Markku Rahikkala, City Manager, Nokia

Mr Pekka Alanen served as Chairperson of the MGB Board of Directors, and Ms Pirkko Jantunen served as Deputy Chairperson. The Board convened eight times during the year under review.

Mr Heikki Niemeläinen was the Guarantee Board's Managing Director and Mr Tuukka Salminen, the Office Manager, was also the Managing Director's deputy. The number of employees during the year was two.

Auditing and Supervision

The Council appoints an auditing corporation authorized by the Central Chamber of Commerce or by the Board of Chartered Public Finance Auditors for a term of office of one calendar year at a time to audit the financial accounts and administration of the MGB. In 2007, the authorized auditing corporation was KPMG Oy Ab, who was also re-appointed by the MGB's Council for 2008.

The activities of the MGB are supervised by the Guarantee Board Auditor, who is appointed by the Ministry of the Interior on the proposal by the Board of Directors of the Guarantee Board. In 2007, the Guarantee Board Auditor was Deloitte Oy, whom the Ministry of the Interior also re-appointed for 2007.

Risk Management

Risks in guarantee operations

According to the Act on the Municipal Guarantee Board, the MGB may grant guarantees against sufficient security. The amount of security during the past year was sufficient. Guarantee activities are arranged in such a way that the MGB's Board of Directors grants guarantees for funding programmes, the most important of which is the EMTN programme. Within the programme the MGB's Managing Director decides on guarantees for individual debt issues. Of the guarantees granted by the MGB, EUR 386.3 million were for use by the former Municipality Finance Plc, EUR 724.9 million by Municipal Housing Finance Plc and EUR 6,607.9 million by the current Municipality Finance Plc.

On 31 December 2007, funding guaranteed by the MGB was divided into the following currencies: euro 27%, Japanese yen 21%, Australian dollar 9%, Swiss franc 6%, US dollar 6% and other currencies 31%. Security items were denominated in euros.

Risks in investment operations

The MGB has an investment policy approved by the Board of Directors. Under this policy the MGB allocates 50% of its investments to regular debt instruments issued by governments and banks and 50% to capital-secured debt instruments issued by banks, corporates, equity investment funds and in real estate companies. The minimum requirement in respect of regular debt instruments issued by governments and banks is that they are investment grade.

Operational risks

MGB's operational risks are dealt with in the Standing Orders and in the Guarantee and Operations Policy approved by the Board of Directors in which the authority and rights within the MGB are stipulated. Operational risks have been mitigated by outsourcing activities and by nominating deputies.

Finances

Income from regular operations consisted of guarantees granted, which produced in 2007 a total guarantee premium sum of EUR 1,750,000.00. Operating costs came to a total of EUR 944,652.56, comprising personnel costs of EUR 361,094.85, depreciation of EUR 4,825.78 and other costs of EUR 578,731.93. The rise in other costs resulted in particular from increased credit-rating costs of about EUR 70,000 and EUR 50,000 for ensuring the legality of security items that were transferred outside of Finnish law. The result from ordinary activities in the financial year was EUR 805,347.44.

No claims on guarantees were made nor paid in 2007 nor were there any recoveries. The nature of MGB's activities makes it unlikely that any claims on guarantees will be made nor paid, nor that recoveries will be made in the foreseeable future.

Income from investments came to EUR 385,676.81 and costs to EUR 22,227.24. The result from investment activities was EUR 363,449.57, approximately 4.63% on the invested capital, and 4.35% on the fund at the beginning of the year. MGB values its investments at fair value in the balance sheet. The fair value fund was EUR -53,020.00. The result for the financial year, i.e. the total from ordinary activities and investment was EUR 1,168,797.01 before transfer to the fund.

A proposal will be made for transferring the result for the financial year in total to the fund. The fund will thus total EUR 9,523,887.72 on 31 December 2007.

The MGB has an ongoing stand-by credit facility of EUR 50 million for safeguarding the Guarantee Board's cash position.

Outlook

The market share and profitability of the municipalities' joint funding systems made significant advances in 2007. The MGB was given the best possible credit ratings again from international credit rating institutions. The Board's regulations were changed into Standing Orders. During 2008 the MGB will have a new stand-by credit facility to match the increased guarantee operations, and to put into effect reforms to the guarantee operations made possible by the amendments to the legislation. Because of these new developments, a bigger role can be expected for the Municipal Guarantee Board and Municipality Finance Plc in financing the municipalities and social housing production.

Income Statement

| | 1.1.-31.12.2007 | 1.1.-31.12.2006 |
|---|----------------------|----------------------|
| Ordinary operations | | |
| Income | | |
| Guarantee premiums | 1 750 000,00 | 1 750 000,00 |
| Expenses | | |
| Staff expenses | -361 094,85 | -276 388,95 |
| Depreciation | -4 825,78 | -10 927,70 |
| Other expenses | -578 731,93 | -451 358,80 |
| Surplus from ordinary operations | 805 347,44 | 1 011 324,55 |
| Investment activities | | |
| Income | | |
| | 385 676,81 | 324 290,00 |
| Expenses | | |
| | -22 227,24 | -6 155,29 |
| Surplus from investment activities | 363 449,57 | 318 134,71 |
| Surplus before transfer to fund | 1 168 797,01 | 1 329 459,26 |
| Transfer to fund | -1 168 797,01 | -1 329 459,26 |
| Surplus for the financial year | 0,00 | 0,00 |

Balance Sheet

Assets

| | 31.12.2007 | 31.12.2006 |
|--|---------------------|---------------------|
| Non-current assets | | |
| Tangible assets | 38 317,77 | 27 870,86 |
| Other shares and similar rights of ownership | 525 956,65 | 523 956,65 |
| Investments | | |
| Other investments | | |
| Shares and similar rights of ownership | 2 064 455,65 | 662 757,00 |
| Certificates of deposit | 3 449 812,88 | 2 027 766,87 |
| Debt securities | 2 206 620,00 | 3 456 618,64 |
| Other investments | 659 680,00 | 1 159 818,06 |
| Current assets | | |
| Debtors | | |
| Guarantee receivables | 437 500,00 | 437 500,00 |
| Receivables | 85 847,92 | 73 901,17 |
| Cash and bank accounts | 102 728,91 | 87 360,70 |
| Total assets | 9 570 919,78 | 8 457 549,95 |

Equity and liabilities

| | | |
|-------------------------------------|---------------------|---------------------|
| Capital and reserves | | |
| Fund | 9 523 887,72 | 8 355 090,71 |
| Fair value reserve | -53 020,00 | 46 757,12 |
| Creditors | | |
| Current liabilities | | |
| Trade creditors | 34 919,26 | 10 987,05 |
| Accruals and deferred income | 64 243,63 | 26 741,86 |
| Other current liabilities | 889,17 | 17 973,21 |
| Total equity and liabilities | 9 570 919,78 | 8 457 549,95 |

Cash Flow Statement

| | 1.1.-31.12.2007 | 1.1.-31.12.2006 |
|---|-----------------|-----------------|
| Cash flow from ordinary operations | | |
| -operating income | 1 750 000,00 | 1 750 000,00 |
| -operating costs | 898 489,84 | 699 113,03 |
| Cash flow from ordinary operations | 851 510,16 | 1 050 886,97 |
| Cash flow from non-current assets | 17 272,69 | 475 823,12 |
| Cash flow from investments | 818 869,26 | 589 974,41 |
| Change in cash funds | 15 368,21 | -14 910,56 |
| Cash funds at the beginning of financial period | 87 360,70 | 102 271,26 |
| Cash funds at the end of financial period | 102 728,91 | 87 360,70 |

Notes to the Financial Statements

The Municipal Guarantee Board observes, where applicable, the Accounting Act and Decree in force.

Investments are valued in the balance sheet at fair value, so the unrealized differences between their book value and fair value have been recognized in the fair value reserve under capital and reserves.

Non-current assets have been valued at acquisition cost, on which planned depreciation is calculated.

Depreciation method:

- IT hardware and software, annual carrying value, 30%
- machinery and equipment, annual carrying value, 25%

Staff expenses

| 1.1.-31.12.2007 | Salaries and fees | Pension expenses | Other personnel-related expenses |
|---------------------------------|-------------------|------------------|----------------------------------|
| Board of Directors | 62 001,76 | 6 580,44 | 1 725,63 |
| Managing Director and Deputy MD | 202 636,28 | 37 425,03 | 8 742,98 |
| Others | 8 111,00 | 1 312,94 | 301,37 |
| Total | 272 749,04 | 45 318,41 | 10 769,98 |

Non-current assets

| | 2007 | 2006 |
|----------------------------|-------------------|-------------------|
| Carrying value 1.1. | 551 827,51 | 86 932,09 |
| Increase | 17 272,69 | 502 243,10 |
| Decrease | 0,00 | -26 419,98 |
| Depreciation | -4 825,78 | -10 927,70 |
| Carrying value 1.1. | 564 274,42 | 551 827,51 |

Tangible assets

| | | |
|-------------------------|-----------|-----------|
| IT hardware | 8 769,96 | 6 052,81 |
| Machinery and equipment | 11 736,71 | 4 006,95 |
| Other assets | 17 811,10 | 17 811,10 |

Other shares and similar rights of ownership

| | | |
|------------------------------|------------|------------|
| Nurmijärvi Golf Club 1 share | 21 713,55 | 21 713,55 |
| As. Oy Topeliuksenkatu 15 | 502 243,10 | 502 243,10 |

Changes to capital and reserves

| | |
|--------------------------------------|---------------------|
| Fund 31.12.2005 | 8 355 090,71 |
| Fund transfer 31.12.2006 | 1 168 797,01 |
| Fund 31.12.2006 | 9 523 887,72 |
| Fair value reserve 31.12.2005 | 46 757,12 |
| Change in financial year | -99 777,12 |
| Fair value reserve 31.12.2006 | -53 020,00 |

Guarantees and collateral

| | 31.12.2007 | 31.12.2006 |
|--|-----------------------|-----------------------|
| Guarantee limits granted | 16 486 765 530,82 | 13 088 864 315,60 |
| Guarantees in use | 7 719 083 283,75 | 6 629 971 187,49 |
| Collateral received and items affecting collateral situation | 8 138 589 618,41 | 7 000 257 457,11 |
| Balance of collateral and guarantees | 419 506 334,66 | 370 286 269,62 |

Signs

SIGNATURES OF THE ANNUAL REPORT OF ACTIVITIES AND THE FINANCIAL STATEMENTS

Helsinki, 8th February 2008

MUNICIPAL GUARANTEE BOARD



Mr Pekka Alanen
Chairman of the Board



Mr Janne Laine
Deputy Chairman of the Board



Ms Maija-Liisa Havia
Member of the Board



Ms Sari Innanen
Member of the Board



Ms Pirkko Janhunen
Member of the Board



Mr Markku Pietarila
Member of the Board



Mr Markku Rahikkala
Member of the Board



Mr Heikki Niemeläinen
Managing Director

The financial statements have been prepared in accordance with normal accounting practices.
We have today given the Auditors' Report.

Helsinki, 8th February 2008

KPMG OY AB



Riitta Pyykkö
Authorized Public Accountant

Guarantees

Million euro

Municipality Finance Plc

| | Guarantees | Funding |
|--|-----------------|----------------|
| | | 31.12.2007 |
| Municipality Finance Plc (-30.4.2001) | | |
| EMTN | 2 000,0 | 315,0 |
| Other Guarantees | 750,0 | 71,3 |
| Total | 2 750,0 | 386,3 |
| Municipal Housing Finance Plc (-30.4.2001) | | |
| EMTN | 1 500,0 | 708,8 |
| Other guarantees | 400,0 | 16,1 |
| Total | 1 900,0 | 724,9 |
| Total | 4 650,0 | 1 111,2 |
| Municipality Finance Plc (1.5.2001-) | | |
| EMTN | 8 000,0 | 4 624,2 |
| AUD 1000 Programme | 596,8 | 122,9 |
| Treasury Bill Programme | 800,0 | 462,6 |
| Domestic Debt Issuance Programme | 800,0 | 401,0 |
| Other foreign funding | 1 500,0 | 806,1 |
| Separate Decisions | | 191,1 |
| Back up facility | 140,0 | 0,0 |
| Total | 11 836,8 | 6 607,9 |
| Total | 16 486,8 | 7 719,1 |

Auditors' Report

To the Council of the Municipal Guarantee Board

We have audited the accounting records, the report of the Board of Directors, the financial statements and the administration of the Municipal Guarantee Board for the year 2007. The Board of Directors and the Managing Director have prepared the Report of the Board of Directors and the financial statements, which include the balance sheet, income statement, cash flow statement and notes to the financial statements. Based on our audit we express an opinion on these financial statements, as well as on the report of the Board of Directors and on administration.

We have conducted the audit in accordance with Finnish Standards on Auditing. Those standards require that we perform the audit to obtain reasonable assurance about whether the report of the Board of Directors and 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, assessing the accounting principles used and significant estimates made by the management as well as evaluating the overall financial statement presentation. The purpose of our audit of administration is to examine that the members of the Board of Directors and the Managing Director have complied with the rules of the Act on the Municipal Guarantee Board.

In our opinion, the report of the Board of Directors and the financial statements have been prepared in accordance with the Accounting Act to the appropriate extent. The report of the Board of Directors and the financial statements give a true and fair view, as defined in the Accounting Act, of the institution's result of operations as well as of the financial position. The report of the Board of Directors is consistent with the financial statements. The financial statements can be adopted and the members of the Board of Directors and the Managing Director can be discharged from liability for the year audited by us.

Helsinki, February 8, 2008

KPMG OY AB



Riitta Pyykkö
Authorized Public Accountant

Board of Directors



Chairperson

Mr. Pekka Alanen
Director
Helsinki

Deputy chairperson

Ms. Pirkko Janhunen
Finance Manager
Varkaus

Other members

Mr. Markku Pietarila
Director of Town Structure
Kemi

Ms. Maija-Liisa Havia
Permanent Undersecretary
Jyväskylä

Ms. Sari Innanen
Lecturer
Kokkola

Mr. Janne Laine
City Manager
Ikaalinen

Mr. Markku Rahikkala
City Manager
Nokia

Council



Jari Blom
Chairperson
Jyväskylä



Mika Munkki
Deputy Chairperson
Vehmaa



Raija Rönkä-Nieminen
Deputy Chairperson
Lohja

Personal Deputy Member:
Liisa Ruokoseikä
Pieksänmaa

Personal Deputy Member:
Leena Koponen
Muurame

Personal Deputy Member:
Pekka Heikkinen
Tuusula

Other members:

Pirkko Miikkulainen,
Helsinki

Markku Pohjonen,
Kokkola

Päivi Yli-Kauhaluoma-Nurmi,
Pori

Hilkka Hiltunen,
Ilomantsi

Asko Meski,
Orimattila

Mirja Okkonen,
Sotkamo

Aimo Ahti,
Kouvola

Kimmo Behm,
Nurmijärvi

Sari Hyytiäinen,
Hollola

Marjo Matikainen-Kallström,
Espoo

Leena Kuha,
Oulu

Torsten Widén,
Kauniainen

Personal deputy members:

Raimo Korjus,
Kotka

Annina Lehtiö-Vainio,
Turku

Markku Harju,
Kemijärvi

Kari Heikkilä,
Miehikkälä

Jouko Luukkonen,
Haapavesi

Sinikka Kangas,
Salla

Olli Viitasaari,
Lempäälä

Jukka Vilén,
Kemi

Päivi Norhio,
Kotka

Armi Salo-Oksa,
Mikkeli

Flemming Bergh,
Kirkkonummi

Gun Kapténs,
Luoto