Low and Moderate Income Rental (LMIR) and Flexible Financing for Capital Costs (FFCC) Programs Procedural Guide

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Introduction – Program Purpose and Background

The purpose of the Low and Moderate Income Rental (LMIR) program is to provide long-term amortizing mortgage debt for multifamily rental housing affordable to low- and moderate-income Minnesotans. Long-term, fixed-rate mortgage loans are available for financing new construction, stabilization of existing properties and for the preservation of existing federally assisted rental housing.

When LMIR loans are used in a tax-exempt bond transaction, short-term bonds may be issued to fund a LMIR Bridge Loan to meet the 50% test in order for the development to qualify for 4% tax credits.

Minnesota Housing also offers a HUD Risk Share Streamlined Refinance product for existing LMIR loans that are insured at 50% in the Level I HUD Risk Share program. This allows owners to take advantage of current lower interest rates and potentially, needed repairs. The maximum loan amount will be the lesser of the original principal balance or the unpaid principal balance plus eligible repair and closing costs. Refer to the HUD Risk Share Streamlined Refinance Term Sheet for more information.

Throughout the rest of this guide, where no distinction is made, the guide is referring to neither permanent amortizing LMIR loans, not LMIR Bridge nor Streamlined Refinance loans.

The Flexible Financing for Capital Costs (FFCC) program works in tandem with LMIR loans. FFCC loans are traditionally structured as deferred loans at low or no interest and are used as a mechanism to reduce the overall interest rate to the development.

Both loan programs work in conjunction with HOME funds, federal Housing Tax Credits (HTC) or other public or private funding sources.

LMIR and FFCC loans are available through the annual Multifamily Consolidated Request for Proposals (RFP) process as well as on an open pipeline basis (subject to the availability of sufficient funding). Refer to Chapter 6 of the RFP Guide for application instructions.

Chapter 1 – Funding Sources and Priorities

1.01 LMIR Funding Sources

LMIR loans are funded through the following two sources:

Housing Investment Fund: Minnesota Housing generates resources from its lending activities and makes them available to fund investment-quality LMIR amortizing first mortgage loans. This is a non-federal resource that works well with 9% competitive housing tax credits.

Federal Tax-Exempt Bond Proceeds: Minnesota Housing issues tax-exempt bonds to fund new LMIR loans along with applications for 4% housing tax credits. If needed for eligibility for tax credits, short-term LMIR Bridge Loans may also be available.

Developers or owners who are considering 4% tax credits for their properties should carry out a preliminary evaluation of their proposal to determine if it will meet minimum eligibility and threshold requirements as called for in the state's Qualified Allocation Plan (QAP) in effect for the year the bonds will be issued. Applicants should also review the Minnesota Bond Statutes to become familiar with state requirements.

If the tax-exempt bond proposal can satisfy the minimum threshold requirements for tax credits, developers should review the Tax Credit Allocation Procedural Manual and the Self-Scoring Worksheet in effect for the year the bonds will be issued. These documents provide much greater detail to allow for the full evaluation of a proposal's potential to access, secure and utilize housing tax credits. In seeking tax credits, a developer or owner must submit a full and complete application package for Housing Tax Credits in in addition to any related application packages for Minnesota Housing's other loan products. Refer to the Minnesota Housing Tax Credits page for the QAP and other tax credit materials.

1.02 FFCC Funding Source

Housing Affordability Fund: The FFCC program offers deferred loans and is financed through the Housing Affordability Fund, which are funds generated through Agency resources. FFCC deferred loans are available only in partnership with LMIR loans and are used as a mechanism to reduce the overall interest rate to the development.

1.03 HUD Risk-Share Mortgage Insurance

In order to minimize Minnesota Housing's risks, all permanent LMIR loans will obtain mortgage insurance through HUD's Risk-Sharing Program. Under Minnesota Housing's Risk-Sharing Agreement with HUD, HUD contracts to reimburse Minnesota Housing for a portion of the loss from any defaults that occur while the insurance is in force. In this way, Minnesota Housing is able to effectively increase its financing capacity. In addition, Minnesota Housing utilizes the program as an incentive to partner with HUD to preserve and renew expiring Section 8 contracts.

HUD's insured portion will be either 50 percent (Level I) or up to 90 percent (Level II).

A Mortgage Insurance Premium (MIP) of 0.125 percent (Level I) or up to 0.25 percent (Level II) will be charged in addition to Minnesota Housing's interest rate on the loan.

- The first year of MIP is paid in advance and will be included in the development cost budget.

Federal Requirements:

- Part 58 Environmental Review
  - All LIMIR loans will undergo Part 58 review to determine the impact of the project on the surrounding area.
  - DO NOT make any choice limiting actions until you have received clearance from the Federal Reviewer indicating your review is complete. Choice limiting actions include:
    - Site Acquisition
    - Contract Execution
    - Demolition
    - Construction
- Davis-Bacon Act
  - In general, loans are insured upon construction completion, therefore Davis-Bacon federal wage requirements do not apply.

2530 Submission

- HUD requires Form 2530 clearance from all project participants including owner, developer, GP, LP, GC and Management Agent prior to issuing their Firm Approval.

Chapter 2 – Eligible Uses and Eligibility Criteria

2.01 Eligible Housing Types

Permanent, general occupancy, rental housing

Permanent, supportive housing

2.02 Eligible Projects

Must contain a minimum of four units.

Generally a development needs to contain a minimum of 24 housing units to be financially feasible; however, smaller developments may be considered.

Scattered site developments must be located in the same city or county and also contain a minimum of four units.

Developments with age restrictions of 55 and older are eligible for LMIR loans.

2.03 Ineligible Projects

Nursing homes, board and care facilities and supervised living facilities licensed by the State of Minnesota or a delegated local Department of Health are not eligible for funding, nor are properties where residents require a 24-hour plan for supervision and/or medical/health care.

2.04 Eligible Activities

New construction

Rehabilitation of existing affordable housing

Adaptive reuse (i.e., conversion to housing from another use)

Preservation of affordable housing

Preservation of federally assisted housing

Construction to permanent financing

Permanent financing

2.05 Eligible Owners and Sponsors

Ownership must be in the form of a single asset entity.

Limited Dividend and Nonprofit Sponsor:

- Minnesota Housing's Mortgage Credit Committee's review ensures that the sponsor has the ability to cover any revenue shortages. Therefore, sponsors will be evaluated as to financial capacity. Factors such as assets, liquidity, length of time in operation and previous housing experience will be considered.

2.06 Income Limits

Income limits are in effect for the life of the mortgage, unless otherwise noted.

At a minimum, 40 percent of the units must be occupied by individuals/families whose income at initial occupancy does not exceed 60 percent of Area Median Income (AMI) (adjusted for family size); or 20 percent of the units must be occupied by individuals/families whose income does not exceed 50 percent of AMI. Refer to the Multifamily Rent and Income Tables for Multifamily Tax Subsidy Projects (MTSP).

No more than 25 percent of the units may have unrestricted incomes.

The balance of units must be occupied by tenants whose incomes at initial occupancy do not exceed 100 percent of the greater of area or statewide median income for a four-person household, as determined by HUD.

Verification Requirements:

At initial occupancy, households must self-certify their gross annual household income in Part I of the Initial Occupancy Statement by Tenant form. Verification of income is not required. This form must be signed and dated by the head of household and the owner or management agent. A more detailed certification used for another program is also acceptable (e.g., HUD form 50059 or 50058, Housing Tax Credit Tenant Income Certification, USDA Rural Development certification form, etc.). The LMIR program does not require annual recertification of income.

For occupied properties, the borrower is required to submit an Income Verification Certification to Minnesota Housing. Within 120 days of closing, the owner will need to contact each tenant to obtain a Tenant Income Verification form.

2.07 Rent Levels

Rent restrictions remain in place for the life of the mortgage, unless otherwise noted. The rent levels will be marketable, taking into consideration the household incomes that must be served, but at a minimum, the rent levels must comply with the following:

- 40 percent of units affordable to persons and families at 60 percent of AMI; or 20 percent of units affordable to persons and families at 50 percent of AMI
- The balance of units with rents at market rates as determined by Minnesota Housing

Refer to the Multifamily Rent and Income Tables for Multifamily Tax Subsidy Projects (MTSP).

2.08 Tax-Exempt Bond Requirements

In addition to the other LMIR requirements, LMIR loans funded with tax-exempt bonds must adhere to the following requirements:

The maximum rent for at least 20 percent of the units must not exceed the area fair market rents.

- o Scattered site developments (non-contiguous pieces of real property separated by more than just a street) must meet this requirement for each building.
- o Developments with project-based rent assistance are deemed to meet this requirement; and

The owner must agree to extend any affordability restrictions and any contract or agreement for rental assistance for the maximum term permitted including any renewals; and

The units required to be set aside for low- and moderate-income tenants must be continuously offered for a "qualified project period," which is generally the longer of 15 years from 50 percent occupancy, the day the bonds are no longer outstanding or the date when any Section 8 assistance terminates; and

Rehabilitation cost must equal or exceed 15 percent of the portion of the cost of acquisition financed by the bonds.

- o Scattered site developments (non-contiguous pieces of real property separated by more than just a street) must meet this requirement for each building; and

95 percent of tax-exempt bond proceeds must be used for qualified costs, which, with certain limitations, means amounts allocable to the capital costs of residential rental property.

- o Ineligible costs of up to 5 percent (including costs of issuance) may be financed with proceeds of the bond issue.

2.09 Common Selection and Common Funding Priorities

In addition to the rent and income limits described above, for selection and funding priorities common to all Minnesota Housing programs, refer to the RFP Guide.

Chapter 3 – General Amortizing Loan Characteristics

Minnesota Housing's underwriting includes a thorough analysis of all aspects of the feasibility of the development proposal. In addition to requirements detailed in this guide, all LMIR loans are underwritten in conformance with Minnesota Housing's Multifamily Underwriting Standards.

3.01 Loan Term

LMIR loans are 30-year, fully amortizing, fixed rate loans.

FFCC loans are generally made with an interest rate of 0 percent. They are co-terminus with the accompanying LMIR loan and will be due and payable upon prepayment or maturity of the LMIR loan. FFCC loans will be in second lien position behind the LMIR loan.

3.02 Debt Coverage Ratio

LMIR Loans are sized to meet Minnesota Housing's minimum Debt Coverage Ratios (DCR), which range from 1.15:1 to 1.25:1 depending on the property characteristics and risk factors (refer to the Multifamily Underwriting Standards for current DCR guidelines).

The development must maintain a break-even cash flow for a minimum of 15 years on a proforma basis.

3.03 Maximum Loan-to-Cost/Loan-to-Value

Level I HUD Risk-Share (HUD shares 50 percent of the risk of loss):

The Loan-to-Value limit for the amortizing first mortgage shall be in accordance with the requirements established in the Multifamily Underwriting Standards.

Level II HUD Risk-Share (HUD shares more than 50 percent of the risk of loss):

In accordance with HUD Handbook 4590.01, paragraph 2-4C(2) and Mortgagee Letter 2010-21:

- The Loan-to-Cost must not exceed 87 percent for affordable new construction/ substantial rehabilitation transactions. Substantial rehabilitation is defined as a minimum of $15,000 per dwelling unit in rehabilitation.
- The Loan-to-Value must not exceed 85 percent for existing affordable properties.

3.04 Operating Deficit Escrows

Effective March 2015, a new requirement for all developments funded with LMIR amortizing loans is an escrow that combines and replaces the previously Working Capital Escrow and the Rent-Up Escrow.

At the time of closing of the LMIR loan, borrowers are required to establish an Operating Deficit Escrow (ODE), funded with cash or an irrevocable and unconditional letter of credit. Cash to fund the ODE must not be derived from the proceeds of any development sources including equity. The ODE is not included in the total development costs.

Minnesota Housing may use the ODE at its sole discretion, on behalf of the borrower, to pay for development rent up and operating expenses during the initial lease-up period.

The Operating Deficit Escrow will be sized based on the greater of:

3 percent of the loan amount; or

The projected operating deficit during the absorption period, as determined by the Agency's underwriting analysis.

The escrow will be maintained until the later of the following two scenarios:

One year after permanent loan closing; or

Achievement of a 1.15:1 debt coverage ratio for six consecutive months. The DCR will be calculated based on actual collected revenue less the greater of actual or underwritten effective gross expenses.

After achievement of both of these scenarios, the letter of credit or the remaining cash and interest earned thereon are returned to the borrower.

Based on Minnesota Housing's Mortgage Credit Committee review, bond rating agency or marketing requirements, Minnesota Housing may require the borrower to extend the period or require a larger ODE.

3.05 Escrows and Reserves

Minnesota Housing collects and holds the operating deficit escrow, replacement reserves, residual receipts, if any, and the tax and insurance escrow during the loan term. Tax and insurance escrows are funded outside of the development budget.

3.06 Monitoring and Reporting Requirements

Minnesota Housing actively monitors each development including tenant incomes, rents and affirmative action and equal opportunity requirements. In addition, the Agency monitors monthly operating statements and conducts management reviews and property inspections. The Agency approves the annual budget and distributions from cash flow.

3.07 Return on Equity

Minnesota Housing statutes currently allow a maximum return of 15 percent based on actual developer equity. Nonprofit owned developments are not allowed a distribution.

3.08 Guarantees

Minnesota Housing requires at least one individual or corporation (sponsor) with adequate financial capacity to guarantee all of the following:

- Construction completion
- All monetary obligations, including operating cost shortfalls and debt service, until the property has achieved a debt service coverage ratio of at least 1.15:1 (based on actual collected revenue less underwritten effective gross expenses, for three consecutive months)
- All monetary obligations except principal and interest for the life of the loan

Chapter 4 – Fees and Interest

4.01 LMIR Fees

All LMIR loans:

A $250.00 Application Fee is required for all LMIR applications, including resubmissions.

An Origination Fee of 2 percent on the first $5 million in financing and 1 percent on amounts above $5 million. The minimum Origination Fee is $25,000.

Tax-Exempt Bond funded loans:

Origination Fees for LMIR Bridge Loans, available only as required to meet the 50 percent test, will be charged an origination fee of 0.50 percent.

Bond Issuance Fees will be charged as part of the development budget as follows:

- $100,000; plus
- 1.0 percent of the par amount of the long-term bonds; plus
- 0.75 percent of the par amount of the short-term bonds.

Tax-exempt bond fees, including bridge loan origination fees, are subject to revision as determined appropriate by Minnesota Housing.

4.02 Interest Rates

Interest rates will be at a fixed rate through the term of the LMIR loan.

Housing Investment Fund: Current interest rates are published on Minnesota Housing's website.

For applications received as part of the annual RFP, rates are set prior to Board selection approval (selection) and will be honored for one year. Rates (at the selected rate if within 12 months; otherwise at the current market rate) will be locked for six months at the time of final Board commitment approval (commitment).

For applications received outside of the annual RFP, the rate will be locked for six months at the time of final Board commitment approval (commitment).

Tax-Exempt Bond funded loans: Interest rates are based on market rates at the time of the closing of the bond issuance, plus a spread based on the size of the loan. The interest rate on the permanent LMIR loan will be fixed for the term of the loan.

4.03 Mortgage Insurance Premium

For all LMIR loans insured under HUD's Risk-Share program, a Mortgage Insurance Premium (MIP) of 0.125 percent (Level I), or up to 0.25 percent (Level II), will be charged in addition to the interest rate on the loan. MIP is paid in advance for the first year and is included in the Development Cost Budget and can be paid from loan proceeds.

4.04 Construction Oversight Fee

Historically, Minnesota Housing has charged a Construction Oversight Fee only to developments funded with a LMIR loan. Effective in 2015, a Construction Oversight Fee will be assessed to all developments receiving Minnesota Housing amortizing or deferred loans. The fee will be assessed at the lessor of 0.25 percent of the construction contract amount or 1.0 percent of the total Agency loans.

Chapter 5 – How to Apply

LMIR and FFCC loans are available on an ongoing, pipeline basis (subject to funding availability). Loans are also available through the annual Multifamily Consolidated Request for Proposals (RFP).

The RFP Guide, Underwriting Standards and application materials will be used for both RFP and pipeline applications. To find application materials refer to Multifamily Rental Housing Common Application Materials.

Chapter 12 of the RFP Guide includes instructions for submitting an application outside of the RFP (pipeline or ongoing basis).

Chapter 6 – Contract Compliance and Equal Opportunity

6.01 Policy

It is the policy of Minnesota Housing to practice affirmative action to provide equal opportunity in all of our projects, programs, and other endeavors. Minnesota Housing's goal is to achieve a client and recipient mix that is representative of the people who live in our state and our communities so that all employment and contractual benefits that develop as a result of our programs will be shared by all Minnesotans. This policy applies to all Minnesota Housing employees and Minnesota Housing's external partners.

6.02 Purpose

The purpose of this policy is to make Minnesota Housing's commitment to act affirmatively to achieve equal opportunity in all facets of its operation, clear to both internal staff and outside parties with whom we do business.

6.03 Goals

Our goal is to ensure minority and female contractors and subcontractors equal access to business opportunities on Minnesota Housing financed projects and to encourage the presence of minorities and women at all levels, including on the staffs of the program participants having contractual agreements with Minnesota Housing. Minnesota Housing's goal is to ensure that the workforces on the projects and programs we finance reflect demographically the area in which they are located. These goals will apply for the length of the contract or the life of the mortgage. Minnesota Housing, at its discretion, may set numerical or percentage goals dependent on the location and size of a given project. Current goals will be determined by staff based on the location of the project.

6.04 Requirements

Minnesota Housing is required to comply with all applicable local, state, and federal laws. These requirements are passed on to everyone that Minnesota Housing does business with, either by contractual agreement or as a Minnesota Housing policy.

6.05 Sanctions

Minnesota Housing has the contractual authority to demand full payment of any loan or grant, stop proceeding with any project at any stage, and cease to do business with any entity or individual that fails to follow its affirmative action policies or fails to meet its/his/her contractual equal opportunity obligations.

Chapter 7 – Fair Housing Policy

It is the policy of Minnesota Housing to affirmatively further fair housing in all its programs so that individuals of similar income levels have equal access to Minnesota Housing programs, regardless of race, color, creed, religion, national origin, sex, marital status, status with regard to public assistance, disability, familial status, gender identity or sexual orientation.

Minnesota Housing's fair housing policy incorporates the requirements of the Fair Housing Act, Title VIII of the Civil Rights Act of 1968, as amended by the Fair Housing Amendment Act of 1988, as well as the Minnesota Human Rights Act. Housing providers are expected to comply with the applicable statutes, regulations, and related policy guidance. Housing providers should ensure that admissions, occupancy, marketing and operating procedures comply with non-discrimination requirements.

In part, the Fair Housing Act and the Minnesota Human Rights Act make it unlawful to, because of protected class status:

- discriminate in the selection/acceptance of applicants in the rental of housing units;
- discriminate in terms, conditions or privileges of the rental of a dwelling unit or services or facilities;
- engage in any conduct relating to the provision of housing that otherwise make unavailable or denies the rental of a dwelling unit;
- make, print or publish (or cause to make, print or publish) notices, statements or advertisements that indicate preferences or limitations based on protected class status;
- represent a dwelling is not available when it is in fact available;
- deny access to, or membership or participation in, associations or other services organizations or facilities relating to the business of renting a dwelling or discriminate in the terms or conditions of membership or participation; or
- engage in harassment or quid pro quo negotiations related to the rental of a dwelling unit.

Minnesota Housing has a commitment to affirmatively further fair housing for individuals with disabilities by promoting the accessibility requirements set out in the Fair Housing Act, which establish design and construction mandates for covered multifamily dwellings and requires housing providers to make reasonable accommodations and to allow persons with disabilities to make reasonable modifications.

Applicants will be required to submit an Affirmative Fair Housing Marketing Plan at the time of application, to update the plan regularly and to use affirmative fair housing marketing practices in soliciting renters, determining eligibility and concluding all transactions.

As a condition of funding through Minnesota Housing, housing providers are not permitted to refuse to lease a unit to, or discriminate against, a prospective resident solely because the prospective resident has a Housing Choice Voucher or other form of tenant-based rental assistance.

Chapter 8 – Program Contact

For questions, contact Susan Thompson, Program Manager, at 651.296.9838 or susan.thompson@state.mn.us. You may also contact the Housing Development Officer (HDO) identified in your selection letter.