MINNESOTA HOUSING

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 percent test in order for the development to qualify for 4% housing tax credits (HTC).

The Minnesota Housing Finance Agency (Minnesota Housing) also offers a U.S. Department of Housing and Urban Development (HUD) Risk-share Streamlined Refinance product for existing LMIR loans that are insured at 50 percent in the Level I HUD Risk-share Program. This allows owners to take advantage of current lower interest rates, and, potentially, address 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.

NOTE: Where no distinction is made, this guide is referring to permanent amortizing LMIR loans, not LMIR bridge nor HUD risk-share 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 the Multifamily Application Instructions: Consolidated RFP and HTC Rounds 1 and 2 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 financial 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 HTC.

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

Developers or owners who are considering 4% HTC 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 Minnesota Housing's Qualified Allocation Plan (QAP) in effect for the year the bonds will be issued. Applicants should also review Minnesota Bond Statutes to become familiar with state requirements along with Minnesota Housing's Tax-exempt Bonds Informational Guide.

If the tax-exempt bond proposal can satisfy the minimum threshold requirements for tax credits, developers should review the Housing Tax Credit Program Procedural Manual and the Housing Tax Credit 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 HTC. In seeking tax credits, a developer or owner must submit a full and complete application package for HTC prior to issuance of the bonds, in addition to any related application packages for Minnesota Housing's other loan products. Refer to Minnesota Housing's Housing Tax Credits webpage for the QAP and other HTC 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 Minnesota Housing resources. FFCC deferred loans are generally 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 LMIR loans will undergo Part 58 environmental review to determine the impact of the development 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.
- **Form 2530 Submission**
  - HUD requires Form 2530 clearance from all development participants including the owner, developer, general partner (GP), limited partner (LP), general contractor (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 Developments

- 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 Developments

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
- Refinance of existing mortgages**

* A minimum of five units is required under the HUD Risk-share program.

** For any refinance loan, existing guarantors are expected to remain in place. For the purpose only of refinance loans, rehabilitation is not considered substantial (as defined in Minnesota Housing's Rental Housing Design/Construction Standards) if otherwise:

- The loan meets Minnesota Housing's Multifamily Underwriting Standards;
- Adequate upfront and ongoing reserves are budgeted to fund the capital needs identified in a Property Needs Assessment (PNA)/Capital Needs Assessment (CNA) and approved by a Minnesota Housing architect, and;
- The cost of repairs does not exceed $40,500 per unit.

2.05 Eligible Owners and Sponsors

- Ownership must be in the form of a single asset entity.
- Limited dividend and nonprofit or cooperative housing corporation.

2.06 Income Limits

Income limits are in effect for the life of the mortgage, unless otherwise noted (also refer to Section 2.08 for additional requirements when LMIR loans are funded with tax-exempt bonds).

- At a minimum, 40 percent of the units must be occupied by individuals/families whose income at initial occupancy does not exceed 60% of Multifamily Tax Subsidy Projects (MTSP) (adjusted for family size); or 20 percent of the units must be occupied by individuals/families whose income does not exceed 50% of MTSP. Refer to the Multifamily Rent and Income Tables for 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, etc.). The LMIR program does not require annual recertification of income.
- For occupied properties, the borrower is required to submit an Owner Certification of Tenant Income Certification to Minnesota Housing. Within 120 days of closing, the owner will need to certify each tenant.

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% of MTSP; or 20 percent of units affordable to persons and families at 50% of MTSP
- 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 (FMR).
  - Scattered site developments (non-contiguous pieces of real property separated by more than just a street) must meet this requirement for each building.
  - Developments with project-based rental 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: (i) 15 years from 50 percent occupancy; (ii) the day the bonds are no longer outstanding; or (iii) 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.
  - 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.
  - Ineligible costs of up to 5 percent (including costs of issuance) may be financed with proceeds of the bond issue.

Refer to Minnesota Housing’s Tax-exempt Bonds Informational Guide for more information on tax-exempt bond requirements.

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 Multifamily Application Instructions: Consolidated RFP and HTC Rounds 1 and 2.

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 fully amortizing, fixed rate loans that may have a 30 year, 35 year, or 40 year term. At Minnesota Housing's sole discretion, a 30 or 35 year term may be considered for developments involving rehabilitation or refinance, and a 40 year term may be considered for new construction.
- LMIR loans may be structured with a 17 year term and 30-40 year amortization, subject to mitigating factors, at the sole discretion of Minnesota Housing.
- FFCC loans are generally made with an interest rate of zero 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. Minnesota Housing may at its sole discretion require 20 percent of eligible cash (as defined in the Multifamily Underwriting Standards) in excess of $50,000 to be repaid annually.

3.02 Debt Coverage Ratio

- LMIR loans are sized to meet Minnesota Housing's minimum debt coverage ratios (DCR), which range from 1.11:1 to 1.20:1 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.
  - The loan-to-value must not exceed 85 percent for existing affordable properties.

3.04 Operating Deficit Escrows

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 ODE 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 Minnesota Housing’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 1.11:1 DCR 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 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 ODE, 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, Minnesota Housing monitors monthly operating statements and conducts management reviews and property inspections. Minnesota Housing approves the annual budget and distributions from cash flow.

3.07 Return on Equity

Minnesota Housing currently allows a maximum return of 15 percent based on actual developer equity. Nonprofit owned developments are not allowed a distribution, unless the nonprofit is the managing general partner in a tax credit development, in which case the maximum distribution is 15% of initial equity.

3.08 Guarantees

Minnesota Housing requires at least one individual or legal entity with adequate financial capacity to guarantee all of the following:

- Construction completion; and
- All monetary obligations, including operating cost shortfalls and debt service, until the property has achieved a DCR of at least 1.11 (based on actual collected revenue less underwritten effective gross expenses, for three consecutive months); and
- 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 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 is also required. The minimum origination fee is $25,000.

Tax-exempt bond funded loans:

- A LMIR bridge loan/construction loan origination fee of 0.50 percent of the bond amount/bridge loan amount is required.
- 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; and, if applicable,
  - 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 at www.mnhousing.gov.

- For applications received as part of Minnesota Housing's annual Consolidated RFP, interest rates are set at board selection and are subject to satisfying specific contingencies established in the selection letter, generally:
  - Board approval to enter into a loan commitment must be obtained by the specified date (generally 12 months after selection); and
  - Closing of the permanent loan by the specified date (generally the end of the third year after selection.
  - Failure to meet either of the contingencies will result in the interest rate being reset at the then current rate.
- For applications received outside of the annual Consolidated RFP, the quoted interest rate will be set at the time of approval of an engagement letter and locked for six months, after which it may be subject to adjustment at Minnesota Housing's sole discretion.

Tax-exempt bond funded loans: Interest rates are based on market rates for the bonds at the time of the sale of the bonds, plus a spread. 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, an 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. After year one, MIP is paid monthly.

4.04 Construction Oversight Fee

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 total Minnesota Housing 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 Consolidated RFP.

The Multifamily Application Instructions: Consolidated RFP and HTC Rounds 1 and 2, Multifamily Underwriting Standards, and application materials will be used for both RFP and year-round funding applications. To find application materials, refer to Multifamily Rental Housing Common Application Materials.

For an application outside of the RFP, refer to the Amortizing Mortgages webpage, and contact the current program manager.

Chapter 6 – 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 nondiscrimination 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 7 – Fraud Disclosure and Suspension

7.01 Fraud Disclosure

The recipient must report all known or suspected instances of fraud in connection with the awarding or receipt of Minnesota Housing funds to Minnesota Housing's Chief Risk Officer as soon as evidence of fraud is discovered by the recipient. "Fraud" means an intentional deception made for personal gain or to damage another.

7.02 Suspension

By entering into any agreement with Minnesota Housing, accepting any award of funds from Minnesota Housing, or otherwise conducting any business with Minnesota Housing, a party represents that the party, or any principal of the party, has not been suspended from doing business with Minnesota Housing pursuant to the Minnesota Housing Finance Agency Board of Directors Participant Suspension Policy. A principal is defined as: (a) an officer, director, owner, partner, principal investigator, or other person within an organization or entity doing business with Minnesota Housing with management or supervisory responsibilities; or (b) a consultant or other person, who: (1) is in a position to handle Minnesota Housing funds; (2) is in a position to influence or control the use of those funds; or (3) occupies a technical or professional position capable of substantially influencing the development or outcome of an activity required to be performed under contract with Minnesota Housing. A party must contact Minnesota Housing for a list of all suspended individuals and organizations.

Chapter 8 – Program Contact

For questions, contact Caryn Polito, Program Manager, at 651.297.3123 or caryn.polito@state.mn.us. You may also contact the housing development officer (HDO) identified in your selection letter.