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Special Board Agenda Item: 3
Date: 4/5/2017

Item: Debt Management Policy

Staff Contact(s):
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Request Type:

☐ Approval
- ☐ Motion
- ☐ Resolution

☒ No Action Needed
- ☒ Discussion
- ☐ Information

Summary of Request:
Staff would like to discuss with the Board the requirements of the Agency's Debt Management Policy regarding the issuance of conduit bonds by the Agency.

Fiscal Impact:
None.

Meeting Agency Priorities:
☒ Address Specific and Critical Local Housing Needs
☐ Finance Housing Responsive to Minnesota's Changing Demographics
☐ Preserve Housing with Federal Project-Based Rent Assistance
☐ Prevent and End Homelessness
☐ Reduce Minnesota's Racial and Ethnicity Homeownership Disparity

Attachment(s):
- Background

The overall purpose of the Agency's Debt Management Policy is stated on page one of that policy as follows:

> The goal of Minnesota Housing (the "Agency") is to raise capital for its programs at the lowest overall cost. The Agency will take into consideration desired mortgage rates and the need to maintain asset and debt management flexibility while carefully managing risk.
>
> To achieve this, the Agency will:
> 1. Establish long-range financial objectives as set forth in Section 1.01. These objectives may change in response to economic and other factors.
> 2. Establish an Affordable Housing Plan that sets forth specific financing objectives for a one to two year period. This plan may be adjusted due to economic and other factors.
> 3. Maintain a debt management policy that provides for optimum access to capital markets and broad distribution capabilities, both horizontally (geographically) and vertically (both institutional and retail investors).
>
> Agency staff will monitor these plans and the policy and recommend changes when appropriate based on results of the Risk Based Capital Study and other circumstances.

Under the Agency's Debt Management Policy, tax-exempt bonding authority is a valuable resource that should be used for conduit bond issuances only if certain conditions are met (emphasis added):

> **1.09 Conduit Debt**
> For purposes of this section, a "conduit bond issue" is a bond issue in which the obligation of the Agency as issuer to pay principal of and interest on the bonds is limited to the payments it receives from a private third-party borrower under a loan or lease agreement relating to revenues derived from the facilities financed or other assets of the third-party borrower.
>
> Tax-exempt bonding authority is a valuable means of producing revenue because it enables the Agency to operate lending programs of a size far in excess of its own resources. It is therefore acknowledged that **the use of bonding authority for conduit debt issuance is generally not in the best financial interest of the Agency. From time to time and under certain conditions, use of tax-exempt bonding authority for conduit issuance may be desirable to meet state housing needs and may be considered. The following threshold conditions should be present in order for staff to recommend a conduit bond issue:**
>
> - Bonding authority used for conduit issues does not cause a significant loss of authority available to operate priority programs, in the sole judgment of the Agency.
> - **The issuance is for preservation of affordable rental units the Agency determines are important units to preserve under its strategic plan.**
> - Significant barriers to issuance by a different government issuer exist, such as properties located in multiple jurisdictions, making public notice and authorization requirements difficult.
> - The Agency has determined not to issue bonds secured by the Agency's general or limited obligation for the project to be financed.

- The Agency assumes no initial or continuing disclosure obligations in connection with the conduit issue.
- The Agency assumes no financial obligation in connection with the conduit issue.
- If publicly offered, the debt is expected to be rated in one of the two highest long-term rating categories by at least one nationally recognized rating agency acceptable to the Agency and, if applicable, the highest short-term rating category by at least one nationally recognized rating agency.
- If privately placed, repayment of the debt must, in the judgment of the Agency and based on information from the Agency's financial consultant, be financially feasible.
- The Agency's bond counsel must be utilized.
- All costs of issuance, maintenance and payment of the bond issue, including all Agency out-of-pocket expenses and fees and disbursements of bond counsel and the Agency's financial consultant, if any, must be paid by the borrower or, if available therefore, may be paid from proceeds of the bonds.
- Administrative fees to be paid to the Agency as issuer will not be less than, subject to arbitrage restrictions, the sum of (1) an upfront fee of 50 basis points times the original principal amount of the bonds, plus (2) an on-going fee payable semiannually equal to the greater of (a) one-half of 10 basis points applied to the then outstanding principal amount of the bonds or (b) a minimum amount to be established for the bond issue.

As stated above, given that conduit debt issuance is generally not in the best financial interest of the Agency, the Debt Management Policy has limited its use by imposing certain threshold conditions, one of which is that the issuance is for affordable rental units determined to be important units to preserve under the Agency's strategic plan. This requirement reflects the directive of Minn. Stat. section 462A.05, subd. 13 that the Agency "shall prefer those housing projects which are federally subsidized and those loans which are federally insured or guaranteed, to the extent that the agency finds such projects and loans to be available at the times and in the amounts needed to meet the shortage of residential housing for persons and families of low and moderate income."

This requirement also echoes the preference for preservation projects set forth in the bonding allocation statute (Minn. Stat. sec. 474A.061, subd. 2a). That statute requires Minnesota Management and Budget (MMB) to give first priority to awards of bonding authority from the Housing Pool for eligible residential rental projects to projects that preserve existing federally subsidized housing.

As Commissioner Tingerthal informed the Board at its December 2016 board meeting, it was possible that non-preservation projects applying for bonding authority from MMB in 2017 would not receive sufficient bonding authority to enable them to move forward. Because of that possibility, and given the Agency's mission to help meet the need for affordable housing, the Commissioner asked the Board if it would be willing to consider using a portion of the Agency's annual entitlement allocation of private activity bonding authority for issuance by the Agency of conduit bonds. The Board indicated it would be willing to consider the matter.

Commissioner Tingerthal's prediction was correct. In the first round of applications for bonding authority from the Housing Pool by MMB in January 2017, the total request for non-preservation projects was for $157,000,000. After allocation of $48,400,000 of bonding authority to preservation projects (pursuant to statutory requirements) only $77,602,000 remained available for allocation to non-preservation projects. Given the inadequacy of the remaining amount to fulfill all requests, MMB ultimately allocated a pro-rata portion to each of the five applicants, so that each project received 49.43% of the amount requested. Those partial allocations appear to be insufficient to qualify one or more of those projects for the 4% low income housing tax credits necessary for the projects to be financially feasible and rendering the projects unable to move forward.

Before developing a process and criteria for evaluating whether any of those non-preservation projects should be recommended to the Board for Agency funding with conduit bonds, staff concluded it was prudent to engage the Board in a discussion of the requirements of the Agency's Debt Management Policy regarding the issuance of conduit bonds.

This discussion will assist staff in deciding whether to evaluate that would benefit from the issuance of conduit bonds by the Agency even though those projects do not meet the threshold condition of the preservation of affordable rental units.