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NEW YORK MULTIFAMILY HUB – NOTES ON SECTION 202 MIXED FINANCE PROJECTS

The attached notes are meant to provide general guidance on processing of Section 202 mixed finance developments through the NY MF Hub. It is not all-inclusive and is subject to change depending upon the nature and structure of each project.

GENERAL DEVELOPMENT ISSUES:

- **The Development Team** – HUD's first and primary point of contact is the approved Section 202 sponsor. Sponsors will have identified their intent to use mixed finance at the fund reservation stage. Therefore, an experienced development team fully knowledgeable in both the Section 202, the LIHTC program, as well as tax-exempt bonds (if being used) should be in place at the time of application. HUD reserves the right to pre-approve a development team member if there is a question as to the firm's knowledge and experience. The limited partnership's consultant and closing attorney should be fully knowledgeable of and experienced in the 202 program with a previous successful track record. All members of the development team must commit to being available for meetings and conference calls on site.
- **Development Team Meeting** - A mixed finance development team pre-application meeting will be held within 30 days of the Section 202 fund reservation meeting. This meeting will allow sufficient time for all members of the development team to discuss the ownership and financing structure, preliminary designs, selection of the tax credit investor, potential waiver requests, etc.
- **Waivers** - Requests for waivers of Section 202 regulations should be submitted as soon as possible after the development team meeting but not later than 120 days prior to the Firm Commitment application in order to allow sufficient time for HUD Headquarters' review and processing. It is the responsibility of the development team to be sufficiently knowledgeable of the mixed finance regulations to be aware of the waivers that a specific project will require.
- **Communications** - HUD must be involved in and informed of any communications with the tax credit allocation agency, the syndicator/limited partner(s) and any other entity that commits funds for the development of the project.
- **Prohibition against Indemnification** - The tax credit recipient including the limited partnership, the GP as well as the HDFC may not indemnify members or other funding entities.

- **Reasonable Development Costs** – The "mixed finance" concept for the Section 202 program has been proffered because the Section 202 Program no longer fully funds the total replacement cost. With the use of tax credits, as well as other non-HUD funding sources, many development costs (including soft costs and those of professional consultants) are resulting in per unit costs far in excess of what might be considered "reasonable". It is the responsibility of the Section 202 sponsor and their professional development team to exercise due diligence and oversight as costs are being developed and reviewed.
- **Additional Equity and Funding** – Be certain you are aware of Section 202 statutes and regulations when applying for tax credits and/or additional funding sources. Do not provide statements or facts that are contrary to HUD Section 202 statutes or regulations in an effort to receive funding or a higher qualifying rating (i.e. income levels to be served other than very low income, occupancy set asides, etc). HUD cannot waive any statutory and some regulatory provisions which may conflict with the requirements of other funders. Each additional source of funding can result in regulatory and/or administrative requirements from that funding source which, in turn, will result in the need to coordinate and review respective regulatory documents prior to initial closing. These regulatory documents often have provisions that conflict with HUD requirements, some of which cannot be waived.
- **Contractual Arrangements** – All contracts for the provision of services must be entered into by the Section 202 Sponsor until the HDFC, GP and LP are formed.

OWNERSHIP STRUCTURE

- The structure of the limited partnership should be determined as soon as possible and presented to HUD for review for compliance with mixed finance regulations or the need for waivers. The structure should be clearly presented in an organizational chart, showing all interests, percentage of interest, type of business entity including beneficial and fee interests (as applicable). Include a narrative description of ownership interests.

FINANCING STRUCTURE

- Provide an organizational flow chart detailing the disbursement of the capital advance, the equity contribution and any other sources of funding. Include a memorandum to present all financial assumptions and the timetable for the use of the tax credits.

SITE CONTROL

- Site control documents will have been approved by HUD at the fund reservation stage. HUD does not expect changes to the documents or the form of site control. Any variation to the documents submitted and approved at fund reservation could result in the project's being unable to proceed or in lengthy approval processes.

- Projects involving leaseholds should comply with HUD's leasehold requirements found at 4571.5, Appendix 14.
- Projects involving ground leases or condominium ownership are discouraged. However, if the development team is committed to such structures provide all draft documents to HUD no later than 120 days prior to submission of the Firm Commitment application.
- If site control is being obtained from NYC HPD, carefully review the CEQR declaration for conditions that may affect the design of the project.

DESIGN/CONSTRUCTION

- Early HUD review of the project's preliminary design is essential. Close coordination of design review with key funding sources will better assure design efficiency. The project architect and other development team members should coordinate with the HUD design architect to advise how design review among the multiple funding/review agencies will be coordinated.
- Developments with multiple uses under a condominium ownership structure must present preliminary drawings to HUD for review and approval in order to clearly identify individual condo ownership interests as well as common elements. Common elements should be kept to a minimum. Provide an allocation table with sq. ft. percentages of the residential and non residential uses, including limited common and common elements, to be used as the basis for cost allocations. HUD will not participate in funding condo elements in which it does not have an ownership interest (i.e. foundations). Condo declarations should not be filed without HUD review. The architectural design for any project containing multiple condo units must be defined and separated by floors with not more than one use per floor. This will enable the multiple condo owners to separate spaces and associated construction and operating/maintenance costs.
- The general contractor (GC) is subject to HUD review and approval prior to submission of the Firm Commitment application. HUD encourages the LP to select a GC with previous residential (and preferably HUD) experience. All GCs must submit a letter from the surety attesting to the availability of a 100% payment performance bond at the time of submission of the GC qualifications. If a joint venture is proposed, the joint venture agreement must also be submitted to HUD at the time of submission of GC qualifications. HUD discourages the use of joint ventures especially in complicated developments.
- If the tax credit syndicator or investor LP require a construction manager (clerk of the works), the position must be filled by the time of initial closing. This cost will not be paid from 202 funds.

FIRM COMMITMENT APPLICATION

The financial assumptions presented in the Firm Commitment Application should be consistent with the information presented to the tax credit allocating agency and the tax credit syndicators. HUD will require a certification to this effect at the time the Firm Commitment Application is submitted.

1. Exhibit no. 1 – HUD 92013 – must include an allocation spreadsheet showing the distribution of costs between HUD and non-HUD funding sources, including ratios of soft and hard costs for the time period from initial closing through construction completion. Allocation lines on the spread sheet should conform to the items on the HUD 92013 and 2264. The allocation spreadsheet must reflect the ratio of HUD and tax credit equity to the total replacement cost. Do not front end HUD funds or use a ratio that does not reflect the funding ratios of funding sources. The approved allocation spread sheet will become an exhibit to the Construction Coordination and Disbursement Plan at initial closing.
2. The HUD 92013 for mixed finance projects must breakout certain expenses in the suggested format attached hereto. Include the three month operating reserve as required by the mixed finance regs.
3. If the project involves multiple condominium units, provide cost allocation ratios and the basis for the allocation.
4. If a project has previously received a HUD Demonstration Planning Grant (DPG), be certain that the replacement cost includes these amounts and that any DPG funding previously released is not greater than the amount shown for the specific line item on the HUD 92013.
5. Include an organizational chart of the limited partnership showing the ownership structure of the limited partnership, the GPs and all limited partners with a 25% or greater interest. This chart must conform to the ownership entities on the HUD 92013 and the HUD 2530 submissions, including EINs.
6. Provide a copy of the application for a tax credit reservation and the tax credit Reservation Agreement from the allocating agency. If an application has not yet been filed, provide the total development and syndication costs and the calculation of your anticipated credit.
7. Provide the tax credit commitment letter from the syndicator/investor limited partner and a draft LPA.
8. Include a financing structure chart and summary showing all sources of funding including the tax credit allocation, anticipated tax credit equity and all other funding sources. Include the type of funding and their terms. The financing structure that involves tax credit investor equity must include an opinion from the investor LP's attorney attesting to its compliance with IRS regulations.
9. Attach the regulatory documents from all funding sources. These regulatory documents may not conflict with HUD regulations.
10. The mixed finance regulatory requirement for 2% working capital may be reconsidered if the tax credit investor requires a working capital or contingency amount already included in the project's total replacement cost on the HUD 92013.
11. Fully completed HUD Form 2530s must be submitted electronically or in paper format for all of the ownership entities: the limited partnership, GP, sponsor, HDFC (if applicable), LP (include general partner & all limited partners with a 25% or greater ownership interest).

12. Exhibit 20 – Developer's fee – will only reflect the tax credit developer's fee rather than the format required under the traditional Section 202 program. The developer's fee may be needed to provide additional equity to the project.
13. During Firm Commitment processing, HUD will contact the tax credit allocating agency to confirm that the proposed costs, eligible basis and the developer's fee are acceptable.

ISSUANCE OF THE FIRM COMMITMENT – SPECIAL CONDITIONS

In addition to the standard additional commitment conditions, the Section 202 Firm Commitment for mixed finance projects will include a set of Special Conditions in addition to the Additional Commitment Conditions. These Special Conditions include the following considerations:

1. All documents associated with the Section 202 initial endorsement including organizational documents and funding commitments must comply with HUD Rules and Regulations, including the mixed finance final rule dated September 13, 2005.
2. Prohibition against cross defaults, encumbrances and additional debt.
3. Non-interference Agreement.
4. Continued use and occupancy as a very low income senior development for forty years.
5. A description of the cost allocation ratios between HUD and non-HUD funding sources for both hard and soft costs.
6. A requirement for preparation of a Construction Coordination and Disbursement Plan reflecting the cost allocation ratios.
7. Use of an inter-creditor agreement among all funding entities, including the investor LP, together with a priority subordination and disbursement agreement.

INITIAL CLOSING – DOCUMENT PREPARATION

- The legal sufficiency of all closing documents must be supported by opinions from both the closing attorney for the Section 202 limited partnership and the attorney for the investor LP. HUD Counsel will not begin its review of the closing documents until the opinions have been submitted.
- Due to the nature of the Section 202 mixed finance ownership structure as a limited partnership, many of the standard Section 202 closing documents require revisions. Among these documents are: the Capital Advance Agreement , Section 202 Mortgage and Note, Use Agreement, Regulatory Agreement and Agreement and Certification.
- A Plan for Construction Coordination and Disbursement will be an initial closing document. This Plan, which describes the payment and funding disbursement process and allocations, must be accepted by all funding sources.
- Depending on the financing and ownership structure, multiple Capital Advance Agreements, Notes and Mortgages may be necessary.
- Regulatory Documents from the tax credit investor (i.e. Limited Partnership Agreement) and all other regulatory agencies (i.e. HPD Regulatory Agreement) must be submitted in

draft form with the Firm Commitment application or in final form with the initial closing documents.

- All funding sources must be in place in order to proceed to initial closing.
- Plan for a two day initial closing.

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