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Long Term Affordability Using NSP and HOME

October 6, 2011

HUD Community Planning and Development

Speakers and Q and A Format

- Speakers
  - John Laswick, HUD
  - Virginia Sardone, HUD
  - Hunter Kurtz, HUD
  - David Noguera, HUD
  - Marsha Tonkovich, ICF
- How to ask questions
  - Change status in Live Meeting from green to purple
  - Press *1 to ask a question through Premiere Conference
    - ✓ Provide Name and Organization
    - ✓ If question already answered, press *2 to remove from queue
  - Change status back to green after question answered

Agenda

- Presentation on key topics:
  - Key HOME rules that apply to NSP
  - Ways to combine NSP & HOME funds
- Per past attendee feedback, will do entire presentation (approximately 75 minutes) & then take questions (approximately 45 minutes)

How HOME Rules Apply to NSP

- In some cases, NSP rules defer to HOME rules as safe harbor & in other cases HOME rules provide general context for NSP:
  - ✓ Concept of assisted units
  - ✓ Cost allocation
  - ✓ Set aside for very low income units
  - ✓ Timing of investment
  - ✓ Affordability period
    - – Resale/recapture and homebuyer affordability period requirements
    - – Rents, income verification, sale of the project, unit mix
- Grantees can choose to adopt HOME rules or develop alternate approach in Action Plan

Concept of Assisted Units

- Applies to rental projects when NSP does not pay 100% of cost or have 100% of units
- NSP-assisted unit has been acquired, rehabbed or constructed with NSP $$$
- NSP-assisted unit must follow NSP rules such as:
  – Property type
  – Eligible costs (more later)
  – Quality/green standards
  – Tenant income
  – Rents, income verification during affordability period
- Other units in project are not necessarily subject to NSP rules

Concept of Assisted Units (cont)

- “Assisted units” ties to meeting LMMI housing national objective (LMMH)

- Two options for meeting LMMH:
  - <u>CDBG approach</u>: At least 51% of units are NSP-assisted
  - <u>HOME approach</u>: Follow HOME cost allocation methodology to determine assisted units or maximum investment
    - ✓HOME has two methods: proportional and actual cost

Cost Allocation

- <u>Concept</u>: NSP funds should not pay more than actual, eligible costs for the number of units designated as NSP assisted
- <u>Basic equation</u>:

$$\frac{\text{NSP \$\$\$}}{\text{Total Eligible Development Cost}} = \frac{\text{NSP Assisted Units}}{\text{Total Units}}$$

- Can solve for units or for dollars
- Approach differs for comparable and non-comparable units

Cost Allocation: Comparable Versus Non Comparable Units

- Comparable units have the same:
  - Number of bedrooms
  - Amenities
  - Square footage
- Non-comparable units have:
  - Different number of bedrooms and/or
  - Different amenities and square footage
- Comparable units can use a proportionate share approach to cost allocation
  - Non comparable units MUST use an actual cost approach

Cost Allocation: Comparable Unit Principles

- Costs are allocated based on a proportionate share of all eligible costs
  - Example: If NSP-assisted units are 30% of total, maximum NSP investment is 30% of total eligible development cost
  - **OR**: If NSP will pay 30% of total eligible costs, a minimum of 30% of units must be NSP-assisted
- If use proportionate share approach, must distribute NSP-assisted units evenly across bedroom sizes

Cost Allocation: Solving For Minimum # Comparable NSP-Assisted Units

- Key steps:

1. Decide level of NSP investment
2. Determine total eligible cost
3. Create ratio of NSP investment to total eligible cost
4. Multiply total units times percentage of eligible cost = NSP's fair share of units

Number Of Comparable NSP Units Example

- Total cost: $900,000
- NSP investment: $400,000
- 10 comparable units in project
- At minimum, how many units must be NSP assisted?

Number Of Comparable NSP Units Example (cont)

1. $$\frac{\$400{,}000}{\$900{,}000} = 0.44$$

2. (0.44) * (10 units) = 4.4, round up to 5 units

Cost Allocation: Solving For Comparable Unit Maximum Investment

- Key steps:
  1. Decide number of project units that will be NSP-assisted
  2. Create ratio of NSP assisted to all units
  3. Multiply NSP assisted unit percent times total eligible development cost = NSP's fair share of eligible costs

Comparable Unit Investment Example

- Total eligible costs: $2,000,000
- Total units: 20 comparable units
- NSP units: 2
- Maximum NSP investment?

Comparable Unit Investment Example (Cont)

1. $$\frac{\text{2 units}}{\text{20 units}} = 0.1$$

2. (0.1) * ($2,000,000) = $200,000

Cost Allocation: Non-Comparable Units

- Must determine which units will be NSP-assisted
- Maximum investment capped at:
  - NSP paying no more than actual costs of NSP assisted units in the project plus
  - Pro-rata (fair share) of common costs such as:
    - ✓ Acquisition
    - ✓ Common areas
    - ✓ Roof, driveway, etc
    - ✓ External building envelope

Set Aside for Very Low Income Units

- In addition to determining total number of NSP assisted units, must determine which units, if any, will count toward LH25
- NSP-paid expenses for any unit meeting LH25 income targeting may be counted toward set-aside
  - Example: 20 units in project, 10 will be NSP assisted
    - ✓ TDC is $2,500,000
    - ✓ NSP investment is $1,000,000
    - ✓ All 10 NSP units will be occupied by households at 50% AMI
    - ✓ $1,000,000 can be counted toward LH25

Set Aside for Very Low Income Units(cont)

- When there will be a mix of LH25 and other units, need to look at portion of TDC paid by NSP and portion of LH25 units
- Example: 50 units in project, all will be counted as NSP assisted
  - ✓ TDC is $5,000,000
  - ✓ NSP investment is $2,000,000 (40%)
  - ✓ 25 units will be occupied by households at 50% AMI
  - ✓ 25 units will be occupied by households up to 80% AMI
  - ✓ All $2,000,000 can be counted toward LH25 because investment is only 40% of TDC but LH25 units are 50%

Timing of Investment

- Like HOME, NSP does not dictate the timing of when funds can be invested
  - Cost allocation can determine maximum NSP investment given NSP proportional share of units (so that project meets LMMH national objective)
  - Establishes cap on what can be spent but not what development cost line item is paid
  - NSP grantee can choose to pay any eligible line item
  - Important for NSP given expenditure deadlines

Timing of Investment (cont)

- Example:
  - Total eligible development cost: $2,500,000
  - Total units 25, NSP-assisted units 10
  - Maximum NSP investment: $1,000,000
  - Of TDC:
    - ✓$400,000 for acquisition
    - ✓$50,000 up front predevelopment/soft costs
    - ✓$2,050,000 for construction
  - NSP could pay 100% of acquisition & predevelopment and $550,000 of construction

Affordability Period

- NSP can use HOME affordability period:

Per Assisted Unit NSP $	Min. Affordability Period
<$15,000	5 years
$15,000 - $40,000	10 years
>$40,000	15 years
Rental New Construction/ Acquisition of New Construction	20 years

- Rules apply to both homebuyer and rental units

Options for Homebuyer Affordability

- HOME rules are safe harbor
  - Can use alternate approach but must get HUD approval
  - HOME affordability periods are minimums – NSP grantees can set longer terms
- For each homebuyer program, UP FRONT, grantee must select compliance approach during period of affordability
  - Two options: Resale or recapture
  - Cannot mix recapture and resale; must choose one or other
  - If no “Direct Subsidy” to homebuyer, grantee must select Resale

Recapture Approach

- Meet affordability requirement by recapturing funds if unit sold by owner during affordability period
  - Amount recaptured depends on sale price and chosen recapture approach
  - Cannot use recapture if assistance = grant
- May re-sell unit to any buyer at any price
  - Once $$$ recaptured & unit sold, no additional unit restrictions

Recapture Approach (cont)

- Affordability period based on “total amount subject to recapture”
- Total subject to recapture is direct homebuyer subsidy:
  - Assistance provided to buyer
    - ✓Downpayment/closing cost assistance
    - ✓Subsidized loan
  - PLUS assistance amounts that write sale cost below market value
    - ✓Need an agreement with buyer
- Does not include NSP amounts to subsidize development when that cost exceeds market value (known as development subsidy)

Recapture Affordability Period Example

- NSP loan to buyer: $15,000
- NSP downpayment assist: $5,000
- NSP developer assist : $50,000
- Market value of home: $160,000
- Sale price of home: $155,000
- Total amount subject to recapture:
  - $15,000 + $5,000 + $5,000 = $25,000
- Affordability period 10 years

Recapture Approach: Amount Recaptured

- Occurs when home is sold during affordability period (whether voluntary or foreclosure)
- Recapture amount is limited to "net proceeds"
- Net proceeds defined as:

  Net Proceeds = Sale Price – Superior Debt – Closing Costs

- Limits amount owed back if net proceeds insufficient – For example:
  - Original NSP investment: $20,000
  - Unit has declined in value & net proceeds at sale are $7,000
  - Maximum amount owned to grantee: $7,000

Recapture Approach: Amount Recaptured (cont)

- Grantee must determine up front how to share net proceeds with owner (seller)
- Four options:
  1. Recapture full amount of direct subsidy to homebuyer;
  2. Forgive direct subsidy pro-rata over affordability period;
  3. Proportionately share net proceeds; or
  4. Allow buyer to recover his/her initial investment first.
- NSP also allows for sharing of appreciation which makes sense for markets that will come back strongly in 5-10 years

Resale Approach

- Meet affordability requirement by limiting unit sale price and eligible buyers for any sale during affordability period
  - Does not preclude having mortgage on unit which is repaid at sale
- Typically used in situations where goal is creation of long term pool of affordable units

Resale Approach (cont)

- Affordability period based on total NSP investment in the property (even if only temporarily in project)
  - Must include $$$ of NSP assistance to buyer
  - PLUS total amount of NSP funds provided to developer
- Note: if use HOME & NSP together, do not add HOME & NSP assistance together – calculate affordability period separately for each

Resale Affordability Period Example

- NSP loan to buyer: $15,000
- NSP downpayment assist: $5,000
- NSP developer assist : $50,000
- Market value of home: $160,000
- Sale price of home: $155,000
- Total amount of subsidy:
  - $15,000 + $5,000 + $50,000 = $70,000
- Affordability period 15 years

Resale Approach: Actions When Unit is Sold

- If there is resale requirement, when home is sold:
  - New buyer must be low-income
    - ✓Next buyer income cap based on original unit income targeting
    - ✓If unit originally counted toward 50% income targeting, new buyers during affordability period must also be 50% or less
    - ✓If unit originally counted toward 120% income targeting, new buyers during affordability period must also be 120% or less

Resale Approach: Actions When Unit is Sold (cont)

- If there is resale requirement, when home is sold:
  - Home must be affordable to new buyer
  - New buyer must occupy house as principal residence
  - Original buyer must receive a “fair return”
  - Remaining resale restrictions apply to new buyer

Enforcement of Resale/ Recapture

- Resale: must use deed restriction / covenant
- Recapture: must use lien (should be recorded) or deed restriction/land covenant
- Must also have compliance agreement with homebuyer & developer (if applicable)

Rental Affordability Period Compliance

- Affordability period dictates rental compliance period
- Covers:
  - Rents
  - Incomes
  - Unit mix
  - Sale during affordability period

On-Going Rent Limits

- Grantee required to define affordable rents in its Action Plan
  - HOME is safe harbor
  - NSP rents must remain affordable for affordability period
- HOME uses high HOME and low HOME rent limit
  - Published by HUD
  - Tenants given notice of increases
  - Actual unit rents can be less but not more than limits
  - Rents are inclusive of utilities -- must adjust rents for tenant-paid utilities
    - ✓Subtract utilities to determine rent paid by tenant
    - ✓Use actual utility costs or use utility allowance schedule
    - ✓Can use PHA schedule if it is up to date

Tenant Income Eligibility

- NSP Caps 100% of initial occupants at or below 120% median
  - Only applied to households in assisted units
- **Unlike HOME**, NSP checks incomes of new tenant only at unit turn over
  - ✓Unit originally occupied by household at 120% of median, new tenant at $\leq$ 120% of median
  - ✓Unit originally occupied by household at 50% of median, new tenant at 50% of median

Determining Income

- Tenant income inclusions and exclusions:
  - Use IRS, Census or Part 5 (Section 8) definition
  - Anticipate income for next 12 months
  - Recommend full 3rd party documentation, e.g., an employer
  - Verifiable self-certification from assisted person is OK
    - ✓WARNING on using this method: If self-certification determined to be incorrect or fraudulent, project may be ineligible
  - Compare income to income limits to determine eligibility
    - ✓See HOME income guide at: http://www.hud.gov/offices/cpd/affordablehousing/library/modelguides/2005/1780.cfm

Managing Unit Mix Over Affordability Period

- Grantee must ensure that owner maintains proper number and type of NSP assisted units
- Key considerations:
  - Total number of NSP v. other units
  - Maintaining number of LH25 units
  - Timing of rent changes
  - Whether units are fixed or floating

Rental Property Sales During Affordability Period

- If assisted project sold, must continue occupant, rent restrictions for balance of affordability period
  - Record requirements as land covenant or deed restriction
  - Include within written agreement with rental owner
  - If project is foreclosed or sold without restrictions, grantee must repay investment minus any PI earned to date

Why Combine HOME & NSP?

- Many reasons to consider programs together:
  - Stretches scarce resources
  - Differences in eligible activities
  - Differences in target populations
  - Yet, many rules across two programs are similar

Ways to Combine NSP & HOME

- Can combine:
  - Together in same project:
    - ✓<u>Example</u>: NSP for acquisition and demolition, HOME for new construction
  - In same program but not same project:
    - ✓<u>Example</u>: Downpayment program – HOME for low income, NSP for moderate income
  - In separate but complementary programs:
    - ✓<u>Example</u>: Goal is neighborhood revitalization. Use NSP for targeted homebuyer and rental programs, use HOME for homeowner rehab in same neighborhood

Rules When Combining NSP & HOME

- When combined in same unit, must meet rules of both programs
  - Generally, most restrictive rule applies
- Example #1: Number of very low income units in a rental development
- Example #2: Sales price of homebuyer units
- Example #3: Income limits

NSP Resource Exchange Links

NSP Resource Exchange	http://hudnsphelp.info
Search the Resource Library	http://hudnsphelp.info/resources
Search the FAQs	http://hudnsphelp.info/faqs
View All Training Materials on the Learning Center	http://hudnsphelp.info/learning
Submit a Policy Question via Ask A Question	http://hudnsphelp.info/question
Request Technical Assistance	http://hudnsphelp.info/RequestTA

Connect with NSP	
Join the Listserv	http://hudnsphelp.info/listserv
Visit the NSP Flickr Gallery	http://www.flickr.com/photos/nspresourceexchange
Visit the NSP YouTube Channel	http://www.youtube.com/user/NSPResourceExchange

Please Give Us Your Feedback

- Answer a few short questions
- Link:

  http://www.surveymonkey.com/s/HOME_NSP_Rules