

IPED LEARN THE BASICS: HOUSING TAX CREDITS 101

Getting Started: Assessing the Market, Working with Your Tax Credit Agency, and Understanding the Development Process

The Lender Perspective



Massachusetts Housing Finance Agency (“MassHousing”)

The Commonwealth’s Affordable Housing Bank

- Quasi-public state agency created by statute in 1966;
- Commenced operations in 1968, first loans made 1969
- Provides construction, bridge, and permanent senior mortgage financing
- Tax-exempt and taxable sources of funds
- Conduit Financing – tax-exempt sources
- Subordinate Loans – Opportunity Fund
- Administrator of Massachusetts Affordable Housing Trust Fund



MassHousing Loan Programs – Tied to Major HUD Initiatives

MassHousing loan programs tied historically to federal programs:

- Section 236 Program – uninsured loans (interest subsidy)
(also Flex Subsidy, Rent Supp, and RAD Programs)
- Section 202 Program
- Section 8 Rental Subsidy
- Low Income Housing Tax Credits
- HOPE VI Program
- CHOICE Neighborhood Program
- ARPA Funds (coming soon!)



MassHousing Loan Programs – Tied to Major State Initiatives

MassHousing loan programs also tied historically to state programs:

- Section 13A (interest subsidy)
- SHARP
- MRVP – Massachusetts Rental Voucher Program
- Subordinate Loan Programs (MassDocs), including:
 - Affordable Housing Trust Fund (AHTF)
 - Community Based Housing (CBH)
 - Housing Stabilization Fund (HSF)
 - Facilities Consolidation Fund (FCF)
 - HOME (state and local), CATNHP, etc.
- M.G.L. c. 40B (“anti-snob zoning”)
- State LIHTC



MassHousing

Roles as Lender and/or Issuer

MassHousing acts as first mortgage lender AND as issuer of either tax-exempt or taxable securities to finance its loans.

The Commonwealth of Massachusetts Department of Housing and Community Development (DHCD) is the credit allocating agency for Massachusetts.

This divided structure is unlike many/most states, where these functions are typically unified within a single agency.



How are LIHTC Developments Financed?

Equity

- LIHTC (9% and 4%) Syndication Equity
- Other (e.g. federal historic credits)

Debt

- Senior Mortgage (Construction and/or Permanent, with or without Bridge Financing)
- Subordinate Mortgage Financing
 - Federal, State and Local Government Loan Programs
 - Seller Financing
 - Sponsor Acquisition Loans
 - Deferred Developer Fee

Which Comes First?

How much debt?

How much equity?

How much affordability?

All three are tied together. The determination of how much affordability drives the determination of how much debt (and forms of debt) and equity is required.



Senior Loan – Pre-Commitment

Getting in the Pipeline

Developers contact MassHousing:

- Share project plans
- Ask questions about underwriting
- Discuss timing
- Request feedback or letters of interest

Origination Team develops and manages a pipeline, taking into consideration:

- Preservation Matrix
- Resources needed – state, local, MassHousing, other
- Readiness to proceed
- Other priorities



Senior Loan – Pre-Commitment

Structuring a Transaction

Understanding Project Elements

- Ground lease
- Condominium structure
- Commercial space
- Homeownership units

Setting the Role of Each Stakeholder

- Construction debt
- LIHTC equity provider
- Other development team members



Senior Loan – Pre-Commitment

Structuring a Capital Stack

Sizing the Senior Loan

- Rental subsidies
- Rent setting
- Operating budget review
- Debt execution

Compiling Diligence

- Development team members
- Entitlements
- Necessary subsidies



Senior Loan – Pre-Commitment

Moving toward Commitment and Closing

Internal Review

- Design and Construction
- Appraisal and Marketing
- Rental Management
- Diversity and Inclusion

Additional Review

- Loan Committee and Board
- HUD Risk Share



Senior Loan – Post-commitment and Closing

Drafting of Loan Documents – principal documents include:

- Loan Agreement(s)
- Note
- Mortgage
- Regulatory Agreement
- Residential Compliance Agreement
(aka Bond Regulatory Agreement)

Tax Exempt Debt – requires:

- Borrower's Tax Certificate
(with 95/5 and 50% Test Letters)



Senior Loan – Post-commitment and Closing

Lender Diligence – Borrower Organizational Documents

Review of Partnership/Company Documents:

- Structure and Timing of Capital Contributions
- Review of Repurchase Provisions
- Reserve Requirements
- Cash Flow Waterfall
- Payment of Developer Fee
- Incorporation of MassHousing Rider
(re: primacy of Loan Documents)



Senior Loan – Post-commitment and Closing

Lender Diligence – Property Management

- Operating Budget
- Management Agreement
- Affirmative Fair Housing Marketing Plan
- Tenant Selection Plan
- Other (e.g. tenant relocation plans, supportive services, commercial leases, etc.)

Senior Loan – Post-commitment and Closing

Lender Diligence – Construction

- Architect's Contract
- Scope of Work/Plans and Specifications
- Construction Cost and Contingencies
- Construction Contract

Other Diligence Materials

- Environmental
- Title and Survey



Senior Loan – Post-commitment and Closing

Closing Diligence – Lender’s Perspective:

The Senior Lender’s interests are both aligned with, and potentially adverse to, the other parties in the transaction:

- Developer/Sponsor
- Investor
- Subordinate Lender(s)
- Government Entities



Senior Loan - Construction

Construction/Rehabilitation Phase

- Construction Monitoring

Senior Loan – Completion

- Construction Completion
- Sustaining Occupancy
- Cost Certification
- Supplement to Borrower's Tax Certificate
(with updated 95/5 and 50% test letters)
- Permanent Loan Conversion (including payoff of construction and/or bridge loans and Risk Sharing Endorsement)

Lender's Perspective: Things to Consider

1. Simplify structures (entities, funding schedules) where possible.
2. Be realistic with schedule/timing – don't continue to compress a schedule to meet a target date if benchmarks are not achieved.
3. Review and refine diligence materials (draft documents, title proformas, surveys, etc.) before they are shared with a wider audience.
4. Seek to understand the institutions and programs that you're working with, and try to recognize potential conflicts.
5. If you need help or discover a potential conflict, reach out to agency/lender to discuss how it might be resolved.
6. Keep a positive attitude – everyone involved wants the same goal – to create affordable housing.

