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Consolidated and Further Continuing Appropriations Act of 2012 Webinar Series
Deadline for Sale of HOME Homebuyer Units & Conversion to Rental

Transcript

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Note: This transcript does not include the Q&A portions of the webinar. HUD will be posting additional written guidance in the form of Frequently Asked Questions (FAQs) that address both questions addressed in this webinar and others that were not addressed due to time limitations. Those will be posted to the www.hometa.info website as they become available.

Minor corrections to the transcript have been made to reflect HOME-program acronyms, inaudible portions of the recording, and the like. In some cases a word or phrase has been inserted or corrected for clarity, it is indicated by italicized brackets like this *{inserted/clarified language}.*

Maryanne (Operator): Good morning and welcome to today's HOME program webinar on the consolidated and further continuing appropriation act of 2012 deadline for sale of homebuyer units and conversion to rental. At this time I would like to turn the call over to Steve Lathom of Training and Development Associates.

Steve Lathom: Thank you, Maryanne and welcome everybody. We are glad to have you with us today. Again, as you can see from the title slide which is a bit of a handful we are here to talk about the deadline for sale of homebuyer units and conversion to rental. And this, of course, is driven by the consolidated and further continuing appropriations act of 2012, a title that only congress could love. We have the next slide here showing you this is part of an overall series. A couple of things I would like to point out about that: the series of webinars is related to CPD notice 12007 that implements the consolidated and et cetera, et cetera which we are going to call today the fiscal year 2012 HOME appropriations law. This is the, what is that, the fifth of the webinars. The first has been posted online, it was only posted online. It was not held live. It has an overview.

We have already done one on IDIS on market analysis and on underwriting developer capacity for homebuyer projects. Today we are talking about the deadline for sale. Also just to note for everybody, the next three webinars have had some date changes. The dates that you see are the appropriate dates. So next Thursday, the 28th will be underwriting and developer capacity for rental. Tuesday, July 10th we will talk about assessing CHDOs development capacity for PJs. And Thursday, July 12th we will do the same thing but talking more to the CHDOs. So I would like to let everybody again just know about those date changes. All of these will be posted to the hometa.info website and so if you are not able to make one of the calls previously or perhaps one of the next

calls you will be able to see the slides, you will be able to download a transcript, a recording, as well as any of the handouts that we have made available.

We will take some breaks today for you to be able to ask questions and a couple things I would like to do just off the bat is let you know that you can ask questions at any point by clicking at the top of your screen on the Q & A menu. You will get a dropdown box and be able to type in your question. So we would love to have you do that at any point in the conversation. Also in the upper right corner of your screen in the Live Meeting client there is a little icon that looks kind of like three sheets of notebook paper. If you open that there are several handouts available for your download today. We will refer to those at various points. You can download the slides and you can download some other resources that we are making available to you. And again, afterwards all of those will be posted to the hometa.info website.

So with that what I would like to do is welcome my other presenters. From HUD today we have Ginny Sardone. Marcia Sigal probably is not going to be able to join us. And we also have Mandy Wampler, all from the Office of Affordable Housing programs. And we will turn it over to them in just a moment. Again, my name is Steve Lathom from Training and Development Associates and you are going to hear from me for a while today. And you are also going to hear from Monte Franke of the Franke Consulting Group. Many of us know Monte and have had the privilege of being in various classes with him over the years out on the training circuit and I am particularly pleased to have him join us today and contribute to the webinar.

We have got several goals today. First and foremost we want to help PJs understand the context of the fiscal year 2012 HOME appropriation law requirements. We know these come at a time when there have been a lot of questions about the proposed rule, the current rule, new CPD notices that have come out earlier this year, and just a lot of changes to the environment in which we all work with the HOME program. Building off of last week's webinar on underwriting homebuyer projects we want to help PJs think more in detail about some of the program design, project selection, and ongoing management considerations that can reduce your risk of having units not sell and being faced with that choice of either converting to rental or in some cases repaying the HOME investment. But no matter how well we plan or execute there will be projects that are not sold and need to be converted so we will talk about how to take those lemons and make some lemonade. Helping to start thinking through how you successfully convert to rental and put the homes you funded into use serving the needs of low income tenants rather than the needs of low income buyers. Finally within that context we will talk a little bit about some exit strategies and reinvestment strategies you can start thinking about now as you back into doing single family scattered site rentals that help make those more sustainable over time. And as we have noted again

we will take breaks at a few points to address questions and we will use time at the end of the webinar to address questions as well.

With that what I would like to do is turn this over to Ginny to talk a little bit about just the legislative and regulatory context where these rules are coming from. Ginny?

Ginny Sardone: Thank you, Steve. Before I do that I would like to introduce two more of my colleagues who are with us today: Peter Huber and Vashawn Banks from the Office of Affordable Housing programs financial and information systems division are with us in case any of the questions that we get veer into the territory of IDIS. So yes, as Steve mentioned there were a lot of things that were going on last year with respect to the HOME program. And most of you know that congress held two oversight hearings of the HOME program last year, both of them in the House. And in those hearings the members of congress expressed a lot of concern regarding the progress of a number of many of the HOME projects that are open in our system right now. And they expressed some particular concern about the number of homebuyer projects that have been either rehabilitated or constructed with HOME funds that are either not in a situation where construction is not complete yet or construction is complete but because of the change in the housing market nationally they are not sold.

And that was one of the things that HUD was addressing in the proposed rule as we were writing it last year. Before the proposed rule was published congress decided that it wanted to take some of the things that were being contemplated in the proposed rule and put them into our appropriations which essentially made them statutory. So there were four provisions that were put into the appropriations law and they are applicable because they are in appropriation and not in an authorizing statute. To fiscal year 2012 HOME funds and given the way that IDIS functions what that really means for participating jurisdictions is that these provisions are applicable to projects that are set up in IDIS under a 2012 action plan. So when you are thinking about how the provisions that we are going to be talking about today are going to apply your programs keep that in mind. These are not applicable to projects that you already have completed or that are already set up in IDIS and underway.

These provisions are applicable to 2012 action plan projects so for the most part they are projects that you have not funded or put into the system yet. As I mentioned, the fact that they are in the appropriations statute and not in a rule do make them statutory and that means that HUD does not have any administrative flexibility with respect to extensions or waivers, the kinds of things that might happen if these were regulatory requirements. So the specific provision that we are talking about today is the requirement in the statute that homeownership units that are not sold to an eligible homebuyer within 12 months of project completion need to be rented to an

eligible tenant. Essentially they need to be converted to HOME rental units subject to all of the HOME rental requirements.

HUD issued a notice recently; it is CPD notice 12-007, that explains this particular provision and the three other provisions that were in that law. We also in that notice essentially tried to talk about how sort of operationally these provisions applied and what that might mean in IDIS. There have been a number of enhancements or changes that we have made to the IDIS system that went live on May fourth. One of them is applicable to this homebuyer deadline requirement that we have as our subject today. And so we can take those questions as they come. Before I hand it back over to Steve I do, though, want to throw out the same caveat that we have been giving through this entire webinar series and that is that the provisions that you see in the 2012 HOME appropriation law are also part of the HOME proposed rule although in some cases not exactly word for word the same. And there has been significant confusion out there between the applicability and the provisions of the HOME proposed rule and the appropriation law.

So I just want to make absolutely clear to everybody that right now we have a proposed rule for the HOME program that is not effective. And nothing in that rule will become effective until HUD completes its review of the comments, completes drafting and clearing a final rule, and publishing it. So what we are talking about today only applies to these 2012 action plan projects and we are not going to be addressing any of the minor differences there might be between the proposed rule and the appropriations language. With that I will turn it back over to Steve.

Steve Lathom: Thank you, Ginny. And again, I think that is a – that last point is one that is really important for everybody to understand. For purposes of today's discussion the proposed HOME rule essentially does not exist. We are going to focus on the statutory requirements that are the law of the land passed by congress, signed by the president, School House Rock version if we all remember that. We are going to talk about that and we are going to start right now by looking at the language in CPD notice 12-007 that outlines the requirements today. And so PJs must convert all 2012 homebuyer units that have not been sold to an eligible buyer within six months of project completion to HOME rentals or to repay the HOME investment.

It starts out right in the first page of the notice or at least the first substantive page of the notice after you get past the cover page. The notice goes on to parse and unpack that language for us. And today I think we are fortunate that to some degree there are fewer moving parts to this specific requirement than we have to deal with with some of the other requirements that Ginny talked about that are talked about in other webinars in this

series. Perhaps the most confusing issue really is defining project completion. And it is only confusing because we know that the HOME rule already defines that same term, project completion, in section 92.2. So the confusion just comes form having two different meanings to the same phrase. Otherwise the notice gives us a really straightforward definition.

What we are talking about here is the completion of construction or of rehab. That the work is done, the house is ready to be lived in. typically that will be measured by either a certificate of occupancy or in cases where your local building code process does not result in a certificate of occupancy or a C of O, particularly these would be acquisition rehab type projects, some other local certification. In most cases in an acquisition rehab situation that is likely to be the PJ staff's final inspection of the unit determining that it meets your local program's written standards and is otherwise ready for occupancy. So project completion for purposes of this statutory requirement really is construction completion, ready for occupancy.

Another thing to point out is that HUD has defined the sale to mean that we have a ratified sales contract. To put that a different way for those of us including myself who are not lawyers, you can count the houses sold for these purposes as long as there is a fully executed and enforceable purchase agreement. It is OK that it takes a little while longer in many cases to actually get to the closing table where the money changes hands and title to the property gets formally transferred. And finally I think there is one other really important issue to note here. And Ginny sort of previewed this already for us. HUD has no waiver authority on this point. They can not administratively give you seven months, for example, because you are really, really close. And this might come as a surprise to some people because if you have read the notice you probably noticed that in the four year project completion deadline, not the topic of today's conversation, HUD does specifically have the ability to grant a one year extension. So while we are not getting into the other aspects of the appropriations requirements here today because of time considerations and to keep the focus on the six month sales deadline, I think it is important for everybody to realize that this six month sales deadline has no waiver authority. It can not be extended. It is essentially carved in stone.

So from there where are we headed for the next hour and a half or two hours? Again we are going to start by talking about program design. We have got two big areas we want to talk about: how do we limit the chances of having to convert a project to rental? And then we are going to take – talk about how to convert when our best efforts were not quite enough. So in addition to talking about overall program design choices the PJs need to be making we will talk about considerations for how to select specific projects and we will give you a framework for how you might think through, track, and adjust the overall sales effort in concert with your development partner.

We will also talk about some fallback strategies that might help you sell units depending on what problem you actually diagnose in your local market in terms of the barriers to affordable housing. Specifically we will be talking a little bit about lease/purchase and using HOME as direct financing for buyers.

From there Monte is going to talk about the conversion to rental. We will highlight some of the key business and regulatory differences you need to take into account when converting a project. And we will also talk about some strategies that might help you exit from the rental business later or at least find the resource needed to support these converted rental units over to the full compliance period. So with that brief preview of where we are headed we are going to move it for a moment to questions and answers and before we do that I would like to remind everybody of a few things: first some of the handouts that you might find useful to you are available for download today. In the very upper right corner of your screen there should be a little button that looks kind of like three sheets of notebook paper. If you open that a dialogue box opens up and allows you download various resources. And so many of you are at computers and can download those and print those live while we are talking.

Additionally if you have got a question please consider using the type-in box. Click on the Q & A at the top of your screen. A dropdown menu will pop down and you will have the opportunity to type that question in. And if you would like to ask your question verbally which we will go to verbal questions over the phone after we have handled some of the written ones. Push star one on your phone now and you will be added to the queue and we will take those questions in the order they come in. if we happen to answer your question because somebody asked it and you would like to drop out of that queue you can push pound one. So with that what I am going to do is go to Ginny and see if we have got any questions to be handled right now.

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Steve Lathom: With that what I would like to do is go back into the material and start to talk about program design. So we are actually almost starting before the beginning in this case. There is a lot you can do to minimize the risk of converting to rental or repaying the HOME funds as we plan our projects.

Long before you commit to a specific project there are decisions you need to make in terms of your local program design and the projects that you will select. As those of you that listened to last Thursday's webinar recall, keep in mind there are additional requirements in the fiscal year 2012 HOME appropriations law that explicitly require

the PJ to assessed the market, evaluated the developer's capacity, and underwritten a project prior to entering into a written agreement. Part of this really starts with a key question long before that. That is should you be funding the development of for sale units at all? Does your market really need additional units or are there better ways to serve the needs of low income buyers?

If you do not fund development, and again, we are talking about both new construction or acquisition rehab, then you will not end up in a situation with units that can not be sold within the six months. And to be very clear this is not a suggestion that you should stop providing assistance to low income homebuyers. There are a lot of income eligible households who can and want to be successful homeowners. And HOME can be a very valuable resource in serving their needs. But in many parts of the country there is still an oversupply of for sale housing on the market with values down and inventories up. We have all heard that it is a buyer's market. And in those situations it is often possible to help buyers purchase existing homes that are otherwise for sale without going through the challenges and the risks associated with development.

Of course there are still neighborhoods where demand is strong and units are in short supply and the decision you make in this regard needs to be based on a solid understanding of your local conditions. When you take a step back, that is what the consolidated planning process was really about, making strategic choices about how to meet local needs in the face of markets that are dynamic. Look carefully at your recent experience with home, with CDBG, with NSP. If you have had homes that are selling slowly, if you have a lot of supply coming on the market from NSP funded units, it may be that homes should be directed to other local housing needs or at least that you assist homebuyers through more of a DPA style program rather than funding the development of more units. So that is a strategic decision needed to be made very early in the process before we even get to talking about specific projects.

When you decide that you do need to add additional units to the local supply it is important, again, that we pay attention to those other requirements coming out of the fiscal year HOME appropriations law. Not just because we have to but because it will reduce your risk as a PJ. So make sure that you structure your projects around market and marketability, that you select strong partners both in this case with the capacity for selling the units and in many cases now you need to think about their capacity to manage the rental conversion. And leave room to maneuver in your project underwriting. Make sure that you do not cut things so close to the bone that if something changes suddenly you have got a real problem with your project.

In that general context we need to think further about sorts of requirements you want to apply to the projects that you will fund. Focusing on projects that are pre-sold where a buyer is identified prior to starting construction is going to be safer than relying simply on the existence of a ready pool of willing and hopefully able buyers. On the other hand both of those are safe than building units on spec hoping that if you build it they will come. On that point in particular we strongly recommend that you limit the number of spec homes that you will allow at any given time. For example, you might let a developer build the first three homes in a project even if only two buyers have been identified and the third house being something of a spec build or almost a model home. But in that case you might not allow additional construction starts without additional pre-sales.

Whether you allow this and how many units you will allow will be informed by your assessment of the local market and the level of risk that your PJ is willing to take on. As we have previously discussed in the prior webinars, it is important to be aware of other products in the pipeline. This might include NST units that are underway and will be coming online over the next year or so. And we have got to remember that there – that we still compete with other market properties including that shadow inventory of foreclosed homes that have not yet been released for sale by the banks or those homes that still have not gone into foreclosure but are likely to. As those units are released to the market many will compete directly with the HOME funded units that we are otherwise considering funding.

I want to pause here for a second and make clear that these perspectives are not just about managing risk. To a large degree it is also about directing HOME to the most pressing housing needs in our communities. Back to that big picture of the consolidated planning process. When we are building homes where the market is more speculative and less demonstrated we are also investing in a need that is sort of by definition less pressing. There are a lot of things PJs can do with HOME where the demand for the resource is much more obvious. So when we talk about whether or not you should be building units at all it is not just an arbitrary notion. We need to be thinking about other needs that are not getting served when we tie up limited resources and projects that are not moving.

When you are building units you also need to think more carefully about what your local goals are. And in some ways this is a major reevaluation for a lot of us on the call. Home at its core is a production program. It was intended to help address the need for more affordable housing. And while many PJs have successfully used HOME funds to do this and also revitalized neighborhoods, some of the places we have seen the biggest problem in projects that got built and did not get sold where those where PJs and their development partners focused

more on the revitalization aspect of a project than they did on producing housing where there was a clear market demand.

In the current environment we may need to come to grips with the idea that HOME is not always the right tool for addressing the very real need of community revitalization. And that is not meant in any way to minimize that there is a big need there. Another issue that you need to think about in terms of site selection is whether conversion to rental will even be possible. If you fund a project in a neighborhood where local zoning does not allow rental units or where the restrictions in the homeowners associations legally prevent rental you may inadvertently paint yourself into a corner where the only option after six months will be to repay simply because you can not convert the project to rental under the legal restrictions in place.

When you do fund development projects you are going to need to consider the implications of the six month deadline on other aspects of the transaction. First and foremost it is going to affect the written agreement. You should build performance benchmarks and decision points into your written agreements that allow you to measure whether there has been adequate progress and when to allow or when to require changes in the strategy the developer is pursuing. As we will talk about later this is not a Showtime Rotisserie Barbecue: you can not set it and forget it. PJs need to better track and actively manage their homebuyer projects to avoid problems with the six month deadline. You may also want to work with your attorneys to build in additional enforcement mechanisms that allow you to bring in a new developer, require a change to the real estate agent, or otherwise bring new personnel to bear on a project that is not progressing. These types of provisions are common in multi-family projects but this requirement; the six month requirement may bring that sort of mechanism into the homebuyer development arena, too.

And you will need to at least anticipate the requirement for conversion after six months if not fully structure the way that you will apply both HOME requirements like rent limits and lease provisions but also local program choices like how you will manage the program rule, what level of reserves you will require to be set aside, who needs to manage the project, and the like. Monte will talk more about these considerations later but the point is you need to almost have a split personality when approaching homeownership development, structuring the best project you can on the front end but also planning for a conversion to rental on the back end even though those are two very different kinds of thought processes.

You also need to rethink how you define and set up the project in IDIS and in many cases there is not really anything new here per se but I think it bears reminding everybody about the definition in the HOME rule for a

project. At 92.2 we talk about a project involving one or more units under common ownership management and financing undertaken as a single undertaking. And in some cases what we have seen as we have helped address different issues out there with prior projects that have been unsold is we see cases where folks are actually setting up each individual address as a single activity when really it should be done as a multi-address activity because it is a single subdivision being done all at once by the same developer under the same written agreement.

On the other hand we have also seen cases where people are setting up several projects, a multi-address project, as a single activity when in fact you really have distinct separate projects taking place at separate times, they may have the same developer and to some degree the same project management. Each financing scheme is separate, they are done with separate loans, and in many cases they even have separate construction loans from different lenders. So pay attention to that because later as we talk about how you unwind and convert a project in IDIS and the implications for conversion to rental, those decisions and how you structure the project has implications later.

Finally the way we project – the way we finance projects needs to be reconsidered. Converting a unit to rental when your construction loan was specifically to build a for-sale unit is often an event of default with the primary construction lender. And even if it is not that loan may not be sustainable based on the net operating income that can actually be generated by renting the unit. So a transaction with substantial leverage may also be harder to do not only as a rental but as a lease/purchase for much the same reason. And if you were to consider the direct HOME financing that we will discuss in a few minutes it is also harder to do that when there is a senior construction loan.

Of course the tradeoff is that you are investing more HOME and fewer units and reducing the level of production. And in some cases you have got more project cost in place than the maximum subsidy allows you to invest or you may have specific line item costs within the overall total for the development cost that are not HOME eligible. For example, using HOME funds to build a detached garage. So you need to think through those transaction structure points. In some ways we are about to get ahead of ourselves. Since assessing the overall project plan, and for purposes of today's discussion the marketing and sales plan, is still part of your project selection and funding decision but I want to start to talk about a framework we can use to both assess the projects in the first place and also help guide ourselves during implementation when we have to make adjustments if things do not go exactly according to plan. So the marketing plan, and those of you that were on the webinar last Thursday probably

remember we suggested that you make the developer submit a marketing or a sales and marketing plan as a part of their application, starts to tie everything together.

The general market analysis you do as part of the consolidated planning process helps identify opportunities and challenges. The project specific market assessment that you do under the fiscal year 2012 HOME appropriations law requirements for underwriting help indicate whether or not this project is likely to succeed. The marketing plan identifies how the developer will actually reach out to the target audience and put that market opportunity together with the project they are actually building or the demand for those units. How are they going to sell the units based on their competitive advantage and how they reach out to folks. In this way it is part of your initial assessment of the developer's capacity helping to demonstrate they have thought through the project and they understand how it fits into the local market and how they are going to reach the other buyers. And it also provides a starting point for building a series of benchmarks and decision points to help you and the developer know if you are on track which also allows you to hold the developer accountable in the event things are not working.

It helps you think about in advance how you can adjust over time to get houses sold before you reach that six month point where you have to make the decision to convert or repay. In a more visual context the marketing plan is intended to articulate the vision to make sure the developer, the PJ, and other partners are on the same page about what we are doing to get homes sold. It lays out the roadmap the developer will follow and provides mile markers we can use to assess whether or not things are working. And when things are not working when we are not getting to our destination fast enough we have to adjust our strategy and work our way back through the cycle. So to assess that marketing plan and the project concept as a whole we are going to suggest that you look at it from several admittedly interrelated perspectives or big questions.

Are you building, or as a PJ funding, the right project, the right product? Are you selling for the right price? Beyond just the sales price, is the overall deal including the amount and the structure of any direct buyer assistance attractive and competitive? Is the developer's outreach plan effective and the potential buyers have access to credit? Because when it comes down to it sales will only happen when someone wants the house we have built or rehabbed at the offered price. In HOME this will typically require we help the buyer on terms that are both fair and attractive and none of this will happen unless we get the word out. Nor does any of it happen if the buyer can not get the financing they need to buy the house.

So let us talk about the product. As you plan your projects it is as much of a cliché as anything but we all know about the importance of location to real estate. And as we mentioned earlier, in some cases we need to reexamine how we are using HOME in this regard. The bottom line is the location of the houses we fund needs to be an asset to their sale, something that helps sell to our target market not something that needs to be explained away. And it is important we build homes that meet market expectations. While HOME is about modest housing, modest does not mean cheap and it does not need to mean bare bones. Think about curb appeal, how the house fits into the surrounding neighborhood. While it is not a new concept anymore, the idea that we can and often should invest a little more on the front end to achieve long term savings and energy usage and maintenance still bears repeating.

Not only are consumers more focused on these issues but those types of design choices and investments do make the housing more affordable over time. We can also learn from the private market in this regard. Homebuilders build to suit for a reason because buyers like to customize aspects of their home. Some buyers, some HOME funded developers have been pretty successful by letting prospective buyer choose things like siding or shingle colors, carpet and paint or cabinets and plumbing fixtures. Obviously this is only possible when a buyer is identified prior to starting or finishing construction and in some cases you might even hold off putting in applianced or doing that final interior coat of paint, having a small custom option can be a marketing feature as you are trying to sell that house. In other places, of course, we see people hold off putting the appliances in simply because of the security issues and that is perfectly appropriate.

In the same way you might want to consider things like a bonus room that can be finished by the buyer later, an egress window in the basement or on some lots even a walk-out basement so that additional living space can be added later even if you are not going to add that fourth bedroom now, we are not suggesting that you need to do that, the fact the buyer has that option if their family grows or if they want to add a home office or whatever, that opportunity adds value to the product that you are offering. Of course the product needs to be priced and the point that we are talking about here is not just to have the lowest price on the block or reflexively cut the price if sales are moving slowly but to be sure the price reflects the actual market. We are not suggesting that you sell homes for less than they are worth, that has both regulatory implications often effectively requiring the use of the resell provisions and it has practical concerns for our neighborhood markets adding one more comparable sale to the sometimes downward spiral of values in distressed neighborhood is not something that we want to be doing.

But the reality may be that homes might be worth less than we would hope in the neighborhoods we are building in or that between underwriting, construction start, and construction completion the market has declined around this. So we need to pay attention about whether or not our pricing is appropriate, reflects the market, and is at a point that will generate interest. You also need to reassess your assumptions about how much mortgage potential buyers can afford. Do we need to provide more HOME assistance in the form of buyer assistance to expand the range of buyers than maybe we have been offering in the past? Remember from the webinar last Thursday that you are still required to size the amount of assistance you provide in the certification you will sign in IDIS, it says that you are providing assistance based on the need and what is appropriate and reasonable for the buyer.

So we are not talking about flat or minimum down payment assistance to everybody. But PJs need to reconsider their guidelines particularly in terms of how much you will offer and how far down you might buy buyer front end housing ratios. Given the lessons from the mortgage meltdown we realize that maxxing out our buyers, particularly our low income buyers, can be problematic and maybe we need to account for lower front end rations than we have had in the past. Finally it is important to note and consider whether the terms of the deal that you are offering are attractive enough to encourage buyers many of whom may be reluctant to buy or are concerned about their ability to succeed. Many of you are going through your consolidated or your annual action plan process right now. This is a good time to also reevaluate how you are structuring your homebuyer assistance.

Are you using recapture or resale? In some cases recapture may be easier to explain to people and more attractive than a resale provision. And again you should base this not only on what is marketable but how your market operates. You may want to consider offering deferred homebuyer assistance if you have otherwise been providing amortizing homebuyer assistance. Or you might have some amount of forgiveness rather than having loans that are fully repaid. Again, the point here is to think about what the deal terms need to be to make the deal attractive to help spur the sale knowing that the context in which our buyers make these decisions is different than it was a few years ago.

In terms of marketing we can build the best house in the world, price it right, and have a great deal. Or as one of my friends like to say, offer a killer house at a killer price but if no one knows about it it is not going to sell. And more importantly, if HOME eligible buyers, those folks whose incomes are below 80% but high enough to qualify for the needed mortgage do not hear about it and do not respond these homes are not going to sell. So like in all things it is important the developers are picking the right partners and here it is about the real estate agent and

whoever else is helping to market the home. It is important to work with folks who have a track record of working with low income buyers. Not, for example, using a well-meaning realtor who really wants to be helpful to a local non-profit but is otherwise known in the community for selling high end homes. You have a mismatch between who is out there reaching out to the buyers and who the buyers are used to going to. So the point is you need partners who are familiar with and familiar to your target market.

Outside of that we all know that neighborhoods are often driven by other key stakeholders whether that is a significant employer, a school, a church, a neighborhood organization, where can a developer find groups of potential buyers who are already in the neighborhood in one way or another who may spend a substantial part of their day nearby and appreciate the value of a shorter commute or who otherwise have an affinity for this location. In many ways what we are talking about is not rocket science but it is important that we force the developers we fund to think through the details, identify how they are going to get the word out, and tell us what they are planning to do. Not only might you have additional insights that they have missed or know partnerships that they should establish as we will discuss more later but it helps to build a framework or a funnel of interim benchmarks like the number of showings, the number of folks referred to counseling, the number of applications submitted that lead to that final measure of success, the actual sale.

In addition to paid media and other advertising do not ignore the value of free media. As buyers are identified and as they close you have got the opportunity to do things like ribbon cuttings, having the press there as you help them move into the house or those other feel good stories that our local newspapers or our local TV stations often like to run. Those can make a great counter story to all the stuff we continue to hear, unfortunately, about foreclosures and how difficult things can be. Finally developers should be looking to other local programs that also identify potential HOME eligible buyers. That could be the homeownership counseling program run by another agency. Some people have even offered to hose those homeownership classes from other agencies in the living room of a home that they are building that is under construction or nearing completion so you have those buyers learning about the process while they are sitting in a house that they could buy.

You could look to your local PHA section eight for homeownership program or family self-sufficiency program. And even we know that most of our local Habitat chapters have more applicants each year than they have capacity to build houses. And so some of those unserved Habitat buyers may well be folks that in fact can afford to buy the houses that we are building. So we need to look through all of those different things.

As we start to talk about access to credit we are going to encourage you to be clear on how buyer are going to get their first mortgage. Does the developer have relationships with lenders, with specific loan officers even who are willing and able to work with your local program? Did those lenders understand the terms of the HOME assistance being provided to buyers? Do they have a track record working with low income buyers and do their mortgage products fit your expectations? We are not talking about doing some sort of inappropriate steering of buyers to specific lenders. Buyers can still choose who they would like to take their loan from but making sure that you have lending partners that are actually ready to work with your program and that buyers are not left totally and entirely to their own devices searching around for a mortgage. In some cases, though, what we find is that the potential buyers are there, they want the house but they can not find banks willing to work with them or that are actively lending in the neighborhood. When this is the issue the barrier to selling the house is buyers' access to credit you have two program design options you can consider: direct financing and lease/purchase. We will approach those in order. But in both cases these options are best addressed from the beginning of your project planning not as a backup strategy four months after construction completion. These both require a lot of additional work, a lot of oversight on your part and the part of your developer and a tremendous amount of ongoing interaction with buyers and different skillsets than we see in a typical build it and sell it type of situation. So in other words these are legitimate options but neither one is a silver bullet.

As we talk about direct financing in essence what we are saying is you consider converting your HOME investment from a construction loan to the developer into an amortizing first mortgage to the buyer. You become the first mortgage lender using those HOME funds. If you have ready, willing, and able buyers who should be credit worthy but for some reason can not obtain financing you can consider providing it yourself. A big caution here is that you are stepping into the lender's role. To some degree you are taking on the notion that you know better than the bank about which buyers to extend credit to. And you need to carefully consider state law implications for origination servicing as well as the federal requirements. There are exemptions to the safe acts that allow states not to require licenses of individuals employed by state or local governments or bona fide non-profits. But depending on how your state implemented new laws and regulations consistent with the safe act there still may be requirements imposed by your state licensing authority. So it is important that you understand local context.

If you are pursuing such a strategy you need to ensure the capacity for underwriting and servicing including dealing with collections and foreclosures. You need to determine who is going to hold the mortgage, the PJ or the developer or the CHDO. In most cases you would not let a for profit developer do this and how those loans will be structured. We would suggest that you have very clear and if anything overly fair lending terms: no origination

fees, low fixed rates of interest, et cetera. If you are interested in pursuing this type of option it is a new role for you. It is a new role for you, it is a new role for some of your developers, and we would encourage you to search out other opportunities and partners that might have some good experience there. For example, if you have a local neighbor works affiliate they often manage loan pools and you can use their experience at least to understand how well this works in your community. Also many of the local Habitat chapters of course originate and service their own loans. So there can be some market intelligence there and some systems of capacity that can be helpful.

Another form of providing access to credit instead of just direct financing, of course, is lease/purchase. Lease/purchase under the HOME program is a homebuyer activity. But it is also a hybrid rental in the mean time. What I mean by that is that for HOME purposes you are going to report this as a homebuyer unit. There is actually a place in IDIS where you can enter the date that the lease/purchase agreement itself was signed. And I think one thing to note here for folks is that as long as you have entered into that lease/purchase agreement within the six month deadline then you are going to have satisfied the requirement here. We will probably cover that more during the Q & A.

But even while it is home/homebuyer, from a local law standpoint you are still going to be a landlord. You are still collecting rent. You still may be subject to other requirements if you have to license the rental and those sorts of things. So you need to be careful about that. The point is that backing into this model is something of a recipe for trouble. You need to approach this as a business model on the front end and if you really think that access to credit is the key barrier and there is otherwise healthy demand for – you built a good house at a fair price and people know about the opportunity lease/purchase might be an option. But your chances of success are best if you design this into the project from day one. You need to identify buyers who are near credit worthy or who are on the cusp and can transition to ownership within that 36 months. And you need to make sure you provide a lot of support to help the household make that transition to ownership. In many ways you are almost talking about a case management level of ongoing counseling and support to the buyers.

And so given the skills to do this and to do it well we really need to ask whether or not the developer seeking the funds has those skills. Have they thought through who will own the property during the lease period? Who is going to provide the property management? Who is going to provide the case management to support the buyers? All of those things, it really needs to be thought through from the beginning.

So we have laid out our vision. We have used big picture questions about product, pricing, the deal, effective marketing, and access to credit. So developers are going to go out and do what they do and start to develop but remember the next stop on our overall cycle. We need to track progress. And by the way, remember, HUD is tracking our progress now, too, because Congress is tracking theirs. It is not my job to comment on who gets to track Congress. But in any event IDIS as we hard in the initial Q & A can not specifically track this requirement. It can only track it approximately by proxy. IDIS does not record the date of construction completion. PJs are responsible under the notice for establishing a local procedure for determining, documenting, recording, and tracking that date so we know when the six month clock runs out. There are some new IDIS reports that will be posted monthly and you have got the link here on your screen to be able to go to the IDIS reports area that will help you identify projects that are likely to be headed towards that six month deadline.

Those will include any homebuyer project that is in final draw. If you have drawn all of the money, remember, under the current regulation you are on a 120 day clock to report the IDIS completion. It will also show you any projects that are, homebuyer projects, of course, that are 90 percent or more drawn and have not had any activity for six months. Of course these reports will have some false positives. Many of the projects identified are likely to be those that have finished construction and may be just sitting on the market. So while IDIS helps you identify the likely suspects your local systems really need to cover this in more detail and they need to cover it a lot earlier. If you do not start paying attention to a project until it hits the IDIS screen you are going to be too late and either converting your projects to rental or repaying your HOME account.

So again, start the marketing process early, even before construction starts. And while HUD is not requiring you to do this, per se, we would strongly suggest that you require the developer to start providing monthly reporting on their marketing activity no later than when the HOME is determined to be complete. Again, that is construction, completion, ready for occupancy at which point the six month clock starts. And you need to establish more formal sit down discussions of progress and actions being taken to achieve sales. Perhaps, say, at 60, 90, and 120 days past construction completion. Each PJ will determine your local process in terms of what makes sense for you. But the key point is to start early in this, start the sales and marketing process as early as possible remember pre-sales would be very nice to have. Require periodic reporting and you increase the level of reporting and your involvement in managing and adjusting the strategy as you get closer to that deadline.

In terms of adjusting the strategy we really go back to the same perspectives we just discussed. Think methodically through what adjustments you can make in terms of product, for example. Will a minor upgrade, perhaps offering a stainless steel appliance package instead of the appliance package you were otherwise going

to put in the house make a difference? Is your pricing still reflective of the market? Are we missing out on interest due to the level of down payment assistance available? And if we had just a little bit more down payment assistance could we reach a lower income scale to where our buyers or potential buyers actually are? Has our marketing been effective or what can we do more? In terms of access to credit, again, we would suggest you plan these options early but perhaps if you are not getting movement it is time to think about offering a HOME first mortgage.

We are not suggesting you have to intervene along all of these five criteria simultaneously but the idea is to use the framework as both an analytic tool and when you have identified a feature that is standing in the way of making a sale we hope this framework can help you make the right changes to actually move things along. So with that we are going to move into questions and answers. I will turn it over to HUD in just a moment but again to remind everybody, if you have a question you can push star one on the phone to get into the verbal queue and before that we will handle the written questions. At the top of your screen, again, there is a little menu that says Q & A, drop that down, you will have an opportunity to type your question into a box and we will be able to get to as many of those as possible. I think I mentioned this earlier and I will mention it again: we do know there will be more questions than we have time to get to today and as a result one of the things that HUD is planning to do is to release a document later of frequently asked questions. We will build that document based on the questions that are coming in that we do not get to, the questions that we get in several times over and we will use that an opportunity to provide with additional written guidance that further clarifies some of the specific on the ground situations that are coming up.

So with that what I am going to do is go back to HUD and Ginny, do we have a question you would like us to answer?

> ***This transcript does not include the Q&A portions of the webinar. HUD will be posting additional written guidance in the form of Frequently Asked Questions (FAQs) that address both questions addressed in this webinar and others that were not addressed due to time limitations. Those will be posted to the www.hometa.info website as they become available.***

Steve Lathom: Great. Well, again everybody, keep those questions coming either over the phones or through the Q & A. We will be posting that FAQ document later. And so with that what I would like to do is turn the presentation over to Monte to talk to us about making rental work. Monte.

Monte Franke: Thanks, Steve. Hi everybody. I see a lot of familiar names out there again. Belated Happy Father's Day to those of you who are fathers. I also see a few names of people I know their kids are graduating this month and congratulations on that. I am trying to think of everything I can think of to say that is pleasant because the topic I have got is not that pleasant of one. But it is something we inevitably have to deal with. If you have exhausted the time that is allowed by the appropriations act to sell then you are required to convert to a rental as you have heard. It is a statutory requirement not necessarily something you or I might choose to do absent this requirement but neither you nor HUD has discretion in this matter given the appropriations language.

So as we begin to talk about rental conversion I am going to be focusing on some of the things you need to think through. There are a number of pitfalls and challenges along the way. It is not an optimal kind of design but a necessary one. But we do believe that it is an important one for you to consider. The homes we are talking about, sitting there vacant are not helping anyone. They are not providing housing to people that need it. The vacant homes do not contribute to the neighborhood in a positive way. And they are in fact a liability to the owners, the developer/owner at this point rather than an asset. So something needs to be done and Congress has given a six month deadline.

As has already been mentioned by Ginny, in addition to converting to rental you always have the option to repay the HOME investment and I will leave the comments there, what she has already said to you if you want to explore that as an option talk to your HUD staff about it. But I am assuming that most of you would like to consider the alternative of operating this as rental. Even before the 2012 appropriations act was passed and this language came to affect us HUD was already asking PJs to deal with unsold inventory out there and to make this choice because there were requirements already in our program for you to complete the projects and you know the metric in our program are completed and occupied units. So these unsold units were not helping our program or helping people there.

The 2012 language gives us a firm deadline to actually take this action but we were already focusing on this issue before this came along. Converting the units to rental is not just a matter of changing the setup of the project in IDIS. That is in fact the easiest part of the challenge. There is a HOME facts, volume four, number one, that was issued in January and it is also available as one of your downloads in this webinar that tells you exactly how to go about doing that and Peter has already answered a few questions when you have a got a mixed project where some units have sold and some have not. But the instructions should be there and you should be able to get the guidance you need to make the IDIS changes. But in my mind they are one of the more straightforward aspects of this conversion. The bigger challenge is to restructure the deal as a rental project.

It now must meet all the HOME rental rules including [inaudible] occupancy requirements, rent limits, lease requirements, ongoing property standards, and an affordability period. But it is not really just about the rules. You do have to meet these rules but you now have a project that has to be operated successfully as a rental. This is a different skillset from a homebuyer/developer project. The owner needs to have certain capacity and we also need to be able to manage the project. In fact, in some cases you may have to consider a different owner or manager. That was part of the issue that came up in this very last question about the co-op. And if any of those changes need to occur it is likely to require some very testy negotiations between the PJ and the developer, the lenders, and other partners in the deal. Not to mention concerns by the abutters who will probably not like the idea of a for sale unit becoming a rental.

Bottom line: the HOME rules and IDIS are only a part of the challenges that you face. I will cover the HOME rules that pertain to you in this segment but I am also going to be talking about the practical matters of doing a conversion to rental when you had not planned to do so. What I would like to do is I would like to take this in five different questions and the rest of my presentation will be structured around: who needs to be involved, what do we need in an owner and manager, who do you seek to serve now that it is going to be a rental, how much will the pay (that is the rent and revenue question but also the marketing question), what will it cost to operate as a rental (you now have to consider operating budgets and covering those operating costs), where is the money going to come from (we are no longer selling the units so we now need to look at other permanent financing arrangements), and how will the performance requirements change over time/what are going to be the compliance issues that you are going to face? If you are going to have to convert you are going to have to move quickly to answer all of these questions while dealing with the regulatory and IDIS changes that you need to make.

Let us talk first about the question that I posed: who needs to be involved, the ownership and management. From a PJ perspective you have to decide who is going to be the property owner and who is going to be the manager. The developer you approved when it was a homebuyer project may not be capable of operating the deal as a rental. You need to honestly assess whether this is really within the capacity of the existing developer including the ability to manage. Not only is rental a whole different ball game than for sale housing in terms of operations but to be honest if we are at this point considering the option the developer has not produced a completed and sold unit and presumably in default for their written agreement with you and possibly any other liens or funding sources that exist for that project. You believe that they can perform with even the more

challenging operation as a rental and the question also comes up do they have the capacity to manage the property?

So the negotiations are likely to get very uncomfortable because you may be discussing whether or not the developer needs to be replaced or others need to be brought in. Sometimes the developer is willing to exit. Other times they are not because it may mean leaving behind their fee and a lot of other vested money that they have in the deal that they would not be able to get out if the project has to be turned over to somebody else. If you are looking for other owners to operate the housing a rental you have got – you certainly want to consider entities that have some experience with affordable rentals such as housing authorities and non-profits. The thing to keep in mind is that this – under most circumstances we are talking about what would likely be a scattered site rental project or a small rental project. In some cases there may be co-op and condo type projects that have more units than this but even in those projects may be partially sold and partially unsold. So it is going to be a very challenging thing and not all rental housing operators want to deal with scattered site rentals.

I also want to remind you that if this was a project that was funded out of the CHDO set aside then for it to remain a CHDO project it would have to continue to meet the requirements of a CHDO being the developer/owner/sponsor, I do want to remind you the definition of CHDO sponsor currently permits a CHDO to turnkey a project to another non-profit who agrees to step into their shoes and operate the project meeting all the HOME rules and that under such a sponsorship option it can retain the CHDO status. So I will mention that again later but just keep in that mind. If these are CHDO dollars that you may want to preserve that character otherwise it may no longer be qualified as a CHDO project.

The second question rant to who is going to live there now and what kind of rent can they pay and how do you have to market the project? Obviously the first thing when you switch to rental is that you have now invoked the HOME rental occupancy requirements including both what we have called the program project rules. As you may recall if you have attended any of the HOME trainings when we talk about the program rule we refer to the fact that 90 percent of the units that you assist, rental or TBRA units that you assist in any program year must initially be occupied by tenants at or below 60 percent of their median income. The project rule, on the other hand, applies to five or more HOME assisted units in a project. And that would trigger at least 20 percent of the assisted units being low HOME rent units reserved for tenants at or below 50 percent of AMI, what we call very low income.

The 90 percent rule: if you have to convert these to rental you would want to add these units into the other rental units you have produced to make sure you are meeting that requirement for the 2012 year. And if you have a scattered site project of five or more assisted units you are also going to have to meet this LI or low HOME set aside that I mentioned under the project rule. You are now also going to have to meet the HOME rent limits. The HOME rent limits come into play with both the high HOME rent and possibly the low HOME rent units if you trigger the project rule and that those rent limits apply to your homes based on bedroom size and also the utility – the tenant paid utility allowance calculation. Just because you have created single family units, for example, and they are larger on a square footage basis than say a multi-family building might have you are still subject to the same two, three, four bedroom limits that all rentals are subject to. You might find that is challenging to you to make certain that you get enough revenue to cover all the costs. But the same rent limits apply based on bedroom size.

We have talked a lot in various underwriting classes and training around the country on HOME but the HOME rent limits will apply for your affordability period. Those rent limits are based on certain calculations mandated by the statute and the regulations. They do not guarantee that the rent limits will go up each year. So if you set the rent limits at the maximum and you allow those – and you sign that next year your HOME rent limits do not go up it would be hard for the owner/operator to increase rent and be able to cover increased operating costs. So standard underwriting recommendation is to set rents below those regulatory limits and also to keep them in line with the market so that you are not trying to rent those units for more than the market will bear. I am sure this will come up again on our next webinar when we get into rental underwriting but I wanted to remind you that it is not always wise to assume that you should go immediately to the maximum rents permissible.

The final thing that I want to mention here, if we are talking about now tenants rather than homebuyers, households at or below 60 percent AMI rather than up to 80 AMI we might be talking about a very, very different marketing base than had been the focus of the original marketing efforts. So it really would be important to do a tenant selection and marketing plan that quickly focuses on who it is you want to serve. Also comment that you want to keep in mind not every renter household is suited for scattered site single family homes. There may be, for example, some elderly, special needs populations, other households of extremely limited means that may not have the capacity to maintain a single family property. Think about lawn mowing, snow removal, other things that you might be asking the tenants to take care of or you would have to provide for yourself or through the owner. And so they may be better served by traditional apartment projects.

Obviously there are a lot of fair housing issues in this as well. And if we have got five or more units you have got affirmative marketing that come into play but it is important that you think through who would be the likely occupants and change the marketing strategy to target those and to do it quickly because you are carrying a project that has no income. Let us go to the operating cost site of the budget now having just talked about rents and rental revenue. I guess the thing that I want to say first and foremost is that these are going to be expensive on a per unit basis to operate. You are going to need to budget an operating budget that is going to have to consider taxes which might in a single family or a scattered site setting be higher on a per unit basis than in a multi-family. Insurance costs will be higher, maintenance costs will be higher, and utilities are likely to be higher because of potentially larger unit sizes. Another thing to consider is that when you have scattered site projects you may have a whole bunch of different kinds of improvements that need to be maintained and you also need to think about your contributions to reserves.

The comment that I have got on the slide there about the diseconomy of small scale. In the rental business we tend to think about having enough units clustered together, like similar units that can be managed and operated efficiently to spread those costs of management across a number of units. If the projects are not only smaller but they are likely to be scattered site or spread out the increased cost and distance of traveling to those sites, overseeing them, maintaining them, having contact with the tenants there are all an important concern. In addition you are likely to have units that are not uniform. Some of them may have different appliance packages and other kinds of things where you end up with maintaining a greater set of replacement appliance and materials than you would in a more uniform multi-family building. All these things are important for you to consider when you try to budget for the cost of operations. It has been the experience of most people that smaller and scattered site rental projects are higher cost on a per unit basis for operating costs.

Then we come to the financing. We are assuming that you had originally counted on having the property sold at the end of the development period. So the permanent financing was built around a permanent first mortgage for the buyer, their down payment, and possibly your HOME gap assistance. All of a sudden that goes away and we are now looking at having to come up with permanent financing for this particular property. In traditional rental permanent financing is based on net operating income. If you are not familiar with this concept you can listen on the next webinar and we will include a session of rental underwriting. But essentially it is the revenue you collected minus the operating expenses which gives you net operating income and it is the net operating income that determines how much you can afford to borrow or finance the project for. And then HOME usually comes in as a gap assistance amount. It could be that you would not have enough rental income because of the high operating costs and low rents that you collect.

To be able to finance it you might also have difficulty financing such a small project with many of the conventional lenders who would not be interested in something so small and not uniform. That may mean you will need to consider more HOME funds in the deal than what you had originally anticipated. When you originally planned it you were thinking about just having the gap money in there for the homebuyer based upon what they could not provide. But you now may have to provide all the financing to the deal. Steve has already mentioned that in terms of the homebuyer side but you may also have to fully finance this deal on the rental side if you are faced with conversion. If you – in terms of the financing if these projects are still open in IDIS and not closed out theoretically you could still increase the HOME funding up to your program limits. As Steve mentioned reminding you the maximum HOME assistance amounts limits exist and go to both what you put in originally as well as what you may be adding now. So please pay attention to those limits and also keep in mind that maybe some of the costs were not HOME eligible when you determine what the total eligible investments could be in those units.

But you could amend the agreement, modify the agreement to include more HOME funding and provide HOME NA through first and second mortgage position to cover the bulk of the cost here. Even if you do end up finding that HOME funds help you may find that the total costs exceed what the HOME program can provide because of the 221(d)3 limits. And you may want to consider other things. Some of these projects are CHDO projects where there have been CHDO proceeds from the units that have been sold and perhaps they can be redirected into the financing of this unit until a later date when the CHDO can sell.

Given the challenges of smaller projects few markets have high enough HOME rents and market rents to support a project for a full 15 or 20 year compliance period. You really need to look carefully at what the project can carry in terms of debt and look at those over the affordability period. You might find that they could carry financing in the near term. Because HOME rent limits do not go up over time, you will need to consider whether or not you need to look at exit strategies that I will get to in just a few minutes. Long term compliance: I would like to remind you there are a number of other phone compliance issues beyond the occupancy and rent standards that I mentioned earlier. And they will certainly be things you have to consider as you shape the project as rental.

We can not cover all the HOME regulations that are triggered by rentals comprehensively in such a brief webinar but I want to highlight some of the key compliance issues that you need to be aware of and analyze. In many cases converting from homebuyer to rental may change the affordability period. The rental affordability period could end up being longer than you anticipated for the homebuyer project for two reasons: first the rental affordability period is based on the total HOME investment per unit, not just the buyer subsidy portion as you are

permitted to do under a capture. So all of a sudden those HOME expenditures that you were considering as development subsidies under a homebuyer scenario now come back into the calculation of affordability period. Second, if the HOME is newly constructed it has an automatic 20 year affordability period under rental rather than what was likely a five to 15 year schedule that was permitted under homebuyer.

So for two reasons you might have to look at even longer affordability periods on the rental side than you had anticipated when it was a homebuyer project. More importantly you have got to think about the ongoing compliance issues that exist. You are going to need to plan to monitor this project for its affordability period whatever it is in that five to 20 year schedule at a minimum. And you are going to need to provide for an annual occupancy report from the owner as is required of all rentals, owners, and operators, giving an update on occupancy of all the HOME assisted units and the rents charged. You are going to have to make a provision for ongoing income certifications. You are going to have to make provision to get out updated rent limits and utility allowances. And you are going to have to make a plan to visit those projects. Currently we are talking about every one to three years as the monitoring schedule. That might change in the future. But right now it is a one to three year schedule depending upon the size of the project.

You also want to keep in mind that the ongoing compliance issues in a rental include ongoing property standards or physical standards. You are going to be doing inspections of the property over time as you do those site visits. And the owner is required to maintain the property standards that you have designed. Unlike homebuyer where it is just a matter of meeting the property standards at time of sale to the homebuyer this is an ongoing issue for the affordability period. Not only a burden for you, the PJ, owners also need to understand what is coming and be willing to work with the PJ to ensure compliance. Back at the beginning of the section I raised the question is the current developer up to it? Well, are they up to it for the whole affordability period? Are they going to be able to handle everything we have just talked about? And there are a few more things, too.

Beyond these certain – these important HOME regulatory compliance issues there are a few more issues in the administration of this activity that I want to go through with you. The written agreements in the associated legal documents: first as Ginny and Steve have mentioned we have got some deep covenant issues that we have to deal with here. It is no longer just simply a recapture note mortgage as you may have been planning for your recapture project. Instead now we have a deep covenant that obligates the owner to operate it as affordable housing for the affordability period. So those documents will have to be changed. In addition the written agreements will probably require wholesale revisions to reflect the substantially different regulatory issues raised by rental as compared to homebuyer. And as I noted before you are also going to have to probably re set up the

project in IDIS and I mentioned to refer you to the HOME facts volume four, number one that is also loaded as one of your downloads today to help guide you through those issues.

A couple other big picture issues that I wanted to mention: Steve already mentioned this but this notion of what is the project is a very important one for you to consider. When you re set up the project you have go to decide how to set it up as projects whether it is a scattered site project with all the units selected, an individual project if you follow the definition in 92.2 but keep in mind that however you decide to set that project up there are implications for the operation. For example, I already mentioned if you had five or more scattered site units in a single project converting it to rental would trigger not only the rental occupancy but also what we call the project rule, the 20 percent of the units at 50 percent of the AMI with a low HOME rent. There are other issues that will also come up. So be very careful and be very clear that you are following the rules and the guidance and making decisions about what constitutes a project when you reset these units up.

Also I mentioned earlier the CHDO set aside issue. If this is a CHDO set aside you need to consider the implications of changing the project and possibly changing the owner. I have already alerted you to the fact that the CHDO sponsorship definition currently permits the conveyance by the CHDO to another non-profit. But if you do not continue to meet this definition then this project may no longer meet the set aside requirement. One of the handouts that are uploaded for you is called considerations for conversion from homebuyer to rental. It covers in a lot more detail than I could in these few brief minutes what all these issues are and what you need to think about as you plan for a conversion of these units.

Finally I want to talk just a minute or two about recapitalization and exit strategies. I start this by reminding you that the project has to remain financially and physically viable for at least the affordability period. The failure or loss of the project or unit during the affordability period could result in a requirement to repay. You may have thought you avoided the repayment requirement by converting to rental but it could come back to haunt you later on if you did not set up a viable project that can be sustained for that affordability period. It is important to make certain that the project can remain, meet its bills, and be maintained to the standards that we have in this program. We previously mentioned that it is important to consider funding reserves, operating replacement reserves. Typically those are funded from rent but the rental revenue may be low and the operating cost high and it may be difficult to fund those reserves. It is important to consider alternative sources for funding or capitalizing those reserves even when HOME cannot pay for them.

Another important thing to keep in mind is that the project may still be open and allow you to advance HOME funds right now but remember that once you close the project out in IDIS and it has been closed out for more than a year you are into the no double dipping rule for the remainder of the affordability period so you may not have the ability to advance HOME funds later on. If there are improvements that are needed now to ensure its viability then you want to consider them before you close the project out because you will not be able to advance more HOME funds. Maybe you could go for CDBG or other kinds of funds if there are rehab needs during this affordability period.

That leads me to the final point and it has already been mentioned and it has been brought up in some of the questions. That is if we have to convert to rental and we go rental what if we have the opportunity to sell it in the future during the affordability period? I would like to remind you that 92.255 of the rule exists and has existed and it is a provision that says you are able to sell a rental unit to the existing tenant during the affordability period. You are not able to run out a tenant and market it on the open market but if you get a tenant that wants to purchase you are allowed to convert it to rental for the remaining affordability period – from rental to homebuyer for the remainder of the affordability period and structure the deal to make it work for a tenant at that point.

So there have been questions that asked about lease/purchase and things of that nature after conversion. I would direct you to this particular part of the rule to look at to see what those rent to own options might be down the road for you. since so many PJs are concerned about setting up these deals for long term rental when they are difficult financially to maintain over that time period, looking at the options you have to find a tenant who wants to ultimately own and working with them to help them move to an ownership position might be a useful exit strategy to explore or plan for. With that I am going to turn it back over to Steve to do a few wrap up slides and then we will be going to some more questions.

Steve Lathom: Yes, thank you very much, Monte. So again before – we know some of you will start to drop off and as much as we would love to have you stay with us until the bitter end we will acknowledge that. So a couple of housekeeping things: first there are several resources that will be available to you. Many of those are already available to you today. Of the stuff posted we have not yet posted the sales self-assessment tool. We will be posting that to the hometa.info website along with the transcript and the recording of the webinar and those sorts of things. Again, you can download the considerations for conversion. There is an additional resource listing that gives you some other places to go look for documents that particularly help you with the conversion to rental but also thinking about the marketing and also lease/purchase. Home facts volume four, number one is

here and several of the question kind of relate to some of those mechanics so we will probably get into that during the Q & A. And finally, if you have not already seen the CPD notice, that is linked from here as well.

So those are available and again if you have not yet done so you can download several of those from within the Live Meeting client in the upper right corner of the window. There is a little icon that looks like three sheets of notebook paper. You click on that and you can select which of the things you would like to download. You can download most of those attachments that we just referenced as well as a copy of the slides from today's presentation. All of that will be posted to the web later. A couple of other reminders: again, this will all be posted. The website is www.hometa.info and importantly I think we want to mention again the FAQs. If you have something that occurs to you after the fact you can certainly submit that question through the evaluation that we are going to ask you to do at the very end of the webinar here.

And if you have highly specific questions about a project please submit those to your field office. Again, we will be – after the final Q & A we are going to post – through the Live Meeting client you can fill out your survey monkey type evaluation right within the Live Meeting window. So we are going to ask you to do that today. And with that what I am going to do is go back into questions and answers. One more reminder: in order to submit a question electronically click on the Q & A at the top of your screen. When that dialogue box opens you type your question where it says ask a question. And you hit enter and we will see that come up. And if you are going to be wanting to ask your question verbally go ahead and push star one on your phone now to get added to the queue. We will start to build that queue up. But we will start right now going back to HUD to see some of the questions that have come in through the Live Meeting client and address some of those at this point. So Ginny?

> ***This transcript does not include the Q&A portions of the webinar. HUD will be posting additional written guidance in the form of Frequently Asked Questions (FAQs) that address both questions addressed in this webinar and others that were not addressed due to time limitations. Those will be posted to the www.hometa.info website as they become available.***

Steve Lathom: Well, with that, Ginny, is there any last comment that you would like to make from a HUD standpoint?

Ginny Sardone: I just want to acknowledge on HUD's part that we do understand how difficult converting homebuyer units to rental are. There are many, many challenges that PJs are actually required to do this would encounter with respect to whether or not the developer of the units have the capacity to run rental units. If they are a scattered site they are always – there is always challenges related to that. Trying to find an owner who is

capable of managing property, the challenges of financing and the restrictions that may exist on the financing that was used to do the construction. So I guess what we would really suggest that folks do is not enter into any agreements to construct or rehabilitate homebuyer housing with their 2012 funds without really having thought through, I think as both Steve and Monte have alluded to, what your plan B would be. This is not the kind of provision where you want to think about that tomorrow if it becomes a reality. You really need to think through if you are going to move forward with homebuyer projects with these funds, what you would do in the event that you can not sell it.

We are all helpful that the homebuyer market is coming back and in a lot of areas it is. But I would just urge that people proceed with really a tremendous amount of caution and hopefully the market will return to some equilibrium in the future and this will be less of an issue. So I think that is really what we want to say is that we do understand how burdensome this may be and how challenging it may be and we are available through our field offices, through headquarters, and through our technical assistance to try and help you as best we can to work through a lot of the issues that you will be encountering. Steve, that is about it for us.

Steve Lathom: Thank you so much. And again, thank you everybody for your participation today. Your questions were helpful and illuminating answers both for yourself and for your colleagues. Thank you again to the HUD staff for your time and for helping us out. And a big thanks to Monte. So thank you everybody. We are about to – we are going to go ahead and briefly show you the schedule for the next ones and now we are going into the evaluation. If you can take the opportunity t please fill out the evaluation this really helps us make sure that we are giving you the answers you need. And if there was something that you wanted answered that we did not get to there should be a pot here about do you have additional questions. Feel free to go ahead and answer that and again thank you so much for your time and participation today. We are going to go ahead and log you guys off now and the presenters will go back into another brief post call conference.

Maryanne: Thank you for participating in today's conference. You may now disconnect.