Long Term Affordability Using NSP and HOME

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Speakers and Q and A Format

• Speakers
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  – David Noguera, HUD
  – Marsha Tonkovich, ICF

• How to ask questions
  – Change status in Live Meeting from green to purple
  – Press *1 to ask a question through Premiere Conference
    ✓ Provide Name and Organization
    ✓ If question already answered, press *2 to remove from queue
  – Change status back to green after question answered
Agenda

• Presentation on key topics:
  – Key HOME rules that apply to NSP
  – Ways to combine NSP & HOME funds

• Per past attendee feedback, will do entire presentation (approximately 75 minutes) & then take questions (approximately 45 minutes)
How HOME Rules Apply to NSP

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

• Grantees can choose to adopt HOME rules or develop alternate approach in Action Plan
Concept of Assisted Units

• Applies to rental projects when NSP does not pay 100% of cost or have 100% of units

• NSP-assisted unit has been acquired, rehabbed or constructed with NSP $$$

• NSP-assisted unit must follow NSP rules such as:
  – Property type
  – Eligible costs (more later)
  – Quality/green standards
  – Tenant income
  – Rents, income verification during affordability period

• Other units in project are not necessarily subject to NSP rules
Concept of Assisted Units (cont)

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

• Two options for meeting LMMH:
  – **CDBG approach**: At least 51% of units are NSP-assisted
  – **HOME approach**: Follow HOME cost allocation methodology to determine assisted units or maximum investment

  ✓ HOME has two methods: proportional and actual cost
Cost Allocation

- **Concept**: NSP funds should not pay more than actual, eligible costs for the number of units designated as NSP assisted.

- **Basic equation**: 
  
  \[
  \frac{\text{NSP $$$}}{\text{Total Eligible Development Cost}} = \frac{\text{NSP Assisted Units}}{\text{Total Units}}
  \]

- Can solve for units or for dollars.

- Approach differs for comparable and non-comparable units.
Cost Allocation: Comparable Versus Non Comparable Units

• Comparable units have the same:
  – Number of bedrooms
  – Amenities
  – Square footage

• Non-comparable units have:
  – Different number of bedrooms and/or
  – Different amenities and square footage

• Comparable units can use a proportionate share approach to cost allocation
  – Non comparable units MUST use an actual cost approach
Cost Allocation: Comparable Unit Principles

• Costs are allocated based on a proportionate share of all eligible costs
  – Example: If NSP-assisted units are 30% of total, maximum NSP investment is 30% of total eligible development cost
  – OR: If NSP will pay 30% of total eligible costs, a minimum of 30% of units must be NSP-assisted

• If use proportionate share approach, must distribute NSP-assisted units evenly across bedroom sizes
Cost Allocation: Solving For Minimum # Comparable NSP-Assisted Units

• Key steps:
  1. Decide level of NSP investment
  2. Determine total eligible cost
  3. Create ratio of NSP investment to total eligible cost
  4. Multiply total units times percentage of eligible cost = NSP’s fair share of units
Number Of Comparable NSP Units Example

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

Example (cont)

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

2. \[(0.44) \times (10 \text{ units}) = 4.4, \text{ round up to 5 units}\]
Cost Allocation: Solving For Comparable Unit Maximum Investment

• Key steps:

  1. Decide number of project units that will be NSP-assisted
  2. Create ratio of NSP assisted to all units
  3. Multiply NSP assisted unit percent times total eligible development cost = NSP’s fair share of eligible costs
Comparable Unit Investment Example

- Total eligible costs: $2,000,000
- Total units: 20 comparable units
- NSP units: 2
- Maximum NSP investment?
Comparable Unit Investment Example (Cont)

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

2. \((0.1) \times ($2,000,000) = $200,000\)
Cost Allocation: Non-Comparable Units

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

- In addition to determining total number of NSP assisted units, must determine which units, if any, will count toward LH25

- NSP-paid expenses for any unit meeting LH25 income targeting may be counted toward set-aside
  
  - Example: 20 units in project, 10 will be NSP assisted
    
    ✓ TDC is $2,500,000
    ✓ NSP investment is $1,000,000
    ✓ All 10 NSP units will be occupied by households at 50% AMI
    ✓ $1,000,000 can be counted toward LH25
Set Aside for Very Low Income Units (cont)

• When there will be a mix of LH25 and other units, need to look at portion of TDC paid by NSP and portion of LH25 units

• Example: 50 units in project, all will be counted as NSP assisted
  ✓ TDC is $5,000,000
  ✓ NSP investment is $2,000,000 (40%)
  ✓ 25 units will be occupied by households at 50% AMI
  ✓ 25 units will be occupied by households up to 80% AMI
  ✓ All $2,000,000 can be counted toward LH25 because investment is only 40% of TDC but LH25 units are 50%
Timing of Investment

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

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

- NSP can use HOME affordability period:

<table>
<thead>
<tr>
<th>Per Assisted Unit NSP ($)</th>
<th>Min. Affordability Period</th>
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</thead>
<tbody>
<tr>
<td>&lt;$15,000</td>
<td>5 years</td>
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<tr>
<td>$15,000 - $40,000</td>
<td>10 years</td>
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<tr>
<td>&gt;$40,000</td>
<td>15 years</td>
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<tr>
<td>Rental New Construction/</td>
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<tr>
<td>Acquisition of New Construction</td>
<td>20 years</td>
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- Rules apply to both homebuyer and rental units
Options for Homebuyer Affordability

• HOME rules are safe harbor
  – Can use alternate approach but must get HUD approval
  – HOME affordability periods are minimums – NSP grantees can set longer terms

• For each homebuyer program, UP FRONT, grantee must select compliance approach during period of affordability
  – Two options: Resale or recapture
  – Cannot mix recapture and resale; must choose one or other
  – If no “Direct Subsidy” to homebuyer, grantee must select Resale
Recapture Approach

• Meet affordability requirement by recapturing funds if unit sold by owner during affordability period
  – Amount recaptured depends on sale price and chosen recapture approach
  – Cannot use recapture if assistance = grant

• May re-sell unit to any buyer at any price
  – Once $$$ recaptured & unit sold, no additional unit restrictions
Recapture Approach (cont)

• Affordability period based on “total amount subject to recapture”

• Total subject to recapture is direct homebuyer subsidy:
  – Assistance provided to buyer
    ✓ Downpayment/closing cost assistance
    ✓ Subsidized loan
  – PLUS assistance amounts that write sale cost below market value
    ✓ Need an agreement with buyer

• **Does not** include NSP amounts to subsidize development when that cost exceeds market value (known as development subsidy)
Recapture Affordability Period Example

- NSP loan to buyer: $15,000
- NSP downpayment assist: $5,000
- NSP developer assist: $50,000
- Market value of home: $160,000
- Sale price of home: $155,000

- Total amount subject to recapture:
  - $15,000 + $5,000 + $5,000 = $25,000
- Affordability period 10 years
Recapture Approach: Amount Recaptured

- Occurs when home is sold during affordability period (whether voluntary or foreclosure)
- Recapture amount is limited to “net proceeds”
- Net proceeds defined as:
  \[
  \text{Net Proceeds} = \text{Sale Price} - \text{Superior Debt} - \text{Closing Costs}
  \]
- Limits amount owed back if net proceeds insufficient – For example:
  - Original NSP investment: $20,000
  - Unit has declined in value & net proceeds at sale are $7,000
  - Maximum amount owned to grantee: $7,000
Recapture Approach: Amount Recaptured (cont)

• Grantee must determine up front how to share net proceeds with owner (seller)

• Four options:
  1. Recapture full amount of direct subsidy to homebuyer;
  2. Forgive direct subsidy pro-rata over affordability period;
  3. Proportionately share net proceeds; or
  4. Allow buyer to recover his/her initial investment first.

• NSP also allows for sharing of appreciation which makes sense for markets that will come back strongly in 5-10 years
Resale Approach

• Meet affordability requirement by limiting unit sale price and eligible buyers for any sale during affordability period
  – Does not preclude having mortgage on unit which is repaid at sale

• Typically used in situations where goal is creation of long term pool of affordable units
Resale Approach (cont)

- Affordability period based on total NSP investment in the property (even if only temporarily in project)
  - Must include $$$ of NSP assistance to buyer
  - PLUS total amount of NSP funds provided to developer

- Note: if use HOME & NSP together, do not add HOME & NSP assistance together – calculate affordability period separately for each
Resale Affordability Period Example

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

- If there is resale requirement, when home is sold:
  - New buyer must be low-income
    - Next buyer income cap based on original unit income targeting
    - If unit originally counted toward 50% income targeting, new buyers during affordability period must also be 50% or less
    - If unit originally counted toward 120% income targeting, new buyers during affordability period must also be 120% or less
Resale Approach: Actions When Unit is Sold (cont)

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

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

• Affordability period dictates rental compliance period

• Covers:
  • Rents
  • Incomes
  • Unit mix
  • Sale during affordability period
On-Going Rent Limits

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

• NSP Caps 100% of initial occupants at or below 120% median
  – Only applied to households in assisted units

• **Unlike HOME**, NSP checks incomes of new tenant only at unit turn over
  ✓ Unit originally occupied by household at 120% of median, new tenant at ≤ 120% of median
  ✓ Unit originally occupied by household at 50% of median, new tenant at 50% of median
Determining Income

• Tenant income inclusions and exclusions:
  – Use IRS, Census or Part 5 (Section 8) definition
  – Anticipate income for next 12 months
  – Recommend full 3rd party documentation, e.g., an employer
  – Verifiable self-certification from assisted person is OK
  ✓ WARNING on using this method: If self-certification determined to be incorrect or fraudulent, project may be ineligible
  – Compare income to income limits to determine eligibility
  ✓ See HOME income guide at:
Managing Unit Mix Over Affordability Period

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

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

• Many reasons to consider programs together:
  – Stretches scarce resources
  – Differences in eligible activities
  – Differences in target populations
  – Yet, many rules across two programs are similar
Ways to Combine NSP & HOME

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

• When combined in same unit, must meet rules of both programs
  – Generally, most restrictive rule applies

• Example #1: Number of very low income units in a rental development

• Example #2: Sales price of homebuyer units

• Example #3: Income limits
## NSP Resource Exchange Links

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Please Give Us Your Feedback

- Answer a few short questions
- Link:

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