Chapter 14
Low Income Housing Tax Credit (LIHTC) and Other Tax Credit Program Guidance

14.1 Introduction

The Low-Income Housing Tax Credit (LIHTC) program was enacted as part of the Tax Reform Act of 1986. It is administered by the Treasury Department and State Housing Finance Agencies (HFAs). In July 2008, the Housing and Economic Recovery Act (HERA) provided statutory rulings for FHA multifamily program changes, to facilitate the use of insured mortgages with LIHTC developments.

This chapter outlines policies and procedures for underwriting and reviewing FHA multifamily mortgage insurance applications for projects using Low-Income Housing Tax Credits. Standard processing of such applications applies except as modified below, and all LIHTC projects are underwritten using the "single underwriter model". Underwriters assigned LIHTC projects must have specialized training in underwriting these deals. Guidance provided here addresses all LIHTC projects underwritten for FHA insurance.

14.2 Affordable Housing Underwriting and Program Guidance In Other Parts of the MAP Guide

Guidance for processing and underwriting insured loans for affordable housing projects under the various mortgage insurance programs can be found in other chapters and appendices of this Guide, noted in the chart below:

MAP Guide Section Number	Content
Section 2.7.E	Identities of Interest (IOI) are permitted between lenders and equity syndicators, investors, or bridge loan lenders, in limited circumstances.

Section 2.7.I	IOI Tax Credit Equity Syndicator or Investor Representation and Warranty certification requirements.
Section 3.1.GG	Underwritten occupancy requirements for LIHTC transactions.
Section 3.3	Loan sizing ratios under 221(d)(4) are provided, and these apply to Tax Credit projects underwritten for that program unless adjusted for the New Pilot in separate guidance.
Sections 3.4, 3.5, & 3.7.	Loan sizing ratios under 220, 223 and 231 are provided, and these apply to Tax Credit projects underwritten for each program unless adjusted for the New Pilot in separate guidance.
Sections 3.2 & 4.2.B.	One stage application processing is permitted for all Tax Credit projects under all Sections of the Act. If lender chooses two-stage processing, no pre-application fees are charged.
Section 5.6	Streamlined processing (including delayed submission of final plans) is permitted for Tax Credit projects, assuming certain conditions are met.
Section 7.4.A	No market study, other than that which would be provided in the appraisal, is required for projects with 90% or more project based rental assistance.
Section 7.4.M	Demand Estimate and analysis of demand for LIHTC properties.
Section 7.7.I.5	Underwriting NOI for projects with Section 8 and LIHTC and projects with above market Section 8 rents for a long term.
Section 7.13 & 8.14.F	Calculating operating deficits (for all Tax Credit projects.)
Section 7.14.G.	Valuation instructions for affordable projects with a lease.
Section 7.15	Underwriting tax abatements and waivers of certain underwriting requirements for Tax Credit projects.
Section 7.16	Valuation of Tax Credit and other affordable properties.
Section 8.2	Special Limited Partners (SLP) and pre-approval of SLP.
Section 8.3	Identifying and underwriting the principals in an LLC, LP, or non-profit for purposes of mortgage credit review and limited review of tax credit equity syndicators and passive investors and Previous Participation Review Requirements.
Section 8.5	Financial requirements and LIHTC Letters of Commitment.
Section 8.7	Secondary Financing requirements for public and secondary financing. Requirements for secondary financing from governmental lenders and for bridge loans used to fund equity during the construction period; use of HUD's form of Subordination Agreement instead of Note Rider.
Section 8.8	Evaluating mortgage credit for non-profit sponsors.
Section 8.12	Firm Commitment Processing with Grants and Loans.

Section 8.14	Cash requirements for Closing
Section 8.15	Requirements for tax exempt bond financing.
Section 11.5	Loan fees for tax-exempt bond financing.
Section 11.8	Prepayment provisions for affordable or subsidized properties.
Section 12.7, 13.1, & 13.4	No cost certification required for tax credit projects if LTC/ LTC less than or equal to 80%.
Chapter 16	Master Leases
Appendix 3B	Developer Fees by Program.
Appendix 3G	Broadly Affordable and Affordable MIP rate categories.
Appendix 4	Application exhibits.
Appendix 8H	Identification and Certification of Limited Liability Investor Entities
Appendix 12A	Disbursement of grant and LIHTC proceeds.

14.3 Historic ("HTC") and New Markets Tax Credits ("NMTC")

The Federal Historic Preservation Tax Credit program encourages private sector investment in the rehabilitation and re-use of historic buildings. The National Park Service and the Internal Revenue Service administer the program in partnership with State Historic Preservation Offices. Some states also offer tax credits for historic buildings and encourage applicants to apply to both federal and state programs together. The HTC can be coupled with other local, state and federal incentives as well, including LIHTC.

New Markets Tax Credits are administered by the Community Development Financial Institutions Fund, or "CDFI" Fund, (a program within the U.S. Department of the Treasury) and the Internal Revenue Service. NMTC can be used to finance a number of property types including mixed-use with multifamily so long as the property is within a low-income community as defined by the U.S. Department of the Treasury. NMTC investors typically invest in intermediary entities, Community Development Entities (CDEs), which then provide funding to the project-level ownership entity, usually in the form of non-traditional debt. No more than 80% of a NMTC property can be residential on a square footage and income basis; 20% or more must originate from a commercial use. NMTCs can be combined with HTC but are not typically combined with LIHTC.

The HTC and NMTC programs are only occasionally used in FHA-insured projects, so policies for each program is not provided in this chapter, however, to the extent it is legally permissible and consistent with FHA's mortgage credit and underwriting standards, HTC and NMTC may be used in a manner similar to that described below for LIHTC projects. For example, Equity Bridge Loans (EBL) may be used by Borrowers and/or tax credit investors as a substitute for the pay-in of HTC equity during a project's development and stabilization phases (see Chapter 14.15). Application of the guidance found in this Chapter to HTC and NMTC is determined on a deal-by-deal basis. The lender and HUD underwriter are responsible for verifying that the amounts and timing of the HTC or NMTC contributions are reasonable and can be expected to meet the development costs of the project. The lender is also responsible for documenting the financing terms associated with HTC and NMTC in the Lender's Narrative and the LIHTC Wheelbarrow 2.0.

14.4 Subsidy Layering Review ("SLR")

Subsidy Layering Review requirements have been eliminated for LIHTC projects using FHA-insured loans but no other sources of Federal subsidy. Thus, most of HUD's mortgage insurance transactions are exempt from the formal SLR. The lender and HUD underwriter must always review the Sources and Uses Statements for both mortgageable and non-mortgageable funds, however, to ensure that costs are not being funded twice and that all costs funded from mortgage proceeds are appropriate and necessary to complete the transaction. Nonmortgageable costs must be certified by the funding source to be reasonable and necessary to complete the project. Documentation must be included in the Firm Application.

In addition to the analysis of the Sources and Uses Statement in the FHA loan underwriting, other public funds combined with the FHA mortgage in a Tax Credit project may require a formal SLR. These public funds might include Home Investment Partnerships Program (HOME) funds and other Federal loans, secondary financing provided from state or local sources, or capitalized debt supported by above-market, budget-based Section 8 rents. If those funds require a SLR, either a state agency, another public source, or HUD will perform the review based on the FHA MAP Lender's analysis.

Criterion 11 on the *Supplement to Project Analysis* (HUD Form 92264-A) is not required. It may be used as an optional worksheet.

14.5 Evidence of Tax Credit or Private Activity Bond Cap Allocations

The Firm Application for any LIHTC project should include evidence of 1) a LIHTC award in the form of a 9% State Agency Allocation or if 4% Tax Credits, an allocation of private activity bond cap, or 2) in the case of Historic Credits or New Market Credits, an equivalent form of verification from the appropriate agency.   However, LIHTC allocation timing varies by state, and in some cases FHA applications must be submitted before final allocations of tax credits can be secured. Accordingly other evidence is allowable, for example, in the case of 4% LIHTC allocations, state agency bond cap allocators' assurances and written procedures stating that bond cap remains available for the period in question, that an application has been submitted for the project in question, and that allocations are obtainable in the time available.

Regional offices have discretion to accept applications proposing 4% LIHTC allocations based on evidence of approval that is customary for the State Housing Finance Agency in question.

14.6 Treatment of HAP Contract Renewals for Section 8 Assisted Projects

Where a Section 8 HAP contract is involved, the borrower and lender are responsible for ensuring that the renewal terms under the Section 8 Renewal Guide have been or will be satisfied prior to loan application submission or Initial Endorsement. Consistent with the definition of "Affordable Housing" in this MAP guide, if an existing Housing Assistance Payment (HAP) contract has a remaining term of 15 years or greater from final endorsement, then no renewals are necessary; the loan can be underwritten based on the remaining term of the HAP contract at the applicable loan parameters for affordable housing (e.g. 3% vacancy rate, 1.11 DCR). If the HAP has less than 15 years remaining, no renewals are necessary, but the lender must underwrite to the lesser of Section 8, market, or LIHTC rents for Criterion 5. Criterion 3 remains value-based using market rents, unless the project is a refinance of a 202 or RAD transaction. For Project Based Voucher (PBV) contracts, a 15-year contract is both typical and acceptable.

In the case of a HAP Contract Renewal Request, the Rent Comparability Study ("RCS") must be reviewed by the lender as part of the underwriting process and when reviewing the MAP appraisal. If the borrower commissions the RCS, the same firm cannot do the appraisal. However, if the lender commissions the RCS, the same firm can do the appraisal. The lender is expected to underwrite the loan using the rents from the RCS to develop income and expense estimates (and/or the Section 8 budget prepared by the borrower in the case of budget-based rents) and to address any inconsistencies in the lender's narrative. The HUD Underwriter will review the Section 8 HAP Contract Renewal Request, RCS and lender's underwriting narrative to verify that the rents requested by the borrower in the Renewal Request are supported by the RCS and that the lender's underwriting is in line with both the RCS and the Renewal Request. At the HUD Underwriter's discretion, the HUD appraiser may be asked to review an RCS to determine its reasonableness. If the Performance Based Contract Administrator's[1] ("PBCA") appraiser has not undertaken a

[1] The PBCA is an agency hired to assist HUD/OAMPO in the administration of Section 8 contracts.

detailed review of the RCS, the HUD appraiser must also review the RCS to determine reasonableness using Guidelines in Chapter 9 of the “Section 8 Renewal Policy”.

Coordination among the assigned HUD Underwriter, the field office’s Asset Management and Portfolio Oversight (OAMPO) representative assigned to the project, and if necessary, HUD HQ’s OAMPO staff is essential to ensure that a) the Section 8 HAP Contract Renewal Request and rent increase, if applicable, are approved in a timely fashion, b) a prepayment approval is obtained if needed, and c) any other waivers are processed and approved in a timely fashion.

Section 8 HAP Renewal Requests and Rent Adjustment Requests must be delivered to the Performance Based Contract Administrator (PBCA) at least 60 days prior to the submission of the Firm Commitment application, and 120 days in advance is preferable. However, the RCS rents and the appraiser’s rents must be determined within 180 days of the issuance of the Firm Commitment, or those rents must be updated according to Chapter 7.6.B. Thus the owner and lender must carefully manage the timing. The rents, expenses and debt service used in the lender’s underwriting must be consistent with those in the Section 8 Contract Renewal Request. Lenders should assist borrowers to ensure that the approved RCS rents are consistent with the underwritten rents.

Similarly, lenders’ requests for prepayment of an FHA insured loan should be submitted to headquarters well before submission of the Firm Application package to the HUD field office (see Mortgagee Letter 2018-07). The PBCA, under the direction of OAMPO, prepares and signs the new contract and attached cover letter for delivery to the owner.

Borrowers and their lenders should refer to the Section 8 Renewal Guide for detailed guidance on Section 8 contract renewals.

If the borrower is submitting a budget-based rent request, the lender must coordinate with the borrower to determine a preliminary debt service figure for the new loan that the borrower will include in the proposed budget to submit to HUD and the PBCA. The final debt service figure is subject to change during the final underwriting process, so this may have to be amended on the HAP contract request later. The income, expenses and debt service amounts listed on the borrower’s request must match the amounts in the lender’s underwriting.

14.7 Application/Submission Requirements

Documentation to be provided in the Firm Application includes the following:

A. HAP Contract Renewal Request and Rent Comparability Study, if applicable. A MAP-compliant appraisal and HUD forms 92264, 92273 and 92274 should be submitted with the application. However, the appraiser may opt to use the 92273 used in the Rent Comparability Study or another format and may use Form HUD 92274 or an alternative format acceptable to the lender and the HUD Underwriter.

The following describes application requirements for LIHTC projects that differ from those described in other sections of the MAP Guide for projects without Tax Credits.

Application documents specific to the New Pilot are listed in the New Pilot Application Exhibits Checklist.

A. Data Submission. The LIHTC Wheelbarrow 2.0, an excel spreadsheet which provides specialized information on sources and uses of funds, net equity pay-in requirements, flow of funds and other matters essential to analysis of LIHTC projects, must be submitted for all Tax Credit projects in place of the standard Wheelbarrow. It is available on HUD's Tax Credit website at: https://www.hud.gov/program_offices/housing/mfh/map/maphome/taxcredit. This Wheelbarrow must be used for all Tax Credit projects.

   Other standard documents will be those used for a given project's Section Of the Act (SOA) program.

   Note regarding RAD/FHA/LIHTC Projects: HUD has issued separate guidance for Rental Assistance Demonstration projects for underwriting RAD transactions with FHA-insured loans and LIHTC.

14.8 Architecture and Engineering

A. The ALTA Survey submission may be waived for Tax Credit transactions involving the refinance of a project with an existing FHA-insured mortgage, if the new FHA borrower submits a statement reviewed and approved by the MAP lender and certifies that there have been no material changes or additions to the structure or property boundaries since the closing of the original loan. HUD may accept an existing survey for such projects rather than requiring a new survey document.

14.9 Identities of Interest in Tax Credit Transactions

IOI Transfers for Non-Profits. Non-profit owners of currently insured or HUD-held properties may syndicate LIHTC properties and form new partnerships subject to HUD's Transfer of Physical Asset ("TPA") policies. (See Housing Notice 2011-31.)

See Chapters 2 and 8 for additional guidance on acceptable IOI relationships.

14.10 Calculation of Mortgage Amounts for Tax Credit Projects

A. Section 223(f) applications for Tax Credit projects that involve transfers of ownership to IOI purchasers may be treated either as acquisitions or refinancing transactions for purposes of sizing the mortgage. Lenders may use either Criterion 7 or 10 on the HUD form 92264A.

B. Substantial Rehab Contingency. Generally, unspent contingency funds in an FHA-Insured loan project may be deposited into a Reserve for Replacement Account ("R4R"), pay down the mortgage, or do further improvements, betterments or upgrades to the property. One exception to this rule applies to Low Income Housing Tax Credit properties with affordability restrictions that meet HUD's definition of "Affordable Housing" and obtain FHA mortgages not sized using the cost criterion. In such cases, HUD allows contingency funds included in the FHA mortgageable cost, but not needed for repairs, appropriate betterments, or deposits to R4R, to be used to pay the Developer Fee (deferred or otherwise) or any other HUD-approved project-related expense (e.g. relocation costs). If contingency funds from LIHTC projects will not be used to reduce the mortgage, they should be placed into an escrow. Such funds may not be released until the later of Final Endorsement or 6 months of sustaining (breakeven) occupancy. Release of funds requires Regional Office approval of project repairs and of performance under the construction contract and all other HUD loan documents. In order for unused contingency to be released and paid toward the Developer Fee, the Developer Fee need not have been a mortgageable cost so long as the project's loan-to-cost is under 80%.

14.11 Structuring of Secondary Debt in Tax Credit Transactions

A. LTV Ratio and Private Secondary Debt. For transactions that do not have Low-Income Housing Tax Credits, Section 223(f) limits the combination of FHA insured and secondary financing to a loan to value limit of 92.5% (except when the debt source is a public entity). For tax credit projects (new construction, substantial rehabilitation, and refinance transactions), debt limits can restrict property basis and tax credit amounts unnecessarily. Accordingly, HUD does not impose a loan to value limit on secondary financing, regardless of the source (public debt or private debt). This means that in some cases debt may exceed value. However, all such secondary debt remains subject to the following conditions:

1. Payments on all secondary debt are restricted to 75% or less of the annual surplus cash, and/or the proceeds of a sale or refinancing of the property. (See 24 CFR 200.85(b).) This limit applies cumulatively to all secondary debt, private and public, to ensure that at least 25% of the surplus cash remains as an incentive to the owner. Owners may make additional payments on the debt out of their remaining 25% of cash flow, or from other sources.

2. The FHA insured loan and the total combined private secondary debt may not exceed the limit of 100% of total mortgageable and nonmortgageable project costs as confirmed by the HUD Underwriter's analysis of a comprehensive Source and Uses of Funds Statement. (Public secondary debt is not included in this calculation.);

3. The maturity date of the secondary debt must be coterminous with, or later than that of the first mortgage. The HUD underwriter may consider exceptions on a case-by-case basis for public debt when other HUD programs (e.g., the HOME program) require shorter amortizations and the risk is mitigated. Examples of mitigants include items such as significant additional public funds, low loan-to-value or loan-to-cost ratios, below market rents or higher than minimum debt service coverage.

4. The secondary debt can reasonably be expected to be paid off over its term with 75% of the project's surplus cash;

5. The debt is documented in HUD's form of Surplus Cash Note (HUD-92223M) or subsequent version with simple interest. HUD will permit compounding of interest if the lender provides a thorough analysis demonstrating that project cash flow will be sufficient to avoid accruals of interest that would undermine the long term financial and physical integrity of the project, and all other risks have been adequately mitigated; <u>and</u>

6. Private debt of up to 100% of Total Project Costs may be secured with the project but it must be subject to automatic re-subordination in any refinancing of the first mortgage.

B. Bridge Loans. Temporary bridge loans are treated differently from other secondary financing and are described in detail below in Part 14.16.

C. Publicly Funded Loans or Public Debt. Loans funded with HOME Funds or other federal, state or local public sources, as well as those funded by quasi-public agency programs such as the Federal Home Loan Bank's Affordable Housing Program (AHP), may be granted or lent directly to HUD's borrower, or to the GP or sponsor of the borrower, who will then loan it to HUD's borrower. All such sources will be treated as public secondary financing sources, and as such need not be included in the calculation of the 100% of total project cost limit applied to private secondary debt. However, none of these sources may be substituted for Tax Credit Equity required by the pay-in schedule provided below and all remain subject to the 75% cap on payments from surplus cash.

14.12 Developer Fees

A. Treatment of Developer Fee. Developer fees can, though are not required to be, treated as mortgageable costs so long as they are 1) in amounts approved by the project's LIHTC allocation agency and 2) scheduled for payment in amounts and at times agreed upon with the syndicator or investor.

Developer Fees for different project types and loan programs are addressed in greater detail in Appendices 3.B.1. and 2.

B. Neither BSPRA nor SPRA may be claimed when a Developer's Fees is included in the project budget, regardless of whether the Developer Fee is treated as a mortgageable cost.

C. Relationship of Developer Fee to General Contractor Profit and Determination of Fees in Cases with an IOI Relationship between Contractor and Owner/Developer. An IOI between the GC and the owner is allowed and does not require a waiver, but it must be disclosed in the application and may affect the fee and profit structure. No blanket restriction has been imposed on the amount of General Contractor profit, except it must be reasonable based on the market and the scope of work. HUD generally relies on the policies of the State tax credit allocation agencies, which often scale fees down when a single party or two related parties are receiving both the Developer Fee and the GC Profit. The Lender's and HUD's underwriters will evaluate the fees and profits for each project and reduce them if they are determined to be excessive, considering the scope of the project. Projects with excessive fees may not be approved.

D. Deferred Developer Fee (DDF). If repayment of the DDF is an obligation of the Borrower, repayment terms must be identified in the Borrower's Limited Partnership Agreement or Operating Agreement, and/or in a Note. The DDF loan does not need to be documented in HUD's form of Surplus Cash Note (form 92223M) or subsequent version. Whether the DDF loan is documented in the Borrower's organizational documents or in a Note, language must be included specifying that repayment is restricted to Surplus Cash (as that term is defined in the Regulatory Agreement between the Borrower and HUD). A DDF loan may not be secured by the project, and its term may be shorter than the term of the FHA mortgage. The DDF loan is not subject to the limits on the amount of secondary debt, and it need not be combined with other private secondary debt to determine if the combined amount exceeds the limit of 100% of total project costs. In the event of any conflict between the provisions of this section and other provisions of the MAP Guide, the provisions of this section control.

E. Payoff of Deferred Developer Fees in a Subsequent Refinance Transaction. Under a Section 223(f) transaction, deferred developer fee debt from the project's most recent transaction (i.e. the construction closing) will be treated as originally structured. If the debt is an obligation of one or more of the upper tier members and not the Borrower, the deferred fee will be treated as equity, the cost of paying it off would not be mortgageable and the liability would have to be satisfied so as not to remain in place after the FHA loan closing. Alternatively, if the DDF was structured as a debt of the ownership entity it may be recognized and paid off in the same manner as other debt or assumed by the purchaser and remain in place after the refinancing.

14.13 Tax Credit Equity Pay-In Schedule

FHA requires minimum Tax Credit equity contributions according to the following pay-in schedule for all LIHTC transactions[2]. This schedule, with actual total equity and net-equity amounts entered, is to be added as a special condition to the Firm Commitment for all Tax Credit Projects. Also to be added as a special condition, is evidence of an agreement that binds the investor to timely and periodically pay to the Borrower tax credit equity to contribute to the completion costs. Waivers of the requirements set forth below will generally not be considered.

Benchmarks for Equity Installments	**Minimum Equity Installment**[3][4]
On or Before Initial/Final Closing for Section 223(f)[5] deals and by Initial Closing for Section 221(d)(4) deals:	20% of Total Equity (of this amount, 10% may be funded with an Equity Bridge Loan)
At 65% Completion of Repairs for Section 223(f) deals and at 65% Construction Completion for Section 221(d)(4) deals:	37.5% of Net Equity remaining after initial installment
At 100% Completion of Repairs for Section 223(f) deals and at Final Endorsement for Section 221(d)(4) deals:	62.5% of Net Equity

[2] This schedule does not apply to equity derived from New Market or Historic tax credits.
[3] Additional equity is acceptable at each benchmark date shown, as well as at other interim dates at the investors' discretion.
[4] With the exception of the first equity payment, which is calculated as a percentage of Total Equity, all percentages used in this column represent percentages of Net Equity.

[5] The repair escrow is not required to be funded at 100% at the time of closing if tax credit equity is being used to fund repair costs. The gradual pay-in of tax credit equity is allowed per the benchmarks in the chart above. The Assurance of Completion, however, must be funded at 100% at the time of Closing.

	remaining after initial installment (cumulative)

Equity investors may fund all or part of the required equity pay-ins defined above, except for half of the first 20% payment (10% of Total Equity), with Equity Bridge Loan proceeds that meet the requirements described in Chapter 14.15 below. Investors may not substitute any grant or loan funds, other than funds in the form of Equity Bridge Loans as described in Part 14.15 below, for the equity payments. The equity installments noted above can be used for mortgageable or non-mortgageable. The actual amount of the initial equity investment should be listed as a line item for immediate disbursement on the initial requisition, HUD Form HUD-92403, Application for Insurance of Advance of Mortgage Proceeds.

A. Definition of “Net Equity”. The term “Net Equity” is equal to Total Equity less the initial 20% installment less 1) “Delayed” Developer Fees for amounts due after the completion of repairs or construction and 2) predetermined reserve amounts to be held by the investor for project uses after the time of the final pay-in noted in the schedule above. Reserves allowed for this calculation may include only amounts that are required in the project’s Partnership Agreement or LLC Operating Agreement but excludes those specifically required by HUD. Allowable items include Lease Up Fees and Escrows, Operating and Debt Service Reserves, Section 8 HAP Contract Transition Reserves, Replacement Reserves, and State Agency Administrative Fees or Escrows, not otherwise required by HUD. The total deductions used to determine Net Equity may not exceed 25% of Total Equity. When calculating the pay-in amounts due at the benchmarks listed on the chart above, owners must first reduce the total amount of equity committed to the project by the initial installment and the allowable deductions, and apply the payment percentages above (37.5% and 62.5% respectively) to the remaining or “Net” Equity. This calculation, specifying each applicable use, must be provided to HUD on the Wheelbarrow included in the FHA insurance application.

B. An example of the calculation of the Net Equity amount, and the resultant pay-in schedule, is provided below:

<u>Net Equity = (Total Equity) – (Equity Pay In #1) – (Allowed Deductions)</u>

Total Equity or Gross Proceeds	**$7,500,000**
<u>Less Payment #1</u>	<u>$1,500,000 (20% of Total Equity Above)</u>
Less Allowed Deductions Not to Exceed 25% of Total Equity (25% x $7,500,000)	= $1,875,000)

Minimum Net Equity = $7,500,000 - $1,500,000 - $1,875,000 = $4,125,000

Sample Owner's Proposed Reductions:

Delayed Developer Fee	$800,000
Lease Up Fees and Escrows	$175,000
Operating Reserves	$145,000
Debt Service Reserves	$200,000
Section 8 HAP Contract Transition Reserves	$235,000
Replacement Reserves	$300,000
State Agency Administrative Fees or Escrows	$45,000
Total	$1,900,000

This total would be disallowed, as the $1.9 million exceeds the 25% of total equity ($1.875 million) allowed. Accordingly, it is reduced by $25,000 in the following calculations.

Net Equity is the Balance, after Total Equity is reduced by Payment #1, and the Allowed Deductions of $1,875,000, or $4,125,000. This number would be adjusted if the owner were to claim less than the maximum Allowed Deductions.

Payment	**Description**	**Formula**	**Amount**
Equity Pay In #1	20% of Total Equity	20% x $7,500,000 =	$1,500,000
Equity Pay In #2	37.5% of Net Equity ($4,125,000)	37.5% x $4,125,000	$1,546,875
Equity Pay In #3	62.5% of Net Equity ($4,125,000)	62.5% x $4,125,000	$2,578,125

C. There is no change in the computation to determine the cash requirements and/or front money escrow on Form HUD-92264-A. The remaining cash requirements not being satisfied with LIHTC equity will be satisfied in accordance with outstanding instructions. The Borrower must pay out-of-pocket when there is no available cash from mortgage proceeds or other committed sources.

14.14 Equity Bridge Loans ("EBLs") in Tax Credit Projects

Equity Bridge Loans may be used by Borrowers and/or tax credit investors as a substitute for the pay-in of equity during a project's development and stabilization phases, thereby deferring the pay-in of equity and increasing the return on equity. The EBL may be the obligation of one or more of the investors or other upper tier partners to the ownership entity (i.e. the limited or general partners), or an obligation of the project ownership entity/single-asset mortgagor itself.

In addition, the following conditions must be met:

A. EBLs must be expressly subordinate to the HUD-insured first mortgage, and may not be secured by a lien on the real estate or on any other "Mortgaged Property" as defined in the Security Instrument, although they may be secured with a pledge of tax credits, tax credit equity, and/or an upper tier (i.e. the limited or general partner or managing member) or investor members' interests in the project's ownership entity. Any security for the EBL may be held by the Borrower in a separate, segregated account, specifically labeled as non-project funds, and which are not part of the Mortgaged Property in Section 1(w) of the Security Instrument.

B. EBLs must be non-recourse to the Borrower (except for Surplus Cash or residual Receipts, as applicable, of the Borrower), and the bridge lender shall have no claim even in an event of default against the Project, FHA mortgage loan proceeds, or any reserve or deposit made with the FHA Lender, or otherwise required by HUD.

C. In the event HUD acquires title to the Project by foreclosure or deed in lieu of foreclosure, the equity bridge loan documents shall be discharged with respect to the FHA Borrower, and the FHA Borrower shall be released of all of its obligation with respect to the EBL. Notwithstanding the required discharge of the FHA Borrower imposed by this paragraph, the equity bridge loan documents may provide that such discharge neither: (1) excuses or relieves any co-signer, guarantor or any other party from the obligation to repay the indebtedness evidenced by the bridge loan note and bridge loan documents; nor, (2) affects, limits, or impairs the bridge lender's ability to seek a monetary judgment and pursue other remedies against the guarantor.

D. The obligation must be evidenced by a promissory note with appropriate subordination provisions and limitations on recourse against the Borrower.

E. The term of the note may last through the construction or rehabilitation period but must be paid in full no later than the following dates:

    1. In the case of EBLs provided by private, for-profit lenders, no later than one year after (a) Final Endorsement for Section 221(d)(4)/220 loans, or (b) 100% completion of repairs for 223(f) loans; and

2. In the case of EBLs provided by not-for-profit, public sector or quasi-public sector entities, no later than ten (10) years following (a) 100% Completion of Repairs for 223(f) loans, or (b) Final Endorsement for 221(d)(4) loans.

F. The FHA Borrower must provide evidence to the lender's and HUD's satisfaction that the bridge loan will be paid in full by the timeframes noted above. In addition, the Borrower's audited financial statement (AFS) must reflect that the EBL was paid on time. This must be reflected in the AFS due in the reporting period after the due dates for full EBL repayment noted above.

G. At Firm Application, or as soon as the need for an EBL is known, the lender must submit for HUD's approval a term sheet describing the key terms of the bridge loan, as well as a certification that a) the loan will be secured only by a pledge of partnership interests or tax credit benefits and not by the project, and b) that the bridge lender will have no claim against the mortgaged property, mortgage proceeds, any reserves or deposits, or against the rents or other income from the property for repayment of the bridge loan.

Bridge loans for other purposes, (i.e. that are not used to advance equity in tax credit projects) are described in Chapter 8.

14.15 Syndicator and Investor Fees Paid from Operations

Tax Credit projects often involve annual asset management related fees paid to the syndicator or an investor representative. HUD's Office of Asset Management and Portfolio Oversight allows usual and customary fees and expenses for operating a Tax Credit project, including payment of a syndicators' and/or investor's asset management fee, state allocation agency compliance and asset monitoring fees, and mandatory interest payments of up to one percent on subordinate debt provided by a government lender to be paid from the operating budget. If the expenses described above are included in the operating budget, however, the loan must be sized accordingly by the lender, and the chosen treatment of the expenses must be documented in the closing documents. Fees paid with surplus cash should not be included in the operating budget. HUD generally requires that at least 25% of surplus cash remains available as an owner incentive, though the remaining 75% may be obligated to payment of secondary debt.

Mark to Market (M2M) Transactions: Owners may receive an Incentive Performance Fee (IPF), and this is paid before the 25%/75% split is calculated. Thus, the IPF is paid first and may be realized in addition to the owner's 25% of surplus cash. M2M also obligates the owner to use the full 75% of surplus cash to pay down the program's secondary M2M loans. Accordingly, in M2M transactions the payment of syndicators' and investors' fees must be limited to the 25% that is not committed for loan repayment.

14.16 Firm Commitment Special Conditions for all Tax Credit and Projects with Master Leases

The following special conditions must be added to the Firm Commitment as they apply to applications for mortgage insurance for projects which will have equity funded from Tax Credit proceeds:

A. This Commitment is conditioned on the availability of the tax credit equity contribution described above and in the Equity Contribution Schedule provided with the firm commitment application and approved by HUD, attached as **Exhibit G**. Changes to equity contribution amounts or the Equity Contribution Schedule require the submission of an updated Wheelbarrow and an amendment to the Firm Commitment.

B. The initial equity investment amount is $ _________ (20% of Total Tax Credit Equity). This amount should be reflected on the initial requisition, form HUD-92403, Application for Insurance of Advance of Mortgage Proceeds, for immediate disbursement at Initial Endorsement.

C. Lender must submit satisfactory evidence of an agreement that binds the tax credit investors to timely and periodically pay to the Borrower entity the tax credit equity to contribute to Project completion costs, in the aggregate amounts set forth in form HUD-2880, HUD-92013, and the Wheelbarrow. A Disbursement Agreement that reflects the terms of the Limited Partnership Agreement or Operating Agreement for the remaining outlay of tax credit equity contributions must be provided prior to Initial Closing.

D. All Tax Credit Equity documents to which either the Borrower or Controlling Participants are a party, and any related land use restrictions, must be approved by HUD prior to the date of Initial Endorsement, and must comply with HUD's legal and administrative tax credit equity requirements, and all related HUD closing forms.

E. In addition to the standard provisions that must be included in the organizational documents for the Borrower entity, a provision must be added that prohibits any changes to the organizational documents that affect the obligations of the tax credit investor without written consent of the Lender and HUD.

F. Special Limited Partner. **[NAME]** has been preapproved to serve as the Special Limited Partner to replace the General Partner for a limited period of time. A "Rider to the Security Instrument for LIHTC Properties" must be submitted with the closing documents.

G. Cost Certification Exemption. {LIHTC Projects, MAP Guide Chapter 13.4} The Project is exempt from providing Cost Certification pursuant to Program Obligations. As an additional condition of this Commitment, when the Project reaches substantial completion, as determined by the HUD Inspector, the Lender will be notified of the substantial completion date, and the Borrower must account for all operating income during construction and ending three months prior to the originally scheduled date of the first principal payment under the Secured Instrument. An operating (or income and expense) statement must be submitted covering the period from first occupancy (if occupancy occurred during construction) or from the date of substantial completion (as determined by HUD) through the period ending three months before the date of the first principal payment as originally scheduled. The Borrower may include in the operating statement all soft costs incurred up to 60 days beyond this date, which will establish the cut-off date. The statement must be submitted to HUD at least 30 days before the date scheduled for Final Endorsement. If the operating statement evidences receipt of net operating income during this period, the Borrower may be required to allocate the income received during this period in accordance with current Cost Certification guidance.

H. Deferred Drawings and Specifications – LIHTC Projects and Certain Eligible Borrowers. {MAP Guide, Chapter 5.6.E}

As an accommodation to the Borrower, this Commitment has been issued and based upon preliminary drawings, instead of the final drawings, specifications and cost estimates. At least 30 days prior to the scheduled date for Initial Endorsement, HUD must receive the final drawings, specifications and the Lender's architectural/cost review report for review and approval to ensure consistency of design and cost. The plans and a complete specifications manual must be submitted to **[Name of Construction Analysist]** at **[HUD office location]** for review and approval. **[Name of Construction Analyst**] can be reached at **[phone number]**. He/She will provide information on where the three approved sets of Plans and Specifications with signature blocks will need to be mailed for the preconstruction conference and Initial Endorsement. In addition, it is the Lender's and General Contractor's responsibility to incorporate the most current Davis-Bacon Wage Rates into the appropriate documents.

If there is a net cumulative construction cost change of more than 5%, or a change in design concept, this Commitment shall be subject to and conditioned upon the further approval of HUD, to be evidenced in writing. Based on such change and review, this Commitment may be terminated and voided by HUD, or, additional conditions may be imposed at HUD's option.

Add if applicable: this Commitment is conditioned on the following corrections that must be made to the Plans and Specifications before Initial Endorsement.

I. Bridge Loan. {Insert: amount, interest rate, repayment terms, maturity date, financing instrument(s), name of maker on the loan.}

This Commitment is conditioned on the availability of the Bridge Loan described above. All Bridge Loan documents to which either the Borrower or Controlling Participants are a party must be approved by HUD prior to the date of Initial Endorsement and must comply with HUD's legal and administrative bridge loan requirements, and all related HUD closing forms. If there is a conflict between the HUD loan documents/Program Obligations (HUD Requirements), the HUD Requirements control.

J. Bonds. This Commitment is conditioned on the availability of the Bonds described above. All Bond documents to which either the Borrower or Controlling Participants are a party must be approved by HUD prior to the date of Initial Endorsement and must comply with HUD's legal and administrative bond requirements, and all related HUD closing forms. If there is a conflict between the HUD loan documents/Program Obligations (HUD Requirements), the HUD Requirements control.

K. Deferred Developer Fee. Whether the DDF loan is documented in the Borrower's organizational documents or in a Note, language must be included specifying that repayment is restricted to Surplus Cash (as that term is defined in the Regulatory Agreement between the Borrower and HUD).

L. {The following additional Tax Credit Equity condition applies to transactions with master lease structures to facilitate Historic or New Market Tax Credits.}

[A master lease structure has been approved for this Loan transaction to facilitate [Historic Tax Credits] [New Market Tax Credits]. The Borrower and master tenant [insert name of master tenant], along with the following (residential and/or commercial) master sub-lessees [insert names of master sub-lessee 1, master sub-lessee 2, etc.] must execute separate Regulatory Agreements with the appropriate HUD Rider attached. The Riders can be found at the following link - https://portal.hud.gov/hudportal/HUD?src=/program_offices/general_counsel/mffaqs.
{HUD staff must also insert here the required special conditions for master lease transactions from MAP Guide Ch. 16.4.A.}]

14.17 Other Matters

A. The market study, appraisal and underwriting for all Tax Credit projects must address the relationship between the Tax Credit ceiling rents, the attainable rents, any subsidy contract rents and terms, and true market rents. Any disparities among these rents and their related risks must also be addressed.

B. HERA's Exception to the Tax Credit Program's 10 Year Holding Period. HERA provides for an exception to the LIHTC's ten year holding period requirement for certain federally assisted buildings, specifically those that are 221(d) or 236-insured. Because the HERA language refers to the two specific programs noted above as well as to "…any other program administered by the Department of Housing and Urban Development…" the waiver should apply to all FHA-insured tax credit projects. HUD does not render tax advice however so owners should seek tax counsel with respect to this interpretation.

C. Bond financed projects in New York City. Section 42 of the IRS Code provides that for projects located in New York City, the "40-60" test (restricting 40% of the units for the use of tenants earning no more than 60% of median income) for determining whether a project qualifies as a low-income project, is replaced by a "25-60" test. Thus, the affordability requirement is reduced from 40% to 25% of the units to be set aside at 60% of area median income. HUD will consider this exception to the set-aside on a case by case basis, when the lender's application demonstrates that the NYC market rents for the additional 15% unrestricted units that would otherwise have been restricted, will still provide for significant affordability in the local market.

D. Lien Priority. The FHA mortgage lien is required by statute to be in first position ahead of all other financing. Restrictive covenants with no monetary obligations are not considered liens and, in some instances, may facilitate a transaction if affordability use restrictions other than the Tax Credit LURA survives foreclosure and is recorded prior to the FHA mortgage. On a case-by-case basis HUD may approve non-monetary use restrictions that run with the land and therefore may be superior in priority to HUD's first mortgage position. When waivers are requested, the Lender must demonstrate, and the HUD Underwriter must verify sufficient financial strength and strong mitigants to offset the risk of a negative impact on the marketability of the project in the event of a foreclosure or loan sale. Mitigants might include a low FHA loan to value or loan to cost ratio, significant amounts of public funds, high levels of funding by the source in question, Section 8 assistance for all the units, and higher than minimum debt service coverage.

E. Tax Credit Regulatory Agreements. In Tax Credit projects, certain IRS Section 42 obligations must be allowed to continue post-default. Generally, however, for the Tax Credit LURA, and/or when public secondary financing with regulatory agreements or restrictive covenants are required, HUD requires the use of its standardized rider to these restrictive covenants, which indicates that in case of conflicts between a LURA or another restrictive covenant and FHA "program obligations," FHA requirements take precedence. Neither this provision nor the use of the rider itself should be waived. Instead, staff must identify the point of conflict and consult with OGC. Alterations of the rider that are once approved can then be used as the template for that jurisdiction, as applicable. Typical conflicts include differing numbers of units set aside for specific income levels, different use agreement termination dates, etc. It is the lender's responsibility to draw attention to potential conflicts between FHA requirements and the LURAs or other restrictive covenants as early as possible (i.e., during Concept Meetings) and no later than with Firm Commitment application submission. If they are not addressed in the Firm Commitment, the lender should assume the closing will be delayed.

F. Tax Exempt Bonds/Take out by FHA Insured Permanent Debt. Tax Credit projects are often financed with the "4%" Tax Credits allocated in conjunction with private activity bond volume cap, rather than the "9%" Tax Credits competitively allocated by State Agencies. Taxable Ginnie Mae securities' yields and the resulting rates on FHA multifamily loans at times can be lower than tax exempt bonds and municipal bond-backed multifamily loan rates. Consequently, investment banks have developed an approach that combines taxable Ginnie Mae securities with short term, tax exempt bonds and 4% LIHTC. This structure establishes several different account funds, along with a series of cash flow events between the various accounts upon a draw request. The tax-exempt bonds are secured by cash collateral initially provided by the FHA lender's warehouse funds (or other funding source, but not FHA-insured loan proceeds), which in turn are reimbursed with proceeds from the sale of Ginnie Mae-guaranteed securities. The tax-exempt bonds are retired with the proceeds of the bond collateral account when the project is placed into service.

This structure allows the borrower to avoid higher loan rates that exist when the loan funding source consists exclusively of tax-exempt bonds, and still take advantage of the 4% LIHTC equity. This bond financing structure is generally acceptable to HUD, but each transaction must be reviewed by Housing field staff and OGC field counsel for programmatic and legal sufficiency, including the review of specific transaction documents. Accordingly, underwriters must involve their OGC counterparts early in the process to ensure these issues are addressed early and do not constrain the transaction's processing.

Note that FHA-insured loan proceeds shall not be used to serve as collateral for the bonds, and they may not be paid to the bond trustee or sent to other accounts to facilitate issuance of the bonds. This is a statutory prohibition that may not be waived, as FHA-insured loan proceeds are only permitted to directly finance the relevant activity authorized under the applicable section of the National Housing Act. To ensure statutory compliance regarding the use of FHA-insured loan proceeds, HUD OGC requires lenders to complete Section F of the Lender's Certificate (form HUD-92434M) or the Request for Endorsement (form HUD-92455M) as applicable for financings structured in this manner.

G. Refinancing of M2M Properties. HUD's Office of Recapitalization, along with the field offices' Asset Management staff, are responsible for reviewing any transactions that have been through an M2M restructuring. Those transactions require a waiver of the "due on sale…" clause and extension of the maturity dates of all subordinate notes originated in the restructuring. Current guidance is in Notice H 2012-10, and it explains when the field offices can process the waivers and when HQs must do it. In complex Tax Credit transactions requiring subordination of M2M debt, the owner or lender must request the waiver as early as possible to avoid delays. FHA Production staff may also be involved to ensure that the Recapitalization office's conclusions are consistent with the underwriting of the project.

14.18 FHA Tax Credit Pilot Program Expansion

See Housing Notice: H 2019-03 for guidance on the Section 221(d)(4) and Section 220 New Construction and Substantial Rehabilitation Multifamily Project with LIHTC Pilot Program.