

## **AMENDED AND RESTATED PASS-THROUGH BOND PROGRAM**

**JULY 30, 2020**

### **(Debt Financing Under Section 44c of the Authority's Act)**

Act 346 of the Public Acts of 1966 (the "Act") permits the Michigan State Housing Development Authority (the "Authority") to participate in "conduit" or "pass-through" financings in which the bonds issued to finance a development are a limited obligation of the Authority; the bonds are not secured by the Authority's capital reserve capital account; and the bonds are not backed by the moral obligation of the State of Michigan. Instead, the bonds are secured by the revenues of the borrower, the real and personal property being financed, and a form of credit enhancement acceptable to the Authority.

Projects participating in this program may use Pass-Through Bonds as long-term financing (construction and permanent financing) or as short-term financing (construction financing only). All projects must show evidence of credit enhancement that is acceptable to the Authority.

Projects initiated under the short-term structure have historically been credit enhanced with a Credit Enhancement and Investment Agreement and are refinanced within 36 months following the issuance of the bonds through the use of a Federal Housing Administration (FHA) insured Ginnie Mae (GNMA) mortgage or other similar financing source. The refinancing occurs after construction or substantial rehabilitation of the development has been completed – at which time the program bonds are redeemed in whole.

#### **I. Eligible Projects:**

Projects must satisfy the eligibility requirements of Section 44c of the Authority's Act. Both new construction and acquisition and substantial rehabilitation of residential rental units will be considered.

Proposals receiving Low Income Housing Tax Credit (LIHTC) must meet the threshold requirements of the LIHTC Program for projects financed with tax exempt bonds as provided in the Qualified Allocation Plan (QAP).

#### **II. Eligible Borrowers:**

The Borrower must be an eligible entity under the Authority's Act (e.g., a limited dividend housing association organized as a limited partnership, a corporation, or a limited liability company). The sponsor or developer must be in good standing at the time of application. Good standing means that none of the other projects involving the sponsor or developer that have been financed by the Authority under this program or another Authority lending/subsidy program are experiencing significant, unresolved problems.

#### **III. Minimum Income and Rent Restriction Requirements:**

For tax-exempt bond purposes, applicants are required to commit to income and rent restrictions targeting either (i) 40% of the units for households whose income is at or below 60% of Area

Median Income (AMI), or (ii) 20% of the units for households whose income is at or below 50% of AMI. These income and rent restrictions must remain in place for the longer of the “qualified project period” of the bonds, as defined in the Internal Revenue Code or the extended use period of the LIHTC.

In addition to the minimum requirements above, applicants will be required to commit to income and rent restrictions to target at least 10% of the total affordable units in the project for households whose income is at or below 40% of AMI (“10% Affordable Unit Restriction”). In lieu of the 10% Affordable Unit Restriction, the Authority may permit applicants to commit to satisfying other important mission objectives such as developing or rehabilitating projects in rural areas, or projects that meet the definition of Permanent Supportive Housing and have all necessary supportive services available, etc. The 10% Affordable Unit Restriction may not otherwise be waived or reduced unless the Authority determines that the restriction impedes the Authority’s ability to finance the rehabilitation or new production of projects under this program.

Developments will be eligible to utilize the income averaging set-aside in order to maximize project Net Operating Income while also achieving the deeper targeting referenced above. However, applicants should be aware that the tax-exempt bond regulations do not allow income averaging as a set-aside option, so the project would need to comply with both the set-aside selected for LIHTC purposes and the set-aside selected for tax-exempt bond purposes.

#### **IV. Threshold Requirements:**

Authority staff will review each application to assure that the use of the State’s volume cap for a project will not impair the Authority’s ability to carry out its programs or finance developments or housing units that are targeted to lower income persons.

The Authority’s Office of Rental Development-Tax Credit Allocation Section will review the applicant’s standard tax credit application to assure that threshold requirements for participation in the LIHTC Program are met if LIHTC are being used to finance the development. As part of its review, to the extent appropriate, Authority staff will utilize the applicant’s HUD loan commitment and documents submitted in conjunction with the applicant’s HUD loan approval, thus minimizing multiple layers of review and delays in the HUD closing process.

#### **V. Volume Cap:**

All proposals are subject to available volume cap, as made available by the Michigan Department of Treasury and as determined appropriate by the Authority. The Bond Cap available to this program will be subject to the Authority having sufficient volume cap for its Direct Lending Multifamily and Single-Family Programs.

Volume cap may be allocated to qualified projects under this program provided that said projects may not have a combined bond amount greater than \$100 million.

This program will terminate at the earliest of: 1) the Authority’s regularly scheduled July 2021 meeting; or 2) the Authority’s regularly scheduled June 2021 meeting if there is no July 2021 meeting; or 3) the \$100 million volume cap is fully subscribed. For a project to be included in the

\$100 million ceiling, a project must have been approved by the Authority for an inducement resolution at or before the Authority's July 2021 board meeting. Any volume cap remaining upon termination of the program (as outlined above) will no longer be available to the program nor will it be added to any subsequent reinstatement of the program that may occur. Once the program has terminated, the Authority will review the program and determine whether, and under what conditions, to extend the program.

#### **VI. Project Limits:**

To qualify as rehabilitation, the rehabilitation expenditures with respect to the project must equal or exceed 30% of the portion of the cost of acquiring the building and equipment financed with the proceeds of the bonds issued to acquire and rehabilitate the project. For a project located in an eligible distressed area, the amount of rehabilitation may be less than the 30% requirement but not less than 15% if the Authority determines and expresses by resolution that the likely benefit to the community or the proposed residents of the project merits the use of this financing source.

Per the MSHDA Act, under this structure, the maximum amounts that the Authority is permitted to commit and lend are:

1. For projects not located in an eligible distressed area, the lesser of the total development cost of the proposed multifamily housing project or \$25 million.
2. For projects located in an eligible distressed area, the lesser of the total development cost of the proposed multifamily housing project or \$50 million.

#### **VII. Application, Commitment, Closing and Other Fees:**

Fees shall be determined as follows:

A. Upon submission of an application, the sponsor shall include an application fee equal to the greater of \$4,000 or .0005 times the amount of the bonds to be issued. This application fee will be credited to the commitment fee due.

B. Upon receipt of a loan commitment, the sponsor/developer shall pay a commitment fee of 0.1% of the principal amount of the bonds to be issued, less any amount paid with the initial application.

C. Upon issuance of the bonds, the borrower shall pay to the Authority a fee not to exceed 0.9% of the principal amount of the bonds for developments located in an eligible distressed area or 1.9% of the principal amount of the bonds for developments not in a distressed area.

D. For each year that bonds remain outstanding, the borrower shall pay an annual compliance monitoring fee in an amount not to exceed 0.25% of the outstanding principal amount of the bonds. This fee shall be paid according to such terms and conditions as may be approved by and Authorized Officer of the Authority and may, at his or her sole discretion, be waived in whole or in part.

#### **VIII. Application Requirements:**

For a project to be eligible to apply for the Pass-Through Bond Program, it must first be submitted to the Authority in order to evaluate whether the project is likely to be competitive under the Authority's Gap Financing Program. The Gap Financing Program makes available a certain amount of gap financing to be used in combination with Authority tax-exempt bond financing. To perform its evaluation, the Authority will consider the following:

1. The financial viability of a project based on the pro-forma analysis, site, and preliminary market analysis; and
2. The overall capacity and experience of the development team.
3. The likelihood that the project will be competitive and be able to proceed with the funds available in the Gap Financing Program. To determine how competitive a project is likely to be, the Authority will primarily evaluate a project's soft to hard debt ratio, which is used to rank the proposals in the Gap Financing Program, to determine if the project appears to be competitive as compared to the current or most recent Gap Financing Program funding round. Applicants are encouraged to view rankings of recent Gap Financing rounds on the Authority's website to determine with more certainty whether their project has a competitive soft to hard debt ratio. *Since the Direct Lending Program is currently oversubscribed, it is anticipated that Pass-Through Program applications during this time will be given MSHDA staff approval to bypass the Direct Lending Program so they can apply under the Pass-Through Program.*

Following the analysis above, if, based on the Authority's determination, a project is unlikely to be competitive in the Gap Financing Program, the project will be eligible to continue under consideration as part of the Pass-Through Bond Program. Additionally, following an evaluation based on the process outlined above, projects that do compete under the Gap Financing Program, but that cannot move forward using gap financing with an Authority tax-exempt loan (as determined by the Authority as part of the Gap Financing Program) will be able to submit an application as part of the Pass-Through Bond Program. However, Authority gap financing such as HOME funds and/or Preservation funds are not available to projects that apply and are financed under the Pass-Through Bond Program.

If the sponsor chooses to proceed to the Pass-Through Bond Program, the following items must be submitted:

A. The sponsor/developer must submit a completed application under the LIHTC Program, including all required attachments.

B. In order to be considered complete, all applications for an allocation of volume cap under this program must include:

- i. A description of the proposed credit enhancement and a statement as to the amount of the tax-exempt bonds (and taxable bonds, if appropriate) requested. The proposed credit enhancement may be in the form of an unconditional, irrevocable letter of credit, guaranty, bond or mortgage insurance, or other security as the Authority deems appropriate to assure the Authority that repayment of the bonds is reasonably secure.

ii. Assurance that all bond issuance costs will be paid and the professional team (bond underwriter, bond trustee, bond counsel, etc.) will be compensated for services rendered in issuing the bonds. All bond issuance costs are the responsibility of the sponsor/developer and are not the responsibility of the Authority.

iii. To the extent not identified in the LIHTC Program application, identification of the full development team, including the bond underwriter, bond trustee, bond counsel, equity partner and rating agency. Bond counsel must have prior experience on Authority bond transactions and must be pre-approved by the Director of Legal Affairs, the Chief Financial Officer, and the Finance Division of the Office of Attorney General. The bond underwriter, bond trustee and rating agency must be acceptable to the Chief Financial Officer.

iv. For proposals involving the acquisition and rehabilitation of existing property, substantiation that the rehabilitation expenditures will equal at least 30% of the bond proceeds used to acquire the building(s) and equipment. (For a project located in an eligible distressed area, the amount of rehabilitation may be less than the 30% but not less than 15% if the Authority determines and expresses by resolution that the likely benefit to the community or the proposed residents of the project merits the use of this financing source.)

v. If applicable, a tenant relocation plan.

vi. A phase I environmental assessment report.

vii. A market study.

viii. The application fee.

C. Applications may be submitted at any time after the program is authorized. Authority staff will process applications on a first-come first-served basis in the order they are received in accordance with the date the application is received by MSHDA. The Authority will advise prospective sponsors/developers of (a) the number of proposals in process, (b) the place "in line" where the application is, based on the submission date/time of the application, and (c) the total volume cap requested by those proposals. Project applications that are submitted but that are found to have substantial deficiencies and which cannot progress along a normal approval timeline may lose their place in line so as to not impede other projects that are more ready to move forward, but were submitted after it. For a project to be included in the \$100 million ceiling, a project must have been approved by the Authority for an inducement resolution.

D. Applications that do not receive a reservation of volume cap due to the then-current unavailability or inadequacy of volume cap will be automatically considered under future re-authorizations of this program, to the extent that it is re-authorized, and will not need to re-apply. All applications will be subject to the guidelines and order of processing as outlined under the Pass-Through Bond Program that is in place at the time they receive a reservation of volume cap.

## **IX. The Authority Processing Sequence:**

A. Upon receipt of an application, staff will conduct a preliminary review, and will notify the sponsor/developer in writing within thirty (30) days as to whether (i) the application is complete or (ii) the application is not complete, and what must be corrected or completed. Staff will review and evaluate a completed application and, if appropriate, make a recommendation to the Authority members that use of the State's volume cap for the proposed project will not impair the ability of the Authority to carry out its programs or to finance housing developments or housing units that are targeted to lower income persons. This process includes:

- i. A determination of the extent, if any, to which the proposed project may adversely affect a project or projects (a) financed with Authority loans, or (b) to which the Authority has extended a loan commitment that has not been terminated, or (c) that is considered to be "active" in the Authority's pipeline.
- ii. A review of the environmental assessment report to confirm that no environmental problems exist that cannot be resolved to the satisfaction of the MDEQ and the Authority.
- iii. A review and evaluation of the proposed credit enhancement and the proposed credit enhancement provider.
- iv. Preparation of an Inducement Report and Resolution for Authority consideration within sixty (60) days of receipt of a completed application. This represents the Authority's formal action for purposes of applicable tax regulation, currently Treas. Reg. §1.150-2(d). It does not constitute a commitment to loan funds or a determination that the proposal is acceptable.

B. The Authority will use its best efforts to complete the processing sequence identified in VIII.A(i) - (v) within sixty (60) days of receipt of a completed application. Once the review has been completed and the application is determined to be acceptable, the Director of Legal Affairs will then issue a letter reserving volume cap for 6 months. This letter must be signed and returned by the sponsor/developer within twenty (20) days or the volume cap reservation will lapse. Additionally, the Authority may approve a 6-month extension of this deadline for a nonrefundable extension fee of \$5,000, which fee shall not be credited against any other fee or payment to the Authority. According to statute, the Authority is only authorized to grant one 6-month extension.

C. Upon issuance of the HUD loan commitment, Authority staff and/or bond counsel will:

- i. Begin drafting loan and bond documents;
- ii. Publish a TEFRA notice and conduct a TEFRA hearing. This must occur prior to the Authority's meeting at which the Bond Resolution will be considered (see (iv) below);
- iii. Prepare a Commitment Report and Resolution for Authority consideration after evidence of a firm commitment for acceptable credit enhancement has been received, reviewed, and evaluated by staff; and

iv. Prepare a Bond Resolution for Authority consideration together with the Commitment Resolution, provided that the principal bond documents requiring Authority signature or approval are in substantially final form.

Both the commitment resolution and the bond resolution must be approved and adopted by the Authority.

D. Proposals that are found unacceptable shall be terminated. The Authority will notify the sponsor/developer in writing of any termination and the basis for termination.

E. Proposals must proceed to loan commitment and authorization of the issuance of the Authority bonds within 6 months after the sponsor's acceptance of the reservation of volume cap. Extensions will be provided only upon payment of a \$5,000 non-refundable fee. According to statute, the Authority is only authorized to grant one 6-month extension.

F. For planning and administrative reasons, closings will not be permitted during the month of December, absent approval from the Authority. Requests will be considered on a case-by-case basis. If a project's 6-month reservation of volume cap terminates during the month of December, however, an additional thirty (30) days will be granted and no extension fee shall be charged to the borrower.

#### **X. Return on Equity:**

A borrower is allowed distributions equal to a 12% return on investment in the project for the first 12-month period following the substantial completion of the development. Thereafter, the allowable return on investment is increased by 1% annually up to 25% (except for developments in eligible distressed areas where there is no cap) and is fully cumulative. The borrower shall be required to submit to the Authority a copy of the annual financial statement evidencing its eligibility for return on investment no later than ninety (90) days following the close of the borrower's fiscal year. The borrower's "investment" is defined pursuant to the Authority's Resolution dated March 13, 1985.

#### **XI. Bond and Tax Credit Requirements**

At the time of the bond closing, the applicant must enter into a Credit Enhancement and Investment Agreement that provides that the proceeds of the Ginnie Mae loan (or other permanent loan if the cash proceeds therefrom are used as credit enhancement) will be invested in tax-exempt non-AMT investments that will be held by the bond trustee. The applicant must also provide the Authority with an opinion of the applicant's tax-credit counsel that the structure of the transaction will permit the applicant to claim the 4% LIHTC. In addition, the applicant must certify in writing to the sources and uses involved in the financing of the development.

#### **XII. Compliance Monitoring and Reporting Requirements:**

On or before September 1 of each year, the borrower must provide the Authority with a report in a form acceptable to the Authority that includes the following statutorily-required information: incomes of the tenants, the estimated economic and social benefits of the housing to the

immediate neighborhoods, the estimated economic and social benefits to the city or community, information with respect to displacement of lower income persons to the extent such occurs, together with steps taken by governmental or private parties to ameliorate the displacement and the results of such efforts, any additional information the Authority needs to report the extent of reinvestment by private lenders in the neighborhood resulting from the housing project, the age, race, family size and average income of tenants, and the estimated economic impact of the project, including the number of construction jobs created, wages paid, and taxes and payments in lieu of taxes paid.