Good morning. Thank you for this opportunity to share HUD's efforts to preserve its multifamily inventory of affordable housing. I am going to be sharing a lot of information so my talking points and comments will be available for your convenience. I hope you find this presentation helpful.

Also, I am not sure if we will have time for questions, so feel free to contact me at john.s.tedesco@hud.gov should you have any. We can also set up conference calls if necessary.

Here we go!

## Slide Two

HUD oversees more than 22,000 privately owned multifamily properties, and more than 1.4 million assisted housing units. These homes were originally financed with FHA-insured or Direct Loans and many are supported with Section 8 or other rental assistance contracts. As you know, HUD's existing stock of affordable rental housing is a critical resource for seniors and families who otherwise would not have access to safe, decent places to call home.

Properties at issue in assisted housing preservation were developed through various programs. Historically, HUD provided mortgage assistance or direct loans to owners through the Section 202 loan program and the Section 236 and Section 221(d)(3) Below Market Interest Rate mortgage insurance programs. HUD also subsidized tenant rents through programs such as the Rent Supplement program, the Rental Assistance Payment program, and the continuing Section 8 project-based rental-assistance program. In some cases, owners received both mortgage financing assistance and rental assistance.

In looking at the future, preserving properties for their affordability means successfully recapitalizing them using long-term rental assistance, improve and modernize properties through capital repairs, and stabilizing them by putting them on solid financial footing.

To make this possible, and also increase the useful life of properties, HUD encourages modernization, having owners consider using Low Income Housing Tax Credits, State, Local Grants, and lock in long-term rental subsidies that provide stable source of rental income.

Other efforts include:

- To encourage better cash flow owners may want to consider refinancing with available lower interest rates to reduce debt service costs and improve cash flow. With lower interest rate loans means less of a risk of default
- Have owners consider tapping into increased equity when a property is refinanced, freeing up income for improvements
- Owners may also possibly receive increased year-end distributions

## Slide Three

Preservation efforts includes housing originally financed through HUD's Section 202 and 811 capital advance programs with Project Rental Assistance Contracts. The Section 202 program funded the development of housing for elderly households. The Section 811 program provides funding to supportive housing designed for disabled, very, and extremely low-income persons.

The earliest Section 202 capital advance properties with project rental assistance contracts (PRAC) are now more than 20 years old. Many of these properties already have capital needs far greater than available capital resources. As capital needs grow with the age of the property, it has proven difficult for owners to build up enough reserves through modest rent increases to adequately fund the reserves for big-ticket replacements. As the country ages and the affordable housing stock is already inadequate for the rapidly growing population of low-income seniors, preservation of existing housing becomes all the more critical. A recent survey of the entire portfolio of 2,875 Section 202 PRAC properties indicates that many of these buildings will need major systems updates, energy saving upgrades, and up-to-date accessibility features, but lack the resources to address them. One study found that 37 communities in their Section 202 PRAC portfolio had an average per property need of $973,264, but Reserve for Replacement (R4R or reserves) totaling less than half of that. However, the nature of the capital advance (being a government-held forgivable grant) does not allow a 202 PRAC property or its sponsors to take on debt or leverage external financing to meet capital needs like other types of HUD-funded properties.

That changed in 2018 when HUD was given the authority to include 202 PRAC-supported properties in its Rental Assistance Demonstration (RAD) program – allowing some owners each year to leverage public and private debt and equity in order to make improvements and convert to Section 8 property based rental assistance or property-based voucher contracts. (Currently, there remains a cap on the number of units converting under this program) The option to convert to long-term Section 8 assistance under RAD provides an opportunity for recapitalization and extending the period the properties must remain affordable. The key here is the conversion of short-term subsidy contracts to long-term subsidy contracts. The longer-term contracts make new financing more possible, thereby facilitating the ability of PRACs with current shortfalls and/or demonstrable capital needs to leverage new capital.

HUD funding for FY 2021 now extends eligibility of RAD conversions to Section 811 Supportive Housing for People with Disabilities properties.

https://www.hud.gov/sites/dfiles/Housing/documents/H-2019-09-PIH-2019-23_RAD_Notice%20Rev4_20190905.pdf

This link to Notice H-2019-09 provides more information on the RAD program. I hope you find it helpful. According to HUD's webpage, Non-profit owners may make an initial submission of interest to undertake a conversion through the RAD Resource Desk at www.radresource.net. HUD will use this submission to discuss the conversion process and the owner's goals for the property. Please also keep your Account Executive apprised of your interest to participate in this program.

## Slide 4

For some time properties with a HUD 202/8 loan have been allowed to prepay:

- So as to enable refinancing for capital improvements and lower interest rates
- And enter into longer term Housing Assistance Payments (HAP)

Other benefits here include:

- Stable income stream
- Reduced processing time and paperwork

- Annual rent increases
- The potential to receive owner distributions
- HUD will consider subordination of debt when there are not enough refinancing proceeds for pay off, but rehabilitation is needed.

If in possession of a 202/8 please remember to make sure you understand your contractual obligations with HUD:

- Also review the existing 202 prepayment notice, HUD Notice 2013-17 to see prepayment requirements
- Owners must be in good standing with HUD requirements
- These include compliance with HUD or PBCA management reviews, REAC inspections, financial statements, and contractual agreements
- Get familiar with other HUD requirements by reviewing HUD's Section 8 Renewal Guidebook

## Slide 5

There are six options discussed in detail in the Section 8 Renewal Guidebook that I am going to focus on in this presentation.

Option 1 is Mark Up to Market (MUTM) and described in Chapter 3 of the Guidebook. This is a preservation tool where an owner can increase rents up to market rate levels, increase distributions, and renovate the property. This has proven to be an effective tool to recapitalize and continue providing affordable housing.

Option 1 is divided into two branches or forks which I will describe in a minute.

- This option is available at any time during your current contract term. Exceptions to this will be those HAP Contracts subject currently to Option 3 and Option 5
- Owners must agree to abide by a Preservation Exhibit, if applicable

(Preservation exhibits are used when HAP contracts are terminated early and time remaining is added to the new extended contract)

- Future rent increases are annual and based on Operating Cost Adjustment Factors
- New HAP Contracts will range from a minimum of five years to 20 years
- The submission of annual budgets to HUD and/or the PBCA are no longer required
- However, owners must submit a Rent Comparability Study every five years
- Access to increased distributions is now possible

Again, please remember owners and their properties must be in good standing with HUD.

Under Option 1 the ownership structure must be either:

- Profit Motivated
- A Housing Authority
- Be a Limited Partnership with non-profit general partners
- Be a Limited Liability Company with non-profit managers

No use restrictions may be in place. Examples of these include:

- Flexible Subsidy Assistance
- Low-income housing Tax Credits
- And the Green Retrofit Program administered by HUD's Office of Recapitalization

The first branch of Option 1 MUTM is Option 1A – Entitlement (Privilege)

- These are properties where an owner's Rent Comparability Study demonstrates comparable market rents are at or above 100% of Fair Market Rents
- Again, the property must not have a low and moderate-income use restriction that cannot be eliminated by unilateral action by the owner
- The property is not subject to a HAP Contract for moderate rehabilitation assistance
- There is no history of one or more tenants provided voucher assistance by a PHA after the HAP contract has been terminated

The second branch of Option 1 MUTM is Option 1B – Discretionary (Flexible)

- These are properties where HUD is given discretion to mark rents up to market not eligible under Option 1A
- These are properties housing a vulnerable population demonstrated by at least 50% of the assisted units rented to elderly families, disabled families, or large families defined as having five or more persons
- The 50% threshold can be inclusive of all categories of the described families

- The property must be located in a low-vacancy market area or in a rural area without comparable rental housing where there is a lack of affordable housing
- The property is a high priority for the local community. This can be demonstrated by showing HUD a contribution of State and/or local funds to the property. Evidence of community support may come in in the form of tax credits, tax abatements, or capital improvement funds that have been provided to the property within the last five years
- Owners who want to renew under the Capital Repairs Program or the Transfer Program may want to review Chapter 15 of the Guidebook as it outlines the procedure for providing HUD budget-based rent increases. This chapter identifies eligibility requirements for "marking up to budget" and provides instructions for future rent adjustments.

Option 2 of the Section 8 Renewal Guidebook (Chapter 4) focuses on those properties whose owners request a renewal of their Section 8 contract where the Rent Comparability Study indicates that the contract's current rents are at or below comparable market rents

- Under this option one to 20-year contracts available
- Rents are adjusted by OCAF or budget
- A Rent Comparability Study is required every five years
- Increased distributions are permitted if the owner is in good standing
- Are available to non-profit and profit entities
- One to 20-Year Section 8 Contracts are also available

Option 3 is the Mark to Market (M2M) portion of the Guidebook (Chapter 5) where contract rents are reduced to market levels. These are properties already subject to a Use Agreement.

Option 3A Lite renews the contract with rents at market levels without restructuring FHA loan debt on the property, a haircut if you will

- The reduced rents are based on a Rent Comparability Study
- The Section 8 Contract Renewal may not exceed 12 months

Option 3B Full entails a mortgage or rent restructuring and contract renewal with the rents marked down to market

- One to 20-Year Section 8 Contracts are available
- FHA loans will be restructured so as to match amortization using reduced rents
- Rents are adjusted annually using Operating Cost Adjustment Factors (only)
- An owner may not terminate this contract early for a different option
- And an owner must renew the contract up to the Use Agreement term

Option 4 of the Guidebook (Chapter 6) describes those "exception" properties that are exempt from debt restructuring under the Multifamily Assisted Housing Reform and Affordability Act of 1997 (MAHRA)

Properties exempt under MAHRA for debt-restructuring are:

- Those for which the primary financing or mortgage insurance was provided by a State or a unit of local government
- Originally financed under the 202/8 and 515/8 programs. However, if refinanced using FHA mortgage insurance they may be eligible for restructuring
- 202 and 811 PRAC properties
- SRO Mod Rehab properties as they have Section 8 contracts funded under the McKinney Act

Under Option 4 multi-year Section 8 contracts at both initial and subsequent renewal must have rents adjusted at the lesser of:

- Current rents as adjusted by the OCAF; or
- Budget based

This option also requires the submission of a Rent Comparability Study They are good for five years and will be adjusted annually using the applicable OCAF

Option 5 (Chapter 7) are for those properties whose owner participated in an early demonstration program with HUD and recorded a subsequent use agreement.

- There are not many of these properties in our inventory; but
- If the property has either a recorded Mortgage Restructuring Demo Program Use Agreement or a recorded Budget-Based Without Mortgage Restructuring Demo Program Use Agreement the Demo contract must be renewed under Option Five
- The owner is required to accept offers from HUD to renew the Section 8 contract throughout the term of the Demo Use Agreement. Therefore, an owner cannot opt-out of the contract.
- Section 8 contract renewals may have a minimum term of one year with a maximum term not to exceed the lesser of 20 years or the remaining life of the existing use agreement

Now I would like to circle back on Chapter 15, Mark-Up-To-Budget, of the Guidebook:

This option is designed to facilitate ownership transfers to nonprofit purchasers and/or capital repairs by nonprofit owners. Rents may be increased on a budget basis for acquisition and/or rehab costs, subject to a market cap. Pursuant to the Renewal Guide, HUD may approve rents at the "post rehab" rent level (the rent that the unit will be able to command in the market after repairs are completed). The post rehab rents will take effect when the rehab is complete. This option was originally only available to nonprofit purchasers and owners (which may include nonprofit controlled for-profit or limited dividend entities). Currently, for-profit owners may request a waiver in order to participate in a Chapter 15 renewal. Note that a nonprofit controlled partnership or LLC may elect to proceed under either Mark-Up-To-Market or Mark-Up-To-Budget.

Chapter 15 Eligibility Requirements, include:

- A nonprofit charter under State law, or in certain cases, a profit-motivated organization (if a waiver is provided by HUD)
- 501(c) tax-exempt status (except for limited-equity cooperatives or projects where such status was not previously required to participate in a HUD program)
- Financial solvency, with no unresolved audit findings

- A REAC score greater than 30 (for capital repairs) or greater than 60 (for transfers without capital repairs)

Additional requirements include:

- Previous ownership or management experience with affordable multifamily housing
- Community ties (a national or regional nonprofit must joint-venture with a local nonprofit, or secure majority tenant support)

Chapter 15 focuses on budget-based rent increase submissions that:

- Address needed repairs
- Increased replacement reserve contributions and/or debt service on a new rehab or acquisition loan
- Where all costs are budget-justified

Chapter 15 also discusses owner distributions, which HUD generally prohibits to nonprofit owners of subsidized properties. However, this limitation does not apply to nonprofit controlled limited partnerships or Limited Liability Corporations.

- Under Chapter 15, nonprofit owners may apply for a regulatory waiver to receive a distribution equal to 6% on initial equity, where applicable

The required Section 8 contract term under Chapter 15

- 20 years
- HUD also requires a Use Agreement that extends for 20 years beyond the term of any existing federal affordability restriction
- There are circumstances where HUD may consider terminating early already existing post-MAHRA contracts with a Mark-Up-To-Budget
- Where rehabilitation is scheduled, rents may reflect the post-rehabilitation market comparable rents (if greater than the current rents)
- Higher rents will not be effective until critical repairs (for moderate rehab) or the entire construction scope (for substantial rehabilitation requiring a construction loan) is completed. HUD may waive this limitation if the lender requires full debt service at closing
- During the contract term, rents will generally be OCAF-adjusted up to the OCAF-adjusted market rent cap. Rents will be re-adjusted to market (up or down) every five years based on the new RCS

- The tenant portion of rents in any non-Section 8 units may be increased no more than 10% in conjunction with the transaction
- Owners will need to prepare a Comprehensive Needs Assessment for HUD's review and approval
- The submission of a rent comparability study (RCS) with "as is" and "after rehab" rents
- Possibly an environmental review
- A source and uses funding statement
- A tenant relocation plan

Now I would like to take a moment to reflect on some key takeaways from this presentation revealing problems that could impede preservation efforts

## Slide 6

- Required documentation is not submitted in a timely manner
- The submission is incomplete or inaccurate
- There is a lack of communication with HUD and the Contract Administrator (PBCA)
- Not familiar with contractual agreements
- Funding from HUD Headquarters
- Processing time for HUD and the owner to complete and/or review rent comparability studies

Please remember, HUD signs last on all documents. So make sure the PBCA, where applicable, is involved in all initial and subsequent discussions.

## Slide 7

Now I would like to end with an overview describing HUD's efforts to preserve a senior housing property in Eugene, Oregon. A property called Ya-Po-Ah Terrace.

Ya Po Ah means very high place in the language of the Kalapuya Indians who inhabited the area before the arrival of European and American settlers.

The property was originally sponsored by the Evergreen Union Retirement Association (EURA, a volunteer-led nonprofit founded by workers in the building trades to provide affordable housing for seniors on fixed incomes.

A $65 million renovation project was put together to bring Ya Po Ah, originally built in 1968, up to current accessibility and seismic codes, replace worn-out building systems and improve energy efficiency.  Specifically replacing the building's curtain wall and windows, potable water systems, and upgrade HVAC to individual heat and air conditioning units in each apartment.

Federal rent subsidies that cover 210 of the 222 apartment units were  renewed, keeping Ya Po Ah affordable to very low-income seniors for an additional 20 years.

To reach funding goals for this major renovation project, the sponsor had to structure the financing into two limited partnerships, creating 2 condo units in the building.  YPA Condo A (floors 4-10) applied for and was awarded 9% LIHTC funding for the 109 units from Oregon Housing and Community Services (OHCS). YPA Condo B (floors 11-18) received 4% LIHTC funding for the 112 units also through OHCS.

To achieve the funding levels for this project, it was necessary to seek and secure various partners. Funding partners include HUD, OHCS LIHTC and other programs, FHA Loans, PNC Bank as Tax Credit Partner, the City of Eugene CDBG funds and a Eugene Water and Electric Board (EWEB) grant.

These transactions involved collaboration between HUD Production, Asset Management, CPD, OGC, and the City of Eugene and the early conversations about bifurcation of the HAP, relocation, environmental, and the condo structure set these transactions up for success.

Well, that concludes my presentation.  Again, I hope you find it helpful and encouraged interest in the preservation of affordable housing.  These efforts involve transactions that are lengthy and complicated, so please make sure you involve HUD early in the conversation to help ease the process.

Thank you.