

Contents

I. Feature:

Looking Locally for Lower-cost Credit Enhancement

II: Senior Living:

Why Refinance?

III: Health Care:

An Option for the Ages

IV: Affordable Housing:

Financing Affordable Apartments in Today's Economic Climate

V: The Nonprofit Minute:

ESP for Asset Allocation: Efficient, Strategic, Purposeful

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Affordable Housing

by Ginger McGuire

Financing Affordable Apartments in Today's Economic Climate

The USDA Rural Development 538 loan program has been a very effective source of guaranteed funding for multifamily properties in rural areas. For this reason, many of us were caught off guard earlier this year when Congress passed and the President signed the 2009 Omnibus Appropriations Bill, which included a provision eliminating interest rate subsidy on new 538 loans. It was this 250 basis point reduction on the first \$1.5 million in debt that made the program so compatible with low-income housing tax credits.

Following the Appropriations Bill, Rep. Shelley Moore Capito of West Virginia introduced HR 1989; a bill that would allow a portion of the 538 money already appropriated in 2009 to be shifted from guarantee funds to subsidy money and to be used for interest rate credit assistance. Rep. Lincoln Davis of Tennessee has cosponsored HR 1989, giving us hope that the interest credit may be restored in the second half of 2009.

Just when things looked promising however, the Administration sent the President's budget request to Congress for 2010 program investment levels and to our surprise, the interest rate subsidy was not included in the President's budget for 2010. In a climate where funding is hard to come by, many developers have begun to look elsewhere for permanent loan sources to finance rural properties.

The President's 2010 budget request is overall extremely supportive of affordable housing finance programs. For example, the budget is requesting \$1 billion from Congress for the National Housing Trust Fund, the first major new housing production program in the past two decades. The Trust Fund, along with stimulus funds from ARRA, should alleviate some of the need for gap funding created by lower prices for tax credits on the equity side, and stricter underwriting standards by



Affordable housing renovations cannot always wait for optimal market conditions, but being familiar with the options can help you move forward.

The Capital Issue: Affordable Housing

most lenders on the debt side.

As the economic climate changes, and as the new Administration places emphasis on different programs, developer/owners are reviewing their financing choices. Below is an overview of the various debt programs that Lancaster Pollard believes are viable financing vehicles for affordable multifamily housing in the next year:

All Geographic Areas

FHA 221(d)(4): The “d-4” insured loan program is a multifamily new construction or substantial rehabilitation program for market rate, moderate-income and affordable housing properties. The maximum loan amount for new construction is the lesser of 90% of estimated replacement costs or the amount supported with a 1.11x debt service coverage. The loan term and amortization is 40 years plus the construction period. The interest rate on d-4 loans is fixed for both construction and permanent phases, removing interest rate risk which makes the d-4 an attractive option for many developers in today’s low interest rate environment. Prevailing wages are required.

FHA 223(f): The 223(f) insured program provides funding for refinancing or acquisition of apartment projects, or for seniors independent living projects. Historically, only projects that are at least three years old were eligible, however, during this economic period, this rule has been waived, making the 223(f) a great program for construction loans or “mini-perm” loan take-outs. Up to 85% of the value can be loaned, and terms of up to 35 years are available.

Fannie Mae: Fannie Mae has permanent loan programs specifically tailored to Low Income Housing Tax Credit and other affordable properties. This includes a forward rate lock option for construction projects, which allows the rate to be locked on the permanent loan up to 3 years before it is actually made. In addition, Fannie Mae has an immediate delivery option for permanent loans on stabilized projects. Fannie Mae loans are generally set with a maximum as the lesser of 80% loan to value or a 1.25x debt service coverage. The loan term is generally an 18-year term with up to 30

years amortization. In addition, the processing time for Fannie Mae loans will generally be quicker than most government programs. Fannie Mae offers a good alternative when processing time is an issue or prevailing wages are detrimental to a project.

Rural Properties

USDA/RHS 538: Even without the interest credit subsidy, the 538 may be a viable funding source for some properties in rural areas because even at market rate, the program allows a 40-year amortization and loan term. According to Rural Development staff in Washington, projects borrowing more than \$5 million in debt are experiencing little difference to the bottom line with no interest credit subsidy, as the subsidy applied only to the first \$1.5 million borrowed. In addition, construction financing can be accessed without triggering prevailing wage requirements, which can be very attractive in these markets.

USDA/RHS B&I Loan: The Business and Industry Loan Guarantee program guarantees loans made by eligible lenders to rural businesses. When apartments are not restricting rents to low-income households (in other words, market rate), the B&I Loan can be used in some circumstances to finance apartment buildings in rural areas of 50,000 population and less. The loan may be used for acquisitions, construction, conversion, expansion, repair modernization or development costs. The maximum loan term and amortization period is 30 years and the interest rate is market determined and negotiated with the participating lender.

Though changes to the USDA 538 program have made it a less viable option for some developers, the other programs that exist to develop, acquire or renovate affordable and rural affordable housing will continue to provide the resources necessary to maintain and hopefully grow the housing stock. Lancaster Pollard Mortgage Company, as a USDA, FHA/HUD and Fannie Mae Multifamily Special Affordable and Seniors Housing lender/servicer, can provide access to and unbiased evaluation of each of these options as they apply to individual borrowers. We will continue to advocate for the affordable housing sector.