



2014 LEGAL SEMINAR

RAD Conversion and Rehabilitation using LIHTC: Key Considerations for PHAs

By Delphine G. Carnes

Crenshaw, Ware & Martin, P.L.C.

WHY RAD?

- **Enormous backlog in needed renovations to public housing units**
- **Insufficient federal funding**
 - HOPE VI and CNI are no longer available. May never come back
 - Capital Funds are not sufficient
 - Public Housing Operating Fund and Capital Fund subsidies are decreasing. HAP funding is more stable
- **Administrative burden of HUD process for public housing units**
- **Long term HAP contract provides stability that lenders and investors like to see**
- **Streamlined review and approval process for RAD conversion (compared to mixed-finance)**
- **RAD is one of the only tools currently available to PHAs to preserve, renovate or upgrade affordable housing units**

HOW DOES IT WORK?

- **Convert public housing units to a HAP contract (PBV or PBRA)**
- **The units are treated more like privately-owned property**
 - Property income is unrestricted
 - Easier for Lenders to understand and underwrite
- **Flexibility to leverage public and private sources of funds**
- **Rents adjusted annually by OCAF (Operating Cost Adjustment Factor)**

RAD MILESTONES

After issuance of commitment to enter into a Housing Assistance Payments (“CHAP”)

- **Within 30 days:** a) lender engagement or commitment letter; and b) statement of capacity of development team
- **Within 60 days:** a) significant amendment to Annual/Five Year plan; and b) election to convert to PBV or PBRA
- **Within 90 days:** a certification from PHA that all lender due diligence –including a physical condition assessment (“PCA”) and environmental reports –has been completed; and the PCA must be submitted to HUD
- **Within 150 days:** a certification from PHA that all applications for firm commitments have been submitted (note: for FHA-insured deals, this is the Firm Commitment Application)

RAD MILESTONES, continued

- **Within 180 days:** the Financing Plan must be submitted to HUD
- **Within 270 days:** HUD will issue RAD Conversion Commitment; Owner has 30 days from date of issuance to execute and return to HUD
- **Within 320 days:** submit a firm commitment for all financing
- **Within 360 days:** financial closing and execution of the HAP contract
- **Within 12-18 months:** after issuance of HAP contract, completion of work

ADDING LIHTC TO THE RAD PROCESS

- **LIHTC is a key component if substantial rehabilitation is needed**
- **The property may not qualify for large enough loan/may not be able to generate enough cash flow for debt service**
- **If the existing units have low contract rents/high expenses and need substantial rehab, 9% LIHTC may be the only way to finance the renovation**
- **Opportunity to earn a developer fee**

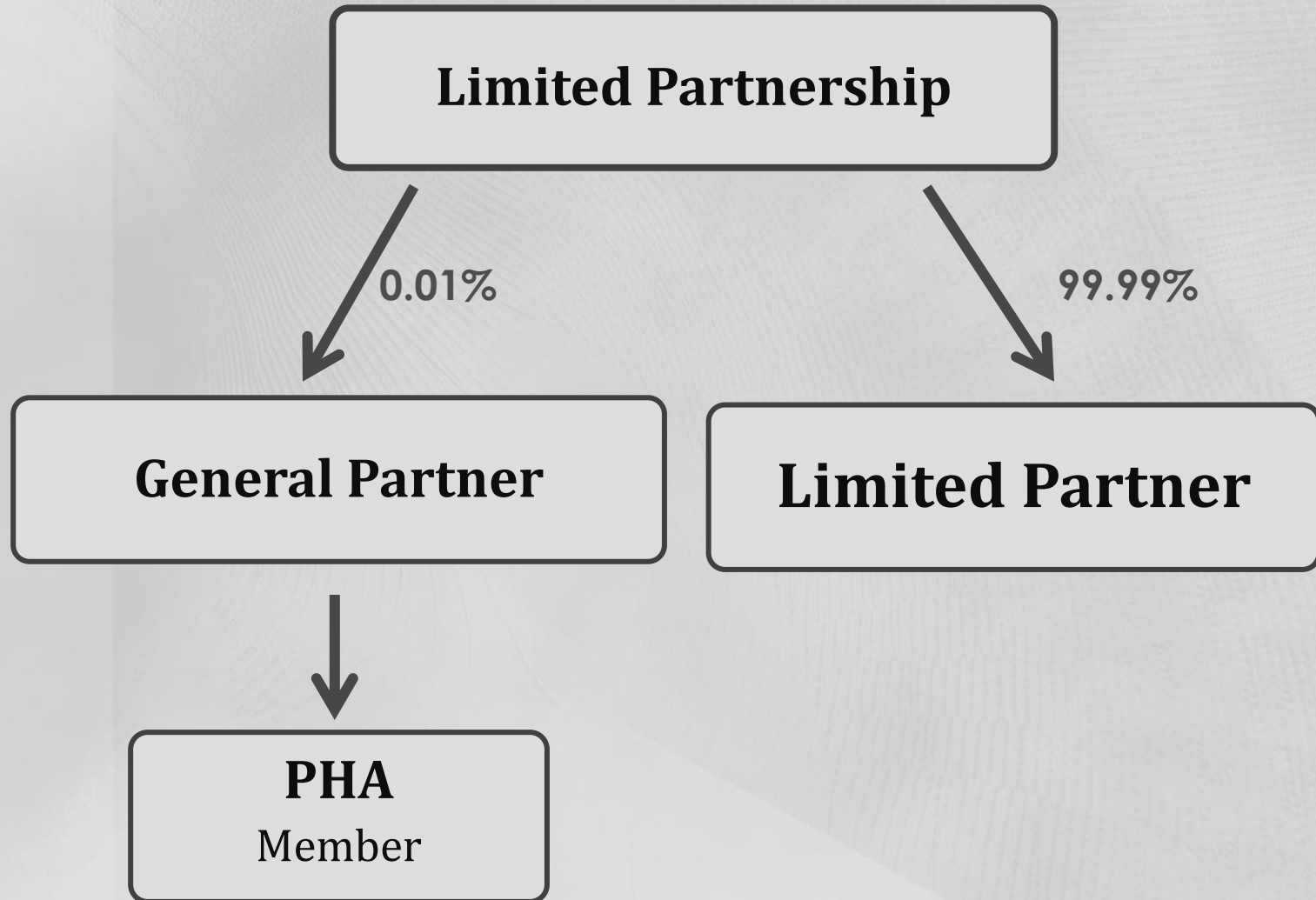
ADDING LIHTC TO THE RAD PROCESS, Continued

- **9% LIHTC are the best you can get**
 - More equity
 - But much more competitive
- **4% LIHTC with Tax-Exempt Bonds**
 - Less equity
 - Easier to obtain (bonds are competitive but 4% credits are automatic)
 - More complex financing structure
 - Higher closing costs

OWNERSHIP STRUCTURE IN LIHTC TRANSACTIONS

- **Owner of the units will be a for-profit entity (limited partnership)**
- **Tax credit investor will be the limited partner and will typically own 99.99% of the entity**
- **PHA must have some control over the limited partnership**

OWNERSHIP CHART for LIHTC TRANSACTION



POTENTIAL ROLES FOR THE PHA

- **PHA can maintain ownership of the land. Ground lease to the limited partnership**
 - Ground Lease Payments
- **PHA can sell the land to the limited partnership**
 - Seller financing
- **PHA can provide subordinate financing, secured by a lien on the units**
 - Financing fees/debt service
- **PHA can serve as sole developer, or co-developer**
 - Opportunity to earn a developer fee

POTENTIAL ROLES FOR THE PHA, continued

- **PHA will generally be a member (or the sole member) of the general partner entity**
 - Cash flow
- **PHA can serve as property manager**
 - Opportunity to earn a property management fee
- **Right of first refusal for sale of the property**
- **Fees earned by the PHA are unrestricted funds**

PARTIES TO THE TRANSACTION

- **Developer**
- **Lender**
- **LIHTC investor**
- **VHDA**
- **Residents**
- **Consultant, General Contractor, Architect, Engineer, Title Company, Locality, Attorneys, Accountants**

INVESTOR CONSIDERATIONS

- **Price per credit matters, but is not the only concern**
- **Investor familiarity with PHAs**
- **Guaranties (construction completion, operating deficit and recapture)**
- **Investors tend to require a developer with LIHTC experience**
- **Investors/their counsel will review all contracts and loan documents. May require Riders**

CHOOSING A LENDER

- **Experience with PHAs**
- **Familiarity with HUD and with RAD. Lack of familiarity with the process may result in delays and increased costs**
- **Underwriting, DSCR requirements and due diligence**
 - **Timeline**
 - **Costs involved (lender's legal fees, third party reports such as environmental reviews)**
- **Investor will want to approve the loan structure and loan documents**
- **Note: FHA financing can be used in conjunction with RAD (Section 223(f) for refinancing or acquisition with minor repairs; Section 221(d)(4) for substantial rehab; Section 223(f) LIHTC Pilot Program for rehab up to \$40,000 per unit). This presentation does not focus on FHA financing.**

CHOOSING A CONTRACTOR

- **Price matters but is not the only concern**
- **Low bidder may be a company that submits a plethora of change orders**
- **Experience with PHAs**
- **Experience with LIHTC process and ownership structure**
- **Investor will want some input on the contractor selection, construction contract and insurance coverage**

RESIDENT RIGHTS

- **Any displacement of existing residents for more than 1 year requires compliance with the Uniform Relocation Act**
- **Existing residents who are temporarily relocated during construction must have the right to return**
- **Rehab Assistance payments provided by HUD to assist with relocation costs**
- **RAD does not allow screening of existing residents who have a right to return**
- **Investor will review and approve the form of lease**
- **Owner entity must sign Consolidated Owner Certification stating that residents had 30 days advance notice**
- **New leases for existing residents must be signed prior to the effective date of the HAP contract**

ADDITIONAL ITEMS TO COMPLETE PRIOR TO CLOSING

- **Obtain Closing Checklist from RAD Resource Desk at <http://radresource.net>**
- **Various forms required under the RAD Closing Checklist are also available from the Resource Desk**
- **complete on-line Registration and Form HUD-2530 Clearance – if required**
- **Obtain a DUNS number and register in SAM (System for Award Management – Government Contract Registration). The DUNS number will be received by e-mail and instructions regarding SAM registration will be provided**
- **Obtain WASS (Web Access Security System) ID and/or access to Multifamily HUD Systems**
- **Complete and submit application for Inventory Removal (at CHAP assignment)**

CONCLUSION

- **RAD can be a good tool, combined with LIHTC, to help finance substantial rehab**
- **Complete re-do or “gut rehab” and new construction will necessitate higher debt**
- **RAD does not always work. Run the numbers carefully**
- **Use all funding sources available: Replacement Housing Factor (RHF) Funds, reserves, HOME, CBDG, AHP, grants, senior and subordinated debt . . .**
- **Select your partners carefully**
- **And, as always, be creative, persistent and patient!**

Delphine G. Carnes
dcarnes@cwm-law.com

CRENSHAW, WARE & MARTIN, P.L.C.

150 W. Main Street, Suite 1500

Norfolk, VA 23510

T (757) 623-3000 | F (757) 623-5735