U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
WASHINGTON, DC 20410-8000

ASSISTANT SECRETARY FOR HOUSING-
FEDERAL HOUSING COMMISSIONER

DATE: October 16, 2007

MEMORANDUM FOR: Multifamily Housing HUB and Program Center Directors, Operations Officers

FROM: Ellen R. Connolly, Acting Director, Office of Multifamily Development

SUBJECT: Interim Guidance for Subsidy Layering Reviews

The Department is in the process of reissuing a new notice with revised instructions for Subsidy Layering Reviews (SLRs) and that notice is currently in Departmental Clearance. This memorandum provides interim guidance for processing SLRs and is effective until publication of the new notice.

PURPOSE

The Department's intent is to simplify the SLRs procedures for HUD staff performing SLRs pursuant to Section 102 of the Department of Housing and Urban Development Reform Act of 1989. These procedures will assist Housing Development staff in streamlining the instructions to follow when processing mortgage insurance applications together with HUD Housing Assistance (HHA) and Other Government Assistance (OGA), especially Low Income Housing Tax Credits (LIHTCs). HUD's Section 102 SLR requirements and Section 911 procedures are set forth in this memorandum. These instructions supersede implementing instructions for Sections 102 and 911 SLRs referenced in Housing Notice H 95-4.

EFFECTIVE DATE

Current HUD applications that have not obtained a firm commitment and require a Section 102 SLR should follow these streamlined procedures. All future HUD applications must follow these Section 102 SLR instructions. Housing Finance Agencies (HFAs) issuing Section 911 SLRs should follow requirements outlined in their executed Memorandum of Understanding (MOU) with their local HUD field or program office.

BACKGROUND

Section 102 of the Department of Housing and Urban Development Reform Act of 1989 requires all projects receiving HUD Housing Assistance (HHA) combined with any form of Other Governmental Assistance (OGA) to undergo a Subsidy Layering Review (SLR). This review certifies no overlap of government subsidies when combining HHA (programs administered by FHA-Housing) with other forms of federal funds when administered by Federal, State, or Local agencies. HUD must review the project's federal subsidy layers and certify there is "no more assistance than is necessary to provide affordable housing." Congress subsequently passed Section 911 of the Housing and Community Act of 1992, which was then amended by Section 308 of the Multifamily Housing Property Disposition Reform Act of 1994. These two pieces of legislation permitted HUD to delegate SLR authority to Housing Credit Agencies (HCAs) or Housing Finance Agencies (HFAs) where LIHTCs are involved in the transaction.

Due to the Department's acknowledgement that HFAs perform their own subsidy layering reviews pursuant to Section 42(m)(2) of the Internal Revenue Code of 1986, the Department developed a MOU that merged the requirements of Section 911 with the IRS Section 42 Code requirements, which HFAs are following in the allocation and administration of the LIHTC program. In order for HFAs to perform the Section 911 SLRs, the State agency must enter into a MOU with their local HUD field or program office.

For projects located in States where the local HCA or HFA has not entered into a Memorandum of Understanding ("MOU"), the local HUD field office must complete the Section 102 SLR. These instructions are intended for both the Multifamily Accelerated Process (MAP) and the Traditional Application Process (TAP).

A. IDENTIFY POTENTIAL OVERLAPPING PROJECT USES

Multifamily housing subsidies are limited resources, so government agencies must administer subsidies they control as efficiently and productively as possible. All certifications of compliance with Section 102 must be supported by a comprehensive project sources and uses. The sources and uses must demonstrate that there are no overlapping uses generated by the combination of HHA and OGA.

Examples of HHA:

1. FHA insurance[1]
2. Section 202/811 Capital Advance Programs
3. Project-based Section 8 rental subsidies
4. IRP-supported rehabilitation loans

[1] Insured loans represent the greatest amount of "debt-related" HHA, and when combined with LIHTCs is the primary focus of SLRs demanding the highest scrutiny.

Examples of OGA:

1. Low-income housing tax credits (LIHTCs) [2]
2. Historic Tax Credits
3. New Market Tax Credits
4. Other federal funds administered by state or local governmental agencies

B. MAXIMUM INSURABLE MORTGAGE

In cases involving HUD mortgage insurance, staff must calculate HUD's maximum insurable mortgage before completing the SLR. Staff will utilize HUD Form 92264-A, Supplement to Project Analysis in order to determine the maximum insurable mortgage. The maximum insurable mortgage is limited by the HUD program and the lowest criterion calculation.

Staff will follow the Form HUD-92264-A, maximum insurable mortgage criteria instructions. When tax credit equity, secondary loan funds, grants, replacement reserves or gift funds are included in the project's financing plan, staff must complete Criterion 11. Criterion 11 instructions are included in the FAQ(s) and the MAP Guide Revisions of Chapter 8 published on 10/07/03, 12/19/03, 1/14/04 and 5/08/07.

C. SUBMISSION REQUIREMENTS

In determining compliance with HUD's subsidy layering requirements, staff should review the submission documents before the issuance of the firm commitment and again at the time of cost certification. After the review and acceptance of the submission documents, the initial Section 102 certification will be executed by the Hub Director or Program Center (PC) Director. If any financing changes have been approved during processing, a final SLR will be completed at time of cost certification.

In order to complete the SLR and issue a Section 102 certification, the following documents must be included in the application submission package for firm commitment and forwarded to the local HUD PC.

1. <u>Sources and Uses Statement</u>. The sponsor is required to submit an initial detailed sources and uses statement that reflects the project's total development budget in conjunction with HUD's issuance of its firm commitment. The statement should include:

   All proposed sources (both public and private) of funds and the dollar amount(s) for each respective source, and

   All uses of funds (including acquisition costs, rehabilitation or construction costs, financing costs and professional fees) associated with the project.

[2] LIHTCs represent the greatest amount of "equity-related" OGA, and when combined with insured loans is the primary focus of SLRs demanding the highest scrutiny.

A reconciliation of HUD's mortgageable costs and other secondary financing or equity (non-mortgageable costs) to the State HFA's total development budget.

2. Applicant/Recipient Disclosure/Update Report (Form HUD-2880).

3. Copy of all secondary financing/equity commitments, letters of intent, bridge loan agreements, LIHTC reservation/allocation letters, Limited Partnership Agreements, Limited Liability Partnership Operating Agreement including all amendments, attachments and exhibits.

4. Form HUD-92264-A, Supplement to Project Analysis.

5. Form HUD-92264-T, Rent Estimates for Low/Moderate Income Units.

6. Additional documentation, as may be requested by the HUD field office for the completion of the SLR.

D. REVIEW OF SUBMISSION DOCUMENTS

1. Sources and Uses Statement Review. The project application package submitted to the local Hub or PC office must include a detailed and balanced sources and uses statement or total development budget. The sources and uses statement or total development budget will include HUD's non-mortgageable and mortgageable costs. The HFA's sources and uses statement or development budget may differ from HUD's sources and uses statement as both agencies may have different limitations on development budget line items. The HFA's development budget will reflect a sources and uses statement with eligible basis versus non-eligible basis. Eligible basis meaning qualified costs for determining the maximum allowable allocation of tax credits. A reconciliation of these development budgets should be reviewed to ensure no overlap of sources or uses.

   Review the uses portion of the statement making sure that appropriate documentation has been provided for each development use. Identify those costs approved as mortgageable costs and costs not recognized in HUD's normal processing procedures. Identify the sources and uses for non-mortgageable items not included on HUD's processing forms. Supporting documentation must be provided on each development use, so the reviewer may distinguish HUD's recognized development costs from those paid from tax credit equity or other sources. The sources and uses statement should be in a format that discloses total development costs and the breakdown of those costs into HUD mortgageable and non-mortgageable costs. The non-mortgageable costs must be paid from tax credit proceeds or other funding sources. Review the uses to determine if the costs are reasonable.

   A total of the HUD mortgageable and non-mortgageable costs should equal the total development cost. In Section 102 SLRs, HUD will reduce the applicable assistance within its control to balance the sources and uses, through such methods as reducing the maximum insurable mortgage (MIM). If any overlap of sources or uses of funds is identified, HUD staff should initiate a discussion with the sponsor or lender to determine which source and/or use should be reduced or deleted while sustaining the financial feasibility of the project.

Initial tax credit equity is based on tax credit rates published monthly under Section 42(b)(2) of the Internal Revenue Code (IRC). Sponsors have the option to lock in a tax credit rate at time of allocation or float the rate until the project is placed in service. Tax credit rates will fluctuate monthly and will determine the final amount of equity committed to the project. During HUD processing, tax credit equity may increase or decrease until the tax credit rate has been selected by the sponsor or the project has been placed in service for occupancy. At time of cost certification, final proceeds of equity or other sources may differ slightly from the initial SLR because of interest rate fluctuations. As stated previously, HUD's development budget also may differ from the HFA's development budget, because both agencies recognize and approve different limitations on specific development line items.

2. Applicant/Recipient Disclosure/Update Report (Form HUD-2880). Sponsors must complete and submit this form along with the project's sources and uses statement. The form requires the sponsor to provide information about the OGA assistance being provided, identify interested parties to the transaction and certify to the accuracy of the information being provided. The form must be reviewed to determine consistency with the sources and uses statement. The form must be properly executed by the submitter. Throughout the HUD application process, any changes to the original Form HUD-2880 must be updated and resubmitted to the local Hub or PC office.

3. Review all reservation/commitment letters for secondary sources of financing, including terms and conditions for all mortgages, grants, subordination agreements and bridge (interim) loans. Review the financing structure of the federal and/or non-federal sources; determine if there are any restrictions on funding certain development line items (i.e. land costs).

   Review partnership agreements to determine the amount of tax credit equity to be provided, the timing of equity disbursements, the amount and term of developer fee, and any interim construction loans provided by the partnership.

4. Form HUD-92264-A. Complete the form using all appropriate Criteria. Depending on the type of HUD application process, the FHA lender or HUD mortgage credit staff will complete HUD Form 92264-A.

5. Form HUD-92264-T. Applicable maximum affordable rents for LIHTC units are determined by household size assuming occupancy of 1.5 persons per bedroom. Efficiency units have income limits based on an occupancy limit of one person.

In order for a household to qualify as a tax credit unit, they must have a household income at or below the program income limit for their respective household size. The calculation of the maximum affordable rent for a tax credit unit is based on the tenant(s) paying no more than 30 percent of their gross monthly income for rent. The HUB or PC, in conjunction with the lender's appraiser and market analyst as applicable, and in consultation with EMAS must assure there is sufficient demand for the tax credit units at the proposed rents.

6. Additional Documentation. After reviewing the secondary financing/ equity commitments, letters of intent, LIHTC reservation/allocation letters and other requested documents, there may be a reference to another document not previously submitted with the original HUD processing package. If there is a concern that the document may conflict or modify information or financing already obtained, contact the sponsor for additional information.

E. DEVELOPER'S FEE

Section 231 and Section 221(d) (4)

When LIHTCs are used as a source, the subsidy layering review will limit the maximum developer's fee to a combination of Builder's and Sponsor's Profit and Risk Allowance or Sponsor's Profit and Risk Allowance (BSPRA/SPRA) in the insured mortgage and the tax credit developer's fee funded outside of the FHA insured mortgage. The combination of these fees may not exceed 15 percent of the acceptable development costs as defined by the State's Qualified Allocation Plan (QAP). (See Memorandum to Hub Directors and Community Builders dated 09/23/99).

Section 223(f)

Developer's fee or BSPRA/SPRA fees are not allowable costs for calculation of the maximum insurable mortgage. If tax credits are reserved or allocated to the project, developer fee will be included in the HFA's development budget. The developer fee in those cases should be limited to the 15 percent of the acceptable development costs as defined by the State's QAP.

F. RISK-SHARING PARTICIPANTS

If the HFA has not entered into a MOU with HUD, the local PC will be responsible for the SLR. Section 542 (b) Level I and Level II approved participants and Section 542 (c) participants of FHA's risk-sharing insurance program will submit a detailed sources and uses development budget to the local PC before initial closing. Any changes from the development budget after initial closing will require another SLR at time of cost certification.

G. SUBSIDY LAYERING REVIEW APPROVAL

The Hub or PC Director will review the sources and uses statement to ensure "no more assistance than is necessary" is provided to the project for the purposes of completing the SLR process.

Upon completion of an acceptable SLR, the Hub or PC Director will certify and execute the following document:

A signed Section 102(d) certification (Attachment 1) with a balanced final sources and uses statement or development budget.

H. COST CERTIFICATION AND FINAL CLOSING

1. A final SLR will be required if additional sources not previously considered are involved; if an increase/decrease to any other funding source occurs; if a mortgage increase has been requested; if construction costs decrease by more than two percent (2%). If required to determine the final approved development budget, the HUD field office may request a copy of the HFA's final audited tax credit development budget submitted by the sponsor's accountant. The final audited tax credit development budget may have housing development items not included in HUD's final development budget. These items would have been funded from tax credit equity or other secondary sources. A detailed cost certification review is required for all programs except for Section 223(f), in which a simplified cost certification will be submitted.

2. If a mortgage increase is requested, sponsors must resubmit the documents set forth in paragraph C. Submission Requirements, in addition to the MAP/TAP instructions to process a mortgage increase. A final SLR will be conducted when the determination for mortgage increase has been finalized by the Hub or PC.

3. In cases where the mortgagor has not requested a mortgage increase, no other funding sources have changed or no additional sources or uses have been identified; a final SLR will not be required.

I. RETENTION

The Hub or PC Director will retain copies of the Section 102 certifications with the corresponding detailed sources and uses statements for each case file. A copy of these documents will be forwarded to the Washington-Headquarters Docket files.

State HFAs or HCAs will submit executed copies of the Section 911 certifications with the corresponding detailed sources and uses statements for each case file to their local HUD field office.

Questions regarding this memorandum may be directed to Joe Sealey, Division Director, Technical Support, Office of Multifamily Development at 202-708-1142.

Attachment 1

SECTION 102(d) CERTIFICATION
REGARDING THE AMOUNT OF HUD ASSISTANCE
PROVIDED FOR PROJECTS UTILIZING LOW-INCOME
HOUSING TAX CREDITS AND/OR ANOTHER FORM OF
OTHER GOVERNMENT ASSISTANCE

Pursuant to Section 102 of the Department of Housing and Urban Development-Reform Act of 1989, regulations at 24 CFR Part 4, and the Revised Subsidy Layering Review Standards, all of which address the prevention of excess project "subsidy layers," I certify that the assistance provided by the U.S. Department of Housing and Urban Development to:__(project number)__, located in ____________________________, is not more than is necessary to provide affordable housing after taking into account other government assistance, including low-income housing tax credits. This certification is based on an/a ___initial/final____ review of the sources and uses development budget contained in Multifamily Housing files and which is available for inspection in the ____HUD field Office.

______________________________________ ____________________
Hub or Program Director Date

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Official Record Copy U.S. Department of Housing and Urban Development form HUD-713.1 (02/03)
Previous edition is obsolete.