INDIANA HOUSING & COMMUNITY DEVELOPMENT AUTHORITY

American Recovery and Reinvestment Act of 2009

Section 1602 - Tax Credit Exchange Program

June 15, 2009 DRAFT GUIDANCE FOR PUBLIC COMMENT

OVERVIEW

The American Recovery and Reinvestment Act (ARRA) created two provisions to enhance the Section 42 Rental Housing Tax Credit program:

- $2.25 billion for Tax Credit Assistance Program (TCAP), and
- The ability for housing agencies to exchange certain allocations for cash from the Treasury (Section 1602 Exchange).

The Indiana Housing and Community Development Authority (IHCDA) will administer distribution of the state's Exchange funding pursuant to these Development Selection Process and Criteria.

I. INTRODUCTION

The purpose of the Section 1602 Exchange program is to create and save jobs and increase the affordable housing supply by using the appropriation to start construction on shovel-ready developments. The Section 1602 Exchange program is expected to address funding gaps created by diminished investor demand for rental housing tax credits.

IHCDA intends to offer the Section 1602 Exchange program to rental housing tax credit participants to enhance development strength and encourage investment from traditional syndicator and investor sources.

IHCDA anticipates exchanging one hundred percent (100%) of the unused 2008 per capita credit carried forward to 2009 and forty percent (40%) of the 2009 per capita credit. Midwestern Disaster Credits cannot be exchanged. The Exchange would result in approximately $164 million funding availability.

Midwestern Disaster Area Counties:

Adams	Bartholomew	Brown	Clay	Daviess	Dearborn	Decatur
Gibson	Grant	Greene	Hamilton	Hancock	Hendricks	Henry
Huntington	Jackson	Jefferson	Jennings	Johnson	Knox	Lawrence
Madison	Marion	Monroe	Morgan	Owen	Parke	Pike
Posey	Putnam	Randolph	Ripley	Rush	Shelby	Sullivan
Tippecanoe	Vermillion	Vigo	Washington	Wayne		

IHCDA's ability to commit or close Section 1602 Exchange awards will be subject to funding availability and further guidance by Treasury. IHCDA's policies and procedures are subject to revision based on changing circumstances including additional federal guidance. IHCDA will announce and publicize revisions using Multi-Family Notices on http://www.in.gov/ihcda/2520.htm

Terms used in the Section 1602 Exchange Criteria will have the same meaning as under IRS Code Section 42, federal regulations, the 2009-2010 Qualified Allocation Plan (QAP), Treasury's "Grantee Terms and Conditions", and legal agreements between the Agency and Owners.

IHCDA will utilize IHCDA approved Financial Service Agents (FSA) for developments that exchange one-hundred percent (100%) of their credits for Section 1602 funding. FSAs and/or other approved entities will be designated to conduct the asset management requirements of the Section 1602 Exchange program.

II. DEFINITIONS

Applicant: An Applicant is a recipient of a 2008, 2009, or 2010 reservation of LIHTC.

Award Agreement: All agreements evidenced by closing documents among the owner of the Development and IHCDA. These also include any extended use agreements.

Construction Completion: Defined as when all of the following are complete:

(i) lien-free completion of construction of the Project in accordance with the approved plans and specs sufficient for all residential rental units to be "placed in service" within the meaning of the Code; and

(ii) issuance of all permanent certificates of occupancy permitting immediate occupancy of all residential rental units (if required by the governing municipality); and

(iii) Architect's Substantial Completion Certification that the Project is completed in accordance with the plans and specifications; and

(iv) receipt by the FSA of a certification by the Owner that the representations and warranties contained in the Award Agreement are true and correct as of the date of the request.

Financial Forecasts: FSA approved Financial Forecasts shall be attached to the Award Agreement at the time of closing of the Award Money.

Section 1602 Exchange Funds: The funds provided by IHCDA to a Partnership under the Section 1602 Tax Credit Exchange and Assistance Program.

Owner: The General Partner, Managing Member or any other approved principal of the Project Property Partnership or Company.

Project Property Partnership or Company: The partnership, LLC, or any other approved entity that owns the Project.

Stabilization: Is defined as the later to occur of the following:

(i) breakeven operations, which is defined as 90% occupancy for 90 days at underwritten rents and expenses as determined by the FSA,

(ii) conversion of all construction financing to permanent financing (if applicable),

(iii) FSA's receipt and approval of the third party review of all of the first year's tenant files for compliance with the Code and State requirements at a Partnership cost not to exceed $50 per file, which cost will be borne by the Project Property,

(iv) 100% of the LIHTC units have been qualified with tenants pursuant to the Code

(v) FSA's receipt of an annual owner certification by the Owner that the representations and warranties contained in the Award Agreement are true and correct as of the date of the request of funds.

III. APPLICATION AND EVALUATION

A. Threshold Eligibility

1. The development must have an award of 9% tax credits from 2008, 2009, or 2010 and require additional funding to be completed and placed in service. The owner must have either an equity investment or made good faith efforts to obtain one. For purposes of the Section 1602 Exchange Criteria, "award" means one of the following:

    a. A reservation of credits approved by IHCDA Board of Directors
    b. A fully executed Carryover Agreement
2. The development and Owner must be eligible under applicable federal requirements and meet or demonstrate the ability to meet applicable federal requirements.
3. The development complies with the terms of its carryover allocation agreement and the Owner has made no material changes after the most current initial accepted application without IHCDA's prior approval.
4. Owners must be able to expend and draw one hundred (100%) of the funds before December 31, 2010 and place the development in service by December 31, 2011. The owner will have until December 1, 2010 to send the information necessary to disburse Section 1602 Exchange funds. Owners will be responsible for securing sources to cover any part of the Section 1602 Exchange funds amount not expended by December 31, 2010.
5. The development must demonstrate that it continues to meet the QAP's Criteria for Approval including: marketability, overall financial feasibility, viability, experience of the development team, and no outstanding noncompliance issues for existing developments.
6. IHCDA has not issued IRS Form 8609 to the development.

B. Application Process
1. An application fee of $1,000.00 is required at the time of application.
2. Eligible applicants may apply to IHCDA when the application forms and deadlines are published.
3. Owners will have to make achievable representations with regard to construction timing.
4. Applicants are required to submit at the time of application:
    a. IHCDA Section 1602 Exchange Application
    b. Amount Requested
    c. Revised Sources and Uses
    d. Anticipated Closing Date
    e. Anticipated construction and completion schedule
    f. Project status report detailing the current status of the project, such as construction/permanent loan commitments, plans and specs, construction contract, permitting, etc.
    g. Explanation of the Section 1602 Exchange request in terms of filling the gap caused by syndicator/investors as compared to the most recent rental housing tax credit application
    h. Documentation/Description of Readiness Criteria
    i. Owners of developments without equity must submit a written description of efforts to obtain an equity investment, including a list of all syndicators and investors contacted including contact information and written correspondences.

C. Eligible Uses of Funds
   1. Section 1602 Exchange funds may be used for capital investment in eligible rental housing tax credit developments. Capital investment means costs that are included in the eligible basis of a development under Section 42 of the IRC.
   2. Section 1602 Exchange assistance provided to a development is subject to the same limitations (including rent, income, use restrictions and compliance monitoring) as required by IHDCA with respect to an award of rental housing tax credits to a development (i.e. as required under Section 42 of the IRC and its implementing regulations), and all other requirements of the Act.

D. Selection Criteria
   1. IHCDA will evaluate, prioritize and award Section 1602 Exchange funds to developments based on the following criteria:
      a. Conformance with the above eligibility requirements
      b. 2008 Developments that have been unable to close on equity
      c. Owner's ability to expend and draw one hundred (100%) of the award before December 31, 2010 and place in service by December 2011. IHCDA's "Readiness Criteria" is determined by the following:
         i. The anticipated building timelines, including any challenges (e.g. extensive site work);
         ii. Owner's and general contractor's recent history of timely construction;
         iii. Completed Environmental Phase 1;
         iv. Executed construction contract;
         v. Building permit or documentation of status approval;
         vi. State approval of plans and specifications;
         vii. Site Plan Approval by locality;
         viii. Complete federal requirement, including environmental and historic review;
         ix. Secure construction loan;
         x. Completed engineering and final construction drawings

   2. IHCDA will review each request based on the materials submitted and deny Section 1602 Exchange funding to those, in IHCDA's sole judgment, unable to meet the criteria. IHCDA's Executive Director maintains the right to commit Section 1602 Exchange funds due to unforeseen circumstances if such commitment will further the housing priorities stated in IHCDA's 2009-2010 QAP, and is determined to be in the best interest of the citizens of the State of Indiana. All Section 1602 Exchange

award results will be posted on IHCDA's website and be made available to the public.

IV. GENERAL REQUIREMENTS

A. Underwriting

1. The award will be equal to the anticipated equity in the development's most recent initial application, subject to increases approved by IHCDA necessary to fund additional reserves. All parameters of the most recent initial application will remain in force.

2. IHCDA will verify that the award is consistent with the requirement of Section 42(m)(2) of the Code that the award made to a development does not exceed the amount necessary to ensure the financial feasibility of the development and its viability throughout the credit period.

3. IHCDA will have the ability to make changes to a development's final accepted application (if applicable), including but not limited to the sources, uses, income, and expenses.

4. The award will be no more than the development's eligible basis.

B. Development Fee

1. The inclusion of development fees must be supported by a development services agreement that recites in reasonable detail the development services provided, sets forth a schedule for accrual of the development fee as specified benchmarks are achieved, and clearly identifies the terms of payment of the fee.

2. The inclusion of other fees to service providers must be supported by evidence that the services: (A) were actually performed and (B) were not duplicative of the services for which the development fee is being paid (or for which, in a customary transaction, the development fee would be paid).

3. Other fees will not be paid to entities related to the General Partner or the Developer except where the General Contractor is a related party and is entitled to general overhead, builder profit, and general requirements.

4. Fifty percent (50%) of the developer fee will be paid as follows:

a. 30% at close of Section 1602 Exchange funds
b. 10% during construction, paid prorata with construction completion
c. 30% at Construction Completion
d. 30% at Stabilization and Final Inspection

5. A Development that does <u>not</u> have any equity investor will be subject to the following deferred developer fee requirements:
    a. If the developer fee is less than $300,000, then 50% of the developer fee will be deferred and the amount deposited into a controlled bank account. The deferred portion will be paid out over 10 years, only if the following annual bench marks are achieved:
        i. Property maintains at least a 1.15 debt coverage ratio
        ii. Property is in compliance with applicable IRS Code Section 42 and IHCDA requirements.
    b. If the developer fee is over $300,000, then 50% of the developer fee will be deferred and paid back out of cash flow.
6. A Development that has an equity investor will be subject to the following deferred developer fee requirements:
    a. 50% of the developer fee will be deferred and the amount will be deposited into a controlled bank account. The deferred portion will be paid back over 10 years, only if the following annual bench marks are achieved:
        i. Property maintains at least a 1.15 debt coverage ratio
        ii. Property is in compliance with applicable IRS Code Section 42 and IHCDA requirements.

C. Types of Financing

1. Section 1602 Exchange funds will be awarded as a loan as determined by IHCDA, for a thirty (30) year term with no interest or principal payments.
    a. IHCDA will agree to subordinate the Section 1602 Exchange loan in priority to lender in first lien position.
    b. IHCDA shall disburse Section 1602 Exchange funds at closing or during construction as needed upon receiving evidence that costs have been incurred.
    c. IHCDA will not close on any development in which Total Development Costs at closing are expected to exceed 221 (d) 4 limits, unless the participant can clearly itemize and demonstrate the overage is due solely to federal funding requirements.
2. The Owner will be permitted to return up to 100% of the annual per capita credits, in exchange for an award equal to the amount of the annual tax credit equity. The total amount of the award will be the

lesser of the total equity value returned or the amount identified in the 2008 or 2009 Carryover Agreement. The Owner will be permitted to request gap financing for shortfalls in the equity investment stated in the most current initial Tax Credit Application.

D. Affordability Period
   1. 30 year affordability
   2. Owner must agree to waive the Section 42 Qualified Contract Provisions

E. Award Agreement

IHCDA will execute a legally binding written agreement with each development owner. The written agreement will set forth all of the Section 1602 Exchange program and Section 1602 sub-award requirements including the requirements of Section 42 of the Code applicable to the funding, and must make these requirements enforceable through the recordation of a restriction that is binding on all owners and successors, e.g. a Lien and Restrictive Covenant Agreement.

The Section 1602 Exchange written agreement must be signed and dated by IHCDA and the development owner before any Section 1602 Exchange funds are disbursed. Federal funds cannot be drawn from the U.S. Treasury in advance of the need to pay an eligible cost. Section 1602 Exchange funds cannot be drawn from the U.S. Treasury and placed in escrow or advanced in lump sums to development owners. Once funds are drawn from the IHCDA's U.S. Treasury account, they must be expended by an eligible Section 1602 Exchange cost within 3 days.

The written agreement shall impose conditions or restrictions, including a requirement providing for recapture, so as to assure that the qualified low-income building remains a qualified low-income building during the 30-year compliance period.

No Section 1602 Exchange funds may be disbursed to owners after December 31, 2010.

F. Reporting and Compliance
   1. Owners will report to IHCDA:
      a. Development completion status
      b. An estimate of the number of jobs created and/or retained
      c. Any other information necessary for IHDCA's federal reporting requirements.
   2. Owners will follow IHCDA's process and procedures applicable to IRS Code Section 42 developments with an investor and any additional compliance requirements made necessary due to Section 1602 Exchange

funding.

3. Non-compliance of award terms will be subject to recapture under the terms from the U.S. Treasury; and
4. Non-compliance of award terms can negatively affect future LIHTC reservations from IHCDA.
5. The Section 1602 Exchange funds themselves do not require compliance with the various crosscutting federal requirements (i.e. Davis-Bacon, Environmental Review, Uniform Relocation, etc.). Other funding sources may require such compliance.

V. FINANCIAL SERVICE AGENTS POLICIES AND PROCEDURES

Developments without an equity investor will be assigned a Financial Service Agent (FSA). IHCDA reserves the right to assign a FSA in its sole discretion to any development receiving an award under the Section 1602 Exchange program.

Designated FSAs require a written Section 1602 Exchange Policies and Procedures statement. This requirement is based on the regulatory belief that there are important policy guidelines that need to be established and followed by everyone associated with a FSA and that they should be in writing for the benefit of IHCDA. Further, this same internal regulatory logic requires that these policies be followed by IHCDA and the FSAs and therefore, will be enforced upon each designated FSA Syndication & Underwriting Department and FSA Asset Management Department. Each FSA and IHCDA may conduct separate annual examinations to confirm compliance with the stated LIHTC Exchange and Assistance Program Policies and Procedures.

IHCDA's Section 1602 Exchange Program provides directives, both explicit and implicit, that specify the objectives of each FSA and the appropriate means to accomplish these objectives. These policies are broad, precedent-setting decisions that allow for guidance for future transactions. The Section 1602 Exchange Program policies and procedures are a set of purposes, principals, and rules of action that will guide the FSA's routine daily activities on the behalf of IHCDA.

If a FSA is assigned to a development, prior to an award by IHCDA the FSA must provide information to IHCDA so that it can determine that such an award (including elements such as the developer, its principals, sponsors, and affiliates) is consistent with the business purpose of the development and is in substantial compliance with IHCDA's Policies and Procedures. In connection with such determination, the FSA must have examined and approved (or accepted as satisfactory) the items and documentation provided in accordance with the policies and procedures (and any other relevant items and documentation).

As part of the application, the owner will request an approved FSA. IHCDA will review the application package and assign a FSA to the development using the priority request from the owner for guidance. The FSA will administer the underwriting, closing, funding of all draws, and the asset management of the development during the Compliance Period.

The assigned FSA will review the submitted information to create an underwriting review package for IHCDA. The FSA will recommend a final financing structure to IHCDA, of which the Section 1602 Exchange Funds will be a source. Upon approval by IHCDA, the FSA will issue an award letter to the Applicant and begin the Section 1602 Exchange closing process.

IHCDA will retain a FSA to administer and provide underwriting, closing and asset management services to IHCDA for Developments that exchange 100% of their tax credits for the Section 1602 Exchange funds. The Partnership will enter into a service agreement with IHCDA and the FSA for those services provided during the underwriting and closing processes. At the time of the award, the Partnership will enter into an asset management agreement with IHCDA and the FSA detailing the reporting requirements and roles of the FSA as asset manager.

IHCDA may retain a FSA to administer and provide underwriting, closing and asset management services for Developments that exchange less than 100% of their tax credits or request additional Section 1602 Exchange funds. Intermediaries who purchase any portion of the tax credits and receive an allocation of funds derived from the exchange of credits or Section 1602 Exchange funds will be required to provide IHDCA with an annual asset management report.

IHCDA Approved Financial Service Agents:

a. City Real Estate Advisors, Inc.
   Brian K. McDonnell
   Senior Vice President
   30 South Meridian Street, Suite 600
   Indianapolis, Indiana 46204
   Phone: 317-808-7257
   Fax: 317-808-7313
   E-Mail: bmcdonnell@cityrealestateadvisors.com
   Web Page: www.cityrealestateadvisors.com

b. Great Lakes Capital Fund
   Jack L. Brummett
   Senior Vice President
   320 North Meridian, Suite 1011
   Indianapolis IN, 46204
   Phone: 317 423-8880
   Fax: 317 423-8855

E-Mail: jbrummett@capfund.net
Web Page: http://www.capfund.net

c. House Investments
Doug Sylvester
Managing Partner
250 West 103rd Street
Indianapolis, IN 46290
Phone: 317-580-2538
Fax: 317-580-2545
E-Mail: dsylvester@houseinvestments.com
Web Page: www.houseinvestments.com

VI. Award Funding Guidelines

A. Project ownership

The ownership of the Project Property must be approved by the FSA. The FSA and IHCDA will not have any ownership in the Project Property.

B. Award —General Requirements

IHCDA and the FSA will award the funds to the Partnership via Award Agreements. The Award Agreement must contain provisions that comply substantially with the policies and procedures detailed herein.

C. Fees:

1. IHCDA Application Fee:	$1,000
2. Legal Fees:	The Partnership will pay the legal fees associated with closing the award documents. These fees will be paid at closing.
3. Third Party Reports:	The Partnership will pay the costs of all third party fees.
4. FSA Fee:	A preset FSA fee will be charged to the Partnership.
5. Asset Management Fees:	Developments without an equity investor will annually pay the *greater* amount of 1) $5,000 or 2) $100 per unit. An amount equal to 15 years of fees will be set aside in a pre-funded reserve established at closing. This reserve will be drawn upon annually to pay for asset management services.

D. Section 1602 Exchange Fund Disbursement:

1. Closing of the Award Agreement: 100% of the proceeds of the funds shall be disbursed on a draw basis to fund allowable costs of the Project Property. Requirements for closing the Section 1602 Exchange funds:
    a. Executed Construction Loan documents, if any
    b. Closing on all Project sources
    c. Receipt of a commitment for a permanent loan, if any
    d. Title Insurance with applicable endorsements
    e. Approved Market Study and Appraisal
    f. Approved Environmental reports
    g. Construction-related documentation: GC Contract/GMP, Resume, Financials, Construction Budget, Construction Schedule
    h. Building Permits
    i. Ownership formation documents
    j. Survey
    k. Architect Agreement
    l. Plans and Specifications (including Site Plan)
    m. Purchase Contract, Deed and Closing Settlement Statement
    n. Property Management Documentation – Management Agreement, Resume, Management Plan, & Form of Tenant Lease
    o. Formation Documentation for the ownership structure
    p. Developer Formation Documentation
    q. Financial Statements for all principals of the ownership structure
    r. Development Agreement
    s. Consultant Agreement, if applicable
    t. All applicable insurance certificates – Builder's Risk, Property, Liability, Fidelity Bond
    u. Additional documents as determined by the FSA

2. Draw Funding: Section 1602 Exchange funds not funded at closing shall be advanced on a draw request basis based upon construction completion and supported by AIA forms G702 and G703 or the equivalent, and certified by the project architect and the Owner. The draw package must include a construction progress report by the third party project architect and may also contain additional documents as determined by the FSA to support the draw request.

    The FSA shall have rights to approve all construction draws, irrespective of the source of funding. Change orders shall require the approval of the FSA.

    Any Section 1602 Exchange Funds not expended by December 31, 2010 will be returned.

E. Award Agreement:

The Award Agreement must comply strictly with the following mandatory requirements.

Mandatory Rights of IHCDA: The Award Agreement will assign the following rights to IHCDA:

1. The right to cause the Owner to remove the property manager and appoint a new property manager in circumstances where the FSA or IHCDA determines that the same is necessary to protect the interests of the Project Property;

2. In addition to the periodic reports specified in the Award Agreement, the right to receive any other information and reports regarding the financial and physical condition of the Project Property as may be reasonably requested by the FSA or IHCDA;

3. The right to approve the appointment of any property manager for the Project Property (subject to any required lender or governmental agency approval);

4. The right to remove the Owner in the event of any gross negligence, willful misconduct, breach of fiduciary duty, breach of any material provision of the Award Agreement, or (subject to customary cure periods) upon the bankruptcy or insolvency of the Developer;

5. The right to approve any proposed sale, exchange, lease (other than leases of dwelling units to individual tenants in the ordinary course of business), mortgage, pledge refinancing, or other disposition of the Project Property (or any portion thereof) or any material asset of the Partnership;

6. The right to approve the withdrawal of the Owner from the Partnership;

7. The right to approve disbursement requests;

8. The right to access the Project Property for site inspections.

F. Other Mandatory Requirements:

No award to any development may be made unless the following requirements are satisfied:

a. The Owner must comply with all Section 42 rules and regulations; and

b. The Award Agreement must contain a reporting section to detail those items needed on a timely basis to be received, reviewed and approved by the FSA in accordance with those requirements under the Section 1602 Exchange Program.

G. Guaranties:

A creditworthy obligor acceptable to the FSA will provide the following guarantees to be included in the Award Agreements:

1. <u>Project Completion</u>

a. A guaranty of completion of the construction or rehabilitation of the Project Property in accordance with the approved plans and specifications and in a good and workmanlike manner, free and clear of all mechanics', materialmen's, or similar liens and the satisfaction of all financial and non financial obligations of the Partnership through Stabilization.

b. Guaranty must be unlimited

c. Amounts paid by the obligor in satisfaction of the Project Completion guaranty are not reimbursable.

2. <u>Operating Deficits</u>

a. A guaranty of payment of operating deficits during the Compliance Period commencing upon the expiration of the Project Completion Guaranty.

b. Obligation must be sufficient to cover twelve months of the sum of projected operating expenses, replacement reserve funding, and must-pay debt service payments.

c. Advances to cover operating deficits must bear no interest and must be repayable solely from cash flow or sale or refinancing proceeds.

H. Section 1602 Exchange Funds Repurchase:

The Partnership and Owner shall guarantee repayment of any and all Section 1602 Exchange funds plus any and all penalties if Section 1602 Exchange funds are recaptured by the Treasury. The obligation is unlimited in size and duration.

I. Owner

1. <u>Reputation/Experience</u>

   The Owner, any Affiliate of the Partnership that guarantees the performance of obligations detailed in the Policies and Procedures (a "***Key Principal***"), and any other individuals or entities identified by the FSA whose continued participation in the development, ownership, and operation of the Project Property and the Partnership is an essential factor in the anticipated success of the Project Property.

2. <u>Financial Standing</u>

   a. Owner: The financial standing of the Owner and the Key Principals (collectively, the "Owner") must be fully investigated by the FSA. Prior year financial statements must be obtained and reviewed (last three years, if available).

   b. Contingent Liabilities: All contingent liabilities and guarantees of the Owner must be fully described in the financial statements.

3. <u>Credit Standing</u>

   a. <u>Development Team:</u> The Owner, developer, Key Principals, general contractor, the property manager, and any other members of the development team must not be the subject of any materially adverse governmental or private inquiry, proceeding, or litigation.

   b. <u>Credit Checks:</u> Detailed credit and background checks must be obtained for the Owner and Key Principals. The geographical scope of the checks shall correspond to the range of activities of the relevant entities.

      i. The detailed credit and background checks must include, but not be limited to, investigations over the last 10 (ten) years of records relating to:

Bankruptcy or Insolvency
Suits and Judgments
Criminal Proceedings
State/Federal Tax Liens
Negative News Media
Negative HUD Actions

ii. All detailed credit and background checks must be no more than six (6) months old as of the date of the anticipated closing of the Section 1602 Exchange Funds in the Project Property.

iii. The cause and resolution of all negative findings must be fully explained and supporting documentation must be available to IHCDA.

4. Real Estate Owned Schedule

Statements of real estate owned must be collected for the Developer. This schedule shall include, but not be limited to, a listing of all real estate ownership, percentage of ownership, construction status, debt service coverage, and occupancy rates.

5. Development Team Members

The Owner must have identified a reliable and qualified development team, with strong multifamily and Code Section 42 experience.

The involvement in the Project Property of any tenant cooperative must be limited to the capacity of nonbinding advisor to the property manager.

The Owner must demonstrate that any other partner has a good reputation and the financial capability to perform its obligations under the Award Agreement.

6. Contractor

The general contractor must meet all current licensing requirements.

If the general contractor is unrelated to the Developer, then the general contractor must secure construction completion in the event of unforeseen problems during construction by one of the following:

a. A Letter of Credit equal to or greater than 15% of the construction contract amount; or
b. 100% payment and performance bonds.

The construction contract must be on an AIA approved form and must provide for a guaranteed maximum price. The Partnership must be a party to the construction contract.

7. Property Manager

The property manager must have experience in the subject market and submarket. The property manager must have experience in LIHTC's and Section 42 compliance and be in good standing with IHCDA.

The property manager may be an affiliate of the Owner, if appropriate; provided that if the property manager is an affiliate of the Owner, the property management agreement must provide that such agreement will terminate if the Owner is removed under the terms of the Award Agreement.

Staffing must be adequate based on the size and social needs of the Project Property.

Payroll expenses for each property must be projected on a stand-alone basis assuming no economies of scale or shared staffing with other properties under common management or ownership. These expenses must be reasonable within the market for similarly qualified employees.

Any social services or tenant programs must be fully explained to the FSA, including the cost allocations and management responsibilities.

8. Architect

The architect must carry Errors and Omissions insurance and must meet all current licensing requirements.

The architecture contract must be on an AIA approved form. The Partnership must be a party to such contract.

a. Development Fee

i. The inclusion of development fees must be supported by a development services agreement that recites in reasonable detail the development services provided, sets forth a schedule for accrual of the development fee as specified benchmarks are achieved, and clearly identifies the terms of payment of the fee.

ii. The inclusion of other fees to service providers must be supported by evidence that the services (A) were actually performed and (B) were not duplicative of the services for which the development fee is being paid (or for which, in a customary transaction, the development fee would be paid).

iii. The inclusion of other fees will not be paid to entities related to the Owner or the Developer except where the General Contractor is a related party and is entitled to general overhead, builder profit, and general requirements.

iv. Fifty percent (50%) of the developer fee will be paid as follows:
   1) 30% at close utilizing Section 1602 Exchange Funds
   2) 10% during construction, paid prorata with construction completion
   3) 30% at Construction Completion
   4) 30% at Stabilization and Final Inspection

v. A Development that does not have any equity investor will be subject to the following deferred developer fee requirements:
   1) If the developer fee is less than $300,000, then 50% of the developer fee will be deferred and the amount deposited into a controlled bank account. The deferred portion will be paid out over 10 years, only if the following annual bench marks are achieved:
      a) Property maintains at least a 1.15 debt coverage ratio
      b) Property is in compliance with applicable IRS Code Section 42 and IHCDA requirements.
   2) If the developer fee is over $300,000, then 50% of the developer fee will be deferred and paid back out of cash flow.

vi. A Development that has an equity investor will be subject to the following deferred developer fee requirements:
   1) 50% of their developer fee will be deferred and the amount deposited into a controlled bank account. The deferred portion will be paid back over 10 years, only if the following annual bench marks are achieved:
      a) Property maintains at least a 1.15 debt coverage ratio

b) Property is in compliance with applicable IRS Code Section 42 and IHCDA requirements.

b. <u>Land Acquisition</u>

i. A copy of the recorded deed must be obtained; and

ii. A copy of the purchase contract(s) and settlement statements must be obtained.

c. <u>Zoning</u>

The site must meet all zoning and land use requirements (including unit density and parking availability) to permit the contemplated improvements and uses (or approval of required variances must be reasonably anticipated within six months).

The Project Property must be in full compliance with the requirements of all governmental authorities having jurisdiction over it, and must conform in all respects to applicable laws and regulations, including housing code, zoning, Americans with Disabilities Act, “wetlands” and drug-free workplace laws and regulations.

d. <u>Ownership and Title</u>

The Owner must have acquired site control to ensure completion of the Project Property on a timely basis. Title must be good and marketable and must consist of fee simple title or a leasehold estate under a land/ground lease with at least 65 years remaining, and may be subject only to loans and other such liens, charges, easements, restrictions, and encumbrances that will not materially interfere with the Local Partnership’s development, operation, and ownership (as determined for federal tax purposes) of the Project Property.

The Partnership must acquire an ALTA owner’s title insurance policy insuring the Partnership’s estate (including all appurtenant easements [e.g., necessary access easements and utility easements]) in an amount equal to the sum of the aggregate principal amounts of the permanent loans and the aggregate loan disbursements to the Partnership. A non-binding "pro-forma policy" is not sufficient. All easements, covenants, restrictions, encroachments, and other exceptions shown on Schedule B must be examined by legal counsel for the FSA to confirm that they will not adversely affect the Project Property by encroachment or otherwise and the policy should comply with the requirements described below. However, the adequacy of title insurance must be determined on a case-by-case basis depending on the facts and circumstances of the specific Project Property and on the laws of the jurisdiction where the Project Property is located (and, to a lesser degree, the customs there). In addition, prior to the Section 1602 Exchange Funds being disbursed, a current title report must be reviewed and approved by the FSA to confirm that there are no new title exceptions or other matters that might adversely affect the Project Property.

i. Any "pre-printed" or "standard" exceptions must be deleted.

ii. Any property tax exception should be limited to taxes that are "not yet due and payable."

iii. Any tenant's rights exception should contain a qualification that such rights are "to leaseholds of parties in possession, as tenants only, under unrecorded leases."

iv. The following endorsements must be obtained:

1) Access;

2) Contiguity (if the Project Property is comprised of adjoining lots);

3) Owner's Comprehensive (with mineral rights coverage if applicable) protecting the existing improvements or, if the Project Property has yet to be constructed, protecting the planned improvements as shown on specified plans;

4) Separate Tax Lot;

5) Subdivision (if applicable);

6) Same as Survey; and

7) Zoning.

e. <u>Environmental</u>

A Phase I Environmental Site Assessment in conformance to the scope and limitations of ASTM E 1527-05 (or in conformance to superseding regulations that are expected to be promulgated by the United States EPA pursuant to section 232 of the Small Business Liability Relief and Brownfield's Revitalization Act) and any additional environmental reports recommended by the Phase I (collectively, the "ESA") must be obtained for the Project Property and the Owner must undertake to investigate and promptly remediate in strict compliance with all applicable laws, regulations, and/or governmental orders any environmental problems identified in such ESA (in a manner satisfactory to the FSA).

As required by sections 11.7 and 1.1.1 of ASTM E 1527-05, the ESA must "include a conclusions section that summarizes all recognized environmental conditions" connected with the Project Property and summarizes the impact of such recognized environmental conditions. In addition, the ESA must address other appropriate environmental issues and "non-scope considerations" discussed in section 12 of ASTM E 1527-05 that are particular concerns for multifamily housing, including the possibilities of asbestos containing materials, radon, lead-based paint, lead in drinking water, mold, and unsatisfactory indoor air quality.

Non Confirmation: If the ESA does not confirm (a) the absence of recognized environmental conditions and other appropriate environmental issues and non-scope considerations (under section 12 of ASTM E 1527-05) (e.g., asbestos containing materials, radon, lead-based paint, lead in drinking water, mold, and unsatisfactory indoor air quality) and (b) the compliance of the Project Property with all environmental laws, regulations, and/or governmental orders, then the Owner must present an O&M plan or other remediation plan to treat, contain, or abate all such identified environmental problems in strict accordance with all environmental laws, regulations, and/or governmental orders prior to completion of the Project Property. All costs associated with any O&M or remediation plans must be contained in the Development Budget. Any O&M and/or other remediation plans must have received all necessary approvals from governmental authorities with jurisdiction over the environmental problems in question.

Surrounding Land: Surrounding land use must also be investigated regarding potentially hazardous materials, including, but not limited to, underground storage tanks, agricultural uses and contaminants, landfill or dumping, and current and prior uses.

Supplements and Updates: The ESA (including any supplements or updates) must be addressed to the Partnership. It should have an effective date not more than 180 days before the effective date of disbursement of the award to the Partnership. An older ESA may be acceptable, as determined on a case-by-case basis between the FSA and IHCDA, with consideration given to whether the Partnership has been in control of the property since the date of the ESA and whether or not there is reason to suspect any new or remaining recognized environmental conditions of concern. In cases where an ESA older than the 180-day period is accepted, a current environmental database records search update with an interpretive letter from an environmental professional must be provided at the disbursement of the Section 1602 Exchange funds to the Partnership to confirm that the public records do not reveal recognized environmental conditions.

Property Description: The property assessed by the ESA must include all property owned or leased by the Partnership and described on Schedule A of the owner's title insurance policy.

f. Utilities

All utilities necessary to construct and operate the Project Property must be available and the Project Property must have access to public water and a public sewage system.

Unit fuse panels must be circuit breakers.

Electrical amperage to all units in the Project Property must be at least 100 amps. Consideration must be given to increasing this minimum based on the number of bedrooms in each unit or if all apartment services are electric, such as cooking and air conditioning.

Access: The Project Property must be accessible via a paved roadway and must have direct access to a public street or highway, and adequate ingress and egress (especially as a consideration for emergency vehicle access). In addition, the Project Property should be in reasonable proximity to necessary infrastructure and community services, including retail, transportation, medical facilities and services, and schools.

g. Site Control

Purchase Agreements: Cost and conditions must be fully described to the FSA and its counsel.

Ground Lease: Terms, cost, conditions and renewal/purchase options must be fully described to the FSA and its counsel.

Agreements with Other Property Owners: Any agreement that burdens the Project Property or entitles the Partnership to use other property, such as a common area agreement, cross use agreement, or homeowners' association agreement, must be commercially reasonable in all respects, including the obligations placed on the Partnership and the compensation provided to the Partnership.

J. Transaction Underwriting

1. Debt Service Coverage

All projects utilizing foreclosable debt should have a minimum projected stabilized DSCR of 1.20:1.00, based on the income and expense projection and trending requirements outlined below, and approved by the FSA. Pro forma rents shall reflect a discount to market rents of at least ten percent. If the discount to market rents is smaller than ten percent, or if the income and expense projections and trending levels do not meet the requirements outlined below, then higher DSCR's will be required.

For purposes of the Policies and Procedures, a Project Property's projected stabilized DSCR for any month will be the ratio of projected operating cash flow to projected must-pay debt service, as determined by the FSA:

a. Operating cash flow for any month will be determined as the excess of (i) gross rental receipts over (ii) all cash expenditures of the Project Property (including required reserve deposits and the FSA Asset Management Fee) other than required principal and interest payments on the loans and fees or expenditures to be paid from capital contributions. For purposes of determining operating cash flow, the cash expenditures of the Partnership described in clause (ii) of the preceding sentence will be determined by taking the sum of all of the Project Property's actual cash expenditures for the current and all prior months of the fiscal year and all anticipated cash expenditures for the remainder of the fiscal year and allocating the sum of such actual and anticipated cash expenditures ratably over the twelve months of the fiscal year.
b. Debt service for any month will be determined as the amount of payments of principal and interest required under the loan documents to be made, but excluding payments of principal and interest funded by capital contributions or other permanent financing sources.

2. Financial Projections

The Owner must prepare, and the FSA must approve, detailed financial projections for the Project Property, including (at a minimum), the following schedules:

a. Development sources and uses, including flow of funds;
b. Initial lease up;

c. Operating income and expense pro forma conforming to the Policies and Procedures described herein;
d. Cash flow;
e. Reserve balances;
f. Operating income and expense pro-forma utilizing stressed factors such as a vacancy rate greater than underwritten factor, no income growth, or lower rents on unrestricted units; and

3. <u>Operating Analysis</u>

The operating income and expense pro forma and residual value analysis must be prepared using the guidelines detailed in this section.

a. Vacancy
   i. A minimum of 7% for physical vacancy.
   ii. Additional losses due to bad debts, concessions, and other miscellaneous causes based upon comparables provided by the Owner and Property Manager.
   iii. Vacancy rates should be projected higher if so dictated by the market study, the appraisal, historical data, and/or a site visit.
b. Rental Income

   i. Trending: Trended over the full Compliance Period using an inflation factor of no greater than 2% and supportable by historical income trends in the market for similar product type; provided, however, that for projects located in counties identified by HUD as zero-growth or negative growth areas and for which the pro forma assumes maximum permitted LIHTC rents, zero percent annual rental income growth until such time as the FSA determines that increases in income levels in the relevant area will permit rent increases.

   ii. Third-Party Validation: Projected rental income must be validated by the market study and appraisal, as well as site visit data. In addition, projected rental income must accurately account for the effect of any tenant-income restrictions contained in any regulatory agreements, loan documents, or other agreements or requirements governing the Project Property. The market study and Appraisal must be dated within twelve months of the date of the initial funding of the Section 1602 Exchange Funds.

Otherwise, an updated or new market study may be requested by the FSA.

iii. Rent Advantage

1) Low-Income Units: Pro forma rents per unit-type, combined with current unit-type utility allowance, should be at least 10% below market rate units in the primary market area, but cannot exceed the LIHTC maximum rents. If the discount to maximum allowable LIHTC rents is less than 10% for the 60% AMI units, the annual income trending factor must equal the lesser of 2% or the level supported by HUD FMR data for the preceding ten years.

2) Market-Rate Units: Pro forma rents per unit-type, combined with current unit-type utility allowance, must be at least 10% below current market rents as supported by the market study and appraisal.

3) Commercial Income: Commercial Income should not be included in calculating total projected income for the Project Property or the final DSCR.

4) Other/Miscellaneous Income

a) Such income can be taken into account only to the extent it is fully supported by historic operations, comparable market information, and other reasonable factors.

b) Other/Miscellaneous Income must be described in detail and cannot include interest income or income from any other one-time events.

iv. Property Expenses

1) Trended over the full Compliance Period using an inflation factor of at least 3% and supportable by historical expense trends in the market for similar product type.

2) Projected property expenses must be validated by the market study, comparable property expenses,

appraisal, site visit data and any existing payment/expense agreements or schedules.

3) The trending factor for expenses must be applied to all operating expenses and replacement reserve deposits over the full Compliance Period.

a) Management Fee: The property management fee must be consistent with market standards for comparable projects, and consistent with IHCDA limits, but no greater than 8%.

b) Property Taxes

(i) Confirmation of tax abatement or PILOT Agreement must be obtained.

(ii) The underwritten estimate for property taxes should be validated by the ongoing expenses of comparable projects as well as prior or expected assessments.

(iii) For properties where tax abatement is subject to annual approval, or has not yet been approved, or will expire during the Compliance Period, sufficient reserves should be maintained to support the Project Property.

c) Replacement Reserves: All underwriting analyses must include at least $250 per unit per annum for new construction projects and at least $300 per unit per annum for rehabilitation projects (or such greater amounts as may be required or recommended by any lender, governmental agency, or third-party engineering report). In all cases, these figures must be higher if property type, condition or market comparables so dictate. Funding of replacement reserves must be increased by an annual inflation factor of 3%.

d) Net Operating Income: The projected net
Operating income should remain above a 1.10:1.00 Debt Coverage Ratio during the term of the award.

K. Capitalized Contingency and Reserves

1. Operating Deficit Reserve: A twelve (12) month Operating Deficit Reserve must be funded at the time of Stabilization. The amount is calculated on must pay debt service, all operating expenses and replacement reserves. The reserve shall be funded out of Section 1602 Exchange Funds proceeds and held at a location selected by the Owner. The reserve must be held in an interest bearing account at an institution insured by the FDIC. Uses of the reserve shall require the signatory approval of the FSA.

2. Lease-up Reserve: A reserve to fund projected lease-up period deficits will be required when indicated by the projected lease-up schedule or market data.

3. Hard Cost Contingency: All rehabilitation/construction estimates must be "hard" and based on completed plans and specifications provided by an architect or other qualified party providing architectural services. Construction hard cost contingencies should be 3% for new construction and 5% for rehabilitation. Such contingency amounts will be disbursed solely upon the approval of the FSA on an "as needed basis" and confirmed by third party cost analysis.

L. Section 8

1. Underwriting of Housing Assistance Payment Contracts: Section 8 payments may only be taken into account in underwriting a Project Property to the extent such payments will be available to the Partnership during the remaining term of a housing assistance payments contract (a "HAP Contract") in existence on the date of disbursement of the Section 1602 Exchange Funds to the Partnership. If a HAP Contract will expire during the Compliance Period, no renewals may be assumed unless such renewal periods are available as a matter of law or contract on the date of disbursement of the Section 1602 Exchange Funds to the Partnership.

2. Restabilizing Reserves: When 20% or more of the units are covered by (a) 1-year renewable Section 8 contracts, (b) Section 8 contracts that are subject to annual appropriations, or (c) older Section 8 contracts (generally contracts originally executed prior to 1979) for which funding has been fully assured through the HAP Contract term and any renewal periods but where the Compliance Period exceeds the term of the Section 8 contract, a restabilizing reserve complying with the requirements outlined below must be established and maintained to

facilitate the transition of Section 8 units to LIHTC units if the Section 8 contracts are not renewed (or funding is reduced or eliminated).

The initial balance in the restabilizing reserve should equal the greater of the Shortfall Amount calculated via the method described below or an amount sufficient to pay operating expenses and must-pay debt service for six months. The balance in the restabilizing reserve cannot be counted towards any other reserve requirements applicable to the project.

a. The size of the Shortfall Amount is to be determined in accordance with the following steps:

i. Recalculate projected rental income of the Project Property by assuming that (A) all of the Section 8 contracts are canceled or non-renewed at the earliest possible opportunity (e.g., the second year of operations under an annually renewing contract), and (B) except as provided immediately below, all of the Section 8 units are turned over upon lease termination. Rents charged to new tenants for the former Section 8 units should be set at the lesser of maximum allowable LIHTC rents (subject to all applicable regulatory and other similar agreements) or a 10% discount to market rents.

ii. In some cases it may be reasonable to assume less than 100% turnover of the Section 8 units if it can be demonstrated through a resident-income analysis that some of the existing tenants will be able to afford the restricted rents.

iii. Using a reasonable lease-up rate supported by the market study, calculate the period of time (the "Restabilization Period") needed to (A) achieve 90% physical occupancy and (B) support the original underwritten DSCR.

iv. The Shortfall Amount is the sum of the amounts each month during the Restabilization Period by which net operating income is less than the level needed to maintain the underwritten DSCR.

b. Restabilizing reserves must remain in place throughout the Compliance Period unless the following occurs:

i. The Section 8 contracts become non-cancellable, or

ii. Utilizing only tenant rent payments, the Project Property achieves a stabilized 90% occupancy at the restricted rents for three consecutive months and maintains a DSCR equal to or in excess of the original underwritten DSCR for six consecutive months.

c. The Award Agreement must provide that draws on the restabilizing reserve and release of the reserve can be made only with the consent of the FSA.

L. Leases

All lease restrictions must be fully described to the FSA. This includes Section 8/HAP Contract terms, commercial space and any other occupancy restrictions.

Commercial leases should be disclosed to the FSA and IHCDA, including terms, tenant identification, and space use.

M. Site Visit

During the underwriting analysis, the FSA must visit the site of the Project Property and should visit, where possible, similar project sites operated by the Developer and Management Agent.

N. Third-Party Reports

1. <u>Market Analysis and Appraisal</u>:

a. An independent market study and appraisal must support the development and operation of the Project Property, including a comprehensive demand analysis, rent comparability analysis, and operating expense analysis. This independent market study and appraisal must conform to current industry standards for LIHTC properties. The Market Study or Appraisal must include:

i. An analysis of comparable rents versus proposed subject rents;

ii. A description of the population of income qualified tenants;

iii. An analysis of how the Project Property compares to the submarket in terms of unit size, design and amenities;

iv. An analysis of the effects on marketability resulting from existing and proposed competition;

v. Operating expense analysis for comparable rental properties; and

vi. Vacancy rate analysis for comparable rental properties.

b. Area vacancy rates should be stable or decreasing over the prior 12 months.

c. The overall demographic characteristics of, and economic trends in, the market and submarket must support the ongoing and consistent success of the Project Property.

d. Market demand for the Project Property must be adequately demonstrated and the projected unit absorption rate must support the ongoing and consistent success of the Project Property.

e. Unit absorption rates for the specific product type(s) must be fully supported. If the Project Property contains market-rate units as well as affordable units, the expected absorption rate for both must be addressed.

f. The market study and appraisal must have an effective date within twelve (12) months of the date of the anticipated closing of the Award Agreement.

2. Engineering Report: For acquisition/rehabilitation projects only, the Engineering Report must have an effective date of no more than 180 days from the date of closing and include:

a. Capital Needs Assessment: For rehabilitation projects, a Capital Needs Assessment (also known as a "Physical Needs Assessment") must be completed by the engineer when applicable. This report must fully address the remaining useful life standards and projections of all building components based upon the as-to-be-completed plans.

b. Draw Requests: A third party architect must confirm construction draw requests and confirm that the Project Property has been completed in accordance with the plans and specifications.

c. Certification of Completion in Accordance with the Plans and Specs: A third-party A/E must be retained by the Partnership to confirm that the Project Property has been completed according to the final plans and specifications.

O. Insurance

1. General Requirements

a. Property and Liability Insurance: Each Project Property must be covered by property and liability insurance during the compliance period.

b. Named and Additional Insured: The Partnership (rather than the Owner or the Developer) must be the named insured in each policy.

c. Per Occurrence Basis: All policies must be written on a per occurrence basis except for earthquake and professional liability coverage which may be written on a claims-made basis.

d. Cancellation Notice: Each policy must have a cancellation provision requiring the carrier to notify the Owner of the Partnership, the FSA at least 30 days in advance of any policy reduction or cancellation for any reason except non-payment of premium. The cancellation provision must provide for at least a 10-day written notification for non-payment of premium.

e. Blanket Policies: The requirements of this section may be satisfied by the use of a blanket or package policy (or policies) of insurance covering the Project Property and other properties and liabilities of the Developer. The policy, however, must provide the same or better insurance coverage as a single property insurance policy, and the property must be listed and identifiable in the policy and/or associated schedules.

f. Carriers' Rating: An insurance carrier must have an A.M. Best general policyholder's rating of "A" or better and a financial performance index rating of VI or better in Best's Insurance Reports or Key Ratings Guide.

g. Term: Each policy must be for a term of not less than one year.

h. Evidence of Insurance: The Owner must provide the FSA with a certificate of insurance for the Project Property on or before the Partnership delivers its consent to invest. ACORD 27, 25S and 75S (and any subsequent substantive equivalents thereof) are acceptable forms of temporary evidence for property/liability insurance. If a certificate is not available, the FSA may accept a letter signed by the Owner and the insurance broker certifying the coverage's required deductibles and exclusions. Originals or certified copies of current insurance policies must be obtained, reviewed and retained in the FSA's permanent files within 90 days after IHCDA has agreed to provide Section 1602 Exchange

Proceeds to the Project Property, or the date of the insurance policy renewal. Temporary coverage has an expiration date. Consequently, the evidence of temporary coverage must be monitored carefully and renewed as appropriate.

2. Property Damage

Each Project Property must be covered by property insurance for the entire compliance period. This section sets out the requirements for such property insurance.

a. <u>Property Damage ("All Risk") Insurance</u>:

i. During Construction: An "All-Risk" Builder's Risk Property Insurance Policy that includes an agreed-value clause or no-coinsurance provision.

ii. During the operational phase of the Project Property: An "All-Risk" Property Insurance Policy protecting the interest of the Partnership.

iii. Maximum Deductible: $25,000 per occurrence for each Project Property.

iv. Amount of Coverage: 100% completed value, on a non-reporting basis during the construction phase, and 100% Replacement cost coverage of the Project Property and personal property during the operational phase.

v. Windstorm, earthquake, tornado and flood exclusions are generally acceptable exclusions from "All-Risk" insurances policies, provided that a separate policy is obtained for these exclusions. The FSA reserves the right, in its sole discretion, to revise its insurance requirements to require coverage once any excluded coverage becomes generally available in the marketplace.

b. <u>Ordinance and Law Coverage</u>:

i. Required Insurance: Ordinance and Law Coverage.

ii. When Insurance must be obtained: When the Project Property represents a nonconforming use under current building, zoning, or land use laws or ordinances.

iii. Amount of Coverage

1) Loss of Undamaged Portion of the Building: Full replacement cost of the structure with agreed-value clause.

2) Demolition Cost: Minimum 10% of the replacement cost.

3) Increased Cost of Construction: Minimum 10% of the replacement cost.

c. <u>Boiler and Machinery Insurance</u>:

i. Required Insurance: Boiler and Machinery Insurance.

ii. Insurance must be obtained:

iii. When any centralized HVAC equipment is in operation at the property.

iv. When the Project Property contains boilers or other pressure-fired vessels that are required to be regulated by the state in which the property is located.

v. Maximum Deductible: No more than the deductibles on the property insurance policy.

vi. Amount of Coverage: Full replacement cost of the building that houses the equipment.

d. <u>Liability Insurance</u>:

Each Project Property must be covered by liability insurance for the term of the Compliance Period, on a "per project" basis. This section sets out the requirements for such liability insurance.

e. <u>Commercial General Liability Insurance</u>:

i. Required Insurance

1) During Construction: General Liability Insurance for bodily injury, property damage and personal injury for the benefit of the Project Property. Where the General Liability policy excludes

damage or injury caused by activities related to the presence of lead or asbestos and/or the abatement thereof, Pollution Insurance will be required for an existing Project Property that is being substantially rehabilitated.

2) After Construction: General Liability Insurance, including Products and Completed Operations insurance.

ii. Maximum Deductible: $10,000 deductible.

iii. Amount of Coverage: $1 million per occurrence/$2 million minimum general aggregate limit, with a minimum Umbrella Liability Insurance (above the primary) of:

1) $3 million for structures with 1 to 3 stories; and
2) $5 million for structures with 4 or more stories.

f. Commercial Auto Liability Insurance:

i. Required Insurance: Commercial Auto Liability Insurance covering all automobiles, and including personal injury protection and uninsured motorist liability. When Insurance must be obtained: If the Project Property uses cars, vans or trucks for business purposes, those vehicles must be covered by Commercial Auto Liability Insurance.

ii. Amount of Coverage: $1 million per occurrence.

g. Architects Professional Liability Insurance:

i. Architect's professional liability insurance in the amount of not less than one million dollars ($1,000,000.00) (including contractual liability coverage with all coverage retroactive to the earlier of the date of the Award Agreement or the commencement of the Architects' services in relation to the Project) covering personal injury, bodily injury and property damages. The policy shall include an endorsement naming IHCDA and the FSA and its successors and/or assigns as Certificate Holders.

ii. Comprehensive General Liability Insurance (including limited contractual liability and completed operations) in the amount of not less than two million dollars ($2,000,000.00) covering personal injury, bodily injury and property damage. The policy shall include an endorsement naming IHCDA and the FSA and its successors and/or assigns as additional insured's and certificate holders.

h. General Contractor Liability Insurance: This is to be provided by the general contractor for the construction / renovation of the Project Property and keep in full force until completion of construction / renovation:

i. Evidence from the Contractor of Worker's Compensation insurance, insuring for occupational disease or injury and employer's liability, and covering the Contractor's full liability for statutory compensation to any person or persons who perform work in, on, or about the Project Property construction, including the employees of sub-contractors of any tier, and liability to the dependents of such persons. The policy will be in a form which complies with the worker's compensation acts and safety laws of the state in which the Project Property is located. Worker's Compensation limits shall be statutory; Employer's Liability Limits shall be at least $1 million per occurrence.

ii. Comprehensive General Liability and Property Damage Insurance (including limited contractual liability and completed operations) in the amount of not less than two million dollars ($2,000,000.00) covering personal injury, bodily injury and property damage, and covering products and completed operations for a minimum of three years following completion of construction.

iii. Comprehensive Automobile Liability Insurance, including hired and non-owned vehicles, if any, in the amount of not less than one million dollars ($1,000,000.00) covering personal injury, bodily injury and property damage.

i. Catastrophic Risk and Additional Insurance Coverage's:
The following sections specify additional insurance coverage's required by the Partnership for each Project Property:

i. Business Income/Rent Loss Coverage

1) Required Insurance: Business Income/Rent Loss Coverage.

2) When Insurance must be obtained: All property types—during and after construction.

3) Amount of Coverage: Actual loss sustained or minimum 12 months' gross income/rents for all other projects.

ii. Workers' Compensation

1) Required Insurance: General Contractor's Statutory Workers' Compensation and Employer's Liability Insurance.

2) When Insurance must be obtained: Where employees of the general contractor are required to be covered by Workers' Compensation laws of the state in which the Project Property is located.

3) Amount of Coverage: Employer's Liability with a limit of $1 million and statutory limits for compensation.

iii. Windstorm Coverage

1) Required Insurance

2) If the "All Risk" property damage insurance excludes wind-related events, a separate windstorm insurance policy must be obtained.

3) The policy must include business income/rent loss coverage for a minimum of 12 months even if a state insurance program is providing the coverage.

4) Amount of Coverage: 100% of replacement cost or actual cash value.

5) Maximum Deductible: 5% of the total insured value.

k. <u>Flood Insurance</u>:
The FSA must determine, for every investment proposed to be funded by Award Proceeds, whether any of the improvements are, or are planned to be, located in a Special Flood Hazard Area (SFHA) and must document, or cause the Owner to document, each determination on a Standard Flood Hazard Determination form issued by the Federal Emergency Management Agency ("FEMA") (FEMA Form 81-93). SFHAs are areas designated by FEMA as Zone A or V. The Owner must place a completed copy of the Standard Flood Hazard Determination form in the closing

binder for the Project Property in which Section 1602 Exchange Funds has been disbursed.

i. Required Insurance: Flood Insurance.

ii. When Insurance Must be Obtained: Flood insurance is required if the Project Property is located in SFHA A or V.

iii. Amount of Coverage: 100% of the full replacement cost or, if that is unavailable, then the maximum amount of insurance available under the National Flood Insurance Program (NFIP). Flood insurance should be in the form of the standard policy issued by members of NFIP. An excess Flood or Difference in Conditions (DIC) policy should provide for the difference, if any, between the maximum limit provided by NFIP policies and the full replacement cost.

iv. Maximum Deductible: 2% of the Total Insured Value per building.

P. Financing

1. Construction Financing

a. Commitment: Construction financing must be committed and closed prior to or concurrent with the Section 1602 Exchange disbursement to the Owner and must meet the following criteria:

i. Term: The term of the construction financing, including extensions, should exceed the anticipated construction period and lease-up requirements of the permanent financing by the greater of at least 25% or 6 months; and

ii. Recourse/Nonrecourse: In general, the construction award may be recourse to the Owner, but in no case may it be recourse to the FSA or IHCDA.

b. Security: The documentation related to the construction financing must not obligate IHCDA or the FSA or any of its affiliates to make any representations, warranties, or covenants directly to the lender, or require IHCDA or the FSA or any of its affiliates to sign promissory notes or enter into any documents or agreements with, or for the benefit of, the lender or other third parties, including, without limitation, estoppel certificates, joint funding agreements, inter-creditor agreements, triparty agreements, guaranties, comfort letters, acknowledgments, or equity assignments, or require IHCDA or the FSA to disburse the Section 1602 Exchange funds to anyone other than the Partnership (unless such payment is made directly to an account owned by, and held in the name of, the Partnership).

c. Notice: The construction loan must include the FSA and IHCDA in the notice section.

2. Permanent Financing

a. Commitment: Permanent financing must be committed to the Partnership prior to the disbursement of the Section 1602 Exchange funds; subject only to the exceptions listed below, and must meet the following criteria:

i. Term: All permanent financing must have a minimum term of at least three (3) years;

ii. Interest Rate: Fixed-rate financing is preferred, but variable rate financing is acceptable;

iii. Funding Conditions: The permanent financing must be unconditionally committed to the Partnership with no more than the following conditions for funding:

iv. Construction completion;

v. No more than 90% physical occupancy for a period not to exceed three months;

vi. A DSCR less than or equal to the level underwritten by the FSA; and

vii. Standard lender closing conditions; and

viii. Recourse/Nonrecourse: The permanent financing can be recourse to the Owner and its affiliates. In no instance shall the permanent financing be recourse to IHCDA or the FSA and its affiliates.

b. Security: The documentation related to the permanent financing must not obligate IHCDA or the FSA or any of their affiliates to make any representations, warranties, or covenants directly to the lender, or require IHCDA or the FSA or any of their affiliates to sign promissory notes or enter into any documents or agreements with, or for the benefit of, the lender or other third parties, including, without limitation, estoppel certificates, joint funding agreements, inter-creditor agreements, triparty agreements, guaranties, comfort letters, acknowledgments, or equity assignments, or require IHCDA or the FSA to pay its Section 1602 Exchange funds to anyone other than the Partnership (unless such payment is made directly to an account owned by and held in the name of the Partnership).

c. Notice: The permanent loan must include the FSA and IHCDA in the notice section.

3. Soft Financing

"Soft Financing" (i.e., financing on terms limiting payment of all or a portion of the principal or interest to available cash flow from operations) must be committed to the Partnership prior to the disbursement of Section 1602 Exchange funds and must meet the following criteria detailed in this section.

a. Funding Conditions: The Soft Financing must be unconditionally committed to the Partnership with the following exceptions:

i. Construction completion;

ii. No more than 90% physical occupancy for a period not to exceed three months; and/or

iii. A DSCR less than or equal to the level underwritten by the FSA.

b. Term: The fixed term of the Soft Financing must equal or exceed the remaining Compliance Period and must not provide for forgiveness of any portion of the principal or interest on the loan.

c. Confession of Judgment: Soft Financing documents should not contain provisions permitting the lender to confess judgment on behalf of the borrower upon the occurrence of a default.

Q. Variances

All employees of the FSA and IHCDA are expected to follow the spirit and the intent of the stated Investment Policies and Procedures. IHCDA recognizes, however, that these policies will not fit every situation and that there will be valid reasons to deviate. When it is clearly in IHCDA's best interest, policy exceptions are permitted. Any exceptions to the stated policies and procedures require IHCDA approval.

R. Watch List Criteria and Procedures

The FSA shall be responsible to IHCDA to identify and measure any Project Property that is deemed "Watch List". The FSA will prepare and deliver to IHCDA a quarterly Watch List which will be delivered to IHCDA no later than February 15th, May 15th, August 15th and November 15th of each year.

There are three (3) distinct ways in which a Project Property can be placed on the Watch List:

- Development
- Operational
- Compliance

1. Development

A Project Property may be placed on the Watch List during its Development Phase based upon the following criteria:

Construction Delays: A delay in construction of the Project Property for any reason which causes the Project Property to be three (3) months behind schedule.

Construction Cost Overruns: Revised Construction Budget exceeds 10% of the original contract and the Contingency Reserve has been spent.

Leasing Delays of All Units: Delay in leasing any units that causes the Project Property to be four (4) or more months behind schedule.

Unresolved Mechanics Liens: There exists a filed lien on the Project Property that is not covered by indemnity nor is cured within 3 months.

Change in Sources and Uses of Funds: There is a change of 3% or greater of the total Sources and Uses of Funds or $100,000, whichever is greater.

Change in Qualifying Units: There is a change in timing of qualifying of any of the units.

Litigation: The Project Property or any member of the Key Principals of the Project Property is subject to litigation specifically related to the Project Property.

2. Operational Phase

A Project Property may be placed on the Watch List during its Operational Phase based upon the following criteria:

Rental Delinquency: The Project Property experiences a greater than 7% rental delinquency of Effective Gross Income (EGI).

High Vacancy: The Project Property experiences a vacancy rate of greater than 10% for three (3) consecutive months.

Negative Debt Service Coverage: Net Income (Free Cash Flow), after payment of all operating expenses and "must pay" debt is negative for three (3) consecutive months. Any draw on the debt service reserve fund or operating reserve fund that is not replaced within thirty (30) days of being drawn.

Unpaid Real Estate Taxes: Any real estate taxes that are past due.

Insurance: The Project Property has any expired insurance policy.

Delinquent Mortgage: Any "must pay" debt service that is more than thirty (30) days late.

Mortgage Default: The Project Property is in default on any mortgage or subordinated debt.

Deferred Maintenance / Extraordinary Repairs: Any repairs that are not budgeted and are in excess of 5% of EGI or $25,000, whichever is less.

Replacement Reserves: There have been draws on the Replacement Reserve and no deposits to the Replacement Reserve have been made for three (3) consecutive months.

Physical Deterioration and / or Natural Disasters: There has been a physical deterioration of the Project Property since the last site visit by the Asset Manager or there has occurred a natural disaster.

Debt Service Coverage: Debt Service Coverage is less than 1.10:1.00 on "must pay" debt for three (3) consecutive months.

Unauthorized Debt: There are unauthorized liens or debt on the Project Property.

3. Compliance Issues

A Project Property may be placed on the Watch List for Compliance Related issues based upon the following criteria:

Reporting: The Project Property's GP or sponsor has not delivered a quarterly report.

Site Visit: The Asset Manager has not visited the Project Property in twelve (12) or more months.

Transfer of Ownership: The Project Property experiences a change in ownership for any reason.

Unit Non Compliance: Any qualified unit in the Project Property that is out of rent compliance for more than sixty (60) days.