NYC HDC

NEW YORK CITY
HOUSING DEVELOPMENT
CORPORATION

MEMORANDUM

To: The Chairperson and Members

From: Eric Enderlin
President

Date: May 26, 2017

Subject: FFB Preservation Program Pilot & FHA Risk Share Loss Reserves

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I am pleased to recommend two proposals related to the Corporation's FHA-Risk Sharing program, also called Housing Finance Agency ("HFA") Risk Sharing program under Section 542 of the Housing and Community Development Act of 1992. First, the Members are requested to authorize the use of unrestricted funds of the Corporation to make certain loans, described herein, in an amount not expected to exceed $200,000,000, which will be subsequently sold to the Federal Financing Bank ("FFB"), a federal corporation under the supervision of the U.S. Department of the Treasury, to facilitate the preservation of projects within the Corporation's portfolio (the "FFB Preservation Program Pilot" and/or the "Pilot"). Second, the Members are requested to authorize the reduction of the Corporation's elective FHA Risk Share loss reserves. Establishing the Pilot will facilitate broader use of this important preservation tool across the Corporation's portfolio, and allow the Corporation's staff to more efficiently transact while more effectively managing credit risk. This memorandum will set forth conforming loan terms and programmatic requirements for new loans participating in the proposed FFB Preservation Program Pilot.

Background

The Members of the Board originally approved the Corporation's participation in the FFB program and the use of the Risk- Sharing program for FFB in September 2014. Under the FFB program, the FFB purchases a beneficial ownership interest in mortgage loans that are originated by the Corporation and insured with FHA Risk-Sharing mortgage insurance that obligates each party to cover 50% of the total loss following a claim on the FHA Risk-Sharing mortgage insurance.

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Since 2014, the Corporation has sold beneficial ownership interests in five mortgage loans to the FFB. FFB financing has become an increasingly attractive and low-cost execution to preserve the Corporation's investments in affordable housing, addressing critical capital needs and preserving long-term affordability. The proposed FFB Preservation Program Pilot is critical to preserving developments within the Corporation's existing portfolio which are facing significant capital needs and increasing market pressure to exit affordability.

FFB Preservation Program Pilot

Members are being asked to authorize the making of loans, in an aggregate amount not expected to exceed $200,000,000, to projects currently in the Corporation's portfolio and in an individual loan amount less than $50,000,000 ("Pilot Eligible Project"). All, or a portion, of the permanent loans may be initially funded with the unrestricted funds of the Corporation with the expectation that the Corporation would be replenished upon FFB's purchase of the loan.

The terms of the FFB Preservation Program Pilot are consistent with the Corporation's conservative underwriting standards, and are detailed in the attached FFB Preservation Program Pilot Term Sheet, as approved and/or amended by the Corporation's Credit Committee. All loans will require the Corporation's Credit Committee approval. Loans greater than or equal to $50,000,000 or loans for projects that are not in the Corporation's portfolio would be presented to the Members for authorization at a later date. The Corporation expects that the average loan amount for the conforming Pilot projects is approximately $17,300,000.

In the interest of establishing conservative and transparent terms, this memorandum proposes a $200,000,000 limit on the loan volume delivered to FFB under the Pilot. Under this proposal, the Corporation's staff would be required to seek additional loan authority from the Members to originate and deliver conforming Pilot loans to FFB in an aggregate amount that exceeds $200,000,000. For further transparency, the Audit Committee will be notified of the number of loan closings, as well as the total volume of originations made under the FFB Preservation Pilot Program annually at the end of Corporation's fiscal year.

The proposed programmatic lending authority is an essential component of the Pilot, as it will enable the Corporation to proactively seek out preservation opportunities, quickly address physical and financial distress within the portfolio, and compete with conventional loan products that would otherwise enable Corporation portfolio developments to exit the program.

FHA Risk Share Loss Reserves

The Corporation's loan loss reserve requirement was established when the Corporation began using FHA Risk-Sharing in November 2011. At the time staff elected to establish a conservative level of loss reserves equal to 20% of the insured amounts to mitigate claims under the program. Based on the Corporation's top-tier Housing Finance Agency designation, no reserves were required at that time, and no reserves are required today. The proposed reduction to the loss reserves are structured to comply with the FHA reserve requirements for participants without a top-tier designation which are calculated based on a percentage of the insured amount of each loan, as follows:

$500,000 minimum, plus
1% of the unpaid principal balance less than or equal to $50,000,000
0.75% of the unpaid principal balance between $50,000,000 and $150,000,000
0.5% of the unpaid principal balance above $150,000,000

The reduced reserves more appropriately reflect the underlying credit risk of the FHA-insured portfolio, will eliminate unnecessary strain on the Corporation's balance sheet and will have no adverse impact on the Corporation's credit ratings. Reducing the loss reserves will enable the Corporation to expand its use of FFB financing without straining the Corporation's balance sheet and free up capital to support the Mayor's Housing Plan.

Risk and Risk Mitigation

The FFB Preservation Pilot will facilitate preservation of the Corporation's existing investments in affordable housing and pose limited financial risk to the Corporation. This risk is partially mitigated by the use of FHA Risk-Sharing mortgage insurance, and the Corporation's conservative underwriting standards and strong asset management. Risk is further mitigated by the $200,000,000 origination limit for the Pilot, as well as the ongoing monitoring and annual financial reporting.

The proposed reduction in loss reserves for the Corporation's FHA Risk Share portfolio also poses limited financial risk to the Corporation. This risk is partially mitigated by conservative loss reserves equal to those required of HFAs without a top-tier designation. Risk is further mitigated by the strong performance of the FHA Risk Share-insured portfolio, the Corporation's conservative underwriting standards and strong asset management.

As a result, the Corporation believes that these changes are structured to effectively insulate the Corporation from credit and real estate risks.

Action By The Members

The Members are requested to approve i) the making of loans to Pilot Eligible Projects in an aggregate amount not to exceed $200,000,000, initially funded with the unrestricted funds of the Corporation until purchase of the Loans by the FFB, ii) the execution by an Authorized Officer of the Corporation of mortgage-related documents and any other documents necessary to accomplish the financing and iii) a reduction to the loss reserves established for the Corporation's FHA Risk Share portfolio.

Attachments

A. Examples of Potential Projects Eligible for the FFB Preservation Program Pilot
B. FFB Preservation Program Pilot Term Sheet

Attachment A

Examples of Potential Projects Eligible for the FFB Preservation Program Pilot

Project Name	Borough	Units	Estimated Permanent Mortgage	Estimated Closing Date
Carol Gardens	MH	315	$23,000,000	2017
Seaview Towers	BX	461	$25,000,000	2017
Bay Towers	QN	375	$24,192,000	2017
David Chavis Senior Apts	MH	153	$16,000,000	2018
Goodwill Terrace	BK	202	$10,100,000	2018
Crotona Ave Proj	QN	86	$3,500,000	2018
2111 Hughes Avenue	BX	72	$3,500,000	2018
Jennings Street Apts	BX	85	$3,500,000	2018
Tanya Towers	BX	138	$6,900,000	2018
Clinton Towers	MH	396	$19,800,000	2018
Hamilton House	MH	176	$8,800,000	2018
Evergreen Gardens	MH	355	$17,750,000	2018
Bedford Gardens	BX	647	$32,350,000	2018
Seagirt	BK	917	$45,850,000	2018
Park Lane	BX	352	$17,600,000	2018
Henry Phipps Plaza East	BX	104	$5,200,000	2018
16 Projects		**4,834**	**$263,042,000**	

NYC Housing Development Corporation (HDC) Term Sheet

FFB Preservation Program Pilot

(Taxable Financing)

Program Description

HDC's FFB Preservation Program Pilot, through partnerships with HUD and the U.S. Treasury's Federal Financing Bank ("FFB"), provides taxable, fixed-rate, first-position mortgage financing for the preservation of existing projects in HDC's portfolio. Under the initiative, the FFB purchases beneficial ownership interests in mortgage loans originated by HDC and insured with FHA mortgage insurance under Section 542(c) of the Housing and Community Development Act (commonly known as Risk-Sharing). No HDC second mortgage subsidy funds are available; however, subordinate financing is permitted subject to HDC approval.

Eligible Projects

Acquisition, moderate or substantial rehabilitation, and equity take-outs to facilitate the preservation of affordable housing developments in HDC's portfolio. Eligible projects must have existing HDC financing or an HDC regulatory agreement.

Eligible projects must qualify as affordable housing with at least 20% of the units set aside for households earning up to 50% of Area Median Income (AMI); or 25% of the units set aside for households earning up to 60% of AMI.

HDC Regulatory Agreement requires occupancy and rent restrictions to be maintained through the term of the loan, and in no event less than 15 years, or 20 years for equity take-outs. More restrictive occupancy restrictions of other public subsidy programs may apply.

First Mortgage

Loan Amount:

$5,000,000-$50,000,000. Smaller or larger loans may be considered on a case-by-case basis.

Debt Coverage: Rental Housing - 1.15 on all financing, or greater as required by permanent credit enhancer. Cooperative Housing - 1.0 on all financing, or greater as required by permanent credit enhancer.

Loan to Value: 80% maximum. Value will be determined using a capitalization rate that does not consider the value of below market financing. Value based on an independent MAI appraisal acceptable to HDC.

Interest Rate:

35 year or 40 year Fixed Rate. Interest rates established prior to pricing by FFB based on market conditions. Interest rate can be locked following the issuance of a Firm Approval from HUD for a period of up to 60 days.

Underwriting Rate:

Approximately 220 basis points over the 10-Year U.S. Treasury. Underwriting rate is inclusive of 20 basis points for HDC servicing and 37.5 basis points for mortgage insurance.

Term:

Moderate Rehabilitation: 35 year with a 35 year amortization schedule.
Substantial Rehabilitation: 40 year with a 40 year amortization schedule.

	Amortization: Fully amortizing. Prepayment: 10-Year prepayment lockout from date loan sale to FFB. Prepayment during the 11th or 12th year shall be subject to a prepayment penalty of 2% and 1%, respectively. HDC Fees: Commitment Fee: 0.75% of First Mortgage amount. Costs of Financing: $25,000 plus two months debt service on First Mortgage. Construction Monitoring: $2,500-$5,000 per month based on total number of units, buildings and scattered sites.
Mortgage Insurance	FHA mortgage insurance with 50/50 Risk-sharing agreements under Section 542(c) of the Housing and Community Development Act is required. Upfront 1st year FHA Annual Premium: 0.375% of First Mortgage.
Rehabilitation Requirements	Rehabilitation requirements based on 15 year capital needs as determined by an approved Integrated Physical Needs Assessment ("IPNA") and approved by HDC. Substantial Rehabilitation, as defined in the HUD Multifamily Accelerated Processing (MAP) Guide, shall be subject to Davis-Bacon wage rates.
Equity Take-outs	Equity take-outs subject to the following conditions: • No defaults in the last 12 months. • 20-year affordable housing deed restriction. • HDC approved IPNA with funds escrowed for all necessary repairs and reserves funded for future capital needs, as determined by HDC. • For projects receiving Section 8 Housing Assistance Payment (HAP) contracts, owners must renew HAP contract(s) for a 20-Year term and set aside existing and post-refinance HAP residual receipts to reduce future HAP payments.
Closing Conditions	Conditions precedent to loan closing include (but are not limited to): • HUD Firm Approval Letter for FHA Mortgage Insurance. • HDC approved IPNA. Please refer to the Pre-qualified list for IPNA vendors. • Completed and satisfactory disclosure documents for principals and known investors in the project, as required by HDC. • Completed and satisfactory HUD 2530 Clearance. • Completed and satisfactory National Environmental Policy Act (NEPA) review as required by Section 542C FHA Risk Share. • Completed and satisfactory State Environmental Quality Review Act (SEQRA) review. • Completed and satisfactory third party reports with reliance letters to HDC. • Financial statements and credit reports. • Historic building operating statements. • Final architectural plans reviewed and approved by HDC and HPD BLDS, if applicable. • Commitment letter from other subordinate lenders, if applicable. • Evidence of all other required funding.

- Note, mortgage, assignment of leases and rents, and UCC's.
- Certifications and attorney opinion letters.
- Satisfactory organizational documents for the borrower and related entities.
- Property and liability insurance in form and substance acceptable to HDC.
- Good and marketable title, free and clear of encumbrances except as permitted by HDC.
- Title insurance and survey in form and substance acceptable to HDC.
- Evidence of real estate tax benefits.
- Evidence of compliance with zoning and all applicable codes.
- All other conditions as required by the mortgage insurer.

Documentation will require that HDC be named a beneficiary on a number of documents, including but not limited to insurance certificates and completion guarantees.

Other

Design Guidelines:

If applicable, projects must meet HPD's Design Guidelines for New Construction and Substantial Rehabilitation.

Building Green:

If applicable, projects must meet Enterprise Green Communities (EGC) standards. HDC encourages all projects to comply.

All projects will be required to retain an HDC pre-qualified benchmarking service provider to track utility usage for heating, electric and water. Benchmarking expense may vary by project.

Real Estate Tax Benefits:

See HPD Tax Incentive Program guidelines for more details on benefits/eligibility.

Maximum Developer Fee:

A developer's fee is only allowed when tax credits are used or funds are combined with other public subsidy programs allowing such fees, as approved by HDC. As described in the HPD Qualified Allocation Plan (QAP), total developer fee is not to exceed 15% of improvement costs (excluding developer fee, reserves, syndication and partnership expenses) and 10% of acquisition costs for tax credit projects. Consultant fees should be paid from the developer fee. The total fee should be deferred during rehabilitation and paid from cash flow during the permanent period, as allowable by IRS rules and the governing QAP.

Marketing:

Marketing plan to be approved by HDC and HPD on jointly financed projects. Marketing process and income certification overseen by HDC.

Must comply with HDC Marketing Guidelines and HUD's Affirmative Fair Housing Marketing Plan. Guidelines are available online, or by contacting HDC's Asset Management Department:
E-mail: hdcmarketing@nychdc.com or Phone: 212-227-5500.

Recourse:

Non-recourse to Borrower, except for environmental indemnity and standard non-recourse "carve out" guaranty for fraud and related misrepresentation.

Collateral:
First on land and improvements.

Subordinate Financing:
Other subordinate liens permitted with HDC approval of terms.

Reserves:
Capitalized Operating Reserve: Minimum of $1,000 per unit collected at permanent loan conversion.

Replacement Reserve: Minimum of $250/unit/year increased with CPI. Smaller projects may require higher replacement reserves.

Taxes, insurance and water/sewer escrows are also required.

M/WBE Build Up:
Projects contemplating capital work must comply with HPD MWBE Build Up procurement requirements, as necessary.

Items Required for Project Review

For consideration, submit project information, including:

- Location and description of site and proposed improvements (including address, borough, block and lots).
- Project history including existing mortgages, use restrictions, tax exemptions and rental assistance including status of any Section 8 HAP or other contracts.
- Preliminary pro-forma including hard and soft costs, unit distribution, current rents and income levels, projected rents, outstanding debt balance and rate, estimated rehabilitation costs, and other financing sources.
- Development team (borrower, contractor, consultant, and management company) and listing of experience and principals.
- Identification of tax credit investor and/or syndicator, if applicable.
- Identification of current or proposed real estate tax exemption.
- Statement of required government and third party approvals

Contact Information

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HDC, in its sole discretion, may, at any time and without prior notice, terminate the program, amend or waive compliance with any of its terms, or reject any or all proposals for funding.

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