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Program Policy Notice: OCD 15-03

Replaces Policy Notice OCD 13-01
and 13-05 Affordability Requirements (July 2013)

SUBJECT: Finance Mechanisms and Affordability Requirements for Office of Community Development Program-Funded Projects

ISSUED: December 31, 2015

DISTRIBUTED TO: Office of Community Development Award Recipients and their Affiliates

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PROGRAM POLICY

This program policy applies to all housing activities completed with federal dollars through all Office of Community Development (OCD) programs.* Finance mechanisms for activities funded with program income must follow at least the minimum funding source requirements and must be defined in the grantee's local Policies and Procedures Manual as approved by OCD.

GENERAL REQUIREMENTS

Except for Habitat for Humanity projects, all grantees with applicable activity types mentioned below must abide by the recapture affordability provisions as outlined in 24 CFR 92.252 and 92.254. All loans must be secured by using a mortgage lien recorded on the property for the length of the loan and/or affordability period. **Grantees are prohibited from adding <u>increased</u> change order amounts either to original mortgage liens or by adding supplemental mortgage liens. Any change order amount that decreases the original mortgage lien must be amended to reflect actual project hard costs. Mortgage liens must be recorded within 30 days of execution.**

<u>Exception:</u> Any change order amount that <u>increases</u> or <u>decreases</u> the original assistance amount for the Rental Rehabilitation activity or the direct assistance portion of the Homeownership activity, must be reflected in a supplemental mortgage lien and be recorded within 30 days of execution.

The following is a summary of OCD's finance mechanism requirements for individual housing program activities:

<u>Owner Home Repair</u>

Home Repair assistance must be provided to the homeowner as either a grant or a 0 percent interest, 100 percent deferred/declining (50 percent annually), two-year term, forgivable loan.

<u>Rental Home Repair</u>

Program participants (landlord/owners) can be low and moderate income or non-low and moderate income. Rental Home Repair project loans must be provided to the property owner as a 0 percent

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* Does not include projects funded with program income, Targets of Opportunity Grant Program funds or projects funded through the Ohio Housing Finance Agency.

interest, 100 percent deferred/declining (50 percent annually), two-year term, forgivable loan. When grantees provide rental home repair assistance to a low- and moderate-income landlord/owner or nonprofit agency, the following will apply:

- Grantees may choose to require match funds – up to 50 percent of the project's hard costs – from the landlord based on a percentage designated in the grantee's local Policies and Procedures Manual.
- Monthly amortized loans are prohibited.

When grantees provide rental home repair assistance to a non-low- and moderate-income landlord/owner, the following will apply:

- Grantees must require 50 percent of the project's total calculated hard costs as match funds from the landlord.

Tenant-Based Rental Assistance (TBRA)

Grantees must provide Tenant-Based Rental Assistance to the tenant as a grant.

Owner Rehabilitation

The U.S. Department of Housing and Urban Development (HUD) does not require an affordability period when providing Owner Rehabilitation assistance. However, all program funds provided for Owner Rehabilitation assistance are subject to the following loan term requirements:

- Assistance must be provided as a 0 percent interest, deferred/declining loan, with a term between two and five years.
- The loan must decline in equal increments annually over the loan term.
- After the loan term, no more than 25 percent of the original assistance amount can be held as a lien that becomes due when the homeowner transfers property ownership and/or no longer occupies the home as the primary residence. Alternatively, the loan can be 100 percent forgiven at the end of the loan term.
- Monthly amortized loans are prohibited.
- Grants are prohibited.

Homeownership (non-Habitat for Humanity)

All loans from financial institutions (i.e. banks, credit unions, etc.) and grantees, if implementing a self-financing mechanism, to low-income households purchasing homes under the Homeownership activity must, at a minimum, meet the requirements outlined in OCD's Underwriting Process and be documented in the project file.

For Homeownership projects, the direct subsidy and rehabilitation assistance requirements are separated in this document. The requirements below apply to the portion of the assistance provided as a direct subsidy to the buyer (the amount of assistance that enabled the buyer to purchase the property, e.g., down payment assistance, closing costs, mortgage buy-down, etc.). The portion of Homeownership assistance provided for rehabilitating the purchased property is subject to the Owner Rehabilitation activity finance mechanism requirements described above. The appropriate requirements for each portion of the Homeownership activity (direct subsidy and rehabilitation assistance) must be reflected separately in the recorded mortgage lien. Alternatively, separate mortgage liens may be recorded. In either case, mortgage liens must be recorded within 30 days of execution. Homeownership direct subsidies are subject to the following requirements:

- Must meet the affordability requirements of 24 CFR 92.254.

- Affordability subsidies must be provided at a reasonable level, in accordance with the HOME Final Rule of 24 CFR 92.254(f), OCD assistance limits, and 2 CFR 200.
- Assistance shall be provided as a 0 percent interest, deferred/declining loan for the entire affordability period.
- The loan must decline in equal increments annually over the loan term.
- No more than 50 percent of the direct subsidy amount can be held as a lien that becomes due after the loan term when the homeowner transfers property ownership. Alternatively, the loan can be 100 percent forgiven at the end of the loan term.
- Monthly amortized loans are prohibited.

Rental Rehabilitation

Program participants (landlord/owners) can be low and moderate income or non-low and moderate income. When grantees provide program assistance to a low- and moderate-income landlord/owner or nonprofit agency, the following will apply:

- The assistance must meet 24 CFR 92.252 affordability requirements. Grantees may choose to require match funds – up to 50 percent of the project's hard costs – from the landlord based on a percentage designated in the grantee's local Policies and Procedures Manual.
- Grantees must provide assistance as a 0 percent interest, deferred loan for the entire affordability period. Rental rehabilitation project loans must not decline during the affordability period. Loans can be 100 percent forgiven when the affordability period ends. Alternatively, grantees may hold up to 25 percent of the original assistance amount as a lien that becomes due upon property sale or transfer.
- Monthly amortized loans are prohibited.

When a grantee provides a rental rehabilitation subsidy to a non-low and moderate income landlord/owner, the following will apply:

- The assistance must meet the 24 CFR 92.252 affordability requirements. Grantees should require match funds – up to 50 percent of the project's hard costs – from the landlord based on a percentage designated in the grantee's local Policies and Procedures Manual.
- Grantees will provide assistance as a deferred or direct loan for the entire affordability period. Rental rehabilitation project loans must not decline during the affordability period. Grantees can forgive 100 percent of the loan when the affordability period ends. Alternatively, grantees may hold up to 100 percent of the original assistance amount as a lien.

Regardless of whether the Rental Rehabilitation activity is CDBG- or HOME-funded, OCD requires grantees to adhere to the HOME requirements found at 24 CFR 92.252, 92.203 and 92.504.

New Construction in conjunction with Habitat for Humanity Assistance

Grantees can provide a program subsidy to Habitat for Humanity affiliates for constructing or rehabilitating a home to be sold to a low-income household. Principal, interest, taxes and insurance, after program assistance, must not exceed 30 percent of the household's total monthly gross income, as calculated for determining income eligibility. When providing a program subsidy to Habitat for Humanity projects, all grantees must abide by the resale affordability provisions as outlined in 24 CFR 92.254. The property must be sold to a subsequent low-income (80 percent of Area Median Income (AMI)) purchaser. The following resale requirements will apply:

- Resale requirements must ensure that the home will be sold to a low-income family and the property will continue to be used as their principal residence for the remainder of the affordability period.

- For the housing to remain affordable, the subsequent purchaser’s monthly principal, interest, taxes and insurance payments cannot exceed 30 percent of the gross income for a family with an income between 30 and 80 percent of median income for the area.
- Deed restrictions or other similar mechanisms must be used to guarantee the resale restrictions (24 CFR 92.254).
- In the event of foreclosure, the subsequent low-income owner will inherit the remainder of the affordability period. If not purchased by a low-income owner, the project will be considered noncompliant, and the grantee must repay any outstanding HOME funds invested in the project to OCD.
- The affordability period is based on the total amount of HOME funds invested in the housing, including any development subsidy.
- Grantees must ensure that, if the property is sold during the affordability period, the price at resale provides the original HOME-assisted homebuyer a fair return on investment. Grantees shall determine the fair return on investment by using the following calculation:

    - The original homebuyer’s initial investment (i.e., any down payment), plus any investment in capital improvements made by the original homebuyer that may add value to the property. This total shall then be multiplied by the percentage change in the Consumer Price Index (CPI) over the period of ownership to determine a fair rate of return for the original buyer. This fair rate of return is then added to the owner’s initial investment and any applicable capital improvement investments. The total amount shall be considered as the homebuyer’s fair return on investment. Capital improvements are defined as improvements made to the home outside of general maintenance items. Actual capital improvement costs must be documented by the original homeowner’s receipts for materials and labor.

- In the event that the resale price necessary to provide fair return is not affordable to the subsequent buyer, additional HOME funds may be invested in the project. Investing additional HOME funds will require grantees to establish a new affordability period.

Length of Affordability Period - Homeownership (non-Habitat for Humanity), Rental Rehabilitation, and New Construction in conjunction with Habitat for Humanity Assistance

The affordability period is based on the amount of HOME funds provided as direct assistance for the recapture option or total amount of HOME funds for resale option. The following table must be used for determining the affordability period for **Homeownership (non-Habitat for Humanity), Rental Rehabilitation, and New Construction in conjunction with Habitat for Humanity Assistance.**

Assistance per Unit or Buyer	Affordability Period
$1,000* - $14,999	5 years
$15,000 - $40,000	10 years
More than $40,000	15 years

*There is a $1,000 minimum expenditure requirement on all HOME-funded projects, including Owner Rehabilitation mentioned above. TBRA is exempt from this requirement.

Requirements for Returned and Recaptured Funds and Program Income

Grantees must comply with the following requirements regarding managing returned funds, recaptured funds, and program income.

Homeownership (non-Habitat for Humanity), Rental Rehabilitation, and New Construction in conjunction with Habitat for Humanity Assistance

Returned Funds

If the grantee receives funds during the grant period (i.e., start date of the grant agreement to the final performance report date), the funds are considered returned and the grantee may reallocate the funds to another eligible project or return the funds to OCD if they cannot be reallocated.

Recaptured Funds

If the grantee receives funds after the final performance report date, but prior to OCD issuing the fiscal grant closeout letter, the funds are considered recaptured and must be returned to OCD.

If the grantee receives funds after OCD issues the fiscal grant closeout letter, but before the unit's affordability period ends , the funds are considered recaptured and the grantee may reallocate the funds to another eligible project. However, no administrative dollars may be used to administer the recaptured funds in the future. Therefore, the recaptured funds must be tracked separately from administration.

Program Income

If the grantee receives funds after the affordability period, the funds are considered program income and the grantee may keep the funds, reallocate them to another eligible project, and use administrative dollars to administer the funds.

Loan payments (i.e., a required monthly repayment of funds to the program) the grantee receives any time during or after the grant period are considered program income**.** In such situations, the grantee may use administrative dollars to administer those funds.

Owner Rehabilitation, Owner Home Repair, and Rental Home Repair

Program Income

If the grantee receives funds any time during or after the grant period, the funds are considered program income. The grantee may keep the funds and use administrative dollars to administer the funds.

<u>Noncompliance of Affordability Requirements</u> – Homeownership (non-Habitat for Humanity), Rental Rehabilitation and New Construction in conjunction with Habitat for Humanity Assistance

Failure to comply with the resale or recapture requirements means that:

1) the original HOME-assisted homebuyer no longer occupies the unit as his or her principal residence (i.e., unit is rented or vacant);
2) the rental unit (rental rehabilitation) is no longer occupied by an eligible tenant, or
3) the homebuyer sold the home during the period of affordability and the grantee did not enforce the applicable resale or recapture provisions.

In cases of noncompliance under either resale or recapture provisions, the grantee must repay any outstanding HOME funds invested in the project to ODSA. The amount subject to repayment is the **total** amount of HOME funds invested in the project (direct subsidy, rehabilitation costs, soft costs, etc.) minus any HOME funds already repaid (i.e., principal payment on a HOME loan). Any interest paid on the loan is considered program income and cannot be counted against the outstanding HOME investment amount. Noncompliance with principal residency requirements by a homebuyer under a recapture provision is not a transfer. Consequently, the amount the grantee must repay is not subject to proration or other reductions included in its recapture provisions.

The grantee must repay the HOME investment in accordance with 2 CFR 92.503(b)(3) whether or not it is able to recover any portion of the HOME investment from the noncompliant recipient. Therefore, it is crucial for the grantee to have enforcement mechanisms in its written agreements to protect its investment and minimize its risk in HOME-assisted projects in the event of noncompliance.

<u>HOME Written Agreements</u> – All HOME-Funded Projects

In addition to the mortgage and promissory note, HUD requires a separate written agreement for all HOME-funded activities. Detailed loan terms must be included in the mortgage lien and promissory note. For each applicable activity type, all grantees must abide by the HOME Written Agreement requirements outlined in 24 CFR 92.504. Projects funded solely with CDBG or OHTF do not require a separate written agreement.

The HOME written agreement must outline the terms and use of the HOME funds. Agreements for Homeownership (non-Habitat for Humanity), Rental Rehabilitation and New Construction in conjunction with Habitat for Humanity activities must include affordability requirements details. The agreement must ensure the home remains affordable for the required period. HUD requires direct subsidy beneficiaries to continue to live in the assisted home even if any or all of the assistance is repaid before the affordability period ends.

Each HOME written agreement must be signed by the person receiving assistance and the grantee. It is acceptable for the grantee to designate, in a legal binding document, a representative to sign agreements on their behalf. **HOME written agreements are not required to be recorded.**

<u>Net Proceeds</u> - All Activities

If a property transfers during an affordability period and the recapture requirements are imposed, the grantee must evaluate the net sale proceeds. The net sale proceeds are the sales price minus superior loan repayment and any closing costs. When the recapture requirement is triggered by a housing unit sale (voluntary or involuntary) and there are no net proceeds or the net proceeds are insufficient to repay the program investment due, the grantee can only recapture the net proceeds amount, if any. The recorded mortgage lien to secure the program assistance must contain language that reflects the net proceeds requirements.