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Program Policy Notice: OCD 15-03

Replaces Policy Notice OCD 13-01

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

ISSUED: July 1, 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 be defined in the grantee's local Policies and Procedures Manual as approved by OCD. The policy is effective beginning with the State Fiscal Year 2015 funded grants (July 1, 2015).

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 change order amounts either to original mortgage liens or by adding supplemental mortgage liens. Mortgage liens must be recorded within 30 days of execution.**

Exception: Any change order amount that increases or decreases the original amount of assistance for the Rental Rehabilitation activity or the direct assistance portion of the Homeownership activity, must execute a supplemental mortgage lien and record the supplemental mortgage 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. The loan must decline in equal increments annually over the loan term.

<u>Rental Home Repair</u>

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

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 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. 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 term of the loan.
- 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.

The following table must be used for determining the period of affordability for the remaining activities.

Assistance per Unit or Buyer	Length of the 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.

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- and moderate-income households purchasing homes under the Homeownership activity must meet the following requirements:

- The interest rate should be fixed. An Adjustable Rate Mortgage is acceptable only if the maximum interest rate does not cause the principal, interest, taxes and insurance to exceed 30 percent of the household's gross monthly income and the lender provided the certified maximum interest rate.
- 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.
- Balloon payments are prohibited.

For Homeownership projects, the direct subsidy and the 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 unit, e.g., down payment assistance, closing costs, mortgage buy-down, etc.). The portion of Homeownership assistance provided for rehabilitating the purchased unit 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 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.

- The affordability requirements of 24 CFR 92.254 must be met.
- 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, the grantee's Policies and Procedures Manual, 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 original assistance amount can be held after the loan term as a lien that becomes due when the homeowner transfers property ownership. Alternatively, the loan can be 100 percent forgiven at the end of the loan term. If the homeowner violates the principal residency requirement during the affordability period, the total outstanding HOME investment must be repaid to OCD.
- 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 at the end of the affordability

period. 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 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 at the end of the affordability period. 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, 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- and moderate-income household. 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. 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. The following requirements will apply:

- Resale requirements must ensure the home will be sold to a low- and moderate-income family, and the property will continue to be used as a principal residence for the balance of the affordability period.
- For the housing to remain affordable, the subsequent purchaser's principal, interest, taxes and insurance monthly payments cannot exceed 30 percent of the total monthly gross income, as calculated for determining income eligibility.
- Deed restrictions or other similar mechanisms must be used to guarantee the resale restrictions.
- The affordability period must be based on the total amount of HOME funds invested, including any development subsidy.
- Grantees must waive resale provisions if the homeowner defaults on the first mortgage and the lender initiates foreclosure proceedings.
- Grantees must ensure that, if the homeowner sells the property during the affordability period, the resale price provides the original HOME-assisted homebuyer a fair return on investment. Grantees must determine the fair return on investment by using the following calculation:

    - Original homebuyer's initial investment (i.e. any down payment) **+** any investment in capital improvements made by the original homebuyer that may add value to the property **x** the percentage change in the Consumer Price Index (CPI) over the ownership period.

This fair rate of return is then added to the owner's initial investment and any applicable investment in capital improvements. The total amount must be considered as the homebuyer's fair return on investment.

Note: Capital improvements must be defined as improvements made to the home outside the scope of general maintenance items. Value of capital improvements must be documented by the original homeowner's receipts for materials and labor.

Affordability Subsidy

Projects funded in conjunction with Habitat for Humanity affiliates are exempt from the following Affordability Subsidy requirements. The affordability subsidy is the difference between a loan value (consistent with what the homebuyer can afford in a mortgage payment) and the sales price (based upon the household's monthly housing costs). The total monthly housing costs (principal, interest, taxes and insurance) must not exceed 30 percent of the household's total monthly gross income, as calculated for determining income eligibility. Grantees must provide affordability subsidies at a reasonable level, in accordance with OCD's assistance limits, the grantee's Policies and Procedures Manual and 2 CFR 200. The affordability subsidy is direct assistance to the buyer. This type of subsidy would apply to homeownership and new construction in conjunction with Habitat for Humanity activities. The method for determining the buyer's direct assistance amount must be documented in the file; and include underwriting guidelines in accordance with 24 CFR 92.254(f), OCD assistance limits, the grantee's Policies and Procedures Manual, and 2 CFR 200. Affordability subsidies must be charged to the mortgage lien.

Down-Payment Assistance

Grantees may provide an affordability subsidy as down-payment assistance. The down-payment assistance amount must be based upon the amount of funds necessary to close the loan with the financial institution for the first mortgage, including closing costs. The prospective homebuyer must be required to contribute at least $500 cash toward the loan closing or related costs (i.e., insurance, homebuyer counseling, etc.). The homebuyer's required cash contribution may be waived if the homebuyer is providing sweat equity to the project. The method for determining the buyer's direct assistance amount must be documented in the file; and include underwriting guidelines in accordance with 24 CFR 92.254(f), OCD assistance limits, the grantee's Policies and Procedures Manual, and 2 CFR 200. The amount of down-payment assistance must be charged to the mortgage lien.

Net Proceeds

If a property transfers during an affordability period and the recapture requirements are imposed, the grantee must evaluate the net sale proceeds. The net 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.

HOME Written Agreements

In addition to the mortgage and promissory note, HUD requires a separate, stand-alone written agreement for each HOME-funded loan that utilized a direct subsidy and required an affordability period. This requirement applies to homeownership and new construction in conjunction with Habitat for Humanity activities. The HOME stand-alone written agreement must outline the terms for HOME funds, including details of the affordability requirements. This stand-alone agreement ensures the home remains affordable for the required period. HUD requires beneficiaries of homeownership and new construction in conjunction with Habitat for Humanity activities to continue to live in the assisted home if any or all of the assistance is repaid before the affordability period ends. For all other HOME-funded activities, a stand-alone written agreement is not required. However, detailed loan terms must be included in the mortgage lien and/or promissory note. For each applicable activity type, all grantees must abide by the HOME Written Agreement requirements outlined in 24 CFR 92.504.