

USING SECTION 108 AS A FINANCING TOOL WITH LIHTCs

NOVEMBER 12,
2020



LLSC LOCAL INITIATIVES
SUPPORT CORPORATION

TRAINING SESSION



Overview of Webinar

- Review of the Section 108 Loan Guarantee Program
- Process for Applying for a 108 Loan with HUD
- Use of the 108 Loan Program with a LIHTC Transaction
- Case Study: City of High Point, NC
- Case Study: Sacramento Housing Authority, CA
- Side Bar: Kansas City, MO
- Questions



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OVERVIEW

SECTION 108 PROGRAM

- CDBG Grantees receive direct access to the program; non-entitlement communities can access Section 108 through the state. Businesses and non-profits can access the program by partnering with their local government or state entitlement.
- Project must meet National Objective requirements of CDBG program
 - LMI Benefit
 - Elimination of Slum and blight
 - Urgent need



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OVERVIEW

SECTION 108 PROGRAM

- Grantee must pledge its CDBG funds to secure the Section 108 loan
 - Other collateral typically will be required, such as a lien on the project property or other City owned property.
- Grantee must propose a financially feasible transaction
- Grantee can access Section 108 loans in an amount up to 5 times the most recent annual CDBG allocation



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OVERVIEW

SECTION 108 PROGRAM

Section 108 loans can be used for multiple purposes:

- Economic Development; Housing; Public Facilities; Infrastructure
- For Housing, new construction generally not eligible for Section 108 funding unless the developer is a Community Based Development Organization, and the activity is part of a community economic development project.
- Housing rehabilitation that meets national objectives criteria is an allowable use of Section 108 funds
- Alternatively, Section 108 funds can be used to fund infrastructure, site acquisition, demolition, relocation costs for an eligible New Construction project if work is performed by a CDBG Grantee and land is in public ownership. Our case studies will look at a couple options of how this can work.



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Process of Applying for HUD Section 108 Guaranteed Loan

- Confirm eligibility of use of Section 108 funds
 - Program Requirements – National Objective, Eligible Activity, Public Benefit Standards (if applicable)
- Obtain all appropriate grantee governmental approvals
- Section 108 application coordinated with local field office
 - Submitted to Both Field and HUD National Offices
- Complete HUD required environmental review (24 CFR Part 58)



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Funding of HUD Section 108 Guaranteed Loans

- Loan term – Up to 20 years
- Initial loan period funded with variable interest rate
 - Variable interest rate set at 3-month LIBOR plus 20 basis points
- Upon aggregation of sufficient size of Section 108 portfolio; HUD arranges for sale of obligations with serial maturities guaranteed under the Section 108 program
 - Bond Market Sale With HUD Guarantee
 - Rate Fixed Based on Market Conditions



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Section 108 Loan and LIHTCs

Can you use a Section 108 Loan to assist a LIHTC deal?

Yes, if structured the right way.

- ✓ A local jurisdiction can use a Section 108 loan to provide additional gap financing to a LIHTC deal
- ✓ Must meet all requirements just discussed
- ✓ Can be used to finance acquisition of property or site improvement work completed by grantee
- ✓ Can be used to pay for costs of rehabilitating residential structures (single or multifamily)



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Section 108 Loan and LIHTCs

Issues to consider:

- ✓ **Coordination of Approval Timeframes:** City/County and Developer must look at timing to obtain Section 108 loan approvals with HUD against state and federal requirements for applying for LIHTCs and also deadlines for starting and completing construction.
- ✓ **Repayment:** Most LIHTC properties are structured with a priority for very low rents and do not have a lot of cashflow. Repayment of the Section 108 loan most likely from the City's pledge of future CDBG allocations or other non-project revenue.
- ✓ **Collateral:** Unless the Section 108 Loan is in first position (unlikely) the City will need to provide additional collateral as determined by HUD based on project characteristics.



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Questions?



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First Case Study

Avondale Trace Apartments

High Point, NC



Avondale Trace Apartments Highpoint, NC

- New construction of 72 units for families with rents at 40-60% AMI. Includes clubhouse, playground and picnic area.
- 9% LIHTCs from North Carolina
- Capital Stack: Conventional first mortgage, NC Rental Production Program Loan, NC Work Force Housing Loan, City of High Point 108 Loan, deferred developer fee and LIHTC equity (9% credits)
- Section 108 Loan used by City to acquire the land and pay for site improvements



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Deal Economics and Key Players: Avondale Trace Apartments

Project Development Costs

Land Acquisition:	\$425,000
Land Improvements:	\$1,801,229
Construction:	\$5,875,068
Soft Costs:	\$1,167,329
Developer Fee:	\$ 936,000
Reserves/Other:	\$244,959
 Total Uses:	 \$10,449,585

Permanent Financing

Conventional First Mortgage Loan:	\$1,028,000
NCHFA Rental Production Program:	\$800,000
City of High Point Section 108 Loan:	\$650,000
NCHFA Work Force Housing Loan:	\$250,000
Deferred Developer Fee:	\$226,010
LIHTC Equity Proceeds:	\$7,495,575
 Total Sources:	 \$10,449,585

Section 108 Uses:

Acquisition and Site Improvements

Key Players:

- City of High Point, NC
- Wynnefield Properties (Developer)
- North Carolina Housing Finance Agency



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Motivation of City of High Point – Section 108 Loans

- Leverage limited gap financing
 - HOME funds used in other projects
- New rental properties at affordable rents
 - (72 Units – Rents \$322 to \$827/month)
- Leverage resources available in NC
 - LIHTCs / LIHTC Equity
 - State Based / NCHFA grants and loans
- Address affordable rental housing shortage in City
- Tax base enhancement



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City of High Point: Leverage of Section 108 Loans- Fourth Transaction

2020 CDBG Allocation	5:1 Leverage Capability	Avondale Trace Section 108 Gap Loan Amount	Cumulative Section 108 Gap Financing	Avondale Trace Units	Cumulative Units Created
\$939,549	\$4,697,745	\$650,000	\$4,694,000	72	298



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Section 108 Loan Structuring Considerations

- Rental Housing Funding with CDBG Funds is Restrictive:
- ✓ Restrictions on Direct Funding to For-Profit Developers
 - Section 108 Loans - Must Be Carefully Structured
 - Permitted Uses: Acquisition, Site Clearance; and Site improvements - With Municipal Partner

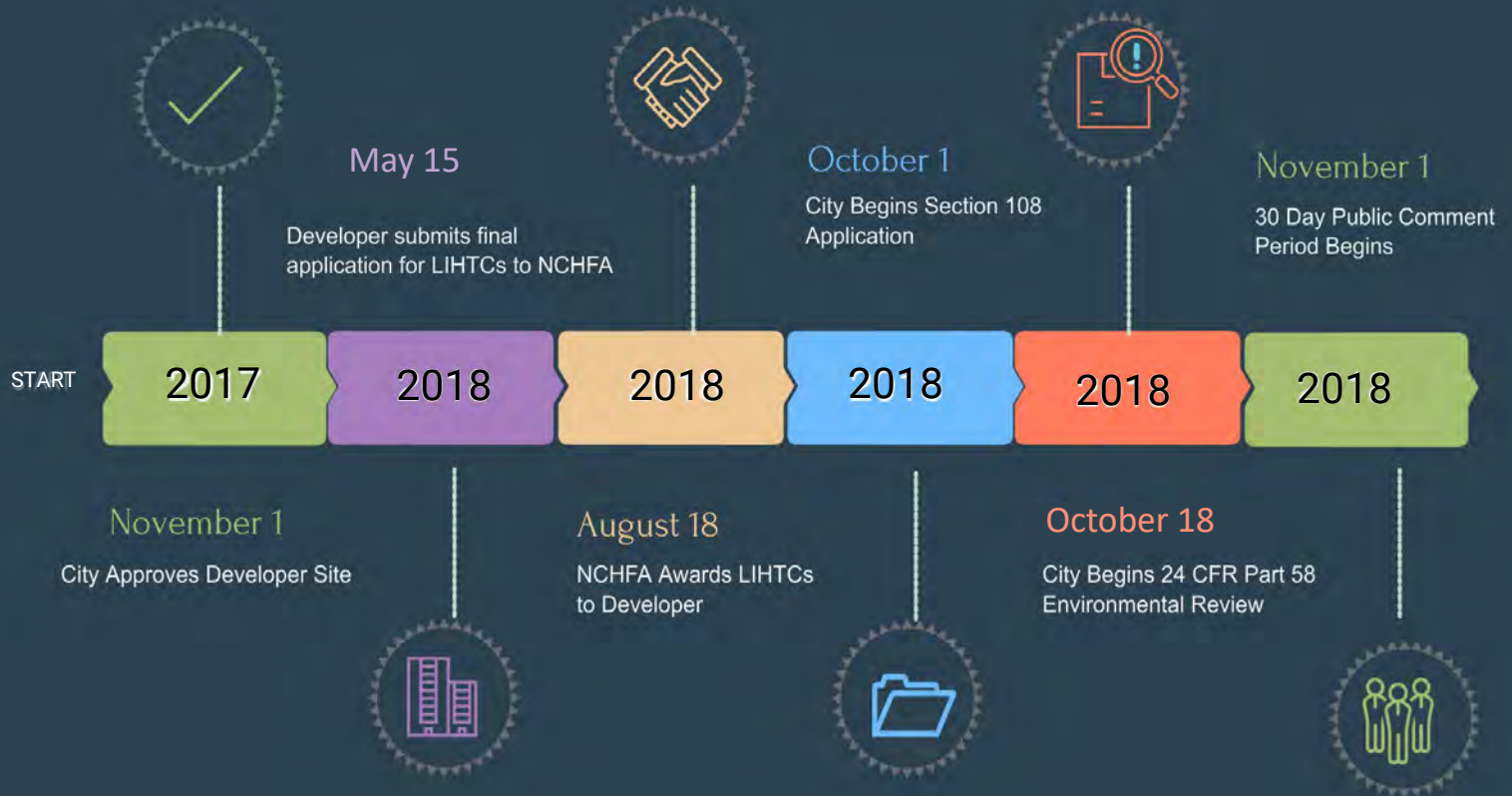
Citation - (24 CFR 570.703(a)or(b)or(f))



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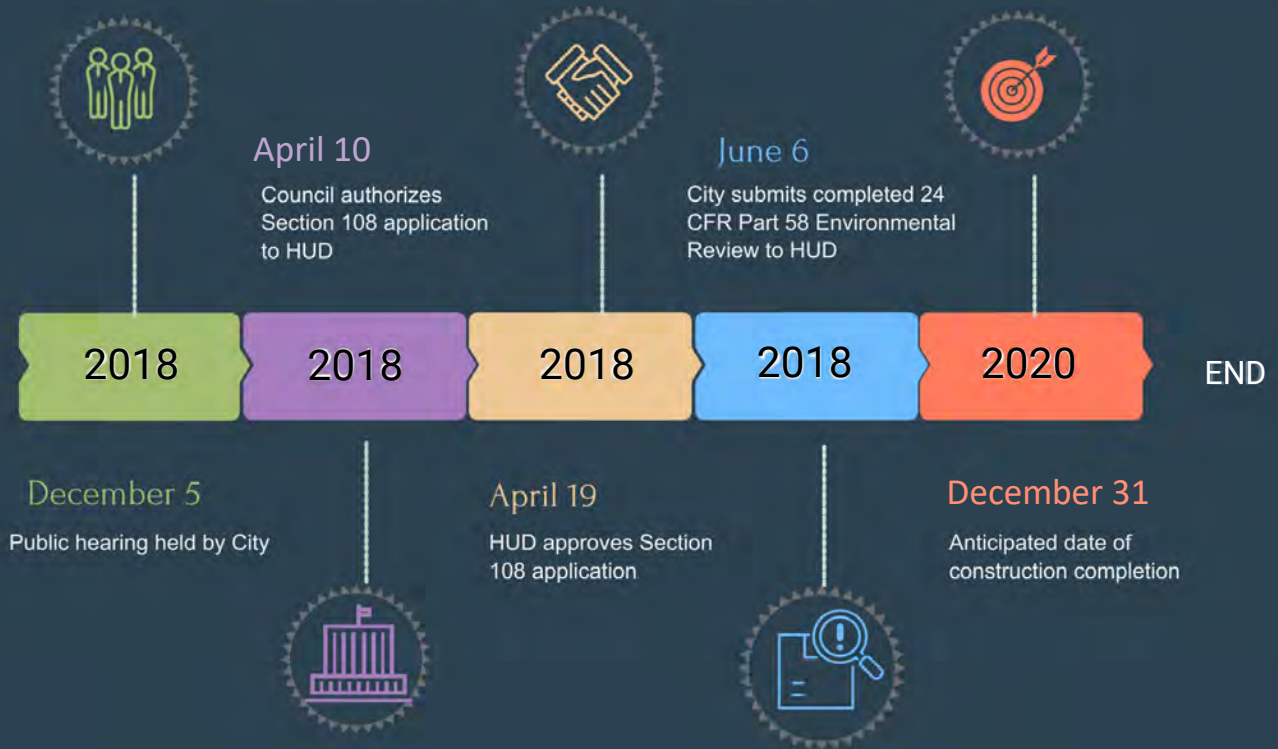
City of Highpoint, NC

Avondale Trace Timeline



City of Highpoint, NC

Avondale Trace Timeline Continued





City and HUD Terms - Construction Period



Phase

HUD Rate to City

Section 108 Capital Cost

Source of HUD Capital

Payment Terms of City

Security

Site
acquisition
and site
improvement
phase

Variable
rate facility

Three month
LIBOR plus
twenty (20)
basis points;
Origination
fee of 2.23%

Money
market
funds

Quarterly
payment of
interest;
annual
payment of
principal

Pledge of first lien
mortgage on site
and improvements;
pledge of future
CDBG funds; best
faith effort of City
to secure
repayment from
General Fund



City and HUD Terms - After Bond Sale



Phase

HUD Rate to
City

Section 108
Capital Cost

Source of
HUD
Capital

Payment
Terms of
City

Security

Completion of
construction/
operating phase

Fixed interest
rate

Rate based on
capital cost in
bond market;
HUD aggregates
multiple Section
108 commitments
prior to bond sale

Bond market
costs for 20 year
facility/remaining
term at time of
bond sale

Semi-annual
payment of
principal and
interest

Pledge of first lien
position of
developer note to
HUD; Secured by
lien on real estate;
pledge of future
CDBG funds; best
faith effort of City
to secure
repayment from
General Fund



City of High Point: Developer Loan Considerations

- Tremendous need for affordable rental housing in City
- Underwriting spearheaded by NCHFA; HUD also underwrites project viability
- Low rents for superior rental housing development
 - City loan 2% interest only – twenty-year term with balloon payment
- Support of City Council / Mayor / City Manager
 - Backstop of HUD Loan with pledge of General Fund of the City



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Avondale Trace Apartments: Conclusions

- Section 108 loan enhanced ability of City to leverage substantial resources for rental housing development
- Development complexities requires coordination by competent developer
- First Section 108 transaction paved way for subsequent projects using the same structure
- Support of local leaders critical to rental housing development goals



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Questions?



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Second Case Study

Mirasol Village Redevelopment

Sacramento, CA



Mirasol Village Redevelopment Sacramento, CA

- Transformation of prior Twin Rivers public housing site into 427 new units for families with rents at 30-80% AMI. Includes 1:1 replacement of 218 public housing units. Will also include neighborhood park, community garden, community space, and fitness center. Being completed in 5 phases.
- 4% credits through a tax-exempt bond allocation from state agency.
- Capital Stack for Blocks B & E: Conventional First Mortgage, State AHSC Loan, HA Ground Lease, HA Choice Neighborhoods Implementation Grant, SHRA Infrastructure Loan, deferred developer fee and LIHTC equity (4% credits)
- Section 108 Loan used by City and SHRA to fund and manage completion of infrastructure work.



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Mirasol Village: Deal Economics and Key Players

Project Development Costs

Ground Lease from HACOS:	\$176,000
Infrastructure:	\$3,839,644
Construction:	\$41,539,770
Soft Costs:	\$9,086,935
Developer Fee:	\$2,702,296
Financing Costs:	\$3,600,325
Other:	\$2,061,557

Total Uses: \$64,119,045

Permanent Financing

Agency First Mortgage Loan:	\$13,537,756
HCD (State) AHSC Loan:	\$12,933,015
HACOS Ground Lease Loan:	\$158,400
HACOS CNI Loan:	\$8,000,000
SHRA Infrastructure Reimb. Loan (108):	\$3,839,644
Deferred Developer Fee:	\$615,374
LIHTC Equity Proceed:	\$25,034,756

Total Sources: \$64,119,045

Section 108 Uses: Infrastructure Work



Key Players:

- Housing Authority of the County of Sacramento (HACOS)
- Housing Authority of the City of Sacramento (HACS)
- Sacramento Housing and Redevelopment Authority (SHRA)
- City of Sacramento
- McCormack Baron Salazar (Developer)



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Motivation of City of Sacramento

- Limited City resources for housing development.
- City CDBG funds could be leveraged to provided needed dollars for infrastructure work at Mirasol Village, and still have CDBG funds available for other projects in future years.
- Leverage other Federal and State sources to move deal to closing.
 - HUD Choice Neighborhoods Implementation Grant
 - State Affordable Housing Loans/Soft Financing
 - LIHTCs
- End result: A transformed mixed income community to replace the obsolete Twin Rivers public housing property and create a more connected and diverse community in the River District after years of planning.



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City of Sacramento: Section 108 Leverage

2020 CDBG Allocation	5:1 Leverage Capability	Mirasol Village Section 108 Loan Amount	Mirasol Village Units
\$4,800,000	\$24,000,000	\$16,490,000	427



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Section 108 Loan Structuring Considerations

- Funding Rental Housing with CDBG Funds comes with restrictions:
- ✓ Restrictions on Direct Funding with For-Profit Developers
 - Section 108 Loans - Must Be Carefully Structured in this scenario
 - Permitted Uses: Acquisition, Site Clearance; and Site improvements – Completed by municipal partner

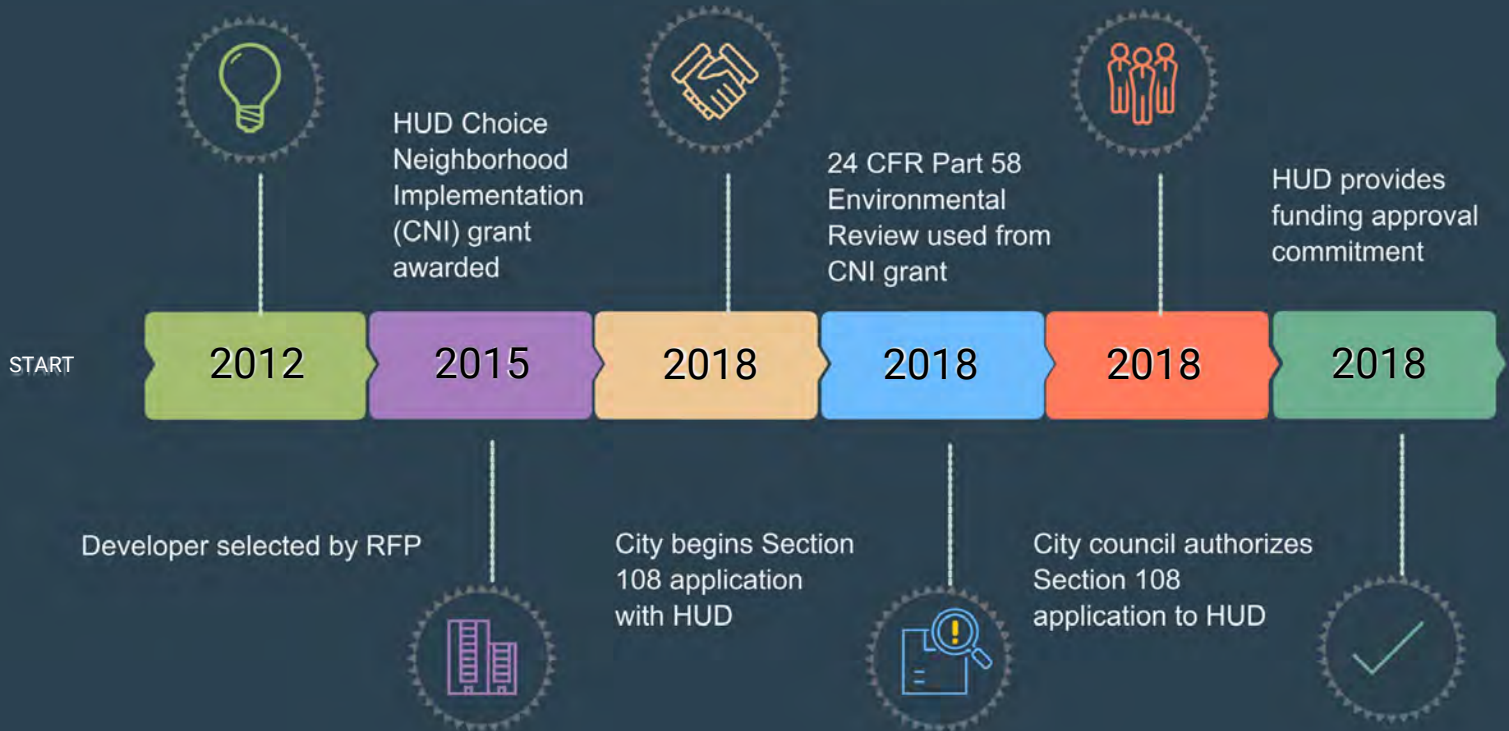
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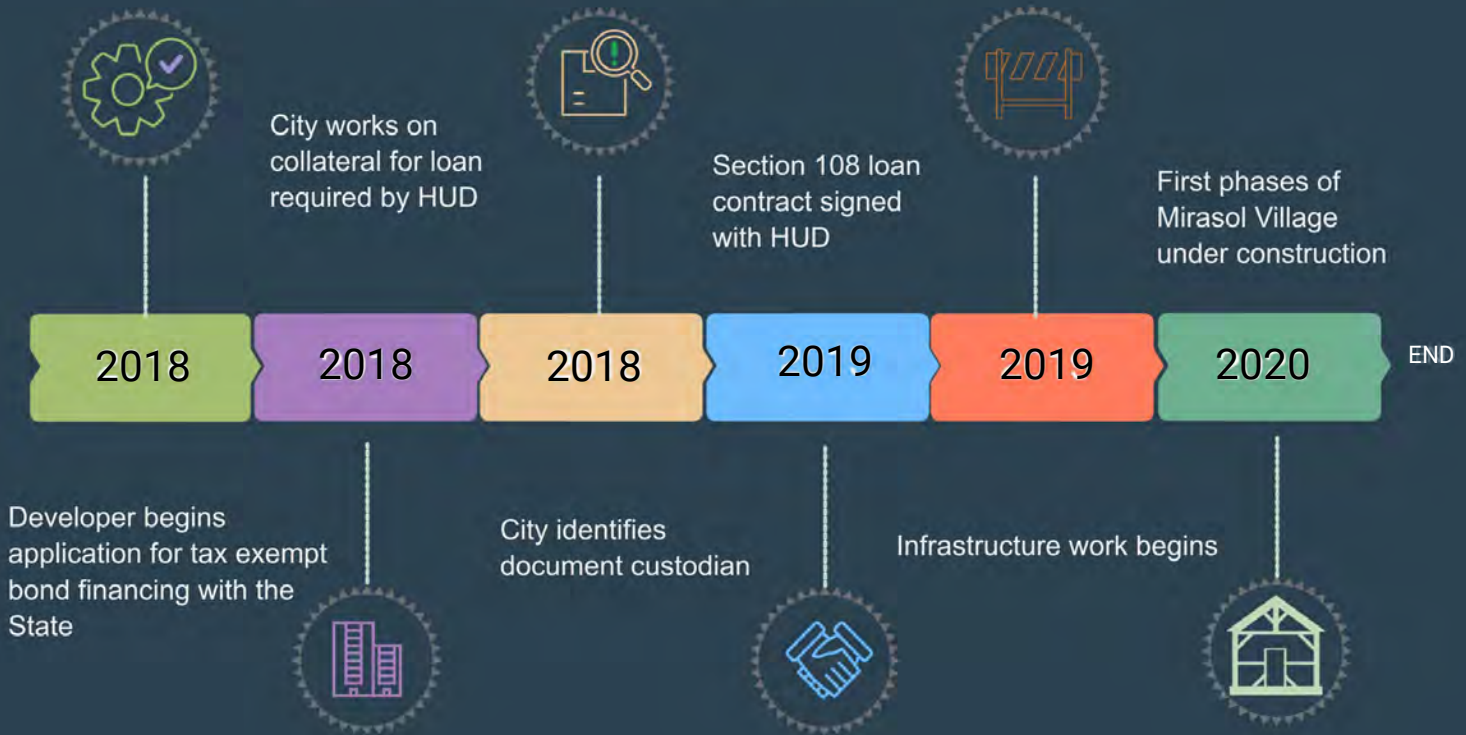
Sacramento Housing and Redevelopment Agency

Mirasol Village Timeline



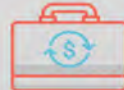
Sacramento Housing and Redevelopment Agency

Mirasol Village Timeline Continued





City and HUD Terms - Construction Period



Phase

HUD Rate to
City

Section 108
Capital Cost

Source of
HUD
Capital

Payment
Terms of
City

Security

Used for
infrastructure
costs; Drawn
down on
phased basis

Variable
rate facility

Three month
LIBOR plus
twenty (20)
basis points;
Guarantee
fee of
2.365%

Money
market
funds

Quarterly
payment of
interest;
annual
payment of
principal

Pledge of first
lien position on
other SHRA
owned property
equal in value to
1.25 times the
loan amount;
Pledge of future
CDBG funds



City and HUD Terms - After Bond Sale



Phase

HUD Rate to
City

Section 108
Capital Cost

Source of
HUD
Capital

Payment
Terms of
City

Security

Completion of
construction/
operating phase

Fixed interest
rate

Rate based on
capital cost in
bond market;
HUD
aggregates
multiple Section
108
commitments
prior to bond
sale

Bond market
costs for 20 year
facility/remaining
term at time of
bond sale

Semi-annual
payment of
interest and
annual
payment of
principal

Pledge of first lien
position on other
SHRA owned
property equal in
value to 1.25 times
the loan amount;
Pledge of future
CDBG funds



Mirasol Village: Section 108 Loan Terms to Developer

- Infrastructure work completed by City with funding from HUD Section 108 Loan.
- Costs allocated per phase of redevelopment and included in project budget.
- SHRA received an Infrastructure Reimbursement Loan at AFR, payable from cashflow.
- Cashflow after payment of first mortgage is split 50% to developer fee and then 50% to payment of all soft loans.
- Any cashflow from the property will be applied to pay the 108 Loan to HUD, but more likely here that the loan will be repaid from a portion of the City's CDBG allocation (per schedule on note this is equal to an average of 16% of the allocation(ranging from 9% to 23% annually)).



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Mirasol Village: Conclusion

- Section 108 Loan provided needed financing for \$16 million in infrastructure improvements for an important redevelopment project spearheaded by the City.
- City had to provide 1st position real estate as collateral and a pledge of future CDBG Funds resulting in long discussions at City Council.
- Timing worked on this multi phase project that utilized an allocation of bonding authority and automatic 4% LIHTCs.



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Side Bar

Faxon School Historic Rehab

Kansas City, MO



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Kansas City: Faxon School Historic Rehab

- Kansas City used the Section 108 Loan Program in 2014 to provide financing for the historic rehabilitation of the Faxon School into 45 units of senior housing.
- Developer is a for-profit.
- Units credited as replacement for affordable units lost upon demolition of another HUD financed property.
- City used HUD 108 Loan funds as a first mortgage loan to the property. HUD had retained their lien on title from the demolished property, precluding a loan from a private lender.
- The Section 108 loan was in first priority position. Loan was structured as a 30-year amortizing loan at market interest rate with a 20- year term to match City's 108 repayment obligation to HUD.
- Project Capital Stack included Federal and State LIHTCs, federal and state historic credits, and soft loans from the City.



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Questions?



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CONTACT INFO

SPEAKERS:

Jim Beachler

JMB Preservation Advisors

Jim@jmbpa.com

Karen Przypyszny

National Equity Fund

Kprzypyszny@nefinc.org

Michael McNair

City of High Point, NC

michael.mcnaire@highpointnc.gov

RESOURCE STAFF:

Joseph Baietti

HUD Section 108

Joseph.A.Baietti@hud.gov

Victoria Johnson

Assistant Director

Sacramento Housing and
Redevelopment Agency



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