HUD Section 108 Loan Guarantee Program as a Financing Tool:

Program Design and Application Process Webinar

June, 2016

Transcript

Part 1

Hugh Allen: Hello. The Department of Housing and Urban Development is pleased to present the second recorded webinar about the Department's Section 108 Loan Guarantee Program. This is our second of three in a series that you have the opportunity to view. The title of this webinar is "Program Design and Application Process". The program staff that are participating in the presentation of this webinar are Shahidat Abbas, myself, Hugh Allen, Bennett Hilley and Jorge Morales. We also have special guest presenters from the City of Cleveland, Ohio and from the State of Iowa.

In this webinar, we are going to give you a brief program overview of the Section 108 Loan Guarantee program and also give you information that will be most useful for you for making application either for a single project that you would wish to finance or for a loan fund in which you would be doing many more loans and guaranteed transactions in your community. We think you'll find this information most useful and helpful for you to present to HUD an effective presentation and representation of what you're trying to do in your state and/or your community.

Also we are going to preview with you some of the additional information and webinars that we have available for you coming up and be sure and watch and look at our underwriting webinar. We also we have the first webinar (2016 Update) you can go back to and review for your reference. And there will be other information and materials including some project profiles and summaries that will be useful for you as you think through the type of the funding and financing you'll need in your community.

In this webinar today we want to emphasize to you that we're talking about loan guarantees. That is the full faith and pledge of the United States government for the notes that you will be

issuing locally, your promissory notes, and these are not grant funds we're talking about. We Don't confuse this program with the Community Development Block Grant, this is about loan guarantees.

Furthermore, what will be helpful to you is you'll find that the Section 108 Loan Guarantee program fits within the framework of the Community Development Grant program so you are going to be seeing requirements and things that you're familiar with, that you've been using in implementing your Community Development Block Grant program. And also the key thing is you are going to learn how a state or a unit of local government or insular area can access some very low cost financing through the capital market by HUD issuing its full faith and credit, its federal loan guarantee for your notes.

One of the key features that you'll want to keep in mind is that this is a noncompetitive application that you'll be submitting to the Department of Housing and Urban Development and also that this application process is always open. It is a rolling application process. It's always open, 365 days a year, except for holidays and weekends.

Another feature that you'll want to focus on is this—when you make this application to HUD you are not being required to pledge the full faith and credit of your government, either state or local government, for the repayment of the Section 108 Guaranteed Loan. This is really a limited liability program, so keep that in mind. And also one of the best features of this program is that you can get five times the amount of your current block grant in this low-cost financing. So if you're getting $1 million a year in Community Development Block Grant funding then you'll be able to get $5 million dollars in Section 108 Guaranteed Loan funding.

The other aspect about this program to be thinking about is this— there are generally three broad types of project developments that you can use this financing for. Much of what we're going to talk about during this presentation is already familiar to you. It's going to be organized around economic development type projects; those projects that create jobs, increase tax wealth to the government, public facilities that are available to members or their community and also the rehabilitation of housing.

So now I'm going to turn the presentation over to Bennett Hilley who will give you the next key points that you'll need to focus on.

Bennet Hilley: Thank you so much Hugh for that overview of the program and getting us started today. So now we're going to move on to general program design considerations. So before you even apply for a 108 Loan Guarantee, what should you be thinking about? And we're always encouraging communities to take a step back and keep in mind the bigger picture. 108 may not always be the right resource or the right financing tool for your community's needs or for that particular need you're looking at at this moment in time.

So here are some key questions. Does Section 108 financing really make sense for this project or program you are considering right now? One of the biggest ones which we encourage communities to really think about is, do you or do your partners that are going to work with you on this project or loan fund really have the capacity to not only underwrite the loans but also administer a loan fund for the long term? And that not only means financial management but monitoring of that portfolio.

So a few other questions that we just wanted to point out to begin with. Another one is 108 is really an ideal resource for a project that is going to be revenue generating. Because it is a loan so you want cash flow to be able to repay that loan. So you either want to target 108 for one of those types of projects, or if you have a larger project, let's say perhaps water and sewer improvements that just can't wait in your community. You can't spend it over time like you would with your $1 million CDBG funds, so instead you really need $5 million up front to pay for those improvements and then you'll repay it over time, either with CDBG or perhaps another public resource.

And then the last item we really want you to think about is whether you have the capacity and whether you started doing some of the pre-submission requirements. Of course this funding is federal so it's related to the CDBG program requirements so you have several pre submission requirements. You also need to do certain steps in the citizen participation process. So be thinking of those before you even start applying and review those and the program regulations.

So as a continuation of the big picture, let's think about the key first steps you need to do before you even start applying or put in an application to HUD for 108 financing. The first one is to review your community strategy, then you want to think about organizational arrangements and I'm going to go into each one of these in more detail in the following slides. And the third one you want to think about is program design. Are you applying for an individual project or are you applying for a larger loan fund so you can fund a portfolio of projects?

Let's start with community strategy. The first thing to think about when you are looking at 108 as a financing tool is to take a step back and really think about what your community's needs are because 108 is just another tool in your toolbox to address those needs. So you really want to think about your most recent comprehensive plans and what needs and goals those outline for your community. If someone comes to you looking for 108 financing make sure that whatever their project is, that it is connected to what your general community goals are. And also a key thing is to think about what's already in play in your community. Are there ongoing initiatives or programs or targeted neighborhoods where a lot is already happening where 108 could be a great resource to connect with those efforts?

The next key thing to consider after considering what your general community strategy is and what your needs are is who's going to manage this program. What are going to be the organizational arrangements involved? Are you as the loan guarantee recipient or the state or local community— are you going to be the one administering the program in house with your own staff or your own economic or community development department? Or, are you going to instead be using a subrecipient such as a local nonprofit affordable housing developer, community development corporation or CDFI (community development financial institution)? Or, are you going to be using and working with another public entity? So that could be your redevelopment authority or perhaps your public housing authority, or even economic development authority. So you have lots of options. You can structure your program in several different ways and it could even be a hybrid.

Now we're going to move on to the fun part and we're going to start getting into the nitty gritty of how to apply for the program. So first I'm going to give an overview before I pass it to Shahidat and Jorge who are going to go into depth on what the application components are.

First we're going to talk about individual projects and how to put in a Section 108 Loan Guarantee application for just one particular project. This is the approach used by a majority of borrowers in our program. Your application is just for that one project. It can be a larger scale project with multiple components. So you could have a mixed use development or you could have a whole neighborhood strategy but you come in with the details on that project or that grouping of those activities.

We really require a level of detail and specificity in those applications so we can truly underwrite them and understand that they are ready to go. And for individual project applications, after HUD approval, the guaranteed loan would then be used by the recipient or re-lent to a third party borrower for these projects.

Here are just a few examples and I'm not going to read through all of them, but these are actually past or current examples of 108 projects just to give you the idea that it can be something as simple as a typical transportation improvement project such as sidewalk repair, but it could be as complicated as you see here, conversion of a former power plant into an educational and recreational site for sailing, adventure sports, museum and amenities. Or even the conversion of a former historic school building into affordable rental housing. So we can span a variety of activities here, so you can be as simple or as complicated as you want to be as long as you fit within the program requirements.

The other way you can come in with an application is for a loan fund. And this is when the application comes in and it doesn't have quite as much specificity or detail as one that would be for a specific project. You come in more with community development objectives and specific types of activities you're going to be funding but you don't necessarily have to identify the individual transactions that are going to take place in a loan fund. For this one HUD provides approval and a commitment for the overall loan fund, but then you still need to come in with a

more specific update afterwards to your field office. But we'll get into these details a little bit later in the presentation.

And here are some example loan fund objectives. Just as we said with the project specific, it can really be as straight forward as you want it to be such as a small business loan fund or it could be more complicated in terms of certain types of projects where you want to provide gap financing or where you want to encourage healthy food retail development in food deserts. So it's really up to you what you want your loan fund to look like.

Now we are going to continue on with how to apply for a 108 loan guarantee. First we're going to start out with individual project applications since that's the type of application we see most frequently and then we'll move on to how to apply for a loan fund.

Let's get started. So you'll see on this slide these are the six primary steps that we've organized the process into and we're going to cover each of these in more depth in the upcoming slides. But to give you a quick overview, here they are so you can see them all at once.

The first step here is to really evaluate the projects you're thinking about applying for Section 108 Loan Guarantees in terms of your community strategy and whether these projects are actually going to help address your community's needs and challenges. So we've just thrown a few out here that we're seeing that come in quite often and the challenges that our communities are facing these days. Which could be aging infrastructure, where a community's bridges need rebuilding, or you need to do water and sewer updates, or it could even mean updating your roads so you have complete streets, that you have sidewalks and you have bike lanes so people can get to work and to school in different ways. It could be the need for workforce or affordable housing. A lot of communities are facing this challenge right now and really needing to rehabilitate affordable housing or build new affordable housing.

And so I've just walked you through a few of them but your community could be facing a variety of challenges, so just make sure before you come in with this application you can connect that—the community development objectives in your community to the application.

Step number two is determining whether the proposed use of funds is an eligible activity under the Section 108 program. For those of you who are familiar with CDBG, none of this will come as a surprise. But here are the four main questions you need to be asking yourselves. One, is the proposed use of guaranteed financing an eligible activity under the Section 108 regulations? Two, does it meet a CDBG national objective? And those are of course, benefit to low and moderate income persons and that is through a variety of ways, addressing slum or blight or, meeting an urgent need in that community and that can be following a disaster or other emergency situation.

Number three is keeping in mind the overall 70% benefit to low and moderate income persons between Section 108 combined with your CDBG. And the fourth one is especially if it's an economic development activity—is it meeting public benefit standards under the regulations? Of course, if you want more information on all of these, they are very much covered on our website and in a number of other TA materials that we have online.

Another component of Step 2 is also making sure that when you're proposing your project that you're considering the cross cutting regulations that will also apply since this is a federal program. This is not a comprehensive list, but here are some key questions you need to be asking yourself. What type of environmental review are you going to need to undertake for this project? And that's going to depend on the nature of the activity. If applicable, and this is mainly for construction of course, who is going to ensure compliance with Davis Bacon? If your project is going to be displacing any residents including tenants and/or businesses, you need to be considering the Uniform Relocation Act requirements. Another example of course is how these funds affirmatively further fair housing, especially concerning the recent rule that HUD has put out.

And now I'm going to pass the mic over to one of our loan officers in the Financial Management Division. I'm going to introduce Shahidat Abbas who is going to start us with Step 3 which is about underwriting projects for financial feasibility.

Shahidat Abbas: Thank you Bennett. The next step, Step Three, is the underwriting of the project for financial feasibility. Is my project ready? Do I have site control? How do I get site control? Is there appropriate zoning? Is there a demand for this project? Please do not "build and assume they will come." Your feasibility study needs to demonstrate that this project will be viable and will be a success. And there are some others— we're not going to go into each and every one of them.

There are two examples of types of loans. Real estate loans and business loans that 108 funds can be used for. For these two types of loans we do offer underwriting guidelines and even a webinar on how to better underwrite these types of projects.

The next step in the process is to ensure that everybody who has a stake in the project is aware of it— your local stakeholders, your citizens, local groups, neighborhood community groups, etc.

So at this point you are ready to submit the application to HUD. Step 5 here is a nice overview of the rest of the process. So you want to notify the Field Office that you intend to submit an application. Submit it to the Field and to Headquarters simultaneously and both parts of HUD will begin the concurrent review. During this process we may have more questions that will come back to the potential borrower so there may be some revisions involved. After that the application is set. HUD will begin the actual approval process and issues the commitment. At this point if the commitment is approved you will get an approval letter from HUD with documents to be sent back to HUD. When you send back those documents and indicate you are ready to actually ready to advance funds we will create a note, contract and other finance documents and send those to you for you to execute and return to HUD. At that point you get financing monies either through our interim or permanent financing vehicle.

So we've covered the application submission process. Now I'm going to dive into the content of the application itself. The first thing to keep in mind is the objective, the big picture goal here. For example, if this is a sewer and water project or to target slum and blight in the community, you want to be very clear about that. And then talk about how this individual project helps to achieve those goals.

Bennett: So in addition to what Shahidat just noted about the community development objectives and how your project is helping to address those, some other big picture items we'll be discussing are what you need to put into the project description. Shahidat will go into more about the project financial information and what we're looking for and some of the other key requirements when you're submitting an application.

So when we say project description, what does that mean? Typically, what we're asking is to get a narrative—this information in a narrative form, so we can read about what you're proposing and what your proposed use of the funds is. But we also want supporting documentation of this. Have you done feasibility studies that show that a community facility is really needed and necessary in that area of town? Or that this business' expansion plans—there is a market for the product that they are expanding to create. Renderings are really helpful so if we can actually see images and see what you are proposing to build on the site—that is also great supporting documentation. Shahidat will discuss in the financial information underwriting reports.

So really the things you have to tell us about are the description of the activities to be financed, noting your eligible activity or activities. And we would love to see a citation from the regulations—that will make it easier for us. The national objectives that you are proposing to meet, and of course, please use the citation as well. And of course, if applicable, how the project meets public benefit standards that are also noted in the regulations. So those are the musts, but as I noted, the more information on the project the better.

Of course we want to know who is actually carrying out the project that you are proposing. Oftentimes it is the borrower directly and we'll see that especially with public facility projects,

but oftentimes it's not. It's an affordable housing developer, or a Community Development Corporation, or some other subrecipient, or even a contractor who is carrying this out because they have more experience with construction, for example. So we just need to know who's carrying it out, what's the project and organizational structure that's really going to administer the program and oversee the activity.

And of course we want to understand the project timeline and development phases. While we're not exactly a bank or typical financial institution, we still want to understand when you need this financing by. When do you expect to close and start getting advances from the Section 108 Program? What is your closing date if you are using a third party borrower? Does that developer or that business need the funding on a specific timeline? If you're building a project with multiple phases, we'd love to understand the development phases. When is predevelopment and site preparation occurring? When is the first building being built? And of course, general estimated start dates, so when is the project going to become operational? When will you lease up the property and when will you start generating revenue to repay the loan?

And now, I'm going to pass this to Shahidat Abbas, who is going to walk you through more of the financial information we are looking for in applications.

Shahidat: So the financial information—this is the meat of the transaction. This is your opportunity to demonstrate to HUD that this is a financially feasible project. What we want to see here is the sources of funds into the project. Are they committed? If there are commitment letters, please submit those as well.

How are the funds going to be used? What is the expected revenue and what are the expenses? If it's a new business there should be projected financials. If this is an existing business that we're supporting here, there should be existing financials. The last two to five years should be submitted along with the application.

Additional financial analysis includes debt service coverage, a ratio analysis, and a loan to value analysis. All of the underwriting materials that you have done—submit those with the application. The more the better. And I won't go into too much detail here because this is just an overview of what we're going to be covering in the financial information section such as the repayment schedule, the need for collateral and the loan financing fee.

Sources. Along with the Section 108 loan guarantee you might be using a loan from a commercial bank, owner equity, or tax credit equity, such as New Market Tax Credits, Low Income Housing Tax Credits, historic tax credits or other state tax credits. You might be using grant funds such as CDBG or other grant funds. There might be other public and private sources, such as TIF, (tax increment financing) or gambling revenue, for example. Tell us about all the different sources of funds, when they are coming into the deal, and if they have been committed to the deal already.

On the uses side, we want to know exactly where the 108 is going to be used in the deal. So there might be other sources of financing. We want to know if the loan is going to finance the acquisition for example, or finance rehabilitation, or finance the construction. But tell us where the 108 is going into the deal.

Loan guarantee financing fee. This is new for those of you who might be familiar with 108. Starting in Fiscal Year 2016, there is a 2.58% fee that is an upfront cost. It's not annual, it's a one-time fee. That fee only applies when you actually advance the commitment. That can be paid from CDBG funds or another source of funding, or it can be financed as part of the guaranteed loan amount.

Repayment. You must indicate in the application the source of repayment. That could be from the project revenues. If it's a non-income producing project it could be from CDBG funds. But you should tell us how you expect to repay the project back and you should also tell us the annual repayment schedule that you want. We don't dictate that to you, so you should tell us how you want to pay it back. But there are some specific terms, such as the loan term may not be more than 20 years.

Collateral. Collateral is required for the Section 108 Loan Guarantee. In addition to the required pledge of CDBG funds,additional collateral is required such as a lien on the property, on a leasehold or a lien on machinery, equipment, accounts receivable or inventory, for example. We want to see in the application what additional security is being pledged. If it is the full faith and credit of the potential borrower, we would like to see a resolution from the authority that says that yes, we can pledge that.

So in addition to the sample collateral I mentioned earlier, other sources of collateral could be tax increment financing, parking revenues, debt or loan reserve or a special taxing district for example. Also guarantees from the third party borrower, if there is one involved— a personal or corporate guarantee. For the guarantee, we will want to see a financial statement from the guarantor, so that we know they actually have the monies to secure this transaction.

Lastly there are certifications that must be submitted along with the application and these are listed in the regulations at 24 CFR 570.704. If you have any questions or need assistance, the Field Office or Headquarters have staff that will be able to help you fill these out. These are forms that actually must be signed by the appropriate authority.

So at this point you submitted the application, it's been approved. Now how do you get your money? Once you tell the loan officer at HUD that the development timeline is about to start and you need to advance your funds, we will create a note and contract for you and send that to you along with other financial documents. You will execute those after a review by your legal counsel, return those to us, and that initiates the actual advancing process.

So HUD is the guarantor of the Section 108 Loan Guarantee and the money actually is going to be coming from the private sector. Also keep in mind that you must record the request in IDIS. We have more information about that available separately on our website.

Part 2

Now I'd like to introduce Tracey Nichols, Director of the City of Cleveland Department of Economic Development at the City of Cleveland, Ohio. Cleveland is an excellent user of the Section 108 loan program and this is a good case study on how to use the program.

Hi, I'm Tracy Nichols. I am Economic Development Director for the City of Cleveland and we're going to talk today about using HUD 108 and in particular, how do you use HUD 108 for job creation and economic inclusion.

If you are setting up a HUD 108 program, if you already originate loans from your department, there is really nothing to add. But if it's new to you, you're really going need to have some type of staff to underwrite the loans. They need to have a finance background. You're going to have to have underwriting guidelines for your staff. You're going to need a lawyer to compete the documents between you and HUD and between you and the Borrower. And a loan committee, somebody volunteers—bankers, business persons, accountants. You always want someone to have a second look at your documents. And then staff to bill for the loans and wire the payments to HUD.

You really should be able to talk to your local HUD office and talk to them about connecting you with a community that has a successful program. And usually they'll give you all their documents, tell you what the makeup of their loan committee is, and really help you get started. Most people I have found in my career have been very generous in sharing information. Borrow all the documents; get their loan Committee makeup… "Oh you have four bankers, that sounds great." Pick their brains. Ask them to help you out. You'll find that people are really kind about that.

Once you have a strategy and guidelines, you really have to talk to your elected officials about what the funds can do to help your community. And really explain what the backstops are and make sure you that can pay back the Community Development Block Grant funds so that there won't be any impact.

In a Neighborhood Revitalization Strategy Area (NRSA) strategy, you come up with a strategy and you find out which areas of your city could be in an NRSA. It's all about just Census tract demographic data, you have to meet certain criteria, and you just start putting together different Census tracts and get the largest contiguous area in your city that is possible. We've done that for our city and then we've set about saying that we have a strategy of what we want to do in our community.

The first is Evergreen Cooperatives. We're working with the Cleveland Foundation; it's our nonprofit partner. To address some of the socio and economic problems of our community in particular we're looking at ex-felons. We know we have a lot of ex-felons in Cleveland and we really want to work to get them gainful employment.

Supporting existing small businesses. We do a lot of storefront and economic development lending for our small businesses. It's just part of our NRSA strategy. You don't have to use HUD 108 to do all the projects you want to do under NRSA.

Health-Tech Corridor Attraction. We have an area that's between Downtown and our university-hospital area and we are working to bring businesses to that area. It was a very blighted area and we've now attracted over 70 businesses to that area and it's been a very successful story and HUD 108 has played a big role for us in that area.

Our Neighborhood Revitalization Strategy Areas are on this slide. You can see all of the Census tract areas, and as I said, what we did was we started out and we looked at which Census tracts we could get in and how we could combine them so that we could get as many Census tracts in the City into the Neighborhood Revitalization Strategy Area.

The importance of the Neighborhood Revitalization Strategy Area is that in these areas, if you're familiar with Block Grant regulations, you now have a presumed low-moderate income benefit. So you don't have to ask every single employee of every business to fill out a form saying what their income level is. That is probably the one form that people hate to fill out as they don't like giving their private information, that's the way they feel because their company

got some money. So when you have a NRSA you don't need to get that form so it makes it a lot easier to do these projects.

For the projects that we're looking at in these NRSA areas, it's harder to get banks to invest in some of these neighborhoods, so HUD 108 plays a big role for us. And we really look at having public private partnerships in order to support our efforts so we're working with hospitals, foundations, community development corporations, etc. So therefore, if we're all working together we'll have more success.

We also pair HUD 108 with New Market Tax Credits. We find that that's a great way to really overcome obstacles of financing. I would say also to take advantage of vacant and underutilized land in close proximity to anchor institutions. That's been a very successful strategy for us. And one of the things that we're doing is creating post incubator space to retain and attract emerging companies. We asked ourselves, "Hey, where do these companies that are being incubated in our hospitals, where do they go?" and what we found out is they were going to the suburbs. So we wanted to create space that would keep them here.

When you're using a HUD 108 strategy in a Neighborhood Revitalization Strategy Area, you have to remember a few things. HUD 108 must be paid back to the federal government. So it really has to be highly secured. We do a few things that are really important and if you can work these into your program it'll really protect you and help make sure you don't have any issues down the road.

The first is we use a debt reserve in the HUD 108 itself. So if you're giving someone a two-million-dollar loan, we might say, "ten percent back," so $200,000. We keep that in a debt reserve and that way if the company has a hard time making the payment we have some funds there to make the payment to HUD.

We ask for a guarantee of a high net worth individual. Sure, developers hate giving personal guarantees. But what we say is, "If you don't believe in the project, why should we?" So we've really been able to get those guarantees and it's helped us a lot.

Positive Arbitrage. What that means is if your HUD rate is LIBOR plus 0.20, we charge LIBOR plus 0.55. That means that with every payment we're getting a little bit of money, that we put in program income, that we put in into a reserve fund. That's helped us a lot when we've had a few loans go bad.

Last is a new tool we've created called a TIF (tax increment financing) debt reserve. We actually put a TIF on to make loan payments or for other economic development purposes. We ran it through our state, Ohio, and we we're able to get that approved and that TIF comes into the City and we collect it as a debt reserve and if we don't need it as a debt reserve we could also use it for other economic development projects in the City.

Doing several low-risk projects allows us to take more risk on a few economic inclusion projects. So you'll see that I'm going to have several projects that I'll show you that have big developers that have deep pockets that are lower risk, and then you'll see a couple of our cooperative projects that are higher risk, because there is no developer in a cooperative. And so it's a little bit different.

Strong Projects. Again, personal guarantees from high net worth individuals, strong collateral, TIF debt reserves, positive arbitrage, and we're accumulating a reserve fund that allows us to do those economic inclusion projects with higher risk such as start-ups, cooperatives, etc.

This is one of our low risk projects. Dunham Square, Midtown Tech Center. This was the site of a used car lot and basically a dumping area, it was vacant. There were submerged basements that had been from former demolitions—it was a nasty area, a brownfield. We were able to take this forward and it was funded in 2009. No bank would touch it. It was a spec building. 128,000 square feet, and we expected to have 150 new jobs; we're currently at 245 just in this building. It's part of our Health-Tech corridor. We used HUD 108 to leverage

New Market Tax Credits. Again it was able to go seven years with interest only which was very important. There was absolutely no bank financing available. City and state were the prime funders with the New Markets.

There's the capital stack in case you want to take a look. We also have a program called the vacant property initiative a forgivable loan that we put in. The developer put in $1.6 million and we were able to put this together. We are collecting .2 percent additional interest on this project as we go. The TIF debt reserve is bringing in $154,000 a year.

Remember, when you do a TIF, it doesn't start coming in until about two to three years after the project starts. The building has to be built and it has to be on the tax roll before you can get that PILOT.

So let's talk a little about economic inclusion projects. These are projects that you really want to do in your community and they're difficult to get done. You really want to target people; for us it was formerly incarcerated. We wanted jobs that actually provided a path to prosperity. We want to have companies that stay in the neighborhood. I don't know, many of you have seen you help a company and ten years later, they get up and move to another community because they're chasing another tax incentive. So the types of companies we're looking at here are cooperatives so there's no developer that has deep pockets who could just come in in and give a guarantee. We still felt they had a lot of value. We're still putting in those same requirements of a debt reserve and a TIF debt reserve and the interest rate arbitrage, but we know that these are riskier projects.

The first one we funded was the Evergreen Cooperative Laundry. It's a green laundry and we put in $1.5 million of HUD 108. The Evergreen Fund is a fund that our anchor institutions have contributed to, to invest in these projects. Again it's a partnership between philanthropy, private industry and the City of Cleveland all working together to create these businesses.

Here are some of the machines for the laundry. 29 jobs were created, 90% minority, 44% from our empowerment zone, 62% formerly incarcerated, our Section 3 for this were over 60%.

Again, these are some of the things that you're going to have to help developers and companies understand; what Section 3 is, how do you meet the requirements. We work with our workforce team to help feed people to the companies that they are going to need to meet that Section 3.

So HUD 108 has helped us to stimulate investment and it really has helped us to leverage a lot of private investment as well. You need less HUD 108 for projects since the Recession. At the beginning you could see I couldn't get a bank to come in, so I was putting in a lot more HUD 108. Later I was putting in less HUD 108 to get bigger projects done. The most important thing is that your developer has to understand the processing time is much longer.

You have to go through an environmental review which includes a Section 106 review which is a historic review so if you have any buildings on the site, they're going to have to be looked at, especially if you want to tear them down. And Section 3 has to be followed and federal prevailing wages. These are all a little bit different for clients and if your staff isn't familiar with them, you're going to have to make sure they're trained so you don't run into audit problems down the road.

What sells HUD 108 is its flexibility and low interest rate. The best thing about it is that it's subordinated debt and as I said you can offer three years of interest only which really helps a developer because he's making small payments until that project is online and stabilized. And then, again, if you can use it with an NRSA, it really cuts down on paperwork because it's really going to help you be able to fully implement and direct the funds where you need them the most.

So I think that's about it for today but I hope everyone really enjoyed it and learned a little bit but what I'll say to you is, I think HUD 108 is a great tool. I don't think enough people use it and if we didn't have it we couldn't have done a lot of the great things we have going on in Cleveland right now and so it's been very successful for us. So good luck in using HUD 108. If you have questions, don't forget, HUD is there— ask questions and ask them who's good in

your region who could maybe sit down with you and figure out how to start your program. Good luck.

Jorge Morales: Thank you Tracey. Let's continue on with the application process. In this case, the loan fund. Remember our considerations for the individual project applications. Remember community strategy. What are the community's needs? What are the organizational arrangements? Who is responsible? Who are the parties who are going to implement the program? What approach are we going to be using for this 108 in the case of the loan funds? At what scale? What is the size of the loan? What is the size that can be managed?

Also, we need to be aware of the marketing and outreach. What is the strategy? How are we going to reach out if the market is a loan fund? Also, the selection and evaluation – what's the process? How are you going to select the different programs and projects? How are you going to make sure they are the right ones for my community?

And finally, the fund management. What is the plan? You have the short term and the long term. You need to make sure that when we implement the program that we comply with the required regulations.

This is a something about the marketing and outreach. The loan fund marketing considerations—we must keep in mind how are you going to market to potential borrowers? How will you get the word out? Are you going to use newspapers, radio, or television? How are you going to make people aware that you have this program available?

Will you be requiring a request for proposals or a request for applications? Are you going to then define existing community efforts that can be used to promote the program? Are you going to promote partnership opportunities among the different entities?

Concerning the selection and evaluation, how will you intend to screen and who is going to do the screening? That is very important. What criteria will be used? What different

materials are required according to your community? Remember, after all, we must keep the community's priorities always in sight.

The overall project feasibility. You don't want to fund a project that doesn't have any chance of success so you have to make sure that the financials are ready. What is the ability to repay the loan? Remember you are pledging the CDBG funds so you have to make sure that they have the ability to make those payments. And after all, you must ensure that they comply with HUD requirements.

One of the things that you need to be clear about is what underwriting standards you are going to be using to underwrite your projects, to assess the risk of those projects. Who will conduct the underwriting? Will the borrower be doing it, or will tyou contract with somebody else to do the underwriting? This is an essential and very important step. After all, these are your assets—you must assume the risks in the deal.

Hugh: Thank you Jorge for those points that you made to us about selection and evaluation.

Let me just move to another topic that is very important as you consider structuring your loan fund. It's fund management. What you'll need to consider under this topic is, have you developed policies and procedures to administer the fund? Who will operate it, who will administer it, how will decisions be made? Do you have a long term management plan that will help you track the individual loans within your loan portfolio so that for any individual loan you can ensure that the debt service payments are being made timely, that there is reporting of outcomes in terms of the number of jobs for instance that are being created, or maybe the amount of increased tax benefits?

And then you will want to have some system that will assist you with monitoring your individual projects that you funded for continued program compliance. Remember that program requirements for this financing, similar to CDBG, extend beyond the initial financing of the project. In other words, you'll extend after your project's construction or rehab has taken place, whatever the case may be.

So let's look more specifically at some of the topics within fund management in terms of the policies and procedures. So you'll want some kind of internal application process, if you will, a pre-screening application. If someone wants to make an application to use your financing, then there ought to be a preliminary set of questions you might ask like, what is the type of development, how will the funds be used by the developer, and of course, where is the location—things like that. Along with the internal application, then maybe if you've done prescreening, you'll move it forward for further underwriting. So that's where you go from prescreening. How would you select the project? How would you move forward to take it to the next phase?

Part of the next phase, I'm looking at bullet number three here, is the underwriting process and criteria. Underwriting process means who will be the staff, or who will be the institution—maybe it's a bank that is partnering with you—or maybe you're partnering with a community development financial institution to assist you with the underwriting. That's what you are looking for there. And then in term of the process, if it meets financial underwriting criteria, it meets program criteria, then how will the decision be made for it to actually be funded.

Once the project is funded or you start developing loans, you'll want to have an approach to your financial management. What financial reports that you may look for, are taxes being paid, things like that. Then you'll also in managing your fund, you'll want to figure out how your monitoring will work and what kind of risk you're concerned about. Are your loans in a first priority lien position, are they in a subordinate lien position, are there any events that are occurring at the project site that may decrease the value of the asset?

And then of course in terms of the reporting, that includes the Integrated Disbursement and Information System, commonly referred to as IDIS. So in IDIS, like block grants, you want to set up the project activities and then going forward you'll want to show either the Section 108 program income being paid back in the repayment account or you'll want report the creation of jobs or other benefits that may have occurred.

Now in terms of some of the tools under the fund management, let's just think about this. You don't want to necessarily reinvent the wheel—there are communities that are doing project loan funds around the country and so you can find out from them, also from us, about identifying a template for an application for a third party borrower. When I say template, it might be a certain set of questions that you always want to ask about your project. Is there site control, is there additional funding involved, who will own or operate the specific project or development? Is it a business, is it a for-profit developer, or is it a nonprofit entity?

And then there's templates you could develop for a commitment letter. You don't have to write a unique commitment letter each time you make a loan. You might have a generic type of commitment letter that will be customized to identify the specific project that that you are addressing. And then at loan closing, what kind of documents do you want at loan closing—your notes, an expression of collateral, identification of mortgages, and other financing that will be there.

Then in record keeping these are things that you are familiar with. We find it helpful that, from communities we have learned, that those who have developed some checklists to ensure that they are being able to meet compliance and keep records to that effect. What was the eligible activity, what was the national objective, and does the project and use of your financing, your Section 108 financing, that funding demonstrates public benefits and is in compliance with the public benefit standards, either jobs or goods and services.

And then it's good to also have a checklist so that you can monitor your portfolio on somewhat of a regular basis. How is the project operating? How is it going forward? Is it in compliance… sometimes a development that you might finance does a commercial building and tenants would be in it, then it takes, after construction, it takes maybe 3 or 4 or 5 years for all the jobs to be created that were estimated initially. So that's how monitoring can be helpful to you.

So under fund management we'll also want to look at some examples for tracking, internal tracking, on your individual projects. So you would have a system for identifying when

payments are due, are they being paid monthly? That's what we recommend that anytime you re-lend this kind of financing to a third party like a developer, like a business, that you get repaid monthly. And then you can accumulate that in your guaranteed loan repayment account and then pay the debt service on your underlying Section 108 guaranteed loan to the bank of New York Melon.

So that's the kind of system you want and the other thing is tracking. You'll want to have a system that identifies that property taxes are being paid on time, especially when a third party developer or business is doing that. You'll want to know if there's tracking on any instances or events in case there's some potential damage caused by fire or storm or something like that. So you want a system for just having an outline and overview of each property.

And then finally, we announced this a bit earlier. There's guidance already out there for you. We've got other loan funds throughout the county at the state level, and also at the individual local government level, in a city, county, small nonprofits, that are being involved and using the loan funds.

Also you can get additional assistance and information through your HUD field staff or us here at headquarters staff. There's also the HUD exchange website which has the Section 108 Loan Guarantee Program there with a variety of resources, webinars, and then some other references for underwriting criteria and for the application webinar that we are recording. And then of course there are partners that you can link up to to help establish your loan fund. Sometimes we've seen communities join with two or three lenders, banks, community development banks to help to run a loan fund, to underwrite, you can join with community development financial institutions even, the community development credit unions are involved in this type of financing. So you've got access to existing loan funds, you've got access to HUD staff, and then there's always partners that are interested in assisting you help you meet your community goals and needs and joining in as partner to do a loan fund with you.

Jorge: Continuing with the loan fund application which is built upon the great opportunity a loan fund program allows the communities because it allows communities to build a portfolio

that will cover a broad variety of needs. It will build a determination based on what projects they want to target, what areas they are going to target, and of course that will be the first step—to determine the focus of that fund.

Identify the eligible activities and target areas. They will complete the citizen participation process and local reviews. They will submit the application to HUD, who will go into the issuance process.

But one of the main aspects that we want to emphasize is that for each individual project that a community approves, a complete citizen participation process has to take place and they will require HUD's field office to issue an eligibility determination for each individual transaction. Once again this is one of the main features of using a loan fund program. If you don't have a specific project and you can cover a lot of different needs with just one single program.

Let's take a look now at the loan fund application content and see what information we would like to see in that application. We will need to see the loan fund description which includes the funding amount, the community development objectives, the eligible activities, national objectives, if required, or if applicable, the public benefit standards information, also the capacity and the identification of partners and players, their role. A description of the underwriting process and criteria that is going to be used to select those projects. Also the loan terms that you are going to be using. We would like to see a pipeline of the potential projects that you may have coming your way. Also what collateral are going to be acceptable for your loans. Also repayment schedules and the required certifications.

The eligibility determination process. Once your loan fund program is approved you must submit the following information to your field office for each individual project that you are submitting. The project description, the eligible activity or activities, the national objectives, and if applicable, once again, the public benefit standards according to the CFR.

Once that information is provided to the field office, the field office will then provide a determination letter which in turn will be submitted to us and we will then proceed to the

advance request if funds are forthcoming. Now we are going to have the opportunity to see a case study from the State of Iowa, with Mr. Ed Basch, Project Manager for Iowa Economic Development Authority.

Ed Basch: We at the State of Iowa Economic Development Authority decided to get into the HUD Section 108 Loan Guarantee program because we were looking for another development tool to offer to, to particularly to non-entitlement communities who of course have no auto access to CDBG funds and we're attempting to put more money out in the communities to work or more money to work, so to speak, across the state. We call our program the Community Revitalization and Economic Enhancement Loan Fund because that's what we hope that it can accomplish.

We have asked HUD for 40 million dollars in lending capacity over the next five years. If you compare that to our annual CDBG allotment, it's nearly twice as much as our annual allotment which is currently about 21.5 million dollars. Applicants, obviously since it's CDBG, must be a general local government, a municipality or a non-urban county. And that indicates of course that it's for small cities and non-urban counties only and we want to facilitate the availability of capital for larger and more comprehensive impactful projects than we have been able to fund through our regular CDBG components. And we feel that the Section 108 can address those unmet community needs that existing resources are not fully serving or in some cases are not serving at all. We believe there's presently a gap in resources available for larger scale projects, particularly for the rehabilitation or renovation of affordable housing.

And we're especially interested in adaptive re-use and conversion of former nonresidential buildings to residential. One particular thing we find in Iowa is through school consolidations, there are a number of communities now with vacant schools and several of them have been converted and we want to spur that on to continue to see those schools reused as apartments.

Actually in 2012, there was a statewide housing study done that identified a need for increased affordable housing throughout the state. Our aging housing stock is a major contributor to the affordable housing shortage. That has resulted in our program's primary focus on housing

rehabilitation and adaptive re-use. Iowa has an exceptionally large number of small rural communities with housing at least 50 years old and often 75 years or more and we have seen that in smaller communities when economic development does occur, you can be faced with the situation where there are few places for new workers to reside in that community.

So the financing split reflects, obviously, our emphasis on housing as 81% of the program funds are expected to serve housing projects. The other 19% would be for economic development projects, mostly probably industrial, some maybe commercial. That would be expected to create at least 380 new jobs and that would be at the minimum amount per job so if we are reserving some flexibility where we can give more than $5,000 a job, which is our state minimum, then that number of jobs could expand. So you can see the table there and the percentage of the total 40 million dollars that's been allocated to us and how that breaks down into our four major components.

So the objectives of those four components are as I said, the larger dollar, larger impact projects for economic development, through business location or expansion, adaptive re-use and conversion of vacant or underutilized buildings for residential purposes and we're talking here about normally something of a former use related to education—perhaps a warehouse, perhaps a hotel—those are the kind of situations that we commonly see.

The third objective would be rehabilitation of upper story residential units, all within a single market area. One of our emphases statewide is to encourage mixed use and upper story development, particularly in traditional downtowns as that's becoming a trendy thing, so to speak. And then finally, the availability of affordable single family housing units, or remediation perhaps even demolition of those units to clear the way for new housing.

Our activities again, direct business loans, adaptive re-use or conversion, upper story residential rehab and mixed use structures where we prefer where the typical traditional downtown has a storefront on the ground level and then loft apartments above and then rehabilitation or demolition of single family residential units. At IEDA we always prefer rehabilitation or remediation of properties, particularly single family units, rather than demolition which we

regard as the last resort but we have allowed that within our program because we do realize that sometimes residential structures become truly uninhabitable and are beyond the point of reasonable repair.

So the applications will be reviewed by us on a first come, first served basis. It will be what we call a rolling application window and we will make awards until all the funds are committed. We have five years to distribute the monies that we have. Loan terms are intended to be 7 to 15 years depending on the type of project that you are undertaking. We expect that the direct business loans would have the shortest terms and that the adaptive re-use projects would probably be more likely to have the 15-year term. Again, just because of the construction time periods and the length of time it takes to start showing a positive cash flow.

As part of our process we do require a meeting be held between the unit of local government and IEDA prior to submitting a full application. Our review team, which would consist of five individuals, will complete underwriting and present the project recommendations ultimately to HUD for the eligibility determination.

And really we want to screen potential projects early on before there's a large amount of time and money and energy expended. Just in the interest of everyone concerned. Our primary tool for the initial review will be what we call a project questionnaire but you could call it a pre application, if you'd like. It is relatively short but gives us enough information to make a determination of viability and eligibility before we get too far along.

In terms of the contacts for this program, you can see them there. Division Coordinator, the Community Investment Team Leader, which of course I am a member of that team. And then myself as the Project Manager. I will be the contact person in the State of Iowa. I will do all of the initial screening and try to determine basic eligibility before it is taken any further. If the project looks good, I will then set up the next steps so that the project can move forward.

Bennett: Thank you so much Ed. We really appreciate you joining us today and giving us an overview of the State of Iowa's loan fund. We are now going to transition to a general wrap

up and talk about some next steps. We're going to hear from Hugh Allan, the Deputy Director of the Financial Management Division again.

Hugh: We hope that today you've learned from this webinar and you've learned about how to draft your application and how to directly submit it to HUD. I want to again thank Bennet for her big picture overview giving you a sense of a program design, and specifically Shahidat and her project specific way to structure an application. And then finally, again thanking Jorge for his presentation of the fund, which should help many of you that have a large need out there, either in a specific neighborhood or numerous neighborhoods, that you'll find that a loan fund will help you build a portfolio and address many of your needs without having to come in each time for a new application for each project that you want to fund.

Also I do again want to thank Tracey Nichols, Director of the City of Cleveland's Department of Economic Development for those excellent examples and case studies she gave. This should give all of you a real insight into the power of this program and this type of financing and how to expand the impact of your Community Development program, in your neighborhoods.

And also to Ed Basch from the State of Iowa, that gives you a clear example of how a state can fund numerous projects throughout a state and spread the risks of the loan fund. That's really a good focus for states to be thinking about and to be using.

Going forward, we have another webinar that we're going to be drawing your attention to and also be recording and putting on our website. It's going to be on underwriting credit for real estate development, the income-production properties vs. direct business loans which gets you into a different credit structure and we can show you a very insightful way to do that underwriting. So be looking forward to that. We think you'll find that very useful. There are other informational items that we're going to be putting on our website—project summaries and then maybe some other interviews with other communities around the county that will be placed in there also. So be on the lookout for things of that nature.

We hope you find that this Section 108 Loan Guarantee program is the program to complete your impact of your Community Development Block Grant program in your community. If you have questions, please be in contact with us either by phone or by email or through our website. Thank you for your attention and your time and the best of luck in putting together those Section 108 Loan Guarantee applications.

End of Transcript