2013 Annual Awards Entry Form
(Complete one for each entry.)

Entry Name	**Maximizing Rural Housing Resources in Virginia**		
HFA	**Virginia Housing Development Authority**		
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Entry form with description, check(s), and visual aids (optional) must be received by NCSHA by **Monday, July 1, 2013.**

Use this header on the upper right corner of each page.

HFA **Virginia Housing Development Authority**

Entry Name **Maximizing Rural Housing Resources in Virginia**

Communications	**Homeownership**	**Legislative Advocacy**	**Management Innovation**
☐ Annual Report ☐ Promotional Materials and Newsletters ☐ Creative Media	☐ Empowering New Buyers ☐ Home Improvement and Rehabilitation ☐ Encouraging New Production	☐ Federal Advocacy ☐ State Advocacy	☐ Financial ☐ Human Resources ☐ Operations ☐ Technology

Rental Housing	**Special Needs Housing**	**Special Achievement**	**Are you providing visual aids?**
☐ Multifamily Management ☒ Preservation and Rehabilitation ☐ Encouraging New Production	☐ Combating Homelessness ☐ Housing for Persons with Special Needs	☐ Special Achievement	☒ YES ☐ NO

"By creating a unique portfolio structure for rural deals, VHDA and Rural Development successfully attracted the necessary funding from tax credit investors. As a result, we accomplished our shared goal of preserving affordable, safe and decent housing in rural Virginia that otherwise may have been impossible to finance."

Byron Waters, Rural Housing Programs Director
USDA-Rural Development in Virginia

Background

When the USDA Rural Development (RD) program made much-needed renovations to an aging portfolio of multifamily developments located in rural Virginia, it was able to work with the Virginia Housing Development Authority and other partners to finance the improvements with a creative combination of new VHDA loans, funds from investors in Low-Income Housing Tax Credits, and, in some cases, other grants and subsidies. RD subordinated its liens to the liens of the new VHDA loans, which enabled VHDA to make the new loans. In exchange, VHDA promised it would inform RD promptly of any default and would cooperate with RD as VHDA sought a solution to the default. RD kept in place all subsidies it had prior to the new VHDA loans. The owners of the developments applied for Low-Income Housing Tax Credits; in one case 4% credits and in another 9% credits. In the case of the 4% credits, VHDA facilitated the award of credits by agreeing to allow tax-exempt bonds to be issued and then retired early—a process sometimes called "bond burning." In the case of the 9% credits, VHDA gave credit to the applicants for preserving units.

To make this deal work and attract investor interest in the Low-Income Housing Tax Credits, the owners applied for credits on several rural multifamily developments at a time so the number of units of all the applications combined was 200 or more. VHDA's loans and RD's loans and subsidies, however, were on each individual development. Investors who bought the tax credits were satisfied that the measures VHDA and RD took to close these loans resulted in the equivalent of a single tax credit investment. The renovation work was managed by VHDA using its construction control officers and construction loan draw process. VHDA kept RD informed about the progress of the work and the decisions made during the renovations.

Why/When it was Undertaken

Approximately 10 percent of all renters in Virginia live in rural areas, and a third of them have very low incomes that depend on subsidized rental units. This situation is why preserving RD properties has been a strategic initiative of VHDA for several years.

This creative initiative solves a major problem: the risk that many small multifamily developments located outside of Virginia metropolitan areas would fall out of the affordable inventory as a result of disrepair. The average RD property assisted by this program ranged from 23 to 60 units, with more than half having 40 or fewer units. Their small size meant these properties were not viable to investors who typically buy tax credits. Although RD lacked the resources and programs to fund these renovations, the agency did provide rental assistance to the projects that made recapitalization possible. Lastly, the underlying RD debt, while attractive as a funding source, was crowding out additional debt due to its high LTV.

This initiative tackles the challenge of how to recapitalize an aging portfolio at a time when RD faces funding cuts. VHDA opened a dialogue with Virginia RD to discuss each other's program constraints, as well as the assets each could bring to the deal. RD agreed to subordinate its Section 515 loan to a VHDA loan because the small rental developments did not have sufficient value to support new debt. As a compromise, the financing statements securing the RD loans remained in first position ahead of financing statements recorded for the new VHDA loan. This measure essentially tied the Rental Assistance Contract to the RD lien. In addition, VHDA agreed not to place additional debt on the property and gave RD an option to cure a default by the owner.

Using 9% tax credits and relatively small, low-cost VHDA REACH loans, the authority underwrote to market rents and based its debt service coverage (DSC) and loan-to-value (LTV) ratios on the VHDA debt only. RD provided a modest increase in the rental assistance to carry the additional debt. Limitations of VHDA's REACH program and the competitive nature of the 9% tax credits made it difficult to do more than a single property at a time, and then only if a tax-credit syndicator could be enticed into investing in a small project. To speed up redevelopment efforts of the RD portfolio, VHDA explored the possibility of financing several properties at one time using different funding sources, including tax-exempt bonds and 4% tax credits. While securing 4% credits was a significant positive investor incentive, the negative from VHDA's standpoint was retiring a large portion of the bonds once the units were placed in service in order to meet the authority's DSC and LTV requirements. Ultimately, VHDA decided that the strategic initiative was a worthwhile use of the bond allocation.

What VHDA has accomplished

VHDA refinancing has provided large-scale renovations ($26,000/unit) for 232 units in six rural multifamily developments. This has kept the units available for low- to moderate-income residents, and employed financial resources that are readily available to other HFAs. Another 193 units in five more rural properties are in the pipeline to be rehabilitated on a similar per-unit scale and preserved for use by very low-income residents. To accomplish these significant rural housing preservation efforts, VHDA combined its resources and skills with those of RD, the tax credit investor, consultant and private developer. VHDA assumed a lead role by serving as the issuer of tax-exempt debt sized to meet the projected needs during construction, as well as once the properties were stabilized. VHDA leveraged prior successful projects with Virginia RD to secure a subordination of their existing Section 515 loan and a 50-year re-amortization of same. With VHDA funding development costs during construction, the developer was able to delay equity pay-in and secure more favorable pricing on the credits.

Why it is Meritorious and Meet NCSHA Award Judging Criteria

<u>Innovative</u>

The Rural Housing Preservation Tax Credit program enables a developer to fund all construction costs with tax-exempt debt by qualifying those costs for 4% credits. In addition, it shifts equity pay-in to the placed-in-service date, maximizing the price the tax credit investor is willing to pay. Since the credits can then retire a significant portion of the new debt, it stays within the targeted DSC and LTV ratios.

<u>Replicable</u>

Any HFA with adequate tax-exempt authority and a strong partnership with their state's Rural Development staff can replicate this program. In addition, those HFAs participating in any sort of government securitization can improve their pricing to multifamily developers.

<u>Responds to an important state housing need</u>

Some 38,690 renter households in rural Virginia earn from 30 to 50 percent or less of the Area Median Income. This makes them totally reliant on the RD's 515 program and Rental Assistance subsidy. Although demand for affordable housing in rural Virginia has increased, RD has no new funding for additional production or preservation of existing units. VHDA's innovative thinking and tax-exempt authority enabled it to partner with RD and preserve affordable rental housing for some of Virginia's most vulnerable residents.

<u>Demonstrates measurable benefits to HFA targeted customers</u>

VHDA has preserved not only 425 units of affordable housing; it has preserved them to meet its high standards of Minimum Design and Construction Requirements. Preservation improvements include energy efficient appliances and HVAC, domestic water conservation, sustainable finishes and best management practices for drainage and water mitigation in and around the buildings. These conservation and sustainability steps lower property operating costs, provide healthier resident environments, and economize the use of Rental Assistance while sustaining this important affordable housing resource in rural Virginia.

Proven track record of success in the market place

Prior to embarking on the portfolio approach, VHDA had forged strong ties with the state RD office by recapitalizing over 40 individual properties in rural Virginia using a similar financing structure. The main components of the single property financing structure -- RD subordination, tax credit equity and VHDA REACH funds – are also found in the portfolio approach. However, a key difference is the use of tax exempt bond financing which permits a larger transaction resulting in more tax credits and the ability to defer equity pay-in by "burning" tax exempt bonds at construction completion. Introducing tax exempt money into the transaction resulted in an estimated $.05 premium the investor was willing to pay for the tax credits.

Benefits that outweigh the costs

When five or six developments are combined to attract an investor, there is a VHDA loan supporting each development with an attendant set of loan documents and title issues. Extra time is invested in setting up, underwriting and closing these deals on the same day. VHDA sends construction control officers to several remote sites to review renovation progress. In most instances, VHDA also provides a REACH interest rate reduction subsidy. In some cases, RD still provides ongoing subsidy in the form of Rental Assistance. Still, the cost of replacing this housing would far exceed the additional investment in time and subsidy.

Demonstrates effective use of resources

VHDA has a surplus of tax-exempt bond allocation; this initiative is an opportunity to maximize the use of this resource while preserving RD units. Using tax exempt bonds to finance RD property acquisition and rehabilitation enables the developer to use an available source of equity. Retaining the RD funding preserves a valuable low-cost financing source that could not otherwise be replaced. Lastly, this approach reduces the need for new sources of funding from RD and minimizes the need for additional Rental Assistance.

Effectively employs partnerships

RD's desire to recapitalize its portfolio dovetailed with VHDA's desire to maintain a strong rural housing inventory. This shared goal led to RD re-amortizing its remaining one percent debt while subordinating to VHDA's loan. VHDA brought construction oversight and a strong track record of success with other RD transactions. VHDA's ability to issue both tax-exempt and taxable debt without the additional cost of credit enhancement made the financing both readily available and affordable, yet none of this would work without RD's Rental Assistance program providing operating subsidy. The last critical element was the equity investor who was enticed to become a partner because an adequate return was available by purchasing the tax credits.

Achieves strategic objectives

With over 60 percent of rural Virginia households making less than 30% of the statewide median income—and other federal housing programs predominantly concentrated in the state's urban areas—the Section 515 rural portfolio is a critical component of Virginia's affordable housing inventory. Combining several small multifamily rental properties into a critical mass attracts investors who would not otherwise be interested, and enables VHDA to save and rehabilitate the affordable housing that rural families depend on—a primary VHDA strategic objective.

Conclusion

When a strategic focus, such as preserving affordable housing for vulnerable rural families, is shared by the HFA and Rural Development, it's critical that each entity understands what the other side brings to the task and why both are necessary to the solution. A shared vision of a single transaction made up of several properties that could be effectively and efficiently financed through a tax credit investor makes our Rural Housing Preservation Tax Credit Program an affordable housing game changer. As a result of this program, a total of 425 units of affordable rural rental housing have been preserved for a minimum of 15 years. By bundling smaller rural rental developments into one tax credit award, we were able to preserve hundreds of units that otherwise would have been lost.

Please see examples below showing the results of VHDA's Rural Housing Program.

Before: Stevens Woods Apartments in Courtland, VA

After: Stevens Woods Apartments in Courtland, VA

Before: Carriage Run Apartments in Emporia, VA

After: Carriage Run Apartments in Emporia, VA