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HOUSING MANAGEMENT BUREAU MEMORANDUM #2009-A-02

To: All Housing Authorities, Chairpersons and Executive Directors

From: Robert Damico, Downstate Director
Housing Management Bureau

Date: May 6, 2009

Subject: Standards and Procedures for Requests by Housing Authorities for Approval of a Public Housing Restructuring

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Public Housing Restructurings ("PHR") are a common means by which Housing Authorities ("HA") refinance and renovate their projects by accessing and combining a variety of funding sources. Each funding program has its own unique requirements for eligibility, so the challenge for any HA choosing to pursue a PHR is to structure a single project to meet the requirements of multiple programs. The PHR creates a hybrid public/private ownership structure which can qualify for programs targeted for either public or privately owned housing. DHCR is presenting this bulletin in order to clarify the PHR process for any HA which has decided to undertake a PHR. Therefore, this bulletin sets forth the standards and procedures adopted by DHCR for the review, approval, funding, and supervision of these restructurings.

Acting through a developer or in partnership with a not-for-profit housing organization, the HA creates an ownership structure involving a private, for-profit entity—limited partnership ("LP") or limited liability company ("LLC")—which includes the HA and is subject to DHCR's oversight. As a private, for-profit owner, this entity can also benefit from Low Income Housing Tax Credits ("LIHTC") and other financing. At the same time, by virtue of the HA's continued involvement, the private entity can also benefit from public housing funds, such as Public Housing Modernization ("PHM") grants from the Housing Trust Fund Corporation ("HTFC"). This arrangement, which is modeled after the federal HOPE VI program, makes possible a completely renovated development which will continue to provide affordable housing for a period of thirty to forty years.

Legal and Financial Considerations.

HA projects were originally financed by the issuance of General Obligation Bonds by the State of New York. To insure regular payment of debt service on the bonds, the State provides a debt service subsidy, by which the State essentially pays off its own debt. Nevertheless, the debt is secured by a Loan and Subsidy Contract ("LSC"), which works in a manner similar to a mortgage, although it is not recorded and does not take a security interest in the property itself, only on the income generated thereby.

The LSC, like a mortgage, prohibits any transfer without the consent of the State (even if the bonds have already been retired). Accordingly, in order to transfer a project to a newly-created private entity, DHCR and the Office of the State Comptroller ("OSC") must review the proposed restructuring, give their consent, the LSC must be amended, and either the bonds must be retired or provision made for continuing the debt service payments.

Section 58-b of the Public Housing Law.

One way to accomplish a PHR is pursuant to Section 58-b of the Public Housing Law ("PHL"), which authorizes DHCR to consent to the transfer of a project upon finding that such transfer will help the project to continue to provide safe, decent, affordable housing, that the project will be receiving a federal subsidy, and that provision has been made for payment of the bonds. This method is viable where the bonds have already been retired, or where the HA can provide sufficient funds to retire the bonds or allow the HA to set up a "defeasance account" to make the debt service payments as they come due.

Special Legislation.

During the past decade, the more common method of implementing a PHR has been pursuant to special legislation. There have been many of these laws, all following a similar pattern, but each applying only to specifically identified projects which are found by the State legislature to be in need of restructuring. Such legislation has required DHCR to make a finding, among other things, that a proposed comprehensive redevelopment plan will provide safe, decent, affordable housing, that the tenants in occupancy will continue to be protected under the PHL, that specific portions of the units will be dedicated to particular income levels, that the developer's fee will be limited to a certain percentage of project cost, and that the project will remain under the HA's control and DHCR's oversight. If DHCR (with the approval of OSC) makes such a finding, then the project may be transferred without any additional provision for paying debt service on the bonds, and the project's debt service subsidy will continue, subject to annual legislative appropriation.

Application for Approval of Restructuring.

In order to obtain DHCR's approval of a transfer in furtherance of a PHR, the HA must submit a letter application to DHCR's Office of Legal Affairs ("OLA"). The application must describe the present condition and occupancy level of the project, the proposed redevelopment work and all associated costs, amounts and sources of funding, the new ownership structure, including the identity of the developer or other sponsoring organization and disclosure of its principals, the manner in which the developer or sponsoring organization was selected, and the measures to be taken to protect the tenants in occupancy.

OLA reviews the application, coordinates with other parts of the agency which have received funding requests relating to the PHR, acts as liaison with OSC in securing its approval, and prepares the necessary legal documents to complete the transaction, including the Commissioner's Findings and Approval ("Findings").

Application for Approval of DHCR Funding.

Most PHRs involve substantial rehabilitation work, often funded by a combination of tax-exempt bonds issued by an appropriate public entity, PHM grants (awarded by HTFC to the HA and then loaned by the HA to the new private ownership entity to perform the rehabilitation work) and equity from the sale of Low Income Housing Tax Credits ("LIHTC") administered by HTF/DHCR's Office of Community Development ("CD") or the New York State Housing Finance Agency ("HFA"). LIHTC's can be either 4% or 9% credits or sometimes a combination of both. Project cash flow is often enhanced by Project-Based Section 8 income.

Where multiple funding sources are involved, the HA or developer must submit a request to HTFC/DHCR for PHM funds and an application to DHCR's "Unified Funding" Program for LIHTCs and Project-Based Section 8.

There is no prescribed time to apply for PHM funding. HAs considering a restructuring may request funding at any time by submitting a proposal describing the transaction, anticipated capital funding sources (including requested PHM funds) and a proposed scope of work including estimates of cost. Given the significant demand for PHM resources, DHCR typically plans for its awards to be phased in over several years (usually three) of PHM appropriations. Should a HA have already received PHM proceeds that remain unspent, additional funding may be requested, depending upon the amount, and may be phased in over a shorter timeframe. HTFC can only enter into contracts for funds actually available during the current fiscal year. Awards may be made for subsequent years but are memorialized in a statement of intention, which HTFC has consistently honored.

Application may be made to CD for 9% LIHTCs following DHCR's standard procedures. 4% LIHTCs may be obtained from other public agencies and are "as of right" in conjunction with the issuance of tax-exempt bonds.

Coordination of DHCR's Review.

Before the Findings and Approval can be issued, OLA must confirm that all HTFC/DHCR approvals have been obtained. The agency conducts reviews necessary to satisfy the respective requirements of the PHM, LIHTC, and Project-Based Section 8 programs, which may include technical specifications, design requirements, contracts, costs, sources of funding, and other underwriting concerns. Every effort is made to coordinate these reviews and avoid duplication.

Review by OSC and the Attorney General.

Once OLA has approved the Findings and LSC Amendment, it forwards them to OSC for review. OSC conducts its own review to insure compliance with the applicable statute, financial viability of the redevelopment, fairness of the procurement process, and full disclosure of the principals. When OSC has given its approval and executed the LSC amendment, it is forwarded to the Attorney General for approval as to form.

Legal Documents.

A PHR involves the following key legal documents:

1. <u>Findings.</u> The Commissioner's Findings and Approval is keyed to the requirements of the statute under which approval of the transaction is being sought, either PHL Section 58-b or special legislation. They include a statement of the requirements of the statute, a description of the property and its present condition and level of occupancy, the redevelopment work and its cost, sources and amounts of funding, the new ownership structure, the rights of the tenants in occupancy, and the Commissioner's findings and conclusions.

2. <u>LSC Amendment.</u> The amendment to the Loan and Subsidy Contract modifies the original LSC to permit the transfer of the project in furtherance of the PHR and to incorporate the requirements of the statute under which approval is sought.

3. <u>PHM Contracts.</u> The Public Housing Modernization contracts are between the HTFC and the HA and commit specific funds to the project in a given funding year.

4. <u>Agreement to Provide Public Housing Units.</u> This is an agreement between the HA and the LP to continue to provide public housing in accordance with the special legislation, if any, and the Public Housing Law. DHCR is a third party beneficiary of this agreement.

5. <u>Building Loan Agreement.</u> This is an agreement between the HA and the LP which governs the disbursement of PHM funds loaned to the LP to perform the rehabilitation work.

6. <u>Enforcement Mortgage and Note.</u> These documents are between the HTFC and HA, and the LP or LLC, and govern the loan by the HA of the PHM funds to the LP or LLC. Debt service is subject to cash flow availability.

Closing.

HTFC/DHCR sends a representative to the closing to facilitate delivery and collection of the relevant documents, and where necessary, to authorize the release of funds. In addition to the legal documents listed above, the agency's counsel will need to collect and/or review certain other documents. A list of typical PHR legal documents involving DHCR is available upon request.

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