



# Credit Underwriting

October 6, 2022



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# Catalyst Training Schedule



[www.flhousing.org](http://www.flhousing.org)

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## Presenters



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## Poll: Who's attending today?

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- Local government
- Nonprofit developer
- For profit developer
- Other

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## Poll: How knowledgeable are you of FHFC's credit underwriting process?

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- Very knowledgeable
- Somewhat knowledgeable
- Not knowledgeable

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# Agenda

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- The development process, FHFC's request for applications process and the role of credit underwriting
- The credit underwriting checklist
- The ongoing role of the credit underwriter after initial closing
- Local government RFP processes and preparing for credit underwriting

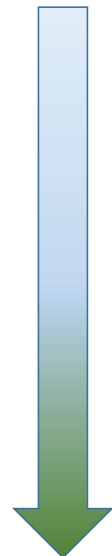
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## The Development Process

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- Conceptual vision
- Site Selection
- Programming/Preliminary Design
- Funding Application
- **Credit Underwriting**
- Funding Award and Initial Closing
- Construction and Lease-Up
- Project Stabilization and Final Closing
- Project Operation and Program Compliance



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# FHFC's RFA Process

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- Rulemaking
- Anticipated timeline
- RFA Workshop
- RFA release
- Application review and recommendations for funding
- Invitation to Credit Underwriting
- Final approval

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# FHFC's RFA Process

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- <http://www.floridahousing.org/programs/developers-multifamily-programs>



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# Credit Underwriting

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- Purpose is to evaluate:
  - Suitability of site
  - Feasibility of the project
  - Borrower capacity
  - Compliance factors
- 3 Credit Underwriters
  - Assigned to project by FHFC
  - Will work with same credit underwriter through entire development process

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## Credit Underwriter's Role Throughout Rental Development Process

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- Preliminary Recommendation Letter
- Final Credit Underwriting Report
- Construction Loan Servicing
- Permanent Loan Servicing
- Compliance Monitoring
- Federal Labor Standards Monitoring

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# Credit Underwriting Report

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- Takes a few weeks to prepare once all required due diligence items and third-party reports are received
- Due at least one month prior the Board meeting where it will be approved
- Most RFAs have a credit underwriting report deadline identified

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## The Credit Underwriting Checklist

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# Applicant/Borrower Information

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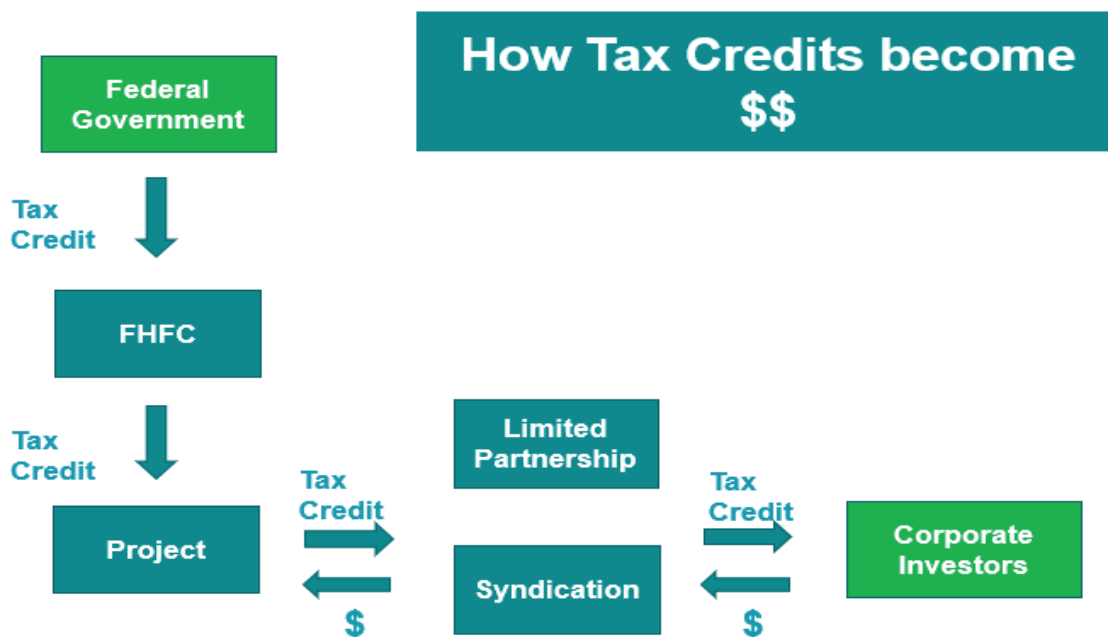
- **Purpose:**

- Clearly identify the entities and parties responsible for executing the development
- Verify the credentials and experience

- **Checklist Items Include:**

- Articles of Incorporation
- Certificates of Good Standing
- Resumes
- Credit Authorization
- Certification of Experience

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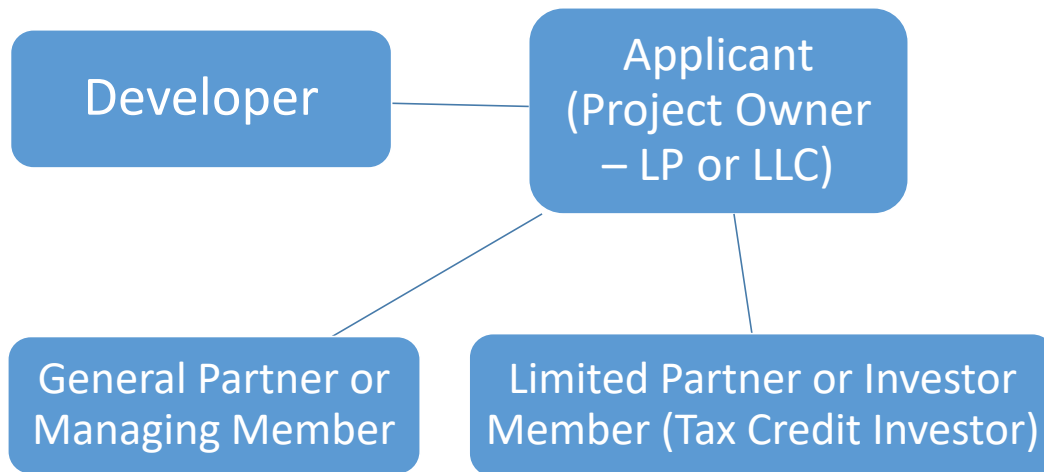
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# Typical Legal Entities for Housing Credit (LIHTC) RFA

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## Financial Information

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### • Purpose:

- Determine the ability of the proposed development to meet financial obligations
- Verify the financial capacity of the applicant to complete construction and operate the proposed development

### • Checklist Items Include:

- Financial Statements
- Tax Returns
- Real Estate Owned and Contingent Liabilities Schedules
- Financing Commitment Letters (firm commitments)
- Sources and Uses
- Operating Pro Forma

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# Property Information

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- Purpose
  - Clearly identify the property where the development will take place in legal terms
  - Verify that the type of development proposed can occur on the property
- Checklist Items Include:
  - Site Plan and Zoning
  - Survey
  - Appraisal
  - Market Study
  - Plan and Cost Review
  - Capital Needs Assessment
  - Title Report

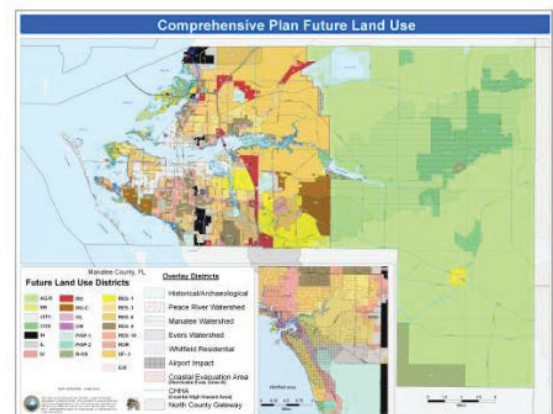
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## Elements of Land Use and Zoning Compliance

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- Future Land Use element
- Housing element
- Zoning – base and overlay
- Other Land Development Regulations
- Special concerns- historic or form based



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# The Survey

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- Must be dated within 6 months of closing
- Must meet lender requirements
- Must be certified to all parties that request it
- Issues may arise that must be addressed prior to closing
- Will be completed again after construction completion

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# The Appraisal: Key Analyses

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- Market overview
- Improvement Analysis
- Highest and Best Use Analysis
- Insurable Value

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# The Appraisal: Valuation Procedures

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- Land value
- Sales approach
- Income Capitalization approach
- Reconciliation of Sales and Income Capitalization approaches

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## Market Study

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- Market study is required
- Key Analyses includes site, demographics, rental and sales prices, competition, impact on existing inventory
- Focus in on: **Average absorption rate** (how quickly the property is expected to lease up)

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# Plan and Cost Review

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- Required for new construction and rehab
- Comprehensive review of all construction-related documents, including:
  - Complete set of plans and specifications (permit set)
  - Architect Contract
  - Construction Contract
  - Schedule of Values
- Determine reasonableness of plans and costs in relation to each other and for program compliance

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# Capital Needs Assessment for Existing Properties

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- Required for rehabilitation or preservation projects
- Will involve detailed inspection
- Focus on immediate needs and cost feasibility
- Will affect:
  - Scope of work for rehabilitation
  - Replacement Reserve requirement

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# Environmental Phase I Review

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- Required for all developments with federal funding
- Involves site inspection and checklist items
- Environmental issues may need to be addressed as part of scope of work
  - May require mitigation to protect habitats, wetlands and endangered species
  - May require mitigation to address impacts to properties with historical or archeological significance

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## Other Environmental Reviews and Clearances

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- Soil studies required for new construction
- Radon Testing required for Zones 1 and 2
  - Must be completed prior to construction
  - Mitigation may be required
  - Retesting required at Completion to show below harmful levels
- Asbestos, Lead-Based Paint and other environmental hazards
  - May require removal or O&M Plans

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# Initial Title Report and Title Insurance Policies

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- Completed by title insurance company or attorney
- Will reveal any issues affecting title for issuance of title insurance policy
- Lenders/investors do not want anything that will negatively affect their ability to recover their investment
- Lender and Owner's policies required; cost included in development budget

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## Permitting Process

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- Will need permit ready drawings for credit underwriting
- Expedited review usually offered for affordable housing developments
- Will need permits or permit-ready letter for initial closing on financing



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## Other Property Information

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- Management Company
  - Property Report – performance of other properties as indication of how well the company will manage the subject property
  - Draft Management Agreement/Plan
- Outstanding obligations of the property
- Rent roll and Operating Statements (for existing properties)
- Service Contracts
- Commercial leases if applicable

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## Other Construction Information

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- Resume, banking and trade references for the General Contractor
- Architect's license and experience with type of development proposed
- Engineering contract
- Construction draw schedule
- Termite inspection report

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# Fees Paid During Credit Underwriting

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- Credit Underwriting Fee
- Market Study
- Appraisal
- Capital Needs Assessment
- Plan and Cost Review Fee
- Building Permit Fees

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## Initial Closing

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# Initial Closing

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- First draw on development funds
- Usually used to close on site acquisition and pay development startup expenses
  - Including “reimbursable” expenses
- May involve payment of developer fee
- May involve repayment of predevelopment financing
- All eyes are on the deal at this time!

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## Initial Closing (continued)

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- Checklist items include:
  - Initial draw with all backup
  - Building permitting
  - Insurance approvals
  - Original, fully executed legal documents
  - Title
- Any checklist item could potentially delay closing!

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# Role of Local Government

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- Obtain and review third-party reports prior to initial closing
- Monitor building permitting process
- Participate in closing calls
- Monitor any changes in closing dates
- Have approvals in place to release funds on closing date if part of initial closing

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# Construction, Lease-Up and Ongoing Compliance

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# Construction Draws: Typical Requirements

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- Updated Draw Schedule
  - Track how the development is staying on budget overall
  - Make line-item adjustments
  - Determine if there is a need to use contingencies
- General contractor's application and certificate for payment
- Any additional invoices for hard and soft costs incurred during period and/or not previously paid
- Title Update
- Third-party inspection report
- Confirmation that insurance is current
- Any other required reports/forms as detailed in agreements

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## Construction Completion

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- The point at which construction is substantially (100%) complete
- General contractor is looking to have “retainage” released – an amount from each monthly payment withheld until construction is complete.

Releasing retainage usually requires:

- Certificates of Occupancy and/or Substantial Completion
- As-built drawings
- Architect and inspector certifications
- Owner and Contractor Affidavits

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# Final Closing on Permanent Financing

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- All required low-income units are qualified
- Stabilized Operations
- Updated title and insurance
- Any required environmental testing and mitigation
- Anything else lenders and/or investors required

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## Stabilized Operations

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- Typical requirements
  - 93% to 95% occupancy for at least 3 consecutive months
  - Debt Service Coverage Ratio of 1.15 or 1.2 for at least 3 consecutive months based on income statements
- Meeting requirements evidenced by rent rolls and income statements

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# Special Requirements for “Closing” on the Tax Credits

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- General Contractor’s Cost Certification – establishes the total cost incurred by the general contractor towards the tax credit calculation
- Owner’s Cost Certification – completed by the Accountant certifying all of development costs eligible for tax credits
- IRS Tax Forms 8609 –
  - Documents the total annual tax credit each building in a development generates
  - Documents the irrevocable income set-aside election (40% at 60% AMI or 20% at 50% AMI)

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# Documents Required and Reviewed by the Compliance Monitor

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- Monthly/Quarterly Financial Statements
- Monthly/Quarterly Rent Rolls
- Program Reports
- Annual Reports
- Tax Returns
- Audited Financial Statements
- Other required IRS Forms
- Files for new move-ins

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# Before Credit Underwriting

A Review of the Local RFP Process

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## Timing of Credit Underwriting

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- Remember that Credit Underwriting takes place after review of applications and recommendations for funding
- FHFC applicants will need commitments for local funding as part of application
- Local governments need to evaluate proposals prior to FHFC's detailed credit underwriting – need for an efficient and thorough local process

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# What type of applicant is desired

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- Minimum threshold requirements for local funding (i.e. nonprofit in existence for at least two years with affordable housing as part of its mission)
- Minimum threshold requirements for other proposed funding sources

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## The Nonprofit Set-aside

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- IRC Section 42(h)(5)
- **At least 10%** of a state's allocation must be set aside for nonprofits (qualified low income projects)
- A **qualified nonprofit organization** must **own an interest** and **materially participate** in the development and operation throughout the compliance period
- Definition of a qualified nonprofit organization (3 requirements):
  - Must be an organization as described in Section 501c3 or 501c4 and tax exempt under Section 501a, AND
  - Must not be affiliated with or controlled by a for-profit company, AND
  - One of the exempt purposes of the organization includes fostering low-income housing

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# How will proposals be evaluated?

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- Three major areas:
  - Organization capacity
  - Project feasibility
  - Ability to proceed
- Know your developer community, nonprofit and for profit
- Support and Patience goes both ways!

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## Offerings

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- What are you planning to offer?
  - Land
  - Money
  - Incentives
- Focus targets
  - Local Government Contribution for FHFC RFA
  - Area of Opportunity Support for FHFC RFA

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# What type of solicitation will work best

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- Request for Proposal
- Request for Qualifications
- Invitation to Negotiate

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# Who needs to be involved

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- Housing Staff
- Social Services Staff
- Planning Staff
- Building Department
- Economic Development
- Legal
- Procurement Department



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# Lining up with FHFC's RFA process

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- Track RFA funding timeline and prepare competitive cycle to coincide with due dates
- Understand each RFA and requirement for Local Government Contribution or Area of Opportunity
- Understand other forms that will be needed:
  - Verification of Zoning and Land Use regulations
  - Verification of Infrastructure- sewer and water
  - Within 21 days of invitation to credit underwriting:
    - Verification of environmental safety Phase 1 ESA
    - Phase II ESA if required
    - Verification of infrastructure- electricity, roads

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## Right-Sizing the Subsidy

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- Why is this important?
  - Fiscal responsibility
  - Ability to produce more units with limited sources
- Thoroughly review sources and uses, and operating budget
- Understand timing and terms of all sources
- Consider utilizing a third-party reviewer (similar though not taking the place of credit underwriters)

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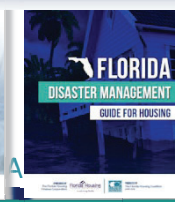
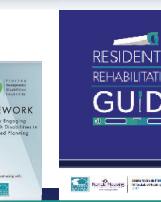
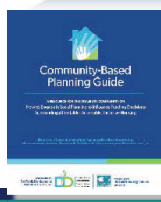
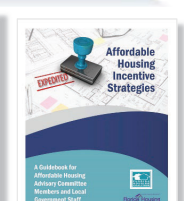
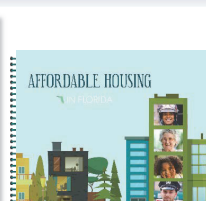
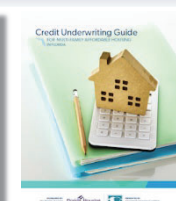
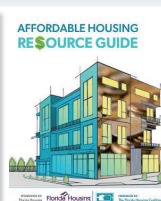
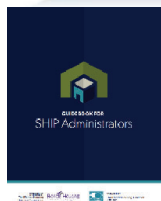
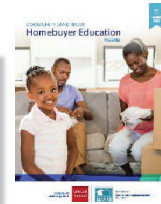
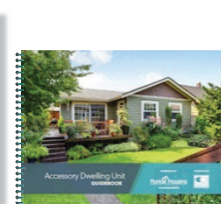
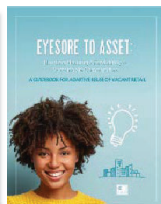
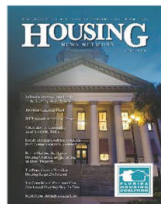


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## FLORIDA HOUSING COALITION PUBLICATIONS

Access these valuable resources and more  
under the Publications tab at [FlHousing.org](http://FlHousing.org)



# Upcoming Trainings

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- **In-Person Training:** The Credit Underwriting Process for Affordable Housing
  - Date: November 3<sup>rd</sup>
  - Location: Tampa
- **Webinars:**
  - HOME Funding for Affordable Housing – Part 2 (October 12<sup>th</sup>)
  - Successful Homeownership Initiatives (October 18<sup>th</sup>)
  - Mixed-Income Rental Housing (October 19<sup>th</sup>)
  - Overcoming NIMBY Opposition (October 25<sup>th</sup>)
- To Register, visit <https://flhousing.org/events/>

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