

## APPENDIX C

### UNDERWRITING STANDARDS RENTAL WITHOUT TAX CREDITS

The application will require the applicant to demonstrate that the project is financially feasible and viable using the least amount of HOME funds. Underwriting will be completed by IFA during the review of the application. IFA may adjust the amount of HOME award based upon the underwriting. Underwriting shall be completed for a project prior to the time HOME funds are awarded, and prior to close out of the project. The pro forma is part of the application.

The application will require the applicant to supply sufficient information to allow IFA to determine whether the project is financially feasible during the construction phase and the operational phase of the project. The application will require the applicant to provide information regarding loans, grants, equity contributions, property tax abatements, tax increment financing, enterprise zone benefits and any other type of financing or contributions that are relevant to the economic feasibility of the project and are available to the project.

The following minimum financial underwriting requirements apply to all HOME rental without tax credit projects. Projects that cannot meet the minimum requirements, as determined by IFA, will not receive HOME funds.

1. Escalation of Income & Operating Expenses - Projects will be underwritten with income and operating expenses escalating, with a minimum spread of one percent (1%) required between the income and expense escalators (expenses must increase at least 1% more than income annually.) For example, if income increases by 2% annually, then expenses must escalate by 3%.
2. Vacancy Rate - Projects will be underwritten assuming the following vacancy rate:

12 or greater total units	8% to 10%
Less than 12 total units	8% to 15%

3. Operating Expenses - The proforma must reflect minimum operating expenses of \$2,750 per unit per year, not including taxes, reserves and resident support services.
4. Reserves
  - A. Replacement Reserve - An initial deposit of \$700 per unit will be required to establish the replacement reserve account at construction completion. Annual deposits of \$350 per unit will be required throughout the HOME compliance period. The reserve shall only be used to cover capital expenditures and are subject to IFA consent for withdrawals exceeding levels established in the contract. Evidence of the replacement reserve account transactions and balance must be provided to IFA annually throughout the compliance period.
  - B. Operating Reserve - The project must establish an operating reserve account within one year of construction completion. The initial operating reserve is an eligible HOME project

cost and may be established with HOME funding. The calculation for the minimum operating reserve is:

Gross monthly rent amount for all units x 3 months

The reserve shall only be used to cover operating deficits with prior written consent from IFA. The operating reserve requirement may be met by provision of an irrevocable line of credit. Evidence of the operating reserve account transactions and balance or proof of the ongoing line of credit must be provided to IFA annually throughout the compliance period.

## 5. Financing Commitment

- A. For all projects proposing private construction and permanent financing, a letter of intent from the lending institution on their letterhead is required. This letter must clearly state the term of the permanent loan, how the interest rate will be indexed and the current rate at the time of the letter, the amortization period, fees, any prepayment penalties, anticipated security interest in the Property and lien position. The letter of intent must extend at least 6 months beyond the Application date due at IFA.
- B. For all other sources, except state HOME funds, a commitment for funding must be made in advance. Documentation that specifies the value of the commitment, the purpose the funds can be used for, and time limitations related to the commitment must be provided from the entity making the commitment.

## 6. Limitations

- A. Developer Fees - Developer fees (including overhead and profit and consultant fees) shall not exceed 15% of Site Work, Construction and Soft Costs items on the Budget page.
- B. Construction Contingency Funding - All projects shall have a hard cost construction contingency line item of at least five percent (5%) but no more than ten percent (10%) of Site Work and Construction items on the Budget page.
- C. Subsidy Layering Review - HUD is required to undertake subsidy layering reviews of each project receiving HUD housing assistance to ensure that the applicant does not receive excessive government subsidies by combining HUD housing assistance with other forms of federal, State or local assistance.
- D. Unit Cost Cap - IFA shall not award HOME funds to a project where the total project costs exceed the per unit dollar limitations established annually by HUD.

The following financial underwriting standards will be taken into account by IFA when determining the financial feasibility of the proposed project.

1. Debt Service Coverage Ratio (DSCR) – A DSCR between 1.15 and 2.00 for the entire HOME compliance period. If the DSCR exceeds 2.00, the applicant must submit an explanation which IFA will take into consideration when reviewing the application.

**NOTE: For Rental without tax credit applications, zero percent loans are available with flexible payment terms.**

