ADFA
ARKANSAS DEVELOPMENT FINANCE AUTHORITY

HOME Single Family Housing Development Program Guidelines

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Contents

1. Program Overview

The Arkansas Development Finance Authority (ADFA) supports the development of affordable single family homebuyer units for low-income households with its annual funding allocation from the U. S. Department of Housing and Urban Development's (HUD) HOME Investment Partnerships Program (HOME program). The HOME program was created under Title 11 of the Cranston-Gonzalez National Affordable Housing Act of 1990 with implementing regulations at 24 CFR Part 92.

ADFA's HOME funds will be used to provide financing to projects that will be marketed and sold to buyers with incomes at or below 80% of the Area Median Income (AMI) for the county in which the project is located. In exchange for development financing, developers will agree to comply with the requirements set forth herein with respect to construction, marketing, and sales.

HOME funds can support the development and sale of homebuyer units in three functional ways. First, HOME funds can be invested in a project's "development subsidy" or "appraisal gap." Due to market conditions in many areas, it costs more to develop and sell a home than the market value of the finished home. Second, to make housing affordable to income-eligible buyers, HOME funds initially used for development costs can be passed on to a buyer in the form of second mortgage financing to help cover the gap between the purchase price of the home at market value (plus closing costs) and the purchasing power of a low-income buyer, that is their cash investment and affordable first mortgage. This use of HOME can be referred to as "direct buyer assistance" or sometimes "affordability gap." Finally, in most cases HOME is also used, in part, as construction financing, covering the difference between interim construction sources (e.g. construction loans from a bank) and the full cost of a project. Since most construction loans are based on conservative loan to value ratios, affordable housing developers often need HOME assistance to bridge the financing gap.

This document sets forth the requirements for ADFA's awards of HOME funds for Single Family Housing Development projects and may be modified from time to time in order to comply with statutory or regulatory amendments.

2. Application and Evaluation Procedure

ADFA is accepting applications on a continual basis but may in the future issue a Single-Family Housing Development Request for Proposal (RFP), if funds are limited. The RFP will outline specific application deadlines, any funding focus (e.g. by project type, etc.), and other special considerations applied to a given funding round.

A. Funding Availability

Upon submission of a proposal for HOME funds, ADFA staff will conduct a review and analysis of the project and developers as presented in the proposal. Only projects with firm commitments for all other sources of funding may receive binding commitments.

B. Submission of Materials

All HOME Single Family Housing Development Program applicants will need to comply with the submission criteria set forth in ADFA's HOME APPLICATION and submit supporting documentation and due diligence items identified in Exhibit A. ADFA reserves the right to require the submission of additional information as needed to complete project underwriting.

3. Project Funding Requirements

A. Eligibility Criteria

Eligible Developer Applicants

ADFA will fund developers of affordable single family homebuyer units, including for-profit developers, non-profit developers, and ADFA-designated CHDOs. Developers must demonstrate the capacity and previous experience developing projects of the type presented in their proposals. Prior to committing funds, ADFA will review the status of any organization seeking funds from the CHDO set-aside to ensure that it meets all HOME requirements and that it has sufficient staff capacity to carry out the project.

Project Location

Projects must be located within the state of Arkansas.

Project Types

ADFA will consider proposals for new construction. In general, ADFA will require that all new construction homes have a minimum square footage of 1,100, at least 3 bedrooms, and at least 2 bathrooms. Applicant may request a waiver of the above type of home if a market study supporting the need for other types of housing is provided with the application.

Parameters of HOME Investment

Applications must include an investment of not less than $1,000 in HOME funds per HOME unit. In no case will ADFA investment exceed the maximum HOME investment allowed under 24 CFR 92.250.

Typically, ADFA will also establish a maximum cap on its investment in a single home. Such a limit will be based on the availability of funding and other ADFA priorities. ADFA's maximum caps: 0 BR- $112,500, 1 BR- $135,000, 2 BR- 157,500, 3 BR-$180,000, 4 BR- $200,000.

Defining the "HOME Project"

HOME defines a "project" as "a site or sites together with any building… or buildings located on the site(s) that are under common ownership, management, and financing and are to be assisted with HOME funds as a single undertaking." In many cases, a developer may apply for financing from ADFA to develop several houses, which may involve defining the group of units as a single HOME project. This is particularly the case for projects involving multiple units being built under a single construction contract – such as a proposal involving a whole subdivision or applications proposing to build attached or semi-attached units like townhomes.

However, in other cases, it will be appropriate to characterize proposals as a "series" of distinct HOME-funded projects. For example, in many cases, ADFA will limit funding to units which have been "presold" with an eligible and mortgage prequalified buyer already identified. In such a case, each unit would be financed individually based on the readiness to proceed and the financial needs of the specific buyer household. In other circumstances, an applicant may be financing each unit with distinct and separate forms of construction financing, for example using Bank A for construction financing on their first house and Bank B for the second. In those cases, the separate financing plans would also dictate defining each unit as an individual HOME project.

So, while applicants may seek financing from ADFA for several units of production through a single submission, in most cases it is likely that funding will be provided on a unit-by-unit basis with each unit defined as a distinct project and therefore funded under a separate written agreement. When multiple units are defined as a single project, there will be one funding agreement and the whole project will be subject to the various deadlines outlined herein. This will mean that the project completion deadline and the start of the affordability period will be driven by the sale of the last unit in a project.

B. Eligible Costs

Costs funded with ADFA's HOME funds must be eligible according to HOME Final Rule 24 CFR 92.206. The following additional limitations also apply:

- HOME funds shall not be used for luxury improvements according to 24 CFR 92.205.
- Unless for nominal consideration, ADFA will require that acquisition costs shall be supported by an independent appraisal of the property.
- HOME funds shall not be used for non-residential accessory structures such as free-standing garages, carports, or storage structures. Applicants must delineate project costs in a manner that allows free-standing structures to be clearly paid for using other project funds.

ADFA Project Soft Costs

The HOME program allows ADFA to include, as project costs, its internal soft costs specifically attributable to a HOME project. These may include consulting, legal, inspection, and staff costs associated with reviewing, processing, and overseeing the award of funds to the project. Projects must provide budget allowances for "ADFA Due Diligence, Inspection & Legal Costs" in the project's sources and uses.

Cost Reasonableness

Per the requirements of 92.250(b) and 2 CFR 200, all project costs must be reasonable, whether paid directly with HOME funds or not. ADFA will review project costs, including hard and soft costs, to evaluate their reasonableness and may, at its option, require applicants to obtain additional quotes, bids, or estimates of costs.

Identity of Interest

Developers must disclose any identity of interest situations that may occur when contracting with related companies during either the development or ongoing operation of the project. ADFA staff must be allowed the opportunity to conduct a cost analysis to determine costs reasonableness. Applications may be determined ineligible if access is not granted or costs are determined to be unreasonable.

C. Property Standards

To meet both HOME regulations and ADFA goals, all HOME-funded projects must meet certain physical standards intended to provide quality affordable housing that is durable and energy efficient.

- Construction must meet all applicable state and local codes including building, electrical, mechanical, and plumbing codes.

- All units must be served by public sewer, public water, and public road. Sites should have ready access to recreational opportunities such as parks, playgrounds, etc., nearby shopping and services including grocery, banking, and medical facilities, and otherwise be located in neighborhoods that provide amenities that support residential development. ADFA also generally prefers that sites have safe, walkable connections – including sidewalks – to the surrounding neighborhood.

- All HOME projects must meet applicable Section 504/Uniform Federal Accessibility Standards (UFAS) requirements. Pursuant to 24 CFR 8.29, single family housing developed with Federal funds must be made accessible upon the request of the prospective buyer if the nature of the prospective occupant's disability so requires. Developers must ensure that projects are designed in a way that can accommodate such a request. Should a prospective buyer request a modification to make a unit accessible, Developer must work with the homebuyer to provide the specific features that meet the need(s) of the prospective homebuyer or occupant. If the design features that are needed for the buyer are design features that are covered in UFAS, those features must comply with the UFAS standard. Developers may be permitted to depart from the standard in order to have the homebuyer/occupant's needs met.

- Units must be equipped with the following appliances: Refrigerator, range/oven, and dishwasher. Developers may also propose to include in-unit clothes washers and dryers, microwave/vent fan combination units, as appropriate. If the Energy Star program rates the type of appliances being installed, the developer must furnish the units with Energy Star rated appliances. Note however that not all appliances are rated by the Energy Star program.

D. Sales Price

Housing developed with HOME funds must be modest, and the sales/purchase prices for homes developed under this program cannot exceed the HOME Homeownership Value Limits published by HUD in effect at the time of project commitment.

Units produced under ADFA's Single Family Housing Development Program must be sold at the fair market value as determined by an "as-completed" or "subject to completion" appraisal completed by an independent state licensed appraiser. Developers shall submit such an appraisal prior to project commitment, and ADFA will require an updated appraisal at construction completion. Any reductions in list or sales price below ADFA-approved appraised value must be approved in writing by ADFA and will generally require updated market information.

E. Eligible Homebuyers

Homebuyers for units produced under ADFA's Single Family Housing Development program must have incomes at or below 80% AMI, not own another home at the time of purchase, and meet the other eligibility criteria set forth in the Buyer Underwriting section of these guidelines.

F. Environmental Review Requirements

Federally assisted projects are subject to a variety of environmental requirements. Developers should be familiar with these requirements and are strongly encouraged to discuss any questions they have with ADFA staff prior to entering into a purchase agreement or submitting an application.

- All projects shall be implemented in accordance with environmental review regulations as defined at 24 CFR Part 58.

- ADFA shall be responsible for conducting the environmental review and completing all necessary public notifications, and the request for release of funds (RROF) from HUD. The applicant is responsible for cooperating with ADFA in the environmental review process and providing information necessary for ADFA to fulfill its responsibilities under Part 58 and other applicable regulations.

- Applying for HOME funds triggers environmental review requirements under 24 CFR Part 58, including the National Environmental Policy Act (NEPA). Once an application for federal funds is submitted, a development proposal is now subject to the environmental review requirements and requires an environmental clearance and issuance of a Release of Funds (ROF) by the US Department of Housing and Urban Development.

- Developers are prohibited from undertaking or committing or expending any funds (including non-federal funds) to any physical or choice-limiting actions on the site prior to an environmental clearance as required by Part 58. Physical and choice limiting actions include, but are not limited to, property acquisition, demolition, conversion, or construction. This prohibition applies regardless of whether federal or non-federal funds are used and taking a choice limiting action prior to completion of the required environmental clearance process will result in the denial of any HOME funds from ADFA.

G. Other Federal Requirements

Nondiscrimination and Equal Opportunity
The following federal nondiscrimination and equal opportunity guidelines apply to all projects and affect both development and sales of assisted housing:

- The Fair Housing Act (42 U.S.C. 3601-19) and implementing regulations at 24 CFR part 100 et seq.;

- Executive Order 11063, as amended by Executive Order 12259 (3 CFR, 1959-1963 Comp., p. 652 and 3 CFR, 1980 Comp., p. 307) (Equal Opportunity in Housing Programs) and implementing regulations at 24 CFR part 107;

- Title VI of the Civil Rights Act of 1964 (42 U.S.C. 2000d-2000d-4) (Nondiscrimination in Federally Assisted Programs) and implementing regulations at 24 CFR part 1;

- The Age Discrimination Act of 1975 (42 U.S.C. 6101-6107) and implementing regulations at 24 CFR part 146;

- Section 504 of the Rehabilitation Act of 1973 (29 U.S.C. 794) and implementing regulations at part 8 of this title;

- Title II of the Americans with Disabilities Act, 42 U.S.C. 12101 et seq.; 24 CFR part 8; Section 3 of the Housing and Urban Development Act of 1968 (12 U.S.C. 1701u) and implementing regulations at 24 CFR part 135;

- Executive Order 11246, as amended by Executive Orders 11375, [[Page 41]] 11478, 12086, and 12107 (3 CFR,1964-1965 Comp., p. 339; 3 CFR, 1966- 1970 Comp., p. 684; 3 CFR, 1966-1970 Comp., p. 803; 3 CFR, 1978 Comp., p. 230; and 3 CFR, 1978 Comp., p. 264, respectively) (Equal Employment Opportunity Programs) and implementing regulations at 41 CFR chapter 60;

- Executive Order 11625, as amended by Executive Order 12007 (3 CFR, 1971- 1975 Comp., p. 616 and 3 CFR, 1977 Comp., p. 139) (Minority Business Enterprises); Executive Order 12432 (3 CFR, 1983 Comp., p. 198) (Minority Business Enterprise Development);

- Executive Order 12138, as amended by Executive Order 12608 (3 CFR, 1977 Comp., p. 393 and 3 CFR, 1987 Comp., p. 245) (Women's Business Enterprise). The nondiscrimination provisions of Section 282 of the National Affordable Housing Act of 1982; and

- The Equal Access Rule, 24 CFR 5.105(a)(2), requiring that assisted housing be made available without regard to actual or perceived sexual orientation, gender identity, or marital status.

Uniform Relocation Act (URA)
All projects fall under requirements of the URA. Applicants must further document that any purchase of property meets the requirements of URA, including provision of notices to the seller identifying the transaction as a voluntary sale not under the threat of eminent domain.

Any project resulting in permanent relocation/displacement of households will not be funded by ADFA.

Davis Bacon
Davis Bacon federal prevailing wage requirements shall apply to all projects with 12 or more units assisted with HOME funds.

Minority Business Enterprise and Women Business Enterprise (MBE/WBE) Plan
Developers must maintain an MBE/WBE plan that demonstrates marketing and solicitation of MBE/WBE businesses and contractors for the construction of the project.

Section 3
Developers must maintain a Section 3 plan that demonstrates a marketing plan to include Section 3 contractors in the construction of the project.

Excluded Parties
ADFA will not fund projects owned, developed, or otherwise sponsored by any individual, corporation, or other entity that is suspended, debarred, or otherwise precluded from receiving federal awards. Nor may the developer contract with any other entity (including but not limited to builders/general contractors, property management companies, or other members of the development team) that are suspended, debarred, or otherwise so precluded. Similarly, the general contractor will be required to determine that subcontractors are not so precluded.

4. Ongoing Project Requirements

A. Deadlines

- **Construction Start** – If construction is not started within 12 months of the date ADFA commits funds to a project, the commitment will be subject to cancellation. If the project is cancelled as a result of failure to meet this deadline, the Developer must repay to ADFA any HOME funds disbursed for the project.

- **Completion Deadline** – Project completion occurs when construction is complete, all HOME funds have been disbursed by ADFA and drawn from the US Treasury, title to the property has transferred to an eligible buyer, and required completion data has been entered in HUD's IDIS system. Project completion must occur within 2 years of the date of commitment of funds to the project. If the Developer fails to meet this 2-year deadline, it must repay to ADFA any HOME funds disbursed for the project.

- **Sales Deadline** – Pursuant to 24 CFR 92.254(a)(3), Developers must have a ratified sales contract with an eligible buyer for each HOME-funded unit within nine (9) months of completion of construction or the unsold units must be converted to rental housing, or the project will be deemed ineligible and all HOME funds drawn must be repaid to HUD.

  If a unit is unsold after six (6) months, the Developer must present an updated sales and marketing plan to ADFA outlining steps being taken to identify buyers. At ADFA's option, the Developer may be required to i) take further steps – such as listing the home with a licensed realtor, adjusting the sales price, etc. – as ADFA may require the facilitation of the sale of the home or ii) transfer title to ADFA or to another entity selected by ADFA that can otherwise identify buyers prior to the regulatory deadline.

  At ADFA's sole option, if a unit remains unsold after nine (9) months, the developer shall be required to i) repay the entire HOME investment, including any ADFA project soft costs; ii) convert the project to rental housing in accordance with 24 CFR 92.252; or iii) to transfer title to ADFA or to another entity selected by ADFA for conversion to rental housing.

  Units converted to rental housing must be rented to eligible tenants in accordance with 24 CFR 92.252, which includes tenant income eligibility and rent limit requirements. Further, any units converted to rental properties shall be operated in compliance with ADFA's Rental Management Handbook.

B. Reporting and Record Keeping

To allow effective oversight of funded projects and document compliance with applicable HOME requirements, all projects must submit periodic reports to ADFA. While this section outlines standard reporting requirements, ADFA reserves the right to require additional reporting or to alter the reporting format or frequency based on future changes to HOME requirements or ADFA policy. Additionally, ADFA reserves the right to require additional or more frequent reporting for projects with compliance deficiencies.

- Developers are required to report quarterly during the development phase and sales phase. Quarterly reports will be due on the 15th of the month following the end of the prior quarter (e.g. by April 15th reports on the first quarter are due);
  - During the construction phase, developers must provide monthly reports detailing construction progress and barriers to progress, copies of invoices being paid, and evidence of appropriate lien waivers.
  - During the sales phase, developers are required to provide monthly reports detailing the number of additional sales, total sales, and marketing activity. These reports are required until all units are sold.

- ADFA may require more frequent reporting due to findings identified during the development and sales phases.

- At ADFA's option, Developers may be required to obtain and submit an audit of project costs (i.e. cost certification) prepared by an independent Certified Public Accountant.

- Developers shall allow ADFA, HUD, the Comptroller General of the United States (aka the GAO), and all other pertinent Federal or State agencies or their designated representative the right to inspect records and property.

C. Conflict of Interest

To comply with HOME requirements and to maintain a high standard of accountability to the public, conflicts of interest and perceived conflicts of interest must be avoided.

Developers shall maintain compliance with all HUD conflict of interest provisions as stated in 92.356(f).

Developers with officers, employees, family members, consultants, or agents that are otherwise eligible to purchase HOME funded units must receive waiver/approval from ADFA staff before entering into a sales agreement with HOME eligible employees. 92.356(f) provisions apply to all HOME projects.

5. Structure of Transaction

A. Loan Types and Terms

ADFA will provide HOME funds in the form of a loan to the entity that owns the property. No grants will be awarded, and funding commitments are not transferable without prior written ADFA approval.
ADFA's HOME Loan may be used for acquisition and construction financing. Proceeds of the HOME loan will only be released following satisfaction of all requirements outlined below.

In all cases, the HOME loan will:

- Have a maximum term of 2 years;

- Be repayable in full upon sale, refinancing, or transfer of the property or upon maturity, except that repayment will be limited to the net proceeds of an ADFA-approved sale to a low-income buyer. Net sales proceeds will exclude any portion of the sale proceeds used to repay senior construction debt, return of ADFA-recognized developer equity, approved sales costs, and any HOME-assistance transferred to the buyer(s) at closing as direct homebuyer assistance; and

- Secured with a promissory note, mortgage, and appropriate UCC liens. Mortgages will be recorded with the applicable County Recorder of Deeds and generally may be subordinate only to an approved amortizing first mortgage.

B. Guarantees

Unless otherwise determined by ADFA, all underlying individuals, corporate entities, partnerships, or limited liability companies with an interest in a project's for-profit developer will be required to provide a completion guarantee including provisions guaranteeing construction completion of the project. For nonprofit organizations, including community housing development organizations (CHDOs), a separate guarantee shall not be required, but in all cases ADFA will require a performance bond or irrevocable letter of credit acceptable to ADFA to ensure project completion.

C. HOME Agreement

In addition to any financing documents, developers of HOME-financed projects must sign a HOME agreement with ADFA for each HOME project. The HOME agreement will identify requirements for compliance with the HOME regulations and ADFA's Single Family Housing Development Program requirements and will remain in effect in the event of any prepayment of the HOME loan.

6. Project Underwriting & Subsidy Layering Reviews

The HOME Final Rule, 24 CFR 92 et seq, requires ADFA to conduct underwriting and subsidy layering reviews of each project prior to committing HOME funds. The rule also identifies minimum elements ADFA must consider and requires ADFA to establish specific guidelines against which projects will be evaluated.

Underwriting is more than a technical requirement, and the term itself is used in several different ways. Depending on the context and the speaker "underwriting" is sometimes used in a limited fashion to refer primarily to the financial review of a potential transaction. Other times, the term "underwriting" is narrowly understood as a "check the box" set of "static" technical reviews resulting in a determination that a project does or does not meet a magic formula. In both cases, these uses of the term are too limited.

In practice, underwriting is a reflexive process. Every project involves risk, and even the best project can fail due to unforeseen factors. The goal of underwriting is to both <u>identify</u> and <u>mitigate</u> risk across a series of perspectives. In other words, the underwriting process is not an up or down review, but it often changes the project itself by imposing requirements to improve viability or business terms that transfer risk from one party (like ADFA or a lender) to another (especially the developer).

In this sense, ADFA's approach to underwriting is informed not only by traditional "lending" perspectives and minimum requirements of the HOME program, but a holistic approach to balancing the various risks inherent in any real estate transaction and the public purposes ADFA seeks to support – not the least of which is producing safe, decent, affordable housing that will be an enduring community resource.

In reviewing applications for HOME assistance, as required by §92.250(b) and prudent business practices, ADFA's underwriting framework includes evaluations of:

- **Regulatory requirements** applicable to the project, including compliance (or ability to become compliant) with HOME's affordability restrictions, property standards, and cross-cutting federal requirements;
- **Market risk**, including whether or not sufficient demand exists for the project(s), the anticipated absorption period, and whether general economic conditions and other competition supports the sale of units;
- **Developer risk**, focusing on whether the owner/developer (including but not limited to the underlying owners of special purpose entities) have the technical capacity to develop and sell the property and the financial capacity to safeguard public funds and backstop the project in the event of cost overruns or slow sales; and
- **Project risk** (or "financial underwriting"), testing the economic and financial projections for the transaction including both sources and uses as well as the projections of likely sales proceeds and

their uses. This includes confirmation that all sources of project financing are available, commercially reasonable, and have been appropriately maximized prior to awarding HOME funds.

A. Market Assessment

ADFA's approach to market assessment of for-sale proposals will generally vary based on whether the applicant is proposing a "pre-sale" or "spec building approach."

Pre-sale Approach: Some developers use a pre-sale approach whereby they identify specific buyers for a given unit prior to beginning construction. This may involve the buyer having formally signed a purchase agreement (subject to appropriate approvals by ADFA) for the unit or may involve other less binding reservation agreements. For example, a Habitat for Humanity organization may have already selected the buyer for a given unit, prequalified that buyer, and begun to recognize sweat equity contributions from the buyer's volunteer time on other Habitat builds even without the buyer having signed a binding purchase agreement.

In such cases, to assess the market for the unit(s) proposed, ADFA will primarily review:

- Information about the specifically identified buyers, focusing on their pre-qualification information suggesting they are income eligible, able to meet ADFA's Homebuyer Underwriting Standards (including their ability to qualify for an acceptable first mortgage as applicable), and the formality of the "pre-sale" arrangement; and
- Information about "excess" pipeline of potential buyers currently working with the developer. This may include formal waiting lists of similarly pre-qualified buyers, lists of interested applicants who are at earlier stages of the pre-qualification process (e.g. individuals who have completed counseling but are not yet pre-qualified for a mortgage, those who are participating in homeownership and/or similar financial counseling and working through credit issues, etc.)

<u>Key Evaluation</u>: In general, when a unit is presold, the primary market risk to address is the potential that a given buyer will "fall out" and need to be replaced. This can happen for reasons ranging from a buyer losing a job, getting sick, receiving a new job outside the region, or backing out of the purchase for some other reason. When the developer has a strong track record of closing with originally identified buyers, ADFA will expect a waiting list of pre-qualified buyers equal to at least 1.5 times the number of units under construction. For example, if a developer is proposing to build six units, then the waiting list must have at least three additional prequalified buyers beyond the six that have "reserved" houses already.

For situations where the pipeline is made up of potential buyers who are in earlier stages of the process but not fully prequalified, ADFA will expect to see a higher ratio of documented pipeline to proposed units. This may be based on a review of the developer's track record of converting its potential buyer pipeline to closings. Alternatively, absent a waiting list of pre-qualified "backup" buyers, ADFA may require submission of market data as outlined in the "Spec Building" section below.

Spec Building Approach: When units are not presold or ADFA is not satisfied with depth of the buyer pipeline, applicants must prepare and submit an analysis of the market for the proposed project. Developers may engage their real estate agent or another qualified party to help assemble the information.

The assessment must:

- <u>Identify the neighborhood market area</u> in which the project is located. This may involve existing, recognized neighborhood boundaries or other relevant boundaries such as jurisdictional or school district lines, major traffic corridors, natural features like rivers, etc. It may also involve recognized "neighborhood" or "submarkets" commonly used in the area Multiple Listing Service (MLS).

- Itemize and summarize residential sales from the past year. Sales should be broken out, insomuch as possible, by owner-occupied vs. rental (investor owned), new vs. existing, and price range. Emphasis should be given to sales within +/-$25,000 of the anticipated market value of the unit(s) being proposed by the applicant. To the degree known, the following data must also be provided:
    - Number of bedrooms/bathrooms, sq. footage, other amenities, etc.
    - Original list vs. final sales price;
    - "Days on market" for each home sale should be listed and an average compiled;
    - Seller concessions offered or provided;
    - Cash sales vs. those financed with a mortgage;

  Data should include all publicly disclosed sales, including any that may have been "for-sale by owner" or otherwise not listed through a realtor and/or identified in the MLS.

- Itemize and summarize current for-sale properties. Other than actual sales pricing, the same information for past sales must be provided for currently for-sale properties. Particular emphasis should be given to homes offered within +/-$25,000 of the unit(s) being proposed.

- Identify and summarize the pipeline of homes under development, including the availability of "build to suit" lots with infrastructure already in place.

- Based on the information above, the assessment must calculate "months of supply" available for both residential homes in general and for those within +/-$25,000 of the proposed unit(s).

Key Evaluation: In general, ADFA will focus on whether the average days on the market for competing units (i.e. within a reasonable price range of proposed units) is less than 90 days and whether, as of the application, there is less than 3 months' supply of competing product available. ADFA will also consider whether sales volume and available supply has increased/decreased over shorter, more recent analysis periods. For example, if the total sales volume from the past year overall is strong but has markedly declined in the last 3-6 months, ADFA may take a more cautious approach.

Note, in all cases, ADFA reserves the right to award funds on an incremental basis, limiting the number of houses under construction without identified buyers. For example, ADFA may award funds for only two spec-built units at a time and incrementally award additional funds as homes are sold (including execution of purchase agreements by qualified buyers prior to completion of construction) such that no more than two unsold homes are under development at any given time.

B. Developer and Development Team

In most cases, ADFA anticipates that projects will be owned, developed, and sold by multi-asset/multi-project developers rather than by single-purpose, single-asset entities created to develop a specific development. For projects funded from the CHDO set-aside, the CHDO itself must hold title to the property during construction and sell directly to income-eligible buyers.

Developer Technical/Professional Capacity

In evaluating the capacity of the "developer" ADFA will use the term more loosely to refer collectively to the underlying corporate entities and individuals that will own and control any single-purpose entity established to develop the proposed project. Additionally, ADFA may require various guarantees and indemnities from all of the underlying corporate and individual owners of the various limited partnership or limited liability corporation entities involved in the ownership and development of the project.

Developers should demonstrate:

- Recent, ongoing, and successful experience with the development of similar regulated affordable housing; and
- The presence of adequate staff, with specific experience appropriate to their role in the project, to successfully implement and oversee the project. This includes the assembly and oversight of the development team.

ADFA requires applicants to provide descriptions of all for-sale projects completed in the last five years, including any under development and land held (or under option) for additional projects. The description should identify the number of units produced, total/average cost, sales prices/market values, and sales history including number of units sold, average (and maximum) time on the market from listing to sales contract, and typical income range of buyers. Developers should identify if any units developed took longer than six months between construction completion and executing a sales contract and whether any units were converted from for-sale to rental due to failure to meet the HOME requirements.

Applicants are also required to provide descriptions of the role played by specific staff members relative to the proposed project along with resumes or other similar information demonstrating experience appropriate to the assigned staff member's role.

Financial Capacity

Developers must also demonstrate the financial capacity to support the proposed project during construction and prior to the sale of the home. This includes not just that the applicant has sufficient financial resources but that it has adequate financial systems in place to appropriately manage project funding, accurately account for all project costs, and provide reliable reporting to ADFA and other project funders.

At minimum, ADFA will review audited financial statements and interim financial statements to ensure that:

- The "primary" development entity's most recent audit must demonstrate compliance with Generally Accepted Accounting Principles (GAAP) and must not express material weaknesses in the entity's system of internal controls or financial management systems.

Development Team

ADFA will also review the capacity of the development team including but not limited to the general contractor, architect/engineer, accountant, attorney, and any other specialized professionals or consultants.

As a whole, the development team should have the skills and expertise necessary to successfully complete and operate the development. Insomuch as possible, on balance the development team should have worked successfully on other projects in the past. That is, while a developer may identify new development team members from project to project, an "entirely new" team may present added risk.

Additionally, when using development team members from outside of the region, ADFA will consider whether assigned team members have recent local experience or have been supplemented with local professionals. This may be particularly important for design professionals and legal counsel.

In no case, may any owner/developer/applicant or any member of the development team be a suspended, debarred, or otherwise excluded party.

Identity of Interest Relationships & Costs

Applicants must disclose all identity of interest relationships/contracts and/or costs involved in a transaction, including during the development period and following completion of the project. ADFA reserves the right to review any such costs further to ensure they are reasonable and consistent with the costs expected from arms-length relationships.

An "Identity of Interest" (whether or not such term is capitalized) is any relationship based on family ties or financial interests between or among two or more entities involved in a project-related transaction which reasonably could give rise to a presumption that the entities may not operate at arms-length. ADFA will take a broad approach to defining identities of interest and expects all applicants to err on the side of disclosure. That is, if there is any question about whether an identity of interest may exist, the relationship should be disclosed and explained to ADFA.

Beyond this general definition, an identity of interest relationship will be deemed to exist if:

1. An entity, or any owner of any direct or indirect ownership interest in such entity, or any family member of any such owner is also an owner, through a direct or indirect ownership interest, or an officer, director, stockholder, partner, trustee, manager, or member of the counterparty; or
2. Any officer, director, stockholder, partner, trustee, manager, member, principal staff, contract employee or consultant of an entity, or any family member of thereof, is an owner, through any direct or indirect ownership interest, or an officer, director, stockholder, partner, trustee, manager or member of the counterparty.

For purposes of this definition, "family member" means the spouse, parents or stepparents, children or stepchildren, grandparents or step-grandparents, grandchildren or step-grandchildren, aunts, uncles, parents-in-law, and siblings-in-law (or their children or stepchildren). It also includes any other similar relationship established by operation of law, including but not limited to guardianship, adoption, foster parents, domestic partnerships, and the like.

C. Financial Analysis

As noted in the introduction, ADFA views underwriting as more than just the financial review of a project. However, a review of the underlying financial assumptions is still a critical and core part of underwriting. In reviewing projects, as a public funder ADFA must balance two potentially competing perspectives.

Projects must be viable, that is they must have sufficient allowances for all costs to maximize the chances the project can meet or exceed its financial projections and thereby succeed in the marketplace. In other words, the project must represent a "safe" investment. However, taken to an extreme, "safe" or overly conservative projections can also result in a project that is over-subsidized, risks providing excessive returns to the owner/developer, and reduces the impact of limited subsidy funding.

As a steward of very limited public funding for affordable housing, ADFA also needs to ensure that costs are reasonable, that they represent a "good deal" to the public, and that returns to the owner/developer are fair but not excessive. In seeking to balance these perspectives, ADFA has established the following review factors and principals.

Development Costs
In general, ADFA will review the entire project budget to ensure that all costs are reasonable and that the budget is sufficient to complete and sustain the project. All line items, whether or not paid directly with HOME funds, must be necessary and reasonable.

ADFA will consider the cost of both specific line items as well as the total development cost on a per unit and per square foot basis, comparing costs to other projects from ADFA's portfolio, similar projects in the region (such as those funded by local HOME PJs), data from the local Building Department, and/or third-party indices such as RS Means.

Selected Development Cost Items
Acquisition – Acquisition costs must be supported by an independent third-party appraisal prepared by a state-licensed appraiser. The purchase price must be at or below the as-is market value of the property. In the event an applicant has previously purchased land prior to applying to ADFA, the project budget may only reflect the lesser of the actual purchase price or the current market value. Standard closing costs from the acquisition may be included.

Applicants who purchased property prior to applying to ADFA, or following environmental releases under National Environmental Policy Act (NEPA) but prior to closing, may not charge or include financing costs associated with interim financing, whether from third-party or related lenders.

Contingencies – Applicants should include a contingency (inclusive of hard and soft costs) within the minimum and maximum amounts noted below. The contingency will be measured as a percentage of hard costs (including the construction contract plus any separate contracts for off-site work but excluding contractor fees).

- New construction projects should include a contingency of least 5% and no more than 10% of hard costs;

ADFA may consider higher contingencies based on identified risk factors such as the known need for environmental remediation or poor subsurface soils.

Contractor Fees – Contractor fees are limited as a percentage of net construction costs as further identified below. Net construction costs exclude the contractor fees, any budgeted contingency, and (even if otherwise included in the construction contract) permits and builder's risk insurance.

- **Contractor Profit:** 6% of net construction costs
- **General Requirements/General Conditions:** 6% of net construction costs. General requirements include on-site supervision, temporary or construction signs, field office expenses, temporary sheds and toilets, temporary utilities, equipment rental, clean-up costs, rubbish removal, watchmen's wages, material inspection and tests, all of the builder's insurance (except builder's risk), temporary walkways, temporary fences, and other similar expenses.
- **Contractor Overhead:** 2% of net construction costs.

With prior approval of ADFA, contractor fees may vary from the limits above provided the gross contractor fees do not exceed 14% of net construction costs.

Developer Fees – Developer fees are intended to compensate a developer for the time and effort of assembling a project, overseeing the development team, and carrying a project to fruition. Developer fees are also intended to compensate for the risk inherent in the development process, including that not every potential project proves viable and that developers must necessarily advance funds for their own operating costs and various third-party predevelopment costs prior to closing (or in some cases for projects that never proceed). ADFA, therefore, allows the inclusion of developer fees as follows:

- **Developer Fee:**
- 10% of total development costs less a) the developer fee itself; b) realtor commissions or other seller closing costs.
- **Maximum Limit:** Regardless of percentage, the maximum developer fee shall be $20,000.
- **Combined Contractor & Developer Fees:** When an identity of interest exists between the owner/developer and the general contractor, the combined total of contractor fees and developer fees cannot exceed 20% of total development cost less a) the developer fee and b) other cost elements excluded from the calculation of the developer fee itself (see above).

Projecting and Using Sales Proceeds
ADFA will review an applicant's projection of sales proceeds to ensure they are reasonable and achievable. All units should be sold at the fair market value as determined by an "as-completed" or "subject to completion" appraisal completed by an independent state licensed appraiser. Developers shall submit such an appraisal prior to project commitment, and ADFA may require an updated appraisal prior to listing or construction completion if the appraisal is more than 9 months old at that point. Any reductions in list or sales price below ADFA-approved appraised value must be approved in writing by ADFA and will generally require updated market information justifying the reduction.

While all units are to be sold at fair market value, actual sales proceeds available to repay interim construction sources are affected by the buyer's purchasing power (the mortgage they can actually afford). A portion of ADFA funds (including HOME, CDBG, NSP, etc.) originally advanced toward development costs are effectively "transferred" to income-eligible buyers in the form of second mortgage assistance at closing. In other words, the buyer will assume a portion of the public construction loan made to the developer at closing in lieu of the developer repaying the construction loan in full.

As a result, the gross sales proceeds will generally be the lesser of the sales price or the buyer's mortgage amount and cash investment (minus the buyer's closing costs). From the sales proceeds, developers must

- Pay seller closing costs (e.g. real estate commissions and other closing fees). These are paid at closing from sales proceeds rather than being directly disbursed by the developer;
- Repay interim construction sources. This may include construction loans from a bank or ADFA-approved equity invested by the developer;
- Pay any outstanding development costs. In limited cases, the contractor may be owed a final payment or other miscellaneous development costs may be outstanding and paid at closing from sales proceeds. Any such arrangement must be disclosed to and approved by ADFA prior to closing; and
- Pay developer fee. ADFA will pay the developer fee at completion of the project and after submission and approval of all project-related retainage documentation.

In most cases, the remaining sales proceeds available after payment of these items is less than the original investment made by ADFA. For a project otherwise meeting all requirements of the program, including all federal requirements of HOME (or other federal funding sources), ADFA will accept the remaining sales proceeds as full and final payment of the construction loan provided to the developer.

Other Funding Sources

Prior to committing funds, all other funding sources necessary for a project must be identified, committed in writing, and consistent with both ADFA's underwriting requirements and the affordability restrictions of the HOME program. In general, developers must make all reasonable efforts to maximize the availability of other funding sources, including construction lending and/or developer equity, within commercially available and reasonable terms.

Additionally, restrictions or limitations imposed by other funding sources cannot conflict with any applicable HOME requirements and cannot, in the discretion of ADFA, create undue risk to ADFA.

To limit the risk of taking on too much construction debt, ADFA generally expects a developer to obtain interim construction sources (loans or equity) equal to no more than 80% of the projected buyer's funds (affordable mortgage minus buyer closing costs).

7. Buyer Underwriting and First Mortgage Requirements

Pursuant to 24 CFR 92.254(f), ADFA is required to establish and implement various homebuyer program policies related to the underwriting of buyer assistance, ensuring that HOME-assisted buyers obtain responsible first mortgages, and the conditions under which ADFA will subordinate its HOME-funded assistance to accommodate future refinancing by assisted buyer.

Through these policies, ADFA intends to ensure that participating buyers will be successful homeowners by providing the assistance each buyer needs to make the home affordable while serving as many households as possible with limited HOME funds. In addition, ADFA must ensure that assisted buyers are informed consumers and avoid the use of risky lending products. To balance these priorities, ADFA has developed these underwriting guidelines based on the following key principles.

- Assisted buyers should have good credit and qualify for competitive lending products on par with those offered to credit-worthy unassisted buyers in the local market.

- Assisted buyers should make reasonable and meaningful contributions to their home purchase in terms of both up-front investment and monthly payment without being left without cash reserves after closing or overburdened by their monthly payment.

These policies are applicable to **all** homebuyer units supported by ADFA's HOME program, whether HOME funds are being used to only provide direct homebuyer assistance (e.g., down payment and closing costs) or are being provided as development funds to build or rehabilitate the unit being purchased by a HOME-assisted buyer. The policies are applicable whether the funds are provided directly by ADFA or through any of ADFA's program partners.

While these policies apply to all homebuyers, there may be individual cases where exceptions are justified for one or more of the local policy requirements. ADFA cannot waive HUD regulatory requirements. Program participants may request specific exceptions in writing, either before a decision is made or after an adverse decision is made.

A. Maximum Homebuyer Assistance

The maximum HOME-assistance available for a buyer is 10% of the current Arkansas Homeownership Sales Price Limit as determined annually by HUD.

Not all buyers will qualify for the maximum assistance. The assistance available to any given buyer is based on ADFA's assessment of the buyer's need using the underwriting and lending criteria outlined in this policy.

B. Definitions of Income for Eligibility and Underwriting

ADFA limits eligibility to buyers with incomes within a range as defined below:

- Maximum 80% of AMI: The HOME statute and regulations limit HOME assistance to households with incomes at or below 80% Area Median Income (AMI) as defined annually by HUD and adjusted for household size.

Homebuyer income eligibility will be determined using the Part 5 definition of income.

The total household income will be used for determining program eligibility and must be documented with at least two-months of source documentation (e.g. paystubs, benefit records, bank statements). Income attributable to all household members, whether related by blood or marriage or not, will be included for eligibility purposes.

However, for underwriting purposes only (that is to determine the appropriate level of assistance), the following adjustments to income will be made:

- The income of adults who will not have an ownership interest in the property will be excluded. For example, the income of an elderly parent that is part of the household but is neither being listed on title to the property nor included on the loan documents will not be included in calculations of the income available to make the mortgage payment. This exclusion for "non-purchasing" adults is not intended to optionally exclude the income of a household member with marginal credit. In the case of married couples, the income of both spouses will always be included for underwriting purposes.

- Significant sources of income such as social security benefits, child support payments, or the like that will not continue for three (3) years will be excluded. For example, child support received for a 16 ½ year old is included in the Part 5 definition of income because it will continue over the upcoming 12 months but will not be counted in buyer underwriting as the income will cease when the child turns 18.

- Any imputed income from assets will be excluded for underwriting purposes.

C. Buyer Underwriting

To ensure that buyers are likely to sustain homeownership, assisted buyers are expected to:

- Purchase a unit for a reasonable price that does not exceed:
  - The fair market value as determined by a third-party appraisal and
  - The HOME Program Homeownership Value Limit as determined by HUD for the type (new or existing) and location of the home.

- Obtain a senior mortgage loan that meets the Responsible Lending policy below for which:
  - The monthly housing expenses (i.e., front-end ratio) do not exceed 28% of the buyer's monthly underwriting income;
  - The monthly housing expenses (front-end ratio) is at least 20% of their monthly underwriting income OR the first mortgage is limited by the loan-to-value ratio and not the buyer's payment capacity; and
  - The total debt burden (i.e., back-end ratio) is not in excess of 43%.

  Even when assisted buyers are willing to take on larger monthly payments and a lender is willing to exceed these ratios, ADFA has determined that Low Income buyers are less likely to be able to sustain homeownership over the period of affordability and will put the HOME funds at unacceptable risk. The minimum front-end ratio is to avoid over-subsidization of homebuyers with excessive debt and similarly constitute unacceptable risk to the HOME funds.

- Contribute at least $1,000 of the purchase price toward down payment and/or closing costs. Documented costs (e.g. an appraisal) "paid outside of closing" by the buyer will be credited toward this requirement.

- In addition to cash toward purchase, buyers should have sufficient liquid assets after closing to cover at least 1 times their total monthly housing payment. For purposes of this requirement, liquid assets are cash and those readily convertible to cash, including but not limited to savings or checking accounts, certificates of deposit, stocks and bonds, etc. Liquid assets, however, exclude life insurance policies and any savings held in a tax-preferred retirement account (e.g. pension, 401(k), IRA, etc.), college savings plan (e.g. 529 account), or health savings account recognized by the Internal Revenue Service.

- Invest liquid assets in excess of $25,000 toward the purchase of the home before receiving HOME-assistance.

- To ensure that other non-housing, non-debt expenses do not unduly threaten an assisted buyer's ability to afford their first mortgage, ADFA will consider the amount by which non-discretionary fixed expenses exceed 25% of buyer income that may be added to other debt for purposes of determining the back-end ratio:

  In all cases, the buyer must still be qualified to spend at least the percentage of their income toward housing costs (minimum front-end ratio) without requiring assistance in excess of the maximum assistance limit, even with reductions in mortgage capacity due to this consideration of other expenses.

D. Pre-Purchase Counseling

In December 2016, HUD published the Final Rule for Housing Counseling Certification which applies to homeownership counseling required by the HOME program. That rule, the final effective date of which is August 1, 2020, requires that HOME-assisted buyers receive counseling from HUD certified counselors employed by HUD-approved Housing Counseling Agencies.

Every buyer of a HOME-assisted unit must receive counseling, regardless of the manner in which the unit was assisted with HOME. Each buyer must receive housing counseling prior to executing the written agreement for HOME assistance.

To ensure that buyers are informed consumers, ADFA requires evidence of attendance within the past 12 months at a HUD-approved pre-purchase homeownership counseling course by all adult household members who will hold title and be party to the senior loan.

E. Responsible Lending: Senior Loan Expectations

To ensure that buyers receive high quality loans that are sustainable over time, ADFA requires that any buyer receiving HOME assistance towards closing costs, down payment, or a portion of the purchase price receive a senior loan (i.e. first mortgage) meeting the following criteria:

- The loan must be:
  - A "Qualified Mortgage" under the requirements of the Consumer Protection Financial Bureau (CFPB) outlined at 12 CFR 1026.43(e); or
  - A mortgage exempt from Qualified Mortgage standards, including:
    - ADFA mortgage revenue bond loan programs,
    - USDA Rural Development, and
    - Habitat or other direct lending nonprofits funded and approved by ADFA.

- Interest rates must be competitive and must NOT be a "Higher Priced" loan defined as (on the date of commitment or loan rate lock):
  - More than 2.00% above the rate to those offered by the state housing finance agency's single-family mortgage program. Please call ADFA at 501-682-5900 and ask for the Single Family Daily Mortgage Rate.

- The loan should be a fixed-rate loan which fully amortizes over a 30-year term. Shorter-term or longer-term loans must be underwritten and approved by ADFA as an exception in writing.

- Loan products used must generally allow loan-to-value (LTV) ratios of at least 95%. While assisted buyers are not required to be approved for loan amounts equal to 95% of the purchase price, buyers who use more restrictive lending products (such as those limiting the LTV to 80%) will not receive HOME assistance toward their purchase if they could otherwise afford the monthly payment on a larger loan consistent with these underwriting guidelines. Buyers are expected to obtain the largest loan they can reasonably afford, and ADFA will not subsidize purchases more deeply just to avoid mortgage insurance on higher LTV lending products.

F. Refinancing/Subordination of HOME-Funded Liens

ADFA has ongoing interests in the success of its HOME-assisted homebuyers, limiting the loss of HOME funds, and avoiding the impact of foreclosures on the jurisdiction's residents and neighborhoods. Refinancing of senior (first) mortgages will be permitted and the HOME loan will be subordinated to the new senior loan <u>only</u> under the following conditions:

- No cash out – New loans for the sole purpose of improving the rate and/or extending the term of the existing loan that result in a low monthly payment for the homeowner and no cash out will be permitted.
    - The proposed new loan must result in a lower monthly payment for the assisted owner and to complete repairs or make improvements to the home
    - The new loan may allow the assisted homeowner to finance their closing costs without being considered cash out. Nominal cash back at closing of less than $500 resulting from last-minute adjustments to payoff figures, closing costs, tax/insurance escrows and the like will not be considered "cash out."

- Any new loan must meet all requirements in the Primary Loan Expectations section above and be approved by ADFA.

- Income eligibility is not required for any refinancing. If the owner's income has risen above 80% AMI, there is no violation of HOME.

This policy will also apply to HOME-funded liens resulting from homeowner rehabilitation programs and to any of the PJ's subrecipients or CHDO's who hold secondary liens securing direct assistance provided to buyers or homeowners.

8. Construction Process

A. ADFA Construction Inspections

ADFA must be provided with copies of all contractor invoices and provided reasonable notice of monthly draw inspections during the construction period. ADFA staff will participate in all draw reviews whether or not the specific draw is being funded with HOME or other project funds and conduct inspections to ensure that the project is progressing and that work completed is consistent with all applicable HOME requirements.

B. Davis Bacon

When Davis Bacon applies to a project, ADFA must be provided with compliance documentation throughout the construction period. Prior to commencing construction, ADFA must approve current wage determinations applicable to the project. The contractor will be required to provide weekly payroll forms to ADFA and allow access to the site and workers for the purpose of completing worker interviews.

C. Drawing ADFA HOME Funds

Proceeds of the HOME loan will only be released as reimbursement for eligible project costs following:

- Review and acceptance of appropriate source documentation by ADFA including evidence of appropriate lien waivers and/or title endorsements.

- A determination by ADFA that all HOME requirements pertaining to the development of the Project have been met, including but not limited to monitoring of Davis Bacon compliance.

For nonprofit developers, including CHDOs, ADFA may release payment based upon outstanding invoices for costs incurred and work completed. In such cases, ADFA reserves the right to disburse through a title company, directly to the vendor, or with two-party checks.

D. Project Closeout

Developers are required to submit demographic data for all homebuyers of HOME funded units. Data shall include elderly status, race, gender, female head of household, number of household members, and percent of area median income.

ADFA requires a copy of the final project sources and uses statement and, at ADFA's option, may require the submission of the project cost certification prepared by an independent Certified Public Accountant following completion of construction and payment of all development costs.