Rental Housing Division
Compliance and Asset Management
Operations Manual

December 2018

1. Overview

1.1 Purpose and Scope

This manual serves as an overview for the VHDA Rental Housing Compliance and Asset Management Department and includes policies and procedures related to Rental Housing Properties in the VHDA loan portfolio, properties with Low Income Housing Tax Credits and Section 8 Properties. The Rental Housing Division in addition to Compliance and Asset Management also includes the Rental Housing Development, Low Income Tax Credit, Strategic Lending, Multifamily Servicing, and Research and Policy Analysis departments.

1.2 Responsibilities and Authority

Responsibilities for the Rental Housing Compliance and Asset Management Department:

- Compliance for VHDA Program Requirements
- Audit of Property Financial Statements and Expense Management
- Active monitoring of the At-Risk/Watch List of properties
- Physical inspections of VHDA financed properties
- Management of the Reserve Funds for each property
- Compliance with LIHTC program requirements
- Training and certification of property managers and owners
- Managing portfolio and program risk for VHDA Rental Housing

1.3 Glossary

AFS – Adjusted for Family Size applied to median income limits

AM – Asset Manager - responsible for monitoring the physical and financial stability of properties in the VHDA portfolio

Assisted Properties –Property with project based Section 8 rental assistance

Commented [EE1]: We no longer have Section 236 properties in our portfolio

BIN – Building Identification Number for Buildings in a LIHTC Property

CO – Compliance Officer responsible for monitoring/auditing developments for compliance with VHDA program requirements and LIHTC requirements

EUA – Extended Use Agreement required by the IRS for all LIHTC properties to ensure the property will be committed for a minimum long term period to low income housing

HDS – Housing Development Software. System used by RH Compliance and Asset Management to track Section 8 and Tax Credit property information (ex: tenants, rent rates)

LIHTC – Low Income Housing Tax Credit is a program created by Congress to incentivize organizations building or rehabilitating multifamily rental properties to include some or all affordable units…

MOR – Management and Occupancy Review protocol from HUD used for compliance monitoring of Section 8 communities

MUMI – Mixed Use and Mixed Income properties

PHA – Public Housing Authority

PIS Date – Date a property is placed in service

ProLink – Software System used by Rental Housing staff for tracking information related to financing new rental housing development loans and LIHTC allocations to properties

RH – Rental Housing Division of VHDA

Section 8 properties – Properties having project based rental assistance from HUD through a Housing Assistance Payment (HAP) contract

Set-asides – The number of affordable units required by a funding source (Tax Exempt Bonds, LIHTC)

Commented [EE2]: We no longer have these properties in our portfolio

TC – Tax Credit

TE Bonds – Tax Exempt Bonds

UA – Utility Allowance Estimate – owner must include UA in gross rent calculations for LIHTC properties if tenants pay utilities out of pocket

WTCMS – The Web Tenant Compliance Management System (WTCMS) allows property managers to enter tenant information directly into a web-based compliance reporting system

Unassisted properties – Any property having no federal funding

1.4 Compliance and Asset Management Functional Overview

1.4.1 Underwriting:

The strength of VHDA's Rental Housing portfolio is dependent on a thorough underwriting process at loan origination. The Compliance and Asset Management Department assists the Development Department during this process. The Asset Manager's involvement may include providing information regarding the market, rents, amenities, operating expenses, comparable properties and/or information regarding the sponsor or management agent. This is accomplished through a team underwriting process.

Asset Managers are encouraged to become involved with new developments during the different underwriting stages and are given the opportunity to become knowledgeable of the various VHDA loan programs and funding sources. As VHDA develops more loan programs and allocates resources through more creative means, it is important for Compliance and Asset Management to remain current in Development's outreach. See organization Chart, exhibit 1.

1.4.2 Physical Monitoring:

Property inspections are an important part of Compliance and Asset Management's responsibility in monitoring the management and operation of developments financed and/or administered by VHDA. Effective monitoring requires formal announced inspections and informal, unannounced site visits.

In January each regional team coordinates the schedule for the calendar year's inspections and compliance audits. The schedule and outcome of inspections and audits is captured in ProLink (VHDA's rental automation system). Compliance Audits are addressed in this manual under section 2.2.4.

Every property funded by VHDA is scheduled for an inspection annually. For unassisted properties, an annual inspection may be waived for no more than 2 years if the property meets the criteria established on the Inspection Waiver in the Risk Assessment process. If the property is under construction, still in the underwriting process or not yet in the final closed status, an inspection waiver should be completed stating the reason why the inspection was not done. Each active property in ProLink will have an inspection report or a waiver generated.

Assisted properties require annual visits by VHDA as required by our role as the contract administrator.

The Regional Portfolio Managers and the Director of Compliance and Asset Management review the inspection schedule generated through ProLink to determine the, scheduling, progress and timeliness of inspections.

1.4.3 Financial Monitoring

Financial monitoring is an integral and important part of an Asset Manager's responsibility in determining the security of a multifamily loan. The financial condition of a development may be assessed by reviewing its financial submissions. Additionally, an evaluation may be made on a development's adherence to regulatory and program requirements by reviewing financial reports.

VHDA financed properties are required to submit monthly and annual financial operating information through the submission of audited financial statements prepared by a third party auditor, annual operating budgets and monthly operating summaries. Reporting requirements are based on regulatory requirements and the amount of outstanding mortgage loan balances. Properties with aggregate loan balances less than $1 million are not required to submit financial operating data unless required by the Asset Manager. The financial data is captured in ProLink.

1.4.4 Risk Analysis

The Risk Analysis tool within ProLink allows the Asset Managers to determine the overall risk rating of a property given a number of factors including a property's financial and physical condition along with the status of its mortgage payments and history of delinquent mortgage payments. The process for identifying properties of concern and the possibility of foreclosure is referred to as the At Risk/Watch Process and information is updated at the end of each quarter. This information is used by our Finance Division to calculate the Authority's loan loss reserve. Documentation of this process is noted in exhibit 2.

1.4.5 Reserve Escrow Accounts

Reserve oversight is an important part of an Asset Manager's responsibility in assuring that funding is available to address all or part of a development's long term and/or specific needs. Most properties maintain a Replacement Reserve Account. These funds are held by VHDA and are released to the owner and/or property manager to meet the needs of the property as requests are approved.

The purpose of the Replacement Reserve Account is to provide a source of funding for capital improvements, extraordinary maintenance, substantial repair or replacement of capital items or for any other purpose authorized by the Asset Manager.

Asset Managers evaluate reserve balances and funding levels in comparison to the needs of a development and in conjunction with the budget review for the property. Monthly deposits to the reserve escrow may be adjusted (i.e., increased, decreased, deferred, waived) as necessity warrants and is determined in discussions with a development's sponsor and/or management agent. A Capital Needs Assessment may be completed by a third-party or prepared by a sponsor or management agent.

Asset Management may establish a unique agreement (Specific Reserve Usage Agreements) between an owner, agent and VHDA on the use of reserve funds over a given period. Such an agreement would be well documented in a standard form letter, signed off on by representatives of the owner/agent and designate the specific usages of funds held in the reserve as well as deposit and withdraw patterns over a period of time. The practice of establishing a reserve usage agreement is a tool used by Asset Management to outline a clear understanding of reserve mechanics. The Director of Compliance and Asset Management will review all such agreements before their proposal to a development's owner/agent.

1.4.6 Loan Assumptions

It is Asset Management's responsibility to determine the validity, feasibility, credit worthiness and structure for various loan assumption requests that are made to VHDA. Having a process for this review provides efficient and professional service to our customers, and enhances VHDA's sound loan review and asset management practices.

There are three (3) basic loan assumption requests that Asset Management will review:

1. Straight assumption, purchaser is known to VHDA
2. Straight assumption, purchaser is unknown to VHDA
3. HUD assumptions (other HUD loans). All HUD loan assumption requests should be referred to Neal Rogers, Director of Compliance and Asset Management.

During the review process, Compliance and Asset Management will consult with Development, Finance and Servicing regarding the eventual terms and conditions of the proposed assumption.

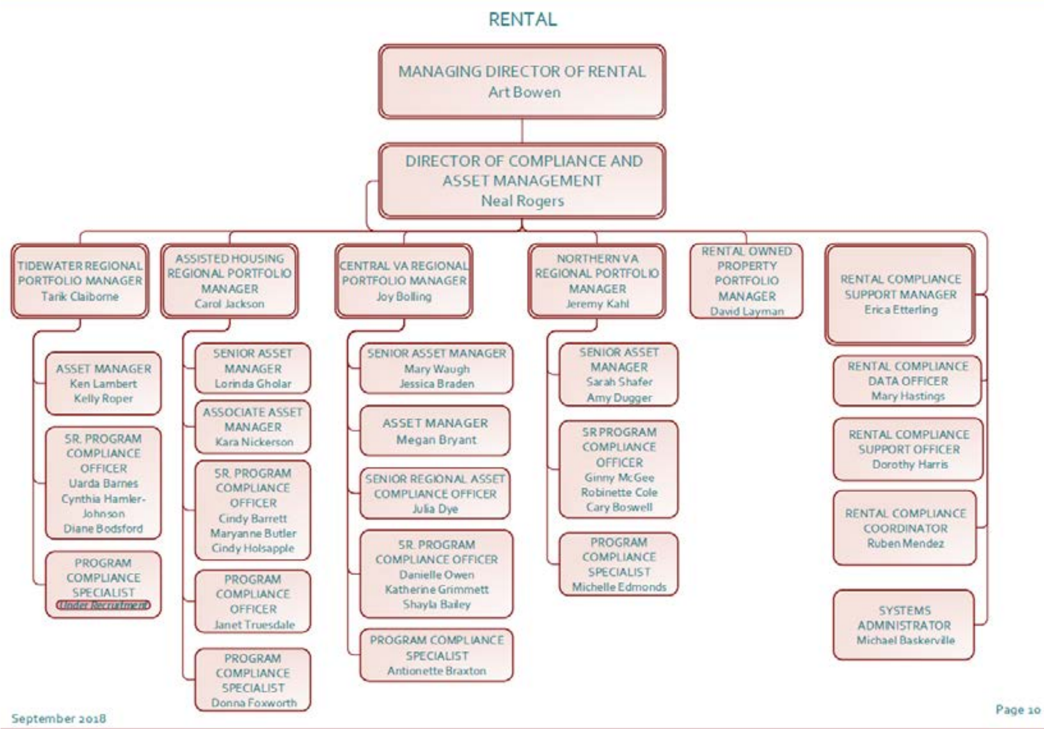
1.4.7 Management Agent Certification Program

VHDA recognizes the importance of professional management pertaining to the success of properties in the VHDA financed portfolio. Originally designed to support efforts in administration of the LIHTC Program, the VHDA Certified Management Agent Program is a fixture for all LIHTC properties receiving allocations since 2007 and all new rental housing business done with VHDA beginning in 2013. Any developer/owner seeking VHDA financing must use a VHDA Certified Agent. This involves an application process and periodic renewals. For smaller and special use properties where retaining a VHDA Certified Agent is not always possible, Compliance and Asset Management will perform a review of the management agent's operations to determine its capability to manage that specific property.

1.4.8 Compliance Monitoring

VHDA is responsible for the program compliance monitoring of various housing programs and financing regulations for properties throughout the portfolio. These include properties participating in the HUD Section 8 program and for which VHDA is the contract administrator, the LIHTC Program, VHDA Program requirements, and IRS tax exempt funding requirements. Compliance audits are performed by Compliance Officers and are scheduled, at a minimum, once every three years. The scheduling of compliance audits and recording of the findings is done within the HDS monitoring system for Section 8 properties and ProLink for all other programs. For the federal assisted Section 8 communities, Compliance Officers follow HUD protocol through the use of the Management and Occupancy Review (MOR). VHDA audit procedures are outlined in Section 2.2.

Exhibit 1


RENTAL
MANAGING DIRECTOR OF RENTAL Art Bowen
DIRECTOR OF COMPLIANCE AND ASSET MANAGEMENT Neal Rogers
TIDEWATER REGIONAL PORTFOLIO MANAGER Tarik Claiborne
ASSISTED HOUSING REGIONAL PORTFOLIO MANAGER Carol Jackson
CENTRAL VA REGIONAL PORTFOLIO MANAGER Joy Bolling
NORTHERN VA REGIONAL PORTFOLIO MANAGER Jeremy Kahl
RENTAL OWNED PROPERTY PORTFOLIO MANAGER David Layman
RENTAL COMPLIANCE SUPPORT MANAGER Erica Etterling
ASSET MANAGER Ken Lambert Kelly Roper
SR. PROGRAM COMPLIANCE OFFICER Uarda Barnes Cynthia Hamler-Johnson Diane Bodsford
PROGRAM COMPLIANCE SPECIALIST Under Recruitment
SENIOR ASSET MANAGER Lorinda Gholar
ASSOCIATE ASSET MANAGER Kara Nickerson
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PROGRAM COMPLIANCE OFFICER Janet Truesdale
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PROGRAM COMPLIANCE SPECIALIST Antionette Braxton
SENIOR ASSET MANAGER Sarah Shafer Amy Dugger
SR PROGRAM COMPLIANCE OFFICER Ginny McGee Robinette Cole Cary Boswell
PROGRAM COMPLIANCE SPECIALIST Michelle Edmonds
RENTAL COMPLIANCE DATA OFFICER Mary Hastings
RENTAL COMPLIANCE SUPPORT OFFICER Dorothy Harris
RENTAL COMPLIANCE COORDINATOR Ruben Mendez
SYSTEMS ADMINISTRATOR Michael Baskerville
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At-Risk/Watch Quarterly Report

Properties of Concern:
The Compliance and Asset Management Department will determine, on a quarterly basis, the risk rating for each property in the VHDA financed portfolio. Utilizing the Risk Assessment activity in Prolink, each Asset Manager determines a property's risk assessment based on a variety of information including the status of the mortgage payment, the physical condition of the property, and the financial performance of each property which includes the most recent operating budget, monthly operating information, and audited financial statements. Prolink takes into consideration these and additional factors (see attached) to establish an overall score for the property, which is then associated with a particular risk rating: At-Risk, Watch, or Acceptable. Risk points that total to less than 7.99 indicate an Acceptable rating. 8.00 to 14.99 reflect a property in Watch status, and properties with a point total in excess of 14.99 indicate an At-Risk status. The Asset Manager may adjust the point criteria based on information that may have recently come to his/her attention that is not reflected in the objective information. This must be accompanied with specific comments and reasoning for the adjustment. All properties with an At-Risk/ Watch rating will appear on the Quarterly At-Risk/Watch Report. Properties on the At-Risk/Watch Reports will require additional monitoring by VHDA. Each of these properties will be inspected at least annually and may include additional visits to the property and additional financial reporting requirements.

If a property is in a workout status, the property will be reflected on the At-Risk report. This is accounted for in the risk rating criteria. Workout is defined as any troubled debt restructuring of the stated loan document including interest deferrals, short term adjustments to principal and interest payment, and adjustments to reserve payments.

Determining the "Potential Loss":
Determining a projected "potential loss" is based on the property's ability to meet its operating expenses and its debt service payments. The variance between the debt that it can support and the outstanding loan balance is the "potential loss" to VHDA. In some cases, we may consider the value of the land to offset a significant potential loss. We recognize that every property has some inherent value, so the possibility of a complete loss is not likely.

For most multifamily income producing properties, the Asset Manager prepares an annualized operating proforma taking into consideration the most recent information available, such as the current budget, most recent financial audit, and current information such as vacancy, delinquency, and concessions. The goal is to arrive at the Net Operating Income (NOI) that will be available to service the existing debt. This process is indicated on the Property Input Sheet. In order to compute the amount of annual debt service that can be supported by the indicated NOI, we take into consideration the current mortgage balances(s), a thirty year term (our typical term for a mortgage loan), the average of the current taxable and tax-exempt interest rates as quoted on the VHDA web site, and the existing interest rates in place for the loans on the property. In an instance where there is more than one loan with different interest rates, we defer to the highest rate which is typically attached to the highest outstanding loan balance. During this analysis, we use the computed NOI for a property and run two computations to determine the amount of debt that can be supported.

The first computation uses the average of the taxable and tax exempt interest rates as listed on the VHDA web site. This rate, a 30 year term, and the NOI will be used to calculate the amount of debt that a property can support assuming a 1.00 DCR. The difference between this amount and the current loan balance(s) is a possible "potential loss".

The second computation uses the same assumptions except for the interest rate. In this scenario, the current interest rate in place of the existing financing is used. As referenced above, in a case where there is more than one loan with different interest rates, we defer to the highest rate which is typically attached to the highest outstanding loan balance. The NOI will be used to calculate the amount of debt that a property can support assuming a 1.00 DCR. The difference between this amount and the current loan balance(s) is another possible "potential loss".

With two possible "potential loss" figures, we will choose the lesser of the two. The computation that results from a scenario using the lower interest rate will allow the NOI to support a higher level of debt. The rationale is that VHDA would likely consider using whichever interest rate puts the property in the best position to succeed. For example, should a purchaser be willing to assume the debt from the owner at the current interest rate, VHDA might consider the possibility of a loan assumption. Alternatively, we could also consider offering the property financing at the current published interest rate.

We recognize that that each property has some value which may exceed the NOI calculated value, particularly in situations where the property will support little or no debt. Also, there are instances where a realistic NOI cannot be calculated as indicated above. For example, there may not be adequate information available to compute an NOI due to the nature of the facility (group home), or the property may be in the early stages of lease-up, generating little income. Therefore, we may consider information such as a recent appraisal, a recent tax assessment (although we may choose to recognize just the value of the land), or a documented recent comparable sale of a comparable property, or a Broker Price Opinion (BPO). These are all third party documented numbers that can be subtracted from the outstanding loan balance, providing a more realistic "potential loss". In an instance in which there exists a third party value and an NOI that can support a certain amount of debt, VHDA will utilize the calculation reflecting the lesser "potential loss". If there is no NOI or third party value available, the loan balance will be the potential loss.

Determining the "Adjusted Potential Loss":
Whether or not there is financial information available to arrive at a NOI, each property on the At-Risk Report may indicate a "potential" loss. We then make one adjustment to this number to arrive at an "adjusted potential" loss.

We subtract any funds that we are holding in reserve accounts. This does not include real estate and insurance escrows, just those in either replacement reserves, miscellaneous reserves or operating reserves. We could apply these directly to the mortgage balance should we choose.

Risk:
For properties with and "At-Risk" status, a potential financial risk to VHDA will be determined using the following criteria:

1) Net Operating Income (NOI) that is not able to meet the operating needs and debt service for the property
2) inability of the owner to advance funds to the property to meet its obligations or an indication from the owner that he/she will not advance funds to the property
3) deteriorating physical condition of the property to the degree that VHDA's security is at risk with no sustainable plan by the owner to address these problems
4) delinquent mortgage payments

A high risk of foreclosure may be indicated if the property's operations are insufficient to cover its expenses and debt service, the owner cannot, or will not, advance funds to meet these needs, the physical condition of the property is deteriorating, and there is a pattern of delinquent mortgage payments.

A medium risk may exist if the property's operations are insufficient to cover its expenses and debt service, the owner's desire and ability to fund deficits is uncertain, the property is not being maintained and managed in a satisfactory manner, and there is no pattern of delinquent mortgage payments.

A low risk of foreclosure may be indicated if the property's operations are insufficient to cover its expenses and debt service, the owner's desire and ability to fund deficits is uncertain, the property is being maintained and managed in an acceptable manner, and mortgage payments are current and there has not been a pattern of delinquent mortgage payments.

In addition to those properties demonstrating some level of risk, there are properties that may be in a Watch status. These properties pose no foreclosure risk, but they do demonstrate some of the issues that result in additional monitoring and oversight. The severity of the issues, though, does not rise to the level that would result in a property posing a risk of foreclosure.

In most circumstances, a poorly performing property will progress from an Acceptable status to a Watch status and then possibly to an At-Risk status. There may be instances, such as a major casualty loss or a delinquent mortgage payment (as noted on Servicing's month end delinquency report), when a property may advance directly from Acceptable to At-Risk status. In these instances, a property will need to gradually work its way off the list should the issue be corrected. A property will not go from an At-Risk status to an Acceptable status from one quarter to the next. There must be at least two quarters of improving performance in Watch status before a property returns to an Acceptable status.

The draft reports will be reviewed by the Director of Compliance and Asset Management and the staff, along with the Director of Rental Programs and the Assistant Director of Multifamily Servicing. Once these reports are finalized, they are forwarded to the VHDA Controller, the Rental Development and Servicing Departments, and other departments throughout VHDA.

Updated 6-10-2014

AM Risk Assessment Criteria

Status Risk Status Point Values

Status	Beginning Point Value	Ending Point Value
Acceptable	(999.00)	7.99
Watch	8.00	14.99
At Risk	15.00	999.00

Monthly Operating Statements

	Point Value
1) If required and last monthly record completed or waived more than 3 months ago.	0.10
2) If required and no monthly records have been completed or waived in the most recent fiscal year activity.	0.20
3) If most recent Rental Income Potential has decreased 25 % from the Rental Income Potential 3 months ago.	0.10
4) If most recent Rental Income Potential has decreased 25 % from average Rental Income Potential of the last 12 completed MOS records.	0.20
5) If most recent Rental Income Potential has decreased 25 % compared to last FYEM.	0.30
6) If most recent Vacancies + Concessions is greater than 10 % of the same month's Rental Income Potential.	0.50
7) If most recent Vacancies + Concessions has increase more than 10 % over Vacancies and Concessions from MOS record 6 months ago (i.e. compare Jan to Jun).	0.30
8) If most recent Vacancies + Concessions is greater than 10 % of the previous 6 months' average of Rental Income Potential (excluding most recent value and waived MOS).	0.40
9) If most recent Accounts Receivable --Tenant increased by more than 10 % over Accounts Receivable -- Tenant from MOS record 6 months ago (i.e. compare Jan to Jun).	0.10
10) If most recent Accounts Receivable - Tenant increased by more than 10 % over the previous 6 months' average Accounts Receivable -- Tenant (excluding most recent value and waived MOS).	0.20
11) If most recent Cash Balance is less than $0 .	0.50
12) If most recent Net Owner Advances CUM TD is greater than Net Owner Advances CUM TD from MOS record 6 months ago (i.e. compare Jan to Jun).	0.20
13) If most recent Receipts from Owner are greater than $0 .	0.10
14) If most recent Management Agent Payables is greater than Management Agent Payables from MOS record 6 months ago (i.e. compare Jan to Jun).	0.20
15) If during any of the past 12 monthly records (including most recent), total move-outs are greater than 60 % of total units.	0.30

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AM Risk Assessment Criteria as of 6/10/14

Annual Financials

	Point Value
1) If required and activity not completed within 9 months of FYEM.	5.00
2) If audit opinion is Qualified or Modified.	8.00
3) If audit opinion is Adverse.	15.00
4) If going concern is an Audit Issue.	8.00
5) If credit risk is an Audit Issue.	1.00
6) If adverse findings is an Audit Issue.	2.00
7) If internal control issues is an Audit Issue.	1.00
8) If regulatory/compliance issues is an Audit Issue.	2.00
9) If commingling of funds is an Audit Issue.	2.00
10) If Liquidity Ratio is less than 100.0 %.	2.00
11) If Vacancies + Concessions is greater than 10 % of Total Rental Income Potential.	2.00
12) If Vacancies + Concessions have increased by 20 % over Vacancies + Concessions from the last FY Annual Financial Activity.	0.50
13) If DCR After Reserve Deposits is equal to or greater than 1.2000.	(2.00)
14) If DCR After Reserve Deposits is between 1.1500 and 1.1999.	(1.00)
15) If DCR After Reserve Deposits is between 1.1000 and 1.1499.	0.00
16) If DCR After Reserve Deposits is between 1.0000 and 1.0999.	1.00
17) If DCR After Reserve Deposits is between 0.8500 and 0.9999.	2.00
18) If DCR After Reserve Deposits is equal to or less than 0.8499.	3.00
19) If Cap Value - OS VHDA Mtg Bal is less than $0.	1.00
20) If LTV is greater than 90 %.	1.00
21) If NOI less DS & Reserve Deposits is less than $0.	2.00

Operating Budget

	Point Value
1) If required and activity not completed within 4 months of FYEM.	0.50
2) If Rental Income has decreased 15 % over last FY Operating Budget Activity.	1.00
3) If Vacancies + Concessions is greater than 10 % of Rental Income.	2.00
4) If Vacancies + Concessions have increased by 20 % over Vacancies + Concessions from last FY Operating Budget Activity.	0.50
5) If DCR After Reserve Deposits is equal to or greater than 1.2000.	(2.00)
6) If DCR After Reserve Deposits is between 1.1500 and 1.1999.	(1.00)
7) If DCR After Reserve Deposits is between 1.1000 and 1.1499.	0.00
8) If DCR After Reserve Deposits is between 1.0000 and 1.0999.	1.00
9) If DCR After Reserve Deposits is between 0.8500 and 0.9999.	3.00
10) If DCR After Reserve Deposits is equal to or less than 0.8499.	4.00
11) If Net Income before Distribution and Cap Expenses minus Cap Expenses funded from Operations is less than $0.	8.00

Physical Inspection

	Point Value
1) If Overall Inspection Results is Needs Improvement.	4.00
2) If Overall Inspection Results is Unsatisfactory.	8.00
3) If inspection has any follow up items that are not closed within 60 days of follow up date.	2.00

Loan/Reserve

	Point Value
1) If Loan Status = Loan In Default (field = 174).	15.00
2) If Loan Status = In Workout (field = 124).	15.00
3) If there is a technical default date.	15.00
4) If current reserve deposit amounts from all loans * 12 is less than all reserve releases in past 12 months.	0.10

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AM Risk Assessment Criteria as of 6/10/14

2. VHDA Compliance and Asset Management Policy and Procedures

2.1 Legal Authority, Regulations, Guidelines and Forms

2.1.1 IRC Section 42 and Regulations Section 1.42-5

2.1.2 Guide for Completing Form 8823, Low-Income Housing Credit Agencies Report of Noncompliance or Building Disposition and the Audit Technology Guide

2.1.3 Occupancy Requirements of Subsidized Multifamily Housing Programs (HUD Handbook 4350.3)

2.1.4 Forms – All VHDA forms for use by CO's and CS's are stored on the Q drive in the Compliance & Asset Management folder

2.2 VHDA Internal Audit Procedures

2.2.1 Notification of Audits

VHDA will give owners written advance notice of file and physical inspections for all Tax Credit, VHDA Bond Financed and Section 8 properties for which VHDA is not the contract administrator. Notice for the HUD-assisted properties must be a formal signed letter. Other properties may receive notice by email. For all Section 8 properties for which VHDA is the contract Administrator, HUD requires that owners be given at least a two week written notice prior to conducting the MOR (per HUD Handbook 4530.1).

2.2.2 Selection of Units

VHDA will make a random selection of files and units to be inspected. Under no circumstance will the owner be made aware of units or files that will be inspected prior to the date of such inspection. If the CO is conducting the file **and** physical inspection, and the physical inspection is conducted first, the list of files to be reviewed should only be given to on-site staff at the time the file review will be performed. The CO also, has the discretion to select a separate set of units for the physical inspection from the file inspection.

A variety of types of files will be included in the audit - move-ins that have occurred since the property was last audited, recertifications, each type of income level, special units required (accessible, developmental disability) and for HUD-assisted units, move-out and rejection files.

2.2.3 Document Control

When performing on-site file and/or physical inspections, under no circumstance should the CO or AM leave written documentation of findings with the property management staff or the owner (this includes all types of documents – even short notes written on 3M note pads). Verbally communicating concerns is permissible. All findings will be disclosed in a final written audit report. The final written audit report will provide a response period of 45 days during which the owner will have an opportunity to respond and submit corrections to any findings. This guidance is applicable to all Tax Credit and VHDA Bond Financed properties and Tax Credit properties with Section 8 and VHDA is not the Contract Administrator.

The only exception to this policy is when there is a Life Threatening Hazard noted during a physical inspection. The AM or CO must be precise in identifying a critical violation including the buildings and units affected. Exhibit 6-4 from the IRS 8823 Guide is the Notice of Critical Violations adopted by VHDA(modified slightly for VHDA's use). The CO or AM issuing this notice must request a signed/dated copy from management prior to leaving the property.

Properties under the Section 8 program for which VDHA is the Contract Administrator must adhere to HUD requirements for owners to respond to audits within 30 days after receipt from VHDA.

The questionnaire portion of the Report of Occupancy Audit Findings that is typically answered by management should not be mailed to management for completion prior to the date of the audit. The questionnaire must be given to management to complete at the beginning of the audit process on the day of the review. The assigned CO should review and go over responses given as part of the exit interview.

2.2.4 Audit Requirements by Program Type and Monitored by Compliance and Asset Management Staff

2.2.4.1 VHDA Loan Products

<u>Taxable Bond Products</u> (includes REACH, SPARC, Housing Fund, General Fund, MUMI and Flex Fund)

The taxable bond program has no federal income or monitoring requirements. However, VHDA has made a determination that units must be rented to households that at move-in have verified adjusted income of no more than 150% of the higher of the median or the 4-person 50% limit x 2, not AFS (effective as of 5/1/1998). Units are referred to as moderate income households. There are no rent restrictions on the units.

There is no restriction on renting to full-time student households.

A. The VHDA regulatory documents for this type of financing stated that the owner is subject to review in a manner specified by the agency.

B. Tenant data must be submitted to VHDA using the WTCMS (HDS) software system.

C. A file audit will be conducted on site within 1 year after loan closing.

D. File Audit - CO will audit unit files for 10% of the required low-income units (or in some cases moderate income for MUMI properties) not to exceed 10 files plus the greater of 5% or 5 units of the 150% moderate households, if any. If property is 100% at 150%, audit 10% not to exceed 10 files. No file audits are completed for market units (those having no programmatic income requirements).

E. After the initial file audit, if VHDA is satisfied the owner and management are adhering to the income, occupancy and reporting requirements of the program, onsite file audits may be eliminated. VHDA will rely on data submitted via WTCMS to determine compliance with income and occupancy requirements. VHDA reserves the right to reinstate on-site file audits based on reviews of data submitted to WTCMS.

F. Instead of an on-site file audit, annually the assigned staff person must complete a WTCMS-HDS Report of Bond Review, including running an Occupancy & Demographics Report in HDS (unless an audit is completed in that year; requirement updated in 2016 from every 3 years to annually) to determine compliance with the income and occupancy requirements.

G. Physical Inspection - depending on schedule and coordination among staff members, at least every three years AM or CO will complete a physical inspection of the property to include common areas and vacant units not to exceed 5 units. Physical inspection may include vacant market units (those having no programmatic income requirements) since the property is funded by VHDA.

H. The review of occupancy reports is documented by completing the WTCMS-HDS Report of Bond Review form and uploading that form and the Occupancy Report to ProLink.

I. CO will send to the owner and on-site staff a notice of noncompliance with income and occupancy requirements if any noncompliance is found during either an on-site or Report of Bond Review.

J. Use current HUD Section 8 income limits for determining income eligibility for taxable bond products. The income limits are not held harmless from increases and decreases.

K. Whenever there is a change in ownership or management agent, VHDA reserves the right to conduct a file review within 90 days after the change to assess the new entity's understanding and implementation of program requirements.

L. Changes in ownership entities, management and site contacts are updated promptly in HDS and ProLink. Upon notification of a change, the Rental Compliance Data Officer updates the owner and management contact information into ProLink, and the CO is responsible for updating the owner, management and property contact information in HDS.

Taxable Bonds for Transitional/Bed/Special Needs Facilities

Properties serving the special needs population or those transient in nature are not subject to file audits due to the privacy of the clients being served and/or length of time households may participate in a program (high turnover). These properties are not required to enter tenant data into WTCMS.

Properties may be subject to any of the following income restrictions and reflected in the VHDA Regulatory Agreement. Examples (not inclusive of all):

- 50% of the units must be rented to persons at or below 50% of the area median income (AMI) not adjusted by family size (AFS) (50% at 50% not AFS; 50% no limit)
- 50% at 50% not AFS; 50% at 150% not AFS
- 100% at 50% not AFS
- 100% at 150% not AFS

Upon request of the assigned CO, Owners are required to complete and submit annually an Income Occupancy and Certification Report (ES-01) certifying that no person has moved in with income exceeding the overall income limit specified in the commitment or regulatory agreement.

A. The ES-01 must reflect occupancy as of Dec. 31st of each year and must be submitted to VHDA by Jan. 31st of the audit year.

B. The ES-01 Form will be uploaded to ProLink following procedures established.

Taxable Bonds for Mixed Use with Mixed Income (MUMI) Properties

Compliance staff follow the audit and documentation guidelines noted for Taxable Bonds. MUMI properties typically have several income restrictions as shown below or other combinations at the discretion of the Development Department's underwriting which will be reflected in the Loan Commitment and Regulatory document:

A. Mixed Income with SPARC

   a. 20% of units at 150% of median income; 80% of units no income limit
   b. 20% of units at 80% of median income; 20% of units at 120% of median income; 60% of units with no income limit

B. MUMI with SPARC

   a. 20% of units at 80% of median income; 20% of units at 120% of median income; 60% of units with no income limit
   b. 20% of units at 150% of median income; 80% of units with no income limit

C. MUMI and REACH

   a. 30% of units at 80% of median income; 20% of units at 120% of median income; 50% of unit with no income limit

D. MUMI with Tax Exempt Bond and SPARC

   a. 40% of units at 60% of median income; 10% of units at 120% of median income; 50% of units with no income limit

E. MUMI with Tax Exempt Bond

   a. 40% of units at 60% of median income; 10% of units at 120% of median income; 50% of units with no income limit

Specific procedures for taxable audits may be found in the most current VHDA Audit Procedures document.

Tax Exempt Bond Properties

Properties with tax exempt bond financing carry income and occupancy restrictions mandated federally. The income restrictions are referred to as set-asides. Tax exempt loans in the VHDA portfolio have one of the following set-asides for the low-income households:

A. 20% of units at 80% of median income; 80% of units at 150% of median income. Bonds issued **between 1983 and 1985** are **<u>NOT subject to</u>** Adjusted for Family Size (AFS).

B. 20% of units at 80% median income limit AFS; 80% of units at 150% of median income. With very limited exceptions (relating to certain refunding of previously issued bonds) bonds issued **during and after 1986** **<u>ARE subject to</u>** AFS.

C. 20% of units at 50% median income limit AFS; 80% of units at 150% of median income.

D. 40% of units at 60% median income AFS; 60% of units at 150% median income.

Units at 150% of the median are required by VHDA regulations not any federal rule and are referred to as moderate income households.

Federal regulations require that the minimum set aside be maintained at all times throughout the term of the loan. The minimum set aside must be met for:

- A new construction property at the time 10% of the units are occupied;
- An acquisition/rehab property prior to the bond closing. If documentation cannot be obtained by bond closing, VHDA is required to certify within 60 days after loan closing that the minimum set aside has been met.

The minimum set aside must be maintained continuously throughout the loan term.

To initially document the minimum set aside, VHDA will accept:

- Tenant Income Certification (TIC) for Section 8 assisted households within 1 year prior to bond closing
- TIC at move-in or initial qualification (that is, supported by third-party verification of income) or, for prior Tax Credit, Tax-Exempt bond or Assisted properties, a TIC from a full annual recertification (i.e., supported by third-party verification of income), any of which must be signed within 120 days prior to bond closing
- TIC at move-in or initial qualification signed within 60 days post-loan closing

VHDA strongly recommends that management rent to a certain number of additional qualified households (cushion) to equal 15% of the required number of units to meet the minimum set aside.

Full-time student households may only reside in a unit included in the low income minimum set-aside upon meeting one of the five exceptions as explained in IRS regulations. Full-time student households may reside in a 150% moderate unit without restriction.

A. Tenant data must be submitted to VHDA using the WTCMS (HDS) software system.

B. A file audit will be conducted on site within 1 year after loan closing.

C. File audit - CO will audit unit files for 20% of the minimum set-aside units plus the greater of 5% or 5 units of the 150% moderate households, if any. No file audits are completed for market units (those having no programmatic income requirements).

D. Properties funded with only VHDA-issued tax-exempt bonds are audited annually. All other properties funded with VHDA-issued tax-exempt bonds (including those combined with tax credits or other funding) are audited on site at least every three years.

E. Instead of an annual on-site file audit, the assigned staff person must complete a WTCMS-HDS Report of Bond Review, including running an Occupancy & Demographics Report in HDS (unless an audit is completed in that year; requirement updated in 2016 from every 3 years to annually) to determine compliance with the income and occupancy requirements. Exception - for properties funded with only VHDA-issued tax-exempt bonds a WTCMS Annual Report of Bond Review and an on-site file audit will take place.

F. Physical Inspection - depending on schedule and coordination among staff members, at least every three years AM or CO will complete a physical inspection of the property to include common areas and vacant units not to exceed 5 units. Physical inspection may include vacant market units (those having no programmatic income requirements) since the property is funded by VHDA.

G. The review of occupancy reports is documented by completing the WTCMS-HDS Report of Bond Review form and uploading that form and the Occupancy Report to ProLink.

H. After completing the file/unit inspection, review year, type and category, date scheduled, date of review, date completed and number of files reviewed must be uploaded into the compliance audit section of ProLink. The completed audit after response from owner and the corrections are finalized is filed in ProLink compliance documents.

I. CO will send to the owner and on-site staff a notice of noncompliance with income and occupancy requirements if any noncompliance is found during an audit.

J. Use income limits published by HUD. The same Multifamily Tax Subsidy Program (MTSP) limits are used for the tax credit program and the tax-exempt bond program. The income limits are held harmless from increases and decreases.

K. Whenever there is a change in ownership or management agent, VHDA reserves the right to conduct a file review within 90 days after the change to assess the new entity's understanding and implementation of program requirements.

L. The assigned CO is responsible for ensuring that changes in ownership entities, management and site contacts are updated promptly in HDS and ProLink.

Form 8703 - Beginning in 2016, VHDA requests that owners of tax-exempt bond properties within the Qualified Project Period submit to VHDA a copy of IRS Form 8703 reflecting that the property is meeting the bond minimum set aside. This form is due annually to VHDA by April 30.

Tax Exempt Bond and Taxable Bond (combined properties)

It is not uncommon for a property to have both taxable and tax exempt bond financing. VHDA will audit for the most restrictive requirements (always tax exempt Bond). The same guidance outlined for TE loans should be followed for TE combined with TX funding.

Tax Exempt Bond Financing for MUMI Properties

The income and occupancy requirement to date for these properties is 40% of units at 60% median income AFS; 60% of units at no income limit. The same guidance outlined for TE loans should be followed for TE with MUMI.

Tax Exempt Bond Financing – 501(c)(3) Rules

Properties funded with tax exempt bonds issued under the 501(c)(3) rules require that the owner continuously meet the 501(c)(3) not-for-profit regulations and that the property be managed by a 501(c)(3) corporation or pursuant to a qualified management contract.

If the property is existing residential rental property and the rehab is not deemed substantial, federal income limits apply:

- Either 20% @ 50% or 40% @ 60% minimum set aside and

- 75% of the units rented to households at 80% of median income AFS (remaining 25% may be market)

Similar to the Form 8703 filing for other tax exempt bonds, beginning in 2017 (following a 3/13/17 meeting with VHDA's outside bond counsel), those tax exempt bond properties issued subject to 501(c)(3) regulations that are within the qualified project period must submit annually to VHDA a 501(c)(3) Annual Questionnaire relating to their ownership entity, operations and continued 501(c)(3) status.

Specific procedures for tax-exempt audits may be found in the most current VHDA Audit Procedures document.

Tax Credit Properties

Properties with the low income tax credit allocation carry income and occupancy restrictions mandated federally. The income restrictions are referred to as set-asides. The properties have one of the following set-asides for the low-income households:

Either (i) 20% of units at 50% median income limit AFS, (ii) 40% of units at 60% median income AFS, or as of March 2018, (iii) 40% of units at 60% must maintain an average unit designation of 60% AMI or less. Federal regulations require that the minimum set aside be maintained at all times throughout the Extended Use Period.

File audit and physical inspection - pursuant to IRC 1.42-5 and Revenue Procedure 2016-15 the housing credit monitoring agency (VHDA) must conduct the initial on-site inspection and file audit for a TC property by the end of the second calendar year following the year the last building in the project is placed in service and at least once every three years thereafter.

VHDA begins the audit cycle for a TC property after the owner indicates the credit period has begun for each Building Identification Number (BIN). The owner will indicate on IRS form 8609 Part II, line 10a any election to start the credit period the year the buildings are placed in service or the following year.

Credits are claimed on an accelerated basis during the first 10 years after a building is PIS (the "credit period"). An owner claims all the credits to be earned during the 15-year compliance period in the first 10 years. If noncompliance is reported to the IRS an owner may be required to pay recapture calculated on the amount of credits lost as well as a penalty on claimed but unearned credits.

Properties are subject to income limits published by HUD named Multifamily Tax Subsidy Program (MTSP) limits. The tax-exempt bond program also uses the MTSP limits. These income limits (and therefore the calculated rent maximums) are held harmless from increases and decreases.

IRS 42(h)(6) requires owners to enter into an Extended Use Regulatory Agreement and Declaration of Restrictive Covenants (EUA) providing for low-income housing for a period not less than 30 years, beginning at the same time as the 10-year credit period. A building is not considered a qualified low-income building and no credit is allowable if an EUA meeting all of the requirements is not in place.
The EUA is an agreement between the state allocating agency and the property owner and is recorded in the Clerk's Office of the Circuit Court where the property is geographically located.

Although the IRS requires that all TC property allocations beginning in 1990 have an EUA executed between the state and the owner, provisions within that agreement are not enforceable by or reportable to the IRS unless violations of those provisions also violate Section 42 regulations.

During the TC application process, the owners select categories with points in an effort to acquire a high score to be awarded credits. Those categories include things such as targeting a percentage of units for rental to lower income residents, lower rents for a percentage of units, and setting aside units for the disabled, elderly housing, etc. Provisions of the TC allocation are documented in the EUA and indicates the owner must provide all of the representations referenced in the TC Application. The owner must comply with such provisions during the 15-year compliance period and continuing through the duration of the EU period which can be up to 50 years.

Annually, according to Section 1.42, the owner is required to complete and submit to VHDA an Owner's Certificate of Continuing Program Compliance certifying the property has continually met Section 42 requirements or, if not, providing an explanation. A compliance monitoring fee, adjusted at VHDA's discretion, is calculated on a per unit basis and is due with the reporting package.

B. Second Allocation of Tax Credits (re-syndication):

Following the end of the original 15-year compliance period, a property owner will continue operating the property into the extended use period and also may request a second allocation of TCs. If a second allocation is received, for continuity, the IRS requires the housing credit agency to continue using the original BIN numbers. New Forms 8609 will be issued with the same BINs however the allocation date, credit amounts and the Placed In Service (PIS) dates will be reflect information pertaining to the second allocation.

The original and second credit allocations may have different income limits and rent maximums. The second allocation starts a new PIS date for the property and the limits for this allocation are often lower than the limits for the first allocation. MTSP income limits published and current at the new PIS date for the second allocation must be used (and again, may be lower than original income maximums and require households moving in to qualify at those lower income levels).

a. Properties that received an original TC allocation before 1990 did not have EUAs. Properties receiving a second allocation of credits that do not have an EUA in place must verify and certify eligibility of each existing household as if they are new move-ins. Properties with BIN numbers that start with VA87, VA88 or VA89 reflect allocations in 1987, 1988 and 1988 and did not have EUA's.

b. Properties that received a TC allocation from 1990 forward were required to have an EUA in place and those properties receiving a second TC allocation should treat existing households as qualified households under the second allocation unless the household is comprised of full time students that do not satisfy one of the exceptions. If the household has full time students that meet one of the IRS exceptions, there also must be at least one original member of the household who originally qualified.

C. General Audit Practices for TC Properties:

When performing TC file and unit inspections, the CO monitors for compliance with:

a. Eligibility – adequate percentage of households meet the correct income maximum

b. Affordability – household paid rent is below the maximum and incorporates an appropriate utility allowance estimate if the household pays utilities out of pocket.

c. Habitability – the units and common areas have no violations of Uniform Physical Conditions Standards.

Full-time student households may only reside in a tax-credit qualified unit upon meeting one of the five exceptions as explained in IRS regulations.

Tenant data must be submitted to VHDA using the WTCMS (HDS) software system.

D. Specific procedures for a TC audit may be found in the most current VHDA Audit Procedures document.

E. The TC Extended Use Period

The compliance period ends on December 31 of the year the last building in an allocation reaches its 15th year following PIS and beginning the credit period. At the end of the compliance period, the IRS is no longer involved and does not require noncompliance to be reported. At that time, the housing credit agency becomes responsible for enforcing the terms of the allocation through the EUA. The additional period of compliance following the end of the 15-year compliance period is called the extended use period which can last up to 50 years.

Certain IRS requirements may be eased during the extended use period, for example, restrictions on renting to full-time student households, ability to transfer from one building to another, lessened file audit and physical inspection schedule.

Owner no longer must complete the Owner's Certificate of Continuing Program Compliance however a property information report and compliance monitoring fee are due to VHDA annually.

Tenant data must continue to be submitted to VHDA using the WTCMS (HDS) software system.

File audit in EU period – CO completes a WTCMS desk audit every 3 years

Physical inspection -

- if TC only or if combined with a VHDA loan, complete physical according to AM risk criteria which would include an on-site physical inspection of up to 5 vacant units by AM or CO at least every 3 years
- if TC only and property is subject to RD/HUD inspection, then VHDA physical discontinued. When the physical is discontinued CO:
    - makes Active Note in ProLink
    - creates a Note to File in HDS
    - uploads form to ProLink reflecting the physical discontinuation policy and year discontinued