

# Oklahoma Housing Finance Agency Multifamily Bonds 101 for Developers

## Tax Exempt Bond Financing For Affordable Housing Projects

October 11, 2016



# RAYMOND JAMES

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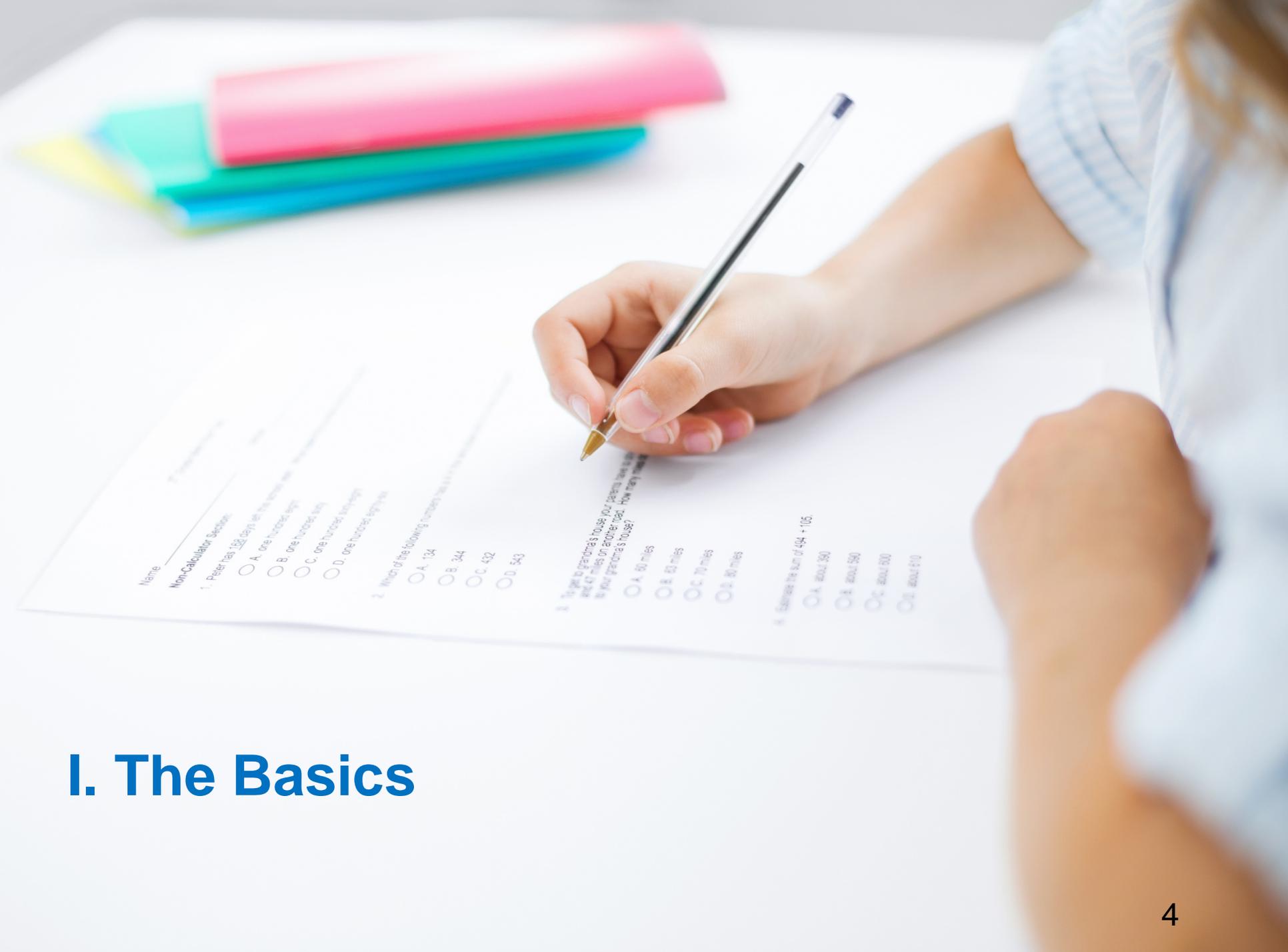
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# Table of Contents

- I. The Basics
- II. Parties to a Multifamily Bond Transaction
- III. Overview of Current Market Structure
- IV. Other Structures
- V. Sample Timeline for Multifamily Bond Issue
- VI. Sample Multifamily Bond Costs
- VII. Application Form and Application Process





Name \_\_\_\_\_

Non-Calculator Section:

1. Peter has 156 days left to finish his homework.
- A. one hundred days
  - B. one hundred days
  - C. one hundred days
  - D. one hundred days

2. Which of the following numbers has a 4 in the hundreds place?
- A. 134
  - B. 344
  - C. 432
  - D. 543

3. To get to grandma's house, you parents have to drive 47 miles on another road. How many miles is your grandma's house?
- A. 80 miles
  - B. 63 miles
  - C. 74 miles
  - D. 87 miles

4. Estimate the sum of  $494 + 105$ .
- A. about 50
  - B. about 590
  - C. about 600
  - D. about 610

# I. The Basics

# Bond: What Is It?

**Bond:** A debt investment in which an investor loans money to an entity (corporate or governmental) that borrows the funds for a defined period of time at a fixed or variable interest rate. Bonds are used by companies, municipalities, states and U.S. and foreign governments to finance a variety of projects and activities.

# Bond: Government and Conduit Bonds

**Government Bonds:** A bond that is issued by a government to provide funding for governmental projects. For example, water and sewer bonds.

**Conduit Bonds:** A bond issued by a government issuer in order to loan the bond proceeds to a third party authorized by law to use the municipal bond proceeds for an eligible use (e.g. affordable multifamily housing). There are two kinds of conduit bonds – Private Activity Bonds (For-Profits) and Qualified 501(c)(3) Bonds (Non-Profits).

# Tax-Exempt Multifamily Housing Bonds – The Advantages

Lowers Interest Rates on Borrowing (subject to market conditions)

- Reduce the “all-in” borrowing rate
  - An investor has a 33% marginal tax rate will make the same amount of interest with a 7% taxable bond as with a 4.69% tax-exempt bond.
  - $(7\% \text{ multiplied by } (1 \text{ minus the marginal tax rate) or } .67) = 4.69\%$
- Lower Rate = More Loan Proceeds or More Project Cash Flow
  - 1% (100 basis points) reduction in interest rate will result in about 8% more loan proceeds with 30 – year level amortization loan.
  - 1% (100 basis points) reduction in interest rate on debt will result in about \$100,000 of additional yearly cash flow on a \$10 million project.

# Tax-Exempt Multifamily Housing Bonds – The Advantages

## Additional Equity Proceeds from 4% Low Income Housing Tax Credits

- Tax-Exempt Housing Bonds are generally eligible to receive “4%” low income housing tax credits.
- State Tax Credit Ceiling – If 50% or more of the aggregate basis of any building and the land on which the building is located is financed with proceeds from the sale of tax-exempt “private-activity” bonds, the regular state tax credit ceiling will not apply and ALL of the qualified project costs will be entitled to the 4% credit.

## LIHTC Equity

- Generally, a 4% LIHTC allocation will raise about 50% of the equity that a 9% LIHTC allocation would raise.

# Requirements Applicable to Tax-Exempt Multifamily Housing Bonds

## General Bond Financing Rules

- 95% of the bond proceeds must be used for qualified costs (land or depreciable property)
- Not more than 25% of the bond proceeds may be allocated to the cost of land
- 15% rehab requirement on acquisition financings
- 2% Costs of Issuance Limitation (e.g., legal fees, title insurance and underwriter's fees)
- The average maturity of the tax-exempt bonds cannot exceed 120% of the average reasonably expected economic life of the facilities being financed

# Requirements Applicable to Tax-Exempt Multifamily Housing Bonds

## General Bond Financing Rules – cont.

- Reimbursements – Bond proceeds may be used to “reimburse” the Owner for expenses that were paid by the Owner prior to the bonds being issued. The Issuer must adopt an inducement resolution and only those qualified expenditures paid up to 60 days prior to the date of the resolution may be reimbursed.
- Arbitrage – You can’t borrow too much, too soon, for too long, or for a bad purpose.

# Requirements Applicable to Tax-Exempt Multifamily Housing Bonds

## General Bond Occupancy Rules

- Must provide residential rental housing
  - No transient housing, hotels, motels, dormitories, frat houses, etc.
  - Separate and complete facilities for living, sleeping, eating, cooking, and sanitation
- Low income occupancy requirements (i.e., 20%/50% or 40%/60%)

# Requirements Applicable to Tax-Exempt Multifamily Housing Bonds

## Required Approvals

- Private Activity Volume Allocation
- Approval of the Issuer's governing body – OHFA's Board of Trustees
  - Inducement Resolution
  - Approving Resolution
- Public Notice & Hearing
- Other local requirements

## **II. Parties to a Multifamily Bond Transaction**



# Typical Participants of a Bond Deal

- Owner
- Issuer
- Underwriter
- Trustee
- Credit Enhancer
- Rating Agency
- Tax Credit Syndicator
- Bond Counsel
- Underwriter's Counsel

# Typical Participants of a Bond Deal (cont.)

## Owner

- Develops, builds, owns and often manages the project
- In some cases, may be a Section 501(c)(3) corporation

## Issuer

- The entity authorized under state law to issue multifamily tax-exempt bonds

# Typical Participants of a Bond Deal (cont.)

## Underwriter

- A municipal securities dealer who assists the owner in choosing optimal financing structure (including credit enhancement, if any), coordinates financing participants, obtains rating, if any. and sells the bonds

## Trustee

- Administers the trust indenture and makes payments to bondholders
- Also serves as dissemination agent under the Continuing Disclosure Agreement on most fixed rate financings

# Typical Participants of a Bond Deal (cont.)

## **Credit Enhancer:**

- A government sponsored enterprise, federal agency, bank, or insurance company that enters into a formal and legally binding pledge of financial support to strengthen the credit of a lower-rated bond issue. The Credit Enhancer assures repayment of the bonds – this normally is what gives most bond issues their “AA” or “AAA” rating.

# Typical Participants of a Bond Deal (cont.)

## Rating Agency:

- Most credit enhanced bonds are rated “AAA” or “AA” (Standard & Poor’s) or “Aaa” or “Aa” (Moody’s) – the top two categories which produce lowest interest rates for an issue of a given maturity

## Tax Credit Syndicator

- Sell credits to investors to generate equity for the project

# Typical Participants of a Bond Deal (cont.)

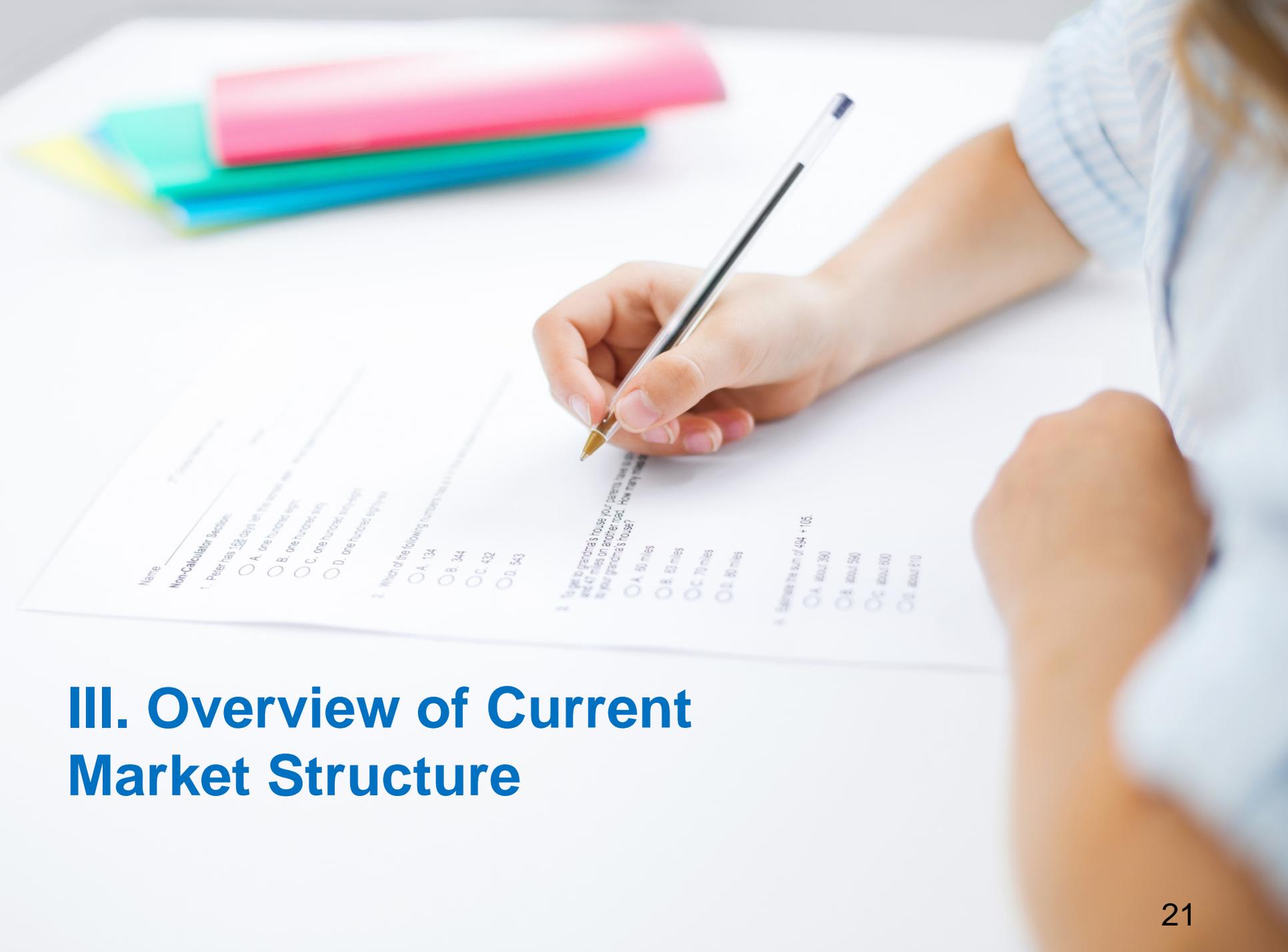
## **Bond Counsel**

- Provides a legal opinion to the bondholders as to the validity of bonds under state law and the tax-exempt status of bonds under federal and state law.
- Drafts the main financing documents such as Indenture, Financing Agreement, Regulatory Agreement, and closing papers.

# Typical Participants of a Bond Deal (cont.)

## Underwriter's Counsel

- A lawyer or firm acting on behalf of the Underwriter in conducting a due diligence analysis of the Issuer (or conduit borrower) while also drafting the Official Statement, Bond Purchase Agreement, Continuing Disclosure Agreement and, if applicable, the Remarketing Agreement.



Name \_\_\_\_\_

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## III. Overview of Current Market Structure

# Typical Bond Documents

## Trust Indenture (between Issuer and Trustee)

- The Trust Indenture establishes the “trust estate” which serves as the security for a bond transaction. The “trust estate” may consist of payments made by the borrower under the loan agreement, revenues pledged to the payment of the bonds or any other collateral pledged to the payment of the bonds.
- The Trust Indenture also provides the terms of the bonds, including payment dates, maturities, interest rates, redemption provisions, registration, transfer and exchange, and other basic financial terms.

# Typical Bond Documents (cont.)

## **Tax Regulatory Agreement (between Issuer, Trustee and Owner)**

- Prepared by Bond Counsel
- Details certain provisions of the Internal Revenue Code and regulations applicable to tax-exempt multifamily housing revenue bonds
- May include certain certificates required by the Internal Revenue Code

# Typical Bond Documents (cont.)

## **Official Statement (between Underwriter and potential buyers of the bonds)**

- Normally prepared by Underwriter's Counsel and signed by the Issuer and/or the Owner
- Provides disclosure to investors and potential investors regarding the terms of the bonds, security, risk factors and financial and operating information concerning the Owner (similar to a stock prospectus)
- The Official Statement is used by the Underwriter to sell the bonds

# Typical Bond Documents (cont.)

## **Bond Purchase Agreement (between Issuer, Underwriter and Owner)**

- Prepared by Underwriter's Counsel
- Provides that, upon the satisfaction of certain requirements, the Issuer will agree to issue the bonds following the pricing of the bonds and the execution of the Bond Purchase Agreement

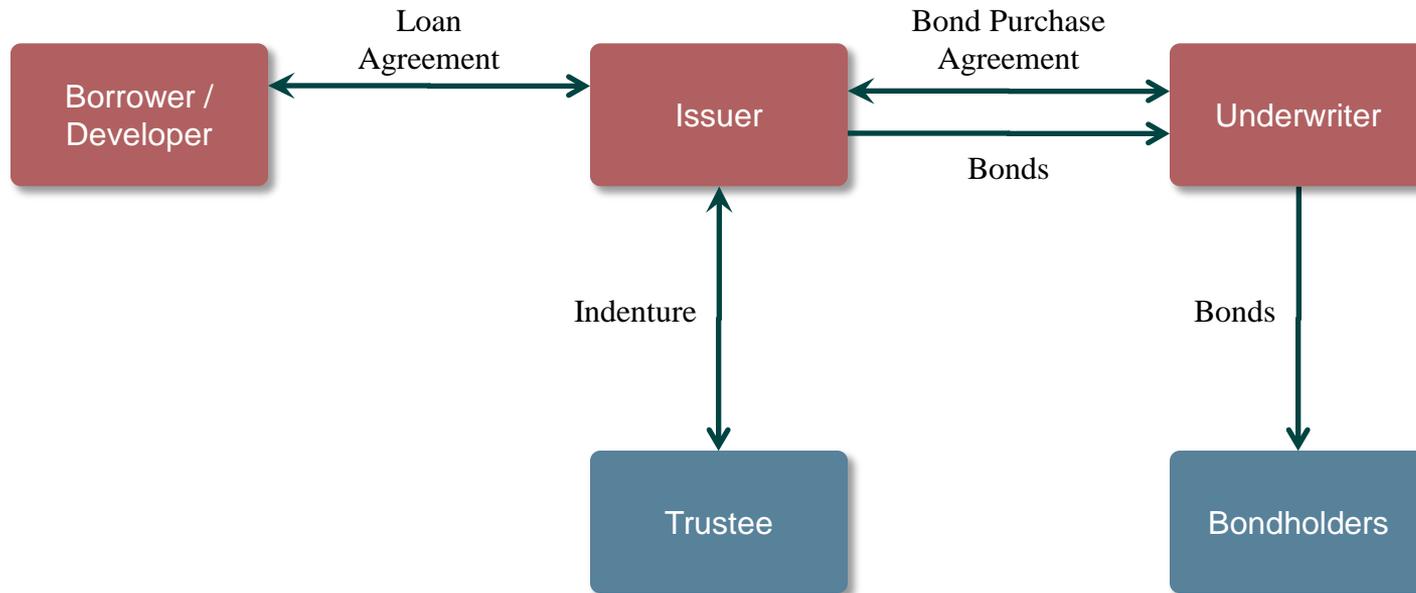
## **Continuing Disclosure Agreement (between Owner and Dissemination Agent)**

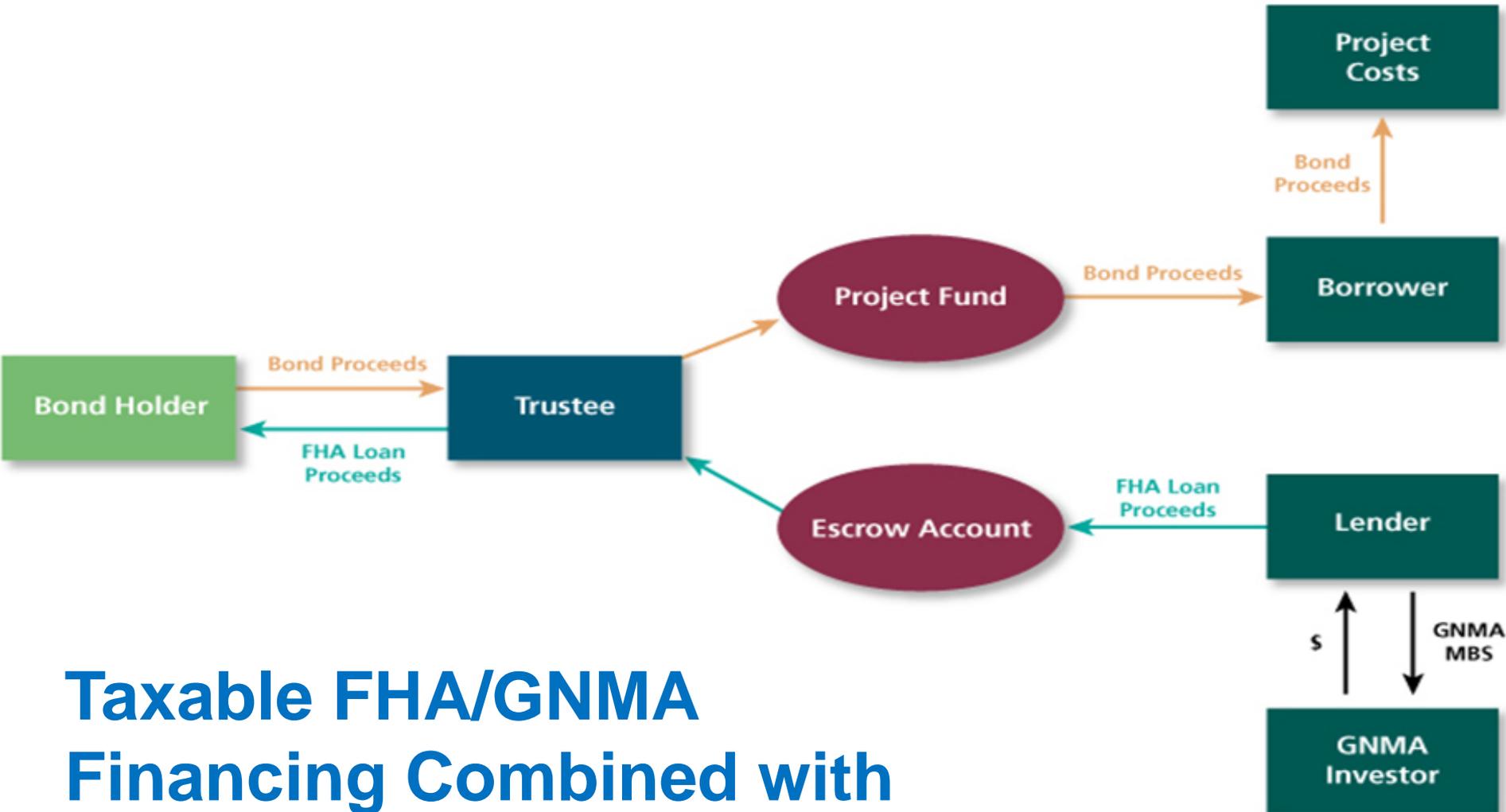
# Typical Bond Documents (cont.)

## Other Common Documents

- Mortgage or Deed to Secure Debt
- Credit Enhancement Facility
- Reimbursement Agreement
- Intercreditor Agreement
- Continuing Disclosure Agreement
- Remarketing Agreement
- Various closing certificates

# The Documents





# Taxable FHA/GNMA Financing Combined with Tax Exempt “50% Test” Bonds

# Sample S&U

## Sources of Funds

HUD 221(d)(4) Loan	\$23,418,000
Project Income	2,182,596
Tax Credit Investor Equity Contribution	13,715,573
Negative Arbitrage Advance <sup>1</sup>	48,319
Insurance Proceeds	930,668
Non-profit Equity Contribution	1,250,000
Deferred Developer Fee	1,308,544
<b>Total</b>	<b>\$42,853,700</b>

## Uses of Funds

Acquisition of the Project	\$15,750,000
Hard Rehabilitation Costs	15,461,545
Other Development Costs	6,676,703
Deposit to Negative Arbitrage Account <sup>2</sup>	48,319
Developer Fee	3,925,000
Reserves	992,133
<b>Total</b>	<b>\$42,853,700</b>



## IV. Other Structures

# Credit Issues

- Generally, without appropriate security investors will not buy bonds
- Underwriters do not have a legal obligation with respect to the creditworthiness of the bonds – they can buy and sell bonds regardless of the credit
- Most conduit multifamily housing bonds are “publicly offered” and rated by the national rating agencies, or sold on a “private placement” basis with sophisticated investors (principally mutual funds or insurance companies) which do their own analysis.

# Credit Issues: Private Placements

**Private Placement:** A private placement is essentially a real-estate loan by the bondholder. The Owner borrows money from a bank or other lender, just as if no bonds were issued, but the debt takes the form of a bond transaction in which the lender holds the bonds.

## Private Placement Lenders

- Commercial Banks
- Non-bank Financial Institutions

# Credit Issues: Private Placements

## Benefits

- Private placement transactions can be put together and closed more quickly than public sales
- Some deals are too small to justify the cost of a public offering
- Private Placement Lenders may be willing to invest in deals that the public market would not

# Credit Issues: Publicly Offered Transactions

## Publicly Offered Bonds - Forms of Credit Enhancement

- FHA/RD Mortgage Insurance & GNMA wrap
- Direct-pay letter of credit
- Standby letter of credit
- Developer Guarantees
- Bond Insurance
- Fannie Mae/Freddie Mac credit agreement

# Publicly Offered Transaction: FHA/GNMA

- **FHA – Federal Housing Administration (HUD), through approved lenders, provides insured mortgages to finance new construction or acquisition and rehabilitation. These programs insure the lenders against mortgage default.**
- **GNMA – Government National Mortgage Association is a wholly owned corporate instrumentality of the United States.**
  - GNMA is authorized by law to guarantee the timely payment of the principal and interest on securities which are backed by pools of FHA mortgages.
  - GNMA's guarantee is backed by the full faith and credit of the United States.

# Publicly Offered Transaction: USDA/GNMA

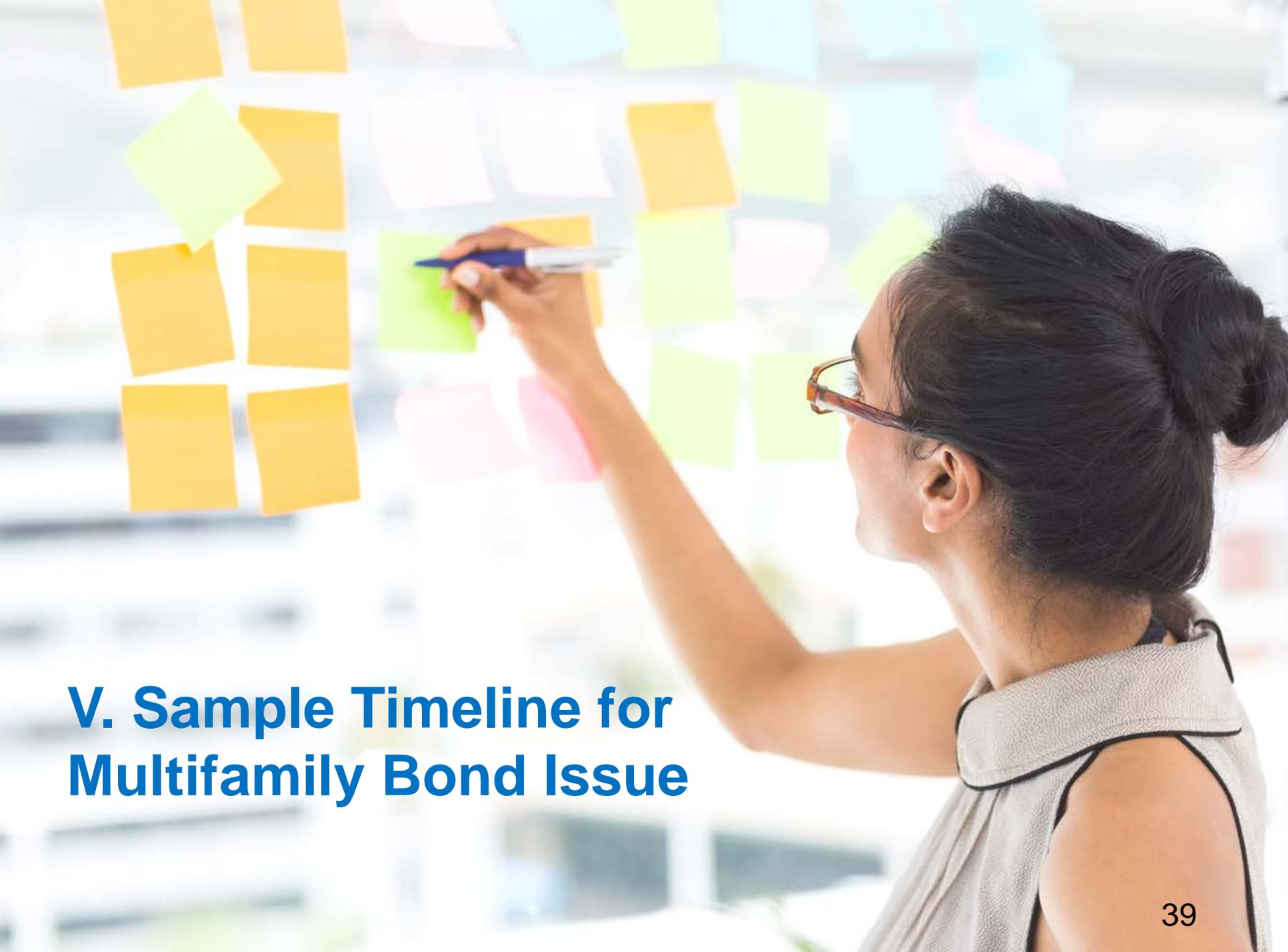
- USDA Section 538 Guaranteed Rental Housing Program (“Section 538 Program”)
- Bond proceeds are used to fund a mortgage loan that is partially guaranteed by USDA from a USDA approved lender.

# Publicly Offered Transaction: Letter of Credit

- Letters of Credit as Credit Enhancement
  - Direct Pay Letter of Credit
  - Standby Letter of Credit
- Federal Home Confirming Letters of Credit

# Additional Financing Options for Multifamily Structures

- 9% Tax Credits - Competitive
- 4% Tax Credits – Not competitive but not automatic
- State Tax Credits
- Historic Tax Credits



## **V. Sample Timeline for Multifamily Bond Issue**

# Sample Timetable of Recent Deal

April 2016						
S	M	T	W	T	F	S
					1	2
3	4	5	6	7	8	9
10	11	12	13	14	15	16
17	18	19	20	21	22	23
24	25	26	27	28	29	30

May 2016						
S	M	T	W	T	F	S
1	2	3	4	5	6	7
8	9	10	11	12	13	14
15	16	17	18	19	20	21
22	23	24	25	26	27	28
29	30	31				

June 2016						
S	M	T	W	T	F	S
			1	2	3	4
5	6	7	8	9	10	11
12	13	14	15	16	17	18
19	20	21	22	23	24	25
26	27	28	29	30		

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**November 18, 2015** Inducement.

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**April 11** TEFRA publication.  
COBO filing.

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**April 13** Conference call – 11:00 AM (Central) / 12:00 PM (Eastern)  
Toll-free: 844 267 3708  
Passcode: 7275675671#

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**Week of April 18** First drafts of bond documents, Preliminary Official Statement and underwriting documents.

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**April 19** Receipt of HUD firm commitment.

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**April 26** TEFRA Hearing.

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**April 28** COBO approval.

# Sample Timetable of Recent Deal (cont.)

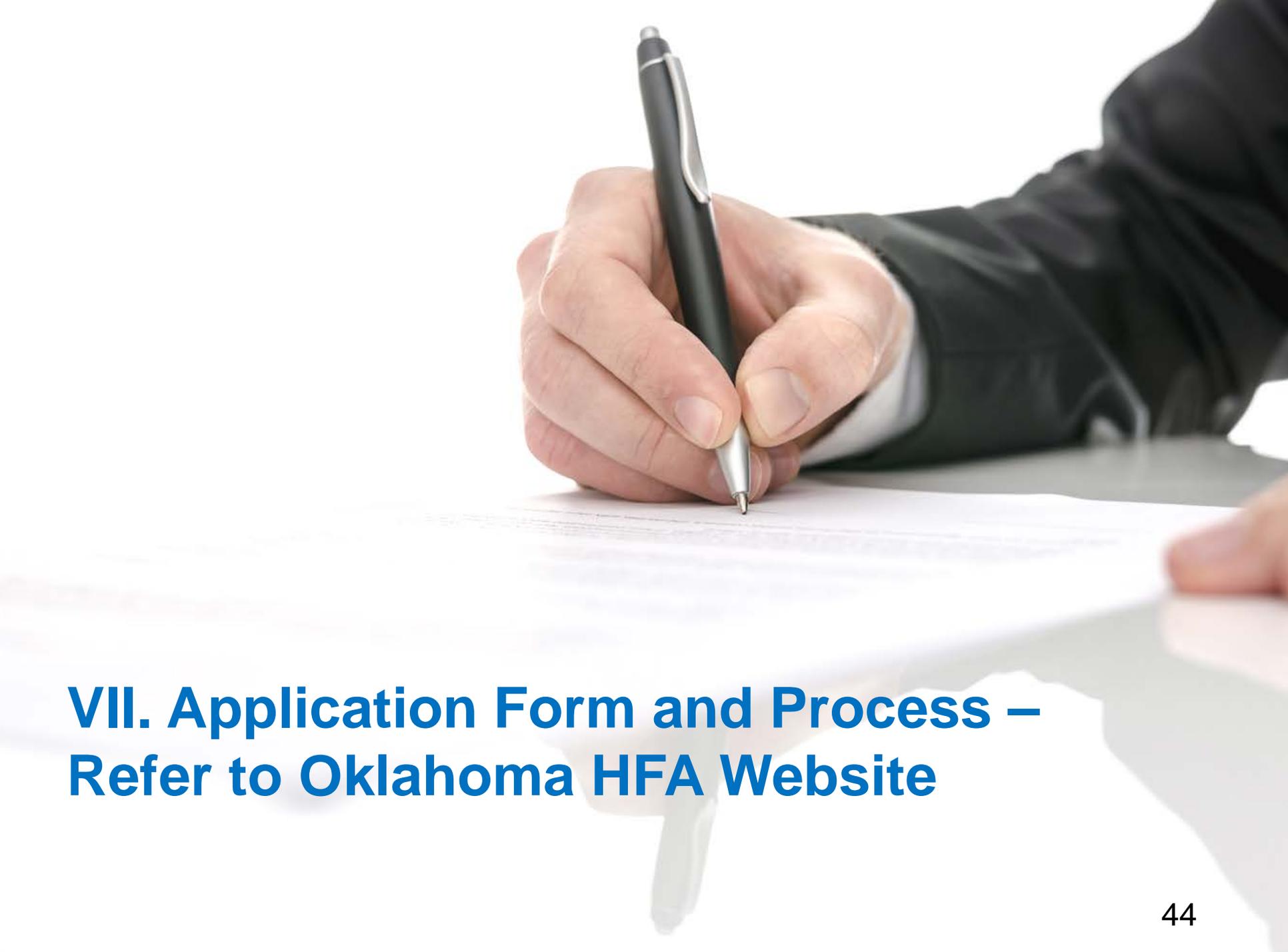
<b>April 29</b>	Substantially final bond documents. Underwriting compete by OHFA.
<b>May 4</b>	HFA board packet deadline.
<b>May 18</b>	HFA board meeting – approval of final bond resolution and 4% tax credit resolution.
<b>May 19</b>	Receipt of verbal rating confirmation. Preliminary Official Statement released.
	Bond pricing.
	Bid investments.
<b>May 25</b>	Verification report released. Rating released. Bond Purchase Agreement executed.
<b>May 27</b>	Final documents circulated.
<b>June 1</b>	Pre-closing – [TBD].
<b>June 2</b>	HUD Closing – [TBD].
<b>June 3</b>	Closing – [TBD].



## **VI. Sample Multifamily Bond Costs**

# Sample Costs

<u>Sample Costs of Issuance</u>			
		(USD)	(USD/Bond)
<b>Par Amount</b>		<b>\$ 10,000,000.00</b>	
<b>Cost of Issuance</b>			
Takedown - <i>Raymond James</i>	\$ 6.000	\$ 60,000.00	\$ 6.000
Underwriter's Expenses <sup>(1)</sup>		9,321.60	0.932
Gross Underwriter's Spread		69,321.60	6.932
Other Estimated Cost of Issuance <sup>(2)</sup>		197,158.50	19.716
<b>Total Cost of Issuance</b>		<b>266,480.10</b>	<b>26.648</b>
<b>(1) Underwriter's Expenses - Detail</b>			
I-Preo		\$ 1,764.60	\$ 0.176
DTC		800.00	0.080
CUSIP		257.00	0.026
Escrow Bidding Agent - <i>Raymond James</i>		4,000.00	0.400
Travel, Misc		2,500.00	0.250
<b>Total Expenses</b>		<b>9,321.60</b>	<b>0.932</b>
<b>(2) Other Estimated Cost of Issuance - Detail</b>			
Bond Counsel - Dinsmore & Shohl LLP		\$ 57,000.00	\$ 5.700
Underwriter's Counsel - <i>Eichner Norris &amp; Neumann PLLC</i>		20,000.00	2.000
Disclosure's Counsel - <i>Eichner Norris &amp; Neumann PLLC</i>		10,000.00	1.000
Financial Advisor - <i>Caine Mitter &amp; Associates Incorporated</i>		10,000.00	1.000
Council of Bond Oversight - Borrower pays to Issuer		2,900.00	0.290
Issuer - <i>OHFA - Closing Fee</i>	0.400	40,000.00	4.000
Issuer - <i>OHFA - Administrative Fee (Annual)</i>	0.125	12,500.00	1.250
Issuer - <i>OHFA - Compliance Fee (Annual)</i>	0.125	12,500.00	1.250
Issuer - <i>OHFA - Closing Fees</i>		8.50	0.001
Issuer's Counsel - <i>Riggs Abney</i>		10,000.00	1.000
Issuer's Special Tax Counsel - <i>J. Brent Clark, P.C.</i>		2,000.00	0.200
Rating Agency - <i>Standard &amp; Poor's</i>		5,000.00	0.500
Trustee Fee - <i>Bank of Oklahoma</i>		7,000.00	0.700
Trustee's Counsel - <i>Public Finance Law Group</i>		4,000.00	0.400
Printing - <i>Imagemaster</i>		2,250.00	0.225
Verification Agent - <i>Causey Demgen (includes \$1,500 for rebate services)</i>		2,000.00	0.200
<b>Total Other Estimated Cost of Issuance</b>		<b>197,158.50</b>	<b>19.716</b>



## **VII. Application Form and Process – Refer to Oklahoma HFA Website**



# Additional Contact Information

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