Ann Arbor Housing Commission Frequently Asked Questions and Risk Analysis

QUESTION: Can the AAHC change from public housing to project based vouchers without using Low-Income Housing Tax Credits (LIHTC)?
ANSWER: Yes. In most cases, the RAD conversion approval requires the AAHC to also fix all of the problems identified in the Physical Needs Assessment. The properties can support some debt but because the rents are restricted, the AAHC cannot take out a large enough loan to fix up all the work that needs to be done and still be able to pay the debt service. If AAHC had sufficient reserve funds in its bank accounts to close the gap between the amount of debt that can be generated from the income stream and the cost of these repairs, LIHTCs would not be necessary. Similarly, if local or state government were to grant sufficient funds to AAHC to complete the repairs, LIHTCs would also not be necessary. However, neither of these conditions exist, so LIHTC is critical to generate enough funding to rehabilitate the larger properties.

QUESTION: Can Council wait to approve the transfer of the property until after all of the due diligence and funding is secured?
ANSWER: Part of the due diligence that needs to be done in order to secure financing is to show evidence of site control by the funding applicant. Funders will not approve financing if the AAHC does not show that it will have site control at the time of closing. The City Council can approve a resolution to transfer the properties to the AAHC contingent on certain items being completed such as the due diligence and securing financing. That resolution can be provided to potential funders to show that the property will be transferred at the time of closing

QUESTION: Why is a PILOT (Payment in Lieu of Taxes) needed?
ANSWER: The City entered into an agreement to exempt the properties from property taxation when HUD provided funding to develop the properties. At the time the properties switch ownership from the City to the new partnership controlled by the AAHC, the properties will no longer be tax exempt, but they will be eligible for a PILOT, under the City's PILOT ordinance. The City's PILOT ordinance allows all eligible affordable housing units targeted at 60% of Area Median Income (AMI) or less to pay $1/unit in taxes per year in lieu of full taxes. MSHDA provides 6 points under its LIHTC application if a City has a PILOT ordinance in place or 15 points if the City has such an ordinance and adopts a resolution giving the specific properties a PILOT for at least 15 years. By adopting project-specific PILOTs the City will enable the AAHC to score 15 points on its application for LIHTC funding. The PILOT will only take effect after the units are converted to project-based vouchers.

QUESTION: When is the AAHC locked-in to making this change from public housing to project-based vouchers?
ANSWER: Any time between now and closing, the AAHC and HUD can agree to discontinue conversion if the AAHC is not able to secure financing to complete all the work required under the physical needs assessment. At the closing three things will happen: the property will be transferred to the AAHC and the AAHC will transfer it to the Limited Dividend Housing Association Limited Partnership or Limited Liability Company; HUD will terminate the Public Housing Annual Contributions Contract for the properties and will instead execute a Project-Based Voucher Contract and Use Agreement on the properties; and the LDHA LP or LLC will execute any financial documents required by the funders.

QUESTION: What if the AAHC is unable to secure capital funds to make project work?
ANSWER: The AAHC units will remain as public housing and AAHC will continue to operate under the challenging regulatory and funding environment that characterizes public housing. In addition, the AAHC will have to absorb the pre-development funding that was already spent for due diligence items such as consultants, legal, surveys, environmental reviews, physical needs assessments, architectural fees etc.

QUESTION: What if Norstar and the AAHC disagree on something, how will it be resolved? Can Norstar remove the AAHC from the partnership?
ANSWER: The AAHC and Norstar will execute a Master Developer Agreement which includes all the roles & responsibilities of the partners during the predevelopment phase. In addition, AAHC's affiliate (the AAHDC – see below), Norstar and the equity limited partner will execute a partnership agreement or LLC operating agreement at the time of the closing which will last for the 15 year compliance period. These documents will guide the relationship. Norstar cannot remove the AAHC from the partnership. However, the limited partner will have the right to remove either general partner (see question below).

QUESTION: Can the equity limited partner remove the AAHDC from the partnership?
ANSWER: The Ann Arbor Housing Development Corporation (AAHDC), Norstar and the Equity Partner will sign a partnership agreement that spells out the roles and responsibilities of the partners. The AAHDC cannot be removed unless it fails to perform in a seriously negligent manner, according to the contract. HUD and/or MSHDA would need to get involved to determine what public housing or non-profit entity would replace the AAHDC. However, this is no different than HUD's right to remove and replace the AAHC right now as the public housing operator.

QUESTION: Can Norstar or the Equity Partner convert the units to market rate housing?
ANSWER: No. HUD has an affordable housing use agreement that precedes all other agreements, financing and legal rights. Only HUD can change the use. In addition, there is a MSHDA Regulatory Agreement for the LIHTCs, which restricts the units as affordable for an extended compliance period (beyond the 15-year initial compliance period).

QUESTION: What happens if there are additional problems discovered after construction begins and the cost increases for construction?
ANSWER: The budget will include both a soft cost contingency and a construction contingency. If the budget uses all the contingency funds and is still short, then there are several options: secure additional funding, reduce the scope of work to remove non-essential items or change to lower cost materials, and/or use the developer fee to cover any shortfalls. If these sources are still not enough to cover the cost increase (which is highly unlikely), Norstar will cover more of the overrun under a guaranty agreement which is still to be negotiated.

QUESTION: What if there are unforeseen construction problems that cause a delay or the contractor fails to perform during the middle of construction?
ANSWER: Norstar is responsible for overseeing construction and providing a construction guarantee. Norstar must cover any short-falls caused by the construction contractor not completing the work by the funder deadlines. In addition Norstar will be providing LIHTC completion guarantees. Norstar will be required to make the investor whole if the investor is not able to deduct its tax credits according to the agreed upon deadlines due to delays is construction or lease-up. In addition to the Norstar guaranty, it is routine for the contractor to pay for a form of insurance, called a payment and performance bond, that covers this risk as well.

QUESTION: What will happen to the tenants who are living in the units?
ANSWER: Each building will be different. Some buildings will require more rehabilitation than others. The goal is to work around residents with the least amount of disruption. Residents will have to tolerate living in a building that is being rehabilitated. Whenever possible, work will be done in an individual unit so that the tenant will not have to be relocated. However, if the scope of work requires the tenant to be without heat, water or cooking devices for more than a few hours, the AAHC will have to temporarily relocate the tenant to a residential inn or another unit until their unit becomes habitable. For units that are demolished, the AAHC will have to relocate the tenants to another unit for the long-term and subsidize the tenants rent, just like the AAHC does now.

QUESTION: What happens if the AAHC is not able to generate enough rent revenue to cover costs while the limited partnership owns the property?
ANSWER: The funders will require a replacement reserve and an operating reserve to cover future capital improvements and any projected operating deficits. There will also be an operating assurance guarantee which will cover any operating losses for the life of the partnership.

QUESTION: What happens to the property after the LIHTC requirements expire?
ANSWER: The partnership agreement will include the terms of the transfer of the property back to the AAHC. These terms are generally in the form of a right of first refusal, exercised at the end of the 15-year compliance period. The purchase price is generally the amount of outstanding debt (which obligation AAHC would simply assume, so no money would change hands) plus $1.

QUESTION: What happens if Congress changes the IRS Code to eliminate the LIHTC program?
ANSWER: The LIHTC program has been in existence since 1986 under Section 42 of the IRC. Although initially a temporary program, the Omnibus Reconciliation Act of 1993 extended the LIHTC permanently. The ORA, was further amended by the Taxpayer Relief Act of 1997. This program is much better protected than HUD funding because the investors in LIHTC are entities with large tax bills and greater influence than low-income people.

QUESTION: What happens if Congress and/or HUD eliminates or reduces the project based voucher/rental assistance programs in the future?
ANSWER: Based on current trends and sentiment, the public housing budget is much more likely to be reduced and cut than the project-based voucher/rental assistance programs. The voucher/rental assistance programs can certainly be cut, but HUD has agreed not to reduce the voucher subsidies provided under the RAD conversion process below the amount agreed to in the first year of the contract. There are no such guarantees for public housing. HUD will have to absorb any project-based voucher reductions with other non-RAD converted units.

QUESTION: Why convert all of the public housing units now? Why not do a few at a time?
ANSWER: The properties could be converted in stages. However, overall it will not save time, effort or money in the long run. If all of the units are not converted within the same general time frame, then the AAHC staff will have to administer two different programs with two different rules – public housing and project-based vouchers. This will be difficult for staff and confusing for tenants because the rules will be different depending on where you live. Separate waiting lists will need to be kept, which are labor intensive and costly. In addition, the AAHC is hiring a developer, architect, engineer, general contractor and other professional services. It is only marginally more work for the AAHC to add additional properties to the same contracts. The professional and trades employees will be paid to do the bulk of the work. And

more importantly, the public housing budget continues to get cut while project-based voucher budgets increase. Also, the RAD Program offers a unique opportunity to accomplish this now.