



Revolving Loan Fund

of the Kentucky Neighborhood Stabilization Program

Kentucky Department for Local Government
Office of Federal Grants

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Introduction

In 2009, the Commonwealth of Kentucky received over \$37 million of Neighborhood Stabilization Program (NSP-1) funding through the U.S. Department of Housing and Urban Development (HUD). Funding was authorized by Title III of the Housing and Economic Recovery Act of 2008 (HERA). In 2011, the Commonwealth received an additional allocation of NSP funding in the amount of \$5 million (NSP-3) through the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010. The overall purpose of NSP is to provide assistance to stabilize communities adversely affected by the foreclosure crisis by funding the acquisition and redevelopment of vacant, abandoned and foreclosed properties in the areas hardest hit. NSP funding is a special allocation of HUD's Community Development Block Grant (CDBG) program. At the state level, the CDBG program is administered by the Office of Federal Grants in the Kentucky Department for Local Government (DLG). The Commonwealth's CDBG program includes housing among its eligible uses. As a result, DLG, with its housing development expertise, administers NSP on behalf of the Commonwealth.

In order to address the destabilizing issues as quickly as administratively possible, HUD imposed stringent deadlines on both funding rounds to expedite the inflow of the financial assistance into distressed communities. The deadlines imposed for the expenditure of NSP funds are far more stringent than what is typically required by HUD for its entitlement programs.

Funding Round	Amount Allocated	Expenditure Deadline
NSP-1	\$ 37,408,788	March 20, 2013
NSP-3	\$ 5,000,000	50% Expended by March 2, 2013
		100% Expended by March 2, 2014

Initial Neighborhood Stabilization Program Design

To meet program objectives and goals, DLG awarded NSP funds to 22 organizations across the commonwealth through a competitive requires for proposal (RFQ) process to undertake eligible activities in sixteen counties. Throughout the implementation of NSP, HUD released revisions to the regulations and several policy updates regarding program requirements. When HUD initially released the NSP regulations, it was required that all program income funds received after July 30, 2013, be returned to the U.S. Treasury. This requirement was revised by HUD in June of 2009, with several amendments to the regulations. The regulatory revisions were issued in the NSP Bridge Notice (Docket No. FR-5255-N-02) that was issued eight months into the program, and in which the requirement to return program income earned after July 30, 2013, was repealed. This revision to the regulation allowed DLG to retain the program income earned to be used for additional eligible activities. One requirement that was not waived, however, was the requirement to expend all program income funds on-hand prior to drawing-down additional grant funds through the Treasury account.

Program income, as defined by HUD in 24 CFR 570.500, is the following types of revenue generated from the use of NSP dollars and includes, but is not limited to:

1. Proceeds received from the sale or long-term lease of real property;
2. Proceeds from the disposition of equipment purchased with NSP funds;
3. Gross income from real property that is used for rental; less incidentals cost (i.e. operating/replacement reserves, maintenance, debt, vacancy, management fees, utilities, etc.);
4. Payments of principal and interest on loans made with NSP funds;
5. Proceeds from the sale of loans made with NSP funds;
6. Proceeds from the sale of obligations secured by loans made with NSP funds;
7. Interest earned on program income pending its use; and
8. Recaptures on sales of homes pursuant to enforcement of NSP affordability requirements.

Current Status of the Commonwealth's Neighborhood Stabilization Program

The majority of Kentucky's NSP recipients used their awards to acquire and redevelop foreclosed and abandoned properties to provide homeownership opportunities to eligible homebuyers. When homeownership units are sold, the proceeds received at closing are considered program income.

DLG also funded several rental projects. After operating expenses are accounted-for, the program income generated by these properties is the net income received.

Although the earning of program income by DLG has been a beneficial attribute of the Commonwealth's program design, it has aspects that are problematic. HUD regulations do not allow for program income to be "stock piled" for a later use. Due to these regulations, it has been difficult for Kentucky to spend-down its grant funds from the U.S. Treasury. Additionally, it is becoming more difficult for DLG to identify additional projects on which to expend program income.

The table below displays the amounts of program income generated and expended as of December 31, 2014.

Funding Round	Program Income Generated	Program Income Expended
NSP-1	\$ 4,521,086.31	\$ 4,521,086.31
NSP-3	\$227,986.57	\$225,878.83

Establishing a Revolving Loan Fund

DLG has chosen to resolve the distribution of program income through the creation of NSP revolving loan funds (RLF). While many other HUD programs prohibit the use of program income funds in this manner, the regulations of NSP mirror that of CDBG and allow for the creation of a RLF. NSP regulations permit the capitalization of RLFs with program income and do not require that program income funds in revolving loan accounts be expended prior to expending grant funds from the U.S. Treasury. In addition, program income funds used to capitalize the account and replenish it are not subject to the federal expenditure deadlines. HUD regulations for RLFs are flexible and allow RLFs to be established to serve any NSP-eligible purpose that generates program income.

The creation of the RLF will be beneficial in the following ways:

- It will create a sustainable long-term funding resource available to be utilized by affordable housing developers.
- It will provide opportunities to expand the Commonwealth's supply of affordable housing stock.
- Recent reductions to the funding allocated for the CDBG program will have an effect on the number of projects funded and the staff time necessary for daily oversight. Creation of the RLF will help to fill that void through the need for additional responsibilities for staff.
- Ten percent of program income remitted can be used by DLG for administrative expenses to cover operational and long-term compliance expenses.

- No less than twenty-five percent of program income generated must be expended on projects benefitting households at or below 50 percent of area median income.
- Program income funds used for the RLF are not required to be expended prior to drawing-down additional grant funds from the U.S. Treasury. This would allow our housing partners to keep expending grant funds to ensure the federal expenditure deadlines are met preventing the Commonwealth from losing any of its allocation.
- Pooling together the small amounts of program income earned each month will allow for the funds to be spent for substantial contributions and have greater impact.
- In a time when we are confronted with budget cuts and reductions to federal allocations, this loan portfolio can be used to leverage other scarce financial resources, such as other public and private funds to continue the efforts of NSP by funding additional projects.

Planning and Implementation

Implementing the establishment of the revolving loan fund requires a lot of planning and collaboration between DLG divisions and staff members. To ensure this solution is a feasible one, it is necessary to determine what is required for federal compliance, how the creation of the RLF would impact the different divisions of the agency, who would be responsible for each piece, and what data is needed to make necessary determinations. To get things started, the following steps were undertaken:

- Research of compliance issues
- Creation of a plan
- Collaboration with staff to determine logistics
- Data collection and analysis

Researching Federal Compliance Requirements

The first step to begin the process was to research all the requirements and regulations set in place by HUD to ensure the establishment of the NSP funds would be compliant with HUD regulations. To understand the level of complexity this undertaking would require, DLG staff researched other state governments' and state housing finance agencies' RLFs using NSP receipts of program income. This research showed that the creation of the RLF was a realistic goal and it would be able to be designed to suit DLG's specific needs.

In June 2013, DLG staff members attended a three-day training course titled *"RLFs and CDBG Compliance,"* hosted in Nashville, Tennessee by the National Development Council. The training consisted of a thorough review of the regulatory requirements for RLFs. Course criteria consisted not only of regulatory requirements, but also included in-depth case studies involving

analysis and discussions of actual situations and factors needed to be taken into consideration when establishing RLFs. This training was an extremely valuable resource in moving toward the establishment of the RLF.

In addition, throughout 2014, HUD facilitated several webinars that covered the establishment and operations of RLFs.

Collaboration with Finance Division and the Kentucky Treasury

Collaboration with DLG's Finance Division is necessary to identify and work-out several logistical issues, such as timing, the budget approval process and staff issues resulting from the additional tasks required for loan servicing, accounting and reporting requirements. This collaborative effort resulted in the identification of crucial components of the plan that needed to be prioritized to begin the process of establishing the budget for its presentation to the Executive Director of the Office of Federal Grants and the Commissioner of the Department for Local Government.

One of the required components is the establishment of the budget and its presentation for approval. Although the loan funds are generated from federal funds and not from state appropriated funds, in order for the outflow of cash from the account to begin, approval of the budget must be granted. Since DLG's budget for the 2014-2015 biennium has already been approved, this will require an amendment to the budget. Once the budget is determined and presented to DLG's Fiscal Manager, it is expected to take 14 days to receive approval. To project revenue and determine the budget amount to request, collaboration with the NSP staff on underwriting requirements was the next step required to move forward.

Another crucial component is the opening of the bank account. Program income regulations require that the RLFs are held in an interest-bearing account that is separate from other DLG funds. It was determined during the meeting that it will take about 21 days to set-up the bank account and that it is not necessary to have the budget for the RLF approved prior to opening the account and depositing funds. Timing for the opening of the account will be coordinated to coincide with the availability of funds for deposit.

The establishment of the RLF will not have significant impact on finance division staff. The division already services a loan fund through the Kentucky Infrastructure Authority, also housed with the DLG, which is similar in nature to the servicing requirements that will be required to service the NSP RLF. Minor adjustments will need to be made to existing processes and procedures to accommodate the addition of the RLF. Ten percent of the program income received to capitalize the fund and of the revenue generated from the fund from repayments will be used to cover the costs incurred to administer the RLF.

Realistic Income Projections

The next step needed was to determine revenue projections for both the initial capitalization of the fund and its eventual stabilization. Revenue generated from the collection of net income earned from the NSP rental and homeownership loan portfolios and excess program income earned from the sale of homeownership units will be used for the initial capitalization and the fund will continue to be sustained from loan repayments (principal and interest) received.

To project revenue as accurately as possible, DLG NSP staff created a revenue projection model, which is based on the anticipated net income to be earned based on the average revenue generated and expenses incurred for a typical single-family home. To arrive at the projected amount, staff used actual revenue data to project the amount of net income to be earned by the portfolio over the course of the next twelve months. DLG NSP staff also projected project revenue on rental projects by collecting data from required financial statements submitted by rental property owners demonstrating current revenue and operating expenses, property tax bills, rent limits and occupancy data. The projection of remitted funds to be received over the course of the next five years is approximately \$675,000.

To forecast the amount of program income that may be available for the capitalization of the revolving loan received from the sale of homeownership properties, the number of unsold homes among NSP partners had to be considered. The potential amount of program income available to capitalize the fund from the sale of the homeownership units can be as much as \$4 million.

The calculated projections for the program income to be remitted from the rental and homeownership loan portfolios were presented to the DLG Finance Division. The determination was made that to ensure budget authority from the state treasury, we would request an annual budget of \$500,000 for the RLF. Once requested, it is anticipated to take up to 30 days to receive approval. It is assumed that all revenue that flows in will flow out, therefore under-estimating the outflow of cash required will cause delays in loan approvals and may limit the amount of loans that can be approved at certain intervals in time.

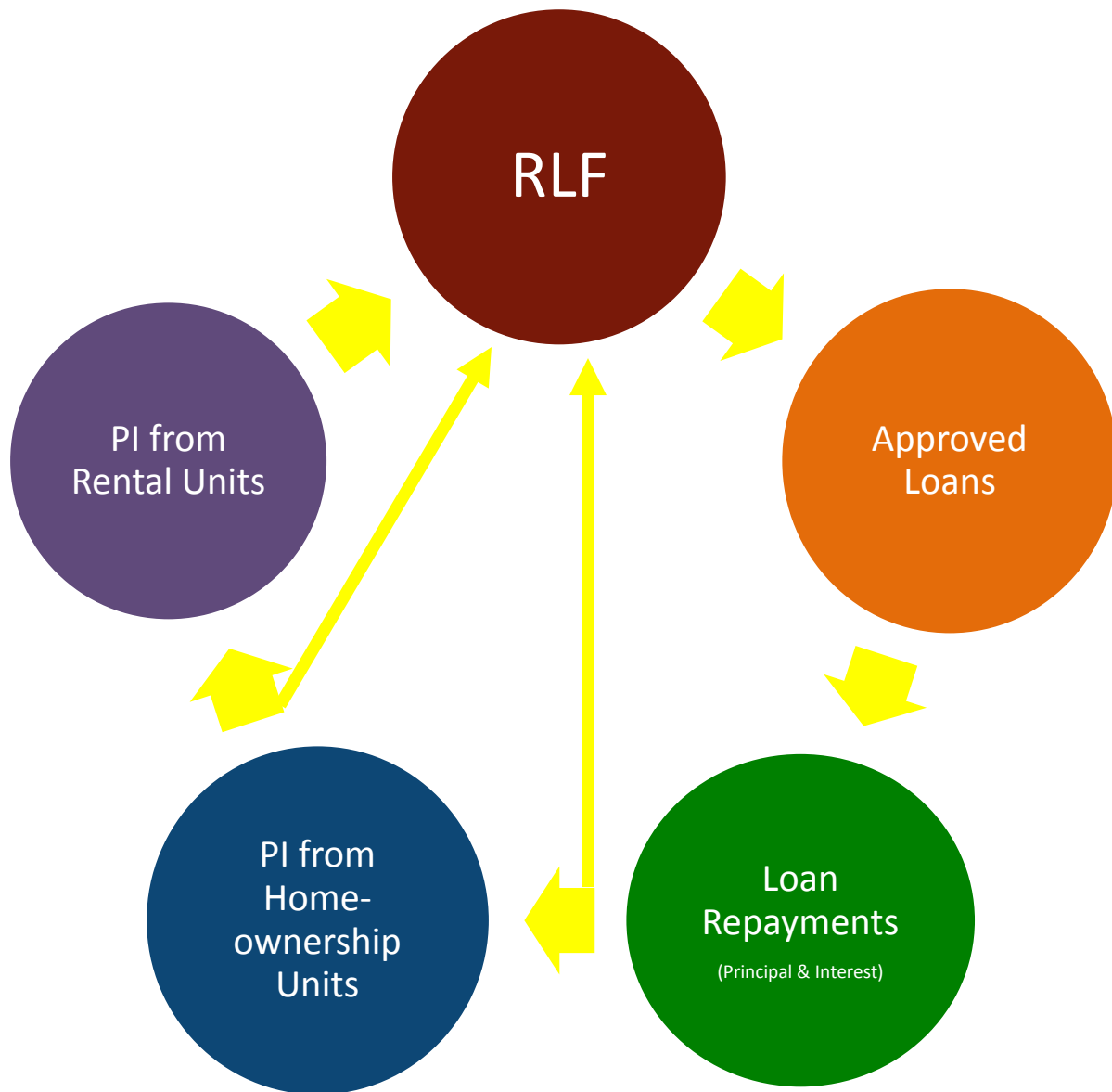
HUD Approval

Upon completion of the revenue projection process, the next requirement is to request formal approval from HUD through an amendment to our NSP Action Plan. All Action Plan amendments are requested and approved online through HUD's Disaster Recovery Grant Reporting (DRGR) System. The amendment process will formally notify the HUD Louisville Field Office representative of the Commonwealth's intent to establish the fund and the anticipated amount of the RLF's budget. Preliminary discussions with the Commonwealth's HUD representative have been ongoing and this part of the process will be to receive formal

approval and to disclose the amendment to the public through the DRGR system, which will incorporate the RLF into the Commonwealth's federal quarterly reporting requirements. The amendment process also requires DLG to follow their adopted citizen participation plan requiring additional steps to allow the public to comment on the planned use of NSP generated program income.

Capitalizing the NSP Revolving Loan Fund

DLG will be ready to begin the initial capitalization of the revolving loan fund as soon as HUD has approved the amendment and the bank account is opened.



Eligible Uses for the NSP Revolving Loan Fund

Eligible Use A: Establish financing mechanisms for purchase and redevelopment of foreclosed upon homes and residential properties, including such mechanisms as soft-second, loan loss reserves, and shared-equity loans for low- and moderate- income homebuyers. HERA [§2301(c)(3)(A)] allows financing mechanisms for purchase and redevelopment of foreclosed upon homes and residential properties, including such mechanisms as soft-second, loan loss reserves, and shared-equity loans for low- and moderate- income homebuyers;

Eligible Use B: Purchase and rehabilitate homes and residential properties that have been abandoned or foreclosed upon, in order to sell, rent, or redevelop such homes and properties.

HERA [§2301(c)(3)(B)] allows the purchase and rehabilitation of homes and residential properties that have been abandoned or foreclosed upon, in order to sell, rent, or redevelop such homes and properties.

a. Acquisition:

- i. Section 2301(d)(1) of HERA requires any purchase of a foreclosed-upon home or residential property under NSP be at a discount from the current market-appraised value of the home or property. Such discount shall ensure that purchasers are paying below-market value for the home or property.
- ii. For mortgagee foreclosed properties, Subrecipients must seek to obtain the “maximum reasonable discount” from the mortgagee, taking into consideration likely “carrying costs” of the mortgagee if it were to not sell the property to the Subrecipient.
- iii. Section 301 of the URA, regarding just compensation, does not apply to voluntary acquisitions.
- iv. All acquisitions of property under NSP require an appraisal for purposes of determining the statutory purchase discount. Appraisals shall be conducted under procedures set forth in Section 2(B) of this Agreement.
- iv. For individual purchase transactions, the purchase discount is to be at least 1% from the current market appraised value of the home or property. Subrecipients shall follow the purchase discount procedures outlined in HUD’s NSP Notice FR–5255–N–02. Subrecipients are strongly encouraged to obtain a minimum 5% discount as originally proposed in their Proposal.
- vi. An NSP Subrecipient may not provide NSP funds to another party to finance an acquisition of tax foreclosed (or any other) properties from itself, other than to pay the necessary and reasonable costs related to the appraisal and transfer of title.
- vii. Subrecipients may not exercise the power of eminent domain to acquire NSP-assisted property.
- viii. HUD is not specifying alternative requirements to the relocation assistance provisions at 42 U.S.C. 5304(d).
- ix. Subrecipients are encouraged to acquire and redevelop FHA foreclosed properties. HUD provides information on such properties at <http://www.hud.gov/offices/hsg/sfh/reo/reohome.cfm>. Subrecipients may also contact their local HUD FHA office for further information.

b. Rehabilitation

- i. Any rehabilitation of a foreclosed upon home or residential property shall be to the extent necessary to comply with applicable laws, codes and other requirements relating to housing safety, quality, and habitability, in order to sell, rent, or redevelop such homes and properties.
- ii. Funds may be used for preservation, improving energy efficiency or conservation, or providing renewable energy source(s).

- iii. The Commonwealth encourages Subrecipients to strategically incorporate modern green building and energy efficiency improvements to provide for long-term affordability and increased sustainability and attractiveness of housing and neighborhoods. Subrecipients must provide, at a minimum, the elements proposed in their Proposal for NSP RLFs.
 - iv. Subrecipient may fund costs such as sales costs and closing costs related to NSP-assisted housing, rehabilitation, or construction activities.
 - v. Subrecipient may rehabilitate property to be operated as rental housing. The costs of purchase, rehabilitation, conversion and sale of such properties are eligible NSP activities, but the expenses of actually operating the rental housing (such as maintenance, insurance, deficits in monthly operating income) and tenant-based rental subsidies are not eligible NSP activities.
- c. Sale
- i. Subrecipient must ensure that homebuyers obtain a mortgage loan from a lender who agrees to comply with the bank regulators' guidance for non-traditional mortgages.
 - vii. Subrecipients are cautioned against providing or permitting homebuyers to obtain subprime mortgages for who such mortgages are inappropriate. The Commonwealth further requires that all non-NSP mortgage financing be in the form of a fixed-rate, fixed-term loan. Balloon loans, adjustable rate loans and similar products are not allowed.

Eligible Use E: Redevelop demolished or vacant properties.

- a. Subrecipients may acquire demolished or vacant properties for redevelopment for purposes other than housing, provided, however, that such redevelopment must be in a targeted area of greatest need and support activities in the area that are acquiring, repairing, and selling foreclosed and/or abandoned homes. Redevelopment of previously undeveloped property is not an NSP-eligible activity.
- b. Subrecipients may fund costs, such as sales costs, closing costs, and reasonable developer's fees, related to NSP-assisted housing, rehabilitation, or construction activities.
- c. New construction of housing and building infrastructure for housing is an eligible use.
- d. Subrecipients may redevelop property to be used as rental housing.

Administrative Costs (Housing and Economic Recovery Act §2301(c)(3))

- a. An amount of up to 5% of NSP Project funds may be used for general administration and planning activities as defined at 24 CFR 570.205 and 206, and could be reduced

by DLG if deemed appropriate. Administrative costs are associated with the planning and implementation of project activities, such as general management, oversight and coordination; public information; fair housing activities; and indirect costs (with an approved cost allocation plan).

- b. Activity delivery costs, as defined in 24 CFR 570.206, may be charged only by Subrecipients to the particular activity performed above and will not count as general administration and planning costs. Project delivery costs can be charged to project funds rather than administrative funds (for example, staff and overhead costs directly related to carrying out activities eligible under § 570.201 through § 570.204). Generally, an administrative cost is not directly related to unit production. Project delivery costs, in contrast, are attributable to a specific unit and must be documented as such. These may include staff cost for the preparation of work specifications and bid documents, property inspections, etc., or external costs such as those related to the sale of the property. Eligible activity delivery costs may also include costs related to the sale of the property such as staff time spent counseling the purchasing household, obtaining appraisals, and engineering and design costs related to a specific activity. For direct costs, staff job descriptions should include the duty (i.e., inspection of NSP-assisted units) and time sheets should document time expended on specific activities for specific NSP units. At the Subrecipient's discretion, it may charge such project delivery costs to individual units produced, or may fund all such costs from its administrative funds.
- c. Housing counseling for prospective purchasers of NSP-assisted units is an eligible activity delivery cost. If a prospective homebuyer completes housing counseling but does not purchase an NSP-assisted home, the costs associated with the counseling are classified as a public service. Other types of housing counseling, such as counseling for prospective tenants, must be classified as a public service. Subrecipients may request reimbursement for such expenses separately from their allocation of NSP funds.

Meeting the National Objective

- 1. All of the funds made available through the RLF shall be used with respect to individuals and families whose incomes do not exceed 120 percent of area median income.
- 2. At least 25 percent of the funds receipted through the RLF shall be used with respect to individuals and families whose incomes do not exceed 50 percent of area median income.
- 3. Although NSP changes the low and moderate income requirement level of the CDBG program, the remaining requirements of 24 CFR 570.208(a) and 570.483(b) regarding area benefit, housing, and limited clientele benefit remain unchanged.

Requirements for Homeownership Activities: Regardless of the Eligible Use under which a property is assisted, for NSP-assisted housing that is being sold to homebuyers, the following shall apply:

- A) If an abandoned or foreclosed upon home or residential property is to be sold to an individual as a primary residence, no profit may be earned on such sale.
 - B) HERA Section 2301(d)(2) directs that the sale of such property shall be in an amount equal to or less than the cost to acquire and redevelop or rehabilitate such home or property up to a decent, safe, and habitable condition. Further, the sale price must be the lesser of the post-development fair market value or the acquisition/redevelopment cost.
 - C) The maximum sales price for a property is determined by aggregating all costs of acquisition, rehabilitation, and redevelopment (including related activity delivery costs, which generally include, among other things, costs related to the sale of property). Cost should equal the total development cost; it may not include holding costs (post-construction utilities, property taxes, insurance, maintenance, etc.).
 - D) In determining the sales price, the Commonwealth will NOT consider the costs of boarding up, lawn mowing, maintaining the property in a static condition, or, in the absence of NSP-assisted rehabilitation or redevelopment, the costs of completing a sales transaction or other disposition to be redevelopment or rehabilitation costs.
 - E) Each NSP-assisted homebuyer is required to complete at least eight hours of homebuyer counseling from a HUD-approved housing counseling agency or a counselor approved by Kentucky Housing Corporation (a HUD-approved housing counseling agency) before obtaining a mortgage loan.
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Ineligible Uses for the NSP Revolving Loan Fund

The following types of activities may not be funded with NSP revolving loan funds:

- Acquisition, construction, or reconstruction of buildings for the general conduct of government;
- Refinancing of existing mortgages;
- Foreclosure prevention activities;
- NSP assistance under Eligible Uses A and B if the properties were acquired by the Subrecipient or Participating Party prior to December 2, 2008;
- Provision of NSP funds for more than 50 percent of the required down payment assistance;
- Acquisition of property via a short sale;

- Political activities;
 - Certain income payments;
 - Construction of new housing by units of general local government, except as permitted under Eligible Use E; and
 - The expenses of actually operating the rental housing (such as maintenance, insurance, deficits in monthly operating income) and tenant-based rental subsidies.
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Loan Awards and Review Committee

The process for awarding loans will be structured very similar to the established processes and procedures we have in place for NSP-1 and NSP-3. NSP loan documents and applications will be revised to meet the requirements of the NSP revolving loan program. Eligible applicants will be entities that completed NSP activities in Kentucky's NSP-1 and NSP-3 programs.

Loan applications will be accepted once each year and will be reviewed on a first-come first-served basis. Maximum loan amounts will be \$500,000 and the terms and interest rates will be determined during the underwriting evaluation and based on the amount of debt service the project can support. Loans will be awarded for the acquisition and rehabilitation of foreclosed and/or abandoned properties located in the designated areas of greatest need identified in Kentucky's Action Plans. At the discretion of DLG, project selection may be also determined if benefitting households at or below 50 percent of area median income.

An internal, independent review committee will make loan decisions based on the recommendations of NSP staff and upon review of the strength of the application, assessment of need, quality of project, and capacity of the applicant. This committee will be made-up: one staff member from DLG's Finance department, one staff member from the Cities or Counties Branch, and one staff member from the Office of Federal Grants.

DLG's NSP staff will be responsible for HUD approval, DRGR data input, HUD reporting requirements, creation of the application and loan documents, awarding the loans, daily project management of the completion of the project and processing draw requests in DRGR.

Additionally, NSP staff members will be responsible for the underwriting requirements of each loan. The Finance Division will be responsible for obtaining budget approvals from the State Treasury, maintaining the bank accounts. NSP staff will be responsible for accounting requirements and loan servicing. NSP staff will also be responsible for the on-site monitoring reviews of projects funded by the RLF through close-out.

Stabilization of the Fund

The anticipated time to begin awarding loans is August 2015. Loans will be awarded for the acquisition and rehabilitation of foreclosed residential properties. On average, NSP-1 funding partners spent \$150,000 to acquire and rehabilitate each single-family property. The same average is expected to occur for projects awarded through the RLF. The availability of the actual acquisition and rehabilitation expense data from the completed NSP-1 projects led to the determination that the average loan amount awarded through the RLF will be around \$300,000, at a two-point-five (2.5%) percent interest rate. Once awarded, it is anticipated that the acquisition, rehabilitation and occupancy will take three to six months per property. Based on this time frame, repayment of the initial loans awarded will begin around October 2015 and the RLF will reach stabilization by May 2017.

Impact of the NSP Revolving Loan Fund

The effectiveness of the NSP revolving loan fund will be measured at both the federal and state level through various reports DLG is required to produce as administrator of NSP. The revenue earned from the RLF will be NSP program income, which is required to be tracked and reported for as long as it is being expended and earned. Program income is perpetual: it never loses its federal identity and is always subject to the NSP federal regulations and reporting requirements. At the federal level, the RLF will have an account established in HUD's DRGR system, which, in essence, puts the RLF on HUD's radar. Once established in DLG's Action Plan in the DRGR system, the RLF will be incorporated into the NSP quarterly reports, which, due to the federal government's initiative to improve transparency and accountability for the expenditure of federal funds, are required to be disclosed to the public. The quarterly reports are utilized by HUD to review funded activities, prepare reports to Congress and other interested parties, and to ensure program compliance. The NSP quarterly report is used by DLG to report accomplishments of funded activities, such as the RLF. The completion data of the properties funded through the RLF, such as the end use (rental or homeownership), number of units produced, demographics of households benefitting, dollars expended and geographic locations served are all included in the report as specific federal performance measurements. HUD also extracts data from the DRGR system to create additional federal reports such as the *NSP Production Reports*, *NSP Snapshots*, and the *NSP Weekly Commitment and Drawdown Reports*, which are posted on HUD's NSP website at:

<https://www.onecpd.info/nsp/nsp-grantee-data/>

The establishment of the NSP RLF will create a sustainable resource for the production of affordable housing in Kentucky and continue the stabilization efforts already in place through DLG's administration of NSP. Recent budget reductions to federal entitlement programs have significantly reduced the amount of funds available to DLG's funding partners for the production of affordable housing in the state. The reduction to the state's CDBG allocation was

around 3 percent. This trend is not expected to change any time soon and it is expected that the budget for the CDBG program will continue to see cuts in upcoming years. In light of current market conditions, the creation of a sustainable funding resource is beneficial now more than ever. The projected annual budget of \$500,000 will fill a void in the reduced funds available due to the anticipated continued reduction of CDBG allocations. The creation of this RLF will contribute toward continued job stability for DLG employees and the employees of the organizations with whom we partner to develop affordable housing.

Exhibit 1: Implementation Timeline

National Development Council’s Revolving Loan Fund Training.....	June 2013
Initial Department Collaboration.....	January 2014
Revenue Projections Completed	April 2015
NSP Revolving Loan Fund Guidelines Published	May 2015
Bank Account Opened and Budget Approved	May 2015
Remittance of Program Income Begins	May 2015
Begin Awarding Loans.....	August 2015
Repayment from Initial Loans Awarded Begins.....	December 2015
Stabilization.....	May 2017

Exhibit 2: NSP RLF Guidelines and Underwriting Criteria

General Guidelines

These guidelines are effective as of May 8, 2015.

Unless otherwise specified in the recipient's RLF agreement, all NSP program income must be returned to the Commonwealth of Kentucky.

Generally, NSP recipients are restricted to a five (5) percent administrative fee. This fee is based on five (5) percent of the requested NSP project funds.

All homebuyer and rental assisted units must adhere to the provision for long-term affordability restriction meeting at least the following requirements:

- | | |
|--|----------|
| • < \$15,000 per unit | 5 years |
| • > \$15,000 < \$40,000 per unit | 10 years |
| • > \$40,000 per unit | 15 years |
| • New construction or acquisition of new constructed units | 20 years |

KY NSP encourages green building, energy efficient design and renewable energy sources in all projects. The cost for certification under these programs is an eligible NSP expense. New construction and rehabilitation should incorporate green building, renewable energy sources and energy efficient components. All costs for green building design and certifications, renewable energy sources, and energy efficient design are eligible NSP expenses. Additional detail regarding construction requirements is contained within each agency's funding agreement.

Homebuyer Activities

1. All homes must be sold for the lesser of the total development cost, excluding holding costs, or the post-construction appraised value. Where the appraised value is the lesser of the two, the home must be sold for the appraised value.

Note: If the land is donated, the appraised or assessed value of the land must be considered as part of the total development cost.

2. Once construction or rehabilitation has been completed, a post-rehab appraisal must be performed and the appraisal report submitted to DLG **PRIOR** to entering into any contract with prospective homebuyers.

Additionally, appraisals that are more than 60 days old, but less than 120 days old, may be updated by the initial appraiser (letter or other documentation is acceptable vs. a new appraisal report.) However, appraisals that are more than 120 days old must be re-done (completely new appraisal).

3. The maximum sales price for a single-family dwelling cannot exceed the following:

- \$150,000-Households at 80% or below of area median income
- \$237,000-Households at 80.1% to 120% of area median income

4. The Kentucky Neighborhood Stabilization Program requires that each NSP -assisted homebuyer complete at least eight (8) hours of homebuyer counseling from a HUD-approved housing counseling agency before purchase. A certificate or other acceptable documentation must be provided to DLG prior to entering into a purchase contract with the buyer at the same time the interim set-up package is submitted.

If the household has recently participated in a HUD-certified housing counseling program, DLG may allow recipients to count this participation without monetary compensation. However, this prior attendance cannot be counted without written DLG approval.

5. NSP recipients must ensure that each homebuyer obtains a mortgage loan from a lender who agrees to comply with the bank regulators' guidance for non-traditional mortgages. See the Statement on Subprime Mortgage Lending issued by the Office of the Comptroller of the Currency, Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, Department of the Treasury, and National Credit Union Administration. <http://www.fdic.gov/regulations/laws/rules/5000-5160.html>.
6. DLG does not allow first mortgage loans that are interest-only, have balloons, etc. Only fixed-rate, fixed-term loans will be approved. DLG strongly encourages subrecipients to review the appropriateness of interest rates and terms and to consider long-term affordability implications.
7. All homeownership households must have an automated underwriting approval.
8. Prospective homebuyers cannot have had any bankruptcies (chapter 7 or chapter 13) or foreclosures within 36 months prior to purchasing an NSP home.
9. To determine NSP homebuyer eligibility, income and asset calculations must include income from ALL household members, per the HOME Part 5 method.

10. Should lenders refuse credit to one or the other co-head of household, additional credit counseling must be provided to enable both co-heads of household to become credit-worthy. If long-term counseling is required, buyers are not appropriate for NSP.
 11. Prior to loan closing, legally married persons who are separated and are not divorced must have the non-occupying spouse sign a legally binding document waiving any courtesy or dower interest in the property.
 12. All households must provide a minimum of \$1,000 from their own funds.
 13. All closing documents must be submitted to DLG no less than 48-hours prior to loan closing. This includes the draft HUD-1 settlement statement and Good Faith Estimate for all mortgages, notes, HUD-1s, and Good Faith Estimates.
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Multi-Family Activities

1. NSP funds can be used to pay reasonable development fees. KY NSP has established the following as reasonable, thus they are the maximum allowable fees based on total development cost of:

\$0 - \$250,000:

General requirements	up to 6%
Overhead	up to 7%
Profit	up to 12%

\$251,000 - \$750,000:

General requirements	up to 5%
Overhead	up to 6%
Profit	up to 8%

\$751,000 and greater:

General requirements	up to 6%
Overhead	up to 2%
Profit	up to 6%

2. Unless otherwise approved by DLG, all multi-family projects must have a minimum debt coverage ratio (DCR) of 1.20 in the first year of operation and for the five years thereafter.
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ENERGY EFFICIENT DESIGN

Utilization of the following combination of Energy Star rated products and energy efficiency technologies during construction helps to determine if a project is considered in compliance with NSP's energy efficiency requirements. New construction and rehabilitation projects should be Energy Star qualified and all of the following items utilized in each unit and incorporated into the specifications and/or work write-up for all units.

- Inclusion of Energy Star rated heating and cooling products. Homes equipped with heat pumps which have programmable thermostats are required to use "adaptive recovery" technology in order to prevent excessive use of electric back-up heating.
 - All windows must be Energy Star rated.
 - Three or more of the following Energy Star qualified appliances must be installed: clothes washer, dishwasher, refrigerator, freezer or range hood.
 - All Energy Star qualified ceiling fans, light fixtures and ventilation fans must be installed. See www.energystar.gov for additional Energy Star guidelines.
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GREEN CONSTRUCTION

For new construction and rehabilitation projects to be considered "green," they must receive a "Green" rating from a nationally certified program such as LEED, National Homebuilders Association or Earthcraft and incorporate at least six of the green construction criteria outlined below. Of the six, two must be water saving methods. For additional information please see <http://www.usgbc.org/>.

- Projects must be located project within ¼ mile of one or more stops for two or more public or campus bus lines available to building occupants.
- Smoking in the building is prohibited and designated smoking areas must be at least twenty-five feet away from entries, outdoor intakes and windows.
- All adhesives, sealants and primers used on the interior of all buildings and applied on site must comply with South Coast Air Quality Management District Rule #1168.

Acceptable VOC limits are listed in the table provided at the following web address (<http://www.arb.ca.gov/DRDB/SC/CURHTML/R1168.PDF>).

- Use of fifty percent (50%) of wood based materials and products that are certified in accordance with the Forest Stewardship Council's (FSC) Principles and Criteria for wood building components.

- A minimum of fifty percent (50%) of parking spaces must be under cover (sheltered).
- Vegetated open space must be provided in an area equal to: 1) 20 percent of the project site area, or 2) equal to the building foot print. Vegetated open space is defined as lawns, gardens, plant beds, and fish ponds with plants, shrubs or trees.
- Easily accessible areas that serve the entire project and are dedicated to the collection and storage of non-hazardous materials for recycling, including (at a minimum) paper, corrugated cardboard, glass, plastics and metals must be provided. Property is responsible of ensuring the proper disposal and removal of recyclables.
- Compact florescent light bulbs (CFLs) must be installed throughout the project.
- Rapidly renewable floor materials, such as bamboo, linoleum, cork or eucalyptus, must be utilized to cover a minimum of 25% of the floor area of each unit. Note: linoleum is not vinyl.
- Covered storage facilities and racks for securing bicycles must be provided for fifteen percent (15%) or more of building occupants.
- A vegetated roof must be installed for at least fifty percent (50%) of the roof area.
- Programmable thermostats must be installed throughout project. (Note: If a heat pump is installed in the units, a programmable thermostat specifically designed for heat pump systems must be utilized.)
- A construction waste management plan that recycles or salvages at least fifty percent (50%) of non-hazardous construction and demolition debris must be developed and implemented.
- Tankless water heaters must be installed in each unit. (Note: Proper installation requires that the heating unit satisfies demand capacity and the manufacturer's energy requirements be strictly followed.)
- Recycled, salvaged, refurbished or reused materials must be used to the extent that the sum of these materials constitutes at least ten percent (10%) of the total value of materials on the project.
- Building materials which have been extracted, harvested, recovered or manufactured within five hundred (500) miles of the project site must be used for a minimum of ten percent (10%) of the total material costs.
- Only carpeting that meets the product testing requirements of the Carpet and Rug Institute's Green Label Plus program is to be used throughout project.

<http://www.carpet-rug.org/about-cri/cri-signature-programs/green-label-plus-carpet.cfm>.

- The average flow rate for all lavatory faucets must be ≤ 2.0 gpm.
- The average flow rate for all showers must be ≤ 2.0 gpm.
- The average flow rate for all toilets must be ≤ 1.3 gpf.
- Toilets must be dual-flush and meet the requirements of ASME A112.19.14.
- Toilets must meet the U.S. EPA WaterSense specification and be certified and labeled accordingly.
- All domestic hot water piping shall have R-4 insulation. Insulation shall be properly installed on all piping elbows to adequately insulate the 90-degree bend.
- Central hot water manifold trunk no more than 6 feet, insulated to R-4, with no branch line exceeding 20 feet.
- Compact hot water supply line design with no run over 20 feet from water heater.
- Prior to construction, create detailed framing plans or scopes of work and accompanying architectural details for use on the job site. Indicate the specific locations, spacing, and sizes of all framing members in the floors, walls, roof and ceiling (if different from the roof).
- Prior to construction, create a detailed cut list in lumber order that corresponds directly to the framing plans and/or scopes of work.

Renewable Energy Sources

The NSP Program encourages the utilization of renewable energy sources in construction and rehabilitation. Renewable energy comes from several sources such as the sun, wind and water. Incorporating these sources into program design is encouraged and is an eligible expense of the NSP Program. For more information on Renewable Energy Sources visit: <http://www.nrel.gov>.

Housing Construction and Rehabilitation Standards

All NSP-assisted units must meet the Uniform Federal Accessibility Standards (UFAS), Fair Housing Design Standards (Green Book), all local housing codes, and occupancy standards

for new or reconstructed units. At a minimum, for rehabilitated units the Subrecipient must adopt the 2006 International Code Council (ICC) Property Maintenance Code. All newly-constructed units (including reconstruction) must meet 2007 Kentucky Residential Code.

On March 15, 2012, the Department of Justice's updated ADA Standards (2010) will become mandatory for new construction and alterations covered by the ADA. On the date, optional use of the original 1991 ADA standards will no longer be allowed. DOJ adopted the updated standards in September 2010, but permitted continued use of the 1991 standards for 18 months to allow time for transitioning to the 2010 edition.

Under DOJ's ADA regulations, the March 15, 2012 effective date applies to the date of the permit application or, where no permit is required, to the physical start of construction or alteration. Copies of the 2010 standards and related information are available on DOJ's website at <http://www.ada.gov>.

Any construction or rehabilitation of residential structures with assistance provided under this Agreement shall be subject to HUD Lead-Based Paint Regulations at 24 CFR 570.608, and 24 CFR Part 35, Subpart B. Such regulations pertain to all NSP-assisted housing and require that all owners, prospective owners, and tenants of properties constructed prior to 1978 be properly notified that such properties may include lead-based paint. Such notification shall point out the hazards of lead-based paint and explain the symptoms, treatment and precautions that should be taken when dealing with lead-based paint poisoning and the advisability and availability of blood lead level screening for children under seven. The notice should also point out that if lead-based paint is found on the property, abatement measures may be undertaken. The regulations further require that, depending on the amount of Federal funds applied to a property, paint testing, risk assessment, treatment and/or abatement may be conducted.

Additional Requirements for NSP-3-Funded Projects

- All gut rehabilitation or new construction (i.e., general replacement of the interior of a building that may or may not include changes to structural elements such as flooring systems, columns or load bearing interior or exterior walls) of residential buildings up to three stories must be designed to meet the standard for Energy Star Qualified New Homes.
- All gut rehabilitation or new construction of mid -or high-rise multifamily housing must be designed to meet American Society of Heating, Refrigerating, and Air-Conditioning Engineers (ASHRAE) Standard 90.1-2004, Appendix G plus 20 percent (which is the Energy Star standard for multifamily buildings piloted by the EPA and the Department of Energy).

- Other rehabilitation must meet these standards to the extent applicable to the rehabilitation work undertaken, e.g., replace older obsolete products and appliances (such as windows, doors, lighting, hot water heaters, furnaces, boilers, air conditioning units, refrigerators, clothes washers and dishwashers) with Energy Star-46 labeled products.
- Water efficient toilets, showers, and faucets, such as those with the WaterSense label, must be installed.
- Where relevant, the housing should be improved to mitigate the impact of disasters (e.g., earthquake, hurricane, flooding, fires).
- Buy American Provision – Sub-recipient agrees that in accordance with ARRA, Section 1605, neither Sub-recipient nor its Sub-recipients/contractors will use ARRA funds for a project for the construction, alternation, maintenance, or repair of a public building or public work unless all of the iron, steel and manufactured goods used in the project are produced in the United States in a manner consistent with United States obligations under international agreements. The Sub-recipient understands that this requirement may only be waived by the applicable federal agency in limited situations as set out in ARRA, Section 1605.

Exhibit 3: NSP Revenue Projection Data

As of December 31, 2014

Single-Family Loan Portfolios		
NSP-1 Single Family Loans	\$ 146,745.27	\$ 733,726.35
NSP-3 Single-Family Loans	\$ 28,553.27	\$ 142,766.35
	\$ 175,298.54	\$ 876,492.70
Multi-Family Loan Portfolios		
Community Ventures Corp.	\$ 1,011.62	\$ 5,058.10
Newport Millennium Housing	\$ 12,319.20	\$ 61,596.00
	\$ 13,330.82	\$ 66,654.10
Single-Family Home Sales		
Community Ventures Corp.	5 @ \$125,000	\$ 625,000
HA of Bowling Green	1 @ \$85,000	\$ 85,000
Housing Partnership, Inc.	16 @ \$120,000	\$ 1,920,000
Louisville Metro Government	4 @ \$115,000	\$ 460,000
Owensboro, City of	2 @ \$110,000	\$ 220,000
Pennyryle Housing Corp.	3 @ \$90,000	\$ 270,000
Purchase Area Housing Corp.	1 @ \$80,000	\$ 80,000
		\$ 3,660,000
Total Revenue Projection		
	Annual	5-Year Projection
	\$ 188,629.36	\$ 4,603,146.80