EXHIBIT 22

Subsidy Layering Policy

(Derived from CPD Notice 98-01)

A. INTRODUCTION

The purpose of this policy is to provide guidance in evaluating projects using HOME funds in combination with other government assistance. This analysis is completed to ensure only the necessary HOME Program funds are invested in any one project. This evaluation is referred to as a “layering analysis”. **LAYERING** is the term commonly used for the practice of combining government resources on a HOME-assisted project in such a manner that it results in an excessive amount of government subsidy for the project. The use of other government funds in a housing project is not prohibited, provided the combination of the assistance provided does not exceed the amount necessary to make the project feasible. According to 24 CFR §92.250 of the HOME final rule, MDOC certifies in their program description the following:

- MDOC will evaluate the project according to the guidelines it has adopted, before the commitment of funds to a project; and
- MDOC will not invest any more HOME funds, in combination with other government assistance, than is necessary to provide affordable housing.

MDOC will complete an evaluation on each project to determine if layering has occurred.

B. DEFINITIONS

For the purposes of this policy, the following definitions apply:

1. **Project.** A site or sites together with any building (including a manufactured housing unit) or buildings located on the site(s) that are under common ownership, management, and financing and are to be assisted with HOME funds as a single undertaking. The project includes all the activities associated with the site and building.

2. **Governmental Assistance.** Governmental assistance includes any loan, grant (including Community Development Block Grant), guarantee, insurance, payment, rebate, subsidy, credit, tax benefit or any other form of direct or indirect assistance from a federal, state, or local government for use in, or in connection with, a specific housing project.

C. EVALUATION

Before MDOC invests HOME funds in a project, it must assess if other government assistance has been, or is expected to be, made available to that project. In performing this evaluation, MDOC will consider the aggregate amount of assistance from the U.S. Department of Housing and urban Development (HUD) and other sources (both public and private) needed to ensure the project's feasibility. In making this determination, MDOC will consider all the factors relevant to project feasibility. These factors include such items as:

- past rates of returns to owners, sponsors, and investors;
- the long term needs of the project and its tenants; and
- the usual and customary fees in the development of the project.

The population being served also will be considered. For example, targeting a population that is very low-income (e.g., below 30% of median income) will often result in an increased level of HOME or other assistance.

MDOC will evaluate projects using HOME funds as follows.

Maximum per Unit Subsidy Limits

MDOC shall review the application to determine that the amount of HOME funds invested on a per unit basis do not exceed the maximum per unit subsidy limits. The *National Affordable Housing Act* established the benchmarks for the maximum per unit subsidy limits for the investment of HOME funds. The per unit dollar limits are established in 24 CFR §§221.514(b)(1) and (c). The maximum subsidy limits are found in the current year's HOME Administration Manual and are published annually in the HOME Application Guidelines, **Exhibit 15**.

Certification of Federal Assistance

MDOC shall obtain a formal certification from the applicant(s) concerning the governmental assistance provided or to be provided to a project. If no such governmental assistance is to be provided at the time of the application(s) or in the future, the applicant should certify to that fact. The applicant(s) should also certify that should other governmental assistance be sought in the future, MDOC would be notified promptly.

Sources and Uses of Funds Statement

MDOC will ensure that the total proposed funding (both private and public) does not exceed the total development costs of the project.

1. **All Proposed Sources of Funds and Dollar Amounts.** MDOC requires each applicant to document all sources of funds shown in the Project Budget. This documentation will include firm letters of commitment from each source of funding. Each letter of commitment must include all terms and conditions for all mortgages, grants, subordination agreements, interim loans and investment tax credits. If the applicant is a partnership, a copy of the partnership agreement, indicating the cash contributions by the general partner(s) and/or limited partner(s) must be provided. For the purposes of the subsidy review, the proceeds from the sale of low-income tax credits are considered a source of funding.

2. **All Uses of Funds Associated With The Projects.** The Uses of Funds include, but are not limited to, acquisition cost, rehabilitation or construction costs, financing costs and professional fees. As part of the application process, MDOC requires the applicant to document all uses of funds associated with the Project. This documentation includes the following:

   - project budgets and pro forma statements;
   - earnest money agreement, buy/sell agreement (option), or closing statement for land and/or building(s);
   - construction cost estimates, construction contract, or preliminary bids and architectural plans;
   - agreements governing the various reserves to be capitalized at closing (to verify that the reserves cannot be withdrawn later as fees or distributions);
   - appraisal (to substantiate the value of the land and the value of the property after rehabilitation or construction);
   - if low income tax credits are utilized, documentation on the syndication costs (legal, accounting, tax opinion, etc.) from the organizations/individual who will syndicate and sell the offering to ensure the project can support the fees necessary to syndicate/fund and all assumptions in the offering should be verified in the supporting documentation; and
   - supporting documentation for all other costs as specified in the Sources/Uses of Funds statement.

Project Development Budget

MDOC will have to make a determination whether the costs outlined in the program budget are necessary based upon the type of development activity (new construction vs. rehabilitation, occupied vs. unoccupied) and the objectives of the HOME Program. The determination of "reasonableness" of the costs will be based on all the following:

(1) costs of comparable projects in the same geographical area;

(2) the qualifications of the costs estimators for the various budget line items; and

(3) comparable costs published by recognized industry cost index services.

As part of the MDOC ranking process, the applicant is asked to provide an overall project budget, a budget narrative and a projected cash flow. The budget should include **all costs** associated with the development of the project regardless of the funding source. Budget items should include any construction costs, soft costs (architectural and engineering fees, consulting fees, legal and appraisal fees) marketing costs, construction loan interest and fees, developer fees, real estate taxes, insurance, all loan fees, building permits, and relocation costs.

Costs outlined in the proposal will be compared to other proposals with similar projects. A proposal including costs that are not reasonable and necessary either will not be funded or will be approved on the condition the project budget is revised to reflect more reasonable costs.

Rate of Return on Equity Investment

As part of the HOME application, an applicant is required to submit a project income and expense statement (pro forma) for all rental projects. If the applicant has a grant for rental rehabilitation for single-family units, a pro forma statement must be completed on each unit. The information provided in this statement will allow MDOC to evaluate the project to determine if the owner is getting a reasonable rate of return on his/her investment and will help ensure that no development receives HOME funds if it is likely to fail financially. MDOC will base the pro forma review on some basic industry standards discussed below and found within the Project Financial Evaluation form.

MDOC must determine that the projected rates of return are reasonable and the applicant is not receiving excessive profit or windfalls from the project.

MDOC will determine the internal rate of return (IRR) on the project. The IRR will be compared to current standards to ensure the applicant's return on invested equity is reasonable.

D. BASIC PRO FORMA INDUSTRY STANDARDS

All income should be included in the pro forma, including rental income, laundry income, and other miscellaneous revenue. All additional equity contributions to the operating budget (such as funds to cover anticipated initial operating deficit or staged tax credit equity payments) will be considered income. The rate of increase for income should not be higher than 3 percent per year for the average project.

All cash expenses should be included and reflect the project's type, services and costs provided by the locality and type of mechanical systems. All debt service, any partnership distributions and non-cash expenses (depreciation, amortization of fees and amortization of principal) will be considered expenses. Operating expenses, as a percentage of gross rents, should be comparable to other rent-controlled projects and increased at a 1 to 2 percent higher rate than the expected annual increase in income. The vacancy rate should be a minimum of 7 percent annually. Property management fees should be approximately 5-7 percent of gross rents. Developer fees should not exceed 10-15 percent of total development costs. [For LIHTC projects, the following are excluded from the total development costs: developer and building fees, land cost, cost of acquisition (if rehabilitation activity); and consultant fees.]

Minimum operating reserves should equal 4 to 6 months of projected operating expenses plus debt service payments and annual replacement reserve payments. Minimum replacement reserves should equal $250 - $300 per unit. Architectural fees as a percentage of total construction costs should be less than 8 percent. The project's debt coverage ratio should be between 1.15 and 1.25.

If an application exceeds the basic standards, the project will be reviewed further to determine whether the additional costs are justifiable and reasonable due to the unique needs of the particular project.

E. OPTIONS

Once the layering evaluation is completed and MDOC determines that only the necessary government funds are used to fund a project, the Project Financial Evaluation will be signed and kept in the HOME Project files.

If it is determined the combined assistance from HUD and other government sources exceeds the amount necessary to make the project viable, MDOC may exercise one of the following options.

1. MDOC may impose a dollar for dollar, or equivalent, reduction for the MDOC assistance to reflect the amount of the other government assistance. This could be accomplished through reducing the development budget accordingly or increasing the non-public funding of the project;

2. Make other adjustments to the project, such as lowering the rents to be charged, reducing the term of the loan to reduce the rate of return; or

3. Deny HOME assistance if the applicant refuses to make reasonable adjustments or to limit its return/costs.