Rental Housing Division
Compliance and Asset Management
Operations Manual

December 2024

1. Overview

1.1 Purpose and Scope

This manual serves as an overview for the Virginia Housing Rental Housing Compliance and Asset Management Department. It includes policies and procedures related to conducting property inspections, reviewing property records for all Virginia Housing Rental properties, and monitoring the financial status of properties with Virginia Housing loans. Monitored programs include federal Low-Income Housing Tax Credits, state Housing Opportunity Tax Credits, Tax-Exempt Bonds, Taxable Bonds, Mixed Use-Mixed Income loans, and REACH financing.

1.2 Responsibilities and Authority

Responsibilities for the Rental Housing Compliance and Asset Management Department:

- Managing portfolio and program risk for Virginia Housing Rental Housing
- Compliance with Virginia Housing Program Requirements
- Audit of Property Financial Statements and Expense Management
- Active monitoring of the At-Risk/Watch List of properties
- Physical inspections of Virginia housing-financed properties
- Management of the Reserve Funds for each property
- Compliance with Housing Tax Credit program requirements

Compliance and Asset Management is comprised of A Director and four regional teams responsible for completing financial reviews, property inspections, and auditing property and tenant records for compliance with Virginia Housing loans and monitored rental programs. All regions are comprised of Asset Managers (AM), Compliance Officers (SO), Compliance Specialist (CS), and a Regional Portfolio Manager (RPM). Each team manages the annual schedule of property inspections and audits of property records.

The regional teams are assigned properties based on four segments of Virginia.

- Capital and Southwest Region
- Central Region
- Northern Region includes properties in the northern areas of Virginia
- Eastern Regional includes properties

The department also includes an Asset Manager of Special Assets, who manages at-risk and troubled rental properties with Virginia Housing loans, and a Compliance Support Team comprised of a Compliance Support Manager, Compliance Support Officers, Coordinator, and Data Officer, who are responsible for coordinating annual reporting, training, communication, and data quality reviews of assigned business systems, (e.g., ProLink, Procorem, HDS NextGen).

1.3 Compliance and Asset Management Functional Overview

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

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

1.3.2 Property Inspections:

Property inspections are an important part of Compliance and Asset Management's responsibility in monitoring the management and operation of developments in the Virginia Housing Rental portfolio. Effective monitoring requires recurring property inspections and on-site visits to review property records.

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

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

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

Assisted properties, such as the HUD Risk Share program, may require Virginia Housing's annual visits as required by our role as the Contract Administrator.

1.3.3 Financial Monitoring

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

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

1.3.4 Risk Analysis

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

1.3.5 At Risk/Watch Quarterly Report

Properties of Concern: The Compliance and Asset Management Department will determine, on a quarterly basis, the risk rating for each property in the Virginia Housing financed portfolio. Utilizing the Risk Assessment activity in ProLink, each Asset Manager determines a property's risk assessment based on a variety of information, including the status of the mortgage payment, the physical condition of the property, and the financial performance of each property, which includes the most recent operating budget, monthly operating information, and audited financial statements. ProLink takes into consideration these and additional factors (see attached) to establish an overall score for the property, which is then associated with a particular risk rating: At-Risk, Watch, or Acceptable.

Risk points that total to less than 7.99 indicate an Acceptable rating. 8.00 to 14.99 reflect a property in Watch status, and properties with a point total in excess of 14.99 indicate an At-Risk status. The Asset Manager may adjust the point criteria based on information that may have recently come to his/her attention that is not reflected in the objective information. This must be accompanied by specific comments and reasoning for the adjustment. All properties with an At-Risk/ Watch rating will appear on the Quarterly At-Risk/Watch Report. Properties on the At Risk/Watch Reports will require additional monitoring by Virginia Housing. Each of these properties will be inspected at least annually and may include additional visits to the property and additional financial reporting requirements.

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

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

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

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

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

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

We recognize that that each property has some value that may exceed the NOI calculated value, particularly in situations where the property will support little or no debt. Also, there are instances where a realistic NOI cannot be calculated, as indicated above. For example, there may not be adequate information available to compute an NOI due to the nature of the facility (group home), or the property may be in the early stages of lease-up, generating little income.

Therefore, we may consider information such as a recent appraisal, a recent tax assessment (although we may choose to recognize just the value of the land), a documented recent comparable sale of a comparable property, or a Broker Price Opinion (BPO). These are all third-party documented numbers that can be subtracted from the outstanding loan balance, providing a more realistic "potential loss". In an instance in which there exists a third-party value and an NOI that can support a certain amount of debt, Virginia Housing will utilize the calculation reflecting the lesser "potential loss". If there is no NOI or third-party value available, the loan balance will be a potential loss.

Determining the "Adjusted Potential Loss":

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

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

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

Risk:

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

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

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

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

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

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

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

The draft reports will be reviewed by the Director of Compliance and Asset Management and the staff, along with the Director of Rental Programs and the Assistant Director of Rental Servicing. Once these reports are finalized, they are forwarded to the Virginia Housing Controller, the Rental Development and Servicing Departments, and other departments throughout Virginia Housing. The At-Risk Watch procedures are included in At-Risk Watch Procedures.

1.4.5 Reserve Escrow Accounts

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

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

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

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

1.4.6 Loan Assumptions

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

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

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

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

1.4.7 Management Agent Certification Program

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

1.4.8 Compliance Monitoring

Virginia Housing is responsible for the compliance monitoring of various housing programs and financing regulations for properties in the Rental Housing portfolio. These include properties participating in the Housing Credit program, HUD Section 811, Risk Share, and Rental Loan Programs including Tax Exempt Bond and Taxable Bond financing, along with other loan programs using Taxable Bonds, REACH, and MUMI program funds. Property audits and inspections are scheduled and conducted at least once every three years. The schedule of property audits and record-keeping for all audit notices, and deficiency reports are saved in the ProLink system for all programs. For the HUD Section 811 and Risk Share properties, Compliance Officers follow HUD protocol. Virginia Housing compliance audit procedures are outlined in Section 2.2.

At-Risk/Watch Quarterly Report

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

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

Updated 6-10-2014

AM Risk Assessment Criteria

Status Risk Status Point Values

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

Monthly Operating Statements

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

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AM Risk Assessment Criteria as of 6/10/14

Annual Financials

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

Operating Budget

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

Physical Inspection

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

Loan/Reserve

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

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AM Risk Assessment Criteria as of 6/10/14

2. Virginia Housing Compliance and Asset Management Policy and Procedures

2.1 Legal Authority, Regulations, Guidelines and Forms

2.1.1 IRC Section 42 and Regulations Section 1.42-5

2.1.2 Virginia Low-Income Housing Tax Credit (LIHLIHTC) Administrative Code

2.1.3 Guide for Completing Form 8823, Low-Income Housing Tax Credit Agencies Report of Noncompliance or Building Disposition (Revised January 2011) and the Audit Technique Guide (revised August 2015)

2.1.4 Housing Opportunity Through Modernization Act (HOTMA) (formerly Occupancy Requirements of Subsidized Multifamily Housing Programs (HUD Handbook 4350.3)

2.1.5 National Standards for the Inspection of Real Estate (NSPIRE) (formerly Uniform Physical Conditions Standards (UPCS)

2.1.6 Forms – All property compliance forms for the Housing Credit and Loan programs are posted to the Virginia Housing website on the Compliance Forms and Documents page.

The compliance monitoring procedure forms are stored on the Q drive in the Compliance & Asset Management folder and

2.2 Virginia Housing Compliance Monitoring and Audit Procedures

2.2.1 Notification of Audit

Virginia Housing will give owners written reasonable notice of a compliance monitoring review and property inspection of not more than 15 days for all rental housing properties except properties under HUD programs monitored by Virginia Housing. Notice of audit and inspection for HUD-assisted properties monitored by Virginia Housing must be a formal signed letter 14 calendar days prior to conducting required HUD inspections, such as HUD Risk Share, Section 811, or Management and Occupancy Reviews. HUD per HUD Notice PIH-2019-09

2.2.2 Selection of Units

Virginia Housing will make a random selection of files and units to be inspected, according to the program requirements. Under no circumstance will the owner be made aware of units or files that will be inspected prior to the date of such inspection. If the Compliance Officer is conducting the file and physical inspection, and the physical inspection is conducted first, the list of files to be reviewed should only be given to on-site staff at the time the file review will be performed. The Agency must select the units for inspection or low-income certification review separately and in a random manner. The same units can only be selected if the property inspection and low-income certification are completed on the same date. If all selected units cannot be completed in the same day, a separate unit selection must be made available on the date of the scheduled inspection and low-income certification review.

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

Reference: §1.42-5(h)(2) and [Federal Register Document 2019-03388]() amended in 2019 for the required program unit selection.

2.2.3 Document Control

When performing on-site file and/or physical inspections, the Compliance Officer and Asset Manager must communicate concerns with the property. All findings must be disclosed in a written report of audit findings and property deficiencies within 30 days of the scheduled audit. The owner will be provided a response period of 30 days to respond and submit supporting documentation of correction for property deficiencies and low-income certification review findings.

Severe, Life-Threatening, and Health and Safety Hazards noted during a physical inspection must be reported in writing by issuing the 24-hour Notice form to the property leasing and management staff. The Asset Manager or Compliance Officer must be precise in identifying a critical and severe violation(s) and include specific details about the affected buildings and units. The Compliance Officer or Asset Manager issuing this notice must request a signed/dated copy from management prior to leaving the property.

This guidance is applicable to all properties with programs monitored and administered by Virginia Housing. unless the ruling program guidance is more restrictive

The questionnaire portion of the Report of Occupancy Audit Findings may be emailed to management for completion prior to the date of the audit with the audit notice, given to management to complete at the beginning of the audit process on the day of the review, or completed by the assigned Compliance Officer at the end of the compliance monitoring visit. The assigned Compliance Officer should review and confirm the responses with the property as part of the exit interview.

2.2.4 Audit Requirements Monitored by Compliance and Asset Management Staff

2.2.4.1 Virginia Housing Loan Programs

Taxable Bond Financing Programs (includes REACH, SPARC, Housing Fund, General Fund, MUMI and Flex Fund)
The Virginia Housing regulatory documents for this type of financing stated that the owner is subject to review in a manner specified by the agency. Compliance monitoring will be conducted according to the terms and requirements included in the Regulatory or Loan Agreement.

A. Tenant data must be submitted to Virginia Housing using the online Procorem online Tenant Portal

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

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

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

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

F. Annually, by 12/31, the assigned staff person must complete a Report of Bond Review, including running an Occupancy & Demographics Report (unless an audit is completed in that year; requirement updated in 2016 from every 3 years to annually) to determine compliance with the income and occupancy requirements.

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

H. The review of occupancy reports is documented by completing the Report of Bond Review form and uploading that form and the Occupancy Report to the assigned business system.

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

J. Use the current published program limits posted to the Program Income Limits website for determining income eligibility for the Loan programs.

Unconventional Loans - Taxable Bonds for Transitional/Bed/Special Needs Facilities

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

Properties with unconventional loans will be monitored according to the terms and requirements in the Virginia Housing Regulatory Agreement.

Unconventional Loan Annual Reporting: Upon request of the assigned Compliance Officer, Owners are required to complete and submit annually an Income Occupancy and Certification Report (ES-01) certifying that no person has moved in with income exceeding the overall income limit specified in the commitment or regulatory agreement.
The annual Unconventional Loan report must:

a. Must reflect occupancy as of Dec. 31st of each year and must be submitted to Virginia Housing by Jan. 31st of the audit year.
b. will be uploaded to ProLink following the established procedures.

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

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

Tax Exempt Bond Financing, 4%

Properties with tax-exempt bond financing carry income and occupancy restrictions mandated federally. The income restrictions are referred to as set-asides. Tax-exempt loans in the Virginia Housing portfolio have a unit limitation at 150% of the median income, not adjusted for family size. The 150% AMI limitation is not a federal rule and is required by Virginia Housing regulations to house moderate-income households.

Federal regulations require that the minimum set aside be maintained continuously throughout the loan term. The minimum set aside must be met for:

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

To initially document the minimum set aside, Virginia Housing will accept the Tenant Income Certification (TIC):

- for Section 8 assisted households within 1 year prior to bond closing
- at move-in or initial qualification (that is, supported by third-party verification of income) **or**,

  for prior Housing Tax Credit, Tax-Exempt bond or Assisted properties, a TIC from a full annual recertification (i.e., supported by third-party verification of income), any of which must be signed within 120 days prior to bond closing
- TIC at move-in or initial qualification signed within 60 days post-loan closing

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

Tax-Exempt Bond-only properties without LIHLIHTC are audited annually. All other properties funded with Virginia Housing-issued tax-exempt bonds (including those combined with tax credits or other funding) are audited on site at least every three years.

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

A. Tenant data must be submitted to Virginia Housing using the Procorem online Tenant Portal

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

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

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

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

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

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

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

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

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

K. The assigned Compliance Officer is responsible for ensuring that changes in ownership entities, management and site contacts are updated promptly in the Procorem online Tenant Portal and ProLink.

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

<u>Tax Exempt Bond and Taxable Bond or MUMI</u> (combined properties)

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

<u>Tax Exempt Bond Financing – 501(c)(3) Rules</u>

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

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

- Either 20% @ 50% or 40% @ 60% minimum set aside and
- 75% of the units rented to households at 80% of median income AFS (remaining 25% may be market)

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

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

Low-Income Housing Tax Credit Properties

Properties with the low income tax credit allocation carry income and occupancy restrictions mandated federally. Federal regulations require that the minimum set aside be always maintained throughout the Extended Use Period (Post Year 15). Compliance monitoring follows the term and requirements in the Extended Use Agreement (EUA).

File audit and physical inspection - pursuant to IRC 1.42-5 and **Federal Register Document 2019-03388**the housing credit monitoring agency (Virginia Housing) must conduct the initial on-site inspection and file audit for a LIHTC property by the end of the second calendar year following the year the last building in the project is placed in service and at least once every three years thereafter.

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

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

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

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

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

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

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

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

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

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

C. General Audit Practices for LIHTC Properties:

When performing Tax Credit file and unit inspections, the Compliance Officer monitors for compliance with:

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

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

c. Habitability – the units and common areas have no violations of the National Standards for the Physical Inspection of Real Estate (NSPIRE).

Full-time student households may only reside in a tax-credit qualified unit if they meet one of the five exceptions explained in IRS regulations.

Tenant data must be submitted to Virginia Housing using the Procorem online Tenant Portal (Procorem online Tenant Portal) software system.

A. The LIHTC Extended Use Period (Post Year 15)

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

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

A property information report and compliance monitoring fee are due to Virginia Housing annually and the owner must annually complete and submit the Owner's Certificate of Continuing Program Compliance, (aka Annual Owner's Certification (AOC)report).

Tenant data must continue to be submitted to Virginia Housing using the Procorem online Tenant Portal.

File audit in extended use period – Compliance Officer completes a desk audit every three years using the tenant reports from the Procorem online Tenant Portal.

Physical inspection -

- if LIHTC only or if combined with a Virginia Housing loan, complete physical according to Asset Manager risk criteria which would include an on-site physical inspection of up to 5 vacant units by Asset Manager or Compliance Officer at least every 3 years
- if LIHTC only and property is subject to RD/HUD inspection, then Virginia Housing physical discontinued. When the physical is discontinued Compliance Officer:
    - makes Active Note in ProLink
    - creates a Note to File in the Procorem online Tenant Portal
    - uploads form to ProLink reflecting the physical discontinuation policy and year discontinued

Change in Ownership: Upon notification of a change, the Rental Compliance Data Officer updates the owner and management contact information into ProLink, and the assigned regional team is responsible for updating the owner, management and property contact information in ProLink. Whenever there is a change in ownership or management agent, Virginia Housing reserves the right to conduct a file review within 90 days after the change to assess the new entity's understanding and implementation of program requirements. Changes in ownership entities, management and site contacts are updated promptly in the Procorem online Tenant Portal and ProLink.