

# CHAPTER 5

## COMPLIANCE AND ASSET MANAGEMENT

### Section 500 Purpose

All real estate finance portfolios must be actively managed to protect their root source of capital, and to ensure that the investments made with that capital are advancing the intended purposes. The Housing Trust Fund portfolio is no exception.

Housing Trust Fund money is specifically mandated to assist low and very low-income citizens in meeting their basic housing needs. Therefore, care is taken to invest Housing Trust Fund dollars in projects that serve households with low incomes, often with special needs, and provide appropriate and well-maintained housing for many years.

The Asset Management Team is responsible for monitoring all projects that have been Placed in Service. Monitoring consists of a combination of desk monitoring and on-site visits that help inform stakeholders as to whether or not the invested dollars are yielding what is expected. Asset Managers regularly monitor:

- The demographics and income eligibility of the residents;
- The vacancy rates of the units;
- The condition of the properties;
- The financial status of the individual projects; and
- The financial status of the property owners.

In monitoring projects, the goal of the Asset Management Team is to ensure that projects are providing safe and affordable housing to our State's vulnerable persons. As well, in doing this monitoring it is our intention to prevent potential compliance issues by working proactively with organizations. We also help organization's address changing conditions and provide technical assistance where appropriate to ensure the long-term viability of Housing Trust Fund projects. The nature of these projects requires a strong and positive relationship between the State and contractors.

**Desk monitoring** primarily consists of reviewing annual reports, audited financial information, and tracking payment history. Submission of timely, complete, and accurate organizational **financial audits**, project **annual reports** and **certificates of proof of insurance** are the primary documents used by asset managers to determine compliance. **Payment history** is also tracked and incorporated into the overall assessment of contract compliance.

**On-site monitoring** is a critical aspect of compliance and asset management. On-site inspections of files and property condition take place regularly for all projects in the portfolio. The frequency of on-site visits depends on the funding source for the project as well as information gained from review of the annual report. Coordination between public funders will occur for desk and on-site monitoring activities. This may include sharing annual report information and sharing on-site monitoring duties and reports.

Contractors may be deemed **out of compliance** with the terms and conditions of their funding for a variety of reasons outlined in this chapter. Asset Managers will assess the seriousness of the compliance issue and determine an appropriate course of action. Providing technical assistance, creating a workout strategy, or in the worst case, foreclosure, are tools available to Asset Managers when working with contractors on compliance issues. Decisions are based on

weighing risks to tenants or the housing portfolio against the monetary or time costs of pursuing action against contractors.

**Housing Division responsibilities during the term of a contract include:**

- Monitoring project performance,
- Providing technical assistance and training,
- Working with property owners to adjust to changing conditions, and
- Enforcing terms of written agreements, up to and including all avenues of recourse.

**Contractor responsibilities during the term of a contract include:**

- Providing a timely and complete annual report for every project that is Placed in Service,
- Providing yearly audits and certificate of proof of insurance,
- Making payments per contract terms,
- Communicating with the Division about any changes that may impact the original agreement and/or ability to continue to provide affordable housing as outlined in the contract,
- Cooperating with on-site monitoring, and
- Participating in workouts or technical assistance strategies.

## **501 Monitoring Housing Contractors**

### **501.1 Desk Monitoring**

#### **501.1(a) Annual Reports**

The Combined Funders Annual Report is the primary tool used in monitoring the viability and stability of our portfolio's housing projects. The annual report was created in combination with other public funders such as the City of Seattle, King County and the Washington State Housing Finance Commission. The report meets the needs of all participating funders. The report must be submitted separately to each funding source. **The Annual Report is due to Commerce's Housing Division no later than June 30 each year.** The annual reporting period is for the calendar year beginning January 1st and ending on December 31st. **Submitting annual reports is an important term and condition of your contract.**

- Failure to submit an Annual Report will result in the contractor being **out of compliance** with the terms and conditions of their funding;
- Incomplete reports will not be reviewed and contractors will be asked to re-submit a completed report. Failure to re-submit the report after being contacted means the contractor is **out of compliance** with the terms and conditions of their funding;

**NOTE: Failing to comply with contractual obligations related to submitting timely, accurate and complete Annual Reports may result in a project being prioritized for an onsite inspection.**

#### **Assessment Criteria**

Asset Managers assess annual reports for project viability and financial stability of the organization. Key elements of this assessment include:

- Whether low income and special needs populations are being served
- Project occupancy level
- Whether tenants are income eligible

- Project cash flow
- Project income and expenses
- Project or Organizational operating and replacement reserves

**NOTE: Contractors are encouraged to explain in their reports any unusual circumstances. Generally, adequate explanations can reduce the need for additional follow-up.**

### **Follow-up**

Follow-up may be conducted on both project-specific and organizational concerns identified through Annual Report review. Follow-up will be prioritized using specific criteria including project category; an organization's current HTF program status, and the number of HTF funded projects in an organization's portfolio.

Best efforts will be made to follow-up with organizations based on the volume of current workload in each of the following project categories:

- **In Compliance:** Projects with Annual Report submissions that do not require additional inquiry will receive a letter to inform them their annual report was received, reviewed and they are in compliance.
- **Inquiry of Concerns:** Asset Managers follow-up on Annual Report submissions that display the following concerns:
  - Failure to submit an Annual Report or poor quality of data submitted;
  - Inaccurate data;
  - Low occupancy rates;
  - Questionable tenant eligibility;
  - Zero or negative cash flow; or
  - Inadequate reserves.

**NOTE: Applicants for HTF funding rounds that have active projects in the HTF portfolio will be prioritized for follow-up if any of these issues are present in their Annual Report.**

- **Tracking:** Projects may be tracked for an additional year if Asset Managers are concerned about a projects viability or organizational capacity. Project tracking may occur for the following reasons:
  - It is the first year of an annual reporting requirement;
  - Did not submit a complete annual report; or
  - Submitted an annual report with major concerns identified.

### **501.1(b) Records and Payments**

As stated in housing contracts, organizations are required to submit **audits and proof of insurance** annually. Audits submission is required no later than nine months after the end of the contractor's fiscal year. Contractors should consult their specific contract's terms and conditions regarding the required types and amount of insurance coverage. Contractors failing to provide audits or current proof of insurance will be **out of compliance** with the terms and conditions of their funding. See Section 506 for information about an Audit Requirement Waiver and for more information about insurance coverage.

Asset managers are responsible for tracking the status of payments. Contractors are encouraged to contact their asset managers if they cannot make their payments or will be late making payments. Contractors that fail to make their payments and do not contact their asset manager are considered delinquent. If a contractor is pursuing a **workout**, their payments may be

suspended during the course of the **workout**.

### **501.1(c) Organizational Reviews**

Organizations with **five or more projects** in the state portfolio may undergo an organizational review, which will include assessing all of the organization's annual reports together and reviewing audited financial information. The purpose of these reviews is to examine an organization's capacity for long-term provision of quality affordable housing projects. Organizations with a large number of projects can represent a significant risk to the portfolio and every effort will be made to support their continued ability to provide housing. Technical assistance will be provided to help organizations understand their projects from a portfolio management standpoint and to advance their understanding of quality management practices and important market conditions.

Organizational reviews are also conducted for the Resource Allocation Team to report on contractor's capacity, portfolio history, and financial position. This information is incorporated into resource allocation decisions.

### **501.2 On-site Monitoring**

On-site monitoring is an important part of ensuring that housing projects are well managed. The purpose of on-site monitoring is to assess the physical condition of the property or place the project in service. The following information pertains to rental properties only, homeownership programs are not covered by this section, please see Chapter 8, Homeownership for monitoring of Homeownership programs.

A portion of site visits may include time spent reviewing documents and policies and procedures to gain an understanding of how the agency functions or as follow up to the Placed in Service visit. Reviewing policies and procedures will usually involve "testing" a sample of **tenant** files to see how the organization would handle particular cases. Several in-house practices are likely to be tested including income certification, calculations of income and **rent** limits, and general file management and organizational best practices.

The second purpose of on-site monitoring is met by a physical inspection of the property and a sample of funded units. Inspections of properties and units will be conducted in accordance with the standards set by the U. S. Department of Housing and Urban Development's Uniform Physical Conditions Standards. The Department of Commerce (Commerce) and other public funding sources use these standards for jointly invested properties. Commerce will use this standard as a basis for inspecting all supported housing projects. Generally, up to 20 percent of the units will be inspected, with more being included if there appears to be compliance issues.

For HOME General Purpose funded multi-family projects, with specific periods of affordability defined, monitoring visits will be scheduled in accordance with HUD requirements. On-site inspections of HOME-assisted rental housing will be conducted no less than:

- Every three years for projects of one to four units;
- Every two years for projects of five to 25 units;
- Annually for projects with 26 or more units.

After the HOME required period of affordability has expired, the project will be placed into the same monitoring cycle as the state funded projects. State funded projects will be visited no less than every 5 years. Projects with annual report concerns or organizations failing to submit annual reports will have higher priority to receive an on-site monitoring visit. Projects

requesting **workouts** or technical assistance may require on-site monitoring, or technical assistance.

On-site monitoring will be scheduled a minimum of two weeks in advance. Notice of an on-site monitoring request will be mailed to the organization. Organizations can reserve the right to reschedule if there is a conflict with the proposed schedule date. However, due to the overwhelming volume of projects needing on-site inspection, organizations are encouraged to be flexible in the scheduling of these visits. Organizations are expected to have appropriate personnel present during the monitoring visit who can answer questions regarding policies, procedures, and projects' maintenance schedules. Organizations must provide 48-hour notice to all tenants prior to a site visit.

A follow-up letter and report from Commerce will detail any findings, concerns, actions required, and recommendations, including opportunities to save energy, best practices, and other technical assistance.

If there are any findings, specific instructions will be given regarding what type of corrections the organization needs to accomplish and a deadline for those corrections. Organizations will be responsible for submitting a **corrective action plan** within 30 days and documentation of corrections to the On-Site Inspector in a timely manner. Any findings related to health and safety issues must be addressed in accordance with the Washington State Landlord Tenant Act (RCW 59.18.070). Failure to do so will mean the organization is **out of compliance**. All corrective action plans will be reviewed by the Compliance and Inspections Section to ensure they are meeting the intent of the original report. If the response does not meet the intent a second request for additional information letter will be sent, with an explanation on why the original submittal was not sufficient. In the second letter a written description of the additional information needed by the organization to meet the requirement will be provided. After a corrective action plan from the organization has satisfied the original report findings, a letter to the organization will be sent acknowledging that the response provided meets the requirements.

Recommendations offered will not require additional action by the organization. If the information, however, will benefit the project's long term, operational viability, Commerce hopes organizations will act and develop an action plan and timeline to act on recommendations.

All public funders conduct some level of on-site monitoring. To most efficiently use public resources and reduce redundancies, on-site monitoring responsibilities will be coordinated between and with other public funders where possible. Coordination can include sharing of inspection reports, on-site visits by any public funder, and joint visits by multiple funders. This coordination may be part of a formal arrangement or an informal agreement between the state and local funders.

### **501.3 Homeownership**

The Asset Management Team has created a separate annual report and review system for homeownership programs. In reviewing homeownership annual reports we are checking if homes are sold to the target population as well as examining the level of activity typically associated with the program. For additional information on Homeownership, please refer to Chapter 8 of the Handbook on Homeownership.

### **502 Technical Assistance**

The Asset Management Team is available as a resource regarding affordable housing projects, especially in aspects related to complying with state requirements. Contractors encountering difficulties are encouraged to contact their asset manager particularly when difficulties impact

their annual reports, ability to make payments, or on-site monitoring.

Technical assistance encompasses a whole range of actions, from answering questions about annual reports to determining need for changes to contract terms and conditions. Referrals to outside contacts may be made for specific property or fiscal management issues.

When a contractor is receiving technical assistance, compliance issues with annual reports, payments, or on-site monitoring will be incorporated into the technical assistance process. If the contractor has been notified that they are **out of compliance** with the terms and conditions of their funding an asset manager will work with them to develop a technical assistance strategy. The ultimate results of such a strategy could be amendments as discussed below. If a project or contractor fails to respond to communication attempts or by not providing necessary documentation, asset managers will assess the project's risk to the portfolio and conduct a cost benefit analysis of pursuing more serious actions.

### **503 Workouts**

The Asset Management Team will work to proactively address problems arising with housing contracts after being **Placed in Service**. The team acknowledges, given the long-term contract relationship and the changing nature of market conditions, that adjustments to contract terms and conditions may be needed. Asset Managers will work with contractors to address these issues.

If a project is encountering difficulties that might involve changes to the housing contract, the contractor is encouraged to contact their asset manager to determine what type of intervention might be needed. Each project and amendment is unique. Specific details of each amendment will be negotiated. When a project is in the process of changing terms and conditions it is referred to as a "**workout**". Below are general definitions and criteria to be used as guidelines. Additionally, Asset Managers may recommend **workouts** upon review and assessment through desk or on-site monitoring.

When determining the need for **workouts**, the asset manager will evaluate benefits to the state portfolio as well as benefits associated with preserving affordable housing options. This will be particularly true if the organization is providing affordable housing in locations with few affordable options.

Any workout that includes amendments or restated legals may involve updates to the overall contract including possible changes to terms and conditions.

Once a **workout** category and strategy are chosen, the contractor is responsible for contacting the state in writing to formally request a **workout**. If requests are sent during times of heavy workload for the unit, such as during a funding round or annual report review, processing of requests will likely not begin until other workload priorities are completed. Workout requests are prioritized based on critical timing, risk assessment, and other public funders' involvement.

Upon receiving a written request, asset managers will work to develop the necessary paper work to address the **workout**. If the request is denied, the contractor will be notified and a secondary strategy will be developed. **Please note that the Asset Management team reserves the right to deny any request for amendment that does not meet criteria.** If an amendment proposal is denied, the asset manager may make a secondary recommendation. If a project or contractor fails to participate in the **workout** process by not responding to unit communications or by not providing necessary documentation, asset managers will assess the projects risk to the portfolio and conduct a cost benefit analysis of pursuing more serious actions.

## 503.1 Workout Categories

### 503.1(a) Sale of Property

**Definition:** Under certain circumstances the sale of property on the open market may be approved and any obligation for providing affordable housing at this site will be released. Circumstances may include:

- End of useful life/structural issues
- Neighborhood issues/concerns/fit
- Demographics have changed/Target population no longer needs housing
- Organization no longer has capacity to provide housing
- Changing market conditions

**Process and Timelines:** Asset Managers must approve any sale. Repayment will be based on contract terms and conditions and may include shared appreciation. Upon repayment necessary legal documents will be released. Sale of property will involve an amendment to the current contract. Some contracts may allow proceeds from the sale of this property to be reinvested in another eligible project. (See Section 2 regarding eligibility) The Asset Manager and contractor will need to negotiate specific benchmarks and timelines to complete this process. Timelines will be dependent on project complexity.

#### **Criteria:**

- Contractor can no longer provide housing
- Cannot secure qualified tenants
- Selling property and recovering funds back to the Division costs less than trying to maintain current housing option. This analysis involves a cost benefit analysis between rehabilitation costs and current property value.
- Selling the property and recovering funds may be a higher and better use with appreciated properties.
- Location and type of housing may not be appropriate for specific client type.

#### **Specific Reinvestment Criteria:**

- Proposed projects must meet eligibility requirements;
- The length of commitment will restart when new site is Placed in Service;
- New contract or update of old contract through amendment will be required; and
- Any projects requesting additional funds for a new site will be required to compete for those funds in the competitive funding rounds.

#### **Information required from requesting organization**

- Justification from organization regarding inability to provide housing
- Current property value (may need to be evaluated through a variety of techniques)
- Current property condition
- Costs for rehabilitation of property or demolition/rebuild

### 503.1(b) Transfer of Ownership

**Definition:** Under certain circumstances properties may be transferred to other eligible organizations for eligible activities with assumption of underlying Housing Trust Fund or HOME investment. (See Section 2 regarding eligibility requirements) New owners will be required to comply with specific contractual obligations to be negotiated with the Asset Manager.

**Circumstances for transfer may include:**

- Organization no longer can or wants to provide housing
- Target population has changed, new population does not fit mission
- Market conditions have changed, subsidies no longer available

**Process:** Organization must complete an Application for Transfer of Ownership. ([See exhibit 5-1](#)) Eligible organizations must meet application criteria. Eligible organizations may be recommended by the current contractor or an Asset Manager. Transfer of ownership may entail purchase and sale agreement, assignment and assumption agreement and other documents as necessary. The Asset Manager and contractor will need to negotiate specific benchmarks and timelines to complete this process. Timelines will be dependent on project complexity.

**Old Organization Criteria:**

- Organization can no longer provide housing
- Subsidies are no longer available
- Cannot secure qualified tenants

**New Organization Criteria:**

- Organization is able to pass new applicant criteria, including:
  - Eligible Organization
  - Eligible Activity
  - Fiscal Soundness
  - Staff Skills and Experience
  - Board Composition

**Information required from requesting organization:**

- Justification from organization regarding inability to provide housing
- Information regarding changes in market condition:
  - Decrease in subsidy availability
  - Changes in target population
- Current property value (may need to be evaluated through a variety of techniques)
- Current property condition
- Status of reserves, if any

**503.1 (c) Loan Restructuring**

**Definition:** Under certain circumstances, projects may need a change in award terms to reduce their financial burden.

**Circumstances may include:**

- Changes in overall market conditions (low housing prices or rents)
- Changes in target population
- Decrease in available subsidies

**Process:** Organizations will need to prove financial hardship related to current loan terms. Amendments reflecting new loan terms will need to be made to relevant legal documents. The Asset Manager and contractor will need to negotiate specific benchmarks and timelines to complete this process. Timelines will be dependent on project complexity.

**Criteria:**

- Project serves 30 percent area median income or
- Project provides service enriched housing to special needs population
- Project is dependent on other funding/subsidies for operating support
- Market conditions have changed substantially from original project projections
- Short-term inability to meet loan terms

**Information required from requesting organization:**

- Justification from organization regarding inability to meet current loan terms
- Detailed information regarding projects financial performance, including status of operating and replacement reserves if any
- Organization's financial capacity
- Current property condition
- Target population or changes within it
- Current operating support and long-term viability of that support
- Other actions taken to address financial situation
- Pro forma demonstrating organization's capacity to meet proposed loan terms.

**503.1(d) Contractor Portfolio Restructure**

**Definition:** This category primarily applies to organizations with five or more projects in the state portfolio. This category may include pursuing other **workout** categories as solutions for different projects.

**Circumstances can include:**

- Organization primarily operates in one geographical location and all properties are experiencing difficulties due to changing market conditions.
- Organizations target population is changing.
- All or most of the projects meet loan-restructuring criteria, which is causing financial hardship.
- Organization can prove that helping one or more projects will help the entire portfolio.

**Process:** Asset Manager will work intensively with organization to provide technical assistance. Organization and Asset Manager will pursue all possible solutions to challenges faced by organization's projects, including training regarding best management practices and review of properties to assess the viability and marketability of any individual property. Specific processes, timelines and benchmarks will be negotiated between contractor and Asset Manager.

**Criteria:**

- Organization has multiple struggling projects
- Projects are struggling for similar reasons
- Project requiring workouts meet criteria for those workout categories
- Assisting any project will help the organizations overall viability

**Information required from requesting organization:**

- Assessment of financial hardship on the organization and relative viability of each of the projects;
- Overall portfolio assessment detailing how projects work together and overall portfolio management practices;

- Conditions of properties;
- Review and assessment of capital and operating reserves;
- Evaluation of operating expenses;
- Review and assessment of organization's management model;
- Consideration and review of properties to assess the viability and marketability of any individual property;
- Assess capital improvements that could reduce operating expenses;
- Assess impact of private debt to consider possible debt reduction if evidence of project specific impact and overall impact to the organization's portfolio.

### **503.1(e) Request for Additional Funds**

**Definition:** The owner of a project that has been **Placed in Service** may request additional HTF funds when additional capital funds are desirable or necessary for the project to continue in operation. Only eligible activities will be considered including rehabilitation.

#### **Circumstances may include:**

- Aging of the property and capital needs issues are not covered by reserves.
- Energy and sustainability measures would improve overall operating efficiency, decrease tenant paid utility costs, or increase project financial viability.
- Health and Safety issues need to be addressed.
- Other reasonable expenses with a positive public benefit need to be implemented.

**Process:** Contractor must complete an amendment request/application for additional funds. [\(See Exhibit 4-8.\)](#) Official release of funds and necessary changes to legal documents will be needed. The Asset Manager and contractor will need to negotiate specific benchmarks and timelines to complete this process. Timelines will be dependent on project complexity.

#### **Criteria:**

- The organization cannot complete necessary work on project without additional funds.
- The property requires work to maintain decent and safe housing.
- Additional funds will only be released through this process to projects that are maintaining units, or project is currently vacant and cannot get occupancy without additional funds for rehabilitation or relocation.
- Additional funds will only be released where necessary to preserve original investment. Any projects requiring funds for expansion of existing project need to apply through the competitive funding round.
- This process is only available for **Placed in Service** projects. All projects in development must contact their Contract Manager. (See Section 4)

#### **Information required from requesting organization:**

- Justification for additional funds
- Current property value
- A current comprehensive Capital Needs Assessment including any needed health and safety repairs, immediate system repair or replacement, and a life cycle cost analysis of the building systems with a 20-year replacement schedule and replacement reserve recommendation
- Cost-benefit analysis of additional rehabilitation versus a demolition/rebuild when

- the cost per square foot for improvements approaches new construction costs
- Current operating and replacement reserve balances
- The current operating budget, a new operating budget based on after-construction status with replacement reserve recommendation included, and a development budget, all in HTF format with a narrative explanation of each line item
- A comprehensive scope of work with a detailed construction cost estimate for the project
- A current title report and property profile showing all liens and easements
- A financing plan that includes other possible funding sources or reasons that they are not available
- Letters of commitment from other funding sources
- A proposed set of terms and conditions for all HTF capital investments (existing and new) that includes a proposed amortization schedule for repayment of the funds, or a written justification for a grant or deferred loan consideration.
- A site inspection by Commerce staff may be necessary
- The asset manager may require other additional relevant information

### **503.1(f) Minor Scope of Work Changes**

**Definition:** This category represents small changes in a project's original scope of work. Several circumstances may necessitate such changes including:

- Change in number of units (creation of common areas, resident manager apartment)
- Change in contractor's organizational structure or name
- Changes in target population

**Process:** Asset Managers must determine if proposed changes meet eligibility requirements for activities or organizations. Changes in relevant legal documents will be necessary. Some changes to contractor structure may require an assignment agreement. The Asset Manager and contractor will need to negotiate specific benchmarks and timelines to complete this process. Timelines will be dependent on project complexity.

#### **Criteria:**

- Organization cannot secure qualified tenants
- Organization's structure or name has changed

#### **Information required from requesting organization:**

- Justification for revised scope of work
- Current property condition
- Market information regarding target population
- Proof of changes to organization structure and name
- In case of organization merger, proof of new organizations eligibility

### **503.1 (g) Refinancing and Subordination**

**Definition:** Contractors may request to refinance private senior debt that is secured by the Property. The Department will require review and approval of private lenders' loan documents and subordination agreements, prior to refinancing. Such approval shall be at the Department's sole discretion and will not unreasonably be withheld. The Department's preference is to subordinate to non-callable, competitive fixed rate, fully amortizing, level payment private debt.

**Reasons for refinancing may include, but not be limited to the following:**

- Market conditions or loan pay-down may have increased the equity that could be captured and put to use.
- The project may need repairs or rehabilitation.
- The contractor may get a better interest rate.
- The contractor may want to pay-down or pay-off other loans on the project including the Department's loan.

**Process:** Contractors will need to submit a written request documenting their proposed plan and how it will enhance the project, the organization, and provide public benefit. Staff will evaluate the proposal, seek additional information if needed, and make a recommendation to the Department's management.

**Criteria for Department approval includes but are not limited to the following:**

- The extent to which improvements are made to the property through repair, rehabilitation, or other capital improvements;
- The extent to which improvements are made to the debt handling capacity and/or the cash flow of the project;
- The extent to which the state's lien position is improved;
- The extent to which the state's loan is reduced or paid off.
- The extent to which additional public benefit is achieved
- The extent to which there is increased risk to the state's original investment.

**Information required from requesting organization:**

- A complete and thorough description of the proposed refinance.
- A description of the organization's financial capacity and how this proposal will affect that.
- A description of the project's financial capacity and the implications of this proposal.
- Proposed new operating budget and a development budget with cost estimates, if applicable.
- Current status of operating and replacement reserves.
- Justification for the proposal based upon the criteria stated above including how the public benefit will be achieved.
- Additional information may be required based upon staff review.

This is not the mechanism by which repairs will usually be accomplished. It is expected that replacement reserves are included in the operating budget and deposited into an interest bearing account. The amount of these reserves needs to be consistent with a life cycle cost analysis of building systems. Routine maintenance should also be covered by line item set-a-sides in the operating budget.

**503.1(h) Year 15 Expiring Tax Credit Projects**

Contractors with tax credit projects nearing the end of their 15-year compliance period are requested to contact Asset Management as they begin planning the project's exit strategy. The asset manager will work with you on any issues that arise during the disposition process. When the exit strategy is finalized the contractor is requested to submit a letter to Asset Management outlining the exit tax liability and the new ownership structure. Department consent and approval of the final plan will be required. It is the Department's hope the project will be sold to the nonprofit general

partner/sponsor and continue serving low-income households in accordance with the HTF contract. In some cases it may be necessary to amend HTF legal documents to reflect the new ownership structure.

## **504 Foreclosure**

After pursuing other avenues of recourse, it may be necessary to foreclose on an organization's property. These foreclosures represent the Housing Trust Fund unit's ultimate responsibility, which is to protect the State's interest. This interest is secured by placing liens on any property purchased or constructed with state funds. These liens provide the State with final recourse through the foreclosure process. Foreclosure is a legal process, which will be conducted in conjunction with the Attorney General's Office and is governed by RCW 61.24. Under some circumstance, foreclosure proceedings may be initiated by a different funder, at which point the State would coordinate foreclosure activities with this funder.

## **505 Contract Closeout**

All contracts have an end date and at that time a contract closeout will take place. Contract closeout does not require the contractor to stop providing affordable housing. The Housing Division encourages projects to continue serving target populations after the state contract has ended.

In order to close out an HTF contract that has completed its commitment period, the state must determine if money is owed to the state and release documents related to the property.

The contractor will be notified in advance of the completion date. It is the contractor's responsibility to notify the state if a continuation of the contract is desired. If the contractor does not contact the state or they wish to go ahead with contract closeout, then all documents will be released, any outstanding issues resolved and the contract will be closed out. A letter will be sent to the contractor when the contract has been officially closed out.

### **505.1 Loan Re-Deferral Process**

Contracts with deferred loans, i.e., lump sum payments due at the end of the commitment period, may be considered for re-deferral under certain conditions. The contractor should submit a request letter and current capital needs assessment to the Asset Management Team. The asset manager will evaluate benefits to the HTF portfolio as well as benefits associated with preserving affordable housing. Staff will seek additional information if needed and make a recommendation to the Department's management.

If the request for re-deferral is approved, the HTF contract will be amended to reflect the revised end date and any other revised terms and conditions. It may be necessary to amend or execute other legal documents such as a promissory note, deed of trust and low income housing covenant agreement.

## **506 Audit and Insurance Requirement**

### **506.1 Audit Requirement**

Contractors are responsible for submitting a copy of their organization's annual audit to Commerce within nine months after the organization's fiscal year end date. Responses to any unresolved management findings and disallowed or questioned costs shall be

included with the audit report. The contractor must respond to Commerce's requests for more information or corrective action concerning audit issues within thirty days of the request.

Per Commerce's Internal Auditor, the threshold for an A-133 audit requirement is currently \$500,000 of federal money expended (or a combination of expenditures and loan balances); a Single Audit is required if an organization expends or maintains loan balances of \$500,000+ in state provided funding; and if an organization receives or maintains loan balances of less than \$500,000 in state funding then a Financial Statement Audit (sometimes referred to as "regular" audit) should be submitted to Commerce on an annual basis.

Payment for the audit is the responsibility of the organization. Audits are to be performed by a Certified Public Accountant (C.P.A.) independent of the organization being audited. If the Contractor is a state or local government entity, the State Auditor's Office shall conduct the audit. Compilations and Reviews are not the same thing as an Audit. Contractors failing to provide an audit on an annual basis will be **out of compliance** with the terms and conditions of their funding.

## **506.2 Audit Requirement Waivers**

In the event that an organization is eligible for an audit requirement waiver, a written request must be submitted to Asset Management. Asset Management has total discretion to grant and revoke the audit waiver.

### **Audit Requirement Waiver Criteria**

- An organization with 3 or fewer contracts with HTF funding **and** a total HTF portfolio debt below \$500,000 is eligible for an audit requirement waiver;
- Organizations that have 4 or more contracts with HTF funding **or** exceed a total of \$500,000 in funding from the HTF are not eligible for an audit requirement waiver;
- Organizations that have projects with Tax Credit funding, HOME funds or are funded by HUD are not eligible for an audit requirement waiver.

### **Audit Requirement Waiver Request Process**

The organization must submit a letter to Asset Management on official letterhead to request an audit requirement waiver.

- The letter should state the organization's eligibility as it relates to the above eligibility requirements;
- The letter must be signed by the Chief Financial Officer (or equivalent finance/accounting position) **and** the Executive Director;
- The letter must include the following language:  
**"In receiving an audit requirement waiver, I agree to submit to the Housing Trust Fund a compiled yearly financial statement that includes organizational financial information and financial information pertinent to the properties held by the organization with HTF funds. The audit requirement waiver becomes void at any time when the organization exceeds the eligibility requirements or does not comply in submitting the yearly financial statement."**

### **Required Criteria of the Financial Statement**

- The statement can be created in-house or by an independent accounting firm;
- The statement will include financial data beginning and ending in the organization's fiscal year;
- The statement is due to Asset Management within ninety days of the fiscal year end.

### **506.3 Insurance Requirements**

#### 506.3(a) Property Insurance

The contract shall keep the building and all other improvements on the premises insured throughout the term of the contract against the following hazards:

- Loss or damage by fire and such other risks (not included earthquake damage) in an amount sufficient to permit such insurance to be written at all times on a replacement cost basis;
- Loss or damage from leakage or sprinkler systems now or hereafter installed in any building on the premises;
- Loss or damage by explosion of steam boilers, pressure vessels, oil or gasoline storage tanks or similar apparatus now or hereafter installed in a building or building on the premises.

The Department of Commerce shall be specifically named as **loss payee** on all policies, and all policies shall be primary to any other valid and collectable insurance. In the case of homeownership revolving loan fund projects, this insurance may be in favor of the contractor.

#### 506.3(b) Public Liability Insurance

The contractor shall at all times during the term of the contract, at its cost and expense, carry and maintain general public liability insurance, including contractual liability, against claims for bodily injury, personal injury, death or property damage occurring or arising out of services provided under the contract. This insurance shall cover such claims as may be caused by any act, omission, or negligence of the contractor or its officers, agents, representatives, assigns or servants. The limits of liability insurance, which may be increased from time to time as deemed necessary by the Housing Trust Fund, with the approval of the contractor (which shall not be unreasonably withheld), shall not be less than \$1,000,000 each occurrence and \$2,000,000 general aggregate. The Department of Commerce shall be specifically named as an **additional insured** on all policies.

Contractors should consult their contract's terms and conditions regarding the required types and amount of insurance coverage. Contractors failing to provide current proof of insurance on an annual basis will be **out of compliance** with the terms and conditions of their funding.