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Concentrating in Municipal Bonds,
Local Government Law, Economic
Development Incentives,
Affordable Housing Development

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Low Income Housing Tax Credit Program
South Carolina State Housing Finance and Development Authority
300-C Outlet Point Blvd.
Columbia, SC 29210
Attn: Kim Wilbourne, LIHTC Manager

Re: 2024 QAP Bulletin and 2025 QAP Draft; Treatment of TEB Collateral Account
Income as Eligible Funding Source (Not Income Generated by a Property)

Ms. Wilbourne:

[REDACTED] in the recent 2023 TEB LIHTC round as a result of listing "TEB Collateral Account Income" as a funding source in their Low-Income Housing Tax Credit / Tax Exempt Bond Applications. We understand SC Housing deemed this cash collateral account income as "income generated by a property during the construction or rent up period", and, consequently, the TEB Collateral Account Income was deemed an ineligible funding source pursuant to the 2023 Qualified Allocation Plan, Section O, Financial Underwriting, Item 9, Funding Sources, which states that "Income generated by a property during the construction or rent up period may not be used as a funding source." We think this position needs to be reconsidered going forward.

We respectfully request that SC Housing issue a Bulletin for the 2024 QAP in advance of the TEB round and add a sentence to the draft 2025 QAP specifically permitting this TEB cash collateral account income as an eligible funding source for the following reasons:

1. Virtually all TEB LIHTC deals require fully funded cash collateral accounts during construction

All 4% bond transactions involving Fannie Mae, Freddie Mac and most HUD loans require a structure with the fully funded bond proceeds being deposited into a cash collateral account held in trust by a bank trustee solely for the benefit of the bond holders. Undisbursed funds are invested by the bank trustee in interest bearing investments with construction draws being funded from this account during the construction period. The income generated by these TEB Collateral Accounts reduces the financing costs of the project, is directly related to the financing structure, and is totally unrelated to the

operations of the property. Therefore, we believe TEB Collateral Account income should be counted as an eligible funding source and not be counted as income generated by the property.

We understand that the practice of some developers may be to simply net out the expected interest income against the expected interest expense and not show the interest income as a separate funding source. We believe it would be in everyone's best interests to have a level playing field and to be consistent in how these bond financing structures are presented in the LIHTC TEB applications going forward.

2. There is little interest rate market risk in counting expected TEB Collateral Account Income as an eligible funding source as interest expense and interest income rise and fall in tandem, minimizing any potential funding gap.

We understand that one business underwriting issue with counting the TEB Collateral Account Income as an eligible funding source is with its perceived market risk being dependent upon the fluctuating interest rate environment at the time of construction rather than what is anticipated at the time of application. However, the interest rate paid on the cash collateral and the interest rate charged on the construction loan move more or less in tandem, with a fairly consistent spread, so that whether interest rates rise or fall during the time between the application and bond closing, the financing costs are not materially changed. In other words, if interest income drops as the result of lower interest rates on the investments in the construction fund, interest expense on the bonds funding the construction fund also drops. The exact same interest rate risk applies to both the expected interest expense and the expected interest income. Unlike the recently experienced rapidly increased construction cost risk in 2021 and 2022, SC Housing is not having to underwrite a potential project funding shortfall whether interest rates rise or fall.

RECOMMENDATIONS

The 2024 QAP needs a new Bulletin stating that "TEB Cash Collateral Income, if any, must be stated as a line item in funding sources, and not netted against interest expense. A waiver request will not be needed as SC Housing will no longer consider such interest income required by the bond financing structure as having been 'income generated by the property'."

The 2025 QAP needs a new sentence at the end of Section O, Financial Underwriting, Item 9, Funding Sources, as follows: "Cash collateral account income, if any, is not considered to be 'income generated by a property'."

Thank you for your consideration.

Sincerely,



Howell Linkous & Nettles LLC