

MEMORANDUM

TO: Management Agents and Certified Public Accountants

FROM: Thomas F. Wolf, Portfolio Manager

DATE: January 1, 2016

SUBJECT: Procedures for Implementing MassHousing's Equity Policy

In order to be consistent with the way the Department of Housing and Urban Development (HUD) and other state housing agencies calculate permissible distributions to equity owners, the Agency has developed the following Procedures for Implementing MassHousing's Equity Policy. Under these procedures, to be eligible to make a distribution, the development must be able to demonstrate that it generated either in this year, or prior years, sufficient Net Available for Equity (as defined on line 80 of Form F.C.-1) to justify a distribution, and that it has Funds Available for Distribution (as defined on line 570 of Form F.C.-5).

Consequently, before a distribution can be made, all operating obligations as set forth in either Section 8, Subsections a, b, and c or Section 7, Subsections a through g, of the Regulatory Agreement must be satisfied. To this end, the Agency has developed its own interpretation of the term "available" funds.

The term Funds Available for Distribution means any unrestricted funds remaining on hand after the payment of:

- (1) Sums due or currently required to be paid under the terms of the mortgage or notes held by MassHousing (including delinquent principal and interest);
- (2) Amounts required to be deposited in the reserve fund for replacement;
- (3) Obligations of the project other than the mortgage loan, including real estate tax, insurance and special escrows;
- (4) Approved expense loans by the general partners of the development for project related costs;
- (5) Tenant security deposits which remain unfunded;
- (6) Accounts payable and accrued items (not escrowed);
- (7) Notes and advances - operating expenses, and
- (8) Deferred revenues represented by prepaid rents.

Before a development may make a distribution, the Owner must certify in writing, if required by the Regulatory Agreement, that:

- (1) It has Funds Available for Distribution, and that no obligations are more than 30 days past due;
- (2) No default, for which notice has been issued, exists under the Contract Document;
- (3) There has been no failure to comply with the Agency's reasonable requirements for proper maintenance of the project;
- (4) There are no outstanding liens or security interest on the Project's assets other than the Mortgage, unless provided for, to the Agency's reasonable satisfaction, by insurance, reserve or in a similar manner, and
- (5) The funds allocated for distribution were not derived from borrowed funds or from the sale of capital assets, except with the prior written authorization of the Agency.

Form F.C.-5, which is part of the Audit Package, is designed to quantify the two dimensions of the calculation. Part I measures the Funds Available for Distribution, after considering all potential sources and uses of available funds, and quantifies the Maximum Allowable Distribution. Part II establishes the Maximum Possible Distribution. Part III is used to gather historical information.

Developments contemplating a distribution must submit documentation and certificates to the Agency no later than March 31 (See Sample Letter). The owners of each development will still have the option of making a distribution when it is earned or allowing the funds to accumulate for the future benefit of the project. In other words, the owners could have a claim to a distribution, which was earned in the past but not distributed, at some future point in time (See Calculation: F.C.-5, line #587) if funds are available at that time.

The three-year limitation, as set forth in the (pre-2000) Regulatory Agreements, applies only in those cases where a development had in the immediately preceding or succeeding three years negative or inadequate Net Available for Equity (See F.C.-1, line #80) and is requesting to "make-up" prior or future year distributions with funds generated in a more successful operating year (See Carry back/Carry forward Calculation: F.C.-5, line #580 & #582). SHARP developments are not subject to the three year carry back/ carry forward rules and thus are deemed to have earned their Maximum Permissible Distribution regardless of the amount shown as Net Available for Distribution (See F.C.-1, Line #80). In the event that there is an extraordinary item in the current year which is readily identifiable with a prior period, the owner may reallocate the appropriate amount to the prior years in computing the three-year limitation. Nevertheless, in all cases, current obligations and payables, as outlined above, must be adequately covered by "available funds" (See Calculation: F.C.-5, line #570) before such a distribution will be allowed.

The Auditor for each development must review the calculations and provide appropriate assurances as part of the Report on Supplemental Financial Information and the Report on Compliance with the Regulatory and Management Agreements.

On July 14, 1998, MassHousing's Board approved a policy containing limitations on equity distributions. On November 9, 1999, the MassHousing Board voted to amend the Agency's Equity Policy by adding paragraphs 4A, 4B and 6A. The changes dealt with three areas:

- 1. The Percentage of Allowable Equity to be Distributed (Paragraph 4A);*
- 2. Reestablishing an Owner's Equity Base (Paragraph 4B); and*
- 3. Disposition of Equity in Excess of the Allowable Distribution (Paragraph 6A).*

The Percentage of Allowable Equity to be Distributed:

MassHousing's enabling statute (the "Act") permits a mortgagor to make distributions of 10% of equity on an annual basis. Prior to 1989, however, the statute limited distributions to 6% of equity. Accordingly, some of the Agency's loan documents provide for this lower limitation. Owners subject to the 6% equity distribution pursuant to their contract documents have, on occasion, requested that the Agency permit them to obtain a 10% distribution. Generally, we have permitted this change, subject to the owners' certification that the change does not violate subsidy rules otherwise applicable to the project. There is no clear guidance on this question, however, and there have also been occasions when consideration has been demanded as a condition of allowing the increased distribution. To clarify the matter, the following policy will govern increases in the equity distribution percentage. The policy will reflect our general practice and not require "consideration" as a condition of a change in the distribution percentage.

1. A mortgagor may not make distributions of equity in any one year in excess of ten percent of the mortgagor's equity in any development financed by the Agency. In the event that the mortgagor's loan contract documents provide for a lower distribution rate, or in the event that the Agency establishes a higher rate of distribution at a later date, a mortgagor may increase its equity distribution to the then permitted rate of distribution, provided that the mortgagor provides certification to the Agency that (a) such increase will not violate any subsidy agreement or regulation applicable to the development and the mortgagor agrees to repay any distribution subsequently deemed to violate such subsidy agreement or other regulation applicable to the development; (b) no increase in subsidy or rental charges shall be required to permit the resulting increased distribution, and (c) all current and owed-to-date Development expenses have been paid and reserves, then due or owing, have been funded. The certification required herein shall be provided to the Agency in writing by an attorney authorized to render such opinion. (Paragraph 4A)

Reestablishing an Owner's Equity Base

Determination of an owner's equity base is generally more significant than the determination of the percentage of equity to be distributed. While the policy previously voted by the Board specified how initial equity would be calculated, as well as how the equity base would be calculated subsequently during the life of the project, it did not specify when the Agency should accede to a request for recalculation of equity. The Agency has been exercising its discretion in a reasonable manner to confer the benefits of an equity base increase only on projects that provide some consideration to the Agency, generally in terms of extended affordability. The following policy codifies this position to ensure uniformity in the consideration of requests going forward.

2. In determining when Agency staff should permit a mortgagor to reestablish its equity, pursuant to the provisions of paragraph 5 herein, the Agency shall consider whether: (a) the mortgagor has made a contribution of equity to the development that is not required

under the terms of the mortgagor's contract loan documents and is designed to improve the financial and physical viability of the project in the long term; (b) the reestablishment of equity is a necessary financial incentive to the mortgagor for the purpose of preserving affordable housing that will otherwise be lost due to prepayment of the Agency's mortgage; and (c) the resulting increase in allowable equity distributions can be paid without any additional commitment of public subsidies (that are not otherwise required to support the development's operations) or other adverse financial impact on the development or on the low and/or moderate income individuals and families living there. In no event shall the Agency permit a mortgagor to reestablish its equity if the financial benefit to the owner is not, in the judgement of Agency staff, commensurate to the public benefit derived from an extension of the development's affordability or other measure designed to make the development more available to low-income persons and families, or if such benefits to be derived are outweighed by any adverse effects the reestablishment of equity may have. Agency staff shall further consider whether the mortgagors shall be granted the right to obtain a revaluation of its equity on a periodic basis, but not more than once in any five year period, or at such shorter interval as may be permitted under the Act, on the basis of the consideration provided. In permitting a mortgagor to reestablish equity, Agency staff shall impose such conditions and restrictions upon the development as are deemed necessary to effect such public benefit. Any determination made by Agency staff to permit an owner to reestablish its equity shall further be subject to the provisions of paragraph 4A herein. (Paragraph 4B)

Disposition of Equity in Excess of the Allowable Distribution

The Agency's standard current form of Regulatory Agreement provides that if an owner is unable, in any year, to make a distribution in the full amount permitted under the terms of its contract documents, it may accrue any deficiency and may subsequently pay such deficiency out of amounts in the Distribution Account that have been accumulated over any three preceding or succeeding years. While, as a practical matter, this concession has not provided significant revenue for most existing developments, the provision has increasingly become a matter of discussion in connection with new 80/20 and assisted living deals, which want to ensure that they are maximizing their ability to obtain equity returns.

While Agency staff recognizes the need to offer favorable equity provisions (in accordance with statutory restrictions) in order to remain competitive with other lenders, it is also cognizant of competing statutory mandates. Among these is the provision in section 6(c) of the Agency's Act, which provides that: "All rentals received by the mortgagor in excess of the below-market rental established for each unit shall be applied, pursuant to such regulations as MHFA shall make ... from time to time and subject to any applicable requirements of FHA or other public agency providing rental assistance ... to reduce rentals so as to make units more available to low-income persons and families.

With respect to this issue, Agency staff devised a policy, which will be applied prospectively only, to balance the owner's ability to plan for a reasonable rate of return, despite minor swings in performance, against the Agency's ability to ensure that additional excess equity is available for the purposes identified in section 6(c) of the Act. The policy is thus intended to complement the owner's ability to reach backwards or forwards, for a limited time period, to make up the difference between any equity payment to which the owner was entitled in a given year and the amount that was available for disbursement. The policy requires the owner to set up an escrow account under the Agency's control that will clearly identify the existence of equity in excess of funds that can be distributed under the Agency's policies and that will be available to the owner only for specific purposes. The following policy will govern disposition of equity in excess of the allowable distribution.

3. In the event that amounts remain in the Distribution Account, as such term is defined in the Agency's standard form Regulatory Agreement ("Regulatory Agreement"), after allowable distributions have been made in accordance with terms governing the distribution of equity set forth herein, such amounts (hereinafter "excess equity") shall be deposited in an interest bearing account maintained by the Agency, which shall be known as the "Excess Equity Account." The Excess Equity Account shall be maintained by the Agency subject to an escrow agreement (the "escrow agreement") between the mortgagor and the Agency that shall provide that funds may be withdrawn solely by the Agency upon the mortgagor's request: (1) during the term of the project, for all purposes for which development Revenues may be expended pursuant to paragraph 6 of the Regulatory Agreement (or any succeeding provision governing use of Development Revenues), subject to a determination by Agency staff that the expenditure is necessary to address the project's physical or financial needs and that no other funds are available to address such needs; (2) upon prepayment or at the conclusion of the mortgage term, to extend the affordability of units available to low income persons and families; to reduce rental charges to low income persons and families; and to provide relocation and transitional assistance to low income persons and families; and (3) at any time, to fulfill otherwise the purposes of section 6(c) of the Agency's Act. In the event that funds are not expended pursuant to the provisions of the escrow agreement, such funds shall become the Agency's funds and shall be used for increasing the supply of housing affordable to low income persons and families in accordance with the Act. The policy shall be applicable solely to developments that receive commitments from the Agency for financing under section 5 of the Act in or after December 1999. (Paragraph 6A)

Calculation of the amount of "Excess Equity" will be done in accordance with the methodology used for HUD Residual Receipts and the Form F.C.-6.

April 1, 2016

Mr./Ms.
Asset Manager
Massachusetts Housing Finance Agency
One Beacon Street
Boston, Massachusetts 02108

RE: Beacon Hill Tower
MHFA# 80-007-R

Dear Mr./Ms. _____:

On behalf of Beacon Hill Tower Limited Partnership Associates, we are requesting MassHousing's approval to distribute \$1,000,000 of the 2015 surplus cash to the partners. To the best of my knowledge, Beacon Hill Tower:

1. Has Funds Available for Distribution and that no obligations are more than 30 days past due;
2. Has no default, for which notice has been issued, under the Contract Document;
3. Has not failed to comply with the Agency's reasonable requirements for proper maintenance of the project;
4. Has no outstanding liens or security interest on the Project's assets other than the Mortgage, unless provided for, to the Agency's reasonable satisfaction, by insurance, reserve or in a similar manner, and
5. The funds allocated for distribution were not derived from borrowed funds or from the sale of capital assets, except with the prior written authorization of the Agency.

For Beacon Hill Tower Limited Partnership

BY: _____ General Partner
J. R. Ewing, III
One Louisberg Square
Boston, Massachusetts 021xx

Pursuant to the Regulatory Agreement [See Section 7(a) and 8(a)], it is recommended that the following letter, based upon an Agreed-Upon Procedure Engagement, be submitted by the auditor to the owner and included in the documentation submitted to MassHousing with the distribution request. The following is a sample of the recommended letter from your auditor.

Independent Accountant's Report on Applying Agreed-Upon Procedures

To the Partners of Beacon Hill Tower Limited Partnership
and
Massachusetts Housing Finance Agency ("MassHousing") ("Agency")

Re: Beacon Hill Tower (the "Development Project")

We have performed the procedures enumerated below to the accounting records of Beacon Hill Tower Limited Partnership (the Partnership), which were specified and agreed to by the General Partner of Beacon Hill Tower Limited Partnership and in accordance with the Agency's requirements with respect to its *2015 Audited Financial Report Requirements Guide*, dated January 1, 2016. These procedures were performed solely to assist you in determining whether the Partnership has met the requirements of Section 7 subparagraph (a)(ii) of the Regulatory Agreement, dated December 10, 2010, between the Partnership and MassHousing (the "Regulatory Agreement") as of December 31, 2015. The General Partner is responsible for meeting those requirements. This agreed-upon procedures engagement was conducted in accordance with attestation standards established by the American Institute of Certified Public Accountants. The sufficiency of these procedures is solely the responsibility of the General Partner of the Partnership. Consequently, we make no representation regarding the sufficiency of the procedures described below either for the purpose for which this report has been requested or for any other purpose.

Section 7 subparagraph (a)(ii) provides for certain conditions to be met for Distributions, as defined, to be made by the Development Project.

The information used to conduct our procedures was provided to us by the Partnership and management agent (hereafter, Management).

The procedures we performed and our findings are as follows:

1. We obtained the MassHousing mortgage activity statement (the "activity statement") for the month of January, 2016. We agreed the mortgage payment and mortgage escrow and replacement reserve deposits, due January 1, 2016, from the activity statement to the Partnership's general ledger in order to determine whether the payments were made and the amounts were in accordance with provisions of the MassHousing Regulatory Agreement, mortgage loan and related loan documents.

No exceptions were noted.

2. We agreed the payments made by the Partnership, in January, 2016, on operating expense loans for Development Project expenses which are payable to the partners and/or their affiliates to the bank statements and the approval letter - [or other documentation – specify] - from MassHousing

for repayment of such loans in order to determine whether the payments were properly made from operating funds of the Partnership.

No exceptions were noted.

3. We obtained the Partnership's detail aged accounts payable listing as of December 31, 2015. We recalculated the aging per the aged accounts payable listing based on the invoice date and service period or delivery date for each payable on the listing in order to determine whether the aging category of the payable was not more than 30 days past due at December 31, 2015. We selected a judgmental sample of 50% of the dollar amount of payables in the 0 - 30 days category on the detail aged accounts payable listing and obtained the invoices - [or other supporting documentation – specify] - for those payables. We traced and agreed the invoice date and service period or delivery date from the invoice - [or other supporting documentation – specify] - to the information included on the detail aged accounts payable listing.

No exceptions were noted.

4. We obtained a detail listing of the Partnership's accrued expenses, related invoices - [or other supporting documentation – specify] - and management's accrual calculations as of December 31, 2015. We examined the invoices - [or other supporting documentation – specify], recalculated management's accrual calculations, and considered the nature of the accrued expense and its related payment terms in order to determine whether the accrued expenses were not more than 30 days past due at December 31, 2015.

No exceptions were noted.

We were not engaged to and did not conduct an examination, the objective of which would be the expression of an opinion on whether the Partnership met the requirements of Section 7 subparagraph (a)(ii) of the Regulatory Agreement. Accordingly, we do not express such an opinion. Had we performed additional procedures, other matters might have come to our attention that would have been reported to you.

This report is intended solely for the information and use of the General Partner of the Partnership and MassHousing, and is not intended to be and should not be used by anyone other than these specified parties.

Attachi & Brown
Certified Public Accountants

Boston, Massachusetts
March 31, 2016

Owner that requests Distribution substantially after March 31, 2016, or who feels that this requirement is financially burdensome, may suggest an alternative way to satisfy the requirements of the above referenced section of the Regulatory Agreement. Each request will be considered by Rental Management staff on a case-by-case basis.

