MaineHousing
Maine State Housing Authority

Analysis of Savings from and Benefits of Tax-Exempt Financing

Pursuant to 10 MRSA Sec. 363

March 2013

MaineHousing
Maine State Housing Authority

March 15, 2013

The Honorable John L. Patrick, Chair
The Honorable Erin D. Herbig, Chair
Members, Joint Standing Committee on Labor,
Commerce, Research and Economic Development
100 State House Station
Augusta, ME 04333-0100

Subject: Analysis of Savings from and Benefits of Tax-Exempt Financing

Dear Committee Members:

Pursuant to 10 MRSA Sec. 363, please find under this cover the above referenced report along with the Independent Accountants Report on Applying Agreed Upon Procedures.

If you have any questions, please contact me or Peter Merrill at 626-4608.

Sincerely,

John G. Gallagher
Director

JGG/pme
Enclosure

353 Water Street | Augusta, Maine 04330-4633 | 207.626.4600 | 800.452.4668 | TTY 800.452.4603 | Fax 207.626.4678 | www.mainehousing.org

MAINE STATE HOUSING AUTHORITY

TABLE OF CONTENTS

**INDEPENDENT ACCOUNTANTS' REPORT ON
APPLYING AGREED UPON PROCEDURES**

The Board of Commissioners
Maine State Housing Authority
Governor of the State of Maine
The Joint Standing Committee on Labor, Commerce, Research and Economic Development

We have performed the procedures in Appendix A, which were agreed to by the Maine State Housing Authority and the Joint Standing Committee on Labor, Commerce, Research and Economic Development (the Committee), solely to assist you with respect to the requirements of the State of Maine 10 MRSA Sec. 363, subsection 11. The Maine State Housing Authority is responsible for the preparation of the "Benefit of 2012 Single Family Issues" (Schedule 1) and the "Benefit of 2012 Multi-Family Issues" (Schedule 2). This engagement to apply agreed-upon procedures was conducted in accordance with attestation standards established by the American Institute of Certified Public Accountants. The sufficiency of the procedures is solely the responsibility of those parties specified in the report. Consequently, we make no representation regarding the sufficiency of the procedures either for the purpose for which this report has been requested or for any other purpose.

The procedures we performed and our findings are summarized in Appendix A.

We were not engaged to, and did not, perform an examination, the objective of which would be the expression of an opinion on Schedule 1 or Schedule 2. 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 Maine State Housing Authority, the Governor of the State of Maine and the Committee and is not intended to be and should not be used by anyone other than these specified parties.

Baker Newman & Noyes
Limited Liability Company

Portland, Maine
March 14, 2013

APPENDIX A

INDEPENDENT ACCOUNTANTS' PROCEDURES PURSUANT TO 10 MRSA SEC. 363

We obtained the "Benefit of 2012 Single Family Issues" Schedule (Schedule 1) and the "Benefit of 2012 Multi-Family Issues" Schedule (Schedule 2), prepared by the Maine State Housing Authority (MaineHousing) which lists the tax-exempt bonds issued in 2012 and performed the following:

1. We agreed the Lendable Proceeds for the Single Family bond issues in Schedule 1, which were 2012 Series A to the estimated uses of funds schedule contained in the Official Statement for the corresponding bonds.

2. We agreed the Lendable Proceeds for the Multi-Family bond issues in Schedule 2, which were 2012 Series B to the estimated uses of funds schedule contained in the Official Statement for the corresponding bonds.

3. We agreed the average mortgage rate of the lendable Single Family proceeds produced in 2012 by MaineHousing of 3.80% to correspondence from Hawkins, Delafield & Wood LLP, MaineHousing's bond underwriters' counsel.

4. We agreed the average Fannie Mae 60 day commitment rate, shown on page 5, of 3.40% rounded to the nearest 0.05%, for 2012, to the average of the Fannie Mae 60 Day Forward Commitment Rate obtained from Bloomberg Data for 2012, as provided by MaineHousing, plus 25 basis points for servicing.

ANALYSIS OF SAVINGS FROM AND BENEFITS OF TAX-EXEMPT FINANCING

In 2012, the Maine State Housing Authority (MaineHousing) issued or converted tax exempt private activity bonds in the aggregate principal amount of $148,755,000 in its Mortgage Purchase Program (MPP) Bond Resolution. The proceeds of the issues were used to fund required debt service reserves, pay the cost of issuance, pay the underwriters fees, refund outstanding bonds, and to make or purchase new single family and multi-family mortgage loans. The issues generated $27 million of lendable proceeds for MaineHousing's programs.

In 2012, MaineHousing purchased $49.5 million in mortgage loans; substantially all of which qualified for tax-exempt financing. About $30 million of the bond proceeds used in these purchases were generated in bond sales from prior years or surplus monies. At year-end $8 million of lendable proceeds remained from 2012 bond sales.

BOND ISSUANCE AND BOND CAP USAGE

In 2012, MaineHousing issued or converted $148,755,000 of tax exempt housing bonds but only expended $40,645,000 in Private Activity Bond cap. That means that approximately $108 million of MaineHousing's issues in 2012 did not require an allocation of bond cap. The three mechanisms used by MaineHousing to issue private activity bonds without utilizing bond cap are explained below:

1. **Refunding:** When the proceeds of a tax-exempt bond sale are used to redeem the outstanding bonds of a prior issue and the refunding bonds have an average life that does not exceed that of the bonds being refunded, private purpose bond cap is not required. MaineHousing sold $108 million of such bond refundings in 2012.
2. **501(c)(3) Multifamily Bonds:** Bonds sold to fund a qualified low-income project, which is owned by a 501(c)(3) entity, do not require private activity bond cap. MaineHousing did not sell any 501(c)(3) bonds in 2012.
3. **Replacement Refundings:** The tax code allows that if, within 90 days of the issuance of new bonds, bonds of similar tax status are retired, that the new bonds in an amount equal to the redeemed bonds may be deemed to be replacing the prior bonds and do not require a bond cap allocation. MaineHousing did not sell any replacement refunding bonds in 2012.

MULTIFAMILY BOND AND THE LOW INCOME HOUSING TAX CREDIT (LIHTC)

Multifamily bonds issued from an allocation of the private activity bond cap produce an additional allocation of the LIHTC equal to 10 years of an annual tax credit equal to 4% of the cost of the low income units in a project. This tax credit is then sold to investors to produce equity capital for the project, thereby reducing the amount of debt required.

Example: A 20-unit project is being built for low-income tenants. The cost is $100,000 / unit or $2,000,000. The project, if financed with private activity bonds, would be eligible for $80,000 of annual tax credits for 10 years or a total of $800,000. Investors are currently paying approximately 80 cents on the dollar, which in this example would generate $640,000 of equity for the project. The required financing would be thereby reduced from $2 million to $1,360,000. If the interest rate on the $1,360,000 mortgage is 6.5%, the rate on a $2 million mortgage would have to be 3.125% to produce the same monthly payments. The LIHTC, therefore, supplements the impact of the lower rate by replacing debt with equity.

INCOME TARGETING: SINGLE FAMILY

The single-family program is restricted to first time homebuyers who are Maine residents buying a principal residence. The income of the borrowers may not exceed 115% of the area median and the purchase price of the residence may not exceed 110% of the area median. In 2012, the average loan size was about $102,000. The average family income was $48,000.

INCOME TARGETING: MULTIFAMILY

In multifamily projects financed with the proceeds of tax-exempt bonds, the benefits of the tax-exempt mortgage rates are passed along to tenants in the form of below market rents. The tax code requires either 20% of the units must be affordable for families at 50% of the area median income or 40% of the units for families at 60% of the area median income. The computation assumes that 30% of gross monthly income is available for rent.

In almost every program, MaineHousing requires or rewards even greater affordability than the tax code.

In multifamily projects the benefits of tax exempt financing should be measured by the rent differential, in units of similar quality and desirability, between market rents and rents in the low-income units in the same locale. In addition, it is important to ascertain the benefits of the economic activity generated by the construction or rehabilitation of the units.

2012 Mortgage Purchase Program (MPP) Bond Issues

Sources and Uses of Funds

Type of Issue	2012A Single Family	2012B Multi-Family	**TOTAL MPP BOND ISSUES**
SOURCES:			
Principal of Bonds	123,870,000	24,885,000	148,755,000
Original Issue Premium	1,502,141	-	1,502,141
MaineHousing Contribution	-	353,140	353,140
TOTAL SOURCES	**125,372,141**	**25,238,140**	**150,610,281**
USES:			
Purchase of Mortgages	23,944,084	3,000,000	26,944,084
Refunding of Prior Bonds	100,372,141	21,885,000	122,257,141
Debt Service Reserve	-	-	-
Cost of Issuance	170,000	140,000	310,000
Underwriters Fee/Discount	885,916	213,140	1,099,056
TOTAL SOURCES	**125,372,141**	**25,238,140**	**150,610,281**
BOND CAP USED	**37,645,000**	**3,000,000**	**40,645,000**

I. BOND CAP AVAILABLE IN 2012

Carryforward from prior years	$ 750,865,000
Initial Allocation in 2012	50,000,000
Re-allocation during 2012	209,560,000
Total Available	$ 1,010,425,000

BOND CAP USED IN 2012	$ 40,645,000
BOND CAP EXPIRING ON 12/31/12	$ 235,625,000
CARRYFORWARD TO 2013	$ 734,155,000

SCHEDULE 1

BENEFIT OF 2012 SINGLE FAMILY ISSUES

Issue	Lendable Proceeds	Average Mortgage Rate
2012 Series A	$23,944,084	3.80%

The weighted average rate of the lendable single family proceeds produced in 2012 by MaineHousing as shown above was 3.80%. MaineHousing's mortgages were substantially all level payment, 30 year term mortgages. We estimate that closing cost grants made in connection with the mortgages funded with the proceeds of the 2012 bonds will average about 2% of the mortgage amount. Assuming average prepayment experience, the grants lower the effective rate to the borrower by about 35 basis points, to approximately 3.45%.

A good proxy for market rates is the Fannie Mae 60 day Commitment Rate plus a servicing fee, which is included in the mortgage rate and averages 25 basis points. In 2012, the average of this market indicator, taken on each business day, was about 3.40%. This 3.40% average market rate was a function of a downward trend during the year. Average market rates dropped from an average of about 3.75% in the 1st quarter to about 3.00% in the 4th quarter. For most of the year, market rates were under the MaineHousing rate and demand for the tax-exempt product dropped off significantly.

Summary of 2012 Benefits

The MaineHousing single family program struggled to stay competitive in 2012. The average mortgage that the lendable proceeds of 2012 bond sales generated was about 3.80%. The $2,000 of down payment assistance offered in connection with MaineHousing represented about 2% on the average mortgage of $102,000. These grants lowered the effective rate to the borrower by about 35 basis points, which would lower the 3.80% average note rate to an effective loan rate of about 3.45%.

Even factoring in the impact of the down payment grant, MaineHousing's product had difficulty competing in 2012. The $29.5 million of single family loans purchased in 2012 was the lowest volume in recent years.

SCHEDULE 2

BENEFIT OF 2012 MULTI-FAMILY ISSUES

Issue	Lendable Proceeds
2012 Series B	$3,000,000

MaineHousing issued one multi-family bond issue in 2012. About $22 million of its proceeds were used to refund prior multi-family bonds and $3 million was used for a portion of mortgage loans made to 9 projects which constructed or rehabilitated 254 units. The lendable proceeds from the 2012 bond sale supplemented $23 million generated from 2011 bond sales. The major benefit of MaineHousing's tax-exempt funded program is not in the interest rate but in the loan terms and in the equity that is generated by the tax credit, which is available when tax-exempt financing is used.

Many of the 30 year multi-family loans financed with the tax-exempt proceeds have interest only payments for the first 15 years or, in some cases, for the entire 30 year life of the loan. A 6% interest only loan has substantially the same monthly payment as a 4.375% 30 year loan. Our ability to extend the duration of the loan has the same impact on the cash flow of the project as a 1.625% lower interest rate on a 30 year level payment loan.

Probably the biggest benefit of the tax-exempt program comes from the 4% LIHTC, which is available with the financing. The nine projects expected to be partially financed with the proceeds of 2012 multi-family bond issue are expected to generate over $13 million in equity from the sale of the tax credit. By replacing debt, this equity lowers the debt service of the projects and subsidizes the below market rents required by the tax code.