

July 29, 2016

TO: State Directors
Rural Development

ATTN: Program Directors
Multi-Family Housing

FROM: Tony Hernandez /s/ *David Lipsetz* *for*
Administrator
Housing and Community Facilities Programs

SUBJECT: Guidance on the Use of Section 538 Guaranteed Rural Rental Housing
Program with Section 515 Properties

The intent of this Unnumbered Letter (UL) is to clarify issues concerning the use of Section 538 loan guarantees in transactions involving the revitalization and preservation efforts of existing affordable housing properties financed with Section 515 direct loans. It is written for the sole use of the Rural Development State Office staff and area offices involved in processing Section 538 guaranteed loan applications received in conjunction with existing Section 515 property transfers and MPR.

The use of the Section 538 program enhances Rural Development's capacity to attract private capital to support the revitalization of the Section 515 portfolio. The Section 515 Rural Rental Housing program and the Section 538 Guaranteed Rural Rental Housing program have different regulatory frameworks. This UL intends to reconcile the procedural differences between the two programs.

The attachment to this UL is titled "SECTION 538/515 PROGRAM REQUIREMENTS MATRIX". Column A contains several program requirements that are addressed in this UL. Column B contains an overview of the program requirement from the Section 538 perspective. Column C contains an overview of the program requirement from the Section 515 perspective. It should be noted that both Column B and Column C are only summary statements. Reviewers should rely on the respective regulations and handbooks for each program for detailed program

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guidance. Column D outlines the program requirements Rural Development staff should utilize for each program requirement contained in Column A. The guidance provided generally directs the user to utilize the most restrictive guidance from either the Section 538 or the Section 515 program.

If you have any questions regarding this UL, please contact Tammy S. Daniels of the Multi-Family Housing Guaranteed Loan Division at (202) 720-0021 or tammy.daniels@wdc.usda.gov.

Attachment

COLUMN A Program Requirements	COLUMN B Section 538 Requirements	COLUMN C Section 515 Requirements	COLUMN D Sections 538/515 Projects Recommended Approach
1. Equity Contribution	<p>For-profit – the greatest of 10% of the Total Development Cost (TDC) or of the appraised value.</p> <p>Non-Profit – the greatest of 3% of the TDC or of the appraised value.</p> <p>Cash or/and land value meet the equity requirement (other Agency approved sources may be considered).</p>	<p>For-profit – 3% of the Agency loan not receiving LIHTC For-profit – 5% of the Agency loan if receiving LIHTC</p> <p>Non-Profit - 0%; can loan 100% plus 2% operating expenses.</p> <p>Not required for properties in the MPR using MPR tools, however still required for MPR properties using Section 515 loan funds.</p> <p>Any additional funds advanced under the MPR program may only be used for MPR authorized purposes.</p>	<p>Prior to the issuance of the Agency’s Conditional Commitment, the lender certifies in its application that Section 538 program’s equity requirements were met and Agency personnel verify lender’s calculations. Prior to the issuance of a permanent guarantee, an appraisal (unless waived) of the project once construction is completed must confirm the borrower’s equity contribution certification.</p> <p>Existing Section 515 Reserve Account Balances will not be used to meet Section 538 equity contribution requirements.</p>

COLUMN A Program Requirements	COLUMN B Section 538 Requirements	COLUMN C Section 515 Requirements	COLUMN D Sections 538/515 Projects Recommended Approach
2. Lease-Up Reserve	<p>Lease-up reserve in lieu of 90/90</p> <ul style="list-style-type: none"> • Required only if the permanent guarantee is to be issued prior to achievement of 90% occupancy for 90 continuous days in the 120-day period immediately prior to the issuance of the permanent guarantee. • Lender and/or developer must elect to use a lease-up reserve prior to the start of construction. • Borrower funded with a non-mortgageable cash contribution. • Reserve must be fully funded prior to issuance of permanent guarantee. • For Option 3 Continuous Guarantees, the lease-up reserve is fully funded on or before the issuance of the guarantee. • Reserve must be at least 2% of the greater of appraised value or TDC. <p>Unused funds are transferred to the Section 538 O&M reserve account and may be returned to the borrower as a cash distribution at the end of the year and if the requirements of HB-1-3565, Paragraph 7.7 E have been met.</p>	<p>No published standard: Discuss individual transactions with a National Office Review Underwriter.</p>	<p>When the lender and/or developer opt to use the lease-up reserve in lieu of the 90/90 requirement, the lease up reserve will be managed pursuant to Section 538 requirements. The lender will control the account and its distributions.</p> <p>If the lender, borrower and Agency choose not to fund a lease-up reserve during the construction period, documentation for the basis of the decision must be in the Agency file. There must be documented evidence that the project will not expect to lose tenants due to displacement or due to increased rents.</p> <p>If a Section 538 lease up reserve is not used, the project must meet the 90/90 test in the 120-day period immediately prior to the issuance of the permanent guarantee.</p> <p>Unused funds are transferred to the Section 538 O&M reserve account and may be returned to the borrower as a cash distribution at the end of the year if the requirements of HB-1-3565, Paragraph 7.7 E have been met.</p>
3. Construction Contingency Reserve	<ul style="list-style-type: none"> • At least 2% of total construction costs. • Borrower funds reserve with a non-mortgageable cash contribution. The lender may release unused construction contingency reserves to the borrower anytime after completion of construction and achievement of the 90/90 test. All other reserve accounts must be fully funded prior to the release of any unused construction contingency funds. • May accept letter of credit (LOC) in lieu of cash. 	<ul style="list-style-type: none"> • 7% -10% and may be funded with Section 515/MPR funds or other third-party financing as authorized in the transfer approval. • Upon final inspection and acceptance by Rural Development any remaining unused funds will be deposited into project's Rural Development capital reserve account. 	<p>For projects using the Section 538 construction guarantee, Section 538 requirements apply.</p> <p>State Offices must approve all change orders for Sections 515/538 construction contracts.</p>

COLUMN A Program Requirements	COLUMN B Section 538 Requirements	COLUMN C Section 515 Requirements	COLUMN D Sections 538/515 Projects Recommended Approach
4. Occupancy & Rent Restrictions	<ul style="list-style-type: none"> At initial occupancy, tenancy restricted to individuals and families whose incomes do not exceed 115% of area median income. 	<ul style="list-style-type: none"> At initial occupancy, and prior to annual or other re-certifications, must qualify as a very low- low or moderate income household meeting Rural Development definitions. Rural Development Section 515 rent levels must reflect realistic operating and maintenance expenses and expectations in accordance with Section 515 program policy. Overly optimistic or unjustifiable expenses will be rejected under Section 515 underwriting principles. 	<p>The most restrictive occupancy and rent restrictions (typically Section 515) will be used.</p> <p>In the event that Section 515 income requirements and/or rent levels exceed the Section 538 levels, the State Office will refer the matter to the National Office for resolution.</p>
5. Operating Costs and Rent Levels	<ul style="list-style-type: none"> Operating costs and rent levels must be adequate to meet program and NOFA requirements on a sustainable basis in the budget analysis. At rent up and on a continuing basis, rents including tenant utility allowances may not exceed 30 percent of 115 percent of area median income adjusted for family size. Average rent for all units in a project cannot exceed 30% of 100% of area median income adjusted for family size. 	<ul style="list-style-type: none"> Rural Development Section 515 rent levels must reflect operating and maintenance expenses that are reasonable, typical, necessary and show a clear benefit to the residents of the property and expectations in accordance with Section 515 program policy. Overly optimistic or unjustifiable expenses will be rejected under Section 515 underwriting principles. Projects must be sustainable and will be underwritten with expenses, costs and incomes that can typically be supported in the market area. At approval of new loans and MPR Tools, transfers, prepayments, etc., rents cannot exceed the Conventional Rents for Comparable Units (CRCU) standard, unless waived by the National Office On an ongoing basis, rents remain budget-based. CRCU standards do not apply to annual budget submissions. 	<p>Underwriters will review both Section 538 and Section 515 anticipated income and expense projects to reconcile the operating projections. If LIHTCs are also included, such projections will also be considered in determining feasibility projections and sustainability determinations.</p>

COLUMN A Program Requirements	COLUMN B Section 538 Requirements	COLUMN C Section 515 Requirements	COLUMN D Sections 538/515 Projects Recommended Approach
6. Construction Monitoring, Inspections, Payouts	<ul style="list-style-type: none"> • New construction, rehabilitation, modular and manufactured structures must meet RD Instruction 1924-A. • Actual work inspected by, or on behalf of, the lender. • Minimum three inspections. • In addition to the three inspections; lender inspections must be done prior to each payment to the contractor. • Lender must coordinate final inspection. • Agency must approve all change orders. 	<ul style="list-style-type: none"> • Agency to inspect all work completed and materials suitably stored on site. • Minimum three inspections at key times • In addition to the three required inspections; Agency encouraged to make monthly inspections if time and resources permit. • Prior Agency concurrence in each pay request and proposed change order. • MPR projects are subject to project-specific requirements under the terms of the MPR Conditional Commitment and only released for the MPR authorized purposes as required under the MPR Conditional Commitment. • Follow RD Instruction 1924-A requirements. 	For Sections 515/538 projects financed with a Section 538 construction guarantee, follow the applicable provisions of HB-1-3565 for construction monitoring. If time and resources permit, State Offices are encouraged to monitor the construction through on-site reviews/inspections. State Office staff should review, but not sign, the contractor's payment requests.
7. Mortgage Terms	Term of not less than 25 years and not more than 40 years.	Third-party loans must: <ul style="list-style-type: none"> • be fully amortized; or • have a maturity date that is after the Rural Development/Section 515 debt matures; or • include a written agreement with third-party lender to extend scheduled maturity through re-amortization or whatever means available to them on terms that do not require rents to exceed CRCU. 	In Section 515 transactions the Section 538 loan term must exceed the term of the Section 515 subordinate financing. The minimum term of the Section 538 loan will be 25 years or the term of the Section 515 subordinate debt whichever is greater. The maximum term of the Section 538 loan is 40 years.
8. Debt Service Coverage Ratio (DSCR)	Requires DSC of at least 1.15 unless Agency approves lower DSCR.	No published standard: Discuss individual transactions with a National Office Review Underwriter.	All transactions will be underwritten with a minimum DSCR of 1.15 or the Agency approved DSCR, whichever is higher. The combined DSCR for the 538 and the 515 debt will be at least 1.0 every year. Rents that exceed CRCU to achieve the 1.15 DSCR, must have a National Office waiver.
9. Interest Credit	If available, generally limited as to basis points and loan amount.	Reduction in the effective interest rate for the Agency's entire loan down as low as 1% with RD Interest Credit Agreement.	Interest credit eligibility, availability and limitations for Sections 515/538 transactions will be published in the annual NOFA.

COLUMN A Program Requirements	COLUMN B Section 538 Requirements	COLUMN C Section 515 Requirements	COLUMN D Sections 538/515 Projects Recommended Approach
10. O&M Reserve/ Initial Operating Capital (IOC)	<p>O&M Reserve</p> <ul style="list-style-type: none"> All borrowers must contribute from their own resources at least 2% of the loan amount. Funds may be provided in cash or LOC. For Options 1 and 2 Guarantees, the O&M Reserve is funded on or before the closing of the permanent loan. For Option 3 Continuous Guarantee, the O&M Reserve is funded no later than 30 days before the issuance of the first certificate of occupancy is anticipated. 	<p>Initial Operating Capital</p> <p>To provide a source of capital for start-up costs, such as the purchase of equipment, and paying operating, maintenance, and debt service expenses. Borrowers are required to make an initial operating capital contribution to the general operating account as described in §3560.64.</p>	<p>O&M Reserve for a Guaranteed Loan is not required when State Office MFH staff concurs that the Section 515 General Operating Account (GOA) is sufficient to cover projected expenses.</p> <p>When Section 538 O&M Reserve is required (i.e. when the Section 515 GOA is not sufficient to cover projected expenses) the O&M will be managed in accordance with Section 538 requirements. The Section 538 lender will control the account and its distributions.</p>
11. Credit Enhancements During Construction	<p>Per 3565.303 (c) (2) acceptable credit enhancements include:</p> <ul style="list-style-type: none"> Surety bonding or performance and payment bonding acceptable to the Agency; An irrevocable letter of credit acceptable to the Agency; or A pledge to the lender of collateral that is acceptable to the Agency. 	<p>Acceptable credit enhancements include:</p> <ul style="list-style-type: none"> Surety bonding or a P&P Bond (preferred). An irrevocable LOC, Rural Development is named as Beneficiary – 100% of contract. Cash deposit in amount of contract. All construction must adhere to RD Instruction 1924-A. MPR projects must also comply with the terms of the MPR Conditional Commitment. 	<p>For projects financed with a Section 538 construction guarantee, follow the applicable provisions of 3565.303 (c) (2) to the extent that it does not conflict with Section 515 conditions, including surety, bonding and final acceptance.</p>
12. Developer Fee	<ul style="list-style-type: none"> Developer fee is an eligible use of Section 538 loan proceeds. Deferred developer fee can be repaid from surplus cash at year end. 	<ul style="list-style-type: none"> Allow reasonable developer fee when the only other funding source is a Section 538 loan that is being used with existing Section 515 property transfers and MPRs. Deferred developer fees cannot be repaid except as part of the approved annual Return on Investment. 	<p>Developer fee will be an allowed cost with Section 538 loan proceeds. The developer fee will be disbursed at closing.</p> <p>The disbursement of a deferred developer fee will be subject to Section 515 limitations on annual distributions.</p>

COLUMN A Program Requirements	COLUMN B Section 538 Requirements	COLUMN C Section 515 Requirements	COLUMN D Sections 538/515 Projects Recommended Approach
<p>13. Reserve Accounts including CNA requirements</p>	<ul style="list-style-type: none"> • Lender holds funds. • Lender approves all release of funds. • Deposits based on Capital Needs Assessment (CNA). CNAs on Section 538 properties should follow 538 Program Requirements. • At least every five years- but no later than each seventh year, the lender must review the CNA as part of adjusting the replacement reserve deposit. The reserve account must be adjusted accordingly. If the reserve deposits as determined by the CNA are not adjusted, the lender must provide a justification to the Agency. The lender must continue to do an evaluation of the property during the annual physical inspection to ensure that the reserve account has acceptable funding levels. • Lenders should require borrowers to obtain bids on major repairs, construction projects, or purchases. A recommended standard is three written bids for any single purchase or project that exceeds \$10,000. Borrowers should be required to justify any bid accepted that is higher than the lowest bid. 	<ul style="list-style-type: none"> • Section 515 reserve account funds required to be held in a supervised account. • Requires prior Rural Development concurrence to release funds. • Emergency situation may request post approval. • Minimum two bids required when costs are more than \$5,000 or when IOI-involved bid is submitted directly to State Office prior to requesting bids from other firms. • Reserve account sized to meet the 20-year inflated needs of the property as determined by an approved CNA. • Rural Development may require frontend loading in MPRs. • A new CNA may be required five years or later. • Reserve accounts established under an approved CNA may only be used for approved capital needs or purposes specifically authorized in the Section 515 transfer authorization or MPR Conditional Commitment. <p>MPR uses are restricted to those items shown on the approved CNA but withdrawals for transfers must follow HB 2-3560.</p>	<p>Requirements of the Reserve Account will be handled in accordance with 7 CFR 3560, section 3560.306 (e).</p> <p>The Section 538 guaranteed lender will hold the funds. Release of funds will require approval of Agency, lender and borrower. Request for release of reserve funds should be processed using RD Form 3560-12.</p> <p>The project will maintain initial and ongoing reserve levels at the greater of the Section 515 or Section 538 requirements.</p> <p>**The Section 515 Requirements will be followed in regards for CNA.</p> <p>Reserve account funds will not be used to pay fees associated with the Section 538 guarantee.</p> <p>Follow 7 CFR 3560, for minimum two bids required when costs are more than \$3,500 or when IOI-involved bid is submitted directly to State Office prior to requesting bids from other firms.</p>

COLUMN A Program Requirements	COLUMN B Section 538 Requirements	COLUMN C Section 515 Requirements	COLUMN D Sections 538/515 Projects Recommended Approach
14. Surplus Cash Distribution/ Return to Owner	Lender may release surplus cash to borrowers annually with no restrictions on the amount. All requirements (HB 3565-1, 7.7 E) must be met prior to release of surplus cash.	<p>There is no statutory authority in the Section 515 program to allow for a distribution of surplus cash.</p> <p>Borrowers may earn a return on their investment (ROI), or in transfer situations, a new Return to Owner (RTO) as authorized in the transfer approval, in accordance with the terms of their RD loan agreement or resolution if there is a positive net cash flow in housing project operations. The authorized return may be taken by the borrower after the housing project's fiscal year, provided that the balance of the reserve account is equal to or greater than required deposits minus authorized withdrawals.</p>	<p>Use Section 515 program requirements to define amount of the annual distributions. Lender will maintain any surplus funds from owner funded reserves (construction contingency, lease up and O&M reserve) in a Section 538 Surplus Reserve Account separate from the Section 515 GOA.</p> <p>Lender may release unused funds in this Surplus Reserve Account only if the requirements of HB-1-3565 Paragraph 7.7 E. have been met.</p> <p>Appraisals are required in ALL cases prior to approval to determine allowable equity payments and RTO.</p>
15. Definition of Total Development Cost	Total cost of project construction cost, financing fees, professional fees and profit.	The cost of construction, purchasing, improving, altering or repairing MFH and related facilities, and purchasing or improving the necessary land, including architectural, engineering, or legal fees and charges and other technical and professional fees and charges, but excluding fees, charges or commissions such as payments to brokers, negotiators or other persons for the referral of prospective applicants or solicitations of loans.	Use the Section 515 definition.
16. Use-Restrictions	The property must remain as affordable rental housing for the original loan term. The restrictive use covenants must be recorded.	Mandated Section 515 extended use restrictions apply to all program loans and may be extended for the full term of the loan for transfers and MPRs on project-by-project basis. Use restrictions are not liens and cannot be subordinated except to the applicable State Agency LIHTC LURAs when necessary.	<p>Both the Section 515 and Section 538 use restrictions will be recorded. In general, Section 515 use restrictions are more restrictive than the Section 538 restrictions and will control during the term of the Section 515 loan.</p> <p>When the term of the Section 538 use restrictions are greater than the term of the Section 515 restrictions, they will survive the Section 515 restrictions.</p> <p>The period of the Restrictive Use Covenant (RUC) in Section 515 transfers utilizing Section 538 funds to pay equity pursuant to 7 CFR 3560.406 will be for a term of 30-years from the closing date of the Rural Development transfer.</p>

COLUMN A Program Requirements	COLUMN B Section 538 Requirements	COLUMN C Section 515 Requirements	COLUMN D Sections 538/515 Projects Recommended Approach
17. Subordination of Section 515 Loan		Section 515 properties selected into the MPR Program must use the Restrictive Use Subordination Agreement approved by OMB No. 0575-0190 which is posted to the MPR Website. Subordinations of existing Section 515 loans in transfer authorization must comply with the Section 515 program transfer conditions currently published in HB-3-3560, Chapter 7.	For Sections 515/538 properties participating in the MPR program, both the Subordination Agreement in HB-3-3560 dated December 17, 2008 PN 425 and any updates will be used along with the Restrictive Use Subordination Agreement approved by OMB No. 0575-0190. A 515 loan may only subordinate to a 538 loan used for eligible 515 purposes.
18. Appraisal	Appraisal must be completed within the 12 months prior to the issuance of the loan guarantee. Refer to 3565.303 (d) (4) for appraisal exemption guidance.	In Section 515 transfers and MPR Program transactions, any required appraisal must be completed as required by the transaction approval conditions. Acceptable appraisals for Section 515 property transactions must comply with HB-1-3560, Chapter 7 and 7CFR 3560 Subpart P.	Appraisals will be completed in accordance with Section 538's 3565.303 for Section 538 loan approval and 7CFR 3560 Subpart P for Section 515. Tax Abatements cannot be used to determine value in an appraisal. Tax Credit Equity cannot be used to determine value in an appraisal.
19. Market Study	A market study is required to support the appraisal.	Either a market study or a market survey, as appropriate is required to establish feasibility for any Section 515 transaction as required by the respective Section 515 HB or NOFA.	For Section 515 projects that have been 90% or more occupied for the 3 consecutive years prior to submitting an application, a market study is not necessary unless specifically required as a condition of the Section 515 transfer or MPR approval.
20. Cost Certification	A cost certification is required that represents the actual cost of the work performed in connection with the construction. However, if a cost certification is prepared for any other funding source (e.g., an Agency providing LIHTC) then a copy of that cost certification is acceptable. An audited cost certification is required from identify of interest (IOI) contractors.	Actual construction costs must be reported. In the instance of an IOI contractor the costs must be certified and audited as outlined on Form RD 1924-13, "Estimate and Certificate of Actual Cost" if required.	For projects with any Section 538 guarantee, use the Section 538 program cost certification requirements. However, if there is an IOI contractor the certified and audited costs will be presented in the format contained on Form RD 1924-13, "Estimate and Certificate of Actual Cost".
21. Single Asset Entity	Borrowers must operate as a single asset ownership entity.	There is no restriction that borrowers must operate as a single asset ownership entity however all transfers and MPRs approvals provide project-specific conditions.	For Section 515 projects using Section 538 guaranteed loan funds, the Single Asset Entity restriction is waived.

COLUMN A Program Requirements	COLUMN B Section 538 Requirements	COLUMN C Section 515 Requirements	COLUMN D Sections 538/515 Projects Recommended Approach
22. Rural Area Designation (Grandfathering)	A Section 538 project for which a subsequent loan will be used to make necessary repairs or improvements to the property or to avert prepayment may be located in an area that has changed from rural to non-rural.	A project for which a subsequent loan or MPR tools will be used to make necessary repairs or improvements to the property, or to avert prepayment may be located in an area that has changed from rural to non-rural.	For subsequent loans in a Section 515 project whose acquisition and/or repair are financed by the Section 538 program, the “grandfathered” rule applies.
23. Underwriting Requirements		Section 515 transfers and MPR must comply with program HB and specific NOFA/NOSA requirements, and generally require review of the Section 538 and any other third-party funding underwriting summaries to accurately complete the UWT for approval.	Lenders are required to submit a matrix summarizing any differences between Section 515 underwriting and Section 538 underwriting.
24. Reporting Requirements: a) Annual Financial Reports b) Affirmative Fair Housing Marketing Plan c). Management Plan	<p>a) The lender must obtain from the borrower, on an annual basis, an audited annual financial statement conducted in accordance with generally accepted government auditing standards. The audit must be sent to the Agency within 90 days of the end of the property’s fiscal year.</p> <p>b) The borrower must prepare and comply with the Affirmative Fair Housing Marketing Plan and all other Fair Housing requirements. AFHMP submitted with the NOFA Response and/or application must be reviewed, approved and signed by the Agency. If the property has interest credit, the AFHMP must be approved and signed by the Agency at least every three years when the agency’s compliance review is conducted. Annually, the lender must review and certify that the AFHMP is in compliance with the Agency’s regulation. This certification and a copy of the AFHMP will be included in the Annual Audit of the property.</p>	<p>a) Borrowers must submit annual financial reports in accordance with 7 CFR 3560.</p> <p>b) Borrowers with housing projects that have five or more rental units must prepare and maintain an Affirmative Fair Housing Marketing Plan (AFHMP) as defined in 24 CFR part 200, subpart M.</p> <p>c) Borrowers must develop and maintain a management plan for each housing project covered by their loan or grant. The management plan must establish the systems and procedures necessary to ensure that housing project operations comply with Agency requirements.</p>	<p>The lender must obtain from the borrower, on an annual basis, an audited annual financial statement conducted in accordance with generally accepted government auditing standards.</p> <p>Lenders may use the same approved AFHMP that the borrower is currently using for the project. The annual reporting requirements for the Section 538 must remain in place.</p> <p>The same Management Plan may be used for Section 515 and Section 538, lender must ensure that the 538 program requirements are included in the Management Plan. In instances where the requirements may differ, the most stringent requirement must be met.</p>

COLUMN A Program Requirements	COLUMN B Section 538 Requirements	COLUMN C Section 515 Requirements	COLUMN D Sections 538/515 Projects Recommended Approach
25. Portfolio vs. Consolidation	<p>If projects are located in different market areas, the deal must be structured as portfolio sale with all projects underwritten as separate properties.</p> <p>If projects are located in the same market area, the deal may be structured as consolidation.</p> <p>Consolidation- all buildings will operate as one project, under one management plan and one NOFA response/application will be submitted.</p> <p>For areas in which separate counties or cities are considered the same market area, the Fair Market Rents must be the same.</p>	<p>If there are 2 or more projects located in different market areas, the deal must be structured as portfolio sale.</p> <p>If there are 2 or more projects located in the same market area, the deal may be structured as a project consolidation.</p> <p>For areas in which separate counties or cities are considered the same market area, the Fair Market Rents must be the same.</p>	<p>If projects are located in different market areas, the deal must be structured as portfolio.</p> <p>If projects are located in the same market area, the deal may be structured as consolidation.</p> <p>For areas in which separate counties or cities are considered the same market area, the Fair Market Rents must be the same.</p>
26. Favorable Financing.	The lender determines the favorable financing in accordance with industry practices.	Section 538 loan may be included as favorable financing.	Section 515 interest credit subsidy is not considered as favorable financing for the Section 538 program.
27. Rent Increases	Rent goes into effect with issuance of the guarantee.	Rent increase begins after construction or the rehabilitation is complete.	Follow the guidelines for Section 515, rent increases will not go into effect until the construction or the rehabilitation is complete.
28. Annual Guarantee Fee	The guarantee fee is calculated as a percentage of the sum of the note principal actually disbursed for all approved draws multiplied by the percentage of the guarantee. Although the fee is paid by the lender, it may be passed on to the borrower.	Not applicable.	The fee should be reflected on the annual budget using RD Form 3560-7 on Part II, Line 32, "Other Administrative Expenses." For combination deals, the fee should not be included in the interest rate.

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