



## **Loan Review Process and Underwriting Guidelines**

This document summarizes the Loan Review Process and Underwriting Guidelines for the San Luis Obispo County Housing Trust Fund (the “Fund”). Its purpose is to convey our current process and practices to prospective borrowers and investors. It is neither comprehensive nor exhaustive and will evolve – change and probably grow – over time.

The process and guidelines described in this document are driven by the mission and values of the Fund. Our mission is to increase the supply of affordable housing for very low, low and moderate income residents of San Luis Obispo County, including households with special needs. This mission is served by providing financing for the development, preservation, improvement and acquisition of housing that will remain affordable for the longest possible time. In addition, forty percent (40%) of the Fund’s resources are committed to benefit households with special needs or very low incomes.

Our values are Leadership, Partnership & Stewardship. We strive to be a leader in the affordable housing field in our community and state. We partner with others to create and preserve affordable housing within our community. We act as a prudent steward of the resources that we receive and manage.

The Loan Review Process describes the general steps that the Fund takes when communicating with prospective borrowers, reviewing applications and approving loans. The Underwriting Guidelines describe how we review loan applications and the standards upon which we base our lending recommendations and decisions.

### **1. Loan Review Process**

Applications for financing from the Fund typically go through a four-step process that begins with an initial inquiry, which may be made by telephone or email or in person. If the proposed project meets basic eligibility and targeting criteria and sufficient funds are available or will be available, the Fund extends an invitation for a complete application. The next step in the process is for staff to review and underwrite the application package. This is followed by a review and consideration of the request by our loan committee, which is called the Commission. The final step in the process is consideration by the Fund’s Board of Directors.

This process can take as little as one month or may take many months to complete.

#### **1.1. Initial Inquiry**

Potential applications are encouraged to call or write to the Fund’s staff to describe their projects and discuss their financing needs. A meeting with staff may be arranged for a more extensive

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review. Staff may discuss prospective applications with the Commission and/or the Board for policy guidance and/or to discuss priorities for the use of available funds.

### **1.2. Staff Review**

When applications are submitted to the Fund, staff reviews, analyzes and underwrites the applications. Preliminary title reports, environmental reports, appraisals or indicators of value, and other third party reports may be ordered. Follow-up information and/or documentation is frequently requested from the applicant. After underwriting and determining that projects meet the Fund's requirements, Staff prepares and submits written reports to the Commission. The staff reports describe the applicants and their projects, analyzes various risks and recommends loan terms and conditions.

### **1.3. Commission Review**

Staff makes formal presentations to the Commission on applications that are recommended for approval and answers questions raised by Commissioners. The Commission evaluates the applications and makes recommendations to the Board of Directors concerning action on the applications. The Commission includes representatives from local jurisdictions, the banking industry, and social service providers so applications are reviewed from multiple perspectives.

### **1.4. Board Approval**

Staff prepares formal reports for the Board of Directors that outline the Commission's considerations and recommendations on each application. Staff and a Commission member make presentations on the applications and Commission recommendations to the Board. The Board considers and makes the final decision regarding each application. The Board may concur with the recommendations of the Commission or may deny applications or approve them with different terms or conditions.

## **2. Underwriting Guidelines**

Underwriting is the process of evaluating whether 1) the request meets our eligibility and targeting requirements, 2) the project is viable, and 3) the loan should be recommended for approval. While the underwriting of single family home loans can be fairly simple and straightforward, the underwriting of affordable housing projects is more involved. These Guidelines include a chart that summarizes many of the standards that we will use in underwriting applications. This chart is followed by short discussions of these and other underwriting considerations.

The fiscal soundness and integrity of the Fund are dependent on the successful repayment of all of the loans that we make. Consequently, we tend to focus on following three areas when underwriting a loan application:

- Whether the project will be completed successfully
- Whether our loan will be repaid on schedule

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- Whether we have adequate loan collateral in case something goes wrong

To the greatest extent possible, the Fund relies on documents that are produced for other lenders or other purposes when underwriting a requested loan. Such documents may include, but not be limited to, application forms, budgets and financial analyses, appraisals, environmental assessments, engineering reports, plans and specifications, market studies and financial statements. This should help streamline the process for the applicant and reduce the need for redundant “paperwork.”

### 2.1. Underwriting Guidelines Table

Eligible Borrowers	Any legal entity including individuals, partnerships, corporations, public agencies or any combination thereof
Eligible Projects	Affordable rental and ownership housing including transitional housing, mixed income developments and mixed use projects. <u>Note – the Fund does not offer financing for individual home buyers or home owners.</u>
Eligible Use of Funds	Project planning and predevelopment, site acquisition, site development, construction, rehabilitation or to fill other financing gaps.
Income Targeting	Very low, low and/moderate income households and/or households with special needs. Note – the Fund will finance mixed income projects that include market rate units.
Location of Project	The Fund will only finance projects that are located in San Luis Obispo County
Collateral Required	Real Estate, including junior and subordinate liens (other collateral may be considered on a case by case basis)
Location of Collateral	Negotiable
Maximum Loan	Negotiable
Maximum Loan to Value Ratio	100%
Maximum Loan Term	Generally 5 years
Required Payments	Borrowers must pay interest at least quarterly. An interest reserve can be provided for these payments.
Debt Coverage Ratio	1:1 An interest rate reserve or other revenues of the borrower may be used to satisfy this requirement.
Source(s) of Repayment	Must be identified and may need to be committed

### 2.2. Fair Housing and Discrimination

The Fund is an equal opportunity lender. We affirmatively support State and Federal fair housing and anti-discrimination laws and expect our borrowers to do the same. When considering applications and approving loans, we do not discriminate against any protected class and will not provide financing to borrowers or for projects that discriminate in such a manner.

The Fund offers financing for housing that is targeted for special needs populations or for specific income groups. While this housing is not available for the general public, the owners

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and sponsors of these projects may not unlawfully discriminate based upon race, ethnicity, religion, source of income or other factors.

### **2.3. Borrower's Capacity and Financial Strength**

The borrower's capacity and financial strength are very important considerations when evaluating whether an affordable housing project will be successful. Ideally, the borrower should have experience successfully completing housing projects that are similar in type and scale. When borrowers do not have direct experience, the experience of their advisors and other team members will be considered. We may also consider training and related experience when evaluating the borrower's capacity.

We review the borrower's financial statements and/or tax filings for at least the past two years plus the current year to date to evaluate whether there is sufficient income, equity and cash flow to undertake, carry out and successfully complete the proposed project. Co-borrowers and guarantors will be considered in this evaluation.

### **2.4. Project Evaluation**

We review and evaluate the project from a number of perspectives, including the following.

#### **2.4.1. Environmental Assessment**

One of first things that we request after we determine that a project is eligible for financing is an environmental assessment for the property that will be used as collateral for our loan. We want to be assured that the property does not have any environmental hazards. If the applicant does not provide an environmental assessment, we will order an Environmental Analysis from VERACheck at a cost of \$145, which will be billed to the applicant. Instructions for ordering a VERACheck Environmental Analysis are included as Exhibit 1 of these Guidelines.

#### **2.4.2. Development Approvals**

We review the development approvals that are necessary to complete the project and the project's current status in the development review and approval process to identify and evaluate risks that the project may not be approved or that the approvals will be delayed significantly. This review is facilitated when the applicant provides a clear timeline or schedule that clearly lists the public reviews and approvals that are needed to complete the project, the project's current status and the dates that reviews and approvals have been and will be received.

#### **2.4.3. Project Budgets and Financing**

We review and analyze the project's pro-forma budgets to determine and evaluate the project's development costs, operating income and expenses, and sales proceeds. We also review and confirm the financing commitments that the project has received. We generally condition our loans on the receipt of financing for the project's development phase. For rental housing, we also generally want the project to have commitments for the key sources of permanent financing.

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### **2.5. Sources of Repayment**

As noted above, we are concerned that the projects we finance will be able to repay our loans on schedule. During the term of our loan, we are concerned that the project or the borrower have sufficient income and cash flow to at least make interest payments on our loan. For development projects, we will consider financing an interest reserve so these payments can be made.

When our loan will be taken out by investors or permanent financing, we generally want commitments from the source of these funds. We will consider making loans without take out commitments for single family homes and small multifamily projects for which financing is readily available in the market.

### **2.6. Loan Collateral**

The Fund is concerned that the properties that serve as collateral for our loans have sufficient value to support the loan. The collateral for our loans is not required to be the project that we are financing. We will consider other property when necessary and appropriate. We will lend up to 100% of the value of the collateral for our loan if there are sufficient indications that the project will be completed successfully and our loan repaid on schedule. We will also subordinate our liens to other financing under these circumstances.

The Fund will not always require independent appraisals of the properties it finances or uses as loan collateral if there are other ways to establish the value of these properties. We will always require a copy of any appraisals that are obtained by our borrowers or other lenders.

### **2.7. Other**

The Fund reserves the right to review and consider other matters as part of the review, underwriting and approval of loan applications.

For additional information, please contact the Fund at:

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### Instructions for ordering an Environmental Analysis from VERAcheck

- Go to [www.veracheck.com](http://www.veracheck.com)
- Choose order form.
- Log in using User Name and Password.
- Complete order form.
- Contact Information – should already be completed by computer.
- Report Type – should be assigned (if not, choose from options).
- Property Information
  - Project/Site Name – enter names of Borrower & Project
  - Name and Type of Business Currently On-site – provide facility name (e.g. Johnson’s Bakery, Joe’s Auto Repair, Kmart, etc....) and/or facility current use (e.g. office building, retail center, bakery, multi-family, vacant land...etc.).
  - Acreage – enter Acreage or Square Footage
  - Loan # (if applicable) – optional
  - Street Address – enter City, County, State and ZIP
    - For raw/undeveloped land or other sites that do not have a good address, FAX a map (appraisal map, Mapquest, Yahoo, Google, Thomas Brothers are fine) which includes street names, with an X marking the subject site. Please FAX the map to the number listed on the order form 888-767-7484, and note the order number on the map.
  - Latitude and Longitude – optional.
- Additional Information – optional.
- Nearest Cross Streets and/or major roads/highways – optional.
- Property Type – select from drop down box.
- Shipping – use if report should be sent to another email.
- Additional Comments – note sending maps or request RUSH (\$50).
- Print order confirmation page for future reference. Be sure that you see the order number on your document.
- An e-mail message that includes hyperlinks to the Environmental Analysis and Invoice will be sent within 24 hours. The links are good for 5 business days.
- Save the Environmental Analysis and Invoice to the project file on the shared drive.
- Print the Invoice and process for payment.

VERAcheck account manager and contact:

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