TEXAS DEPARTMENT OF HOUSING AND COMMUNITY AFFAIRS

PROGRAMS COMMITTEE

Thursday, February 10, 2005
Waller Creek Office Building
507 Sabine Street, Room 437
Austin, Texas

COMMITTEE MEMBERS:

C. KENT CONINE
VIDAL GONZALEZ

STAFF:

EDWINA CARRINGTON

A G E N D A

P R O C E E D I N G S

MR. CONINE: I'll call to order the Program Committee meeting of the Texas Department of Housing and Community Affairs 9:35 in the morning. The first thing on the list is to call roll. Chairman Conine is here. Beth Anderson is not here. Vidal Gonzalez?

MR. GONZALEZ: Here.

MR. CONINE: We have two here. That's a quorum in my book. I don't know about our counselor's book. It's a quorum in my book.

If there is any public comment from anyone, please fill out a witness affirmation form for the agenda. Most of you know the drill. Right down here in front. Give it to Ms. Penny and she will allow you to speak. We have none currently. Is that correct?

VOICE: We don't have any.

MR. CONINE: We'll skip the public comment, because we have none. Moving on to item number one, which is a possible approval of the minutes from our meeting on November 12.

MR. GONZALEZ: So moved.

MR. CONINE: There's a motion and I'll second. Any further discussion?

(No response.)

MR. CONINE: All in favor say aye.

(Chorus of ayes.)

MR. CONINE: All opposed, say no.

(No response.)

MR. CONINE: The motion carries. Item two, we are going to talk about the standard op, SOPs I guess. Whatever that is, of the declaration of events of default on multi-family obligations. This ought to be fun. And the creation of new asset management committee, Ms. Carrington.

MS. CARRINGTON: Thank you, Mr. Conine. Last fall, the Department formed an ad hoc committee that included senior staff that had areas of responsibility related to asset management in our multifamily developments, and the group has been meeting on a regular basis. I think they meet twice a month.

And as they continued -- as they started their meetings and continued their meetings, we found out that really there was very valuable information that was coming out of these discussions. And the reason the Department created this committee was to be able to get ahead of transactions, multi-family, primarily financed with the HOME programs that were experiencing leasing difficulties, completion difficulties. In other words: to get a heads up on what was potentially going to be a workout situation.

And this is something that the department has not done in the in the past. We felt like this was a very prudent step for us to take.

And this committee, we are calling it the Asset Management Committee, and it consists of the Deputy Executive Director, the Chief of Agency Administration, the Director of Real Estate Analysis, the Director of Portfolio Management and Compliance, the Director of Multi-family Finance Production. The Director of Financial Administration and also our Agency's primary real estate attorney, and then other staff that was designated by the Executive Director.

And so I think the only other staff that I did designate on this committee was Tim Irvine, who is the Executive Director of Manufactured Housing Division. And the reason Mr. Irvine was included in this committee was because he does have a lot of really good experience as a regulator, as a lender, and we felt like he would bring some very valuable skills to this committee.

We have developed, as we do in this Agency, a standard operating procedure, an SOP. And we have provided you a copy of that SOP. And this SOP is in the format of all of our standard operating procedures over the last two years.

As we went through our reorganization and as we reviewed all of our processes, we did develop somewhat of a new format for our SOPs and part of our exercise over the last couple of years has been to put all of our SOPs, review them, first of all, and make sure they are still applicable. And then put them in this kind of format.

So with that, I have Tim Irvine who was elected probably unanimously by the committee to serve as the chair of the Asset Management Oversight Committee. And he is here to answer any questions, or to go through the SOP and kind of talk about the process we are using. And maybe some of the issues that we have identified that we are addressing early on so that it doesn't get into a foreclosure and a perhaps payback situation to HUD.

MR. IRVINE: If I may, I am Tim Irvine. I am the Executive Director of Manufactured Housing. And I also serve as consultant to TDHCA. And one of the things that Ms. Carrington has asked me to get involved with is this issue of how we manage, identify problems proactively in the multi-family portfolio. This is a task that has gone a number of directions which all fit together rather neatly, as you see in this SOP.

The first thing is simply to devise a policy statement, that when a multi-family transaction is identified that had as issue of non-compliance that would constitute an event of default under the operative documents, albeit a minor or technical default. That still kicks it out for an appropriate review and unless somebody with appropriate authority, namely the Executive Director, or her designee determines that the event of default should be waived or addressed through a modification, events as identified are to be declared.

And that puts the Department in the proactive position of managing these assets from the earliest possible moment. As we begin focusing on the information that was in hand, there were two things that were pretty obvious. One, we needed to refine our management reporting.

And we, at that juncture, involved the loan servicing area from financial accounting, and also the portfolio management and compliance section which does compliance reviews and documentation reviews and handles many of the amendment processes. So working with those two areas, we have been developing good management reports that identify these issues early on, and we are systematically going through the identified assets and referring them to the asset management function which is under real estate analysis, which is under the direction of Tom Gouris.

And we are asking them to provide right up to analyze these assets, prioritized from the most serious to the least serious. We are trying to knock out about half a dozen a month. That is probably a little bit of an aggressive goal, but I think it is something that some urgency is needed, because we really haven't fully gotten our hands around them yet.

Anyway, then as these presentations are brought to the committee, you have got all kinds of expertise in that room. You have got people who have been involved in compliance and monitoring issues. People who are intimately familiar with the intricacies of the HOME program or other program regulatory requirements. You have lawyers, workout specialists, multi-family production people. All of the different people who can bring these issues out and frankly, fashion the best possible recommendation.

And the Committee works on a recommendation basis. The Committee does not take any definitive actions. And as it makes recommendations, it will be sending them to the Executive Director for appropriate decisions. The Committee was also pretty meticulous about the requirement that all of this documentation be reviewed and approved by the Legal Services Division.

So that, in a nutshell, is what that committee does. I would say probably the greatest benefit of this committee, though, is a little less tangible. And that is developing inter-divisional trusts and working relationships between the people that originate the assets, the people that manage the assets, and the people that provide the support functions. I would be glad to answer any questions.

MR. GONZALEZ: Have you identified any common problems among some of the --

MR. IRVINE: Well, I think that the most common things are simply what we would call minor technical non-compliances, such as: failure to submit required reports on time, failure to maintain required documentation. And rather than let these situations languish, we think it is the Committee's charge to tell the affected obligors, I'm sorry, your project is not in compliance, and we are giving you notice and a reasonable opportunity to cure. And if you don't fix it, we are going to recommend that you be declared in default.

MR. CONINE: It won't surprise you probably, that I would have thought we were doing this already. Because the word compliance to me defines what you just described, basically. And so I now have a feeling of concern of what is going on with the Compliance Department relative to all the historical and all the documentation they give.

So back me up a little bit and say, tell me what we have been doing before last fall when the Compliance Department realizes that a report was not in, or a home loan skipped a payment. What was going on then, or what has changed significantly now?

MR. IRVINE: Sure. Frankly, there was already a great deal being done. As problems were identified, they weren't just filed away in a drawer. They were brought to the obligor's attention and efforts were initiated to bring these parties into compliance.

To the extent that serious issues were involved, that would threaten the viability of an asset, or whatever, the asset management function under Tom Gouris was also involved in specific programs and plans for these assets were being fashioned. This Committee was essentially an ad hoc committee originally that was brought together to add expertise, and flesh out this process.

And we simply viewed this as an opportunity to formalize the process to make sure in accordance with RP-36 that we have appropriate documented procedures and policies and reports in place so that we can show the board and other appropriate bodies with confidence that the systematic review and management of these assets is being handled. So yes, it was being addressed before. This is largely making it more systematic.

MS. CARRINGTON: It was being addressed in a very compartmentalized fashion. When we did our restructuring, we created a workout function. And that workout function is within the Department of Real Estate Analysis.

So when Portfolio Management and Compliance recognized that we had a HOME multi-family loan that was going down the tubes, they knew that that was something that is their responsibility and obligation to identify it. Why is it their responsibility and obligation to work it out? That is over with the real estate analysis division.

And what this has allowed us to do is involve all of the parties who have some interest and some function and some responsibility related to the particular asset, to be all together and saying this is what we see.

This is what we think needs to be done. This is what the financials look like. So that has really been the benefit.

Because I think what would happen in the past is that someone would recognize these issues and concerns. And as Tim says, it did not necessarily go into a drawer, but maybe we weren't prioritizing it, because we didn't have the right people in there talking about it. And so that is what this has allowed us to do.

And what we really were talking about for the most part is multi-family. Well, it is multi-family. And it is loans that have been funded through the HOME program, which, of course, is --

MR. CONINE: But that is a segregated unit of what we do as a multi-family umbrella.

MS. CARRINGTON: Right.

MR. CONINE: Are we just focusing on the HOME loans and multi-family, or are we doing everything?

MR. IRVINE: We are focusing on all multi-family activities.

MS. CARRINGTON: But I will say that the Department's greatest vulnerability and greatest liability is on developments that are funded through the HOME program, because we are the first lien lender. And so those are the properties that we have the greatest risk if it goes into foreclosure of not being repaid.

MR. CONINE: Right.

MS. CARRINGTON: Posted for tax foreclosure, when we could step in with an amount of money and pay the taxes, determine whether the asset can be salvaged, determine whether it can be reworked. Determine whether it can be sold.

So we don't solely focus on that, but it is, again, this part of our risk based review and analysis and where are our greatest risks. And our greatest risks are in multi-family transactions that are financed with the HOME program, because we are the first lien lender.

MR. CONINE: But we were doing that already. But now we are formalizing it?

MR. IRVINE: We are doing it more.

MR. CONINE: I mean, that is a little different spin than what I originally heard from you.

MR. IRVINE: I apologize.

MR. CONINE: So that makes me feel a little better.

MS. CARRINGTON: Well, I think in a very much more concerted, in concert with all of the divisions that need to be in the discussion.

MR. CONINE: So as a for-instance, if we have a HOME loan, a multi-family project that is now in default and Tom, for instance, can go back and look at the market study and the 115 debt service coverage that he originally thought he was going to get, and see actuals as to why that didn't work. He will be able to get some actual feedback on some of the front end underwriting he has been doing.

MR. IRVINE: He will then come back to the Committee with a recommendation as to the next steps to be taken. And the Committee will provide different vantage points that flesh out, question, test that recommendation and ultimately turn into a committee recommendation to the Executive Director.

For example, on a situation where you had somebody who had become delinquent in taxes, the Committee not only is involved in the issue of looking at the value in the property and the cash flows in the property and those kinds of things. But also it is the strategy of positioning yourself so that you have a leadership role in making sure that the property, however it is resolved, is ultimately used for housing purposes.

MR. CONINE: What size portfolio do we have where HOME loans of first liens, out there right now?

MR. IRVINE: I am sorry, I don't know that number.

MS. CARRINGTON: I see Laura Lang, do you have any sense of what that number is? Or Lucy? Ms. Trevino?

MR. IRVINE: You need to come to the microphone so that it can be recorded.

MS. CARRINGTON: Anyone from PMC can answer that question?

MS. GRONECK: Get her name.

MR. IRVINE: Introduce yourself and state your position.

MS. TREVINO: Lucy Trevino. I am the manager in PMC. And total HOME properties, we probably have about 140. I am not sure exactly how many of those we are first lien on, but it would probably be at least 50 percent.

MR. CONINE: Okay. Thank you. Once you get past the HOME portfolio, will this committee also take a look at our private activity bond portfolio, and our 9 percent tax credit portfolio?

Recognizing there is no direct loan funds that will be exposed to the Department, but there is a lot of other kind of liabilities hanging on the Christmas tree there that I think you should probably ought to take a look at. Is that just too big a job to do, or will this committee be able to do that?

MR. IRVINE: No, Mr. Chairman. That is not too big a job. It ultimately needs to be done. You will notice the language in the standard operating procedure doesn't talk about loans. It talks about program obligations, and that includes tax credits, LURAs, anything else. Anything where someone has an obligation to this Department relative to funds that were used for multi-family development.

MR. CONINE: So again, I will use a hypothetical example here for just a minute. Someone sends in their financial statement that they are required to do on property or whatever frequency it is. Quarterly, or annually or whatever. And it shows a negative cash flow for the year. Is that something that then would jump out. This committee would kind of take that information and do something with it? Make a phone call? Or is that sort of information being just thrown in a file somewhere?

MR. IRVINE: It would be my intention, and I believe it is consistent with the SOP that the assigned division that monitors that particular obligation would identify that as being a contractual event of default, and therefore it would be reported to the Committee for appropriate action.

MR. CONINE: What are we doing? What were we doing last fall when we get in a financial statement on a property that shows a negative cash flow for the year?

MR. IRVINE: I'll let Tom Gouris answer that.

MR. GOURIS: Tom Gouris, Director of Real Estate Analysis. We will continue to do what we have been doing. And that is a project that has a negative cash flow, if we have a loan document that is an issue, we could possibly bring it to this Committee.

Aside from that, we work with the applicant or the owner to see if there is anything that we can do to help resolve the cash flow situation. There are quite a few transactions that have cash flow difficulty, and especially with our HOME and Housing Trust portfolios, because we are the lender of last resort. And a number of those transactions are set up as cash flow loans or as deferred forgivable loans.

And so there was, in many of those cases, there wasn't an expectation of much if any cash flow to be available. So our ability to work something like that out is a little bit more difficult, but oftentimes, you know, we are still going to be looking at that, monitoring it, and seeing if there is a need for the ownership to change. Or if we have actually had some ownership changes occur because of those sorts of issues.

I think this committee is going to help us be more proactive in getting on top of deals before they get to the workout situation. We have been working out about 23 transactions. Well, we have right now, about 23 transactions that are in some form of workout with us.

MR. CONINE: Out of the 150 that she mentioned?

MR. GOURIS: Plus Housing Trust Fund, in addition to that. In addition to those 150 there is also Housing Trust Fund.

MR. CONINE: And what kind of volume have we got sitting over there? In the portfolio?

MR. GOURIS: Certainly less than the HOME number. So probably something more like probably something less than 100. And a big chunk of those, in recent years have been associated with tax credit transactions, and so they are less likely to be distressed.

They are less likely to be the type of transaction that to put on the transaction that we are seeing that is distressed is one where we are either the first or second lienholder. There likely isn't a conventional lender. And we are truly a lender of last resort with some other grant or subsidized financing.

Those are the transaction that are the workout transactions.

MR. CONINE: Okay. I can fully comprehend and understand why those might be having some trouble. I mean, we deep skewed some of them to 30 percent units and those sort of things. So I understand that. If you think about the magnitude of our quote multi-family portfolio, and we have been between 9 percent tax credit deals, between 4 percent bond deals, between HOME and Housing Trust Fund transactions over the last 15 years or so -- the program has been around.

You have over 100,000 units in the State of Texas that we have some sort of compliance monitoring associated with. And that is not a small job for anybody. And I appreciate the strategic tiering of responsibilities; it was take care of our own portfolio first before the rest, but I guess I want to hear that as we move forward with this project, that we are making progress at monitoring the rest of the portfolio.

And the areas that are especially critical to your job, Mr. Gouris, which is underwriting these things on the front end. Because if you are not getting the back end actuals of what the front end pro formas -- if you are not getting the feedback from those results, you can't do your job as well as you possibly could. And I think you need to be getting that sort of info. Have you been, in the past?

MR. GOURIS: Yes, sir. For the past seven years, I think, we have been getting owner's finance and possibly longer than that. But as long as I can recall, we have been getting owners' financial certifications, which is a part of our annual housing sponsor report, which is their financial statement for the year. And we have over the past three or four years, maybe five years actually, been able to use those as a tool in our evaluations and new transactions.

MR. CONINE: Yes.

MR. GOURIS: And in fact, we just finished automating that process. So now this year will be the first year that the owner or ownership group will be able to enter that information in electronically. And it will allow us to do a lot more analysis of that information, rather than have an entry of that information.

Because as you said, we have quite a few developments that we get information on, and sometimes it has been hard to get that information into the system and then analyze it. The time to analyze it has been smaller. The automated system is going to help us quite a bit.

MR. CONINE: Ms. Carrington, we can handle this task with the current staff that we currently have? It sounds like a FTE issue to me, but maybe it is not.

MS. CARRINGTON: Actually, the number of units, according to our legislative appropriation request is something like 227,000.

MR. CONINE: I was 50 percent short. Sorry about that. Try and do the math quickly in my head.

MS. CARRINGTON: And we do this monitoring really, in two different ways. We do it in-house, in our Portfolio Management and Compliance Division. We also have some contractors that do count against our FTE cap, and I think there are five of those contractors that we contract with to do inspections for our portfolio. And then we also have an outside contract with Texas State Affordable Housing Corporation, TSAHC, to do asset management on our bond and credit portfolio.

So we do it through a variety of different sources. And we did raise our fees this year, as you are well aware. And one of the reasons we have raised those fees is because the portfolio continues to grow and our responsibilities in monitoring continue to grow also.

MR. CONINE: So I think you answered the question. We don't need anymore people to do the function described in this standard operating procedure?

MS. CARRINGTON: Real Estate Analysis is working on adding one additional FTE that would not be a technical type of person. But we think would free them up to focus more on their technical work. But we are attempting to manage within our budget and within our FTE cap.

MR. CONINE: Okay. Any other questions?

MR. GONZALEZ: No.

MR. CONINE: Thank you. We appreciate that. There is no -- I guess. Do we need to recommend to the full board that this is a good idea, probably, from a motion standpoint?

MR. GONZALEZ: So moved.

MR. CONINE: I'll second. All that is in favor, say aye.

(Chorus of ayes.)

MR. CONINE: All opposed?

(No response.)

MR. CONINE: The motion carries. That looks like the last item I had on the Program Committee agenda. We stand adjourned. Thank you.

(Whereupon, at 10:00 a.m., the meeting was adjourned.)

C E R T I F I C A T E

IN RE: TDHCA Programs Committee

LOCATION: Austin, Texas

DATE: February 10, 2005

We do hereby certify that the foregoing pages, numbers 1 through 23, inclusive, are the true, accurate, and complete transcript prepared from the verbal recording made by electronic recording by Penny Bynum before the Texas Department of Housing and Community Affairs.

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Transcriber (Date)

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