Requirements for Volume Cap Recycling:

To preserve and recycle volume cap, bond issuers must (i) establish necessary programmatic documents, policies and procedures, (ii) accurately track and report activity on an ongoing basis, (iii) pay legal and other costs to establish and maintain a recycling program, and (iv) in most cases, pay interest costs on debt required for successful volume cap preservation and recycling.

All of this requires a significant allocation of resources by bond issuers.

Recycling Steps
Step 1:

Step 1: The California Municipal Finance Authority (CMFA) enters into a "Funds Exchange Agreement (Prepayment)" with the Trustee, Fiscal Agent or bank that holds the debt for an affordable housing project. As the project prepares to pay down tax exempt debt as it converts from construction to permanent financing the CMFA will advance funds from its credit line to the prior tax-exempt debt holder. This transaction allows the bond allocation to be captured and recycled into a new project. The volume that CMFA captures can be used as a recycled bond in a new project.

Under current federal tax law, the Available Recycling Amount must be allocated to finance a new qualified residential rental housing project under Section 142(d) of the Code within 6 months of the pay-down or pay-off, or the tax-exempt bond volume will expire.

Recycling Steps
Step 2:

Step 2: Prior to the issuance of the tax-exempt debt under Section 142(d) of the Code for another qualified residential rental housing project, CMFA will enter a new "Funds Exchange Agreement (New Loan)" with the Trustee or Fiscal Agent on the new tax-exempt issue. On the closing date of the new issue, a designated portion of one or more Available Recycling amounts carried by CMFA will be transferred to the Trustee, Fiscal Agent or new tax-exempt debt holder. The new lender will transfer to the CMFA a like amount of proceeds of the new tax-exempt issue, which the CMFA will use to retire that amount of its prior borrowing which funded the Available Recycling amount.

The transferred tax-exempt recycled bond volume will NOT count for purposes of allowing the borrower under the new tax-exempt debt issue to satisfy the 50% Test under Section 42 of the Code with respect to the 4% LIHTC, if any, on that issue.

California Debt Limit Allocation Committee's (CDLAC) Role:

CDLAC, as steward of the state's volume cap, has a compelling interest in supporting bond issuers developing effective and efficient recycling programs. Programs should be designed to preserve as much available volume cap as possible (minimizing losses resulting from failure to "capture" mortgage loan prepayments) and to recycle into new affordable housing transactions as much preserved volume cap as possible.

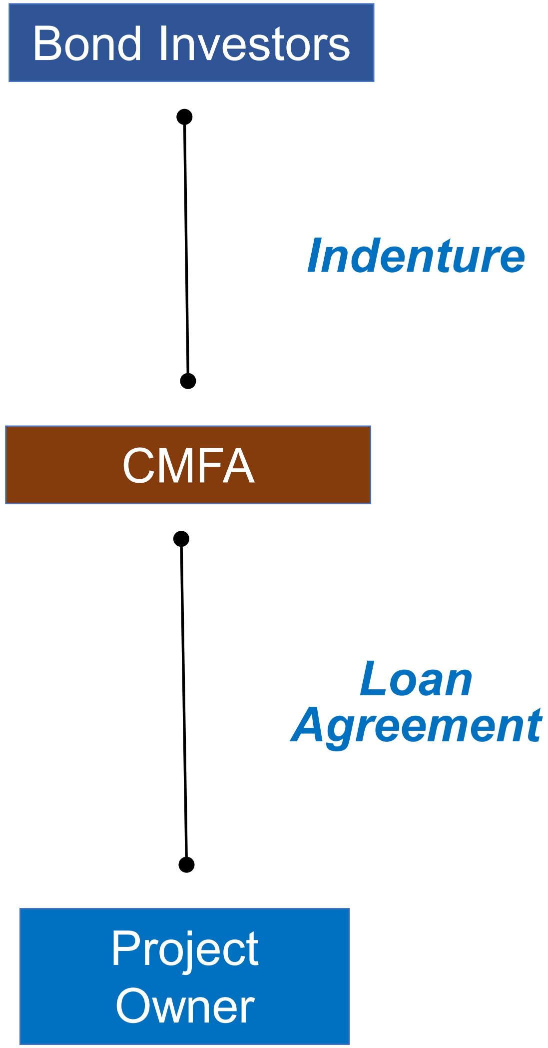
The preservation of Bonds can be recycled into new 4% deals or 80/20 deals that do not need LIHTC. By having 80/20 deals use recycled bonds it preserves new allocation for bond/tax credit transactions.

California Tax Credit Allocation Committee Regulations provide as follows:

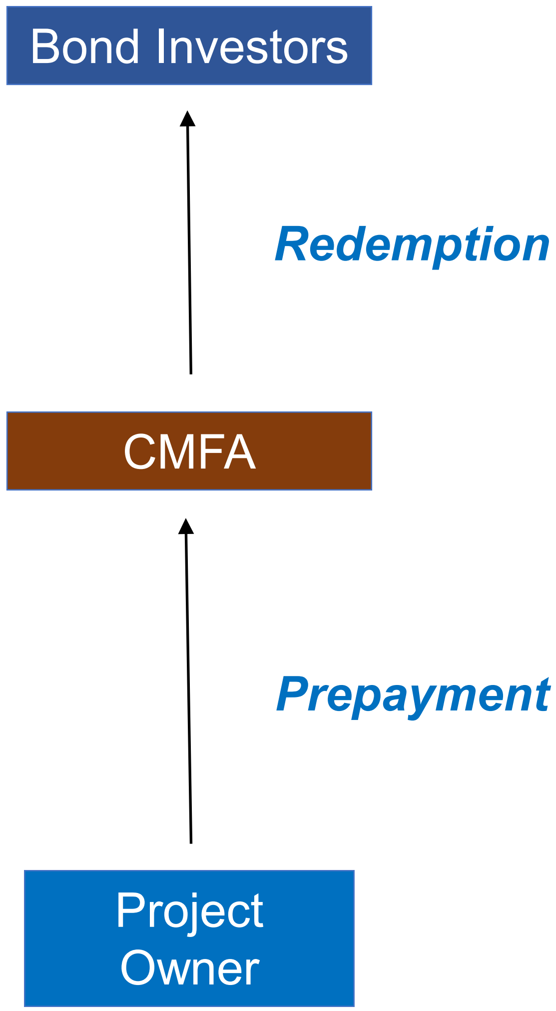
"For 4% credit applications, recycled private activity bonds (whether they be used for construction or permanent financing or both) shall be considered <u>leveraged soft resources</u> so long as the loan terms are consistent with market standards."

Because "leveraged soft resources" count favorably in CTCAC Tie-Breakers, developer sponsors are incentivized to make use of recycled private activity bond volume cap.

Initial Bond Transaction

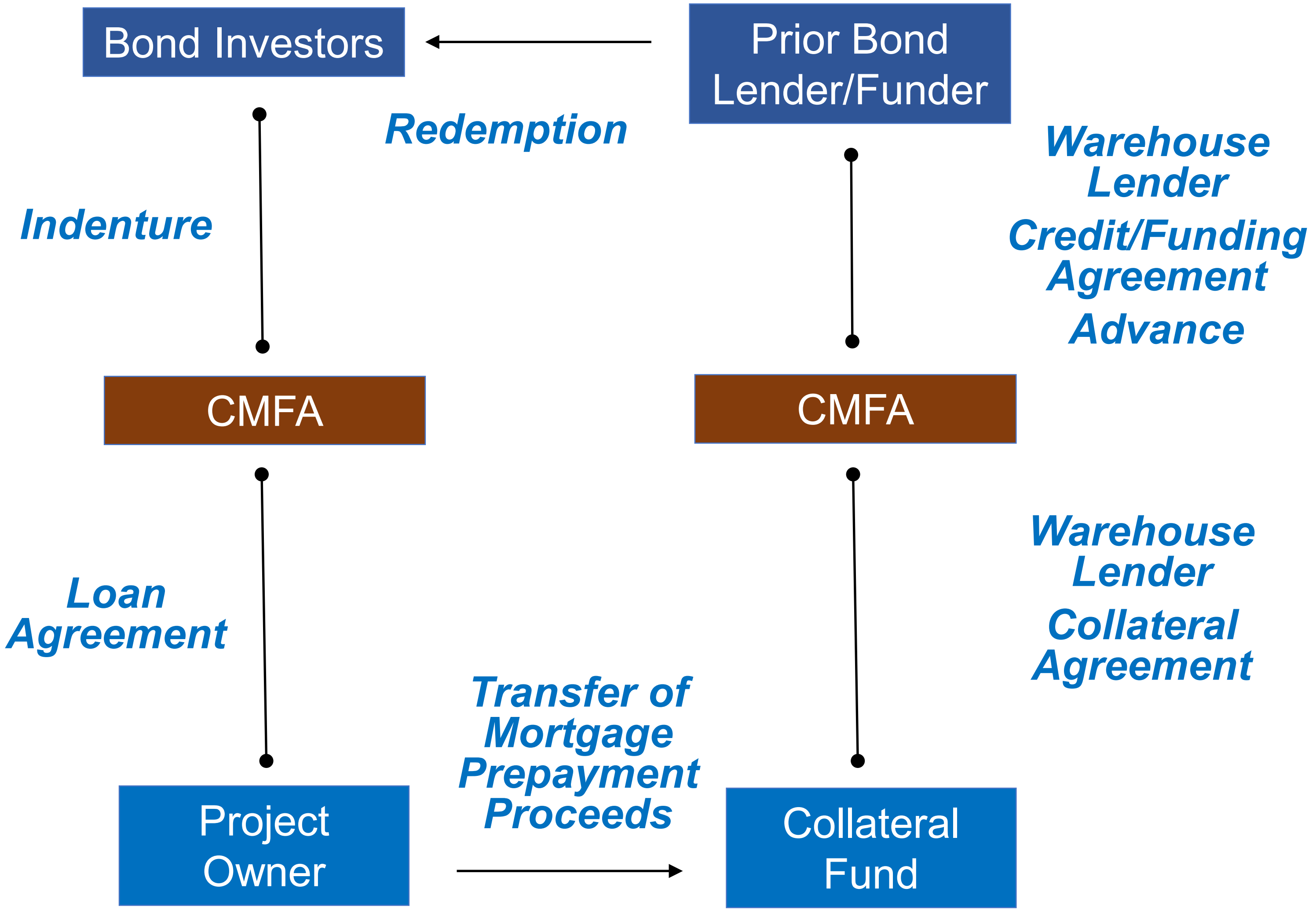


Normal Conversion Process



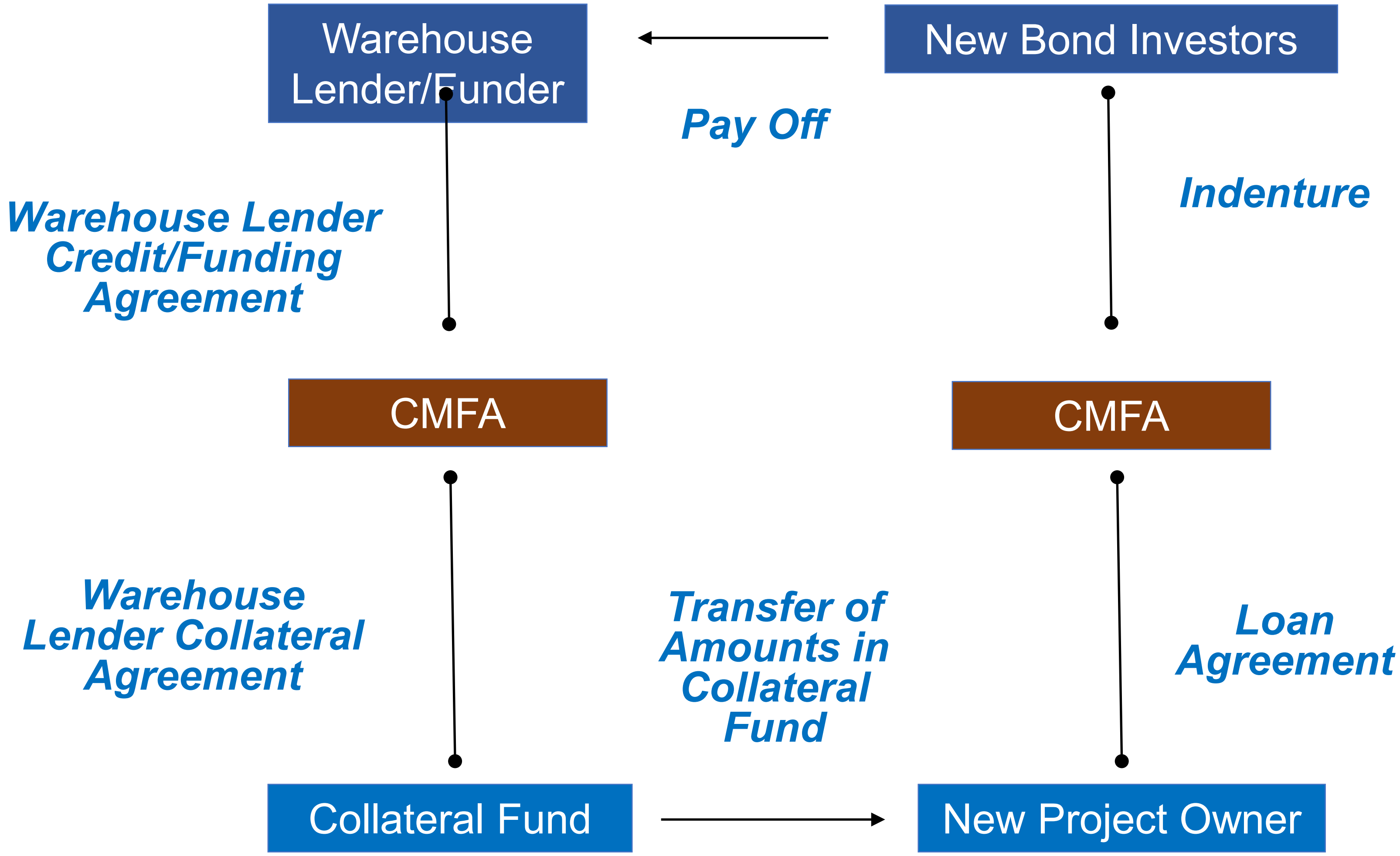
- Mortgage Loan prepayment passes through issuer
- Bonds are extinguished
- Volume cap is lost

Conversion with Preservation



- Mortgage prepayment in amount of $X is diverted into Collateral Fund
- Bonds in amount of $X are redeemed from proceeds of Lender/Funder advance
- Collateral Fund secures Lender/Funder Advance
- Volume cap is preserved for up to six months

Recycling into New Project



- Must occur within six months of Preservation
- Proceeds of new bonds are used to pay off advance from Warehouse Lender/Funder
- Amounts in Collateral Fund are advanced to make loan to new Project Owner
- Preserved volume cap is used to make new bonds tax-exempt

Current Law

- Recycled volume expires 6 months after a bond issue is paid down if not reallocated and closed within 6 months of the pay down.
- Recycled volume also expires 4 years after the original bonds were issued. No recycling of issues which are a refunding of prior bonds.
- The new tax-exempt bonds issued to which the recycled proceeds are reallocated must mature no later than 34 years after the original tax-exempt bonds were issued.
- The purpose for which the volume will be used must remain the same.

Post AHCIA

The **Affordable Housing Credit Improvement Act** of 2019 would improve recycling as follows

- Would expire 12 months after pay down.
- Would expire 10 years after original bonds issued.
- No exclusion of recycling volume of issues which have been previously refunded.
- Would allow recycled multifamily rental housing bond volume to be used to fund new loans for the first-time homeowners and veterans
- Would allow recycle bonds to go towards other bond allocation categories.