Request for City Council Committee Action
From the Department of Community Planning & Economic Development

Date: February 15, 2005

To: Council Member Lisa Goodman, Community Development Cmte
Council Member Barbara Johnson, Ways and Means/Budget Cmte

Prepared by: Mark S. Anderson, Senior Contract Management Specialist, Phone 612-673-5289

Presenter in Committee: Mark S. Anderson

Approved by: Lee Sheehy _____
Jack Kryst _____

Subject: Approval of policies for management of CPED loan assets

RECOMMENDATION: Approve policy recommendations A, B, C, and D as shown in the attached policy report relating to the ongoing management of the loan assets of the City of Minneapolis that were established by CPED/MCDA

Previous Directives: A series of previous policies were approved by the MCDA Board. The City also adopted a policy in 1999 for management of debt that gave the Finance Officer and City Attorney certain powers to write off or otherwise settle certain uncollectible debt. The 1999 report identified three exceptions for debt management policies that were separately adopted for the Utility Billing, Licensing and Inspections departments. This report would provide an exception for management of activities associated with CPED development and finance actions.

Financial Impact (Check those that apply)
_X_ No financial impact - or - Action is within current department budget.
(If checked, go directly to next box)

Community Impact (Summarize below)

Ward: All wards

Neighborhood Notification: Not required

City Goals: No impact on City goals

Comprehensive Plan: Not applicable

Zoning Code: Not applicable

Living Wage/Job Linkage: Not applicable

Background/Supporting Information

The MCDA Board and Executive Director established a number of administrative policies and procedures to conduct the business of that agency. Two of the policies related to the management of those City and MCDA loan assets that were originated through the various programs and services of the MCDA. In general, these policies authorized the Executive Director to manage financial assets – primarily loan obligations - by a combination of restructuring or write-offs within thresholds set by the MCDA Board. The intent of the policies was to provide staff with some flexibility to efficiently manage minor changes in financing terms and write off low levels of uncollectible debt.

As a consequence of the transition of MCDA to CPED, the City Council is now requested to approve the following policies that existed under the MCDA Board. These policies have been updated from the previous versions and the recommended changes are outlined below. Changes are highlighted under the title "What's Changed." Two key changes are to move the authority for such restructuring from the department director to the Finance Officer, and to raise the thresholds for restructuring and/or write offs from $20,000 to $50,000.

Policy Issue 1: Deferral of Loan Repayments

The borrower wants to temporarily defer making loan payments. The following policies will apply to such a request, which request must be in writing:

Policy Recommendation A:

If the loan is for $200,000 or less, the Finance Officer may approve a loan deferral for up to one year. Any other deferral request will first require review by the Development Finance Committee and then approval of the City Council.

What's Changed:

The previous policy approved by the MCDA Board gave this authority to the Executive Director. This change moves this authority to the Finance Officer. There has been no previous policy in existence for the City regarding deferral of debt payments.

<u>Policy Issue 2</u>: Restructure of Financing Terms

A borrower has made a written request for a change in the terms of a loan. Actions that fall into the category of restructuring are as follows:

1. Change in interest rate.

2. Forgiveness of any portion of a loan (principal or accrued interest).

3. Change in terms of City participation in project cash flow, income, or appreciation in value of a project.

4. Any action that results in a longer period for repayment of the loan, other than a deferral as described in Section I above.

5. Change in the collateral or security for a loan, or an increase in the amount of debt to which the City loan is subordinate.

<u>Policy Recommendation B</u>:

1. If the restructuring comes as a request for subordination of the City's loan on an owner occupied residential property, the request should be evaluated against the Residential Loan Subordination Policy (see Issue 4 below).

2. Any other loan restructuring or change in loan terms must be approved by the Finance Director or City Council, as indicated below, based upon a written report that documents the basis for the action.

    a. The Finance Officer may approve:
        i. A change of ownership provided the Project Coordinator has verified the experience, capacity, and financial strength of the new owner/partner.
        ii. A change in loan terms on a loan where the outstanding principal amount of the loan is $50,000 or less (other than a deferral which is subject to approval as described in Policy Issue 1) or where the change results in a potential reduction in revenue to the City of $50,000 or less over the life of the loan.
        iii. A change in loan terms for affordable multifamily rental housing with prior loan funds from the MCDA/CPED Multifamily Rental and Cooperative Program or the Affordable Housing Trust Fund program as long as:
            - The loan restructuring accomplishes long-term property stabilization and preservation (and/or extension) of the affordability of the units.
            - There is no retroactive interest or principal forgiveness.
            - The new loan terms are consistent with current AHTF guidelines (generally 1% interest with 30 year deferred term).
            - The loan restructure encompasses a change of ownership, but only if a related entity remains in the new ownership structure. Note: Effort should be made to reduce exit taxes paid to exiting limited partners.

- The loan restructure involves subordination, but only if the change either will make it more likely that the City's loan will be repaid or will not materially impact the likelihood of repayment of the City's loan.

iv. A change in loan terms for business finance or business development activity as long as:
- There is no retroactive interest or principal forgiveness.
- The loan restructure involves subordination, but only if there is no material impact on the likelihood of repayment of the loan.

v. A change in collateral or other security for a City loan provided the change will either make it more likely that the City's loan will be repaid or will have no material impact on the likelihood of repayment of the City's loan.

b. The City Council must approve any restructuring not covered above. Any restructuring requiring City Council approval, must also go to the Development Finance Committee for review and comment prior to City Council Committee review.

NOTE: If the current mortgage, promissory note, or other security agreements do not contain a default notification requirement, such a requirement must be included in the restructuring plan. The language to be included must specify that the borrower is required to notify the City within ten days of any default of its obligation on any other loan secured against the property. The language must also state that failure to provide this notice is considered a default on the City's loan. In addition, if another lender is involved in the proposed restructuring or changes in loan terms such as a request to have the City subordinate its loan to other financing, then that lender should be required to notify the City whenever the lender notifies the borrower of a default.

<u>What's Changed:</u>

The previous policy of the MCDA Board limited the Executive Director's approval authority to $20,000 or less. This policy raises that limit to $50,000 and moves the approval authority to the Finance Officer. The old MCDA Board approved a policy in the early 1990's that set the limit at $20,000. Staff is recommending that the limit be updated and selected the limit established under the City's purchasing policy at a logical limit. This policy recommendation also adds some language to more clearly address the management of business loans. The closest similar City policy deals with disputed or negotiated transactions that have been place with a claims adjuster. This policy relates only to activities that are a part CPED development or finance activities.

Policy Issue 3: **Delinquency**

A loan becomes delinquent.

Policy Recommendation C:

1. The Project Coordinator and legal counsel will review the circumstances and provide a report to the Finance Director. The Finance Officer may authorize any action deemed necessary and consistent with the governing documents of a loan and applicable law to enforce payment of loans, including commencement of a lawsuit, foreclosure, seizure of collateral, or any other remedy the law may provide.

2. The Finance Officer may authorize a write-off of a loan with an outstanding principal amount of less than $50,000 if the Finance Officer determines that the loan is uncollectible or the cost of collection will exceed the amount which is reasonably likely to be recovered.

3. Any other recommended action will require the approval of the City Council. If the recommendation is to write off the loan as uncollectible, then the following information should be included in the report:

    a. Original pro forma data and any other information that would be helpful in understanding the original recommendation and circumstances which resulted in approval of the loan.

    b. A summary of any neighborhood involvement in efforts to deal with the loan delinquency.

What's Changed:

The previous policy of the MCDA Board limited the Executive Director's write-off authority to $20,000 or less. The recommendation raises this limit to $50,000. The MCDA Board approved a policy in the early 1990's that set the limit at $20,000. Staff is recommending that the limit be updated and propose the limit established under the City's purchasing policy. In addition, the approval authority would move to the Finance Officer. The current City policy limits the Finance Officer's authority to $10,000 and gives a higher $25,000 limit of authority to the City Attorney. This recommended increase creates an exception to the 1999 limits by giving additional authority to the Finance Officer when it relates to debt that is uncollectible relating to CPED development and finance activity.

Policy Issue 4: **Residential Loan Subordination**

A homeowner has requested that the City subordinate its interest in a loan on a residential property.

Policy Recommendation D:

1. The CPED Director or a person or persons designated by the CPED Director may approve a residential subordination request that meets the following terms and conditions.

   a. Processing/Review Fee

      i. The City will be entitled to charge a reasonable fee for processing and review of each occasion where subordination is requested, even if there are multiple loans to be subordinated for a property. If a subordination request is resubmitted because of a change in the loan amount, an additional charge may be imposed. The Servicer must submit the fee at the time of the request.

      ii. The Servicer of a City loan is entitled to a reasonable fee for processing a subordination request. The Servicer may charge an additional fee per document for each additional loan.

      iii. The fee schedule and any subsequent changes must be approved by the CPED Director.

   b. Subject to conditions identified below, subordination may be granted to permit the mortgagor to benefit from an interest rate reduction or to shorten the term of their primary mortgage loan. This refinance may include any and all debt that is superior to the City's debt in lien status and may also include cash from the equity of the home. In no instance may the combined loan-to-value (CLTV) of the City loan and any loan that would be superior in lien status exceed 100% after the new refinance is closed.

      i. If the CLTV is above 80%, cash may only be obtained to complete repairs and improvements to the home. Any cash proceeds must be escrowed with the mortgage company or title insurance company and cash disbursements may only occur after construction work is completed. Any remaining proceeds left over after the work is completed may go for additional work to the home or it must be paid to the principal balance of the loan.

      ii. If the CLTV is 80% or less, the mortgagor may obtain cash without the completion of home repairs or improvements.

      iii. Except as provided for under number ii above, under no condition may the borrower receive proceeds from the refinance transaction, except to reimburse expenses paid by the borrower during the loan process, i.e. credit report and appraisal fee. If any cash is identified as a result of changes in the closing transaction, it must be applied to the principal balance of the new loan.

iv. CPED reserves the right to deny any subordination request it deems not in its best interest.

v. The original signed subordination document may not be released by the Servicer to the mortgage company or title company until the loan is closed. Upon receipt of the signed HUD-1 Settlement Statement (signed by the mortgagors and the closer) the executed subordination agreement can be forwarded to the title company for recording. A copy of the recorded document must be returned to the Servicer when available.

2. Any request that does not meet these requirements must be presented to the City Council for approval.

What's Changed:

The previous policy was approved by the MCDA Executive Director and not the City Council. This action provides policy approval by the City Council.

Signing Authority for These Policies

Contracts and other documents approved by the Finance Officer pursuant to authority delegated in these policies must be signed by the Finance Officer or his designee(s), as identified from time to time in written designation actions, and approved as to form by the City Attorney or an Assistant City Attorney. Residential loan subordination and satisfaction documents that use a document form that has previously been approved by the City Attorney or an Assistant City Attorney do not need to be routinely approved as to form.

What's Changed:

There is no specific change outlined in this policy point. It is being presented for the purposes of clarifying and providing guidance to staff.

Attached to this report is the City of Minneapolis policy coversheet and template, which presents the proposed policy is a concise format.