

Housing Finance Agency Innovation Fund for the Hardest Hit Housing Markets

Kentucky Hardest Hit Fund (HHF) Proposal Kentucky Housing Corporation August 31, 2010

SECTION ONE

Overview of Program

Background

On August 11, 2010, President Barack Obama announced an expansion of funding under the Housing Finance Agency Innovation Fund for the Hardest Hit Housing Markets, also known as the Hardest-Hit Fund (HHF). The expansion provides funding to states with the highest unemployment rates to offer a standard unemployment bridge program that will pay a portion of a borrower's mortgage while they are unemployed or underemployed.

The economic realities impacting the citizens of the state that led to Kentucky's selection as one of the states eligible to participate in this program are devastating to individuals and families and daunting to state and local agencies attempting to provide relief. In order to better respond to these needs, Kentucky Housing Corporation (KHC) is pleased to submit this plan in response to the U.S. Treasury Department's Guidelines for Housing Finance Agency Proposal Submission.

A. OVERVIEW

The Kentucky Unemployment Bridge Program is a statewide program focused on unemployed and under-employed homeowners who are at risk of mortgage loan default or have defaulted in payment of their mortgage loan due to involuntary loss of employment income. Homeowners in all 120 counties in Kentucky will be eligible for assistance under the program equally, although KHC will set aside \$10,000,000 in funding for the first 12 months of the program for rural counties as defined in this proposal.

Program Goal

The goal of this program is to prevent avoidable foreclosure for homeowners who have experienced loss of income due to unemployment or underemployment by providing funds to pay the household's mortgage payments during the period of unemployment/underemployment and for two months after re-employment, if needed up to the maximum dollar threshold for assistance.

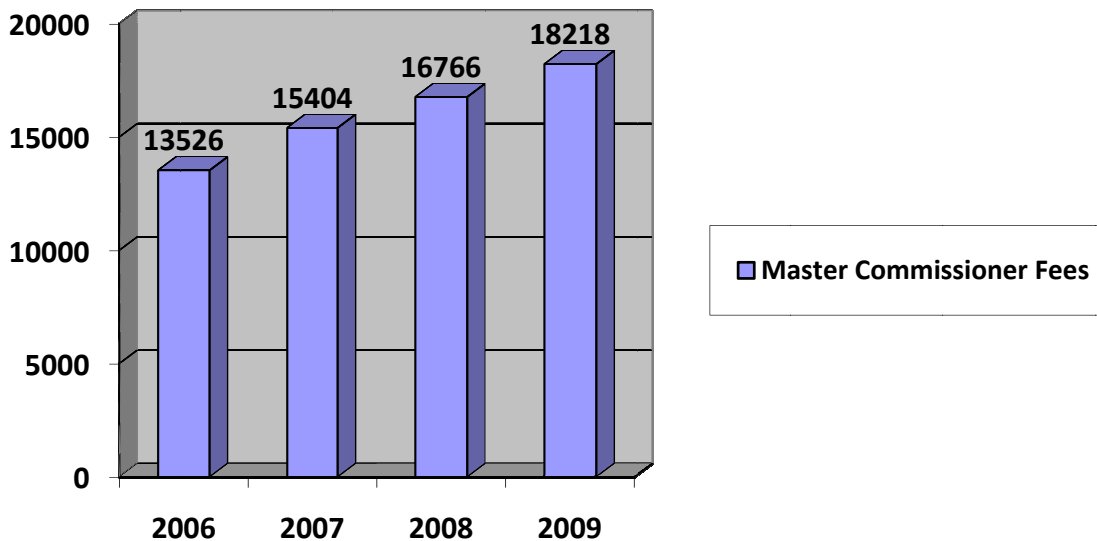
Unemployment, Mortgage Default, and Foreclosures in Kentucky

Kentucky's unemployment rate has consistently been above the national rate for several months, remaining at 9.9 percent as of July 2010, according to the U.S. Bureau of Labor Statistics. Kentucky has historically experienced unemployment rates higher than the national average. Beginning in fall of 2008 when national rates began to climb, Kentucky's rate consistently remained above the national rate by approximately 1 percent, climbing to a high of 10.8 percent in June 2009, and remaining at or near this level through mid-2010.

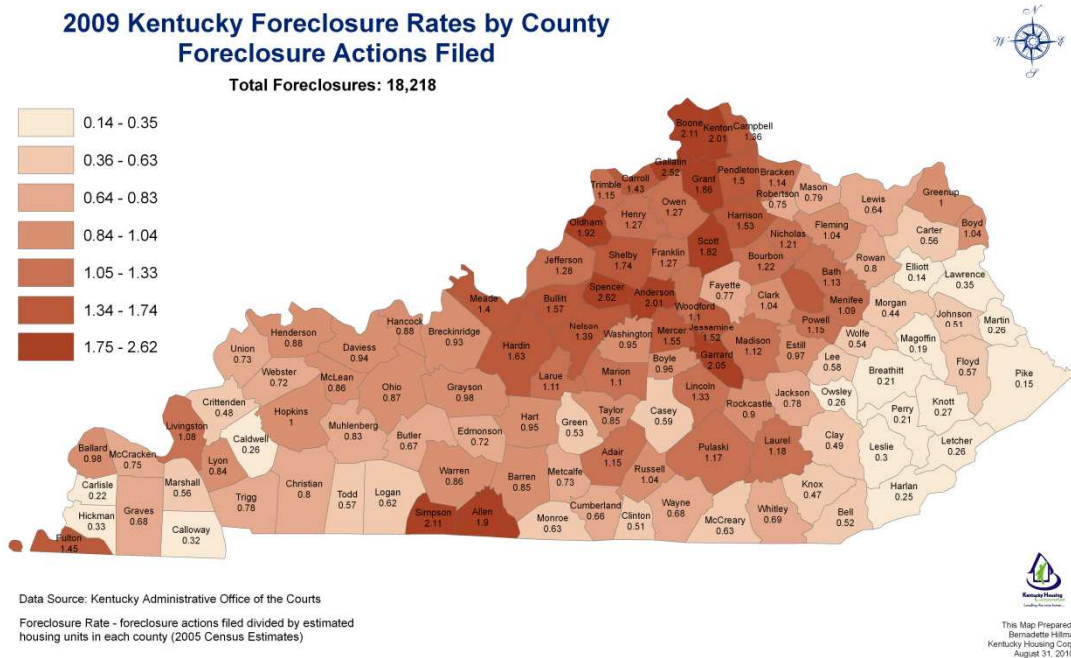
Current data suggest that more than 203,000 persons are unemployed statewide. More than 26,000 Kentuckians have lost their jobs so far in 2010 alone. Kentucky has experienced nearly 200 "mass layoffs" since January 2010. Over 91,000 persons in Kentucky have been unemployed for more than six months. The median length of unemployment is currently over 23 weeks.

More than 30,000 mortgages in Kentucky are in default – including those at least 30 days delinquent up to and including those in foreclosure. Since 2006, the number of foreclosures in Kentucky each year has been increasing. The Kentucky Administrative Office of the Courts (AOC) collects data monthly from county court systems on the number of foreclosure actions filed. Foreclosure actions in Kentucky have increased tremendously since 2006.

Foreclosures increased 14 percent from 2006 to 2007 and 9 percent from 2007 to 2008 and 8.7 percent from 2008 to 2009. It is expected that total foreclosures for 2010 will be higher than 2009.



The highest number of foreclosures, as expected, occurred in the highest population centers in the state as indicated on the following map.



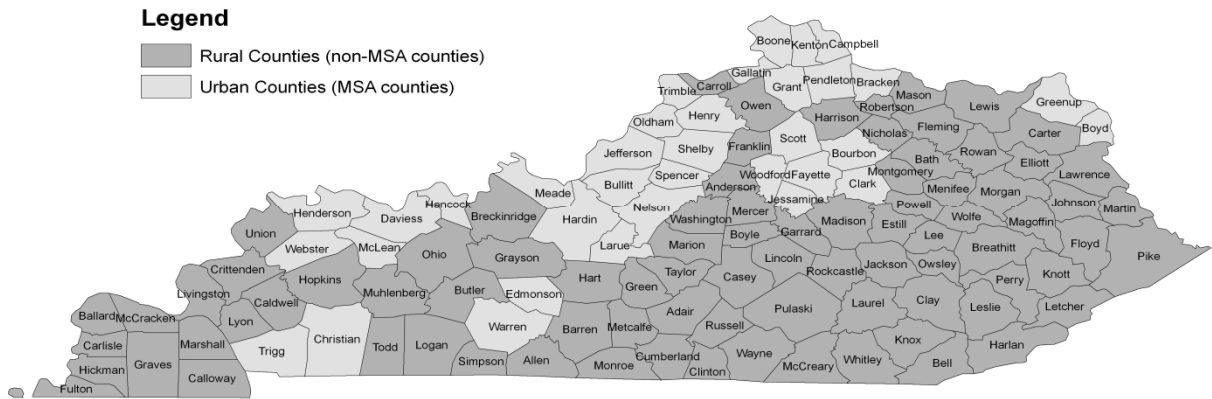
The program described in this proposal will serve the hardest-hit households in Kentucky who have experienced loss of household income due to the loss of or decrease in employment. As the data indicate, there is more need for assistance than assistance available. Therefore, Kentucky’s program will be limited to mortgage assistance for unemployed or underemployed households who are seeking employment and who meet the additional criteria of the program.

Kentucky Unemployment Bridge Program Design

The Kentucky Unemployment Bridge Program will provide funds to lenders and servicers on behalf of qualified homeowners who are delinquent on their mortgage payments or anticipate default due to unemployment or underemployment (loss of income). Maximum assistance per household is set at \$10,000 for the payment of eligible expenses as detailed in Subsection B of this program proposal. There is a time limit of 12 months for households to utilize the assistance – assistance ends at the sooner to occur of 12 months from the loan closing or \$10,000 in assistance, so long as other conditions of eligibility are met and continue. Funds will be available on a first-come, first-served basis. During the first 12 months of the program, \$10,000,000 will be set aside to serve rural counties, which are defined as counties not located

within a Metropolitan Statistical Area (MSA). A map depicting the MSA and rural counties follows.

Kentucky Urban and Rural County Designation



Timeline for Deployment

KHC will implement the program in two stages. The pilot program, estimated to begin January 2011, will target assistance to households in KHC’s loan portfolio, which is composed of families of low to moderate income. Statewide deployment to remaining eligible households is scheduled for April 2011. Additional timeline details are in the following table.

Estimated Date	Milestone/Activity
September 1, 2010	Proposal submitted to U.S. Treasury Department.
September 23, 2010	KHC provides information and technical assistance to counseling agencies at state housing conference pertaining to expectations under the proposed program.
Day 0	Treasury approves KHC plan
+30 days	KHC issues Request for Proposals (RFP) for title companies (if needed). KHC begins entering into Participation Agreements with servicers. KHC posts openings for available internal positions. KHC enters into Performance Agreements with counseling agencies. KHC finalizes assistance application package. KHC reviews loan portfolio and identifies potential households for assistance. KHC starts software development/enhancements and installs additional telephone lines.

+60	KHC begins offering additional training to counseling agencies as needed. KHC staff positions filled. Title company RFPs reviewed, approved. KHC/counseling agencies begin processing applications for assistance for households in KHC's loan portfolio. RFPs approved by KHC board of directors and filed with state. Marketing campaign design completed.
+90 days	Assistance Loans begin closing (pilot testing).
+180 days	Program is implemented statewide.

State Stakeholder Feedback

Since notification of receiving the funds to create the unemployment bridge loan program, staff members have been discussing the program design and use of funds with partners and other stakeholders across the state. Specifically, staff attended the Jefferson County Foreclosure Conciliation meeting in Louisville, Kentucky, on Friday, August 20, 2010. This group is composed of Metro Louisville government staff, County Clerk, Master Commissioner, counselor agencies, legal aid, attorneys representing lenders/servicers, nonprofits providing outreach to homeowners served a summons, the sheriff's office, judges, and staff from KHC. Staff discussed the purpose and scope of the HHF. Many were very excited to have another solution for struggling homeowners. Some were concerned that borrowers' salaries might have permanently decreased and that even though this loan would make their current payment, they were concerned that the mortgage may not be sustainable with new employment at the lower income level.

Staff also conducted five lender regional trainings where they discussed details of the HHF program with the partners. These trainings were held in Owensboro, Ft. Mitchell, Louisville, and Lexington and the discussions were held with over 200 lenders.

KHC also sought feedback regarding program design and use of funding through a survey that was conducted with our partnering counseling agencies and other partnering nonprofits and agencies. Overall, the feedback was supportive of the program and its design, as well as the proposed use of funds. Several counseling agencies identified the need for increased funding to support the level of counseling activities required under the program. Most agencies indicated that unemployed borrowers are a target population that they see often in their offices in need of assistance.

KHC will continue to solicit feedback from its partners and stakeholders. The statewide affordable housing conference, which typically hosts over 600 affordable housing providers from non-profit and for-profit agencies, occurs September 22-23, 2010. Staff will provide an explanation of the HHF program and solicit comments through a paper survey provided to each attendee in their conference packet. Likewise, KHC staff in the Homeownership and Loan

Servicing Departments, as well as in the Homeownership Protection Center (Protection Center), will continue to discuss the program design with partners and stakeholders in any meetings that will be held between September 1, 2010, and the date of program inception.

Program Implementation Obstacles and Mitigation

Communications and Marketing Challenges:

KHC, as well as other mortgage lenders and servicers, continues to experience challenges in the housing market due to declining home sales, extended periods of high-rate unemployment statewide, and a negative shift in homeowners' attitudes toward homeownership as a long-term, valuable investment. Foreclosure rates have increased, home loan rescue scams have been on the rise, and consumer confidence is low. All of these factors affect the efficacy of the message.

In the current environment, public perception will be challenging as information spreads about the bridge assistance and funds become available. KHC has not been able to offer rescue funds in the past to help homeowners and worked to encourage homeowners in need to seek loan modifications and payment decreases rather than to quit their jobs in order to receive the help they sought.

Communication and Marketing Solutions:

The overall objective of marketing is to communicate to unemployed/underemployed homeowners about a qualifying, forgivable loan option to protect long-term homeownership for those seeking employment meeting eligibility requirements. Low- and no-cost marketing options will be explored through a variety of communication methods to best reach targeted demographics over the course of the allotted \$300,000 budget. As a grassroots approach, KHC will partner with other state agencies, including the Kentucky Department of Financial Institutions, and the existing network of counselors for training, implementation, and statewide and targeted community outreach. KHC will begin marketing the pilot program to help current mortgagors and use its existing Web site to house and market program information.

Due to economic realities, targeted marketing tactics may entail traditional and nontraditional advertising methods, including television and radio public service announcements, billboards, newsprint, Web-related advertising, and community events, to reach audiences in various demographics and of various ages.

Counseling Network Challenges:

Kentucky has a strong counseling network in place that is trained in providing both homeownership education and counseling or legal services to those borrowers in need of foreclosure intervention and delinquency counseling services. This network of counselors has a decade-long history of working with KHC borrowers and staff and continues to provide service

to KHC clients on a daily basis. There are 51 agencies in Kentucky that provide counseling services in partnership with KHC who employ a total of 146 trained and certified counselors with an average of ten years of counseling experience. All of these counselors are certified through either the U.S. Department of Housing and Urban Development or NeighborWorks America. However, implementing a program to serve this number of clients will place a strain on agencies to provide the level of counseling and services required. Additionally, counselors work with many different programs, not solely KHC's programs, and they will need training on program requirements, eligibility determination, as well as counselor roles and responsibilities.

Counseling Network Solutions:

In order to strengthen the existing network of counselors within the state to best provide staffing for this program, KHC will use a portion of the grant funds to conduct training and provide technical assistance to build the capacity of the counseling agencies to participate in the HHF Program. KHC's Homeownership Protection Center staff will provide training on borrower eligibility and program compliance requirements with all counseling and support agencies as soon as possible. This will prepare the partner agencies to qualify borrowers using pre-determined eligibility requirements. In addition, agencies will be trained in HHF program requirements to prepare them to provide services within the rules of the program. All agencies will be trained in accessing updates and program information from the U.S. Treasury and other relevant governmental web sites as well as through notices from KHC as to program requirements and updates.

As an adjunct to this training and during the implementation stage, a complete assessment of training needs will be undertaken to gauge the skills and competencies of all agencies in using informational, client management and other data repository systems.

Individual counselor skills and competencies throughout the partner network will be measured to determine any additional training necessary to update counselors or to train new counselors on the new program guidelines and interaction with existing loss mitigation programs. This training will also encompass data capturing processes.

KHC will establish performance measures for the counseling agencies to ensure counselors are adhering to the roles and responsibilities outlined in signed Performance Agreements to receive funds under the HHF grant. KHC's Homeownership Education and Counseling department will oversee the counseling portion of the HHF program and will implement specific performance goals expected of each of the counseling agencies based on their case management capacity. In addition, KHC will include in the Performance Agreement with each counseling agency a specific work plan template for eligible HHF borrowers that will include required data and service points under the requirements of the program. In doing so, specific responsibilities and expectations of each of the counseling agencies in providing services to borrowers will be delineated and measureable by KHC.

KHC will use existing performance metric frameworks established through the NeighborWorks Foreclosure Mitigation Counseling (NFMC) Program, the HUD-trained counseling network or other programs with counseling agencies to measure programmatic compliance with both production goals and substantive service goals. In reviewing accomplishments through performance measurement, it may become apparent that the state needs additional counselors to fill service provider gaps. KHC Homeownership Protection Center staff understand that they may have to provide services in these underserved areas for a period of time. Likewise, KHC will reserve the option to hire additional counselors to provide statewide coverage in needed geographical areas.

Infrastructure/Program Setup Challenges:

KHC anticipates the need to add staff and technology to its existing infrastructure to meet the demands under the program. Included are new staff positions, staff locations, upgrades to the phone system, phone lines and software integration. Although KHC currently operates the statewide Protection Center, it is anticipated that the demand under this program will be greater than the existing level of staff and phone lines can handle. In addition, numerous loan servicing entities will be involved with households affected under the program. Negotiating and entering into Participation Agreements with these entities will be challenging.

Infrastructure/Program Setup Solutions:

These challenges will be partially alleviated by initiating the program with households in KHC's loan portfolio first before announcing the program statewide. This will allow KHC to begin assisting lower-income households first while operational staff members complete the infrastructure necessary to serve the broader public. The Kentucky Department of Financial Institutions will be instrumental in assisting KHC in obtaining Participation Agreements from the numerous loan servicing entities that are anticipated to be a part of the program.

Leveraging Other Resources

Kentucky's HHF program will dovetail with existing programs including the PROTECTION CENTER, the Homeownership Education and Counseling Program funded through HUD and KHC, and the NFMC. Homeowners who participate in the program will work with a KHC-approved counselor and utilize the Homeownership Protection Center web site for their initial information. Counselors will assist borrowers in ensuring they have used all other loss mitigation options before being eligible for HHF funds. This program will not be combined with other financial resources.

KHC staff members currently participate on the HOPE Now Alliance conference call with National Council of State Housing Agencies (NCSHA) and have solicited feedback on these calls, as well as through local outreach to community banks. KHC will also partner with the Kentucky Department of Financial Institutions, Mortgage Bankers Association, the statewide network of Area Development Districts, Kentucky Credit Union League, local governments, County Extension offices, nonprofit housing and social service entities, and the Kentucky Legislative Research Commission's Office of Constituent Services to market the program and integrate other social services that may be available to assist households in need.

B. POPULATION SERVED AND ALLOCATION METHODOLOGY

Current data suggest that over 30,000 first mortgage loans in Kentucky are delinquent or in foreclosure. The average age of these loans is 51 months and the average loan balance is approximately \$117,000. Using this data, KHC has determined that the average monthly mortgage payment per household (including principal, interest, taxes, insurance, mortgage insurance premium) is \$1,000. Unemployment in Kentucky is also very high, with over 203,000 persons presently unemployed. The average length of unemployment is six months.

Based on this data, KHC has established the maximum level of assistance under the program at \$10,000, which would allow the program to serve a minimum of 4,500 households. Given that unemployment averages six months and the program is designed to assist during the period of unemployment and for two months thereafter, the average amount of assistance is anticipated to be \$8,000, which would allow the program to serve 5,700 households. KHC is estimating that between 4,500 and 5,700 households will be served over the term of the program. The program's budget has been developed based on closing 5,000 assistance loans.

The program will be available statewide. KHC has excluded households whose mortgage payment does not equal or exceed 31 percent of present household income, those who have a loan-to-value ratio of greater than 125 percent, and those who are eligible for other loss mitigation options. To ensure that more moderate-income households are assisted, KHC has also limited the maximum total mortgage debt level to \$275,000.

Allowable uses of funding under the program include:

- Delinquent mortgage payments for first and second mortgages.
- Late fees, inspection fees, and attorney fees.
- Delinquent property taxes, homeowner's insurance, homeowner/condominium association dues or escrow shortage incurred as a direct result of the unemployment or underemployment event.

- Up to one year of standard homeowner's insurance, if the servicer has previously imposed forced-placed insurance and the forced placement was a direct result of the unemployment or underemployment event.

The total funding for the program is \$55,588,050 of which \$9,959,865 will be used for counseling costs, administrative costs, closing costs, etc., as described in the program budget. The remaining \$45,628,185 will be used for direct household assistance. Funds will be available on a first-come, first-served basis.

Eligible households must meet ALL of the following requirements:

- The homeowners must be legal U.S. residents.
- The financial hardship (loss of employment income) must have occurred after January 1, 2009.
- Monthly payment of principal, interest, taxes and insurance (PITI), including both first and second lien mortgages, must exceed 31 percent of the borrower's gross monthly income at time of application for HHF, including any unemployment benefits.
- The homeowner's cash reserves cannot exceed six months, excluding retirement. For purposes of this program, "cash reserves" includes reasonable and sufficient funds (as defined by the Internal Revenue Service Financial Collection Standards) for the payment of food, clothing, housekeeping supplies, miscellaneous household expenses, out-of-pocket health care expenses, utilities, child care, and transportation.
- The homeowner must be experiencing a financial hardship due to involuntary loss or reduction in employment income documented by an executed hardship affidavit. Unemployment or underemployment as the result of a documented short-term disability will also qualify.
- Payments due on the homeowner's mortgage(s) must have been current for 12 months preceding the unemployment and/or underemployment event.
- All final eligibility determination will be made by KHC.
- The homeowner must agree to participate in ongoing homeownership counseling through a KHC-approved counselor during the term of assistance.
- The homeowner must be currently seeking employment and/or participating in a job training/educational program with the goal of obtaining employment during the term of assistance.

Property/Loan Eligibility Requirements:

- Owner-occupied primary residence is located in Kentucky
- Combined loan-to-value cannot exceed 125 percent and a maximum of \$275,000.

- Existing single-family homes or condominiums (attached or detached) and manufactured or mobile homes on foundations permanently affixed to real estate owned by the borrower.

Program Exclusions:

A household is not eligible for the program if:

- Borrower's total unpaid principal balance exceeds \$275,000, including first and second mortgages combined.
- Borrower owns other real property.
- Borrower's hardship is a result of voluntary resignation of employment or voluntary reduction in hours or income.
- Borrower has consummated a cash-out refinance after January 2009, unless the proceeds were used for improvement of the subject property or for debt consolidation (KHC reserves the right to make a final determination in all cases).
- Borrower's application is for a second home or investment property.
- Borrower is participating in or eligible for other loss mitigation options.
- Borrower does not occupy the property as a primary residence.
- Borrower's present household income is sufficient to pay mortgage expenses (mortgage payment does not exceed 31 percent of gross income).

The program will not fund job training costs.

Structure of Assistance:

Participating households will receive a non-recourse, non-amortizing, zero percent interest, five-year loan secured by the property that will only be repaid from equity proceeds of a refinance or sale. The lien will be subordinate to the homeowner's existing first and second mortgages. Twenty percent of the loan balance will be forgiven each year on the anniversary of the closing date. Loan repayments and unused proceeds will be recycled back into the program and used to provide assistance to additional homeowners through the end of the program, December 31, 2017. Any funds on hand on or after the program end date will be returned to the U.S. Treasury.

Maximum Household Assistance:

The maximum amount of assistance per household under the program is \$10,000 to include eligible items described previously. The cost of application processing, counseling, and loan closing will be paid through administrative fees and not charged against the household's eligible level of assistance. There is no maximum amount of assistance per month.

Duration of Assistance:

Payment of assistance will end on the first to occur of: (1) 12 months from assistance loan closing date, (2) two months after re-employment, (3) the expenditure of the maximum amount of assistance (\$10,000), or (4) the household no longer complies with other required program provisions.

In the case of a new qualifying event of unemployment or underemployment, the household may reapply for assistance, provided, that the new assistance will be made available only to the extent funds are available, up to the maximum total assistance for the household, and the maximum time period for assistance has not been exhausted.

As described under “Structure of Assistance,” loan funds will be due and payable if the property is sold, refinanced, or no longer occupied by the owner as a primary residence. Twenty percent of the loan balance will be forgiven each year on the anniversary of the closing date.

C. DEMONSTRATION OF CAPACITY TO IMPLEMENT

KHC, the state housing finance agency, was created by the 1972 Kentucky General Assembly to provide housing opportunities for lower- and moderate-income Kentuckians. KHC is a self-supporting, public corporation administratively attached to the Kentucky Finance and Administration Cabinet. Through the sale of tax-exempt mortgage revenue bonds and the receipt of administrative fees, KHC offers lower-than-market rate home mortgages, multifamily housing production financing, homeownership education and counseling, a variety of rental assistance, housing rehabilitation and specialized housing resources programs.

KHC is uniquely qualified to create and administer the Kentucky Unemployment Bridge Program and utilize the HHF dollars as the state’s lead agency in assisting families to stay in their homes and to prevent avoidable foreclosures. Additionally, KHC administers numerous federal housing programs as the state’s affordable housing finance agency.

Although KHC is the state housing finance agency for the Commonwealth of Kentucky, it is not a state agency. KHC is defined in its enabling legislation as: “an independent, de jure municipal corporation and political subdivision of the Commonwealth which shall be a public body corporate and politic to be known as the Kentucky Housing Corporation.” [See KRS 198A.030 (1) attached] KHC was “created and established as a de jure municipal corporation and political subdivision of the Commonwealth to perform essential governmental and public functions and purposes in improving and otherwise promoting the health and general welfare of the people by the production of residential housing in Kentucky. [KRS 198A.030(2)] KHC is governed by an independent board of directors [See KRS 198A.030(3) attached] pursuant to bylaws. [See Bylaws attached] Since KHC is a de jure municipal corporation, it has no separate Articles of

Incorporation; the enabling legislation serves the function of the Articles of Incorporation. Additionally, as the HFA, KHC meets the definition of a “financial institution” through its loan functions. KHC makes mortgage loans to help provide affordable housing options to low and moderate income Kentuckians, either through single-family loans or loans for rental housing production. Based on this business, KHC is regulated as a financial institution by state and federal laws. [See 198A.040 attached] Given KHC’s status as a de jure municipal corporation and as a lending institution, KHC should qualify as an “eligible entity” in order to receive the Hardest Hit Funds from the Emergency Economic Stabilization Act of 2008, as amended (EESA).

KHC currently operates the Homeownership Protection Center (Protection Center), a statewide program that provides a centralized location for information on public services to assist Kentuckians in keeping their homes. Established by the 2008 Kentucky General Assembly to address the foreclosure crisis in Kentucky, the Protection Center helps homeowners find information on the foreclosure process, utility assistance and home repair assistance to help them make smart choices and avoid losing their homes. Financial counselors, attorneys, and public assistance agencies work through the Protection Center to help borrowers understand their options, receive counseling at no cost to the homeowner, and obtain assistance for eligible borrowers through the Kentucky Legal Aid Society when they cannot recover from their circumstances through counseling alone.

In addition, KHC administers the National Foreclosure Mitigation Counseling (NFMC) program which provides foreclosure counseling and budgeting assistance to homeowners at risk of losing their homes. Since 2008, nearly 4,000 homeowners have received counseling services through this program. KHC has developed a strong network of partners throughout the state to assist homeowners. Collectively, this network of counseling agencies employs more than 70 foreclosure counselors and specialists with an average of ten years of experience. KHC’s Homeownership Education and Counseling Program has been in operation over ten years and has counseled thousands of homeowners and prospective homeowners throughout the state with a staff of KHC counselors and through the same network of partners who provide assistance under the NFMC program.

KHC currently administers other programs funded through the American Recovery and Reinvestment Act (ARRA) including the Tax Credit Exchange Program allocated through the U.S. Treasury, Tax Credit Assistance Program, Homeless Prevention and Rapid Rehousing Programs through the U.S. Department of Housing and Urban Development, and Weatherization Assistance Program through the U.S. Department of Energy. The infrastructure required to administer HFA has already been established as a result of administration of existing ARRA programs and other federal housing programs.

KHC's Homeownership Program was established in 1972 as the first program at KHC. KHC has financed affordable first-time homeownership for over 81,000 households over the past 38 years. The KHC Homeownership Education and Counseling Program, under which the HHF will be housed, consists of a program director, program administrator, assistant program administrator, program evaluator and certified comprehensive homeownership counselors. The HHF will be overseen by the senior director of KHC's Homeownership Department and the director of the Homeownership Education and Counseling Program in partnership with staff from KHC's Loan Servicing, Organizational Planning and Performance, Program Tracking and Funding, Accounting, Compliance, and Audit Departments as described below.

Key Staff

Brenda Weaver, chief program and policy officer, will oversee coordination of the program and the development and implementation of program policy and partner relationships, including acting as the primary contact with the U.S. Treasury. Ms. Weaver has 28 years of experience in the affordable housing industry with KHC and other financial entities.

The HHF will be primarily administered through KHC's Homeownership Department headed by *Brenda Walker* as senior director. Ms. Walker provides oversight in the planning and development of programs for clients and homeownership counselors. She has over 22 years of experience in the housing industry, including 16 years with KHC. Ms. Walker directs all aspects of KHC's multimillion dollar single-family mortgage lending program that has provided homeownership to thousands of families and is financed by a bond program rated AAA by Moody's Investor Services.

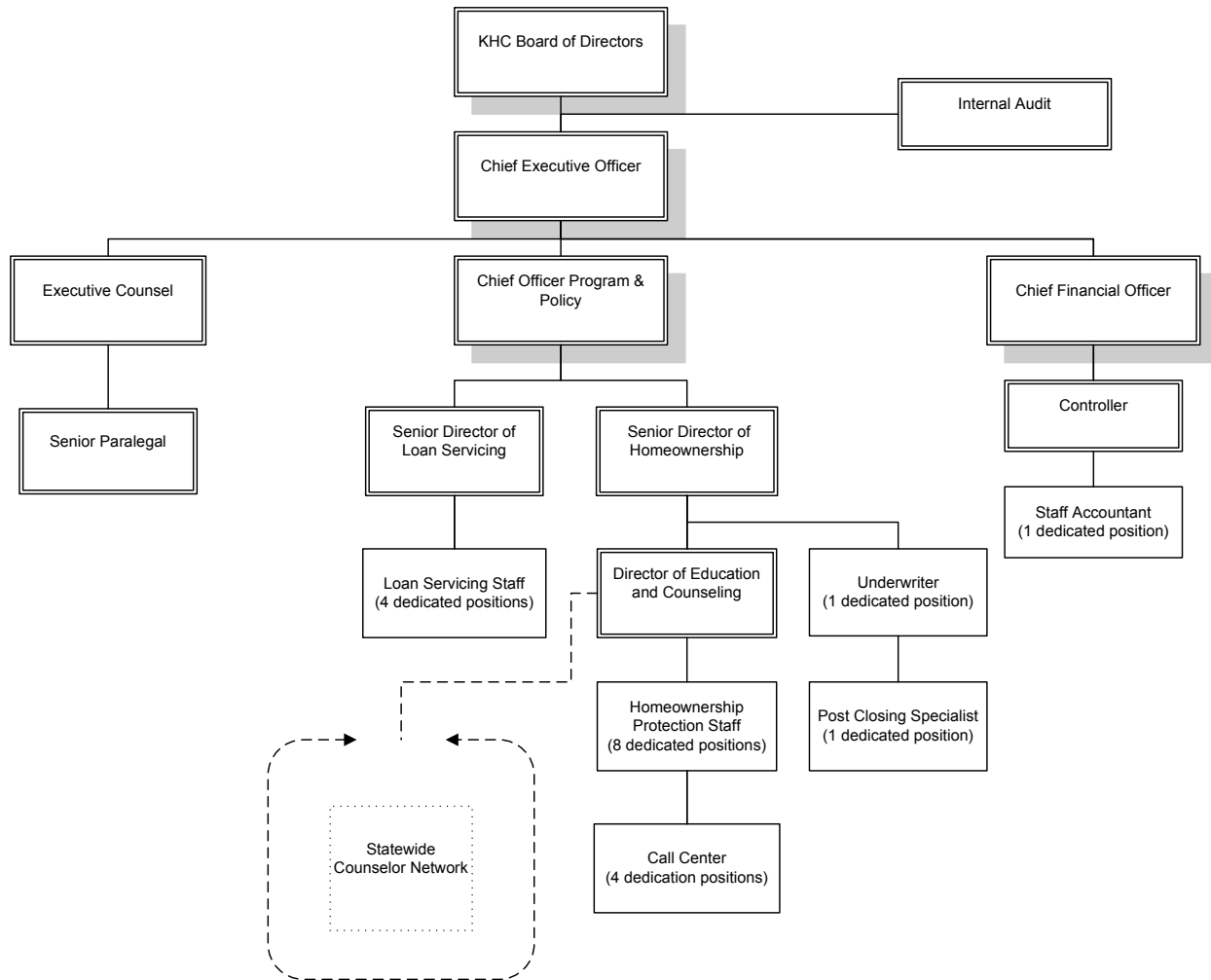
Abdon Ibarra, J.D., is director of KHC's Homeownership Education and Counseling Program. Mr. Ibarra is bilingual and has over 22 years of housing-related experience, including housing counseling and training, nonprofit agency management and foreclosure law. Mr. Ibarra also oversees the NFMC program and the Protection Center. Mr. Ibarra and his staff will assume responsibility for the operation of the program.

Numerous other staff responsible for the day-to-day operation of the program have numerous years of experience in foreclosure and loss mitigation counseling and mortgage underwriting.

Loans will be serviced in-house by KHC's Loan Servicing Department, a staff of 42 persons with many years of experience in all aspects of servicing single-family mortgage loans, currently with a portfolio of 25,000 loans.

The organizational chart on the following page details the reporting structure and internal relationships for the program.

**Hardest Hit Fund
Organizational Chart
(8/27/10)**



Compliance Infrastructure, Audit and Internal Controls, Risk Mitigation

KHC’s Internal Audit infrastructure is detailed in Subsection F of this program proposal. KHC will establish protocols for the program and performs reviews of outside partners who are administering funding allocated to them. The Internal Audit Department is responsible for evaluating internal controls established by management to mitigate fraud risks. In addition, KHC employs an outside, independent firm that performs an annual audit. Separation of duties

as described in the internal control plan also serves to mitigate risk of fraud. Monetary compliance is a separate function of program compliance.

KHC's accounting software system is Microsoft Dynamics. It is structured with unique cost centers for each source of funds, activity, and/or department and includes sufficient details to allow for tracking and reporting of each budget line item. Program activities and funds are also tracked in separate systems, including FICS, Housing Counselor Online, and CounselorMac. Protocols are in place to allow staff to balance program expenditures against receipts and to track funds allocated to each household assisted, title company, and housing counseling agency, as well as internal administrative expenses associated with the HHF.

KHC will underwrite each loan funded under the HHF before closing and will coordinate the loan closing and disburse funds directly to the household's mortgage servicing entity. KHC will also actively monitor the counseling agencies that will be required to submit electronic data through Housing Counselor Online that will allow KHC to monitor the success of households assisted. In addition, housing counselors have access to the Hope Loan Portal, an online interactive communications system that allows counseling agencies and loan servicers to share information and communicate about their common clients.

KHC will require the following minimum activities be performed to assist in mitigating errors and fraud under the program:

- KHC staff will underwrite each loan to ensure households and properties are eligible.
- Loan closings will be conducted by legal entities and personnel who will be responsible for –
 - Verifying the identity of the borrowers and
 - Recording legal documents.
- Loans will be serviced in-house by KHC's Loan Servicing Department.
- KHC will perform post-closing review of loan documents to ensure compliance.
- Staff will perform monitoring of each counseling agency to ensure that the agency is performing its responsibilities under the program.
- KHC program funding staff will be responsible for overseeing draws from U.S. Treasury and reconciling program reports, separate from program staff.

Reporting Protocols, Systems Infrastructure

KHC's Organizational Planning and Performance Department has established reporting protocols and systems for all stimulus-related sources of funding and serves as the internal reporting entity for these programs. Reports submitted to the Office of Management and Budget (OMB) and the U.S. Treasury, as required by regulation, are prepared and submitted by staff of

this department following the infrastructure in place for the six current programs at KHC funded with stimulus dollars.

Program data will be collected at different points of contact including:

- Initial inquiry
 - Number of phone calls
 - Disposition of inquiry
- Application receipt by counseling agency
- Ongoing counseling sessions by counseling agency

Program metrics expected to be collected and reported to U.S. Treasury include:

- Number of inquiries
- Number of qualified applicants
- Number of closings
- Number of months assistance provided and total dollar amount of assistance
- Total funds disbursed by budget line item
- Additional metrics as collected by the Protection Center detailed in the next section.

Relevant Program Implementation Experience

Since 2008, KHC has operated the statewide Protection Center, a program that provides a centralized location for information on public services to assist Kentuckians in keeping their homes. Established by the 2008 Kentucky General Assembly to address the foreclosure crisis in Kentucky, the Protection Center helps homeowners find information on the foreclosure process, utility assistance, and home repair assistance to help them make smart choices and avoid losing their homes. Financial counselors, attorneys, and public assistance agencies work through the Protection Center to help borrowers understand their options, receive counseling at no cost to the homeowner, and obtain assistance for eligible borrowers through the Kentucky Legal Aid Society when they cannot recover from their circumstances through counseling alone.

Through August 25, 2010, KHC has received nearly 10,000 inquiries through the Protection Center from homeowners needing assistance. The following data details the activities and outcomes tracked under this program.

Initial Mortgage Position

30 Days Late	939
60 Days Late	1,946
90 + Days Late	2,483
Current but anticipating delinquency	1,692
Summons has been served	2,006

Not a foreclosure issue	527
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Current Status

Referred to Counseling Agency	3,541
Referred to Legal Aid	577
Complete	1,211
No Response – Letter Sent to Client	658
Withdrawn – Duplicate or Client Denied	2,868
Initial call to KHC	346
Returned call by KHC	251
Reassigned	141

Client/Loan Information

Adjustable Rate Mortgage	810
Fixed Rate Mortgage	4,519
Average Original Mortgage Amount	\$100,000
Average Appraised Amount	\$82,702
Average Borrower Income	\$34,335

Outcomes

Chapter 13 Bankruptcy	58
Chapter 7 Bankruptcy	40
Mortgage Brought Current	61
Counseled & Referred for Legal Assistance	141
Counseled & Referred to Social Svc Agency	108
Entered Debt Management Plan	18
Executed Deed-in-Lieu	9
Forbearance Agreement	71
Foreclosure Prevention/Budget Counseling	169
KHC Client Referred to Counseling	12
Mortgage Debt Forgiven	2
Mortgage Foreclosed	67
Mortgage Modified	196
Mortgage Refinance - HECM	2
Non-Compliant	1
Obtained Partial Claim Loan from FHA Lender	2
Over Income – Referred to Private Bar	153
Pre-foreclosure Sale	17
Received Second Mortgage	1
Repayment Plan	34
Sold Property/Chose Alternative Hsg Solution	32

D. STAFFING AND BUSINESS PARTNERS

Staffing Plan

The HHF grant will be administered by KHC through the Protection Center which is staffed and housed by KHC. KHC will be executing agreements with its network of counseling agencies throughout Kentucky to provide eligibility determination and submit client financial information to the Protection Center for review and approval. KHC staff will provide administrative support for the daily activities associated with this grant, through the staff of the Protection Center and also through its staff in other departments to include marketing, legal and accounting services, as well as compliance monitoring and audit services.

The Protection Center will handle the day-to-day program delivery with regard to intake and processing of clients in the program. The Protection Center personnel primarily assigned to the delivery of the program include:

- Director of Education and Counseling (1)
- Default Counselor (1)
- Loss Mitigation Counselor (4)
- Program Administrative Assistant (2)
- Counseling Specialist (1)
- Call Center Manager (1)
- Call Center Representatives (4)

Director of Education and Counseling (1): The director will manage all aspects of the program, including counseling activities through the Protection Center and the statewide counseling network, as well as coordinate fiscal and compliance responsibilities.

Default Counselor (1): The counselor will oversee the pipeline of borrowers submitted to the program for evaluation and determination.

Loss Mitigation Counselor (4): The counselors will work directly with the borrower to collaboratively determine borrower eligibility for the program, as well as maintain case management responsibility with internal and external servicers or lenders.

Program Administrative Assistant (2): The program administrative assistants are responsible for maintaining program reports and other functions relating to the overall program administration.

Counseling Specialist (1): The specialist will oversee counseling plans and conduct follow-up on counseling plans designed for each individual borrower as required for participation under the program.

Call Center Manager (1): The manager will oversee four direct reports working as call center representatives, manage and monitor agency pipeline, and coordinate counselor transfer of clients to the Protection Center.

Call Center Representative (4): The representatives will take calls from the Protection Center hotline and web site requests, completing preliminary intake and demographics to determine the appropriate referral agency, mail the Comprehensive Intake and Document request package to the prospective client, track of all referrals and documents sent to partner counseling agencies, monitor agency pipeline, and oversee response to referrals.

KHC staff from the Homeownership Department and the Legal Department will underwrite the loan, ensure the loan file is complete before transfer to servicing, as well as assist in the loan closing. These staff members include:

- Underwriter (1)
- Post closing specialist (1)
- Senior paralegal (1)

Underwriter (1): The underwriter will review the borrower's financial package to determine if they meet all criteria outlined in the program summary guide. The underwriter will approve or deny the loan and communicate the determination to the counselor and/or homeowner.

Post Closing Specialist (1): The specialist will coordinate the loan closing date, as well as prepare the closing package. Once the loan is closed, the specialist will verify execution of all closed loan documents, work with the closing attorney to correct errors or omissions and enter the status in FICS software to begin payments on behalf of the homeowner.

Senior Paralegal (1): The paralegal will provide legal support for the program, to include assistance in closing the loans.

KHC staff in the Loan Servicing department will be responsible for processing and making payments on behalf of borrowers once loans are closed. Staff primarily assigned to the daily administration of the program include:

- New Loan Specialist (1)
- Customer Service Specialist (1)
- Investor Accounting Specialist (1)

New Loan Specialist (1): The specialist will process the loan import from KHC's origination software, audit data for accuracy, key in missing data and corrections, and prepare temporary coupons and welcome packages to all new mortgagors.

Customer Service Specialist (1): The specialist will answer all incoming calls regarding mortgage loan payments on behalf of the borrower as it relates to payment amount changes, name/address changes, etc., and assist in providing general customer service to borrowers.

Investor Accounting Specialist (1): The specialist will post payments and payoffs, balance daily receipts, ACH imports, prepare deeds-of-release, and research payment discrepancies.

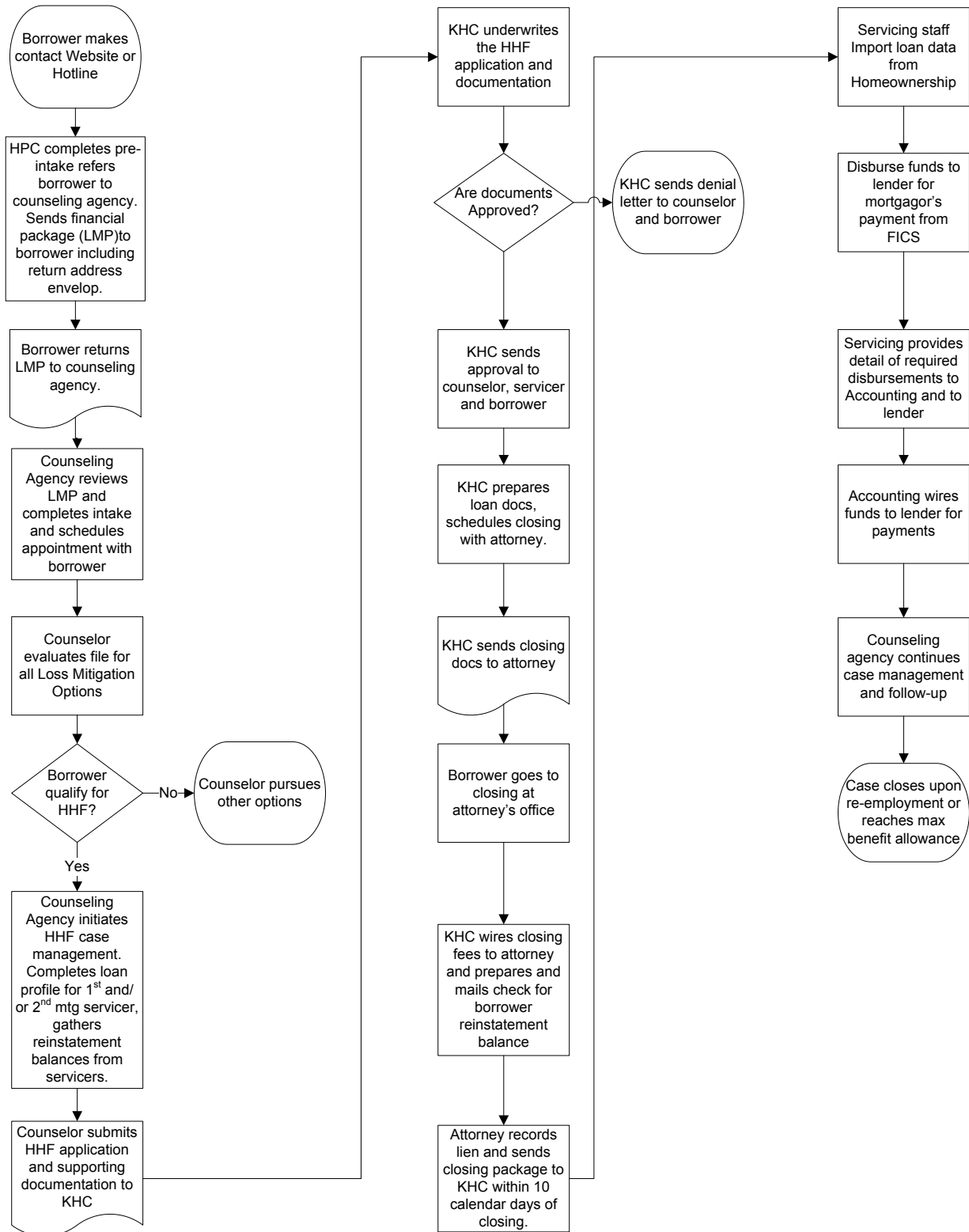
Staff in the Accounting Department will be responsible for making payments to the servicers. There will be one staff person, a staff accountant, assigned to the work and responsible for the daily processes in Accounting.

Staff Accountant (1): The staff accountant will process or assist in processing incoming receipts and incoming disbursements ,as well as fund transfers, and will provide support to the investor accounting and other specialists as needed.

The process is represented in the following flowchart.

Hardest Hit Fund Process

as of 8/25/10



Key Partners

The HHF will include the following partners and contract agencies.

1. Housing Counseling Agencies

Under the Protection Center, NFMC Program and Housing and Education Counseling Program, a network of housing counseling agencies exists that will be utilized to assist homeowners under the HHF. KHC will enter into agreements with counseling agencies, providing funding for pre-screening and ongoing counseling and program tracking. Counseling agencies will be paid \$300 for each program participant application review plus \$100 per counseling session for participating households, up to \$1,000 total. Because it is anticipated that most counseling sessions will be provided by telephone, counseling agencies must agree to provide counseling to program participants located statewide.

Partner Housing Counseling Agencies include:

Apprisen Financial Advocates (formerly Consumer Counseling Service)

Barren River Area Safe Space (BRASS)

Barret Center, Inc./Henderson Housing Authority

Bell-Whitley Community Action Agency, Inc.

Bluegrass Domestic Violence Program

Brighton Center

Catholic Charities

Chrysalis House, Inc.

Community Housing, Inc.

Community Ventures Corporation

Daniel Boone Community Action Agency, Inc.

Gateway Community Action Agency, Inc.

Homeownership Protection Center

Hopkinsville-Christian County Habitat for Humanity, Inc.

Kentucky Communities Economic Opportunity Council, Inc.

Kentucky Domestic Violence Association

Kentucky River Foothills Development Council, Inc.

Leslie, Knott, Letcher, Perry Community Action Council, Inc.

Kentucky Communities Economic Opportunity Council, Inc.

Kentucky Housing Partnership, Inc.

Live the Dream Development

Louisville Central Community Centers, Inc.

Louisville Urban League
 McCreary County Community Housing Development
 Merryman House
 Northern Kentucky Community Action Commission
 OASIS, Inc.
 People's Self-Help Housing, Inc.
 Pennyrile Housing Corporation
 Potentials, Inc.
 R.E.A.C.H., Inc.
 Sanctuary, Inc.
 Spring Haven
 Safe Harbor
 The Housing Foundation, Inc.

2. Servicers

Loan Servicing entities are important participants in the program. These entities are expected to act as an additional referral system for the HHF, review current portfolios of delinquent loans to determine which borrowers may qualify for assistance for the program, refer them to KHC, and work with counseling agencies and KHC to accept payments on behalf of borrowers participating in the program. The loan servicing entities with which KHC has a working relationship for this program include the servicers listed below plus numerous local loan servicing entities with which KHC currently works under the Protection Center:

AMHSI	Loan Care	Roundpoint Mortgage
Aurora	Litton	Saxon
Bayview	LBPS	SPS
Bank of America	MetLife	SunTrust
Citi	Nationstar	Vericrest
Chase	Ocwen	Vantium
GMAC	One West Bank	Wells/Wachovia
HomeEq	PNC	Hope Loan Port
Home Loan Services	Quicken Loans	HOPE NOW
HSBC	Residential Credit Solutions	Kentucky Housing Corporation

3. Closing/Title Companies

In order to mitigate fraud and error, KHC will utilize closing and/or title companies to close loans under the HHF. Once KHC's agreement with U.S. Treasury has been executed, KHC

will issue a Request for Proposals for these services. KHC is estimating that closing and recording costs will be a maximum of \$275 per transaction.

4. Other entities (no contractual relationship)

The following entities in Kentucky have expressed interest in participating with KHC in the program and do not fall under the previous categories.

- The Kentucky Department of Financial Institutions is the state agency responsible for oversight of mortgage brokers and lenders and other financial entities throughout the state. Their role will include outreach, marketing, and assisting with relationships between KHC and mortgage lenders and servicers operating in the state.
- The Kentucky Legal Aid Society currently participates in the Homeownership Protection Center Program and National Foreclosure Mitigation Program by providing legal services to persons facing foreclosure who income-qualify. It is anticipated that Legal Aid will assist some homeowners who wish to participate in the program and may be experiencing difficulty working with servicers or legal firms involved in the foreclosure process.
- Nonprofit affordable housing and social service entities throughout Kentucky will be instrumental in marketing the program, providing referrals, and offering additional non-mortgage assistance for which households may qualify.
- The Kentucky Legislative Research Commission (LRC) Office of Constituent Services works for all 138 of Kentucky’s legislators and receives inquiries from Kentucky citizens in need of assistance. Since the inception of the Protection Center, LRC staff has referred more than 2,000 citizens to the Protection Center of which more than 200 were related to unemployment.

E. ADMINISTRATIVE EXPENSES

Administrative expenses under the program are detailed in the table below and are based on 5,000 client loan closings.

	Kentucky
<i>One-time / Start-Up Expenses:</i>	
Information Technology	\$105,000
RFP advertising for Professional Services	\$1,500
Marketing	\$100,000
Computers	\$6,600
Telephone sets	\$2,500

Chair, desk set-up supplies	\$1,500	
Cabling for phones and computers	\$500	
Bank of New York start up fee	\$400	
Subtotal	\$218,000	2.19%
Operating / Administrative Expenses:		
Salaries	\$2,925,788	
Professional Services (Closing Attorney)	\$1,375,000	
Credit Reports	\$84,000	
Marketing	\$200,000	
Bank of New York Fee	\$1,975	
Training	\$10,000	
Utilities	\$10,270	
Cleaning	\$4,582	
Telephone line	\$35,550	
Supplies	\$13,200	
Postage	\$19,250	
Travel	\$19,750	
Subtotal	\$4,699,365	47.18%
Transaction Related Expenses:		
Recording Fees		
Wire Transfer Fees	\$42,500	
Counseling Expenses	\$5,000,000	
File Intake		
Decision Costs		
Successful File	\$1,500,000	
Key Business Partners On-Going	\$3,500,000	
Subtotal	\$5,042,500	50.63%
Grand Total		
Grand Total	\$9,959,865	
% of Total Award		
	17.92%	
Award Amount	\$55,588,050	
Program Funds	\$45,628,185	

Timeline for expenditures:

Fiscal Year	Administrative	Program	Total Expenditures
FY 2011	\$1,309,801.00	\$6,250,000.00	\$7,559,801.00
FY 2012	\$2,152,022.50	\$12,500,000.00	\$14,652,022.50
FY 2013	\$2,133,522.50	\$12,500,000.00	\$14,633,522.50
FY 2014	\$1,096,450.75	\$3,608,184.51	\$4,704,635.26
FY 2015	\$1,096,450.75	\$3,590,000.00	\$4,686,450.75
FY 2016	\$1,086,450.75	\$3,590,000.00	\$4,676,450.75
FY 2017	\$1,085,167.25	\$3,590,000.00	\$4,675,167.25
Total	\$9,959,865.50	\$45,628,184.51	\$55,588,050.01

F. OVERVIEW OF RISK MANAGEMENT/FRAUD PREVENTION

KHC has established an Internal Control Plan, implemented policies and procedures and designated an internal control officer in an effort to deter, prevent, and detect fraud and corruption. The Internal Control Plan delineates the concepts of adequate internal controls including the lines of authority and responsibility, segregation of duties, proper authorization for transactions, proper and adequate control over resources, as well as adequate supporting documentation.

The designated internal control officer is responsible for maintaining and updating the Internal Control Plan and ensuring its availability to corporate personnel and auditors. In addition, the internal control officer is responsible for ensuring that recommendations for the improvement of the internal control structure are promptly evaluated by KHC’s executive management team and implemented in a timely manner.

Furthermore, KHC employees are bound by Executive Order 2008-454; the Executive Branch Code of Ethics contained in the Kentucky Revised Statutes (KRS) Chapter 11A, and the KHC Code of Ethics adopted by the Board of Directors, as well as the requirements of KRS 198A.210 as it pertains to conflicts of interest. A copy of the Guide to the Executive Branch Code of Ethics is provided with all hard copies of the Employee Handbook. Additional copies may be obtained from the Human Resources or Legal Department or at <http://ethics.ky.gov>. Employees must avoid any actual conduct which constitutes a conflict of interest or conduct which gives a reasonable basis for the perception of a conflict of interest between their private and public interests.

- Employees are prohibited from taking action, performing any duty, or giving any preferential treatment from which they would benefit personally.

- Employees are prohibited from taking action which would result in illegal receipt of public or private funds.
- Employees may not participate in any official action relating to any entity or individual in which they or their immediate family has a financial interest.
- Current or former employees or officers must comply with restrictions regarding other employment, unwarranted privileges or self-exemptions, or improper exemptions.
- Employees must adhere to other standards of conduct described in Section 02-06 of the *Employee Handbook*.

Other fraud prevention measures require that all new employees, as well as temporary and contract employees, be pre-screened or subjected to background investigations including a criminal background check. KHC will also verify all applicants' employment history, education, and personal references prior to making an offer of employment.

All vendors, contractors and suppliers must be active, in good standing and authorized to transact business in the Commonwealth of Kentucky. Vendors, contractors and suppliers are subject to screening, including verification of the individual's or company's status as a debarred party.

In addition, contractual agreements with Kentucky Housing will contain a provision prohibiting fraudulent or corruptive acts and will include information about reporting fraud and corruption.

Compliance and Monitoring

Pursuant to *KRS 198A.170*, KHC is subject to an annual audit to be performed by a resident independent certified public accountant. The annual audit and examination of financial statements for Kentucky Housing Corporation must be performed in accordance with generally accepted auditing standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States and the Single Audit Act of 1984. This Independent Auditor's Report includes the consideration of KHC's internal control over financial reporting and the results of tests of KHC's compliance with certain provisions of laws, regulations, contracts and grant agreements. Furthermore, the OMB has determined that all Recovery Act federal awards be considered higher-risk programs per *Circular A-133 Compliance Supplement*, and therefore, subject to the requirements of the Single Audit Act, without regard to the \$500,000 threshold of expenditures for federal awards.

The most recent Annual Audit Reports of KHC's financial statements performed in accordance with *Government Auditing Standards*, and the annual Single Audit Reports performed in accordance with OMB Circular A-133 are available for review at <http://www.kyhousing.org/>

KHC established an internal audit function in 1987 by a Board- adopted resolution. With this resolution, an internal Audit Charter was approved. The charter outlines the purpose, authority and responsibilities of the internal audit function within KHC.

Specifically, the internal audit department was established as an independent, objective assurance and consulting activity reporting directly to the Finance Committee of the Board of Directors and administratively to the chief executive officer. The Internal Audit staff performs all audits and reviews with the objectives of evaluating the efficiency and effectiveness of internal controls, ensuring the accuracy of recorded information, and determining the extent of compliance with federal regulations and corporate policy.

In addition, Internal Audit staff also performs quality assurance reviews of KHC's Loan Origination and Loan Servicing Departments. These quality assurance reviews are performed in order to evaluate and ensure that loans comply with regulatory and program requirements.

Testing by the Internal Audit Staff is performed on a sample basis, but consideration is given to the loan correspondents to ensure that reviews performed during the year include files from all correspondents during the audit period. Special reviews are performed for all loans that have defaulted within six months of closing. On completion of the review, a report is prepared and forwarded to the appropriate department for comment. The Internal Audit director reviews all work papers and reports. Any responses are incorporated in the report and forwarded to management.

KHC intends to comply with the requirements of the Emergency Economic Stabilization Act of 2008 and allow oversight by U.S. Treasury, the Comptroller General of the United States, Government Accountability Office, Congressional Oversight Panel, and the Special Inspector General of the Troubled Asset Relief Program, as to the application of any Emergency Economic Stabilization Act (EESA) funds. KHC will make available upon request all records and communications regarding the use of EESA funds. Compliance with EESA will be achieved or provided by the existing internal control framework and through the inclusion and monitoring of program specific requirements. These program requirements will include an evaluation of homeowner eligibility, verification of income and/or employment status, and verification of mortgage payment amount.