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BOARD AGENDA ITEM: 8.A.(2)

DATE: February 26, 2009

SUBJECT: Approval, Proposed Revisions to the Qualified Allocation Plan (QAP) and Procedural Manual, 2010 Housing Tax Credit Program

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BACKGROUND:

The Federal Tax Reform Act of 1986 created the Housing Tax Credit Program (HTC) for qualified residential rental properties. The HTC program is the principal federal subsidy contained within the tax law for acquisition/substantial rehabilitation and new construction of low-income rental housing.

Section 42 of the Internal Revenue Code (IRC), requires that state allocating agencies develop an Allocation Plan for the distribution of the tax credits within their jurisdiction. The Allocation Plan is subject to modification or amendment to ensure the provisions conform to the changing requirements of the IRC and applicable state statute. Staff has reviewed the HTC program and is preparing the necessary modifications.

The Board approved the amended HTC 2009 QAP at its December, 2008 meeting. At the beginning of January, Minnesota Housing published the amended HTC 2009 QAP. This culminated a complex and tightly scheduled revision effort which began in July, 2008, in response to the Housing and Economic Recovery Act of 2008 ("Act"). The Act was a result of congressional response to volatile economic and market conditions. These conditions continue to exist with the potential for additional federal response likely resulting in additional HTC program changes in the coming months.

Historically, each year the HTC QAP is revised through Board action in a two stage process. Preliminary QAP approval is typically obtained in January with final approval in March. However, due to the continued volatility of the economy contributing to the complexity of the proposed revisions, an additional conceptual stage Board review was completed in January with preliminary approval this month and final approval in March.

DISCUSSION:

Proposed Revisions for the 2010 Qualified Allocation Plan and Procedural Manual

Attached is a summary of the proposed revisions to the 2010 Qualified Allocation Plan (QAP), Procedural Manual and Selection Criteria (Attachment A).

TIMETABLE:

2010 HTC PROGRAM SCHEDULE

February 26, 2009	Agency Board asked to approve preliminary 2010 QAP and Manual
March 4, 2009	Minnesota Housing 2010 HTC Public Hearing
March 26, 2009	Agency Board asked to approve final 2010 QAP and Manual
April 20, 2009	Publish RFP for HTC 2010 Rounds 1 and 2
June 16, 2009	HTC 2010 Round 1 and Fall 2009 Super RFP Application Deadline
July, 2009	Agency Board asked to approve qualifying accelerated selections of HTC 2010 Round
October 22, 2009	Agency Board asked to approve HTC 2010 Round 1 selection recommendations
January, 2010	HTC 2010 Round 2 Application Deadline (Tentative)
April, 2010	Agency Board asked to approve HTC 2010 Round 2 selection recommendations. (Tentative)

On January 8, 2009, staff met with tax credit suballocators to review, in concept, proposed revisions for the 2010 QAP and to adopt the 2010 HTC Program Schedule.

It is anticipated that Duluth, St. Cloud, and Rochester will again enter into a Joint Powers Agreement with the Agency to administer their 2010 housing tax credits.

A summary of the proposed revisions for the 2010 Qualified Allocation Plan and Manual were made available for public review on the Agency's web site following the January Board approval along with a notice of the upcoming HTC 2010 QAP public hearing. The Agency invites comments from tax credit developers, industry representatives, and the public regarding the Allocation Plan at a public hearing scheduled for Wednesday, March 4, 2009. Staff will review all comments, and changes will be incorporated into the HTC Allocation Plan and/or Manual where appropriate. The Board will review the Final 2010 HTC Allocation Plan and Procedural Manual at its March Board meeting.

Upon obtaining final Board approval of the HTC Qualified Allocation Plan and Procedural Manual, the application packets will be distributed to the potential applicants and staff will provide training.

MEETING AGENCY PRIORITIES:

- [x] **End Long-Term Homelessness**
- [x] **Finance New Affordable Housing Opportunities**
- [ ] **Increase Emerging Market Homeownership**
- [x] **Preserve Existing Affordable Housing**

RECOMMENDATION:

Staff is recommending adoption of a motion for preliminary approval of the proposed revisions to the 2010 Housing Tax Credit Qualified Allocation Plan and Procedural Manual.

ATTACHMENT:

Attachment A – 2010 Housing Tax Credit Program, QAP and Procedural Manual Proposed Revisions.

Attachment A

2010 Housing Tax Credit Program, QAP and Procedural Manual
Proposed Revisions

Statutory

- **Amend the 2010 QAP to reflect new language of State Statute on HTC Allocation regarding the SRO/30 percent Affordability Threshold Requirement <u>at such time as revision to State Statute is successfully accomplished.</u>**

  - ♦ One of the threshold items within Minnesota Statute 462A.222 d) provides that for applications submitted for the first round, an allocating agency may allocate tax credits only to certain types of projects in the metropolitan area. One of these project types as designated in 462A.222 d) i) is:

    - new construction or substantial rehabilitation of projects in which, for the term of the extended use period, at least 75 percent of the total tax credit units are single-room occupancy, efficiency, or one bedroom units and which are affordable by households whose income does not exceed 30 percent of the median income

      Stakeholders and developers of tax credit affordable housing have expressed significant concerns that the required percentages of SRO units at 30 percent AMI affordability level as required by Statute are very difficult and challenging to produce and operate in an efficient and long term stable manner. This condition is even more aggravated in the volatile economic and market conditions we are currently experiencing.

      Minnesota Housing is pursuing an amendment to the current Statute which would lower the required percentage of SRO units at 30 percent affordability levels and thereby assist in fostering the continued development of long term viable and affordable units of this type. The current statute requiring at least 75 percent of the total tax credit units to be single room occupancy units with rents affordable to households whose income do not exceed 30 percent of the AMI, is being reviewed and is subject to a revision of the required percentage of qualifying units, contingent upon legislative outcome. At such time as this statutory amendment is achieved and approved by the legislature, the revision will be incorporated into the 2010 QAP in the appropriate manner and content.

Qualified Allocation Plan and/or Procedural Manual

- **Clarification of HTC fees required for Additional Credits awarded at Carryover.**

  - ♦ Current HTC Manual language is not clear in indicating that an additional 3.5 percent Reservation fee is required for any additional credits a development may be issued at the time of issuance of the Carryover Agreement. Revision is proposed to the current language to clarify the fee requirement.

- **Extend the temporary $ 1,000,000 Per Development Credit Limit Increase to apply to the 2010 QAP.**

  - ♦ In response to the Housing and Economic Recovery Act of 2008, the Board approved an amendment of the 2009 QAP to temporarily increase the per development credit limit to $1,000,000. Due to a continuation of adverse market conditions, it is recommended that this temporary increase to the per development limit be approved for the 2010 QAP.

- **Continue to make the State designated 30 percent basis boost available to developments requesting the boost and meeting criteria established in the QAP.**

- In response to the Housing and Economic Recovery Act of 2008, the Board approved an amendment of the 2009 QAP to provide for a 30 percent State designated basis boost and establish criteria pursuant to the Implementation Plan for buildings placed in service after date of enactment of the Act.

  It is the goal of the Agency to optimize the use of all available sources of funding for multifamily developments; including private investor equity, amortizing loans and deferred loans; to produce the maximum number of affordable rental units in the most sustainable, quality, cost effective and geographically diverse developments possible which meet the Agency's strategic priorities. Consistent with this goal, the Board approved the following criteria as part of the Amended 2009 QAP to be used to determine if, when, and in what amount, the Agency will provide a basis boost for housing tax credit developments on a building by building basis to obtain financial feasibility.

  - ♦ Development must meet state identified housing priorities as evidenced by competitive tax credit score.
  - ♦ Funding gaps remain for top ranking tax credit developments.
  - ♦ Credits allocated in connection with the basis boost shall be no more than needed to achieve financial feasibility.

  Due to a continuation of adverse market conditions, it is recommended that the boost continue to be available to qualified developments as part of the 2010 QAP.

- **Revision of the Ineligible Properties section of the Procedural Manual to lessen restrictions relating to acquisition/rehab projects with certain pre-existing subsidies.**

  - ♦ Chapter 4. R. Ineligible Properties, of the current Procedural Manual states that "Acquisition and/or Rehabilitation projects with a pre-existing subsidy (any building substantially assisted, financed, or operated under HUD Section 8, Section 221(d)(3), (d)(4), Section 220, Section 8 existing, Moderate Rehabilitation, or the Section 236 program or under the Farmer's Home Administration Section 515 program) will be eligible to apply for tax credits only under the following conditions:

1. It preserves assisted low income housing which, due to mortgage prepayments or expiring rental assistance, would convert to market rate use. This must be demonstrated to the satisfaction of Minnesota Housing; or
2. It has been demonstrated to the satisfaction of Minnesota Housing that the building qualifies as a "troubled property." In order to qualify as such, a responsible official of a governmental lender, such as Minnesota Housing, HUD, or RD, must provide a written explanation and documentation that the property is troubled. Generally, the property must be in default or foreclosure.

These restrictions were created in the QAP in the late 1980's. Staff research indicates that in the early years of delivering the tax credit program, these restrictions applied to applications seeking to obtain tax credits on developments which at that time were recently constructed and had also recently received subsidies through Project Based Section 8 and other similar federal subsidy capital source streams. It is believed that the provisions were intended at that time to prevent newly constructed developments from essentially "double dipping" into Agency resources within a relatively short time after their initial construction with other federal subsidy resources.

Staff believes that this provision has out-lived its purpose. Developments to which the restrictions were targeted back in the late 1980's are now more than 20 years older and have rehabilitation needs which could be assisted through access to the credit.

It is important to note that through significant points currently made available to qualifying developments via the HTC Self-Scoring Worksheet, the QAP will continue to provide competitive priority to developments which propose to preserve federally assisted low income housing which, due to mortgage prepayments or expiring rental assistance, would convert to market rate use or due to physical deterioration or deterioration of capacity of current ownership/management entity would lose its federal subsidies. Staff is not proposing to remove this incentive from the QAP.

- **Revision to the Rental Assistance section of the Scoring Worksheet to provide a wider and more equitable range of points for the rehabilitation of existing project based assistance proposals.**

  - The Rental Assistance section of the Self-Scoring Worksheet currently has a narrow range of points incenting varying levels of project based assistance units within a development. The current ranges do not provide enough incentive for higher levels beyond a 20 percent composition of project based assistance units. Staff believes that this condition of disincentive should be corrected.

    Developments proposing a 50 percent or less composition of project based assistance units <u>also</u> have the potential to obtain selection points for the remaining non-project based class units through the Serves Lowest Income section of the score sheet.

Developments proposing greater than a 50 percent composition of project based assistance units do not have the potential to also obtain selection points for the remaining non-project based assistance units through the Serves Lowest Income section.

Points cannot be obtained from both sections for the same units. The Serves Lowest Income section requires at least 50 percent of the units to meet its criteria. An inequity therefore exists which disincents a development proposing a composition of greater than 50 percent project based assistance units. A revision to the range of points is needed to promote a more equitable relationship between the two scoring sections in addressing developments proposing project based assistance units.

- **Revision of the Procedural Manual and Scoring Worksheet to add Selection Priorities for HTC developments which have been previously awarded tax credits but not yet placed in service and are ready to proceed to closing and project construction.**

  - In response to the Act and its stimulus provisions intended to facilitate the progress of tax credit affordable housing developments, at a time of declining tax credit pricing, Staff is proposing to provide a Selection Priority within the Self-Scoring Worksheet for developments which have been "previously awarded tax credits, but are not yet placed in service". A higher priority (higher points) within the Selection Priority is proposed for qualifying applications reflecting the earliest year of credit (not placed in service). Additionally, a higher priority (higher points) within the Selection Priority is proposed for qualifying applications which do not reflect a funding gap at the time of application (but for the additional credit requested). An accelerated selection process and accelerated Board approval process is proposed in conjunction with qualifying applications being awarded points via this "previously awarded credits" Selection Priority. It is intended that these two revision items work directly and dynamically with each other to further the intent of the Act to get developments already awarded tax credits moving forward as quickly as possible and to get the related affordable housing units produced and available. To cross-reference details of this accelerated process, please refer to the related item appearing next on this Attachment.

    Two separate scoring sections within the Self-Scoring Worksheet are proposed to be created for assigning points based on the "gap" condition of "previously awarded credits" applications. One section will be for applications which do not reflect a funding gap at the time of application (but for the additional tax credit requested). The second section will be for applications which do reflect a funding gap existing at the time of application (in addition to the additional credit requested). It is anticipated that a specific and accelerated review process for gap funding will be carried out through RFP processing for those qualifying "previously awarded credit" developments which have limited gap funding needs. To the extent possible, the review will try resolve the qualifying development's gap needs with accelerated gap funding awards.

Points will be tentatively "assigned" at the initial stages of review of an application's gap need determination. Upon further detailed analysis, review and ultimate gap funding decisions involving both HTC and RFP accelerated reviews, the points initially "assigned" will either be "awarded" to the application or the initially "assigned" points will be "unassigned" and removed from the application's points total. Qualified "previously awarded credit" applications successfully completing the accelerated review and selections process will be forwarded on to the Board for selections approval actions (please refer to related item section). If an application is unsuccessful in maintaining the "previously awarded credit" points necessary to be eligible for the proposed accelerated selection process and accelerated Board selection approval process (i.e. needed gap funds are not secured by the development through the accelerated RFP gap funding process), then the application will be returned to the general RFP/HTC competition and processed in the standard RFP processing timeline with Board approvals in October.

The objective is to prioritize, through the award of selection points, the selection of HTC developments which have already been selected and reserved tax credits in the last few selection rounds, have a "no gap" condition and which are under the most demanding timelines due to the earliest year of credit award. Developments of this type are more advanced in their development and finance planning efforts and, due to critical timelines and market volatility, are most in need of receiving the assistance an award of additional tax credits would provide to them.

It is proposed that developments receiving points through this new Selection Priority provision and successfully receiving an award of credits be expected to make significant progress, as determined by Minnesota Housing, in closing on the development's financing and its housing tax credit syndication. Developments receiving such points and awards would be required to do so with the understanding that their failing to show such continued and significant progress, as determined by Minnesota Housing, may result in the development's housing tax credit award being rescinded by Minnesota Housing. Credits rescinded by Minnesota Housing in this manner would be subsequently awarded to other competitive tax credit developments having the ability to quickly move forward to financing and credit syndication closings and the start of project construction.

Developments which demonstrate a readiness to proceed are central to this prioritization. Therefore, criteria to be met in order to receive the point award would include:

- Development must have previously received tax credits and must have an annual tax credit shortfall of no more than 50 percent of the total qualified annual tax credit amount.
- The current tax credit application must contain an executed Letter of Intent from the Syndicator which is acceptable to Minnesota Housing. The letter must:

    - Be current within 15 days of submission of the tax credit application
    - Contain a Projected Closing Date for the development
    - Contain a Projected Equity Price for purchase of the credit
    - Contain a detailed explanation of what Assumptions are being used by the Syndicator to arrive at the Projected Equity Price.
  - The current tax credit application must contain an executed Firm Commitment Letter from the Providers of all other funding sources which is acceptable to Minnesota Housing.

- **Revision to the QAP and Procedural Manual to provide for an accelerated Selection process and an accelerated Board approval process for those deals meeting the newly created "Previously Awarded/Ready to Proceed" Selection Priority.**

  - One of the primary objectives of creating the "Previously Awarded Tax Credit" Selection Priority is to help qualifying developments which have already received a tax credit award (not yet placed in service) and would be gap free if awarded additional tax credits move forward to construction as soon as possible. As intended, applications awarded points from the newly created priority will be clearly positioned in the strongest positions to be selected for tax credits from the current HTC round. Consistent with this objective, Staff is proposing to review and identify those applications/developments which will be receiving these points and to provide them with accelerated selection processing and accelerated Board approval. This will assist the developments in moving forward as soon as possible. To cross-reference details of this accelerated selection and Board approval process, please also refer to the related "previously awarded credit" Selection Priority item appearing as the previous item on this Attachment. It is anticipated that these developments will be brought to the Board for selection approvals in July. The remainder of the qualifying applications will be fully reviewed and processed through the Fall 2009 RFP along normal timelines and brought to the Board in October. The selection process sections of the Manual and QAP will be revised as appropriate to describe this process.

- **Revision to the Tax Credit Design Standards to Allow for Minor Deviations from Current "Large Family Point" Additional Design Requirements (relating to Minimum Living Room and Bedroom Square Footage and Dimensional Requirements) for proposals for Rehabilitation of Existing Buildings.**

  - In applying certain Housing Tax Credit Design Standards to existing buildings involving acquisition/rehabilitation tax credits, situations have come up which cause Staff to conclude that revisions are needed to the requirements. Staff believes that flexibility is needed at the staff architect level to be able to allow for and approve of a minor amount of deviation from the standard living room and bedroom square footage and dimensional requirements for developments involving the rehabilitation of existing buildings. Language clarifications are also needed with respect to the units subject to the requirements (all or just HTC) and the room dimensions subject to the requirements (single dimension or all room dimensions).

Current Housing Tax Credit Design Standards with respect to Large Family Points taken were crafted with a primary focus on new construction development. Staff observation is made that the current dimensional and square footage requirements do not easily or reasonably translate to existing buildings. Current requirements put a hardship on preservation deals that were built to HUD and Minnesota Housing standards when they were originally constructed but now fail to meet the minimum bedroom and living room dimensions per the HTC Large Family Housing requirements.

Current HTC Design Standards with respect to Large Family Points taken are as follows:

- Additional design requirements will also be imposed if a developer claims and is awarded Large Family Points on the HTC Self-Scoring Worksheet.
  - For the living room - 11 feet 6 inches.
  - For the bedrooms – 9 feet 6 inches; and 100 sq. ft. in area.

  Staff recommends that a revision be made to the General Requirements section of the Housing Tax Credit Design Standards/additional requirements for Large Family Points taken to allow Minnesota Housing staff architects flexibility to allow for and approve of minor deviations from the requirement (15 percent or less) for developments involving the rehabilitation of an existing building.

<u>**Scoring Criteria Impact:**</u>

1. Rental Assistance:
   The proposed revision would provide one or more additional selection point ranges for developments agreeing to set aside and having the required binding commitment for 50 percent or more of the total units as project based rental assistance (PBA) units. The additional point ranges would provide incentive for percentages of PBA units greater than 50 percent of the total units in the development.

2. (NEW SECTION) Previously Awarded Tax Credits (and not yet Placed in Service) <u>with no funding gap</u> reflected at time of application (but for the additional credit requested):

   a. 1000 points available for qualifying developments which have previously been awarded 2008 or 2007 tax credits but have not yet placed in service and have no funding gap reflected at the time of this current application for tax credits.

   b. 900 points available for qualifying developments which have previously been awarded 2009 tax credits but have not yet placed in service and have no funding gap reflected at the time of this current application for tax credits.

3. (NEW SECTION) Previously Awarded Tax Credits (and not yet Placed in Service) with a funding gap reflected at time of application (in addition to the additional credit requested):

   c. 500 points available for qualifying developments which have previously been awarded 2008 or 2007 tax credits but have not yet placed in service and have a funding gap reflected at the time of this current application for tax credits. *

   d. 400 points available for qualifying developments which have previously been awarded 2009 tax credits but have not yet placed in service and have a funding gap reflected at the time of this current application for tax credits. *

   * *Points assigned through this section are subject to being unassigned if needed gap funds are not secured by the development through the accelerated RFP gap funding process.*

General Administrative and Clarifications:

Perform various administrative checks, for spelling, formatting, text and instruction corrections and clarifications within QAP, Manual, Self-Scoring Worksheet, and other 2010 tax credit program related documents.