Cost Containment Report

2021

MINNESOTA HOUSING

OVERVIEW AND CONTEXT

Containing the cost of housing development is a critical issue in Minnesota. In 2019, about 536,000 Minnesota households were cost burdened by spending more than 30 percent of their income on housing.[1] If we are to address the severe shortage of housing that is affordable, we must build and preserve as many affordable units as possible with the limited resources available, which requires us to be cost conscious. However, cost containment requires tradeoffs and a balanced approach.

- Using lower quality materials and less efficient systems will reduce upfront costs, but they can also increase ongoing maintenance, repair, and utility costs, which may not be cost-effective in the long run.

- Using lower quality materials and more basic designs for a building's exterior will also reduce costs, but they will also make it more challenging to fit affordable housing in the surrounding neighborhood, particularly higher-incomes communities, which can lead to community opposition and increase costs related to delays, re-design, and projects not moving forward.

- Siting developments in less expensive locations can save money, but it can also reduce the tenants' access to jobs, services, amenities, safe neighborhoods, public transportation, good schools, and other benefits.

We based our 2020-23 Strategic Plan on the principle that housing is the foundation for success, providing individuals, families and communities the opportunity to thrive. To achieve this outcome for as many lower-income households as possible, our goal is to finance high-quality, durable, location-efficient housing that provides access to jobs, transit, and other amenities and is built at reasonable costs. We are balancing the goal of cost containment with other policy objectives.

[1] Minnesota Housing analysis of data from the U.S. Census Bureau's American Community Survey (2019, 1-year sample).

Overall, as the following assessment shows, we have been effective at containing costs for nearly two decades – maintaining relatively consistent total development costs (TDC) while pursuing other policy objectives that can increase costs, including supportive housing for people experiencing homelessness and people with disabilities, energy-efficient and healthy homes, and locations that provide access to jobs, transit, and other amenities. We continue to identify and pursue additional strategies to contain and reduce costs, including encouraging different types of construction methods.

This report is broken into two sections – the first addresses multifamily costs, and the second addresses single family costs.

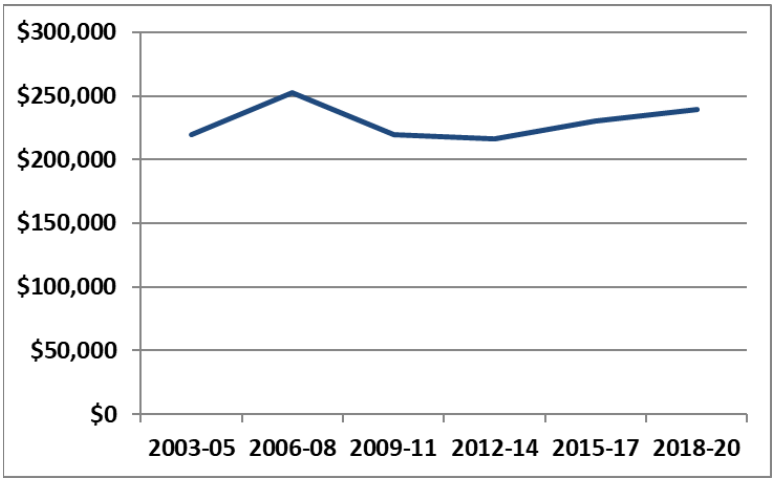
MULTIFAMILY COSTS

In a typical year, we distribute $150 million to $200 million for multifamily development.[2] We work to allocate these funds efficiently and effectively to address the significant shortage of housing that is affordable, particularly for those with the lowest incomes. The first part of this Multifamily section provides an overview of our results, and the second part outlines our strategies for achieving those results and pursuing additional cost containment.

Overview of Multifamily Costs

Overall, the average TDC per unit for the housing we have financed has been around $225,000 for the last decade and a half, after controlling for inflation in residential construction. The data in Figure 1 applies to all types of developments, including new construction, rehabilitation, metro area, Greater Minnesota, tax credit, non-tax credit, workforce housing, and supportive housing. The trend line is influenced not only by the underlying cost trends but also by the mix of projects in a given year.[3] For example, a larger share of resources going to new construction with tax credits in the metro area will increase average costs, while a larger share going to rehabilitation without tax credits in Greater Minnesota will decrease average costs.

Figure 1: Average TDC per Unit 2003 to 2020 – All Types of Developments (Adjusted for Construction Inflation, 2021 Dollars)



To control for the mix of projects in the trend line, Figure 2 shows average TDC per unit just for new construction projects with tax credits in the metro area. Again, average costs are relatively

[2] This includes syndication proceeds from 9% housing tax credits.

[3] To increase the comparability of the data, we excluded developments with a TDC per unit that were less than $40,000, which took out rehabilitation projects with a more limited scope of work and added consistency to the level of rehabilitation being assessed. We also excluded developments with an overall acquisition cost of less than $10,000, which excludes projects with no acquisition or heavily subsidized acquisition.

constant, but at a slightly higher level, around $300,000. Costs are relatively consistent or contained cost over time.

Figure 2: TDC per Unit 2003 to 2020 – New Construction with Tax Credits in the Metro Area (Adjusted for Construction Inflation, 2021 Dollars)

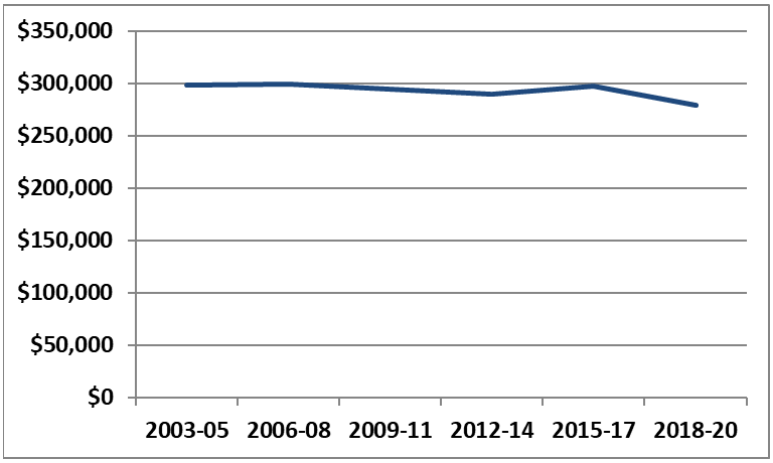
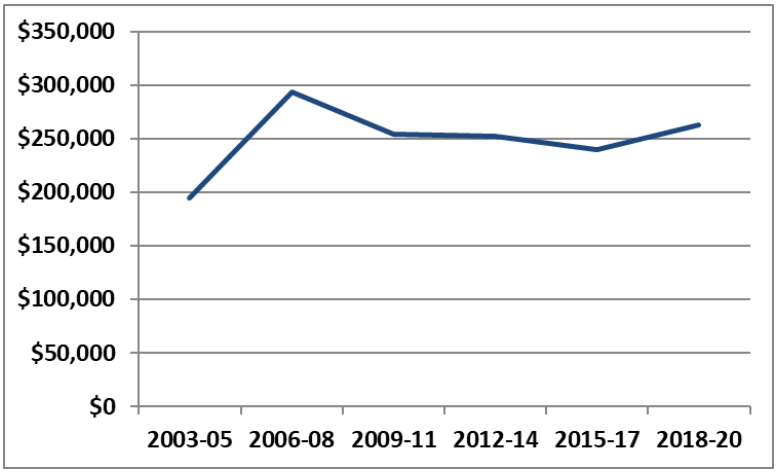


Figure 3 shows the equivalent graph for Greater Minnesota, with lower costs ($250,00) but similar cost containment.

Figure 3: TDC per Unit 2003 to 2020 – New Construction with Tax Credits in Greater Minnesota (Adjusted for Construction Inflation, 2021 Dollars)



Most importantly, we have contained costs while also taking on policy initiatives that can increase costs.

- In 2003, we added a selection and funding priority for supportive housing for people experiencing homelessness, which is generally a more costly type of development.

- In 2007, we added our Green Communities Overlay, which requires our developments to have energy-efficient and healthy-home features.

- In the last several of years, we strengthened our location efficiency priority by making it more geographically precise and increasing the points it receives in the selection process. Housing that is in a walkable neighborhood and near transit, jobs, and other amenities can be more expensive.

While we added or enhanced these policy objectives, we also added cost containment provisions.

- Starting in 2006, we developed and used our predictive cost model, which compares a development's proposed costs with the costs that we would expect for that development based on the Agency's experience with similar projects and industry-wide standards. This process flags high cost developments and helps maintain costs at a reasonable level.

- With the Qualified Allocation Plan (QAP) for the 2014 Low-Income Housing Tax Credits (LIHTC), we added a selection criterion to incentivize minimizing costs by giving a preference to the 50 percent of tax credit applications with the lowest TDC per unit, taking into account unit sizes, location and type of activity (new construction versus rehabilitation). With the 2022-2023 QAP, we dropped this scoring criterion. We were concerned that the points were a disincentive to use innovative energy efficiency/conservation efforts, which can add to upfront development costs but provides long-term benefits and savings. The scoring also became complicated by the fact that some state requirements, such as prevailing wage, increase costs and apply to most tax credit developments but not all. Finally, having the criterion did not appear to have a substantial impact on costs, which did not go down after it was put in place, and we were able to effectively contain costs prior to it being added. We will continue to monitor costs to see if dropping this selection criterion has an impact on the costs going forward.

- In 2014, we also launched the Minnesota Challenge to Lower the Cost of Affordable Housing, which was initiated as an idea competition to identify and address system-level factors (such as land use policies or design standards) that increase costs for all developments. Since this initial competition, we have carried out several activities to address these systemic-cost drivers.

- In 2019 through 2021, we participated in and co-sponsored the Construction Revolution, which is an initiative to increase innovation in residential construction techniques with a focus on modular and offsite construction.

More information on these initiatives is provided in the report's next section.

To contain costs, it is important to understand the factors that drive costs. Table 1 provides a break out of costs by project type, location and cost component.

- New construction with tax credits in the Twin Cities metro area is the most expensive type of project, while rehabilitation without tax credits in Greater Minnesota is the least expensive.

- Not surprisingly, construction accounts for the clear majority of costs in new construction projects, while construction and acquisition costs are both key cost drivers of rehabilitation projects. Addressing these costs will have the largest impact in reducing or containing TDCs.

- While soft costs (non-construction costs) account for a smaller share of TDC (15 percent to 24 percent), they should be a key focus of cost containment strategies. Reducing construction costs can affect the quality, durability, and energy efficiency of the housing; and reducing acquisition costs can affect location efficiency. While soft costs are a necessary component of a housing development, eliminating inefficiencies in these costs will not affect the quality of the housing.

- Low-Income Housing Tax Credits (LIHTC) appear to add six to seven percentage points to the share of TDC attributable to soft costs, likely due to the added complexity and cost of putting together and financing a tax credit deal. For developments without tax credits, soft costs account for 15 to 17 percent of TDC. That percentage jumps to 21 to 24 percent for developments with tax credits.

Table 1: Share of TDC by Project Type, Location and Cost Component
Developments Completed between 2003 and 2020 (Adjusted for Construction Inflation, 2021 Dollars)

			Avg. TDC per Unit	Share of TDC			N
				Construc-tion	Acquisi-tion	Soft	
New Const.	LIHTC	Metro	$294,378	69%	7%	24%	91
New Const.	No-LIHTC	Metro	$234,741	73%	10%	17%	20
New Const.	LITHC	Greater MN	$242,804	73%	5%	22%	64
New Const.	No-LIHTC	Greater MN	$211,660	78%	7%	15%	17
Rehab	LIHTC	Metro	$233,172	35%	42%	23%	42
Rehab	No-LIHTC	Metro	$160,906	44%	41%	15%	26
Rehab	LITHC	Greater MN	$145,434	42%	36%	21%	40
Rehab	No-LIHTC	Greater MN	$101,665	42%	42%	16%	21

Strategies for Containing and Reducing Multifamily Costs

As mentioned earlier, we have taken a three-pronged approach to containing costs up to this point.

1. Assess Cost Reasonableness

2. Incent Cost Containment and Reductions in the Selection of Projects for Housing Tax Credits, which is being dropped with the 2022-2023 QAP.

3. Address Systemic Cost Drivers

Strategy 1: Assess Cost Reasonableness

Minnesota Housing assesses each development for cost reasonableness. An important tool for identifying high cost developments is our predictive cost model. The model predicts a development's TDC per unit based on its characteristics. To develop the parameters for the model, we run a multivariate regression analysis on the inflation-adjusted costs and characteristics of the developments that the Agency financed between 2003 and 2020. The analysis uses the historical data to assess the effect that each of the following factors simultaneously has on TDC per unit:

- Activity Type:
    - New Construction
    - Extensive Rehabilitation[4]
    - More Limited Rehabilitation

[4] This involves more extensive work on the interior, exterior, electrical, and mechanical systems of a property. "Extensive" versus "more limited" is determined by staff using internal definitions.

    - Combination of New Construction and Rehabilitation
    - Conversion/Adaptive-Reuse
- Building Type:
    - Walkup
    - Elevator
    - Townhome
    - Single Family Home/Duplex
- Number of Stories
- Unit Size – based on average number of bedrooms per unit in the development
- Gross Square Footage
- Location:
    - Minneapolis or Saint Paul
    - Suburbs in Twin Cities Seven-County Metro Area
    - Greater Minnesota – Large City[5]
    - Greater Minnesota – Regional Job Center[6]
    - Greater Minnesota – Rural
- Year Built
- Underground Garage
- Acquisition:
    - Land
    - Structure
    - None
- Financing:
    - Tax Credits
    - Number of Funding Sources
- Special Costs:
    - Historic Preservation
    - Environmental Abatement
    - Supportive Housing
    - Prevailing Wages

[5] The large cities are Duluth, Rochester, St. Cloud, Moorhead, and Mankato; and include a five-mile commute shed around the cities.

[6] There are 51 regional job centers, which are the top 15 percent of cities and townships in number of jobs. They include: Albert Lea, Albertville, Alexandria, Austin, Baxter, Bemidji, Brainerd, Buffalo, Cambridge, Cloquet, Cold Spring, Crookston, Detroit Lakes, Elk River, Fairmont, Faribault, Fergus Falls, Goodview, Grand Rapids, Hibbing, Hutchinson, International Falls, La Prairie, Little Falls, Marshall, Montevideo, Monticello, Morris, North Mankato, Northfield, Onamia, Owatonna, Park Rapids, Perham, Pipestone, Red Wing, Roseau, Saint Michael, Saint Peter, Sartell, Sauk Rapids, Thief Rivers Falls, Virginia, Waite Park, Waseca, Willmar, Windom, Worthington, and Wyoming. These areas also include a five-mile commute shed around the cities.

We apply the model's cost parameters for these factors to a proposed development to predict its costs. The model is also benchmarked against industry-wide cost data to ensure that our costs are in line with the industry. With different development characteristics, the predicted total development costs for new construction can vary from $200,000 to $450,000 per unit.

Overall, the model explains a sizable portion (56 percent to 73 percent) of the variation in the costs for developments that we financed between 2003 and 2020, which is a robust result.[7] For comparison, Abt Associates (a national consulting firm) released in August 2018 a cost analysis of housing tax credit developments from across the county, and their regression models explained 52 to 54 percent of the variation in the national data.[8] Similarly, the U.S. Government Accountability Office (GAO) released in September 2018 another cost analysis of tax credit developments, and their regression models explained 63 to 65 percent of the variation in their national data.[9] Besides the statistical rigor, the model has proven very effective over the last decade and a half in objectively and systematically flagging developments with high costs. Each year, we revise and enhance the model based on the previous year's results and staff feedback.

Over time, we have tested models that predict costs on a per-unit and a per-square-foot basis. Based on our testing, the per-unit models have explained a larger share of the variation. We believe this has occurred for two reasons. First, some costs are clearly tied to the unit and do not increase with the size of the units. For example, apartments regardless of unit size have one kitchen (unless single-room-occupancy). Second, and most importantly, the per-unit model that we use includes a cost factor that accounts for unit size. Developments with larger units and more bedrooms have higher predicted costs.

Under current practice, when staff recommend to the Board developments for funding, they identify the developments with a proposed cost that is more than 25 percent higher than the model's predicted cost, and the Board can decide to grant a waiver allowing the higher cost. For the higher-cost projects that staff recommends for funding, staff needs to explain why the proposed costs are reasonable even though they are above the 25 percent threshold. There are a wide range of valid reasons why the costs could be reasonable. For example, a housing development and site may be critical to meet a local housing need, but the site requires an unusually large amount of environmental remediation.

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[7] The model explains about 73% of the variation in construction costs and about 56% of the variation in soft costs.
[8] Abt Associates, *Variation in Development Costs for LIHTC Projects* (prepared for the National Council of State Housing Agencies, August 30, 2018). The adjusted R-Squared values shown in the appendix varied from 0.5222 to 0.5433.
[9] U.S. Government Accountability Office (GAO), *Low-Income Housing Tax Credit: Improved Data and Oversight Would Strengthen Cost Assessments and Fraud Risk*, (September 2018, GAO-18-637). The adjusted R-Squared values shown in Appendix II varied from 0.626 to 0.648.

While the predictive cost model is a useful tool to identify high-cost developments, it is not the only way that Agency staff review cost reasonableness. The professional judgment and expertise of our underwriting and architectural staff also play a critical role in the assessment of cost reasonableness. Even if a project has costs that are within the 25 percent predictive cost model threshold, staff can still question costs if they seem high given the context of the development. Our staff has extensive experience reviewing funding applications and development costs. Each year, they typically evaluate 75 or more applications.

Strategy 2: Incent Cost Containment and Reductions in the Selection of Projects for Low-Income Housing Tax Credits

For the Qualified Allocation Plans (QAPs) for 2014 through 2021 Low-Income Housing Tax Credits, we added a cost criterion for selecting developments that receive the credits. The 50 percent of tax credit applications with the lowest TDC per unit were eligible to receive six points in the selection process. We controlled for activity-type and location cost differences by dividing the applications into four groups.

1. New Construction in the Twin Cities metro area
2. New Construction in Greater Minnesota
3. Rehabilitation in the Twin Cities metro area
4. Rehabilitation in Greater Minnesota

Within each of the four groups, the applications with the lowest costs are eligible for the points. As a result, projects are only competing with similar projects for the points. When comparing costs and awarding points, we also adjust the costs to account for unit size differences. Projects with predominantly smaller units (efficiencies and one bedroom) have their costs adjusted upward when making comparisons; and projects with predominantly large units (three or more bedrooms) have their costs adjusted downward.[10] This levels the playing field when comparing costs.

As explained earlier, we eliminated these cost containment points with the 2022-2023 QAP

Strategy 3: Address Systemic Cost Drivers

The first two tactics address costs that are specific to individual developments. Systemic cost drivers outside the control of developers are critical issues that also need to be addressed. These cost drivers ranged from local policies and regulations that increase the cost of housing

[10] To be classified as a development with small units, 75 percent or more of the units have to be efficiencies or have one bedroom. To be classified as a development with large units, 50 percent or more of the units have to have three or more bedrooms.

(such as maximum densities), to the large cash reserves that funders and investors may require for affordable housing developments, to the complexity of assembling the multiple sources of funding that make an affordable housing deal work.

In January 2014, Enterprise Community Partners and the Urban Land Institute's (ULI's) Terwilliger Center for Housing released a report on best practices from across the country to address these systemic cost drivers.[11] Overall, the report finds that containing and reducing costs in a prudent and effective way does not involve a single magic bullet. Rather, housing costs are driven by dozens of small inefficiencies. As one of the lead authors described it, "death by a thousand cuts."[12]

To take on these cost drivers, we partnered with the McKnight Foundation, Enterprise, and ULI/Regional Conference of Mayors to create an initiative for Minnesota to implement these types of practices, which became the MN Challenge to Lower the Cost of Affordable Housing. It began in the winter of 2014 as an idea competition. We asked the development community to create cross-discipline teams (developers, funders, attorneys, local officials, housing advocates, etc.) and develop and submit ideas to address these systemic cost drivers. From the 12 submissions, we selected one to receive $70,000 for implementation.[13]

The winning idea was submitted by the Center for Urban and Region Affairs at the University of Minnesota, the Housing Justice Center, and Becker Consulting. Their proposal addresses the issue of local practices and policies that add to the cost of affordable housing, including fees, land-use and zoning policies, approval processes, and others. These cost drivers have been identified and known for years. The value of this idea was identifying and implementing best practices to address them, which included providing technical assistance to communities to pursue the practices and encouraging regional organizations to incorporate the implementation strategies into their policies and guidelines, including the Metropolitan Council's Planning Handbook and Housing Performance Scores and ULI's Tool Box for local communities.

As part of our overall cost containment strategy, we have initiated several initiatives that address systemic cost drivers.

- **2014 – Minnesota Housing's Multifamily Remodel Project.** We carried out a project for our Multifamily Division to redesign and streamline its application and funding processes - everything from proposal inception through application, selection,

[11] Enterprise Community Partners and Urban Land Institute's Terwilliger Center for Housing*, Bending the Cost Curve on Affordable Rental Development: Understanding the Drivers of Costs* (January 2014).
[12] Michael Spotts, Enterprise Community Partner, presentation to the Affordable Housing Investors Council (AHIC), Portland Oregon, October 9, 2014.
[13] The initiative was jointly funded by the McKnight Foundation and Minnesota Housing.

underwriting, closing, construction management, and lease up. The purpose of the remodel is to reduce the time it takes a development to move from concept to occupancy. A key finding from the Enterprise/ULI report identified complexity, uncertainty, and delays in the funding process as cost drivers. The project has achieved positive outcomes. For example, we created a customized online portal to receive funding applications for the multifamily consolidated RFP, eliminating paper applications.

- **2015 – MinnDocs – Consolidated Legal Documents**. Most affordable housing projects have multiple deferred loan funding sources, each with their own set of legal documents and attorneys, which add unnecessary costs. The Enterprise/ULI report highlighted Massachusetts' practice that consolidates legal documents for all subordinate debt into a single set. The development community in Minnesota was intrigued, and we took initial steps to pursue the concept. The complexity of making this work turned out not to be worth the limited cost savings that would result.

- **2016 - Minnesota Housing's Design and Construction Standards.** As part of our annual preparation for the consolidated RFP, we review these standards. During 2016, we specifically reviewed the standards with an emphasis on cost containment. We focused on reducing life-cycle costs (which includes ongoing maintenance, repair, and utility costs), not just upfront development costs. Specifically, we surveyed architects, general contractors, and developers who work on the developments that we finance about the standards and costs. We received 66 responses. Based on the feedback, we made several design changes that should reduce costs. For example, we clarified that a separate dining room is not required in units with two or more bedrooms but that a dining area (or eat in kitchen) is sufficient. Each of the changes to the standards will unlikely result in significant savings, but they are more examples of small savings that can lead to larger savings when combined with each other over time.

- **2017 – Developer Fees.** These fees compensate developers for the time, compliance requirements, and risks associated with developing affordable housing and can account for a substantial portion of a development's softs costs. The maximum developer fee that Minnesota Housing allows is 15 percent of TDC for the first 50 units and 8 percent for additional units. In 2017, we assessed our fees and found that they are consistent with other states and that the average fee taken by our developers is 7 percent of TDC, well below our maximum. Given our cost containment incentives, it appears that developers are typically taking the minimum fee that still allows the deal to work for them. If developers take a higher fee, their applications will be less competitive in a highly competitive process, particularly for 9% tax credits. Based on this analysis, we

decided not to adjust our developer fee structure at that time, but it is an area that we will continue to assess given the size of these costs.

- **2018 – Housing Task Force.** Minnesota Housing was a lead sponsor of the Task Force, providing much of the staff support. The cost of developing housing was a primary issue addressed by the Task Force, which made several cost-related recommendations, including:

    - Position Minnesota as a national leader in the advancement of housing innovation and technology, which should increase the efficiency and productivity of developing housing and reduce the costs.

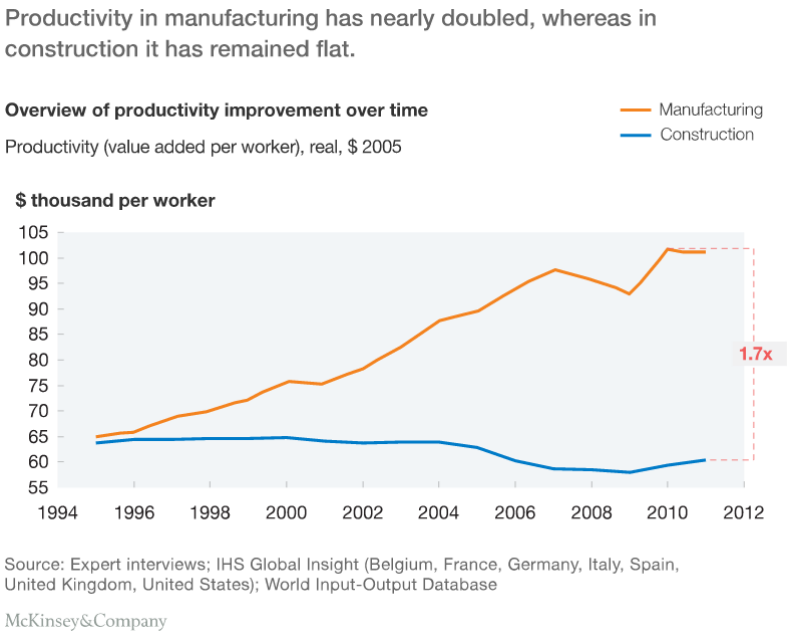
    - Grow the pool of talent in Minnesota's building trades to enable the sector to meet current and future demand, which should address the current shortage of skilled labor.

    - Create a statewide review panel to evaluate regulations related to building standards, land use, and environmental stewardship for their impact on housing affordability.

  While these actions are largely outside the scope of our work, they would directly impact the cost of the housing that we finance.

- **2019 through 2021 – Offsite Construction and Other Innovative Techniques.** In 2019, we helped organize and co-sponsored the Construction Revolution Summit, which pursued the innovation and technology recommendation from the Housing Task Force. The summit brought together construction industry leaders to discuss barriers and opportunities to advancing offsite construction (including modular and panelized). Offsite construction, particularly modular, has struggled to take hold in the United State but has the potential to significantly reduce construction costs.

  Housing construction is ripe for a major systemic change. Unlike other industries, it has not experienced meaningful productivity increases over the last few decades. We are largely building homes the same way we did 50 years ago.



Without productivity gains, reducing the cost of housing construction will remain elusive. Some estimates suggest that offsite construction could reduce costs by as much as 20%.

The action plan that came out of the Summit called for, among other things: (1) establishing learning opportunities on how to develop housing using modular construction, and (2) having public funders finance some developments using offsite construction as a pilot.

- In the winter of 2021, the Construction Revolution team provided a course on using modular construction, bringing together developers, architects, general contractors, and others from the industry. One of Minnesota Housing's architects participated.

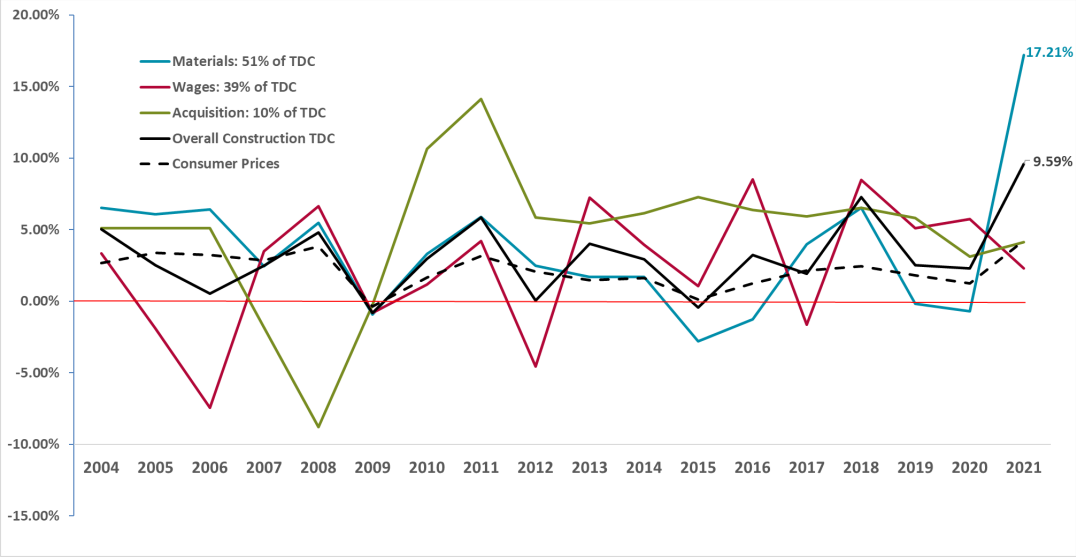
- In our scoring for the 2021 and 2022 consolidated RFPs, we have added a selection preference for developments that use innovative construction techniques (including offsite construction) and have to potential to reduce construction costs by at least 10% and construction time by at least 20%.

Costs for Upcoming Projects

One of the reasons that we now seeing the cost of new rental housing in some parts of the state surpassing $300,000 per unit is the recent increase in construction costs, primarily driven by material costs. Supply chain issues have continued longer than originally expected, significantly driving up costs. Based on data through October, housing developments costs in

2021 now look like they will be nearly 10% higher in 2021 than 2020. Figure 3 shows housing development cost increases by component – material costs, wages for construction labor, and acquisition costs – along with the Consumer Price Index (CPI) for comparison. Since 2003, the CPI has increased on average by about 2% each year, while the cost of residential development has increased by about 3% on average, one percentage point higher. As shown in Figure 4, the 17% increase in material costs has played a key role in the nearly 10% increase in overall development costs in 2021.

Figure 4: Rental Housing Development Inflation 2004 through 2021



SOURCE: Material costs from the Bureau of Labor Statistics' Producer Price Index (PPI) for residential construction inputs; labor wage costs come from the Minnesota Department of Employment and Economic Development's Quarterly Census of Employment and Wages for new multifamily housing construction; and the acquisition costs from the CoStar's property acquisition data.

The developments that Minnesota Housing's Board will select through the 2021 Consolidated RFP will quite likely be constructed and use the awarded funds in 2023. In most cases, these projects will have another 12 to 24 months of construction inflation. The most recent Philadelphia Federal Reserve Bank survey of economic forecasters has CPI increasing by 2.7% in 2022 and 2.4% in 2023, which indicates that these forecasters expect the current high level of inflation to subside soon. Assuming construction inflation continues to be a percentage point higher than CPI increases, development costs would increase by about 3.7% in 2022 and 3.4% in 2023, higher than the typical 3% but not a lot.

For the 2021 Consolidated RFP, we will likely see total development costs per unit for new construction in the Twin Cities metro area in the range of $350,000 per unit, or about 17% higher than the historical costs shown in Figure 1, adjusted to 2021 dollars. Two factors account for the increase:

- As explained, the projects that we select for funding through the 2021 RFP will face another year or two of construction inflation, which may add another 3.7% to 7.1% to the average $300,000 baseline costs in the metro area.

- In addition, the projects shown in Figure 1 largely do not reflect the cost of paying prevailing wages, which the developments that we now finance must pay, for the most part. We estimate that prevailing wages add about 12% to total development costs.

Accounting for the roughly 17% combined increase outlined in the previous two bullets and our 25% buffer to assess cost reasonableness, we are likely to see some projects recommended for funding with costs over $400,000 per unit.

SINGLE FAMILY COSTS

We typically distribute around $10 million for single family development through our Community Homeownership Impact Fund. The level of cost data that we collect is currently less than what we collect and analyze for multifamily developments, but evaluating costs and cost containment are a part of our selection process.

Overview of Single-Family Costs

The total development costs for the single-family projects that we have financed are reasonable and consistent with industry benchmarks. Table 2 shows the median cost per home by location and activity for developments that we have financed over the last eight years.

Table 2: Impact Fund – Median TDC by Location and Project Type
Loans Closed October 1, 2012 through March 17, 2020

Location	New Construction	Acquisition/Rehab/ Resale
Greater Minnesota	$210,195	$195,393
Metro	$367,056	$285,476
Total	**$355,141**	**$280,666**

Excludes projects by Habitat for Humanity and Community Land Trusts

The costs in Table 2 are generally consistent with industry standards. Table 3 shows the RSMeans industry-wide costs for new construction (excluding acquisition and some soft costs) in Minneapolis/Saint Paul for different sized homes. Our costs are in line with these benchmarks.

- The RSMeans construction costs for a 1,600 square-foot, 2-story home with an unfinished basement and average class design is $250,787, which is in the middle of the cost range shown in Table 3 ($177,997 to $321,986).

- Assuming that construction costs account for 75 percent of the TDC and that acquisition and additional soft costs account for the remaining 25 percent, the TDC would be $334,383. This a smaller and basic home by today's new construction standards (1,600 square feet, one-car garage, and one bathroom). According to the Minneapolis Areas Realtors, the median sale price of newly constructed homes in the 16 counties in and around the Twin Cities is $430,000.[14]

- The $367,056 median TDC for new construction financed by Minnesota Housing in the metro area (see Table 2) is relatively consistent with the RSMeans costs, but 10% higher than the $334,383 benchmark.

Table 3: RSMeans Estimated Construction Costs, 2020 (Excluding Acquisition and Some Soft Costs)
In Minneapolis/Saint Paul, Average Class, Wood Siding, Attached One-Car Garage, One Full Bath

	1,000 Sqft	1,400 Sqft	1,600 Sqft	2,000 Sqft
Two Story				
No basement	$177,997	$214,098	$235,702	$270,865
With unfinished basement	$189,061	$227,756	$250,787	$288,414
With finished basement	$206,337	$252,095	$278,255	$321,986

Source: RSMeans, *Residential Cost Data, 2021*

Strategies for Containing and Reducing Single-Family Costs

Since 2015, we have focused on becoming more systematic and objective in our assessment of costs. Table 4 shows the range of costs per home that we have financed for new construction over the last eight years. The benchmark for the 80th percentile is our threshold for flagging developments with a high cost per home. For example, if a new construction project in Minneapolis/Saint Paul proposes a TDC per home that exceeds $393,413, it will be flagged for additional scrutiny by staff. This is similar to using the threshold of 25 percent above the predictive model for multifamily projects.

As we collect better single-family cost data over a longer period of time, we will start reporting trend data and potentially develop a predictive cost model. This will allow us to create an accurate and formal process for reporting cost outliers to the Board when making selection and funding recommendations. While the current threshold of the 80th percentile has proven valuable for an initial discussion, it has deficiencies. It does not account for cost difference resulting from home sizes, garages, number of bathrooms, varying land costs, and other factors.

Costs are largely driven by land costs and the costs of construction (materials and labor), but other factors such as state-imposed requirements (such as prevailing wage) and unique factors

[14] Minneapolis Area Realtors; data applies to June 2021.

(such as historic rehabilitation) can increase costs. Those factors are reviewed and considered during the selections process.

Table 4: Impact Fund – TDC Benchmarks for New Construction, by Location

	TDC
Greater Minnesota	
Median	$210,195
20th percentile	$174,180
80th percentile	$252,296
Twin Cities Metro	
Median	$367,056
20th percentile	$343,046
80th percentile	$393,413
Total	
Median	$355,141
20th percentile	$236,927
80th percentile	$387,993

Excludes projects by Habitat for Humanity and Community Land Trusts

CONCLUSION

For a decade and a half, we have worked to contain upfront development costs while adding new policy initiatives that can increase costs. Given the shortage of affordable housing, limited resources, and the need to do more, cost containment will remain a critical issue. Since many of the cost drivers are outside the direct control of the agency and driven by other stakeholders, we will continue to pursue multiple strategies in the affordable housing development process.

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