MINNESOTA NAHRO

UTILIZING LIHTC AND/OR HIB IN THE SUBSTANTIAL REHABILITATION OF PUBLICLY OWNED PROPERTIES

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Developing Expertise

AFFORDABLE HOUSING RESOURCES IN MINNESOTA –AN OVERVIEW

Minnesota Housing

- Primary resource for affordable housing resources
- Annual Consolidated Request for Proposal (RFP) due July
- Available Resources:
  - LIHTC
  - HIB
  - Deferred Loans
    - Economic Development and Housing Challenge Program (EDHC)
    - HOME Investment Partnerships (HOME) Program
    - Preservation Affordable Rental Investment Fund (PARIF)
    - National Housing Trust Fund (NHTF) Program
    - Publicly Owned Housing Program (POHP)
  - First Mortgages
    - LMIR

Funding – At a Glance

2021 RFP / 2022 HTC

- 64 proposals that requested approx. :
  - $162MM in deferred loans
  - $134MM in permanent first mortgages
  - $54MM in Agency-administered 9% LIHTC

- The federal government allocated $10.9M to MHFA ($14.7MM to state including suballocator jurisdictions)

- Of the 64 proposals, MHFA selected 22 developments for further processing, or 34%.

HIB Overview

- Housing Infrastructure Bonds = HIB
- Limited obligation tax-exempt bonds issued by Minnesota Housing, authorized by the Legislature.
  - GO, 501c3, allocated housing revenue bonds
- Intended to fund the development of affordable rental housing and ownership to address specific housing needs.
- First authorized in 2012.

The Good

- Large amount of funding allocated by legislature for housing using this tool - $500 million since 2012.
- Principal and interest on bonds is paid by the state.
- Generally, the funds are provided to the development as a zero percent deferred loan. Principal and interest is due at the end of the loan term.
- Flexible funds. May be used with other sources. May qualify a development for 4% housing tax credits.
- Awarded directly to a developer. No unique ownership model required.

The Small Print

- Funds awarded through competitive application process. Commitments made in application process memorialized in declaration. Declaration runs with land for term, regardless of repayment.
- Uses are restricted, like other bonds (reserves and financing costs are ineligible).
- Developments are restricted in the legislation. Current allowed uses include:
  - Independent Senior Housing serving households at or below 50% AMI.
  - Preservation of existing federally subsidized housing.
  - Permanent supportive housing for households experiencing homelessness.
  - Permanent supportive housing for people with behavioral health needs.

The Bottom Line

- MHFA has discretion as to whether development will be HIB/deferred only or HIB/deferred with tax credits.

- Typically, HIB only when:
  - Development is too small to attract an investor (less than 30 units).
  - Development is in a small community.
  - Developer is a first-time developer.
  - MHFA is nearing their portion of the state volume cap limit.

Deferred Only Example

- 18 Units
- 100% Supportive Housing
- Committed Rental Assistance
- Serving Homeless Youth
- $6,560,000 Development Cost
- Funded with MHFA HIB and other deferred funds

Minnesota Housing Finance Agency – HTC and Deferred Funding Criteria (Scoring)

Scoring Priorities:

1. Greatest Need Tenant Targeting
2. Serves Lowest Income for Long Durations
3. Increasing Geographic Choice
4. Supporting Community and Economic Development
5. Efficient Use of Scarce Resources and Leveraged Funds
6. Building Characteristics

MHFA Scoring Criteria

Criteria	Point Range
1. Greatest Need/Tenant Targeting	
A. Large Family Housing	12-15
B. Senior Housing	3-7
C. Permanent Supportive Housing	7-32
D. People with Disabilities	7-13
2. Serves Lowest Income	
A. Preservation	15-40
B. Rental Assistance	6-25
C. Lowest Income Tenants	8-20
D. Long Term Affordability	8-9
3. Increasing Geographic Choice	
A. Needs More Affordable Housing Options	8-10
B. Workforce Housing Communities	3-5
C. Transit and Walkability	1-9
4. Supporting Community and Economic Development	
A. Community Development Initiative	3
B. Equitable Development	3
C. Rural/Tribal	4
D. QCT/Community Revitalization	4
E. Multifamily Award History	4
F. BIPOC/MBE	1-7
5. Efficient Use of Scarce Resources and Leverage	
A. Financial Readiness	4-16
B. Other Contributions	2-10
C. Intermediatory Costs	1-6
6. Building Characteristics	
A. Universal Design	3
B. Smoke Free Buildings	1
C. Enhanced Sustainability	1-5

MHFA Scoring Criteria

			Point Range
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3.	Increasing Geographic Choice		
	A.	Needs More Affordable Housing Options	8-10
	B.	Workforce Housing Communities	3-5
	C.	Transit and Walkability	1-9
4.	Supporting Community and Economic Development		
	A.	Community Development Initiative	3
	B.	Equitable Development	3
	C.	Rural/Tribal	4
	D.	QCT/Community Revitalization	4
	E.	Multifamily Award History	4
	F.	BIPOC/MBE	1-7
5.	Efficient Use of Scarce Resources and Leverage		
	A.	Financial Readiness	4-16
	B.	Other Contributions	2-10
	C.	Intermediatory Costs	1-6
6.	Building Characteristics		
	A.	Universal Design	3
	B.	Smoke Free Buildings	1
	C.	Enhanced Sustainability	1-5

BACKGROUND AND BASIC INFORMATION ABOUT LOW-INCOME HOUSING TAX CREDITS

What are Low-Income Housing tax credits?

- Since 1986, low-income housing tax credits (“LIHTC”) have encouraged private sector investment in affordable housing through a federal income tax credit. Tax credits are a mechanism to achieve a public benefit using private investment.

- Housing Tax Credits are derived from Section 42 of the Internal Revenue Code and administered by the IRS and state allocating agencies – Minnesota Housing Finance Agency (“MHFA”) in Minnesota. Minnesota is unique in that we also have “suballocators” composed of certain cities/counties.

- Each state receives Housing Tax Credits to allocate annually to projects. The amount is determined by the state’s population and apportioned by the Treasury Department.

What are the Minimum Requirements to Qualify for Housing Tax Credits?

- Housing Tax Credits are generated by certain apartment buildings that rent a portion of the units to low-income persons. At a minimum, one of the following must be met:
  - At least 20% of the units are rented to persons whose income does not exceed 50% of the area median income; or
  - At least 40% of the units to persons whose income does not exceed 60% of the area median income; or
  - At least 40% of the units must be rent restricted with rents set between 30% and 80% with the average being 60% AMI or less.
- Rents for low-income units are restricted to 30% of income and/or rental limits established periodically by HUD.
- The building generating the Housing Tax Credits must comply with rent/income restrictions for 15-30 years from the date the building is placed in service. Failure to satisfy this requirement can lead to recapture of tax credits.
- Non-transient rental housing
- New construction, substantial rehabilitation, and/or acquisition/substantial rehabilitation

How are Housing Tax Credits Awarded?

- At least annually, each state will seek applications for projects seeking Housing Tax Credits. The projects that “score” the best are awarded credits out of the state’s apportioned credits.
- Scoring criteria is determined by each jurisdiction to reward projects that include features deemed to be the most desirable.

How are Housing Tax Credits Claimed?

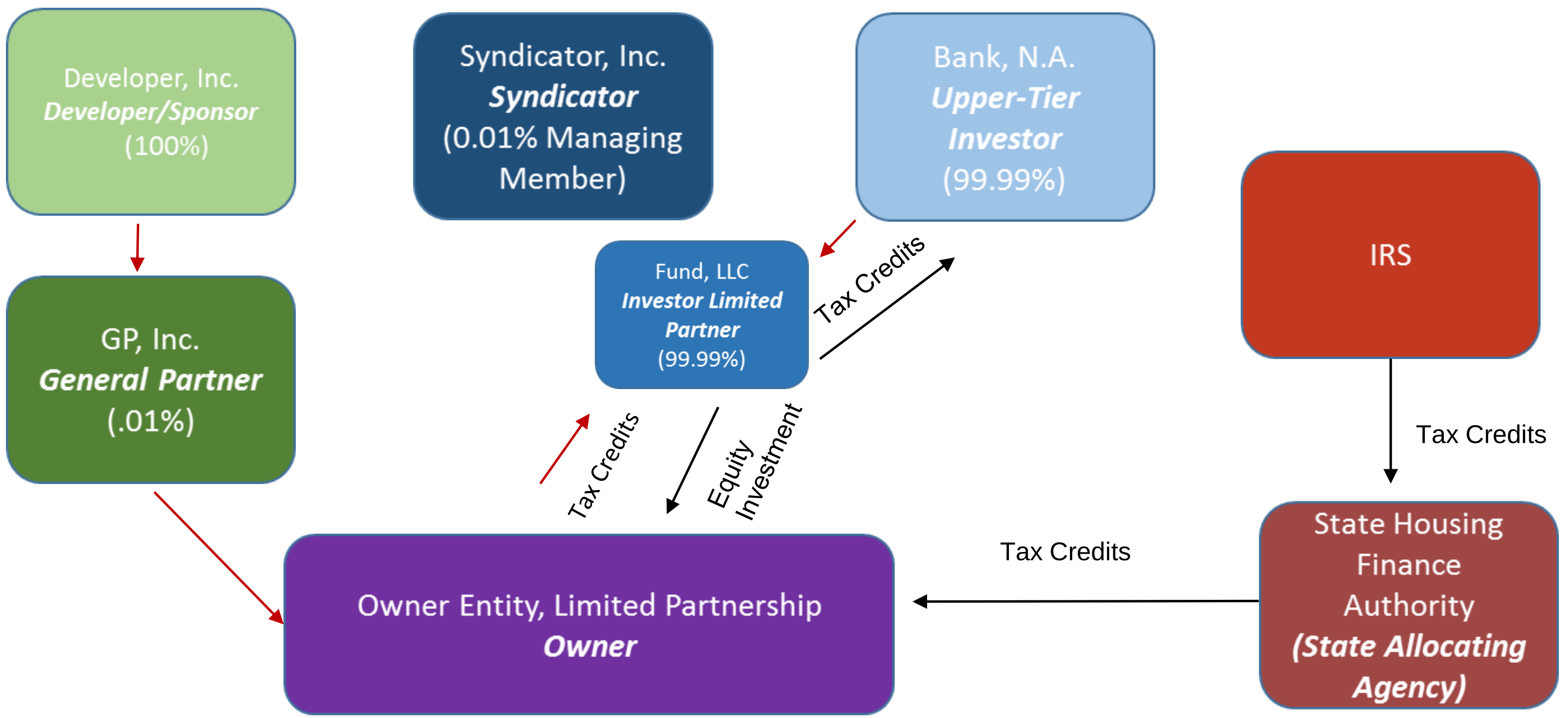
- Projects that are awarded or allocated Housing Tax Credits generally receive them equally over a 10-year period starting when the project is completed and leased up with qualifying tenants.
- Example: A project awarded $200,000 of annual credits would receive $2,000,000 of credits over 10 years.

Why are tax credits beneficial?

A tax credit allows a dollar-for-dollar reduction of a tax liability, whereas a tax deduction is a reduction of taxable income.

Tax Credit	Tax Deduction
$1,000,000 of gross income	$1,000,000 of gross income
	- $150,000 tax deduction
	= $850,000 taxable income
X 21% tax rate	X 21% tax rate
= $210,000 Tax Liability	=$178,000 Tax Liability
- $150,000 Tax Credit	
- = $60,000 Adjusted Tax Liability	

How does it work?



TAX CREDITS AND PUBLIC HOUSING

What is RAD?

- Allows conversion of public housing units to Section 8
  - Private financing
  - LIHTC

- Help to address backlog of deferred maintenance of public housing
  - Estimates range from $26 billion to $70 billion
  - Deferred maintenance continues to grow even with RAD

RAD Accomplishments

- $5.7 billion for construction and rehabilitation
- Leverage $19 for each $1 of public housing fund
- 140,000 units benefitted

Possible Uses of RAD - Creativity

1. Conversion of property with minimal needs
2. Conversion with material capital needs
3. Consolidation of scattered site
4. New construction
5. Create mixed income

Process

- Takes 6 to 18 months
- Multiple steps
  - Meetings with tenants
  - Application to HUD
  - HUD commitment (CHAP)
  - PHA submits financing plan
  - HUD issues RAD conversion commitment (RCC)
  - Closing

Two Types of Section 8 Assistance

	PBV	PBRA
Contract Term	15 years but can be increased to 20 years with 15-year renewal	20 years
Rent	Lesser of reasonable rent or 110% of FMR	120% of FMR, except if rents are below market can go up to 150% if supported by rent comparability study
Rent Increases	OCAF adjustments up to reasonable comparable rent	OCAF annual adjustments
Choice Mobility	Tenant has right to move after 12 months	Tenant can move 24 months after later of HAP Contract date or move-in date – PHA can limit
Administrator	HUD’s Office of Public and Indian Housing	HUD’s Office of Housing
Number of Units that can be Converted	50% of a building (can be up to 100%)	100% of units in a building

Tenant Protections

- Notification and relocation requirements
- No rescreening or income targeting
- Right to remain
- Tenants organizing rights
- Limited rent increases
- Right to receive tenant-based voucher

PHA Involvement

- PHA or non-profit must remain involved
- PHA or affiliate can be general partner or managing member
- Ground Lease
- PHA can be developer or co-developer
- RAD Use Agreement must remain in place for term of HAP contract and renewals
    - Must be in first position

Potential Issues

- Can’t relocate over income tenants
- Rents may exceed permitted LIHTC rents - contract pre 1/19/2017
- Student rules differ
- Use Agreement – first priority requirement may limit available financing

CALCULATING THE HOUSING TAX CREDIT

2 Types of Housing Tax Credits

- 9% Tax Credits (or 70% present value credits) – Are awarded competitively each year by the applicable state allocating agency. The highest scoring projects are awarded credits up to the amount apportioned to the state.
  - Pros: Generate more Housing Tax Credits = more tax credit equity.
  - Cons: Costly and time-consuming to apply and there is no guarantee of successfully obtaining an award.

- 4% Tax Credits (or 30% present value credits) – Automatically generated by financing at least 50% of a project with tax-exempt bonds that meet certain criteria.
  - Pros: Not competitively awarded, so the risk of not getting credits is very low.
  - Cons: Generate less Housing Tax Credits so projects must carry more debt financing.

Computing LIHTC

Credits are computed as follows:

Annual Credits	**=**	**The Applicable Percentage**	**X**	**The Qualified Basis of each Qualified Low- Income Building**

And the Applicable Percentage will be either or both of following:

Applicable Percentage	**=**	**30% Present Value Credit (4% Credit)**	**Or**	**70% Present Value Credit (9% Credit)**

Credit Calculation Example

9% Example

$10,000,000 Qualified Basis	X	9% Applicable Percentage	=	$900,000 Maximum Amount of Annual Credits

4% Example

$10,000,000 Qualified Basis	X	4% Applicable Percentage	=	$400,000 Maximum Amount of Annual Credits

Credit Limitation - Lesser of the amount calculated or the amount awarded by the Credit Agency.

Qualified Basis Computation

Computed as follows:

Qualified Basis	=	Eligible Basis	X	Applicable Fraction

Applicable Fraction

- The Applicable Fraction is the lesser of:
- The Unit Fraction (Low-Income Units/total residential rental units), or;
- The Floor Space Fraction (Low-Income Unit floor space/total residential rental unit floor space)
  - A unit is not Low-Income unless it is occupied by qualified Low-Income occupants and is rent restricted.
  - In the first Credit Period year, a special computation is required to reflect varying monthly occupancy

Example – 4% Credits

80 Units

Section 8 Contract for 100% of Units

All units serve households at 50% AMI or below

Applicable Fraction = 100%

Qualified Basis Example

$8,000,000 Qualified Basis	=	$10,000,000 Eligible Basis	X	80% Applicable Fraction

Eligible Basis

- General Rule – Subject to a number of exceptions, Eligible Basis equals adjusted basis (depreciable basis) of the residential rental space
- Depreciable includes items such as construction, architect fees, construction period interest, developer fee, etc.
- Eligible Basis is determined separately for new construction/rehabilitation and acquisition
- New Construction – Eligible basis equals the Adjusted basis (hard +soft construction costs, including developer fee)

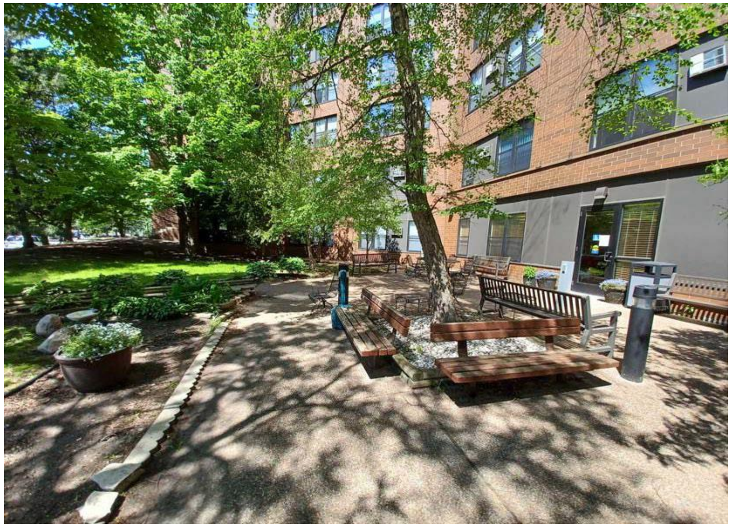
Eligible Basis – Rehabilitation Costs

- Rehabilitation costs – Eligible basis equals the Adjusted basis (hard +soft construction costs, including developer fee)
- To qualify for LIHTC, the rehabilitation costs incurred within a 24-month period must be at least the greater of:
  - $6,700 per unit, plus inflation, or
  - 20% of the acquisition costs

Eligible Basis – Acquisition

- Existing Buildings – Eligible Basis for an existing building equals the cost of purchasing the building (but not land costs).
- 4% Credits Only – The costs of Purchasing an Existing Building are only eligible for 4% Credits, whether or not there is tax-exempt bond financing.
- Must Have Rehabilitation Credits – LIHTCs are allowable for the acquisition of an existing building only if rehabilitation LIHTCs are also allowable with respect to such building.
- 10-Year Rule - Generally LIHTC is available for the costs of purchasing a building only if the building has not been last placed in service in the 10 preceding years. There are certain exceptions and special rules for determining placement in service.

Example – 4% Credits



Item	Cost	Basis
Land	$1,200,000	$0
Building Value	$5,200,000	$5,200,000
Rehab Cost	$8,356,458	$8,356,458
Professional Fees	$1,283,500	$1,041,867
Developer Fee	$1,600,000	$1,600,000
Financing Fees	$849,170	$340,740
Reserves	$530,497	$0
TOTAL	**$19,019,625**	**$16,539,064**

Eligible Basis = $16,539,064

Example – 4% Credits

$16,539,064 Qualified Basis	**=**	**$16,539,064 Eligible Basis**	**X**	**100% Applicable Fraction**

$16,539,064 Qualified Basis	**X**	**4% Applicable Percentage**	**=**	**$661,562 Maximum Amount of Annual Credits**

Example – 4% Credits

$661,562 Maximum Amount of Annual Credits	X	10 Years	=	$6,615,620 Maximum Amount of Credits

$6,615,620 Maximum Amount of Credits	X	$0.87 Price Per Credit	=	$5,755,589 Syndication Proceeds

Example – 4% Credits

Source	Amount
Syndication Proceeds	$5,755,569
LMIR Mortgage	$1,635,000
PARIF	$5,741,000
HIB	$1,459,000
Existing Reserves	$441,865
Sales Tax Rebate	$139,547
Seller Notes	$3,847,644

Example – 9% Credits

45 Units

15 Units of Supportive Housing serving Homeless Youth

All units serve households at 60% AMI or below

Applicable Fraction = 100%

Example – 9% Credits

Item	Cost	Basis
Land	$1,103,969	$0
Building Value	$0	$0
Construction Cost	$8,983,417	$8,573,385
Professional Fees	$1,058,600	$797,150
Developer Fee	$725,000	$725,000
Financing Fees	$349,900	$254,350
Reserves	$174,338	$0
TOTAL	**$12,395,334**	**$10,349,885**

Eligible Basis = $10,349,885

Example – 9% Credits

$10,349,885 Qualified Basis	**=**	**$10.349,885 Eligible Basis**	**X**	**100% Applicable Fraction**

$10,349,885 Qualified Basis	**X**	**9% Applicable Percentage**	**=**	**$931,489 Maximum Amount of Annual Credits**

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Example – 9% Credits

$931,489 Maximum Amount of Annual Credits	X	10 Years	=	$9,314,890 Maximum Amount of Credits

$9,314,890 Maximum Amount of Credits	X	$0.885 Price Per Credit	=	$8,243,677 Syndication Proceeds

Questions

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