THE Kennedy COMMISSION

SCANPH

SOUTHERN CALIFORNIA ASSOCIATION OF NONPROFIT HOUSING

TCAC Crash Course: Understanding LIHTC with Bill Pavao

Executive Director Emeritus of TCAC and Current SCANPH Board Member

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Thursday, February 14th

1:00 pm - 3:00 pm

City of Tustin Council Chambers

300 Centennial Way

Get All Your TCAC Questions Answered!

Low Income Housing Tax Credits

Overview of the California Program

William Pavão, SCANPH Board Member

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Outline

- How affordable housing is financed
- Federal Low Income Housing Tax Credits
- The California Program

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Financing

- Combination of debt and equity
  - Like home purchase loan & downpayment
- Affordable housing:
  - **Conventional debt** - bank loans
  - **Equity** - through Low Income Housing Tax Credits
  - **Gap financing** - “soft debt”

Conventional Debt

- Using assumptions about project size, unit configuration, rents, subsidies, and design, developer creates a pro forma operating budget estimating annual income and expenses

- Establishes how much Net Operating Income (NOI) remains after paying operating costs

- Private (conventional) debt may be borrowed using a portion of NOI: Debt Service Coverage Ratio (DSCR).

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Soft Debt and Low Income Housing Tax Credit Equity

- The development costs not paid by a conventional loan must be covered by capital that does not require a fixed repayment schedule

- Soft debt is typically low-interest and due on an annual “residual receipts” basis. Unpaid balance is due at the end of a specified term (e.g., 55 years)

- Equity is induced in by tax benefits

Low Income Housing Tax Credits (LIHTCs)

- Created by the Tax Reform Act of 1986
- Federal government no longer a significant lender
- Induces in equity from investors who become limited partners (LPs) in ownership (single asset partnerships)
    - LP: 99.9% vs. 0.01% ownership of partnership
- Ten years of credits against federal taxation,15 years of programmatic compliance (recapture)

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The Basics

- Two types of credits: “9%” and “4%”
    - 9% credit authority for the State is limited
    - 4% authority is unlimited, but tied to tax exempt bond authority (must pay for at least 50% of development’s basis costs)
- Income and rent restricted to 60% Area Median Income (AMI) - now up to 80% in limited cases
    - HH of 4 in Orange Co.: 60% AMI = <u>$65,580</u>, 80% AMI = <u>$87,440</u>

The Basics about Basis

- Basis = costs associated with the development of a depreciable asset

- Does <u>not</u> include land, some legal costs, some interest costs

- Can be increased or “boosted” by location

  - Qualified Census Tracts (QCTs)

  - Small Difficult Development Areas (SDDAs)*

* State-designated DDAs in 9% program for Special Needs projects and State credit applicants.

Two Types of Credits

- 9% credits (formerly 70% present value (PV) credits)
- 4% (30% PV credits)
    - Used with tax-exempt bond financing
- Floating rate:
    - “9%” = 9% fixed (no longer floats)
    - “4%” = 3.32%, floats monthly to maintain 30% approximation

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9% Example:
$23 million Project

- $20 million in “basis”
- QCT or DDA boost: 130% x $20M = 26M(!)
- 9% Credits: 9% x $26M = $2.34M annually
- **$23.4 million** in credits over 10 years*

* Exceeds total development cost (TDC)

Same Project Using 4% Credits

- $20 million in “basis”
- QCT or DDA boost: 130% x $20M = $26M
- 4% Credits: 3.32% x $26M = $863,200 annually
- **$8.632 million** in credits over 10 years

*Note: $6.64 million received over 10 years = 30% of unboosted $20M (PV)

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9% Competition: Annual Federal Credit

- Total: 39.5M population x $2.70 = $106M
- Set-Asides
  - Nonprofit: Homeless Assistance (10%) $10.7M
  - Rural (20%) $21.4M
  - At-risk (5%) $ 5.2M
  - Special Needs (4%) $ 4.2M

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Geographic Apportionments: Annual Credits Plus State Credits

City of LA (17.6%)	$11.3M
Balance of LA Co. (17.2%)	$11.1M
Central Valley (8.6%)	$ 5.5M
San Diego (8.6%)	$ 5.5M
Inland Empire (8.2%)	$ 5.3M
East Bay (7.4%)	$ 4.7M
Orange Co. (7.3%)	$ 4.7M
S&W Bay Area (6.0%)	$ 3.8M
Capital Region (5.7%)	$ 3.6M
Central Coast (5.2%)	$ 3.3M
Northern (4.4%)	$ 2.8M
San Francisco (3.7%)	$ 2.3M

9% Scoring

• GP Experience	6 pts.
• Management Experience	3 pts.
• Housing Needs w/ Amenities	10 pts.
• Site Amenities (SN - NonSN)	15 pts.
• Service Amenities (SN - Non-SN)	10 pts.
• Sustainable Building Methods	5 pts.
• Lowest Income Targeting	52 pts.
• Readiness to Proceed	10 pts.
• Misc Fed and State Policies	2 pts.
	113 pts.

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Tiebreakers

Within City of LA: HCID Letter of Support

Otherwise:

First: Housing Type Goal

- Large Family (65%)
- LF New Construction, High Resource (30%)
- Special Needs (30%)
- At-Risk (15%)
- Seniors (15%)

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- Rural Acq/Rehab (30%)

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Tiebreakers cont.

Final: $\dfrac{\text{Soft Resources}}{\text{TDC (Residential)}}$

+

$$\left(1 - \left(\frac{\text{Requested Unadjusted Eligible Basis*}}{\text{Total Residential Development Costs}}\right)\right) / 3$$

* Decreased basis requests will benefit the tiebreaker only to the extent that they exceed committed soft public funds.

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Final Tiebreaker Example

Final:

$$\frac{\$4.6\text{ Million}}{\$23\text{ Million}} + \left(1 - \frac{\$10\text{ Million*}}{\$23\text{ Million}}\right) / 3$$

* Decreased basis requests will benefit the tiebreaker only to the extent that they exceed committed soft public funds.

Final Tiebreaker Example

Final:

20 %

+

1 - (43.4%) / 3

= 20% + (56.6% / 3)

= 20% + 18.84% = 38.84%

2019: Opportunity Area Bonus

• Highest Resource Area (non-rural)	20%
• High Resource Area (non-rural)	10%
• Highest Resource Area (rural)	10%
• High Resource Area (rural)	5%

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Final Notes

- California State Credits
  - Certificated Credits
- First Time Applicants for Credits: Consultants
- TCAC application forms

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Q&A Session

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