State of California **California Tax Credit Allocation Committee**

M E M O R A N D U M

January 6, 2004

To: **All Interested Parties**

From: **Jeanne Peterson**
Executive Director

Re: **Draft 2004 Tax Credit Program Regulations**

As many of you know, staff of the Tax Credit Committee has spent considerable time in formulating new draft regulations for our 2004 program year. The attached, 1st Draft of those Regulations shows the proposed changes (both deletions and additions). This memo explains some of the changes and the thinking behind them.

Please also note that public hearings and a public comment period will be held to receive your comments on the proposed regulations. The Notice of Public Hearings (to be held in Los Angeles on January 28, and in Sacramento on January 29, also accompany this memorandum.

Mindful that the development process is an ongoing and lengthy one, staff is not proposing major changes to many of the point categories at this time. However, as promised, there are several changes that you should be aware of. The geographic areas and the set-asides that "count" against the geographic areas have changed (a fuller explanations of the proposed areas and percentages follows). Also, the tie-breakers have changed to reflect the percentage of credit to the total development costs of projects. Additionally, at the Committee's urging, the penalties for incorrect and/or misleading information have been strengthened. In an effort to recognize increasing costs associated with increasing labor costs, the basis limit exceptions for such projects has been increased, as has the permissible developer fee.

We recognize that not only does the 9% tax credit program remain highly competitive, but that there will never be consensus amongst all users as to the best methodology for allocating this important and valuable resource. Staff has already received numerous comments from our users. We have attempted to incorporate those ideas that we believe will further the public policy goals of the Committee and to achieve balance between many competing factors and ideas.

Explanation of the New Geographic Areas

In revising the current geographical distribution system, staff considered several indicators of need to arrive at the new suggested percentages:

County Population: This is the basis for the federal credits that are distributed to California as a whole. The Department of Finance's most recent annual population estimates by county (July 1, 2002) was used as the basis for revising the geographic apportionment percentages.

County Housing Cost: Staff considered and discarded multiple data sets as potential indicators of housing costs within counties, including, among others, CalHFA Homeownership Price Limits, HUD Estimated Fair Market Rents for a Two-Bedroom Apartment, and TCAC project costs per square foot on a county by county basis. The data set chosen to indicate housing costs is the TCAC Project Costs Per Square Foot from 1999-Present for 9% New Construction Projects. Where possible, staff used final project costs and square footage figures from final cost certifications to update the initial cost and square footage data in the TCAC database. These figures will be updated on a rolling 5-year basis. In cases where the there were fewer than three projects in a county, that county's figures were adjusted using the regional average.

Poverty: Staff considered various multiple data sets as potential indicators of housing costs within counties, including Bureau of Labor Statistics Per-Capita Personal Income, HUD Estimated Unadjusted Median Family Income for a Family of Four, and so on. The data set chosen to indicate poverty is the 2000 Census Data on the Proportion of the Population Earning Less Than 2x the Poverty Line.

County Urbanization: By law, 20% of all federal credits are set-aside for rural developments. While staff removed all 100% Rural Counties from the geographic apportionment system, many of the remaining counties still had heavily rural populations. Staff adjusted the distribution of credits to address this issue by using 2000 Census Data on Percentage of Population Living in Urban Areas. (It should be noted that the Census definition of urban is more inclusive than that used by TCAC, as only four counties are considered entirely rural according to the Census data.)

In developing the new set of geographic regions staff, considered three issues: 1) the geographic relationship among the counties, 2) how similar the counties were when ranked by each of the various data sets considered for use as housing and poverty indicators, and 3) the current set of geographic regions.

Each county, with the exception of those that are 100% rural for tax credit allocation purposes, is included in one of the new geographic areas. And because a larger percentage of the overall credit is proposed to be ascribed to the geographic areas (since a smaller amount will be ascribed to set-asides not "counting" in the geographic areas), no previous geographic area will have a smaller percentage of credit than it has had under the previous system.

Assuring that no one Geographic Area has a huge over allocation

Many people that have been involved in discussions prior to the publication of these draft regulations have mentioned that the geographic areas should have their "fair share" allocations. Although Committee staff does not necessarily embrace the "fair share" notion as expressed by some (there is no absolute "right" of any applicant or any geographic area to receive a certain amount of credit), we have attempted not only to create more logical geographic areas, but we have also suggested that the "over allocation" issue be dealt with by adjusting (either adding to, or subtracting from) an area's available amount in each funding round, based on the previous funding round outcomes.

New Tie-breaker

As many of you are aware, the last tie-breaker in 2003 measured the requested eligible basis per bedroom and rewarded projects with the least requested eligible basis per bedroom. This resulted, particularly in some areas, in an abnormally large percentage of four bedroom units, irrespective of whether such units were actually the most needed. Several suggestions were received that would have that tie-breaker replaced with a tie-breaker advantaging the percent of public funds committed to a development. And although staff believes that communities, the state, or the federal government committing funds to tax credit developments is worthwhile, that it shows support, and that such developments are subject to further scrutiny and monitoring than those that do not involve public funds, it believes that a better measurement, for purposes of the Committee, is a more neutral one that also recognizes the benefit of developments that may not have public funds. Thus the proposed new measurement, which could be achieved by several means, would advantage those applications with the lowest ratio of credit requested to total project costs, excluding deferred developer fee and general partner equity.

These are a few of the proposed changes. You are encouraged to read the entire document for other changes, and to submit your comments in writing to Committee staff within the next few weeks so that we may consider them prior to presenting a final recommendation to the Committee.

As always, thank you for your interest and participation in creating affordable housing opportunities for Californians.