Memorandum

TO: Agency Partners and Stakeholders
FROM: Minnesota Housing Staff
SUBJECT: Possible Changes to the 2014 Qualified Allocation Plan (QAP)
DATE: September 24, 2012

In an effort to give agency partners and stakeholders sufficient time to assess possible changes to Minnesota Housing's Qualified Allocation Plan (QAP) for its Low Income Housing Tax Credit (LIHTC) program, the agency is articulating some possible changes in September 2012, well in advance of the draft 2014 QAP that will be submitted for formal public comment in January 2013. This memorandum does not represent all the changes that may be incorporated into the draft 2014 QAP, but it captures some of the larger changes that the agency is currently considering.

The agency will be accepting comments on these initial proposed changes through October 31, 2012. Comments supported with data, research, and thorough analyses are the most beneficial.

Cost Containment

In the draft 2013 QAP, Minnesota Housing proposed moderate- and low-cost thresholds for the first time. If a project's total development costs were below the moderate-cost threshold, the project would have received 5 points in the selection process. If a project's total development costs were below the low-cost threshold, the project would have received 10 points. Because these cost thresholds were new and partners/stakeholder felt that they did not have sufficient time to fully assess them, Minnesota Housing decided to wait a year to include them in the QAP.

The cost thresholds were designed so that only a portion of projects would receive the cost containment points. The Agency created the thresholds by looking at total development costs for the tax credit projects that it funded since 2003 (adjusted for inflation) and setting the thresholds so that roughly: (1) 50 percent of the developments in each of the cost categories would receive no points, (2) 25 percent would receive 5 points, and (3) 25 percent would receive 10 points.

When originally proposed, the agency received comments about the thresholds. The following list summarizes the comments and includes the agency's response and logic as it revised the proposed cost thresholds for the coming year:

- By not having a large-unit category (large number of bedrooms per unit), the thresholds discourage the development of large-unit properties for large families.

> *The agency agrees with this comment and has added a large-family cost category. (See the new proposed thresholds below.) During our Regional Housing Dialogues in April of 2012, we heard a lot about the need for larger units for larger families.*

- Minnesota Housing should separate the Greater Minnesota cost category between the metropolitan communities like Duluth, St. Cloud, and Rochester from other parts of Greater Minnesota. The comments contended that costs in these communities are more similar to the Twin Cities metro area than other parts of Greater Minnesota.

Using cost data for the tax credit developments that Minnesota Housing has funded since 2003 (adjusted for inflation), we tested this assertion. We separated the developments in Greater Minnesota counties that are part of a Metropolitan Statistical Area or border the seven-county Twin Cities metro area from all the other Greater Minnesota counties. The difference in average total development costs between these two groups was not statistically significant and for practical purposes the same. While developments in these more metropolitan areas may have some costs that are higher (e.g. land costs), projects in other parts of Greater Minnesota likely have other cost features that are higher (e.g. building in remote locations). Our revised cost thresholds do not make this suggested revision.

- One comment suggested that the cost thresholds for Greater Minnesota were disproportionately low and that the agency needed to verify its cost data.

The analysis is based on the total development costs of 169 tax credit developments that the agency has funded since 2003. The agency is comfortable with the validity of the data.

- One comment referred to the cost thresholds as "limits".

The thresholds are <u>not</u> limits that represent maximum allowed costs. A project can have costs above the thresholds and be selected. It just won't receive the cost containment points.

- Several comments indicated that the thresholds will discourage developments that achieve other public policy objectives and have higher costs. For example:
    - Supportive housing for the long-term homeless,
    - Transit oriented development,
    - Historic Preservation,
    - Environmental abatement, and
    - Energy-efficiency and green building.

The 169 developments in the analysis that created the thresholds include some properties that are supportive housing, transit-oriented development, historic preservation, environmental abatement, and/or energy-efficient/green. Thus, these costs are already built into the analysis. It is true that that it will be harder for higher cost developments to meet the thresholds, but the agency is trying to balance multiple (and often conflicting) priorities through the QAP's pointing structure in the selection process. A supportive housing development may not receive cost containment selection points, but it will receive the supportive housing points. The agency recognizes these other public policy objectives through the other priorities receiving selection points. A development that meets multiple priorities will have a good shot at being selected even if it does not meet the cost containment criterion. More importantly the agency wants to give developers the incentive to not only meet multiple policy priorities but also contain costs.

It should also be pointed out that Minnesota Housing requires all its developments meet energy-efficient/green standards.

The essence of the cost-containment criteria can be explained in one statement: All else equal, Minnesota Housing wants to select lower cost projects, and the thresholds help the agency identify the lower cost projects.

- The thresholds ignore ongoing life-cycle operation and maintenance costs and may encourage lower quality construction.

The design of the properties that Minnesota Housing finances, along with their systems, are reviewed by the Agency's architects, who take steps to ensure that all the properties are well built and efficient. Again, all 169 properties in the analysis that created the thresholds were funded by Minnesota Housing with the expectation that they are well built and efficient.

As mentioned under the previous bullet, Minnesota Housing requires all its developments to meet energy-efficient/green standards.

- Several comments suggested that developments in Tribal communities have higher costs because of procurement requirements (TERO fees, Native Contractor Preferences, fewer contractor options, less competitive bids, etc.) and the construction of single-family detached homes with tax credits.

These comments raised several interesting points that the Agency has been unable to fully assess. The Agency may decide to add a cost adjustment factor when assessing tribal developments, but the agency is still trying to assess this. One of the comments on the original thresholds provided some data to backup its assertion about higher costs, but the Agency needs more information, particularly about the incremental costs per housing unit that the TERO fees, contractor preferences, and other requirements add. Developers who have worked both in and out of Tribal communities are encouraged to provide comparative data.

- A few comments suggested alternatives for assessing costs, which included:
    - Using tax-credit-basis per unit rather than total-development-cost (TDC) per unit;
    - Using some type of adjusted-TDC, which could include some combination of the following cost exclusions:
        - Amounts for social services and reserves (homeless units),
        - Assumed debt, and
        - Costs paid by other agencies, including:
            - ✓ Brownfield remediation costs covered by funds from environmental agencies,
            - ✓ Historic preservation costs covered by historic tax credits, and
            - ✓ New infrastructure costs covered by tax increment financing.

There are numerous ways that Minnesota Housing can define the costs that it wants to contain. While TDC encompasses more costs than the tax credits finance, the agency wants to ensure that all resources going into the developments that it finances are being used cost effectively. Ideally, developers in Minnesota will build or rehabilitate the maximum number of affordable housing units with the limited funds available (regardless of the *source). In fact, the National Council of State Housing Agencies (NCSHA) adopted a cost containment policy in December of 2011. The policy states:*

"In addition to carefully rationing the amount of Housing Credit allocated to eligible developments, as federally required, each Allocating Agency should develop a per unit cost limit standard. That standard should be based on total development costs, including costs not eligible for Housing Credit financing and costs funded from sources other than the Housing Credit…Finally, each Allocating Agency should regularly review its QAP and related allocation guidelines with the goal of reducing development costs."

In the current financial and political environment, Minnesota Housing and all housing finance agencies need to demonstrate that they are using housing tax credits and other public resources as cost effectively as possible.

- Several comments mentioned the possibility of unintended consequences with the cost containment requirement – for example, lower quality construction, less visually appealing buildings (encouraging NIMBYism), etc.

A risk of any change is unintended consequences. There are ways for Minnesota Housing to manage these risks. One approach is to phase in the points awarded for the cost containment over time. For the 2013 QAP, Minnesota Housing proposed 10 points for low-cost developments and 5 points for moderate-cost developments; and the Agency decided to delay its implementation. For the 2014 QAP, Minnesota Housing could award 3 points for low costs and 2 points for moderate costs. If this point structure helps contain costs without creating significant unintended consequences, the agency could then increase the points to 5/3 and eventually to 10/5 with on-going monitoring. The goal is to provide sufficient incentive for projects to prudently control costs without significantly restricting quality and creating unintended consequences.

The following table lays out the some possible draft cost-containment thresholds for the 2014 QAP.

Table 1: Draft Cost Containment Thresholds for 2014 QAP

	Low Cost Threshold	Moderate Cost Thresholds
New Construction Metro for Singles	$182,000	$203,000
New Construction Metro for Families/Mixed	$207,000	$229,000
New Construction Metro for Large Families	$209,000	$233,000
New Construction Greater Mn for Singles	$125,000	$144,000
New Construction Greater Mn for Families/Mixed	$157,000	$177,000
New Construction Greater Mn for Large Families	$159,000	$181,000
Rehabilitation Metro for Singles	$124,000	$150,000
Rehabilitation Metro for Families/Mixed	$158,000	$183,000
Rehabilitation Metro for Large Families	$165,000	$193,000
Rehabilitation Greater Mn for Singles	$70,000	$95,000
Rehabilitation Greater Mn for Families/Mixed	$105,000	$132,000
Rehabilitation Greater Mn for Large Families	$112,000	$142,000

"Singles" applies to developments where the share of efficiencies and 1 bedroom units is 75% or greater.
"Large Families" applies to developments where the share of units with 3 or more bedrooms is 50% or greater.
"Families/Mixed" applies to all other developments.
“New Construction” includes regular new construction, adaptive reuse to residential housing, and projects that mix new construction and rehabilitation.

As needed, please comment on the proposed thresholds, a phased-in pointing structure, and the Agency’s responses to last year’s comments.

Workforce Housing

In the 2013 QAP, Minnesota Housing gives points to developments that are in top growth communities (jobs or households). For the 2014 QAP, the agency is considering an alternative approach that focuses exclusively on jobs, a different jobs dataset, and a more refined analysis. The change emphasizes workforce housing and investing resources in areas with a large number of jobs or job growth. The following discussion outlines the potential changes:

Elements maintained from last year:

- Basing eligibility for job growth points on cities or townships that have at least 2,000 jobs in each year of the analysis (2005 and 2010 in the current analysis).
- Calculating job growth based on the number of total jobs in cities and township (rather than on the number of low- and moderate-wage jobs).
- Identifying the top 20 communities in Greater Minnesota and top 10 communities in the Twin Cities Metro based on their absolute change in jobs (rather than a percentage change).
- Allowing for a modest commute shed; projects are eligible to receive points if they are within 10 miles of a selected city/township in Greater Minnesota and within 5 miles of a selected city/township in the Twin Cities Metro.

Elements changed in this proposal:

- Removing household growth from the analysis.
- Changing the underlying dataset to the Census Bureau’s Longitudinal Employer-Household Dynamics (LEHD) data because it is more geographically precise on the location of jobs.
- Decreasing the period being analyzed for job growth from 10 years to 5 years. This is due to data availability and integrity for the LEHD dataset in years prior to 2005.
- To be eligible for a classification as a top job-growth community in Greater Minnesota, the job change within the city and 10 mile buffer must show growth. A city or township that ranks high in job growth within the city or township but is losing just as many jobs in the 10 mile commute shed will not be selected. The purpose is to identify communities with an overall growth, not shifting of jobs within the community.
- Adding to the list of the top job growth communities the top communities in the absolute number of jobs - 10 communities in Greater Minnesota and 5 communities in the Twin Cities metro. (Communities qualify if they have a large number of jobs or a large increase in the number of jobs.)

The results of the revised methodology are shown on the following pages. Tables 2 and 3 list the top communities. Map 1 visualizes these workforce housing communities, which includes the commute shed.

Table 2. Twin Cities Metro – Workforce Housing Communities – Proposed 2014 QAP

Top 5 Cities – Total Jobs	2010 Jobs	Rank	Top 10 Cities - Job Growth*	2010 Jobs	2005 Jobs	Change	Rank
Minneapolis	292,778	1	Golden Valley	37,332	26,960	10,372	1
Saint Paul	174,011	2	Eagan	46,916	37,010	9,906	2
Bloomington	85,888	3	Eden Prairie	49,061	44,714	4,347	3
Edina	60,106	4	Woodbury	16,358	12,183	4,175	4
Minnetonka	49,387	5	Coon Rapids	20,877	16,757	4,120	5
			Apple Valley	13,644	9,794	3,850	6
			Shakopee	15,554	12,095	3,459	7
			Richfield	16,747	13,753	2,994	8
			Mounds View	5,812	2,995	2,817	9
			Anoka	13,641	10,896	2,745	10

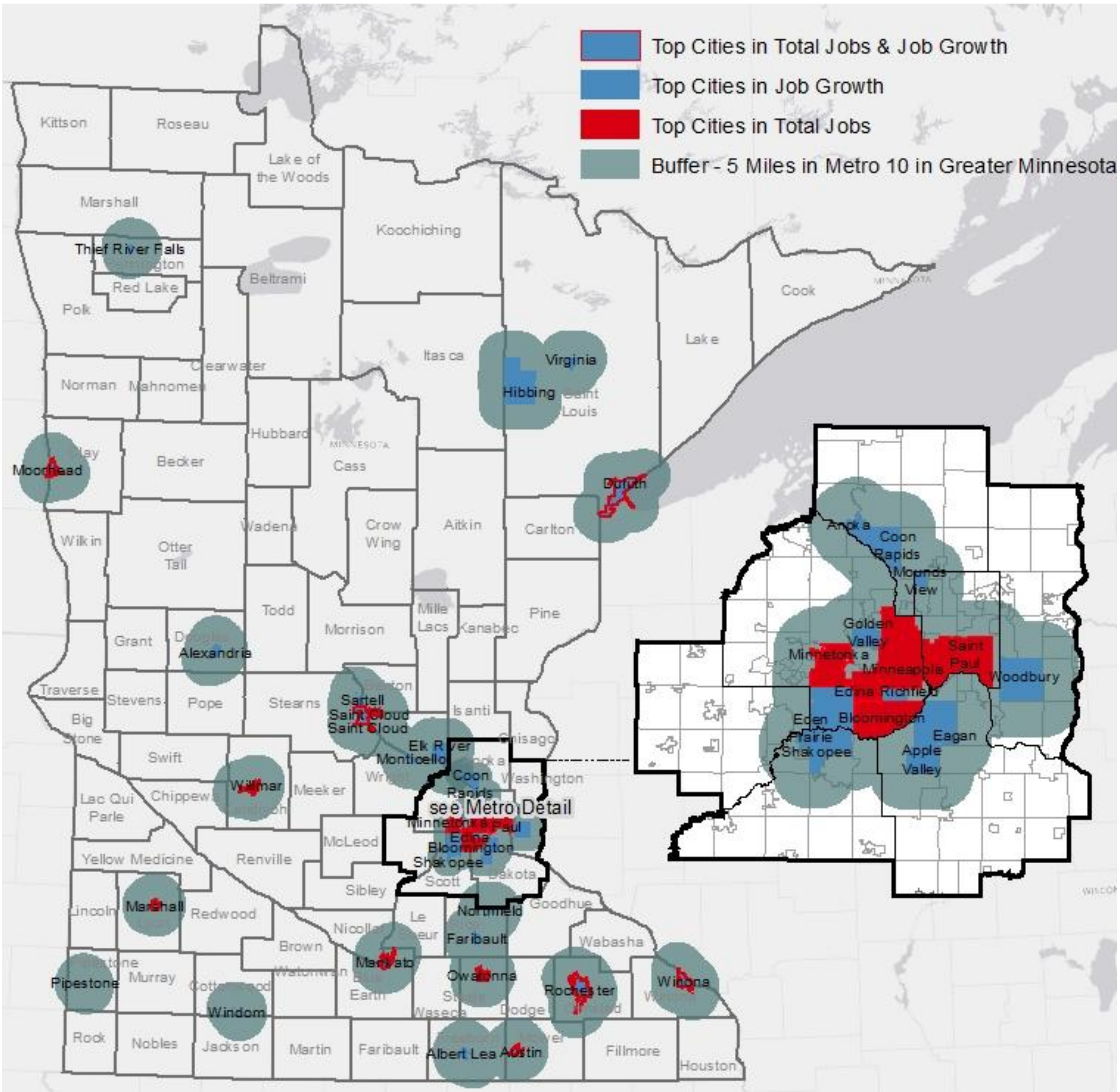
Table 3. Greater Minnesota – Workforce Housing Communities – Proposed 2014 QAP

Top 10 Cities – Total Jobs	2010 Jobs	Rank	Top 20 Cities/Townships - Job Growth**	2010 Jobs	2005 Jobs	Change	Rank
Rochester	77,743	1	Rochester	77,743	69,080	8,663	1
Duluth	59,521	2	Marshall	17,517	8,982	8,535	2
Saint Cloud	46,426	3	Duluth	59,521	51,803	7,718	3
Mankato	32,555	4	Saint Cloud	46,426	40,569	5,857	4
Winona	19,206	5	Mankato	32,555	28,582	3,973	5
Marshall	17,517	6	Austin	15,234	13,238	1,996	6
Owatonna	16,755	7	Winona	19,206	17,218	1,988	7
Austin	15,234	8	Elk River	10,347	8,500	1,847	8
Moorhead	14,650	9	Moorhead	14,650	12,989	1,661	9
Willmar	13,574	10	Northfield	10,185	8,907	1,278	10
			Windom	3,192	2,067	1,125	11
			Faribault	10,713	9,628	1,085	12
			Monticello	5,130	4,087	1,043	13
			Sartell	4,026	3,030	996	14
			Hibbing	8,314	7,437	877	15
			Virginia	7,018	6,392	626	16
			Alexandria	12,653	12,031	622	17
			Albert Lea	10,162	9,627	535	18
			Thief River Falls	6,519	6,015	504	19
			Pipestone	4,625	4,163	462	20

*Top cities in job growth require a minimum of 2,000 jobs in 2005 and 2010

**In Greater Minnesota, cities and townships with job growth must have growth within 10 mile buffer to make the list.

Map 1. Map of Top Workforce Housing Communities



This is a fairly significant change from the list of communities identified in the 2013 QAP. Realizing that as job location data improves and the agency's ability to conduct more refined spatial analyses improves, we expect more changes in our analysis in the future. We are fully aware that developers plan projects many months in advance of the QAP being published and that changing the list of communities receiving workforce housing (or top growth) points creates problems if the location of a project is no longer in an area that receives points. Thus, we are testing out the concept of a "change-transition provision" to facilitate planning. The provision would keep communities identified in the previous year's QAP as "workforce housing communities" eligible for workforce housing points for another year. In the 2014 QAP, we propose to identify the new list of communities eligible for workforce housing (the list above and accompanying map) but also keep as eligible the communities listed as top growth communities in the 2013 QAP. If a development is within the new 2014 list or the 2013 list, it will receive points. For the 2015 QAP, we will again develop a new list, and a project will receive points if it is on the 2015 or 2014 lists. Communities in the 2013 list will no longer be eligible for points, unless they are on the 2015 or 2014 lists.

For reference, here is the top growth communities identified in the 2013 QAP. Under the proposed hold change-transition provision, projects in these communities would still be eligible for points under the 2014 QAP.

Table 4: Top Twin Cities 7 County Metro Cities – 2013 QAP

Top 10 Cities - Household Growth	2010 HH	2000 HH	Change	Rank	Top 10 Cities - Job Growth**	2010 Jobs	2000 Jobs
Woodbury (Washington)	22,594	16,676	5,918	1	Maple Grove (Hennepin)	30,030	18,205
Maple Grove (Hennepin)	22,867	17,532	5,335	2	Maplewood (Ramsey)	27,150	18,703
Shakopee (Scott)	12,772	7,540	5,232	3	Eagan (Dakota)	49,316	42,741
Blaine (pr. Anoka)	21,077	15,898	5,179	4	Shakopee (Scott)	18,327	13,903
Lakeville Dakota)	18,683	13,609	5,074	5	Richfield (Hennepin)	15,408	11,565
Forest Lake (Washington)	7,014	2,805	4,209	6	Golden Valley (Hennepin)	33,552	30,074
Plymouth (Hennepin)	28,663	24,820	3,843	7	Woodbury (Washington)	19,260	16,077
Eden Prairie (Hennepin)	23,930	20,457	3,473	8	Lakeville (Dakota)	13,540	10,583
Farmington (Dakota)	7,066	4,169	2,897	9	Mendota Heights (Dakota)	11,360	8,479
Hugo (Washington)	4,990	2,125	2,865	10	Blaine (pr. Anoka)	20,045	17,419

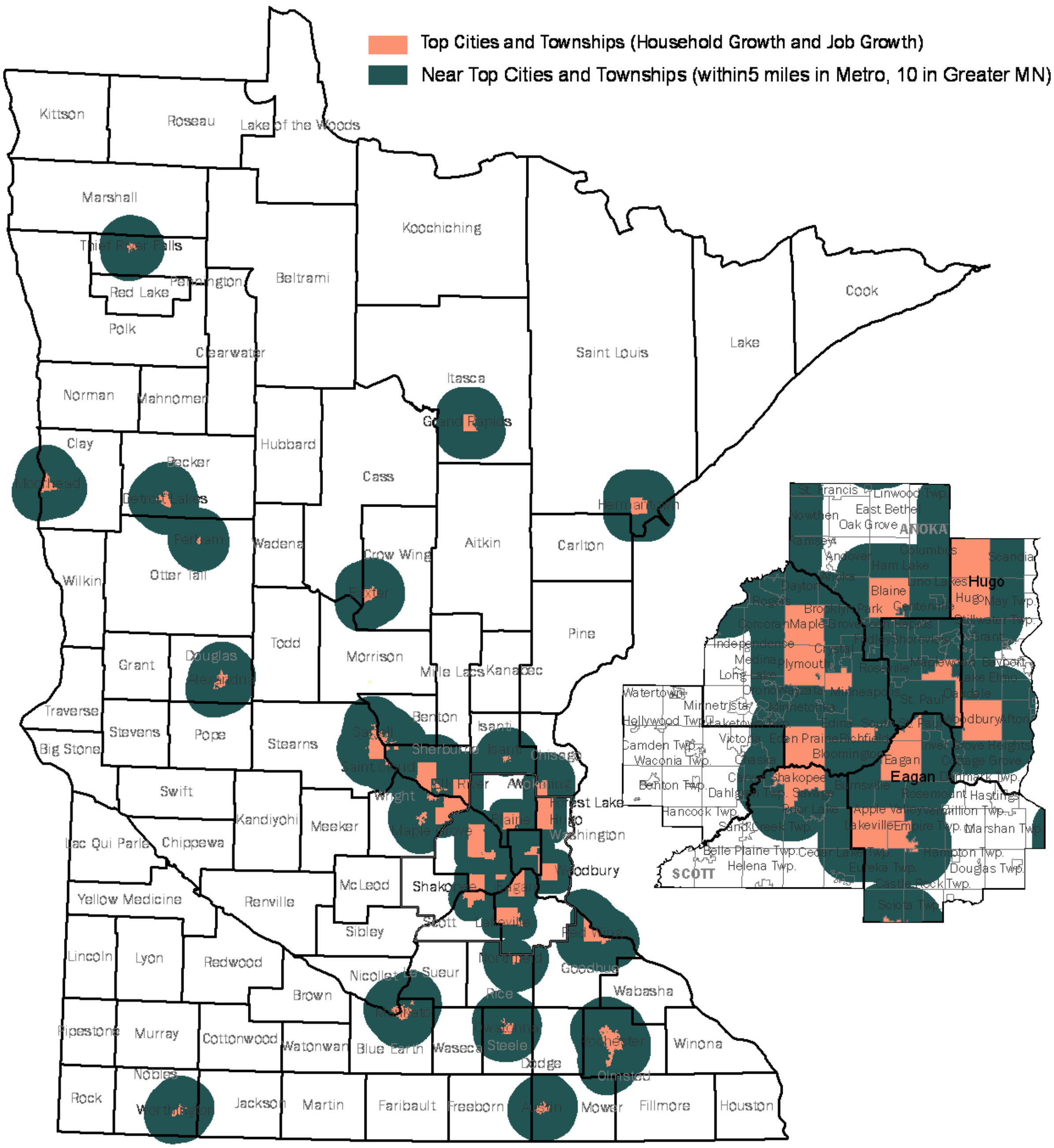
Table 2: Top Greater Minnesota Cities and Townships – 2013 QAP

Top 20 Cities/Townships - Household Growth	2010 HH	2000 HH	Change	Rank	Top 20 Cities/Townships - Job Growth**	2010 Jobs	2000 Jobs
Rochester (Olmsted)	43,025	34,116	8,909	1	Rochester (Olmsted)	81,480	77,835
St. Cloud city (pr. Stearns)	25,439	22,652	2,787	2	Baxter (Crow Wing)	7,079	3,641
Otsego (Wright)	4,736	2,062	2,674	3	Mankato (Blue Earth)	30,719	27,916
Moorhead (Clay)	14,304	11,660	2,644	4	Red Wing (Goodhue)	13,033	10,649
Mankato (pr. Blue Earth)	14,851	12,367	2,484	5	Worthington (Nobles)	8,368	6,172
Sartell (pr. Stearns)	5,859	3,443	2,416	6	Elk River (Sherburne)	10,933	8,864
Elk River (Sherburne)	8,080	5,664	2,416	7	Albertville (Wright)	3,211	1,155
St. Michael (Wright)	5,239	2,926	2,313	8	Sartell (largely Stearns)	4,536	3,049
Buffalo (Wright)	5,699	3,702	1,997	9	Monticello (Wright)	6,990	5,562
Monticello (Wright)	4,693	2,944	1,749	10	North Mankato (Nicollet)	8,653	7,325
Wyoming (Chisago)	2,738	1,023	1,715	11	Hermantown (Saint Louis)	3,632	2,439
Owatonna (Steele)	10,068	8,704	1,364	12	Detroit Lakes (Becker)	8,533	7,597
Becker (Sherburne)	1,496	169	1,327	13	Moorhead (Clay)	14,155	13,333
Big Lake (Sherburne)	3,377	2,117	1,260	14	Buffalo (Wright)	7,289	6,490
Alexandria (Douglas)	5,298	4,047	1,251	15	Saint Michael (Wright)	2,965	2,208
Grand Rapids (Itasca)	4,615	3,446	1,169	16	Perham (Otter Tail)	3,809	3,160
Albertville (Wright)	2,377	1,287	1,090	17	Northfield (Rice)	9,202	8,562
Isanti (Isanti)	1,871	816	1,055	18	Thief River Falls (Pennington)	7,645	7,160
Baxter (Crow Wing)	2,963	1,921	1,042	19	Waite Park (Stearns)	6,727	6,305
Sauk Rapids (Benton)	4,960	3,921	1,039	20	Austin (Mower)	13,538	13,128

*"pr." designates primary county of multicounty cities.

** Cities and townships need at least 2,000 jobs in 2010 to be included in the top growth cities and townships.

MAP 2. Top Growth Communities (with Commute Shed) – 2013 QAP



Please comment on the new workforce housing criteria and methodology and on the “change-transition provision.” Comments must be submitted no later than October 31.