Low Income Housing Tax Credits and Other Background for Resolution No. 13-0566

The Ann Arbor Housing Commission (AAHC) is requesting Council approval to transfer ownership of 26 properties that the City acquired for the AAHC. Twenty parcels are public housing sites, one parcel is a Turnkey III property which is a lease to own program, and five parcels are vacant parcels intended for use as affordable housing.

Housing Commission's Community Role

The Ann Arbor Housing Commission is currently the largest administrator of rent and income-restricted affordable housing units in the City of Ann Arbor and Washtenaw County. The AAHC manages or administers:

- 355 units of public housing in the City limits (and 6 community centers)
- 1333 vouchers and 150 Veteran's vouchers, primarily in Washtenaw County
- 96 units of Shelter Plus Care Vouchers and 34 units of Supportive Housing for 6 nonprofits
- over 200 units of project based rental assistance for Cranbrook Towers

The AAHC intends to use this opportunity to not only rehabilitate and invest in the properties, but to also secure additional funding for services to provide a better living environment for existing tenants and to enable the AAHC to serve high need tenants. The following information shows the demographics of existing tenants in the public housing units.

Female Head of Household	71%
Black	61%
White	37%
Other Minority	2%
Disabled	46%
Income less than $10,000/year	60%
Income $10,000 to $19,999	30%
$20,000 or more	10%
60+ years in age	18%

City Ordinance Creating the Housing Commission

The City created the AAHC in 1965 by City Ordinance 1:209 through state enabling Act 18 of 1933, as amended. Section 3 of the ordinance states that:

> All deeds, mortgages, contracts, leases, purchases, or other agreements regarding real property which is or may be put under the control of the housing commission, including agreements to acquire or dispose of real property, shall be approved and executed in the name of the City of Ann Arbor. The Ann Arbor City Council may, by resolution, decide to convey or assign to the housing commission any rights of the city to a particular property owned by the City of Ann Arbor which is under the control of the housing commission and such resolution shall authorize the City Administrator, Mayor and Clerk to take all action necessary to effect such conveyance or assignment.

The City of Ann Arbor currently holds the deeds to these properties, which are controlled by HUD regulations because HUD provided the funding to acquire and build the properties. It is very unusual for a municipality to own the properties that a Housing Authority manages. The typical structure is that the

Housing Commission owns the properties. The City has the authority under its own ordinance to transfer the deeds to these properties to the AAHC at any time. The AAHC is requesting that the City approve the transfer of these deeds in order to facilitate reinvestment in these properties, which have been underfunded for many years.

HUD Funding

The AAHC is completely dependent on funding from Congress to HUD to maintain the public housing units the City owns. Congress continues to cut funding for public housing which has had a negative impact on the AAHC's ability to take care of these properties, which continue to deteriorate.

There has been no funding for new public housing units since 1986. HUD estimates that they are losing 10,000 – 15,000 units of public housing each year. Some units are being replaced with mixed-income, mixed-finance properties through HOPE VI, but most have been demolished without replacement. The year 1976 was the watermark year for HUD, with the highest funding in its existence at $86.8 billion, and it has decreased since then to a total of $41.7 billion in 2012.

Some HUD programs have received greater support from Congress and HUD than others. There has been a shift in support from public housing to voucher programs. HUD funds several voucher programs, including the Housing Choice Voucher (HCV) program, commonly known as Section 8 vouchers. The HCV program is administered through housing authorities and it enables tenants to take a voucher subsidy to a private landlord so that no matter where the tenant lives the tenant receives a rent subsidy, OR the housing authority can convert HCV vouchers to Project Based Vouchers (PBV) and attach the voucher to a property so that whoever lives in the unit benefits from a rent subsidy. A second voucher program is the Project Based Rental Assistance (PBRA) program which is administered by HUD. Again, the property owners can attach vouchers to a property so that whoever lives in the unit benefits from a rent subsidy. Both voucher and public housing funding are used for rent subsidies (i.e. operations).

Change in How Affordable Housing is Financed (Technical Part)

In addition, the current paradigm to fund the development of new affordable rental housing units is called Low Income Housing Tax Credits (LIHTC), an IRS program established in 1986 that leverages private capital to fund affordable housing. The IRS allocates LIHTC to state housing authorities, like the Michigan State Housing Development Authority (MSHDA). MSHDA issues a competitive application twice a year for private non-profit and for-profit developers to compete for tax credits. If the developer does not need the tax credits for its own business (a non-profit developer for example), then the developer finds an investor or syndicator to purchase the LIHTC so that the investor can receive tax benefits, primarily by receiving tax credits equal to the value of the LIHTC they purchased, over a 10-year period. The investor purchases the tax credits with cash, which is used by the developer to develop the affordable housing. LIHTC typically can provide 50% - 60% of the funding needed to develop the affordable housing. The rest of the funding comes from grants and loans.

The IRS has its own rules and regulations that govern this transaction and one of the requirements is that a single-purpose entity is created to have an ownership interest in the affordable units that are developed (these can be new construction or acquisition and rehabilitation). This single-purpose entity has no other assets and is known as a Limited Dividend Housing Authority Limited Partnership, and it is a partnership between the equity investor (limited equity partner) and the developer (general partner). The limited equity partner stays in the Limited Partnership to protect its interests in the asset so that it can receive tax benefits for the 15 year IRS compliance period. The developer is the general partner that manages the asset. After a 15-year IRS compliance period is over, the equity investor sells its remaining interest in the property to the developer (at a pre-determined value) and the developer becomes the sole owner of the property. LIHTC properties limit the income to 60% of the Area Median Income (AMI) or below. A LIHTC property may or may not also have project-based vouchers or tenant vouchers that subsidize rents (ongoing operations) so that the target population can be even lower than 60% AMI.

The proposed structure for the AAHC tax credit projects is as follows:

1. City transfers ownership of properties to AAHC.
2. AAHC ground leases the properties to the project partnerships for a term (usually over 60 years) as required by the tax credit investor.
3. The ground lease calls for an upfront capital lease payment equal to the appraised value of the structures (the value of the land is not included as it generates no tax credit basis).
4. AAHC provides purchase money loans to the project partnerships in the amount of the capital lease payments, provided that, if there are sources of funds that will allow payments to AAHC for the lease payments, after all project costs and developer fees are made, then the amount of the AAHC purchase money loan is reduced by the amount of the cash payment for the lease payments to be made at closing.
5. In year 15, after the investor leaves the partnership, the lease structure can be collapsed, leaving AAHC as unencumbered owner of the properties.

A long-term ground lease is alternative to transfer of ownership. It is an evolving issue that provided a mechanism for public organizations like a housing commission using Hope VI to be able to develop the properties without transferring ownership. The long-term lease ensures there is no risk of loss of site control.

HUD Encourages Public Housing to Convert to Project-Based Vouchers

HUD recognized that the public housing program has been historically underfunded and proposed a new program called the Rental Assistance Demonstration (RAD) to convert public housing to project-based vouchers to provide a more stable source of rental subsidy and to access funding for capital improvements. HUD will provide new voucher to the AAHC for each unit converted. In addition, public housing is statutorily prohibited from accessing LIHTC, HOME, and other funding sources and therefore this change in structure allows the housing authorities to access funding to reinvest in rehabilitation of their units. HUD's own analysis showed that the capital repair immediate needs in public housing exceeded $25.6 Billion dollars, averaging over $23,000/unit. HUD's 20-year projection of capital repair needs in public housing exceeds $80,000/unit.

The AAHC's consultant conducted a Physical Needs Assessment that showed a need for just over $14.5 million or $40,000/unit in capital repairs over the next 15 years. Most of these buildings were developed 30-40 years ago and are at a point that major reinvestment is needed. If HUD capital funding remained constant based on the capital funding the AAHC received in 2012, the AAHC would only receive $18,000/unit from HUD over the next 15 years to maintain its properties. The AAHC cannot maintain these properties without an increase in funding from HUD OR an annual contribution from the City of Ann Arbor of about $500,000/year OR converting the units to project-based vouchers and accessing private and public funding to redevelop the properties through the RAD program.

The AAHC initially applied to HUD and was approved to convert 282 out of 355 of its units under the RAD program with the intention of eventually converting 100% of the public housing units. The AAHC has been approved by HUD to amend its RAD application to include conversion of 100% of the units in several phases. Each site is going through a financial and physical needs assessment to determine the scope of work and the total development costs in order to secure all of the funding needed to redevelop the properties. The AAHC issued a request for proposal for a developer and development consultant. Norstar Developers, Inc. has been selected as the co-developer and Avalon Housing as well as RECAP Real Estate Advisors have been selected as consultants.

The RAD program allows conversion to project-based vouchers at a fixed rent limit that is initially set at the current total rental payment that the AAHC receives from its tenant rent, operating subsidy, and capital grant. Due to sequestration, HUD has modified the RAD program rules so that Commissions can covert to PBV's at the 2012 pre-sequestration rates, if the conversion occurs in 2013. The chart below shows the initial 2012 RAD rent rates allowed by HUD if the Commission converts in 2013. Under the RAD program HUD committed to increasing the total rent cap each year according to an inflation cost factor and never reducing the rent cap below this initial rent rate. The total rent received for public housing has no such commitment from HUD and it has decreased from one year to the next.

Rent Rates if convert in 2013		
Bedrooms	**AAHC East Side Properties**	**AAHC West Side Properties**
1	$503	$535
2	$654	$660
3	$815	$859
4	$847	$897
5	$1000	$1022

Projected Rent Rates if convert in 2014 (HUD will determine based on sequestration average rents in CY 2013)		
Bedrooms	**AAHC East Side Properties**	**AAHC West Side Properties**
1	$412	$439
2	$536	$541
3	$668	$704
4	$694	$736
5	$820	$838

The AAHC's initial development budget was about $22 million and the final budget to redevelop all of the properties is expected to be close to $48 million. Redevelopment of these properties will increase energy efficiency, air quality, accessibility, and the quality of life for residents. In addition, it will provide for hundreds of jobs to contractors, professionals, and tenants.