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September 8, 2016

Mr. Steve Auger
Executive Director
Florida Housing Finance Corporation

Re: Long Term Affordability: 9% Housing Credits and SAIL

Dear Steve:

I am writing to strongly support the continuation of the 50 year set-aside period for all 9% Housing Credit and SAIL deals. If anything, FHFC should consider giving bonus points to applicants that agree to affordability periods longer than 50 years.

The arguments to reduce the set-aside period to 30 or 35 years are specious, and would serve only to provide tens of millions of dollars of windfall profit to developers in exchange for no public benefit. To be clear: there is no public benefit to the proposed reduction in the affordability period.

Florida Housing's constituents are not the developers, who are only an intermediary in the system. The real constituents are the working families and elderly who inhabit the units. Reducing the long term affordability period will directly and profoundly harm those that FHFC was created to serve.

The following will explain this position in greater detail:

Does the current system work?
Yes. High quality developers are lined up, fighting for Housing Credits and SAIL—with the 50 year set-aside period in place. Why would FHFC reduce the affordability period when there are an excess of quality developers who are willing and able to make their deals work with the 50 year set-aside?

What would happen if the affordability period was reduced from 50 to 30 years?
Many of the newer Housing Credit deals are located in prime market locations, and have market rent appraisals as high as 400% of restricted appraisals (almost all new Housing Credit deals have market rent values at least twice as high as restricted rent values). If the affordability period was reduced, the existing residents, who are the reason these programs exist, would be displaced, and the developer would sell the properties and net a massive profit. The units could not be replaced, because in these prime locations, land will not be available or will be prohibitively costly in 30 years.

Is the request to lower the affordability period prospective, or would it impact existing deals?
At this point, the request appears to be prospective. However, it is difficult to imagine that if developers are successful in convincing FHFC to reduce the affordability for new deals, that they would not then start a push to amend the requirements for existing deals.

How many units would be at risk?
The Shimberg Center can provide exact numbers on the negative impact of reducing the affordability period.

Is the FHFC 50 year requirement an "outlier"?
No. Many states require 50 years, and several require even longer set-asides.

Why doesn't FHFC have larger set-asides for non-profits, as other states do?
FHFC decided many years ago that the "who" was not important—the "what" was delivered to the residents was the key. For-profit or not-for-profit didn't matter, so long as there was long term affordability and other public purpose features (resident programs, energy efficiency, etc.). Developer fees were allowed on the high side, compared to other states, to attract developers willing to deliver the long term affordability and quality product for the residents.

Isn't a compromise in order?
The 50 year affordability period WAS the compromise—between 30 years and perpetuity.

What does the Internal Revenue Code say about this issue?
Section 42(m)(I)(b) of the IRC requires the selection system of each state to reward "projects obligated to serve qualified tenants for the longest periods". It is difficult to understand how this requirement of federal law can be met when FHFC has routinely been massively oversubscribed for Housing Credits while requiring a 50 year affordability period—and then voluntarily reduces that requirement to a shorter period without any evidence that the development community cannot deliver and maintain developments with the 50 year affordability period.

What about federal law and "disparate impact"?
The developments which are most likely to utilize the shortened affordability period to convert to market rate housing—displacing existing residents—are the ones located in better market areas. There will be a disparate impact on protected classes if the affordability period is reduced.

Will Areas of Opportunity impact the disparate impact?
Yes. FHFC is, as a result of the US Supreme Court ruling, strongly incentivizing developers to locate properties in higher-end market areas. Because of this, more and more of the FHFC portfolio will be in locations where the housing cannot be replaced if the affordability period is reduced. Additionally, these areas are where the property value without rent restrictions will increase the likelihood that the developments will be converted to market rate units whenever the affordability period expires. Changing the affordability period to less than 50 years will have a direct disparate impact, and this will be amplified by the Areas of Opportunity targeting.

What is the problem this is supposed to fix?
I'm not really sure. There is only one written comment advocating for this change—and it simply advocates for the change absent any rationale for the policy shift. Some developers have stated that the problem is that deals will not be able to recapitalize, leading to disrepair of the units. Some have said they will take better care of their units if they are able to convert to market rate housing more rapidly. The proposal to reduce the affordability period appears to be a classic "solution" in search of a problem.

As is explained below, the Housing Credit and SAIL deals being done today carry extremely low debt, have high quality construction, and are located in prime areas. These deals should have no problems recapitalizing. As for the argument that a developer would have more incentive to take

care of the property if they had an earlier conversion payday—the owners already have a contractually binding obligation to properly maintain the properties.

Is there any evidence that shows a widespread problem with inability to recapitalize deals?
No. In fact, the opposite is true. For example, the recent successful and lucrative sale of the Wilson portfolio—with the 50 year set-asides intact—shows that the long term affordability is not an impediment to recapitalization. Another recent example, from last month's FHFC Board package, is the Sunset Bay SAIL deal—which recapitalized so successfully that the developer was able to take $7 million cash out of the deal and retain the long term affordability.

What is the key to recapitalization?
The key is the low debt ratio on Housing Credit properties. Many recent deals have debt equal to 30-50% of the restricted value of the property. That limited debt will be paid down to an even lower level over time. When it is time to recapitalize, there will be sufficient restricted value to refinance, recapitalize, and provide needed repairs.

Isn't it just a few Miami-Dade properties that are in this great financial position?
No. Almost all new Housing Credit deals carry extremely low debt.

How much would a developer make if the affordability period was reduced?
A sampling of recent Housing Credit deals in Miami-Dade County show that their restricted value totaled $20.99 million, while their market value was $79.87 million. Reduction of the affordability period would allow the owner to convert to market rate and sell the property at the market value after only 30 years. While Miami-Dade deals have the largest difference between market and restricted value, even deals in poor markets have a market value twice that of the restricted value.

Could an example of a few real deals be shown?
Yes.

Pinnacle Heights is a 105 unit family high-rise in Miami-Dade County. It has a market appraised value of $15.23 million and a restricted appraised value of $5.78 million. It carries only $2.7 million of debt, which is a loan to restricted value of 41.7%. The DSC is a strong 1.65-1.00. The developer fee was $3.8 million, with only 6% deferred. There is no doubt that this deal will be able to easily recapitalize when required. The only results from lowering the affordability period from 50 years would be to displace the residents and provide a $10 million payday for the owner.

Brandon Palms is a 120 unit family mid-rise in Hillsborough County. It has a market appraised value of $11.3 million and a restricted appraised value of $5.02 million. It carries only $2.31 million of hard debt, which is a loan to restricted value of 46.0%. The DSC is a strong 1.84-1.00. The developer fee was $3.2 million, with only 9% deferred. There is no doubt that this deal will be able to easily recapitalize when required. The only results from lowering the affordability period from 50 years would be to displace the residents and provide a $6 million payday for the owner.

Casanas Village is an 88 unit family mid-rise in Leon County. This deal is included in this paper because Leon County is arguably the worst market of any large or medium county. It has a market appraised value of $6.53 million and a restricted appraised value of $3.61 million. It carries only $1.685 million of hard debt, which is a loan to restricted value of 46.7%. The DSC is a strong 1.83-1.00. The developer fee was $2.7 million, with only 10% deferred. Even in a market such as Leon County, there is no doubt that this deal will be able to easily recapitalize when required. The only results from lowering the affordability period from 50 years would be to displace the residents and

provide a $3 million payday for the owner.

Are there some deals that will have trouble recapitalizing?

Yes. However, those deals will tend to be older, bond financed projects with stick/stucco construction, located in less desirable areas. The proposed "solution" of eliminating income restrictions will not help these deals, as the market rate rents on these units will be similar to the restricted rents. Therefore, the proposed solution won't help those they actually need help.

What is the best solution for the deals that need help recapitalizing?

Simply allowing those deals to access FHFC resources would solve the problem. Right now, deals with existing land use restrictions cannot apply for new FHFC resources. Changing this requirement would actually help those who need help, and in a manner that would have minimal negative impact on the residents of the properties. These deals can be dealt with on a case-by-case basis.

Conclusion

Some developers claim that the 50 years does not work. At the same time, they spend massive amounts of money hiring lobbyists, consultants, and attorneys to compete for the tax credits and SAIL—with the 50 year affordability requirement in place. If a developer truly believes that 50 years does not work, they should move aside and let the rest of the line running down the block—that are all willing and able to provide 50 years of affordability—have the credits and SAIL.

I do not believe this is an issue with a good argument on both sides. But if you have doubts on the issue, FHFC should always err on the side of its constituents, the working families and elderly renters that you exist to serve. FHFC can always help an individual development in need—but if you give away 20 years of affordability across the board, you will never get it back.

Sincerely,

Mark Hendrickson

cc: