RURAL NEIGHBORHOODS

Building Livable Places for Working Families
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August 21st, 2018

Mr. Harold L. "Trey" Price
Executive Director
Florida Housing Finance Corporation
227 N. Bronough Street, Suite 5000
Tallahassee, FL 32301

Re: RFA 2018-111 Housing Credit Financing for Affordable Housing Developments Located in Miami-Dade County

Dear Mr. Price et al:

Rural Neighborhoods [RN] is pleased to comment on Florida Housing Finance Corporation's "*Non-Profit Goal*" in RFA 2018-111 Housing Credit Financing for Affordable Housing Developments Located in Miami Dade County. It asks that these comments be extended to all pending RFA's in which FHFC seeks to establish a similar non-profit goal.

Florida Housing Finance Corporation's [FHFC] express intent in the selection process is to select an application for funding that qualifies as the highest-ranking eligible application wherein the applicant applied and qualified as a non-profit applicant. The rationale is simple: IRC §42(h)(5) requires that a portion of each state's annual credit ceiling be set aside for allocation to projects involving qualified non-profit organizations. Specifically, not less than 10% of the state's allocable credit must be set-aside for a non-profit pool. In addition, Section II.F of the 2018 QAP allocates 15% of its housing credit authority to non-profit applicants. RN argues such a preference contributes toward other public policy objectives that enhance meeting Florida's housing needs. Evidence suggests non-profit developers often target harder-to-serve populations ranging from farmworkers to the homeless to the disabled and locate projects in neighborhoods to promote economic revitalization. The set-aside also builds significant real estate development, property and asset management capacities among organizations with housing and community development as their principal charitable mission.

Rural Neighborhoods, however, believes the listed conditions to be qualified as a non-profit applicant are inadequate and requests substantive changes in RFA 2018-111 and others establishing non-profit goals. It requests FHFC:

Either:

- Limit qualified non-profit applicants to those partnerships or LLCs in which the non-profit(s) owns 100 percent of the ownership interest held by the general partner or managing member entity, or
- Entities having a structure as defined above be prioritized over those in which the non-profit holds less than 100 percent but more than 51 percent ownership interest.

In addition:

- Economic benefits shall be commensurate with the nonprofit ownership interest, e.g. 51 percent ownership shall result in 51% of the Developer Fee, and cash flow and residual net sales proceeds allowable to the general partner/managing member should be realized by the non-profit; and
- Developer Fee shall be paid pro rate between the for-profit and non-profit developer prohibiting the for-profit from collecting its portion of the fee before the non-profit.

RN argues revised requirements such as the above substantively addresse the shortfalls, criticisms and concerns it expresses below.

FHFC Failure to Ensure Material Participation. The non-profit pool is a requirement placed upon FHFC by the IRS and is only satisfied when the allocating agency determines in good faith that a project will satisfy the requirements of IRC §42(h)(5) *throughout* the compliance period. RN believes FHFC's past and current administration of IRC §42(h)(5) fails the good-faith test.

First, FHFC's approach continues to count so-called *"joint ventures"* by and between for-profit and non-profit Developers toward the non-profit goal. From time to time FHFC has taken minor steps to amend its RFA requirements for the non-profit pool: it requires applicants to answer no more than the most rudimentary questions, and it has increased no more than a single economic benefit, e.g. the percentage of Developer Fee, to 25%. For example, the current proposed rule requires the applicant to submit:

(a) The IRS determination letter;

(b) A description/explanation of how the Non-Profit entity is substantially and materially participating in the management and operation of the Development (i.e., the role of the Non-Profit);

(c) The names and addresses of the members of the governing board of the Non-Profit entity; and

(d) The articles of incorporation demonstrating that one of the purposes of the Non-Profit entity is to foster low-income housing.

If the Applicant applies as a Non-Profit entity and meets the requirements outlined above to be considered a Non-Profit for purposes of this RFA, it must remain a Non-Profit entity and the Non-Profit entity must (i) receive at least 25 percent of the Developer's fee; and (ii) contractually ensure that it substantially and materially participates in the management and operation of the Development throughout the Compliance Period.

In addition, Rule 67-48.0075, F.A.C. requires the non-profit to own at least 51 percent of the ownership interest held by the general partner or managing member entity. This constitutes the false appearance of *"majority"* ownership; however, the requirement fails to similarly divide economic benefits or insure a non-profit contributes to or controls the project in any substantive way.

RN believes the above actions are inadequate, subject to widespread abuse and place FHFC at significant risk of failing the good-faith requirement to allocate housing credits to the non-profit sector. In failing to meet IRC §42(h)(5), this arguably places the LIHTC program in its entirety at grave risk.

First, FHFC has a duty to assure a project satisfies the non-profit requirement throughout the *compliance period.* There is scant evidence FHFC performs any due diligence in monitoring/auditing non-profit participation in these pool deals subsequent to credit underwriting review and board approval. The apparent standard seems to be no more than a non-profit corporation remain in the ownership structure – be it the original participant or a charitable replacement. RN believes FHFC's approach is deficient. IRC §42(h)(5) requires that the qualified non-profit organization *"materially participates"* in both the development and operation of the project throughout the compliance period. The IRS LIHTC Audit Technique Guide, for example, provides guidelines to help define material participation:

- *Material participation is most likely to be established in an activity that constitutes the principal business/activity of the taxpayer.*

  [Comment: FHFC requires no more than low-income housing be mentioned in the non-profit applicant's mission as a purpose].

- *Involvement in the actual operations of the activity should occur. That is, the services provided must be integral to the operations of the activity. Simply consenting to someone else's decisions or period consultation with respect to general management decisions is not sufficient.*

  [Comment: RN believes from its review of several co-development agreements that for-profit partners often require the non-profit to consent in advance to most significant development and operational decisions including selection of the for-profit's related construction of property management firm.]

- *Participation must be maintained through the year. Periodic consultation is not enough.*

  [Comment: The available anecdotal evidence suggests non-profit participation is limited in both the development, construction and operational periods and tails off appreciably as the compliance period ensues.]

- *Regular on-site presence at operations is indicative of material participation.*

  [Comment: Few nonprofit partners indicate on-site participation in asset and property management.]

- *Providing services as an independent contractor is not sufficient.*

  [Comment: Non-profit partners often are expected to provide case management and wrap-around supportive services. Such services are most often paid for by contracts from third-parties, particularly governmental sources, and are often not project-specific suggesting services are provided as an independent contractor.]

In summary, a non-profit materially participates where it is regularly, continuously and substantially involved in the development and operations of a rental housing project. RN believes FHFC's rules have resulted in few past for-profit/non-profit joint ventures that meet such a standard.

Nonetheless, some do -- as perhaps best represented by certain projects involving Carrfour Supportive Housing and Rural Neighborhoods. In these instances, co-development agreements go far beyond the FHFC rules and preserve requirements advocated by RN. Unfortunately, the common sharing ratio in FHFC non-profit pool projects is a co-development agreement is which Developer Fees are split 75:25. Few, if any, establish the non-profit partner or member as the managing member or partner; provide the non-profit significant decision-making in project design, income targeting, general contractor selection, property management or marketing; or call for the withdrawal of the for-profit partner. Indeed, as noted in the comments above, for-profit partners retain nearly all such decisions in many, if not most, co-development agreements.

There is even not even any assurance the non-profit partner retains a non-profit right of first refusal sanctioned by IRC §42 or benefit from sale proceeds or cash flow from operations in percentages related to their ownership interest.

RN's concern is that FHFC does little to review or regulate co-development agreements nor has a mechanism to determine if there is any material involvement by the non-profit throughout the compliance period (let alone one that is regular, continuous or substantial). Rule revisions that limit qualified non-profit applicants to partnerships or LLCs in which the non-profit owns 100 percent of the ownership interest would help FHFC both ensure material participation and achieve a new standard of excellence in satisfying IRC §42(h)(5).

Past Arguments. Discussions on changes to the non-profit pool lead to several common, fabricated arguments to preserve the status quo:

- *Insufficient numbers of capable non-profit developers exist to carry out FHFC's 10% set-aside requirements.*

  Non-profit Developers in adequate numbers with strong capabilities do exist to meet FHFC's pool requirements, and this number will grow as the rule is amended. It is the scarcity of non-profit projects set-aside by FHFC and the inadequate accompanying rules that stymies greater non-profit participation. First, there are capable non-profit Developers situated throughout Florida including Carrfour Supportive Housing, Opa-Locka Community Development Corporation, New Urban Development and Rural Neighborhoods in Greater Miami alone. Scores of national and regional non-profit Developers have forsaken competing in Florida given their perception that the current non-profit pool is a fiction. Large non-profit Developers such as Community Housing Partners, Preservation of Affordable Housing have succeeded in the past and still maintain a current footprint in Florida but are foiled by for-profit dominance in the non-profit pool. For them, in the absence of substantial change, there is little reason to invest risk capital here. RN's proposed rule changes will increase the number of non-profit applicants.

- *Joint ventures enable non-profit organizations to bring affordable housing developments to their target population or geographic area of interest through recruitment of for-profit partners.*

  If only it were so. FHFC's most recent RFA 2017-112 in Miami-Dade received a total of 29 LIHTC applications; twenty of these applications qualified as non-profit applicants – nearly 70% of all applications. RN's review shows just two applications (10%) of the non-profit applications were from non-profits in which the non-profit was the sole Developer. More in-depth analysis shows the YWCA to be the sole non-profit applicant holding prior site control and who competitively solicited a potential for-profit partner to bring housing to its constituents and target neighborhood. RN is troubled that the

remainder appear to be no more than convenient partnerships that enable the for-profit partner to participate in the non-profit goal.

RFA 2017-112 stated goals included one non-profit set-aside and two Geographic Areas of Opportunity/HUD SDDA projects. Is it a coincidence that only 1 of 7 projects in the GAO/HUD SDDA goal included a non-profit co-developer where there was no competitive advantage to include one? RN thinks not. For profit developers in multiple RFAs make it common practice to partner with non-profits only for the sake of (qualifying for the non-profit goal. In the absence of a non-profit goal, joint ventures are few and far between.

- *For-profit/non-profit co-development enables inexperienced charitable organization to gain expertise and experience;*

It is true many non-profit organizations do not have the requisite real estate development experience to go it alone and may need to partner with someone that does. Nonetheless, there are qualified and experienced non-profit Developers that inexperienced non-profits could call upon to partner. In addition, there are national housing organizations including NeighborWorks America, Enterprise Community Partners and the Local Initiative Support Corporation that are available to provide seed capital, predevelopment loans, technical assistance and purchase credits. Surely there may also be well-qualified for-profit Developers that can help build the skills of non-profits. But the assumption commonly argued is that for-profit Developers are the preferred or sole source of skill-building expertise. Such reasoning is unfounded and belied by recent legal events that have bedeviled the for-profit tax credit community.

Rural Neighborhoods believes RFA 2018-111 offers FHFC a unique opportunity to better exercise its responsibilities under IRC §42(h)(5) before greater scrutiny is placed on how well it fulfills its responsibilities in meeting the non-profit pool. Be it limiting qualified non-profit applicants to those with 100% non-profit ownership; prioritizing their selection; requiring participation in the Developer Fee, cash flow and sales proceeds proportionate to its percentage ownership; or taking more detailed substantive steps to maximize material participation, Rural Neighborhoods and other non-profit Developers urges FHFC to act.

I remain available to discuss means and methods to accomplish this goal. Please do not hesitate to call me at 305-242-2142.

Sincerely,

Steven Kirk
President