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Ms. Josie Kotsioris,

Thank you for the opportunity to provide comments on the draft 2022 Qualified Allocation Plan (QAP). The following written comments supplement and expand on the comments delivered at the QAP Public Hearing on August 25, 2021.

Total Development Costs

We greatly appreciate the ability to request an exception to the total development costs (TDC). This exception is an important tool which will allow developers to continue providing high-quality, affordable rental housing throughout Tennessee. As Tennessee Housing Development Agency (THDA) is well aware, costs for labor and materials have been increasing and Covid-19 accelerated that trend. While there has been some stabilization in some commodity pricing, the building supply chain is still stretched very thin. There has also been a dramatic run-up in the cost of land and building acquisitions this year which will likely continue into 2022.

The draft 2022 QAP notably does not include changes to the total development cost (TDC) limits. It has been THDA's practice to adjust TDC limits based on construction costs annually and we hope that THDA will do so again in the final 2022 QAP. We suggest THDA consider some combination of the following strategies:

- Increase the TDC limits across the board by 10 – 20 percent. At a minimum we recommend raising costs in the urban category to reflect the additional costs that are playing out most dramatically in the growth areas prioritized under the new project location score.
- Retain the current limits in the QAP but exempt land costs, building acquisition costs and site improvements from TDC calculation. These costs are variable and largely driven by project location.
- Alternatively, THDA could rely on the U.S. Department of Housing and Urban Development's (HUD) mortgageable cost limits for the Section 221(d)(4) program calculated pursuant to the practices and limits cited in the Federal Housing Administration's (FHA) Multifamily Accelerated Processing (MAP) Guide 8.10.A.1c. This has several advantages – it becomes an evergreen item in the QAP that does not need to be updated when HUD adjusts its limits (typically annually). HUD's limits, in conjunction with its cost adjustment factors, also delineate numerous factors including geography, bedroom

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numbers, construction type (elevator vs. non-elevator buildings) and other relevant factors. It should be noted that HUD's mortgageable cost limits are applied only to mortgage proceeds (not development cost) and do not consider equity (Low Income Housing Tax Credit (LIHTC) or traditional). We believe that it is appropriate for THDA to set limits on the amount of cost that can be paid by LIHTC proceeds (and that HUD's mortgageable limits by construction type and geography are a reasonable standard) but these limits should not be the boundaries of a cap on total outlay of cost. Costs more than this limit that are paid for by other sources (i.e., debt and gap-funding) should be permissible.

- In addition to altering the TDC limits, we recommend THDA also raise rehabilitation hard costs per unit in table 14-7 across all categories to align with rising construction costs.

We urge THDA to continue to revisit TDC limits more frequently until the current construction crisis resolves itself. It does not seem unreasonable, given the current market conditions, for THDA to update TDC limits quarterly. An increase was overdue before COVID and the run-up in construction costs, and is now all the more necessary. A front-end increase would decrease the likelihood that the exceptions and other extraordinary back end mitigating measures that THDA is currently taking will be less likely in the future.

Project Location Score

The proposed transition for project location scores from counties to census tracts is a major shift in allocation policy. We recognize that the proposed changes will likely achieve THDA's desire to diversify the number of jurisdictions that can compete for an allocation in the nine percent LIHTC new construction pool. The methodology THDA has developed will also encourage development in higher opportunity areas, which is a desirable public policy outcome for affordable housing residents.

There are several potential implementation issues with the proposed changes that give many of our members cause for concern. THDA must recognize that there will be significant cost implications for this change – this is a navigable issue if THDA adopts additional supporting policy changes. There are only so many developable sites in any given census tract and only a limited number of census tracts that will be able to effectively compete for allocation. Many of the highest scoring sites are in qualified census tracts, which by their nature have higher development costs that have been acknowledged by the federal government with a 130 percent basis boost. We are also concerned that this could drive up the cost of land in these jurisdictions, which likely already have higher than average land costs (given the desirable qualities of the census tract that leads them to have high scores). These are not necessarily insurmountable issues for projects seeking nine percent allocations, particularly if THDA addresses our concerns in the previous section regarding total development costs.

We are very concerned that if this methodology is used in the bond program, it will make new construction bond deals financially infeasible, particularly in Davidson County and middle Tennessee. Furthermore, there are many four percent developments in our members' pipelines that were unable to

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acquire volume cap this year due to the scarcity of resources that will be negatively impacted and may face minimum score threshold issues next year as a result. Millions of dollars have been spent on pre-development activities like site acquisition and control, all based on county needs scores and the relative certainty of execution that the bond program provides. Should THDA move forward with implementing this change, we humbly request that it only be implemented in the nine percent program in 2022 and 2023 and that THDA retain the current Housing Credit Development Location scoring in Section 20 for projects financed using tax-exempt bonds. This will give THDA the opportunity to evaluate the methodology in practice and give the development community the opportunity to build the methodology change into future development pipelines.

New Construction in QCTs

The Tennessee Developers Council applauds THDA's decision to permit new construction housing in Qualified Census Tract (QCT) in the draft QAP, thank you! However, we believe the requirement that the site must be wholly within a Concerted Community Revitalization Plan (CRP) is too onerous and may harm smaller communities that would be best served by the provision. CRPs require legislation and funding from local government, which can take years to accomplish. Many smaller communities that might support affordable housing and benefit from this provision do not have the resources to develop a CRP. Other communities have community revitalization plans that do not meet the formal threshold of a CRP, developments in those areas should be eligible. We also point out that this requirement may create a new avenue for NIMBYs to quash the development of affordable housing; all they would need to do is not adopt a CRP and no new affordable housing could be built in the census tract.

There are several policy solutions that THDA could implement to address these concerns while achieving its public policy goals. One potential solution is to change the language in sections 11 and 20 to prohibit development in QCTs if it conflicts with a CRP. Furthermore, THDA could seek additional comfort by requiring developers to submit an analysis for proposed new construction projects that are not located in a CRP to demonstrate the proposed project's overall potential impact on concentration of poverty within the census tract. This could potentially be part of the market study requirement or a separate third-party report with threshold standards established by THDA in an application addendum.[1]

Letters of Intent & Tie Breaker

We disagree with points being awarded for, and the tie breaker being based on, the Letters of Intent in Section 14.A.11. Rational developers will attempt to secure eight points to maximize their points, despite extraneous sources not being necessary to finance deals. This will add costly and avoidable transaction expenses and could drive up the cost of developing affordable housing in the long term.

[1] Tennessee Developers Council's affiliate, the National Council of Housing Market Analysts (NCHMA), is developing potential methodologies THDA could consider, which will be submitted under a separate cover.

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Financial Feasibility Threshold Requirement

The proposed change to limit deferred developer fee sources to the developer fee amount earned during the construction period takes a valuable funding source off the table. Deferred developer fee generates basis, which in turn generates federal four percent credits which can be used to make deals financially feasible. In absence of the additional equity from the deferred basis, developers would need to use other sources. However, Tennessee does not have its own state LIHTC or significant gap funding. Arbitrarily restricting the near limitless federal four percent credits creates gaping holes in projects and developers are provided with no solution on how to finance them.

Likewise, we suggest that THDA not remove the ability to make owner contributions to support developments (outside of deferred developer fee). This is a common tool used in many affordable housing transactions including:

- public housing Rental Assistance Demonstration (RAD) conversions,
- non-profit transactions utilizing organization profits or fundraising as a source,
- mixed-income and mixed-use transactions to support market rate and commercial portions of the project (particularly, but not exclusively, when condominium structures are utilized), and
- historic tax credit transactions where owner equity is required to comply with tax requirements set out in the *Historic Boardwalk Hall, LLC v. Commissioner* decision.

We also observe that investors and syndicators provide an additional layer of comfort in their underwriting of transactions. Investors require paid developer fees and construction contingencies to be sufficient to address potential issues that may arise during construction. They also conduct extensive underwriting as part of their tax analysis to ensure that deferred developer fees are sized appropriately so that there is a reasonable certainty that they will be paid through operations during the first ten years of operations.

Zoning Letter Threshold

Zoning is a critical aspect of ensuring a project is ready to proceed – that being said, we do not believe that requiring a written letter from the local government zoning agency is the appropriate standard for demonstration of readiness to proceed. There are many jurisdictions across the state that simply refuse to provide a zoning letter. Historically, THDA has allowed either a written letter demonstrating zoning or an analysis that no such regulation exists that prevents development at the proposed site. In fact, this is process is articulated elsewhere in the QAP in the definitions section. We suggest that this threshold be amended to allow for a zoning letter or positive proof that the proposed project conforms with current zoning.

Average Income

Given the current draft of Internal Revenue Service (IRS) regulations regarding the average income election, we understand THDA's reticence to incentivize developers to select this permanent election.

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The benefits of mixed-income communities are well documented, and we believe THDA should do everything in its power to encourage their development.[2,3,4] The average income election is a particularly important tool in the deconcentration of poverty in QCTs. As it stands, most of our members are not comfortable pursuing average income election until the IRS promulgates final regulations. However, we anticipate the IRS will be issuing final regulations, perhaps as early as this fall, that will address the industry's concerns in the draft regulations. Compliance challenges THDA may be concerned about under the current regime are unlikely to be an issue in the future: if the current regulations are made final, there will be little to no market demand to make the election. In the absence of final regulations, we suggest that THDA retain the current points available. Preventing developers from receiving those points will force an irrevocable election of 20 at 50 or 40 at 60 and leave them with no option to change should the circumstances change.

Developer or Related Parties Limits

We understand and see the value in what THDA is trying to do by restricting a developer's ability to apply for new credits if they have two or more pre-2022 deals still open. However, with COVID and HUD financing we believe this test should be more lenient, at least for this year's QAP. HUD financing is notoriously slow and COVID has caused delays for even the most well-prepared developers. We propose changing pre-2022 to pre-2021 and/or changing two to three.

Recapitalization Waiver Points

We do not support the proposed changes to adjust the points for extended recapitalization waivers in Section 14 Part A(13) of the draft QAP. We understand the desire to not use scarce resources on recapitalizations too soon in the life cycle of an affordable housing project, but we think creating an incentive to push out recapitalization to 30 years will have significant affordability opt-out implications and likely result in adverse physical conditions issues. There are so many variables at play that could impact the resource environment or a property's physical needs (e.g., extreme weather events and inflation), that we think it is more responsible to review the portfolio's needs annually and address priorities on which properties are eligible to recapitalize in the current QAP. We recommend retaining the recapitalization waiver language as it stands in the 2021 QAP.

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[2] Raj Chetty et. al. The Effects of Exposure to Better Neighborhoods on Children: New Evidence from the Moving to Opportunity Experiment. 2016. American Economic Review. 106(4): 855-902. Retrieved from: https://scholar.harvard.edu/files/ lkatz/files/chk_aer_mto_0416.pdf.

[3] Robert Collinson and Jens Ludwig. Neighborhoods and Opportunity in America. September 19, 2019. The Brookings Institution. Retrieved from: https://www.brookings.edu/research/neighborhoods-matter-for-opportunity-time-for-more-placeconscious-policy/.

[4] Raj Chetty and Nathaniel Hendren. The Impacts of Neighborhoods on Intergenerational Mobility I: Childhood Exposure Effects. 2018. Quarterly Journal of Economics 133(3): 1107-1162.

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Other Items

Consultants offer valuable outside expertise and should be properly remunerated. Adding the consulting fees to the maximum allowable developer fee will cause developers to spend less on consultants or not hire consultants at all. The aforementioned changes to the developer fee to not allow deferred developer fee beyond what is earned during construction compounds this problem. Consultants help make complicated funding streams available to developers, which adds value for residents and communities. Relocation consultants, especially, should not be paid out of developer fee; moving existing tenants to accommodate construction should be considered a construction cost, not a fee the developer must bear.

There are instances in which scattered sites, as well as properties proposing a combination of new and existing housing, make good sense. RAD projects as well as Choice Neighborhood projects come to mind as easy examples, but there are many others. A blanket prohibition on these types of deals will, once again, take a valuable option off the table, thereby making it significantly harder to develop and finance affordable housing. We understand the rarity and logistical challenges of these types of deals, but nonetheless believe the benefits to tenants and communities outweigh the costs.

We appreciate the opportunity to comment on these proposed changes and look forward to further engagement as the 2022 QAP revision process takes place. As always, please don't hesitate to reach out with any questions or concerns.

Sincerely,

Thom Amdur
President

cc: Ralph Perrey
Felita Givens
Ed Yandell
Don Watt