Technical Recommendations for California Debt Limit Allocation Committee (CDLAC) Regulations

These technical recommendations are intended as a supplement to the letter from Secretary Castro Ramírez on November 10, 2021, highlighting Administration priorities. Those priorities for housing investments include:

1. Creating more affordable housing, with deep affordability, while continuing to emphasize cost efficiency.
2. Preventing and ending homelessness, through the production of housing, including supportive housing, for individuals experiencing homelessness.
3. Affirmatively furthering fair housing choice.
4. Aligning policy and funding cycles across State housing finance agencies.
5. Reducing barriers for new and historically excluded developers.
6. Encouraging location- and climate-efficient site selection.

The full range of available policy tools and levers built into the CDLAC system, including points, pools/set-asides, and reversions/carryforwards should be utilized to advance State policy goals. These elements of the CDLAC system are interdependent. Finalizing a Public Benefits Tie-Breaker is the priority for immediate attention at the meeting on November 17, 2021, due to CDLAC regulation section 5231(g)(3), which requires CDLAC to implement a tie-breaker that measures state investment relative to public benefit. Understandably, committee and public discussion of CDLAC regulations must be phased in order to be manageable. Thus, the Administration recommends a subsequent meeting to for pools, set-asides, reversions, carryforwards and remainders. This memo addresses tie-breaker and point category recommendations only. Once this meeting date is set, the Administration will follow up with a subsequent memo.

Thank you for your team's work on these important issues and your consideration of the recommendations within.

Tie-Breaker Recommendations

Tie-breaker recommendations are based upon the CDLAC Committee discussion on November 10, 2021, and the Working Group tie-breaker proposal; these will be the basis for the final tie-breaker methodology adopted by CDLAC. As discussed, four types of public benefits must be weighted and balanced against one another: Production Benefits, Population Benefits, Rent Savings Benefits, and Location Benefits. Tallied total benefits offered by the project are then compared to the total State investment required in an effort to maximize cost-efficiency. We request that the Controller's Office and Working Group tie-breaker methodology be adopted with weighting and metrics for the following outcomes. Suggested strategies to obtain these results follow:

- Consistent prioritization of deep affordability
- Equitable geographic distribution of funds
- Enhanced emphasis on location-efficiency
- Streamlined development timeline

1. For a period of one year, subject to renewal, include four benefit categories in the Location Benefits tie-breaker category: (1) Highest Resource Area, (2) High Resource Area, (3) Moderate Resource Area, and (4) Transit Oriented Development. The unique tie-breaker benefits to projects located in either Highest or High Resource Areas would "turn off" after 50% of the annual volume cap designated for multifamily housing is allocated to these projects.

   We suggest that maximum Transit Oriented Development (TOD) tie-breaker advantage be earned with a higher standard than maximum amenity points. For instance, tie-breaker TOD benefit could be earned by having received an award under the AHSC, TOD, IIG or TCC programs. These programs ensure developments attain climate goals and the programs also build-in geographic diversity.

   As an alternative to offering tie-breaker benefits to climate program awardees, maximum TOD tie-breaker advantage might be earned with one or both of the following TOD metrics: (1) ¼ mile walkable proximity to transit with 30-minute headways, rather than 1/3 of a mile. (2) ½ mile walkable proximity to transit with 15-minute headways.

   <u>Rationale:</u> The combination of Location Benefits suggested would add nuance to point scores. It would maintain priorities for High/Highest Resource Areas, while recognizing the value of investments in Moderate Opportunity designations, especially when coupled with excellent transit access. It would also strengthen climate goals. For instance, a High Resource Area location with excellent transit access would be prioritized over another High Resource Area site with poor transit that is otherwise equivalent.

   <u>NOTE:</u> Location benefits in the tie-breaker should not overshadow depth of affordability or homeless priorities, particularly in the near-term. The Administration is actively analyzing best ways of identifying location-efficient sites and at that time it might be appropriate to increase weight of this tiebreaker category and/or add a point (perhaps with soft-cap) for location-efficient sites. Adding points or partial points for TOD at this time would become, by default, a threshold requirement for bond allocation in 2022 and could have undesirable geographic equity impacts.

2. Calculate Rent Savings Benefit over a 30-year term and implement solutions for geographic inequities resulting from the use of Fair Market Rent (FMR) in the benefit calculation. Preliminary modeling results suggest we can achieve geographic equity across all pools and set-asides by (1) revising geographic allocation maps to group like-counties and (2) applying the statewide basis delta adjuster in the denominator of the Tie-Breaker at a 25% or 50% weight. Further modeling should refine or confirm this methodology.

   Rationale: Rent Savings benefit appropriately values deeper affordability, but the current calculations are resulting in undue advantages for places with a high FMR, particularly when bond and state credit request in the denominator is adjusted downward using the statewide basis delta adjuster. We encourage CDLAC to ensure projects with deep affordability are tie-breaker winners, including in both regional and non-regional pools. This can be most effectively achieved by grouping high-FMR counties with other high-FMR counties, low-FMR counties with low-FMR counties, and by separating the City and County of San Francisco from the Bay Area pool.

3. Create a "cap" and a "floor" on affordability levels for the purpose of calculating Production Benefit and Rent Savings Benefit. Thus, maximum Rent Savings Benefits would be achieved at a project-wide average affordability of 30% or 40% AMI. A cap could balance this floor- neither production benefit nor rent-savings benefit should be awarded for units serving households over 80% AMI.

   Rationale: Rental units priced above 80% AMI are at or above market-rate pricing in much of the state. While we must increase production at these levels through reduced regulation and pro-housing incentives, the scarce resource of bonds should be reserved for below-market-rate units. We should also create a floor on Rent Savings benefits to ensure that projects are not driven to build deeply affordable housing without the operating subsidies needed for long-term financial sustainability and quality.

4. The Population Benefits Category should include chronically homeless, homeless, and disabled/special needs units only.

   Rationale: The Population Benefits Category should be limited to populations that are higher-cost to house and support. Conversely, many other important target populations, such as seniors, farmworkers, and veterans, while critically important as state priorities, should be removed from this category to remove undue advantage. While we fully support the Treasurer's policy priority on funding senior housing, senior buildings tend to be faster and less costly to build, partly due to NIMBY advocacy, thus they do not require a tie-breaker advantage to be successful in the competition. Similarly, other target population types can and should remain equally competitive, but since they do not add cost to the project, they do not require favorable weighting in this part of the tie-breaker.

5. The denominator of the Tie-Breaker should be limited to solely Tax Exempt Bonds or, alternately, to only Tax Exempt Bonds and State Tax Credits.

   Rationale: State bonds are currently the most restricted funding source that is critical for many affordable housing developments. Over time, both state agencies and local funders are adapting to this new shortage of bond debt with alternate financing pathways. Federal legislation may also relieve this shortage affecting the 4% pipeline. In the meantime, we must ensure a streamlined development pathway for projects already in the pipeline and already identified as state and local priorities. We will work with CDLAC to monitor for when to add other state funds and local funds to the denominator for maximizing cost-efficiency across all public sources.

NOTE: Above recommendation could move to Short-Term if a 1-year timeline for re-examining the tie-breaker denominator is desired.

Point Category Recommendations

The Administration strongly supports the emphasis and priority on Affirmatively Furthering Fair Housing (AFFH) in the current CDLAC point categories and are pleased to see that the additional location-based preference for High and Highest Opportunity Areas is already changing investment patterns. As discussed, the unique advantage of the additional point to projects located in High and Highest Opportunity Areas have been borne out in the data. To mitigate concerns of the additional point, we suggest the following adjustments to this particular point category:

1. For a period of 1 year, subject to renewal, the additional point available only to projects located in High/Highest Resource Areas will "turn off" after 50% of the annual [or per-round] bond volume cap designated for multifamily housing is allocated to these projects. The soft-cap strategy should be implemented with a priority for geographic distribution of High/Highest Resource Area awards. Again, the soft cap allows for flexibility for specific projects and allows for the Committee to make decisions on such projects.

   Rationale: Continue to rebalance our Statewide portfolio of affordable housing by making substantial investment in High and Highest Opportunity Areas, while also ensuring that all communities can benefit from affordable housing investments. This will also reduce over-correction of developer pipeline investment.

2. High/Highest Resource Area projects must earn a minimum threshold of site amenity points to be determined by the committee.

   Rationale: Site amenity points measure quality-of-life necessities and conveniences for residents that are not captured by the Opportunity Indicators. Some of these necessities are particularly important for individuals without cars, who are likely to be housed in permanent supportive housing. However, in order to not excessively limit the number of viable High and Highest Opportunity sites, we recommend a lower threshold of site amenity points. For instance, High/Highest Opportunity applicants could receive a bonus of three site amenity points or be required to earn seven out of ten amenity points.

3. High/Highest Resource Area points will be made available to the following project-types and construction types:

   New Construction
   - Large Family, Special Needs, SRO

   Acquisition-Rehabilitation
   - Other Rehabilitation Project

   Rationale: We must continue to rebalance the portfolio for all target populations and avoid further concentration of low-income singles, special needs populations, individuals experiencing homelessness, and youth. We recommend expanding the types of projects incentivized to locate in high/highest resource areas. Only two types of applicants would be ineligible for AFFH High/Highest Opportunity Area points: Preservation projects and Senior projects. Unfortunately, due to NIMBY opposition, Senior projects tend to be those easiest to build in high opportunity locations. Allowing Senior projects to access High/Highest Opportunity Area points could reinforce the pattern of senior-only affordable housing in more exclusive neighborhoods. Existing affordable housing is largely located in low resource and high poverty areas. If the state de-prioritized rehabilitation of these buildings by virtue of their location, it would repeat disinvestment patterns that have been so detrimental to disadvantaged communities.

4. The 9-point AFFH category should be simplified to apply to any project with public funds of at least $1 million committed on or before 6/30/22.

   Rationale: Projects that are already in a state or local "pipeline" will become more expensive the longer they must wait in the queue for a bond award. Even as state and local funders are becoming better aligned with CDLAC and TCAC on priorities, cost containment requires prioritization of the existing pipeline. Additionally, CalHFA and HCD projects have, through the selection process, been confirmed to be advancing the Administration's AFFH priorities.

5. All projects earning 8 to10 points under the AFFH point category must provide, at minimum: 10% units at or below 30% AMI and additional 10% at or below 50% AMI.

   Rationale: Data demonstrate that the most severe housing shortfall is for ELI and VLI individuals and families. For this reason, and to encourage de-concentration of poverty, some level of deep affordability should be expected of all projects receiving substantial State investment.

6. Remove recycled bonds from the TCAC definition of "leveraged soft resources" or exclude recycled bonds from the leverage point calculation.

   Rationale: This provision has not had the intended benefit of "making room" within the volume cap. We urge continued exploration of how the Administration and Statewide policy can encourage greater use of recycled bonds and applaud the CalHFA program.

7. Refine the Preservation and Other Rehabilitation point category and defined terms to close loopholes and maximize public benefit.

   Rationale: Although the Preservation definition was refined in the last cycle of regulatory revisions, there is a small loophole that should be addressed. Some projects with expiring Housing Assistance Payment (HAP) contracts are not truly at-risk but are prioritized within the pool.

   Acquisition and rehabilitation of "Naturally Occurring Affordable Housing (NOAH)" can have a triple benefit to the state: (1) cost efficiency, (2) displacement prevention, and (3) creation of quality units with lasting affordability. These projects are currently de-prioritized for bond allocations because there have been challenges with defining and selecting rehab projects to advance Statewide goals. We should take this opportunity to modify the point category and definitions to focus on deep affordability, truly at-risk projects, and on converting NOAH into dignified housing with lasting affordability. Staff might consider adjustments for NOAH projects like requiring a minimum level of rehabilitation, prioritizing projects

that achieve an average of 50% AMI income targeting, and restricting developer fees and equity take-outs.
NOTE: If NOAH and Preservation projects are both carefully defined and prioritized, the Other Rehab Pool and the Preservation Pool could possibly be combined.

NEXT STEPS

1. Over the course of the next year, Agency staff will work closely with the HCD/TCAC Opportunity Mapping Task Force to examine how we can accurately and objectively identify locations that are opportunities for place-based investment, such as:
   A. Places with meaningful community-investment and community-development activities including large-scale public, private, and philanthropic investment as well as concerted place-based community development strategies in disadvantaged communities.
   B. Neighborhoods with culturally-specific amenities.
   C. Locations that offer benefits that are particularly relevant for non-family. residents like individuals experiencing homelessness, seniors, or young adults.
   D. Places where existing low-cost and affordable housing opportunities are disappearing due to gentrification.

   We hope that in the next round of regulatory amendments at CDLAC, TCAC, HCD, and CalHFA, we can all make use of this research to help us intentionally invest in a diversity of place-types.

2. The Administration is considering available and potential means of prioritizing location efficient housing sites using indicators tied to infill, transit proximity and other measures. The Administration is interested in strategies that prioritize equitable identification of low-VMT locations across diverse geographic regions and housing densities.

3. In considering the future of State funding priorities, we would like to continue collaborative investigation into two additional policy topics that affect all State housing finance agencies:
   A. How might we shift more development activity toward preservation, acquisition/rehab, and "NOAH"-preservation projects that have high public-benefits and low costs?
   B. How might we more consistently select projects that provide the best quality product, management/services, and sustainable long-term financial planning?

4. Calibrating the new tie-breaker is a technical challenge. The Administration stands ready to support modeling and problem-solving to ensure the outcomes of tie-breaker calculations are aligned with our shared State policy goals and recommends an annual review of the tie-breaker proposal.