CALIFORNIA TAX CREDIT ALLOCATION COMMITTEE
Minutes of the May 20, 2015 Meeting

1. Roll Call.

   Alan Gordon for State Treasurer John Chiang chaired the meeting of the Tax Credit Allocation Committee (TCAC). Mr. Gordon called the meeting to order at 11:58 a.m. Also present: Lynn Paquin for State Controller Betty Yee; Eraina Ortega for the Department of Finance Director Michael Cohen; California Housing Finance Agency (CalHFA) Executive Director Tia Boatman-Patterson; and Laura Whittall-Scherfee for Department of Housing and Community Development (HCD) Acting Director Susan Lea Riggs.

   City Representative Lucas Frerichs was absent.

2. Approval of the minutes of the March 18, 2015 Committee meeting.

   MOTION: Ms. Ortega moved to adopt the minutes of the March 18, 2015 meeting. Ms. Paquin seconded and the motion passed by a roll call vote.

3. Executive Director's Report.

   Executive Director, Mark Stivers announced that staff would soon be ready to post the list of preliminary recommendations for 2015 First Round awards. He reported that TCAC needed to resolve some outstanding issues including one pending appeal. He predicted that TCAC would fund about 47 9% tax credit projects and 4 4% plus state tax credit projects.

   Mr. Stivers explained that if 4 projects were awarded 4% plus state credits, TCAC would likely exhaust all the state credits available for 4% projects in 2015. He estimated that TCAC would have about $400,000 in state credits remaining for 4% projects. He stated that HCD expects to issue HOME awards soon, and these projects are counting on state credits, which may not be available Early passage of Assembly Bill (AB) 35 would solve this problem as TCAC would receive additional state credits.

   Mr. Stivers announced that there was a pending regulation change, which affected projects that were scheduled to receive funds under the Veterans Homelessness and Housing Program and the Affordable Housing and Sustainable Communities program. The proposed regulation change would allow the projects to apply for tax credits as long as they were on a recommended list for funding (though they might not have received an award as of the TCAC application deadline), provided they receive an award prior to TCAC awarding tax credits. Mr. Stivers stated that staff held a public hearing and comment period, which expired on May 15th. He reported that no responses were received during the comment period and the pending regulation change would be up for consideration at the June meeting.

Mr. Stivers stated that TCAC staff was in the process of reviewing a large set of regulation changes. The staff has worked internally and conducted listening sessions and focus groups to gather feedback regarding the changes.

Mr. Stivers explained that one of the proposals would extend the difficult to develop (DDA) status of projects by a year if they were to lose the DDA status. He reported that starting January 1st, the Department of Housing and Urban Development (HUD) would change the way it assigned DDA's by designating them based on zip code rather than county. The change would affect California more than any other state. Projects that relied on the 130% basis boost might not be able to access that advantage. Mr. Stivers stated that TCAC had authority within the 9% program to consider any project within a DDA. He proposed to use the authority to grandfather projects into DDA status for a one-year period if they should lose the status.

Mr. Stivers stated that TCAC has supported the set aside for Native American projects over the last two years and staff was seeking ways to continue this effort. In addition, staff was researching a potential housing goal for acquisition and rehabilitation projects. Mr. Stivers explained that staff wanted more of those projects in the 4% credit program though there was a need to have them in the 9% program as well. He suggested establishing a goal for the projects to help ensure that new construction was the top priority.

Mr. Stivers reported that staff and their state agency partners have been in discussions about whether TCAC could provide some certainty to projects like the veterans projects that received a state program award and then had to start the competitive process over again for TCAC funding. Staff raised the idea of using TCAC's non-profit set aside, which has a priority for homeless projects, to prioritize projects funded by the HCD Veterans program, the Supportive Housing program or CalHFA's MHSA program. Mr. Stivers explained that there was some opposition to the proposal because there were other types of meritorious homeless projects and most of the state funding was committed to the veteran population. The result of such of change would be that TCAC would primarily fund projects for veterans.

Mr. Stivers reported that there has been a high amount of equity take-out from projects over the last few years. Staff has been researching ways to return a share of the equity back to the projects. He explained that this issue was controversial, but staff would continue their research efforts.

Mr. Stivers reminded the Committee that a number of projects associated with the developer, ADI, were being investigated by the Federal Bureau of Investigation (FBI) for allegations of fraud. As a result of the allegations, TCAC convened a panel of accountants to research ways TCAC might change its policies related to cost certifications. Ultimately, TCAC required that at placed in service each applicant provide a copy of their accountant's peer review, which the State Board of Accountancy required all accounting firms to produce to ensure the correct processes were in place.

Mr. Stivers reported that TCAC staff was in discussions about contracting with an accounting firm and possibly a construction engineer to audit a sample of the final cost certifications for accuracy and reasonableness. He advised the Committee that he would ask for their feedback on staff's regulation change proposals at a later time.

4. Discussion and consideration of the 2015 Applications for Reservation of Federal Four Percent (4%) Low Income Housing Tax Credits (LIHTCs) for Tax-Exempt Bond Financed Projects.

   Development Section Chief, Anthony Zeto, reported that staff recommended 20 projects for approval. The projects were reviewed for compliance with federal and state regulations. He explained that the Agenda originally showed 23 projects, however three applicants withdrew their projects prior to the meeting. He noted that the Agenda was revised to indicate which projects had been withdrawn and that the Committee members received the revised version in their meeting binders.

   MOTION: Ms. Ortega moved to adopt staff recommendations. Ms. Paquin seconded and the motion passed unanimously by a roll call vote.

5. Discussion of previously awarded projects now deemed "High Cost" as defined in CTCAC Regulations, Section 103259(d).

   Mr. Stivers explained that staff has carefully reviewed the cost of California projects over time. He stated that the Committee passed a regulation change some years ago, which provided that TCAC would not recommend projects for funding if their eligible basis was greater than 130% of the adjusted threshold basis limit. Applicants that did not receive a funding recommendation by staff could still come before the Committee to seek approval for an award. Mr. Stivers reported that applicants have come in with initial cost estimates below the 130% limit; however some of them later reported costs above the limit. He explained that staff recalculated costs based on the 2015 threshold basis limits as opposed to the limits in place on the date of application to give projects the benefit of an adjustment for inflation. After the recalculations; however there were still some projects that exceeded the 130% limit.

   Mr. Stivers stated that there were currently no regulations in place to address the high cost issue therefore the projects listed on the agenda would not be penalized. He suggested the project representatives could give the Committee a better idea of what caused costs to escalate after the initial application and award.

   Mr. Gordon invited representatives of Martin Luther King, Jr. Way, Whittier Place Apartments, and Immanuel Senior Housing to comment.

   Jessica Sheldon stated that she represented Resources for Community Development (RCD), the owner of Martin Luther King, Jr. Way.

Elissa Dennis stated that she represented Community Economics, a consultant for the project.

Mr. Gordon asked where the project was located.

Ms. Sheldon stated that the project was located in downtown Oakland.

Andrew Gross stated that he represented Thomas Safran & Associates, the developer of Immanuel Senior Housing, an adaptive reuse project in Long Beach.

Osvaldo Garcia stated that he represented East LA Community Corporation, the owner and developer of Whittier Place Apartments located in unincorporated East Los Angeles.

Alejandro Martinez stated that he also represented East LA Community Corporation.

Mr. Gordon stated that the cost per unit at the policy and political levels were very problematic and that the Treasurer's administration was worried about how the federal government viewed the cost of building low income housing in California. He suggested that as political cycles occurred politicians may start to think the tax credit program was too expensive and should be eliminated. Mr. Gordon stated if he were a politician in Washington, D.C. who felt hostile toward low income housing he would focus first on areas with projects that cost $400,000 or $500,000 per unit.

Mr. Gordon stated that when John Chiang was the State Controller, he tasked Mr. Gordon and Mr. Stivers with trying to determine if there was a solution to the high cost issue. He explained that the LAO report described a major problem with supply and demand due to a shortage of land in coastal zones. Mr. Gordon noted that all three projects under discussion were located in coastal areas where people desired to live and where job opportunities were. He asked the project representatives to explain the change in their costs between the time they applied for tax credits and the present day.

Mr. Gordon invited the representatives for the Oakland project to comment.

Ms. Sheldon stated that project costs increased by $1 million since the initial application. She explained that costs were just under the 130% limit at the time of application and were currently just over the limit. She stated that one reason the project exceeded the limit was an increase in construction costs.

Mr. Gordon asked Ms. Sheldon what was driving construction costs. He stated that he read macroeconomic data, which indicated workers were not getting wage increases. He stated that labor cost did not seem to be the cause of increased construction costs because wages were flat.

Ms. Sheldon stated that construction in Oakland had been increasing since the time her firm applied for the credits. She noted that the city had a local hire policy, which reduced the pool of contractors and sub-contractors her firm could draw from. In addition, the pool of contractors had more demands and interests.

Mr. Gordon asked Ms. Sheldon if increased labor costs were causing the increase in construction costs in Oakland.

Ms. Sheldon stated that a review of the total budget revealed the amount paid to sub-contractors had increased. She stated that she did not know if the additional amount was going to the workers.

Ms. Dennis stated that she worked on a lot of projects statewide but particularly in Alameda County. She recently reviewed a project that she hoped could apply in the 2015 Second Round; however the sub-contractor for the project reported a 20% increase over the bids the firm received a year ago. Ms. Dennis noted that the newer bids were better; however the increased cost was so significant that the sponsor was not going to apply for tax credits.

Ms. Dennis stated that she was working on three projects that were similar to the one Ms. Sheldon was working on. She stated that Martin Luther King Jr., Way was a small 26-unit project with small unit sizes. The project was a Special Needs housing type in an infill site right in the middle of downtown. Ms. Dennis stated that the project was a very critical project that could help maintain affordability among the unaffordable market rate developments in downtown.

Ms. Dennis explained that a small project with 26-units comprised of studio and 1-bedroom apartments would not get the threshold basis limit that would provide flexibility. The projects she was currently working on were 22-32 units with a mixture of 1-bedrooms and larger units. Costs for these projects were near 150% of basis. She noted that Ms. Sheldon's project was much closer to meeting the threshold limit.

Ms. Dennis stated that as she reviewed properties in Alameda County she noticed that small projects with small unit sizes did not meet the threshold basis requirements. When Ms. Sheldon's firm submitted the application in the middle of 2013, the estimated cost and credit pricing seemed realistic and RCD committed to building the project based on the estimates. Ms. Dennis stated that the firm was fortunate to receive an additional $600,000 through the Housing Opportunities for People with AIDS (HOPWA) program. In addition, the firm received higher equity pricing than expected. At the time of application the firm estimated $0.98 in equity pricing, which was somewhat conservative but not unreasonably low. The firm ultimately received $1.10 in equity pricing.

Ms. Dennis stated that even though project costs increased due in part to higher bids~~,~~ the applicant still had the resources to make the project better than it would have been if they had to value engineer everything out. She stated that the applicant would have built the project within the original parameters if they had not received the additional funding.

Mr. Gordon asked what was on the site prior to the housing development.

Ms. Sheldon stated that a warehouse was on the site.

Mr. Gordon asked if the applicant had to deal with any toxic contamination issues.

Ms. Sheldon stated that fortunately there were no toxic contamination issues. She noted that the developer did not proceed too deeply into the ground.

Mr. Gordon asked Ms. Sheldon why her firm limited the project to 26 units as opposed to making it larger.

Ms. Sheldon explained that the parcel was very small, covering about 1/3 of an acre. The project included 5 occupied stories and a patio on the roof. She stated that her firm could not build the project any higher.

Mr. Gordon noted that Ms. Sheldon's firm was using wood frame construction for the project. And the firm would have to use steel construction to build the project higher.

Mr. Gordon stated the Rocky Mountain Institute was in the process of designing 32 new cities in China for the Chinese government. He explained that each city would include an estimated 2 million people. The type housing being built consisted of large apartment blocks. Mr. Gordon stated that the apartments were obviously built using steel construction, which allowed them to be very high. He stated that when projects reached a height between 5 and 15 stories the cost of construction might increase so much that the projects are no longer feasible; however costs could decrease after a certain point if the projects were built even higher than 15 stories.

Mr. Gordon asked why California developers did not try to build super large projects. He stated that building small 26-unit projects would not impact the immense need for housing. He asked if there were public policy issues the state government could address to help provide California citizens the housing they needed.

Mr. Gordon stated that there was an article in the Economist magazine, which reported that there could be thousands more jobs in the Bay Area if California housing was at least at the national median in terms of cost. He stated that code writers cost a company like Google $100,000 in Austin but $150,000 in San Francisco so employees could afford to live there. Mr. Gordon concluded that if Google had $1 million to hire additional staff, the $1 million in the Bay Area would create fewer jobs. He explained that the single biggest impediment to employing Californians was housing.

Mr. Gross stated that his firm's goal was to build larger projects with 70 to 100 units. In building large projects the firm could spread the cost among more units. Mr. Gross noted that his firm did the same amount of work for a 25-unit project that it did for a 70 to 100-unit project. He stated that from a project specific view the cost of the Immanuel Senior Housing project increased due to a need for structural retrofitting, which the applicant learned about after their plans were already in progress. He noted that adaptive reuse of a church to build the project was a smart infill. When the site was purchased, his firm determined that the best use of the church was a senior housing project.

Mr. Gross stated that the market was changing, but he did not know if the change was due to the cost of labor or materials. He explained that when production of market rate units was high general contractors and subcontractors that may have been interested in affordable housing would move to the market rate development. However when market rate production decreased, contractors would return to affordable housing because low income programs could still build projects with the added benefit of lower costs.

Mr. Gross stated that the projects he worked with were small unit types. He explained that when fixed costs were spread over the smaller number of units, the resulting cost per unit was higher. He stated that his firm generally preferred to develop larger projects; however unique projects such as special needs developments could not be built in large quantities.

Mr. Martinez stated that policy was a critical component. He explained that his firm missed an opportunity to apply for veterans funding because their project did not meet the entitlement threshold, which required a confirmation of California Environmental Quality Act (CEQA) clearance on the project. He noted that the project fell under the SB 1818 Affordable Housing Incentives law. He commented that his firm should have the ability to propose a project to the city or county within the limits of the law and obtain signatures on their TCAC forms which indicate the firm has a by right project.

Ms. Boatman-Patterson stated that the firm was having an issue with the local government.

Mr. Martinez stated that without the local government signatures the firm could not meet the threshold requirement and also could not apply for funding. As a result, the project, which could have had 60 to 90 units, was delayed an additional year. Mr. Martinez stated that firm dealt with this kind of impediment on a daily basis.

Mr. Martinez stated that sometimes the firm will review a great project in a blighted area that no else will develop; but without the necessary signatures on the TCAC forms the project would be delayed. He explained that the process for the city and county were completely different. There could be a property within the city boundaries and another property across the street within county limits. The zoning for the properties would be the same; however the requirements and entitlement process could be completely different. The project within city would have much higher density by right, whereas the project within the county would require a list of requirements such as conditional use permits, general plan amendments, and height variances.

Mr. Martinez suggested that TCAC lobby the city and county governments in Los Angeles and the rest of the state to better enforce or implement SB 1818 and other affordable housing incentive laws.

Ms. Boatman-Patterson stated that the local land use and local controls of the city and county were completely inconsistent and consequently incompatible with development. She stated that developers needed certainty. If a developer wanted to build a project on one side of a street and then move to the other side where planning and entitlement departments were completely different, the developer would have to continually recreate itself to figure out the process of how it deals with local government. Ms. Boatman-Patterson explained that the local government should maintain local land use and control; however there should be standardized best practices.

Mr. Martinez explained that his firm needed to have certain approvals from state and local governments to secure funding from lenders and prevent delays in development.

Mr. Gordon reported that in Connecticut, developers had the right to appeal a denial at the local level. He explained that the state government could override local government decision based on certain findings. He asked Mr. Martinez if developers could prevent delays if they had access to a similar appeals process.

Mr. Martinez stated that developers should respect the local process. He suggested revising the TCAC forms to include a section where the local governments could place their mark to indicate the project in compliance with affordable housing incentives.

Ms. Boatman-Patterson stated that there was a potential problem with not running the processes concurrently. She explained that projects could receive TCAC or other state awards, but would not have the certainty of site control and entitlements.

Mr. Martinez stated that if the projects were by right during the escrow period then they should receive the local approvals.

Mr. Gordon stated that he wanted to find out what kind of disruptive legislation could change the current system, which was leaving thousands of units undeveloped in California. He noted that sprawl development was a great threat to the environment, according to a report by Bank of America. He asked the presenters how they would change legislation to get more density from the existing system.

Ms. Dennis stated that it was important to acknowledge that developers were seeking opportunities to increase density. She stated that large projects were also limited by financing from each level of government.

Ms. Boatman-Patterson suggested it would help if projects had access to true gap financing. She stated that the revenue stream would provide gap financing to be able to leverage some of the various federal and state tax credits.

Ms. Dennis stated that even when developers had access to RDA funding, they also had local funding and tax credits in order to provide some level of affordability. She stated that there was a limit to how far costs could be lowered, but she was optimistic about potential increases in funding from various sources. Ms. Dennis noted that the additional funding would not bring her project costs under the threshold limit, but it would make the projects feasible.

Mr. Gross suggested that developers seek ways to finance larger projects in order to lower the cost per unit. He recommended creating an incentive mechanism such as a funding source for projects of a certain size. He noted that lowering per-unit cost should not be the only goal. He noted that one of the past tax credit pools called Balanced Communities incentivized building affordable housing in upper income locations.

Ms. Boatman-Patterson stated that it was very important to have mixed income and balanced communities.

Mr. Gross stated that another tax credit pool was the small unit set aside. He recalled that the small unit set aside was for projects with up to 20 units. He suggested government should incentivize low per-unit costs, but he also noted the reasons for building in balanced and mixed income communities.

Mr. Gordon asked Mr. Martinez to explain the reasons for increased costs in Los Angeles.

Mr. Martinez stated that he discussed with his colleague how their firm managed costs of its 7 projects in predevelopment. He explained that the firm spent money on the land, design, engineering and entitlements. At a certain point the firm stopped spending until it received commitment letters for the projects. Mr. Martinez explained that if the firm continued spending funds on all the predevelopment projects, it would incur millions of dollars in costs.

Mr. Martinez explained that change orders always come up in the face of project closing deadlines. Inevitably, developers had to make changes, whether architectural or structural or civil, during the remaining 15%-20% of the process.

Mr. Martinez reported that his firm was unable to get a building permit for its project because the Fire Department raised an additional requirement at the last minute and asked the developer to propose a solution rather than provide the developer with a specific way to comply.

Ms. Boatman-Patterson noted that a different staffer in that department may have given the firm a different response.

Mr. Garcia stated that the Fire Department would not give its stamp of approval until it received the developer's proposal.

Mr. Martinez stated that other developers had the same issue with many of their projects. He commented that the Fire Department staff may think his firm was trying to circumvent the local process. He stated that his firm must stay on top of their requests for permits but unfortunately it was sometimes halted by employees who had the power to deny their requests.

Ms. Paquin asked Mr. Gross to describe his experience with balanced community projects. She asked if there had been opposition at the local level.

Mr. Gross stated that his firm developed projects in Calabasas, West Los Angeles, and Playa Vista. He explained that the Regional Housing Needs Assessment (RHNA) process, which required communities to provide their fair share of affordable housing, has helped the firm gain approval to develop in areas like Calabasas.

Mr. Martinez stated that his firm tried to acquire sites that the community identified as problem sites. Sometimes the sites were large enough to have up to 50 units. And sometimes the firm would purchase the neighboring sites. Mr. Martinez explained that due to his firm's process the community was likely to identify small sites and ask the firm to develop them. He commented that he did not want to dissuade staff or his organization from developing small projects. He stated that for-profit developers would not build the kind of projects that his firm was trying to build.

Ms. Dennis stated that neighborhood opposition to affordable housing was often related to traffic and density as a result of the proliferation of poor people; however non-profit organizations have invested years into establishing relationships with their communities and to provide projects that were well maintained and managed. She cautioned that the relationships could be destroyed if developed began to focus solely on lowering their costs.

6. Adjournment

The meeting adjourned at 2:00 p.m.