External Funding Sources Available for Affordable Housing Development and Preservation

PREPARED BY THE CITY OF MADISON COMMUNITY DEVELOPMENT DIVISION

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WHEDA 9% Tax Credits

- Opportunity
  - Also known as competitive tax credits, this resource has received bipartisan praise as the most effective tool for creating affordable housing in the US. These tax credits generate a greater amount of equity compared to 4% credits. Due to the competitive nature, WHEDA prioritizes applications that maximize project financing coming from other sources
- Source
  - Federal Tax Credits/Investor
- Additional Information
  - Timeliness requirements limit how large projects can be in scope. WHEDA does not allow an income-averaging approach for 9% tax credit projects

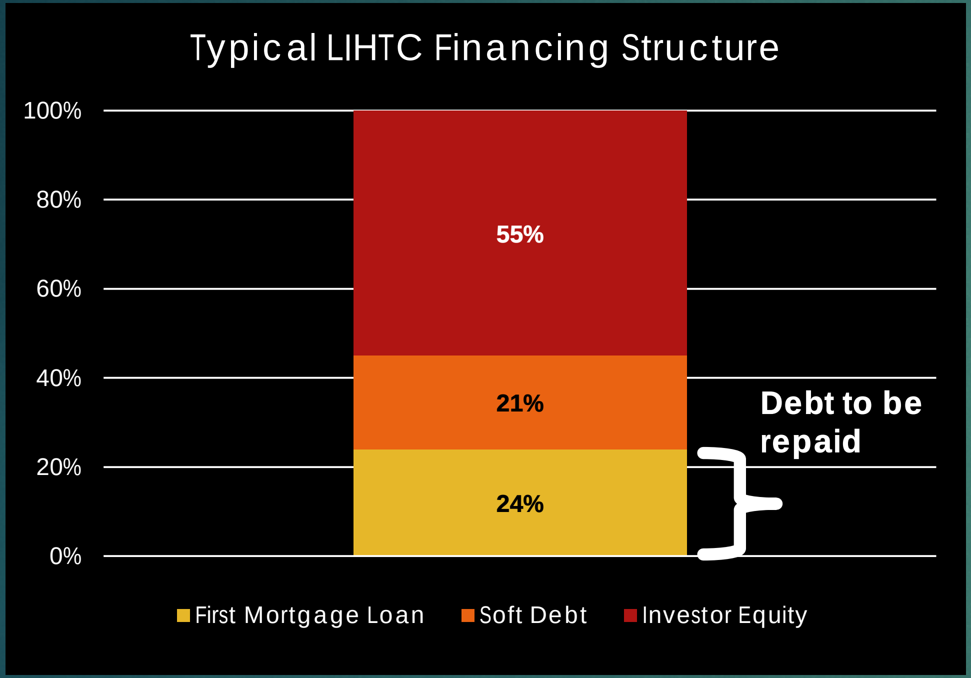
WHEDA 4% Tax Credits

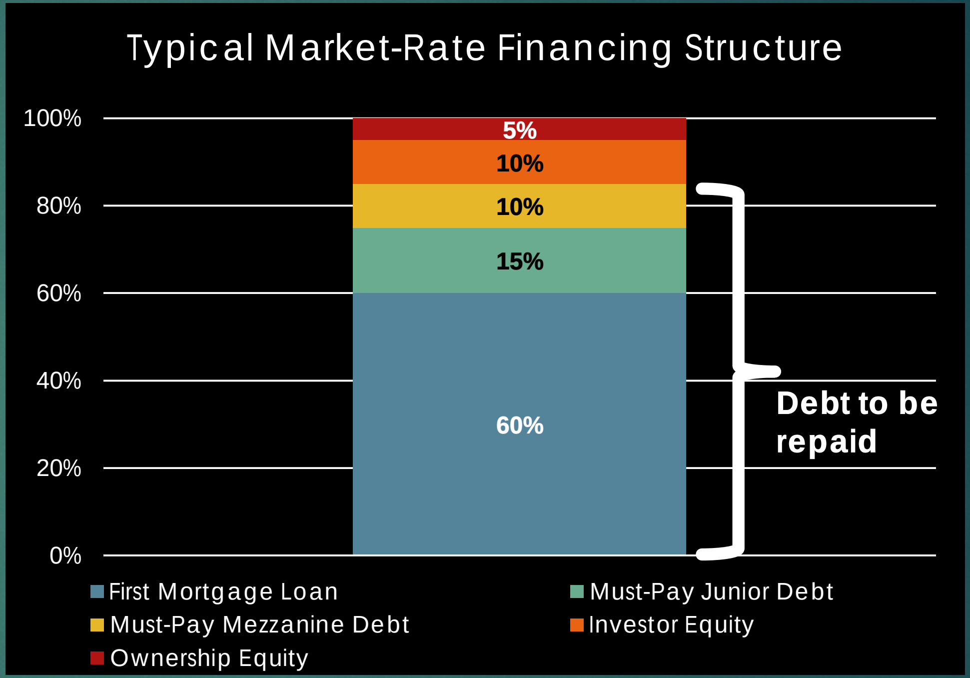
- Opportunity
  - Also known as noncompetitive tax credits, there is virtually no cap to the amount of tax credits that a developer can claim, so as long as they have enough eligible costs to match their request to WHEDA. Applications are accepted on a rolling basis. There are much fewer timeliness requirements compared to 9% tax credits. Noncompetitive credits often lead to the creation of more units since these credits generate less equity
- Source
  - Federal Tax Credits/Investor
- Additional Information
  - Income-averaging is a new feature allowed by WHEDA and enables developers to deliver a mix of 20%-80% CMI units as long as the average income restriction does not exceed 60% CMI. Traditional 4% developments typically do not target 30% units
  - WHEDA also offers a competitive state 4% tax credit, with a credit cap, but prioritizes applications with a greater mix of incomes
  - Best used for acquisition-rehabilitation deals, but also frequently used on very large (100+ unit) new construction deals

Wisconsin Affordable Housing Tax Credits

- Opportunity
  - Also known as state 4% tax credits, this competitive tax credit program was enacted in 2018 by the Wisconsin state legislature as tool to be used with federal 4% tax credits. WHEDA's process for allocating these credits is a competitive process similar to that of the 9% credits, but there are additional scoring categories. Unlike the federal tax credit, the state credit is allocated of six years instead of ten, making this resource more valuable to investors looking to offset their state income tax liability, and thus increasing the amount of equity a developer can raise
- Source
  - State Tax Credits/Investor
- Additional Information
  - Can make 4% deals more feasible to be developed since the amount of equity able to be generated through the sale of these credits nearly doubles equity from federal credits
  - Maximum credit request of $1,400,000 per proposal
  - State requires a preference for allocating state credits to communities with populations under 150,000
  - Cannot use with 9% tax credits and applicant must apply for federal 4% credits simultaneously

How Tax Credit Developments Support Reduced Rents





- In a market-rate deal, developer must assume more debt at higher interest rates, necessitating increases rents to support loan payments
- In a tax credit deal, developer raises majority of funds through sale of LIHTCs, so less debt is needed and development can operate with lower rents since loan payments are smaller

Private Activity Bonds (PABs)

- Opportunity
  - Private lenders purchase tax-exempt bonds from a bond issuing agency as collateral for a low-interest construction loan to finance affordable housing development
- Source
  - Bonds: Agency with bonding authority (e.g. City, CDA, DCHA)
  - Capital: Private lenders
- Additional Information
  - Section 142 of the IRC requires that developers provide at least 40% of units to tenants earning at or below 60% CMI, or 20% of units to tenants earning at or below 50% CMI. Units may be income-restricted below those CMI thresholds, but units offered at the market-rate or with higher CMI limits do not count toward the 40-60 or 20-50 tests
  - Typically paired with 4% LIHTCs, but not a requirement
  - Cannot be used with 9% LIHTCs

WHEDA 7/10 Financing

- Opportunity
  - Requires developers to set aside at least 20% of units for households earning 80% CMI or below in exchange for a favorable interest rate. Developers can opt to income-restrict units to lower CMI levels
- Source
  - WHEDA
- Additional Information
  - Municipalities can impose deeper affordability restrictions beyond 80% CMI
  - Maximum loan amount is $10 million
  - May be allocated to for-profit or non-profit developers
  - Cannot use with LIHTCs

Opportunity Zones – Private Financing

- Opportunity
  - Private investors with realized capital gains may invest in a project in a Qualified Opportunity Fund in order to reduce and delay payment of capital gains taxes
- Source
  - Private Financing
- Additional Information
  - Very difficult to pair LIHTCs with investment in Opportunity Zones, due to competing interests of traditional investors and tax credit investors
  - Need to meet public benefit test of at least 51% of units affordable at or below 80% CMI

Opportunity Zones - FHA Lending

- Opportunity
  - Reduce application fees for multifamily developments within an OZ tract applying for 221(d)(4), Section 220, and Section 223(f) mortgage products; The FHA will also designate staff to fast track applications to reduce the underwriting time; These application fees can be reduced from $3 to $1 per $1,000 of loan requested if at least 90% of units have Section 8 PBRA or at least 90% of units are LIHTC units
- Source
  - First Mortgage Lender/Federal Government
- Additional Information
  - These loans trigger Davis-Bacon wage requirements when the mortgage is placed within 3 years of the start of construction, so it may not be enough to offset that cost
  - Very difficult to pair LIHTCs with investment in Opportunity Zones
  - Can use for traditional homeownership development and financing

Section 108 Loan Guarantee - Lending

- Opportunity
  - Cannot typically use to fund new affordable housing construction. Typical or more common uses of Section 108 loan guarantee proceeds are commercial developments, including malls, hotels, and convention centers
- Source
  - Federal Government/Community Development Division
- Additional Information
  - The City of Madison would likely need to provide the loan to a private for-profit developer for a large-scale project due to capacity and focused missions of non-profits
  - The City of Madison guarantees future CDBG entitlement money to HUD in exchange for getting access to Section 108 liquidity
  - This funding source carries all CDBG requirements, including Davis-Bacon wage requirements and LMI job creation targets

U.S. Department Housing & Urban Development: HOME/CDBG

- Opportunity
  - Gap financing available through Community Development Division, loan is provided as deferred payment/shared appreciation
- Source
  - Federal Government/Community Development Division
- Additional Information
  - Must go to non-profit, federal compliance requirements
  - Cannot use CDBG to fund new construction of housing
  - Any development using CDBG for construction or rehabilitation triggers Davis-Bacon wage requirements
  - Can use for traditional homeownership development and downpayment assistance

"Badger Fund"/United Way Economic Stability Group

- Opportunity
  - Group of private investors interested in increasing the supply of affordable rental housing in the Madison area have pooled money into a fund to provide gap financing to developments
- Source
  - Private & Non-Profit Investors
- Additional Information
  - There has not yet been a project funded with this funding source, and the requirements associated with this group are still largely unknown
  - Goals of the group are largely unknown and the amount of funds available are unknown