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Increasing the Cost-Effectiveness of Housing Trust Fund Investments

Recommendations to the Legislature required by SHB 2640 (2012)

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Report to the Legislature
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Executive Summary

Overview

The Washington State Housing Trust Fund was established in 1986 under Chapter 43.185 RCW "to assist low and very low-income citizens in meeting their basic housing needs." The Department of Commerce (Commerce) administers the activities funded through the Housing Trust Fund. Capital funds for the development and preservation of affordable housing are awarded on a competitive basis, using criteria established in RCW 43.185.070, as well as other criteria established by Commerce and the Washington State Legislature.

In 2012, the Housing Trust Fund statute was amended by Substitute House Bill 2640 (SHB 2640) to require that Commerce consider cost when evaluating projects for funding from the Housing Trust Fund. It directed Commerce, with advice and input from the Affordable Housing Advisory Board or their subcommittee, to report recommendations for awarding funds in a cost-effective manner, including an implementation plan and timeline.

Commerce is committed to implementing policies that will increase the cost-effectiveness of Housing Trust Fund investments without compromising the primary goals of the program. This report identifies measures that Commerce proposes to implement over the next two years, as well as measures that have already been taken, to ensure that Housing Trust Fund investments are both efficient and effective. It also reflects Commerce's intent to continue exploring additional options to further enhance the cost effectiveness of its investments.

Recommendations

Based on input from stakeholders and a survey of other state housing agencies, Commerce proposes to undertake the following actions.

1. Establish per-unit cost limits based on a cost assessment of comparable projects.
2. Require applicants to describe specific measures to reduce project costs and to quantify projected savings.
3. Conduct additional research and evaluation of other states' policies and identify best practices for potential implementation.
4. Identify potential incentives for cost savings during the project development phase.
5. Conduct an inventory and impact analysis of regulatory requirements that contribute to project costs.
6. Establish a methodology for factoring long-term operational cost efficiencies into the evaluation of project development costs.
7. Develop policies to limit project "soft" costs.
8. Develop construction expertise within the Housing Trust Fund staff.
9. Document and monitor per-unit and other project cost data over time.

Introduction

Background

Capital funds appropriated to the Housing Trust Fund are used to provide grants and loans to eligible organizations for the development and preservation of affordable housing. Priority is given to projects that serve very low-income households and persons with special needs. In addition, statute requires that at least 30 percent of funds awarded are targeted to projects located in rural areas.

Housing Trust Fund investments total more than $900 million since 1987, resulting in more than 39,000 units of affordable housing across the state. These investments have leveraged an additional $3 billion from non-state public and private resources.

In 2008, the Legislature instructed Commerce to evaluate the costs associated with affordable housing development financed through the Housing Trust Fund. The resulting *Affordable Housing Cost Study* (2009) included a set of policy recommendations intended to create or incentivize cost savings in Housing Trust Fund projects. Some of those recommendations have been implemented and are discussed in this report.

The first recommendation identified in the *Affordable Housing Cost Study* was to "place increased emphasis on cost control as a funding decision factor." In 2011, Substitute House Bill 2640 (SHB 2640) required that Commerce consider cost when evaluating projects for funding from the Housing Trust Fund. Commerce was directed to develop recommendations for awarding funds in a cost-effective manner, an implementation plan, and timeline, and to provide a report to the Legislature by December 1, 2012.

Process to Establish Recommendations for This Report

In April 2012, the Affordable Housing Advisory Board directed its subcommittee, the Policy Advisory Team, to work with Commerce to accomplish the requirements of SHB 2640. Commerce and the Policy Advisory Team convened the Housing Trust Fund Cost-Effectiveness Committee. The committee included a broad-based group of stakeholders representing various aspects of affordable housing development, including nonprofit housing providers, housing developers, public and private funders, architects, construction managers, and low-income advocates. Members represented both urban and rural areas, Eastern and Western Washington, and experience with a broad spectrum of housing types.

In addition to consulting with Housing Trust Fund stakeholders, Commerce contracted Washington State University Extension Energy Program (WSU) to conduct a survey of cost-containment policies implemented by other state housing trust funds. The report resulting from that survey, *Cost-Containment Policies, Practices and Recommendations from Seven State Housing Trust Fund Programs* is included in Appendix A of this report.

Key Considerations in the Development of the Recommendations

There is broad acceptance by Commerce and Housing Trust Fund stakeholders that cost should be a key consideration in awarding funds to projects, and that policies should be established that encourage cost savings and maximize the state's return on its investment. At the same time, there is acknowledgement that cost-containment policies, if not carefully implemented, have the potential to create unintended consequences.

The goal of the Housing Trust Fund Cost-Effectiveness Committee was to develop a policy that would ensure an appropriate level of investment in affordable housing projects, while maintaining flexibility to ensure that public priorities are met and the quality, durability, and sustainability of projects are not compromised.

Contributors to the Higher Cost of Affordable Housing

It is frequently suggested that affordable housing can be developed at a lower cost by the private market. The *Affordable Housing Cost Study* includes a case study comparing two 100-unit multi-family projects developed in the Seattle region – a market-rate development and a Housing Trust Fund affordable housing project. The case study found that the affordable housing project cost $14,804 more per unit than the market-rate project; however, the affordable housing project had slightly lower costs per square foot and overall development costs were relatively comparable. The majority of the additional costs of the affordable housing project were attributed to the complexities of the public funding sources and additional regulatory requirements related to those sources.

Public policy goals

Many regulatory requirements associated with public funds are designed to promote a specific public policy or benefit, but may contribute to the cost of projects. For example, publicly funded projects are subject to prevailing wage requirements, which can add substantial cost, particularly when commercial wage rates are applied to a project.

Another example is the Housing Trust Fund's Evergreen Sustainable Design Standard, developed in response to RCW 39.35D.080. The Evergreen Sustainable Design Standard is designed to reduce energy consumption by 7 percent, and includes numerous other "green" criteria designed to achieve certain goals, such as water conservation, waste reduction, improved indoor air quality, preservation of open space, and increased access to public transportation. More durable building materials are also encouraged. Although the standards are designed to reduce costs over time, a higher investment may be required at the time of construction.

Public policy goals may also be furthered through budget provisos or funding preferences. State and local funding priorities are often established to address a specific need, area, or population, or to pilot a new concept. Projects designed to respond to these priorities may not be cost-competitive with other projects, but they achieve a specific policy priority. For example, housing for persons with special needs may require specific design accommodations that add cost, and on-site services can trigger commercial prevailing-wage rates. Historic preservation projects can incur extra costs for the replication of period details or structural stabilization. Costs may also be driven up because of specific siting needs, as in the case of transit-oriented development and seasonal farmworker housing, both long-standing priorities.

Local jurisdiction requirements

Affordable housing projects are sometimes subject to additional requirements at the local level that add to their development cost. Local jurisdictions may require a project to include certain elements, such as structured parking, or to contribute to development of off-site infrastructure, such as water and sewer line extensions, street improvements, sidewalks, and street lights. Projects may also be subject to "payments in lieu of taxes" (called PILOT fees) imposed by the jurisdiction to offset foregone property tax revenue.

Layering of multiple fund sources

On average, affordable housing projects require at least five sources of funding, each with its own set of requirements. Significant costs must be incurred just to achieve a level of readiness to even be considered for funding. Interim financing costs, legal fees, and other carrying costs accrue pending full funding of a project, adding to the overall cost. The *Affordable Housing Cost Study* found that, on average, development or "soft" costs make up 23 percent of the total cost of an affordable housing project. While the layering of fund sources and associated requirements clearly contributes to these costs, it also maximizes the state's investment. Each dollar invested from the Housing Trust Fund in 2011 leveraged another $5.50 from other non-state sources.

Ensuring a Sound Return on Investment

When comparing the cost of publicly funded affordable housing with private market development, it is important to recognize that Housing Trust Fund investments guarantee the creation of safe, decent housing that will remain available and affordable to some of the state's most vulnerable populations for 40 years or more. Projects are monitored on a regular basis to ensure they are properly maintained and continue to serve eligible households throughout the compliance period. Privately developed housing is built to maximize financial return to the developer and owner. There is no guarantee that units will remain affordable or that the property will be maintained to appropriate standards for any period of time.

More than 70 percent of households in Housing Trust Fund projects have extremely low incomes (less than 30 percent of area median income). Half of all households served include people with special needs, including the elderly, developmentally disabled, homeless veterans, and persons with mental illness. Because of their low incomes and special needs, these households are considered undesirable tenants and are generally not well served by the private market. As a result, they may be forced to live in substandard conditions and are often at risk of homelessness. Public investments provide stable housing for at-risk populations, increasing their health and safety, stabilizing families, improving their ability to succeed in school and at work, and reducing demand for other costly social and health services. Market studies required at the time of application ensure that projects are addressing an unmet need and are appropriate for the proposed location.

Measures to Enhance the Cost Effectiveness of Investments

Commerce currently conducts a detailed analysis of development and operating costs when evaluating projects for funding from the Housing Trust Fund. An informal comparison of costs is made between projects, with allowances made for variances in project type, location, size, and design, as well as target population, but there are no established cost limits and there is no formal definition or method for determining “acceptable” costs.

Measures Proposed for Implementation

Commerce proposes to develop and implement a set of policies and practices to increase emphasis on cost when awarding funds. The recommendations are based on input from stakeholders and a review of policies implemented by other state housing trust funds. A more detailed explanation of each proposed measure is provided on the following pages.

	Recommendation	Implementation
1	Establish per-unit cost limits based on a cost assessment of comparable projects	Spring 2013
2	Require applicants to describe specific measures to reduce project costs and to quantify projected savings	Spring 2013
3	Conduct additional research and evaluation of other states’ policies and identify best practices for potential implementation	Summer 2013
4	Identify potential incentives for cost savings during the project development phase	Fall 2013
5	Conduct an inventory and impact analysis of regulatory requirements that contribute to project costs	Fall 2013
6	Establish a methodology for factoring long-term operational cost efficiencies into the evaluation of project development costs	Spring 2014
7	Develop policies to limit project soft costs	Spring 2014
8	Develop construction expertise within the Housing Trust Fund staff	Fall 2014
9	Document and monitor per-unit and other project cost data over time	2013-ongoing

Recommendation 1:	Establish per-unit cost limits based on a cost assessment of comparable projects (Spring 2013 or next funding round)

Beginning in 2013, when evaluating projects for funding Commerce will conduct a comparative assessment of project development costs to determine whether the cost of each project is reasonable compared to other projects of a comparable type and location.

Preference will be given to projects that:

- Meet funding criteria and priorities established by the Legislature and Commerce.
- Address an identified need within the community.
- Are determined to have a reasonable cost, based on the cost evaluation criteria established by Commerce.

Project costs will be deemed reasonable if the per-unit cost is at or below 110 percent of the average per-unit cost of comparable projects in a similar geographic area. Project costs in excess of 110 percent of the average may be deemed reasonable if the applicant provides adequate evidence that the higher capital costs will result in sufficient savings in long-term operating and maintenance costs to justify the additional expense. Allowances may be made for other high-cost factors on a case-by-case basis.

Data from at least two years of Housing Trust Fund rounds will be used to determine what types of projects and locations can be reasonably compared, taking into account such factors as type of activity, target population, and project size and composition. To the extent feasible, a comparison will be made between projects within the same funding round. If there are insufficient projects of comparable type and geographic area, historical data from the prior application round may be used.

Costs will be evaluated on a per-unit basis, with consideration given to the proposed number of bedrooms per unit. The cost per unit calculation will exclude the cost of land and capitalized reserves. If per-unit costs of comparable projects are found to be substantially equivalent, cost per square foot will be used for further comparison.

Land acquisition costs will be evaluated separately from per-unit costs, due to its variability. A third-party appraisal and market study will be required to ensure that the purchase price does not exceed the market value of the property and that the site is appropriate for the type of project proposed.

Commerce does not have the capacity or data necessary to routinely compare the cost of proposed projects to similar projects being developed by the private market. An alternative may be to periodically engage a third party to compare a sample of different types of Housing Trust Fund projects against a sample of similar private sector projects. Resulting data could potentially be used to establish benchmarks that would help ensure that Housing Trust Fund project costs stay within an acceptable range of private sector costs. Commerce will continue to explore this alternative.

Basis for the Recommendation

The most obvious way to control the cost of projects is to establish a limit on the allowable cost. Six of the seven states interviewed by WSU have imposed some sort of cost-limiting policy, but each is different and only one state could provide any evaluative data on the effects of their policy. Setting a cost limit may seem straightforward, but there are a variety of possible approaches and potential consequences to be considered.

Defining cost

There are many ways to define cost and different types of costs to consider when evaluating a proposed housing project. In addition, costs can be broken down a multitude of ways. Some costs are largely beyond the control of project developers, and certain items can cause huge variances in project costs, even among similar project types and locations.

Development costs include a variety of activities, from pre-development to acquisition and through construction. Some of these costs can be highly variable and are often beyond the control of the developer. One of the most significant variables is land acquisition. Land costs can vary significantly by location, even within the same geographic area. Establishing cost limits that fail to account for this could potentially reduce development in higher-cost areas and concentrate development in lower-cost areas. Another highly variable cost is capitalized reserves. Substantial reserve requirements dictated by investors can put projects at a competitive disadvantage if included when comparing costs against other projects, placing substantial amounts of leverage at stake.

Project development costs are typically compared on either a per-unit or per-square-foot basis. Committee members acknowledged that neither measure is perfect, and that costs should not be viewed in only one way or in isolation of other factors. It was the consensus of the group that per-unit costs provide the most reasonable basis for comparison.

Three of the six surveyed states with cost-limit policies apply cost-per-unit limits, and the Washington State Housing Finance Commission implemented a cost-per-unit limit for its Low Income Housing Tax Credit Program in 2011, but each of these programs define cost and establish their limits in a different manner.

Housing project types

The Housing Trust Fund invests in a broad spectrum of project types, including emergency shelters, group homes for the developmentally disabled, senior housing, seasonal housing for migrant farmworkers, self-help housing, and small and large multi-family developments serving a wide variety of populations. Development activities also vary, and may include new construction, moderate rehabilitation, substantial rehabilitation, redevelopment, or any combination of those activities within a project.

Due to differences in project type, size, design, and target population, and how those factors impact costs, not all projects can be reasonably compared with one another. Further, certain fund sources and the requirements associated with them may also have a significant effect on project costs.

Location

Similar to housing type, project location can impact the cost of a project. For example, data shows that development costs in Seattle are higher than other areas of the state. Costs can also be considerably higher for projects in remote rural areas.

Recommendation 2:	Require applicants to describe specific measures to reduce project costs and to quantify projected savings (Spring 2013 or next funding round)

The Housing Trust Fund application will require a description of specific measures taken, or proposed to be taken, to reduce project development and long-term operating and maintenance costs and, to the extent possible, to quantify projected savings.

Basis for the Recommendation

This information will supplement the comparative assessment of project development costs. Data provided will be compiled and used to identify and promote best practices. Data provided may also support Recommendation 6.

Recommendation 3:	Conduct additional research and evaluation of other states' policies and identify best practices for potential implementation (Summer 2013)

Commerce will continue to research and evaluate the policies of other public funders in an attempt to identify additional cost-saving measures that could be adopted by the Housing Trust Fund.

Basis for the Recommendation

Six of the seven states surveyed for this report by WSU identified specific cost-containment policies or practices, but no evaluative data was available to assess their effectiveness. In addition, due to time and cost constraints, the survey included a relatively small sample and was limited to state housing trust funds. Additional time is needed to research practices implemented by other funders and whether they are producing the intended results.

Recommendation 4:	Identify potential incentives for cost savings throughout project development (Fall 2013)

Commerce will continue to work with stakeholders to identify additional strategies and incentives for cost savings at all phases of project development.

Basis for the Recommendation

Under SHB 2640, Commerce was charged with developing recommendations for awarding funds in a cost-effective manner. Commerce and Housing Trust Fund stakeholders recognize that there are opportunities for savings at various points in the life of a project, not just at the award phase. Commerce will continue working with stakeholders to develop additional policies that create incentives for, or directly result in, cost savings during construction, as well as over the life of the project.

Recommendation 5:	Conduct an inventory and impact analysis of regulatory requirements that contribute to project costs (Fall 2013)

Commerce will work with stakeholders and other public funders to identify specific regulatory requirements that significantly increase project costs, evaluate the extent of their impact, and explore potential strategies to mitigate them.

Basis for the Recommendation

It is widely recognized that federal, state, and local regulatory requirements contribute to the cost of projects. Additional work is needed to identify those that have the most significant impact and evaluate practical solutions to eliminate or minimize their impact. For example, Commerce is currently conducting a survey to determine the relative incidence of commercial prevailing wage rates being imposed on affordable housing projects and the degree to which that impacts project costs.

Recommendation 6:	Establish a methodology for factoring long-term operational cost efficiencies into the evaluation of project development costs (Spring 2014)

Commerce will work with stakeholders to research and develop practical methodologies for factoring long-term operating cost efficiencies into the evaluation of project development costs.

Basis for the Recommendation

A primary concern raised by stakeholders in considering a cost containment policy was the impact it might have on the quality, durability, and sustainability of projects. Significant progress has been made in recent years to encourage "green" building practices that reduce the long-term operation and maintenance costs of a project, in addition to reducing the impact on the environment. The Housing Trust Fund's Evergreen Sustainable Building Standard has been embraced not only by housing developers, but by other public funders who have adopted the standard into their own programs. The standard is unique in that it was specifically designed for affordable housing development in the Pacific Northwest.

Although many sustainable features will result in long-term savings that offset the additional upfront investment, reliable data is not always available on the payback of those measures. The Evergreen Standard is designed to achieve a 7 percent reduction in energy use. It provides methodologies for ensuring selected energy conservation measures will achieve those results, but similar methodologies or payback data are not available for all sustainable design features and products. Since there is not a practical or reliable method for factoring the cost benefits into the project cost analysis at the time of application, there is concern that increased emphasis on cost as a competitive criterion will discourage investments in design, engineering, and materials that require a higher upfront capital investment, but produce savings over time.

Recommendation 7: Develop policies to contain soft costs (Spring 2014)

Commerce will work with stakeholders and other public funders to identify policy changes that can reduce soft costs and the proportion of public funds used to pay for them. Soft costs are non-construction development expenses like engineering architectural and developer fees, site feasibility and permitting, and closing costs.

Basis for the Recommendation

The *Affordable Housing Cost Study* found that development costs for affordable and private market housing tend to be similar, but there are more significant differences in soft costs. While much of this is attributable to regulatory requirements, as noted earlier, there may be other underlying causes as well.

All of the states surveyed limit developer fees, and at least two place limits on professional fees or other soft costs. Commerce currently limits developer fees paid by the Housing Trust Fund, but does not have any other limits on soft costs. Costs are evaluated for reasonableness and may be negotiated with the applicant, but there are no established limits. Other public funders in Washington have practices similar to this, but concerns have been raised about the proportion of funds sometimes paid for project soft costs, and particularly legal and professional fees, such as architecture and engineering. It is recognized as an area for potential cost-savings, but additional work is needed to identify and analyze specific costs, the reasons for their variability, and establish appropriate policies to control them.

Recommendation 8: Develop construction expertise within the Housing Trust Fund staff (Fall 2014)

Commerce will develop additional construction-related expertise to better inform project funding decisions and asset management planning, and to provide technical assistance to project sponsors related to project design, property maintenance, and planning for long-term capital needs.

Basis for the Recommendation

The survey of other states found that capacity is a factor in effectively evaluating project development costs. All seven states interviewed have in-house staff with construction-related expertise in areas such as construction cost estimating, construction project management, or architecture. These staff review proposed construction budgets, plans, and specifications, and visit project sites prior to funding. This allows for a more informed analysis of development costs and helps ensure appropriate investment levels, as well as providing insight into potential risks and opportunities that could either inflate or reduce costs during development. It also allows greater opportunity to influence project planning and design to ensure the quality, durability, and long-term sustainability of projects.

Commerce currently contracts with a third party to provide construction reviews prior to contracting and throughout construction of a project, but does not conduct this level of review prior to awarding funds, and does not have the capacity to conduct this level of review in-house.

Recommendation 9: Document and monitor per-unit and other project cost data over time (2013 and ongoing)

Commerce will document and monitor per-unit costs and other project cost data across funding cycles to evaluate cost trends and refine Housing Trust Fund cost policies as appropriate.

Basis for the Recommendation

The policies proposed in this report are intended to be a first step. It is expected that they will need to be monitored and adjusted over time in order to ensure that they are producing desired results. Commerce will also continue to research other funders’ cost policies and outcomes and refine Housing Trust Fund practices to improve results.

Measures Already Implemented

In response to the *Affordable Housing Cost Study*, stakeholder input, and best practices of other public funders, Commerce has already implemented a number of policies and practices designed to reduce affordable housing development costs, either directly or indirectly.

Housing locator service

A fundamental way to reduce program costs is to address needs through other means and reduce demand on program resources. Commerce recently partnered with the Housing Finance Commission to explore an online housing locator service that will help households locate existing affordable housing units. The city of Seattle and other local jurisdictions have been using a Web-based system that has been a great service for rental property owners and prospective renters. The system enables rental owners to market available units at no cost, and renters can easily search for housing that meets their needs. Commerce has agreed to expand the service statewide and expects to make the service available in early 2013. The website will be available for use by the public at no charge. The system will also provide data regarding the availability of rental units by local area, which will help to determine local capacity to meet demand for affordable housing.

Coordination with other funders

Substantial effort has been made to coordinate with other public funders at various stages of project development and operation, and to align policies and procedures to streamline processes for project sponsors.

- A common application was developed and is shared by several state and local public funders, reducing the time, effort, and expense required of project sponsors to apply to multiple funders. Partners in the development of the Combined Funders Application included King County, city of Seattle, A Regional Coalition for Housing (ARCH), and the Housing Finance Commission.
- Commerce coordinates with other public funders on the timing of application rounds to reduce the time it takes a project to apply for and secure multiple sources of funding. This coordination has reduced application costs, as well as the additional holding costs that can accrue until all funding is secured and development can begin.
- Prior to making awards, Commerce coordinates with other public funders to ensure that information is consistent and there is a common understanding of expectations and priorities. Funders work in partnership to coordinate their resources to address state and local priorities as efficiently and seamlessly as possible.
- After a project has been developed and placed in service, Commerce coordinates with other funders to conduct on-site monitoring, which reduces costs for all of the funders involved. Prior to this coordination, each public funder conducted on-site monitoring independent of other agencies.
- A web-based annual report system (WBARS) was developed in partnership with the Housing Finance Commission and is shared with several local jurisdictions, providing greater efficiency for funders and project sponsors.

Market studies

Applicants to the Housing Trust Fund are required to provide a market study prepared by a professional independent analyst. The market study cannot be not be more than 12 months old and must include the following:

- A detailed project description, including site amenities, unit mix, comparison to market rate projects, comparison to other rent restricted projects (not just tax credit properties), and a precise delineation of the market area.
- Detailed data and description of the market-rate and rent-restricted housing supply and demand, including under-served or specialized low-income markets and vacancy rates specific to the target population of the proposed project, with a conclusion about the proposed project's competitive position.
- A rent gap analysis, including both market rate and rent restricted housing. It must include specific conclusions, supported by data, on both the current and projected market need, the size of the pool of qualified potential residents, the demographic profile of the typical income eligible resident, absorption rate, and the viability of the proposed project as sited.

The market study helps demonstrate that a market exists for the proposed project and that rents are appropriate. This helps ensure that funds are invested in projects that meet an identified need, and that the project will achieve occupancy levels that will support the long-term operation of the project.

Projects addressing special needs not adequately served by the private market are exempted from the market study requirement, such as:

- Projects for people with developmental disabilities or chronic mental illness.
- Emergency shelters for homeless persons or victims of domestic violence.
- Projects for people with chronic substance abuse issues combined with homelessness or other conditions that require intensive support.
- Group foster care.
- Projects on tribal land.
- Seasonal housing for migrant farmworkers.

For projects serving these special needs, applicants must provide other documentation of need, including letters of support from state and local service providers, and consistency with local housing plans.

Appraisals

For every project that involves the acquisition of property, whether or not the Housing Trust Fund is being asked to pay for it, Commerce requires that the application include a current appraisal from a certified appraiser to ensure that the purchase price does not exceed the market value of the property.

Capital needs assessments

In 2011, the Housing Trust Fund began requiring new construction projects to submit a Capital Needs Assessment (CNA) six months post-construction. Prior to that, a CNA was only required in advance of rehabilitation activities. The CNA includes a life cycle and cost analysis showing the long-term life expectancy of building components, typically up to 20 years. It also includes a replacement reserve analysis. For rehabilitation projects, the CNA ensures that proposed rehabilitation is appropriate and necessary, that all necessary measures are being performed, that costs are appropriate, and that the timing of improvements is coordinated to ensure greater cost-efficiency. For new construction projects, it causes project developers to consider and plan for the long-term capital needs of the project in the early phase of project development. This helps encourage more efficient design, as well as maintenance of appropriate reserve levels, which improve the viability of the project over the 40-year term of the Housing Trust Fund contract.

Third-party construction review

After funds are awarded to a project, the Housing Trust Fund uses a third party to review construction plans, specifications, and contracts prior to contract execution to ensure that the proposed work will meet applicable standards and the construction budget is appropriate. As each request for reimbursement is received, the work is inspected and documentation is reviewed to ensure that the billed work is appropriate and has been properly performed. A report and recommendation is provided to Housing Trust Fund staff regarding costs billed, issues identified, potential adjustments to the budget, or the need for additional documentation. Ongoing construction review helps ensure that construction costs are appropriate and unnecessary costs are avoided. Services are contracted because the Housing Trust Fund does not have sufficient capacity and expertise to perform them in-house.

Reduced construction contingency

As recommended in the 2009 *Affordable Housing Cost Study*, the Housing Trust Fund has lowered project costs by easing its construction contingency requirement. In the past, the Housing Trust Fund required a minimum construction contingency of 10 percent for new construction and 15 percent for rehabilitation projects. The contingency was intended to cover unanticipated cost overruns, but projects consistently spent the entire amount. Applicants are now allowed to establish lower contingency levels that are more appropriate to the individual project. The third party construction review includes an assessment of contingency levels prior to contracting to ensure they are appropriate to the project, and the use of contingency funds is monitored throughout development as part of the ongoing construction review.

Savings at project completion

If there are excess funds as a project nears completion, Commerce negotiates with the project sponsor regarding the use of the excess funds. Commerce generally allows remaining Housing Trust Fund dollars to be used for additional project expenses if there is a clear cost benefit to the project, such as installing energy-efficiency measures, upgrading to more durable materials that will reduce replacement costs over time, or capitalizing replacement reserves. If Commerce does not feel there is an appropriate and cost-effective use for the funds, they are returned and made available for other projects. Commerce is working with other public funders to explore ways to incent additional cost savings during development.

Bridge loans

The *Affordable Housing Cost Study* recommended offering bridge loans as a way to reduce interim financing and holding costs for project sponsors. The Housing Trust Fund had piloted offering bridge loans in 2007. Three loans were provided and were paid back in full, with interest, within three years. The concept was thought to be an effective use of funds by Commerce and project sponsors, but the practice was prohibited in subsequent appropriations. Limited funds are available specifically for land acquisition under a separate program administered by the Washington State Housing Finance Commission. The Land Acquisition Program is a revolving loan fund established by the Legislature in 2007 to provide low-interest loans to eligible organizations to purchase land to be developed into affordable housing within eight years.

Efficient design and construction practices

Another recommendation of the *Affordable Housing Cost Study* was to sponsor project management workshops to share best practices related to site selection, project design, and construction management. Commerce partnered with the Housing Development Consortium of King County to establish a design and construction benchmark workgroup. The Efficient and Quality Development workgroup includes nonprofit developers, contractors, architects, and public funders. This effort brings the affordable housing industry together in a collaborative approach to address concerns about the cost of affordable housing and to share best practices with the broader affordable housing community. Members of the workgroup have developed and presented a number of workshops at the annual statewide affordable housing conference, Housing Washington.

Appendix A: Cost-Containment Policies, Practices and Recommendations from Seven State Housing Trust Fund Programs

Prepared for the Washington State Department of Commerce, Housing Trust Fund Program

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Cost-Containment Policies, Practices and Recommendations from Seven State Housing Trust Fund Programs

EXECUTIVE SUMMARY

This report provides a review of seven states' Housing Trust Fund (HTF) programs and their approaches to cost-effectiveness. To gather this information, staff from HTF programs in Illinois, North Carolina, Vermont, Minnesota, Delaware, Ohio and Colorado provided program information and participated in phone interviews with researchers from Washington State University. While the seven programs vary in size and organization, several commonalities emerged:

- Each program valued the flexibility of the funding, which allows them to meet local housing needs. Interviewees noted that HTF projects provide housing for populations with very specific needs and that the projects change in location, size and scope through the years. Because HTFs are intended to meet the needs of low-income and special-needs populations, each state noted that having the ability to use professional judgment to direct the funds to different types of projects is essential to meeting these needs.

- All of the programs had some level of construction expertise on their staff. While there was not specific data to show cost savings achieved as a result of this expertise, each state mentioned that having this expertise resulted in more cost-effective projects being funded.

- All seven states conducted site visits prior to awarding funds. Each state cited anecdotal information about how the site visits resulted in cost savings.

- All of the states have policies in place to limit developer and professional fees as a measure to reduce project costs.

This report provides an overview of the seven states' programs followed by a table summarizing the findings. The conclusions offer several recommendations for next steps:

- *Engage in additional dialogue with other state HTF programs.* This report provides an overview of practices in other selected states. Washington may want to consider following up with some of these states, or additional states, in order to learn more about their practices and consider implementing some of them in Washington.

- *Participate in national housing organizations.* Staff from the HTF programs in most of the seven states mentioned that participating in the national organizations keeps them connected to their colleagues, issues and practices around the nation, which helps them strengthen their own programs.

- *Formalize communications about the Housing Trust Fund.* Many of the cost-containment policies and practices implemented in the other seven states are already in place in Washington's program. Formalizing communication about the cost-effectiveness approaches that Washington's HTF already has in place will highlight the steps that have already been taken to ensure cost effectiveness in Washington's program.

INTRODUCTION

In the 2012 legislative session, HB 2640 directed the Washington State Department of Commerce to develop recommendations for awarding Housing Trust Fund (HTF) resources in a cost-effective manner. To that end, the Department of Commerce convened a sub-committee of the Affordable Housing Advisory Board (AHAB) to review current practices, look at model practices and prepare a response for the Legislature. As part of this process, Commerce contracted with Washington State University (WSU) to analyze HTF programs in other states in order to identify alternative ways to incorporate cost effectiveness into the award process.

CONTEXT

Washington state government has been operating with a severely reduced budget for the last few budget cycles. In an effort to bring spending into line with reduced revenues, legislators have reviewed the state budget to identify areas of potential savings. Rather than making across-the-board cuts, legislators have given specific programs time to review, clarify and improve their practices.

Nationally, HTFs are intended to provide funding for housing for low-income and special-needs populations. The HTF programs in each state are complex and nuanced in the way they award funds and manage their properties. They are intentionally designed to be flexible in order to be responsive to the changing housing needs of communities and to allow for targeted investments for specific populations.

In addition to being cost-effective, HTF projects must meet many different objectives. They must be designed to meet the specific need of the target population, be close to public transportation and other services, meet sustainable building requirements, and be able to remain financially viable over the long-term. Washington's HTF considers cost as one of many factors when evaluating projects for funding, and a number of cost-saving measures have been implemented in the program but no formal process has been established to consistently evaluate cost effectiveness during the award process. For this reason, it has been a challenge for the Department of Commerce to demonstrate how cost effectiveness can be assured when awarding funds to projects.

The focus on cost effectiveness is also a concern beyond Washington state. Low-income housing programs all over the country have been asked these same questions. One participant in these interviews noted that he had "cost-cutting fatigue" from being asked each year to create new ways to implement cost savings. The National Council on State Housing Agencies conducted a nationwide survey on cost-containment policies and practices during the summer of 2012. The survey shows that:

- Cost effectiveness is one of many goals of HTF projects, and
- States are pursuing cost effectiveness in a variety of ways, depending on their state's circumstances.

METHODOLOGY

WSU researchers worked with Department of Commerce staff to design the research protocol and to select the states that would be contacted. Initially, national research on HTF programs across the country identified state programs that may be of interest to Washington state. Mary Brooks, a researcher with the Center for Community Change, was identified as a leading expert on HTF programs across the country.[1] She recommended ten states that may be of interest to Washington because they have comparable programs, very different programs, excellent staff, promising practices, legislative support or a similar urban/rural split.

This list of ten states was presented to the Affordable Housing Advisory Board sub-committee, which suggested removing several of the proposed states and recommended including several other states. Between the two lists, WSU researchers and Commerce staff narrowed the list of participating states to seven: Illinois, Colorado, Vermont, Delaware, North Carolina, Minnesota and Ohio.

To learn about the approach to cost effectiveness in the seven states' HTF programs, WSU combined web research and telephone interviews with HTF experts in each state. An interview protocol was designed based on the questions the Affordable Housing Advisory Board sub-committee and Commerce had about cost-containment efforts underway in other states. The questions were intended to uncover information about states' policies, practices and research that were related to cost containment.

In an effort to put the information in context and test the interview protocol, WSU first conducted an interview with Washington's HTF staff and reviewed related materials that were available online.

Interviews were then conducted by phone with staff from HTF programs in each of the seven states. The interviews were recorded and transcribed for accuracy. (A brief overview of the states' programs is provided on page 20.)

[1] http://housingtrustfundproject.org/wp-content/uploads/2011/10/2010-CFED-report-on-State-Housing-Trust-Funds.pdf

FINDINGS

During the course of the interviews, it became clear that the way that HTFs are funded and administered varies from state to state. Some states use HTFs only for gap funding to complete projects that have already been funded by other sources. Some provide funding only to non-profit developers. In some cases, the HTF is managed by the same agency and staff that manage the Low Income Housing Tax Credit programs; in other cases, the two programs are managed by different agencies. Because each state is organized somewhat differently and the approaches to awarding funds vary, the data collected covered a wide range of issues.

Policies: What specific policies related to cost containment do you apply during the application review and award process?

The complexity of HTFs was evident when discussing policies with the states. While cost containment was a focus, they all mentioned the multiple objectives of HTF projects. For example, all the states had polices related to sustainability, energy efficiency, population to be served and a variety of other factors. Of the seven states surveyed, six had specific cost-containment policies in place.

Their approaches to these policies varied widely (as summarized here in random order).

- **Vermont** indicated that they do not have cost-containment policies with per-unit or per-square foot limits in place because they worry that such a policy may get in the way of other program goals that they deem to be equally or more important than cost. They do, however, have appraisal, bid and procurement policies in place that limit how much can be paid for property using HTFs. Vermont talked about making funding decisions based on the whole HTF portfolio and not getting too bogged down in the details of any one project.

  In an effort to support new projects, Vermont has pre-development and feasibility funds available. By the time a proposal gets to the review stage, HTF staff members are already very familiar with the details of each proposed project. Vermont describes this advance work with developers as one way that staff can advise projects and encourage cost effectiveness.

- **Delaware** requires cost certifications for each proposal. Developers must bid out projects to at least three contractors. Overhead and profit have to be less than 7 percent of the total project costs. Delaware uses a scoring sheet to evaluate proposals. Extra points can be earned by reducing municipal fees such as permits or local taxes.

- **Colorado** has a very prescriptive square footage limit for hard costs and also has ranges for soft costs, all of which are designed to contain costs. The ranges are determined using the Marshall Swift database, a national construction database of costs by region.

- **Ohio** determined that using the ARRA[2] cost certification resulted in increased due diligence and that, as a result, projects achieved some cost savings. Ohio permanently adopted the ARRA cost certification and created a mechanism for sharing cost savings between the HTF and the developer. Savings realized at the completion of a project are split 50/50.

- **Minnesota** conducts a consolidated review process for all funding sources. They require a detailed scope of work, including architectural requirements. An on-staff architect reviews each proposal and compares it to current market costs for materials and labor. They also use a very detailed predictive model to evaluate proposal budgets (described further on page 8).

- **North Carolina**'s cost-effectiveness policy comes in the form of a cost limit. They have identified one line item that comprises all the hard costs of the project. That one line item is $60,000. While it is possible that a project that came in over that amount may be funded, that would be rare since the cost limit is worth so many points on the score sheet.

- **Illinois**' HTF money is used as a gap-filler for projects that are supported with other funding sources. They focus on the projects that offer the highest benefit to the lowest-income households. Their objective is to address the needs of the working homeless and to prevent homelessness. The policy is that 51 percent of the units funded with HTF dollars must address households at or below 50 percent of the area's median income.

  Illinois has no application deadlines, accepting project applications on a rolling basis. This is another approach to giving the projects and staff enough time to work together to ensure that projects are cost effective before they get to the review process.

All seven states expressed an ongoing interest in ensuring that developer and professional fees were a reasonable and worthwhile investment of HTF resources. North Carolina expressed a preference for a per-unit fee for developers as opposed to a percentage of the total project because they believe that the project percentage approach may inadvertently provide an incentive for building larger project budgets or may reward inefficient unit production.

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[2] American Recovery and Reinvestment Act of 2009

All of the states had some mechanism in place for ensuring that developer fees remain reasonable for the scope of each project. While the approaches vary, they were all developed in conjunction with the stakeholders in each state in an effort to be good stewards of the funds.

States limit developer fees in several ways. For example:

- **Illinois** developer fees can only be 12 percent of the total project cost.
- **North Carolina** developers can charge up to $12,000 per unit.
- **Ohio** caps professional fees (including developer fees) at 20 percent of the total project cost.

Incentives for cost savings: Does your program provide any incentives for cost savings?

In North Carolina and Colorado, the program's cost limits are so prescribed that additional incentives for savings are not part of the process. Proposals that do not adhere to the cost limits are simply not eligible for funding. Incentives vary in the other five states:

- **Ohio** projects that can demonstrate cost savings upon completion can share the savings with the HTF. The money is then redistributed to another HTF project.

- **Delaware** uses a score sheet to evaluate projects. Proposals that show savings in municipal fees, such as permitting or local taxes, can earn additional points on the score sheet.

- **Vermont** has considered but elected to not put cost-savings incentives in place. While they take cost into account, they expressed a concern that an over-emphasis on cost savings would get in the way of meeting the other program goals that are in place. After successfully running their program for 25 years, a 2008 Cost Study in Vermont noted, "…Vermont's development costs are in line with the average prices experienced throughout the New England region during the study time period. When individual prices exceed the average, it is often due to attractive cost/benefit tradeoffs."[3]

- **Minnesota** encourages projects to leverage other funding sources and seek contributions from partners such as local municipalities.

- **Illinois** encourages projects to leverage funds from other sources and gives preference to projects with the highest benefit for the lowest-income households.

[3] Santucci, R.M. Urban Renovation Consultants, Inc., *A Comparison of Costs in Vermont Multifamily Developments to U.S., Northeast States & Vermont Case Studies: A Selected Review* February 2008.

Cost limits: If your agency/program has a cost limit, what is it and how was it determined?

All but one of the states interviewed implement specific cost limits for specific line items. Of these, Delaware and North Carolina also set minimum costs for rehabilitation projects in an effort to ensure that they are funding rehabilitation projects that are big enough to have an impact. For example, they do not want to fund projects that are simply asking to redo the floors and replace the furnace because they know they have buildings and tenants with greater needs, such as plumbing, roofing and electrical work. In a policy they referred to as “Worst First,” North Carolina provides an incentive for more expensive rehab projects because those tend to be the situations where people are living in the worst conditions.

- **Colorado** has established a cost limit range, including hard and soft costs, of $135 - $210 per square foot.

- **Delaware** has established cost limits of $45,000 per unit, with a total project limit of $2.7 million.

- **Ohio** limits all professional fees (attorneys, architects, developers, etc.) to 20 percent of the total project cost. Ohio also has an annual goal for unit production that is bumped up each year.

- **North Carolina** has established one specific line item that includes all hard costs, but excludes soft costs such as site improvements, legal fees and construction interest. Projects that exceed the $60,000 limit for that line item are very rarely funded. The exceptions are for single family or duplex design, downtown locations, public housing redevelopment, or using steel and concrete construction. Such projects have a line-item limit of $71,000 per unit.

- The most elaborate model was described by **Minnesota**, which evaluates projects using a predictive cost model[4] based on previous years’ costs. Using this model, they establish cost limits each year. Initially, those costs were 22 percent above comparable projects funded by other sources. The cost limit was established at that level during the first year using this model and has been

[4] The predictive model is a linear regression analysis that models total development costs for projects completed between 2003 and 2011 (adjusted for inflation). The model measures the individual effect that a set of explanatory variables (building type, building characteristics, project size, project location, etc.) have on costs while holding all other explanatory variables constant. For example, it measures the effect that building location (Twin Cities metro versus greater Minnesota) has on total development costs, assuming that the exact same building is built in both locations, which requires that building type, building characteristics and project size be held constant. In the end, the model predicts the total development costs of a proposed development based on its characteristics. Developers know that their costs will be compared to the predictive cost model but the cost model amounts are not published.

stepped down each year thereafter. Project limits are now only 16 percent above comparable projects – a 6 percent reduction in project costs.

The ways that states describe and set their cost limits vary. Two states set specific per-unit limits ($45,000 in **Delaware**, with a total project limit of $2.75 million, and $60,000 in **North Carolina**). In these two cases, the limits are firm and only rarely are projects that fall outside of these limits funded.

Ohio ensures that projects are not over-subsidized by limiting the debt service coverage ratio (DSCR) to 1.15 – 1.3.[5]

Illinois describes their cost limits like this: Limits are based on average cost per unit by number of bedrooms.[6] Total hard costs include site work, trade payments, general conditions, contractor overhead, contractor profit, payment and performance bond fee, and permit fees. They do not have a total project cost limit inclusive of soft costs. Other fee limits include a developer fee not to exceed 12 percent of total project cost and contractor general conditions, and profit and overhead not to exceed 14 percent of trade payments and site work.

Vermont does not set specific cost limits because they consider that the complexity of the program and the projects call for a case-by-case analysis. They also mentioned concern that setting cost limits can inadvertently push support toward low-cost projects and that projects tend to take the pre-set limits and simply build their budgets to meet that limit regardless of the actual costs. North Carolina supported this by noting that, because their cost limit is $60,000, most project budgets come in at $59,900.

Cost calculations: What factors are included in your cost calculation? What is excluded?

In conversations about cost effectiveness, there is concern about which costs are being compared. Because HTF projects vary so much in size, scope and location, it is

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[5] DSCR is a ratio of cash available to service the debt incurred. This measure is used in commercial real estate as well as personal and commercial finance. A DSCR over 1 indicates that the entity generates enough cash to pay its debt obligations.

[6] Cost limits in the Illinois HTF program:

Bedrooms	Average Cost Limit
0	*$139,177*
1	*$159,994*
2	*$193,772*
3	*$249,391*
4+	*$275,728*

important to understand which costs are included when making comparisons among projects. Five of the seven states evaluate projects' costs using methodology that is based on the total project cost:

- **Vermont** takes the total project cost and calculates a per-unit cost.
- **Delaware** and **Colorado** calculate a square-footage cost.
- **Minnesota** and **Ohio** simply look at the total cost of the projects.

Illinois evaluates their projects' costs without including land acquisition costs, and sometimes labor costs are removed because they vary depending on whether the project is paying union scale or not. Illinois intentionally compares projects to other comparable proposals. They also look for projects that leverage other funding sources and aim to provide the highest benefit to very low-income households.

North Carolina created one budget line item that includes all the construction hard costs and uses that single line item to evaluate projects.

Cost drivers: What do you consider to be the most significant factors driving increases (or decreases) in development costs?

Among the seven states surveyed, there was no consensus about what specific items were driving up project costs. For every state that mentioned that property prices were rising, another mentioned that land prices were flat, or even that existing buildings are less expensive now so rehab projects are now more affordable. Several states described how the labor costs varied depending on if projects were unionized and adhering to Davis-Bacon or state standards, or were meeting some other wage criteria. One state mentioned that because projects are getting more complex and involve more funding sources than ever, legal fees have risen. Another mentioned that the cost of relocating tenants during a rehab project had increased.

One factor that all seven states mentioned is the change in local municipalities' ability to help with low-income projects. Cities and counties used to be in a position to waive fees or even donate land. Now, developers are noting that they are increasingly hesitant to even ask for such special consideration because city budgets have been so tight.

Long-term Operations and Maintenance (O&M): How are O&M costs factored into the decision-making process?

All seven states carefully scrutinize the approach that projects propose for the long-term O&M of their buildings. They all require a plan that demonstrates the reserves and cash flow needed to support the O&M for each project for 15 to 20 years. Two states require completed projects to report their O&M expenses monthly. All states require an annual report and, uniquely, Illinois conducts annual site visits to all the buildings in their portfolio.

Even though all of these projects are built with the long-term in mind, forecasting all the potential expenses can be challenging. As the interviewee from North Carolina noted, "After about five years, the crystal ball becomes a bowling ball." This is why North Carolina requires on-going reporting and site visits. The initial application process always includes a review of the quality of the materials to be used. This is important because of the focus on keeping the buildings operational so far into the future.

All seven states discussed the balancing act that is required when trying to reduce costs and also use durable materials, meet green standards, and customize the construction to meet the needs of specific populations. All of the states indicated that their agency and their boards continue to agree that these other objectives are at least equal in importance to cost savings. Only North Carolina mentioned that they are not increasing their requirements for green building practices this year because of the upfront investment required.

Evaluation: Have you evaluated the results of your cost-containment policy?

The seven states each had a variety of approaches to cost containment, but not one had systematically evaluated their program such that they could prove that specific actions result in specific savings. In some cases, their policies have been in place so long that there is not the "before" data that would be needed to do a comparison study. In other cases, the policy or limit is so new that data is not yet available.

All seven states conduct site visits before awarding funds to ensure that the proposed expenditures are reasonable. Interview participants repeatedly mentioned project amendments, improvements and savings that resulted from having staff out on the project sites both before awarding funds and while construction was underway. While they anecdotally state that this practice results in cost savings, there is not a formal study with data to support this assertion.

Delaware is currently conducting a cost-containment study. Colorado is evaluating the cost savings resulting from reduced demand on other social services when low-income housing is available. Both studies will be available in fall 2012. Meanwhile, evaluation activities by the other states have led to improvements and the implementation of new practices.

- **Vermont** maintains cost data for all projects funded during its 25 years of operations. The data is maintained in uniform categories which permits analysis of trends by category (construction, acquisition, soft costs, fees, and reserves) on a per unit, per square foot and project type basis. VHCB has periodically contracted with national consultants to evaluate the reasonableness of its costs and make recommendations for improvements. Recently, they contracted with national consultants to evaluate their existing building stock. The consultants concluded that Vermont had not required enough money for O&M. HTF projects target low-income and special-needs populations, which can restrict rental income that could go toward ongoing O&M. The study found that Vermont's buildings were in decline and many needed rehabilitation work, which prompted the state to recognize that more up-front investment in quality materials can save money in the long run. They are now requiring more money in reserve for O&M at the outset of a project, and more follow-up once the project is completed. Vermont is very concerned that there are adequate capital reserves for multifamily projects. They maintain minimum reserve for replacement requirements and with other agencies in the state have adopted an Asset Management/Capital Needs Assessment policy for funded projects.
- **Delaware** has projects submit their operating budgets annually. Then they use that data to compare and evaluate the projects and offer suggestions for savings. Insurance is one example of a cost that they have found varies greatly between projects. HTF staff can help projects realize savings by sharing how other projects are managing the same issues.

- **Illinois** now accepts preliminary applications that briefly describe the location and scope of the project. If a project passes the initial screening, the developer is invited to come back with a full proposal that includes all the budget details. This change has reduced staff costs for evaluations and reduced developers' costs because they are only working on proposals that have a chance to be funded. Illinois also cites savings from having staff with construction expertise visit the building sites as the project is being built so they can evaluate changes that are being considered. They have been able to spot and stop questionable construction practices.

- **Colorado** is assessing the savings that low-income housing can provide by helping to reduce other social costs that are associated with inadequate housing, such as costs for corrections and mental health support. They have five pilot projects underway, one of which includes respite care in the housing unit. The study will be available in late fall 2012.

Housing needs assessment: Has your state done a comprehensive housing needs assessment in the last 10 years?

Four of the seven states interviewed have completed a comprehensive housing needs assessment in the last 10 years.

Both Vermont and Delaware have recently conducted comprehensive housing needs assessments. Each year, Colorado tracks the number of households that earn less than $20,000 annually and how much of that income goes toward rent. If a household is paying 35 percent or more of their income for housing, they are identified as a target for HTF housing. Colorado currently has 146,000 families who meet these criteria. Quarterly, Colorado surveys the rents and vacancies of 160,000 market-rate rental units in the state. The data is used by the entire housing industry in an effort to not over- or under-build rental units.

While Minnesota has not conducted a formal assessment, they do scan the housing landscape every six months. A person on staff with GIS expertise has created a map tool using 24 housing indicators from county and census data. The tool allows users to overlay maps with income, job and transportation data in order to see where the housing needs are. They have geocoded every HTF investment made so that legislators can easily see projects in their districts.

Those who have not conducted an assessment recently indicated either that another agency had done the work or that they had done such assessments previously and did not find them to be useful in the HTF world. All agreed that, inevitably, housing needs assessments illustrate that there is more need for low-income housing than can ever be met by the resources available through this program.

States' feedback to these interview questions is summarized in Table 1.

Table 1. Summary of Feedback from HTF Teams Interviewed

	Illinois	Vermont	Delaware	Colorado	Ohio	North Carolina	Minnesota
Construction Expertise on Staff	x	x	x	x	x	x	x
Conduct site visits prior to funding	x	x	x	x	x	x	x
Limit Developer Fees	x	x	x	x	x	x	x
Have specific cost limits in place	Yes – per-unit cost based on number of bedrooms	No	Yes – $45K per unit, total project cost $2.75M $30K per unit minimum for rehab projects Overhead and profit must be less than 7 percent	Yes – $135 to $210 per sq ft (includes hard and soft costs) Use debt-coverage ratio of 1.15 – 1.3 to determine appropriateness of budget	Yes - All professional fees capped at 20 percent of project cost	Yes - $60,000 per unit, excluding soft costs Total cost per unit cannot exceed $120,000	Yes – Use predictive cost model to evaluate proposals
Have cost-containment policy in place	No – The Illinois fund is used for gap funding, They give preference to projects that benefit the lowest-income households.	No	Yes – Additional points awarded for reducing municipal fees Cost certifications required for each proposal Developers must bid project out to 3 contractors	Yes – Set rates using Marshall-Swift database	Yes - Require ARRA-enhanced cost certification at project completion Points awarded for local tax abatements Savings achieved are split between project and the HTF program	Yes – Created one line item that includes all hard costs and sets $60K limit for that line Not increasing green standards in 2013 in effort to reduce costs	Yes – Policy uses predictive cost model to reduce project costs compared to private sector projects Policy has reduced overage from 22 percent to 16 percent

	Illinois	Vermont	Delaware	Colorado	Ohio	North Carolina	Minnesota
Unique Feature	There are no deadlines for applications; they are accepted all year long	Provides pre-development and feasibility funding for most projects	The governor in Delaware is very supportive of the HTF program because of the economic benefits They estimate that every $1 invested in HTF projects results in $7 of economic activity Delaware hold the O&M reserves for all the projects	Colorado has 5 pilot projects underway with a goal to measure the cost savings realized in other social programs (corrections, Medicaid, etc.) by providing adequate housing to vulnerable populations	Requires that all projects meet the Universal Design criteria, which causes more upfront investment but works well over the life of the project Adopted the enhanced cost certification process that was required by ARRA	Intentionally keeping green requirements to a minimum to hold down costs	Every HTF project funded in the last 10 years has been geocoded so that legislators can see a map of projects in their districts

Conclusions

While the approach and organization of HTF programs varied across the seven states, several policies and staffing practices were common across these states.

Staffing and site visits

Most notably, all seven states have staff members with construction expertise (including architects, engineers, project managers and permitting specialists) who conduct visits to each site before awards are made. While not yet supported with concrete evidence, each state mentioned savings that were realized as a result of having these staff in the field. States also noted that these site visits resulted in amendments being made to plans and gave staff a better understanding of each project, which was said to result in cost savings.

One fact that emerged from the interviews is that HTF staff members tend to have many years of experience. The person interviewed with the least amount of experience had been with the program for ten years. Others had closer to 20 years of experience. This suggests a deep knowledge of – and commitment to – the HTF program in organizations across the country.

Cost effectiveness: one of many goals

Each state is working to achieve a balance between cost effectiveness and a range of other goals that have been deemed essential. All interviewees noted that the HTF projects have impact precisely because of the flexibility of the funds. This flexibility allows staff to direct funds to projects that serve specific populations and meet the changing housing needs in their states. HTF projects appear to be filling a need and serving a specific niche in the market (low-income and special-needs populations) that would not otherwise be served. While each of the seven states had cost effectiveness on their agenda, it did not often rise to the top of their lists of priorities because of the other objectives the program seeks to address.

Recommended Next Steps

Engage in additional dialogue with other states

Several states had unique approaches to cost containment, such as creating one line item for comparison or creating a cost-prediction model. If the HTF community in Washington state finds ideas in this report that may be applicable here, it would be useful for Commerce staff to talk directly with staff from those states that were interviewed. Because of the complexity of the funds and the variety of ways they are managed, it would be useful for Washington HTF staff to invite staff with HTF expertise in these other states to share their insights.

Participate in national HTF organizations

The Department of Commerce may also want to consider getting involved with the national housing organizations to keep current with the approaches that are being used successfully around the country. Most other states mentioned the value of having colleagues in other states to consult with and learn from, given that the HTF communities face similar issues yet are taking different approaches to effectively implement the program.

Formalize HTF communications

Many of the suggestions from other states, such as setting a goal of the number of units to be built annually, dedicating money to specific regions of the state, limiting developer fees and building with long-term sustainability in mind, are already in place in Washington state. Yet, it appears that the underlying procedure for awarding funds and the professional judgment that is used to make funding decisions have not yet been clearly communicated to the Washington public. The Department of Commerce may consider formalizing and communicating the many good practices that are already in place.

Summary of Housing Trust Funds Programs in Seven Participating States[7]

State	Type of Program	Revenue Source	Size of Program	Start Date/Agency
Illinois	Affordable Housing Trust Fund	Real Estate Transfer Fee	FY11 $18.9 million	1989 / Housing Development Authority
Vermont	Housing and Conservation Trust	Real Estate Transfer Tax; general Fund	FY11: $6+ million to support 392 units.	1987 / Housing and Conservation Board
Delaware	HTF	Document Recording Fee and General Fund	$4.5M in 2010, $18 M in 2012	1986 / State Housing Authority
Colorado	Housing Development grant fund	State appropriation, allocated annually	About 50 projects annually; Funds used to fill gaps in projects funded by other sources	Colorado Division of Housing
Ohio	HTF	Document recording fees	$44.1 million in FY11	1991 / Department of Development
North Carolina	HTF	General fund appropriation	$9.5M in 2010	1987 / Housing Finance Agency
Minnesota	HTF	General fund; interest on bonds application fees; interest on real estate brokers' trust account	$134M in 2012 (doubled since 2011 due to Housing Infrastructure bonding bill); 3,100 units	1988 / Minnesota Housing

[7]Sources provide varying information about state programs. This table created with data from: National Housing Trust http://nhtinc.org/state_and_local_preservation_resources.php , http://www.mnhousing.gov/news/index.aspx and The Center for Community Change http://housingtrustfundproject.org/

Washington	HTF	Document recording fee	$50 M in 2012; 4,500 units each biennium	1987 / Department of Commerce