



RETHINK HOUSING

INNOVATING A NEW APPROACH
TO AFFORDABLE HOUSING

OCTOBER 2019

MADE POSSIBLE
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Executive Summary

Affordable Housing is Fundamental to Equity & Prosperity

There is an affordable housing crisis in the U.S. – a shortage of more than 7.2 million affordable and available rental homes for the 11 million low-income renter households in this country. This crisis disproportionately impacts the most vulnerable including extremely low-income renter households who are more likely to include people of color, children, seniors, and individuals with disabilities. The impact to Black households is particularly devastating, exacerbating the existing racial wealth gap and impeding upward mobility. This can lead to poor health outcomes, less educational attainment, and lower lifetime earnings, particularly for children and those already most vulnerable. These poor outcomes impact not only the households affected by housing instability and the communities they live in, but the nation as a whole. While there is a shortage of affordable and available rental homes in every state and major metropolitan area across the nation, especially for extremely low-income households, the crisis is particularly acute in California and especially Los Angeles.

Innovative Approaches are Needed to Eliminate the Shortage

Affordable housing development and operation is premised on balancing a simple equation: the cost to build and operate the affordable housing must be less than or equal to the expected rent to be collected from the housing over time. Unfortunately, current approaches to affordable housing development often result in a significant financing gap – it costs more to build and operate than the rent which can be collected, especially

while maintaining affordability and quality for target tenants. This gap is typically filled by both supply-side and demand-side subsidies, the most common of which are Low-Income Housing Tax Credits (LIHTC) and Section 8 Housing Choice Vouchers (Vouchers). However, while these subsidies are critically necessary in closing the gap, they are insufficient in meeting the escalating need for affordable housing. These resources are scarce, securing them is highly competitive, and the total current allocation of LIHTCs and Vouchers is inadequate to build enough affordable housing to address the existing need. New approaches to affordable housing development and operation are needed to close the gap and address the critical shortage of affordable rental housing.

RETHINK Housing is Innovating a New Approach

The RETHINK Housing model aims to build more housing units, at lower cost, in less time, while relying less on a limited capital subsidy like LIHTCs and Vouchers and more on project financing from market-based financing sources. To achieve this, the model uses six key levers to dial down the time and cost of development, thereby shrinking the financing gap, altering the nature of subsidy needed, and as a result, increasing the speed and volume of production. The six key levers employed in the RETHINK model include 1. a coordinated team approach, 2. smaller site selection, 3. low/no cost acquisition, 4. efficient design, 5. “by-right” development, and 6. simplified financing. There are currently 10 RETHINK pilot projects underway at various stages of acquisition and development across Los Angeles.

The three that are furthest along are showing promise in terms of reducing costs and time to develop while relying on less capital subsidy. Among those, the average cost per unit to develop is \$180,000 versus \$531,373 for LIHTC projects while the average capital subsidy required is \$64,000 per unit versus \$450,000 for LIHTC projects (see Figure 3). In addition, the three projects that are furthest along are also showing promise in terms of reducing the total time to develop – approximately 26 months versus 42 to 60 months for LIHTC projects (see Figure 6).

Barriers Must be Removed and Assets Leveraged to Scale & Replicate Innovative Approaches

While the housing crisis is the same across the country – every state has a shortage of affordable rental housing for the lowest income renters - how an innovative approach like RETHINK Housing can be used as a tool to address that crisis must be tailored to each community and its particular barriers and assets. In order to scale and replicate the model, barriers to the effective application of the RETHINK levers must be removed while at the same time leveraging the assets that can facilitate their application.

Recommendations for removing barriers include:

- 1. Simplify the process** and reduce the amount of time it takes to find sites that are conducive to affordable housing development.
- 2. Reduce the time and cost** of property acquisition.
- 3. Reduce the bureaucracy and inefficiency** in government operations, particularly local planning and approval processes.
- 4. Expand access to new sources of stable, flexible rental subsidies** that can facilitate the use of market-based financing options in the development of affordable housing.

Recommendations for leveraging assets include:

- 1. Engage philanthropy** - they can play a pivotal role by being an early adopter and risk taker in piloting new models and approaches.
- 2. Engage state & local government agencies** - they can be valuable assets in creating policy environments and by providing large, flexible pools of capital from unexpected sources that can help take innovative new approaches to scale.
- 3. Partner with community-based organizations** - such as churches and social service agencies - they can be invaluable partners in facilitating the identification of sites, organizing and exerting influence over policymakers - pushing them to create the necessary enabling policy environment - and can ensure that projects are designed to best meet the needs of the community in which they are located.
- 4. Don't forget about the private sector** - Developers can RETHINK the size and scale of projects. Capital providers can RETHINK how they approach underwriting. Hospitals, healthcare systems and others can begin to think more broadly about affordable housing as health in order to best serve the most vulnerable. Faith-based organizations can think about their real estate and financial resources as assets to be leveraged in meeting local affordable housing needs.

Affordable Housing: Fundamental To Equity & Prosperity

The U.S. Housing Crisis Disproportionately Impacts the Most Vulnerable

There is a severe shortage of affordable rental housing across the U.S. leading to countless Americans experiencing severe housing cost burden. This is contributing to the burgeoning homeless epidemic – forcing many to become homeless and putting a growing number at risk of becoming homeless. For those with the most limited resources, they must at times choose between paying for rent or paying for food and healthcare.

There are 43.8 million renter households in the U.S., of which 11.2 million are extremely low-income. This represents 25.7% of all renter households and 9.5% of all households in the U.S. This group of Americans has available only 35 affordable rental homes for every 100 households – a shortage of more than 7.2 million affordable and available rental homes for extremely low-income households.¹

The cost burden is crushing, particularly for the lowest income households, though the burden is borne across the income scale; 71% of extremely low-income, 32% of very low-income, 8% of low-income and 2.3% of middle-income renter households are severely cost-burdened, spending more than half

their income on rent and utilities.² This burden has significant ramifications for both the households bearing it and the communities in which they live. A recent study found that when housing prices force households to spend more than 32% of their income on rent, those communities experience rapid increases in homelessness.³

Box 1: Definitions

AREA MEDIAN INCOME (AMI): The median family incomes in the metropolitan or nonmetropolitan area

EXTREMELY LOW-INCOME (ELI): Households with incomes at or below the Poverty Guideline or 30% of AMI, whichever is higher

VERY LOW-INCOME (VLI): Households with incomes between ELI and 50% of AMI

LOW-INCOME (LI): Households with incomes between 51% and 80% of AMI

MIDDLE-INCOME (MI): Households with incomes between 81% and 100% of AMI

COST BURDEN: Spending more than 30% of household income on housing costs

SEVERE COST BURDEN: Spending more than 50% of household income on housing costs

^{1,2} Source: National Low-Income Housing Coalition, "The Gap: A Shortage of Affordable Homes." March 2018.

³ Source: Zillow Economic Research, "Priced Out: Rising Rent and Homelessness Across America." An analysis by Zillow Research Fellow Chris Glynn of the University of New Hampshire, Thomas Byrne of Boston University and Dennis Culhane of the University of Pennsylvania.

The crisis disproportionately impacts the most vulnerable - extremely low-income renter households who are more likely to include people of color,⁴ children, seniors, and individuals with disabilities. For example, 35% of Black and 29% of Hispanic renter households are extremely low-income versus 21% of White renter households; a result of a variety of racial wealth and income disparities. For Black and Latinx households in the U.S., rent accounts for approximately 50% of household income with many Black Americans paying twice as much for rent as white households.⁵ This perpetuates the racial wealth gap that stems from American slavery and continues to impede upward mobility for Black Americans.

Housing Impacts Health, Education, and Economic Outcomes

Housing instability and homelessness can lead to poor health outcomes, less educational attainment, and lower lifetime earnings, particularly for children and those already most vulnerable.

Health Outcomes

Poor quality and inadequate housing contribute to health problems like chronic disease and injury as well as negatively impact childhood development.⁶ For example, water leaks, poor ventilation, dirty carpets and pest infestation are examples of poor quality, inadequate housing that can lead to an increase in allergens like mold and mites which result in a higher incidence of asthma.

Homelessness also contributes to poor health outcomes and higher rates of hospitalization and emergency room utilization. Individuals who lack housing have higher rates of hospitalizations for physical illness, mental illness, and substance abuse

than other populations. People without homes have higher rates of tuberculosis, hypertension, asthma, diabetes, and HIV/AIDS. In addition, rates of mental illness among the homeless are twice the rate found in the general population.⁷

The higher rate of hospitalizations and emergency room utilization by homeless patients, coupled with the complexity of their clinical conditions, places a significant financial burden on the hospitals and health systems that serve them. One Chicago hospital points out that the cost to serve their homeless patients can be 70 times higher than for other patients.⁸ The problem is so severe that hospitals across the country are investing hundreds of millions of dollars into housing projects based on research findings that it is more cost-effective to provide housing with supports than it is to have these individuals cycle in and out of emergency rooms and in-patient stays.⁹

Box 2: Health Systems Investing in Housing

In early 2019, the Center for Community Investment (CCI) at the Lincoln Institute for Land Policy in Cambridge, Massachusetts, launched an initiative called Accelerating Investments for Healthy Communities. The initiative is designed to help health systems and hospitals marshal resources to increase affordable housing in the communities they serve. Participants include:

- ✓ **Bon Secours Mercy Health** Cincinnati, OH
- ✓ **Boston Medical Center** Boston, MA
- ✓ **Dignity Health** Oakland, CA
- ✓ **Children's Hospital** Columbus, OH
- ✓ **UPMC** Pittsburgh, PA

Source: HealthLeaders, "How 6 Major Health Systems and Hospitals Hope to Boost Housing." March 4, 2019.

⁴ Source: Greater Washington, "Who's hit hardest by the affordable housing shortage?" January 10, 2019.

⁵ Source: Shelterforce: The Voice of Community Development, "Just as I Suspected, Paying Rent is Racist." July 26, 2017.

⁶ Source: Robert Wood Johnson, "How Does Housing Affect Health." May 1, 2011.

⁷ Source: American Psychological Association, "Health & Homelessness."

⁸ Source: NPR, "ER Use Goes Down As Hospital Program Pays Homeless People's Rent." January 30, 2018.

⁹ Source: Healthcare Finance, "Hospitals Invest in Housing for Homeless to Reduce ER Visits." October 18, 2017.

Education Outcomes

There are multiple ways that housing instability and homelessness impacts education outcomes including lower kindergarten readiness, lower academic proficiency, lower likelihood of high school graduation and lower educational attainment by age 25.¹⁰

These outcomes are the result of challenging conditions in the home, frequent moves, and multiple school changes caused by housing instability. Living in environments that are overcrowded and unsanitary create significant obstacles to learning. A child living in an overcrowded shelter may not have a place to complete homework and may experience noise and chaos that interferes with her ability to complete assignments. A child living in unsanitary housing conditions - exposure to infestations of cockroaches, mice, mold and/or lead - may suffer from higher rates of asthma or developmental delays leading to higher rates of absenteeism, lower attentiveness in the classroom and ultimately lower educational outcomes. Moreover, students who move often, frequently changing schools, have been found to lag nonmobile students by a year or more in math and reading because they constantly have to catch up and adapt to new curriculum and teachers, as well as make up work covered previously in the school year.¹¹

Economic Outcomes

Affordable housing improves economic mobility, reduces poverty and homelessness, and strengthens the local and national economy. It helps families, and especially children, climb the economic ladder. Research has shown that economic outcomes as an adult are significantly improved the earlier in life an individual moves into a more stable and resourced community. In fact, one study of upward economic mobility for children found that adult earnings increased more than 30% when that individual was able to move into a lower poverty neighborhood before the age of 13.¹²

Access to affordable housing also helps to reduce poverty and the likelihood of homelessness. When families experience housing cost burdens, especially extremely low-income households, they struggle to pay for food, transportation, medical care, and other basic needs while families in affordable housing can spend nearly five times as much on healthcare, a third more on food, twice as much on retirement savings and can pay down debt, and/or save for college.¹³ The struggle to pay for basic needs impacts an individual's health and their ability to obtain stable employment, keeping them in poverty and putting them at greater risk for homelessness. In fact, a HUD study showed that long-term housing subsidies reduced the number of homeless or doubled-up families by 50%.¹⁴ In addition, an analysis of Census data showed that housing assistance raised 4 million people out of poverty in 2012 (including 1.5 million children).¹⁵

Finally, access to affordable housing helps to strengthen the local and national economy - it creates jobs, boosts family incomes, and encourages additional development. It also benefits local business through increased patronage by new neighborhood customers. In fact, the National Association of Home Builders estimates that building 100 affordable rental homes generates \$11.7 million in local income, \$2.2 million in taxes and other local government revenue, and creates 161 local jobs in the first year alone.¹⁶ Affordable housing also strengthens the national economy. When families are burdened by housing costs, their ability to increase earnings is constrained causing slower GDP growth. Researchers estimate that during the period from 1964 to 2009, GDP would have been 13.5% higher, leading to a \$1.7 trillion increase in total income.¹⁷ To put that in perspective, that is more than the 2017 annual GDP of 167 out of 185 countries listed by the World Bank.¹⁸

¹⁰ Source: How Housing Matters, "How Housing Can Determine Educational, Health, and Economic Outcomes." September 19, 2018.

¹¹ Source: Urban Institute - What Works Collaborative, "Housing as a Platform for Improving Education Outcomes among Low-Income Children." Mary Cunningham and Graham MacDonald. May 2012.

¹² Source: Chetty, Raj, Nathaniel Hendren, and Lawrence F. Katz. 2016. "The Effects of Exposure to Better Neighborhoods on Children: New Evidence from the Moving to Opportunity Experiment." *American Economic Review*, 106 (4): 855-902.

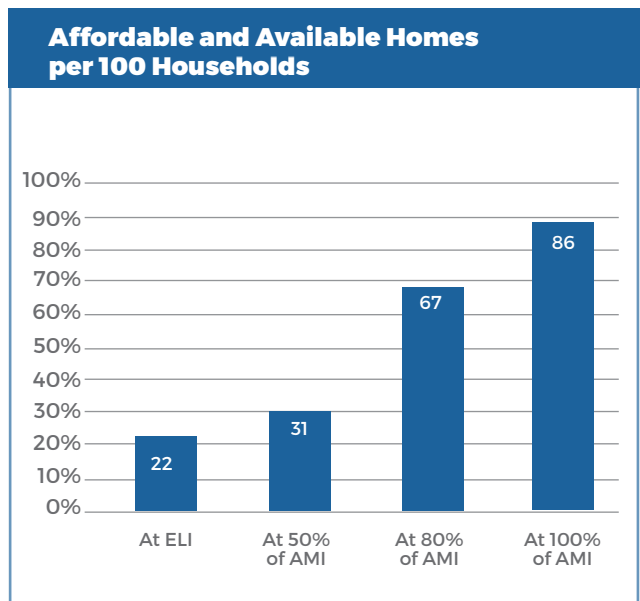
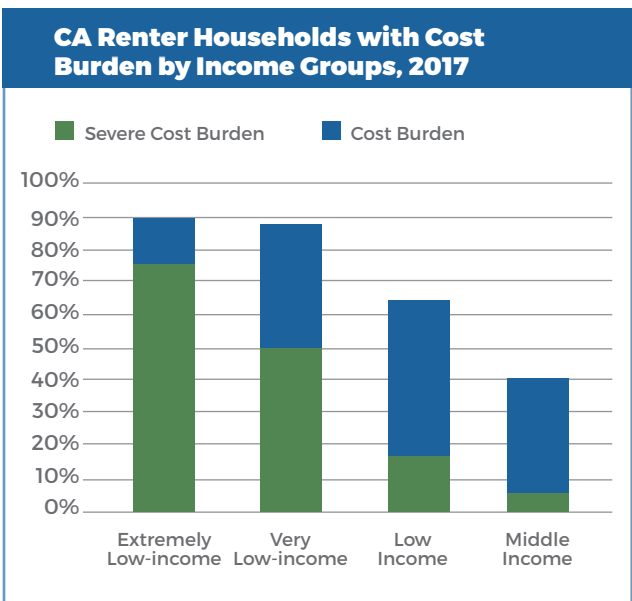
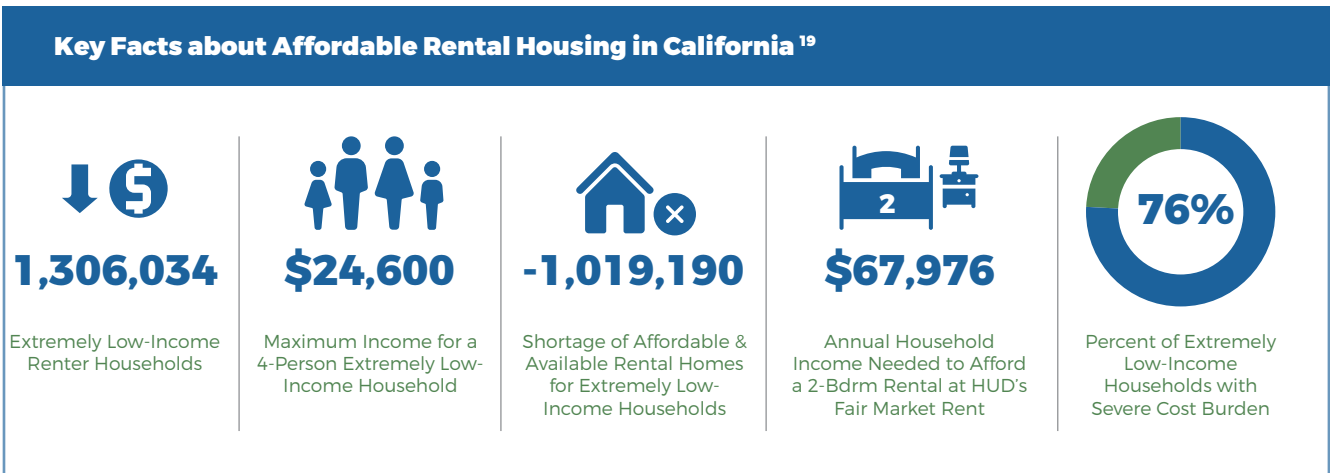
¹³⁻¹⁷ Source: A Place to Call Home: The Case for Increased Federal Investments in Affordable Housing.

¹⁸ [https://en.wikipedia.org/wiki/List_of_countries_by_GDP_\(PPP\)](https://en.wikipedia.org/wiki/List_of_countries_by_GDP_(PPP))

Acute Housing Shortage - A Spotlight on California and Los Angeles

While there is a shortage of rental homes affordable and available to extremely low-income people across the country, the problem is particularly acute in California where high housing costs are coupled with disproportionately low incomes. California needs 1.4 million more affordable rental units - there are only 22 affordable and available rental homes for every

100 extremely low-income households. This is behind only Nevada which has a ratio of 15 to 100. The majority of extremely low-income renter households are also severely cost burdened in every state, though again, California ranks among the highest burden with 77%, after only Nevada (80%), and Florida (79%).

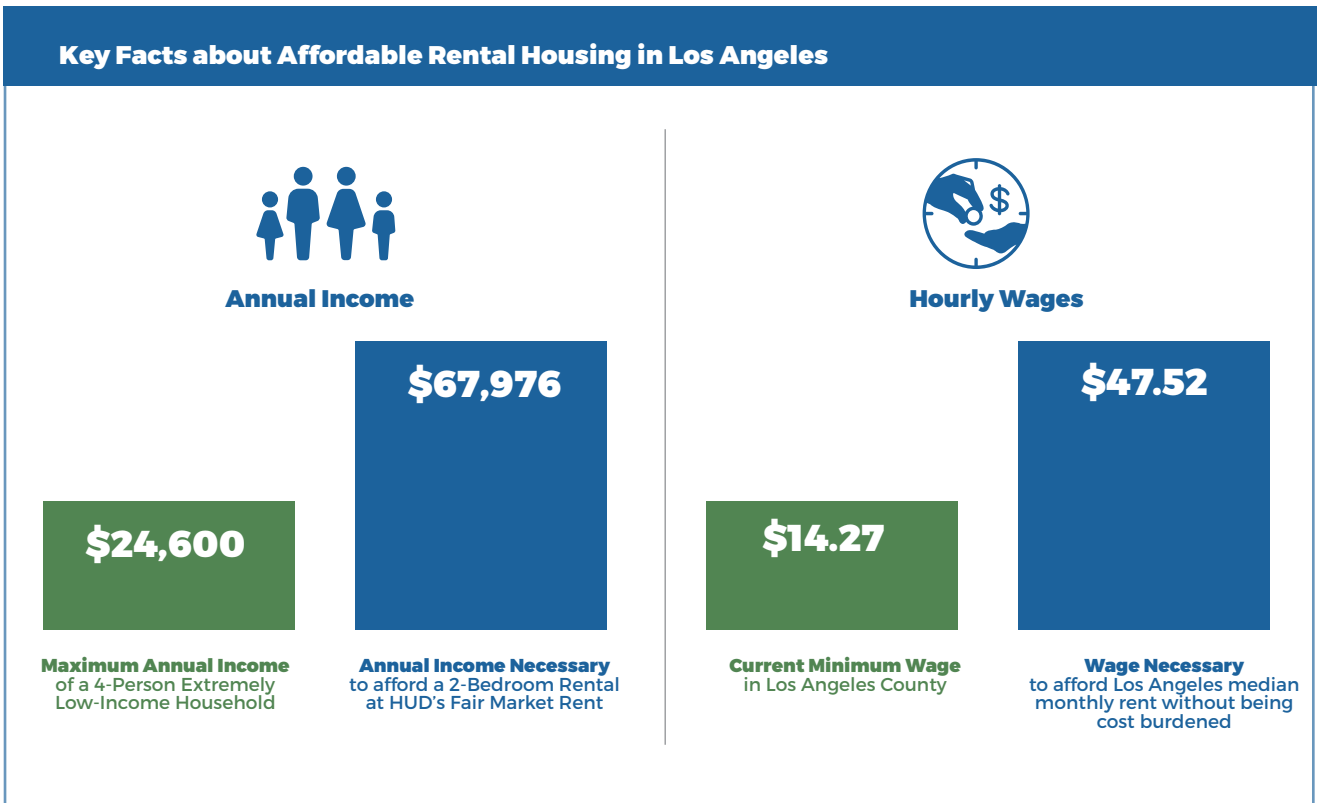


¹⁹ Source: National Low Income Housing Coalition, Housing Needs by State/California.

Los Angeles, as the second largest city in the nation, is particularly impacted by the affordable housing crisis given the scale of the problem. According to California Housing Partnership, Los Angeles County needs 516,946 more affordable rental homes to meet the current demand.²⁰ That is more than one third of the state’s need for 1.4 million affordable rental units. Within Los Angeles, there are approximately 750,000 very low- and extremely low-income renter households and less than 250,000 rental units affordable and available for them. In addition, 91% of extremely low-income renter households are considered cost burdened, paying more than 30% of their income on housing, while 79% are considered severely cost burdened, paying more than 50% of their income

on housing costs (this is compared to only 3% for moderate-income households).

The crisis in Los Angeles, like in California and the nation overall, is being driven by the rising cost of housing combined with wage stagnation at the lower end of the income spectrum. For example, in Los Angeles County the median monthly asking rent is \$2,471. A renter in Los Angeles County would need to earn \$47.52 per hour in order to afford that rent without being cost burdened. However, that is more than 3x the local minimum wage.



²⁰ Source: California Housing Partnership, “Los Angeles County’s Housing Emergency Update.” May 2019.

Eliminating The Shortage: Innovative Approaches Needed

The Financing Gap

Affordable housing development and operation is premised on balancing a simple equation: the cost to build and operate the affordable housing must be less than or equal to the expected rent to be collected from the housing.



For developers, the costs to build and operate are referred to as *uses* of capital. The primary uses involved in building affordable housing include acquisition, soft costs (professional services and fees), hard costs (construction), financing costs, and developer fees. Acquisition costs include the cost of obtaining the land to build on as well as any necessary planning, entitlements or land carrying costs. Construction includes the cost of building on the land and can often be the biggest expense. Financing costs include the interest developers must pay on predevelopment loans which can balloon if entitlement and approval processes are drawn out. Finally, the developer fee is the

compensation paid to the developer for developing the project. Operating costs for affordable housing typically include ongoing expense items such as utilities, insurance, maintenance, management and administration, and can also include supportive services and special programming.²¹

To cover the costs of building and operating affordable housing, developers use a combination of debt, equity and subsidy. These are referred to as the *sources* of capital. A developer must not only find sufficient sources to cover its uses, but it must also find the right mix of sources (debt, equity and subsidy) for any given project. For example, how much a developer can borrow depends on the project’s anticipated net operating income (NOI) – the money to be collected from rents after accounting for operating expenses. In addition, a developer will also invest equity into a development deal. The combination of debt and equity invested into affordable housing deals is often insufficient to cover the cost of developing and operating the project, resulting in the need for subsidy to fill the gap. However, subsidies are not always readily available so cannot be guaranteed for every project. Even if a project qualifies, federal, state and local governments have limited available amounts of subsidies like tax credits and grants.

²¹ Source: Urban Land Institute, “The cost of affordable housing: Does it pencil out?”

In addition, there is downward pressure on NOI for these developments resulting from classifying these projects as affordable and therefore eligible for subsidies. To achieve such classification, rents must be capped at rates working families can afford. Currently the standard is that families should pay no more than 30% of their income on rent and to qualify for tax credits, the units in a project must be affordable to a family earning no more than 60% of AMI. In addition, rent subsidies are often aimed at extremely low-income families – those earning less than 30% of AMI – making the equation even harder to balance. Depending on the target level of affordability (low-income, very low-income, and/or extremely low-income), the anticipated net operating income may be quite low or perhaps even negative. This can result in a significant gap between what it costs to build and operate affordable housing and what a low-income renter can afford to pay.

Current Approaches - Necessary but insufficient

There are a variety of supply- and demand-side subsidies available to assist in increasing the supply of and access to quality affordable rental housing, yet the gap continues to exist, growing

Sources

- ✓ Debt
- ✓ Equity
- ✓ Subsidy

Uses

- ✓ Acquisition
- ✓ Construction
- ✓ Developer Fees
- ✓ Other

Loan Interest
Financing Fees
Reserves
Project Management Fees

in many urban markets, while the need for affordable housing balloons. Available subsidies include a range of federal, state and local programs providing a combination of supply- and demand-side assistance (see Figure 1 for Sample Federal Subsidy Programs). The primary source of supply-side assistance is the Low-Income Housing Tax Credit (LIHTC) while on the demand-side it is Section 8 Housing Choice Vouchers. Both are critically necessary but insufficient in meeting the growing need for affordable housing.

Box 3: Low-Income Housing Tax Credits

Created in 1986 as part of Tax Reform Act and made permanent in 1993, LIHTCs provide indirect federal subsidy to finance construction and rehabilitation of low-income affordable rental housing. This is delivered in the form of a tax credit that provides a dollar-for-dollar reduction in federal tax liability to investors in exchange for providing equity to develop affordable rental housing.

There are two types of credits: the 9% credit is generally used for new construction while the 4% credit is used for rehabilitation or new construction financed with tax-exempt bonds. Although the two types of LIHTC are usually

Example

Assume a new construction affordable housing project has a qualified basis of \$1 million and qualifies for the 9% credit. The project will generate an annual stream of tax credits equal to \$90,000 (9% x \$1 million) for a total credit over 10 years of \$900,000. Under the appropriate interest rate, the present value of the stream of tax credits should equal \$700,000 or a 70% subsidy on the \$1 million qualified basis.

referred to by their credit rates (9% or 4%), in reality, it is the amount of subsidy targeted that is explicitly specified in the Internal Revenue

Code (IRC). The target subsidy is either 70% or 30%. The 70% subsidy is achieved with the 9% credit and the 30% subsidy with the 4% credit.

The LIHTC works as follows: investors provide equity for projects and in exchange receive tax credits paid annually over 10 years. The amount of tax credit claimed by investors each year equals the credit rate (9% or 4%) multiplied by the project's qualified basis. The qualified basis equals the proportion of the cost of the housing project that is rented to tenants meeting the income tests. In most projects this is 100% in order to maximize the equity contribution from the LIHTC.

The process of allocating, awarding and then claiming LIHTCs is long and complex. It begins at the federal level with each state receiving an allocation that is then administered by the state's Housing Finance Agency (HFA). The HFA then awards the credits to developers according to federally mandated, but state created, allocation plans – a competitive process and one that is particularly fierce for the 9% credits. Developers then sell those credits to investors for equity. The allocation each state receives is based on its population. In 2019, states received an allocation of \$2.75625 per person, with low population states receiving a minimum of \$3,166,875.22 For example, since California has approximately 40 million people, its 2019 allocation is approximately \$110.25M (40M people x \$2.75625 per person).

To be eligible for LIHTCs, projects must meet certain requirements and must maintain compliance with those requirements for a minimum of 30 years after completion (generally 55 years for California). Moreover, projects must meet both an income test and an affordability test to be eligible. It used to be that the income test required at least 20% of units be affordable to households earning less than 50% of area median income (AMI) or at least 40% of units be affordable to households earning less than 60% of AMI. However, after the Consolidated Appropriations Act of 2018,

households earning up to 80% of AMI are eligible to access LIHTC projects, as long as the average income of all households occupying the project is 60% of AMI or less. Theoretically this might help to subsidize lower income tenants since renting to a household earning 80% of AMI means that a landlord must also rent to a household earning 40% of AMI to achieve the blended target of 60% of AMI or less. In addition to the income test, projects must also meet an affordability test. That is, rents cannot exceed 30% of either 50% or 60% of AMI, depending on the share of tax credit rental units in the project.

The LIHTC program costs the federal government more than \$9 billion annually and is by far the largest federal program incentivizing the creation of affordable housing. Its advocates - and even its critics - are quick to point out that the program has substantially increased the stock of affordable housing, adding nearly 3 million units since its inception. However, despite its success, the program is not without its challenges including economic inefficiency, complexity, and unintended consequences. Even the most ardent advocate for the LIHTC program would likely admit that the subsidy used per unit is higher than it needs to be because of the numerous intermediaries involved in the process – syndicators, attorneys, accountants, etc. The regulatory and procedural complexity of the program not only necessitates all these participants, but it also adds considerable time to the development timeline – both of which add significant expense. And while the program has succeeded in adding desperately needed affordable housing units, it has also created unintended consequences including concentrated poverty and racial segregation through state approval processes that concentrate low-income communities where they have been historically segregated and have limited economic opportunity. In addition, while the program has helped to create affordability, it does nothing to maintain that affordability after the expiration of the required compliance period.

Box 4: Section 8 Housing Choice Vouchers

Created by the Housing and Community Development Act of 1974, Section 8 Vouchers theoretically assist very low-income families, the elderly, and the disabled to afford safe and sanitary housing in the private market. Section 8 is a federally funded rental assistance program that pays private landlords the difference between what a low-income household can afford and the fair market rent.

Section 8 is administered by public housing agencies (PHAs) with federal funds received from HUD. It works as follows: eligible families and individuals apply for the vouchers. If/when those vouchers are received, those families and individuals can use the vouchers to cover the difference between what they can afford to pay in rent and the fair market rent of a Section 8 eligible rental unit. Section 8 determines the maximum amount it will pay for each voucher based on a combination of factors including Fair Market Rent (FMR), Payment Standards, and a calculated Tenant Portion. In some cases, the vouchers also provide an allowance for utilities. The Fair Market Rent is a figure calculated by HUD for over 2,500 areas in the country. It is set at the 40th percentile of rents in an area (i.e. 40% of units in that area rent for less than the FMR while 60% of units rent for more). Each public housing agency then uses the HUD FMR as a guide to determine their payment standard which is the maximum they are willing to pay for each number of bedrooms. This is typically within 90% to 110% of the FMR. Finally, each tenant receiving a voucher is also required to contribute a portion of the rent. This is calculated as the greater of A. 30% of monthly adjusted income, B. 10% of gross income, C. the welfare rent, or D. the minimum rent amount set by the public housing agency. Eligibility for Section 8 vouchers is based on

total annual gross income, family size, and is limited to US citizens and specific non-citizens who have eligible immigration status. In addition, family income must be 50% or less of AMI for the County or Metropolitan area where the family chooses to live and the PHA must provide 75% of vouchers to applicants with income at 30% or less of AMI.

The fiscal year 2019 appropriations law signed by President Trump in February provides \$22.6 billion for Section 8 Housing Choice Vouchers²³ which serve more than 5 million people living in 2.2 million low-income households.²⁴ Advocates argue that the program's most important advantage is that it provides recipients the freedom to choose the kind of housing that best meets their needs. However, even those advocates acknowledge that the program's shortcomings, like with LIHTC, lead to inefficiency and unintended consequences. Because there is significantly more demand for than supply of vouchers, people often end up on long waiting lists. When they ultimately do receive a voucher, they often have to request multiple extensions due to the challenge of locating a landlord receptive to accepting Section 8 (vouchers can be lost if not used within 60-90 days). Also contributing to inefficiency are the challenges with "portability" – taking vouchers from one jurisdiction to another – which does not work as smoothly as it should. And, while the program serves many low-income households who need the rental assistance desperately, it also creates unintended consequences like keeping voucher holders in areas of concentrated poverty both because the calculation of FMR relegates people to impoverished neighborhoods and because landlords in many nicer neighborhoods will do what they can to keep voucher holders out.

²³ Source: Center for Budget and Policy Priorities, "Funding Bill and Carryover Funding Should Enable Agencies to Issue More Housing Vouchers in 2019." February 21, 2019.

²⁴ Source: Center for Budget and Policy Priorities, "United States Housing Choice Vouchers Fact Sheet." August 2017.

Figure 1: Sample Federal Programs

Program Name	Description
<p>Community Development Block Grants (CDBG) ²⁵</p>	<p>A flexible program providing communities resources to address a wide range of unique community development needs, including affordable housing. Begun in 1974, it is administered by the U.S. Department of Housing and Urban Development (HUD) and provides grants to 1,209 general units of local government and states.</p>
<p>Homelessness Assistance Programs ²⁶</p>	<p>Provides funding to states and local governments and nonprofit providers to serve individuals and families affected by homelessness. Administered by HUD, examples of these programs include the following:</p> <ul style="list-style-type: none"> <li data-bbox="459 763 1449 999"> <p>✓ Continuum of Care (CoC) Program: Designed to assist individuals (including unaccompanied youth) and families experiencing homelessness and to provide the services needed to help such individuals move into transitional and permanent housing, with the goal of long-term stability. Eligible costs, among others, include tenant-based (TBRA), sponsor-based (SBRA), or project-based (PBRA) rental assistance.</p> <li data-bbox="459 1039 1449 1196"> <p>✓ Emergency Solutions Grants (ESG) Program: Designed to prevent families and individuals from becoming homeless and to rapidly re-house homeless individuals and families among other activities. Eligible costs, among others, include rental assistance, financial assistance and services.</p> <li data-bbox="459 1236 1449 1588"> <p>✓ Title V - Federal Surplus Property for Use to Assist the Homeless: Enables eligible organizations to use unutilized, underutilized, excess, or surplus federal properties to assist persons experiencing homelessness. Eligible applicants are states, local governments, and nonprofit organizations. Properties, including land and buildings, are made available strictly on an “as-is” basis. No funding is available under Title V. Leases are provided free of charge and range from 1 to 20 years, depending on availability. Successful applicants may use the Title V properties to provide shelter, services, storage, and other benefits to persons experiencing homelessness.</p> <li data-bbox="459 1628 1449 1863"> <p>✓ Base Realignment and Closure Program (BRAC): Homeless assistance providers may use buildings and other resources on former military bases for a wide range of activities, from emergency shelter to permanent housing to support services. Eligible applicants include Local Redevelopment Authorities (LRAs) and homeless assistance providers. The program applies to all military installations closed after October 25, 1994.</p>

²⁵ Source: U.S. Department of Housing and Urban Development.

²⁶ Source: HUD Exchange – Homelessness Assistance Programs.

Program Name	Description
	<p>✓ HUD Veterans Affairs Supportive Housing Program: This program targets currently homeless veterans. It is a joint program between HUD and the U.S. Department of Veterans Affairs (VA). HUD provides housing choice vouchers and VA provides case management and outreach. Vouchers are generally tenant-based though on a case-by-case basis, project-based vouchers may be used.</p>
<p>Housing Opportunities Made Equal (HOME) Funds</p>	<p>Grants to states and units of general local government to implement local housing strategies designed to increase homeownership and affordable housing opportunities for low and very low-income Americans. This program provides financial support to states and local governments (a minimum of \$3 million/state, \$500,000/local government) to be used for home purchase or rehabilitation assistance, building or rehabilitating homes for rent, site acquisition or improvement, or funding designated Community Housing Development Organizations. In every project, the state or local government must pledge \$0.25 for every \$1 of federal funds; this money can come as cash or materials donations (construction materials, land, labor, and others).²⁷</p>
<p>National Housing Trust Fund</p>	<p>Created through the passage of the Housing and Economic Recovery Act of 2008, the NHTF uses surplus revenues from Fannie Mae and Freddie Mac operations to fund affordable housing solutions. 90% of all funds are to go to building, preserving, repairing, and operating rental units for low-income and very low-income households, while 10% can support home ownership assistance for first time home buyers.²⁸</p>

Although the equation upon which affordable housing development is based is simple, achieving balance in that equation is far from it. In fact, the challenges and constraints associated with each of its inputs and the financing gap that results are among the key drivers leading to the critical shortage of affordable rental housing. And while the primary supply- and demand-side forms of assistance are critically necessary in closing the

gap, they are insufficient in meeting the escalating need for affordable housing. New approaches to affordable housing development and operation are needed to close the gap and address the critical shortage of affordable rental housing.

²⁷ Source: U.S. Department of Housing and Urban Development - The Home Program: Home Investment Partnerships.

²⁸ Source: National Low Income Housing Coalition.

Rethink Housing: Innovating A New Approach

The Goal - Build More Units, at Lower Cost, in Less Time, with Less Capital Subsidy

The RETHINK Housing model aims to build more housing units, at lower cost, in less time, while relying less on limited capital subsidy and more on project financing from market-based financing sources. To achieve this, the model uses six key levers to dial down the time and cost of development, thereby shrinking the financing gap, altering the nature of subsidy needed, and as a result, increasing the speed and volume of production. The six key levers employed in the RETHINK model include 1. a coordinated team approach, 2. smaller site selection, 3. low/no cost acquisition, 4. efficient design, 5. “by-right” development, and 6. simplified financing.

Lever #1: Coordinated Team Approach

The model relies on a core team of partners executing a coordinated “one-stop-shop” approach to project development. This includes site selection, acquisition, design, development, financing and the provision of supportive services. Working together, the team creates a body of knowledge leading to scalability and efficiency through replication, which contributes to reducing costs. Key to the success of the team is assembling members who bring the right efficiencies among them to make small projects viable again – members who are smaller, nimble, creative, and flexible. The RETHINK team includes the organizations providing the respective core functions summarized in Figure 2.



Figure 2: RETHINK Housing Team

Partner Function	Description
<p>Genesis LA (GLA) <i>Financing</i></p>	<p>Started in 1998 under Los Angeles Mayor Richard Riordan, today Genesis LA is a certified Community Development Financial Institution (CDFI) and Community Development Entity (CDE). As a CDFI, GLA makes loans to and investments in community and economic development projects through the Genesis Community Investment Fund (GCIF). As a CDE, GLA has received \$320 million in New Markets Tax Credit (NMTC) allocation. GLA also provides technical assistance, financial structuring, capital raising, and acquisition/construction assistance, designed to build the capacity of borrowers and the financial viability of their projects.</p> <p>GLA has provided predevelopment, construction and/or permanent financing for all the pilot projects in the RETHINK Housing pipeline, essentially filling the role of 3 different funding sources. GLA is also now directly acquiring properties, for projects that will ultimately leverage Proposition HHH funding (please see Box 5 for a discussion of HHH funding), to continue efforts to accelerate project completion timelines. The organization expects repayment of equity invested in acquisitions from the HHH subsidy, which is expected to be funded at construction.</p>
<p>Restore Neighborhoods LA (RNLA) <i>Development</i></p>	<p>RNLA is a nonprofit organization that works to reduce blight and create affordable homeownership and rental opportunities in neighborhoods throughout Los Angeles and surrounding counties by purchasing, rehabilitating, selling and/or disposing of residential properties. RNLA brings extensive experience in small-scale affordable housing development through its history of implementing the City of Los Angeles' Neighborhood Stabilization Program (NSP).</p> <p>RNLA serves as the developer on most of the RETHINK Housing pilot projects and has contracted with Curtom Dunsmuir for construction on all but one.</p>
<p>Lehrer Architects LA (Lehrer) <i>Design</i></p>	<p>Founded in 1985 as a sole proprietorship by Michael B. Lehrer, FAIA, Lehrer has extensive experience in designing, managing, master planning and working with community and cultural organizations on projects throughout Los Angeles and beyond. The firm, its people, and their experiences are all rooted in the various neighborhoods and communities they serve.</p> <p>Lehrer has provided the designs for all but one of the pilot projects in the pipeline. Lehrer has worked to identify development "types" and to create "prototype" designs that can be quickly rolled out and customized for each project within the constraints of the City and County's evolving ordinance landscape.</p>

Partner Function	Description
<p>Special Services for Groups (SSG) Service Provider</p>	<p>Incorporated in 1952, SSG is a nonprofit health and human service organization dedicated to building and sustaining community-based programs that address the needs of vulnerable communities. The organization provides services to address the social, health, behavioral health and economic needs of the diverse communities it serves.</p> <p>SSG has been both a borrower of capital to develop a project and a provider of comprehensive support services to the tenants within its projects. Typically, the service provider weighs in early in the design process, after the architect has laid out the site, to provide functional feedback on things like materials and finishes to ensure that those details facilitate rather than impede service delivery.</p>
<p>Jovenes, Inc. (Jovenes) Service Provider</p>	<p>Founded in 1990 by Fr. Richard Estrada, a priest at La Placita Church on Olvera Street in Downtown L.A., Jovenes is a nonprofit organization providing sanctuary and hope to homeless youth. Their mission is to help youth, ages 18-25, end their cycle of homelessness by not only focusing on their need for housing but also by providing healthcare, education, employment and trauma recovery.</p> <p>Jovenes has been both a borrower of capital to develop a project and a provider of comprehensive support services to the tenants within its project.</p>

Using the same coordinated team on project after project allows for the development, refinement and transfer of experiential knowledge, trust, and working relationships that creates efficiency in site selection, acquisition, design, development, financing and operations - all contributing to the reduction of time and cost in project development.

Box 5: Proposition HHH - Supportive Housing

Proposition HHH is a \$1.2 billion bond passed in the City of Los Angeles to build approximately 10,000 units of supportive housing for the homeless and those at risk of homelessness. To facilitate project and program proposals using both traditional and innovative financing and construction techniques, the City released three funding and/or City-owned property proposal opportunities seeking the best design and development ideas from the community. These included the following:

1. Innovative Design Projects on a City-Owned parcel using HHH Funding
2. Call for Projects (multiple rounds)
3. Housing Innovation Challenge

In September 2019, the RETHINK Housing team was selected for a \$10 million award as part of the \$120 million HHH award under the Housing Innovation Challenge.

Lever #2: Smaller Site Selection

The model targets smaller sites that can accommodate approximately 2 – 25 units. Targeting such sites also helps to reduce acquisition costs by reducing competition for sites from LIHTC project developers, who are typically competing for larger sites, and by expanding the neighborhoods in which projects can be located. Traditional LIHTC projects are not viable on these sites because they need to achieve scale in order to absorb various fixed costs associated with those projects.

Lever #3: Low/No Cost Acquisition

The model seeks to eliminate or significantly reduce land costs by partnering with public and private land owners willing to contribute land to help house the region’s homeless population. Such owners can include churches, nonprofit organizations, local government, and private land owners. By eliminating or significantly reducing land cost, the RETHINK model drives down acquisition cost – one of the largest development cost components – as well as interest expense incurred during the predevelopment period.

Lever #4: Efficient Design

The model uses a more efficient and cost-effective design and construction than typical large-scale, LIHTC developments, relying largely on the prototype designs, such as those developed by Lehrer. Strategic design decisions are made to reduce cost while maximizing the number of units on a site. Examples of such decisions include:

- ✔ Reducing and even eliminating parking through land use incentives;
- ✔ Single-story construction to eliminate elevators, stairways, engineering, and higher construction costs;
- ✔ Placing circulation outside along courtyards and walkways to eliminate the cost of interior hallways and lobbies; and
- ✔ Designing compact and efficient floorplans for each unit.

The design innovation is based on “mass customization,” standardized prototype designs that can be re-used and customized for each new site, giving each project a sense that this is home.

Lever #5: “By-right” Development (Planning Approval & Construction)

The model develops projects that can be built “by-right” because they conform to existing land use regulations. This avoids discretionary review and approval processes and NIMBY (“Not In My Backyard”) opposition, thereby aiming to save time and as a result, reduce total project costs. To date, the team has primarily used land use incentives made available under the City of Los Angeles Transit Oriented Communities (“TOC”) land use program

Lever #6: Simplified Financing

The simplified financing core to the model’s effectiveness is made possible by two key components: 1. patient, flexible capital provided to GLA in part by the Conrad N. Hilton Foundation, and 2. a local, flexible and readily available rental

subsidy provided by Los Angeles County Department of Health Services (DHS) through their Housing for Health Division (HFH).

The Hilton Foundation provided GLA a long-term flexible loan in the form of a program-related investment (PRI) and it also provided grant dollars.

Box 6: “By-Right” Development

California Senate Bill 35 (SB 35)

By-right development refers to projects able to bypass additional planning and environmental reviews because they are located in cities that have been unable to meet the housing growth targets set by the state of CA and they meet a variety of zoning, affordability and labor standards.

California SB 35 was signed into law on September 29, 2017, as part of California’s 2017 Housing Package. It allows developers to apply for a streamlined approval process in municipalities not meeting Regional Housing Needs Assessments (RHNA). In order to qualify, a development must:

- ✔ Be zoned for residential use.
- ✔ Designate at least 10% of units as below market housing if located in localities that did not meet above moderate income RHNA.
- ✔ Designate at least 50% of units as below market housing in localities that did not meet low income RHNA.
- ✔ Not be built in an ecologically protected area.
- ✔ Be multi-unit housing (not single-family homes).
- ✔ Pay construction workers union-level wages.

Source: Los Angeles Times, “How a new California law could kill a 30-year-old rule that slowed development in Los Angeles.” October 5, 2017.

Source: California Legislative Information, “CA Senate Floor Analyses: SB35.” “Senate Rules Committee,” September 1, 2017.

The Hilton Foundation PRI to GLA contains key features that allow GLA to take more risk than it otherwise might be able to in order to finance these projects. These key features include loan forgiveness – if an underlying loan does not repay GLA, then GLA is not required to repay Hilton Foundation – and an option to extend the loan beyond 10 years, allowing better alignment of the term of the loans with the operational timeline of the projects which are closer to 15 years. These features are vital to GLA’s ability to finance the RETHINK projects.

Also pivotal is the Los Angeles County DHS Housing for Health Division flexible rental subsidy. This division was formed in 2013 with a mission to create permanent supportive housing for homeless patients of the DHS system - a relatively small but costly cohort of individuals, whom due to their lack of housing, remained hospitalized for greater lengths of time and/or had repeated and unnecessary contact with the public health system. By housing homeless individuals that have been high utilizers of DHS services with complex medical and behavioral health conditions, HFH seeks to improve their health outcomes, reduce the costs to the public health system serving them, and demonstrate the division’s commitment to improving the lives of homeless in Los Angeles.²⁹

In February 2014, to advance its mission, HFH launched the Flexible Housing Subsidy Pool (FHSP), a locally funded rental subsidy program launched with initial contributions of \$13 million from DHS, \$1 million from the Office of LA County Supervisor Mark Ridley-Thomas, and a \$4 million grant from the Hilton Foundation. The goal of the FHSP is to provide quality affordable housing for homeless DHS patients, many of which do not qualify for federal housing subsidies because of their documented status, past violations while

using a federal housing subsidy, or involvement with the criminal justice system. In addition, during the budget sequestration, the federal government froze issuance of new Housing Choice Vouchers, making the need for the FHSP even more urgent.³⁰

DHS contracts with Brilliant Corners, a private nonprofit supportive housing management agency, to administer the FHSP. The organization provides housing coordination, move-in assistance, and administers the rental subsidies. When a unit has been identified for a client, Brilliant Corners enters into a subsidy agreement with the landlord and the landlord enters into a lease agreement with the client. Additionally, Brilliant Corners contracts with a separate social service provider to provide direct social services to each tenant at no additional cost to the property owner or the tenant. The DHS contracts come in the form of three 5-year terms (totaling 15 years) and cover units falling within the Los Angeles’ city and county Fair Market Rent (FMR) as determined by HUD. As long as the landlord complies with the rental subsidy agreements, DHS fully expects to renew the rental subsidy every 5 years. The reason for the multiple terms is that the County is prohibited from budgeting such expenses in terms greater than 5-years.

The flexible, long-term rental subsidy provided by the FHSP increases and stabilizes proforma net operating income, allowing GLA to underwrite a loan to a developer for a project that has secured that rental subsidy, often without the need to pursue additional complicated, costly and scarce capital subsidies. This significantly simplifies and streamlines the necessary financing sources and provides the opportunity to pursue market-based financing options.

²⁹ Source: County of Los Angeles Department of Health Services.

³⁰ Source: ABT Associates, “Flexible Housing Subsidy Pool Brief Evaluation of the Conrad N. Hilton Foundation Chronic Homelessness Initiative.” March 2017.

Pilot Projects Show Promise and Provide Key Lessons

RETHINK Pilot Projects

There are currently 10 RETHINK projects underway at various stages of acquisition and development across Los Angeles. While those projects are not yet fully developed, they are showing promise in terms of reducing costs and time to develop while

relying on less capital subsidy. Among those, the average cost per unit to develop is \$180,000 versus \$531,373 for LIHTC projects while the average capital subsidy required is \$64,000 per unit versus \$450,000 for LIHTC projects (see Figure 3). In addition, the three projects that are furthest along are also showing promise in terms of reducing the total development time; approximately 26 months versus 42 to 60 months for LIHTC projects (see Figure 6).

Figure 3: Comparison Profile - RETHINK Housing vs. LIHTC

	RETHINK	LIHTC
Number of Units per Project	2 - 25	50+
Average Cost per Unit	\$180,000 ³¹	\$531,373 ³²
Capital Subsidy per Unit	\$64,000	\$450,000

Figure 4: RETHINK Housing Pilot Projects

	Borrower	Address	Units	Approx. Cost	Description
1.	Special Service for Groups (SSG)	4618 E. Compton Blvd. Compton, CA 90221	10	\$800,000	New construction of 2-unit (10-bed) youth facility on County site
2.	Bungalow Gardens (RNLA)	920-926 W. 81st Street Los Angeles, CA 90044	8	\$1,200,000	New construction on RNLA-owned site
3.	4th Street (Jovenes)	3551 E. 4th Street Los Angeles, CA 90063	8	\$1,200,000	New construction on City of LA-owned site
4.	Willowbrook (LA Co./RNLA)	11909 Willowbrook Ave. Los Angeles, CA 90059	7	\$1,000,000	New construction on County-owned site
5.	Greater Cornerstone Baptist Church	5904 S. Figueroa Street Los Angeles, CA 90003	10	\$1,200,000	New construction on church-owned lot
6.	RETHINK Housing LLC - Westlake	405 N. Westlake Ave. Los Angeles, CA 90026	18	\$4,500,000	Purchased with Genesis LA equity
7.	RETHINK Housing LLC - Normandie	1408 W. 62nd Street Los Angeles, CA 90047	23	\$4,700,000	Purchased with Genesis LA equity
8.	RETHINK Housing LLC - Figueroa	5900 S. Figueroa Street Los Angeles, CA 90003	21	\$4,200,000	Purchased with Genesis LA equity
9.	Jovenes Aliso Triangle	1208 Pleasant Ave. Los Angeles, CA 90033	15	TBD	Development of vacated City of LA cul-de-sac
10.	Claremont	Baseline Dr. Claremont, CA	15	TBD	Property owned by nonprofit

³¹ The average cost per RETHINK unit is based on 8 of the 10 projects currently in the RETHINK pipeline. These 8 projects account for 105 units at a total projected cost of \$18,800,000 or \$179,047 per unit on average.

³² Source: USA Today, "Some of Los Angeles' homeless could get apartments that cost more than private homes, study finds." October 8, 2019.

Figure 5: Map of RETHINK Housing Projects

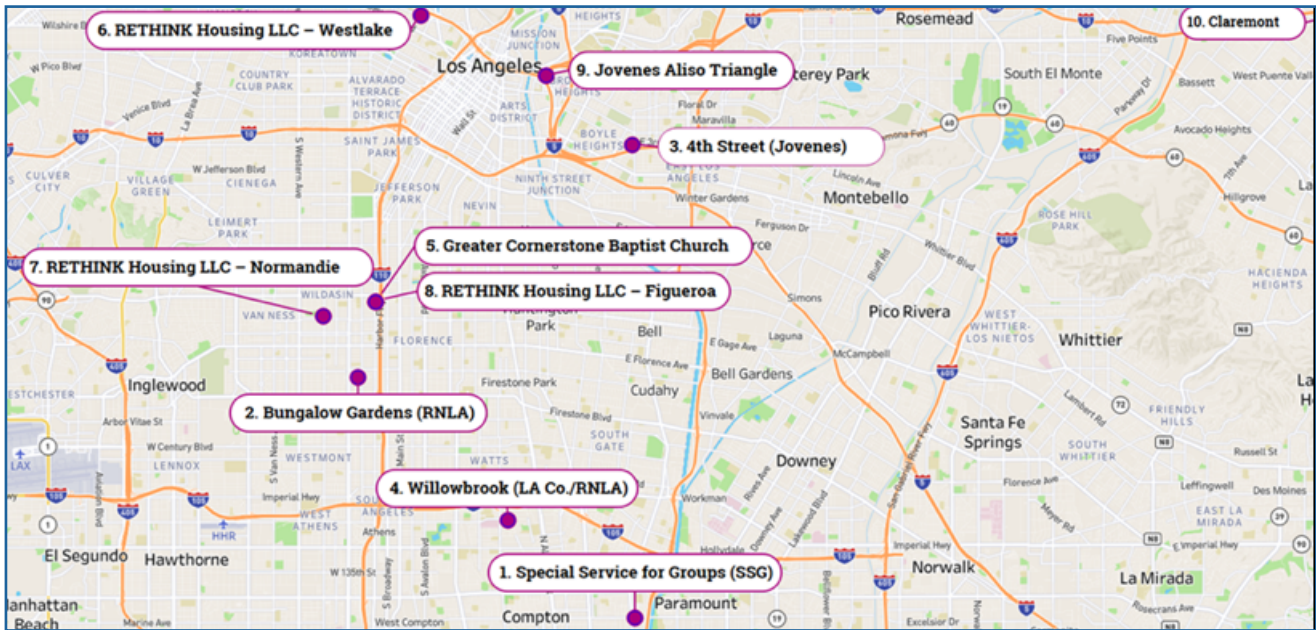


Figure 6: Time & Cost Comparison - LIHTC v. RETHINK Housing

	Special Service for Groups - Compton	Bungalow Gardens	4th Street (Jovenes)	RETHINK Housing, LLC	LIHTC
Average Cost/Unit	\$80,000	\$150,000	\$150,000	\$220,000	\$531,373
Predevelopment Period	13 Months	21 Months	24 Months	9 Months (est.)	24 - 36 Months
Construction Period	13 Months	15 Months (est.)	12 Months (est.)	15 Months (est.)	18 - 24 Months
Total Development Time	26 Months	36 Months (est.)	36 Months (est.)	24 Months (est.)	42 - 60 Months (est.)

Since launching the RETHINK Housing model in 2017, the team has expanded to pursue projects that also include the direct acquisition of land. The projects listed above under RETHINK Housing, LLC are sites that have been acquired using Genesis LA equity to obtain site control from the open market. These projects will ultimately be financed with a

combination of debt from Genesis LA and subsidy from HHH. As a result, these projects include land costs and are generally larger (averaging 20 units) to spread the acquisition costs across more units.

Project #1: Special Service for Groups, Inc. (SSG) - Compton

The SSG Compton project is in unincorporated Los Angeles County near Compton (see Figure 4, Project #1). It involves the construction of a two-story, two-unit building, which will provide 10 bedrooms (5 on each floor) for youth supportive housing. Each of the youth housed at the Project (one per bedroom), will have access to a wide

range of supportive services onsite such as counseling, addiction treatment, and job training and placement services. The project will also be built according to Title 24 standards, incorporating various green features to ensure sustainability in keeping with local policies and plans.³³

The cost to develop this project was approximately \$800,000, resulting in a per unit cost of \$80,000,

Project #1: Special Services for Groups, Inc. (SSG) - Compton.

RETHINK Lever	Description
1. Team	The team for this project consists of SSG, Genesis LA, RNLA, and Lehrer. In this case, SSG was both the borrower for the project as well as the service provider because the property had previously been donated to SSG. Genesis LA provided the financing – a \$72,500 predevelopment loan that closed 05/17/18 and a \$727,500 construction loan that closed 10/01/18. RNLA provided development services and Lehrer provided architectural designs.
2. Site Selection	The site measures 4,100 sf and is zoned commercial. Under zoning in unincorporated LA County at the time, a conditional use permit was required to build affordable housing in a commercial zone. SSG had obtained a conditional use permit prior to the Team becoming involved in the project, and the permit allowed for a two-unit residential building with two parking spaces required. However, after the Team was engaged, the design started from scratch and went through a typical “by-right” plan check and building permit process.
3. Acquisition	The property for this project was a vacant, former Community Redevelopment Agency (CRA) site donated to SSG by the County of Los Angeles.
4. Design	The design challenge with this project was to maximize the number of youth being served, providing enough space and individuality to each resident, staying within the two-unit constraint imposed by the existing zoning, and while keeping costs down. As a result, Lehrer Architects designed a project containing two units with five bedrooms and two bathrooms each – providing each resident their own bedroom but sharing amenities like kitchens, living rooms and laundry in order to maximize the efficiency of the space. It is essentially a shared housing model which recent reports indicate is a promising model for youth and other populations.
5. Development	By the time the team became involved in the Project, it was considered a “by-right” development because a conditional use permit had already been obtained. As a result, the approval process took slightly more than a year (386 days). Construction began 10/31/18 and is scheduled to be completed on 12/06/19.
6. Simplified Financing	Genesis LA was able to underwrite the project as the single source of financing, relying on support from the fixed rental revenue stream provided by the Department of Mental Health Services. ³⁴ In this example, the costs of the project were minimized through the team’s coordinated approach, the small site selection, no-cost acquisition, and efficient design allowing for by-right development that significantly reduced the development time. In addition, because the costs were lower and DMH provided the rental subsidy that increased and stabilized proforma net operating income, Genesis LA was able to underwrite the project without need for capital subsidy to fill a financing gap.

³³ Title 24 is California’s energy standards that address the energy efficiency of new and redeveloped homes and commercial buildings. Since 1978, California residents are required to meet the energy efficiency standards contained in Title 24, Part 6 of the California Code of Regulations. Source: California Energy Commission.

³⁴ The Department of Mental Health Services (DMH) contracts with SSG as a service provider to its clients. DMH also provides rental subsidies for its clients. In this project, SSG was able to obtain commitments from DMH for those rental subsidies on behalf of clients to be placed in this project.

resulting in a per unit cost of \$80,000. The team began predevelopment on the Project on 10/07/17 and completed all permitting on 10/31/18. Construction began on 10/31/18 and is expected to be completed on 12/06/19, resulting in total project completion time of 411 days. The monthly rent per unit is \$800.

Project #2: Bungalow Gardens

The Bungalow Gardens project is located in South Los Angeles, within the City of Los Angeles (see Figure 4, Project #2). It involves the construction

of an 8-unit homeless housing project. Each tenant housed at the Project will receive a wide range of supportive services such as counseling, addiction treatment, and job training and placement services. The project will also be built according to Title 24 standards, incorporating various green features to ensure sustainability in keeping with local policies and plans.

The projected cost to develop this project is approximately \$1,200,000, resulting in a per unit

Project #2: Bungalow Gardens.

RETHINK Lever	Description
1. Team	The team for this project consists of RNLA, Genesis LA, and Studio 15 (the architect). The service provider is yet to be identified. In this case, RNLA is both the borrower for the project as well as the developer. Genesis LA provided the financing – a \$920,000 construction-permanent loan that is anticipated to close by 11/01/19.
2. Site Selection	The site measures 9,000 sf and is zoned R-3, allowing for one unit per 800 sf of land prior to any Transit Oriented Communities Density Bonus (TOC) incentives. ³⁵ TOC incentives were used to eliminate any parking requirements.
3. Acquisition	The property for this project was a vacant, former Community Redevelopment Agency (CRA) site donated to SSG by the County of Los Angeles.
4. Design	This project consists of 8 units, all accessible or adaptable, and each around 350 sq. ft. studios and one-bedroom units with a full bathroom and kitchen as well as a sleeping/living room. There is one laundry facility for the building as well as significant outdoor community space and a small office for a case manager. The project is all one story and organized in the form of a traditional bungalow court with four buildings, each containing two units and situated around a central courtyard.
5. Development	This project is utilizing land use incentives under the TOC guidelines, which allow affordable housing projects to be built without parking (thus maximizing units on the site). These land use concessions require certain affordability levels for 55 years, regardless of the rental subsidy. Under TOC, the project is considered “by-right” and did not involve any discretionary approvals. Construction is anticipated to begin in November 2019 and to be completed by January 2021.
6. Simplified Financing	RNLA secured a commitment letter for a long-term rental subsidy through DHS and Brilliant Corners. The subsidy runs up to 15 years, with three 5-year terms that renew if the landlord remains in good standing with the program. This committed long-term rental subsidy through FHSP increased and stabilized operating revenues and the RETHINK levers reduced development costs, thus eliminating the financing gap necessitating capital subsidy for development. As a result, Genesis LA was able to underwrite the project as the single source of capital, thus simplifying and reducing the costs of financing.

³⁵ The Transit Oriented Density Bonus (TOC) program was part of Measure JJJ passed by voters in November 2016. It is a density incentive program tied to providing affordable housing. TOC developments require that a certain percentage of residential units be deed-restricted as affordable housing in exchange for which developers can increase density by as much as 80% and receive other incentives such as parking breaks.

cost of \$150,000. Predevelopment began 03/07/18 and construction is scheduled to begin in December 2019. If everything proceeds according to plan, construction is anticipated to be completed by February 2021, resulting in total project completion time of 420 days.

Project #3: 4th Street (Jovenes)

The 4th Street project is in the Boyle Heights neighborhood in the City of Los Angeles (please see

Figure 4, Project #3). It involves the construction of an 8-unit Permanent Supportive Housing (PSH) development for homeless and at-risk youth living under 60% AMI. All tenants housed at the Project will receive a wide range of supportive services such as counseling, addiction treatment, and job training and placement services. The project will also be built according to Title 24 standards to achieve energy efficiency and preserve outdoor and indoor environmental quality.

Project #3: 4th Street (Jovenes).

RETHINK Lever	Description
1. Team	The team for this project consists of Jovenes, RNLA, Lehrer, and Genesis LA. In this case, Jovenes is both the borrower for the project as well as the service provider. Genesis LA provided the financing – a \$63,000 predevelopment loan that closed on 04/13/18 and a \$720,000 construction to permanent loan that is in the closing process at the time of writing this paper.
2. Site Selection	The site is 6,000 sf and is zoned C-2, allowing for R-4 density (or one unit per 400 sf of land) prior to any TOC incentives. TOC incentives were used to eliminate any parking requirements.
3. Acquisition	In 2017, Jovenes, in partnership with RNLA and GLA, successfully responded to an RFP from the city of Los Angeles Housing and Community Investment Department (HCID) for a former redevelopment site located at 3551- 3551 1/2 E. 4th Street. Jovenes currently has an Exclusive Negotiations Agreement (ENA) with HCID wherein there is an agreement to enter into a Disposition and Development Agreement (DDA) upon the achievement of predevelopment milestones. It was approved by the HCID Loan Committee in May 2019 and was approved by the City Council in early July 2019, triggering the DDA and then the preparation of the 99-year ground lease by the City Attorney. Moving from ENA to DDA and ground lease proved to be a much longer process than expected, due to the busy workload at HCID as well as the fact that this RETHINK Housing project did not conform with the traditional HCID terms under a typical LIHTC transaction.
4. Design	This project consists of 8 units, all accessible or adaptable, and each 300 sq. ft. mini studios with a full bathroom and kitchen as well as a sleeping/living room. There is one laundry facility for the building as well as significant outdoor community space and a small office for a case manager. The project is all one story and very simple construction that should be quick and easy for any contractor to build.
5. Development	This project is utilizing land use incentives under the Transit Oriented Community guidelines, which allow affordable housing projects to be built without parking (thus maximizing units on the site). These land use concessions require certain affordability levels for 55 years, regardless of the rental subsidy. Under TOC, the project is considered “by-right” and did not involve any discretionary approvals. Construction is anticipated to begin early 2020 with completion expected within 12 months.
6. Simplified Financing	While the RETHINK Housing model seeks to fully finance smaller affordable housing projects and leverage the DHS rental subsidy, Jovenes serves a unique youth population, not all of which qualify for the DHS rental subsidy because they are not chronically homeless. Therefore, four of the units in the Project will not utilize DHS’s subsidies. These units will be leased directly to youth at lower rents of \$650 per month (about half of the rent levels paid by FMR under the DHS rental subsidy). This will result in a lower Project income and therefore, the Project cannot leverage as much debt. To account for the lower debt financing, Jovenes secured a \$300,000 grant from LA County to provide the equity needed in the Project in order to sustain rents at \$650 for four of the units. While in this project the RETHINK model did not eliminate the financing gap, it significantly reduced the gap, necessitating far less capital subsidy and lowering overall development costs. This came in the form of the \$300,000 grant from Los Angeles County that provided the equity needed in the project to sustain rents at \$650/unit for four of the units.

The projected cost to develop this project is approximately \$1,200,000, resulting in a per unit cost of \$150,000. Site control was obtained on 12/15/17 when the Team entered into an ENA with HCID and construction is scheduled to begin in early 2020. If everything proceeds according to plan, construction is anticipated to be completed in early 2021, resulting in total project completion time of approximately 12 months or 360 days.

KEY LESSONS

While it is still early days, there are key lessons emerging from the RETHINK pilot projects. Early indications are that the model does in fact help to build more units, at lower cost, in less time, with less capital subsidy.

Lesson #1: Not only is low/no-cost acquisition important, but so is efficient and timely acquisition. The prolonged timeline and complications in acquiring the site for the 4th Street project was the motivator for figuring out if Genesis could create an acquisition fund, potentially using HHH funds as equity. Furthermore, negotiations with third-party land owners, such as churches, can take substantial time to complete and many are reluctant to tie up their land for new development.

Lesson #2: Simple, easy to approve and build designs that maximize the use of small infill parcels is key to accelerating project completion times. Use of infill parcels reduces competition for acquisition. Moreover, simple designs and reduced or no parking streamline the planning approval and construction process – all of which combined help to reduce project completion times.

Lesson #3: There is a lack of clarity, transparency and consistency in the planning review process that leads to duplication and inefficiency. The planning review and approval process is one carried out by individuals, each with their own approach to and interpretation of policies and ordinances. This leads to inconsistency, a lack of clarity, and even duplicative efforts in the planning review and approval process. The RETHINK Housing team has experienced these delays with implementation of such “by-right” land use policies as they relate to TOC, accessibility standards, and Low Impact Development standards designed to retain stormwater runoff onsite.

Lesson #4: The source and fluidity of rental subsidy is vital. Stable, ready access to rental subsidy is vital to a streamlined approach to financing without the need for substantial capital subsidy.

Scale & Replication: Removing Barriers & Leveraging Assets

The affordable housing crisis is the same in every state of the nation – there is a severe shortage of affordable and available rental units for the lowest income renter households that prevents equity and prosperity, not only for those households in need of affordable housing, but for the nation as a whole. While the crisis is the same across the country, how an innovative approach like RETHINK Housing can be used as a tool to address that crisis must be tailored to each community and its particular barriers and assets.

The RETHINK Housing model aims to build more housing units, at lower cost, in less time, while relying less on limited capital subsidy and more on project financing from market-based financing sources. To achieve this, the model uses six key levers to dial down the time and cost of development, thereby shrinking the financing gap, altering the nature of subsidy needed, and as a result, increasing the speed and volume of production. Those key levers include a coordinated team approach, smaller site selection, low/no cost acquisition, efficient design, “by-right” development, and simplified financing.

In order to scale and replicate the model, barriers to the effective application of the levers must be removed while at the same time leveraging the assets that can facilitate their application.

Recommendations for Removing Barriers

1. Site Selection. Simplify the process and reduce the amount of time it takes to find sites that are conducive to affordable housing development. For example, a city, county or state can create a central repository of sites available for affordable housing development. This repository can be populated by a variety of property owners including:

- ✓ **Public Agencies:** Local, regional or federal government agencies can list surplus sites from their own inventory that are available for affordable housing development. For example, King County, Washington, has a long-standing policy that gives affordable housing providers a “first look” at county-owned land, and California has a statewide policy that requires local agencies disposing of surplus public land to give first priority to affordable housing.³⁶ California is also preparing to RFP state-owned sites for affordable housing development per Executive Order N-06-19. In addition to streamlining site identification, public agencies can also create an expedited site disposition process.
- ✓ **Private Owners:** Private individuals willing to contribute land (perhaps in exchange for tax breaks or other incentives).

³⁶ Source: Urban Wire, “How Communities Are Rethinking Zoning to Improve Affordable Housing.” By Solomon Greene. June 12, 2019.

- ✔ **Philanthropic Organizations:** Institutional or private family foundations with real estate portfolios.
- ✔ **Religious Organizations:** Churches with land or buildings.

2. Acquisition. Reduce the time, complexity and cost of property acquisition. The rising cost of land continues to make the financing gap larger. Even when land is contributed by local government, lengthy and complicated approval processes prior to relinquishing site control can add significant time and cost to property acquisition. For example, developers often experience delays in accessing property for basic predevelopment activities like surveys, soils, environmental, etc. Delays also happen during permitting when the current owner (prior to transfer) needs to sign certain documents to complete permitting. Public agencies could address such delays by creating an expedited process for transferring land and/or property intended for affordable housing development. For example, they could immediately enter into a 24-month ground lease with options to extend. This would provide absolute site control to the developer and owner of the eventual improvements. If the developer and owner of the eventual improvements do not perform within the 24-month period, the lease reverts back to the public agency. If they do perform, a 99-year lease could then be executed. In addition, streamlined leases could be used in project after project, with simple addenda that relate to the particulars of each deal.

3. Planning & Approvals. Reduce the bureaucracy and inefficiency in government operations, particularly local planning and approval processes. In addition, modernize and streamline land-

use regulations to facilitate more affordable housing development. For example, Los Angeles has started implementing Transit Oriented Communities, which provides incentives like no parking requirements for PSH and that has significantly increased the number of PSH units approved in the city. California recently adopted a statewide law that streamlines and expedites approvals for affordable housing developments in cities that are not meeting their share of regional housing needs. In addition, Pinellas County, FL and Austin, TX have expedited their review processes and waived fees if the project involves dedicated affordable housing. Fairfax County, VA recently eased height and density restrictions near transit stations and Buffalo, NY; Hartford, CT; and San Francisco, CA have all eliminated parking requirements in certain neighborhoods for certain types of projects. Finally, Seattle recently rezoned several single-family neighborhoods as “residential small lot” areas to allow for smaller, denser multifamily housing that maintains a neighborhood’s character while providing greater affordable options.³⁷ Los Angeles could push these efforts even further by increasing the threshold for site plan review to 150 dwelling units from the current threshold of 50 units.

Furthermore, at a much more basic level of permitting, cities must improve the plan check process. There seems to be a lack of clarity and consistency among plan checkers and their interpretation of codes. A feedback loop should be established that can quickly and continuously elevate questions to supervisors who then issue directives to plan checkers so that consistency can be ensured. This is particularly true for housing developments, for which all cities are trying to streamline permitting. Finally, cities should eliminate duplicate review processes that may be

³⁷ Source: Urban Wire, “How Communities Are Rethinking Zoning to Improve Affordable Housing.” By Solomon Greene. June 12, 2019.

undertaken by multiple departments. For example, Los Angeles undertakes multiple accessibility reviews at both the building department and HCID (when public land or funds are involved), adding time and cost to project reviews. When multiple agencies perform similar reviews, the agency with a more stringent standard should take the lead in performing the review and all other agencies should defer to their approval in order to eliminate duplication of processes in an already long and complex permitting process.

Such efforts can reduce the time, cost and complexity of affordable housing development, allowing for more effective and scalable application of the RETHINK levers.

4. Financing. Expand access to new sources of stable, flexible rental subsidies that can facilitate the use of market-based financing options in the development of affordable housing. For example, the County of Los Angeles realized that subsidizing supportive housing for the County’s homeless population resulted in savings to the County’s bottom line. In fact, a RAND Corporation study found that for every \$1 the County invests in housing the homeless, they receive a return of \$1.20 in savings across other budget items like emergency room services and criminal justice. That is a return on capital of 1.2x or 20%. To put that in perspective, that is a better return than the 3-year, 5-year, 10-year, 15-year, and 20-year benchmark indices for Cambridge Associates LLC US Venture Capital, S&P 500, Russell 2000 and 3000, and NASDAQ Composite Price Indices.³⁸

Recommendations for Leveraging Assets

While not all communities can rely on access to the same scale and combination of assets for

affordable housing development, all communities have some assets that can be drawn on to facilitate application of the RETHINK levers.

1. Engage Philanthropy. Philanthropy can play a pivotal role by being an early adopter and risk taker in piloting new models and approaches. They can serve as vital connective tissue between community-based organizations with innovative solutions and the public and private sector stakeholders needed to scale those solutions. Philanthropy can also help support the critical data and research necessary to document the efficacy of new and innovative approaches. In Los Angeles, early adoption and commitment of resources by the Conrad N. Hilton Foundation helped create a facilitating environment for County officials to also make the necessary commitment of resources to fully capitalize the FHSP upon which RETHINK Housing relies. Additional financial support from the Hilton Foundation allowed RAND to complete its evaluation of the Housing for Health Permanent Supportive Housing Program, documenting the return on investment it provides.

2. Engage State & Local Government. State and local government partners can be valuable assets in facilitating the application of the RETHINK levers by creating facilitating policy environments and by providing large, flexible pools of capital from unexpected sources that can help take innovative new approaches to scale. In Los Angeles, DHS dedicated \$13 million from its budget to the FHSP, committing to the Housing for Health principle that providing housing to vulnerable patients can lead to better care and significant cost savings. Across the country, there is an opportunity to better align Medicaid and supportive housing resources, which have typically operated in silos though they often serve many of the same individuals. Better aligning

³⁸ Source: Cambridge Associates, “US Venture Capital: Index and Selected Benchmark Statistics.” March 31, 2019.

these resources, in particular to meet the needs of homeless individuals, could improve the cost and effectiveness of care.⁴⁰ State Medicaid programs have substantial flexibility to cover particular housing services and activities for Medicaid enrollees. As of July 2019, 36 states and the District of Columbia have chosen to adopt Medicaid expansion to the new adult group.⁴¹

3. Community Based Organizations. Community based organizations are invaluable resources in the effective application of the RETHINK levers. They can facilitate the identification of sites, organize and exert influence over policymakers – pushing them to create the necessary enabling policy environment - and can ensure that projects are designed to best meet the needs of the community in which they are located.

4. Private Sector. The private sector - including developers, capital providers, hospitals, healthcare systems, and others - can also play a vital role in ensuring the effective application of the RETHINK levers. Developers can RETHINK the size and scale of projects that are possible and the design of those projects that makes a smaller scale possible. Capital providers can RETHINK how they approach underwriting, being more open to relying on a steady, readily accessible stream of rental subsidy to make the affordable housing development equation balance without the need for capital subsidy. Hospitals, healthcare systems and others can begin to think more broadly about affordable housing as health – being more creative in thinking about how to re-align and redeploy resources to serve the most vulnerable.

³⁹ Source: American Journal of Public Health, "Frequent Emergency Department Visits and Hospitalizations Among Homeless People with Medicaid: Implications for Medicaid Expansion." 2015, November; 105(Suppl 5): S716-S722.

⁴⁰ Source: Medicaid and CHIP Payment and Access Commission (MACPAC), "Medicaid expansion to the new adult group."