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Using Private Equity To Aid Struggling Housing Authorities

The pandemic has created a financial nightmare for federal and state housing authorities who are being mandated to upgrade, improve infrastructure, and maintain service, all while dealing with a dramatic drop in revenue. One solution has been for these authorities to partner with private sources of equity.

By Miriam R. Milgrom

The pandemic has created a financial nightmare for both federal and state housing authorities: governmental authorities, both federal and local, have mandated requirements to upgrade, improve infrastructure, and maintain service during the pandemic, while at the same time, housing authorities are confronted with a dramatic drop in revenue. However, this set of facts spurs a unique opportunity for housing authorities to innovate, partnering with private sources of equity, utilizing the expertise and financial resources of private developers, who will prepare and process the application for federal low income tax credits (commonly referred to as LIHTC).

Housing authorities have a myriad of options with respect to restructuring ownership, while maintaining continued management and control of the property. These private/public partnerships provide the housing authority with much needed funds as well as creating new ongoing revenue streams, while at the same time, providing upgraded housing for its residents, without burdening local taxpayers. Depending on the condition of the housing, a property may qualify for a tear down and rebuild, renovation, or if the housing authority is fortunate to own or have the opportunity to acquire vacant land, the opportunity to construct new development. Most developments utilizing this structure are dedicated to projects for qualified seniors or to work force housing, many near the central downtown area of the local municipality.

The infusion of private capital relies on the housing authority partnering with a private developer who will take on the financial risk of construction. The private developer will secure the necessary tax credit investor (i.e., providing the equity), construction funds, and state funds and grants available for projects like these.

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I will write on this topic often, because there is no question that the times will require most if not all housing authorities repositioning their properties using private sources of funding.

The housing authority's selection of the developer as a joint venture partner is instrumental to the success of the redevelopment, often a step taken without the involvement of knowledgeable counsel. After a memorandum of understanding or development agreement is executed, it is generally too late to restructure material terms. While this news alert concentrates on housing authorities, the information translates well to other not for profits including religious institutions that seek to develop their excess properties, utilizing federal low income tax credits.

It is very important that the developer selected has the experience to identify, secure and close on multiple sources of funding for each project. The selected developer must be well versed in the NYS HCR application process, both for 4% awards and the highly competitive 9% awards. If a federal housing authority, the housing authority should also inquire as to the developer's experience with applicable HUD regulations. Although tax credits are federally based, they are awarded and administered by the state, and in the case of New York state, NYSHCR.

A housing authority's first step is to prepare with experienced counsel a request for proposals or request for qualifications. Counsel will advise as to the benefits and drawbacks of both. In my experience, the private developer chosen must have demonstrated extensive experience in developments which involve mixed-finance sources of funds, housing tax credit developments, tax exempt bonds and section 8 project based vouchers. Funding sources may include, in addition to federal low income housing tax credits, tax exempt bonds, HOME funds, public housing modernization funds housing trust fund loans, federal home loan bank grants, NYSERDA grants, Section 8 Housing Programs & Vouchers and Governor's Office of Storm Recovery.

Oftentimes, the developer may have a construction arm and a separate company established for asset management. There are pros and cons to the developer's principals having an interest in the construction company, and again advice of counsel is critical at the early steps, as well as later when the closings occur. Also, the housing authority must insure that the asset manager chosen has the necessary experience with the ongoing federal compliance tests, which are very complicated.

Further relevant experience on the part of the developer includes detailed knowledge of the design and engineering guidelines mandated by New York state, green building programs and green building programs including NYSERDA MPP, LEED and Passive House, and M/WBE & Section 3 participation requirements of New York state and other subsidy sources, and debt restructuring of the properties upon completion of construction.

Upon selection of a developer, the key agreement will be the development agreement between the housing authority and the developer. The housing authority has leverage to negotiate a significant percentage of the developer fees because it brings site control and the not for profit entity to the table. Also, the housing authority typically is instrumental in obtaining HUD and applicable local approvals. All fees and responsibilities of each party should be addressed in the initial agreement with the developer.

Conclusion

With the proven track record Fsof public private partnerships and use of LIHTC's in developing and rehabilitating housing properties, all levels of government will seek to replicate and expand the use of tax credits and make use of the private markets to develop municipal projects. Utilizing tax incentives efficiently will be the key to success.