

DATE: March 1, 2019
TO: Raymond Kan, Metro Vancouver
FROM: ECONorthwest and Enterprise Community Partners
SUBJECT: B3 IMPLEMENTATION TYPOLOGIES MEMO – FINAL

Introduction

To advance policies relating to the Metro 2040 Regional Growth Strategy and the Regional Affordable Housing Strategy, Metro Vancouver is exploring the feasibility of a transit-oriented affordable housing (TOAH) revolving loan fund (“the TOAH Fund”). Understanding that housing and transportation costs are closely linked and represent the two highest costs for most working households in Metro Vancouver, a TOAH Fund would blend several types of capital to fund purpose-built rental housing that is affordable to households earning up to 80% of the regional median household income (equivalent to \$60,000 per year as per the 2016 Census), in transit-oriented locations in the Metro region.

The first phase of Metro Vancouver’s work evaluated the development feasibility of new rental housing affordable to lower income households in transit-oriented locations across the region. Collaborators identified revolving loan funds as a potential tool to aid this rental housing development. Such funds have been established elsewhere, including several major U.S. metros.

In this second phase, a team of consultants led by ECONorthwest is evaluating the applicability of U.S. TOAH Fund models in the Metro Vancouver region, and will evaluate whether the fund model can be advanced in this region. Prior research completed in this phase includes an assessment of current practices relating to the potential for a TOAH Fund. CitySpaces, a local Vancouver planning consultant, prepared a memorandum on the local affordable housing development context that evaluated the needs for capital and capacity in the local industry. Enterprise Community Partners, a U.S. based affordable housing fund administrator and syndicator, prepared a memorandum that evaluates the U.S. context for TOAH Funds, identifying key takeaways and best practices from an administrative and implementation perspective.

Defining a TOAH Fund

We define a TOAH fund as a revolving loan fund that invests in transit-oriented affordable housing and requires a return on investment to the fund’s capital sources. Other types of financing or funding – e.g. zero-interest loans or grants – would not be considered “a fund” under this definition.

Purpose of this Memo

This memorandum summarizes key findings from an Experts Round Table event held in Vancouver in November 2018, and discusses the applicability and considerations needed for a potential TOAH Fund in the region. The Round Table event gathered industry leaders from the affordable housing sector, including philanthropic and public funders, developers of affordable and market-rate multifamily properties, lenders, and policymakers. These leaders confirmed the

gaps and needs found in the local context memo, and discussed the applicability of three potential fund models that are commonly used in the U.S.

This memorandum will feed into a final report that will conclude this second phase of work. The final report will recommend the most applicable TOAH Fund options, evaluate their potential effectiveness and deliverability, and identify pathways for implementation on a regional scale. A glossary of terms is included in the final report. Throughout this report, γ denotes that a term is defined in the glossary.



Expert Round Table Discussions

At the Experts Round Table, the consultant team guided a robust discussion with local leaders and industry experts about the applicability of revolving loan ^{γ} fund structures. These discussions helped the team understand how a revolving loan fund might or might not encourage the development of affordable housing ^{γ} in the Metro Vancouver region. Participants rotated through three breakout groups to consider how three different hypothetical fund models might meet local affordable housing sector needs.

Fund Definitions and Fund Applicability

As a starting point for the round table discussion, participants were asked to confirm or rebut the consulting team's understanding of a TOAH Fund's general applicability in the Metro Vancouver region. First, participants were introduced to the team's definitions of a TOAH Fund, like the affordable housing revolving loan funds that exist in the United States.

- We consider a *capital solution* to be a fund or facility that gathers public and/or private capital sources that expect repayment and likely a modest return. A fund of this type anticipates some loss commensurate with the lending product but would not offer grants from this capital pool as it would need to return capital to investors.
- We consider a *public subsidy solution* a source of funds that does not expect a financial return or repayment. This source of funding would likely come from public or philanthropic organizations that would expect a social return on their investment. These could be early grants, zero interest loans, or additional permanent subsidy for projects.

Secondly, the attendees were introduced to the team's understanding of the local affordable housing development context, particularly the challenges and gaps faced by developers in the region. Based on the intersection of the two topics—TOAH definitions and local development roadblocks—the consulting team offered several propositions to be confirmed or rebutted by attendees.

Table 1 below considers whether the challenges and gaps identified in the local Metro Vancouver affordable housing sector might be addressed by a *capital* or *subsidy* solution to meet the needs of the local affordable housing sector, or whether another solution is needed (e.g. policy changes, technical assistance, etc.). It is color coded: red indicates the TOAH Fund would not be a solution and yellow indicates it could potentially help. For many of the identified gaps, a fund may only address one part of the challenge and other solutions would need to be paired with a fund for it to be effective.

Table 1. Matrix of Local Affordable Housing Sector Limitations and Potential Fund Solutions

#	Gap / Limitation	TOAH capital fund solution?	Public subsidy fund solution?
1	Non-profit development knowledge capacity	Maybe (Fund could be momentum needed to grow non-profit development capacity; growing non-profit assets could improve development knowledge / sophistication)	Yes (Grants for technical assistance, capacity building, or training)
2	Non-profit financial / competitive capacity	Maybe (Line of credit / faster moving acquisition funds to increase non-profits' ability to compete)	Maybe (Flexible funds to increase non-profits' ability to compete)
3	Access to predevelopment funds	Maybe (Forgivable loans if project ends up infeasible)	Yes (Subsidy does not need to be repaid if project ends up infeasible)
4	Access to acquisition funds	Maybe (Patient equity to procure land – difficult if land is costly or unavailable)	Yes (Patient equity to procure land – difficult if land is costly or unavailable)
5	Rigid public sector terms (e.g. income levels, populations served, energy efficiency requirements)	No (New capital cannot affect other existing public sector terms)	No (Public subsidies will likely carry the same terms)
6	High construction costs in TOD markets	No (Interest-bearing loans are not a good financing mechanism to address high costs)	Yes (Gap subsidy or operating subsidy to cover high costs and service additional debt)
7	Limited private sector funds	Maybe (Consider PPPs or public sector alternatives, consider credit enhancement)	Yes (Offer gap funding ⁷ as either grants or loans)
8	Policy tools are constrained	No (New capital cannot affect other policy tools; fund could create momentum to spur policy changes)	No (Alone, new subsidies in the industry cannot affect other policy tools; could create momentum to spur policy changes)

Hypothetical Fund Products

To help spur the roundtable discussion, attendees were asked to respond to several suggested TOAH Fund options (included at the end of this memo). These hypothetical funds were posed as “crash test dummies” that would help everyone in the room understand how varied TOAH Fund options might perform in practice. The fund typologies – their terms, uses, and eligibility requirements – were based on the research into the local affordable housing sector and the key findings from U.S. based revolving loan funds. The three fund structures that formed the basis of discussion were:

1. **Predevelopment funding** – filling the predevelopment gap that exists due to CMHC’s recent policy shifts that now requires projects to have proven feasibility before receiving the region’s most common form of predevelopment funding. Now there is a lack of early predevelopment funding for project visioning, design, and other pre-construction, pre-award due diligence. Additionally, TOAH design development and engineering is substantially more complex and thus costly than other projects, suggesting that low cost predevelopment funds could be impactful in project feasibility.

The predevelopment fund concepts presented at the Round Table focused on early-stage predevelopment funding (for project visioning, feasibility and business planning) since funding for later-stage predevelopment funding (for permitting and funding awards) already exists.

2. **Acquisition funding** – filling the acquisition gap that provides low-cost funds for land acquisition (for new construction) or property acquisition (for rehabilitation or repositioning). Currently, most funding opportunities in the Metro Vancouver region require land to be contributed, or favor projects that already have site control.
3. **Permanent debt⁷ funding** – providing lower cost permanent financing⁷ after the construction of mixed-income properties has been completed. Such a fund might offer more advantageous terms than current permanent financing available in the region.

Each Round Table participant discussed and evaluated the different lending terms associated with each potential TOAH including: fund model, including fund type and purpose, eligible borrowers, eligible development projects, fund products (loans versus grants), interest rates, amortization length, and other terms. Discussion questions for each breakout group included:

- Would this type of fund solve the development gaps?
- What form would the fund need to take to be effective?
- Should we redefine the problem?
- What else needs to be done to meet this issue?
- What is needed from the different players in the group? (policymakers, funders, for profit developers, mission-based developers, others?)

Predevelopment Fund

There are two different needs for predevelopment financing: early stage funding (for project visioning, design, and other pre-construction, pre-award due diligence) and later stage funding (for permitting and funding awards). The Local Context memo prepared by CitySpaces noted that the bigger challenge facing the local affordable housing development sector is in early stage predevelopment financing. The predevelopment TOAH Fund concept discussed at the Round Table was created to fill this early predevelopment funding need. Table 2 below demonstrates the hypothetical fund terms discussed at the Experts Round Table.

Table 2. Predevelopment Revolving Loan Fund Terms

Potential Uses	Potential Borrowers	Funding Terms (Interest rates, loan terms, etc.)
<p>Multifamily mixed income, mixed-use rental projects with a minimum percent of affordable units.</p> <p>Acquisition only Revolving Line of Credit (ALOC) has worked well as long as approvals are quick, and the structure is designed well.</p> <p>Early stage predevelopment (e.g. project visioning, design, and due diligence)</p>	<p>Mission-driven developers that meet a minimum set of entity level covenants and criteria to ensure that there is sufficient financial strength, organization experience and staff capacity to execute if they have this tool.</p>	<ul style="list-style-type: none"> • Full, partial or no recourse: allow recourse and/or security to evolve as the development opportunity matures or additional funds are drawn down. • Security, coupled with recourse, will determine the marketability of this product type. Consider un-securing a portion of the loan. • Interest only repayment with takeout at acquisition financing close; potentially converting to secured at acquisition with repayment at construction close. • 2-5 years, dependent on borrower and project predevelopment stage.

Source: Enterprise Community Partners

This fund concept was aimed at filling the gap identified in the local development sector. CitySpaces notes that non-profits often have difficulty accessing capital in the early stages of development due to limited funding opportunities or due to less development knowledge or capacity. However, many projects in the early stages of predevelopment planning end up infeasible and cannot repay loans. CMHC and Vancity recognize this and offer grants for this stage of development. A revolving loan fund cannot offer many grants – its main product needs to be loans.

Table 3 below describes the key themes of the discussion, and suggests implementation steps for each to continue evaluating the applicability for predevelopment financing.

Table 3. Predevelopment Fund Discussion Points

Term	Participant Direction	Implementation Steps
Eligible Borrowers	Participants thought that access to predevelopment funding should be limited to non-profit sector developers.	Establish a list of borrower criteria, e.g. non-profit status, development experience, available collateral, etc.
Eligible Uses	Participants think there is need in the very early stages of project visioning, design, and feasibility. Other funding – such as CMHC Seed funding – is available for later stages of predevelopment once the project is determined to be financially and operationally feasible.	Establish a list of criteria governing eligible funding uses and timeframes, e.g. architecture and design, funding applications, site evaluation, meetings and conversations with planning departments.
Eligible Products	Participants suggested that funding for projects in this early stage of predevelopment is much riskier, as it is not clear that the project will proceed to development. As such, funding at this stage would need to be grants instead of loans, and the ability for repayment was limited.	Refine the needs for loans versus grants, considering different types of loan products, e.g. zero-interest, low-interest, forgivable, interest-only payments, etc.
Capital Sources	Participants agreed that public subsidy or philanthropic funding would be needed for predevelopment grants.	Establish a list of potential funders, their amounts and financial return expectations.
Funding Terms	Participants considered a 1 to 3 year timeframe acceptable for predevelopment. Extensions may be necessary if rezoning was required.	Establish funding terms, working with local affordable housing developers to ensure terms meet their needs.
	Participants agreed that the need for early stage predevelopment funding was about \$80,000 to \$150,000 per project.	Establish criteria for initial timeframe and amount, as well as criteria for extensions or increases (e.g. what do borrowers need to prove for an increase/ extension?)

Although most agreed on the need for early stage predevelopment funding, Expert Round Table participants did not have unanimous consensus on the most likely borrowers (e.g. should market rate developers be allowed?), sources of fund investment capital (e.g. would the fund need patient capital?), and overall use of the funding (e.g. how long should the predevelopment stage last?).

Most participants agreed that a revolving loan fund was not an appropriate funding mechanism for projects at this stage of development due to the amount of uncertainty in a project moving forward and the uncertain likelihood of repayment. However, there was no consensus to abandon research into filling this predevelopment gap. While later-stage predevelopment funding was not one of the critical gaps identified in the Local Context memo, projects with more proven feasibility are able to carry debt and could benefit from lower interest rates from a TOAH Fund.

Acquisition Fund

The acquisition-focused TOAH Fund was envisioned to fill a need for funding to acquire or assemble land for development of (newly constructed) affordable rental housing, or property acquisition (for rehabilitation or repositioning) in transit-oriented sites. In the Metro Vancouver affordable housing sector, most funding sources require land to be contributed to a project, or favor projects that already have site control, so acquisition loans could help strengthen the project pipeline. Acquisition lending has been the most active segment of TOAH Fund activity in the U.S. context, so examining this with the Experts Round Table participants was a priority. Table 4 below lists the terms for this type of fund that the consultant team presented for feedback.

Table 4. Acquisition Revolving Loan Fund Terms

Potential Uses	Potential Borrowers	Funding Terms (Interest rates, loan terms, etc.)
<p>ETOD projects in high-impact areas/target geographies</p> <p>Multifamily mixed income, mixed-use rental properties with a minimum % of affordable housing units in mixed-income deals.</p>	<p>Non-profit or for-profit developers with sufficient financial strength, organization experience and staff capacity to execute if they have this tool.</p>	<ul style="list-style-type: none"> • Loan to value - requirement drives a developer's required investment in a site • Interest Rates - many pricing structures exist depending on the needs of funders and clients. For longer-term loans, fixed-rate pricing adds certainty for borrowers, requires lower rates to be a viable option • Recourse – Full, partial or none. Could allow recourse and security to evolve as the development opportunity matures or additional funds are drawn down. • Repayment – Interest only with takeout coming at the close of construction or permanent financing • 3-5 year term

Source: Enterprise Community Partners

There was generally consensus from participants that acquisition funding was not an applicable use for a TOAH Fund in the same way as in the U.S. Participants agreed that there is a strong need for acquisition financing, but the very high cost of bus and rail-adjacent land in the Metro Vancouver region was seen as a barrier. With land costs so high, projects must source land from public or non-profit owners, typically redeveloping a site that is currently lower density multifamily housing or a community facility.

Further, participants noted that this fund would not generally help the local non-profit sector as they often already have land, and are asset rich, cash poor. Funding for land acquisition, site assembly, or redevelopment could be a (smaller) part of a TOAH Fund focused on later stage predevelopment financing. This fund, as imagined, would not help increase capacity or balance sheets for leveraged future financing.

Due to the general agreement that financing market acquisition was not likely a viable use for a TOAH Fund, we did not evaluate the implementation steps for key discussion points.

Post-Construction / Permanent Financing Fund

The post-construction/permanent financing-focused TOAH Fund concept shared with roundtable participants was envisioned to fill a need for funding lower cost permanent debt for affordable projects, thereby reducing ongoing operating expenses. It would target mixed-income properties with adequate cash flows. The fund would have terms that are more flexible than current federal or provincial sources, allowing developers to be more creative in how they reduce rents, income-mix units, and put the development deal together. Table 5 below lists the terms that the consultant team presented to the Expert Round Table participants for feedback on the applicability of this type of model in the Canadian context.

Acquisition Fund became Predevelopment Fund

Conversations shifted toward a hybrid fund model that would likely be more beneficial to the non-profit sector: a TOAH Fund that is essentially a large predevelopment fund with flexibility to cover predevelopment and relocation (hard and soft costs), to free up and entitle site redevelopment.

Participants noted that rezoning a site and relocating current occupants can cost \$1.0-\$1.5 million, limiting these projects to very well capitalized developers.

Table 5. Post-Construction or Permanent Financing Revolving Loan Fund Terms

Potential Uses	Potential Borrowers	Funding Terms (Interest rates, loan terms, etc.)
Mixed income or high impact market rate TOD developments	Strong developers with substantial experience and track record of success with mixed use/mixed income projects, and appropriate financial strength to support equity partnership.	<ul style="list-style-type: none"> Financial return depends on market and product Loan would be maximum 25% of total sources Distributions would be typical equity terms, including hurdles and waterfall to repay different investors with first, second position cash flows 5-10 year money
Equity joint venture in ownership entity, with a maximum of 90% limited partner interest, with sponsor as General Partner or Managing Member.		
Mini-perm loan - provide a moderately more patient source of equity to allow for asset and market appreciation		

Source: Enterprise Community Partners

Based on the conversations at the Experts Round Table, there is meaningful potential for a post-construction / permanent financing TOAH Fund to operate in the region, however there was a desire that the products be distinct from what was initially proposed by the consulting team. Table 6 below describes the key themes of the discussion, and suggests implementation steps for each to continue evaluating the applicability.

Table 6. Post-Construction / Permanent Financing Fund Discussion Points

Term	Participant Direction	Implementation Steps
Eligible Borrowers	<p>Participants thought that this financing would best serve the region's goals by focusing on non-profit borrowers delivering non-market projects.</p> <p>That said, participants did not necessarily want to exclude non-profit housing providers that sought to deliver mixed-income projects should that be the best way to further their non-profit missions.</p>	Establish a list of desired borrower criteria, e.g. non-profit status, development experience, available collateral, etc.
Eligible Uses	<p>Convertible:⁷ Most participants thought this fund would be most useful as a simplified convertible debt product, one that funds both construction and the operating asset for a period of five years after occupancy. It was hoped that this product could serve as the primary or only debt source for each development project (90% of project costs), supplanting existing construction and mini-perm debt sources.</p> <p>Mezzanine:⁷ While considered lower impact for the delivery of non-market projects, participants were intrigued by a mezzanine debt product that would serve as permanent gap financing (max 25% of project costs) but be structured like equity⁷ with deferred payments.⁷</p>	Establish a list of desired funding uses
Capital Sources	<p>Convertible: Participants suggested that this fund could borrow the best features of multiple existing programs, perhaps blending them into a single product with one point of contact, one set of terms, and a single underwriting effort. Participants were interested in the features of the following existing programs:</p> <ul style="list-style-type: none"> • BC Housing <i>HousingHub</i> – Appreciate product but non-market housing developers would appreciate different terms related to BC Housing's required operating agreements • New Markets Funds – Appreciate fixed rates but only offers take-out financing and capacity is relatively small (\$25M) • Vancity "ESCROW Product" – Appreciate convertible debt, but this product has only been used on a handful of occasions • Vancity impact investments - Appreciate the flexibility of Vancity's terms but would need to be much larger scale or layered with other funds to have regional impact <p>Mezzanine: Participants identified the New Markets Fund as a model, but the existing fund's \$25M capacity was considered insufficient to have broad impact. Mezzanine debt requires a slightly higher rate of return which can impact applicability of use for affordable housing developers.</p>	Establish a list of potential funders, their amounts and financial return expectations.
Funding Terms	<p>Convertible: Participants suggested that the key term that made this hypothetical product interesting would be a fixed interest rate, which would provide certainty for decision makers.</p> <p>Mezzanine: Participants agreed that a fixed rate could change proformas and go/no-go decisions on projects. Participants suggested that the existing New Markets Fund terms were attractive and that scaling this type of financing could help address limited private sector funds in the local industry. Mezzanine debt requires a slightly higher rate of return which can impact applicability of use for affordable housing developers.</p>	Establish desired funding terms, working with local affordable housing developers to ensure terms meet their needs.

In general, participants thought that two new funding sources deserved further exploration, though others may also be identified during subsequent exploration and limits on available equity may limit the uptake of such products. Participants determined that there would be interest in a fixed-rate⁷ mezzanine debt/equity product. While a mezzanine debt product was intriguing, participants asked why a publicly led TOAH effort would not explore a more robust solution that provided more than gap financing for worthwhile projects. The conversation evolved into a discussion of a convertible debt product that would be a “one-stop” source of construction debt and “mini-perm” financing for non-market rental housing projects. It was recognized that if the “one-stop” product were to fund numerous projects, it would require a very large fund, which may be an impediment to its implementation. For this reason, both options remained on the table during the discussions.

Takeaways

Serve the nonprofit sector

The conversations at the Expert Round Table provided helpful feedback on the three potential TOAH Fund models. It was generally agreed upon that any fund put forth for implementation consideration should only serve the non-profit sector. Market rate developers have enough development experience and large enough balance sheets to compete in this market. In addition, the fund would not likely be able to offer enough incentives to encourage market rate developers to bring rents down to affordable levels targeted.

Instead, the fund should focus on increasing the financial capacity and competitive ability for the local non-profit sector. Patient capital⁷ at any stage of the development process would go far in helping these organizations achieve their goals.

Predevelopment gaps won't be solved with a revolving loan fund

In addition, it was also clear that a predevelopment revolving loan fund – seeking to aid in the visioning, feasibility, and due diligence stage – would not be appropriate. At this stage, before a project is considered feasible, participants felt that zero-cost financing (grants) would be the most helpful, meaning that the funds could not revolve to generate financial return and that a TOAH Fund was not applicable.

Participants agreed on the need for predevelopment financing, since CMHC's Seed funding shifted toward funding projects that have proven feasibility, so research into financing tools for this stage of development should not be abandoned. Seeing as the most likely source of low-cost grants is public capital, advancing this type of tool will be difficult since the voting public generally wants to see direct outcomes for public spending.

Post construction / permanent financing and acquisition financing need more evaluation

As Metro Vancouver continues to evaluate the implementation options of a construction / permanent financing or an acquisition financing TOAH Fund, it will need to ensure that the fund's uses are aligned with the priorities of investors (including the public if public funds are blended). It will be important that the fund helps to fill the gaps of the local industry.

Experts' Round Table Discussion Cut Sheets



For Discussion Purposes only

Acquisition Concepts

Acquisition capital is the most commonly offered loan product among transit oriented development (TOD)-specific funds in the United States. Many of the active TOD funds in the U.S. operate in tight real estate markets, where quick-strike acquisition capital is a necessity to compete with market-rate developers. In these contexts, acquisition funds aim to secure site control while borrowers secure project financing, and often cover some of the early design and entitlement expenses.

Potential Borrowers and Uses

Finding appropriate acquisition capital that can stretch to meet the needs of an affordable housing project is typically the biggest hurdle for mission-aligned nonprofit TOD developers. Offering flexible acquisition capital helps mission-aligned developers carry out what they are already best suited for: responsible, equitable development in the communities they know well. Community-based nonprofit developers are typically well-attuned to the best potential sites for affordable housing TOD development and may even have relationships with current owners that they can leverage before a property goes on the market. Equipping mission-driven developers to compete for transit-accessible sites is a critical building block to shaping a more equitable future for these neighborhoods and regions. Without access to acquisition capital for mission-aligned developers, transit-adjacent properties will be acquired by market-rate developers using conventional capital available in the market.

Acquisition/Rehab Loan Product

This product would be targeted for acquisition of TOD-adjacent sites with existing improvements for the purposes of affordable housing, mixed-income development, or mixed-use development. In recent years, funds in some markets have looked to this approach to redevelop sites to their full zoned capacity, have income from existing operations cover some of the interim interest costs, and, in the case of existing housing, manage the transition of residents that might otherwise be displaced. The downside is that existing building typically cost more at the acquisition stage and can have more environmental and relocation costs and complications.

Potential Fund Terms and Discussion Questions

- **Eligible Borrowers** – Non-profit or for-profit developers with sufficient financial strength, organization experience and staff capacity to execute if they have this tool.
 - What minimum requirements/covenants would you impose?
- **Loan to Value(LTV)¹** – This requirement drives a developer's required investment in a site
 - Are target geographies sufficiently mature that sale prices are supported by appraisal?
 - Will sites need any entitlement or rezoning funded by this loan?
 - How will LTV limit otherwise eligible borrowers?
- **Project Type** – ETOD projects in high-impact areas/target geographies
 - What ETOD outcomes should the fund achieve?
 - Is there an ecosystem of mission-aligned developers?

¹ Typically expressed in percentage terms, this is the amount of the loan relative to the value of the collateral. In these funds the collateral is typically the site being purchased.

- Who determines the social benefit criteria, and are they local or community driven?
- What submarkets would be most appropriate to expand organizational capacity and acquire sites?
- **Eligible Uses** – Multifamily mixed income, mixed-use rental properties with a minimum % of affordable housing units in mixed-income deals.
 - Should mixed income, mixed tenure be eligible?
 - Are both new construction and preservation/rehab projects eligible?
- **Term** – Part of the specific challenge of ETOD addressed is the complexity inherent in the deal structure, and the need for more patient capital in response.
 - How long of a term is reasonable and achievable (3-5 years)?
- **Interest Rates and Fees** – Many pricing structures exist depending on the needs of funders and clients. For longer-term loans, fixed-rate pricing adds certainty for borrowers.
 - How low? Fixed or variable? Origination or draw fees?
 - Longer terms require lower rates to be a viable option
- **Recourse²** – Full, partial or none. Could allow recourse and security to evolve as the development opportunity matures or additional funds are drawn down?
 - Could a portion of the facility, likely grant funded, be non-recourse or partial recourse?
 - What other characteristics would need to be present for this to occur?
- **Repayment** – Interest only with takeout coming at the close of construction or permanent financing

² Recourse debt is debt backed by collateral from the borrower. In case of default, the lender collects the collateral instead of foreclosing on the property.

Post Construction/Permanent Financing for Mixed-Income TOD

The richness and complexity of healthy equitable transit-oriented communities is also amongst the greatest challenges in their development. The multifaceted, dynamic and diverse mix of uses interrelated with each other and public infrastructure creates a challenging development environment under the best of circumstances. Therefore, a healthy environment with a range of housing options attractive to market rate investment is a critical indicator of functioning neighborhoods.

Potential Borrowers and Uses

Strong developers in strong markets are seeking equity resources that support mixed use and/or mixed income development programs. The complexity of this execution minimizes or eliminates traditional equity players - developers with an interest in a double or triple bottom line product type that contributes to equitable transit-oriented development (ETOD) principles of the local area, but lack this key piece of the financing stack to execute on that vision.

This equity product would offer a below market rate of return while recognizing and accommodating the additional complexity of TOD and mixed income/mixed use developments. In return, these investments could deliver ETOD benefits including affordable and/or workforce housing, and the demonstrated higher value appreciation that quality TOD has delivered to investors in comparison to other multifamily development.¹

Given the market strength and subsidy constraint of our core regions, a mixed income- friendly equity fund has the potential to simultaneously create a desirable niche multifamily investment product while accelerating production of affordable homes by leveraging market rate and/or workforce multifamily development.² A flexible equity product might also allow for a richer mix of income types, including workforce housing that currently lacks a feasible execution.

Potential Fund Terms and Discussion Questions

- **Developer profile** – Strong developers with substantial experience and track record of success with mixed use/mixed income projects, and appropriate financial strength to support equity partnership.
- **Project Type** – Mixed income or high impact market rate TOD.
 - Are there submarkets where wood frame market rate could subsidize affordable units?
- **Product Type** – Equity joint venture in ownership entity, with a maximum of 90% limited partner interest, with sponsor as General Partner or Managing Member.
 - These terms refer to tax credit financing in the U.S.
- **Eligible Uses** – Acquisition? construction costs? Mini-perm?
- **Return** – Dependent upon market and product,
 - Would market component be more likely to be for sale or rental product?

¹ <http://www.reconnectingamerica.org/assets/Uploads/cpatransport2.pdf>

² For instance, a 200 unit multifamily opportunity that is developed in an 80-20 structure could produce 40 very low income homes in a far more cost effective manner than trying to subsidize a stand-alone affordable community, all while producing a healthy mix of incomes within the TOD.



- **Sizing** – Maximum 25% of total sources.
 - Maximum per project?
- **Distributions** – Typical equity terms, including hurdles and waterfall.
 - Could for sale product return bulk of capital, giving strong overall IRR with modest yield requirements in out years?
- **Term** – Five to ten years.
 - Due to the nature of the need for this product (i.e. transitioning markets), this fund is intended to provide a moderately more patient source of equity to allow for asset and market appreciation.
 - Disposition or refinance at the end of the term?

Predevelopment Concepts

Transit oriented developments are often more complicated than typical commercial real estate transactions, and therefore developers require more flexible sources of financing during early stages of predevelopment. These developments can be difficult to cultivate because of early costs and slower schedules resulting from their complexity. Some of these early costs of equitable transit-oriented development (ETOD) include detailed environmental analysis, complicated site planning involving infrastructure improvements, extensive land assemblage planning and negotiation, complicated public-private partnership structures, option payments, etc. The inclusion of affordable housing, with additional regulations, lower rents, and higher funding gaps further complicates transit oriented development.

Potential Borrowers and Uses

Without access to flexible predevelopment financing, most developers are unable to pursue complex ETOD opportunities, and will instead gravitate to more “vanilla” opportunities that will attract conventional capital available in the market. Additionally, many community-based nonprofit developers, while having some deal experience and deep roots in the communities they serve, do not have the financial capacity to access capital sufficient to build ETOD at the scale. Equipping mission driven developers to compete for transit accessible sites is a critical building block to shaping a more equitable future for these neighborhoods and regions.

Unsecured Early Predevelopment Financing

This product would be targeted as early predevelopment capital to facilitate challenging ETOD opportunities that might not qualify for more conventional predevelopment sources. Unsecured predevelopment loans or recoverable grants would unleash the capacity and creativity of qualified developers and allow for development of more ETOD of better quality. This product would have a two-fold impact; expanding the pipeline in target markets, and creating capacity building opportunities for qualified entities that lack the capital resources to move complicated ETOD opportunities forward.

Potential Fund Terms and Discussion Questions

- **Eligible Borrowers** – Mission-driven developers that meet a minimum set of entity level covenants and criteria to ensure that there is sufficient financial strength, organization experience and staff capacity to execute if they have this tool.
 - What minimum requirements/covenants would you impose?
- **Project Type** – ETOD projects in high-impact areas.
 - What ETOD outcomes are worthy of a specialized, unsecured predevelopment debt product?
 - Who determines the social benefit criteria, and are they locally or community driven?
 - What submarkets would be most appropriate to expand capacity.
- **Eligible Uses** – Multifamily mixed income, mixed use rental properties with a minimum % of affordable housing units in mixed income deals.
 - Should mixed income, mixed tenure be eligible?

- **Interest Rates and Fees** – Many pricing structures exist depending on the needs of funders and clients. For longer-term loans or draws, fixed-rate pricing is always preferred.
 - How low? Fixed or variable? Origination and/or draw fees?
- **Recourse¹** – Full, partial or none. We could allow recourse and/or security to evolve as the development opportunity matures or additional funds are drawn down?
 - Could a portion of the facility, likely grant funded, be non-recourse or partial recourse?
 - What other characteristics would need to be present for this to occur?
- **Repayment** – Interest only with takeout coming at the close of acquisition financing, or potentially converting to secured at acquisition with repayment at construction close.
- **Term** – Part of the specific challenge of ETOD addressed is the complexity inherent in the deal structure, and the need for more patient capital in response.
 - How long of a term is reasonable and achievable (3-5 years)?

(Acquisition and) Predevelopment Line of Credit

Better access to entity level lines of credit or other financing vehicles could (1) allow strong, experienced housing developers to build affordable or mixed income pipelines through more nimble and competitive acquisitions capacity, and/or (2) invest deeply in the bolstering the balance sheet of smaller non-profit groups, allowing them to acquire sites and advance projects with more certainty around the risk to the organization. Equipping mission-driven developers to compete for transit accessible sites is a critical building block to shaping a more equitable future for these neighborhoods and regions. This fund would allow large to medium sized developers predictable access to acquisition and predevelopment financing to build pipelines through more nimble and competitive acquisitions capacity.

Potential Fund Terms and Discussion Questions

- **Eligible Borrowers** – Mission driven developers (nonprofit or for profit) that meet a minimum set of entity level covenants and criteria to ensure that there is sufficient financial strength and capacity to execute if they have this tool. Management team, experience and financial strength will be important.
 - What minimum requirements/covenants would you impose?
- **Product Type** – Acquisition only Revolving Line of Credit (ALOC) has worked well as long as approvals are quick and the structure is designed well.
 - Are there aspects of TOD that need to be further considered for product effectiveness?
- **Eligible Uses** – Multifamily mixed income, mixed use rental properties with a minimum % of affordable housing units in mixed income deals.
 - Should each deal have a minimum % of square feet dedicated to community uses?
 - Should homeownership be considered?
- **Interest Rates and Fees** – Many pricing structures exist depending on the needs of funders and clients. For longer-term loans or draws, fixed-rate pricing is always preferred.
 - How low? Fixed or variable? Origination and/or draw fees?

¹ Recourse debt is debt backed by collateral from the borrower. In case of default, the lender collects the collateral instead of foreclosing on the property.

- **Recourse** – Full, partial or none.
 - Could a portion of the vehicle be non-recourse or partial recourse?
- **Security**² – security, coupled with recourse, will be issues that will determine the marketability of this product type. Developers are really focused on these issues.
 - First liens, second liens on real estate?
 - Other collateral acceptable?
 - Could a portion be unsecured?
- **Repayment** – Interest only, with takeout at the close of construction financing.
 - Amortizing repayment (consistent monthly payment of principal and interest)?
 - Balloon payments (low interest repayment for a period of time then a larger payment)?
 - Cash flow dependent (interest accrues and is only paid if the property has operating cash flow)?
 - Others terms?
- **Term**³ – longer-term including an origination period of 2-3 years to start.
 - How long for a facility?
 - How long for an individual loan/draw?
 - Five years, seven years, ten years, other?

² A loan is secured when the borrower pledges an asset – collateral or a property deed – against default. Unsecured loans are riskier and often carry higher interest rates.

³ The loan term is the length of time the borrower has to repay the loan. Terms vary depending on the use of the loan – predevelopment loans would just cover the first few years of development concept and design, while bridge loans may cover the time between funding awards and the construction loan.