

# Memorandum



TO: Economic Transformation, Stabilization & Workforce Development Advisory Commission  
 FROM: Cheryl Cohen, Division Administrator, Commerce  
 DATE: July 30, 2021  
 SUBJECT: Gap Financing for Affordable Housing Developments Impacted by COVID-19

**Overview:** Montana Housing with the Department of Commerce proposes to direct up to \$15,000,000 of ARPA Section 602 funds under HB 632 Section 12(1) to ensure affordable housing in the development pipeline that has already received federal funding awards or Housing Credit allocations in prior years will be successfully completed. These funds will provide critical gap financing for projects experiencing significant development cost increases due to COVID-19 related worker shortages, supply chain disruptions, and price escalations in key building materials like lumber. These cost escalations have jeopardized the financial feasibility of these projects, and gap funding is critically needed to ensure affordable housing developments that the state of Montana has already invested in will be successfully completed and placed in service.

**Background:** A total of seventeen (17) affordable housing pipeline projects responded to a July 2021 survey summarizing COVID-19 impacts on development costs. The total gap financing need indicated by developers is \$19.5M, with the average percentage increase in development cost at nearly 17%. These projects include nearly 1,000 affordable rental homes (995) and are geographically distributed across the state. Developers were asked to outline specific reasons for cost increases, how cost increases are related to COVID-19, and to outline what additional resources and cost cutting techniques have already been pursued to address increased costs.

**Summary of Survey:**

Housing Type	Construction Type	County	# Units	Gap funding needed	% Increase	Housing Credit (4% or 9%)	HOME	HTF
Family	Acq/Rehab	Big Horn	43	\$1.9m	25%	Yes		
Senior	New	Cascade	36	\$427k	5.7%	Yes		
Senior	Acq/Rehab	Deer Lodge	74	\$375k	18.3%	No		Yes
Family	Acq/Rehab	Gallatin	41	\$300k	2.6%	Yes		Yes
Family	Adaptive Re-Use	Fergus	16	\$350k	12.7%	Yes	Yes	
Family	New	Flathead	38	\$280k	3.4%	Yes	Yes	Yes
Family	Acq/Rehab	Hill	60	\$250k	15%	Yes		Yes
Family	Acq/Rehab	Hill	32	\$832k	25%	Yes		Yes
Family	New	Lake	24	\$201k	3.5%	Yes	Yes	
Family	Acq/Rehab	Lewis & Clark	44	\$150k	2.2%	Yes		Yes
Family	New	Missoula	200	\$2.5m	15%	Yes	Yes	
Family, PSH	New	Missoula	202	\$2.5m	19.5%	Yes	Yes	Yes

Family	Adaptive Re-use	Park	37	\$510k	20%	Yes	Yes	
Family	New & Adaptive Re-use	Yellowstone	29	\$3.4m*	44.5%*	Yes		
Family	New	Yellowstone	19	\$1.6m	32.8%	Yes	Yes	
Family	New	Yellowstone	38	\$2.4m	26.8%	Yes	Yes	
Senior	Acq/Rehab	Yellowstone & Carbon	62	\$1.5m	16.4%	Yes		

\*Project includes other public service uses (shelter, medical facilities, and vocational training) in addition to affordable housing units. Scope involves adaptive re-use of 100-year building. The \$3.4m ask represents approx. 19.5% of total 44.5% cost increase with developer contributing nearly \$8m from capital campaign.

**Allocation Request and Deadline:** To ensure prompt availability of funds to meet immediate needs of projects under development, propose Advisory Commission take action during the August 12, 2021 meeting to recommend the Executive allocate \$15M of ARPA Section 602 funds to provide gap financing for affordable housing developments impacted by COVID-19. Montana Housing will work with the Executive branch and budget office to rapidly deploy funds to impacted projects.

**Structure:**

**Eligibility:** Eligible applicants would be limited to affordable housing projects in the Montana Housing development pipeline previously allocated Housing Credits (9% or 4%) or awarded HOME or HTF funds. Priority would be given to the seventeen (17) projects that responded to the July 2021 COVID-19 gap financing need survey. Developers will be asked to submit an updated Uniform Application, documenting the shortfall the project is experiencing, describing steps the development team has taken to fill the funding shortfall and identify the remaining gap financing request needed to successfully complete the project. In accordance with ARPA Sec. 602 requirements, eligible costs for gap funds are limited to those incurred during the “Covered Period” beginning March 3, 2021. Montana Housing staff will assess the updated Uniform Application, developer narratives and documentation to verify the shortfall identified and then determine the amount of gap financing needed to ensure the project’s financial feasibility.

**Proposed Funding Terms:** Gap financing would be provided in the form of a grant. These projects have already met underwriting standards set by investors as well as underwriting standards of public funders. Developers have exhausted alternative cost cutting techniques (i.e., value engineering, securing commitments of favorable terms – or refinancing to more favorable terms - with private financial institutions, successful capital campaigns and even full project re-configurations in some cases). The margins on these projects are incredibly tight, making the additional debt of loan structures unworkable. Private market project investors will likely be unable to approve the addition of a new loan. Even a “soft loan” approach with extended 40-year term at 0% interest and payments cash flow dependent could present an unsurmountable hurdle in getting these projects to the finish line, in addition to adding significant administrative burden and cost generated by the long-term nature of a loan program.

Finally, we still do not have clarity from the U.S. Department of the Treasury on how a loan program can be structured, adding uncertainty and increased audit and compliance risk (and to meet the immediate need these projects are experiencing, this program must move forward now).

- Maximum grant amount of \$2 million per project.

- In the event application of Treasury Interim Final Rule or Reporting and Compliance Guidance results in a determination that a pipeline project is ineligible for ARPA Section 602 funds, Montana Housing may shift funds that would have been allocated to the ineligible project to another eligible project. Should this scenario occur, Montana Housing may increase the maximum grant amount to \$2.5 million per project.
- Montana Housing would assess any remaining funding gaps not covered by this \$15M ARPA 602 allocation on a case-by-case basis and determine whether gaps can be closed with other existing resources.

***Use of Existing Programs:*** Gap financing grants would be provided under the framework of existing programs administered by Montana Housing staff, such as the HOME Program, Housing Trust Fund, and various Multifamily Development programs. The additional ARPA 602 funds and associated Treasury requirements may be incorporated within the project’s existing HOME or HTF contract via a contract amendment process. This approach could be used for 13 of 17 projects. The remaining four projects could have the proposed grant administered by Montana Housing’s Multifamily Development team, also via an executed contract. Montana Housing can utilize the expertise of our long-standing outside legal counsel to ensure deployment of grant funds will adhere to Treasury requirements. The Montana Housing staff and legal counsel have prior experience deploying funds under the 2009 American Recovery and Reinvestment Act via a written program agreement.

HOME Investment Partnership Program (HOME)-

The federal HOME Program was established in 1990 and is set forth in Subpart A, Title III of the Cranston-Gonzalez National Affordable Housing Act. The purpose of the HOME Program is to increase the number of families served with decent, safe, sanitary, and affordable housing and expand the long-term supply of affordable housing. This mission fits within the Department of Commerce’s statutory functions to survey and investigate housing needs in Montana, maintain and disseminate information on housing assistance programs, and promote research and development in matters relating to, or affecting the provision of decent, safe, and sanitary housing in a suitable living environment. (Section 90-1-106, MCA.).

Housing Trust Fund (HTF)-

The federal Housing Trust Fund Program was established in 2008 under Title I of the Housing and Economic Recovery Act of 2008, Section 1131. The HTF Rule found in 24 CFR Part 93 made the consolidated plan regulations at 24 CFR Part 91 applicable to the HTF. HTF is an affordable housing production program that will complement existing federal, state, and local efforts to increase the supply of decent, safe, and sanitary affordable housing for extremely low income (ELI) families, particularly the homeless, disabled, elderly, and other disadvantaged populations. The HTF program helps qualified subrecipients direct funds to foster and maintain the construction, rehabilitation, and preservation of affordable rental housing for Montana’s most vulnerable families. This mission fits within the Department’s statutory functions to survey and investigate housing needs in Montana, maintain and disseminate information on housing assistance programs, and promote research and development in matters relating to, or affecting the provision of decent, safe, and sanitary housing in a suitable living environment. (Section 90-1-106, MCA.)

Multifamily Development Programs-

- Housing Credits (4% and 9%)
- Multifamily Loans (e.g., Coal Trust Homes Program; Housing Montana Fund; Insured Loan Program; General Obligation Bonds)

**Resources Needed to Execute:**

- Allocation or Program Specialist – (0.5 FTE)

- HB 632 Section 12(4) Up to 3% of the funds appropriated in this section may be allocated for administrative costs.

**Performance Metrics:**

- Support development of nearly 1,000 affordable rental homes
- Leverage existing resources - Housing Credits (4% and 9%), HOME, and Housing Trust Fund
- Preserve current year Housing Credit, HOME and HTF funds for new development. Absent this allocation, a significant portion of current year funds will likely need to be directed to pipeline projects to ensure successful completion, drastically hindering production of critically needed new affordable homes.

Awarded projects will need to meet both HB 632 Section 27(2) Performance measures requirements and Department of U.S. Treasury [Coronavirus State Fiscal Recover Funds Compliance and Reporting Guidance](#). Montana Housing proposes the following generally applicable outcomes under HB 632 Section 27(2):

- # of affordable homes completed
- % of ARPA 602 funds respective to total of all other project financing sources (leverage)

Treasury requires Project and Expenditure Quarterly and Annual Reports on projects funded, expenditures, and contracts and subawards over \$50,000:

- Projects: Project Name; Identification Number (created by recipient); Project Expenditure Category (3.10 Housing Support: Affordable Housing); Description; Status of Compliance
- Expenditures: Current period obligation; Cumulative obligation; Current period expenditure; Cumulative expenditure
- Project Status: Not Started; Completed less than 50 percent; Completed 50 percent or more; Completed
- Project Demographic Distribution: Physically located in Qualified Census Tract (QCT); Primary intended beneficiaries live within a QCT; Eligibility criteria of intended beneficiaries earn less than 60% of median income; Eligibility criteria of intended beneficiaries include 25% with income below federal poverty line

The above summary is not inclusive of all Treasury requirements. Montana Housing will coordinate with the Executive branch, budget office, legal counsel, and fund recipients to ensure all Treasury compliance and reporting guidance is met.

**Recommendation:** Allocate \$15,000,000 in ARPA Section 602 funds. These funds will ensure affordable housing projects in the development pipeline impacted by cost escalations due to the COVID-19 pandemic can be successfully completed to provide nearly 1,000 quality, affordable homes to Montana’s lower wage workforce, seniors, and persons with disabilities – populations that have, in many cases, experienced disproportionate hardships under the COVID-19 pandemic. The Montana Department of Commerce Office of Legal Affairs certifies that the above eligible uses and entities comply with the American Rescue Plan Act.

This is a final copy of the memo.