Evaluation of affordable housing investment opportunities

October 2024

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Overview

This report summarizes findings from technical analysis and engagement conducted by the Metro housing department between February and August 2024. The purpose of this process was to evaluate possible future affordable housing investment strategies. However, it is expected that findings will inform a range of future planning and policy efforts related to affordable housing, including a Regional Housing Coordination Strategy that Metro is mandated by the state to create in 2025.

This analysis was conducted at the direction of Metro Chief Operating Officer (COO) Marissa Madrigal, as part of a COO-convened exploration of options for future regional affordable housing revenue in spring 2024, amid continuing housing need and the near full commitment of the 2018 Metro affordable housing bond. Initially, this exploration focused on identifying possible funding sources, and later expanded to priorities and needs associated with expanding allowable uses of Metro supportive housing services funds (SHS) to invest in housing production that could also support SHS goals.

Supported by a team of consultants, this work included a scan of national and west coast best practices; high-level analysis of funding and economic factors impacting production feasibility and costs; illustrative modeling of gap financing costs and leverage scenarios; technical engagement of subject matter experts in housing development, operations, finance, and policy; and evaluation of lessons learned from the 2018 Metro affordable housing bond.

Potential investment strategies analyzed included:

- Gap funding for new rental construction
- Preservation of existing regulated affordable rental housing
- Acquisition and conversion (new market-rate, naturally occurring affordable, hotel/motel, office)
- Affordable homeownership (shared equity homeownership models and programmatic supports)
- Complementary strategies, including policies and practices that support innovation, development and operational supports, financial incentives and barrier reduction (e.g., tax abatements, streamlined permitting, infrastructure funding)

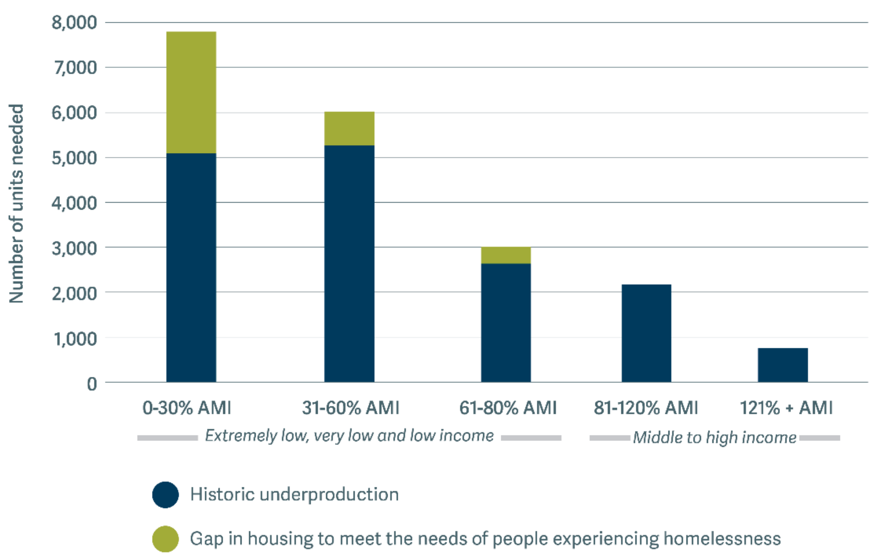
The evaluation summarized in this report has taken place within a dynamic national, state, and regional context. These conditions have factored into the breadth of this project, indicated priority focus areas, and influenced findings shared.

Affordable housing need

Across greater Portland, communities continue to struggle with having enough safe and affordable homes for everyone. This housing crisis has hit particularly hard for populations who have already been impacted by unjust systems and policy; Black, Indigenous and other people of color; immigrants; veterans; people with disabilities and other low-income households. That's why in 2018, voters across the region approved funding for much-needed affordable housing. The Metro bond generates $652.8 million, with the goal of funding 3,900 affordable homes to house about 12,000 people. With over 1,811 homes completed and 2,860 in construction or pre-construction, the bond is on track to produce 700 more homes than initially projected.

Though the bond has supported significant progress, there is still considerable need. Metro's draft 2024 Urban Growth Report estimates a total of 24,000 housing units needed to fill the region's existing gaps, and an additional 150,000 homes over the next 20 years. As demonstrated below, at least two-thirds of future housing development will need to be affordable to households earning less than 80% AMI. The greatest need is among households with extremely low incomes – below 30% of area median income.

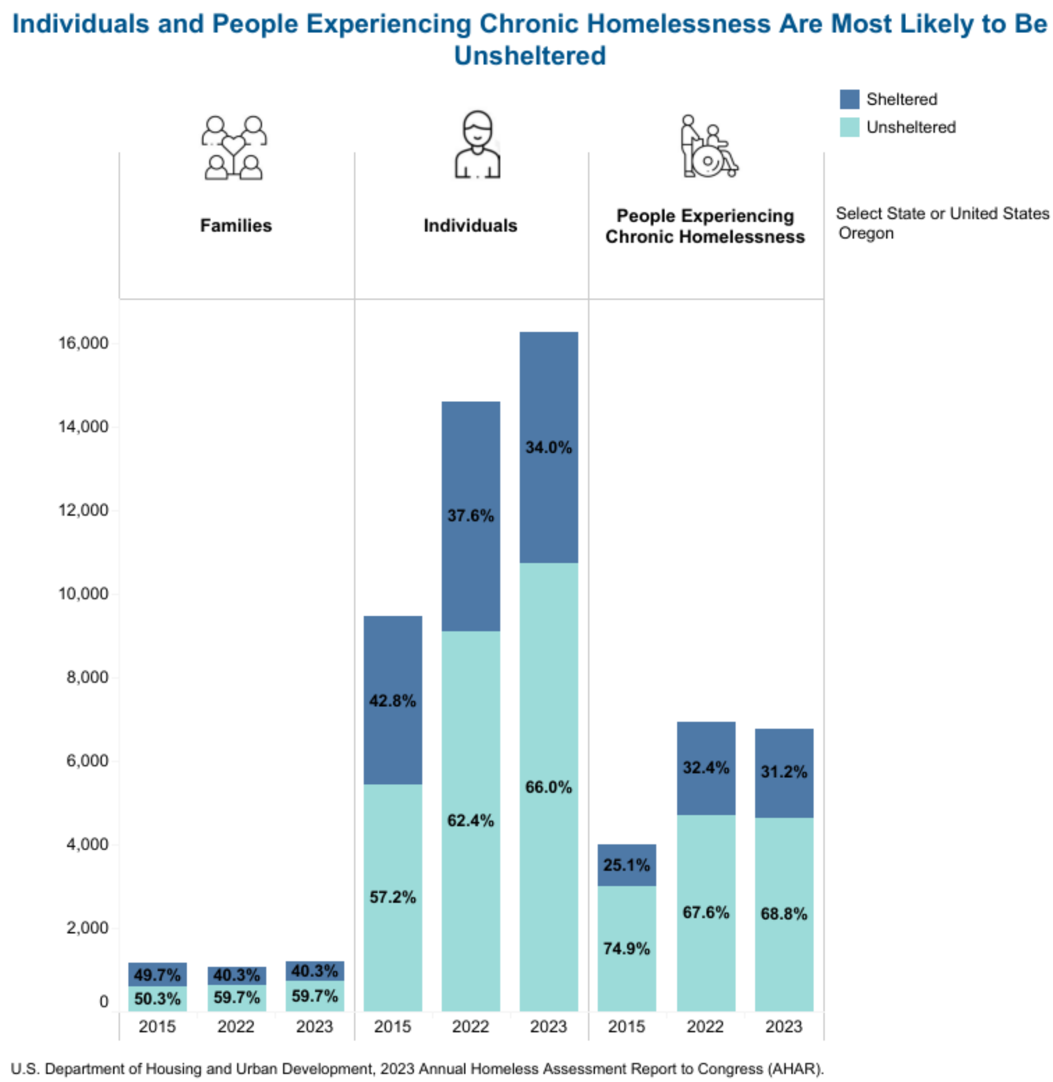
Figure 1- Housing production needed by AMI level, Source: DRAFT 2024 Urban Growth Report, Metro



There are many factors driving this demand for deeply affordable housing. One notable factor is an aging population, which includes many households who rely on fixed incomes like pensions or Social Security. Without significant and unprecedented increases in Social Security payments many of these households will continue to need deeply affordable housing options. Older adults also represent the fastest growing segment of the homeless population. According to the National Alliance to End Homelessness (NAEH) 2024 Point-in-Time count report, nationwide, almost one in four individuals experiencing homelessness last year were over the age of 55.

This is occurring in the national context of generally increasing rates of homelessness, especially among individual adults and those experiencing chronic homelessness, or long-term/recurrent homelessness combined with a disability. Lack of housing supply, a growing wage gap between the highest and lowest earners, institutional racism, increasing rents, and other social issues have created an environment where once housing stability is lost, it's difficult to regain. When households experience long-term homelessness - especially unsheltered homelessness - this often exacerbates existing conditions, worsening disabilities and negatively impacting health and wellness. The table below, from NAEH's 2023 State of Homelessness Report, illustrates unsheltered homelessness trends in the state of Oregon over the last decade, demonstrating this marked increase.

Figure 2 – Oregon sheltered and unsheltered homelessness by group, Source: NAEH State of Homelessness, 2023



These trends, among others, are driving a heightened need not only for more deeply affordable units, able to serve households with incomes between 0-30% of AMI, but also for services to support those households in stabilizing in housing. Housing First interventions, including permanent supportive housing (PSH), are proven models for addressing unsheltered homelessness and stabilizing households long-term. PSH combines permanent housing, rental subsidy, and tailored, wrap-around long-term services to ensure households exiting chronic homelessness have the best chance at addressing complex barriers to housing stability.

A range of unit sizes are needed to address shortages and expand needed PSH. The data shown above articulates at the state level what many providers have shared with Metro – the region needs more housing units to serve individuals and people exiting chronic homelessness. Regionally, gaps in available affordable housing units and need can be illustrated by analyzing application data from the first 14 Metro affordable housing bond properties to lease-up (accept residents). The table below shows that across every unit type, especially for smaller unit sizes, demand has outstripped supply.

Figure 3 - Demonstrated need through applications received, Source: Post-occupancy reporting, Metro 2024

	Studios	1 BR units	2 BR units	3 BR units	Total
Clackamas					
Total units available	48	17	63	20	**148**
Total rental applications received	55	40	108	22	**225**
Multnomah					
Total units available	160	226	129	129	**644**
Total rental applications received	928	1075	580	382	**2965**
Washington					
Total units available	29	154	154	35	**372**
Total rental applications received	42	291	250	64	**647**

	Studios	1 BR units	2 BR units	3 BR units	Total
Total units available	237	397	346	184	**1164**
Total rental applications received	1025	1406	938	468	**3837**
Total percentage of applicants housed	23%	28%	37%	39%	**30%**

While primary data sources, like those referenced above, tend to show greater current need for smaller unit sizes, it is not uncommon for community based organizations to emphasize an ongoing need for larger unit sizes when engaged around the needs of the communities they serve. These providers sometimes share that families, particularly families of color, are more likely to be undercounted in official point-in-time (PIT) counts of people experiencing homelessness. Undercounts can be attributed to methodological limitations associated with the PIT count, including its exclusion of "doubled up" households, or households temporarily sheltering with another household while experiencing homelessness. Additionally, despite attempts to affirmatively market units, some communities may not have equal access to application opportunities, skewing application data. This means that a wider range of data sources, including independent evaluations and direct engagement with providers and historically marginalized communities, should be considered when planning for needed units. For instance, the Metro Housing Bond 2020 Annual Report Executive Summary highlighted that engagement with communities of color and other historically marginalized communities had surfaced that larger unit sizes were a priority. Another resource, the 2023 Point in Time Double Up Report for the Tri-County region, estimated that 1,092 youth living with families were experiencing homelessness while doubled up, based on available data from local school districts. Moving forward, it will be important to continue to reference a range of sources, including direct engagement, to ensure funded units meet shifting community needs.

Due to the legacy of overtly racist policies and ongoing harmful and oppressive practices, communities of color are disproportionately represented among people experiencing cost burden and homelessness, including chronic homelessness. For this reason, racial equity should be a key consideration for all work done to address homelessness – both individually and systemically. Investment in culturally specific service models, including culturally specific PSH, aims to respond to the needs of those most impacted by homelessness. So long as these inequities remain, investment priorities should be evaluated with respect to their ability to support progress in closing these gaps. This is why racial equity has been a core value and commitment of both the Supportive Housing Services funding program (discussed below) and the Metro bond from their inceptions. Continuing to understand and center racial equity as a core outcome will remain a primary focus for future regional housing funding and investment.

In grappling with this urgent need while experiencing post-pandemic economic and social trends, many affordable housing industry partners and community leaders have expressed interest in evaluating more innovative solutions to affordable housing shortages, and a wider range of investment strategies for housing and stabilizing households long-term. While the Metro bond has focused primarily on maximizing new construction of affordable rental housing, acquisition and conversion and some affordable homeownership opportunities were eligible expenditures. Though important strategies, some types of expenditures, like preservation of existing affordable housing, were ineligible for bond funds. This has led to repeated calls for Metro to explore the feasibility and potential of a range of investment strategies. When the Metro COO launched a public conversation about options for potential future capital housing funding and investment, Metro staff prioritized responsiveness to this feedback in evaluating affordable housing system needs and capital investment opportunities.

State and regional context

Addressing these issues requires intentional coordination across funders and systems at all levels. Metro plays an important role as a regional convener, land use authority, and funder of affordable housing and homeless services. This work is occurring in the context of a variety of efforts to increase and support affordable housing production and address homelessness.

Several key pieces of housing-related state legislation in recent years have focused on better meeting the housing needs of Oregonians. Starting with House Bill 2003 (2019) the legislature has redirected statewide planning Goal 10: Housing toward promoting housing production, choice, and affordability. This legislation initiated what is now called the Oregon Housing Needs Analysis (OHNA), which includes a methodology for the state to estimate city housing needs on a six- or eight-year cycle and created a requirement for cities to adopt Housing Production Strategies, among other reforms. In more recent years, legislation has refined OHNA to be more outcomes based and tied to city housing production targets that will be developed by the state. Unique to the Metro region, counties will now also complete housing production strategies for urban unincorporated areas like Bethany, Oak Grove, etc.

Under the OHNA Metro is tasked with conducting the regional housing needs analysis and coordinating with local jurisdictions to produce a housing coordination strategy. Much like housing production strategies cities must adopt, Metro is tasked with adopting a regional Housing Coordination Strategy that includes actions to promote needed housing—including diverse and affordable housing, housing with access to opportunities, and development patterns in compliance with fair housing laws. Metro is required to adopt its coordination strategy one year after adopting its housing capacity determination (through the urban growth decision), making it due to the state by the end of 2025.

Building on this momentum, housing production and homelessness response have been cornerstones of Governor Kotek's agenda. In early 2023, Governor Kotek issued several executive orders spurring action across these systems. Among other actions ordered, Executive Order 23-04 set an ambitious statewide housing unit production target of 36,000 units per year to address housing needs. More recently, the Governor's Office has created Housing Production and Homelessness Response Frameworks, and the Governor's staff are currently working with a cross-section of identified agency and legislative leads to develop plans for needed system reforms across dozens of focus areas for the 2025 legislative session.

The state's amplified focus on housing production and homelessness response has also supported unprecedented funding allocations to Oregon Housing and Community Services (OHCS), the state's housing finance agency. OHCS has also implemented an agency-wide strategic legislative implementation process called Operational Excellence (OPEX), consisting of at least 36 significant implementation projects. This effort has included repositioning and consolidation of OHCS's Affordable Rental Housing Division funding program processes. This new consolidated process, the Oregon Centralized Application (ORCA), allocates funds on a non-competitive first-ready, first reviewed basis to ensure project readiness, via a rolling application and pipeline management process. OHCS has introduced a wide range of initiatives and supports to complement the ORCA, including new project readiness and pre-development resources, a risk mitigation pool, and a comprehensive Affordable Housing Preservation Strategy Framework and public dashboard.

Despite current historic funding levels and the introduction of these supports, available resources still fall well below what will be needed to address the Metro region's housing production and preservation needs. This level of investment is not guaranteed to be ongoing, and these funding programs are unlikely to achieve the depth of affordability or the amount of PSH required to address the region's housing needs; most are structured to achieve moderate levels of affordability. This is why local investment plays a key role in achieving local priorities. Especially with a non-competitive, project-readiness focused funding structure, local funds – particularly for early development activities – can leverage these state funds to create deeper subsidy.

Local investment functions within this funding and policy context., andmplementers must consider these conditions when evaluating options for potential impact and feasibility. For instance, in late 2023 Governor Kotek recommended a three-year moratorium on new taxes for jurisdictions in the Portland metropolitan area in response to the input of the Governor-appointed Portland Central City Task Force. This recommended moratorium, alongside public perception of new tax measures, has limited the potential viability of some options for generating new local revenue for affordable housing development.

Another example: though OHCS is administering a record allocation of gap funding this biennium, the agency is also managing a challenging shortage of private activity bonds (PAB), which are necessary for leveraging federally funded 4% Low Income Housing Tax Credits (LIHTC). A shortage of this primary financing tool for affordable housing development impacts the ability of funders and developers to plan for and fund needed affordable housing.

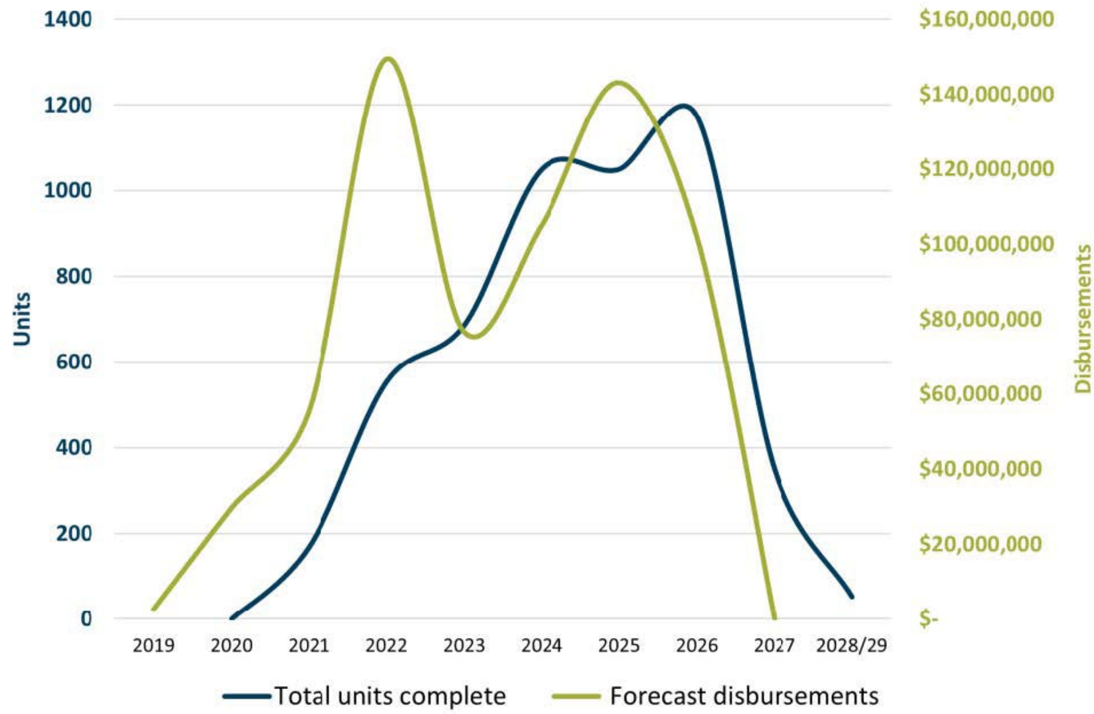
It is with these needs and conditions in mind that the Metro Council directed COO Marissa Madrigal to convene a community conversation about regional affordable housing funding in January of 2024, and directed the Metro housing department to undertake an evaluation of a variety of funding strategies – including some that do not require LIHTC leverage, or that take advantage of evolving market opportunities.

2024 Regional funding exploration

Metro has demonstrated success in meeting the community's need with regional funding. As mentioned above, the Metro bond has outpaced production targets. By the time it is fully expended, and all projects are in operation, the bond will have supported the development of nearly 5,000 affordable homes.

This bond, implemented with partners including the three county housing authorities, the cities of Portland, Beaverton, Gresham, Hillsboro, and the Metro Transit-Oriented Development team's Site Acquisition Program, has helped produce the type of deeply affordable units needed in the region, and has had limited investments in acquisitions and affordable homeownership. However, this resource will soon be fully committed, with final funding disbursements projected to take place in 2026. This is illustrated in the graph below.

Figure 4 - Forecasted timeline for remaining disbursements and unit completion, Source: 2023 Metro Housing Bond Annual Report



Meanwhile, another Metro funding measure, Supportive Housing Services (SHS), has to date generated more revenue than was anticipated when it was referred to and approved by the region's voters in early 2020. SHS is the country's largest per-capita investment in providing housing services at a regional scale. It is funded through high-earner and business income taxes. Proceeds from SHS flow from Metro to Clackamas, Multnomah, and Washington counties.

A key intention of SHS was to increase resources for funding needed services and rental assistance to ensure investments like the bond could effectively serve those exiting homelessness, particularly long-term homelessness. However, due to both higher-than-anticipated revenues and the time needed to expand the homeless response systems, the fund has accumulated some carryover across fiscal years.

These considerations underpinned the regional conversation initiated by Metro COO Madrigal, with Metro Council direction, in 2024.

Among other tracks of input, COO Madrigal convened a broad stakeholder advisory table (SAT) to discuss possible funding sources to continue regional investments in affordable housing. These included a new property-tax funded bond, expanding allowable uses of SHS to include investments in affordable housing, or taking no action at this time. Stakeholders broadly agreed that additional funding was needed, while a new bond is unlikely to be viable. This led the table to discuss the potential of SHS-funded affordable housing investment more explicitly, and to consider the priorities that would accompany this funding source. Although the advisory table was not structured to issue recommendations or reach consensus, most members preferred prioritizing housing investments with SHS funds to support people experiencing or at risk of homelessness, particularly long-term or recurrent homelessness. These priorities then shaped the evaluation in progress and focused the work more fully around the potential impacts of different investment options for SHS-service populations.

Similar themes of prioritization were heard in community discussion groups led by the Coalition of Communities of Color, stakeholder and partner conversations, and public opinion research that also informed COO Madrigal's recommendations to the Metro Council in July 2024. This recommendation and appendices describing these processes in more depth are available at oregonmetro.gov/housingfunding.

Key findings and considerations

Through technical evaluation and engagement, we have identified the following key findings.

Key Finding 1: Affordable housing industry developers and operators are currently experiencing significant barriers to production and successful long-term property operations. These trends are occurring nationwide but are acutely felt in coastal metropolitan areas like greater Portland.

Developers are experiencing substantial increases in cost and risk for projects, most impacted by the following:

- Unprecedented construction cost escalation driven by broader economic trends, including supply chain issues and labor shortages
- Rising interest rates, for both construction and permanent financing, which creates particular challenges for smaller and culturally specific organizations
- Oversubscription for private activity bonds (PABs) impacting access to 4% LIHTC, a primary financing tool for affordable housing
- Complex capital stacks and lack of coordination between funders, lengthening development timelines and creating uncertainty and risk for developers, which is exacerbated by PAB oversubscription.

Housing operators are experiencing unprecedented operating cost escalations, associated with the following:

- Increased acuity of residents' support needs and/or unmet needs -- particularly for households exiting homelessness without long-term rental assistance and/or adequate supportive services. This is connected to widespread rental arrears, high resident turnover, and a higher-than-expected need for more robust resident services, maintenance, property management, and security staffing.

- High staff turnover and staff shortages due to lack of sufficient wages and needed training/support, exacerbated by challenging working conditions and complex reporting requirements
- Rapidly rising insurance premiums, which are impacted by frequency of claims and lack of choice in insurance providers
- Inadequate operating funding supports, including rental assistance payment standards that do not fully cover operating costs, and insufficient access to risk mitigation funds or other operating subsidies to manage the full cost of operating these properties
- Competitive development funding processes and cost containment policies that have encouraged or required lower estimates for ongoing costs than are currently required to successfully manage affordable housing properties.

As a result, regional affordable housing experts and stakeholders have noted the following industry impacts:

- Some properties are struggling to stabilize and achieve debt service coverage ratios required by institutional lenders and investors, which can impact the property's ability to convert from a higher-interest construction loan to a lower-interest permanent loan. This trend is causing investors to increase financing requirements, creating barriers that particularly limit access to financing for smaller, community-based providers.
- Residents' stability and well-being are negatively impacted by high staff turnover and challenging on-site environments.
- Housing operators in the region are using their own funds to fill operating gaps. While this is a common risk of property ownership, it is not sustainable for the long term and could impact operators' organizational well-being and ability to pursue additional projects.
- Housing developers are struggling to recoup deferred developer fees, payments owed to the developer for their work developing the project, due to operating costs exceeding projections. This most impacts smaller, emerging, and culturally specific organizations' ability to maintain and build development capacity.

For more information about the current state of affordable housing development, including gap financing scenarios, please see memoranda "Market Incentives, Actions, and Policies to Support Affordable Housing Production" (Appendix E) and "Gap Funding for New Construction by Capital Scenario" (Appendix C).

Key Finding 2: Capital investments for future regional affordable housing funding should be coordinated across funders to provide predictability, and funding requirements should be informed by actual cost. Funders should seek to balance maximizing unit production with ensuring quality and long-term stability for future residents and housing providers.

A recurrent theme from recent engagement efforts, supported by research and analysis, has been the importance of thoughtful, well-coordinated investments across funders. Affordable housing is difficult to develop and operate, and this difficulty is compounded when funders' requirements, priorities, or funding cycles are misaligned. As mentioned above, housing developers and operators frequently noted challenges brought about by PAB oversubscription, which many attributed to poor communication and coordination between funding partners.

Further, funders should evaluate cost containment practices, including underwriting requirements, to ensure that they don't incentivize developers to understate costs necessary to build and operate high-quality affordable housing to qualify for funding. This is especially needed for investments targeted toward service populations with specialized needs, such as quality PSH. Funding practices should move away from simple per unit caps and toward tiered standards and ranges that are informed by analysis of actual costs and aligned with policy priorities focused on quality and long-term success of future residents and housing operators. This may mean that funders support production of fewer units at a higher subsidy level to stabilize the industry and ensure safe, high-quality housing for future residents and ongoing stability for organizations and staff.

Key Finding 3: Across all investment strategies evaluated, the following best align with SHS goals and service population priorities, while also responding to industry challenges and market opportunities:

- **Gap financing for affordable rental construction**
- **Preservation of existing affordable housing**
- **Acquisition and conversion of market rate multifamily housing, hotels, and motels**
- **Operating and risk mitigation support funds**
- **Strategic land acquisition**
- **Pre-development funding**

If SHS funds are to be used for creating affordable housing, our evaluation of investment strategies found that the above strategies best support the production of deeply affordable and permanent supportive housing—the housing types that most align with the goal that 75% of SHS funding go toward supporting housing access and stability for individuals with extremely low income, who have one or more disabling conditions, and are experiencing or at risk of experiencing long term or frequent episodes of literal homelessness.

Maintaining some flexibility in allowable expenses will support responsiveness to shifting needs, industry challenges, and market opportunities—as well as shifts in revenue availability over time. For instance, if revenue levels allowed, innovative strategies to build organizational capacity and lower the cost of development, in partnership with local jurisdictions, may be appropriate investments. This could include grant-making, below-market financing products, insurance pooling, and other approaches that support the industry in delivering projects more efficiently and effectively.

Strategies to invest in affordable homeownership opportunities have deep impacts for households they serve and have the potential to contribute to addressing inequities and building generational wealth. Similarly, incentives for moderate-income housing can play an important role in our region's broader fair housing and anti-displacement goals. These are important investment strategies that Metro should continue to explore and support. However, for the purposes of considering potential use of SHS funding for capital investment, Metro has received clear stakeholder feedback that these approaches do not sufficiently align with SHS's focus to be considered for this funding source.

Key Finding 4: Homeless services and affordable housing systems need more comprehensive integration.

Lack of coordination between homeless services and affordable housing systems delays people getting into housing and impacts housing retention, through longer lease-up times and inadequate supports for some households referred to housing through homeless services systems. While these challenges are most acutely felt in Multnomah County, multiple operators across the region identified challenges in coordinating with homeless services providers and funders, including prolonged processes for referrals to PSH units through county coordinated entry systems as well as lack of responsiveness and inadequate supports for some referred households.

For example, housing operators identified barriers to supporting households referred into housing through rapid rehousing (RRH) or other short-term interventions, but who demonstrate need for ongoing rental subsidy and supportive services beyond what the property is funded to provide in site-based resident services. Some housing providers call this "lower-case PSH" or "de-facto PSH" in that they characterize these households as needing a level of support and rental assistance like what PSH offers, but lacking access to ongoing operating subsidies and/or services necessary to achieve housing stability.

Homeless services system partners are addressing many challenges in housing and stabilizing people through tailored interventions. At times, these struggles are compounded by a lack of regional alignment in definitions, contractual obligations, and data management systems and metrics, as well as differing approaches to operating subsidies and payment standards. For both systems to best serve people and achieve equitable outcomes, funders and implementing partners should work together to identify best practices and regionalize some standards, while maintaining enough programmatic flexibility to ensure a menu of options to meet a wide range of needs.

Description of evaluation criteria

To guide our analysis, Metro staff developed criteria to evaluate potential investment strategies. Staff then worked with consultants to scan existing research, determine high-level market and economic conditions and funding landscape, and review themes from technical stakeholder engagement to evaluate the cost, impact, feasibility, alignment with SHS funding priorities, and racial equity implications of the strategies considered. Prioritized evaluation criteria and sub-criteria are as follows:

- **Policy outcomes:**
  - **Populations served,** including alignment with SHS priority populations and associated unit type and depth of affordability needs, potential for referral partnerships, and possible service population demographic considerations contributing to racial equity outcomes
  - **Geographic considerations,** including distribution of opportunities, access to transportation and amenities, and fair housing and anti-displacement considerations
  - **Equitable contracting and workforce opportunity,** for trades and construction as well as housing operations and service supports
  - **Environmental justice,** including considerations such as access to green space, sustainability, and climate resilience
- **Feasibility:**
  - **Production potential,** including cost, market factors, leveraged funding availability, and project delivery timelines
  - **Administrative considerations,** including asset management and monitoring requirements and funder and developer capacity considerations

Additional criteria detail can be found in Appendix A.

Investment strategy evaluation

In evaluating potential investments against the priority criteria, Metro has found notable benefits, limitations, and considerations for each. This section provides a high-level summary of the most relevant findings for each investment strategy.

GAP FINANCING OF NEWLY CONSTRUCTED AFFORDABLE RENTAL HOUSING

Given the existing and projected need for deeply affordable housing discussed above, public financing of affordable units – commonly called gap financing – will continue to be needed. Gap financing is required to achieve deep affordability because these units cannot generate enough revenue to pay for the up-front costs of developing and constructing the building. While gap financing for new rental construction is provided through Oregon's statewide housing finance agency, Oregon Housing and Community Services (OHCS), this funding is insufficient to meet the state's overall housing needs. Most funding is structured to be able to support moderate affordability levels. The 2016 Portland housing bond and 2018 Metro bond were designed to be layered with state funding to achieve deeper affordability levels. With these bonds nearly fully deployed, new funding is needed to continue to sustain a pipeline of deeply affordable housing in the region.

To understand potential costs and production potential for future gap financing investments, Metro assessed lessons learned from the bond and feedback from practitioners regarding the critical need for interventions to stabilize the affordable housing system. Metro also worked with a consultant to update gap financing considerations and financial modeling assumptions, as summarized in "Gap Funding for New Construction by Capital Scenario" (Appendix D).

Benefits of gap financing

Gap financing is most universally impactful when compared to other possible investment strategies across evaluative criteria. It increases overall housing stock and achieves increased production through higher public and private funding leverage. It also provides the ability to target funding toward various priorities and policy outcomes through project selection processes, and to shift policy priorities and funding criteria over time to respond to changing needs and conditions.

Gap financing provides funders with the ability to:

- Produce deeply affordable units with long-term regulated affordability
- Tailor unit mixes and site amenities to local needs, and purpose-build properties to accommodate specific target demographics and/or referral partnerships – such as older adults or permanent supportive housing referrals from coordinated entry systems
- Especially when combined with funds specific for land acquisition, site properties in locations that affirmatively further fair housing, contribute to anti-displacement efforts, and achieve environmental justice and quality-of-life benefits for future residents through access to transit, services and amenities
- Effectively leverage investment, including private equity investment through the federal LIHTC program, as well as state, federal, and other private funding, to bring additional resources to the region
- Intentionally braid capital funding with services and rental assistance funding available through the SHS measure and other sources, to ensure that affordable housing developments

are intentionally designed and financed to serve households experiencing or at imminent risk of chronic homelessness

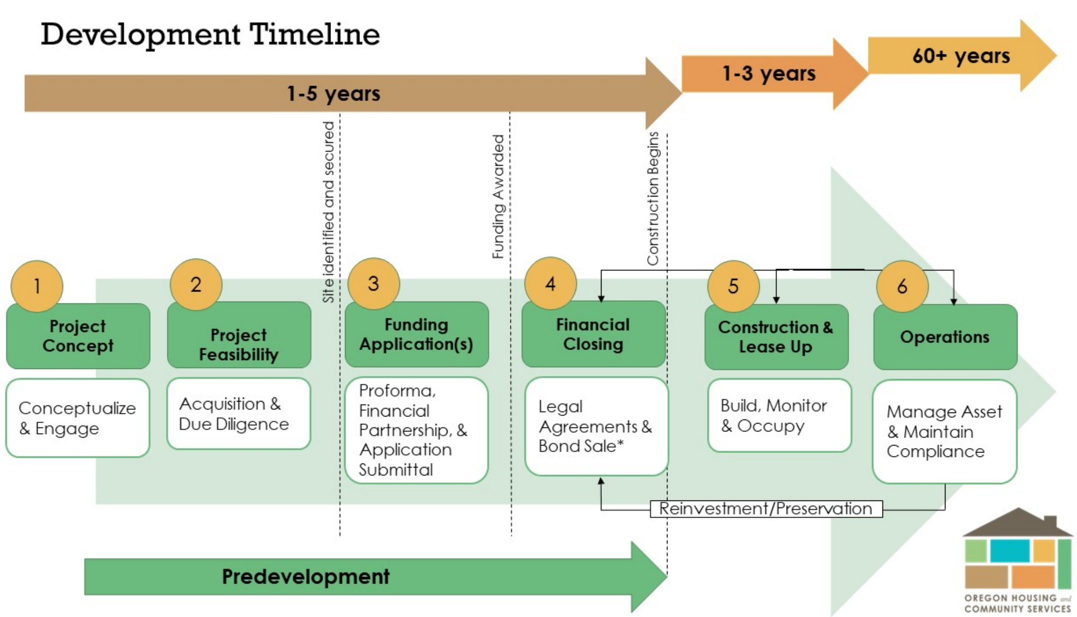
- Prioritize alignment with complementary investment programs, such as the OHCS Co-location Fund, $10 million in OHCS funds administered by BuildUp Oregon to support co-locating early care and education facilities with affordable housing, or other state and federal funding to achieve improved outcomes for residents and the community
- Establish goals and requirements and advance practices related to equitable construction contracting opportunities and workforce benefits

Limitations of gap financing

While continuing to invest in gap financing for the construction of affordable rental housing has clear advantages and remains a priority, there are notable areas where gap financing falls short compared to other strategies. As a result, many stakeholders and practitioners have urged Metro to also explore alternative investment models that respond to market conditions and innovations.

Gap financing is likely among the slowest of all evaluated approaches, as developers typically need to acquire land, secure multiple financing sources, and go through multiple rounds of review and permitting before beginning construction on a new property. Costs associated with land acquisition are also made early in the process, before gap funding is approved for a project, which exposes developers to additional risk and holding costs. It is typical for a single multifamily property to take three to five years, and sometimes longer, to develop from an initial concept to an occupied property. The figure below, created by OHCS, illustrates a sample production timeline for newly constructed affordable rental housing.

Figure 5- Development Timeline Overview, Source: OHCS 2024

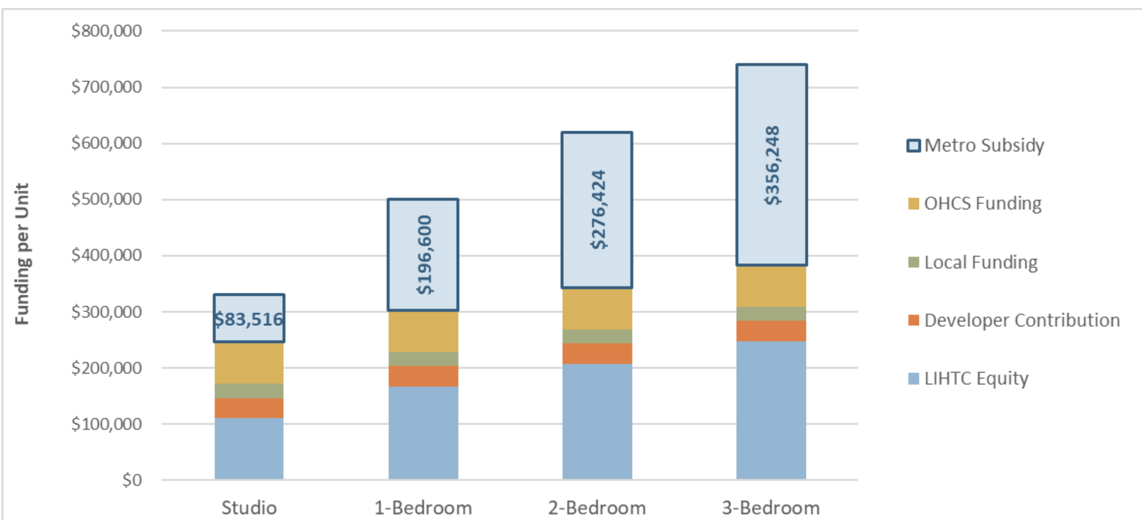


As outlined in “Complementary and Supportive Investments” below, there may be opportunities to improve development timelines, but it will likely remain the case that developing and constructing a property will take multiple years.

Gap financing of new multifamily housing is also among the most expensive investment strategies on a total cost per unit basis, due to the need to develop properties from the ground up and the additional costs associated with this. However, these higher costs are meaningfully offset by the availability of leveraged funding sources that are not available for other strategies. Higher costs are attributable to a range of factors including increasingly limited land availability, complex policy priorities, rising construction and financing costs, prevailing wage requirements, and the time it takes to layer funding from multiple sources. Though these are long-term investments and achieve significant outcomes, cost is an important factor that must be considered.

As seen in the figure below, the estimated per unit Metro subsidy that will be required to fund a deeply affordable housing unit in 2026 will be between $83,000 to $360,000 depending on unit size, based on BAE Urban Economics analysis of recent investments and relevant market factors.

Figure 6 - Estimated Capital Stack and Metro Subsidy needs by Unit Size, for 30% AMI Unit without Basis Boost, Source: BAE Urban Economics



Another limitation of gap financing for new affordable rental housing is that affordability restrictions typically have an expiration date, and development typically relies on public-private partnerships that include participation of for-profit as well as non-profit entities. Gap funding models can establish affordability terms that are significantly longer than the federally mandated 30 years for LIHTC. For instance, OHCS requires 60+ years of affordability for most investments and Portland Housing Bureau (PHB) requires 99+ years. The Metro bond required a minimum of 60 years for new construction and 30 years for acquired properties that were more than 10 years old. However, even in instances where the regulated affordability period is prolonged, additional public investment will typically be required to support periodic recapitalization and major system updates and improvements. This is discussed further in “Preservation of Existing Regulated Rental Housing” below.

Additional considerations for gap financing

Metro’s findings suggest that funders should assist developers in reducing project risk and cost, and ensure ongoing operational viability and resident success through:

- Aligning funding timelines and priorities, and where feasible, braiding funding and aligning applications across funders
- Communicating funding availability and priorities well in advance of funding opportunities, to ensure that developers can tailor projects to community need
- Streamlining project approval processes to improve clarity, consistency and predictability of funding requirements (reduced subjectivity in review) and to reduce duplication in review by local jurisdictional partners, Metro, and OHCS
- Ensuring that funding requirements and underwriting guidelines do not encourage artificially low project cost projections, which result in capital and operating funding shortfalls that impact resident outcomes and organizational sustainability for owners/operators
- Allowing funding to be used for predevelopment activities and/or providing land acquisition funding to ensure that developers with fewer financial resources, including small/emerging community based and culturally specific organizations, can participate in development opportunities

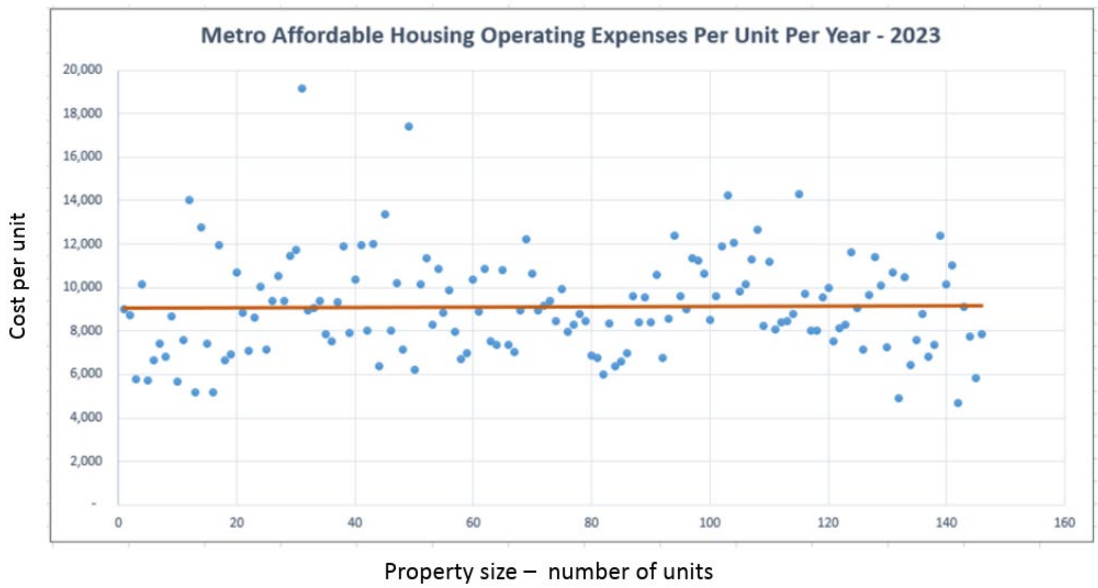
Additionally, findings pointed to the need for improved coordination and alignment between housing and homeless services systems, including:

- Improving and expanding access to long-term supportive services and rental assistance to ensure that households placed into housing through homeless services interventions have the support they need to achieve long-term housing stability
- Unlocking potential for housing developers to leverage SHS-funded Regional Long-Term Rental Assistance (RLRA) in securing private financing, by extending the SHS measure sunset by a minimum of 20 years, with 25-30 years being more ideal
- Providing opportunities for data system alignment and shared tracking of housing access and stability metrics and outcomes
- Working with finance industry partners to support continued access to private financing, which is particularly important for PSH projects and small/emerging developers who face barriers in meeting higher underwriting standards such as increased liquidity, higher debt service coverage ratios, and increased security and insurance requirements
- Ensuring that operational funding for housing providers allows for the staffing necessary to effectively coordinate with service providers and supporting staff access to comprehensive

racial equity and trauma-informed property management training as well as other needed proficiencies to serve resident populations, as described below.

To better understand and illustrate needed operational funding, the Housing Development Center (HDC) collected portfolio data for nearly 150 affordable housing properties in the Portland Metro area. This anonymized portfolio data showed a median operating cost per unit around $9,000 per year, which is well above what many properties budgeted for and what recent state and local underwriting standards have projected as necessary. For a table of property data informing this graph, please see Appendix B Attachment 3.

Figure 7 - Operating cost expense table, Source: HDC analysis of Metro region portfolio data



PRESERVATION OF EXISTING REGULATED AFFORDABLE RENTAL HOUSING

Housing affordability in typical affordable rental housing is achieved by regulating the amount of rent that a property can charge for a unit restricted for households based on their income level, such as 60% of area median income. When properties are developed using certain funding sources – for instance, the Metro bond – they do so with an agreement to regulate affordability at an agreed-upon level or levels for a specified amount of time. In the case of the Metro bond, this is a minimum of 60 years of regulated affordability for a newly constructed building (the City of Portland regulates for 99 years in accordance with local policies).

Because this affordability is not permanent, once this agreement is fulfilled it allows for the property owner (sometimes, but not always, the original developer) to convert all or some of the property to market-rate housing. This sometimes happens through the sale of a property to a new, for-profit owner. In cases where properties are owned by non-profit or public entities, the risk of conversion to market rate housing is somewhat mitigated, as the mission of these organizations often compels them to maintain affordability. However, in the cases where private, for-profit entities own the property, given that these owners have fulfilled their commitment, they may need to be incentivized to maintain affordability or sell the property to an organization that will.

Through legislative action and programmatic improvements, the state of Oregon has made substantial progress in the last seven years toward better tracking preservation needs, enhancing contract provisions and tenant protections, and creating a refined funding framework. As part of these improvements, OHCS has developed a regularly updated list of properties in need of preservation and developed a new preservation dashboard.

Within the Metro region, 5,289 existing affordable housing units are set to have their affordability restrictions expire within the next 10 years. This creates an environment wherein these expiring properties – and the residents that call them home – are at risk of losing affordability. For many of these residents, this would lead to harmful impacts, such as the loss of home, community, and possible displacement from their neighborhood or even homelessness.

Without intervention, the affordable housing inventory in our region could decrease despite investments in affordable housing production, due to expiring affordability covenants or federal rental assistance contracts. Though the region may not lose these units as part of the overall housing stock, they may become unaffordable to people with low or extremely low incomes.

State preservation resources vary year by year and are consistently oversubscribed, meaning there is more demand for the funding than funding available. For example, the Oregon State Legislature allocated $50 million to affordable housing preservation for the 2023-2025 biennium. While OHCS allocates set-asides of other funding sources and tax credits that allow for preservation expenditures, this is dependent on available resources and changing policy priorities. According to interviews with preservation experts, OHCS estimates that approximately $1 billion in funding over the next ten years, or roughly $200 million each biennium, would be required to address acquisition and rehabilitation of properties with expiring federal rental assistance contracts and affordability covenants.

Benefits of preservation investments

Investments in preservation of existing affordable housing are key to preventing homelessness and displacement. Because these properties are occupied, funders can have much more certainty about the demographic makeup of the residents being served, allowing for strategic investments – particularly opportunities that advance equity goals – where they'll have the most impact.

Needed funding varies significantly from property to property, but in general, preserving what we have can be more cost effective and sustainable than building new. This can be especially true if funding can be made available to purchase a property or incentivize an extension of regulated affordability early – with at least 5 years left of regulated affordability. Preservation experts have shared that it is commonly the case that when affordability expiration is imminent, real estate investors begin to take interest, thereby increasing the price of the property and with it, the amount of public funding needed to maintain affordability.

Since OHCS now keeps a list of properties that need to be preserved, including their attributes, locations, and expiration dates, they can prioritize preservation investments based on criteria such as urgency, resident vulnerability, and potential loss of federal rental assistance. This allows for the possibility of investing resources years before expiration, to maximize the impact of limited funding in supporting fair housing and anti-displacement outcomes.

In addition to funding the purchase of properties, funders can incentivize property owners to maintain affordability with financial support, for instance, by paying for major capital improvements to the property. For example, one of the funding programs New York City administers, the Participation Loan Program (PLP), provides a city-funded below-market interest 30-year loan to property owners, which is intended to be used alongside private financing to preserve existing affordable housing. The city leverages this funding to achieve multiple priorities by requiring the owner to then rent 10% of the funded property units to people experiencing homelessness, upon turnover of units. Because the funding is in the form of a loan, the city can then reuse funds once repaid. While OHCS's funding focus to date has primarily supported direct funding of acquisition and rehabilitation of expiring properties, a model akin to this could be worth further exploration as part of a regional strategy.

Limitations of preservation investments

While preserving properties is beneficial, it does not actively increase the overall housing stock. Given the shortage of housing units, some may argue that building new units, though expensive, has a greater impact because new construction also reduces pressure on the lower end of the housing market, even if some affordable units are lost to market rate conversion.

Relatedly, the new Oregon Housing Needs Analysis (OHNA) methodology for determining production needs, including the affordability levels cities must plan for in their Housing Production Strategies, does not currently account for units lost due to expiring affordability. As a result, dedicating limited regional funding to this strategy may not strongly align with the state's production-focused OHNA framework.

In addition, some property owners, particularly for-profit owners, may not be motivated to preserve affordability. Because these owners have often invested private equity into the development with the intention of generating increased profit upon conversion, these deals may not have favorable terms. Though OHCS maintains right of first refusal for more recently funded properties and requires advanced notice of intention to sell or convert, this does not guarantee that OHCS or its designated purchaser will be able to match offers from other prospective purchasers.

Lastly, properties being considered for purchase to preserve affordability should be evaluated thoroughly, with all capital needs identified. Older properties may require significant upgrades that increase the overall cost per unit substantially, beyond the cost of acquiring the property, and may require additional investments or ongoing funding to support equitable and stable operations.

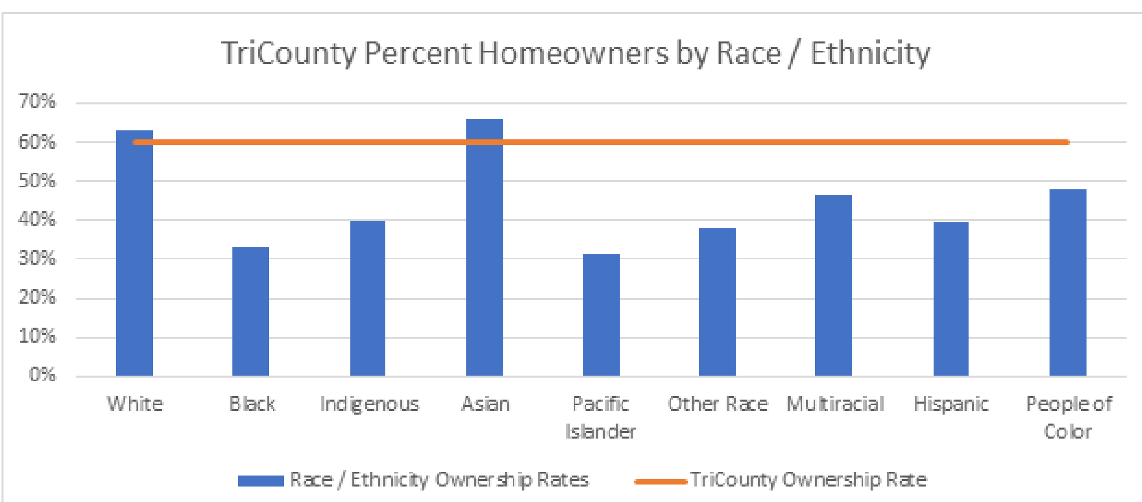
Additional considerations for preservation

Though preserving long-term property affordability is a best practice, when this is not possible due to resource limitations or other constraints, funders could elect to direct funding toward tenant supports in the case of property conversion to market-rate. For example, funders could elect to provide vouchers that are non-portable, non-transferable and that reduce market rate rent to maintain affordability for current residents of converting properties. These vouchers could help residents stay in their units for a specified period or indefinitely, mitigating harmful potential impacts of conversion.

AFFORDABLE HOMEOWNERSHIP OPPORTUNITIES

Homeownership has historically presented an opportunity for households to build wealth. As the value of a home increases over time and the amount the homeowner owes decreases, equity and household wealth is accumulated. This equity can often be borrowed against, improving access to financing for personal investments, like secondary education or entrepreneurship, that can increase household earnings over time. For many years, Black, Indigenous, and People of Color households - especially Black households - were systematically excluded from homeownership opportunities and their corresponding wealth creation opportunities through redlining and other racist policies and practices. The legacies of these exclusionary policies persist today, as illustrated by homeownership rates that present stark differences by race/ethnicity.

Figure 8 – Tri County homeownership rates disaggregated by race/ethnicity, Source: Metro analysis of American Community Survey data (2018-2022)



This disparity has been exacerbated by other oppressive practices, such as urban renewal efforts, which have disproportionately impacted and often decimated neighborhoods where Black residents and other communities of color had higher rates of homeownership.

Historically, homeownership has been attainable through a combination of a down payment, often 10-20% of overall purchase price, which the homeowner must contribute, and a mortgage, or loan product that pays the remaining cost. As of June 2024, Redfin estimated that the median home price in Portland was approximately $524,450; assuming a traditional mortgage, this could require a down payment of around $52,000-$105,000, which is unattainable even for many middle-income households.

Benefits of affordable homeownership investments

Affordable homeownership development can offer significant benefits for households selected to purchase homes, due to the model's potential to generate financial equity for the household over time—benefits that can support intergenerational wealth and stability.

Some affordable homeownership models maintain that benefit even once sold to another homeowner. Shared equity models, like community land trusts (CLT), keep home prices affordable for multiple generations of future buyers. Although shared equity models limit the amount of equity an individual homeowner can earn, the model enables multiple generations of owners to access benefits.

According to a brief prepared by Habitat for Humanity U.S., homeownership also contributes to decreased rates of moving from residence to residence, which can improve social engagement, and through this, increase social capital. Compared to renters, homeowners are better able to access resources and support through their networks and provide support in return. Homeowners also often experience more autonomy, freedom and privacy in their homes than renters.

In addition to growing the overall housing stock, when intentional coordination and referrals occur with organizations offering Individual Development Account (IDA) programs and other down payment assistance programs, affordable homeownership opportunities can be more effectively targeted to affirmatively further fair housing. Investments in these types of programs support households accessing homeownership opportunities through a range of financial education programs, savings match supports, and grants. Because these supports are targeted toward those with the highest disparities in homeownership, homeownership investments can achieve more significant equity impacts.

According to Neighborhood Partnerships, administrator of the Oregon IDA Initiative, annual financial match disbursements for households completing IDA programming in the Metro region have accounted for between 40-50% of state-wide disbursements over the past five years. In its most recently posted evaluation report (2022), Neighborhood Partnerships also estimated nearly half of all match funds in the previous two years went to BIPOC participants, over two-thirds of enrollees were women, and people born outside of the US accounted for 24% of enrollees. This success in serving those most left out of the market can be attributed to the reach of the provider network – including many culturally specific partners and trusted community based organizations across the state.

It is also possible for this strategy to serve households who once experienced homelessness or housing instability, but who have since stabilized in housing. When resources allow, programs that support financial education, building credit and increasing earned income, like many that are connected to IDAs, are often among service offerings for households in regulated affordable housing.

With appropriate service funding, affordable rental housing investments can then be effectively tied to long-term homeownership goals. Homeownership opportunities and the programmatic supports that make them more accessible to these resident populations can be considered a part of a housing stability continuum. However, even with adequate service funding and strong partnerships, the impact of these service investments will be constrained without more affordable homeownership development.

Lastly, like gap financing investments in affordable rental construction, these affordable homeownership investments can also contribute to attainment of contracting equity goals, climate justice goals, and other policy outcomes. However, these benefits may take different forms and overall impact may vary, since most investments in community land trust homes are lower density than typical multifamily rental properties.

Limitations of affordable homeownership investments

Generally, affordable homeownership opportunities are limited in the level of affordability they can achieve and are very unlikely to serve households transitioning directly from homelessness, especially those transitioning from long-term homelessness with significant barriers to housing stability.

As a point of reference, the homeownership opportunities in the Metro bond pipeline have ranged in targeted affordability from 35%-80% of AMI, due to being constrained on the upper end by bond funding affordability requirements. However, given relative difficulty in saving for even a reduced downpayment and qualifying for these homes, it is reasonable to expect that many households that come to own these homes are likely earning toward the top end of this range. The homes produced through this investment strategy are therefore unlikely to align with homeless system referral priorities, particularly those focusing on PSH.

It's also the case that these homes may cost more per unit to build. Current challenges around producing condominiums in Oregon are related to state funding limitations, the state's approach to construction defect liability laws, and the increased complexity of the commercial building code, which impacts condos. As a result, there are very few condos produced in the state. This means that most affordable homeownership properties are single-family detached homes or townhouses, which have a higher total cost per unit to develop compared to multifamily condo or rental properties.

ACQUISITION AND CONVERSION OF MARKET RATE HOUSING

Investing in the acquisition of market rate housing and then regulating those units as affordable is another possible strategy for increasing affordable housing stock. Depending on market conditions and available properties, this strategy has the potential to achieve multiple policy outcomes. Given high development costs and lengthy processes for newly constructed affordable housing, combined with a market where existing units may be purchased at a much lower cost than building new ones, stakeholders such as business owners, developers, and elected officials have expressed growing interest in acquisition as an allowable expense for capital affordable housing funding. However, there are currently very limited public funds available for this sort of acquisition.

This strategy can be divided into two general types of investment – acquisition of naturally occurring affordable housing (NOAH) and newly built market rate housing. NOAH are unregulated rental units that are inexpensive because of low market values, sometimes called “Class C” properties.

On average, NOAH properties are often older, in less desirable locations, have fewer amenities, and are sometimes in disrepair. Newly built market-rate housing tends to be built with the intention of generating profits for investors, but due to current market conditions, are currently selling at prices well below the cost of new construction. These newer properties are often richer in amenities and require less rehabilitation.

Benefits of acquisition and conversion of market rate housing

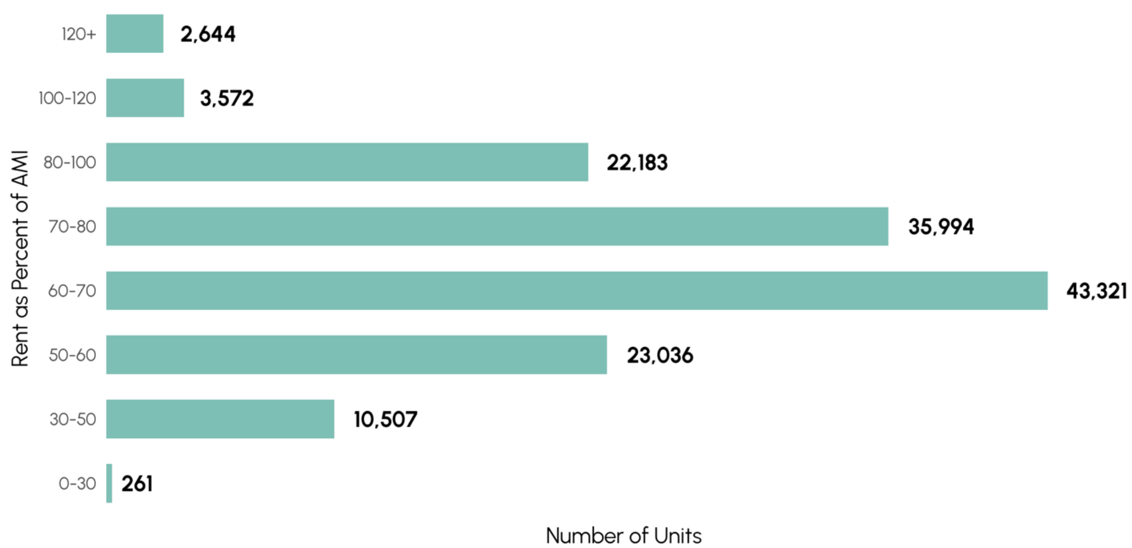
One of the most significant benefits of acquiring and converting units is that it’s generally much more expedient than other production strategies. This is especially the case for newer market-rate units, which typically require fewer renovations to support conversion to regulated affordable housing. For this reason, investing in acquisition and conversion of market rate properties can increase the availability of regulated affordable units much more quickly than building them or converting properties from other uses to housing.

Newly built market-rate housing is often located in higher opportunity neighborhoods where demand for housing has attracted investment, presenting a chance to further fair housing or prevent displacement in gentrifying areas that offer access to amenities. Newer properties also often have updated finishes and appliances, as well as major building systems, providing operational advantages compared to older properties.

NOAH acquisitions can help to maintain affordability to prevent displacement, and depending on location, may contribute to stabilizing gentrifying neighborhoods. As with preservation funding strategies, because these properties are typically occupied, it's possible to effectively target investments toward populations most likely to experience displacement or homelessness, and to geographically balance investments.

According to ECONorthwest, there are roughly 1,500 multifamily properties in the region with 25 or more units that are not regulated for affordability. ECONorthwest analyzed available data for 1,400 of these properties to understand their likely level of affordability. Though not reflective of currently available property, this data provides a broader look into what range of costs could be expected.

Figure 9 - Distribution of units by rents as a percentage of AMI, Source: ECOnorthwest analysis of CoStar data



ECONorthwest analysis identified a median per unit price for properties listed on CoStar is $280,900 for homes that are currently affordable to households with incomes between 80-100% AMI (see table below). Given that projects currently underway in the City of Portland have a total cost averaging about $505,000 per unit, this represents substantial cost savings when considering total unit cost.

Figure 10 - Range of estimated acquisition prices per unit by AMI level, for current market-rate inventory, Source: ECOnorthwest analysis of data from CoStar.

	0-30 AMI	30-50 AMI	50-60 AMI	60-70 AMI	70-80 AMI	80-100 AMI	100-120 AMI	120+ AMI
Minimum	$73,900	$85,400	$134,700	$156,000	$203,000	$226,000	$295,000	$381,600
Median	$85,100	$134,800	$172,100	$206,100	$238,300	$280,900	$352,000	$441,800
Maximum	$92,700	$173,900	$242,700	$279,900	$297,000	$369,600	$450,700	$726,100

Values rounded to the nearest hundred.

Limitations of acquisition and conversion of market rate housing

Acquisition and conversion of market rate units are highly opportunistic, and each property is likely to present unique advantages and challenges. In general, this strategy presents the following limitations:

- There are fewer state and federal funding sources to leverage for acquisitions, especially those that do not require substantial rehabilitation, meaning regional subsidy requirements for acquisition may be commensurate with new construction, despite an overall cost that is much lower.
- Because the properties are already built, there is generally much less flexibility in tailoring a property to the needs of a projected resident and service population. Assuming a focus on deep affordability and PSH, it is necessary to find properties that have an appropriate mix of unit sizes to meet existing need, and adequate service and office space – or space onsite that can be reasonably converted.
- Organizations pursuing acquisitions may have limited options that meet multiple policy priorities. For instance, a property may be located near transit and green space, but there may be no usable office space on-site and multiple entrances, which creates challenges for property management. Or a property may have the right unit mix and ample service space but be located far from services and amenities.
- Like with preservation, acquisitions require thorough evaluation of capital needs to ensure the total expense for the property is known. NOAH, especially, may require significant upgrades, which may increase the overall cost substantially. Properties that might initially seem promising may be cost-prohibitive due to needed improvements.
- When major rehabilitation or improvements are not needed, like with some more recently built properties, there may be fewer opportunities to support equitable construction contracting and workforce benefits.

Additional considerations for acquisition and conversion of market rate housing

The occupancy status of properties is an important consideration in evaluating the potential impacts of acquisitions and should be considered through a racial equity lens. Most properties have some level of occupancy, and especially in the case of NOAH, may have nearly full occupancy. Some existing residents may not income-qualify for units once regulated, which could create a risk of displacement for some or all the existing residents. Particularly for conversion projects seeking to provide deeply affordable units or PSH, this may need to occur upon unit turnover, which could take longer than the time frame to build new PSH units and complicate administration of regulatory requirements. Funding programs for conversions may also only pay per unit converted with a new qualified tenant, exposing developers to additional risk if existing, non-income qualified tenants are unwilling or able to relocate. Whenever possible, a property's resident demographic profile should be evaluated, and displacement risks and mitigation strategies defined before purchases are made.

Property availability may not necessarily align with the timing of funding availability, so periodic solicitations may not be the best funding strategy for market rate acquisitions. Instead, an earmarked funding pool with rolling applications may better deploy available funds at the right time, for the right property. This type of acquisition opportunity fund should set parameters for acquisitions – both newly built and NOAH – and should be regularly evaluated and/or periodically recapitalized by funders so long as favorable market conditions persist.

ACQUISITION AND CONVERSION OF HOTELS AND MOTELS

Due to recent economic conditions, including a pandemic-related decrease in travel combined with a rise in visible homelessness in many major cities nationwide, there has been significant interest in the conversion of hotels and motels to affordable housing and non-congregate shelters. Demonstration projects, such as Oregon Community Foundation's Project Turnkey, have responded to this interest and opportunity through successfully supporting the conversion of hotels and motels to shelter, transitional housing, and permanent supportive housing across the state of Oregon. The relative success of efforts like these has inspired Oregon Representative Suzanne Bonamici to introduce legislation to expand this program nationally through the "Project Turnkey Act" (H.R.8297). There is continued interest among regional stakeholders in exploring opportunities for future investments in hotel/motel conversion to housing and shelter.

Benefits of acquisition and conversion of hotels and motels

As noted above, in recent years, hotels and motels have been available for purchase at a reduced price, presenting an opportunity for expeditious expansion of non-congregate shelter and PSH at a cost that is significantly lower than building new multifamily housing. Because hotels and motels are typically already configured with separated rooms and plumbed for individual bathrooms, renovation needs are often minimal to moderate depending on the age of the building.

The reuse of hotels and motels has had broader benefits beyond expansion of housing and shelter. Notably, renovating and reusing facilities is a more sustainable approach to housing production than building from the ground up or demolishing existing structures to make use of the land they are occupying. Additionally, while hotel/motels may have a shorter lifespan than newly built apartment building, these sites may also present opportunities for phased redevelopment of affordable housing in the future.

Limitations of acquisition and conversion of hotels and motels

Due to a rebound in the travel and tourism industry in recent months, the overall feasibility of hotel/motel conversions has shifted. Another consideration for this approach is that much like other conversions, hotel and motel conversions are highly opportunistic.

Existing building attributes can limit impact of this investment strategy. Many hotels and motels, and particularly remaining budget motels well-suited for conversion due to acquisition opportunity and cost, have moderate to substantial renovation needs. These include modifications to meet residential building code standards and support accessibility, and other needs related to long-term regulated affordable housing. However, if the underlying property is viable for future redevelopment, more moderate investments can be made to make the hotel or motel operable for temporary housing or shelter while development into new housing is pursued. For example, Metro's Housing Bond Site Acquisition Program purchased a motel and leased it as temporary shelter space for 3-5 years prior to the site's development into permanent multifamily housing.

Given that these properties are most often considered for deeply affordable housing and PSH, office and service space relative to the service needs of the projected resident population is typically needed. While some motels and hotels have rooms that can be converted to these uses, in many cases these properties require renovations to add these spaces. In some cases, this may look like reducing the number of potential units on the property to accommodate these spaces or building out new space onto the property to accommodate these uses.

Property layout, the ability to manage foot traffic and generally secure the property are also important. Sightlines, the number of entrances, and other security elements are key to successful building operations, which impact the stability and success of the households that will reside on the property.

The locations of these opportunities may also present limiting factors. Some hotel/motel properties may not be zoned appropriately for residential use and may require additional coordination with local jurisdictions to allow for this type of development. Recently, there has been a high-profile example locally of a motel conversion garnering negative attention and opposition from adjacent property owners and tenants due to the proposed change in building use, resulting in an otherwise funded project not moving forward. Because deeply affordable housing and PSH can receive this sort of push-back from neighbors, discretionary reviews of requested code changes may create risks and uncertainty for this approach.

Further, many viable motel or hotel conversions are also located on or near highways and freeway exits. This can provide for ready access to transportation or economic opportunities but may also present higher exposure to environmental hazards and limited access to green spaces and other basic needs.

ACQUISITION AND CONVERSION OF OFFICE BUILDINGS

Among the conversion opportunities created by the post-pandemic market, office-to-residential conversions have garnered interest due to high vacancy rates among office buildings in the Metro area, especially in Downtown Portland. There is a desire to make use of these existing structures, so some have encouraged exploration of office to residential conversions to expand affordable housing, particularly for people exiting homelessness.

Benefits of acquisition and conversion of office buildings

Like other conversion opportunities, converting existing buildings to new uses represents a more sustainable option than purpose-building new structures. These properties are often located near amenities, such as services and public transportation, as well as economic opportunities. As with other conversions, making use of under-utilized buildings is a strategy that can, given the right building attributes, bring units online more expediently than new construction because of existing infrastructure and building envelope. Due to the significant construction needs associated with office conversations, these properties may also present equitable construction contracting and workforce opportunities.

Limitations of acquisition and conversion of office buildings

Office conversions are limited by the configuration of the office building. A key consideration is the size of the building floor plate, and the distance between the external walls and windows and the center of the building. With too small or too large of a floor plate, it can be difficult to program the space to suit residential uses due to the need for units to have window access that meets code and supports livability while maintaining efficient use of internal space. Newer office buildings tend to have larger floor plate sizes, which may be ill suited for conversions for this reason. It is not possible to know whether a property is truly well-suited for conversion without site-specific analysis.

ECOnorthwest analysis of property data from CoStar has demonstrated that more than half of the office buildings that may be physically suitable for conversion are located in downtown Portland, with all but a few being located within the city of Portland. In addition to geographically limiting the potential of these investment opportunities, this also means that these properties would be required to make significant seismic improvements to meet Portland's updated seismic codes for residential buildings.

Due to the need for substantial renovations, office conversations are likely to have an overall cost per unit that is comparable to new construction, including extensive work to expand plumbing and utility systems. These expenses can be mitigated somewhat by focusing on single-room occupancy (SRO) units, with shared facilities like bathrooms and kitchens. However, this further reduces the number of suitable properties to floor plate sizes that align with SRO configuration needs. That said, with a focus on PSH, there could be limited opportunities for cost effective conversions.

Overall, given all the limitations of this strategy, it may be better suited for housing conversion serving households with higher incomes than those served by deeply affordable housing and PSH.

COMPLEMENTARY AND SUPPORTIVE INVESTMENTS

In addition to the above affordable housing investment strategies, Metro and its consultant team analyzed the potential benefits and feasibility associated with a variety of complementary strategies that could support affordable housing production. While there are many potential policies and actions that could support production more broadly, this section highlights five opportunity areas with the strongest potential to complement and align with creation of deeply affordable and permanent supportive housing, given current funding considerations and priorities. These have been established through research on best practices, interviews with subject matter experts, and impact analysis. For a review of additional strategies evaluated, please see Appendix E.

Land acquisition and banking

In recent conversations about investment priorities, affordable housing developers consistently identified funding to support land acquisition and banking as an ongoing priority. Land acquisition programs can support strategic siting of affordable housing to maximize access to amenities and support fair housing and anti-displacement outcomes. This strategy can also mitigate the overall costs of development, by acquiring land and holding it until a development opportunity arises. Because land value appreciates over time, purchasing land earlier helps reduce costs. Due to land acquisition being a time intensive aspect of the development process, having land readily available for development can support faster development timelines overall.

Metro has an existing Site Acquisition Program within its Transit Oriented Development Program in which Metro staff acquire sites throughout the region based on established criteria, which align with many policy priorities discussed above including anti-displacement and fair housing outcomes, as well as access to transit, amenities, and opportunities. Metro allocated $62 million from its housing bond to support strategic acquisition and subsequent development of affordable housing, in partnership with local jurisdictional partners who typically provided additional contributions from their local share of bond funds. Several Metro bond jurisdictional partners noted the value of this program in ensuring strategic siting and appreciated the ability to work with Metro staff on development strategies for these sites. Others shared that while this program is valuable, developers are also interested in funding opportunities that would allow them to participate in site selection and make strategic investments that align with projected service population and organizational needs.

Pre-development financing

Allowing public funding for pre-development financing at a zero or below-market interest rate can reduce costs and risks for housing developers. This policy reduces the need for developers to secure traditional pre-development loans or use their own capital, decreasing needed gap funding and supporting the growth of small/emerging developers by enabling them to pursue opportunities without risking their own limited capital or relying on traditional pre-development loans.

Structuring these financing opportunities as revolving loan funds, whether administered directly or through a partnering Community Development Financial Institution (CDFI), allows for re-using the same public dollars for multiple projects. Typically, loans are repaid at financial close, upon sale of the property, or after a pre-determined period (for instance, 5 years). An example of this type of program is OHCS's new Pre-Development Revolving Loan Program (PDLP), launched in 2024 and seeded with an initial $9.1 million. Agreements can include options such as loan forgiveness guidelines and contingencies, including the rights of the funder, such as recouping of study results (feasibility, market, zoning, Geotech, etc.), design renderings, community engagement reports, or other results of completed with the funding.

Unfortunately, some funding sources disallow these activities or make them difficult to administer. Property tax funded bonds like the 2018 Metro Affordable Housing Bond, for instance, require all expenses to be "capitalizable", meaning that pre-development expenses that do not result in a physical structure – projects that do not move forward, for instance, are not allowable. This encourages some caution on behalf of funders and can result in a reimbursement-based model, which disadvantages the smaller developers mentioned above.

Stakeholder interviews have highlighted a strong desire to allow use of alternative capital funding sources for pre-development activities, or to leverage other funding sources to support pre-development grants or loans. An example of this is Portland Housing Bureau's successful approach leveraging funding sources, including Tax Increment Financing (TIF) awards and Construction Excise Tax earnings, as revolving pre-development loans to supplement 2016 Portland Bond and 2018 Metro Bond funding. This strategy not only reduces project costs and risks but is also responsive to the state's increased emphasis on affordable housing project readiness, making pre-development dollars more crucial for smaller organizations to identify and pursue competitive projects.

The primary impact of this policy is the reduction of early-stage risks for affordable housing developers, enabling them to undertake more projects. Access to pre-development funds particularly benefits small, emerging, and culturally specific developers by supporting capacity and removing financial barriers. Estimated cost savings for these efforts could be between $2,000 and $5,000 per unit.

Operating support and risk mitigation

In addition to the cost of building or acquiring and converting a property, funders and housing providers must consider the costs to operate the building long-term. In recent years, as noted throughout this summary of findings, operating costs have risen at an unprecedented rate. These cost escalations have outpaced projected expenses for many properties – not due to poor planning, but because economic and social conditions have changed rapidly over the past several years, and many properties' plans pre-dated these shifts. This represents a significant risk to the long-term stability of these properties and the organizations that operate them and could jeopardize future development opportunities.

Operating costs are impacted by a range of factors, among them staffing needs and pay, rental revenue received, maintenance and repair costs, insurance, fees, and utilities. A housing operator's ability to respond to changing needs at a property, such as improving staffing, making physical alterations to the property or managing major incidents and repairs, is directly tied to the property's operating budget. Because these properties rely on rental revenue to fund operating costs, widespread arrears or delays in leasing units impact a property's ability to sustain long-term operations and respond to emerging needs.

The level of operating costs relative to revenue also affect the level of up-front funding a property may need. When revenue exceeds operating costs, this means the property has positive cash flow. A property's projected cash flow can impact the supportable debt it can manage. Measures to decrease operating costs or increase reliable operating revenue can support more private financing leverage, which in turn may lower the amount of up-front gap funding a property requires.

Organizations will also often contribute to up-front development costs through deferring their collection of a developer fee and recouping that payment within a specified period once the property is in operation and collecting rent. However, if a property does not have the expected cash flow, it may struggle to recoup its deferred fee. This is especially challenging for smaller nonprofit developers, as it can constrain their ability to pay staff and pursue future developments.

Below are a few examples of strategies that can have an impact on the long-term operational viability of funded properties.

Operating subsidies

An operating subsidy covers the difference between what a property earns in rent and what it costs to operate the property and respond to needs over time. In some cases, operating subsidies are required for a property to function. For instance, most units regulated at 30% AMI in our region cannot charge rents that pay for needed building operations, especially if those units serve people with enhanced service needs.

Operating subsidies can come in the form of rental assistance payments that are contractually guaranteed to the property, such as federal project based rental assistance (PBRA) or project-based vouchers (PBV). These types of rental assistance programs are key to achieving deeply affordable housing and are necessary for creating PSH, as they pay the difference between what is affordable for a household (typically 30% of gross income or less) and what the property needs to earn in rent for the unit. Because they are reliable over time, banks and lending institutions have confidence in the projected income and have increased comfort in financing a larger amount of the development.

Currently SHS funds a regional rental assistance program – Regional Long Term Rent Assistance (RLRA). RLRA can be committed to properties through set-aside agreements, referred to as project-based RLRA. However, RLRA cannot be fully leveraged like other project-based programs such as PBVs or PBRA, because rental payments cannot be guaranteed beyond 2030 due to the SHS sunset. Without a voter-approved extension of at least 20 years for SHS, RLRA is not considered reliable long-term income and may be treated more like a tenant-based voucher by funders and private lenders.

Payment standards and other aspects of rental assistance vary across programs, and some programs – RLRA for instance – may provide some administrative flexibility, creating key differences in how jurisdictions handle specific aspects of the program. Payment standards, which define how much a property can charge rental assistance programs for specific units, can have a meaningful impact on a property's cash flow. A lower payment standard may serve more households by spreading the resource further, but a higher payment standard creates a deeper subsidy that may better support the operational needs of a property.

Currently RLRA guidelines allow for payments for affordable housing between 60% and 80% of AMI rents. In some cases, 80% rents are being agreed to, but some jurisdictions are more often agreeing to the lower-end 60% AMI payment standard. This mirrors a state-administered PSH PBRA program, which sets payment standards at 60% AMI. When these guidelines were developed, these rents were expected to be sufficient to pay for building operations. However, in response to operating costs exceeding projections and putting PSH properties at risk, OHCS' draft Agency Request Budget includes a policy option package (POP 513) for the 2025/2027 biennium that would increase this to 80% AMI. In much the same way, it may be necessary to consider the benefits and disadvantages of aligning the RLRA payment standard at 80% AMI across the region.

In addition to rental assistance, operating subsidies can come in the form of other types of support funds. These funds could be one time, time-limited, or ongoing. A one-time support could address widespread arrears, stabilizing households and properties to move forward in a better financial position. Time-limited funds could support a property through a difficult period – for instance, initial lease up, when many residents need additional services. Ongoing funding could support a property when operating deficits are expected to continue or become compounding. Regardless of strategy, allowing flexibility in administration of operational support funds to serve both new developments and existing properties could ensure that funders are able to respond to shifting industry needs without having to structure new funding programs.

Some jurisdictions provide operational support funds to cover supplemental expenses like amplified resident services, maintenance, security, or other types of expenses for specific property types. For instance, the Washington State Department of Commerce, one of the state's two housing finance agencies, also provides a fund called the "Permanent Supportive Housing Operating, Maintenance, and Services (PSH-OMS) program that provides "gap" operating and maintenance funds, as well as some tenancy supporting services to awardees that have been funded in part by the state's Housing Trust Fund. Locally, Washington County has also leveraged SHS to fund enhanced operational supports in properties that meet a specific percentage threshold of PSH units.

Affordable housing developers and operators have shared that expanding access to rental assistance, increasing payment standards and/or providing additional operating support funds would likely have a significant impact on the current operating challenges being felt across the industry, and ensure new properties are better able to serve residents transitioning from extended periods of homelessness.

Capitalized operating reserve fund

In addition to providing direct operating subsidies, another potential strategy is to create a capitalized operating reserve fund that can cover projects when operating costs exceed revenues. These funds are essentially savings accounts tied to specific properties that can be funded with up-front capital, but that can pay for unexpected operating cost overruns.

While there is some interest in exploring portfolio-wide or community-wide operating reserves, these funds may need to be project-specific, as that allows for the fund to be capitalizable and provides certainty to the developer and funding partners that the reserves will be available for that individual project. The amount of funding required is dependent on potential future cost overruns, but conversations with owners and operators of affordable housing indicated that their properties were experiencing $1,000 to $2,500 per unit in annual operating cost overruns. If this fund was expected to cover potential cost overruns for the first 15 years of the project, that would translate in up to $37,500 per unit of required funds in the capitalized operating reserve.

Risk mitigation pool

Another strategy to support existing and future projects against unexpected costs is to create a risk mitigation pool (RMP). An RMP would not be project-specific, but would instead allow eligible projects facing unexpected costs, such as repairs to extraordinary property damage, to apply for funding to cover those costs. One benefit of an RMP is that it can reduce a housing operator's reliance on claims to insurance providers, who base their insurance rates off the operator's history of filing claims. As operators continually file claims to cover unexpected costs, insurance providers then increase rates, impacting already strained operating budgets. Given that rising insurance rates are a primary cost driver in operating cost escalations, this can be a valuable resource for eligible properties.

Depending on how an RMP is structured, another benefit is that it could, if programmed to do so, provide a level of certainty for project funders that there are potential funds to cover operating cost overruns. In this way, an RMP could achieve some benefits on a portfolio- or community-wide basis that an operating cost reserve achieves on a property level, covering unexpected operating costs and reducing risk in affordable housing investments throughout the region.

In an acknowledgement of the risk that insurance rate and other cost escalation poses, OHCS' draft 2025/2027 Agency Request Budget also includes a request for $10 million in funds to expand access to RMP-type coverage to a wider range of affordable properties in its portfolio, structured similarly to its existing $4 million RMP for PSH investments (POP 517).

Currently, some Metro bond-funded properties have access to RMPs, such as properties with SHS-funded RLRA commitments or those with OHCS PSH investments. With future funding at the regional level, allocations to existing RMPs or structuring additional RMP-like funds to cover gaps may not necessarily translate into direct cost savings on a project-level basis, but could provide a necessary backstop to prevent regional affordable housing providers from having to use their own funds to cover excess costs and help attract more capital to the region.

Jurisdictional support for implementation

Local System Development Charges (SDCs) and other fees charged by local jurisdictions contribute to the cost of building affordable housing. Jurisdictions can choose to offer waivers or deferrals for projects meeting specific criteria to reduce these costs and lessen the reliance on state and regional funding. At the same time, SDCs and other fees are essential for necessary infrastructure expansion to accommodate these new homes, so waivers can contribute to local funding challenges and must balance local funding needs. Some local jurisdictions in the Metro region already offer fee waivers, while others contemplate them for future support of affordable housing as part of their Housing Production Strategies. Future regional funding could provide support to jurisdictions in the form of grants or other incentives, resulting in efficient use of gap funds, especially if upcoming state investments in infrastructure reduce local reliance on SDC revenue. SDC waivers can save $10,000 to $25,000 per unit, depending on location and project size.

Capacity building support for smaller organizations

Smaller organizations, emerging, and culturally specific developers play a critical role in the provision of affordable housing that meets the wide-ranging needs of our diverse region. As noted throughout this document, these smaller or newer development groups generally have fewer resources and capital, limiting their ability to take on debt and risk. Future regional funding could allow for grantmaking to these organizations to increase their capacity and ability to be competitive in securing state, federal, and private funding. Investments could also include technical assistance and training.

It is worth noting that other strategies mentioned above, such as land acquisition and pre-development financing, are also tools that have robust impacts for smaller, emergent developers and can support improved resident outcomes through more tailored, culturally specific, community-driven approaches.

Additional evaluation

Though ranging across a variety of strategies, this evaluation was limited in scope and scale and was intended to offer a high-level understanding of general feasibility and possible outcomes of select strategies. The evaluation was constrained by the funding sources considered, priorities associated with current political and market conditions, and the timeline of the COO-convened Stakeholder Advisory Table conversation. This moment-in-time is especially dynamic, as several funding partners are in the midst of consequential change processes that impact funding and data availability.

Further research, engagement, and analysis is recommended to have a more complete understanding of opportunity and investment need, if resources and policy conditions allow. It will also be important to consider a range of changes that occur between this evaluation and any deployment of new funding, and the administrative constraints of the eventual governance model.

Among possible future focus areas, the following should be further evaluated:

Social housing

In recent years, several innovations in affordable housing financing and ownership structures have demonstrated success. For example, models like the city of Vienna, Austria's social housing program have stood out as presenting opportunities for replicating these successes in the Portland Metro region. In this model, the city of Vienna collaborates with private developers to provide affordable housing through a combination of publicly sponsored land and loan products, both with more favorable terms than the market would provide, and in exchange requires half of funded units to be affordable for lower-income residents, with the remaining able to be leased to moderate income residents. While not in scope for this evaluation, analysis of the feasibility and potential outcomes of the Vienna social housing model should be a priority as new funding and policy making opportunities arise.

Middle income housing

This evaluation was focused on affordable housing development strategies and supporting the production and preservation of deeply affordable housing. However, there is a growing need for public funders to consider how best to maximize production at all levels, including middle income housing affordable to households with incomes between 80-120% AMI (sometimes called workforce housing). In March of this year the state legislature approved the allocation of $75 million to OHCS to seed a revolving loan fund to support financing gaps for local jurisdictions to develop this sort of housing. Additional research and evaluation should occur to understand the role of local and regional funders, such as Metro, in the financing and development of middle income housing.

Environmental justice

Because Metro and its consultant team considered these investment strategies through a range of criteria, the evaluation for all strategies across most of these criteria was limited. One key area where a fuller understanding of need and opportunity exists is within the areas of climate resilience, sustainability, and environmental justice. A deeper look into this could support prioritization of property investment focuses, available leverage, benchmark setting, and relevant metrics for the region.

Fair housing evaluation

Metro has a role as a land use authority in the region and funder of affordable housing and some key infrastructure, in supporting efforts to affirmatively further fair housing and prevent displacement across the region. More work is needed to understand the current state of fair housing regionally, to evaluate opportunities to improve housing choice and access, and to determine Metro's role in supporting this work. The state-mandated Regional Housing Coordination Strategy, which must be produced by the end of 2025, presents an opportunity for Metro to work with local jurisdictions to conduct this evaluation and develop plans to improve fair housing outcomes.

Resident and participant engagement

The Metro COO Recommendation process was supported by engagement with a diverse cross-section of stakeholders, including community engagement conducted in partnership with local community-based organizations. This work surfaced the need for further engagement with residents and participants in Metro-funded housing and services, to understand existing barriers and needs and to inform continued program evaluation and improvement, planning and policy analysis, and future investment strategies.

Finance sector engagement

Further work with financial stakeholders is recommended to better understand the projected impacts of specific actions and investment considerations once more is known about possible funding and priorities. While multiple subject matter experts with this type of expertise were engaged for this high-level evaluation, as planning continues, it would be necessary to engage a more diverse group of investors around specific issues such as underwriting standards, risk mitigation opportunities, rental assistance leverage, tax credit equity considerations, development capacity building and support, and other key investment considerations.

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Appendix A: Evaluation criteria detail

Evaluation criteria detail and tables

Overview

To support comparative analysis, Metro created an evaluation framework to consider the feasibility, impact, and equity considerations associated with different investment strategies.

Below is a description of selected criteria and sub criteria with relevant research questions, organized under two focus areas – policy outcomes and feasibility considerations. Not all focuses or questions are addressed in the summary of findings provided in the attached report. More detail is intentionally provided in areas that most align with the Metro Chief Operating Officer's needs in developing a regional housing funding recommendation to Metro council.

Policy Outcomes

Policy outcomes can be characterized as possible impacts that could be achieved through funding of a specified strategy.

For this evaluation the following possible policy outcomes were considered:

Populations Served

- Unit Size / Type:
    - What size households are best served by this investment strategy? What are the relevant constraints?
    - What is the relative need for serving these household sizes?
    - What are the demographics served currently by this type of investment strategy?
    - How do the unit types most created by this investment strategy support racial equity, improved accessibility, etc.? Any special populations prioritized?
    - Do these unit sizes and types align with PSH household need?

- Depth of Affordability:
    - What income levels are served by this strategy?
    - What is the relative need for this type of affordability range?
    - Who is served by this affordability level? How does it align with Metro region housing needs?
    - How does this depth of affordability serve specific populations to achieve racial equity, improved accessibility, etc.?

- Length of Affordability:
    - What are the specific issues relative to this type of investment that constrain levels of affordability?
    - Does this strategy meaningfully advance long-term household stability and upward economic mobility relative to other strategies? For whom? What considerations exist?

Appendix A: Evaluation criteria detail

- SHS Alignment / Preference Considerations:
    - Does the strategy support alignment with homeless response systems, including coordinated entry, to address placement goals?
    - Does the investment strategy support project-based PSH set-asides, RLRA voucher overlay, etc.
    - How does the investment strategy fund and support partnership or placement through culturally specific providers or other population specific organizations (e.g. veterans, youth aging out of foster care, LGBTQIA+, etc.)

- Resident Demographics:
    - What are the existing or projected resident demographics of possible investment opportunities?

Equitable Contracting / Workforce opportunity

- Contracting Equity – Trades / Construction & Operations:
    - What are the opportunities to improve both trades and construction as well as ongoing operations contracting equity using this strategy?
    - What are the tradeoffs of this approach vs. others?

Geographic Considerations

- Distribution of Sites:
    - Where are the available opportunities? Are these equally distributed throughout the Metro region?
    - Are there opportunities that further goals due to location?
    - Does the strategy support affirmatively furthering fair housing or mitigating displacement?

Environmental Justice

- Climate Resilience:
    - Does the investment strategy encourage or allow for environmentally resilient buildings or mod / rehab to achieve this?
    - How does the strategy protect or support future residents through climate change?

- Sustainability:
    - How environmentally sustainable is the investment strategy when compared to others?

- Equity of Access to Nature:
    - Does the investment strategy support improved access to nature / green space for marginalized communities?
    - Are the opportunities near green space?

Appendix A: Evaluation criteria detail

Feasibility Considerations

Feasibility considerations are intended to evaluate the overall achievability of different strategies given known and unknown constraints.

For this evaluation the following feasibility considerations were considered:

Production Potential

- Leveraged Funding Availability:
    - What funding is available to leverage at the state and federal levels? What are high-level requirements and considerations?
    - How much leverage would be needed for different production strategies as part of the overall capital stack?
    - Is this investment strategy impacted by PAB constraints? What are the impacts?
    - Are there additional funding types needed to support deployment and what is the availability of these resources? Are there other constraints for these resources?
    - What are potential equity considerations for leveraged funding sources?

- Cost:
    - What is the per unit cost for different unit sizes, types, affordability levels, etc.?
    - What are the costs and are there underwriting premiums when programmed as PSH?
    - What cost differentials exist across the Metro region? Is this strategy less feasible in specific jurisdictions?

- Market Factors:
    - What economic conditions must exist for this to be a feasible production strategy?
    - What positively or negatively impacts overall production?
    - What is the scale of opportunity across the Metro region specific to this strategy?

- Project Delivery Timeline:
    - Does this strategy help deliver housing at a faster pace?
    - What conditions are required to support an expedited delivery timeline?

Administrative Considerations

- Affordability Management:
    - How is long-term affordability managed?
    - Is long-term management and monitoring needed?
    - What are the specific constraints that determine length of affordability for this strategy?

- Developer / Provider Capacity:
    - Are there constraints relevant for this investment strategy due to developer or provider capacity concerns?
    - Does the strategy require expertise that we do not yet have or do not have enough of?
    - Does the strategy offer opportunities to build needed capacity?

Evaluation of affordable housing investment opportunities: Technical engagement summary

September 2024

Introduction

Between February and August of 2024, Metro interviewed dozens of industry stakeholders and subject matter experts in affordable housing development, finance, funding, operations, and policy to understand opportunities, challenges and considerations for future affordable housing investments. The purpose of this effort was to inform an affordable housing funding recommendation process led by Metro COO Marissa Madrigal. The resultant recommendation and appendices describing this process in more depth are available at oregonmetro.gov/housing funding.

Interview participants included affordable housing developers with 2018 Metro affordable housing bond funding awards and jurisdictional staff involved in administering Metro bond funds, as well as experts in finance/lending, housing operations and services, housing policy, and related fields. Many interviews spanned multiple subjects and were flexibly structured to center the interviewees' priorities for feedback. A list of those interviewed can be found attached to this engagement summary (Engagement Summary Attachment 1).

Interviews were designed to gather a range of in-depth insights and support a more nuanced discussion. Through the interviews, Metro sought a better understanding of the current market conditions, funding and programmatic constraints, and opportunities and considerations for future regional investments in affordable housing. Metro also sought feedback on the implementation of the Metro bond, to inform lessons learned and note opportunities for improvement. A narrative overview of key takeaways from these subject matter expert (SME) interviews are summarized by area of analysis below.

In addition to these interviews, Metro regularly updated Housing Oregon membership during Portland Metro Policy Council Meetings. Housing Oregon is an industry group of 75 organizations that build, finance, and support affordable housing. Metro is an affiliate member and coordinated agenda items at several Policy Council meetings related to the housing funding recommendation process and this technical engagement between March and May of 2024.

During the visits, Metro informed the group about the exploration of continued funding for affordable housing construction, invited members to participate in the technical engagement process, and heard priority considerations from members. This group repeatedly raised concerns that escalating operating costs were quickly becoming a significant challenge to the stability of the affordable housing industry. To better understand this issue, Metro convened a listening session around operating costs with Housing Oregon and Housing Development Center. This listening session is outlined below as well, along with key findings.

Appendix B: Technical engagement summary

Summary of Findings by Area of Analysis

Below is an overview of findings that informed Metro's investment strategy analysis. Interviews were tailored to each person's areas of expertise and involvement with affordable housing, with interview notes documenting key takeaways from each discussion. Due to this, direct quotes are not provided, and perspectives are not directly attributed to individual interviewees. Instead, common themes are shared.

Acquisition and Conversion

To better understand acquisition and conversion opportunities and considerations, Metro interviewed SMEs with experience in recent acquisitions and conversions, both regionally and outside of the state. Experts interviewed had a breadth of experience related to hotel/motel, office/commercial, newly built market rate housing, and naturally occurring affordable housing (NOAH) acquisition and conversion.

Metro learned from these SMEs that acquisition and conversion is typically highly opportunistic, and that a range of factors impact potential outcomes for this investment strategy. The conditions of the existing property, including its age, design, location, current zoning, level of occupancy and other property attributes, impact the type of conversion it may be best suited for, as well as the overall project cost and timeline. For this reason, the acquisition process should ideally include a robust capital needs assessment, an evaluation of impacts to existing residents and staff, and an assessment of possible barriers to successful conversion.

Experts shared key factors impacting potential cost of conversion, including the location and current use of the property, as well as the property's capital improvement needs. Modifying a building use or undertaking a major renovation could trigger substantial seismic upgrade requirements in selected jurisdictions, or zoning / code changes, for instance. In addition to any code-required renovations, experts advise that budgets for acquisition and conversion should consider accessibility upgrades as well as needs for successful ongoing operations. Because many housing providers lack expertise in acquisition and conversion, direct funding for technical assistance is also needed.

Evaluation of properties for acquisition and conversion funding should also center the populations to be served post-conversion, and evaluation criteria should consider the breadth of needs of these service populations, as well as the trade-offs associated with each property. For example, acquiring an existing multi-family, market-rate building for conversion to permanent supportive housing (PSH) may be less ideal if the property does not have space for the programming and services residents will need, needed building security features, or an adequate capital improvement budget to achieve needed upgrades.

Some SMEs cautioned that displacement risks need to be evaluated, particularly for market-rate residential buildings with existing tenants and hotels/motels currently in operation. Especially if the conversion is intended to achieve a deep level of affordability, or overlay a program type with specific referral requirements, like PSH, occupied buildings may require more nuanced approaches to conversion. Some jurisdictions require relocation assistance for residents that will not meet eligibility criteria, which is a best practice, but there may be limited available funding options for permanent relocation assistance.

Despite these considerations, several SMEs encouraged Metro to fund acquisition and conversion opportunities, as the total cost per-unit is currently sometimes lower and there may be an opportunity to make regulated affordable units, including urgently needed PSH, available faster than new construction. Though some existing state funding programs technically allow for acquisition, there are often constraints – such as one source's requirement that the acquisition require substantial upgrades – that impact the availability of these funds for emergent opportunities. This means that time-limited market conditions, such as cost-effective acquisition of newly built market-rate multifamily properties have been difficult to capitalize on with existing funding sources.

Preservation of Regulated Affordable Rental Housing

Across many interviews, housing industry experts emphasized the importance of preservation funding. State and federal funding for preservation is currently unreliable and typically insufficient. Multiple SMEs highlighted the need for a more reliable, dedicated funding source, with some SMEs suggesting that Metro should engage partners to establish this sort of fund. Preservation funding is often split between several priorities, including manufactured home park preservation.

Some interviewees shared that inadequate preservation funding and unsupported operating cost escalations were closely linked in presenting substantial risk to non-profit organizations and the regional housing and homeless response systems overall. One local leader warned that it was important that our region take this seriously, and that the 2022 collapse of the Skid Row Housing Trust – a large Los Angeles area non-profit that operated dozens of properties specializing in serving people exiting homelessness – is an example of what can happen if systemic financial challenges aren't addressed.

SMEs also suggested funding tenant protections and alternative approaches to ensure housing stability for residents of properties with expiring affordability restrictions. In cases that properties' affordability is unable to be preserved, regional tenant protection vouchers, which could subsidize rent for existing tenants but that would be non-transferrable and sunset if the household moved, could be a cost-effective strategy to support the ongoing stability of residents and mitigate against cost burden, displacement, or homelessness as rents increase.

SMEs shared that the state of Oregon has done significant work recently, with the support and advocacy of partners like the Network of Affordable Housing, to track and evaluate affordable housing preservation needs across the state. This has included the development of and needed updates to the Publicly Supported Housing Preservation (PuSH) program, and developing an updated Affordable Housing Preservation Strategy Framework, last updated in 2023, to characterize OHCS's funding preservation funding strategy and prioritize future investments. SMEs shared that these updates will enable funders to make strategic investments in preservation, because they will have up-front information about what the funding will support and can better help legislators understand the specific risks to their constituencies if adequate funding is not allocated.

Affordable Homeownership

Once fully expended, the Metro bond will have contributed to the development of nearly 160 affordable homeownership opportunities across the Metro region. SMEs with experience in affordable homeownership provided a range of suggestions for potential future actions Metro could take to support continued investment in affordable homeownership opportunities, including considering urban growth boundary extensions to incorporate affordable homeownership opportunities, and drawing inspiration from programs such as the Black Homeowner Initiative (BHI) in the greater Seattle area. The BHI is focused on increasing homeownership among Black households in the region and has set a goal of making homeownership a reality for 1,500 new low- and moderate-income Black homeowners. The initiative brings together nonprofit, government, financial, housing development, and philanthropic partners to innovate on homeownership solutions to reach their goal of 1,500 new Black homeowners by 2027. Some SMEs also encouraged Metro to fully fund a project, rather than asking developers to braid multiple gap funding sources.

The city of Hillsboro's efforts to support affordable homeownership could also serve as a model for Metro's future investments and actions. During 2023, the city sold 20 permanently affordable homes to low- and moderate-income earning families. Using federal Community Development Block Grant funding, the city of Hillsboro funds payment assistance via a partnership with Proud Ground. Additionally, the city donated land in 2022 for the development of 18 affordable townhomes. SMEs highlighted the need for racial equity to be a primary consideration in future affordable homeownership investments, to help mitigate the racial homeownership gap, and corresponding wealth gap, brought upon by historic and current exclusionary land use and lending policies and practices.

One SME expressed that the community land trust model, which is the most common affordable homeownership model in our region, may not be suitable for populations who seek to own land and that more should be done to ensure that affordable homeownership opportunities are available with a more traditional land-ownership structure. Funding for down payment assistance and programs which reduce interest rates are alternative options that Metro could support to meet this need.

Gap Financing of New Rental Construction

Through this technical engagement, Metro sought to update assumptions for gap financing of new multifamily rental construction and understand opportunities for administrative improvements.

Across interviews, SMEs suggested Metro and its implementation partners better align with other funders – for instance, state and federal funders. Some interviewed emphasized the time required to put together an application as well as the fees associated with applying for funds, and how burdensome this can be for developers. Multiple interview participants, including developers and jurisdictional partners, emphasized the impact of a perceived lack of coordination around private activity bond (PAB), and encouraged Metro to factor PAB and OHCS gap funding availability into any future production modeling. Some recommended considering supporting some projects without 4% LIHTC, which is constrained by PAB availability, with future funding.

Most developers shared that development costs have increased and encourage Metro to consider adjusting subsidy caps, expanding allowable uses and reexamining existing underwriting guidelines. SME shared that some of these changed in the implementation of the Metro bond, which was a challenge when developments were already in progress. For instance, a developer fee cap was introduced after implementation began, and many have shared concerns that this developer fee cap is overly restrictive, impacts smaller non-profits' ability to build capacity and manage cost increases, and that fee caps should not be a flat rate but should be instead tiered based on the size and complexity of developments. Further, SMEs urged greater clarity in underwriting guidelines and allowable expenses, as there were inconsistencies or shifts experienced by developers.

Those interviewed shared ideas for improving deal terms, including options like providing guarantees that could increase access to loans, as well as eliminating the Supportive Housing Services (SHS) measure sunset or extending it sufficiently (20-30 years) to further enable projects to secure loans based on a long-term commitment of SHS-funded Regional Long-Term Rental Assistance (RLRA).

Development timelines are a key challenge for this strategy. Projects experience delays for a myriad of reasons – including slow permitting, which is impacted by inadequate staffing, discretionary design and land-use review practices, lack of responsiveness from utility operators, and other factors. When project approval timelines lag, this can complicate an already challenging and lengthy process. Developers interviewed recommended streamlining Metro's funding approval processes to reduce duplication and uncertainty and working with local jurisdictions to simplify permitting processes or requiring SDC waivers and other supports.

Operational challenges were a consistent priority identified by interviewed SME involved in property development and operations, including insufficient funding to meet the service needs of residents and address other areas of cost escalation, such as insurance and rising interest rates. SMEs pointed to a range of strategies to address these challenges, including adjustments to SHS RLRA payment standards, use of SHS funding for operating subsidy, creation of pooled insurance funds, higher developer fee standards, and coordination with lenders/investors to support improved terms. For more detailed feedback on this subject, see key takeaways in "Operating Cost Listening Session" below.

Policies, Actions, and Incentives to Support Affordable Housing Development and Operations

Across interviews Metro and its consultants requested feedback about needed supports, system gaps, and innovative strategies for creating and sustaining affordable housing. Several SME had ideas for innovations that could take advantage of market conditions, reduce development costs, or expedite delivery of new affordable housing. Others encouraged Metro to consider the needs of existing properties, and to prioritize eligible expenses and system improvements that could bolster housing operators who are struggling to meet the needs of residents with robust support needs, particularly those exiting homelessness.

As mentioned above, streamlining processes was a priority identified across many interviews. In addition to improvements in funding availability processes, application review and funding dispersement / approval processes, SME recommended Metro consider funding other types of system improvements that could create more streamlined processes. Some included directly funding improvements identified through processes such as the Governor's Housing Production Advisory Council, which was convened to recommend improvements to the state's housing production system. Among these, improvements to permitting processes or land readiness activities were offered for consideration. One SME discussed the role Metro plays in land-use planning and how it could leverage its role to streamline transportation study and upgrade requirements, which may have a meaningful impact on project costs and timelines.

Those interviewed regularly discussed the role of SDCs and tax abatements in supporting affordable housing development and encouraged funders to implement these strategies to encourage development. However, some partners raised concerns about the cost of SDC waivers and tax abatements to jurisdictions, sharing how this often complicated their ability to expand infrastructure and services for these properties. There is a tension between complementary incentives such as these and land-readiness, especially. Some felt that directly supporting implementing jurisdictions in providing these incentives could address this tension.

Many SME offered feedback about specific, targeted investment strategies that could improve conditions for new construction. Production challenges shared included difficulty in accessing land acquisition, capacity-building, and pre-development funding, particularly for smaller and culturally specific developers. Due to rising interest rates and the challenging operating environment many housing operators are navigating, private capital needed to pursue new developments can be difficult to access. Many SME shared that making pre-development an allowable expense for future funding should be a priority. Whether through an advance on an early commitment of funds, mirroring City of Portland's administration of the Metro bond, or through structuring a pre-development grant or below-market revolving loan program, SME felt that Metro should work with implementing partners for new funds to ensure smaller, culturally responsive organizations are able to participate through better supporting pre-development activities.

Similarly, those interviewed regularly mentioned the importance of land acquisition funding. Funding commitments can be difficult to secure without site control, and small, non-profit developers can struggle with purchasing and managing the carrying costs of sites while pursuing developments. SME shared that Metro's Site Acquisition Program, which secured key sites for development in all implementing jurisdictions, was valuable but that it was also important to have access to direct funding for land acquisition. Like pre-development funding, direct land acquisition funding could be administered through a grant program or a revolving, below-market interest loan program.

Capacity building support, especially for small non-profits and culturally specific organizations was offered as an investment opportunity by multiple interviewees. Especially with an increased focus on readiness-to-proceed for OHCS funding programs, some felt that large, for-profit developers would be at an unfair advantage in securing funds, because they can often afford up-front costs and to maintain a larger development team, allowing them to move more quickly in some instances. One opportunity for building capacity, outside of a grant program, is reapproaching developer fees, which historically have allowed organizations to build capacity over time. Regularly, developers connected current industry challenges in cost escalation to increased risk for investors and lenders, encouraging Metro and other funders to better support current properties in navigating challenges to ensure the development pipeline was not negatively impacted.

Among innovations suggested by those interviewed, exploring investments in modular construction, mass timber, and funding more acquisition and conversion opportunities were regularly mentioned. One interviewee had significant expertise in modular construction and emphasized the cost savings and expedited development potential of this innovation, but also the up-front investment needed to achieve cost savings at scale. Some discussed the benefit of investing in mass timber at scale, and how this innovation could eventually bring down the cost of larger developments. A number of interviewees mentioned feeling frustrated that funders weren't able to better support the acquisition of properties that were for sale for a price well-below new construction, with some identifying specific sites they would be interested in purchasing and converting if funding were made available.

Operating Cost Listening Session

Across subject matter expert interviews and during updates with the Portland Metro Policy Council an often recurring theme was rapidly increasing operating costs as a pressing challenge for affordable housing providers. To better understand this, Metro co-convened a focused discussion aimed at enhancing our understanding of the cost drivers, impacts, and possible solutions for property operations with Housing Oregon and Housing Development Center (HDC). The listening session focused on various types of affordable rental housing, including PSH, and illuminated considerations for the types of operational support needed in the industry.

Content and Approach

Metro, Housing Oregon, and HDC invited affordable housing developers, operators, and industry experts in the region to attend a 90-minute virtual session in May of 2024.

The virtual session opened with a welcome and a short review of the meeting context and discussion of goals. Most of the session was spent in an interactive question and answer session, using the live polling tool Menti to gather input as well as the conference call chat function. The session had limited open discussion, which was spent seeking clarity and additional detail around Menti and chat inputs. Session organizers provided a survey option for affordable housing providers who couldn't attend the session. For a full overview of responses, please see Engagement Summary Attachment 2.

Additionally, attendees had the option of providing more detailed feedback following the session via a follow-up survey and through sending Real Estate Owned Schedules to HDC to include in an anonymized analysis of operating costs across the region. The results of HDC's analysis are covered in Metro's full findings report (page 20), with the collected data informing these results attached to this summary (Engagement Summary Attachment 3).

Key Takeaways

Cost Drivers: When asked to rank cost drivers, housing providers shared that four key factors most contributing to operating budget difficulties are insurance rates, unexpected major repairs, onsite staff salaries, and nonpayment of rent. Almost half of respondents also shared that staffing challenges, particularly staff turnover, contributed to operating budget difficulties.

When asked to provide more information about operating cost drivers, vacancy rates and resident acuity were mentioned multiple times. Comments captured in Menti about cost drivers included:

"Units operating as "de facto" PSH, but serving residents with PSH needs."

"PSH provider turnover and serious capacity issues of service providers."

"Frequent turnover of PM [property management] agencies and AM [asset management] staff which causes gaps in service and oversight."
"For us the turnover timeline for any voucher based unit in multco [Multnomah County] is minimum 3 weeks simply due to the voucher application process…"

"Vacancy. Long leasing times due to overlapping screening/ referral processes; and limited applicants within narrow income bands."

Current State: Discussion attendees identified units without rental assistance regulated at 30% and 60% area median income (AMI) PSH units as the unit types with the greatest operating budget difficulty. Among these, 30% AMI units without rental assistance or other operating subsidy were by far the most likely to experience operating cost difficulties, with almost all respondents indicating this unit type on average was experiencing extreme financial difficulty.

Relatedly, attendees and survey respondents identified non-PSH units serving people exiting homelessness, units serving PSH households and other homeless system referrals, and units serving families as the most predictive of operating budget difficulty. Homeless system referrals and lack of access to risk mitigation and operational subsidy supports were identified as other factors most predictive of operating budget challenges. Respondents also shared that small units, particularly single-room occupancy units, and scattered site and low-density developments are experiencing significant operating cost related challenges.

Impacts: According to attendees and survey respondents, operating cost challenges impact residents in widespread ways. They most impact residents through staff retention and working environment, the cleanliness of property or maintenance responses, and perceived or actual safety. Choice of property management and resident or supportive services providers is also impacted by these challenges.

When asked "How do operating cost challenges most impact residents?" in an open-ended format, Menti comments included:

"Staff turnover isn't just about workload, but also about availability/predictability and relationships for residents"

"poor customer service from property management due to turnover/open positions"

"Staff turn means constantly reengaging with someone new and the impact of having to retell your trauma to someone new."

"Overall decreased quality of life."

"less safety and concerns about safety; longer times to respond to maintenance requests; overall reductions in housing stability if services are impacted"

"Lack of stability as staff turns over or isn't properly trained, lack of community feeling."

Appendix B: Technical engagement summary

Solutions: Respondents shared how property developers are responding to the current operating cost environment in planning new projects. Common responses included budgetary adjustments such as minimizing debt, updating budget assumptions, seeking additional public funding sources as well as advocacy and shifting development focuses in ways that may impact regional outcomes.

Menti Comments included:

"Less PSH; more higher income"

"Seeking rural location options"

"Sharing operating costs with developers and sitting down with developers to review material choices, appliance selection, space for programming in the design"

"minimize debt, show real cost to funders"

"Reducing / eliminating lowest income restrictions, which means we are not serving highest needs; pushing back on underwriting expectations when possible; maximizing rent assistance; look at mixed income"

Respondents also identified several ways funders can best respond to the current operating cost environment in funding new projects, including:

- Increased and flexible subsidy amounts; for instance, increasing per unit funding, more capital and gap funding, and increased subsidy limits.
- Expanding rent assistance to serve more households.
- Expanding risk mitigation pool (RMP) like assistance to cover more units.

Other ideas that emerged were systems-level support work and funder flexibility.

When asked to rank a list of possible solutions, attendees ranked expanding rent assistance to serve more households as the top solution to unanticipated cost increases, followed by development supports (for example, pre-development grants, lower than market interest loans, and land acquisition grants), increased payment standards for rental assistance, and an annual operating subsidy "premium" for specific property or unit types.

Illustrative open-ended responses included:

"Increase rent assistance payments"

"Get rid of subsidy caps! Set thresholds for what kind of housing they want then FULLY fund it. Braiding funding takes time and money."

"update operating assumptions"

"Operating support: Move from project to portfolio (operator)(flexibility)"

"Expand RMP-type assistance to more units"

"Underwrite to a realistic pupy [per unit per year]; prioritize subsidy > capital"

"Set a systems table – better connect behavioral health support"

"No debt service for deeply affordable projects"

"Funding should be more flexible so projects don't need to have multiple sources for one project."

"vouchers for 30% ami units"

Appendix B, attachment 1: List of technical engagement interviewees

Metro offers its sincerest appreciation for the following subject matter experts, listed below, whose generous contribution of time and expertise across dozens of interviews conducted between February and August 2024 informed our understanding of current affordable housing investment needs, opportunities, and priorities.

Noah Rosen, Director of Development, Pacific Northwest, BRIDGE Housing Corporation

Martin Leung, Director of Acquisitions & Planning, BRIDGE Housing Corporation

Smitha Seshadri, Executive Vice President of Development, BRIDGE Housing Corporation

Javier Mena, Affordable Housing Manager, City of Beaverton

Ashley Miller, Housing Services Manager, City of Gresham

Hawie Petros, Housing Development Coordinator, City of Gresham

Chris Hartye, Senior Project Manager, City of Hillsboro

Danell Norby, Housing Investment & Portfolio Preservation Manager, Portland Housing Bureau, City of Portland

Helmi Hisserich, Director of Portland Housing Bureau, City of Portland

Michael Buonocore, Interim Deputy Director of Portland Housing Bureau, City of Portland

Jessica Woodruff, Chief Development Officer, Community Development Partners

Jilian Saurage-Felton, Housing Director, Community Partners for Affordable Housing

Rachael Duke, Executive Director, Community Partners for Affordable Housing

Claire Parisa, Director, Acquisitions – Housing Credit Investments, Enterprise Community Partners

Emily Alvarado, Vice President Northwest Market, Enterprise Community Partners

Jess Blanch, Program Director, Pacific Northwest, Enterprise Community Partners

Scott Greenfield, Senior Director of Acquisitions, Real Estate Equity, Enterprise Community Partners

Bryan Guiney, Field Office Director, Department of Housing and Urban Development (HUD)

Kirsten Ray, Senior Program Analyst, Department of Housing and Urban Development (HUD)

Nora Cronin, Director of Real Estate Development, DevNW

Jill Sherman, Co-Founder, Edlen & Co

Sarah Radcliffe, Director of Government Relations, Habitat for Humanity Portland Region

Steve Messinetti, President & CEO, Habitat for Humanity Portland Region

Maryam Bolouri, Director of Real Estate Development, Hacienda CDC

Amanda Saul, Assistant Director of Development, Home Forward

Donna Kelley, Lead Asset Manager, Home Forward

Jonathan Trutt, Director of Development, Home Forward

Jessy Ledesma, Principal, HomeWork Development

Devin Ellin, Director of Housing Development, Housing Authority of Clackamas County (HACC)

Andrea Sanchez, Development Director, Housing Development Center

Traci Manning, Executive Director, Housing Development Center

Bill Van Vliet, Executive Director, Network for Oregon Affordable Housing

Rob Prasch, Preservation Director, Network for Oregon Affordable Housing

Appendix B, attachment 1: List of technical engagement interviewees

Destin Ferdun, Director of Development, Northwest Housing Alternatives (NHA)

Trell Anderson, Executive Director, Northwest Housing Alternatives

Jocelyn Beh, Project Turnkey Coordinator, Oregon Community Foundation

Megan Loeb, Senior Program Officer, Oregon Community Foundation

Keeble Giscombe, Homeownership Division Director, Oregon Housing and Community Services (OHCS)

Matt Rosen, Homeownership Division Planning and Policy Analyst, Oregon Housing and Community Services (OHCS)

Michael Parkhurst, Policy and Initiatives Manager, Oregon Housing and Community Services

Natasha Detweiler-Daby, Director Affordable Rental Housing Division, Oregon Housing and Community Services

Scott Shaw, Assistant Director of Homeownership Lending, Oregon Housing and Community Services (OHCS)

Andy Miller, Executive Director, Our Just Future

John Warner, Consultant, Petros Partners

Kymberly Horner, Executive Director, Portland Community Reinvestment Initiative

Tom Cody, President and CEO, Project PDX

Dom Merriweather, Executive Director, Proud Ground

Kathleen Mertz, Director of Housing Development, REACH CDC

Stefanie Kondor, Senior VP of Development, Related Northwest

Ryan Hood, Vice President of Development, Related Northwest

Alec Lawrence, Project Manager, Related Northwest

Michael Anderson, Senior Researcher, Sightline Institute

Julia Metz, Housing Fellow, Sightline Institute

Anna Mackay, Founder and Principal, Sister City

Matt Tschabold, Housing and Homeless Initiatives Director, State of Oregon Governor's Office

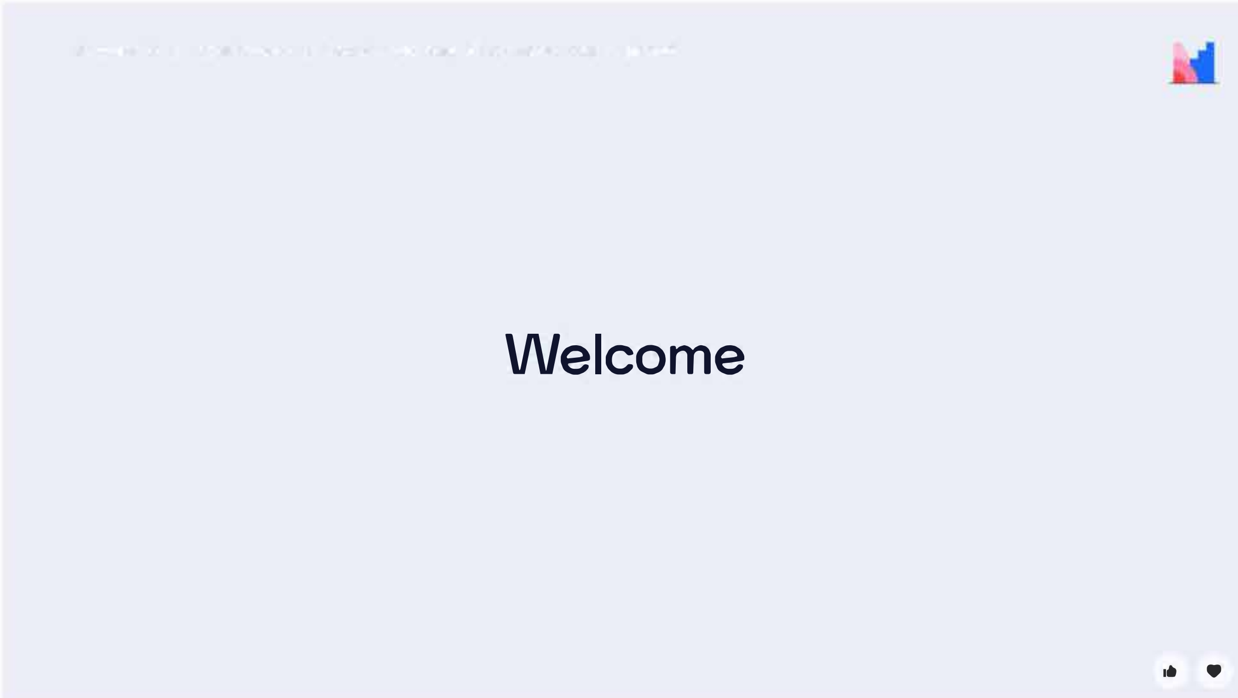
Ann Melone, Senior Vice President & Business Development Officer, US Bank

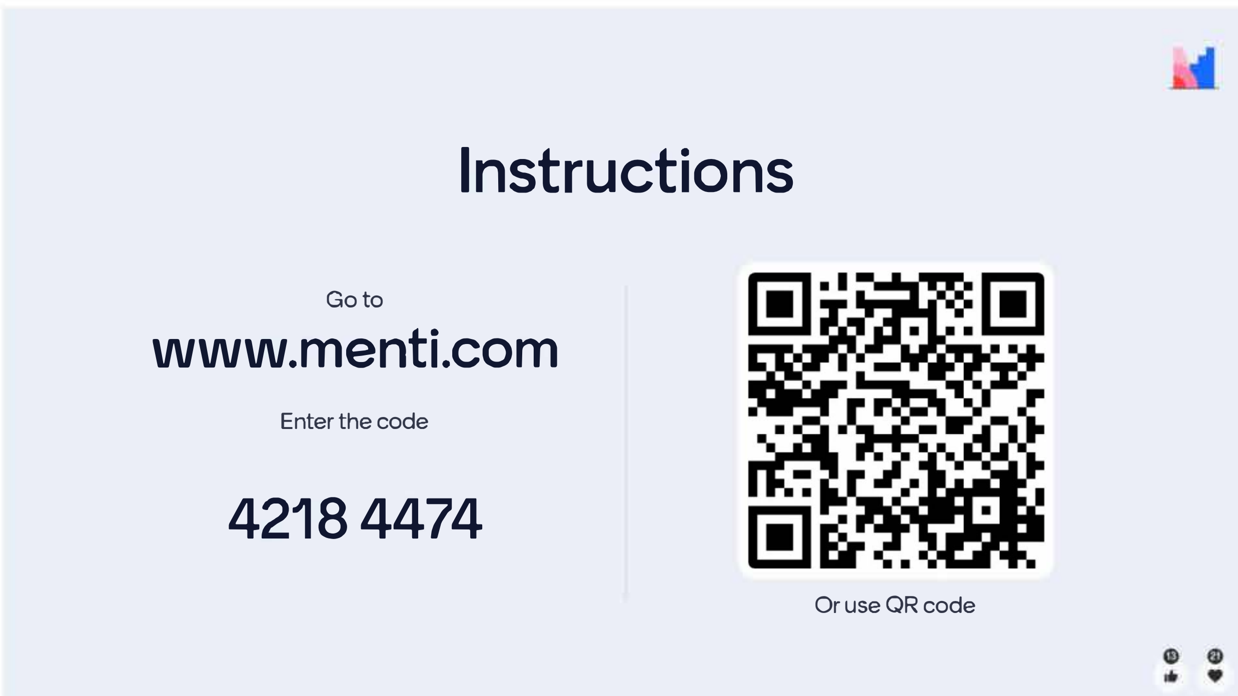
Andrew Crampton, Development Manager, Washington County Department of Housing Services

Jill Chen, Assistant Director, Washington County Department of Housing Services

Metro would also like to thank those who participated in and observed the Metro, Housing Oregon, and Housing Development Center co-convened Operating Cost Discussion and follow up survey, which have improved our regional understanding of current and emerging operating cost drivers, impacts, and possible solutions. Special thanks to Kevin Cronin, Policy and Advocacy Director, Housing Oregon and Liz Winchester, Senior Asset Manager, Housing Development Center for their continued advocacy, collaboration, and support of the affordable housing industry and their assistance in convening this productive conversation.

Appendix B, attachment 2: Operating cost discussion result detail





Appendix B, attachment 2: Operating cost discussion result detail

WELCOME

Who is joining us today?

Kevin Cronin, he/him, Housing Oregon Policy and Advocacy Director	TJ Norton (he/him), Asset Manager, Home Forward	Travis Phillips (he/him), Housing Development Center	Michael Parkhurst (he/him), Policy & Initiatives Manager, OHCS
Reese Neufeld (she/her), Asset Manager, Central City Concern	Christina Dirks, she/her, Director of Policy and Planning at Home Forward	Lydia Slocum (she/her), Senior Housing Developer and Policy Coordinator, Northwest Housing Alternatives	Chris Copland, he/him, Housing Retention & Stabilization Program Manager - JOIN

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WELCOME

Who is joining us today?

sean hubert, central city concern, he/him	Janelle Kent, she/her, Vice President of Finance at New Narrative	Heather Hebert, Sr Asset ManagerHacienda CDC	Tony HE/Him, Our Streets
Will Allen, he/him, new narrative, vp of operations	Michelle Martin, CFOCornerstone Community Housing	Jake Kirsch (he/him), HDC, Asset Management Project Manager	Gena Scott, PHB Risk Analysis & Compliance Manager

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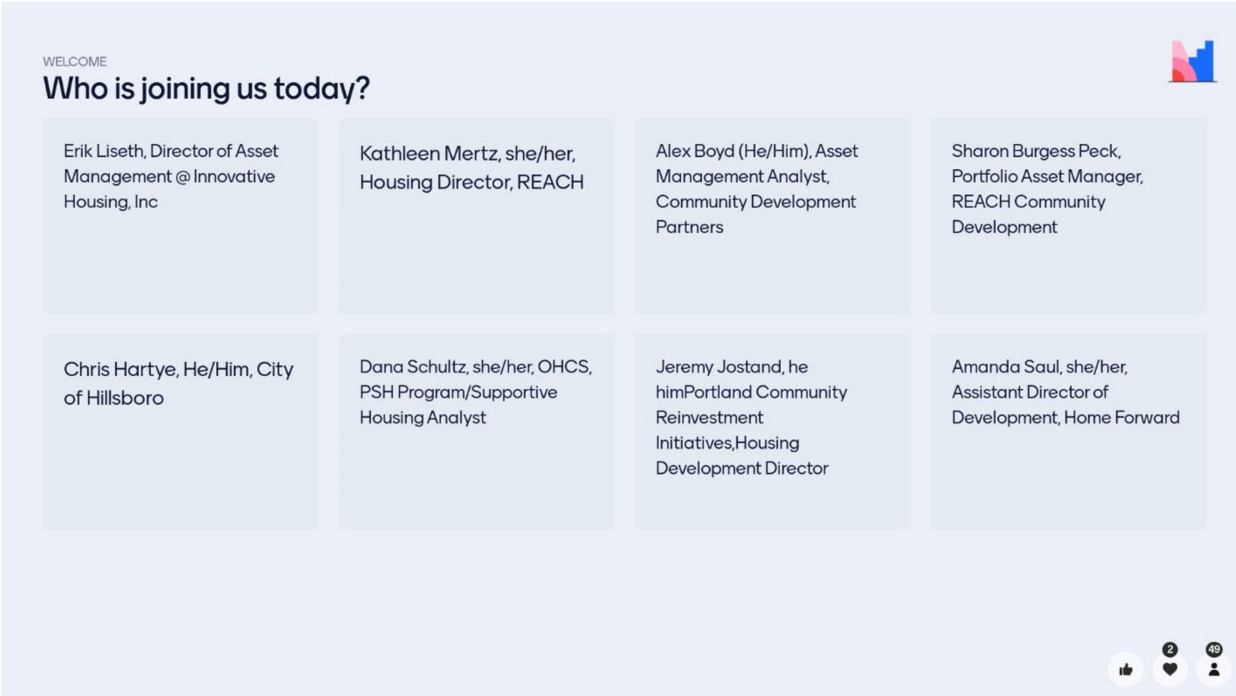
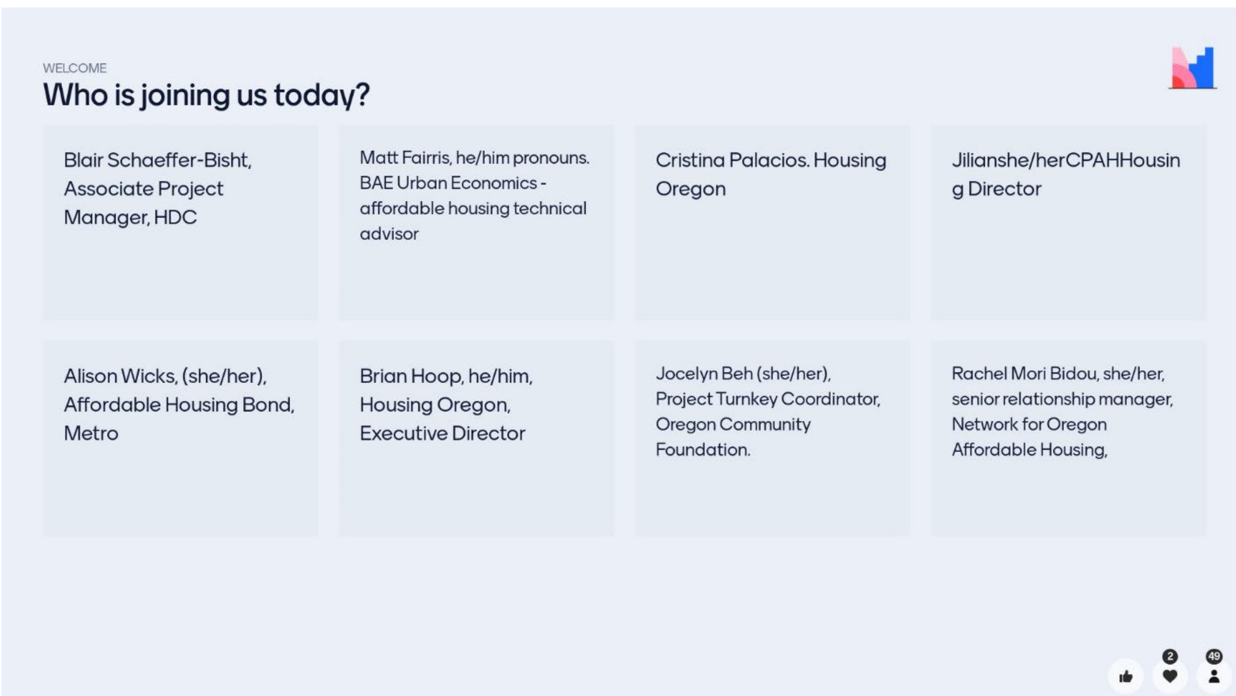
Appendix B, attachment 2: Operating cost discussion result detail





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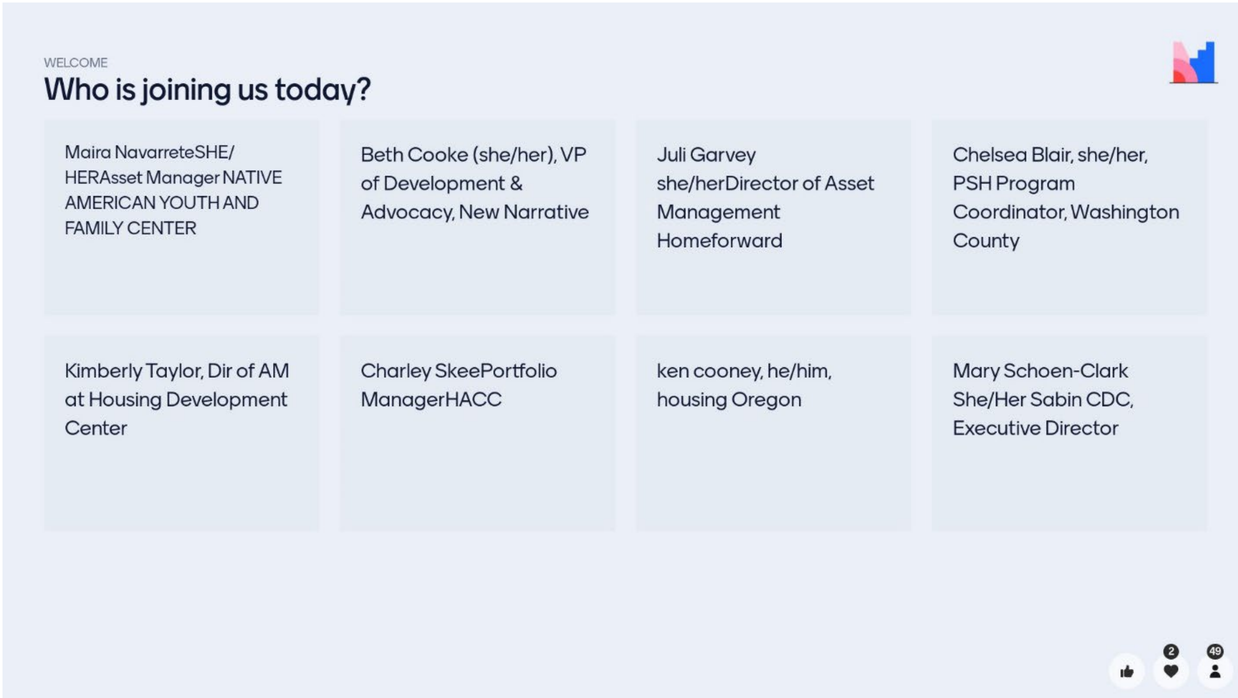

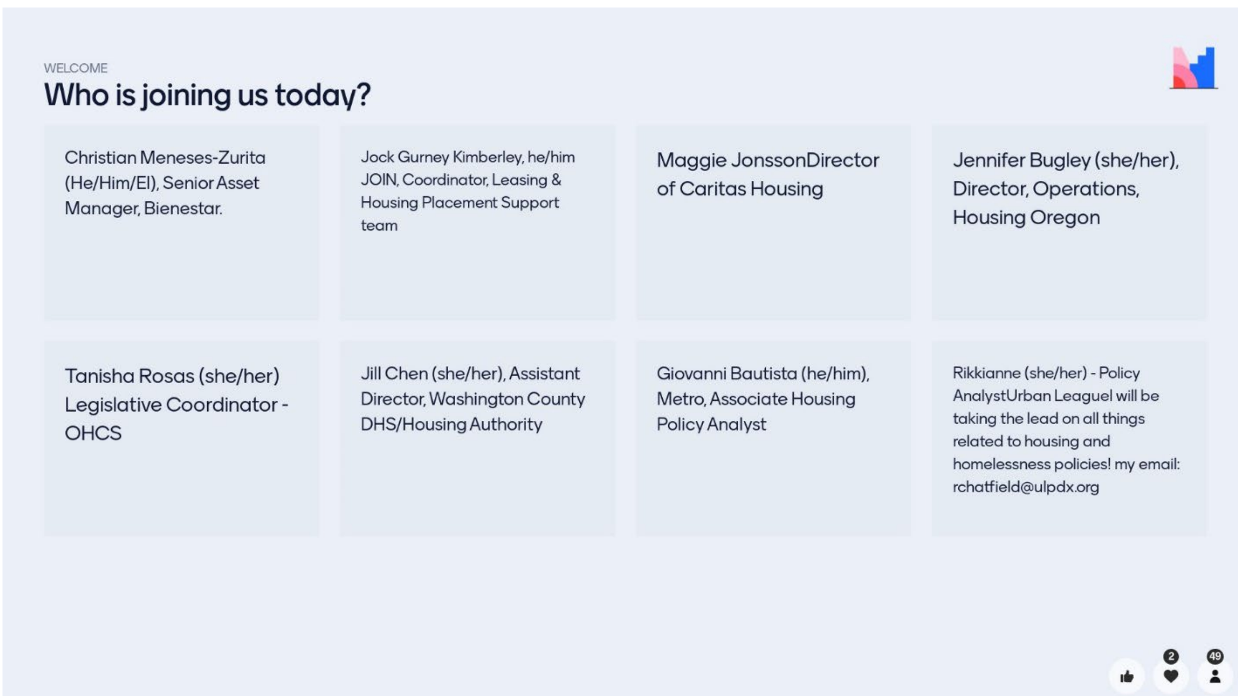

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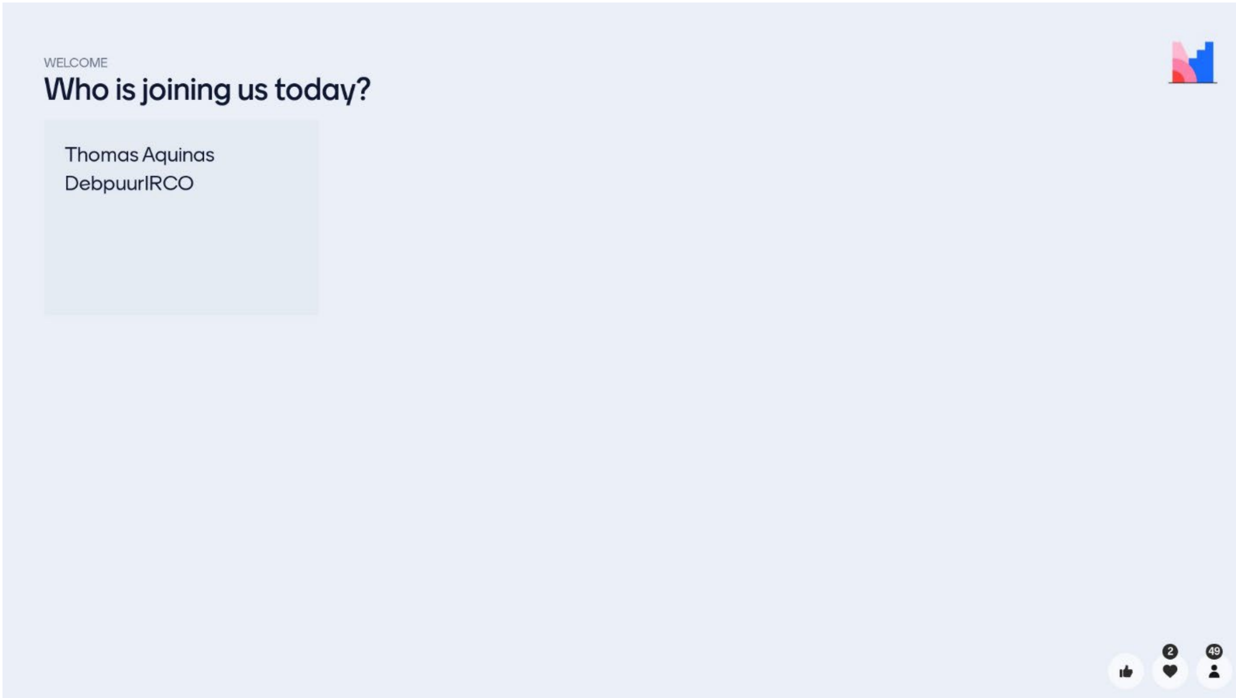

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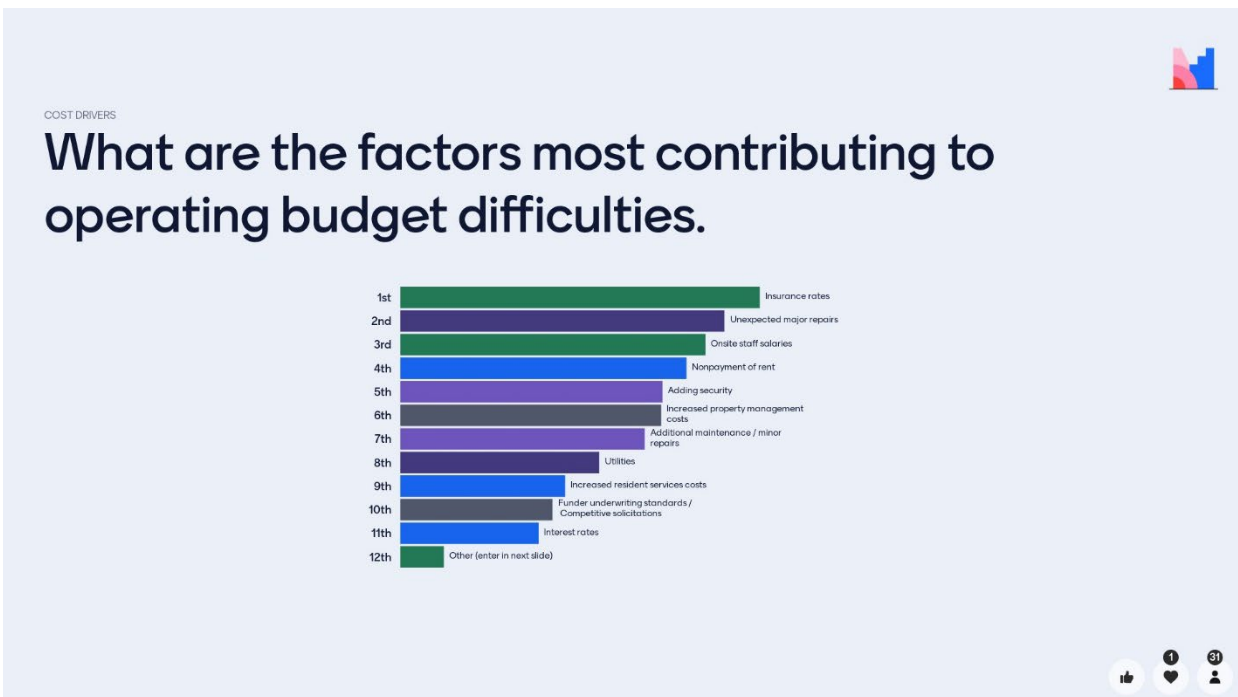

Appendix B, attachment 2: Operating cost discussion result detail

COST DRIVERS

Please tell us more about operating cost challenges your organization is experiencing. What other factors are most driving changes in operating costs?

Increased vacancy, which is tied to not being able to hire property management staff etc.	Units operating as "de facto" PSH, but serving residents with PSH needs.	vacancies and non-payment of rent or inconsistent payment of rent	Staff turnover
Vacancy. Long leasing times due to overlapping screening/ referral processes; and limited applicants within narrow income bands.	Vacancy lossResident acuity (PSH populations in non-PSH buildings)Staff turnover	Frequent turnover of PM agencies and AM staff which causes gaps in service and oversight.	lowercase "PSH"

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COST DRIVERS

Please tell us more about operating cost challenges your organization is experiencing. What other factors are most driving changes in operating costs?

High vacancy/low occupancy; High A/R;Staff turnover	Staff turnover and inexperienced staff	For us the turnover timeline for any voucher based unit in multco is minimum 3 weeks simply due to the voucher application process. Once you add on waitlist issues, getting past barriers, actually get	PSH provider turnover and serious capacity issues of service providers.
Staff turn over	Limited scope of existing risk mitigation funds	Vacancy, Staff turnover, small pool of management companies.	Required overtime popping normally eligible applicants into over income status

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Appendix B, attachment 2: Operating cost discussion result detail

COST DRIVERS

Please tell us more about operating cost challenges your organization is experiencing. What other factors are most driving changes in operating costs?

Expiring OAHTC's

Staff turnover and inability to hire

Turnover timeline for units is too long due to many factors

Occupancy, staffing challenges

Most insurance companies won't cover affordable housing in Portland, thus driving pricing up due to lack of competitive bids. We're supporting security costs from an ownership level vs pmt from sites.

working with specific wait lists such as N/NE Preference Policy

units operating as defacto PSH that do not have services funding or rent assistance. Not enough property management companies.staff turnover at PM and RSC.Vacancy.

Break-ins during unit turns, damaging construction progress

1 1 29

COST DRIVERS

Please tell us more about operating cost challenges your organization is experiencing. What other factors are most driving changes in operating costs?

staff turnover due to insufficient tenant supports that overwhelm site staff

High turnover costs, longer turn time,, software fees

Time to get people into units, damage levels, total revenue vs debt ratio allowed by under writing standards

Primary is repeated big expenses - fires, floods, heavy unit damage. Secondary is higher staff coverage requirements

Higher needs populations coming without appropriate support. Property management is being asked to do more (ie delivery of services)

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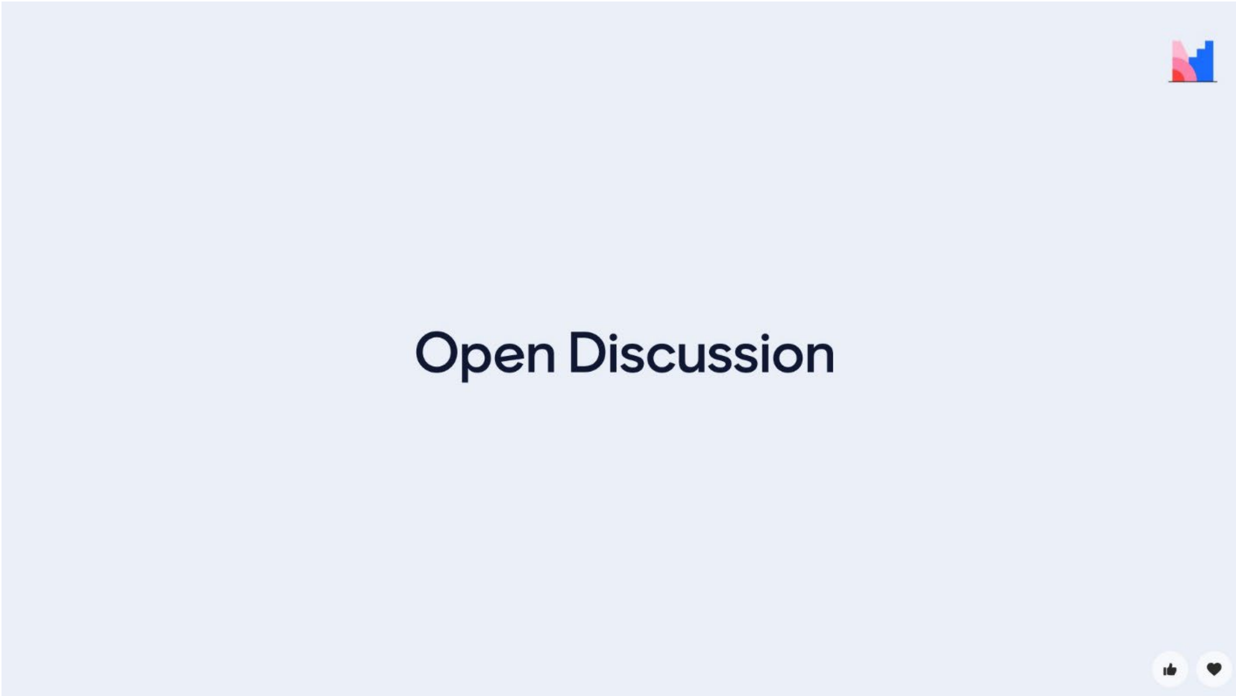

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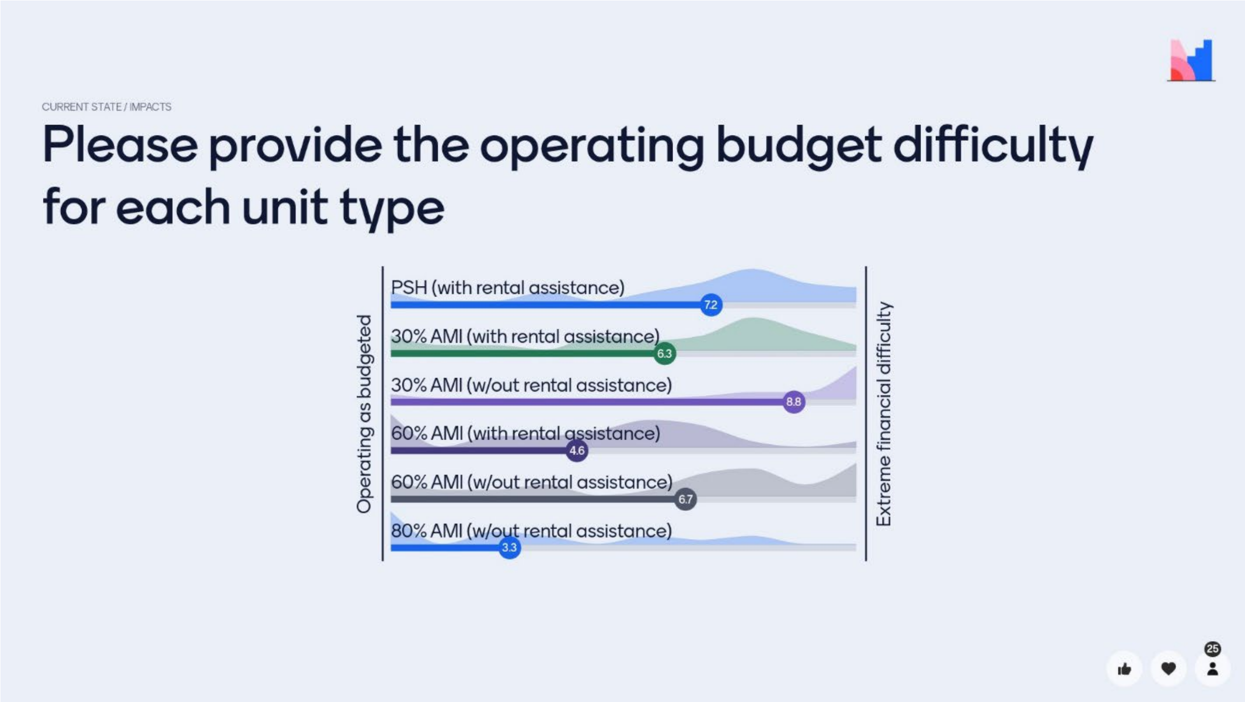

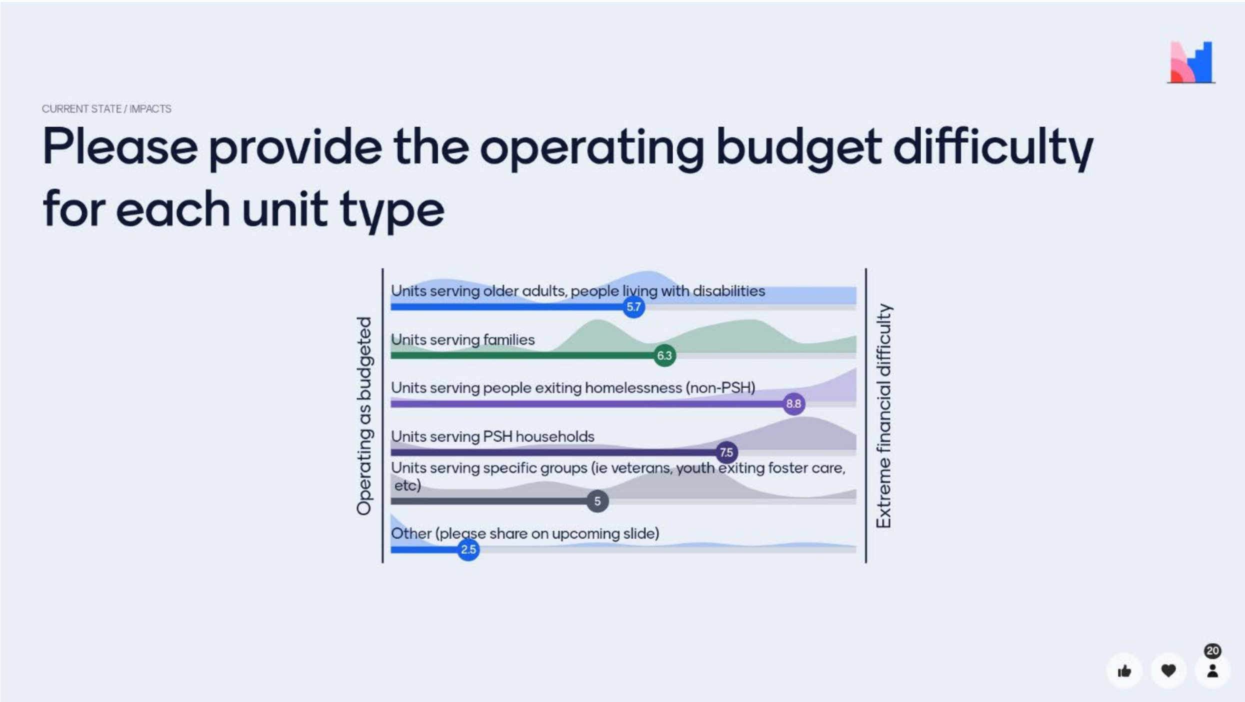

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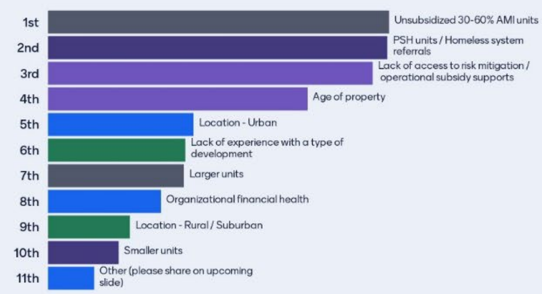
CURRENT STATE / IMPACTS

What are the factors that are most predictive of operating budget challenges?



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CURRENT STATE / IMPACTS

What unit types are experiencing the most signifcant operating cost related challenges?

shared rooms/SRO	Scattered sites that don't have economies of scale.	SRO	SRO
Developments serving a high density of 30-60% AMI units without onsite supports	SRO and small studios	larger familly can be hard on the building; SRO can be hard to fill	Scattered

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Appendix B, attachment 2: Operating cost discussion result detail

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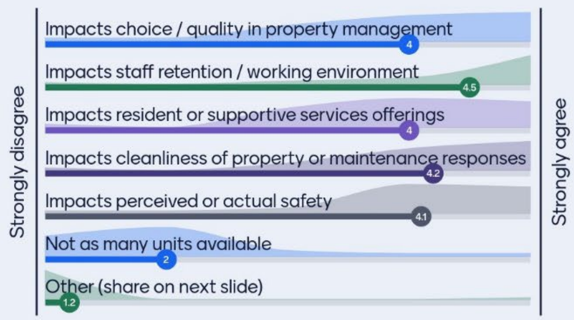
How do operating cost challenges most impact residents?



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CURRENT STATE / IMPACTS

How do operating cost challenges most impact residents?

Reduced quality of life

Overall decreased quality of life.

poor customer service from property management due to turnover/open positions

Staff turnover isn't just about workload, but also about availabiliity/predictability and relationships for residents

Stress! If PM staff are stressed out, then the whole property suffers

Degraded sense of community support and appreciation for residents.

Safety concerns from residents

Units staying vacant because the property can't pay for turn costs

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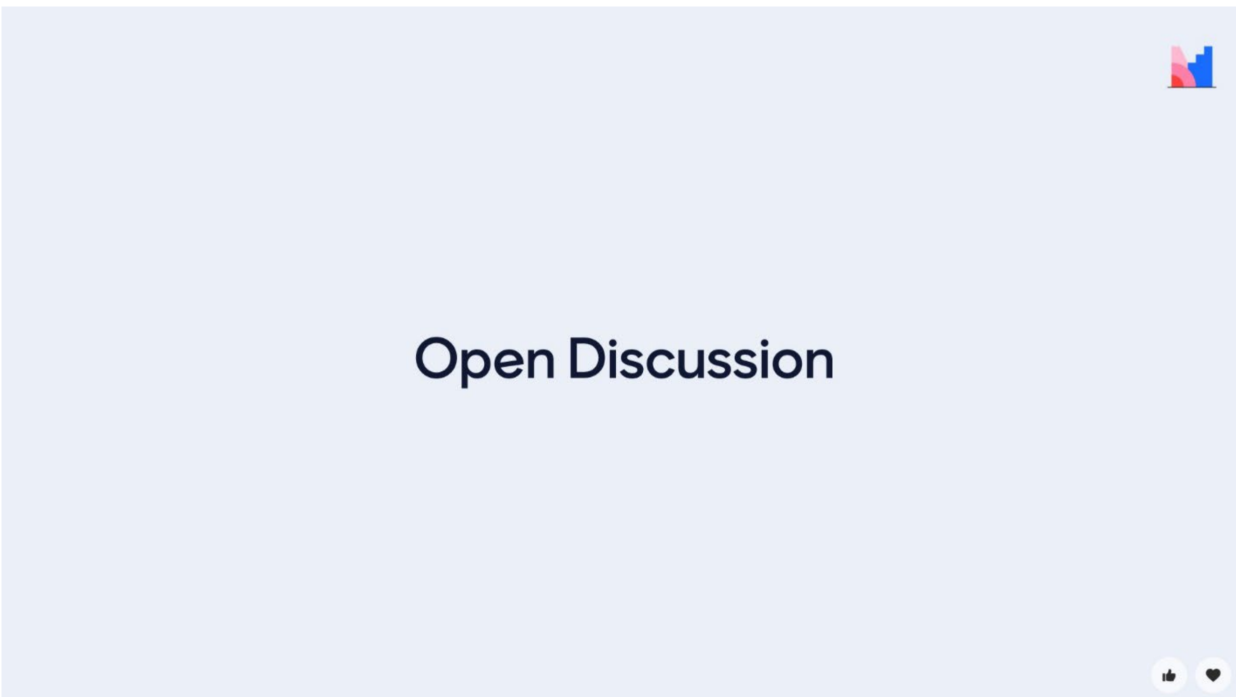
Appendix B, attachment 2: Operating cost discussion result detail



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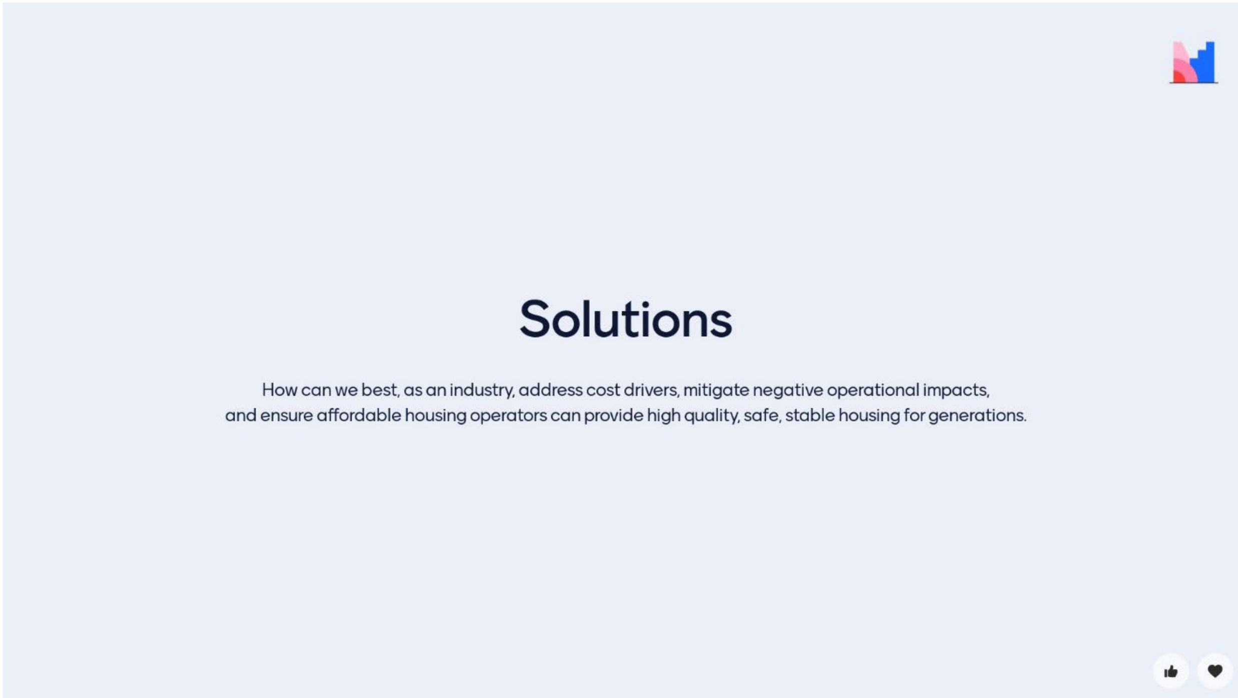

Appendix B, attachment 2: Operating cost discussion result detail

How are property developers responding to the current operating cost environment in planning new projects?

- Funders tie their hands as they need to meet a per unit cost that isn't realistic so they are moving more costs below the line such as resident services.
- Using more long-term rent assistance when available.
- Larger units sizes, multigenerational family housing, looking at new types of housing
- building better budgets with real time assumptions
- More conservative underwriting. More public subsidy per unit and less commercial debt
- Reducing / eliminating lowest income restrictions, which means we are not serving highest needs; pushing back on underwriting expectations when possible; maximize rent assistance; look at mixed income
- Trying to pay for damage out-of-pocket instead of submitting to insurance
- going rural

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How are property developers responding to the current operating cost environment in planning new projects?

- Raising insurance deductibles
- pushing back on lender underwriting
- Reql time budgets get slashed by investors near close.
- Sharing operating costs with developers and sitting down with developers to review material choices, appliance selection, space for programing in the design
- Trying to get contracts in place to provide supportive services.
- Close involvement with property management, debt restructure, better budgets/monitoring
- Maximizing developer fee and minimizing deferred fee - this is always the firs thing to get cut when there are problems

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Appendix B, attachment 2: Operating cost discussion result detail

Appendix B, attachment 2: Operating cost discussion result detail

How can funders best respond to the current operating cost environment in funding new projects?

- higher per unit subsidiesallow for better materials for longevity of the building
- On going operational subsidy for services.Larger risk mitigation pools to offset expenses not covered by insurance or due to high deductible.
- Be realistic about what asset management and resident services really cost
- Don't limit cash dev fees for non-profits.
- Reduce NOFA requirements (i.e. amount of PSH, etc.)
- No debt service for deeply affordable projects
- fully fund the cost of resident services including salary, fringe, supervision, and admin.
- Set a systems table - better connect behavioral health support

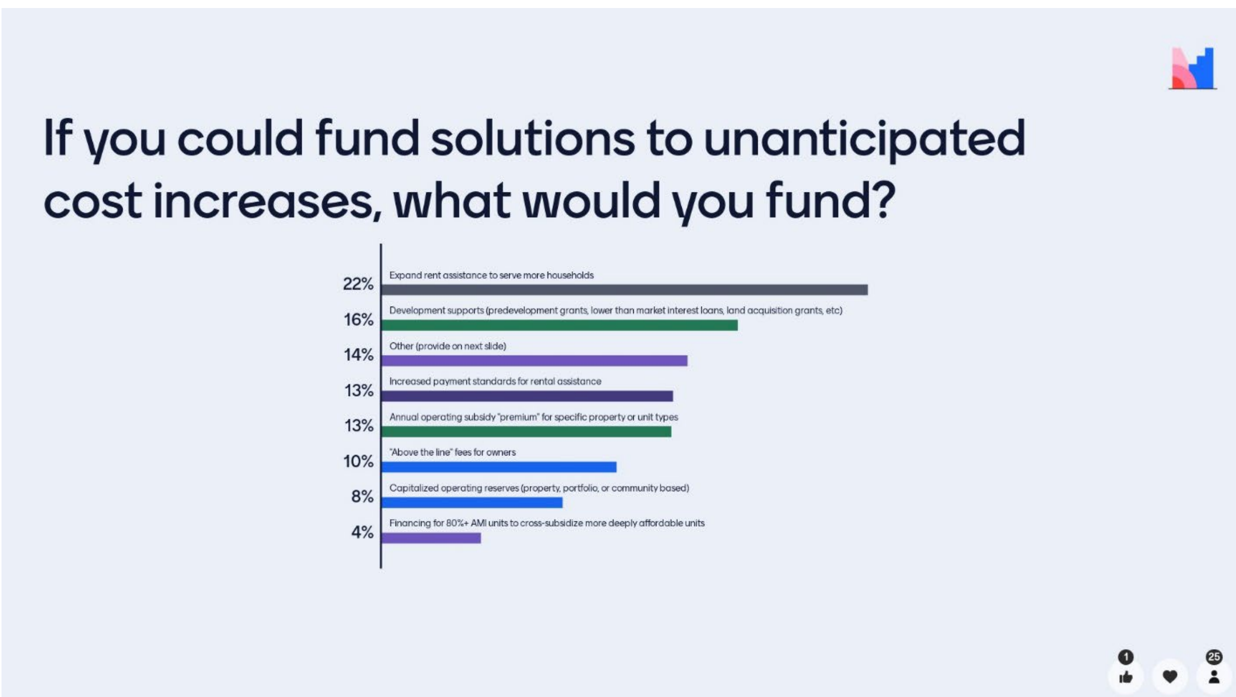
19

How can funders best respond to the current operating cost environment in funding new projects?

- More subsidy. Expand RMP to cover affordable housing not just PSH
- Materials matter!
- Minimize cash flow split requirements - allow these to remain in property
- Longer-term commitments from behavioral health funders. The annual contract renewals are exhausting, and sometimes there's a long delay before we get paid.
- funding assistance for security patrols
- vouchers for 30% ami units
- Prioritize making money for the nonprofit in both Dev Fee and cash flow. Without the nonprofit sponsor there is no project. We need money to keep the lights on, and are more
- Include PM and Resident Services providers in the design, budget for larger insurance

19

Appendix B, attachment 2: Operating cost discussion result detail

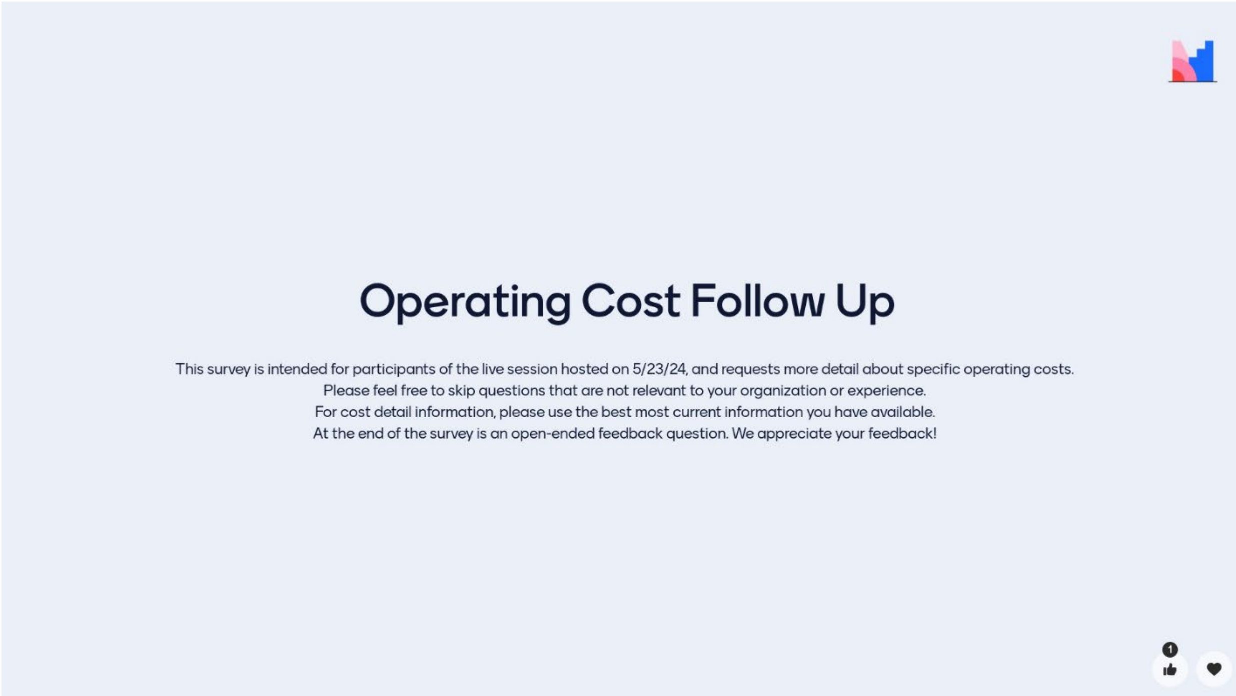


Appendix B, attachment 2: Operating cost discussion result detail

Open Discussion

What else? Is there anything else you'd like to share about the current operating cost environment, impacts, or support strategies?

Appendix B, attachment 2: Operating cost discussion result detail



Appendix B, attachment 2: Operating cost discussion result detail

Appendix B, attachment 2: Operating cost discussion result detail

How are resident services (excluding PSH supportive services) costs paid for your most recent developments?

3

How are resident services (excluding PSH supportive services) costs paid for your most recent developments?

Other - in most cases, we're having to hold resident services fees, because the properties can't pay them through regular operating cash. So, they sit as an accrued AP item month after month.

Often tied to contracts with JOHS, County behavioral healthy, etc. Newer developments more likely to have tenant services agreements.

Also paid by developer fees or other organizational resources (MTW flexible funds).

3

Appendix B, attachment 2: Operating cost discussion result detail

What are typical per unit resident services costs, and how are these impacted by differences in regulated unit income levels?

We typically start out between 450-650/unit. As mentioned in previous slide we can't pay Resident Service Fees. Also, we haven't been able to achieve the max rent, because for most, rent is too high.

Depends on the property. Some just have an RSC on staff, some have tenant service agreements that cover a range of positions.

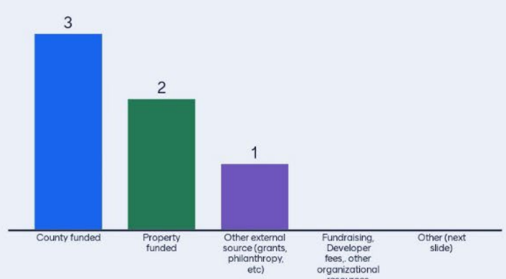
Resident services costs range greatly depending on underwriting crunches. It's an unfunded mandate that is so important but is often the first to get cut when you can't cut property management, audits

, insurance, utility costs or other expenses that are absolutely required to operating a project. In a perfect world resident services would increase as income levels decrease, but that is often not

the case. Our last 3 projects have resident services ranging from $521 - $824/PUPY. We are hearing from our community services department that this is not enough.

3

How are PSH supportive services (excluding resident services) costs paid for your most recent developments?



3

Appendix B, attachment 2: Operating cost discussion result detail

How are PSH supportive services (excluding resident services) costs paid for your most recent developments?

JOHS, County behavioral health, and the property itself when there are shortfalls in funding. We often elect not to pay ourselves when there isn't enough funding, which is a problem.

1

Have you experienced any differences in underwriting and/or per unit operations costs for PSH? What are they?

To me, there is no difference in operating costs with PSH or non-PSH. Affordable housing operating costs are high no matter the population, specifically in Portland. Insurance rates reflect this, too.

Yes, funders not ready to recognize how incredibly expensive PSH is to operate. Also, acuity of residents has increased, so even we haven't been prepared for the reality of it.

Yes, our PSH projects tend to have higher staffing costs for 24-hour desk coverage, other property management staff, insurance, janitorial, maintenance and repairs.

3

Appendix B, attachment 2: Operating cost discussion result detail

What are current typical annual PSH supportive services costs per households?

9,000/unit or more, trending more with non-PSH or PSH

Hard to say because costs are spread between housing and supportive housing departments. We do have tenant service agreements going up to $2,900 PUPY for properties with heavy supportive component.

Supportive services costs have been based on what funders will pay, not what is needed. On a current project that requires 24-hour staffing, our SS costs are estimated to be $24,000/year/household.

3

COST DRIVERS

Please tell us more about operating cost challenges your organization is experiencing. What other factors are most driving changes in operating costs?

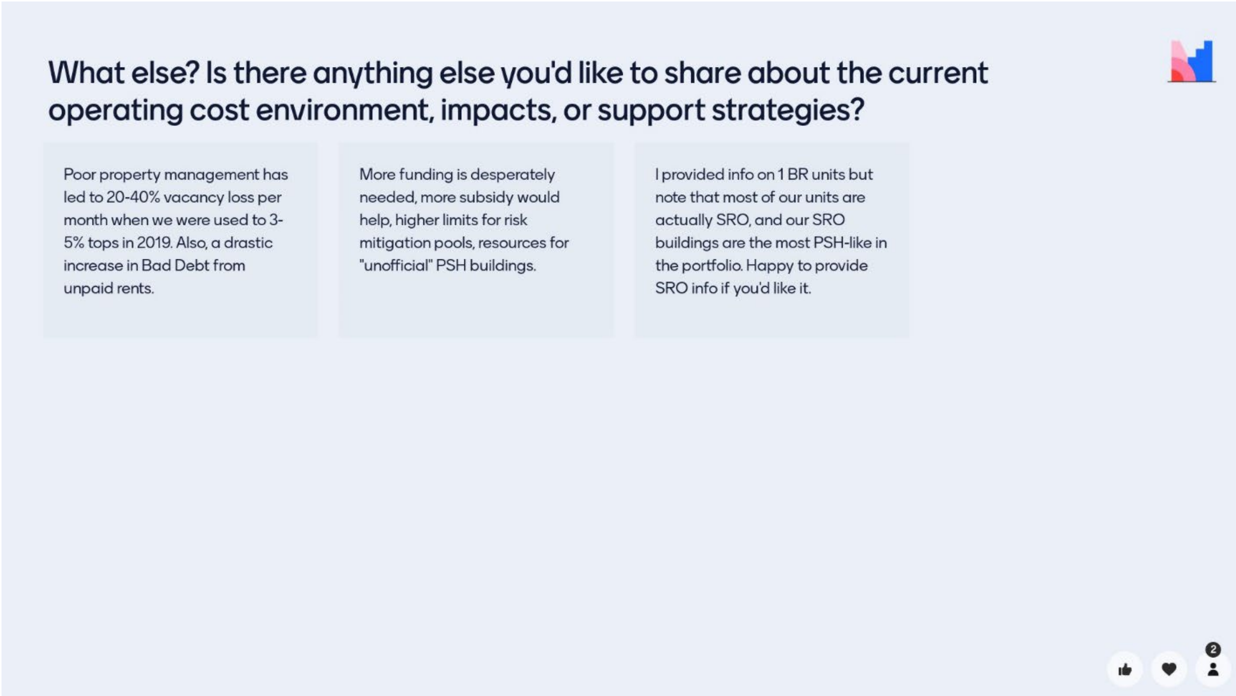
Portland downtown and anywhere within city limits. Insurance, security patrols, lack of good/reliable management companies, not able to realize max rents at 60% or below, because amounts too high.

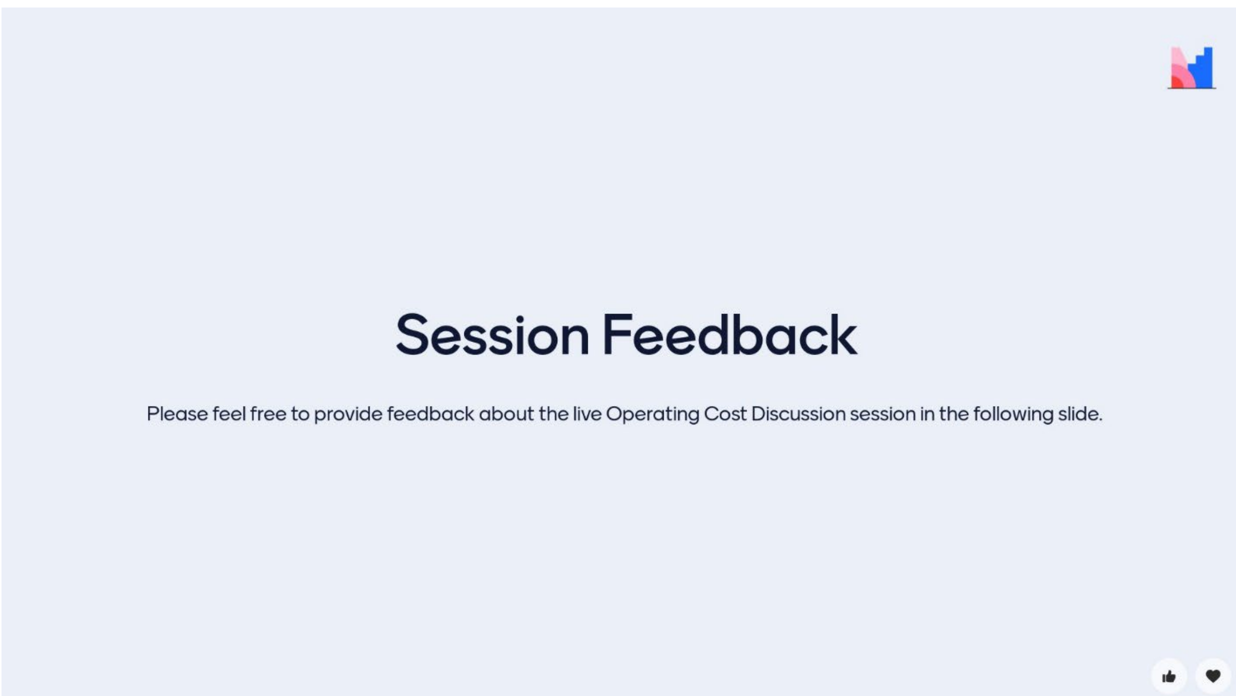
"Workforce" properties that turn out to be PSH but don't have funding, increasingly expensive unit turns (resident damage/housekeeping), security and staffing costs, insurance, self-insured losses

Staffing costs, increased need for security, and insurance are the main cost drivers.

3

Appendix B, attachment 2: Operating cost discussion result detail





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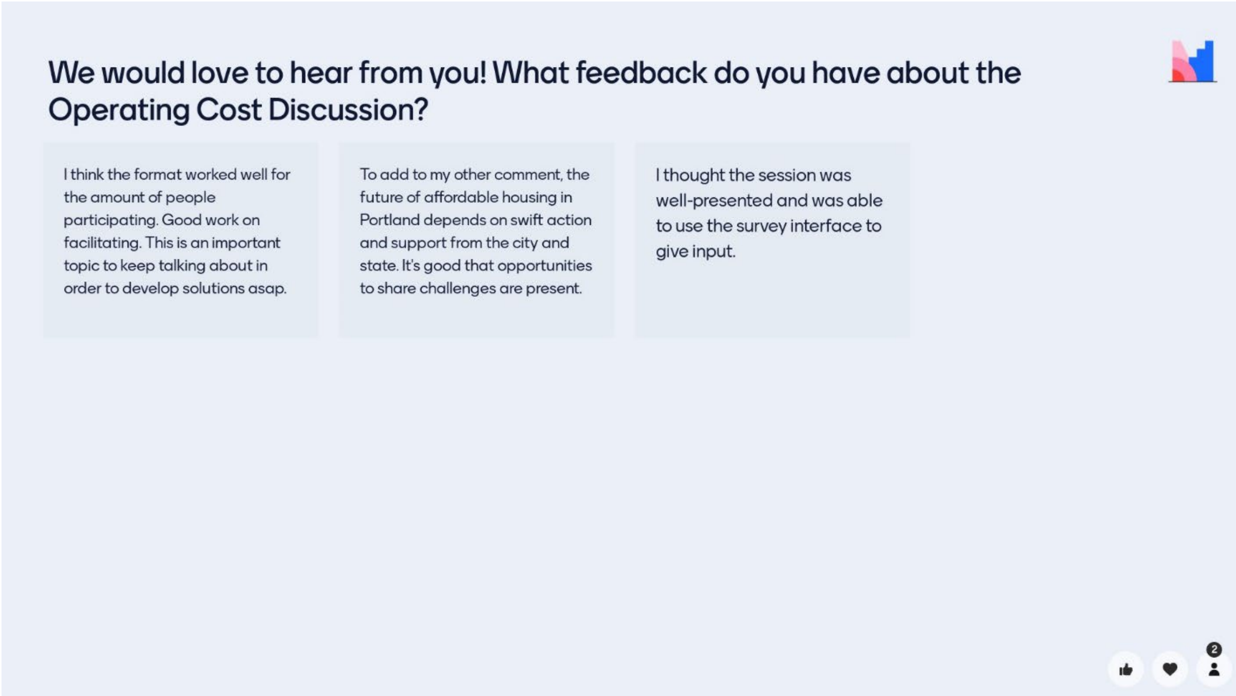
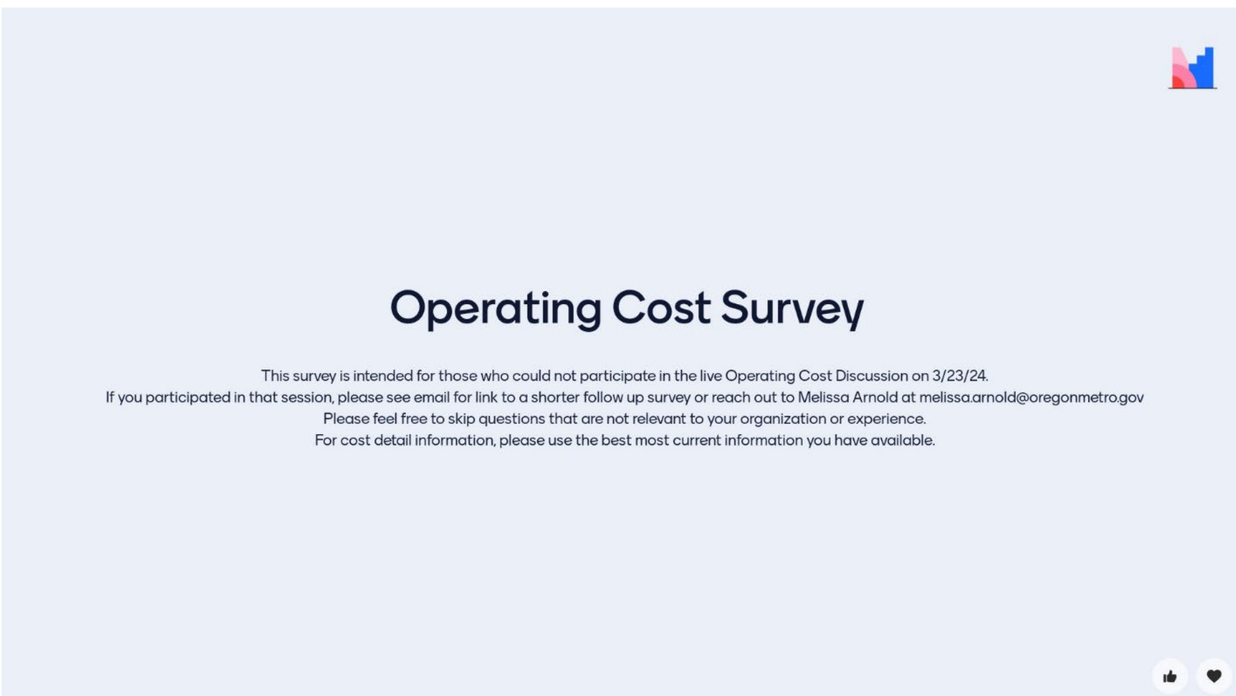




Appendix B, attachment 2: Operating cost discussion result detail

Costs and Cost Drivers

Current Costs and factors impacting rising and/or unplanned for costs in affordable housing

What are current typical annual property operating expenses per unit for a 1 bdrm unit (not including resident or supportive services)?

$6,450

$7,814/unit/year (data not split out by bedroom type)

2

Appendix B, attachment 2: Operating cost discussion result detail

Appendix B, attachment 2: Operating cost discussion result detail

How are resident services (excluding PSH supportive services) costs paid for your most recent developments?

How are resident services (excluding PSH supportive services) costs paid for your most recent developments?

Through operations and from grant support we raise separately

Most Resident Services budgets are paid from Property Operations. Considering the heightened needs of most families, RS has been perceived as under-funded. Property unable to support more load.

While PSH projects are able to apply for and receive solid RS funding, non-PSH projects are seeing similar tenant behavior issues (esp those at 50% AMI or less) & are having to bear the weight in Ops.

Appendix B, attachment 2: Operating cost discussion result detail

What are typical per unit resident services costs, and how are these impacted by differences in regulated unit income levels?

$612/unit/year. However only $176 is calculated in the operating budget because of the restrictions on rents. Adds much more work to have to raise that additional capital.

Portfolio RS costs in 2024 are estimated to be $700 / unit (for non-PSH properties). We have tried to establish RS Reserves from Dev Fees for our partners where possible but that is not sustainable.

The inability to increase rents to max due to rent burden concerns creates a continued cycle of expense inflation overtaking income achievement and constantly places the project in jeopardy.

The Resident Services, even for non-PSH projects, continues to be an essential operating service needed to stabilize households.

2

How are PSH supportive services (excluding resident services) costs paid for your most recent developments?

2

Appendix B, attachment 2: Operating cost discussion result detail

How are PSH supportive services (excluding resident services) costs paid for your most recent developments?

Through fundraising

Most are through state or local PSH contracts. These are better funded than other mechanisms (e.g. COC funds, etc); however, we have noted that $10k PUPY is not enough to cover operating expenses

related to PSH households. Most PSH projects are being underwritten at needing $15-18k PUPY to cover 24/7 staffing, janitorial, maintenance, increased mgt fees, security, etc.

2

Have you experienced any differences in underwriting and/or per unit operations costs for PSH? What are they?

Typically expenses raise higher than the allowable inflation in your proformas, thus when the rents cannot cover those, the project goes into the red.

Yes - non-PSH projects in portfolio operate at ~$7,500 PUPY (or less).Integrated PSH projects (where PSH is less than 20% of project makeup) operate at $8,500 PUPY or less

PSH projects operate anywhere from $9,500-12,000 PUPY depending on scale, location, site design and service/mgt partners

2

Appendix B, attachment 2: Operating cost discussion result detail

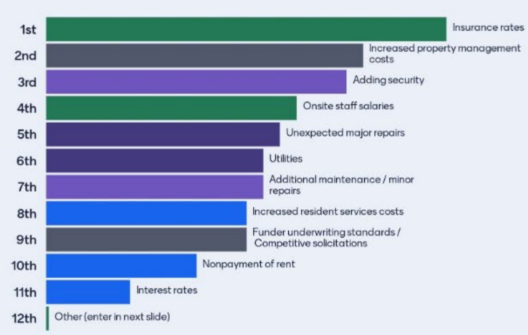
What are current typical annual PSH supportive services costs per households?

$400 per unit per year

Averaging $15,000 PUPY when including 24/7 staffing, increased mgt fee load from PSH, increased unit turnover / R&M expectations, and capital needs.

COST DRIVERS

What are the factors most contributing to operating budget difficulties.



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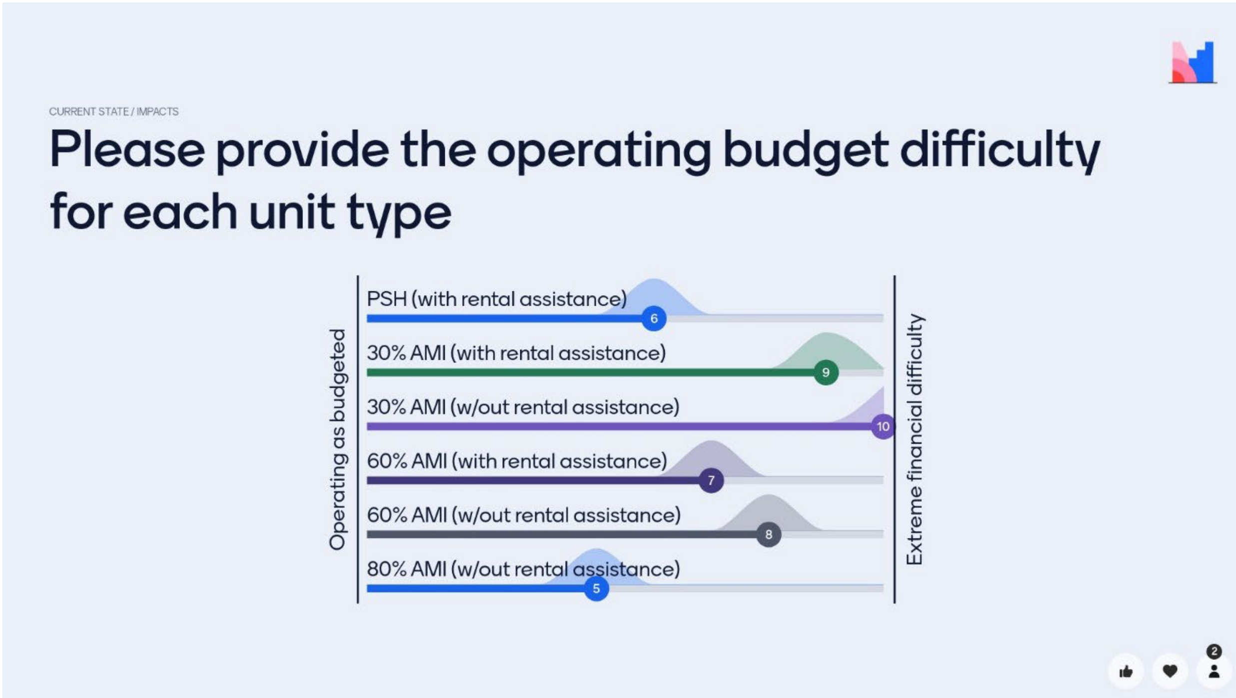
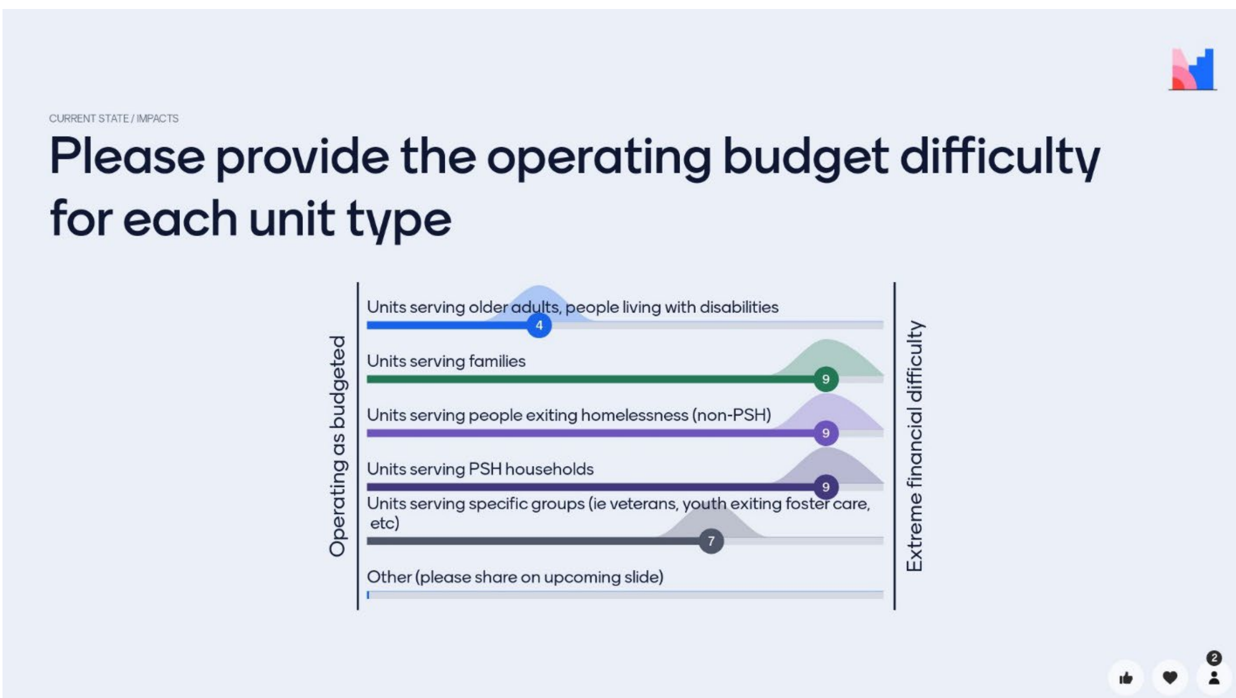
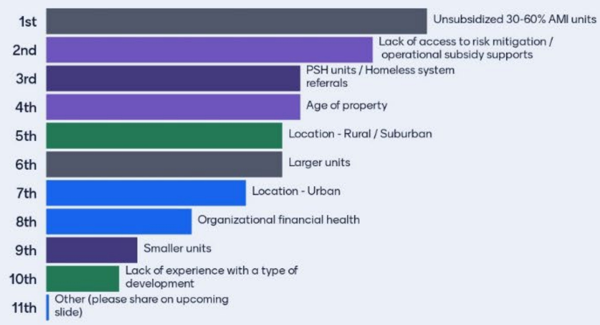




Appendix B, attachment 2: Operating cost discussion result detail

CURRENT STATE / IMPACTS

What are the factors that are most predictive of operating budget challenges?



2

CURRENT STATE / IMPACTS

What unit types are experiencing the most signifcant operating cost related challenges?

Larger units have more people so the wear and tear on the unit is greater.

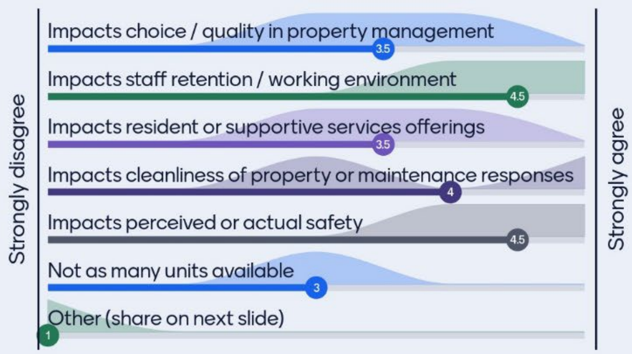
Unsubsidized or under-subsidized (e.g. PBV units only achieving 60% AMI rather than 100-110% FMR) units. Income from these units unable to cover most operating costs in this inflated environment,

Insurance - carriers charging premium for PSH or integrated PSH sitesSecurity - underfunded police depts mean need for private security of some kind.

2

Appendix B, attachment 2: Operating cost discussion result detail

How do operating cost challenges most impact residents?



CURRENT STATE / IMPACTS

How do operating cost challenges most impact residents?

Impacts staffing retention -- if they perceive issues in getting expenses approved and work done, work won't be done and frustration to occurImpacts R&M -- lengthens timeline to turn spaces if expens

if external vendor is engaged, expenses are typically higher. Unit turnover tends to be a bigger challenge in this market environment and turns have been noted as heavier and costlier than pre-Covid.

Appendix B, attachment 2: Operating cost discussion result detail

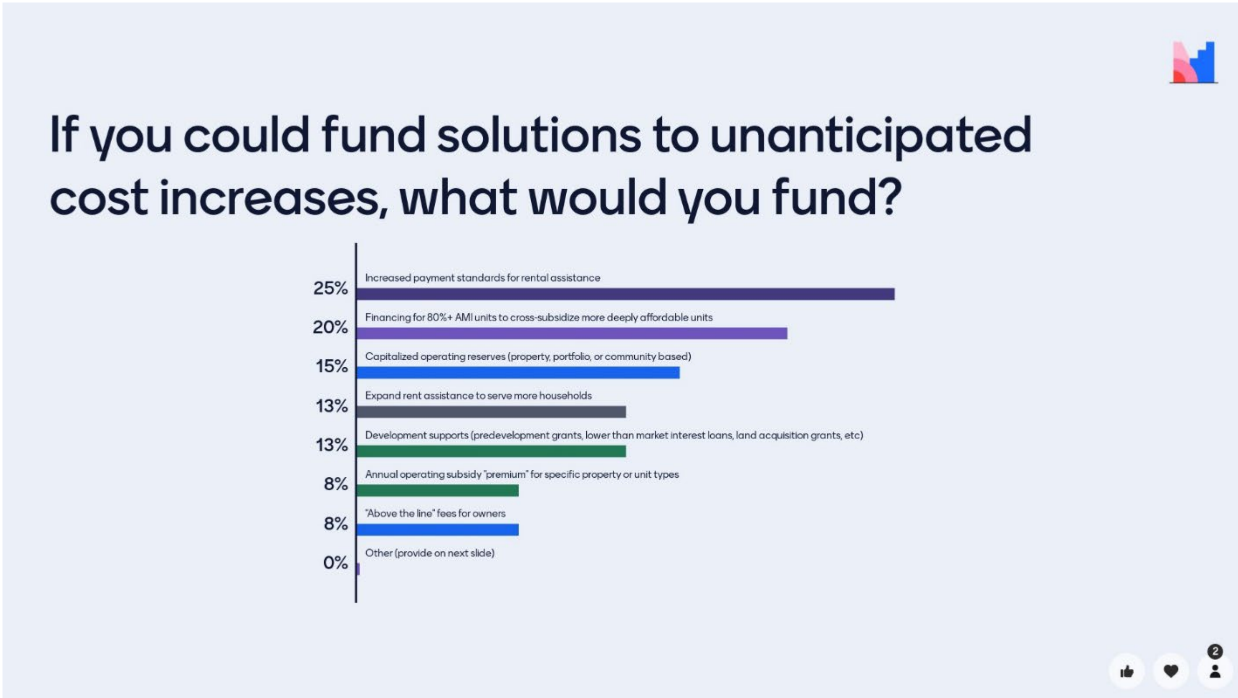
Solutions

How can we best, as an industry, address cost drivers, mitigate negative operational impacts, and ensure affordable housing operators can provide high quality, safe, stable housing for generations.

How are property developers responding to the current operating cost environment in planning new projects?

- Being more realistic and advocating for change so that our stock of afford hsg does not go belly up.
- Seeking funding sources post-conversion to fund Resident Services and additional capital improvements for community benefit
- Forced to increase rents above 5% in response to the expense environment.

Appendix B, attachment 2: Operating cost discussion result detail



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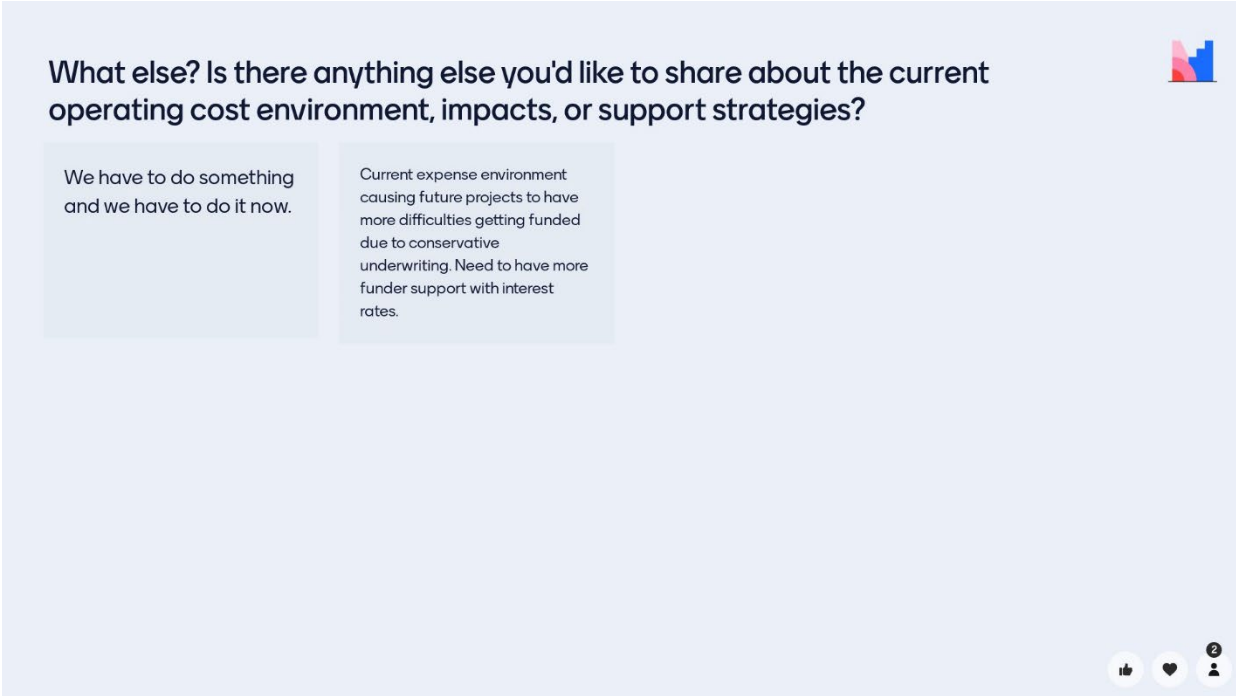


Appendix B, attachment 3: HDC portfolio analysis data

Location	Number of units	Operating Expenses*	OpEx PUPY
Aloha, OR	40	359,363	8,984
Aloha, OR	6	52,324	8,721
Aloha, OR	78	449,385	5,761
Beaverton, OR	20	202,553	10,128
Canby, OR	50	285,539	5,711
Canby, OR	51	338,255	6,632
Fairview, OR	328	2,425,451	7,395
Forest Grove, OR	40	271,482	6,787
Forest Grove, OR	36	311,631	8,656
Forest Grove, OR	17	96,283	5,664
Gresham, OR	20	151,801	7,590
Gresham, OR	46	644,445	14,010
Gresham, OR	36	185,879	5,163
Gresham, OR	195	2,492,185	12,780
Gresham, OR	18	133,207	7,400
Gresham, OR	72	372,861	5,179
Gresham, OR	208	2,489,763	11,970
Hillsboro, OR	138	919,610	6,664
Milwaukie, OR	8	55,595	6,949
Milwaukie, OR	52	555,928	10,691
Molalla, OR	24	212,215	8,842
Newberg, OR	24	170,391	7,100
Newberg, OR	15	128,859	8,591
Newell, OR	32	321,340	10,042
North Plains, OR	12	85,699	7,142
Oregon City, OR	19	178,141	9,376
Oregon City, OR	15	157,977	10,532
Portland, OR	88	823,917	9,363
Portland, OR	40	457,880	11,447
Portland, OR	21	245,927	11,711
Portland, OR	130	2,492,896	19,176
Portland, OR	67	599,618	8,950
Portland, OR	27	244,603	9,059
Portland, OR	129	1,206,914	9,356
Portland, OR	152	1,191,188	7,837
Portland, OR	105	792,103	7,544
Portland, OR	12	111,864	9,322
Portland, OR	80	952,600	11,908
Portland, OR	181	1,429,749	7,899
Portland, OR	44	455,076	10,343
Portland, OR	199	2,376,731	11,943
Portland, OR	93	745,599	8,017
Portland, OR	76	910,980	11,987
Portland, OR	132	844,250	6,396
Portland, OR	24	320,428	13,351
Portland, OR	62	495,331	7,989

Appendix B, attachment 3: HDC portfolio analysis data

Portland, OR	80	815,817	10,198
Portland, OR	158	1,131,476	7,161
Portland, OR	32	557,244	17,414
Portland, OR	18	112,212	6,234
Portland, OR	8	81,352	10,169
Portland, OR	160	1,815,546	11,347
Portland, OR	44	364,702	8,289
Portland, OR	14	152,040	10,860
Portland, OR	18	158,678	8,815
Portland, OR	43	425,116	9,886
Portland, OR	56	445,162	7,949
Portland, OR	42	282,519	6,727
Portland, OR	88	615,144	6,990
Portland, OR	6	62,194	10,366
Portland, OR	100	890,140	8,901
Portland, OR	28	303,870	10,853
Portland, OR	71	535,245	7,539
Portland, OR	26	190,876	7,341
Portland, OR	38	410,762	10,810
Portland, OR	73	535,853	7,340
Portland, OR	106	742,728	7,007
Portland, OR	95	848,016	8,926
Portland, OR	62	757,716	12,221
Portland, OR	36	383,772	10,660
Portland, OR	24	214,594	8,941
Portland, OR	62	568,986	9,177
Portland, OR	44	413,396	9,395
Portland, OR	180	1,518,444	8,436
Portland, OR	76	754,496	9,928
Portland, OR	40	318,536	7,963
Portland, OR	99	819,473	8,278
Portland, OR	47	412,845	8,784
Portland, OR	60	507,312	8,455
Portland, OR	194	1,336,230	6,888
Portland, OR	132	890,729	6,748
Portland, OR	49	292,811	5,976
Portland, OR	153	1,273,333	8,322
Portland, OR	51	325,553	6,383
Portland, OR	124	820,839	6,620
Portland, OR	172	1,196,053	6,954
Portland, OR	60	575,099	9,585
Portland, OR	47	393,932	8,382
Portland, OR	315	3,001,311	9,528
Portland, OR	75	630,304	8,404
Portland, OR	144	1,521,219	10,564
Portland, OR	95	641,223	6,750
Portland, OR	60	515,093	8,585

Appendix B, attachment 3: HDC portfolio analysis data

Portland, OR	130	1,609,897	12,384
Portland, OR	108	1,036,463	9,597
Portland, OR	240	2,159,728	8,999
Portland, OR	131	1,486,747	11,349
Portland, OR	250	2,805,826	11,223
Portland, OR	131	1,395,763	10,655
Portland, OR	350	2,981,541	8,519
Portland, OR	101	971,148	9,615
Portland, OR	75	893,299	11,911
Portland, OR	47	668,650	14,227
Portland, OR	140	1,687,474	12,053
Portland, OR	259	2,544,459	9,824
Portland, OR	396	4,027,265	10,170
Portland, OR	24	270,619	11,276
Portland, OR	28	353,943	12,641
Portland, OR	10	82,097	8,210
Portland, OR	18	201,429	11,191
Portland, OR	80	645,799	8,072
Portland, OR	20	167,871	8,394
Portland, OR	70	593,083	8,473
Portland, OR	73	640,912	8,780
Portland, OR	24	343,063	14,294
Portland, OR	31	301,495	9,726
Portland, OR	40	320,212	8,005
Portland, OR	14	112,203	8,015
Portland, OR	32	304,600	9,519
Portland, OR	19	189,374	9,967
Portland, OR	31	233,953	7,547
Portland, OR	17	137,865	8,110
Portland, OR	17	141,063	8,298
Portland, OR	37	430,111	11,625
Portland, OR	36	325,736	9,048
Portland, OR	63	449,187	7,130
Portland, OR	25	241,367	9,655
Portland, OR	64	730,863	11,420
Portland, OR	48	485,583	10,116
Portland, OR	50	362,502	7,250
Portland, OR	93	992,478	10,672
Portland, OR	63	310,084	4,922
Portland, OR	88	923,222	10,491
Portland, OR	60	386,949	6,449
Portland, OR	62	469,861	7,578
Portland, OR	50	437,603	8,752
Portland, OR	34	232,045	6,825
Portland, OR	60	443,179	7,386
Portland, OR	58	719,589	12,407
Portland, OR	95	964,264	10,150

Appendix B, attachment 3: HDC portfolio analysis data

Portland, OR	14	153,918	10,994
Portland, OR	6	28,124	4,687
Portland, OR	90	820,441	9,116
Portland, OR	141	1,090,313	7,733
Troutdale, OR	4	23,242	5,811
Troutdale, OR	44	344,510	7,830

bae urban economics

Memorandum

To: Emily Lieb, Housing Policy Director
Melissa Arnold, Strategic Initiatives Lead

From: Paul Peninger, Principal
Matt Fairris, Vice President

Date: July 5, 2024

Re: Gap Funding for New Rental Housing Construction by Capital Scenario

Introduction

To support a conversation about addressing affordable housing need throughout the Portland region, Metro convened a team of consultants to provide technical analysis of a range of affordable housing investment options and scenarios. This includes investment strategies to support new affordable rental housing projects, acquisition and conversion projects, and affordable homeownership projects, among other potential strategies. The following memorandum estimates the **"per unit"** amount of Metro gap funding required to support new affordable rental housing construction throughout the three-County Metro region, broken down by unit size and affordability level. Given that affordable housing projects rely on a range of federal, state, and local funding sources, which will vary by project, this analysis summarizes the per-unit Metro gap funds based on a range of financing scenarios. The analysis includes the following four project financing scenarios:

Scenario 1: Metro Gap Funding and Permanent Debt

Scenario 2: Metro Gap Funding, Permanent Debt, Four-Percent Low-Income Housing Tax Credits (LIHTC), and Developer Contribution

Scenario 3: Metro Gap Funding, Permanent Debt, Four-Percent LIHTC, Developer Contribution, and Oregon Housing and Community Services (OHCS) Funding

Scenario 4: Metro Gap Funding, Permanent Debt, Four-Percent LIHTC, Developer Contribution, OHCS Funding, and Local Funding

The following Metro gap funding estimates can then be plugged into a broader Metro Capital Investment Modeling Tool, which will analyze the Metro funding required to support a range of potential investments. For example, using these estimates, Metro staff can estimate the required Metro funds to support housing projects without the use of LIHTC versus assuming all projects will leverage LIHTC and OHCS funding.

This analysis only estimates the required Metro gap funding taking into account the most important capital funding sources. BAE will, however, incorporate the use of operating subsidy sources, such as Section 8 Vouchers and Regional Long-Term Rent Assistance (RLRA) subsidies, as part of the broader Metro Capital Investment Modeling Tool assistance.

Methodology

To estimate the amount of Metro funding required to support each project financing scenario, BAE first estimates the typical per-unit development cost, broken down by unit size. This estimate is informed by a review of the 50 rental projects funded by the 2018 Metro Bond, with a particular emphasis on more recent projects that are currently under construction or nearing construction. In addition, BAE in partnership with Metro staff conducted a series of interviews with local affordable housing developers and industry subject matter experts to understand current market conditions and development costs relative to previous Metro Bond projects.

After estimating the total development cost by unit size, BAE then estimates the typical amount of per-unit funding contributed to projects from each financing source. For the Four-percent LIHTC program, the per-unit financing amount is based on a standard formula that is based on the total development cost. For other sources, such as OHCS and local funds, the per-unit financing amount is based on historic financing amounts allocated to Metro bond projects, in addition to a review of recent funding guidelines. Lastly, permanent debt is calculated based on the net operating income generated by each unit size and affordability level, based on a standard set of underwriting criteria. In summary, the required Metro gap funding estimate is based on the following formula:

Total Development Cost Per Unit

-

Estimated Non-Metro Funding
(i.e., Permanent Debt, LIHTC, OHCS, Local Funds, etc.)

=

Required METRO Gap Funding

Development Cost Assumptions

Based on recent 2018 Metro Bond rental projects, combined with stakeholder feedback, BAE estimates the average development cost per square foot for affordable housing projects in the Portland region is roughly $660 per gross project square foot. Based on a review of comparable projects, the typical unit size range from 400 square foot studio units to 900 square foot three-bedroom units. To convert net residential square footage to total project square footage, the following analysis differentiates between Non-Permanent Supportive Housing (Non-PSH) and Permanent Supportive Housing (PSH) projects. PSH developments include more non-leasable space to support the provision of additional resident and supportive services. As such, the following analysis assumes 40 percent of PSH developments are non-leasable, while Non-PSH developments only include 20 percent of the building for non-leasable space, including commons areas and circulation. Therefore, the estimated development cost of units in the Portland region range from $330,000 to nearly $800,000, as seen below:

Estimated Development Cost per Unit

Unit Type	Unit Size (sf)	Total Development Cost per SF	Total Development Cost per Unit (Non PSH) (a)	Total Development Cost per Unit (PSH) (a)
Studio	400	$660	$330,000	$356,400
1BR	600	$660	$500,000	$540,000
2BR	750	$660	$620,000	$669,600
3BR	900	$660	$740,000	$799,200

(a) Assumes Non-PSH developments have a 20 percent non-leasable ratio to accommodate common areas and circulation, while PSH developments have a 40 percent non-leasable ratio to accommodate additional resident and supportive service space.

Non-Metro Capital Financing Sources

As noted above, the methodology for calculating the required Metro gap funding per unit begins with analyzing the amount of capital funding from other traditional affordable housing funding sources, including LIHTC, permanent debt, developer contributions, OHCS, and local jurisdictions. This analysis reviews the amount of funding contributed to projects that also received funding from the 2018 Metro Bond. In addition, for sources that are reliant on project development costs or operating revenues, the analysis calculates the amount of supportable funding. After calculating the amount of supportable funding from each source, the following section calculates the total amount of Metro funding required to fill the remaining funding gap based on the four financing scenarios. Note that these estimates do not include more variable funding sources, such as other federal funding from the Housing and Urban Department (HUD) or additional grant funding, like the Affordable Housing Program (AHP) grants from Federal Home Loan Banks throughout the Country.

LIHTC

The Low-Income Housing Tax Credit (LIHTC) program provides “equity” to an affordable housing program through the form of a tax credit against Federal tax liability. The tax credits that are awarded to a project are then sold to a tax credit investor to generate upfront capital to an affordable housing project. The Federal LIHTC program has two different sources of funding programs, called the nine-percent and the four-percent LIHTC program. The nine-percent program is competitive and often committed to projects that do not require a significant amount of additional funding sources. The four-percent program is intended to be non-competitive, but requires the use of Private Activity Bonds (PABs) to cover at least 50 percent of the project costs during construction.[1] The PABs are also allocated by OHCS and are limited, which led OHCS to recently create a competitive application for four-percent tax credits and PABs. For reference, 90 percent of 2018 Metro Bond projects leveraged the four-percent LIHTC program. As such the following analysis estimates the funding requirements assuming project receive LIHTC through the four-percent program.

The method for calculating project-specific LIHTC eligibility is set by the Federal government. The method is based on a project development cost, times the credit rate (either four percent or nine percent). This results in an annual credit amount, which is given the project for ten years. These ten years of tax credits are then sold to an investor for upfront capital.

A critical component of the amount of LIHTC contributed to a project is whether a project is located in a “Difficult to Develop Area” (DDA) or “Qualified Census Tract” (QCT). If a project is located in one of these areas, the project is eligible for a 30 percent “basis boost” in the number of tax credits. As such, the tables below distinguish between projects located in a DDA or QCT and those outside of the areas. While these DDA and QCT areas change every year, roughly 72 percent of the 2018 Metro Bond projects were located in a DDA or QCT area in the given year. Given the amount of LIHTC does not differ by income level, but is solely based on the project’s cost, the estimates below do not differentiate between affordability level.

4-Percent LIHTC Allocation per Unit

LIHTC Amount	Studio	1 BR	2 BR	3 BR
LIHTC per Unit, No DDA/QCT Boost	$107,136	$160,704	$197,532	$237,708
LIHTC per Unit, with DDA/QCT Boost	$139,277	$208,915	$256,792	$309,020

Permanent Debt

Projects that generate excess revenue after covering operating expenses, including resident services, will take on permanent debt to support upfront capital costs. Based on maximum rental rates by affordability level, the estimates below indicate that most units affordable to households below 40 percent of the Area Median Income (AMI) do not generate excess revenue and instead require operating subsidies to support ongoing property management, maintenance, resident services, and other operating costs. For units affordable to households at or above 40 percent of AMI, the excess revenue can be used to support debt. Assuming traditional lending terms noted below, the table on the following page provides an estimate of the per-unit support debt amount by unit size and affordability level:

[1] According to the Internal Revenue Code (IRC) Section 42(h)(4)(B), affordable residential rental projects leveraging the 4% LIHTC must finance the at least 50% of project costs with tax-exempt bonds from a state’s bond volume cap under IRC 142 and 146.

Appendix C: Gap Analysis for New Construction by Capital Scenario Memorandum, BAE Urban Economics

Supportable Permanent Debt Per Unit

AMI	Studio	1 BR	2 BR	3 BR
PSH	*No Debt*	*No Debt*	*No Debt*	*No Debt*
30%	*No Debt*	*No Debt*	*No Debt*	$6,284
35%	*No Debt*	*No Debt*	$10,767	$25,533
40%	$4,175	$8,394	$27,511	$44,914
45%	$17,096	$22,369	$44,255	$64,295
50%	$30,148	$36,345	$60,999	$83,544
55%	$43,200	$50,188	$77,743	$102,925
60%	$56,253	$64,163	$94,487	$122,306
80%	$108,330	$120,064	$161,463	$199,697

Note: Based on the estimated Net Operating Income by MFI-level, assuming the following conservative lending terms based on recent project information and developer interviews:
- 1.2 Debt Service Coverage Ratio
- 6.50% Interest Rate
- 30-Year Term

Developer Contributions

Projects that receive LIHTC also include a developer fee. Often, developers will contribute a share of this upfront developer fee back to the project as upfront capital to reduce the number of funding sources required to build the project, called a "deferred developer fee." In some cases, developers will also contribute their own capital resources to the project in order to fill any financing gaps. Together, these funds contribute additional funding to the project. Based on a review of Metro Bond projects currently under construction and nearing construction, developers are contributing an average of approximately **$36,000 per unit** in direct capital to the project through a mix of deferred developer fees and direct cash contribution. As such, the analysis assumes this developer contribution will continue for any project leveraging LIHTC.

OHCS

As the State of Oregon's Housing finance agency, OHCS has a range of funding programs to support new affordable housing production in addition to the federally funded LIHTC. Approximately $100 million of OHCS funding has been contributed to support the 50 Metro Bond projects. The Local Innovation and Fast Tract (LIFT) program accounts for the highest share of OHCS funding provided to Metro bond projects, at roughly $54 million, followed by the Permanent Supportive Housing program ($21 Million), General Housing Account Program ($12 Million), Housing Trust Fund ($10 Million), and the Multifamily Housing Energy Program ($3.2 million).

Not every Metro bond project, however, received an allocation of OHCS funding. For Metro rental projects slated for construction in 2024, roughly 60 percent of projects received funding, with the bulk of funds coming from the LIFT program. For recent projects that received OHCS funding, the average funding allocation was nearly **$50,000 per unit.**

Appendix C: Gap Analysis for New Construction by Capital Scenario Memorandum, BAE Urban Economics

It is worth noting that the capital funding available to OHCS in the future is expected to be well beyond historic amounts. According to a recent presentation, OHCS anticipates roughly $544 million in total capital spending for 2024. While only a portion of these funds will be available to projects in the Portland Metro region, currently estimated at roughly 40 percent of the available funding, the increased funding may result in higher per-unit OHCS gap funding contributions or more projects with similar per-unit gap amounts. However, the potential increase in OHCS funding may not result in a commensurate increase in housing unit production due to recent increases in development costs.

Local Funding

Local jurisdictions throughout the Metro region have also contributed funding to Metro bond projects. Roughly half of the projects funded by the 2018 Metro Bond also received funds from the local jurisdiction, the majority of which came in the form of SDC waivers and clean energy funds to offset increased project costs. Based on an analysis of the projects that received funding from local jurisdictions, the average subsidy amount was approximately **$25,000 per unit.** If local jurisdictions continue funding affordable housing projects alongside Metro, it will further decrease the necessary Metro bond subsidy per unit.

Required Metro Gap Funding Per Unit

Using the expected development cost and funding amounts from the prior sources, the following section summarizes the resulting required Metro gap financing amounts broken down by unit type and affordability level. Figure 1 at the end of the section compares the various scenarios and the resulting per-unit Metro gap funding required to support a typical unit under each capital investment scenario.

Funding Scenario 1: Metro Gap Funding with Permanent Debt

The first funding scenario assumes Metro provides all the funding necessary to fill the funding gap beyond a supportable debt amount. As seen in Table 1 on the following page, the supportable debt amount ranges from zero to nearly $200,000 per unit depending on unit type and affordability level. Broken down by unit size, the required gap for a studio unit ranges from $220,000 to $360,000 per unit, while a one-bedroom units ranges from $380,000 per unit to $540,000 per unit, a two-bedroom unit ranges from $460,000 to $670,000 per unit, and a three bedroom unit ranges from $540,000 to $800,000 per unit.

These estimates are well above the per-unit subsidy amounts Metro contributed to recent projects due to the lack of additional leveraging. These types of projects will likely only be relevant if Metro intends to fund projects when OHCS has already committed the available LIHTC and PABs to other projects, like is the case in 2024, or when local jurisdictions and other federal programs do not have available capital to contribute for affordable housing production.

Table 1: Estimated Metro Gap Funding, Scenario 1: Permanent Debt Only

	Unit Type			
% of MFI	Studio	1 BR	2 BR	3 BR
Development Cost per Unit, Non-PSH	**$330,000**	**$500,000**	**$620,000**	**$740,000**
Development Cost per Unit, PSH	**$356,400**	**$540,000**	**$669,600**	**$799,200**
Supportable Debt by Unit				
<30% AMI PSH	No Debt	No Debt	No Debt	No Debt
30% AMI	No Debt	No Debt	No Debt	$6,284
35% AMI	No Debt	No Debt	$10,767	$25,533
40% AMI	$4,175	$8,394	$27,511	$44,914
45% AMI	$17,096	$22,369	$44,255	$64,295
50% AMI	$30,148	$36,345	$60,999	$83,544
55% AMI	$43,200	$50,188	$77,743	$102,925
60% AMI	$56,253	$64,163	$94,487	$122,306
80% AMI	$108,330	$120,064	$161,463	$199,697
Metro Gap Funding				
<30% AMI PSH	**$356,400**	**$540,000**	**$669,600**	**$799,200**
30% AMI	**$330,000**	**$500,000**	**$620,000**	**$733,716**
35% AMI	**$330,000**	**$500,000**	**$609,233**	**$714,467**
40% AMI	**$325,825**	**$491,606**	**$592,489**	**$695,086**
45% AMI	**$312,904**	**$477,631**	**$575,745**	**$675,705**
50% AMI	**$299,852**	**$463,655**	**$559,001**	**$656,456**
55% AMI	**$286,800**	**$449,812**	**$542,257**	**$637,075**
60% AMI	**$273,747**	**$435,837**	**$525,513**	**$617,694**
80% AMI	**$221,670**	**$379,936**	**$458,537**	**$540,303**

Sources: Metro; BAE, 2024.

Funding Scenario 2: Metro Gap Financing with Permanent Debt, 4-Percent LIHTC, and Developer Contribution

All but two rental projects funded through the first Metro Housing Bond leveraged the LIHTC program. By including LIHTC in the assumed capital stack, the required Metro funding per unit is reduced significantly. As seen in Table 2 on the following page, the required Metro funding amounts are reduced by nearly half, reaching amounts between $100,000 to $450,000 for most unit types and affordability levels. As noted previously, the amount of LIHTC will depend on whether the project is in a DDA/QCT area. Therefore, Table 2 presents two separate Metro Gap Funding estimates for each unit type and affordability level. Projects located in a DDA or QCT will be allocated more LIHTC, which will reduce the resulting funding gap.

Funding Scenario 3: Metro Gap Financing with Permanent Debt and 4-Percent LIHTC, PABs, Developer Contribution, and OHCS Funding

The third funding scenario more closely aligns with Metro's existing development pipeline by including the use of OHCS funds. As noted previously, approximately two-thirds of all Metro-funded new affordable rental housing projects also received an allocation of OHCS gap funding. Using the historic typical subsidy amount for projects that received OHCS funding, of roughly $50,000 per unit, the required Metro gap funding amount is further reduced. As seen in Table 3 on the following page, the majority of the resulting per-unit subsidy amounts are still above the typical Metro funding from the 2018 Bond, of roughly $150,000 per unit. This is driven by several factors, including the increasing construction costs and operating costs in the current affordable housing development environment, as well as conservative assumptions around the amount of OHCS funding. In addition, this scenario only accounts for the most common and reliable funding sources available to support affordable housing production.

Funding Scenario 4: Metro Gap Financing with Permanent Debt and 4-Percent LIHTC, PABs, Developer Contribution, OHCS Funding, and Local Funding

While less reliable than the previous funding sources, local jurisdictions provided some form of funding for roughly half of the projects supported by the 2018 Metro Bond. As noted above, projects that included local funding generally received $25,000 per unit. This local contribution further reduces the required Metro gap funds. As seen in Table 4 on the following pages, layering in local funding sources reduces the Metro gap to similar levels as seen in projects funded with the 2018 Metro bond. For example, a one- or two-bedroom unit affordable at 50 percent of MFI, generally representative of the average unit supported by the 2018 Metro Bond, requires between $200,000 and $270,000 in gap funding, depending on whether the project is located in a DDA or QCT. As noted previously, while this financing scenario incorporates a significant number of funding sources, there are other more variable sources of funds that are contributed to similar projects, including other federal sources and other debt sources. These sources can be incorporated into the next step of the analysis, discussed below.

Appendix C: Gap Analysis for New Construction by Capital Scenario Memorandum, BAE Urban Economics

Table 2: Estimated Metro Gap Funding, Scenario 2: Permanent Debt, LIHTC, and Developer Contribution

	Unit Type			
% of MFI	Studio	1 BR	2 BR	3 BR
Development Cost per Unit, Non-PSH	**$330,000**	**$500,000**	**$620,000**	**$740,000**
Development Cost per Unit, PSH	**$356,400**	**$540,000**	**$669,600**	**$799,200**
Supportable Debt by Unit				
<30% AMI PSH	No Debt	No Debt	No Debt	No Debt
30% AMI	No Debt	No Debt	No Debt	$6,284
35% AMI	No Debt	No Debt	$10,767	$25,533
40% AMI	$4,175	$8,394	$27,511	$44,914
45% AMI	$17,096	$22,369	$44,255	$64,295
50% AMI	$30,148	$36,345	$60,999	$83,544
55% AMI	$43,200	$50,188	$77,743	$102,925
60% AMI	$56,253	$64,163	$94,487	$122,306
80% AMI	$108,330	$120,064	$161,463	$199,697
LIHTC Per Unit				
LIHTC, No DDA/QCT Boost	$110,484	$167,400	$207,576	$247,752
LIHTC, with DDA/QCT Boost	$143,629	$217,620	$269,849	$322,078
Developer Contribution				
Per Unit	$36,000	$36,000	$36,000	$36,000
Metro Gap Funding				
<30% AMI PSH				
No DDA/QCT Boost	***$209,916***	***$336,600***	***$426,024***	***$515,448***
With DDA/QCT Boost	***$176,771***	***$286,380***	***$363,751***	***$441,122***
30% AMI				
No DDA/QCT Boost	***$183,516***	***$296,600***	***$376,424***	***$449,964***
With DDA/QCT Boost	***$150,371***	***$246,380***	***$314,151***	***$375,638***
35% AMI				
No DDA/QCT Boost	***$183,516***	***$296,600***	***$365,657***	***$430,715***
With DDA/QCT Boost	***$150,371***	***$246,380***	***$303,384***	***$356,389***
40% AMI				
No DDA/QCT Boost	***$179,341***	***$288,206***	***$348,913***	***$411,334***
With DDA/QCT Boost	***$146,196***	***$237,986***	***$286,640***	***$337,008***
45% AMI				
No DDA/QCT Boost	***$166,420***	***$274,231***	***$332,169***	***$391,953***
With DDA/QCT Boost	***$133,275***	***$224,011***	***$269,896***	***$317,627***
50% AMI				
No DDA/QCT Boost	***$153,368***	***$260,255***	***$315,425***	***$372,704***
With DDA/QCT Boost	***$120,223***	***$210,035***	***$253,152***	***$298,378***
55% AMI				
No DDA/QCT Boost	***$140,316***	***$246,412***	***$298,681***	***$353,323***
With DDA/QCT Boost	***$107,170***	***$196,192***	***$236,408***	***$278,997***
60% AMI				
No DDA/QCT Boost	***$127,263***	***$232,437***	***$281,937***	***$333,942***
With DDA/QCT Boost	***$94,118***	***$182,217***	***$219,664***	***$259,617***
80% AMI				
No DDA/QCT Boost	***$75,186***	***$176,536***	***$214,961***	***$256,551***
With DDA/QCT Boost	***$42,040***	***$126,316***	***$152,688***	***$182,225***

Sources: Metro; BAE, 2024.

Appendix C: Gap Analysis for New Construction by Capital Scenario Memorandum, BAE Urban Economics

Table 3: Estimated Metro Gap Funding, Scenario 2: Permanent Debt, LIHTC, Developer Contribution, and OHCS Gap Funding

	Unit Type			
% of AMI	Studio	1 BR	2 BR	3 BR
Development Cost per Unit, Non-PSH	**$330,000**	**$500,000**	**$620,000**	**$740,000**
Development Cost per Unit, PSH	**$356,400**	**$540,000**	**$669,600**	**$799,200**
Supportable Debt by Unit				
<30% AMI PSH	No Debt	No Debt	No Debt	No Debt
30% AMI	No Debt	No Debt	No Debt	$6,284
35% AMI	No Debt	No Debt	$10,767	$25,533
40% AMI	$4,175	$8,394	$27,511	$44,914
45% AMI	$17,096	$22,369	$44,255	$64,295
50% AMI	$30,148	$36,345	$60,999	$83,544
55% AMI	$43,200	$50,188	$77,743	$102,925
60% AMI	$56,253	$64,163	$94,487	$122,306
80% AMI	$108,330	$120,064	$161,463	$199,697
LIHTC				
Per Unit, No DDA/QCT Boost	$110,484	$167,400	$207,576	$247,752
Per Unit, with DDA/QCT Boost	$143,629	$217,620	$269,849	$322,078
Developer Contribution				
Per Unit	$36,000	$36,000	$36,000	$36,000
OHCS Funding				
Per Unit	$50,000	$50,000	$50,000	$50,000
Metro Gap Funding				
<30% AMI PSH				
No DDA/QCT Boost	***$159,916***	***$286,600***	***$376,024***	***$465,448***
With DDA/QCT Boost	***$126,771***	***$236,380***	***$313,751***	***$391,122***
30% AMI				
No DDA/QCT Boost	***$133,516***	***$246,600***	***$326,424***	***$399,964***
With DDA/QCT Boost	***$100,371***	***$196,380***	***$264,151***	***$325,638***
35% AMI				
No DDA/QCT Boost	***$133,516***	***$246,600***	***$315,657***	***$380,715***
With DDA/QCT Boost	***$100,371***	***$196,380***	***$253,384***	***$306,389***
40% AMI				
No DDA/QCT Boost	***$129,341***	***$238,206***	***$298,913***	***$361,334***
With DDA/QCT Boost	***$96,196***	***$187,986***	***$236,640***	***$287,008***
45% AMI				
No DDA/QCT Boost	***$116,420***	***$224,231***	***$282,169***	***$341,953***
With DDA/QCT Boost	***$83,275***	***$174,011***	***$219,896***	***$267,627***
50% AMI				
No DDA/QCT Boost	***$103,368***	***$210,255***	***$265,425***	***$322,704***
With DDA/QCT Boost	***$70,223***	***$160,035***	***$203,152***	***$248,378***
55% AMI				
No DDA/QCT Boost	***$90,316***	***$196,412***	***$248,681***	***$303,323***
With DDA/QCT Boost	***$57,170***	***$146,192***	***$186,408***	***$228,997***
60% AMI				
No DDA/QCT Boost	***$77,263***	***$182,437***	***$231,937***	***$283,942***
With DDA/QCT Boost	***$44,118***	***$132,217***	***$169,664***	***$209,617***
80% AMI				
No DDA/QCT Boost	***$25,186***	***$126,536***	***$164,961***	***$206,551***
With DDA/QCT Boost	***($7,960)***	***$76,316***	***$102,688***	***$132,225***

Sources: Metro; BAE, 2024.

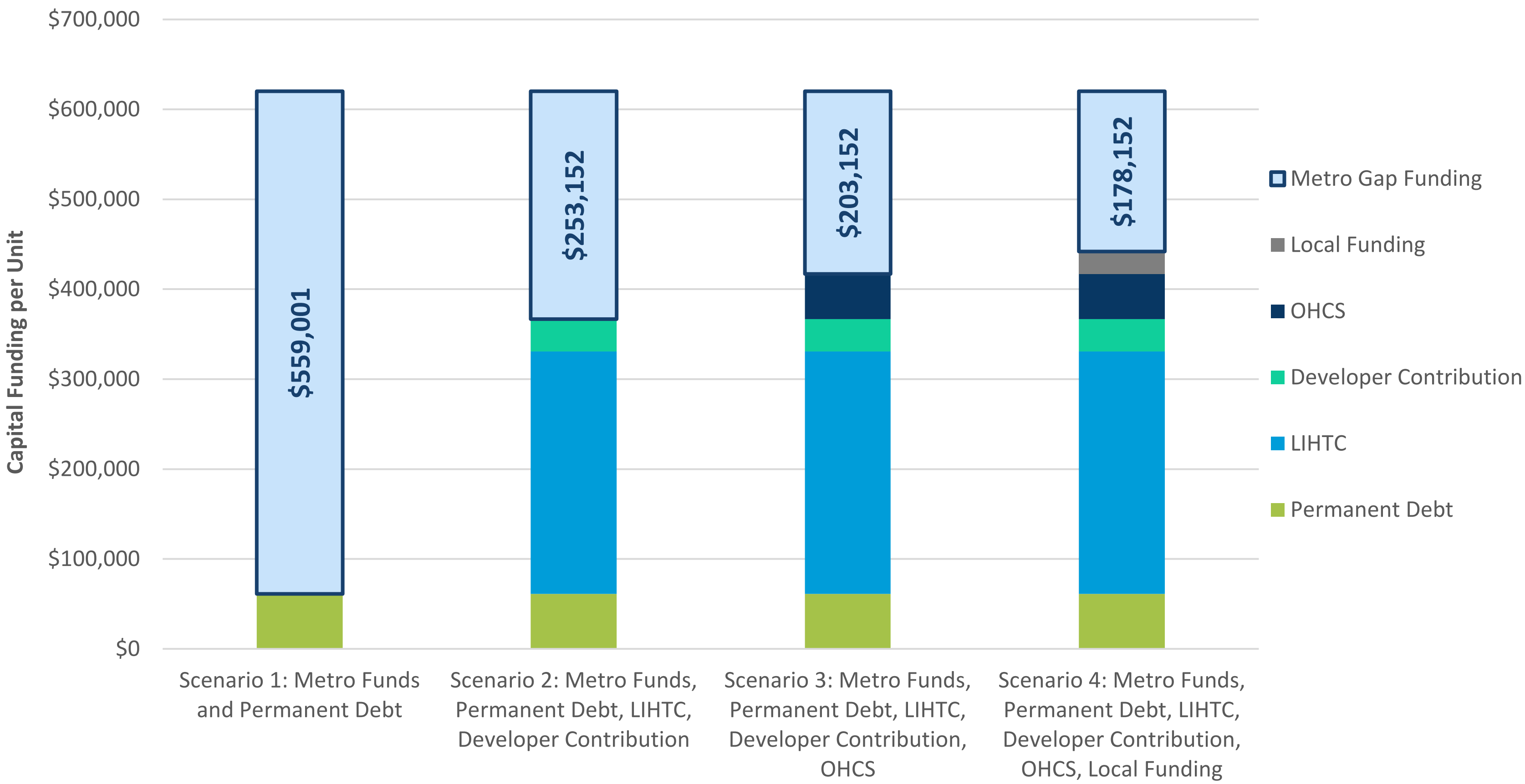
Appendix C: Gap Analysis for New Construction by Capital Scenario Memorandum, BAE Urban Economics

Table 4: Estimated Metro Gap Funding, Scenario 2: Permanent Debt, LIHTC, Developer Contribution, OHCS Gap Funding, and Local Funding

	Unit Type			
% of AMI	Studio	1 BR	2 BR	3 BR
Development Cost per Unit, Non-PSH	**$330,000**	**$500,000**	**$620,000**	**$740,000**
Development Cost per Unit, PSH	**$356,400**	**$540,000**	**$669,600**	**$799,200**
Supportable Debt by Unit				
<30% AMI PSH	No Debt	No Debt	No Debt	No Debt
30% AMI	No Debt	No Debt	No Debt	$6,284
35% AMI	No Debt	No Debt	$10,767	$25,533
40% AMI	$4,175	$8,394	$27,511	$44,914
45% AMI	$17,096	$22,369	$44,255	$64,295
50% AMI	$30,148	$36,345	$60,999	$83,544
55% AMI	$43,200	$50,188	$77,743	$102,925
60% AMI	$56,253	$64,163	$94,487	$122,306
80% AMI	$108,330	$120,064	$161,463	$199,697
LIHTC				
Per Unit, No DDA/QCT Boost	$110,484	$167,400	$207,576	$247,752
Per Unit, with DDA/QCT Boost	$143,629	$217,620	$269,849	$322,078
Developer Contribution				
Per Unit	$36,000	$36,000	$36,000	$36,000
OHCS Funding				
Per Unit	$50,000	$50,000	$50,000	$50,000
Local Funding				
Per Unit	$25,000	$25,000	$25,000	$25,000
Metro Gap Funding				
<30% AMI PSH				
No DDA/QCT Boost	***$134,916***	***$261,600***	***$351,024***	***$440,448***
With DDA/QCT Boost	***$101,771***	***$211,380***	***$288,751***	***$366,122***
30% AMI				
No DDA/QCT Boost	***$108,516***	***$221,600***	***$301,424***	***$374,964***
With DDA/QCT Boost	***$75,371***	***$171,380***	***$239,151***	***$300,638***
35% AMI				
No DDA/QCT Boost	***$108,516***	***$221,600***	***$290,657***	***$355,715***
With DDA/QCT Boost	***$75,371***	***$171,380***	***$228,384***	***$281,389***
40% AMI				
No DDA/QCT Boost	***$104,341***	***$213,206***	***$273,913***	***$336,334***
With DDA/QCT Boost	***$71,196***	***$162,986***	***$211,640***	***$262,008***
45% AMI				
No DDA/QCT Boost	***$91,420***	***$199,231***	***$257,169***	***$316,953***
With DDA/QCT Boost	***$58,275***	***$149,011***	***$194,896***	***$242,627***
50% AMI				
No DDA/QCT Boost	***$78,368***	***$185,255***	***$240,425***	***$297,704***
With DDA/QCT Boost	***$45,223***	***$135,035***	***$178,152***	***$223,378***
55% AMI				
No DDA/QCT Boost	***$65,316***	***$171,412***	***$223,681***	***$278,323***
With DDA/QCT Boost	***$32,170***	***$121,192***	***$161,408***	***$203,997***
60% AMI				
No DDA/QCT Boost	***$52,263***	***$157,437***	***$206,937***	***$258,942***
With DDA/QCT Boost	***$19,118***	***$107,217***	***$144,664***	***$184,617***
80% AMI				
No DDA/QCT Boost	***$186***	***$101,536***	***$139,961***	***$181,551***
With DDA/QCT Boost	***($32,960)***	***$51,316***	***$77,688***	***$107,225***

Sources: Metro; BAE, 2024.

Figure 1: Example Capital Stack by Funding Scenario, Two-Bedroom Unit at 50% AMI with DDA/QCT Boost



Sources: Metro; BAE, 2024.

Incorporating into Investment Scenario Modeling Tool

The intent of the above Metro gap funding subsidy estimates by scenario is to inform future investment scenario modeling for potential regional affordable housing funding. The various per-unit Metro gap subsidy amounts can be used to evaluate various investment scenarios, including providing larger subsidy amounts to projects in order to streamline the development process. Similarly, these estimates allow Metro staff to model the amount of funding required from other sources in order to meet a potential housing production target. For example, Metro staff will be able to project the total amount of four-percent LIHTC required to meet the goals of a specific investment scenario. Metro staff can then compare the resulting amount of LIHTC with the amount of LIHTC available from OHCS. If the housing production target requires more LIHTC than is available, Metro staff will decide whether to delay certain housing production targets, or use one of the alternative funding scenarios highlighted above to support housing production.

bae urban economics

Memorandum

To: Emily Lieb, Housing Policy Director
Melissa Arnold, Strategic Initiatives Lead

From: Paul Peninger, Principal
Matt Fairris, Vice President

Date: July 11, 2024

Re: Market Incentives, Actions, and Policies to Support Affordable Housing Production

Introduction

To consider options for addressing affordable housing needs throughout the Portland region, Metro convened a team of consultants to provide technical analysis of a range of affordable housing-related topics. The following memorandum provides a range of potential market incentives, actions, and policies that Metro could support to address current challenges to the feasibility of affordable housing developments. These incentives, actions, and policies are based on a scan of national literature and technical studies on mechanisms to support housing production, as well as a review of statewide and regional analyses aimed at decreasing costs and improving the production of housing in Oregon and the Portland region. In addition, BAE conducted a series of stakeholder interviews with local subject matter experts to better assess the opportunity for these incentives, actions, and policies to improve the feasibility of affordable housing production.

Metro Overview

It is important to note the role of Metro as a regional jurisdiction and funder, and that Metro does not directly control many of the various factors that impact the production of housing. Notably, a regional entity like Metro does not directly control local land use policy, such as zoning, entitlement process and timeline, design standards, affordable housing requirements, or infrastructure upgrade requirements, among others. Similarly, Metro does not control various one-time and ongoing costs to affordable housing developments, including one-time permitting fees and System Development Charges, as well as ongoing property taxes. Metro also does not control the allocation of State and Federal financing sources that are used to support the production of affordable housing, including State and Federal Low-Income Housing Tax Credits (LIHTC), and State of Oregon loan and grant programs. However, while Metro does not directly control local land use policies and other local programs, through its regional planning, state and federal policy advocacy, and regional funding and grant programs, Metro does have the ability to influence and support local policies that reduce barriers and lower costs for affordable and equitable housing development.

Based on a review of similar regional approaches to supporting affordable housing production, the role of a regional entity with limited control of local land use authority or State and Federal affordable housing funding sources is most commonly to provide gap financing to affordable housing projects that meet the regional housing need.

Below BAE identifies actions throughout the Country that intend to spur affordable housing production, regardless of the jurisdiction or jurisdictional level supporting the policy. However, the memorandum also identifies if and how Metro could potentially implement a similar incentive, action, or policy in the region. In some cases, Metro may be best positioned to simply provide or fund technical assistance and advice to local jurisdictions regarding the successful implementation of these policies and actions. In other cases, Metro may be able to directly implement such policies and programs to achieve the desired goal of increased housing production.

Affordable Housing Financing Overview

To contextualize the potential actions that can support affordable housing production, this section provides an overview of the typical financing structure for affordable housing, as well as relevant challenges in the current development and market context. Affordable housing development projects typically require the use of public funding in order to provide affordable housing to low-income households, defined as those with incomes at or below 80 percent of the Area Median Income (AMI). This is due to the lower rental rates or sale prices charged to provide affordable homes to lower-income households. These reduced rents or sale prices are insufficient to support a typical real estate investor return requirement or support sufficient permanent debt to cover the project cost. As a result, affordable housing developers leverage a range of public funding sources including:

> **Low Income Housing Tax Credit (LIHTC):** The LIHTC program provides tax credits to qualifying affordable housing projects in return for reduced rental rates. These tax credits are sold to financial institutions and investors to raise a portion of the funds required to build the affordable housing project. In return, the financial institutions and investors use these credits to offset their annual tax liability. The primary source of LIHTC come from the federal government, though the State of Oregon also has a State Housing Tax Credit program, called the Oregon Affordable Housing Tax Credit (OAHTC), which increases the funding available for affordable housing projects. Due to the structure of the program, the funds raised through the Federal LIHTC program typically provide between 30 and 70 percent of the total funds required to build an affordable housing project, resulting in a need for additional financing sources.
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> **State Financing Programs:** The State of Oregon, through Oregon Housing and Community Services (OHCS), provides a range of financing programs to address the funding gap of affordable housing projects using the State and Federal LIHTC program.

These programs, often called “gap financing”, offer funding to projects that meet specific criteria, such as specific targeted tenant populations, project readiness, geographic location, among others. The majority of OHCS financing programs, like the Local Innovation and Fast Track (LIFT) program, are allocated through the Oregon Centralized Application process, which allocates funds on a first-ready, first-reviewed basis to ensure project readiness.

Other Gap Financing Programs: Affordable housing projects may require additional gap financing to compile all the necessary funds to construct the project. Other sources of gap financing include funds from local, regional, and federal sources. At a local and regional level, one major source of funding comes from voter-approved funding programs, such as the 2016 Portland Housing Bond and the 2018 Metro Housing Bond. These voter-approved funding sources are most often one-time bonds that raise a large amount of funding to support housing production over a modest amount of time. Local and regional jurisdictions also leverage other funding sources to support affordable housing production, including general fund dollars, tax increment financing district revenues, and construction excise tax revenue, among others. Lastly, the federal government provides additional financing sources for affordable housing development through programs like the HOME Investment Partnerships Program and Community Development Block Grant, among others. These federal funds are either allocated directly to larger jurisdictions or to smaller jurisdictions through the State’s competitive allocation process.

Permanent Loan: While affordable housing projects rarely support sufficient debt to cover a large amount of the project costs, projects anticipating positive net operating income can leverage a portion of revenue to support a permanent loan amount. The loan amount differs by project based on projected revenue, but typically covers around 20 percent of an average project cost. While permanent debt typically leverages positive net operating income, additional revenue supported by project-based rental assistance can support additional permanent debt if the rental assistance amount exceeds to operating costs and the rental assistance contract is long enough to support debt leveraging (roughly 20 years).

Developer Contributions and Fee Deferrals: Affordable housing developers will contribute to developments in order to aggregate the necessary funds to build the project. Often, these funds are in the form of deferred developer fees, which delays the time over which the developer receives a standard fee for building affordable housing projects. Developer teams may also contribute other forms of support to a project, including land and direct cash.

The role of a typical affordable housing developer, sometimes called the project sponsor, is to assemble all the necessary financing to cover the cost of developing the project. As the cost of building new affordable housing increases, or other market factors change, developers must increase the amount of financing to cover project costs. As detailed below, recent rises in total development costs have created financial feasibility challenges in the local affordable housing market.

Current Challenges to Affordable Housing Production

To identify potential solutions to increasing the production of affordable housing, the following section summarizes the current challenges to affordable housing production in the Portland region. These findings are based on local subject matter expert interviews and recent analyses to support local and statewide housing projection analyses. Challenges include:

> **Increasing Development Costs:** Local stakeholders identify increasing development costs as one of the major impediments to affordable housing production. Recent analysis produced by the Portland Housing Bureau indicate that the cost of building multifamily unit in Portland increased by more than 50 percent since 2016.[1] Similarly, an analysis of affordable housing projects funded through the 2018 Metro Housing Bond indicate that the cost of projects under construction in 2024 are roughly 50 percent higher than projects that started construction in 2020. The increase in cost is driven by a variety of factors, including increased labor and materials costs, increased soft costs associated with project approval timelines and funding application timelines, as well as local fees. As the cost of building residential developments in the region increase, the required financing sources must increase to fully fund affordable housing developments.
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> **Challenges in Financial Markets:** Given that developers leverage construction loans and permanent loans to support the production of affordable housing, increases in interest rates will impact the ability to deliver affordable housing. In the current financial market, rising interest rates have resulted in higher interest payments during construction, which increase the overall cost of development. Similarly, higher permanent loan interest rates decrease the amount of supportable debt, resulting in worsening project economics and the need for more financing sources to fund a higher feasibility gap. In addition to increased interest rate challenges, smaller non-profit and less capitalized developers are also facing challenges qualifying for debt due to perceived risk and increased underwriting standards from debt sources.
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> **Scarcity of Development Sites:** The number of sites that can accommodate new development are becoming more limited as the Portland region continues to densify within the urban growth boundaries. As a result, existing vacant sites are requiring higher purchase prices, or developers are being forced to look at redeveloping existing

[1] Portland Housing Bureau, Inclusionary Housing Calibration Study, June 30 & July 7, 2023 Working Group Presentation. Available at: https://www.portland.gov/phb/inclusionary-housing/calibration-study

underutilized sites, which bring unique challenges and risks to the development process.

Escalating Operating Costs: According to local stakeholders, the cost of operating affordable housing has increased significantly over the past few years, leading to current and future operating and financial challenges. In addition, stakeholders noted that the needs of residents in affordable housing, especially permanent supportive housing residents, have increased significantly in the past few years. Stakeholders also noted a higher rate of vacant units, nonpayment of rent, and the high cost of unit turnover from unexpected damage. From a financial perspective, increasing operating budgets, higher vacancy, nonpayment of rent, and higher resident service needs will decrease the amount of permanent debt the project can support, leading to larger financial feasibility gaps. Similarly, stakeholders noted that existing buildings are challenged by these increasing operating costs and may require future funding to remain in operation.

Complex Capital Stacks: As project costs increase, the number of capital financing sources and subsidy amounts have also increased, leading to increasingly complex capital stacks to deliver affordable housing. Local stakeholders noted that each distinct financing source often requires project elements to meet specific goals, leading to challenges with ongoing operating and management of a property. Similarly, each financing source requires a new package of proposal materials to compete for financing, adding time and costs to projects. As projects require more financing sources, the application timeline and associated costs increase, leading to greater feasibility challenges.

Project Timing: Typical affordable housing projects often take several years to entitle, secure all the necessary financing sources, and construct. The longer timeline leads to increased overall cost, due to inflation trends, and reduced development capacity for development firms throughout the region. First, development projects often have holding costs, which may include property taxes, insurance, and any interest paid on debt. As project timelines extend, whether due to local approval delays or challenges with accessing all necessary financing sources, the associated project costs increase due to inflation, which ultimately increase the amount of public gap financing required to build the project. Secondly, if local development projects have longer timelines, development companies are required to focus staff time on individual projects for longer times, resulting in few projects delivered throughout the region.

Incentives, Policies, and Actions to Support Affordable Housing Production

The following section summarizes the incentives, policies, and actions local and regional governments are enacting to support housing production at various income levels. These are broken down into ***Financing Tools, Development Costs, Operating Costs and Subsidies, Land***

Use and Development Authority, Project Delivery Timeline, and ***Other Actions.*** For each incentive, policy, or action, BAE estimates the relative cost impact in terms of reduced building costs, increased debt capacity, or other direct project benefits that translate into a per-unit reduction in required public subsidy.

Affordable Housing Financing Tools

Financing solutions are powerful tools to support affordable housing production. This includes gap financing, like the 2018 Metro housing bond program, as well as direct lending to address current challenges in the financial markets and allowing more flexible use of funds.

Increase Availability of Gap Financing

Policy Description: The primary source of funding to support affordable housing is increasing the availability of gap financing at a local, regional, or state level. Gap financing is contributed to affordable housing projects that commit to a certain length of affordability, often paired with other sources of funds such as LIHTC and permanent debt. The primary challenge with increasing gap financing sources is identifying a new revenue source, such as a voter-approved ballot measure or major reallocation of existing funds.

Context for Metro: Increasing the availability of gap financing would be similar to the original 2018 Metro Affordable Housing Bond, which provided gap financing to a range of affordable housing projects throughout the region. Based on a preliminary assessment of the projects financed with the 2018 Bond dollars, Metro often provided between $50,000 and $150,000 of gap financing per affordable unit. Depending on the availability of similar gap financing sources at the local, state, or federal level, discussed in a separate memo, the required gap financing per unit likely has increased since the 2018 bond.

Policy Cost Impact: Raising a pool of funds to provide regional gap financing is unlikely to have a direct impact on the cost of development but will spur a significant increase in units produced and may allow Metro to explore alternative investment strategies beyond those implemented with the 2018 bond. BAE has provided a separate memorandum outlining gap financing conclusions, including cost and production estimates.

Create a Construction Loan Fund

Policy Description: Due to high interest rates, well capitalized public agencies are exploring a construction loan fund that would offer short-term construction loans at lower interest rates. The reduced-rate construction loan fund reduces the overall accrued construction loan interest, leading to lower overall development costs.

Context for Metro: To be most impactful and warrant the administrative time, a successful construction loan fund will likely require over $100 million of investment, allowing the fund to be used to support several projects during the construction period. Another critical aspect of a construction loan fund is the existing requirement that affordable housing projects seeking the four-percent LIHTC program must use Private Activity Bonds for at least 50 percent of their construction debt. Those bond sources offer relatively low interest rates and account for a large share of the required construction loan, indicating any regional construction loan fund may not result in significant cost savings for those projects. However, should Metro consider other project types, including nine-percent LIHTC projects, or projects not leveraging LIHTC, a low-interest construction loan fund could translate into cost savings. This would reduce the required amount of public gap financing provided to these projects, and the loan would be repaid, allowing Metro to reinvest the fund into future projects. Metro could consider partnering with a local bank or Community Development Financial Institution (CDFI) to implement a construction loan fund.

Policy Cost Impact: Reduced Construction-period interest of between **$10,000 and $30,000 per unit**, depending on unit cost and size, construction term, interest rate, and the percent of total construction funding.

Create a Permanent Loan Fund

Policy Description: Higher interest rates on permanent loans results in higher ongoing payment or a lower loan amount. By offering a lower-cost permanent loan, public entities allow projects to take on a larger loan to support the delivery of affordable housing, which reduces the total amount of gap financing sources required to support a feasible project.

Context for Metro: Like a construction loan fund, a successful permanent loan fund requires a significant amount of upfront capital that can be paid back over time. Any permanent loan fund will only impact projects with cash flow available for debt service, indicating projects with the deepest affordability levels may not benefit from this program. Instead, a permanent loan fund is better paired with an affordable housing project targeting the higher affordability levels (i.e., above 40 percent AMI), or a project with a significant amount of operating subsidies that can be used to pay debt service. Similar to above, this fund can also potentially be implemented in partnership with a local bank or CDFI to minimize administrative costs to the public entity.

Policy Cost Impact: The impact of a permanent loan fund will vary significantly by project, due to rental rates and operating costs. Assuming an interest rate equal to half of the prevailing interest rate, offering a low interest rate permanent loan to a standard affordable housing project can increase the debt amount, and therefore reduces the additional gap funding sources required, by between **$15,000 and $35,000 per unit.**

Create a Mezzanine Loan Fund

Policy Description: Similar to the permanent loan, offering a lower-interest mezzanine loan product increases the supportable debt amount that improves the project economics. A mezzanine loan is a higher-risk loan product that provides additional debt beyond debt and equity. Typically, mezzanine debt has higher interest rates than traditional debt sources, and therefore does not lead to substantial improvements in typical project economics. However, a low-interest mezzanine loan product can fill a gap in the funding at a relatively low cost of capital and lead to savings on the required public gap funding per unit.

Due to the unique nature of traditional LIHTC developments, however, this loan product is more challenging to incorporate into a capital stack for a deeply affordable property. The reason for this is mezzanine debt is often repaid over a shorter amount of time relative to a longer-term debt source. In deeply affordable housing, properties rarely generate sufficient income to pay off a short-term permanent debt source. Therefore, the low-interest mezzanine loan funding may be better positioned to support middle income housing developments which do generate sufficient rental revenue to support the repayment of a mezzanine loan program.

Context for Metro: As noted above, this shorter-term low-interest rate mezzanine loan product is best positioned to support projects that generate ongoing revenue and can refinance or attract additional equity to repay the mezzanine loan a few years after project delivery. The typical project economics of deeply affordable housing units, such as those funded through the LIHTC and other public financing sources, rarely include a near-term opportunity to recapitalize or attract new equity to the project. This indicates that should Metro explore offering a mezzanine loan fund, it is best suited for housing developments targeting higher income levels without a traditional affordable housing capital stack, like Governor Kotek's recent middle income housing finance source that provides short-term mezzanine loans that are repaid through property taxes.

Policy Cost Impact: Depending on the amount of mezzanine debt provided per unit, a low-interest mezzanine debt product can reduce the required return threshold and lead to improved project economics of between **$5,000 to $10,000 per unit.**

Provide Permanent Loan Collateralization

Policy Description: Proposed as a potential tool for Oregon jurisdictions to support housing production in a recent Oregon Department of Land Conservation and Development (DLCD) housing production strategy guidance document, a public entity can provide collateral to support improved lending terms for projects with permanent debt. The public entity would provide a form of guarantee to a lender on behalf of a developer in return for lower interest rates due to the perceived reduced risk in the loan. While affordable housing developments have historically generated stable income as projected in the underwriting process, discussions with local property owners indicate substantial challenges in operating revenues. If a public entity were involved as a loan guarantor, the public jurisdiction would then be required to make up for any inability to meet the required debt payments.

Context for Metro: As noted in the DLCD document, providing a guarantee is most useful in attracting capital to areas where perceived investment risk is high rather than strictly lowering interest rates. Loan guarantees can also support smaller and emerging developers with less cash flow and development experience. Based on discussions with local stakeholders, it is not clear how loan terms would improve with a guarantee from a local jurisdiction. If Metro were interested in providing collateral to support improved loan terms, additional discussions with lenders and investors will be necessary to understand the potential improved loan terms.

Policy Cost Impact: Assuming an average unit type and affordability level generates roughly $4,000 in annual net operating income, based on the 2018 Bond portfolio, a 1.0 percent reduction in the permanent loan interest rate, possibly achievable through the loan collateralization offered by Metro, would result in an improved supportable debt amount, and therefore reduced public gap financing amount, of **$10,000 to $12,000 per unit.**

Create an Infrastructure Investment Fund

Policy Description: Recognizing that required on- and off-site infrastructure investments often add costs to residential development projects, a fund that is dedicated to improving and upgrading infrastructure in areas with inadequate existing infrastructure can translate to cost savings for future development projects. The fund could assist individual housing developments by providing funds to support site-level infrastructure requirements or could be used to address neighborhood-level infrastructure upgrades that support a range of future development opportunities.

Context for Metro: Based on interviews, several local developments identified unexpected infrastructure upgrade requirements, which led to a shortage of funding and project delays. Metro could consider reserving a portion of available funds to help projects address unexpected infrastructure requirements. This will not lead to a more efficient use of Metro funds but will allow projects to continue building in the event of unexpected costs when all other project financing is finalized.

Policy Cost Impact: Providing funds to fill any gap associated with unexpected infrastructure requirements will only minorly impact the project costs by saving the holding costs associated with the potential project delay. However, it could require the use of Metro dollars that otherwise would have gone to support other projects, resulting in a less efficient use of Metro dollars rather than true cost savings. The trade-off is then helping individual projects and less capitalized development organizations address unexpected hurdles and continue with construction versus spreading Metro dollars across more projects.

Allow Funds to be used for Predevelopment

Policy Description: Allowing public funding to be used for predevelopment at a zero interest rate reduces potential costs and risks for developers. This program can reduce costs by eliminating the need for housing developers to take out predevelopment loans or use their own capital, which otherwise could be yielding a return. In turn, these cost savings will translate into a smaller required public gap subsidy amount. Allowing firms to use funds for predevelopment also increases the capacity of smaller development groups by allowing them to pursue more development opportunities without risking their own capital or if they cannot access traditional predevelopment loan products.

Context for Metro: A constant theme from stakeholder interviews indicate the desire to use Metro funding during predevelopment. While Metro could create a predevelopment fund, it is likely more efficient to allow projects that receive an allocation of Metro funding to use a portion of these funds for predevelopment efforts. According to stakeholder interviews, the Portland Housing Bureau allowed projects to use a portion of their funding for predevelopment efforts which helped developer push projects forward without incurring interest on a loan or using their own capital to support individual projects. In addition to reducing project costs, discussed below, given the state's recent plan to prioritize affordable housing funding based on project readiness, predevelopment dollars are critical to help smaller organizations identify and pursue projects that will be competitive for state funding.

Policy Cost Impact: The most significant impact of allowing funds to be used for predevelopment is reducing the early-state risk of pursuing an affordable housing project for developers and allowing developers to pursue more projects. In particular, access to predevelopment funds will help remove barriers for small, emerging, and culturally-specific development organizations. Assuming a project without adequate predevelopment funding would take on a loan to support these efforts, allowing projects to use Metro funds for predevelopment could save between **$2,000 and $5,000 per unit.**

Create a Land Acquisition Fund

Policy Description: Identifying and purchasing land for affordable housing development is a major challenge for developers due to the high cost of site acquisition and the competition from traditional market-rate developers and investors. Many jurisdictions are exploring the use of public funds to acquire sites for future affordable development. Based on local stakeholder interviews, developers identified a potential need for Metro dollars to support land acquisition by the developers. This program could spur more development by supporting the purchase of sites ready for affordable housing production rather than relying on affordable housing development companies to identify and purchase sites using their own funds. By offering public funding, affordable housing developers will be more likely to acquire properties for future development. In addition, leveraging funds for land acquisition allows Metro to prioritize acquisition of sites meeting specific criteria, such as anti-displacement criteria, high opportunity areas, and transit-oriented sites, among others.

Context for Metro: While Metro already has an internal Site Acquisition Program and Transit Oriented Development program which supports Metro staff to acquire sites throughout the region based on certain site criteria, local developers also suggested allowing development teams to leverage Metro funds to acquire sites. One concern associated with granting Metro funds to developers for site acquisition is the deal terms and what happens with the land after a certain period without project feasibility. It is common, however, for local jurisdictions to require that the land ownership returns to that local jurisdictions if the project does not break ground over a short period of time. This indicates a need for Metro underwriting and staff review should Metro allow funds to be used for land acquisition outside of the internal Site Acquisition Program.

Policy Cost Impact: Similar to other programs, using Metro funds for land acquisition does not directly result in significant cost savings, but rather allows Metro to influence the location of affordable housing projects throughout the region and prioritize projects that meet certain geographic goals.

Development Costs

Development costs are the primary driver of the required gap funding. With increasing development costs comes the need for higher levels of public gap funding. Several jurisdictions throughout the Country, including New York and San Francisco, are analyzing methods for reducing development costs through a mixture of using existing public resources, reducing jurisdictional fees, and supporting the construction industry in hopes of achieving future cost savings.[2]

Identify and Leverage Public Land

Policy Description: Publicly-owned land, whether under the ownership of a City, County, school district, or other special district, represents an opportunity to support affordable housing production. Most commonly, public land is contributed to a project for a discounted price in order to subsidize affordable housing development. A recent trend in publicly-owned land is identifying sites owned by other public entities that are less connected to the affordable housing world. Cities and regional entities are working to identify these sites and coordinate with partner jurisdictions to collaborate on potential housing development plans.

Context for Metro: Several regional entities, including cities and transit providers, are leveraging land to support housing production. Metro should identify ways to support

[2] San Francisco Housing For All Plan is available at: https://www.sf.gov/news/mayor-breed-and-board-president-peskin-announce-housing-fee-reform-plan-advance-accelerate-and

development on these sites to further incentivize the use of public land for affordable housing. The other way for Metro to support leveraging public land is to identify other sites that are under ownership by entities not commonly involved in housing production. These may include school districts, utility districts, park and recreation districts, among others. Metro could reserve a portion of funds to support developments on existing publicly-owned sites recognizing these sites will likely have a lower acquisition cost and will lead to a more efficient use of gap financing.

Policy Cost Impact: Based on the 2018 Metro bond portfolio, the average land cost was roughly $15,300 per unit. Assuming Metro can identify existing publicly owned sites that can be contributed to the projects at a significantly reduced cost, these projects could realize average cost savings of between **$10,000 and $20,000 per unit.**

Support SDC and Other Fee Waivers or Deferrals

Policy Description: Local System Development Charges (SDCs) and other local fees contribute to the cost of building affordable housing projects. Many jurisdictions throughout the Country are offering fee waivers or deferrals for affordable housing projects that meet certain requirements, including affordability level and non-profit ownership. By reducing local fees, local jurisdictions are reducing the project costs that require gap financing from state and regional funding agencies. However, these local jurisdictions often rely on these SDC fees to support necessary infrastructure upgrades to best serve their communities, so the fee waivers and deferrals must be sensitive to local funding needs. In fact, interviews with smaller local jurisdictional partners did identify challenges offering these waivers due to the need for funding to support local capital improvement projects.

Context for Metro: Several jurisdictions in the Metro region offer SDC and other fee waivers for affordable housing developments, while others have identified SDC waiver and deferrals as future actions to support affordable housing production.[3] Metro could consider allocating a portion of funds specifically to jurisdictions with fee waivers and deferrals in order to use gap funds more efficiently. It is also worth noting that the State has identified infrastructure as a major target for investment to support housing production. Should funds be made available to support local jurisdictional infrastructure needs from the State, jurisdictions will be less reliant on SDC revenue and may then support SDC waivers to meet affordable housing production goals.

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[3] According to the 2022 Annual Report of the Metro Affordable Housing Bond Program, the following cities offer SDC waivers for affordable housing: Beaverton, Happy Valley, Hillsboro, Portland, Tigard, Lake Oswego, and Wilsonville. Available at: https://www.oregonmetro.gov/sites/default/files/2023/06/13/2022-Metro-Housing-Bond-Annual-Report-06-01-23_0.pdf

Policy Cost Impact: While SDCs vary throughout the region, stakeholders noted SDC waivers can save between **$10,000 to $25,000 per unit** depending on location and project size.

Support and Increase the Construction Workforce

Policy Description: Intended to improve production over a longer-term, several jurisdictions are investing in construction workforce training programs and supporting the growth of small and minority-owned construction firms. The intent is to build a larger workforce that can deliver more units faster and to support equitable economic opportunities through the construction trades. Supporting the growth of the regional construction workforce could lead to cost reductions due to the adequate supply of construction labor.

Context for Metro: As part of the 2018 Bond program, Metro established contracting equity goals to support certain business types. In fact, according to the 2022 Annual Bond Report, approximately 24.7 percent of all construction collars were paid to businesses certified by the State of Oregon Certification Office for Business Inclusion and Diversity. Metro may consider continuing or increasing these investment requirements that support these types of firms. In addition, Metro may consider investing in and collaborating with local colleges and universities to offer construction workforce training to expand our local workforce and further aligning with existing Metro programming like the Construction Career Pathways program, spearheaded by its the Diversity, Equity, & Inclusion department.

Policy Cost Impact: In the near term, efforts to expand the construction workforce may not immediately result in cost savings. However, the effects could be realized over the long term as there would be a sufficient supply of skilled labor to meet housing production goals.

Support Innovation in the Construction Industry

Policy Description: Several jurisdictions throughout the country are exploring housing development innovations intended to lower the cost of housing production. Most notably for affordable housing is innovations like modular housing and mass timber, among other cost reducing practices and materials. These innovations are intended to decrease housing costs through expedited development timelines and the use of more cost-efficient materials. The innovations will take time to integrate into the development environment and achieve the desired cost savings, but local support can help these innovative technologies gain traction and begin to achieve cost savings.

Context for Metro: According to stakeholder interviews, there is interest in both modular housing and mass timber developments in the region. Metro could consider supporting these innovations by reserving funds or prioritizing projects that offer innovative solutions to housing production. While these innovations may not yield cost savings in the early projects, the expectation is that the cost savings will be achieved when the technology is fully adopted and integrated into the development process.

Policy Cost Impact: The near-term cost impact is likely limited, but the potential long-term cost savings through innovation will result in reduced public funding requirements.

Operating Costs/Subsidies

Operating costs impact the amount of supportable debt a project can support, indicating that any action that decreases operating costs or increases operating revenue will reduce the amount of required upfront gap funding. In addition to potentially increasing the ability for projects to support debt, operating subsidies can also play a critical role in supporting units at deeper affordability levels, including permanent supportive housing. Stakeholder interviews highlighted the need for more operational subsidies to stabilize existing properties and allow future projects to provide the necessary resident and supportive services to best serve residents.

Pursue Property Tax Abatement Programs

Policy Description: Property taxes increase a property operating budget, leading to a lower supportable permanent mortgage amount and higher amount of required gap funding. To reduce ongoing property costs, many jurisdictions offer property tax abatement to affordable housing projects.

Context for Metro: According to a 2022 survey of Metro jurisdictions, roughly half of the jurisdictions in the region provide some form of property tax abatement for affordable housing projects. Metro may consider reserving funds or prioritizing developments in those areas as a way to more efficiently use Metro funding and incentivize jurisdictions to offer a property tax abatement program for projects that include affordable housing units.

Policy Cost Impact: By providing property tax abatement, estimated at roughly $1,500 per year for a multifamily development, a project could support an additional debt amount of roughly **$10,000 to $15,000 per unit** depending on the unit type and loan terms.

Provide Operating Subsidies

Policy Description: Rather than provide upfront capital, some jurisdictions offer operating subsidies to cover operating expenses and resident services for specific property types. This is particularly associated with permanent supportive housing, with programs like San Francisco’s Local Operating Subsidy Program (LOSP). Often, this is intended to strictly cover operating deficits for deeply affordable units, although providing a higher subsidy amount with a long-term agreement would allow a project to take on additional permanent debt and reduce the required public gap funding amount per unit.

Context for Metro: Metro currently provides operating subsidies through the Regional Long-Term Rent Assistance (RLRA) program in both tenant-based and project-based subsidies. These funds are paid through the Supportive Housing Services (SHS) funding and are intended for units with deep affordability levels. Metro could consider increasing the RLRA subsidy and extending the committed term of the subsidy to allow leveraging of the revenue for upfront capital. Alternatively, Metro could consider allocating potential new funding to an operating subsidy program aimed at specific income levels and population types. Using SHS funding in this way would require changes to extend or eliminate the current scheduled sunset of the measure in 2030.

Policy Cost Impact: The impact of operating subsidies depends on the subsidy amount, length of subsidy guarantee, and whether the subsidy is intended only to cover typical operating costs and resident services or provides excess cash flow that can be leveraged to take on additional debt.

Support Existing Properties with Operating Challenges

Policy Description: While the majority of actions and policies presented in the memo support new development projects, it is worth noting that a significant number of local stakeholders highlighted operating challenges in existing buildings throughout the region. According to interviews, the cost of managing and providing services to affordable housing projects in the region has increased significantly. For many projects that rely on rental revenue to support debt payments and ongoing building operations, the increasing operating costs have led to a negative net operating income for recent years. Properties with negative net operating income can rapidly spiral into disrepair and insufficient services for vulnerable populations. To combat these cost savings and potential long-term building impacts, Metro could dedicate future funds to help stabilize existing properties.

Context for Metro: Any program that supports existing properties will reduce the capital available to support new affordable housing projects. However, local stakeholder interviews indicated a significant need to help stabilize these properties and support local non-profit affordable housing development and management companies that are losing money due to increasing operating costs in the region. Metro could earmark funds for specific project needs, such as building improvements, added security systems, and any other improvements that will reduce ongoing operating costs or help stabilize the property. This approach is likely more efficient than committing to providing ongoing operating subsidies to properties.

Policy Cost Impact: Every property has unique operating challenges, so the cost impact to help stabilize will differ significantly by project.

Appendix D: Market Incentives, Actions, and Policies to Support Affordable Housing Production Memorandum, BAE Urban Economics

Land Use Authority and Development Standards

Local jurisdictions, through their land use authority and development standards, influence the ability and support for delivering affordable housing. This includes the ability to craft policies that support the provision of affordable housing alongside market-rate development, adjusting local development standards to remove barriers to project feasibility, and supporting innovative housing typologies to further reduce the cost of construction.

Implement Inclusionary Housing Requirements

Policy Description: One tool to support affordable housing is to require that any new residential developments restrict a portion of the units for affordable housing, also called inclusionary housing. The policy often allows for alternative delivery methods, including off-site construction and land dedication. Through the inclusionary housing program, local jurisdictions can stimulate affordable housing production with limited public resources. However, market-rate projects must be feasible in order for the local jurisdiction to receive any affordable units, indicating the policy must be crafted to balance affordable housing production and overall project feasibility.

Context for Metro: Local jurisdictions approve inclusionary housing ordinances, leaving Metro with limited influence over whether a jurisdiction has program or not. In addition, the intent of inclusionary housing is to require some affordable units within market-rate buildings without public subsidy. Therefore, Metro funding would not necessarily be impacted by inclusionary housing program, except if jurisdictions allowed off-site construction or land dedication, in which case a 100 percent affordable building may be delivered.

Policy Cost Impact: Inclusionary Housing would have limited impact on the overall gap funding amount needed to support housing production, but it may provide opportunities for land dedications or bigger off-site production which would likely result in a project that could leverage Metro funding to support a greater number of units.

Support Revisions to Local Development Standards

Policy Description: To combat rising development costs and changing market conditions, some local jurisdictions have recently revised local development standards to improve the overall economics of residential development projects. These revisions include increased zoning to allow more units, lower automobile and bike parking requirements, adjusted ground floor use requirements, permit streamlining, and relaxed design standards, among others. Individual policy and development standard adjustments may not result in major cost changes; however, collectively, a set of regulatory adjustments can reduce costs by a significant margin which will lower the required public funding gap per unit. For example, the Portland Bureau of Planning and Sustainability (BPS) recently approved a package of regulatory reforms aimed at reducing the cost of building housing in Portland. While the approved regulatory reforms adjusted based on City Council feedback, an initial study of potential regulatory reforms found that adjusting just four local policies could decrease the cost of building multifamily housing in Portland by between $10,000 and $40,000 per unit.[4]

One particular local requirement that dramatically increases the cost of providing affordable housing is a requirement of commercial space on the ground floor. Based on the Oregon Bureau of Labor and Industries (BOLI) standards, any affordable housing building with ground-floor commercial space is subject to pay higher wages for all building construction labor. By waiving the ground-floor active use requirement for affordable housing projects, the total development cost of the project would decrease considerably, leading to a lower required public subsidy amount. Furthermore, the BOLI wage requirement also limits projects' ability to easily co-locate partnering services such as health clinics or childcare centers that serve the broader community within buildings, impacting feasibility of these types of amenities, which would be a benefit to many supportive housing residents.

Context for Metro: Changes to local development standard changes will require local jurisdictions to pursue and approve adjusted policies. Metro could provide technical assistance to help local jurisdictions understand the cost impact of certain local policies. Similarly, Metro could reserve funding for local jurisdictions that have approved cost-saving regulatory changes to support housing production.

Policy Cost Impact: While the impact of local policies and development standards differ throughout the region, it is reasonable to assume cost savings of between **$10,000 and $40,000 per unit** be realized, similar to the Portland housing development cost study.

Project Delivery Timeline

Recognizing the cost of a longer project review and approval process, many jurisdictions and affordable housing funders are attempting to reduce the time for an affordable housing project to receive local approval and apply for the various financing sources necessary to develop the project.

Align Financing Timelines and Application Requirements

Policy Description: Some local and regional jurisdictions that provide capital for affordable housing projects are structing their financing allocation processes to align with State timelines and requirements. Given State departments often control the majority of affordable housing funding, including LIHTC, bonds, and state-specific gap financing programs, other funding partners can decrease the complexity and length of

[4] Residential Development Cost Analysis – BAE Urban Economics – Jan. 4, 2024. Available at: https://www.portland.gov/bps/planning/housing-regulatory-relief/documents

receiving all of the required funding sources by aligning with the State process. This includes the timing of local funding awards as well as the requirements. In terms of timing, it is most efficient for a project to apply and receive their funding allocations within a shorter period of time, allowing the project to be under construction rather than waiting for additional funding allocations. Similarly, it is significantly easier for affordable housing developers to compile funding applications if each funding source has similar or identical application requirements, especially with financial models for project underwriting.

<u>Context for Metro:</u> The most common input from local stakeholder interviews is a need for Metro to collaborate with Oregon Housing and Community Services (OHCS) to align project goals, applications requirements, funding timelines, and definitions. Given OHCS has an estimate of the potential State funding that will be available for the Portland metro region, there is an opportunity for Metro to facilitate collaboration with OHCS and reduce the time burden of multiple funding sources requiring multiple applications on different schedules. It would be even more impactful if OHCS and Metro collaborated on a single project application for projects seeking OHCS and Metro dollars. By limiting the amount of time and level of effort required by local affordable housing developers to submit various applications for various funding sources, Metro and other funding partners can expedite the approval process and get more units built in a shorter amount of time.

<u>Policy Cost Impact:</u> Aligning funding timelines and requirements may reduce costs by shortening the project's hold period, however the main benefit is reducing the level of effort for affordable housing developers to seek the required funding sources and instead focus on delivering the projects and producing more units than under the current structure.

Support Local Permit Streamlining

<u>Policy Description:</u> Another challenge associated with delivering affordable housing is the local approval process timeline. The review and entitlement process can take several months, which adds costs through accrued interest and additional soft costs, and it can also lead to higher costs than originally budgeted due to increases in the cost of labor and materials while the project seeks local approvals. While slightly less important for subsidized affordable housing, the approvals process also adds risk to a project, which increases developer and investor return requirements. For example, in the City of Los Angeles, a recent program, called ED-1, mandates that developers building affordable housing, defined as below 120 percent of the Area Median Income, are given approvals within 60 days of project submission. The intent was to reduce the time for subsidized affordable housing projects built by non-profit organizations. However, in practice, the guaranteed expedited review time led to several market-rate developer applications who were willing to build housing with slightly discounted rents and sale prices in return for a guaranteed approval process and fast timeline. This

indicates the benefit of a transparent and fast approval process, which translates into cost savings and reduced risk to the developer and investor team.

Context for Metro: Given Metro has limited control of local approval processes, the main mechanism for supporting local permit streamlining is to prioritize a portion of funds for projects in jurisdictions that have committed to an expedited local approval process. If Metro prioritizes funding for certain jurisdictions, however, it may not achieve the distribution of affordable units throughout all jurisdictions in the region. Alternatively, Metro could provide technical assistance in demonstrating the benefit of a faster approval process or provide funding to jurisdictions in order to hire additional staff to support project reviews.

Policy Cost Impact: A faster approval process reduces risk and will save a modest amount of costs associated with a typical project entitlement process, especially with rapidly increasing development costs. However, each project is unique and the most significant benefit of a faster approval process is a faster delivery of affordable housing units.

Technical Assistance

Metro can support the affordable housing industry and local jurisdictions by providing technical assistance. Technical assistance can support a range of entities involved in the affordable housing ecosystem, including emerging developers interested in supporting communities through affordable housing, as well as local jurisdictions that may benefit from understanding the affordable housing development process and ways local jurisdictions can support housing production.

Provide Technical Assistance to Emerging Developers and Property Owners

Policy Description: Affordable housing developers have a range of skills and institutional knowledge within development teams and property owners. Emerging developers that have an interest in producing affordable housing may benefit from technical assistance in understanding the full scope of navigating the affordable housing finance and development process. In addition, as new regulations, financing sources, and investment targets shift at the federal, state, and local level, a regional government could provide ongoing technical support to emerging developer teams on the methods to produce competitive projects that meet the specific targets of public funding sources.

Context for Metro: As a regional entity, Metro has the unique ability to support the regional affordable housing development ecosystem through the provision of technical assistance. Metro may not necessarily need to allocate a significant amount of funds to a technical assistance program, but these investments may support and diversify the existing inventory of affordable housing development teams in the region.

Policy Cost Impact: Assuming technical assistance supports new affordable housing developers, this investment may not decrease the cost of housing production directly, but will increase the unit production potential throughout the region and may support developers who are currently underrepresented throughout the region.

Provide Technical Assistance to Local Jurisdictions

Policy Description: Many local jurisdictions struggle to support affordable housing within their communities for a range of reasons. Some jurisdictions are simply too small and under-staffed to adequately underwrite affordable housing deals. Similarly, many staff within local jurisdictions do not have expertise in affordable housing finance and do not have the adequate skillset to identify mechanisms for supporting affordable housing in their communities. Given this, a program aimed at increasing the knowledge of affordable housing finance and operations within local jurisdictions can ensure staff and policy makers understand how local policy impacts affordable housing construction. In some examples, technical assistance grants are provided to help communities update land use codes and conduct analyses that support housing development. In other cases, the technical assistance can take the form of a multi-day workshop for jurisdictional staff to understand affordable housing finance and development.

Context for Metro: Metro could convene jurisdictional partners to organize a series of technical assistance programs aimed at increasing the general knowledge of affordable housing, including the finances, operations, and unique property attributes that lead to the best outcomes for residents. Metro could consider prioritizing a portion of potential future funds for projects in jurisdictions that have sent staff to participate in an organized technical assistance workshop around affordable housing development.

Policy Cost Impact: This investment may not directly lead to cost savings, but it may highlight potential policies and actions outlined above that local jurisdictions can enact in order to support affordable housing, which translate into direct cost savings.

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ECOnorthwest

Date:	May 15, 2024
To:	Melissa Arnold, Daisy Quiñonez, and Emily Lieb, Metro
From:	Erik Bagwell and Amanda Ufheil-Somers, ECOnorthwest
Subject:	Task 1.2 Inventory and Cost Analysis of Conversion Opportunities

Purpose and Background

Since the passage of the Metro Bond in 2018, Metro has invested $662 million into expanding affordable housing within its service area. Metro's bond measure has funded 4,361 new units of affordable housing, exceeding the original target of 3,900 units.

As Metro considers policy options to maintain progress toward meeting affordable housing needs in the Portland Metro region, acquisition, conversion and adaptive reuse projects can offer several benefits over new construction. In some cases, converting existing buildings can be more cost-effective than new construction to create regulated affordable units. This is especially true as the cost of construction for affordable housing—including materials, labor, and financing costs—increases. Conversions can also create housing faster than a typical ground-up development project, both in construction time and because of different permitting and review requirements.

ECOnorthwest's national scan of best practices highlighted important considerations for the conversion of underutilized assets to affordable housing, including identifying key criteria for evaluating three types of conversions: office-to-residential, market rate-to-affordable, and hotel/motel-to-affordable housing.

The contents of this memo outline ECOnorthwest's findings related to the availability and cost implications for each of these types of conversion opportunities in the Metro region.

Key Findings

- **Office conversion opportunities in the Metro region are limited and concentrated in downtown Portland. Successful conversions would likely require participation from the City of Portland to make the shift to residential use financially feasible, even at market rate rents. This includes waiving seismic upgrade requirements, SDC and CET waivers, IH waiver, and a tax abatement.**

- **The most promising opportunity for converting market rate housing may be among properties that are currently renting at prices between 60 and 80 percent of AMI. This is the largest segment of the region's multifamily housing stock, with an estimated per unit acquisition cost of about half the current cost of new construction for regulated affordable housing.**

- **Multifamily properties in the region built since 2010 are currently valued at between $186K to $335K per unit, a deep discount compared to the average cost of new construction.[1] Acquisition of existing new construction properties could serve as an opportunity to place regulated affordable housing in areas of the region that currently lack affordable housing opportunities.**

[1] CoStar value estimates of 3 to 5 star rated properties in the Metro region.

» Project Turnkey demonstrated that hotel conversions to temporary or transitional housing were possible at relatively low cost per unit. The potential for converting these—or additional—properties into long-term or permanent housing is uncertain.

Inventory and Cost Analysis

Office to Residential Conversions

Physical form is the most important factor in the potential for converting existing office buildings to residential uses. Commercial offices built over the last several decades tend to have large floor plates that provide greater space and cost efficiencies for office tenants but make the buildings difficult to adapt to the shallower depths needed for residential uses. Beyond these dimensional constraints, the cost of conversion can approach the cost of new construction for residential building types, creating additional challenges for an acquisition and conversion strategy, especially for regulated affordable housing.

Inventory

We identified approximately 2,300 office buildings in the Metro region larger than 5,000 square feet using property data from CoStar. Of this supply, we determined that 59 properties are physically suitable for office conversion given the size and shape of the floor plate, the total building area, and the available surface area for windows. More than half of these buildings are located in downtown Portland, as shown in Exhibit 1, with only five properties identified outside the City of Portland.

Exhibit 1. Summary of Office Properties Suitable for Conversion, Metro Region

Source: ECOnorthwest analysis of CoStar data

LOCATION	TOTAL PROPERTIES	TOTAL AREA (SF)	SMALLEST BUILDING (SF)	LARGEST BUILDING (SF)
Downtown Portland	34	2,608,500	30,400	223,400
Portland (other)	20	960,100	31,900	118,300
Beaverton	2	71,000	32,200	38,800
Wilsonville	2	79,000	38,800	40,200
Tualatin	1	53,600	–	–

Values rounded to the nearest hundred.

Beyond size considerations, conversions are more attractive for office buildings with fewer amenities (i.e., Class B and C properties) that rent at lower rates and have higher vacancy. Class B properties tend to be older Class A buildings. They are typically not in disrepair but are usually in less attractive areas of commercial or financial districts and offer fewer amenities than class A buildings. Class C office buildings, unlike either of the other property classes, are often located in less-than-desirable locations. They tend to be situated outside city centers, entertainment, and financial districts. Most Class C buildings are 20 or more years old and are in a state of disrepair. As a result, Class C buildings normally collect lower-than-average rents and have lower values.

Exhibit 2 summarizes aggregated lease information for office buildings in Portland, broken out by building class as defined by CoStar. Class C buildings in downtown Portland have the lowest rents among the observations, as well as the lowest occupancy rates.

Exhibit 2. Summary of Lease Information for Portland Office Properties, Metro Region
Source: ECOnorthwest analysis of CoStar data

PROPERTY TYPE	TOTAL PROPERTIES	AVERAGE OCCUPANCY	AVERAGE RENT (PER SF)	TOTAL AREA (SF)
Downtown Portland				
Class B	21	71%	$13.70	1,455,600
Class C	10	62%	$10.40	636,900
Portland (other)				
Class B	15	78%	$16.00	661,600

More granular identification of offices that might be better positioned for conversion is difficult without a site-specific analysis. Buildings that are fully leased by a single tenant may make for easier conversion compared to a building with lower occupancy, but multiple tenants with staggered lease expirations. Owners would also consider shifts in a building's assessed value compared to revenues in deciding whether to reposition or redevelop the property rather than waiting for more favorable market conditions. For any conversions to PSH, it is important to consider that office conversions may have comparable costs to developing new affordable housing depending on the age of the office building and scope of work required for conversion. Office buildings in Portland that have converted to either PSH or some other form of supportive housing (See Ankeny Square Apartments and the Henry Building on SW), have typically done so by creating SRO style units and shared common areas and utilizing existing restroom facilities as shared bathrooms. This approach saves on costs as re-plumbing an entire office building for individual in unit bathrooms is a meaningful cost in the overall conversion budget.

Cost Analysis

Conversion cost estimates vary based on a building's size, construction type (e.g., masonry, concrete), and configuration of the building systems, including the elevator and utility core. At a high level, per square foot conversion costs could range from about $300 to $450 per square foot. These costs cover only the "hard costs" of conversion, including materials and labor, but not the additional development costs of design, engineering, permitting, and financing. This range of costs also include the hard costs associated with seismic retrofitting required by City of Portland statute. Crucially, these estimates also assume the building is converted by the existing owner, at a $0 acquisition cost.

Converted office buildings in Portland would also be subject to the City's inclusionary housing policy, which requires a 20 percent set aside of units (or bedrooms) affordable at 80 percent of AMI or a 10 percent set aside affordable at 60 percent of AMI. City policy also offers an option to pay an in-lieu fee of $27 per square foot of building area. It is possible that Metro may choose an investment strategy that either seeks to incentivize the inclusion of regulated affordable units through the City's IH policy or supports conversions to 100% regulated affordable housing.

ECOnorthwest analysis for Prosper Portland estimated that converting downtown offices to market-rate residential uses could cost between $300 and $450 per square foot depending on the age of the building and the level of improvements required for the conversion. The study also found that conversions would require a suite of development incentives in order to deliver a return on cost aligned with market expectations. These incentives include:

- A 10-year property tax abatement

- Waiver of all System Development Charges
- Waiver of the Construction Excise Tax
- Waiver of the in-lieu Inclusionary Housing fee
- Waiver of the City of Portland's seismic retrofit requirements (for buildings that are not unreinforced masonry)

Among these incentives, the seismic retrofit waiver had the largest value.

Market Rate to Affordable Conversions

Rising interest rates and overall cost increases have created challenging conditions for financing new construction of any kind. At the same time, high interest rates have softened real estate asset values such that asking prices for market rate (i.e., unregulated) multifamily properties are well below the cost to construct a comparable building. There are several avenues to bring market rate multifamily properties under regulation as permanently affordable housing that can serve Metro's housing goals.

Newly Constructed Occupied Properties

Softened real estate asset values creates an opportunity for Metro and its partners to acquire properties built over the past decade or so at a discount compared to new construction. Such acquisitions offer opportunities to secure affordable housing in high opportunities neighborhoods (i.e., neighborhoods that based on research have a positive effect on economic mobility). They also create an opportunity to add to the stock of affordable housing at a much lower cost per unit than developing new affordable housing. In most instances market rate multifamily properties will be at least partially occupied. Units that are vacant could become automatically regulated affordable housing. Occupied units may have to convert to regulated affordable upon turnover. The additional income generated from the market rate units could help to leverage additional debt, potentially reducing the amount of Metro subsidy needed for acquisition

If acquiring occupied market rate properties to convert to PSH, Metro and its partners will need to account for similar considerations about what to do with the occupied units. Existing residents may voluntarily leave the units upon finding out about the conversion to PSH or they may not. Additionally, existing multifamily properties may not have the unit mix, common space, or office space that are often needed for PSH residents and the provision of onsite support services. Consequently, not all market rate properties may be appropriate for PSH conversions and even those that may have the right unit mix and sizes may still require property upgrades to provide office space for services and common areas for residents.

Unoccupied Properties in Construction

There may also be instances where Metro and its development partners have opportunities to purchase market rate multifamily properties currently in development and convert those to regulated affordable housing or PSH. Colliers data shared with Metro as of January 2024 indicate that there are approximately 44 market rate multifamily developments (6,367 units) under construction in the region units that could be available for purchase and conversion to affordable housing. If pursuing this strategy, Metro should consider that acquiring multifamily market rate developments under construction and converting to PSH may require intense evaluations of properties and developer proposals to provide adequate support services. Metro will need to evaluate whether the design and features of the property align with the needs of PSH residents and the provision of onsite support services and assess the level of property improvements needed for the property to convert to PSH. For example, PSH typically offers more studio, or 1-bedroom units and those units have design features informed through the lens of generational and lived trauma, and safety. Therefore, in unit improvements and unit reconfigurations may be needed post construction, which could prove very costly and may require additional subsidy beyond the cost of acquisition.

Naturally Occurring Affordable Housing (NOAH)

Existing conditions in the region's multifamily market offer opportunities to increase the supply of regulated affordable units with strategic investment—especially at properties where rents are currently affordable to low-income households—but would not add to the overall supply of housing needed to meet the Metro region's calculated needs. Acquiring distressed properties in areas in need of investment can support neighborhood stabilization (i.e., prevent displacement) and improve housing conditions while preserving affordable rents over the long term. Converting discounted properties in areas of higher opportunity to regulated affordable housing could also improve outcomes for residents and advance Metro's equity goals. There may also be opportunities to use Metro's resources to incentivize rent stabilization and/or regulation with incentives for existing owners, rather than through acquisition.

Many NOAH properties have below market rents because the physical condition of the properties cannot command higher rents and they often lack the amenities provided with new construction market rate properties. When considering the acquisition of such properties to either prevent displacement, preserve existing supply of affordable housing, or improve conditions, it is critical that Metro and its partners understand the existing resident population and their needs. Despite the lower rents at NOAH properties, existing residents may still be rent burdened and most likely qualify for rent subsidies and may need support services. A plan to offer support services, rent subsidies, and make any necessary improvements to the property should be in place before advancing an acquisition.

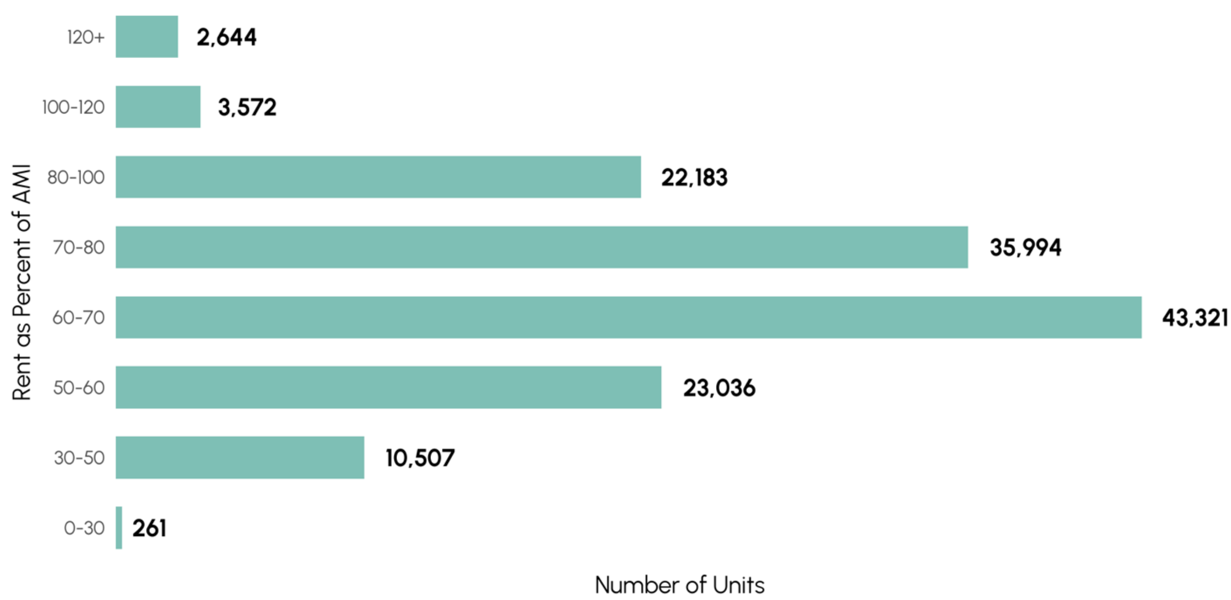
Inventory

Using data from CoStar, we identified a total of about 1,500 multiunit properties in the Metro area with 25 or more units that are not regulated by affordability covenants (i.e., have market rate rents). Of these records, approximately 1,400 properties (with a total of 141,518 units) had rental data for the purposes of estimating value and potential acquisition prices.[2]

Most apartments in the region are currently renting below what is affordable to a household of median income (adjusted by household/unit size. Exhibit 3 shows the distribution of units by how affordable they are relative to AMI. There are roughly 102,000 units currently renting at prices affordable to households earning between 50 and 80 percent of AMI. About 30 percent of this segment of multifamily housing stock rents between 60 and 70 percent of AMI.

[2] CoStar data does not always reflect up to date information but is generally more consistent and up to date with larger properties owned and managed by real estate investors (rather than local, small-scale owners).

Exhibit 3. Distribution of Units by Rents as a Percentage of AMI
Source: ECOnorthwest analysis of CoStar data



Cost Analysis

To estimate potential acquisition prices, ECOnorthwest calculated a net operating income for each property using current rents. We assumed an observed regional vacancy rate of 6 percent and estimated annual operating expenses (including property taxes) at 33 percent of gross revenue. Each property was assigned a capitalization rate based on the star rating—a CoStar measure of property quality—between 5.1 and 5.9. This range is relatively conservative and aligns with observations for recent transactions.

The range of estimated acquisition prices for existing units is shown in Exhibit 4.[3] Even for units renting near the top of the market, prices are generally less than the average per unit costs for affordable housing. Across the Metro bond portfolio, the average per unit cost is $420,000. Projects currently under construction in the City of Portland average about $505,000 per unit, and projects in the planning stages trend higher. For apartments currently renting at prices affordable to households between 80 and 100 percent of AMI, the per unit acquisition price is close to half the cost of new affordable housing construction, at a median price of $280,900.

[3] Per unit prices at the lowest end are likely an underestimate due to the limited observations (7 properties) and the likelihood that CoStar's data on average rents for those properties are out of date.

Exhibit 4. Range of Estimated Acquisition Prices Per Unit, by Current Rents as a Percentage of AMI

Source: ECOnorthwest analysis of data from CoStar.

	0-30 AMI	30–50 AMI	50–60 AMI	60–70 AMI	70–80 AMI	80–100 AMI	100–120 AMI	120+ AMI
Minimum	$73,900	$85,400	$134,700	$156,000	$203,000	$226,000	$295,000	$381,600
Median	$85,100	$134,800	$172,100	$206,100	$238,300	$280,900	$352,000	$441,800
Maximum	$92,700	$173,900	$242,700	$279,900	$297,000	$369,600	$450,700	$726,100

Values rounded to the nearest hundred.

Hotel/Motel Conversions

Oregon's Project Turnkey has demonstrated the potential for adapting hotels and motels into emergency shelter, transitional housing, and PSH. While such conversions can be completed at much lower costs compared to purpose-built construction, they may also involve potentially substantial rehabilitation costs to bring older non-residential buildings up to current standards, as well as zoning issues due to the change in property use. Long-term ongoing subsidies are also a significant need and challenge for properties offering supportive housing. Because of these considerations, hotel/motel conversions are likely best suited to transitional or shelter housing rather than conversion to permanent affordable housing.

Inventory

Using data from CoStar, we identified 253 hotel and motel properties in the Metro region. Properties at the higher end of the hospitality market and are less likely to be available for conversion to affordable housing. Excluding the upscale and luxury segments, as categorized in CoStar, the Metro region has 171 hotel and motel properties with a total of roughly 13,000 rooms.

Exhibit 5. Summary of Hotel Properties by Class, Metro Region

Source: ECOnorthwest analysis of CoStar data

PROPERTY CLASS	NUMBER OF SITES	MEDIAN ROOMS PER SITE	TOTAL ROOMS
Economy	85	36	3,520
Midscale	32	98	3,250
Upper Midscale	54	102	6,330
Total			**13,100**

Economy hotels (e.g., Motel 6, EconoLodge, Super8) are the most numerous but tend to be smaller sites, while midscale (e.g., ExtendedStay America, Best Western) and upper midscale (e.g., Hampton Inn, Holiday Inn) hotels tend to be larger buildings with interior corridors. Some midscale hotels such as ExtendedStay America have in unit kitchens which are an attractive feature for converting to transitional housing or PSH. Upper midscale hotels also likely offer amenity spaces such as meeting rooms that could be converted to office and other common areas that can be used for the provision of onsite support services.

Existing Project Turnkey sites in the Portland Metro region provide guidance on the kinds of conversions that could be opportunities for future investment of Metro funds. Exhibit 6 summarizes details of the seven Metro region hotel conversions completed (or underway) with funds from Project Turnkey 1.0 and 2.0.[4] These properties are primarily operating as temporary or transitional housing, though some owners intend to convert the properties to permanent housing in the future.

Exhibit 6. Project Turnkey Sites, Metro Region

Source: Oregon Community Foundation

PROJECT NAME	OWNER/OPERATOR	CITY	UNITS	TYPE
Ponderosa Inn	College Housing NW	Gresham	74	Transitional*
Bridge to Home	Family Promise of Tualatin Valley	Tigard	115	Transitional
Casa Amparo	Centro Cultural	Forest Grove	21	Transitional
Bridge Shelter Program	Housing Authority of Washington County	Hillsboro	61	Temporary, planned conversion to PSH
Rockwood Tower	Rockwood CDC	Gresham	75	Temporary / Transitional
River Haven	Central City Concern	Portland	70	Transitional
Stark Street Shelter	Joint Office of Homeless Services	Gresham	43	Temporary / Transitional

* Student housing meets the state's definition of transitional housing, though these units will operate much like permanent housing.

Across the statewide Project Turnkey portfolio, property sizes and required features or amenities were largely driven by the needs of the population served and existing acquisition opportunities. For example, some operators insisted on exterior corridors for ease of resident access while for others, interior corridor buildings were a priority for resident security..[5] Other operators highlighted the need for onsite office space and shared kitchen areas needed for the provision of onsite support services for residents. In the Metro region, properties ranged from 21 units to 115 units—the largest acquisition among all Project Turnkey sites. The scale of the Bridge to Home site required Family Promise to bring in other funding sources beyond Project Turnkey dollars in order to execute the acquisition.

Cost Analysis

ECOnorthwest was not able to estimate values and potential acquisition costs for regional hotel properties on a per building basis without purchasing revenue and occupancy data. With existing data, there is too much variation in the conditions and amenities of properties, even within broad class categories, to create useful estimates about value and purchase prices under current market conditions.

Considering market trends at the regional level, however, occupancy rates and revenue have generally rebounded from the period of reduced travel during the COVID-19 pandemic, when many Project Turnkey sites were acquired. The administrators of Project Turnkey funds at Oregon Community Foundation noted that prices in 2020 and 2021 during the first round of acquisitions were not as low as expected, given the overall decline in the tourism economy. Many of these properties were serving as

[4] Under the revised program rules for Project Turnkey 2.0, the Urban League of Portland received a grant to acquire a 7-unit multifamily building for use as transitional housing for women exiting incarceration. We do not include this property in the summary and cost analysis because of its different building type and market value.

[5] Interview with Oregon Community Foundation.

long-term residences for housing-insecure households and had relatively stable demand through the early years of the COVID-19 pandemic. When considering an acquisition, plans should be in place to engage the existing resident population and ensure that they either have the support they need to remain housed onsite or to be relocated to potentially more suitable regulated affordable housing for their household size, composition, income, and level of support service need. Additionally, there is disagreement among operators as to whether motels and hotels are suitable as PSH. Some believe they work well as emergency shelters with additional support services, thus providing an important step for households transitioning out of homelessness but the motel layout and design is less than ideal as PSH. Others believe that if the operations and services are run well, motels and hotels can work as suitable PSH.

Exhibit 7 summarizes the total and per unit costs for the Project Turnkey sites in the Metro region. These state funds covered acquisition and renovation costs, though some projects—such as Bridge to Home in Tigard—may have brought in additional sources to cover the total development costs of conversion.

Exhibit 7. Total and Per Unit Development Costs of Project Turnkey Sites, Metro Region

Source: ECOnorthwest analysis of data from Oregon Community Foundation

PROJECT NAME	OWNER/OPERATOR	CITY	GRANT	UNITS	COST PER UNIT
Ponderosa Inn	College Housing NW	Gresham	$6,600,000	74	$89,189
Bridge to Home	Family Promise of Tualatin Valley	Tigard	$10,200,000	115	$88,696
Casa Amparo	Centro Cultural	Forest Grove	$2,200,000	21	$104,762
Bridge Shelter Program	Housing Authority of Washington County	Hillsboro	$6,200,000	61	$101,639
Rockwood Tower	Rockwood CDC	Gresham	$6,800,000	75	$90,667
River Haven	Central City Concern	Portland	$7,000,000	70	$100,000
Stark Street Shelter	Multnomah County	Gresham	$3,500,000	43	$81,395
Average					**$93,764**

Going forward, there may only be occasional opportunities to convert distressed or discounted hotel sites in the region to transitional housing. Central City Concern's recent purchase of the Lolo Pass hotel into a drug treatment facility is a recent example of such acquisitions conversions that are well suited for supporting extremely low-income households suffering with drug addiction. In some cases, sites may be better suited in the long-term for redevelopment, as with the Metro-owned Portland Value Inn on Southwest Barbur Boulevard. The hotel is currently in use as shelter operated by Multnomah County and Do Good Multnomah but will eventually be redeveloped by Community Partners for Affordable Housing,