

**CITY OF LOS ANGELES
PROPOSITION HHH
CITIZENS OVERSIGHT COMMITTEE**

To:	Proposition HHH Citizens Oversight Committee
From:	Miguel Santana, Chair Tunua Thrash-Ntuk, Vice Chair Nicholas Halaris, Member
Date:	November 9, 2018
Subject:	REPORT ON INITIAL RECOMMENDATIONS TO IMPROVE PERMANENT SUPPORTIVE HOUSING PROCESS AND FUNDING STRUCTURE

I. SUMMARY

Bold action is necessary for the City of Los Angeles (“City”) to solve its homeless crisis. Encampments continue to grow—and despite the \$1.2 billion bond approved in Proposition HHH (“Prop. HHH” or “HHH”) to develop housing and fund supportive services, there are valid concerns that improvements are coming at too slow a rate and costs run the risk of ballooning. At the same time, there is a public health emergency in our streets. The Los Angeles County Health Department has declared a typhus “outbreak,” and with conditions growing worse, the City recently designated a “typhus zone” in downtown Los Angeles near Skid Row, a well-known area where the homeless congregate.¹

On April 11, 2018, the City Council directed the Citizens Oversight Committee (“COC” or “Committee”) to make comprehensive recommendations to the Homeless and Poverty Committee to improve and expedite the City’s processes to build permanent supportive housing. This Report follows. Below, we offer an outline of 11 initial recommendations intended to improve how HHH projects are financed, developed, and ultimately utilized to achieve a maximum impact in the community. Of particular note, this Report focuses on the creation and implementation of a pilot program to reform, improve, and advance the ways HHH funds can and should be used, while also taking immediate action to help control and stop the typhus outbreak and prevent similar health emergencies in the future.

The recommendations presented here are intended to be a part of a continuing dialogue with the City, its departments, and the community to make progress in solving the homeless crisis. For this reason, the Committee is first forwarding this Report to the Los Angeles Housing + Community Investment Department (“HCIDLA”) and the Office of the City Administrative Officer (“CAO”) for review and comment. We respectfully request that HCIDLA and the CAO provide detailed written comments to this Report no later than December 14, 2018, at which time the Committee

¹ See <https://www.nbcnews.com/news/us-news/typhus-outbreak-los-angeles-county-surpasses-100-patients-n926496> (accessed Nov. 2, 2018).

plans submit recommendations for review by the HHH Administrative Oversight Committee (“AOC”). Upon the additional input of the AOC, we hope to transmit a final set of recommendations to the Homeless and Poverty Committee on or around January 2019.

II. RECOMMENDATIONS

As discussed in this section, the Committee developed several initial recommendations intended to improve the health and safety of the homeless, increase and streamline access to HHH funds, reduce project costs, expedite the delivery of projects, and encourage innovation. These recommendations fall into three general categories:

- The creation of a “Pilot Program” to spark the development of 1,000 units of permanent supportive housing within 24 months of project approval to address public health emergencies besetting the homeless;
- Changes to the “Call for Projects” Application Process and HHH Permanent Supportive Program Regulations (“HHH Regulations”) currently used by HCIDLA as a means to encourage more applications, more competition, and the reduction of project costs; and
- Various requests that HCIDLA and the CAO prepare reports on specific potential reforms that could be made within the City to revise local policies that create barriers to HHH-financed projects, or create new policies to assist parties interested in developing permanent supportive housing.

The Committee will remain available to answer any questions or clarify any recommendation should that be necessary.

Recommendation No. 1: **Declare State of Emergency and Create Pilot Program to Build 1,000 Units of Permanent Supportive Housing within 24 Months**

On May 31, 2018, the Los Angeles Homeless Services Authority reported that over 31,000 residents of the City are homeless. Meanwhile, it still takes three to five years to complete permanent supportive housing projects in the City.

The ramifications of the current housing backlog are materializing in a real way. In late 2017, increased reports of hepatitis A among the local homeless population forced the City to establish the “Skid Row Community ReFresh Spot,” a personal care center providing showers and toilet facilities—basic necessities that are not available to the homeless due to the lack of permanent supportive housing. These problems continued, resulting in a serious typhus outbreak in the City that followed in late 2018. This newest emergency, which is ongoing, forces the City to dedicate additional resources to stop the spread of disease and seek out state and federal

assistance. Stop-gap measures can only do so much to alleviate a homeless problem that has sparked outbreaks of hepatitis A and typhus.

In light of emerging threats to public health, this Committee recommends that the City declare a State of Emergency and develop a Pilot Program for the express purpose of building 1,000 units of permanent supportive housing—using HHH funds—under a streamlined “Innovative” Request for Proposals (“Innovative RFP”) that would be released with the next Call for Projects, with the goal of completion within 24 months of project approval.

As part of this process, we further recommend that the City create a select team of City representatives known as the “Red Team” to work with the COC, the AOC, and the City Council to administer the Pilot Program. *See Recommendation No. 2, infra.* Moreover, the Committee recommends the implementation of certain temporary changes to the HHH Regulations to facilitate the development of permanent supportive housing. *See Recommendation Nos. 3-4, infra.*

Recommendation No. 2: As Part of the Pilot Program, Create a “Red Team” to Expedite Project Delivery and Help Solve Public Health Emergencies Caused by the Lack of Housing

The expertise necessary to assist interested parties with the application, permitting, construction, and operation of permanent supportive housing is dispersed among various City departments. This decentralized approach, which is difficult at best for conventional developments, slows down the construction of permanent supportive housing at a time when immediate action is needed.

To advance the Pilot Program and consolidate subject matter expertise, we recommend the creation of a “Red Team,” led by the Mayor’s Office. The Red Team would further comprise representatives from the COC and departments deemed necessary by the Mayor and City Council.

As proposed here, the Red Team would administer the solicitation, procurement, and management of the 1,000 HHH-financed units approved under the Pilot Program, subject to the oversight of the COC, the AOC, and City Council. The Red Team would be responsible for reviewing applications and for providing developers with day-to-day support for HHH-financed projects, as a means to promote the speedy delivery of projects. At the culmination of the Pilot Program, we recommend that the Red Team prepare a report with written recommendations to improve City processes relating to HHH-financed projects.

Recommendation No. 3: As Part of the Pilot Program, Temporarily Eliminate Limits on Maximum Per-Project and Per-Unit HHH Contributions and Modify Limits on the Number of Projects Allowed per Developer

The existing HHH Regulations place a cap on project financing to “the lesser of 50% of total development cost based on final cost projections at the time of loan closing or \$16 million.”

There are similar per-unit contribution restrictions. The HHH Regulations also state that “[t]he maximum number of developments one entity, or its subsidiary(ies) can participate in at any one time is seven (7); of which a maximum of four (4) can be in pre-construction and a maximum of five (5) can be in construction and/or processing Final Close-Out.”

Prop. HHH does not place a cap on funding or limit the number of projects for which a developer may receive HHH financing. Such restrictions may be useful to ensure the widest distribution of HHH funds and to prevent an overconcentration of developers, but in the context of the Pilot Program, these limits could discourage rapid development or delay when a project begins, as developers are forced to seek additional funding from outside the City. Furthermore, such restrictions could prevent the City from establishing a core group of developers with expertise who can regularly develop projects quickly and efficiently.

For the pendency of the Pilot Program, the Committee proposes that the per-project and per-unit funding restrictions in the HHH Regulations be eliminated. By eliminating such restrictions for a comparatively limited number of projects (i.e., totaling 1,000 units), HHH funding can be used to close funding gaps on viable projects that are not moving forward simply because of City-imposed restrictions. Meanwhile, in order to incentivize cost control in a way that is consistent with current funding caps, we recommend interest rate incentives for developers to keep costs within per-unit restrictions of \$100,000, \$140,000, or \$400,000 per unit, depending on the project. *See Recommendation No. 4, infra.*

We also propose modifying the restriction on the number of projects that a developer may propose for HHH financing, allowing a developer to receive financing at any given time for seven projects (which is currently permitted under the HHH Regulations) or 500 HHH-financed units, whichever is greater. However, the limits on the overall number of units under development by an applicant may be waived upon the approval of the City. These changes would remain even after the completion of the Pilot Program.

Please see Appendix A at Sections 2.4 and 2.6 for additional details.

Recommendation No. 4: As Part of the Pilot Program, Create an Interest Rate Incentive Program That Aligns with the Goals of the Pilot Program and Program Priorities in the HHH Regulations

The City should provide financial incentives for projects that most closely align with the goals of the Pilot Program and the current Program Priorities in the HHH Regulations. This is especially necessary to ensure the expedited delivery of 1,000 units of permanent supportive housing in a 24-month period. Accordingly, during the pendency of the Pilot Program, we propose changes to the HHH Regulations to provide interest rate reductions for the following:

- Up to a 2% interest rate reduction for projects completed early;

- 2% interest rate reduction for partnerships involving properties owned by faith-based institutions, or by private landowners willing to provide long-term leases;
- 2% interest rate reduction for “Transited Oriented Developments”;
- 2% interest rate reduction for projects located in the highest, high, and moderate resource areas/census tracts in the City, as determined by the California Department of Housing and Community Development and California Tax Credit Allocation Committee’s Opportunity Mapping Tool;
- 2% interest rate reduction for projects located within 1/2 mile of a facility that operates to serve the population living in the development, including but not limited to a qualifying medical clinic that accepts Medi-Cal or Health Care for the Homeless payments or another entity that has an equally comprehensive subsidy program for low-income patients, or that operates near similar facilities delivering high-quality services designed to improve the quality of life for tenants;
- Up to a 3% interest rate reduction for projects leveraging tax credit financing by requesting 75%, 85%, or 95% less than the maximum HHH per-unit contribution permitted under the HHH Regulations;
- Up to a 3% interest rate reduction for projects at tiers of 15-20, 21-30, 31-40, 41-50, 51-60, or greater than 61 permanent supportive housing units;
- 2% interest rate reduction for non-tax-financed projects where permanent supportive housing is developed at a cost of no greater than \$140,000 per unit;
- 2% interest rate reduction for 4% Low-Income Housing Tax Credit (“LIHTC”) projects where permanent supportive housing is developed at a cost of no greater than \$140,000 per unit; and
- 2% interest rate reduction for 9% LIHTC projects where permanent supportive housing is developed at a cost of no greater than \$100,000 per unit.

An applicant could qualify for more than one of the aforementioned interest rate incentives, with the ability to reduce the total interest rate on a HHH-financed loan to a 1% floor. However, if the total development cost of a project based on final cost projections at the time of loan closing is less than \$400,000 per unit, then the City would provide a 0% loan.

Furthermore, the Committee recommends that the current 3% interest rate for HHH loans be reconsidered, and increased to 4%, to further encourage developers to submit applications for projects that meet the overall programmatic goals of the Prop. HHH.

Please see Appendix A at Section 1.10.2.2 for additional details.

Recommendation No. 5: Encourage Innovative Development Such as Modular, Prefabricated, or Manufactured Housing and the Construction of Accessory Dwelling Units

Given the need for housing and increasing construction costs, the City should incentivize different development methodologies. Modular, prefabricated, or manufactured housing has been identified by the community as an innovative way to reduce the per-unit cost of projects as well as expedite the delivery of housing. Likewise, interested stakeholders have promoted the development of Accessory Dwelling Units (“ADUs”) within the City as a solution to help address the homeless crisis. As a result, the Committee believes steps should be taken to more closely evaluate how to encourage modular housing, ADU development, and similar innovations.

The Committee we recommend that HCIDLA and the CAO take immediate action to modify the next Call for Projects to encourage the development of modular, prefabricated, or manufactured housing, or similarly innovative construction methodologies.

In addition, we respectfully requests that HCIDLA and the CAO prepare a report on (i) whether any revisions in the HHH Regulations could be made to promote the development of modular, prefabricated, or manufactured housing, similarly innovative construction methodologies, and ADUs; (ii) whether the HCIDLA architectural guidelines require any changes to make modular, prefabricated, manufactured or housing, similar innovative methodologies, and ADU construction easier, and the risks and benefits of waiving the application of such guidelines in the HHH Regulations; and (iii) whether any City land use permitting processes could be streamlined or modified to encourage modular, prefabricated, manufactured hor ousing, similarly innovative construction methodologies, and ADUs. A written report in accordance with the foregoing should be presented to the Committee within 30 days of this Report.

Finally, the Committee requests that HCIDLA and the CAO review and report on ways to incentivize (i) public-private partnerships between the City and modular, prefabricated, or manufactured housing unit manufacturers to open a facility in the City and mass produce a certain number of units (for example, by preparing an incentive package for a firm to relocate such housing manufacturing in the City that could include land, tax benefits, and a guaranteed order of units), and (ii) the development of ADUs. A written report in accordance with the foregoing should be presented to the Committee within 30 days of this Report.

Recommendation No. 6: Make Housing Easier to Finance and Build by Addressing Mandatory Federal, State, and City Requirements in the HHH Regulations That Slow Down the Development Process

The HHH Regulations incorporate certain requirements that are not required in Prop. HHH, or federal, state, and local law. Requirements based on health, safety, and important homeless housing policy considerations such as protecting public funds and ensuring social equity should be

given their due weight, but it may be appropriate to make self-imposed regulations waivable at the City's discretion, given the substantial impact that regulations have on cost and time.

First, the Committee respectfully requests that HCIDLA and the CAO, with the support of the City Attorney, conduct a thorough review of current federal, state, and City requirements in the HHH Regulations in order to distinguish those that are expressly mandated by law from those that are not. To the extent such requirements are mandated by law, we also request that HCIDLA and the CAO identify whether these requirements may be waived by the City Council or the responsible government agency. Similarly, City rules or processes that could be amended or waived in order to maximize density and increase the permitting of projects should also be investigated, with the submission of recommendations for improvement, if any. A written report in accordance with the foregoing should be presented to the Committee within 30 days of this Report.

Second, we ask HCIDLA and the CAO to prepare, within 30 days of this Report, a form to be included with the Call for Projects and permitting applicants to seek a waiver of any non-mandatory requirements included in the HHH Regulations. The waiver form should require the applicant to provide a written explanation for the need for a waiver and establish standards by which applicants could determine whether a waiver of requirements is appropriate. The waiver of any non-mandatory requirements would be determined based on the needs of a particular project.

Third, in the spirit of streamlining City processes, we recommend the deletion of Section 2.7 of the HHH Regulations, which requires a "Letter of Acknowledgement" from the City Councilmember who represents the location where a proposed project is situated as a prerequisite to HHH financing. The Committee received community input that this requirement, which is not mandated in Prop. HHH, results in delays. City Council approval is already required in order to approve HHH projects, so the requirement of a Letter of Acknowledgement from a particular member of the City Council appears to be unnecessary.

Fourth, the Committee respectfully requests that within 30 days of this Report, HCIDLA and the CAO submit to the Committee for review a "Request for Information" that would solicit input of the public, including developers and service providers, to identify the following:

- Requirements in the HHH Regulations that impede the delivery of projects;
- Requirements in the HHH Regulations that increase the cost of housing;
- Issues with City permitting processes that increase the time and cost for projects;
- Recommendations for the improvement of the "Call for Projects" application process;
- Recommendations to encourage innovative financing and construction methodologies for HHH-financed projects; and
- Any areas HCIDLA and the CAO believe are necessary to improve the HHH program.

Recommendation No. 7: Make Housing Easier to Finance and Build by Having the City Take a More Active Role in Assisting with Property Acquisition

Identifying suitable properties for development is critical to ensuring that permanent supportive housing is actually built. The Committee believes the City can play a more active role in assisting with the identification of properties, beginning with unused or underutilized property owned by the City or other government agencies.

The Committee recommends that HCIDLA and the CAO research and develop a list of all properties located within City limits that are owned by the City, the State of California, the County of Los Angeles, the Los Angeles Unified School District, and the federal government and currently eligible for the development of permanent supportive housing. The list would then be published for the public, with an invitation to developers to identify which sites they believe could be suitable for development. To the extent feasible, the City would assist in connecting potential public-private partners to facilitate property acquisition. We recommend that such a list be published weekly, with the first publication made no later than the end of the first quarter of 2019.

Recommendation No. 8: Make HHH More Accessible by Revising Applicant Eligibility Requirements

The current technical capacity and experience requirements for HHH applicants appear to be overly restrictive, discouraging private developers and property managers with experience in building multifamily projects. This could affect development regardless of the Pilot Program. Accordingly, the Committee finds that there is a need to revise the applicant eligibility requirements in the HHH Regulations to increase access.

First, we propose modifying requirements that focus solely on the experience of pre-selected HCIDLA developers or certain managing general partners, in favor of requirements that look to a “Development Team,” with a emphasis on opening HHH financing to developers that are well versed in developing projects with 10 or more units of permanent supportive housing.

Second, we propose that applicant eligibility be considered in view of persons with “Responsible Charge” of important elements of a project, defined as those “with independent and ultimate control and direction . . . over all decisions relating to the financing, construction, property management, identifying target populations, and provision of services on a project,” rather than according to current regulations which strictly require a managing general partner with 51% voting control over all aspects of a project.

Third, we propose that the eligibility requirements for property managers be based on the number of units managed by a person or entity, rather than the number of projects, along with similar changes to the HHH property management requirements.

Please see Appendix A at Section 1.4 for additional details.

Recommendation No. 9: Make HHH More Accessible by Permitting the Submission and Review of Unsolicited Applications, and Revise Project Eligibility Requirements

Currently, HCIDLA accepts applications only when there is a Call for Projects. In addition, the HHH Regulations impose project eligibility requirements that appear to go beyond the programmatic guidelines approved by the voters in Prop. HHH. While the Committee acknowledges the benefit of having staggered Calls for Projects and implementing additional requirements for project eligibility, these changes disincentivize projects, especially those funded through private resources. Developers may require faster decision making and do not want to be held to project eligibility requirements normally associated with tax credit financing.

The Committee proposes changes to the HHH Regulations to allow for the submission and review of unsolicited applications (i.e., proposals submitted outside of the fixed Call for Projects schedule) at any time. Please see Appendix A at Section 1.1 for additional details.

In addition, we propose establishing a set of minimum project eligibility requirements for non-tax-credit-financed projects in a way that more closely aligns with the HHH Bond Program Guidelines. Please see Appendix A at Section 1.5 for additional details.

Recommendation No. 10: Make HHH More Accessible by Encouraging More Non-Tax-Credit-Financed Projects

Private financing should be more central to the City’s overall strategy to development of HHH projects. Non-tax-credit financing structures should be encouraged. Furthermore, as indicated in connection with certain recommendations noted above, the HCIDLA Call for Projects and the HHH Regulations tend to utilize requirements that normally apply to tax-credit-financed projects and impose them on all projects, even if those projects are not receiving tax credit financing. This has the unintentional effect of imposing restrictions and burdens on applicants whose projects do not require tax credit.

We propose modifying the “Financing Structure” provisions of the HHH Regulations to clearly indicate that non-tax-credit financing structures will be considered. This includes the deletion of a requirement that “[a]pplications submitted to HCID for the first time under these HHH Regulations must be structured using tax-exempt bonds and 4% tax credits. . . .” HHH funds are not limited to tax-credit-financed projects. The Committee recommends that HCIDLA review all applications, regardless of whether the first application to HCIDLA is seeking 4% tax credit financing. Please see Appendix A at Section 1.2 for additional details.

In addition, the Committee respectfully requests that HCIDLA and the CAO conduct a thorough review of the HHH Regulations to separate requirements that are mandated for tax-credit-financed projects from those that are not. To the extent current HHH Regulations impose requirements on non-tax-credit-financed projects are not necessary, the HHH Regulations should be revised such that “Additional Requirements for Tax-Credit Financed Projects” are clearly

distinguished.² A written report in accordance with the foregoing, along with revised HHH Regulations, should be presented to the Committee within 30 days of this Report.

Recommendation No. 11: Reduce Construction Costs and Delays

While market conditions are a primary driver of construction costs, changes to the HHH Regulations could be made to encourage the reduction of construction costs or to expedite the construction process. As a result, the Committee recommends the following:

First, the competitive bidding requirements described in the HHH Regulations should be improved to encourage faster project delivery and cost savings. Accordingly, the Committee recommends changes to more clearly direct developers to seek out the lowest bids for general contracts, place limits on when developers or general contractors are required to solicit multiple proposals, place limits on when City approval is necessary for change orders, and establish a process to allow waiver of certain requirements where compliance will not result in significant cost savings. Existing construction cost audit provisions in the HHH Regulations shall remain in effect. Please see Appendix A at Section 3.7.4 for additional details.

Second, the Committee recommends that the HHH Regulations give developers the option of using fixed-price contracts. The HHH Regulations currently mandate the use of Guaranteed Maximum Price (“GMAX”) contracts “wherein the basis for payment is the cost of the work plus a fee.” While this is a common contract type in residential construction, it may not always be the best contract type for saving costs, because it incentivizes contractors to get to the maximum price in order to maximize their fee, even in cases when an owner attempts to cap costs. In some circumstances, a traditional fixed-price contract type may make sense when the plans for a project are fully developed prior to hiring a general contractor, because the contractor has a better basis for estimating construction costs. Please see Appendix A at Section 3.7.7.1 for additional details.

Third, the HHH Regulations should offer developers incentives to keep construction costs down. Accordingly, the Committee respectfully requests that HCIDLA and the CAO review the HHH Regulations and develop recommendations to incentivize developers to reduce construction costs. For example, if feasible, it may be advantageous to provide a fee bonus for certain projects that are delivered under budget. Similarly, stronger controls to reduce or prevent the use of construction contingencies may warrant investigation.³ A written report offering recommendations to address this issue should be presented to the Committee within 30 days of this Report.

² As an example, the Committee has prepared recommended changes to the HHH Regulations at Sections 1.5.1, 2.1, 2.3, and 2.11. See Appendix A. However, a more in-depth review is necessary.

³ The Committee has attempted to address this issue in part by recommending an interest rate incentive program during the aforementioned Pilot Program for projects that keep costs within certain per-unit limitations.

III. PROPOSED NEXT STEPS

As indicated above, there is an immediate need to implement the Pilot Program, along with the other recommendations made in this Report. With this in mind, the Committee proposes the following course of action:

- HCIDLA and the CAO shall submit all reports and other deliverables requested in connection with the recommendations above, such as a draft Request for Information soliciting input to improve the HHH program (*see* Recommendation No. 6, *supra*), no later than 30 days from this Report;
- HCIDLA and the CAO to provide review and written comments to the recommendations in this Report no later than December 14, 2018;
- The COC shall adopt recommendations at its next scheduled meeting on December 14, 2018 and submit to the AOC for review and approval;
- The COC plans to approve Request for Information soliciting input to improve the HHH program for immediate release;
- The AOC adopts recommendations at its next scheduled meeting in December 2018;
- Present recommendations to the Homeless and Poverty Committee in January 2018;
- Homeless and Poverty Committee to present recommendations to the City Council;
- City Council to declare a State of Emergency, request the formation of the Red Team led by the Mayor's Office, and approve any additional recommendations;
- Innovative RFP to be released no later than February 1, 2018, concurrent with the release of the next Call for Projects;
- Projects submitted under the Innovative RFP shall be approved with sufficient time to be included in the 2019 HHH Bond Issuance (expected summer 2019); and
- Projects approved under the Innovative RFP should be completed within 24 months of project approval by the City Council.

IV. CONCLUSION

No single approach will solve the homeless crisis. However, the City needs to incubate and promote creative ways to finance and develop permanent supportive housing. We hope that the Recommendations in this Report help achieve this goal. We look forward to the input of HCIDLA and the CAO.