July 8, 2025

RE: 2026 QAP Comments

Dear Ms. Kim Wilbourne:

We thank you for the opportunity to offer the following comments ahead of SC Housing's upcoming 2026 QAP:

- ***Minimum Hard Cost Requirement.*** We recommend that SC Housing look at either reducing the 65% hard cost ratio requirement, or removing altogether. With tap, impact, and permit fees increasing exponentially across South Carolina, it is becoming increasingly difficult to meet this requirement. Additionally, with the higher interest rates, and even more exacerbated on Tax-Exempt Bond developments that have more units and consequently longer construction timelines, construction interest is also heightened making this 65% requirement difficult to achieve. When the 50% test drops to 25% (and the difference is made up with taxable debt, which is likely), interest carry will further increase for TEB developments in future years.

  If SC Housing keeps the hard construction cost requirement in, we recommend 3 changes:
  - We recommend including tap, impact, and permit fees into the hard costs. These costs are out of the developer's control and are generally correlated with construction costs with permits being directly impacted by costs and the tap and impact fees being larger with more units and more bedrooms.
  - We recommend excluding land from both hard costs and total development costs for purposes of this calculation. It should be encouraged to seek lower cost land, or even to work with municipalities or other entities for a low-cost land lease. However, it becomes more difficult to achieve the 65% hard cost requirement with low land cost. Land cost is neither a hard cost nor a soft cost, and including the land cost in this calculation implicitly favors developments in some neighborhoods vs other neighborhoods. Conversely, it is worth noting that excluding land cost from the hard costs but keeping in the total development costs would have a similar but opposite effect, still favoring developments in certain neighborhoods. Removing from the calculation altogether alleviates this issue.
  - In conjunction with excluding land from hard costs, it would become necessary to adjust the 65% limit accordingly, and it would also become necessary to separate New Construction from Rehab to provide a limit that accurately reflects what should be reasonably achievable for a Rehab development.

- ***Tax-Exempt Bond (and State Tax Credit) Scoring.*** While we recognize that the state legislation on the state housing tax credit dictates that SC Housing "must establish uniform criteria for allocating the South Carolina housing tax credit to eligible projects pursuant to a competitive process that promotes highest value and greatest public benefit," we believe the manner in which this is promoted needs to be changed. As currently structured, the scoring for Tax Exempt Bonds and the State Tax Credits results in a Race-to-the-Bottom format that incentivizes cutting costs as much as possible, even below what is realistically achievable.

  From 2023 to 2024, the Tax-Exempt Bond request per unit for New Construction deals stayed about the same. However, from 2024 to 2025, the Tax-Exempt Bond request per unit decreased by about 10%. While that sounds like a success that is saving SC Housing resources, it is the opposite. This decrease implies that developments are being underwritten with costs that are 10% less than a year ago. Comparing market conditions from the application date in 2024 (or 2023) to the application date in 2025, 2025 faces higher costs (which are threatening to increase even further due to looming tariffs), lower equity rates (which are threatening to decrease even further with the reduction in the 50% test), and similar-to-marginally-lower interest rates. Overall, costs and the required Tax-Exempt Bond request from SC Housing should be equivalent or higher, not 10% lower. This suggests that the Race-to-the-Bottom scoring structure is encouraging developments to get underwritten with costs that are unrealistic for the purpose of receiving an award from SC Housing with the intent to figure out how to make the development feasible after an award, instead of including realistic costs that would be comfortable to close with. This could lead to lower-quality projects seeking lower costs or, even worse, projects that need to return funding allocations due to being infeasible. Both of these outcomes would decrease the public benefit of the state credits and the bond allocations.

  While the QAP is set up such that developments with costs outside a standard deviation from the mean could fail threshold, which in theory should protect against developments underwritten with unrealistically low costs, when every development does so, the mean moves lower and those developments pass threshold.

  We recommend 2 solutions that simultaneously should help curb the current Race-to-the-Bottom issue:

  - First, we recommend making item #4 of Bulletin #1 posted March 6, 2025 that developers with developments failing to close be suspended from participating in any SC Housing program for 3 years a permanent portion of the QAP moving forward. Of course, we recognize that there could be occurrences outside a developer's control that warrant a waiver of this penalty, but we believe anything within a developer's control that causes this failure to close should be subject to this penalty. We consider any underwriting issues, whether it is construction costs, equity rates, or interest rates, even if it is an unexpected change after the application, to be within the developer's control as it is within the developer's ability to provide buffer in the underwriting to safeguard against market disruptions.

- Second, we recommend SC Housing come up with a new method of enforcing cost reasonableness. There are a variety of ways this can be accomplished. One option could be to use recent Placed-In-Service applications that show actual incurred costs, adjusted by CPI from date of construction commencement to account for inflation, to compare to new applications to ensure costs are not too far beyond reason. A second option could be similar to a scoring component that North Carolina used as recently as their 2021 QAP. Essentially, they gave bonus points to developments that were within a certain percentage of the average credit per unit ask in the pools. If SC Housing were to give some priority to developments that are close to the average TDC per unit or TDC per square foot, that would be strong incentive to underwrite as realistically as possible with the goal being to fall in the middle instead of a Race-to-the-Bottom. If there was, say Priority "A" for developments within 5%, Priority "B" for developments outside 5% but within 10%, and Priority "C" for all others, SC Housing could keep the same scoring format they currently have, but commit to funding projects in Priority "A" first followed by "B" then "C". This would still meet the state housing credit requirement to promote greatest public benefit while ensuring it is done in a way that also promotes cost reasonableness.

- ***Tax-Exempt Bond (and State Tax Credit) Pools.*** Similar to the last comment of promoting cost reasonableness, we believe implementing 2 pools, one for New Construction and one for Rehab, is necessary. Under the current structure, Rehabs have significant advantages, even with the 10% scoring disadvantage, as Rehab developments can manufacture their construction costs (of course needing to stay within QAP requirements) in order to outscore other applications, both other Rehabs but more specifically New Construction projects that aren't able to manufacture construction costs by picking and choosing how substantial of a rehabilitation to complete.

  Because Rehabs score better, this also artificially drives up the cost of acquisition for these properties as developers, between sellers and brokers who know this to be the case, and developers competing for the same acquisitions. In turn, this actually serves to go against the state housing credit requirement to provide the most public benefit. A majority of the total development costs for rehabs is going into Acquisition instead of into hard construction costs. It’s very common to see Rehab applications where the hard construction costs are less than 30%. Hard construction costs would provide public benefit by putting new renovations into buildings that benefits the tenants who will live there. Meanwhile, acquisition costs simply benefit the original owner or developer providing no public benefit. Consequently, a Race-to-the-Bottom scoring structure that incentivizes Rehab developments while also incentivizing reducing costs is ultimately incentivizing developers to reduce the hard construction costs that go into the rehabilitation of these developments, putting a lot of state resources directly into the prior owners’ pockets, hindering public benefit.

While we believe it is ultimately necessary to add other regulations that help ensure that Rehab developments are doing a better job of benefiting the residents first and foremost, dividing New Construction and Rehab into 2 distinct pools that don’t compete against each other is a good first step.

Thank you for your consideration of these comments, and we look forward to working with the Authority to bring high-quality affordable housing to South Carolina.

Sincerely,

Parker Zee

Parker Zee, Vice President of Development
The Annex Group