Association of Bay Area Governments **Bay Area Housing Finance Authority**

Housing Committee **Oversight Committee**

October 8, 2025 Agenda Item 7.a.

BAHFA Strategic Planning

Subject:

Report and next steps regarding Module 3 of BAHFA Strategic Planning process, including design and launch of initial Mixed-Income Financing Program providing affordable housing tools while generating a reliable revenue stream to contribute toward BAHFA operational sustainability.

Background:

In June and July 2025, staff introduced the concept of a new Mixed-Income Financing Program to the BAHFA Advisory Committee and the joint meeting of the BAHFA Oversight and ABAG Housing Committees. The update provided an outline of draft program elements and criteria along with key considerations and next steps. Since that presentation, staff and the consultant team have continued to develop the concept by gathering additional stakeholder feedback and performing more extensive financial analysis.

This item provides an overview of the progress to date, potential program refinements based on the last several months of stakeholder engagement and due diligence, and next steps. To date, stakeholder engagement has focused on high-level testing of whether a program could accomplish BAHFA's stated goals under current market conditions. As noted elsewhere in this report, pending Committee direction to proceed with the program concept, the next phase will commence to determine more detailed components of program design, rollout, and administration.

The proposed terms referenced in this presentation and attachments remain preliminary, and may be updated following further staff analysis, feedback from policymakers and community partners, and/or future market conditions.

Module 3 Recap & Initial Conclusions

The purpose of Module 3 is to develop a new, regional project financing program. If feasible and subject to availability of funding, this program concept would allow BAHFA to launch a new financing product(s) prior to a future successful ballot measure, both demonstrating and testing BAHFA’s potential as a public lender and creating a stable revenue stream for the agency. Essential components of this effort would draw from current established BAHFA programs as well as introduce new elements, to provide a holistic menu of tools to affordable housing entities, and enhance the value BAHFA can provide toward the preservation and production of housing in the region.

Below is summary of the program elements discussed during the June/July meetings, as well as updates that reflect further analysis during the last several months:

- **Senior Lending Assistance**
  - Tax-Exempt Bond Issuance. BAHFA would offer its services as an issuer of various types of tax-exempt bonds. These tax-exempt bonds will help eligible projects and borrowers access long-term capital at rates lower than similar taxable financing sources, thus increasing potential senior loan proceeds and reducing financing gaps. Additionally, as an issuer of essential purpose bonds, BAHFA will add value to eligible projects as an owner, and under a 501(c)(3) bond structure as a partner with the owner.

    Update: Based on consistent feedback from stakeholders as well as financial modelling, this new program is expected to be a strong value-add opportunity by improving project feasibility as well as offering greater accessibility to tax exempt bond financing for many project sponsors.
  - Top-Loss Lending Partnership. To help serve projects for which tax-exempt bond issuance is infeasible (e.g., due to the project's proposed ownership structure or current market conditions), BAHFA could partner with a Freddie Mac lender to create a top-loss lending program. Such a program was initially projected to reduce the interest rate on the Freddie Mac senior debt by 30-50 basis points (0.30-0.50%).

    Update: While value would likely result from the reduction of interest rates and thus increase borrowing power, the capital required and elevated risk more than offset the projected benefit. As noted below, staff recommend dropping this component of the program.
- **Property Tax Abatement.** Building upon BAHFA's current Welfare Tax Exemption Preservation Program (WTEPP), the new proposal would involve enacting regulatory agreements necessary to achieve a property tax exemption. The reduction in annual tax burden will significantly reduce operating costs, thus increasing income available to pay debt service, resulting in increased potential loan proceeds. Further, under a governmental/essential purpose bond structure, property tax abatement could be applied to additional units above 80% AMI, to the extent that the public benefit of doing so outweighs public costs and subject to resolution of the possessory interest issue, providing deeper benefits to eligible projects.

  Update: There continues to be demand for this program and case study analysis has indicated it to be a powerful tool to achieve affordability while providing real public benefit.
- **Matched Subordinate Debt.** A key feature of the proposed program is for BAHFA to use its limited cash resources to match project sponsors' investment by providing subordinate debt to close the gap between required senior debt service coverage (DSC)

levels and 1.05x DSC on projects. One proposal currently under consideration is for BAHFA to size the interest rate on the subordinate debt at approximately 200 basis points (2%) above the senior loan rate to adequately compensate BAHFA and the project sponsor, and to align incentives for prudent management and success through the life of the project.
Update: A matched subordinate debt product was received warmly by stakeholders and deemed to be of value across a spectrum of different project types/executions. In response to stakeholder concerns about the current interest rate environment, staff is considering a cap of 8.00%. And to mitigate against the potential for a return to low interest rates, staff is exploring a floor of 6.00%.

- **Marketing Assistance.** BAHFA will offer Doorway Housing Portal services to help ensure low economic vacancy, thus reducing the risk of project defaults in the long term. The mixed-income nature of the projects will be marketable to a broader population than fully middle- or low-income developments that have faced challenges reaching target demographics. The Program will also promote participation by Section 8 voucher holders, where possible, to help maintain high and stable occupancy and increase operating income.

  Update: Doorway continues to be viewed in a positive light. Some questions have arisen as to the implications of more robust Doorway offerings, which are currently under review.

Results of Recent Due Diligence and Stakeholder Engagement

Due diligence efforts during the last several months included multiple components.

- Case Study Testing: First, to ground truth the initial program modeling and test program viability across the Bay Area's diverse submarkets, staff and the consultant team analyzed the impact of the proposed program elements on six recently-completed transactions. As part of these "case studies," staff obtained detailed project-level financials to evaluate impact of the proposed program terms on actual as opposed to modeled projects. Second, the team conducted an exit analysis of the six case studies to understand whether the program as applied to current market conditions would still enable sufficient return to investors to yield demand for the program. Finally, the team reviewed these new analyses with the Technical Advisory Group (see roster in **Attachment E**) and other partners to strengthen and refine the conclusions.

- Research Viability of/Demand for Proposed Elements: In addition to feedback from the Technical Advisory Committee, staff reached out to other stakeholders, representing lenders, investors, governmental agencies and project sponsors to further test the viability of the various elements of the program. These discussions helped staff refine the proposal that was subsequently presented to the Technical Advisory Group for feedback. This outreach also identified potential strategic partners and ways in which the program elements could be aligned with other non-BAHFA programs.

In summary, all proposed elements, with the exception of the top tier loss program, were found to provide value as projects that would otherwise be market rate are converted to affordable at 50% to 80% AMI levels. While a top tier loss program would provide a lower cost of capital to borrowers, the capital required to launch such a program did not reflect the added value it would provide. Staff will continue to look for other ways to further reduce the price of taxable senior debt that would require less capital commitment by the agency.

The combination of proposed tools reduced funding shortfalls by an average of 60%, with savings ranging from 30% - 97%, depending on local conditions and deal size. To fill remaining funding shortfalls, private equity capital was found to be feasible in 5 of the 6 cases, delivering market returns to an equity investor, and additional mission-oriented capital was found to be feasible in the remaining case study. The proposed BAHFA subordinate debt was less impactful on larger projects or projects with higher total per unit costs, due to the proposed $2.5 million loan cap. The pros and cons of the proposed cap will continue to be weighed as program development continues.

In addition to the target project profiles originally contemplated, stakeholders identified other needs in the market for which the BAHFA tools could provide value, including refinancing expiring use projects or restricting units not otherwise regulated by the more traditional affordable housing programs.

A summary of the first round of stakeholder feedback (June-July) is included as **Attachment C**, and a summary of the second round of feedback (August) is included as **Attachment D**.

Potential Adjustments to Program Concept

As a result of the most recent round of stakeholder feedback, along with the case study analysis, the following high-level changes to the program are proposed:

- **Expand Upper Limit Income Restrictions from 80% AMI to 120% AMI:** There are some parts of the region where 120% of AMI is below market and public benefit can be derived at this level. In all cases, any income-restricted unit would still be required to set rents set at a level that is at least 10% below market.
- **Allow New Construction to the Extent Feasible:** While staff had intended the suite of program elements to be targeted toward acquisition and preservation projects, there are program elements that can provide value to new construction and certain instances under which BAHFA's entire suite of proposed program elements will provide value. As BAHFA's ability to increase its Subordinate Debt loan amounts changes, new construction could become an increasing portion of the portfolio.
- **Consider an Equity Product:** In addition to the Subordinate Debt product, staff is exploring the viability and need for an Equity product, whereby BAHFA would co-invest equity pari-passu with a developer/project sponsor. This would inherently come with increased risks but also additional potential upside, and may be appropriate where

additional debt is not possible. This type of investment would only be made if underwriting and structure projected regular, current returns to the equity investors (to meet BAHFA's cashflow needs) and the project sponsor has a strong track record.

- **Eliminate Top Tier Loss Program in Near Term:** As indicated above, the cost and risk of this proposed program element did not appear to provide sufficient value to dedicate BAHFA's limited resources at this time. Staff will continue to explore other ways in which BAHFA can assist with reducing the cost of taxable debt. The efficacy of a Top Tier Loss program could be re-evaluated at a later date, as part of a future program evaluation process.
- **Expand Welfare Exemption Program to Apply to New Construction:** While originally contemplated as an important tool for preservation of affordable housing in the region, BAHFA has also experienced demand for this program for new construction projects. A change to allow new construction will help increase production of new affordable units, furthering BAHFA's mission.

In addition to the above adjustments, more detailed program parameters and underwriting standards will be developed over the coming months. A summary of draft terms for key program elements that were used during viability testing of the program concept is included as **Attachment B**. In general, a thorough list of requirements and more conservative assumptions will be applied to projects in which BAHFA's involvement represents elevated risk to the agency, such as serving as a subordinate debt provider or an owner (either via an Equity contribution or use of essential purpose bonds). Programs in which BAHFA's risk is less, such as providing services through a conduit bond issuance, welfare tax exemption, or Doorway Housing Portal, BAHFA's underwriting requirements will be less in-depth and focus on basic underwriting criteria and alignment with BAHFA's policy objectives, under the assumption that the senior debt provider will apply its own underwriting standards.

Other Updates:

Fundraising: The Chan Zuckerberg Initiative has awarded BAHFA a grant of $6 million for the Module 3 program, consisting of $1 million for operating & start-up costs and the remaining $5 million for the subordinate debt program. On September 24, the Commission approved reprogramming $5 million previously set aside for election related costs for Regional Measure 4 to satisfy a match requirement for the subordinate lending capital. Pending refinement and approval of the program design, the Mixed-Income Financing Program is anticipated to launch with an initial $10 million pilot subordinate debt fund in spring 2026

Program Feasibility: Initial modelling of the program from preparation through launch and stabilized operations shows that the program eventually can be self-sustaining and potentially generate on the order of $700,000 annually to contribute to other BAHFA costs. The majority of income comes from interest earned from the subordinate debt program, with additional funding coming from closing costs and monitoring fees associated with the other programs. This plan assumes the program will be launched with an initial $10 million subordinate debt program funded by the grant commitment and MTC match mentioned above. Over time, additional resources will be added to the subordinate debt program as other BAHFA pilot loan programs wind down and additional fundraising is achieved. The draft model assumes an additional $20 million in subordinate debt added over the next four years, primarily from revolved funds in current BAHFA and MTC housing finance programs. The draft operating model will continue to be refined as revenue and expense estimates are adjusted based on the final set of program terms.

Next Steps

Based on the due diligence conducted to date, staff has determined that there is sufficient need and resources to move ahead with establishing the Module 3 program concept as outlined in this report. Staff seek confirmation from the Committee about the overall approach and direction about program elements, draft terms, and other issues that will be incorporated as program development continues. During the fall and early winter, staff will continue to engage the stakeholder community, socialize the program with potential users and other stakeholders, and identify potential partners who might be able to leverage BAHFA's programs for greater impact.

Following additional program development, staff will return to the BAHFA Advisory, BAHFA Oversight, and ABAG Housing Committees with more detailed proposed program guidelines for review and approval. Contingent upon final Board approvals, staff anticipate launching the new Mixed-Income Financing Program in approximately spring 2026.

Issues

None

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Recommended Action

Information

Attachment

A. Presentation

B. Proposed Terms and Underwriting Guidelines for Program Elements

C. Summary of Round 1 Stakeholder Feedback (June-July)

D. Summary of Round 2 Stakeholder Feedback (August)

E. Technical Advisory Group Roster (as of September)

Reviewed

Andrew B. Fremier