



**Response to 2008 City Audit Report on Limited Term Tax Abatements
and Outline for Next Steps**

October 22, 2008

**Report to Commissioner Nick Fish on
Limited Term Residential Tax Abatements
From Gil Kelley and Bruce Warner**

Commissioner Fish:

The purpose of this document is to report on the status of our organizations collective response to the 2008 Tax Abatement Audit. It also includes an annual report of outcomes and monitoring of tax abatements which were active during the 2007-08 tax year. This report was suggested in the City Audit and Multnomah County Audit; and previously committed to Multnomah County by PDC and Planning in a resolution from November 2007.

The 2008 City Audit made the following recommendations to ensure social goals and project benefits from limited tax abatements are clear and measured:

Recommendations made to City Council:

1. Clarify the goals and objectives of the housing tax abatement programs, and assign responsibility for oversight, evaluation, and reporting.
2. Direct the responsible bureau to submit an annual report of program activities to Council. The annual report should include information on compliance status of abated properties, annual foregone revenues, created by each abatement program, and progress in meeting program goals established by Council.

To improve program administration and ensure ongoing compliance with program criteria, the Auditor recommended PDC:

3. Draft a regulatory agreement with each multiple-family project developer that specifies responsibilities for monitoring project financial performance, affordability, and all other required public benefits.
4. Review the method for assessing financial need for multiple-family condominium projects and make recommendations to Council for revising City Code.
5. Review and update processes for verifying applicant and tenant incomes.

We are committed to working with City Council and other taxing jurisdiction partners to continue this annual reporting mechanism based on clearly established roles and responsibilities in the implementation and administration of the programs. In addition, we will seek to clarify the goals and social benefits intended for all residential abatement programs. We will also collaborate with our partners to address other areas in the audit and incorporate improved systems to deliver on the expectations resulting from City Council policy discussions which will be occurring over the next few months.



Gil Kelley
Bureau Director
Portland Bureau of Planning



Bruce Warner
Executive Director
Portland Development Commission

Response to Audit Recommendation #1

Clarify the goals and objectives of the housing tax abatement programs, and assign responsibility for oversight, evaluation, and reporting.

Response: As outlined in Commissioner Fish's cover letter, in late 2008 and early 2009 City Council will examine Limited Tax Abatement program goals and objectives in the context of a larger housing policy discussion. This will include assessing the multiple tools available to the City to advance housing goals and could result in changes to the LTA programs. Some of these tools will likely be implemented in 2009 and others will be deferred to the *Portland Plan* community effort being led by BoP. The NMUH program will be updated through the *Central Portland Plan*.

PDC and BoP are committed to providing the necessary back ground materials and other support to facilitate these discussions. At their conclusion, we will work with the City Attorney's Office to craft the appropriate Code changes including a clearer articulation of the roles and responsibilities. These responsibilities will also be memorialized through an inter-governmental agreement to the extent it is deemed necessary.

In the meantime, PDC and BoP have clarified current roles and responsibilities for program oversight, evaluation and reporting. BoP will take lead responsibility for general policy/program oversight to ensure the LTA programs continue to meet City goals. BoP will also assist in providing historical policy intent for these programs. PDC will take lead responsibility for project compliance monitoring as it relates to the ownership and affordability components of the programs. Information on the results of 2008 compliance monitoring is contained in the attached 2008 Annual Report.

Prior to the audit, PDC developed and implemented expanded compliance monitoring for all ownership projects. That process is more fully detailed in the monitoring report that accompanies this letter. In September 2008, PDC completed the second ownership project monitoring cycle and presented termination recommendations to City Council for action¹. Additionally, 2007 compliance monitoring of all rental projects is complete and all units are in compliance with the affordability terms outlined in the respective City Council ordinance.

Monitoring of secondary benefits has not been completed by either BoP or PDC. As BoP included in its response to the City Auditor, it is important to distinguish between primary and secondary benefits required by these programs and that the costs and benefits of monitoring of secondary public benefits warrants further discussion with City Council².

¹ See attached Annual Report for details.

² See response to Recommendation #3 for more detail.

Response to Audit Recommendation #2

Direct the responsible bureau to submit an annual report of program activities to Council

Response: Attached is the 2008 Annual Report for tax abatements which were active during the 2007-08 tax year. The report includes information on performance in relation to program goals and objectives; as well as outcomes of compliance monitoring. This report will be delivered annually to both City Council, Multnomah County Commission, and affected school districts. The BoP will have lead responsibility for reporting on program outcomes relative to their policy goals and PDC will have lead responsibility for reporting on the result of annual compliance monitoring activities.

Response to Audit Recommendation #3

Draft a regulatory agreement with each multiple-family project developer that specifies responsibilities for monitoring project financial performance, affordability, and all other required public benefits

Response: When Council exercised its statutory authority under Oregon law to create multiple-family tax abatement programs to achieve certain primary policy objectives, it also designated the programs to achieve some secondary objectives. Specifically, Council required each applicant for a multi-family abatement to provide certain “public benefits” to achieve one or more local policy objectives such as the provision of affordable housing, family-sized units, or dedication of open space for public use. Both the NMUH and TOD programs have their own affordability requirements and list of “public benefit” options.

These “public benefits” fall into three categories:

- Structural requirements (e.g. the requirement that a building contain a space that may be used for public meetings, or a space appropriate for a day care center);
- Programmatic requirements (e.g. the requirement that the building have an operating day care center of a particular size); and
- Affordability requirements (e.g. provisions that limit the rent on some percentage of the units and/or provisions that restrict tenancy to persons with income below a certain income threshold).

We will reserve our assessment of the secondary policy objectives for the overall assessment of tax abatement programs. At that time, we will also evaluate of the City’s success at achieving these objectives through the use of a ‘public benefits’ menu.

Public Benefits Menu:

TOD Program	NMUH Program
<p>1. Affordability Requirement</p> <p><u>Homeownership</u>: 100% MFI for family of four.</p> <p><u>Rental</u>: One of the following</p> <ul style="list-style-type: none"> ▪ At or below 60% MFI for 20% of the units or ▪ At or below 30% MFI for 10% of the units 	<p>1. Affordability Requirement</p> <p><u>Homeownership</u>: 100% MFI for family of four.</p> <p><u>Rental</u>: At or below 80% MFI for 15% of the units</p>
<p>2. Public Benefits Options List Applicant must provide three public benefit options:</p> <ol style="list-style-type: none"> 1. 20 percent of units dedicated to persons with special needs. 2. 10 percent of rental units include 3 or more bedrooms. 3. Provide childcare on-site or support child care facility. 4. Provide residential unit-per-acre density equivalent to at least 80 percent of maximum density 5. Permitted ground floor service or commercial use. 6. Office space or meeting room for community. 7. Permanent dedications for public 8. Family oriented recreational facilities. 9. A dedicated car-share space(s). 10. Structured parking. 11. LEED Silver certification from the US Green Building Council 12. Twice the percentage of affordable units, or percentage of residential building square footage, for affordable units, than is required by the affordability requirement. 13. Other benefits as proposed by the developer and approved by the Planning Commission. 14. Transportation improvements above those required 15. An agreement to sell off-street parking spaces separate from condominium units so that a unit can be purchased without a parking space. 	<p>2. Public Benefits Options List Applicant must provide one or more of the following:</p> <ol style="list-style-type: none"> 1. Open spaces available to the general public; 2. Day care facilities; 3. Permanent dedications for public use; 4. LEED Silver certification from the US Green Building Council; 5. 20 Percent of the rental units have 3 or more bedrooms; 6. A total of 25 percent of the rental units are affordable to households at 80 percent MFI; or ; 7. Other public benefits approved by the Planning Commission and the City Council.

The Audit also cited City agencies did not consistently monitor the developer's compliance with its agreement to provide certain "public benefits". This is correct. There are several reasons for this situation. The developer's agreement to provide one or more "public benefits" is memorialized as a condition to the Council ordinance granting the abatement. However, it is not necessarily reflected in the Regulatory Agreement. The asset management system is set up to monitor compliance with the Regulatory Agreement, and does not look back to the ordinance.

Even if the "public benefit" terms of the ordinance were included in the Regulatory Agreement, the ability of the current asset management system to monitor compliance would hinge on the nature of the public benefit.

- **Structural requirements:** The system is set up to monitor structural requirements prior to occupancy. Monitoring is accomplished through plan review and on-site inspection. However, the system is not set up to verify that structures remain in place after occupancy. For example, if a developer agreed to include a community meeting room in a common area, the system would be able to verify that it was constructed, but does not have the capacity to verify that it remains available as a meeting place for the public for the term of the abatement.
- **Programmatic requirements:** The system does not have the capacity to monitor on-going programmatic requirements (e.g. the requirement that a building have an operating day care center). If the program is to be provided by a third party, the system does not have the authority to compel third-party compliance with the condition of the abatement. Moreover, if the developer asserts that there is insufficient demand for the program, the system is not in a position to mount a challenge.
- **Affordability requirements:** Annually the system monitors rents and tenant incomes, for all tax abated units. There may be funding needs in order to maintain the expanded level of monitoring safeguards. We are in the process of estimating the cost of monitoring abatement affordability provisions and will have more information later in the year.

PDC has added all projects to its Asset Management tracking system, regardless of whether or not a Regulatory Agreement was issued. Also, PDC legal staff has developed a draft regulatory agreement form which outlines the requirements that will be recorded against all new TOD and NMUH projects. This will be implemented as new abatements are approved by City Council. Longer term monitoring of secondary and other public benefits merits a discussion with City Council and the Planning Commission. These benefits include public art, community meeting rooms and other amenities. We will likely be examining whether the City consider a more systemic approach to monitoring which involves regulatory/permitting entities such as the Bureau of Development Services. These changes would result in updates to the City Code.

Response to Audit Recommendation #4

Review the method for assessing financial need for multiple-family condominium properties and make recommendations to Council for revising City Code

Response: PDC and BoP are in full agreement with this recommendation. Staff recommends sale price and homebuyer income limitations be used on ownership condominium projects to test financial need in place of the Internal Rate of Return (IRR) test currently required in City Code. This is due to the fact that once the unit(s) are sold the developer/builder has no future stake in the project. Furthermore, the tax abatement primarily benefits the purchaser of the condominium unit, with some benefit to the developer/builder based on their ability to market the units with the tax abatement. This recommendation will be formalized for City Council consideration and action at the appropriate time during the larger housing policy discussions.

Response to Audit Recommendation #5

Review and update processes for verifying applicant and tenant incomes, to ensure that intended income groups are being served

Response: PDC staff has reviewed their processes for evaluating applicant and tenant income and have inquired with other jurisdiction that perform similar functions for their communities. We are confident the systems used by PDC conforms to HUD CDBG standards and are reasonable and adequate to protect the interests of the City and to ensure that projects serve the intended populations.

For ownership projects current standards include verifying buyer income using the following documents:

- Most recent W-2(s) and current 30-day pay stub(s),
- If self-employed, copies of the past two years signed tax returns and a current profit and loss statement.

PDC will examine requiring signed tax returns as an additional safeguard for assuring proper use of the programs³.

The Audit report also commented on the multi-family housing projects. The majority of TOD and NMUH tax abated projects are financed with tax-exempt bonds and/or low income housing tax credits which have a stringent annual income verification process. PDC relies on the professional property management firms to perform this process and the data is reflected on the Tenant Survey that is collected on an annual basis by PDC. PDC is comfortable with this practice given the regulatory requirements of the State and Federal programs and best practices instituted by the professional property management firms to utilize third-party income verification. In this case, third party income verification is defined as collection of information provided by a third party that states the tenant income (e.g., current pay-stubs, recent tax returns, current bank statements, etc.). We will need to have further discussions with the Auditor's Office to determine exactly how such a change would be specifically be implemented and how it would substantially improve existing practices as a safeguard to public resources.

For projects whose only public investment is a property tax abatement, PDC is in the process of developing income verification guidelines that would require the owner/property manager to collect and maintain comparable records to the State and Federal programs. PDC will take the additional step to periodically audit a random sample of these units to ensure compliance.

As of September 2007 PDC has been collecting tenant surveys on all TOD and NMUH tax abated projects, which contain reported income and rent level for each unit. This safeguard goes beyond existing City Code which states subsequent monitoring is not required until the unit is vacated and again becomes available for rent at which time it must be rented to an income qualified household.

³ For a full explanation of PDC compliance monitoring steps see attached Annual Report.