L.D. 2169, Resolve, Directing the Office of Policy Innovation and the Future to Recommend Proposals to Support the Development of Affordable Housing

Report to the Joint Standing Committee on Housing and Economic Development

From the Governor's Office of Policy Innovation and the Future

January 15, 2025

L.D. 2169, Resolve, Directing the Office of Policy Innovation and the Future to Recommend Proposals to Support the Development of Affordable Housing, directed the Governor's Office of Policy Innovation and the Future (GOPIF) to develop recommendations for potential programs designed to assist developers with financing housing for households with incomes above 80% of area median income. The resolve tasked GOPIF with seeking input from a range of organizations in developing those recommendations, which were to include feasible options for the creation of both ownership and rental housing opportunities for Maine people and an evaluation of potential public/private partnerships. An overview of the issues and specific recommendations follows below.

Maine, like many other states across the country, has long experienced a shortage of affordable housing options for low-income residents. For decades, households with incomes lower than 60% of the area median income have endured long waiting lists for homes with a price point they could afford, or for housing vouchers to supplement their incomes in paying for housing units that would otherwise be unattainable. This problem has generally been more acute the farther down the income ladder the household falls. In the private market, the cost of constructing and operating housing units generally requires monthly rent revenues that are well beyond what low-income households can afford to pay.

Government programs – whether in the form of supply-side subsidies to help pay for the cost of developing new homes or demand-side supports like housing vouchers to supplement household incomes – have proven to be highly successful in accomplishing their objectives but are not funded at a scale that comes close to meeting the need.

Over the past several years, the state's housing affordability challenge has expanded to impact more households with higher incomes in some parts of the state, for several reasons including: (1) the reduction in market-rate homebuilding nationwide in the years following the Great Recession; (2) supply-chain and employment disruptions associated with the COVID pandemic; (3) the continued shortage of construction-related tradespersons; (4) elevated borrowing costs; and (5) in-migration to Maine, primarily among households with higher incomes than those already living in-state, which has skewed costs upward in both the home sale and rental markets.

A comprehensive housing needs report commissioned by the Governor's Office of Policy Innovation and the Future, the Department of the Economic and Community Development (DECD), and MaineHousing, released in the fall of 2023, found that Maine needs approximately 38,500 homes to remedy historic underproduction and will need an additional 37,900 to 45,800 homes to meet expected workforce needs, population growth, and household formation changes by 2030.

While continued, robust investments in proven housing programs and reforms at all levels of government will be necessary to address the housing needs of lower-income Mainers, the recent dynamics described above have created the need to consider initiatives that would also promote the production of housing opportunities for households with incomes above 80% of the area median income (referred to herein as “middle-income”).

As stated in the 2023 housing needs report, a key state policy priority is to “have enough homes affordable, available and in the right locations to support the workforce necessary to sustain and grow Maine's economy. The State’s Economic Development Strategy focuses on the need for a workforce to support Maine’s long-standing industries and to foster growth and innovation in new areas. To achieve these goals, Maine’s economy requires workers to fill open positions as an increasing number of Mainers reach retirement and room for new workers to fill positions created as local businesses and the economy grow. Without enough homes for workers filling open job positions, businesses will continue to struggle and at times fail—harming the prosperity of all Mainers.”

One important means by which to support the creation of housing opportunities for middle-income households is through reforms to the zoning, land use, permitting, and regulatory environment that would allow for the development of more housing units, more quickly, at a lower cost. The Governor and Legislature have already made important strides in this work with the passage of LD 2003 in 2022, and the 132nd Legislature will be weighing many proposals that seek to make further progress in this area. The “Roadmap for the Future of Housing Production in Maine,” commissioned by GOPIF, DECD and MaineHousing and due to be released later this month by HR&A Advisors, will outline numerous such recommendations as well.

Additionally, based on discussions with a wide range of partners in Maine’s business, real estate development and housing finance sectors, we offer two specific recommendations for further consideration in the effort to bolster production of homes that are affordable to middle-income households: one for rentals and one for homeownership.

1. **Mixed-Income, Public/Private Partnerships**

Affordable housing projects undertaken in Maine and elsewhere typically involve the construction of buildings in which 100% of the units are affordable. This is because the aggregate costs of development (land acquisition, site improvements, construction, soft costs, financing, required fees and reserves, etc.) are so high that a developer usually cannot sacrifice the government subsidies which accompany the affordable units. While the inclusion of market-rate units in a project, with the promise of their higher rent revenues, can in some cases serve to subsidize the affordable ones, the reality is that high borrowing costs tend to severely limit the number of market units for which a developer can “sacrifice” the loss of subsidy dollars that are attached to affordable units only.

One approach to addressing this problem and adding more middle-income units than would ordinarily be feasible involves the creation of a public/private partnership in which the state and the private sector provide new, matching resources on projects that are undertaken at a scale sufficient to reduce operating costs below what they would otherwise require on smaller projects.

For example, a 100-unit pilot project on Maine’s Midcoast, undertaken through a partnership with a major local employer such as Bath Iron Works or MaineHealth, could be made feasible by combining 70 units for households at the highest end of the low-income housing tax credit eligibility range with 30 units that have no income eligibility restrictions. Under such a scenario, the state would need to provide roughly $33,000 per affordable unit in new subsidy funding, to be matched by the private sector through $33,000 per affordable unit in subsidy delivered through the donation of land and/or monetary contributions (totaling about $2.3 million each from the public and private sectors). The 30 middle-income units would be set-aside in a master lease arrangement with the employer-partners, and those residents would be selected entirely by the employers without any income eligibility restrictions.

Such an approach assumes that the project would include a mix of two- and three-bedroom units, with rents between $1,400-1,600 for the 70 affordable units (serving households with annual incomes between $50,000-$62,000) and rents between $1,750-$2,600 for the 30 market units.

A similar pilot could be undertaken in a different area of the state, in partnership with other local employers, to produce another 100 units of housing for local workers. Taken together, these 200 new homes would require a $5 million allocation by the State through an appropriation or as an element of a housing bond package.

This model is similar to a recommendation included in HR&A's forthcoming "Roadmap" report referenced above, regarding the establishment of a housing fund to finance mixed-income development.

Both approaches involve combining public resources with private sector investment. In the HR&A example, however, federal low-income housing tax credit subsidies (and their accompanying income eligibility restrictions) are not utilized at all, and the loss of those subsidies are offset by contributions to a housing fund by either government or mission-driven investors willing to accept a lower rate of return than the private market would typically require. This approach becomes more successful to the degree that such a housing fund is paired with other sources of low-cost capital, such as donated or discounted land, tax-increment financing agreements and tax-exempt bond financing.

Also included in the HR&A report are two case studies providing further detail on how public/private partnerships can be utilized to create housing units for middle-income households. One such case study, the Colorado Affordable Housing Financing Fund, is an interesting and relatively new resource made possible in part by a recent state law there requiring 0.1% of state income tax revenue to be set aside for housing production. A portion of those funds is being used for below-market equity investments in mixed-income housing developments, and a Maine-based organization is currently utilizing that program for a project it is building in Colorado. If the Committee would like more information about the feasibility and replicability of such an approach, they have expressed willingness to provide it.

2. **Expansion of Maine's Affordable Homeownership Program**

As part of the Maine Jobs and Recovery Plan enacted in 2021, $10 million was allocated to MaineHousing for the Affordable Homeownership Program (AHP). AHP is an updated version of a previously existing production program at MaineHousing which had been used to assist in the creation of homes for purchase by low-income families. AHP increases the prior program's income eligibility limit from 80% of area median income to 120%, increases the per-unit production subsidy to keep up with rapidly rising construction costs, and extends the required affordability covenants, among other changes. Following the successful deployment of AHP's initial $10 million allocation, which is being used to build over 150 new homes for purchase in 10 different communities across the state, Governor Mills and the Legislature allocated another $10 million to the program in the Supplemental Budget that was approved in the spring of 2024. Applications for this second round of funding are due to MaineHousing this month, and awards will be announced this spring.

The underlying model of AHP is fairly simple: production subsidies of up to $90,000 per unit are provided to developers to bridge the gap between the market cost of creating modest, single-family homes and the cost of creating such homes at a price point of no more than $350,000-$378,000. Purchasers of the homes must have household incomes of no more than 120% of the area median income and a 15-year affordability covenant is applied.

If the Legislature seeks to bolster the production of homes for purchase at a price that is affordable to a wider group of Maine households, AHP could be revised to raise income eligibility and increase home price limits, the required subsidy for which would be lower than that in the existing version of the program.

Furthermore, as in the case of the recommendation above related to rental housing production, a public/private partnership that shares costs with local employers or mission-oriented investors would allow many more such homes to be created for the same amount of public dollars. For example, the 20-unit AHP project known as Wilbur's Woods that is now under construction in Brunswick could conceivably be creating 40 new homeownership units (or more, if the AHP income eligibility threshold were raised) for local workers, if the private sector had matched the $1.4 million subsidy provided to that initiative through MaineHousing.

Governor Mills and the Maine Legislature have made historic investments in affordable housing production over the past six years, through a broad range of initiatives utilizing tax credits, General Fund appropriations, general obligation bonds and housing finance innovations. These critical investments have led to the largest pipeline of affordable housing development in MaineHousing's history: more than 1,500 affordable housing units have been fully constructed, completed and occupied since the Governor took office in 2019, while another 1,400 units are under construction and nearly 2,300 more are in the underwriting stage. These successful programs require continued investment as part of the urgent effort to increase housing affordability for tens of thousands of low-income Mainers.

Additionally, however, recent demographic and market trends call for discussion and analysis of how the State can feasibly support, through zoning, land use and other regulatory reforms, as well as through new development subsidies, the creation of homes targeted to middle-income Maine households. The establishment of public/private partnerships is key to the success of such an effort, which could provide vital support to Maine's growing economy and to the many businesses now struggling to fill open positions due to the limited housing options available to potential employees.