Financing Tools and Incentives for Developers in Missing Middle Housing

November 2024

Victoria Benson, Charity Karanja, Brooke Kessler, Kay Simmons

About the Authors

The 2024 Caren S. Franzini Fellows

Top Left: **Victoria Benson**, President, Mustard Seed Hill

Top Right: **Charity Karanja**, Attorney, Butler Snow LLP

Bottom Left: **Brooke Kessler**, Senior Incentives Servicing Officer, NJEDA

Bottom Right: **Kay Simmons**, Finance Specialist, Maryland Department of Commerce

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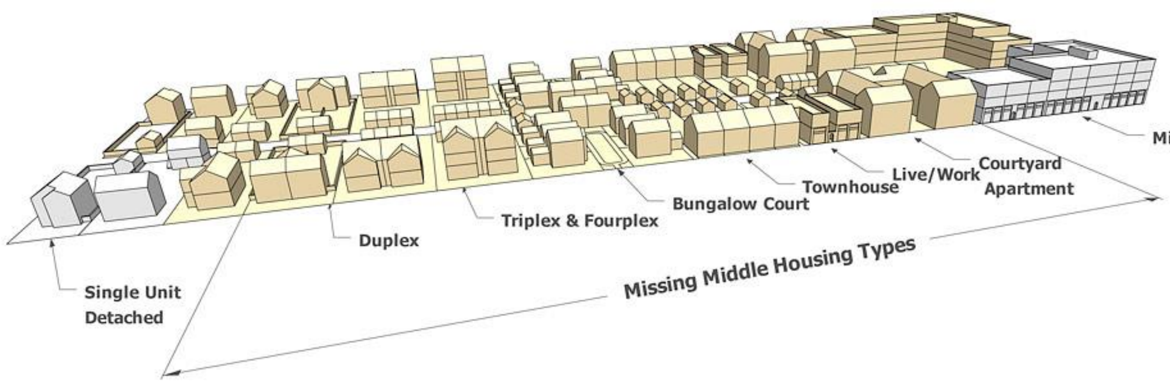
Introduction

Most low- to moderate-income households in North America have to contend with the critical shortage in medium-density housing. Since the mid-1940s, American cities have been emblematic of low- and high-density developments with little in-between. The shift was due to strict density-based zoning laws, which made “blended densities” illegal, and car-centric transportation policies, which prioritized private over public transportation such as buses, trains, and streetcars. In response to this housing shortage, the federal government as well as state and local governments have developed several economic development and incentive programs in an effort to bridge the gap. This Toolkit summarizes the key development finance tools and incentives available to developers and homebuilders in connection with medium-density housing developments.

What is Missing Middle Housing?

Medium-density housing is considered “missing” because it has historically been illegal or difficult to build due to zoning laws and “middle” because it occupies the space between low-density single-family houses and high-density large apartment complexes. The term “missing middle” was coined by Opticos founding principal Daniel Parolek following the 2007-2009 financial meltdown when the housing bubble burst and housing production ground to a lingering halt.



Source: Opticos Designs, Inc.

Missing middle housing (also referred to as essential housing, workforce housing, or attainable housing) provides a variety of housing options along the spectrum of affordability. The housing options include one- to three-story buildings that are more similar in scale and appearance to single-family homes than higher rise residential buildings. This type of housing often “blends in” better with the existing spatial and architectural fabric of lower-density neighborhoods and can allay the concerns of residents worried that larger housing projects may change the character of their neighborhoods.

Typical missing middle housing types include multi-unit structures such as duplexes, triplexes, fourplexes, townhomes, courtyard units, and bungalows. Other examples can include cottage courts and cluster homes. Cottage courts are a group of small (1- to 1.5-story) detached structures arranged around a shared court visible from the street. Cluster homes are groups of smaller dwellings that are clustered together around a shared open space. Pocket Neighborhoods™ are the archetypical cluster homes.

Creative Solutions for Missing Middle Housing: Pocket Neighborhoods

Pocket Neighborhoods™ (coined by Architect Ross Chapin) represent a great example of sustainable and affordable missing middle housing. The neighborhoods represent a pattern of housing designed to foster a keen sense of community among neighbors, while preserving the need for privacy. Each neighborhood consists of a grouping of smaller residences, often around a courtyard, common garden, or shared green space. The neighborhoods are designed to promote close-knit communities. Such neighborhoods are attractive to people who want to live in an involved and affordable community and have the appeal of affordable multi-unit or multi-family homes built near shared resources, such as local retail, community centers, business incubator spaces, and fitness facilities. The neighborhoods often incorporate traditional architectural styles and materials that blend seamlessly with their surroundings.

Source: Ross Chapin Architects

The key characteristics of Pocket Neighborhoods include (a) community building, (b) affordability, (c) sustainability, (d) flexibility, and (e) preservation of character. Pocket Neighborhoods are designed to foster a sense of community and belonging. The smaller scale and shared spaces encourage residents to interact and form strong bonds. This sense of community can contribute to safer, more vibrant neighborhoods overall. By focusing on smaller, more efficient homes and shared amenities, Pocket Neighborhoods can be more affordable than traditional single-family homes. This affordability can help create more diverse and inclusive communities. Moreover, Pocket Neighborhoods often have a smaller environmental footprint due to their efficient use of space and shared resources, and can be integrated into existing neighborhoods, preserving their character and charm. Their location within existing neighborhoods can also promote walkability and reduce reliance on cars.

Pocket Neighborhoods are a creative and innovative approach to addressing the "missing middle" housing shortage. They can be designed to meet the needs of different communities and changing demographics and accommodate a wide range of residents, including families, seniors, and individuals. By fostering community, promoting affordability, and prioritizing sustainability, Pocket Neighborhoods can help create more vibrant, equitable, and resilient neighborhoods.

Benefits of Missing Middle Housing

There are many benefits to this style of housing. Missing middle homes can: (1) bridge the gap between low- and high-density areas; (2) support walkable neighborhoods; (3) locate residents near neighborhood retail and transit options; (4) appeal to a broader range of residents; and (5) meet the needs of a more diverse and inclusive cross-section of the community, including: (a) young adults, just starting their careers; (b) growing families who may need additional rooms or on-site dwelling units for children, guests, parents or grandparents; (c) older adults who may wish to age in place or near family and friends; (d) empty nesters who may wish to downsize; and (e) public servants such as firefighters, police officers, and teachers in search of medium-density homes.

Missing middle housing is one solution to the on-going housing affordability crisis. Missing middle housing is typically more affordable than single-family housing. Because missing middle housing units have lower per-unit construction, material, and land costs, often due to government and private-sector investments, they are generally priced lower. These affordable units provide another housing option that may better fulfill the needs of many residents, particularly those with lower incomes. For example, housing cost-burdened seniors, families, or others facing the prospect of being priced out of their communities may be able to continue living in or near their current neighborhoods by downsizing from single-family homes to cheaper duplexes or townhouses rather than moving out of the area entirely. Further, because missing middle housing is more space efficient, utilizing less land per housing unit, replacing single-family homes with middle housing (or building middle housing in lieu of single-family homes) increases the overall supply of available homes in a region. Furthermore, as evinced by Pocket Neighborhoods, missing middle housing can promote an area's walkability, creating a walkable neighborhood. Walkable neighborhoods are neighborhoods where school, work, shopping, services, leisure, and homes are accessible by foot. Walkable neighborhoods can be linked to social benefits such as a stronger sense of community.

Potential Barriers for Developers

Administrative, financing, and construction barriers continue to hinder the widespread development of missing middle housing. Developers in missing middle housing face several regulatory hurdles, including (a) zoning restrictions on the types of housing that can be built in certain areas, (b) complex and time-consuming permitting procedures that increase development costs and delays, and (c) strict design standards that make it difficult to build affordable and efficient housing. Zoning regulations, permitting processes, and other regulatory barriers can increase the complexity and risk associated with missing middle development.

Many developers and housebuilders require at least 12% return on investment (ROI) on missing middle housing projects. However, among other things, the costs of materials, labor, and land have been increasing, cutting into profit margins and making it more difficult to build affordable housing. Global supply chain issues have led to delays and increased costs, while a shortage of skilled workers in the construction industry continues to contribute to delays and higher costs, particularly in the wake of the COVID-19 pandemic.

Example: Demolish-and-Rebuild Project

Assume a developer acquires an abandoned house and aims to make the home affordable for a double-income household earning $25/hour ($104,000 annually). The final product will be a 1,300 square foot energy efficient starter home with three bedrooms and two bathrooms, with the sale price capped below $400,000 to keep mortgage payments under 30% of the target income. The parcel already has public sewer and water and has electric service. All the property requires is the construction of a short driveway. Developer serves as both the developer and construction company owner, eliminating one profit margin, and reuses existing architectural plans to reduce design costs. Even with these cost-saving measures, the developer would likely earn below 12% ROI.

Sale Price	$399,900
Design	$10,000
Purchase Price	$20,000
Site Preparation	$20,000
Construction	$280,000
Marketing	$20,000
Financing Costs	$15,000
Total Costs	$365,000
Profit	$34,900
ROI	9.56%

Another challenge to developing medium-density housing is financing. Missing middle developers struggle to finance smaller-scale projects, especially from traditional lenders. Missing middle housing often lacks the standardization and predictability of larger-scale projects, making them less attractive to institutional investors who prefer lower risk, higher-return investments. Institutional investors may have a perception that missing middle housing is more vulnerable to market fluctuations or economic downturns. As a result, developers often struggle to secure traditional forms of debt and equity from national banks, private equity firms, and pension funds. These institutions often deem missing middle projects too small or too risky due to their lack of scale. Developers are often forced to rely on local sources of capital that are more tolerant of risk and smaller returns. These sources of capital typically carry higher interest rates on debt compared to sources on larger-scale projects. Moreover, projects in smaller cities or rural areas often face additional challenges due to limited access to capital markets and a smaller pool of potential investors.

Potential Solutions

By addressing the challenges to missing middle housing developments and exploring innovative solutions, it is possible to increase the availability of financing for medium-density housing and promote the development of more affordable and sustainable communities. There are several potential solutions to the missing middle housing crisis, such as (a) implementing more flexible zoning codes that allow for a variety of housing types and densities in different neighborhoods, (b) simplifying and accelerating the permitting process to reduce development costs and delays, (c) providing grants, subsidies, low-interest loans, and other financial incentives to support missing middle housing development, (d) encouraging local communities to invest in missing middle projects through mechanisms like community land trusts or impact investing, (e) implementing impact fees on new development to fund affordable housing initiatives to help offset construction costs, (f) pursuing collaborations between governments, nonprofits, and private developers to create shared equity programs where homeowners contribute a portion of their equity as consideration for attainable housing, and (g) exploring more efficient and cost-effective construction methods, such as modular or prefab construction, tiny homes and Accessory Dwelling Units (ADUs).

Spotlight: Accessory Dwelling Units

ADUs are smaller residential dwelling units located on the same lot as single-family homes that can offer several benefits, including (a) increasing housing affordability for homeowners and tenants, (b) increasing housing options within the community, (c) providing an opportunity for seniors to live close to family, and (d) leveraging the use of existing housing units.

The missing middle housing crisis is tiered and multidimensional and requires adaptive solutions aimed at achieving sustainable development. When used in concert, these solutions can help raise funds, eliminate regulatory barriers, and reduce construction costs, thus incentivizing medium-density housing development.

Example: Demolish-and-Rebuild Project

Let's assume that the local government where the project in the preceding example is located has several incentive programs that, among other things, (a) provide publicly owned land at a discount or for free to developers to reduce project costs; (b) assist with site preparation using public works resources; (c) eliminate marketing expenses by partnering with a local bank to pre-qualify buyers; and (d) offer low-cost loans through a revolving loan fund. Assume that these programs can help eliminate the purchase price ($10,000), site preparation costs ($20,000), and marketing expenses ($20,000), and reduce the financing costs by $5,000.

Sale Price	$399,900
Design	$10,000
Construction	$280,000

Financing Costs	$10,000
Total Costs	$300,000
Profit	$99,900
ROI	33.3%

By taking advantage of these incentives, the developer is likely to earn a return on investment closer to or higher than the desired 12%, in this case, earning a 33.3% ROI.

Missing Middle Resources

National League of Cities; https://www.nlc.org/article/2024/01/23/what-is-missing-middle-housing/

Affordable Housing Finance; https://www.housingfinance.com/policy-legislation/financing-rent-restricted-housing-for-middle-income-households

The Press Democrat; https://www.pressdemocrat.com/article/north-bay/pocket-neighborhood-rincon-valley-green-space/?artslide=0

Local Housing Solutions; https://localhousingsolutions.org/housing-policy-library/missing-middle-housing/

National Housing Trust; https://nationalhousingtrust.org/news/missing-middle-zoning-reform-just-start-solving-affordable-housing-crisis

ChangeLab Solutions; https://louisvilleky.gov/office-planning/document/changelabsolutionsbenefits-and-barriers-middle-housing-memoradum

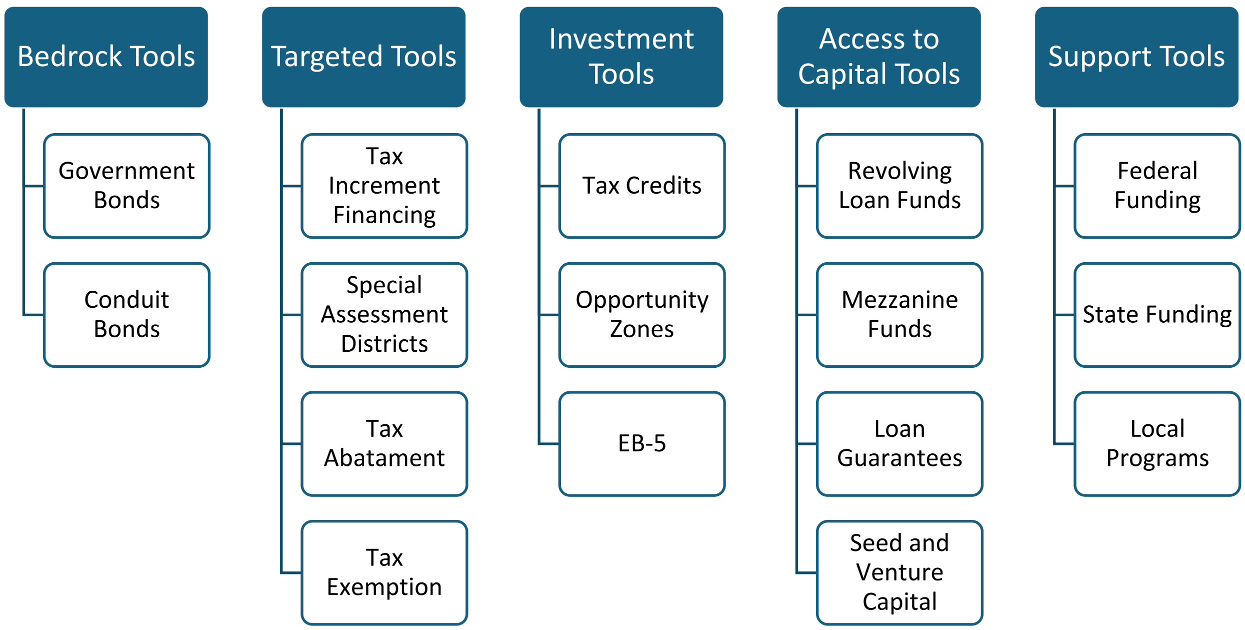
City of Arlington, VA; https://www.arlingtonva.us/files/sharedassets/public/v/1/housing/documents/missing-middle/mmhs_phase-1-report-final-draft.pdf

Camoin Associates; https://camoinassociates.com/resources/how-to-build-more-missing-middle-homes-in-rural-america/

Terner Center and Labs; https://ternercenter.berkeley.edu/wp-content/uploads/2022/12/Missing-Middle-Brief-December-2022.pdf

What is Development Finance?

Development finance plays a pivotal role in fostering economic growth and improving the quality of life within local communities. The development finance spectrum visually represents the different financing approaches commonly employed in development practices. It provides a framework for understanding the range of options available to support community growth and development and involves strategic efforts to support, encourage, and catalyze expansion through public and private investments in physical development, redevelopment, and business and industry. There are five key categories of tools within the development finance spectrum: (1) Bed Rock Tools, (2) Targeted Tools, (3) Investment Catalyst Tools, (4) Access to Capital Lending Tools, and (5) Support Tools. This Toolkit is organized around these five pillars.



Source: Council of Development Finance Agencies (CDFA)

The development finance spectrum includes a wide range of instruments available to support various projects and initiatives. These tools can be customized to address specific needs and circumstances, as well as specific challenges faced by different communities across the nation.

Economic development represents a concerted effort by the governing bodies of federal, state, and local governments to incentivize private sector investment in various aspects of the governments' constituents. Sustained economic growth means livable incomes for local workers, profits for businesses, and tax revenues for the governmental units. Private sector investment is the main engine for economic growth. Consequently, there are many initiatives by federal, state, and local governments created to support and encourage investments to stimulate economic growth. These initiatives, in addition to private interventions, are the focus of development finance.

Development finance utilizes public- and private-sector funds and programs to strategically address the needs of communities, businesses, developers, and investors. It aims to create proactive approaches that maximize the impact of public resources. Each development finance problem requires tailored solutions. The lack of access to capital in underserved markets and industries, such as the missing middle housing market, is one such problem—a problem that calls for unique and targeted financing solutions. This Toolkit explores the financing mechanisms and incentives within the development finance spectrum that are designed to encourage developers to locate, expand, or invest in missing middle housing markets.

Development Finance Resources

CDFA Practioner's Guide to Economic Development Finance by Toby Rittner; https://www.cdfa.net/cdfa/cdfaweb.nsf/fbaad5956b2928b086256efa005c5f78/6c862d113ee4404c862572c20064ba9c/$file/pg-toc.pdf

CDFA Development Finance Resource; https://www.cdfa.net/cdfa/cdfaweb.nsf/pages/df.html

Bedrock Tools

Bonds are the bedrock of development finance and can be a great tool to utilize for missing middle housing developers. Bonds are government loans or debts that are sold or issued to public investors. The investors negotiate the terms and interest rates of the bonds they buy. When investors buy qualified bonds, the interest they earn as income on the investment is tax exempt income. This allows the government entity to negotiate favorable contracts, allowing them to lend the proceeds to the borrower at a rate lower than the market rate.

The proceeds are issued to borrowers to finance projects that benefit the public, for instance, missing middle housing development. The borrower is obligated to make loan payments in accordance with when the bondholder's (or investor's) principal and interest payments are due. The public benefit of the project qualifies the interest made by the bondholder as tax exempt income, resulting in the borrower's favorable rate and lowering the cost of capital for the project.

Tax-Exempt Government Bonds and Private Activity Bonds

Housing projects can be financed through traditional government bonds or private activity bonds (PAB). As used herein, traditional government bonds are bonds that are issued by states and local governments to fund their own projects, as opposed to private activity bonds, which are issued by states and local governments in their capacity as conduit issuers, for and on behalf of private entities. Developers should note that there are several types of municipal bonds. There are various types of traditional government bonds, including general obligation bonds and revenue bonds. On the other hand, there are seven categories of qualified PABs, including exempt facility bonds, qualified mortgage bonds, qualified veterans' mortgage bonds, qualified small issue bonds, qualified student loan bonds, qualified redevelopment bonds, and qualified 501(c)(3) bonds. Tax increment financing bonds (hereafter discussed) are a special type of PAB.

Traditional government bonds are the most flexible and low cost when compared to other bonds, but these are significantly harder to accomplish when involving the private sector. These are effective for affordable housing projects. On the other hand, private activity bonds allow for more private sector involvement in missing middle housing bond financing tools. PABs do permit private sector involvement in the project more readily than traditional government bonds, but the project must still meet many regulations to qualify for tax exemption.

In the Context of Missing Middle Housing

Missing Middle Housing as a Public Purpose Investment

Public purpose investments refer to investments that benefit the public. Bonds utilized to build missing middle housing often meet the criteria of supporting a public need and qualify for tax exemption. Common arguments for using tax-exempt bonds to finance missing middle housing is that medium-density housing can (a) provide affordable housing options for low- to medium-income families, which can help alleviate poverty and distress, and (b) reduce the need for government-subsidized housing, which can lessen the burdens on government budgets. Tax-exempt PABs, paired with Low-Income Housing Tax Credits (LIHTC), are the most common housing bonds issued for low-income, affordable housing development. In addition to tax-exemption, these bonds allow investors to claim 4% LIHTC, generating equity in the project. Developers should, however, note that these bonds are subject to the private activity bond volume cap (discussed below). Moreover, to qualify for LIHTC, PABs must be used to finance at least 50% of the housing development.

Municipal Bonds in Action: Mono County and the Town of Mammoth Lakes

The photo to the right from Mono County, CA's website depicts the rural area around the seasonal resort town of Mammoth Lakes. This is one of the many towns in the US struggling with a housing shortage, specifically for the workforce that supports the town. There is job deterioration resulting from low-wage and visitor-serving jobs being priced out of living in the area and a lack of transportation infrastructure. According to the California Association for Local Economic Development (CALED), houses in the area average $800,000 and condominiums are $450,000.

There is a strong need for missing middle housing to meet the demand for workforce housing to allow this town's economy to grow. A small rural-seasonal town such as Mono County and Mammoth Lakes needs federal assistance to meet the gap left that their established Housing Trust Fund is not able to cover.

CALED expands on six incentives to help attract affordable housing developers to the town, starting with access to LIHTC funds (federally tax-exempt private activity bond funds issued by HFA) to bridge the gap left by Mammoth Lake's Housing Trust Fund. This bond financing, combined with CALED's suggestion for the town to establish inclusionary zoning ordinances that incentivize affordable housing and creative medium-density housing units, is projected to attract developers for the missing middle housing development that is sorely needed by Mono County's year-round residents.

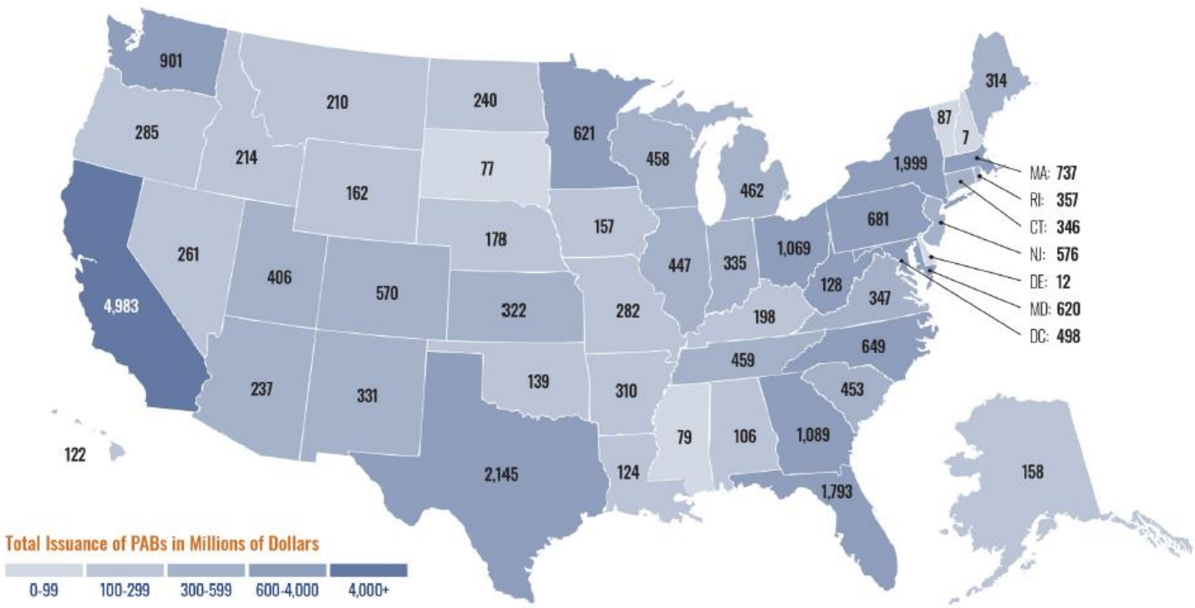
Source: CALED

Applying for Tax-Exempt Bond Financing

Housing Financing Agencies (HFAs Directory), and state and local government entities issue and sell Multifamily Tax-Exempt Housing Bonds to investors and loan the proceeds to developers who apply to the appropriate state agency. Developers may need to partner with local bond counsel to seek out an issuer. Contact your local agency to find out the policy, regulations, and process for applying for housing bond financing.

Housing bond financing has a private activity volume cap for each state. There is ample opportunity for developers to apply for and utilize this low-cost capital in their stack. See below the CDFA Private Activity Bond Issuance by State from the CFDA's 2021 analysis of 2019-2020 PAB & Volume Cap Trends.

Figure 4. Private Activity Bond Issuance by State



Source: [CDFA]

Examples of Bond Financing Programs for Missing Middle Housing

State of Colorado. The [Colorado Middle Income Housing Authority Program], in its pilot phase, offers bond financing for up to 3,500 middle-income units, 80% of which must be new construction. The program is administered by the Middle-Income Housing Authority (MIHA), a special purpose entity independent of the state of Colorado, tasked with the purpose of promoting affordable workforce rental housing projects throughout the state. MIHA is empowered to issue bonds and/or enter into public-private partnerships. Bonds issued by MIHA are exempt from state and local taxes and assessments. In connection with its purchase and use of property, MIHA is exempt from state and local sales and use taxes and may make payments in lieu of taxes to the state or local governments. The program targets households between 80% and 120% of the area median income adjusted for family size (AMI), or 140% of AMI for rural resort areas.

State of California. The [Workforce Housing Program], administered by the California Statewide Communities Development Authority (CSCDA) Community Improvement Authority (CSCDA CIA), provides funding assistance through the issuance of tax-exempt government purpose bonds. The CSCDA CIA acquires market-rate apartment buildings with the bond proceeds and then converts the properties to income- and rent-restricted units for moderate- or middle-income households. The units are generally available to households earning 80% to 120% of AMI. Annual rent increases are capped at no more than 4%, with the stipulation that existing tenants must not be displaced. The CSCDA CIA has acquired and converted more than 7,700 units through the program. This is the largest workforce housing program in the state of California.

Challenges in Obtaining Tax-Exempt Bond Financing

Missing middle housing is less commonly funded by bonds when compared to affordable housing. Bond financing for missing middle housing requires a lot of education and assistance for the developer due to the considerable oversight and due diligence required for projects to meet tax exempt qualifications. Policies differ between states and state agencies, so there is a lot of partnership required to accomplish a bond deal. Considerable fees are also included in the partnerships required to meet qualified bond regulations, making bonds ineffectual for smaller multifamily housing projects.

Financing Considerations

Using bonds for missing middle housing is particularly advantageous. Bonds can be effective with medium to large housing projects such as Pocket Neighborhoods or 6-unit dwellings. Bonds are particularly suited for larger projects because they involve multiple key players, each of whom incurs fees. In contrast, smaller projects often operate with very low margins, making bond funding less practical and cost-effective for them.

Housing projects that can meet tax exemption qualifications are ideal candidates for bond financing. Developers should however note that the bond financing process may take more time to implement, so planning ahead is essential. Moreover, bonds work best in states and municipalities with strong credit ratings and available volume caps. Some states do not fully utilize their Volume Cap, presenting an opportunity for missing middle housing projects to access PABs.

Bedrock Tools Resources

CFFA Rural Development Finance Toolkit; www.cdfa.net/cdfa/cdfaweb.nsf/ordredirect.html?open&id=2023%2BRural%2BDevelopment%2BFinance%2BToolkit.html;https://www.cdfa.net/cdfa/cdfaweb.nsf/ordredirect.html?open&id=2023+Rural+Development+Finance+Toolkit.html

CDFA Practioner's Guide to Economic Development Finance by Toby Rittner; https://www.cdfa.net/cdfa/cdfaweb.nsf/fbaad5956b2928b086256efa005c5f78/6c862d113ee4404c862572c20064ba9c/$file/pg-toc.pdf

CDFA Development Bond Finance Reference Guide; https://www.cdfa.net/cdfa/cdfaweb.nsf/ord/dbfguide.html

Orrick; https://media.orrick.com/Media%20Library/public/files/insights/2024/tax-exempt-bond-financing-for-middle-income-housing-pbf-greenbook.pdf

CDFA Annual Volume Cap Report; https://www.cdfa.net/cdfa/cdfaweb.nsf/ordredirect.html?open&id=VolumeCapReport-2019-2020.html

CALED; https://www.cdfa.net/cdfa/cdfaweb.nsf/ordredirect.html?open&id=CALED-2019-Rural-Infrastructure-Finance-Guidebook.html

CDFA Rating Agency Presentation; https://www.cdfa.net/cdfa/cdfaweb.nsf/ordredirect.html?open&id=2017NDFS-Patricia_Filippone.html

Mono County, CA; https://monocounty.ca.gov/planning/page/studies

Targeted Tools

Targeted finance tools represent the fastest growing area of development finance. Targeted tools are unique because their objective is to target specific geographical areas. The main goal of targeted tools in development finance is to create investment and transformation amongst the real estate values in specified geographic areas. These programs are also designed to set aside financial resources for investment, maintenance, beautification, safety, and other improvements to the built environment. Built environment is defined as the physical spaces, structures, features, and facilities that people create or modify in order to live and work. Communities using these tools have shown increases in property values, overall community improvement, and business development. Even smaller and rural communities have applied these tools effectively.

This section specifically highlights Tax Increment Financing (TIF) as a targeted tool for missing middle housing. TIF districts are designed to generate new taxes within a specific geographic area through improvements to the built environment. This creates a self-liquidating system where the increased property, sales, or other taxes generated by the improvements can, in turn, be used to finance some of the improvements. Developers should note that there are other "targeted tools" that may be applicable to specific developments, including special assessment districts, brownfield development, sustainable development, Property Assessed Clean Energy (PACE) financing, tax abatements, tax exemptions, and other tax incentives.

Examples of Targeted Tools in Missing Middle Housing

State of Florida. The Multifamily Project Ad Valorem Tax Exemption, administered by the Florida Housing Finance Corporation (FHFC), offers a "missing middle" tax exemption for newly or recently constructed multifamily rental developments that offer affordable and workforce units. Units within qualified properties (as defined under state statute) that house individuals or families with annual incomes not exceeding 80% of the AMI are exempt from ad valorem taxes. An exemption of 75% of the assessed value must be provided for units in qualified properties that house individuals or families with incomes between 80% and 120% AMI. The exemption is available to owners of eligible properties beginning in Fiscal Year 2024.

State of Washington. The Multifamily Housing Tax Exemption Program, codified as RCW 84.14, allows municipalities within the state to provide ad valorem tax exemptions for multifamily projects with a minimum of four residential units. The exemption can be for 8 or 12 years, with the 12-year exemption available only to developers who commit to rent or sell at least 20% of the units to low- and moderate-income households.

Tax Increment Finance

First created in 1952 in California, Tax Increment Finance was designed to act as a catalyst for redevelopment areas. Now 48 states have TIF districts (also known as Tax Allocation Districts in Georgia, Project Development Financing Districts in North Carolina, and Tax Increment Reinvestment Zones in Texas). TIF is a method for capturing the future tax revenues from real estate improvements to pay for the present costs of those improvements. TIF can be used to channel government funds toward public improvements in distressed or underdeveloped areas where development would not otherwise occur.

A TIF district is created within a designated area in order to direct benefits to the residents within that area. TIF districts last between 10 and 40 years, or for as long as the bonds issued to fund the improvements remain outstanding. TIF uses the increased property or sales taxes generated by new development to finance the costs related to that particular development. Individual states authorize local government and municipalities to designate TIF districts. While each state's TIF statute varies, similar policy goals and objectives exist. These intentions include blight elimination, infrastructure additions, and improvements.

A TIF district is often used to advance economic development priorities such as (a) developing industry niches and opening new markets for products and services that may not already exist in an area, (b) creating and retaining jobs while supporting industrial development, (c) supporting overall development, (d) reusing existing infrastructure for development, and (e) cleaning up brownfield sites and creating clean energy opportunities. TIF can be used for a variety of improvements to a geographic location, including public infrastructure, land acquisition, relocation, demolition, and improvements to utilities. TIF can also be used to pay debt service, planning costs, and other qualified development costs.

A TIF district generates money for development or redevelopment for a local government by capturing the tax revenue—or increment—above the initial assessed value during the life of the district. The tax increment from a TIF district is created without raising taxes or dipping into the base tax revenues present at the time of adoption. The increment thus becomes a repayment stream for debt used to finance some aspects of what is driving the increase, such as retail, commercial, residential, or mixed-use development.

How it works

Let's say that an existing property generates $10,000 a year in real estate taxes. The tax base for the property is thus frozen at $10,000. A developer proposes a new project for the property. Assume that, once the project is completed, the project will raise the property taxes generated to approximately $100,000 per year. The developer agrees to make a significant investment and seeks TIF funds from the government as reimbursement for eligible public improvements. The government wishes to issue TIF bonds to finance the project. Before designating the property as a "TIF District," the government must first conduct a "but for" test.

The "but for" test is a crucial requirement for establishing a TIF district. The local government must demonstrate that "but for" the use of TIF, a proposed development would not occur. This test requires that TIF is only used to support projects that would not be feasible without public assistance. The test also ensures that the benefits of the project justify the use of public funds. Once the "but for" test is satisfied, the local government can establish a TIF district and issue tax-exempt bonds to finance the infrastructure improvements. TIF bonds are attractive to investors because they are exempt from federal and state income tax.

After the project is completed, a new assessment is done on the property to determine the increased property tax revenue that will be captured by the TIF district. This revenue is then used to repay the bonds and cover the costs of maintaining the infrastructure improvements.

How it works

Let's say the previously discussed property is now generating $100,000 in real estate taxes each year. The original $10,000 tax base will continue to flow to the government (city, county, state, schools). The tax increment ($90,000) will go towards paying debt service on TIF bonds issued for the project. Once the principal and interest on the TIF bonds is paid in full, the tax increment in addition to the original tax base goes to the government.

In the Context of Missing Middle Housing

Targeted tools can be used in unique ways to invest and transform geographic areas that may otherwise be ignored or forgotten. Tax increment financing was created as a tool to help repair blight in American cities. Most state TIF statutes continue to highlight this as an important aspect of TIF. Historically, one of the most effective ways to utilize TIF is for blight elimination. Conditions that qualify as blight include dilapidation, obsolescence, deterioration, failure to meet code, inadequate utilities, environmental cleanup, and deleterious land use. By using TIF for blight elimination, a community can ultimately encourage development to promote the community's goals where it may otherwise not occur.

Some state and local governments have authorized the creation of TIF districts which offer a range of benefits. Within these districts, the state or local governments can provide bond financing, density bonuses, and other incentives geared towards the development and preservation of medium-density housing. A key feature of these TIF programs is rent and income restrictions. These restrictive covenants safeguard against rent hikes stemming from the increased private investment within the TIF districts. Because increased development often results in raised property values, affordability restrictions are often imposed for long periods of time. Considering the restrictive covenants, these programs present a promising opportunity for the development and preservation of attainable housing within TIF districts.

Examples of Tax Increment Financing in Missing Middle Housing

Pittsburg, KA. The city has established a Rural Housing Incentive District (RHID) intended to address the shortage of moderately priced homes within the city. The city captures 100% of the incremental increase in real property taxes within the RHID in order to reimburse developers for eligible expenses. The RHID financing is available over a period of 25 years and can be used to offset certain land acquisition and site preparation costs as well as numerous infrastructure costs. The Creekside East and Silverback Landing subdivisions are beneficiaries of the RHID program, and both target middle-income households earning incomes between 80% and 140% of AMI as well as higher-income households.

State of Minnesota. The state of Minnesota allows for the creation of Housing TIF Districts, with the incremental tax revenue used to finance housing developments for low- and moderate-income individuals. The financing can cover the costs associated with the acquisition, construction, and rehabilitation of housing units, professional costs, and the costs of public improvements related to the development. This program has been utilized by municipalities across the state. For instance, the City of Edina has financed several housing TIF District projects, spurring millions in new investments in property.

State of Utah. The Housing and Transit Reinvestment Zone Act provides for the creation of Housing and Transit Reinvestment Zones (HTRZ) within a given radius of light rail, bus rapid transit, or commuter rail stations by municipalities in Utah. The Act enables municipalities to capture a portion of the incremental tax revenue growth generated within the HTRZs over a period of time and invest in mixed-use, multi-family, and affordable housing developments.

TIF is an effective financing tool for public infrastructure improvements. Public infrastructure and structures eligible for TIF financing include schools, libraries, parks, public parking, cultural facilities, water, sewer, and flood control facilities, public roads and highways, and street lighting. Developers and investors are interested in building homes in areas that attract buyers and renters. Pertinently, the value added by these improvements is that communities can more easily attract developers and homebuyers to be in a geographical area with functional and workable public infrastructure. This makes such areas attractive to developers in missing middle housing.

Targeted Tools Resources

CDFA Rural Development Finance Toolkit; https://www.cdfa.net/cdfa/cdfaweb.nsf/ordredirect.html?open&id=2023+Rural+Development+Finance+Toolkit.html

CDFA Practioner's Guide to Economic Development Finance by Toby Rittner; https://www.cdfa.net/cdfa/cdfaweb.nsf/fbaad5956b2928b086256efa005c5f78/6c862d113ee4404c862572c20064ba9c/$file/pg-toc.pdf

National Housing Policy Guide; https://nhc.org/policy-guide/tax-increment-financing-the-basics/how-tifs-can-be-used-for-affordable-housing/

St. Paul District, U.S. Army Corps of Engineers; https://www.mvp.usace.army.mil/Media/News-Stories/Article/622007/harpers-slough-restoration-gains-ground/

Local Housing Solutions; https://localhousingsolutions.org/housing-policy-library/tax-increment-financing/

Investment Catalyst Tools

Investment catalyst tools include various tax incentives and subsidies designed to encourage investment in communities across the country. These can include tax credits, opportunity zones, and other financial assistance. Investment tools in the housing market often take a tiered approach, with different housing programs catering to varying income thresholds. Many federal, state, and local programs, including the LIHTC program and the Section 8 Housing Choice Voucher Program, are primarily for low-income households, leaving a gap for the "missing middle." A potential solution could be the creation of Middle-Income (or Workforce) Housing Tax Credits (MIHTC), akin to LIHTC but targeting households with incomes between 60% and 120% of AMI. Another solution could be expanding the Section 8 program and other programs administered by the United States Department of Housing and Urban Development (HUD) to include funds specifically designated for middle-income households. The focus of this section is tax credits. However, developers should note that other investment tools are available for housing developments. Allowing tax credits to be stacked with other incentives could make projects more financially viable.

Federal Tax Credits

Tax credits directly reduce a taxpayer's tax liability, making them an attractive incentive for investment. The issuers of the tax credit allocate credits based on the actual outlay of resources. To receive a tax credit, an investor must demonstrate a resource commitment, such as a real estate investment or cash injection into a project. Tax credit programs can be a powerful tool for stimulating investment and economic development, but they can be complex, requiring a careful understanding of eligibility criteria and regulations. Moreover, not all projects qualify for tax credits, and the specific requirements can vary depending on the program. Tax credits are often limited, making securing them for projects a competitive process.

There are three main federal tax credit programs: Low-Income Housing Tax Credits, Historic Rehabilitation Tax Credits, and New Markets Tax Credits.

State Tax Credits

Most state tax credit programs mirror federal programs, with slight variations. These programs can often be combined with federal tax credit programs to ensure maximum investment and are designed to finance a variety of projects, including low-income housing, brownfield cleanup, and targeted area redevelopment. Many of these programs are industry- or area-specific.

> Example of State Tax Credit Program
>
> *State of Maryland.* The Enterprise Zone Tax Credit (EZTC), administered by the Maryland Department of Commerce, is available to employers in designated Enterprise Zones who hire for newly created full-time jobs. The EZTC includes a one-time credit for each new employee and a three-year credit for hiring an employee who is economically-disadvantaged (as determined by the Maryland Job Service). The employer may claim an unlimited number of employees, and the EZTC can be claimed together with the Federal Work Opportunity Tax Credit (WOTC), the Federal Empowerment Zone Tax Credit, and the Maryland Employment Opportunity Tax Credit (EOC). Tax credits range between $1,000 and $4,500 per year. The employer must pay a wage equal to at least 150% of the federal minimum wage and must be certified by the local zone administrator to be eligible for the tax credit.

In the Context of Missing Middle Housing

Low-Income Housing Tax Credits

The LIHTC program, established by the Tax Reform Act of 1986, is the primary federal government initiative aimed at promoting the development and refurbishment of affordable rental housing. Although this Toolkit is designed for medium density housing, which is consistent with medium-income households, there have been on-going discussions and proposals on expanding the LIHTC program to cover more households. Through the LIHTC program, state and local LIHTC-allocating agencies issue tax credits to developers and homebuilders to fund the acquisition, rehabilitation, or construction of rental housing targeting lower-income households. Developers receive federal tax credits to help cover construction costs in return for committing to designate a certain portion of units for lower-income households. The LIHTC program is estimated to cost the federal government approximately $13.5 billion annually. The program offers a 4% tax credit (30% subsidy) for new construction, acquisition, and rehabilitation of existing buildings financed by tax-exempt bonds. In addition, the program provides a 9% tax credit (70% subsidy) for new construction and substantial rehabilitation not financed by federal subsidies.

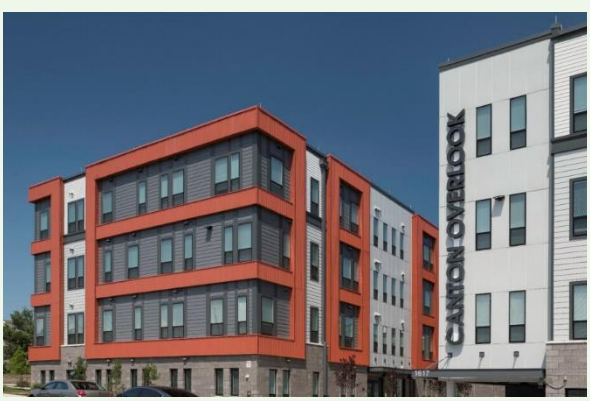
Potential Legislative Reform

To qualify for the 4% LIHTC under current law, developers must finance at least 50% of the project using tax-exempt PABs. The proposed Tax Relief for American Families and Workers Act lowers the PAB financing threshold to 30%, creating room for other financing tools within the capital stack and reducing the strain on state PAB volume caps. The legislation also seeks to restore the 12.5% annual increase in 9% LIHTC allocation that ended in 2021. In addition, the proposed Accelerated Supply of Affordable Production Housing Act seeks to eliminate volume caps for PABs used to finance the preservation, improvement, or development of rental housing units if all (100%) of the units are affordable for low-income households. Developers should note that, besides these two bills, there are likely other legislative proposals that may affect the LIHTC program.

The LIHTC program is mainly administered by state housing finance agencies (HFAs) that allocate tax credits to developers. For instance, in Maryland, the Department of Housing and Community Development (DHCD) administers this program. To finance the construction of low-income rental units, developers typically sell their tax credits to external investors, mostly financial institutions, in exchange for equity financing. This equity reduces the financing developers would otherwise need to secure and enables LIHTC-financed properties to offer more affordable rents. Developers can claim the tax credits annually in 10 equal installments (over 10 years) once a property is completed and available to rent.

LIHTC in Action: Canton Overlook Development

Canton Overlook is a 150-unit apartment complex located in Southeast Baltimore, Maryland. The complex offers modern amenities, including a fitness center, business center, and communal patio, and is intended to address the housing needs of the area's growing workforce, including employees at nearby Amazon facilities.



The $58 million project was funded as follows:

Sources	Amount	Percent
Bond Financing	$23,000,000.00	39.66%
LIHTC	21,000,000.00	36.20%
Rental Housing Loan Program	9,000,000.00	15.52%
Leveraged Capital	5,000,000.00	8.62%
Total Sources	**$58,000,000.00**	**100.00%**

Source: Southway Builders

LIHTC in Action: Perkins Square Development

Perkins Square is a 12-block redevelopment project located in downtown Baltimore. The development includes new mixed-income workforce- and market-rate housing units, to be built in several phases. Perkins Square replaces the original Perkins Homes, a public housing project built in the 1940s for shipyard workers and their families. Perkins Homes comprised of fifty (50) three-story brick buildings and was demolished in 2023. The project aims to provide attainable, high-quality living units, including low-rise affordable apartment buildings, townhomes, and market-rate apartments. The development will also include small-scale retail establishments, a large public park, and a public school with playing fields.

The project has leveraged public-private partnerships, private debt and equity, and public resources including HUD Choice Neighborhood Implementation Grants. The capital stack for the project consists of several funding sources, including the following:

Sources	Amount	Percent
Bond Financing	$12,000,000.00	28.24%
LIHTC	18,000,000.00	42.35%
Federal HOME Program	4,000,000.00	9.41%
Rental Loan Program	2,500,000.00	5.88%
Leveraged Capital	6,000,000.00	14.12%
Total Sources	**$42,500,000.00**	**100.00%**

Sources: HUD and Housing Authority of Baltimore City (HABC)

Developers and homebuilders receiving LIHTC must satisfy an income and gross rent test. Generally, the tax credits are reserved for housing units occupied by households earning less than 60 % (and in some cases, 80%) of AMI. The LIHTC program has been successful in financing affordable housing, supporting the construction and/or rehabilitation of approximately 115,000 affordable rental units each year between Fiscal Year 2000 and Fiscal Year 2016, with over 3 million housing units built by the end of Fiscal Year 2023. Nonetheless, the number of LIHTC credits available is outpaced by the demand for affordable housing. Furthermore, the allocation of the credits often varies across states and regions, leading to disparities in the availability of affordable housing units. The LIHTC Program is also notoriously complex, limited to rental units as opposed to owner-occupied units, and income-restricted to levels that edge out moderate-income households.

New Markets Tax Credits

The Federal New Markets Tax Credit (NMTC) Program provides tax credit allocations to Community Development Entities (CDEs) through a competitive application process. CDEs act as financial intermediaries that facilitate the flow of private capital from an investor to a qualified NMTC business located in a low-income community. CDEs offer NMTCs to investors in exchange for equity investment in the CDE. With the capital from these equity investments, CDEs can provide loans and investments to businesses operating in low-income communities at better rates, terms, and more flexible features than the market. Investors who invest in CDEs can claim NMTCs worth 39% of their equity investment. The NMTCs are claimed over a seven-year period.

NMTCs are typically used to finance investments in operating businesses, commercial real estate, and construction in qualified census tracks. Generally, residential rental real estate is not an eligible business for NMTC equity. However, mixed-use rental developments and for-sale homes may be eligible for NMTC financing. To qualify, at least 20% of the housing units financed by NMTC must be maintained as affordable housing units. Affordable housing units are defined as properties that are affordable to households with incomes equal to or less than 80% of AMI, and these households must not pay more than 30% of their income for housing. Moreover, the developer must meet the definition of a Qualified Active Low-Income Community Business (QALICB) under the Federal Tax Code.

How it works

CDEs obtain funds to invest in QALICBs from private investors. The NMTC program provides these investors with tax credits based on equity investments made in CDEs. This investment is known as a Qualified Equity Investment (QEI). Investors receive a tax credit for 39% of a QEI, which is claimed over a seven-year schedule. A QEI must be fully invested in a CDE for seven years for an investor to meet NMTC compliance requirements. In most cases, a QEI is linked to a specific project. Therefore, the amount of subsidy a project can receive is dependent upon the size and cost of the project itself. CDEs must use the proceeds of a QEI to provide below-market rate equity or debt capital to qualifying businesses or real estate projects. The capital that a CDE provides for a qualifying project is known as a Qualified Low-Income Community Investment (QLICI). CDEs typically structure QLICIs as seven-year, interest-only loans to mirror the NMTC compliance period for QEIs. To finance a project with NMTCs, a CDE must first be certified by the Community Development Financial Institutions (CDFI) Fund as a valid CDE and must then obtain NMTC allocations from the CDFI Fund through a competitive application process. After a CDE receives NMTC allocations, it can sell these tax credits to an investor to generate subsidies for the project.

Historic Rehabilitation Tax Credits

The Federal Historic Rehabilitation Tax Credit (HTC) Program is an indirect federal subsidy that helps finance the rehabilitation of historic buildings and can finance the development of affordable low-income housing as well as middle-income housing. It provides a 20 percent tax credit for qualified expenditures. The credit is only applicable to properties to be used for business or other income-producing purposes, and a "substantial" amount must be spent on rehabilitating the historic building. The building needs to be certified as a historic structure by the National Park Service (NPS). Rehabilitation work must meet the Secretary of the Interior's Standards for Rehabilitation, as determined by NPS.

HTCs in Action: Rosenwald Court Apartments

Chicago, IL. The Rosenwald Court Apartments, a 421-unit Art Moderne-style residential building complex, was built in 1929 by Julius Rosenwald to provide housing for the growing black middle class in

Chicago. The complex, designed by his nephew and son-in-law, aimed to generate a substantial return on investment but only yielded a 2.4 percent profit over seven years. After Rosenwald's death in 1932, the complex was sold to the Chicago Department of Urban Renewal and eventually transferred to the Chicago Housing Authority (CHA). The CHA later vacated the building, and the complex closed in 1999, remaining vacant and deteriorating under the ownership of the City of Chicago. The complex was rehabilitated and reopened on October 4, 2016, providing 235 one- and two-bedroom units for senior and family housing. The inner court's landscape was restored, and retail spaces refurbished. The $132 million rehabilitation project utilized multiple tax incentives, including federal historic tax credits, low-income housing tax credits, tax-increment financing, and a loan from the CHA.

Source: [Landmarks Illinois]

Moving Forward

Tax credit programs can be a powerful tool for stimulating investment in missing middle housing. However, tax credits have historically been unavailable for these projects. In response, there are on-going efforts to develop a federal program for missing middle housing tax credits, including a proposal to create a Workforce Housing Tax Credit (WFHTC) Program, which would complement the LIHTC program by providing financing for housing developments geared towards middle-income households. The legislation for the WFHTC program is under consideration by the United States Congress.

States alike have been focused on developing financing programs for missing middle housing. Some states have created investment tools for mixed-use and multi-unit housing. Other states have taken a step further and created tax credit programs specifically for workforce housing.

Examples of State Tax Credit Programs for Missing Middle Housing

State of Colorado. The Middle-Income Housing Tax Credit Program (MIHTC), administered by the Colorado Housing and Finance Authority (CHFA), offers tax credits for multifamily projects with rent-restricted units affordable for households earning between 80% and 120% AMI or 40% AMI for projects located in rural resort counties (as defined by the Colorado Department of Local Affairs). For mixed-income projects, MIHTC is prorated based on the proportion of income-restricted units. Projects are subject to restrictive covenants requiring rent-restricted units for at least 15 years. MIHTC is the first tax credit program of its kind in the nation. Beginning January 1, 2025, the CHFA is authorized to competitively award up to $5 million each year through 2026 and up to $10 million each year beginning in 2027 and ending in 2029. Any credits that remain unallocated as of December 31, 2029, will be transferred to the LIHTC program and allocated by the CHFA. Projects financed through federal or state LIHTC programs are ineligible for MIHTC.

State of Kansas. The Kansas Housing Investor Tax Credit (KHITC), which is administered by the Kansas Housing Resources Corporation (KHRC), was created for the purpose of facilitating investment in housing development in order to attract new employees, residents, and families and promote the development and expansion of businesses throughout the state. 13 million in KHITC credits is available annually for eligible projects. To be eligible, applicants must be either the builder or developer of a proposed housing project located within a county with a population of not more than 75,000. KHITC credits are limited to 40 credits per year for both single- and multi-family units.

Investment tools such as tax credits can be valuable in subsidizing development costs and expanding the supply of affordable medium-density housing. Most of these tools can be used in tandem, expanding their reach and impact. However, it is important to be cautious about the difficulties involved in stacking incentives. Challenges may arise in terms of timing, construction costs, and design requirements. Despite these challenges, these projects are particularly meaningful as they involve the revitalization of cultural landmarks, the rejuvenation of communities, and the creation of attainable housing for moderate-income households.

Investment Tools Resources

Maryland, Department of Commerce; https://commerce.maryland.gov/fund/programs-for-businesses/enterprise-zone-tax-credit

State of Maryland Website; https://www.dllr.state.md.us/employment/eztc.shtml

Congressional Research Service; https://sgp.fas.org/crs/misc/RS22389.pdf

National Park Service; https://www.nps.gov/subjects/taxincentives/tax-credit-basics.htm

CDFI; https://www.cdfifund.gov/programs-training/programs/new-markets-tax-credit

NCSL; https://www.ncsl.org/human-services/middle-housing-filling-a-gap-in-available-housing-options

Urban Institute; https://www.urban.org/sites/default/files/publication/103956/which-types-of-projects-receive-new-markets-tax-credit-funding_0.pd

NACO; https://www.naco.org/resource/advancing-local-housing-affordability-naco-housing-task-force-final-report

Landmarks Illinois; https://www.landmarks.org/preservation-programs/success-stories/rosenwald-court-apartments/

Afire; https://www.afire.org/summit/missingmiddle/

Tax Policy Center; https://taxpolicycenter.org/briefing-book/what-low-income-housing-tax-credit-and-how-does-it-work

Nixon Peabody LLP;
https://www.housingonline.com/Documents/Developing_For_Sale_and_Rental_Housing_Using_NMTCsa.pdf

Access to Capital Lending Tools

Access to capital lending tools are resources that provide financial backing for a wide array of economic development projects. Capital programs are highly versatile and can be tailored to fill financing gaps in a variety of contexts. These programs range from large government-backed loan funds to conventional mortgages issued by local banking institutions. Capital programs can finance both small- and large-scale projects. There are many capital programs that can finance or refinance the construction or acquisition of medium-density housing, including, but not limited to, conventional mortgage loans, bank construction loans, commercial mortgage-backed securities (CMBS) loans, bridge loans, hard money loans, revolving loan funds, mezzanine funds, loan guarantee programs, loan participation programs, linked deposit programs, collateral support programs, subsidies, housing microfinance, seed and venture capital, and crowdsourcing. Although these tools are the most flexible in the development finance toolbox, they are widely underutilized. It is important to explore the differences between the different tools and select the optimal structures that best suit each project or that address specific industry needs. It is also important to consider market conditions and the projected rental income for each project to ensure enough income is generated to support debt service payments and construction costs.

Revolving Loan Funds

Revolving loan funds (RLF) are self-replenishing pools of money that use debt service payments on existing loans to fund new loans. RLFs are often gap financing measures that can be used in combination with more conventional funding sources. With competitive rates and flexible terms, RLFs provide reliable access to capital for borrowers while lowering investment risk for lenders. Many states and local governments have established RLFs to help build and preserve missing-middle housing. Provided the developer meets the requisite terms of a given financing product, including any AMI requirements, these tools can support a wide variety of needs. The table below provides just a few of the states with middle-income or workforce housing RLF programs.

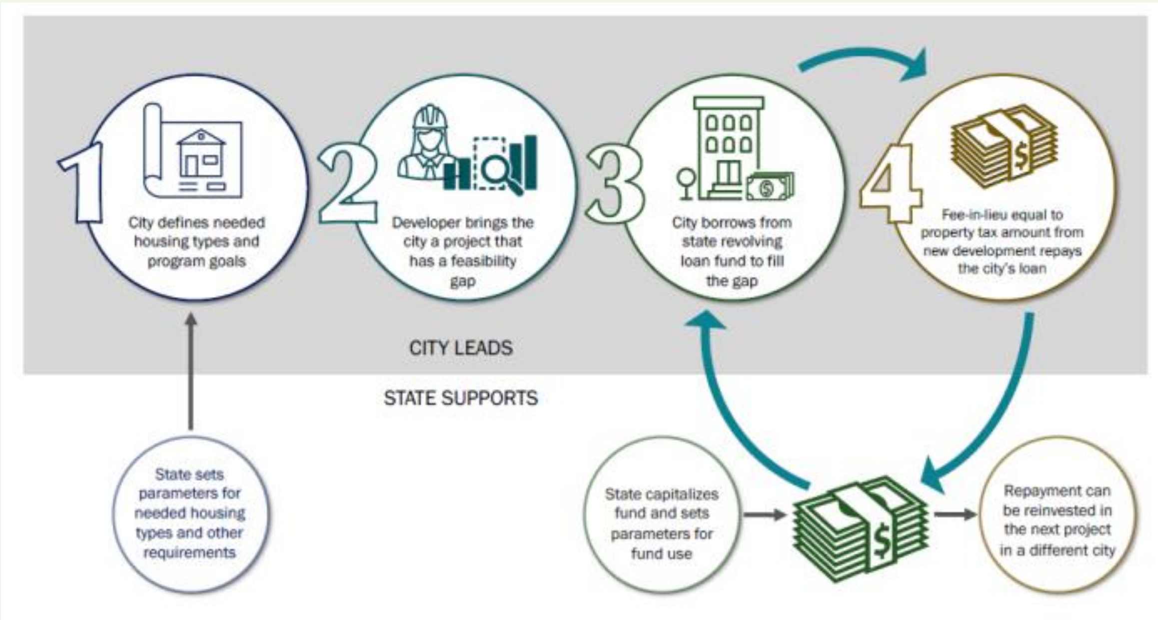
Examples of State Revolving Loan Funds for Missing Middle Housing

State of Kansas. The Moderate Income Housing (MIH) Revolving Loan Fund Program (KHITC), which is administered by the Kansas Housing Resources Corporation (KHRC), provides loans on a rolling basis for the purpose of promoting the development of moderate income housing in the state. The program targets housing projects for households between 60% and 150% of AMI. In Fiscal Year 2024, the program aims to issue approximately $9.55 million in loans to eligible applicants, including builders and developers, for moderate income housing development. In accordance with statutory requirements, 50% of available funds must be applied towards projects in cities and counties with populations of less than 60,000.

State of Mississippi. The Mississippi Affordable Housing Development Fund (Revolving Loan Fund), administered by the Mississippi Home Corporation (MHC), provides loans for the construction of low- to moderate-income housing. The funds can be used for construction, site control and development, and rehabilitation of new owner-occupied or rental units. The loans are available to for-profit, nonprofit, and public entities but not to individuals. The structure of the loans is negotiable.

State of New Mexico. The Opportunity Enterprise and Housing Revolving Loan Fund, administered by the New Mexico Finance Authority (NMFA), provides loans for the construction of workforce and affordable housing. The program aims to address the state's housing shortage for workers and provides low-cost financing for the development of rental and homeownership workforce housing in addition to financing for traditional affordable housing projects. The first round of funding, which ended in October 2024, had $30 million in available funds. Approximately $125 million is available for the second and third rounds of funding scheduled for Fiscal Year 2025.

State of Oregon. The State Revolving Loan Fund was created by the Oregon Legislature under its 2024 Housing Stability and Production Package and seeded with $75 million to assist cities and counties in the development of moderate-income housing. Eligible jurisdictions can borrow funds through the program and make grants to developers. The increase in property taxes stemming from the housing projects is then pledged as security for the loan, with interest and principal payable over a period of 10 years. The local jurisdiction provides a ten-year tax abatement on the improvements and a fee-in-lieu of taxes equivalent to ad valorem taxes on the improvements. The fee is then used to repay the loan, with the repayment proceeds used to make loans to other jurisdictions or projects. After loans are repaid, the fee terminates, and the property taxes are retained by the local jurisdictions.



Source: Oregon Legislature, Press Release, March 4, 2024

State of Vermont. The Rental Revolving Loan Fund (RRLF), administered by the Vermont Housing Finance Agency (VHFA), was created under the Vermont Housing Made for Everyone (HOME) Act of 2023 for the purpose of incentivizing the development of rental housing for middle-income households earning between 65% and 150% of AMI. The RRLF program provides developers and builders with subordinate loans not exceeding 35% of the development cost per rental unit. In 2024, the VHFA awarded about $10 million in RRLF funds for the development of 265 apartments across the state, at a cost of approximately $100,000 to $125,000 per unit.

State of Washington. The Workforce Housing Accelerator Revolving Loan Fund Program, under the Washington Department of Commerce in partnership with the Washington State Housing Finance Commission, was created by the Washington Legislature in 2024 to administer loans for the development of workforce housing. The program aims to incentivize for-profit developers to build housing units for households earning 50% and 80% of AMI.

Mezzanine Financing

Mezzanine financing is a type of financing used to supplement traditional, first-priority lien loans (often bank loans) when such primary financing is insufficient to cover the full cost of a project. It is a layer of financing that fills the gap between senior debt and equity and is typically structured as subordinated debt or preferred equity or a combination of both, with the order of priority within the capital stack being as follows: (1) senior debt; (2) mezzanine financing; (3) preferred equity; and (4) common equity. Mezzanine lenders typically rank below senior lenders in their ability to claim against the borrower's assets or earnings, and in case of default, are compensated only after all senior debts are satisfied. Such lenders, however, enjoy higher rates of return due to the increased risk of the secondary lien position.

Mezzanine financing provides a great deal of flexibility. It can be used for new construction as well as acquisition of existing properties, and the proceeds can be used to fund the development or acquisition of multi-unit residential, commercial, industrial, as well as other types of properties. However, the mezzanine financing structure can be complex, and it is essential for borrowers to consult with experienced professionals, such as real estate attorneys and financial advisors, to navigate the complexities of each financing option and make an informed decision.

Examples of Mezzanine Financing Programs for Missing Middle Housing

Atlanta, GA. The Housing Opportunity Bond Fund (HOB), administered by InvestAtlanta, provides second mortgage loans to homeowners, builders, developers, and non-profits to finance a portion of the acquisition, construction, and/or renovation of workforce housing units in the City of Atlanta. The program has different requirements depending on the type and size of housing and the recipient of funds. HOB funds serve as gap or bridge loans and may be used in conjunction with other financing tools, including conventional loans and bond financing.

State of Colorado. The Middle-Income Access Program (MIAP), administered by the Colorado Housing and Finance Authority (CHFA), provides construction gap financing up to 36 months, non-recourse permanent debt for up to 15 years, and subordinate debt for the acquisition, new construction, and rehabilitation of units for renters earning between 80% and 120% of AMI. The Peña Station Development, a mixed-income development in Denver, Colorado, with 25% workforce housing and 75% market rate housing, was the first urban-oriented MIAP-funded community. Workforce housing units, reserved for tenants with incomes up to 80% of AMI, are intended to provide an attainable housing option for individuals working at the Denver International Airport. CHFA provided a $4,000,000 subordinate MIAP interest-only loan payable within three years. Other funding sources included Wells Fargo (senior lender) ($28,213,082), the City of Denver HOST ($1,000,000), the Impact Development Fund ($2,000,000), and MGL Partners (the developer).

Source: Peña Station Next

Loan Guarantee Programs

Loan guarantee programs mitigate some of the risks inherent in lending by providing partial coverage on the risk of default. These programs provide to the lenders, protection and to the borrowers, credit enhancement, thus allowing borrowers who might not otherwise have access to credit under conventional loan programs to obtain financing. There are many government-backed loan programs, both federally and locally. Nonetheless, most of the loan guarantee programs are geared towards traditional affordable housing.

Examples of Loan Guarantee Programs for Missing Middle Housing

Philadelphia, PA. The Workforce Housing Credit Enhancement Program (WHP), administered by the Philadelphia Redevelopment Authority (PRA), offers partial construction loan guarantees to developers in order to promote the development of middle-income housing within the city. The program provides credit enhancement for construction loans that cover up to 85% of construction costs and covers 25% of the construction loan for an amount not exceeding $3 million dollars. The program targets households between 80% and 120% of AMI and is available for any workforce housing project built on vacant land owned by the city in emerging neighborhoods. The city, developers, and lenders have taken advantage of the WHP incentives in an effort to meet the goals outlined in the city's 2018 housing action plan, which calls for the development of 6,000 units over the next decade. One success story under the WHP program is Francis Villas, which consists of 16 two- and three-story, 1,200 sq. ft. rowhouses in Francisville, with at least 3 bedrooms and 2 bathrooms targeted for households earning up to 120% of AMI. The developer acquired the land from the city at a discounted sale price of $228,609, which enabled the developer to offer the houses for $229,990, significantly less than the market-rate price in Francisville. The risk associated with this development was low enough not to necessitate the credit enhancement. However, other projects, such as the West Poplar Homes Development, have taken advantage of the partial guarantee.

Source: West Poplar Homes

State of Vermont. The Middle-Income Homeownership Development Program, which is administered by the Vermont Housing Finance Agency (VHFA), provides financial incentives and resources to support the development of middle-income housing units for households earning up to 120% of AMI. The program was initially funded through State and Local Fiscal Recovery Funds (SLFRF) allocated under the American Rescue Plan Act of 2021 (ARPA) and has since been funded through state appropriations. The program provides (a) construction loan guarantees not exceeding 15% of development costs and (b) development subsidies not exceeding 35% of development costs on eligible homes. In 2023, the VHFA awarded approximately $23 million to 24 homeownership projects, which are projected to create 172 middle-income housing units across the state.

In the Context of Missing Middle Housing

Because capital lending tools are so flexible, they can be used to support a variety of needs in the missing middle housing industry. Capital programs play an important role in supporting new constructions, property improvements, and acquisitions. Some common features of these programs include (a) supporting development of units for households generally between 60% and 120% AMI; (b) leveraging strategic opportunities to use publicly owned vacant land within appreciating neighborhoods; (c) ensuring workforce housing units are deed restricted as affordable; and (d) complementing, rather than replacing, traditional financing mechanisms. These programs offer benefits to developers, lenders, and governmental entities alike. To the developer, the programs defray the costs of developing missing middle housing. To the lenders, the programs offer security through credit enhancement for the developer or additional sources of funds within the capital stack. And to the governmental entities offering the incentives, increased attainable housing stock and, in many cases, revenues from, for instance, the sale of land.

Every missing middle housing project is different, and thus the financing needs must be matched to the right financing product. Due to the versatility of capital lending tools, the financing products can be tailored to finance almost all elements and stages of a missing middle development.

Access to Capital Lending Tools Resources

CDFA Revolving Loan Fund Resource Center; www.cdfa.net/cdfa/cdfaweb.nsf/resourcecenters/rlf.html

CDFA Revolving Loan Fund Finance Update Newsletter;
www.cdfa.net/cdfa/cdfaweb.nsf/newsletter.html?open&news=888990616&archive=show&pager=hide

Janover, Inc.; https://www.multifamily.loans/multifamily-financing

Dealpath; https://www.dealpath.com/blog/what-is-real-estate-mezzanine-loan-definition/

Investopedia; https://www.investopedia.com/terms/m/mezzaninefinancing.asp

Find Venture Debt; https://www.findventuredebt.com/types-of-venture-debt/mezzanine-financing

CGap; https://www.cgap.org/sites/default/files/researches/documents/CGAP-Donor-Brief-Housing-Microfinance-Aug-2004.pdf

Federal Support Tools

Federal support tools can fit into other categories of the Development Finance Spectrum, including bedrock tools, targeted tools, access to capital lending tools, or investment catalyst tools. Federal support tools, however, tend to be more flexible than most other tools within the development finance spectrum and are often used as gap financing measures. There are hundreds of federal support programs that finance various eligible uses as provided in federal statutes and regulations. Most of these programs provide financing to state and local governments. Others provide funding to nonprofit and for-profit organizations and industries, as well as natural persons. Federal support tools are often guarantees, loans, or grants, typically available on an annual basis. Some programs are, however, available for a set period or in response to specific financing challenges or economic situations. For instance, in 2021, the 117th United States Congress passed the American Rescue Plan Act (ARPA), a $1.9 trillion economic stimulus package aimed at helping communities recover from the COVID-19 public health crisis. As authorized under ARPA, the Coronavirus State and Local Fiscal Recovery Funds (SLFRF) program allocated $350 billion to state, territorial, local, and tribal governments for eligible uses responsive to the economic and health effects of the COVID-19 pandemic.

Federal support tools are intended to supplement, rather than substitute, state, and local efforts. Coordination between federal and state and local agencies dictates the efficacy of federal programs. Federal agencies often publish program guidelines and reference guides and, in some cases, offer technical assistance and resources to help communities navigate federal funding programs. On the other hand, state and local agencies often employ program coordinators and professionals who provide assistance at the local level. For instance, HUD administers the HOME Investment Partnerships Program (HOME), which provides formula grants to states and local governments for the purposes of financing various housing projects, including the construction, acquisition, and rehabilitation of affordable rental and owner-occupied units. Often in partnership with local nonprofit organizations, local governments in turn use the grant proceeds and other available funds to finance housing projects and provide direct rental assistance to qualifying homebuyers, particularly low- and moderate-income persons. There are several federal programs that finance affordable housing, including LIHTC, HOME, the Choice Neighborhood Initiative, and the Community Development Block Grant (CDBG) Program.

Examples of Federally Funded State and Local Programs for Missing Middle Housing

State of Michigan. The Missing Middle Housing Program (MMHP), which is administered by the Michigan State Housing Development Authority (MSHDA), is designed to address the lack of attainable housing and other housing challenges amplified by the COVID-19 pandemic. The MMHP is intended to defray costs for developers investing in, constructing, or substantially rehabilitating rental and single-family housing units targeted at residents with household incomes between 60% and 120% of AMI. The program aims to increase the supply of workforce housing and encourage economic mobility in Michigan. The MMHP is funded by federal resources allocated under ARPA. As of the date hereof, $110 million in ARPA funds from the United States Department of Treasury has been dedicated to the program. MSHDA is exploring new funding sources for future grant cycles.

State of Rhode Island. The Middle Income Loan Program, which is administered by Rhode Island Housing, seeks to promote the development of affordable housing units for households earning between 80% and 120% of AMI. The program is funded by the SLFRF allocated to the state under ARPA. The program offers deferred loans secured by mortgage and deed restriction for rental units and 0% loans secured by deed restriction for non-rental units. In connection with rental units, at least 20% of units in the development must be income restricted. Rhode Island Housing aims to commit $20 million by December 31, 2024, through several competitive funding rounds.

Tigard, OR. The Middle Housing Revolving Loan Fund, managed by the Network for Oregon Affordable Housing, Craft3, and the Community Housing Fund, was created to increase missing middle housing in the City of Tigard. In addition to other loan conditions, a minimum of 30% of the units must be offered to low-to-moderate income homebuyers with household income not exceeding 100% AMI. The city used ARPA funds to finance the program.

In the Context of Missing Middle Housing

Federal support tools can play a pivotal role in catalyzing missing middle housing projects. However, missing middle housing has traditionally been ineligible for tax credits as well as other federal, state, or local support tools. These tools are often limited to projects that restrict units for tenants earning less than 60% AMI (in rare cases, up to 80% AMI), which edges out the middle-income workforce with incomes too high for affordable housing but too low for market rate housing. Consequently, there have been ongoing discussions and a variety of proposed federal programs addressing the housing shortage. For instance, legislation has been introduced to establish a Workforce Housing Tax Credit (WHTC) for middle-income families. If passed, the WHTC would be the first-ever middle-income housing tax credit and would finance approximately 344,000 rental units. The program would build on the LIHTC program, which targets tenants below 60% AMI, by providing additional tax credits for households earning between 60% and 100% of AMI. Moreover, the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac), both government-sponsored enterprises, each have programs steering financing towards workforce housing.

Appendix A provides an array of federal support tools (and links to the respective federal support resources) that may be leveraged in connection with housing developments. Developers should, however, note that, due to the proliferation of federal programs, the list provided in Appendix A is not exhaustive.

Federal Support Tools Resources

Internal Revenue Service (IRS); https://www.irs.gov/

National Park Service (NPS); https://www.nps.gov/index.htm

U.S. Department of Agriculture (USDA); https://www.usda.gov/

U.S. Department of Energy (DOE); https://www.energy.gov/

U.S. Department of Health and Human Services (HHS); https://www.hhs.gov/

U.S. Department of Housing and Urban Affairs (HUD); https://www.hud.gov/

U.S. Department of the Treasury; https://home.treasury.gov/

U.S. Department of the Treasury: CDFI Fund; https://www.cdfifund.gov/

U.S. Economic Development Administration (EDA); https://www.eda.gov/

U.S. Environmental Protection Agency (EPA); https://www.epa.gov/

U.S. Small Business Administration (SBA); https://www.sba.gov/

State and Local Support Tools

Like federal support tools, there are many state and local government capital support tools ranging from grants and loans to tax exemptions and other subsidies and incentives. Some of these tools, such as bond financing, are discussed in other sections of this Toolkit.

The lack of affordable housing for low- and moderate-income households has adversely affected the economic mobility of workers and families and caused workforce shortages throughout the nation. In response to the housing shortage for medium income households, many states and local governments have adopted measures to incentivize developers to build middle income housing. These measures are expansive, including, but not limited to, (a) providing grants, loans, real estate tax exemptions, subsidies, and other financial incentives; (b) loosening land use and zoning restrictions and providing density bonuses; (c) streamlining the development process including permitting, licensing and inspections; (d) building capacity and boosting access to capital for small-scale developers; (d) integrating middle housing and transit-oriented development into existing neighborhoods; (e) abating the cost of land acquisition for infill developments and other housing projects; (f) forming public-private partnerships with various stakeholders within the workforce and deed-restricted housing market; (g) providing technical assistance and training resources; and (h) providing down-payment assistance to first-time and second-time homebuyers.

State Grant and Loan Programs

State and local governments provide homeownership opportunities to low- and middle-income individuals and families through a variety of loan, grant, and guarantee programs. These programs make funding available to for-profit and non-profit developers as well as individuals to finance vital improvements and often leverage private sector investment to ensure sustainability and long-term affordability. Eligible uses for program funds often include new construction, rehabilitation of existing property, and adaptive reuse and conversion of market-rate units to income- and rent-restricted rental- and owner-occupied units. Most medium-income housing is reserved for individuals and households earning above 60% AMI.

Examples of State Grant Programs for Missing Middle Housing

State of California. The California Accessory Dwelling Units Grant Program, administered by the California Housing Finance Agency, offers grants of up to $40,000 to reimburse developers of medium-density ADUs for qualifying pre-development and non-recurring closing costs.

State of Georgia. The Rural Workforce Housing Initiative, administered by the Georgia Department of Community Affairs and the OneGeorgia Authority, offers grants, loans, and other forms of assistance through the OneGeorgia Equity Fund. Workforce housing funds are awarded on a competitive basis to projects addressing (a) ongoing workforce housing needs, as evidenced by recent housing studies; (b) workforce needs in areas or communities with low unemployment rates; or (c) a commitment by a community or region to expand and improve its existing housing stock. The program is financed through state appropriations and was initially allocated $35.7 million in 2023, with an additional $50 million requested for Fiscal Year 2024 and an extra $6 million for Fiscal Year 2025. Financing for workforce housing is limited to no more than $1,000,000 per applicant and development, while infrastructure grants are limited to no more than $2,500,000 per application and development. The workforce housing program targets housing projects for households between 60% and 150% AMI. As of the date hereof, the Rural Workforce Housing Initiative has awarded approximately $24 million in infrastructure grants to local governments that will fund the construction of more than 1,000 units. Applications are due quarterly on the 2nd Friday of January, April, July, and October.

State of Kansas. The Moderate Income Housing Program (MIH), administered by the Kansas Housing Resources Corporation and funded through the State Housing Trust Fund (SHTF), provides grants and loans to local governmental units with populations fewer than 60,000 for the construction of, conversion to, or rehabilitation of single or multi-family properties for homeownership or rental purposes. In Fiscal

Year 2024, the program was allocated approximately $60 million in response to the rising need for moderate income housing. A portion of the program was financed using SFRF funds received under ARPA. MIH financing is limited to no more than $650,000 per awardee, with funds issued through multiple application rounds. During the second round of funding in Fiscal Year 2023, SHTF awarded about $13.6 million in MIH funds, in addition to $5.4 million in Kansas Housing Investor Tax Credits. The City of Pittsburg, for instance, received $840,000 in MIH funds. The city has formerly used MIH funds to successfully redevelop a city block that previously housed an elementary school. The city used the MIH funds to relocate water and sewer lines in addition to providing homebuyer assistance in connection with the development of 10 single-family units costing approximately $166,750 per unit.

Source: City of Pittsburg

State of Massachusetts. The Massachusetts Workforce Housing Initiative (MWHI), administered by MassHousing, provides up to $100,000 of subsidy per workforce housing unit for households earning 60 to 120% of AMI, with a preference on new construction. To date, MassHousing has invested more than $100 million in MWHI. The Gateway North Development, a 71-unit mixed-income development with 53 affordable housing units, 10 workforce units and 8 market-rate units, was the first to receive funds through the program. The units include one-, two-, and three-bedroom apartments with access to a gym and community room. The development was built on a vacant parking lot and received $21 million in MassHousing financing, including $1.6 million in MWHI funds. Additional financing came from various sources, including the City of Lynn HOME funds and the Massachusetts Department of Housing and Community Development.

Source: Gateway North

State of Minnesota. The Workforce Housing Development Program (MHDP), administered by Minnesota Housing, provides deferred loans for the purpose of financing market-rate residential workforce rental housing. WHDP financing is available as zero-interest, three-year deferred loans. The loans are unsecured and forgivable. In Fiscal Year 2024, the program had $39 million in available MHDP funds. The funds are awarded to local governmental entities and communities, which in turn provide loans or grants to developers of mixed-income residential rental properties. Eligible projects include market-rate as well as rent- and income-restricted rental units.

State of Nebraska. The Middle Income Workforce Housing Investment Fund (MWHF), which is administered by the Nebraska Department of Economic Development (NDED), provides matching grants to non-profit development organizations that award funds to workforce housing projects located in Lancaster, Sarpy, and Douglas counties. In addition to the MWHF program, the state has two Workforce Housing Match (WHM) programs administered by the Nebraska Investment Finance Authority (NIFA): (a) the Rural Workforce Housing Match Program (RWH), and (b) the NIFA Urban Workforce Housing Match Program (NUW-HOM). The WHM programs require a percentage of housing units to be targeted to moderate income households earning not more than 150% of AMI for a family of four (currently, $160,092).

Land Use and Zoning Laws

The missing middle housing crisis arose from restrictive land use and zoning laws that traditionally prevented the development of multi-unit and mixed-use housing units. In view of this historical background, there has been a proliferation of zoning law changes allowing Expanded Housing Options (EHO). The EHO laws allow for the development of medium-density housing, including duplexes, triplexes, quadplexes, and multiplexes, in areas zoned for conventional single-family housing.

In addition to EHO zoning laws, state and local jurisdictions have pursued several land use and zoning solutions in connection with missing middle housing, including: (a) adopting pre-approved housing plans and other cost and time saving measures; (b) eliminating parking minimums in order to lower costs and increase the amount of land available for housing units; (c) relaxing minimum lot sizes; (d) promoting infill and transit-oriented development on vacant or under-utilized parcels within existing urban areas; (e) promoting brownfield and greyfield redevelopment; (f) providing technical assistance and guidance; and (g) offering developers and builders other financial incentives including density bonuses, property tax exemptions and abatements, and subsidized land acquisition costs. Developers should explore all available incentives offered by the state and local jurisdictions where prospective housing projects will be located.

Examples of Land Use and Zoning Efforts in the Missing Middle Housing Context

Breckenridge, CO. In 2022, the Town of Breckenridge created a Workforce Housing Five-Year Blueprint for deed-restricted housing. Under its Five-Year Plan, the town plans to invest $50 million in workforce housing, which will potentially incentivize more than $300 million in private sector investment and add 150 to 200 deed-restricted units per year. Before adopting the Blueprint, the town had 1,130 workforce units. In 2022, the town added 179 units in both new constructions and conversions of existing housing into deed-restricted housing, and in 2023, added 96 additional units. The town has set a goal of having 193 additional units in 2024, 173 additional units in 2025, 75 additional units in 2026, 103 additional units in 2027, and 111 additional units in 2028.

Buffalo, NY. In 2017, the City of Buffalo implemented the Buffalo Green Code, which, among other things, (a) expanded housing options in areas zoned for mixed-use, allowing for stacked units, row homes, and carriage homes, albeit not eliminating single-family zoning; (b) encouraged the development of walkable, mixed-use neighborhoods and infill development; and (c) eliminated minimum parking requirements.

Minneapolis, MN. The 2040 Minneapolis Comprehensive Plan allows multi-unit developments to be constructed in single-family plots throughout the city. When the city adopted these EHO regulatory reforms in 2020, it became the first large city in the nation to eliminate single-family residential zones.

Portland, ME. In 2008, the City of Portland created its Infill Design Toolkit as a guide for developers, builders, and property owners involved in designing, building, or participating in medium density infill developments within the city. The toolkit includes an overview of housing types, neighborhood patterns, and design strategies and provides models of residential infill developments and examples of previously approved projects. The toolkit is a great starting point for developers and builders locating housing projects on infill parcels within the city.

State of Maine. In 2023, the Maine Legislature enacted LD 2003, "An Act To Implement the Recommendations of the Commission To Increase Housing Opportunities in Maine by Studying Zoning and Land Use Restrictions," which, among other things, requires that municipalities (a) allow between two and four housing units per lot in areas zoned for residential use, and (b) allow ADUs on land zoned for single-family housing.

State of Montana. In 2023, Montana passed a zoning reform package that included four bills: (a) Senate Bill 323 allowing duplex housing on lots zoned for single-family residences and streamlining the permitting process for commercial and residential developments by eliminating the requirement for review of designs by local boards; (b) Senate Bill 382 requiring local governments to update their land use plans and zoning and subdivision regulations and changing the approval process for housing developments; (c) Senate Bill 528 allowing the construction of ADUs; and (d) Senate Bill 245 allowing multi-unit and mixed-used developments in areas previously zoned for commercial uses. The Gallatin County District Court subsequently issued a preliminary injunction against Senate Bill 323 and Senate Bill 528, preventing the laws from going into effect.

State of Oregon. In 2019, the Oregon Legislature passed a bipartisan bill, House Bill 2001, requiring municipalities to provide middle housing choices to residents. The bill requires cities to update their zoning requirements. Cities with populations greater than 10,000 and less than 25,000 are required to allow, at a minimum, the development of duplexes. Cities with populations greater than 25,000 are required to allow for the development of all medium density housing types, including duplexes, triplexes, quadplexes, cottage clusters, and townhouses.

Pre-Approved Housing Plans

A growing number of communities are considering pre-approved housing plans as cost- and time-saving measures intended to reduce costs and delays in the housing approval process. In practice, the authorizing jurisdictions review and approve a list of housing types and designs, subject to land use and zoning regulations. Catalogues of the pre-approved, permit ready plans are then made available to developers and builders seeking approval on housing developments. The purpose of these plans is to fast-track the permitting process. Approved units must be built in accordance with the plans, including all architectural and design elements, with minor variations permitted. The plans are made available to developers and homebuilders generally at no cost. In theory, this is a straightforward process. However, the implementation of pre-approved plans can be nuanced and technical.

Examples of Pre-Approved Plans in the Missing Middle Housing Context

Omaha, NE. The 2024 Duplex by Design Contest, hosted by Omaha by Design in partnership with AARP, the City of Omaha, and other local agencies, was created to raise awareness on the need for missing middle housing, especially for the aging population. The contest asked participants to create workable duplex designs for age-accessible and affordable units. AARP awarded Omaha by Design a Demonstration Grant of approximately $24,000. The contest received about 20 duplex plans, with 3 designers winning the contest. The winners received cash prizes, and their designs are scheduled to be featured in the

Affordable by Design Playbook published by Omaha by Design. The Omaha Planning Department also agreed to create a "fast-track program" under which the winning designs may be pre-approved by the city, streamlining the duplex approval process.

Pittsburg, CA. The City of Pittsburg has adopted Pre-approved Plans for ADUs and Junior ADUs (JADUs) in an effort to increase housing options for low- and moderate-income residents.

South Bend, IN. The City of South Bend has adopted a Pre-approved Plan Catalog with housing plans for small- to middle-scale infill housing developments within the city. The catalog is available to individuals and developers at no cost.

In the Context of Missing Middle Housing

State and local governments have in recent years pursued a variety of affordable housing solutions to increase missing middle housing and bring down prices for renters and homeowners. These support tools are intended to incentivize developers and homebuilders to design and build affordable homes for medium income households, including infill and transit-oriented developments and conversions. Efforts to create innovative financing schemes and streamline review and permitting processes are ongoing and will likely continue to proliferate in the next 10 years.

Developers should note that the federal, state, and local programs described herein are authorized under the laws of the respective jurisdictions as of the date of this Toolkit. The information provided was taken from individual federal, state, and local agencies to ensure accuracy. However, due to the nature of public governance, legislation, and budgeting, federal, state, and local programs are often subject to amendment and/or repeal. There is no guarantee that the public finance programs described in this Toolkit will be funded in the future. Developers should check with each federal, state, and local agency before attempting to pursue financing under the programs described in this Toolkit. Moreover, the financing tools and incentives described herein are a small, non-exhaustive sampling of the programs available. Developers should consult local development finance agencies and professionals for a more comprehensive examination of available financing options for any proposed development.

State and Local Tools Resources

National Conference of State Legislatures (NCSL); https://www.ncsl.org/human-services/middle-housing-filling-a-gap-in-available-housing-options

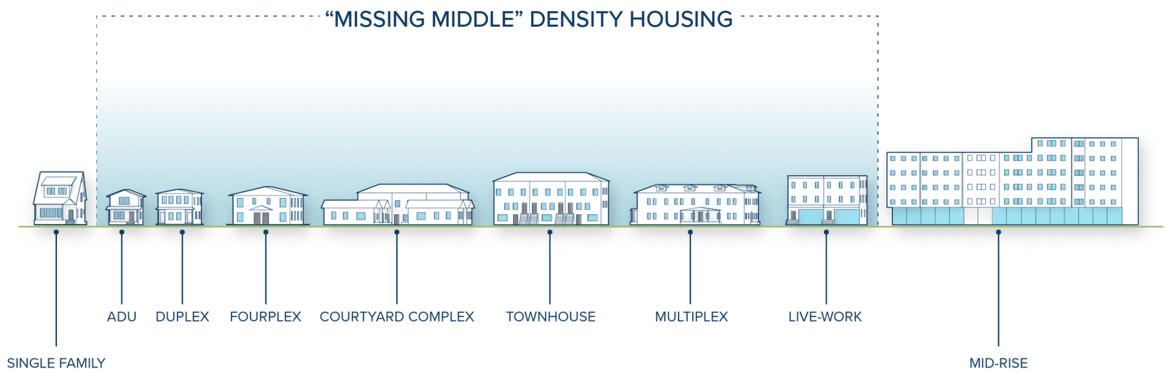
Planetizen; https://www.planetizen.com/features/130226-top-10-tips-cities-considering-pre-approved-housing-plans

Joint Center for Housing Studies of Harvard University; https://www.jchs.harvard.edu/blog/middle-income-housing-programs-emerge-affordability-challenges-climb-income-ladder

Summit Daily; https://www.summitdaily.com/news/can-breckenridges-workforce-afford-to-live-there-a-multimillion-dollar-plan-aims-to-help/

Recommendations

Addressing the shortage in missing middle housing requires a multifaceted approach. This Toolkit has recommended several potential solutions in connection with these developments. However, on a high-level view, there are two main solutions, namely, zoning reforms and public-private partnerships. Relaxing restrictive and outdated zoning codes that have historically favored single-family homes paves the way for medium-density housing options. Moreover, collaborations between developers, public entities, philanthropic organizations, and investors can leverage resources to scale up middle housing projects.



Source: Regional Plan Association

Policy Reforms

Many of today's zoning regulations were established in the 1940s and 1960s, primarily to promote single-family detached housing and enforce bulk standards. These outdated rules hinder the development of medium-density housing, limiting opportunities for developers and architects to create much-needed, missing middle housing. Areas with strict zoning often miss out on cost-effective construction options, despite having robust transportation networks and emerging job opportunities. Without adequate housing to support the workforce, these communities risk stifling their own economic growth.

Missing middle housing offers a creative and sustainable approach to making the most of small spaces, fostering community-oriented, affordable living. To address these challenges, it's crucial for developers and municipalities to collaborate in revising outdated and biased zoning regulations.

> "It takes creativity to make these kinds of transactions work. We have to look at housing differently because we are not able to build ourselves out of this housing demand supply gap."
>
> Brenda Weaver, Community Ventures

Brenda Weaver has worked in real estate finance for 50 years. According to her, "For non-profits looking to make swift change, the magic to it is getting everyone in the community to come to the table and to have brought their own dish." Developers must approach municipalities with a proactive mindset. Advocating for missing middle housing-friendly zoning regulations should also include a commitment to collaboration. Here are some strategies to enhance this dialogue:

Creative Solutions: Policy Reform

Build Relationships	• Establishing strong connections with community members, city leaders, and planners can create a foundation of receptivity for discussions about missing middle
Advocate for Community Benefit Agreements	• Propose shared parking solutions instead of requiring per-unit garages, with the condition that there will be development of community spaces, such as parks
Request Relaxation of Building Height Regulations	• Encourage adjustments that enable the construction of 2–6-unit housing on existing lots, increasing housing options
Demonstrate Community Needs	• Gather and present data to highlight the demand for more bedrooms, making a compelling case for the necessity of missing middle housing

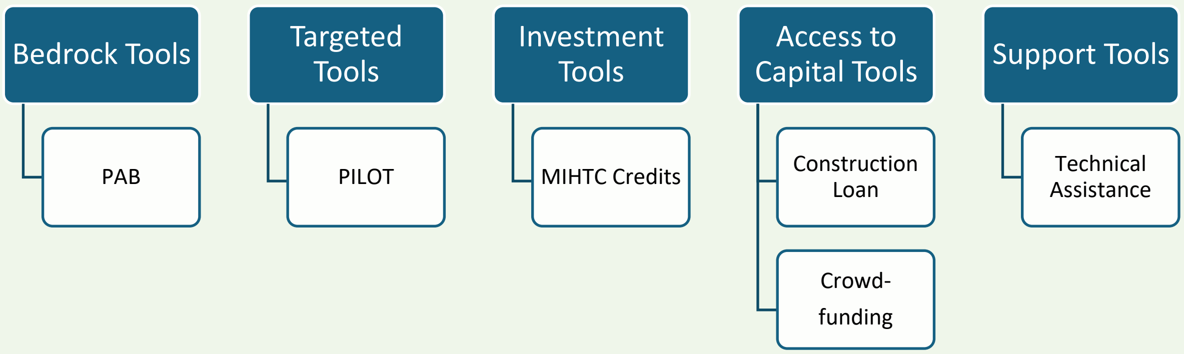
By approaching these conversations with a collaborative spirit and clear proposals, developers can help pave the way for meaningful zoning changes that benefit both the community and the housing market. Cities that involve developers in the reform process tend to achieve faster progress in providing the affordable housing that is essential. It's crucial for cities to first understand the needs of architects and developers and then integrate those insights into their reform plans. By fostering this collaborative approach, municipalities can create more effective strategies that align with the realities of the housing market, ultimately accelerating the delivery of affordable housing solutions.

Blended Development Finance

The lack of access to capital for developers in the missing middle housing industry does not have a one-size-fits-all solution. Public sector funds and incentives cannot bridge the gap alone. And neither can private sector programs. However, when combined, public and private sector interventions can result in a solution that benefits all parties. Developing risk-sharing partnerships between developers, investors, and governments can help mitigate the perceived risks associated with missing middle projects. These partnerships are the focus of blended finance, a structuring approach focusing on the use of development finance tools as well as philanthropic funds as a catalyst for private sector investment in sustainable development. This approach leverages the risk tolerance and return expectations of market participants, enhancing an investment's potential return or mitigating its risk factors in order to make it more attractive to private investors. In blended finance transactions, public and/or philanthropic entities incentivize private investments by intervening in several ways, including (a) providing catalytic or concessional capital, (b) providing guarantees to lenders, (c) purchasing insurance against certain risks, (d) providing technical assistance, policy, and transactional advisory services, or (e) otherwise assisting in the development of the project.

Example of Blended Finance in Missing Middle Housing

Assume that a developer intends to build a missing middle housing development on an abandoned lot owned by a city in Colorado. The developer has several financing tools available. For instance, the developer might approach the city and seek a payment-in-lieu-of-taxes (PILOT) in order to limit or defer the property taxes on the development. The developer might also approach CHFA and apply for, among other things, (a) MIHTC credits, (b) construction loan, and/or (c) below-market financing through PABs. Additionally, the developer might explore crowdsourcing through a real estate crowdfunding platform such as Small Change as well as local technical assistance programs such as the use of inmate labor to build attainable housing.



If used effectively, this blended structure would create substantial cost savings for the developer. The developer could use these interventions to subsize or cover development costs, including capital costs (site planning, construction), operating costs (building operations, staffing), and program costs (social services).

The lack of blended capital can hinder the ability of developers to meet their needs. Blended finance combines various forms of tools and incentives to make funding more suitable for the needs of developers in the missing middle housing market. This blending can occur in different ways and at different stages of the development. In many cases, the intervention by public, philanthropic, or private entities may not involve cash but rather services and other cost-saving measures that can make a real estate development worthwhile. Blended finance has been used in a variety of contexts and has a successful track record. Nonetheless, for blended finance to have a significant positive impact, a variety of tools must be utilized. Developers should research and keep up to date on financing and incentive programs as they become available.

Development Finance in Action

Case Study: Gateway Oak Cliff Project

Project Overview

The Gateway Oak Cliff Project is a mixed-income housing development located in the Oak Cliff Gateway TIF District in Dallas, Texas. Situated on the former site of the Dallas County Government Center, the project aims to address the growing need for affordable housing in the area. By combining affordable housing, urban design improvements, and strategic financing, the Gateway Oak Cliff Project seeks to create a vibrant and sustainable community.

Key Features

- ☐ Mixed Income Housing: 80% of the 230 total units will be rent-restricted.
- ☐ Urban Design: The project emphasizes preserving existing trees, designing buildings that fit the neighborhood context, and creating a pedestrian-friendly environment.
- ☐ TIF Subsidy: The City of Dallas has provided a TIF subsidy of up to $4.245 million to support the project.
- ☐ Developer: Gateway Oak Cliff, LP, a Texas limited partnership, is developing the project with equity investment from National Equity Fund.

Project Goals

- ☐ Address housing affordability: The project provides affordable housing options in a gentrifying area.
- ☐ Enhance urban design: The development has a shared green space and walking paths that create a more walkable and sustainable neighborhood.
- ☐ Leverage TIF funds: The developer will utilize TIF funds to bridge the gap between project costs and available financing.

Financing Structure

- ☐ TIF subsidy: The TIF subsidy will be used to offset higher construction costs and the increased cost of permanent debt.
- ☐ Developer fee: A portion of the developer fee will be deferred to provide a contingency fund for potential cost overruns.

☐ Non-City resources: The developer will be required to maximize non-City resources to fill the funding gap.

Sources	Amount	Percent
Permanent Loan (Citi Community Capital)	$24,300,000.00	53.00%
3rd Party Equity as 4% LIHTC (National Equity Fund)	15,623,419.00	34.00%
Deferred Developer Fee	1,800,000.00	4.00%
City (Oak Cliff Gateway TIF Funds)	4,245,432.00	9.00%
Total Sources	**$45,968,851.00**	**100.00%**

Sources: Gateway Oak Cliff and Texas Department of Housing and Community Affairs (TDHCA)

Case Study: Community Gardens Project

Project Overview

Community Gardens is a Pocket Neighborhood in Springfield, Ohio. The $10.4 million project was unveiled in October 2018 and includes 50 freestanding rental houses with individual covered front porches that open into a shared green space, with each unit designed for comfortable aging in place. More than 500 applications were received within the first few weeks of opening. The neighborhood is fully occupied with a significant waitlist. Developers have planned a second phase of the development and hope to add 60 one-bedroom units and a community building with a fitness room and gathering space. Although targeted towards traditional affordable housing, this case study showcases blended development finance in action.

Key Features

- ☐ Location: The neighborhood was built on the former site for Springfield Regional Medical Center.
- ☐ Mixed Income Housing: Of the 50 total units, 30 are open to tenants earning up to 60% of AMI, 12 up to 50% of AMI, and 8 for 30% of AMI or less.
- ☐ Age in Place Housing: Suitable for low-income seniors aged 55 and older.
- ☐ Design: The Pocket Neighborhood is designed to encourage social interaction and a strong sense of community and includes 2-bedroom ranch-style houses with attached garages facing an access road, all arranged in clusters of 8 to 12 homes and facing a shared green space.
- ☐ Developers: The Neighborhood Housing Partnership of Greater Springfield (NHP) and the Buckeye Community Hope Foundation (BCHF).

Project Goals

- ☐ Address housing affordability for seniors: Units are single-story, fully accessible with no steps and walk-in showers, suitable as age-in-place residences.
- ☐ Create a more walkable and sustainable neighborhood: Garages face away from the shared green space, leaving the neighborhood vehicle-free and walkable.
- ☐ Enhance community interaction: The development has open spaces and outdoor recreation, including interconnected walking trails, a gazebo, and a playground.
- ☐ Emphasize privacy: Units have covered front porches, offering privacy.

Financing Structure

- ☐ Private Investment: Developers sold ownership interests in the project to investors in exchange for LIHTC credits.
- ☐ Government subsidies: The project was financed through various government programs.
- ☐ Developer fee: A portion of the developer fee was deferred to provide for potential cost overruns.

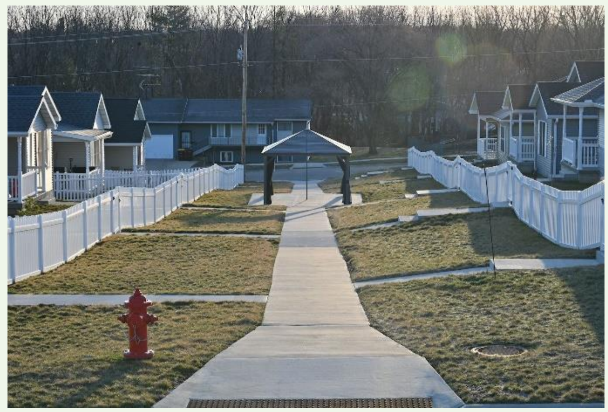
Sources	Amount	Percent
3rd Party Equity through LIHTC	$9,000,000.00	86.05%
Deferred Developer Fee (BCHF)	815,572.00	7.80%
Affordable Housing Grant (Federal Home Loan Bank)	423,075.00	4.04%
City (Federal HOME Funds)	220,908.00	2.11%
Total Sources	**$10,459,555.00**	**100.00%**

Source: HUD Office of Policy Development and Research

Case Study: Bear River Cottages

Project Overview

The Bear River Cottages project is a Pocket Neighborhood located in Maquoketa, Iowa. The $2.3 million project was completed in 2022 and includes 10 single-family homes with a shared common courtyard. The homes sold for about $150,000 per unit, with the developer, in partnership with the Eastern Iowa Housing Trust Fund (EIHTF), offering homebuyers $10,000 in down-payment assistance and the Iowa Economic Development Authority providing an additional $15,000 towards each down payment.



Key Features

- ☐ Location: The neighborhood was built on land formerly owned by Jackson County and is located northeast of Highways 61 and 64, off Creslane Drive.
- ☐ Mixed Income Housing: Restricted to tenants earning up to 80% of AMI, which is about $35,800.
- ☐ Design: Includes 10 single-family bungalow style homes with two-bedroom, two-bathroom 1,060-square-foot units, located on 2.5-acres and facing a shared green space.
- ☐ Developer: East Central Development Corporation (ECDC).

Project Goals

- ☐ Address housing affordability: Intended as an affordable housing option for first-time homebuyers.
- ☐ Create more housing in rural Iowa: Intended to address the housing shortage in Jackson County and Maquoketa, with about 300 new homes needed by the year 2030.
- ☐ Enhance community interaction: Shared open spaces will create the sense of a close-knit community. The development features a central shared courtyard with units facing inward, with raised gardens, a green space, and a pergola possibly included, and a homeowner's association for maintenance of the common spaces.

Financing Structure

- ☐ Federal subsidies: The project received an Affordable Housing Program (AHP) grant from the Federal Home Loan Bank (FHLB) of Des Moines, along with other grant funding sources.
- ☐ Local subsidies: The project site was purchased for $10 from Jackson County and added into the city's Urban Renewal Plan in order to receive TIF funds for public infrastructure improvements, including the extension of water, sewer, and streets to the site.

☐ Community partnership: Three undergraduate students studying civil engineering at the University of Iowa created the original design plans as part of their senior capstone project, saving time and money.

Sources	Amount	Percent
AHP Grant (FHLB of Des Moines)	$200,000.00	8.69%
Equity Contribution (EIHTF)	250,000.00	10.87%
City (TIF Financing)	450,000.00	19.57%
Other Sources (County, Community, etc.)	1,400,000.00	60.87%
Total Sources	**$2,300,000.00**	**100.00%**

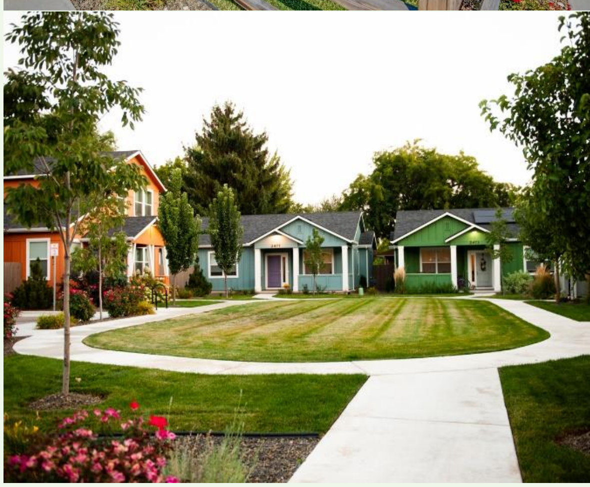
Source: The Gazette

Case Study: Cole Bluff Cottages

Project Overview

Cole Bluff Development is a Pocket Neighborhood in Boise, Idaho. The project was developed in two phases, with the last phase completed in 2023, and includes 39 single family units with 46 parking spaces, remote and connected garage parking, landscaping, community gardens, and a shared courtyard. The units are estimated to sell for as low as $300,000.






Key Features

- ☐ Location: The neighborhood was built on the former site for the Cole School, at the southwest corner of Cole Road and Fairview Avenue.
- ☐ Mixed Income Housing: 30% to 40% restricted to 80% of AMI, and remainder sold at market rate.
- ☐ Design: The Pocket Neighborhood is designed to encourage social interaction and a strong sense of community and includes single family homes with 1 to 3 stories and 2 to 4 bedrooms, ranging between 816 sq. ft. and 1,998 sq. ft.
- ☐ Developer: NeighborWorks® Boise (NWB).
- ☐ Architect: Slichter Ugrin Architecture Inc. of Boise, with some designs developed by Sherry McKibben of Boise.

Project Goals

- ☐ Address housing affordability: Creates affordability through the land trust model, with the trust retaining part ownership for the income-restricted units.
- ☐ Create a more walkable and sustainable neighborhood: Cars and parking spaces are located on the perimeter of the development to foster walkability.
- ☐ Emphasize energy efficiency: Units are Energy Star Certified, solar-ready, and have electrical vehicle outlets.
- ☐ Enhance community interaction: The central communal space, with gazebos and common areas, builds a sense of community and encourages interaction and community building.

Financing Structure

- ☐ Government subsidies: The project was financed by, among others, the City of Boise (HUD commercial development block grants) and the Idaho Housing and Finance Association.
- ☐ Philanthropy: A portion of the development was financed by charitable organizations such as the Harry W. Morrison Foundation.

Source: NeighborWorks Boise

APPENDICES

Appendix A: Federal Support Tools

Fannie Mae Programs

- ☐ Construction-to-Permanent Loans

Freddie Mac Programs

- ☐ Workforce Housing Preservation Program
- ☐ Employer-Enabled Permanent Supportive Housing
- ☐ Develop the Developer Program

Internal Revenue Service (IRS)

- ☐ Energy Efficient New Homes Tax Credit for Home Builders
- ☐ Modified Accelerated Cost-Recovery System (MACRS) and Bonus Depreciation

National Park Service (NPS)

- ☐ Historic Preservation Tax Incentives
- ☐ Historic Preservation Fund Grants

U.S. Department of Agriculture (USDA)

- ☐ Multi-Family Housing Direct Loans
- ☐ Multi-Family Housing Loan Guarantees
- ☐ Rural Business Development Grants
- ☐ Business and Industry Loan Guarantees Program
- ☐ Intermediary Relending Program

U.S. Department of Energy (DOE)

- ☐ Energy Efficiency and Conservation Block Grant Program

U.S. Department of Health and Human Services (HHS)

- ☐ HHS Community Services Block Grant Program

U.S. Department of Housing and Urban Affairs (HUD)

- ☐ HUD Community Services Block Grant Program
- ☐ HOME Investment Partnerships Program (HOME)
- ☐ Community Services Block Grant Entitlement Program
- ☐ Community Services Block Grant Insular Areas Program
- ☐ Low-Income Housing Tax Credit (LIHTC)
- ☐ Neighborhood Stabilization Program
- ☐ Non-Entitlement CDBG Grants in Hawaii
- ☐ Rural Housing and Economic Development Program
- ☐ Section 108 Loan Guarantee Program
- ☐ HUD Multifamily Loans
  - HUD 207 Loans
  - HUD 213 Loans
  - HUD 220 Loans
  - HUD 221(d)(4) Loans
  - HUD 223(a)(7) Loans
  - HUD 223(f) Loans

- HUD 231 Loans
- HUD 234(d) Loans
- HUD 241(a) Loans

☐ Self-help Homeownership Opportunity Program
☐ State Community Services Block Grant Program
☐ State Community Services Block Grant: Colonias Set-Aside

U.S. Department of the Treasury

☐ 1603 Program: Payments for Specified Energy Property in lieu of Tax Credits
☐ Office of Small and Disadvantages Business Utilization
☐ State Small Business Credit Initiative (SSBCI)

U.S. Department of the Treasury: CDFI Fund

☐ Community Development Financial Institution (CDFI) Program
☐ Native Americans CDFI Assistance Program
☐ New Markets Tax Credit (NMTC) Program
☐ Bank Enterprise Award Program

U.S. Economic Development Administration (EDA)

☐ Economic Adjustment Assistance Program
☐ Public Works Program
☐ Local Technical Assistance
☐ Partnership Planning Program
☐ Revolving Loan Fund Program

U.S. Environmental Protection Agency (EPA)

☐ Brownfields Area-Wide Planning Program
☐ Brownfields Assessment Grants
☐ Brownfields Cleanup Grants
☐ Brownfields Multipurpose Grants
☐ Brownfields Revolving Loan Fund Grants
☐ Targeted Brownfields Assessments
☐ State and Tribal Response Program

U.S. Small Business Administration (SBA)

☐ 7(a) Loan Program
☐ 504 Loan Program
☐ Disaster Loans
☐ Office of Small Business Development Centers
☐ Office of Veterans Business Development
☐ SBA Microloan Program
☐ Small Business Investment Company (SBIC) Program
☐ Surety Bond Guarantee
☐ Women's Business Centers