

Program Description

The Preservation through Smart Rehab Program (“Smart Rehab”) is a newly created program by the Pennsylvania Housing Finance Agency (“PHFA”) with the goal of preserving Pennsylvania’s affordable rental housing by identifying and financing energy efficient improvements that result in measurable operating cost savings and long term financial stabilization. While Pennsylvania has had as a priority the funding of preservation deals through our PennHOMES and LIHTC Programs for several years, Smart Rehab offers another tool to bolster our preservation efforts with an efficient and timely process that does not rely on the long approval and underwriting route of a LIHTC application nor does it rely on the availability of long term financing and investor interest.

Smart Rehab begins with a simple application to PHFA requesting approval to move forward with an energy audit. For qualified developments, PHFA may provide resources to assist with the payment of up to one-half of the cost of the audit. An energy audit is a detailed examination of how the multifamily facility uses energy and other controllable utilities, quantification of the building’s energy and water consumption, the cost of energy, a technical analysis of the building and associated systems, concluding with recommendations to reducing energy costs.

Upon completion, the audit is forwarded to PHFA for review and analysis. For those identified energy retrofit recommendations that will generate sufficient savings within 10 years to cover the costs of the upgrade, PHFA will provide loan and/or grant funds (depending on the financial capabilities of the development) for the capital improvements. Whether the funds will be provided as a loan or a grant will be determined by the financial condition of the development and the type of resources we are able to pull together.

A copy of the program guidelines has been included with this submission.

Motivation for Program

Pennsylvania has approximately 139,000 affordable rental units in HUD, Rural Development, PHFA and LIHTC inventories. Of this portfolio, more than 50 percent of the units were originally placed in service more than 25 years ago. The affordable housing stock in Pennsylvania has generally not been at risk of conversion to market as the subsidized rents are often above market or the units are located in soft markets. Instead, like many other states, our preservation efforts have focused on the dire need for rehabilitation and upgrades of many of our units. We have used LIHTC set asides and tax exempt bonds to assist with meeting this need, but with the limitation of these resources, each year we can only finance a small percentage of the vast inventory we have.

We are now faced with a third threat to preservation and that is the ongoing operating needs of the properties. Due to low rents and high operating costs, many owners cannot afford to continue to meet the operating needs of their properties or are not able to generate sufficient return to stay motivated. This is expected to worsen given stagnant or decreasing rents and continued escalating expenses. This will be compounded in Pennsylvania when our utility companies significantly raise their rates next year when rate caps are eliminated due to deregulation.

We needed to find a way to assist our owners in reducing their operating costs or raising capital to encourage them to preserve the inventory. Since we do not have additional tax credits or volume cap authority to increase the funding for preservation (and given the current market conditions, would not be able to attract investors even if we had the increased funding), we knew we needed to go in an entirely new direction.

Hence, the creation of the Preservation through Smart Rehab Program. It provides a mechanism to achieve a reduction in utility costs (thereby decreasing operating expenses) to generate sufficient savings to maintain the viability of many developments, without the need for full blown acquisition/rehab restructurings.

Accomplishments

To move Smart Rehab forward, we realized there were two major obstacles that we would have to overcome in order to allow the program to succeed. The first related to the energy audits. While we needed the expertise of qualified auditors to examine the structures and determine potential areas of energy efficiency improvements, along with the expected costs and anticipated savings, we could not find any qualified energy auditors of multifamily buildings in Pennsylvania. While we have auditors trained in single family and commercial structures, multifamily requires a specific protocol that was beyond the scope of these professionals. When we went out for bids, the only qualified auditors responding were from New York (given NYSERDA's long standing program). To meet this need, we set up a training program for Pennsylvania auditors utilizing funds received from the MacArthur Foundation. To date, we have trained 22 Pennsylvania auditors that are now certified as Building Performance Institute Certified Multifamily Analysts. Additionally, 17 more are completing their training and testing this week. This has provided Pennsylvania with a group of trained professionals to accomplish the task. Not only will we be able to have more audits completed in a shorter time frame, we have already seen the average costs of audits reduced by 30 percent given the increased competition.

The second obstacle was finding sufficient resources to maintain the program. While we could provide market rate loans to developments already experiencing a positive cash flow, we also wanted to assist those developments facing deficits each year. When we first starting designing this program in 2007, we had no idea how it would tie in so well with the green energy movement and other opportunities. But our timing proved to be very fortunate.

At the end of 2007, the John D. and Catherine T. MacArthur Foundation ("MacArthur Foundation") offered states and local governments the opportunity to apply under the Window of Opportunity initiative. We saw this as an opportunity to refine a program we had been developing and submit the Smart Rehab Program for funding. We were fortunate to receive a \$1 million dollar grant from the MacArthur Foundation (over a three year period). We are utilizing these funds to help defray the costs of the auditor training, fund a portion of the energy audits, and design a means for measuring the energy savings.

Besides PHFA providing \$2 million of its own reserves to support this program, we also started to outreach to new potential partners.

- We applied for and were successful in receiving a \$2 million loan from the U.S. Department of Agriculture Rural Housing Service Preservation Loan Fund for energy efficiency improvements in existing Rural Housing Section 515 developments.
- By working through Pennsylvania's Public Utility Commission, we met with and achieved agreements with five major electric utility companies to partner with us to provide funding for certain electric related improvements and to provide funding for energy audits and training.
- The Pennsylvania Department of Community and Economic Development has agreed to provide Section 108 loan authority to Smart Rehab developments in rural communities
- We recently were granted the authority to receive \$22.5 million of ARRA Weatherization Assistance Program funds as a subgrantee for use in multifamily buildings.
- The National Housing Trust has agreed to provide predevelopment loan funds to assist with the cost of plans and specifications once the energy audit has been completed.
- The West Penn Sustainable Energy Fund is providing financial assistance for the training of energy auditors and the performance of energy audits in the western part of the Commonwealth.

Our goal, when we first applied to the MacArthur Foundation, was to preserve 5,000 units under this program within three years. Given the level of resources we have been able to accumulate, we believe that we will be able to double that amount.

We offered the Smart Rehab Program to our developers five months ago. Since that time, we have received over 80 applications requesting approval and funding to begin the energy audits. To date, we have approved the funding of 36 audits that are currently underway, with more under review. Initial results indicate that we can save 25 to 30 percent in energy costs with under \$4,500 per unit in investment. We expect the loan/grant sizes to run from \$200,000 to \$600,000 per development.

Conclusion

We are not the first state to consider the energy retrofitting of multifamily developments. But we believe we are the first to achieve it on this scale as a major preservation program and in bringing such a variety of resources together. When they announced our award, the press release from the MacArthur Foundation highlighted this: “In the largest such effort in the nation, Pennsylvania will conduct comprehensive energy audits to determine the most appropriate and cost-effective improvements for increasing energy efficiency in rental homes.”

To date, most federal and state legislation around the greening of America has focused on single family homes. Our introduction of this program has provided an opportunity to display the benefits of multifamily energy retrofitting (preserving needed units, reducing the use of energy resources, reducing operating costs, and reducing the carbon footprint of the buildings) to state officials, local municipalities, nonprofit organization, property owners, etc. We are starting to see a shift in policy in recognizing these benefits, as demonstrated by our recent approval as a subgrantee under the Weatherization Assistance Program.

Many new partnerships have been formed – the MacArthur Foundation, the Public Utility Commission, the Department of Environmental Protection, Rural Housing, the West Penn Sustainable Energy Fund, and electric utility companies; and many existing partnerships have been further supported – the Department of Community and Economic Development, the National Housing Trust, and developers. Each state has access to similar relationships and should be able to replicate the program we have initiated in Pennsylvania.

We are excited about our Preservation through Smart Rehabilitation Program and believe it will provide a great support to our efforts to preserve the multifamily units in our extensive portfolio. We expect to do a wide range of developments – general, senior, and special needs occupancies, under a wide range of programs – HUD, Rural Development, LIHTC, PHFA’s portfolio.

Thank you for your consideration of our entry.