

**Joint Center for Housing Studies  
Harvard University**

**Revisiting Rental Housing Policy:  
Observations from a National Summit**

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## **Introduction**

In November 2006, the Joint Center for Housing Studies of Harvard University convened government, business, and nonprofit leaders to discuss the ways in which decades of experience, research and evaluation have helped inform our understanding of the nation's rental housing challenges and what can be done about them. While underscoring the importance of generating broad political support in the long-term for the allocation of more resources to rental housing programs, the conference revealed that there are concrete steps that can be taken in the short-term to make better use of the limited resources now available to address the nation's four primary rental challenges: 1) relieving rental affordability problems, 2) preserving low-cost rental housing; 3) revitalizing neighborhoods; and 4) using rental housing assistance to help improve the lives, opportunities, and productivity of the poor.

Rental housing assistance is increasingly being used not only to relieve affordability problems, but to preserve affordable rental housing, spark neighborhood redevelopment, help aid recipients move to areas with lower poverty rates if they choose to, help them make transitions from welfare to work, and help them save and build assets. As a result, policy makers and practitioners have gotten better at knowing what to do to reduce cost burdens, to improve the quality of the rental housing and the neighborhoods where low-income renters live, and to expand their opportunities to leave poverty.

Experience and research has already led to important improvements in rental housing programs. Affordable housing developments today are more financially stable and more appropriately scaled.<sup>1</sup> The housing choice voucher program has greatly increased opportunities to live in low-poverty areas (vouchers are now used in over 83 percent of the nation's census tracts with eligible rental housing).<sup>2</sup> Pilot programs are shedding light on how to remove work disincentives in older programs and help participants increase their incomes and build assets. Many troubled public housing developments have been turned around. Over 200 public housing developments with over 140,000 units in over 100 cities have received HOPE VI grants to redevelop communities on a smaller scale and revitalize the surrounding neighborhoods. All these new directions are cause for optimism that rental assistance can achieve positive outcomes beyond just helping people afford to rent.

This brief outlines the nation's primary challenges, the principal findings of the symposium, and possible new directions for rental policy discussed at the symposium.

## **Primary Challenges**

Rental housing is a key component of the nation's housing supply. Nearly one-third of American households—some 36.8 million in 2005—live in rental housing. While many rent by choice, others do so because ownership is not a viable option for them. This makes rental housing especially critical to those who lack the savings to cover the costs of buying a home, those who have incomes too small to cover the recurring costs of homeownership, and those with poor or no established credit history.

Of the rental problems facing the nation, affordability is by far the most widespread and is getting worse. As of 2005, nearly half of all renters were cost burdened<sup>3</sup>, up from only about one-third in 1980. Burdens are worst and often excessive among those with the lowest incomes. For example, approximately half of extremely low income renters spend<sup>4</sup> 79 percent or more of their incomes on rent. Even as the incomes of those at the bottom of the distribution have stagnated and the percentage of jobs paying middle-income wages dropped, rents have been creeping up for those with low wage work.

And even these striking cost burden statistics understate the true magnitude of the problem for renters because some households control their housing costs by making difficult tradeoffs, such as living in distressed neighborhoods, or locations that raise their transportation costs, or living in overcrowded or substandard units. These are tradeoffs that often have negative effects on a renter's safety, their physical and mental health, the quality of the schools their children attend, the quality of municipal services they receive, and their access to employment opportunities

Exacerbating the affordability problem is the alarming rate of loss of affordable rental housing. Over just the ten-year period from 1993-2003, the number of units that are affordable to renters in the bottom third of the renter income distribution (\$400/month or less) fell by 13 percent (1.2 million units). This has given rise to calls for preserving the existing stock of affordable rental housing. Though for now, federal, state, and local responses have been focused mostly on subsidized housing, interest is growing in searching for ways to preserve unsubsidized housing where losses are more numerous.

Despite widespread and rapidly growing affordability problems, federal housing initiatives still only assist one-third of the nation's poorest renters, and federal funding for new production

and rehabilitation of affordable rental housing has clearly not been enough to stave off large net losses from the stock.

Meanwhile, many neighborhoods continue to struggle with weak housing markets and other indicators of neighborhood distress. These problems are most pronounced in areas of poverty. Today, about 19 percent of poor blacks, 14 percent of poor Hispanics, and 10 percent of all the nation's poor live in neighborhoods where poverty rates exceed 40 percent.<sup>5</sup> While not all high-poverty tracts have the same level of social and economic distress, many studies indicate that living in areas with high poverty rates above even 20 or 30 percent generally has high social costs in terms of resident well-being, safety, education and unemployment.

Making matters worse, and reflected in the large net losses of affordable rental housing, it has grown much more difficult to gain government approvals to build affordable rental housing. As a consequence of this, and of the reduced transportation costs of living closer to city centers and mass transit, rental housing, and especially affordable rental housing, is mostly located in or near older city centers—distant from the areas of most job growth. Indeed, in the 91 largest metropolitan areas, over half of all renters and 62 percent of all low-cost units are located within 10 miles of the central business district while only 42 percent of all households live in these areas.

### **Lessons Learned in Rental Housing Policy**

Rental housing assistance has been used for several purposes: to relieve the housing cost burdens of low income and special needs populations, to spark neighborhood redevelopment, to give low-income households more opportunities to live outside of high poverty areas, and to support efforts to foster economic self-sufficiency.

Much has been learned about the strengths and weaknesses of various policy and programmatic approaches, as well as how one might improve their cost-effectiveness. At the same time, there is general agreement that some of the biggest barriers to addressing rental housing cost and location issues remain formidable, such as declining federal support for rental housing assistance and local land use restrictions.

## **Affordability – What Is Working and What Is Not**

### ***Current rental housing assistance programs are effective in reducing housing costs and housing quality problems but serve less than one third of the nation's poorest renters***

It is well documented that easing housing affordability problems leads to important benefits, such as reducing overcrowding, improving the quality of the housing in which recipients live, and enabling recipients to spend more on food and health care. Yet, even though housing is the largest single expense most very low income households face, housing assistance differs from other supports targeted to the poor, the elderly, and the people with disabilities because it is not an entitlement

Funding constraints have meant that despite a long history of using housing assistance to help the neediest among us, the percentage of eligible renter households receiving help has changed little in the past 25 years. Funding constraints also mean access to assistance is not predictable, as waiting lists are often closed. Under HUD definitions, households with incomes below 50 percent of median are generally eligible to receive housing assistance. However, only one fourth of these households report receiving housing assistance even though 40 percent pay more than half their incomes for housing. Furthermore, over two-thirds of households with incomes considered extremely low, below 30 percent of median, receive no housing assistance even though 4 million of these 6 million unassisted households pay more than half their income for housing.<sup>6</sup> Also contributing to such high shares of burdened households is that even some who do receive assistance may be burdened if they live in LIHTC developments that don't cap the share of a renter's income dedicated to housing.

### ***Federal housing production programs have created high quality, well-managed housing, though much is targeted to households with incomes at 50 percent-60 percent of median income***

Many of the shortcomings of earlier federal production programs have been corrected. Earlier programs often removed incentives for owners to manage properties soundly due to a lack of equity, over-regulation of rents, overly generous rents that bore no relation to market costs, and the failure to require long-term affordability restrictions.

Newer programs--- most notably the Low Income Housing Tax Credit (LIHTC) and HOME programs--use simpler designs (capital subsidies only) and rents based on area incomes.

These newer approaches recognize the importance of having market forces police outcomes (rents can only go up as area incomes rise and tax credit syndicators, bond underwriters, and investment groups carefully monitor general partners) and give owners an incentive to maintain their developments. In the case of LIHTC, use of the tax code has also protected the program from budget appropriation pressures and funding fluctuations, while the provision for state Qualified Allocation Plans (QAPs) has made it easier for states to customize their programs and introduce innovations. Compliance is also easier to enforce: if a project falls out of compliance, investors lose their tax credit for the year. As a result, the LIHTC program has a strong track record in terms of housing quality and financial stability, has created units in more diverse locations than earlier programs, and enjoys wide bi-partisan support.

Unfortunately, because developments created by these programs have rents set at 50 percent-60 percent of area median, extremely low income households cannot afford them unless they have a voucher or unless the developer is able to obtain additional capital and operating subsidies. This fact, combined with the recent lack of incremental voucher funding, means most new rental housing production is now tilted away from the neediest households.

In addition, like all other real estate investments, land is not included in either the depreciable basis, or the project's eligible basis upon which the value of the tax credits is calculated. Hence, it is less common for tax credit housing to be built outside of low-income neighborhoods, restricting the location choices of low-income renters. A recent study has found that 58 percent of all LIHTC units built in the 1990s are located in central cities, in neighborhoods that have much lower median incomes and much higher poverty levels on average than the neighborhoods of suburban LIHTC developments.<sup>7</sup>

***Income-based rent formulas provide an important safety net, but may discourage some recipients from increasing work efforts; refining these formulas can help raise resident incomes***

Like other income support programs for low-income households, the largest rental housing assistance programs (public housing and Section 8) impose a high tax on work by setting rents generally at 30 percent of income. The effect of rent tax is magnified by the fact that income gains reduce a host of other federal and state tax benefits and subsidies at the same time, including Food Stamps and Medicaid. One recent study of Pennsylvania single-parent

households with children found that those in the \$10,000-\$40,000 income range who did not receive housing aid had an average effective marginal tax rate of 58 percent; for those with housing assistance, the rate was 88 percent.<sup>8</sup>

Income-based rents do a good job in rationing scarce public assistance by providing more assistance to families that need it more and less assistance to those that need it less. At the same time, however, it appears that without specific compensating policies, income-based rents can discourage some recipients from making a full work effort or increasing their incomes. The risks associated with the prospect of graduating off of assistance altogether can also be a disincentive. The loss of housing assistance due to large income gains can turn catastrophic if one needs to re-apply for aid given the long waits for assistance. Given the lack of job security and limited availability of fringe benefits in the low-wage sector, this is a logical concern on the part of recipients. The need to address this concern adds to the challenge of designing rent-setting and eligibility strategies.

HUD has sponsored a number of initiatives to test whether alternative rent formulas can raise labor force participation and incomes. Better known efforts include the Family Self-Sufficiency program (FSS), public housing rent reforms, the recently completed “Jobs Plus” pilot, and the “Moving to Work” pilot now underway. These efforts vary in terms of the programs and populations targeted, support services provided, and the type of rent incentives offered.

Most of these efforts have shown increases in hours worked and some (notably FSS) have shown major gains in incomes and asset growth. Early results from “Jobs Plus” suggest rent incentives can play a direct role in raising incomes and encouraging work, especially if bundled with support and employment services. Still, the evidence in some cases is still tentative, underscoring the value of further experimentation under carefully controlled and evaluated circumstances.

***Preserving existing low-cost housing is critical to keeping affordability problems from worsening and can achieve other key goals, such as neighborhood preservation and more efficient use of limited resources***

The nation’s supply of low-cost rental housing (rents of \$400 a month or less) is shrinking as losses from the existing inventory exceed new subsidized units. In the past decade



(1993-2003), the net loss was 1.2 million units (by contrast, the total number of households receiving rental housing assistance totals about 6 million). These losses are occurring both in declining neighborhoods (due to abandonment and deterioration) and in rising neighborhoods (due to gentrification), and in both the private subsidized stock (200,000 units lost) and the unsubsidized stock. In addition, underfunding of the federal Public Housing Capital Fund is undermining the continued viability of many more units.

Preserving existing low-cost units is far less expensive and far easier than building new units, especially new subsidized units. It is generally estimated that rehabilitating existing affordable rental housing units costs 40 percent less than new construction<sup>9</sup> and some analyses of early transactions to preserve subsidized developments have found even higher differentials (50 percent - 75 percent).<sup>10</sup> The local approval process for preservation projects also tends to be faster than for new construction, especially in greenfield areas where the prevalence of highly restrictive local land use restrictions and building codes often make such development time-consuming.

The benefits of preservation suggest that strategies to preserve *unsubsidized* low-rent properties should also be pursued, as unassisted units accounted for the vast majority of the low-rent units lost between 1993 and 2003. Much of this stock is concentrated in small properties. Over 70 percent of unassisted units occupied by very low income households are in 1-4 unit structures and 90 percent are buildings with less than 20 units.<sup>11</sup> Many of these small properties are owned by individuals with very small portfolios and a significant portion (12 percent in 2001) operate at a loss.

The risks to the continued availability of unassisted low-rent units vary. In neighborhoods with strong demand and tight housing markets, low-cost units tend to become unaffordable due to rent increases or conversion to higher value uses, while units in neighborhoods and regions with weak housing demand are more likely to deteriorate, be taken off the market or be lost to abandonment or demolition. Census data limitations make it difficult to know what percentage of the recent losses in low cost units is due to rising rents as opposed to weak demand and falling rents but the limited studies to date indicate both dynamics have been major contributors to recent losses.<sup>12</sup> Small properties are particularly at risk of deterioration because of their age (half are more than 30 years old), the fact that financing for improvements is generally high-cost and at adjustable rates, and the disincentive to sell due to exit taxes. To date,

however, there has been very little in the way of a coordinated and concerted effort to determine how government could help improve the condition and the management of this housing.

## **Location – What Is Working and What’s Not**

### ***Rental housing assistance programs that enable households to live in lower poverty neighborhoods help them achieve better outcomes***

Much of the older subsidized housing inventory is located in relatively high poverty areas. One goal in creating the Section 8 voucher program was to provide housing assistance in a form that gave recipients greater geographic choice. Studies show that in many ways the voucher program has achieved that goal. While vouchers are often difficult to use in high cost neighborhoods, generally their use is de-concentrated – over 80 percent of all census tracts have voucher recipients and those households tend to represent small percentages of local renters.

In recent years, there has been a growing interest in using vouchers specifically to help households move from high-poverty areas to low-poverty areas. The earliest effort, the Gautreaux program in Chicago, started in the late 1970s as part of a court-ordered remedy to segregation in Chicago public housing. It provided vouchers that could only be used in less segregated lower poverty areas and initial follow up studies found that families who moved to suburban communities experienced many positive changes, including increased employment and better educational outcomes for their children.

A second effort, the Moving To Opportunity (MTO) Demonstration Program, was designed to compare how families who received vouchers that could only be used to move to areas with poverty rates below 10 percent fared compared to similar families who received vouchers that could be used more freely or who did not receive vouchers at all. Families with restricted vouchers also received search assistance while the other groups did not. While long-term effects are still under study, an interim MTO evaluation found that families with restricted vouchers experienced a number of benefits relative to the control groups. They moved to better neighborhoods (with substantially less poverty, crime, drug activity, etc.) and lived in higher quality housing. They also experienced health improvements (reductions in psychological distress, depression, and obesity) and girls had lower rates of problem behaviors (boys, however, appear to have experienced more problem behaviors). While the interim evaluation found no measurable differences in academic achievement, the evaluators noted many

parents stayed in the same city and thus the same school system. The interim evaluation also found no statistically significant effects on adult employment or earnings. Additional study is needed to determine the long-term effects of these moves.

***Local land use restrictions have had a negative impact on rental production, especially in suburban communities***

Increasingly restrictive local land use and development requirements have contributed to the rise in housing costs over time. This is the result of reducing allowable density, limiting the land supply for development, imposing costly building requirements, and using administrative procedures that add delays and uncertainties. Many municipalities have also have restricted the supply of family housing by banning (or imposing requirements that effectively ban) new construction of multifamily developments and/or manufactured housing, imposing age restrictions, or prohibiting units with more than two bedrooms.

Collectively, local restrictions have many negative regional and national effects in terms of environmental, economic and social goals, but individual jurisdictions have little incentive to change their behavior.

- Many regulations reflect a general opposition to development – an attitude which is fundamentally at odds with national needs, given that the number of households in the U.S. is expected to grow by almost 30 percent between 2005-2030 and the demand for more housing will grow by an even higher rate as some existing units leave the inventory. Regulations that raise housing costs and limit supply also hurt regional economic competitiveness.
- Similarly, while many localities oppose density and new development on environmental grounds, citing the desire to preserve open space, these local policies collectively have strongly negative environmental consequences both within communities and regionally. High minimum lot sizes and land costs fuel sprawl, drive new development further from job centers, decrease neighborhood walkability, and increase commuting distances and times.
- These restrictions also promote concentrations of poverty and restrict access to good schools by keeping the supply of rental housing outside urban centers artificially low

and are more prevalent in metropolitan areas which consist of many independent suburban governments.

***Rental housing assistance programs can turn around struggling neighborhoods***

While old federal housing programs have sometimes helped to create or continue concentrations of poverty, more recent programs have also been used to try to help turn around struggling neighborhoods. Research is shedding more light on the dynamics of neighborhood decline and how housing policies might prevent or reverse such declines. These efforts make sense given the impact of poverty rates on property values and social distress (i.e. higher poverty rates are associated with higher levels of social distress).<sup>13</sup> A recent study found neighborhood property values start to slide as poverty rates rise somewhere above 10 percent and that a massive fall occurs once poverty rates rise above 20 percent, indicating programs to address neighborhood decline should aim to avert neighborhoods in the 10-20 percent poverty range from falling into deeper concentrations of poverty.<sup>14</sup> It is estimated that the cost of allowing areas to rise above a 20 percent poverty rate and stay there exceeds \$400 billion nationwide in terms of lost property values and reduced rents.

The good news is that neighborhoods can turn around. Nationally, the number of high poverty rate (over 40 percent poor) census tracts fell by 25 percent between 1990 and 2000. In addition, over half of high poverty urban census tracts became at least slightly less poor between 1970 and 2000 and 14 percent of tracts with poverty rates of 30-45 percent became relatively low poverty (rates of 15 percent or less). At the same time, 19 percent of urban census tracts that had poverty rates below 15 percent in 1970 became poorer by 2000, including 3 percent that had poverty rates above 30 percent by 2000.<sup>15</sup> Most high poverty areas have important strengths, including good access to public transportation and proximity to the central business district that revitalization efforts can build on. These attributes, plus the presence of subsidized or low-cost unassisted housing and social and cultural networks, are also factors in residents' decisions to remain despite neighborhood problems.

Rental housing assistance policy can play an important role in improving neighborhoods. The "HOPE VI" program has evolved from an effort to replace the nation's largest, most distressed public housing developments with smaller scale, scattered site developments into a program to create mixed-income neighborhoods. A number of these more ambitious efforts have

led to major neighborhood improvements, including increases in local income levels and property values, reductions in crime, and new commercial and residential investment. At the same time, there is strong consensus that more needs to be done to protect the low-income families displaced by HOPE VI, by providing supports to help them settle into a new location and/or helping them to return to the revitalized community.

Experience has also shown that revitalization strategies must be selective. Cities with weak regional housing markets and economies and very high vacancy rates require different strategies (including possibly demolition of vacant properties, land banking) than those with strong regional demand. When strategies include new construction, the design and scale of these developments must be tailored to neighborhood and regional conditions. Research also shows that neighborhood revitalization strategies work best when they are comprehensive, addressing multiple properties simultaneously and addressing non-housing issues as well (e.g. public services, quality of transportation). The research also indicates that strategies are more likely to succeed if they support a broader mix of incomes in revitalization areas.

***Program experimentation and controlled policy evaluation can improve rental housing assistance programs but the lessons learned must be put into practice***

Pilot programs and program evaluations have provided important information about the effectiveness of some recent initiatives to remove work disincentives, to improve outcomes for the disadvantaged in terms of employment and asset building, and to revitalize neighborhoods. The effectiveness of other recent initiatives, by contrast, is less clear because program outcomes have been difficult to measure.

Well-designed experimentation and evaluation is relatively low cost and can increase the value of existing resources by creating more effective policies. Pilots must use large samples, multiple sites (to assess variations in different settings) and randomized trials - and examine a wide range of impacts by participant characteristics. Evaluations must include an assessment of how the pilot was implemented at each site and a cost-benefit analysis from the perspective of various participants. Pilots should also test whether the impacts of interventions vary by housing program (e.g. public housing, vouchers) and how different levels of intervention affect goals. For example, the cost of the Jobs Plus model (\$2,000-\$3,000 per household) means it probably will only be used on a limited scale; therefore, research is needed to see if less extensive and thus

less costly interventions (such as public housing rent reforms alone or efforts to more effectively integrate existing services in the community) can also raise incomes.

### **New Directions for Rental Policy**

Overall, there was a general consensus that project-based assistance (production and preservation programs) and voucher strategies should be refined to meet very specific goals, including expanding housing opportunities in low poverty neighborhoods, subsidizing the development of housing for those unable to find suitable housing with vouchers (people with disabilities, the elderly, large families), and helping to revitalize neighborhoods.

Special attention should be paid to siting of developments in areas with poverty rates in the 10 percent to 20 percent range because policies that are likely to increase poverty concentration can result in neighborhood destabilization. While there is strong support for increasing opportunities to live in low-poverty areas, participants also emphasized that not all poor neighborhoods are the same and that recipients of assistance have a right to choose where they live.

### **Program-Specific Suggestions**

#### **Housing Choice Vouchers**

##### ***Extend fair housing protections to voucher holders to improve access to low poverty areas***

Use of vouchers is not evenly distributed among all neighborhoods. A recent study comparing the number of voucher units to the supply of affordable units (gross rents within area Fair Market Rents) in the 50 largest metropolitan areas found that almost 40 percent of census tracts had less than *half* the number of voucher users that one would expect if all tracts had the same ratio of program units to affordable units.<sup>16</sup> Voucher units occupied by minority households were even more unevenly distributed with African American voucher users far more likely to be in tracts with above-average percentages of voucher units.

Expanding fair housing protections to voucher holders could improve access to low-poverty areas. A number of states, including California, Massachusetts, Utah and Wisconsin, as well as several cities and counties, already have made source of income (including housing vouchers) a protected class. Even in these states, discrimination against voucher holders still exists and victims are often reluctant to pursue legal action. Creating a pilot program that

provides special funding to those states to test strategies to encourage voucher holders to pursue their fair housing rights could provide useful policy lessons.

Efforts to expand housing opportunities for voucher holders should include educating them about the merits of different neighborhoods and other supports to help families succeed in unfamiliar neighborhoods, making it easier for them to visit and settle in a diverse range of neighborhoods.

***Continue research on how vouchers can help recipients achieve better outcomes***

Several initiatives to help voucher recipients raise their incomes and build assets have yielded significant positive results and the Moving to Opportunity program has shown that moving to low-poverty areas provides health and safety benefits. A small investment in randomized controlled trials to advance our understanding of what strategies work best could improve program outcomes over 5 to 10 years. The proposed reauthorization of the Moving to Work demonstration could provide a platform for such experimentation if research objectives and funding are adequately built into the core structure of the next phase of that demonstration.

Voucher program experiments can help shed light on the impact of a variety of program elements and their relative costs and benefits. For example:

- the effect of various types of rent incentives on participant income and asset building (e.g. whether these differ for programs that use flat rents which provide immediate rent savings as opposed to programs where participants continue to pay rent increases but pay them into an escrow account that can later be taken as a lump sum)
- the effect of various types workforce services, such as tuition reimbursement or job coaching that support job retention and advancement rather than simply helping someone find a job;
- the effectiveness of rent incentives and work services alone and when combined;
- how the length of time incentives and services are offered affects outcomes;
- the effect of providing incentives and services to households living in low poverty areas compared to households living in neighborhoods with higher levels of poverty; and

- the effect of specific characteristics of low-poverty areas (such as absolute area poverty rate and changes over time, strength of school system attended) on family health and educational achievement.

One way to do this would be to expand the FSS program to allow for randomized trials that test its potential as currently structured and using alternative incentives. Another would be to require that new allocations of incremental vouchers for families with children include a well-designed experimental component (e.g., require use in neighborhoods with high performing schools or add funds for workforce services.). A third approach is to require that a minimum percentage (e.g. 1/10<sup>th</sup> of one percent) of HUD's budget be specifically for pilot programs and evaluation.

***Experiment with regional or cooperative program administration to make it easier to use vouchers in low-poverty areas and to provide mobility counseling and housing search assistance***

Some of the disparity in the rate of minority and non-minority use of vouchers in low-poverty areas may be due to the fragmented nature of housing authority administration which makes it difficult to get information about openings and obtain applications. The potential benefits of moving to a regional administrative approach deserve testing and evaluation. Regional administration or cooperation offers efficiencies that could also make it easier to fund and deliver mobility counseling and housing search assistance.

**Low Income Housing Tax Credit Program**

***Establish Pilot Programs to Improve Geographic and Economic Targeting***

There are a number of steps that could be taken to better target scarce tax credit dollars to ensure that projects better serve needy populations and create opportunities while giving states needed flexibility:

***Revise Qualified Allocation Plan (QAP) mandates and allow income limits above 60 percent of median in some circumstances.*** Many state-developed QAP mandates are vague and some work at cross-purposes. Replacing them with more explicit locational and income mix requirements



would encourage more siting and preservation in low-poverty areas, and improve the delivery of assistance to underserved households. At the same time, allowing slightly higher income households as part of the mix in projects sited in areas undergoing neighborhood revitalization could boost turnaround efforts (some believe higher income residents are needed to attract stronger retailers, better services, and strengthen local schools). Possible mandates include:

- requiring that some projects be located in low-vacancy areas with high population growth rates where voucher use is low and that some be targeted to above-Fair Market Rent locations.
- favorable treatment for projects located in communities with high-performing schools.
- explicit income mixing goals to ensure each development serves some extremely low income households combined with authority to allow income limits above 60 percent of median for a portion of the tax credit units in neighborhood revitalization areas.
- favorable treatment for developments with set-asides for special populations combined with services.

***Establish a pilot program to include land costs in the LIHTC eligible basis or to eliminate the use of “qualified basis” in the LIHTC program. Have states allocate credits based on their determination of a project’s public purpose benefits instead.*** Including the cost of land in the eligible basis would remove the current bias toward production in areas with low land costs (neighborhoods with relatively high poverty rates or on the fringes of metropolitan areas) and make it possible to develop projects in areas where land costs are higher (e.g. smart growth corridors, low poverty neighborhoods).

Eliminating the use of qualified basis entirely would make the program easier to administer and make it possible to purchase higher cost land. Eliminating the current qualified basis boost-up of 30 percent for qualified census tracts and difficult development areas would also remove an incentive for siting developments in high poverty neighborhoods. Alternatively, one could provide a qualified basis boost-up for projects located in low-poverty communities with strong school systems.

### ***Make it easier to use LIHTC with other subsidies***

Simplifying current rules regarding the use of HOME and CDBG funds for LIHTC projects that limit the ways in which the funding can be used (e.g. HOME funds must be used for rehabilitation and can't be used for simple refinancing) would also make it easier to target needy populations and/or low-poverty locations by adding resources to the projects. Eliminating the current restrictions on use with other subsidies such as the Moderate Rehabilitation program and TANF grants would also serve these goals. The federal government would need to give states guidance on subsidy layering review.

### ***Require state tax credit allocating agencies to collect demographic and locational data on LIHTC properties***

The LIHTC program is administered by the IRS, and unlike HUD programs, little detailed information is available about the demographic and locational characteristics of LIHTC developments – including household characteristics (size, composition, age), racial and ethnic characteristics, bedroom distributions and use of vouchers. Requiring states to collect project data annually would make it possible to understand how the LIHTC fits with state and federal housing strategies.

### **Preservation of Subsidized and Unassisted Low-Rent Housing**

Mortgage restrictions and rental assistance contracts covering over one million units of subsidized housing will expire by 2013<sup>17</sup> and many small unassisted low-rent buildings are also at risk of being lost through demolition, abandonment or gentrification. Some owners who are interested in continuing to operate their properties as low-cost housing will need help with capital needs; other properties may need to be purchased to preserve affordability. While much is known about ways to preserve subsidized developments, preservation strategies for the unassisted stock have received little attention. States and localities that want to preserve properties at risk of loss from the low-cost inventory need resources and strategies.

### **Develop a dedicated federal program to preserve subsidized properties**

One solution may be to provide preservation block grants, which would give states and localities more flexibility regarding where and how they preserve housing developments. A *strategic* approach to preservation might be based on the following guidelines:

- Efforts to continue project-based assistance should target developments in low-poverty areas where voucher use is difficult with specific attention to larger families. Developments for the elderly or people with disabilities should be subject to the same analysis unless they have special physical features or non-housing services not present in alternative housing. Targeting should favor good managers/owners (transfers of ownership can be encouraged when necessary).
- Preservation decisions should also be based on a review of building characteristics (e.g. unit sizes, property type and age), including current demand and prevailing vacancy rates over time (e.g. demand for third floor walkups may be weak in some neighborhoods) and likely demand in 20 years for that type of property.
- Underwriting should keep rents close to the market, set debt service coverage ratios high enough to cover income/expense shocks, and assume projects will need capital improvements every 20 years. Programs should also provide a flexible way to change owners and managers without requiring a property transfer or acceleration of financing.
- A second suggestion may be for the federal government to create a carve-out of private activity bond authorization for exclusive use on multifamily housing. This would encourage states to use their bonding authority to leverage use of the uncapped 4 percent low income housing tax credits for preservation deals, resulting in an increase in the amount of federal resources for preservation.

### **Experiment with new ownership models for smaller unassisted properties**

Most smaller properties, especially 1-4 unit buildings, are owned by individuals with very small portfolios (one or two properties), making it difficult for them to realize economies of scale. Small owners also have trouble obtaining funds for capital improvements that could generate operating savings, assuming rents could bear the cost. Given their age, many buildings are energy-inefficient and/or have faulty plumbing and may be in weaker locations.

Creating a federally-sponsored small property REIT (S-REIT) could help preserve this stock by bringing in new equity funding and allowing for more professional management. It would also solve the exit tax problem by allowing owners to exchange properties for S-REIT

shares while still providing them with cash flow. S-REITs could also provide access to the LIHTC and to the benefits of securitization – non-recourse, longer term loans at fixed rates.

Given the complexity of such a strategy (federal tax and housing statutes would have to be modified); it makes sense to test the concept on a small-scale pilot basis first. Possible funding sources including financing provided by housing authorities through the issuance of essential function bonds or existing rental housing programs such as LIHTC and HOME . While managing a scattered site portfolio can be challenging, several CDCs and private investors have experience that could guide the design of the pilot program.

### **Create pilot programs to test other low-cost strategies to preserve smaller rental properties**

A number of initiatives to help preserve small properties deserve testing. The federal government could encourage this by providing a small amount of funding for well-designed experiments. Once proven, several would likely be self-sustaining. Strategies to consider evaluating include:

- programs to organize small landlords to obtain group benefits (e.g. insurance) at lower cost (this would improve their bottom line without putting upward pressure on rents);
- programs to encourage small owners to take landlord education classes (much like the first-time homebuyer training programs offered by lenders), perhaps by making graduation a requirement for financing or reward graduates with more favorable terms;
- adoption of a more flexible code for older properties; and
- creating programs that provide a mix of public funds and conventional bank loans for rehabilitation, and changing the Section 8 program to reward long-term ownership (New York City provides a good model for study for the last two).

## **Local Regulatory Barriers**

### **Take federal action to reduce state and local regulatory barriers to housing production and especially affordable housing production**

While states are best suited to reduce local barriers to affordable rental housing production, the federal government must motivate them to take on this role. Such efforts are more likely to be effective if combined with direct federal financial incentives to states and localities that take steps to increase their supply of affordable housing, or disincentives to those that don't. Suggested approaches include the following:

- ***Condition federal transportation aid and other federal assistance on progress in reducing regulatory barriers.*** While this brief focuses on suggestions to advance rental policy in the near term, reducing regulatory barriers clearly involves longer term solutions that would require significant political will in order to be advanced. One such solution would be to require states to create planning and land-use regulations that encourage localities to adopt inclusionary zoning and “streamline” unnecessary regulations, as a condition for receiving federal transportation funds.
- ***Provide technical assistance and supporting research through HUD or others to identify what strategies are most effective.*** A number of states and localities--most notably California, New Jersey and Massachusetts, and Montgomery County in Maryland--have statutes that encourage or require localities to allow the development of affordable housing. Some provide planning funds to help communities get started and funds to address fiscal impact and/or infrastructure costs. HUD could also award bonus funds (community development or other sources that can be used for activities beyond housing) to states and localities that adopt policies that increase their supply of affordable housing in ways that reduce concentrations of poverty and increase access to jobs and good schools.
- ***Link housing development planning to transportation planning.*** A starting point would be for the federal government to provide funding to Metropolitan Planning Organizations (MPOs) in partnership with regional housing agencies to develop regional housing strategies to complement regional transportation plans and require

that HUD-funded activities be consistent with the strategies. As in conditioning federal transportation funding, any additional federal funding would require a great deal of political will, but greater consistency would provide returns through increased effectiveness of both housing assistance and transportation funds.

### **Neighborhood Revitalization**

The fact that high poverty neighborhoods can often be turned around justifies a public commitment to strategic revitalization programs, given the negative effects on residents and on property values. Many of these neighborhoods are characterized by good access to public transportation and proximity to central business districts and revitalizing them has important environmental benefits

### **Revise and continue the HOPE VI program to fix troubled public housing and revitalize neighborhoods both physically and socio-economically (through income mixing)**

The HOPE VI program has succeeded in providing better public housing and improving neighborhood conditions and should be continued but modified to better protect displaced residents and ensure that there is no net loss in assisted units.<sup>18</sup> Currently pending re-authorization legislation provides such an opportunity. The housing authorities that have had the greatest successes in terms of neighborhood revitalization made it a goal in their initial planning and made extensive investments throughout the neighborhood, building new schools, etc. The complexity of such undertakings means most projects require significant public and private investment, strong partnerships with state and local agencies as well as the private sector (for financing and management) and a multi-year implementation schedule. While mixed-income housing in high-poverty areas frequently means that subsidy funds effectively assist market rate tenants, including a market rate component without rent and profit restrictions gives the private sector an incentive to participate.

With HOPE VI's successes has come a significant decrease in the number of public housing units and a concern that displaced tenants have not always been well-served (research indicates that about 30 percent of former residents end up living in other high-poverty neighborhoods and that some have become homeless). Protections for existing tenants must be improved. Strategies for improvement include the following:

- setting minimum performance goals for grantees with regard to tenants' temporary and permanent relocation and self-sufficiency.
- requiring that program plans and budgets include appropriate case management, housing search and support services.
- improving HUD's tracking of impact of HOPE VI projects on the supply of housing assistance (net public housing units lost or created plus replacement vouchers issued) for extremely low-income households.
- mandating or setting HUD goals to improve the degree of integration between HOPE VI and existing programs at housing agencies. For example, many sites with HOPE VI programs do not regularly enroll HOPE VI participants in the Family Self-Sufficiency program, despite the obvious benefits of doing so and despite the fact that they're already providing work-promoting case management that could be used to satisfy the requirements of FSS as well.

**Establish pilot programs to test how best to use voucher, production and rehabilitation programs to revitalize neighborhoods and prevent their decline.**

Vouchers, housing production and rehabilitation programs can strengthen neighborhoods as long as they do not increase concentrations of poverty. Neighborhoods with poverty rates of 10 percent-20 percent are vulnerable to decline if poverty rates start to climb.<sup>19</sup> By contrast, neighborhoods with low poverty rates are less likely to experience major increases in poverty rates over time.<sup>20</sup>

Well-designed pilot programs in one or more cities can shed light on the extent to which voucher and project siting strategies can turn around higher poverty areas and prevent decline in at-risk neighborhoods and the costs and benefits of such efforts (including property tax effects). Potential strategies to test include:

- providing vouchers that can only be used in low-poverty areas, providing housing search assistance and allowing more flexible payment standards (removing the administrative and financial barriers to portability for housing authorities would also help); and

- revising the LIHTC program (as discussed above) to encourage siting in tracts with poverty rates below 10 percent.

Research on the effects of development and rehabilitation programs on neighborhood property values in New York City suggests that a number of other factors also affect revitalization benefits (as measured by property values), including site and neighborhood characteristics, project scale and size, income mixes and property manager characteristics (non-profit vs. for-profit).<sup>21</sup>

### **Strengthen HUD's Research Capacity and Funding**

Federal programs have not been designed to experiment carefully with different approaches. Although several experiments have been attempted by the federal government and increasingly housing authorities have gotten freedom to experiment as well, HUD has not been tasked or gotten funding to make sure these experiments have been set up with proper controls. Therefore opportunities to improve the delivery of housing assistance and better understand its potential value for fighting poverty and addressing concentrations of poverty have been lost. In an environment favoring experimentation and having given local authorities flexibility to experiment themselves, a small expenditure of resources aimed at setting up more rigorous experimental designs and evaluating them could yield more benefits.

### **Conclusion**

We know a lot about how to use rental housing assistance programs to reduce affordability problems, to help low-income households achieve better outcomes, and to revitalize distressed neighborhoods. This knowledge can and should be used to improve existing programs, to guide additional experimentation by states, localities and local housing agencies, to use rental housing programs to generally improve the quality of life of low-income renters (by improving workforce outcomes, improving the outcomes of poor children and supporting asset building), and to improve the quality of neighborhoods where low-income renters live.

However, absent a significant increase in federal funding, we cannot expect to serve more than about one in three of the nation's poor households with severe housing needs. While much discussion was devoted to how much it might cost to create an entitlement program for the



neediest households, including frail elders and people with special needs, and potential funding sources, including caps on mortgage interest deductions for very expensive homes, there was general agreement that dealing with the most intractable rental housing problems – resource constraints and regulatory barriers – is a longer term effort that requires changing public attitudes and political will.

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- <sup>1</sup> While data on the financial stability of older assisted housing is not available, studies to date have shown that LIHTC properties “operate with a foreclosure rate well below that of other real estate assets” with an annualized foreclosure rate of 0.02 percent in 2004 and 2 percent overall since the start of the program (47 projects). Ernst & Young, “Understanding the Dynamics III: Housing Tax Credit Investment Performance” (December 2005). Average project sizes have also fallen, especially in public housing (projects built in the 1980s averaged 48 units and in the 1990s 30 units). The median size of LIHTC projects was 48 units as of 2001.
- <sup>2</sup> Deborah J. Devine, Robert W. Gray, Lester Rubin and Lydia B. Taghavi, “Housing Choice Voucher Location Patterns: Implications for Participants and Neighborhood Welfare” (Washington, D.C.: the U.S. Department of Housing and Urban Development, January 2003), pp. 11-12.
- <sup>3</sup> Defined by US Dept. of Housing and Urban Development as a household paying over 30 percent of household income on rent.
- <sup>4</sup> Extremely low-income households are defined as those with incomes of 30 percent or less of area median. Keith Wardrip and Danilo Pelletiere, “Recent Data Shows Continuation, Acceleration of Housing Affordability Crisis (Research Note #06-05)” (Washington D.C.: National Low Income Housing Coalition, December 2006), pp. 1-2.
- <sup>5</sup> “State of the Nation’s Housing 2006”, (Cambridge, MA: Joint Center for Housing Studies of Harvard University, 2006), page 27.
- <sup>6</sup> Hardiman, D, Martin, M., Shroder, M., Steffen, B., Susin, S., Vandenbroucke, D., & Yao, D., “Affordable Housing Needs: A Report to Congress on the Significant Need for Housing”, U.S. Department of Housing and Urban Development – Office of Policy Development and Research, Washington, D.C. (2005) – Tables A-4 and A-3. The authors note that 2003 American Housing Survey found that 32.9% of extremely low income renter households reported receiving housing assistance, but that this figure probably overstates the number actually receiving assistance (p.17).
- <sup>7</sup> Lance Freeman, “Siting Affordable Housing: Location and Neighborhood Trends of Low Income Housing Tax Credit Developments in the 1990s” (Washington, D.C.: The Brookings Institution: 2004), p.1
- <sup>8</sup> C. Eugene Steuerle, Adam Carasso, “The True Tax Rates Confronting Families with Children” (Washington, D.C.: Tax Policy Center, 2005). Article online at [http://www.urban.org/UploadedPDF/1000846\\_Tax\\_Fact\\_10-10-05.pdf](http://www.urban.org/UploadedPDF/1000846_Tax_Fact_10-10-05.pdf) See also Daniel Shaviro, “Effective Marginal Tax Rates on Low Income Households” (Washington, D.C.: Employment Policies Institute, 1999). Article available online at [http://www.epionline.org/studies/shaviro\\_02-1999.pdf](http://www.epionline.org/studies/shaviro_02-1999.pdf)
- <sup>9</sup> “Issue Brief: Why Preserve Affordable Rental Housing” (Washington D.C.: National Housing Trust, undated), p 2. Article online at [http://www.nhtinc.org/documents/Why\\_preserve\\_issue\\_brief.pdf](http://www.nhtinc.org/documents/Why_preserve_issue_brief.pdf)
- <sup>10</sup> “Window of Opportunity: Preserving Affordable Rental Housing”, John D. & Catherine T. MacArthur Foundation, undated. Available from [http://www.macfound.org/atf/cf/percent7BB0386CE3-8B29-4162-8098-E466FB856794percent7D/HCD\\_WINDOWSOPP\\_BROCHURE.PDF](http://www.macfound.org/atf/cf/percent7BB0386CE3-8B29-4162-8098-E466FB856794percent7D/HCD_WINDOWSOPP_BROCHURE.PDF);
- <sup>11</sup> Alan Mallach, “Landlords at the Margins: Exploring the Dynamics of the One to Four Unit Rental Housing Industry, National Housing Institute; 2006; “State of the Nation’s Housing 2006”, (Cambridge, MA: Joint Center for Housing Studies of Harvard University, 2006),
- <sup>12</sup> ICF Consulting, “Rental Market Dynamics: Is Affordable Housing for the Poor an Endangered Species” (Washington D.C.: U.S. Department of Housing and Urban Development – Office of Policy Development and Research, December 31, 2003), pages 2 and 11-17. Article online at <http://www.huduser.org/intercept.asp?loc=/Datasets/ahs/RENTALMARKETDYNAMICS.pdf> The Census Bureau’s American Housing Survey (AHS) provides the most detailed information on changes in the affordable rental housing inventory, but is limited by a lack of data on vacant units, year to year rent change data for individual units and changes in the way it screens out subsidized units. Within those constraints, there have been several studies of the factors contributing to changes in the low-rent housing supply, with somewhat contradictory findings regarding the relative importance of filtering up and down. A 1996 HUD study of changes between 1985 and 1992 in 41 MSAs found that filtering up played a larger role in the net loss of 527,000 units affordable to households at 35% of median, than filtering down, demolition and units taken off the market. A more recent HUD study of 1995-1999 changes in six MSAs, by contrast, found net *gains* in low-rent units as more units in those markets filtered down than up.
- <sup>13</sup> A recent Census Bureau report, “Areas of Concentrated Poverty: 1999” (Washington D.C.: 2005) provides data on tract demographics by poverty rate using four categories (tracts with poverty rates between 0-12.39% (the national poverty rate), between 12.4-19.99%, between 20-39.99% and 40%+). It shows that higher poverty rate

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tracts (40%+ and 21-39%) had much higher unemployment rates (18.6% and 10.9% respectively) than those in the tracts below 20% (6.8%) and below 12.4% (4.0%). Higher poverty tracts also had higher percentages of adults without a high school degree (37.9% and 35.5%) than lower poverty tracts (25.9% and 14.3%), more single-parent households (47% and 31% vs. 20% and 13%) and more families with incomes below \$10,000 (28.5% and 14.1% vs. 7.5% and 2.7%).

<sup>14</sup> George Galster, “The Social Costs of Concentrated Poverty: Externalities to Neighboring Households and Property Owners and the Dynamics of Decline” (draft), (presented at “Revisiting Rental Housing: A National Policy Summit”, November 2006), .page 48.

<sup>15</sup> Stuart Rosenthal, “Where Poor Renters Lives in Our Cities” (draft), (presented at “Revisiting Rental Housing: A National Policy Summit”, November 2006), page 31.

<sup>16</sup> Devine et. al, p. 13.

<sup>17</sup> U.S. Government Accounting Office, “Multifamily Housing: More Accessible HUD Data Could Help Efforts to Preserve Housing for Low-Income Tenants (GAO-04-20)”, (Washington D.C.: January 2004), p. 13.

<sup>18</sup> Susan J. Popkin, Bruce Katz, Mary K. Cunningham, Karen D. Brown, Jeremy Gustafson, and Margery A. Turner, “A Decade of HOPE VI: Research Findings and Policy Challenges”, Washington D.C.: The Urban Institute and the Brookings Institution, May 2004), pp. 47-51.

<sup>19</sup> George C. Galster, Jackie M. Cutsinger and Ron Malega, “The Social Costs of Concentrated Poverty: Externalities to Neighboring Households and Property Owners and The Dynamics of Decline” (draft); (presented at Revisiting Rental Housing: A National Policy Summit, Joint Center for Housing Studies of Harvard University, November 2006), Abstract.

<sup>20</sup> Rosenthal, page 23.

<sup>21</sup> Ingrid Gould Ellen, “Spillovers and Subsidized Housing: The Impact of Subsidized Rental Housing on Neighborhoods (draft)”, (presented at Revisiting Rental Housing: A National Policy Summit, Joint Center for Housing Studies of Harvard University, November 2006), pp. 15-16.