

---

# CHAPTER ONE

---

## Developing Affordable Housing in the Twenty-First Century

- |  |   |  |    |
|--|---|--|----|
| 1.1 Introduction   | 3 | 1.4 Current Trends in Affordable Housing                                       | 6  |
| 1.2 The Current State of America's Affordable Rental Housing       | 4 | 1.5 Unique Opportunities for Nonprofit Organizations: Rental and Homeownership | 10 |
| 1.3 The State of America's Working Poor Seeking Affordable Housing | 4 |  |    |

### 1.1 INTRODUCTION

Affordable housing development came of age in the twentieth century. Many significant federal programs were created from the Federal Housing Act of 1934 through the Affordable Housing Act of 1990 that stimulated supply and subsidized demand for both homeownership and rental housing. By the early 1990s, these programs had helped to provide decent, safe, and affordable homes to millions of working American families. At its height, the industry was managing more than 5.5 million units of federally supported, affordable rental housing. By 2005, more than 33 million people had utilized federally insured mortgage programs to become homeowners.<sup>1</sup>

Today, the homeownership rate is at an all-time high of almost 70 percent. The private sector has created loan programs that now make it possible for very-low-income people, especially people of color, to buy a home with no money down and to prove creditworthiness in many unconventional ways such as showing 12 months of cell phone bill payments.<sup>2</sup> In fact, these innovations have helped whole segments of the population who historically have been shut out of homeownership to do so in record numbers. For example, Hispanic homeownership increased

---

<sup>1</sup> [www.hud.gov/offices/hsg/fhahistory.cfm](http://www.hud.gov/offices/hsg/fhahistory.cfm).

<sup>2</sup> "Housing Industry Awakens to the Latino Market," *Wall Street Journal*, August 3, 2005, page B8. Innovative efforts by Fannie Mae and Freddie Mac to help low-income people become homeowners are discussed fully in Chapter 11.

## DEVELOPING AFFORDABLE HOUSING IN THE TWENTY-FIRST CENTURY

by almost 20 percent from 1993 to 2004 due to increasingly flexible underwriting and outreach.<sup>3</sup>

The same type of robust growth cannot be found in affordable rental housing. Today, less than 4 million of the more than 5 million units available in the 1990s still exist. The last major piece of housing legislation was enacted more than 15 years ago. No new major initiatives are expected in the coming years. Despite the fact that almost 100 million Americans are in need of affordable housing, resource constraints mandate that the industry focus on how to preserve the units still remaining and how to get the most out of the shrinking pool of resources available to build new ones. This chapter helps the nonprofit housing developer to understand the current state of the affordable housing industry. It highlights the trends that are likely to shape and impact development in this first decade of the twenty-first century.

### 1.2 THE CURRENT STATE OF AMERICA'S AFFORDABLE RENTAL HOUSING

America's affordable rental housing stock is dwindling. According to the U.S. Department of Housing and Urban Development (HUD), as of 2000, there were 1.3 million units of public housing, 1.8 million units made affordable through rent vouchers provided to tenants, and 800,000 units developed through the low-income housing tax credit. Many more units are inhabited by low-income people; however, they often provide substandard shelter or are made affordable by crowding multiple families into a single unit.

The single largest funding source of funding for new rental housing is the low-income housing tax credit (LIHTC).<sup>4</sup> Approximately 1,300 new projects, adding 90,000 new units each year are funded through this program. In contrast, less than 50,000 units were built in the entire decade from 1990 to 2000 using every other federal program such as public housing, Section 8, and other federally insured loan programs.<sup>5</sup>

### 1.3 THE STATE OF AMERICA'S WORKING POOR SEEKING AFFORDABLE HOUSING

While the supply of affordable rental housing shrinks, need continues to rise. Simply put, Americans do not have income sufficient for decent, safe, and affordable housing. As recently as 2001, 95 million Americans had

---

<sup>3</sup> Id.

<sup>4</sup> See Chapter 9 for a full discussion of this important source of equity.

<sup>5</sup> [Huduser.org/datasets/lihtc.html](http://Huduser.org/datasets/lihtc.html). See Chapters 7, 8, and 11 for a full discussion of other federal grant, loan, and project enhancement programs.

### 1.3 THE STATE OF AMERICA'S WORKING POOR SEEKING AFFORDABLE HOUSING

excess housing costs burdens (paid more than 30 percent of their income for housing) or lived in crowded or inadequate conditions.<sup>6</sup> In 2004, the number of people earning \$32,000—50,000 who spent more than 30 percent of income on housing jumped to 4.5 million.<sup>7</sup> Even more troubling, fully one-half of the lowest-income Americans spent at least 50 percent of their income on housing—leaving an estimated \$161 a month available for food and \$34 a month for health care.<sup>8</sup> These statistics do not even address the more than 2.5 to 3.5 million homeless people on the streets each year. Today, more than twice as many people face housing problems as lack health insurance, widely considered the biggest issue facing working class Americans.<sup>9</sup>

Immigrants account for more than a third of household growth since the 1990s.<sup>10</sup> Of the 12 million foreign-born householders, 3.4 million (28 percent) arrived in this country during the 1990s.<sup>11</sup> In fact, the number of renter households in America would have fallen during that period were it not for immigrant and minority households.<sup>12</sup> If this influx continues at this level, more than 1 million new immigrant households could be added in the next ten years. This reality has significant ramifications for the sector. First, affordable housing developments will have to be more immigrant-friendly. That means that property management staff, tenant communications, unit size, and more will have to reflect the language and culture of this customer base. Second, the median income of these renters continues to drop, meaning that even less money will be available industry-wide for rent payments.<sup>13</sup>

But demand is not stimulated only by the growing immigrant population. Increasingly, communities are recognizing that they cannot recruit and retain essential workers because their housing costs are prohibitively high. Firefighters, teachers, police officers and service workers are being priced out of many markets. This leaves local governments and industry without the workers they need. This reality has led many in the industry to change the vernacular from “affordable housing” to “workforce housing.” This change is important for two reasons. First, it speaks directly to public and private sector leaders because it is their inability to attract a workforce that will engage them in housing issues. Second, it better frames the issues surrounding affordable housing as ones about real

---

<sup>6</sup> *The State of the Nation's Housing*, 2004, Joint Center for Housing Studies of Harvard University at 25.

<sup>7</sup> *Id.* at 27.

<sup>8</sup> *Id.* at 26.

<sup>9</sup> *Id.* at 27.

<sup>10</sup> *Id.* at 2.

<sup>11</sup> *Id.* at 11.

<sup>12</sup> *Id.*

<sup>13</sup> *Id.* at 23.

## DEVELOPING AFFORDABLE HOUSING IN THE TWENTY-FIRST CENTURY

working people, like teachers that you know and trust, not theoretical welfare recipients.

### 1.4 CURRENT TRENDS IN AFFORDABLE HOUSING

#### (a) The Rise of the States and the Decline of the Federal Government

The role of the states in financing affordable housing continues to grow especially as federal programs and funds become more scarce. The states have become increasingly important players since the enactment of the federal Low Income Housing Tax Credit (LIHC) in 1986. Unlike prior federal housing programs that were largely managed and approved by HUD, the LIHTC delegated awarding of these credits to the states. Since 1986, each state, usually through their housing finance agency, has determined the best way to allocate the credits. In the process, each state has developed its own affordable housing expertise, development priorities (for example, homeless, rural, disabled) and, in many cases, their own state funded housing programs. In short, the increased professionalism at the state level has led to a much more sophisticated and more highly funded response to affordable housing issues in that state. For example, a number of states, such as California and New Jersey, have created programs to preserve affordable housing units in their states that were developed originally under federal housing programs but that are now at risk of loss.<sup>14</sup>

This growth of state action in affordable housing is in contrast to the decline in federal support over the past two decades. Federal support has shrunk in every category. Funds for housing rehabilitation fell 60 percent from 1992 to 2002. Section 8 rent subsidies were reduced from \$32 billion to \$16 billion during that same period. At the time that this book went to press, it appears that this trend will continue for Fiscal Year 2006. Tenant-based rental assistance is expected to remain about \$16 billion (\$15.53 billion). However, Home Ownership Partnership (HOME) funds are scheduled to drop \$41 million to \$1.9 billion; Community Development Block (CDBG) funds are expected to fall \$250 million to \$4.2 billion with most other programs staying at or about 2005 levels (homeless programs \$1.346; public and Indian housing \$6.8 billion; housing for people with AIDS \$285 million, and elderly housing programs \$741 million). A big question mark for 2006 remains the comprehensive

---

<sup>14</sup> California, Colorado, Iowa, Massachusetts, Maryland, Minnesota, Michigan, New Jersey, Pennsylvania, Rhode Island, Vermont, Washington, and Wisconsin have all taken actions to utilize state resources to preserve their affordable housing stock. See State Housing Finance Agencies: Developing Programs to Preserve Affordable Housing, September 2004, National Housing Trust and New Jersey Housing and Mortgage Finance Agency, <http://content.knowledgetplex.org/kp2/cache/documents/66651.pdf>.

#### 1.4 CURRENT TRENDS IN AFFORDABLE HOUSING

public housing redevelopment program, HOPE VI. The president and the House propose to eliminate the program for 2006. Experts believe that it will be salvaged but funded at low levels, possibly for the last time in 2006.

##### **(b) The Shift to the Suburbs**

The LIHTC has not only shifted power to the states, but it has also brought affordable housing to the suburbs in record numbers. Prior to the LIHTC, approximately 76 percent of all federal housing funds were invested in central cities. Since the inception of the LIHTC and its administration by the states, housing investment in the suburbs has increased almost 75 percent. A recently published Brookings Institution study found that approximately 42 percent of all LIHTC developments have been built in suburban locations.<sup>15</sup> This trend is significant given the fact that most affordable housing built today is built with the LIHTC. Moreover, it is likely to continue as power bases in many states shift from largely Democratic urban central cities to largely Republican suburban and rural areas.

##### **(c) Emerging Role of Affordable Housing As a Platform for Bringing Individual Economic Development Opportunities to Low-Income Residents**

Five years ago, Rey Ramsey and I started a new nonprofit organization, One Economy Corporation, in order to use affordable housing as a platform for connecting low-income people to the opportunities provided by the Internet. Our goals were: (1) to change state housing finance policies so all units financed with the LIHTC provided free or low-cost high-speed Internet access to residents, and (2) to build a "self-help, self-sufficiency" destination online that residents could use to find a better job, qualify for health insurance, help their children with homework, or learn how to save money.

In January 2004, we launched the Bring IT Home campaign with the U.S. Senate majority and minority leader as co-chairs and underwriting from housing giants Freddie Mac and Fannie Mae and support from technology and telecommunications companies such as Verizon, Qwest, SBC, Bell South, Yahoo!, eBay, Google, Cisco, Intel, and Microsoft. Over the campaign's first 18 months, more than 33 state housing finance agencies changed their LIHTC requirements to require or incent affordable housing developers to bring affordable high-speed access to each resident in the privacy and dignity of their own homes.

---

<sup>15</sup> Lance Freeman, *Siting Affordable Housing Location and Neighborhood Trends of LIHTC Developments in 1990s*, Washington D.C. The Center on Urban and Metropolitan Policy, Brookings Institution (2005).

## DEVELOPING AFFORDABLE HOUSING IN THE TWENTY-FIRST CENTURY

Mayors, governors, and other elected officials have embraced this approach enthusiastically. They see affordable housing as a cost-effective way to insure that low-income people have the means to take advantage of economic opportunities available through the Internet. These opportunities include continuing education, workforce training or retraining, applying for and receiving public benefits, and finding new markets for microenterprises. One Economy's online portal, the Beehive ([www.thebeehive.org](http://www.thebeehive.org)) has helped make these possibilities a reality. The site, now localized to serve 26 different cities and states, serves more than 150,000 people a month in English and Spanish.

### (d) Fall in Rental Housing Supply Overall

The United States has seen an extraordinary boom in homeownership over the past ten years. This boom, in many ways, has been to the detriment of the rental housing market. Fewer rental units are being built, and more and more existing units are being lost from the housing stock. Overall, rental housing production fell from 275,000 units in 2002 to 262,000 units in 2003.<sup>16</sup> Unlike rental housing built prior to 1990, today's rental units are being built for higher-income people. Nearly half of the rental housing units that have been built since 1990 have rents greater than \$750. Only one-fifth of new rentals during this period were targeted to the bottom income tier. This is in stark contrast to the rents at units built prior to 1990. Only 29 percent of those units had rents at the \$750 level or above.<sup>17</sup>

In many areas of the country, new units barely replaced the number of units lost to the housing stock. From 1992 to 2001, for every three new units added, two existing units were removed.<sup>18</sup> In the Midwest, more units were lost than were added over this period. The Northeast added only 100,000 more units than were lost.<sup>19</sup>

Nationwide, many LIHTC developments are at particular risk of being lost from the housing stock because their initial 15-year use restrictions are expiring. While the LIHTC was enacted in 1986, the program did not begin producing units at any level of scale until the early 1990s. Thus, many of these projects reach their 15-year anniversary in the next few years. As noted above, state housing finance agencies are waking up to this reality and developing programs to preserve these units for the long term.

---

<sup>16</sup> *State of Nation's Housing* at 20.

<sup>17</sup> *Id.* at 23.

<sup>18</sup> *Id.* at 22.

<sup>19</sup> *Id.*

#### 1.4 CURRENT TRENDS IN AFFORDABLE HOUSING

##### (e) Fundamental Transition in the Industry to Fewer, Longer Term Owners

In many ways, we have seen the nature and character of the affordable housing industry change dramatically since the 1990s. Federal policies from the 1950s to the 1970s were focused on stimulating the supply of affordable housing. These policies brought an array of for-profit developers into the emerging sector with the promise of making money by sheltering profits from federal taxation, generating considerable fees from financing, construction and management activities, and the later conversion of these developments into for-profit housing in no more than 30 years.

As time passed, federal policy turned from stimulating supply to supporting demand (rent subsidies). As noted above, more than 50 percent of HUD's budget is dedicated to rent subsidies currently. More importantly, the ability to use rental housing as a way to shelter income from federal taxation was all but eliminated by tax reform in 1986. These changes have had dramatic impacts on the sector. First, many of the developers who were in the business simply to shelter income and for the quick fees are long gone. They left once their primary reasons for keeping their capital in affordable housing were no longer available to them. Second, the exodus of the opportunistic many has left the committed few. That means that the industry now is primarily populated by entities that are in the business based on its inherent economics, cash flow from rents, not short-term fees and tax benefits.

This evolution has led many of the remaining owners, policymakers and funders who work with them, to look more to the long term. In many ways, this is bringing a new, holistic discipline to the sector. Historically, programs and policies would veer from focusing exclusively on supply or on demand. Now, many are focusing on how to stabilize and grow the sector by insuring that new *and* existing developments are structured financially so they will both remain in the housing stock for the long term.

##### (f) Broad Embracing of Mixed-Income Communities

The federal government's emphasis on supply from the 1950s to the 1970s had another unexpected outcome: extreme concentrations of low-income people in a limited number of neighborhoods. Troubled "projects," such as Cabrini Green public housing in Chicago or HUD-insured Geneva Towers in San Francisco, became the face of federal housing policy. By the late 1980s, policymakers began looking for alternatives to this "warehousing of the poor." The Affordable Housing Act of 1990 authorized funds that would demolish the worst of these developments. New "mixed-income" communities would rise up in their place populated with people

## DEVELOPING AFFORDABLE HOUSING IN THE TWENTY-FIRST CENTURY

of low, moderate, and even high incomes. Although the federal program that initiated this approach, HOPE VI, has had its detractors, the reality of building or rebuilding neighborhoods as mixed-income communities has become the norm. Today, many of the most successful “new communities” across the country are composed of inhabitants with incomes from across the spectrum.

### **(g) Increased Scrutiny of Government-Sponsored Enterprises (Fannie and Freddie)**

Fannie Mae and Freddie Mac are two government-sponsored enterprises (GSEs) that were created in the 1960s and 1970s to buy home mortgages made to low- and moderate-income households by financial institutions around the country. Fannie and Freddie buy home mortgages of low- and moderate-income households that financial institutions otherwise would have had to hold for 15 to 30 years, thereby freeing the capital up earlier and enabling the lenders to make more homeownership loans. This approach has not only increased homeownership dramatically but also created two incredibly profitable companies that enjoy the perception that their activities are guaranteed by the full faith and credit of the federal government.

In the past decade, the GSEs have come under sharp attack by many on Wall Street who believe that Fannie and Freddie, as for-profits, enjoy an unfair advantage because of their special federal relationship. Critics also argue that the market no longer needs the GSEs because there now are many other players who do the same work as Fannie and Freddie without the implicit federal guarantee.

Pressure on the federal government to act on the GSEs has increased in the past three years as they both have been found to have had accounting improprieties. Congress is considering legislation that could result in greater focus on and increased investment in affordable housing.

## **1.5 UNIQUE OPPORTUNITIES FOR NONPROFIT ORGANIZATIONS: RENTAL AND HOMEOWNERSHIP**

As a whole, these trends point to unique opportunities for nonprofit organizations as we turn to the second half of this millennium’s first decade.

**(i) Homeownership.** The increased pressure on Fannie Mae and Freddie Mac is forcing them both to focus more on their missions of serving the underserved. They both have raised the visibility and support of initiatives to help minorities and people of color to become homeowners. Moreover, a number of proposals pending before Congress suggest that

### 1.5 UNIQUE OPPORTUNITIES FOR NONPROFIT ORGANIZATIONS

the two GSEs use a portion of their profits to establish a fund that will make resources available for affordable housing.<sup>20</sup>

**(ii) Rental Housing.** Most opportunities, however, are likely to be found in the developing of rental housing for a number of reasons. One, the sector has shown that it can attract and allocate tax credits efficiently and effectively. The private sectors interest in investing more than \$5 billion a year in housing through the LIHTC has strengthened this tool in the eyes of everyone, most importantly, elected officials. These successes not only have made affordable housing advocates of the American business community but also have laid the foundation for possible expansion of the LIHTC or the creation of new tax credit initiatives. The establishment of the New Markets Tax Credit in 2000 is an excellent example of this.

Second, government, financial institutions, and philanthropic organizations now acknowledge the need to both preserve the existing affordable housing stock and continue to build new stock. This reality combined with the third factor, that the public and private sector has an enormous amount of confidence in the nonprofit housing development sector, means that nonprofits are poised to play an ever-increasing role in the future. Nonprofits now have a 20-year track record of taking on troubled developments and turning them around in communities big and small. Nothing succeeds like success.

---

<sup>20</sup> [www.washingtonpost.com/wp-dyn/content/article/2005/07/26/AR2005072602033.html](http://www.washingtonpost.com/wp-dyn/content/article/2005/07/26/AR2005072602033.html).

