

Public Housing Summit Investment Group Concepts

- A. *Goal: to sustain public housing as an affordable housing resource for future generations, by eliminating the backlog of capital needs over ten years and providing for long-term financial stability*

The United States should not countenance substandard public housing, and should not allow this irreplaceable national resource to be lost by failing to make the investments needed to preserve it for the next generation. The backlog should be eliminated through repair, revitalization or replacement of current public housing sites. The repaired, revitalized or replacement housing should be affordable on a long-term basis, and primarily serve families with extremely low incomes, in poverty-deconcentrated settings to the extent possible. The overall result should be a net gain in viable affordable housing. This housing must be managed efficiently and financially stable on an ongoing basis.

The capital needs study that Congress mandated in the fiscal 2008 appropriations act should help to refine this goal, by articulating both the capital backlog needs and ongoing (accrual) needs fully and by category of development (for example, elderly/disabled sites, family sites; levels of capital needs). The necessary level of repair or revitalization or the need for replacement will depend upon the condition and potential long-term viability of individual current public housing developments. While cost is a key issue, the goal must be housing that will be viable over the long term, and be a clear asset to its community. At a minimum housing should meet the quality standards used to determine which units families can rent with Section 8 vouchers and be of a quality that could command rents similar to those charged for affordable decent-quality housing in the local market. Matching the quality of units produced by the low-income housing tax credit program (tax credits) would more likely ensure units that would remain a viable asset.

If this effort is to be sustained over time, and maximum investment to be attracted to begin with, the funding system for completed developments must change. Whether through project-based voucher funding or a reconstituted public housing funding system including predictable operating funding, a capital replacement reserve, and a mechanism for recapitalization after 20-30 years, the ongoing funding of these developments must achieve the funding stability of other multifamily real estate if these resources are to be preserved.

- B. *Resources Needed: at least \$32 billion with full hard unit replacement as needed, plus adequate ongoing funding for debt service, replacement reserves and operating expenses*

The \$32 billion estimate was derived by the Center on Budget and Policy Priorities, and included for calculation purposes the preservation of approximately 1.06 million of the 1.16 million units available in 2009, and replacement of 100,000 units demolished or disposed of with hard units. The Center used results from the HUD study of capital backlog needs as of 1998, adjusted for (1) construction cost inflation, (2) appropriations levels, (3) use to date of the Capital Fund Financing Program (CFFP), and (4) annual new (accrual) needs based on results from the HUD study, adjusted for inflation and to take into account that some of the backlog has

not been addressed and thus some over-age systems are not accruing new needs, to estimate renovation needs. The Center used per-unit amounts based on HUD's total development cost limits to estimate replacement needs. This is only the roughest estimate, pending the results of the new study. Because the last HUD study assumed only modest upgrades of decades-old housing, the amount estimated for renovations is likely a minimum amount and would be considerably greater if properties are to be brought, for example, to tax credit standards.

Using these assumptions, the cost of replacing 100,000 units with newly-constructed housing is roughly 45% of the total. This illustrates that the amount needed would vary greatly with the number of units to be demolished or disposed of rather than rehabilitated, and with the proposed mix of replacement with hard units or tenant-based vouchers.

C. Mechanisms

1. Conversion to project-based vouchers for selected family developments: Project-based vouchers (PBV) are a particularly effective mechanism for use in connection with some family developments with modest to moderate rehabilitation needs, because such needs could be financed within eligible rent levels, additional financial discipline would result from separating the development's income stream from others, and the structure of PBV allows for mobility after one year's occupancy. PBV also is fairly easily combined with tax credits to support more extensive rehabilitation.

Such conversions could be done in a systematic way, with a target as high as 400,000 units over 10 years. The program rules would be altered to work with current public housing sites (for example, the limitation on number of subsidized units per building would have to be removed, subject to a reasonable limitation on the share of an agency's vouchers that could be project-based, to ensure that the mobility option remains viable). Developments could be prioritized where the rent levels will support critical rehabilitation or replacement and/or where other local and federal resources can be leveraged, and where sites are in deconcentrated settings. A workable mechanism to facilitate borrowing, through FHA or otherwise, must be in place.

2. Recapitalization and stabilization, including necessary services, for senior/ disabled developments: There is broad support for our public housing serving elderly and disabled families. Given national demographics, the continuing need for this public housing should be apparent. Even though such families or individuals constitute more than 50% of public housing households, however, support has not been reflected in public housing appropriations levels.

A more directed approach is needed. The capital backlog needs of the elderly/disabled developments should be addressed fully and promptly through appropriations. This could be done with a dedicated annual appropriation of approximately \$400 million over the next decade. To assure ongoing viability, each rehabilitated development should be provided a separate annual contributions contract under which both operating funding and capital replacement reserve funding would be made available. Reasonable initial amounts would be adjusted annually for inflation. Each rehabilitation transaction would include a demonstration of sufficient services resources or a commitment to seek them, through various resources including Medicare/Medicaid where possible, and a further goal could be included of 100,000 service-enriched units. The mechanism also would build in the potential for mortgaging and annual

subsidy increases to the extent needed in the future to allow recapitalization. The contract could be provided under a reconstituted public housing program, or a new initiative similar to project-based Section 8.

3. Expanded availability of Low-Income Housing Tax Credits: PHAs already are successfully using both 9% and 4% credits on a substantial scale, but competition for 9% credits is tight, and use of 4% credits for public housing rehabilitation has been relatively limited. This approach bolsters individual revitalization efforts, by bringing additional financial discipline and the judgment and requirements of private investors into the mix.

Additional availability of the tax credits for public housing rehabilitation, revitalization or replacement efforts is needed, as follows:

- The 4% tax credit should be revised to support a higher level of public housing renovation or revitalization costs. This could be done, for example, by providing for a 200% basis bump-up or a credit rate above 4% for such efforts, or perhaps to the extent the housing will serve extremely low-income families. A national carryover of unused bond cap authority could be made accessible to areas that need it, so that those areas could access 4% tax credits.
- Authorization of an additional pool of 9% credits, modified somewhat to take into account specific characteristics of public housing revitalization or redevelopment, or an alternative credit of similar value, would be an even stronger mechanism. Any such approach must be designed carefully to avoid competition for resources with the current 9% credit. These changes could be for the decade during which the public housing backlog is to be addressed.

4. Green investments: Efforts to provide for “greening” investments to improve the Nation’s long-term environmental and energy prospects rightly will become prominent during the coming years, and the greening of public housing must be included. New sources of funds, such as from carbon taxes, should be harnessed. These investments will address the capital backlog at the same time as they accomplish greening objectives.

5. Other structural reforms: Particularly with respect to the public housing Operating Fund, reforms should be considered that will contribute to funding stability. Such reforms may include measures such as stronger incentives for energy conservation (for example, lengthening or freezing of the “rolling base” in situations other than those involving third-party financing, to provide PHAs more of an incentive to undertake energy-conserving improvements). More flexibility should be provided to allow for development of replacement public housing in diverse locations.

6. State and local efforts: All of these mechanisms should recognize substantial state and local housing efforts, such as local trust funds and state housing bond issues (e.g., several billion dollars for affordable housing in California), and facilitate and favor these efforts’ use in connection with federal resources to address the backlog. The new Affordable Housing Trust Fund is another potential source. Competitive federal funding awards and streamlined federal processing should facilitate and reward State and local financial participation wherever possible.

7. Transitional continuation of current mechanisms (Operating Fund, Capital Fund, Capital Fund Financing Program, energy performance contracting (EPC), public housing project-basing, HOPE VI)

Current mechanisms for raising capital should be continued to the extent they are working efficiently and are needed as part of an overall strategy to eliminate the backlog and sustain viability. An essential element during the transition period must be full operating funding to meet reasonable ongoing expenses. The Capital Fund is an efficient mechanism for relatively modest per-unit rehabilitation where financing is not cost-effective, gap funding for project-based voucher transactions where capital needs are greater than repairs that can be financed within market rents, and debt service repayment for CFFP, and this implies transitional annual funding somewhat above that needed to meet debt service and accrual/replacement reserve obligations. CFFP already has leveraged about \$2.6 billion in the past five years, should remain available, and could be strengthened with further streamlining and adoption of a proposal such as tax credits for bond-holders that would reduce borrowing costs. Any new funding mechanisms must fully honor outstanding CFFP commitments, and should be designed to facilitate additional CFFP borrowing where this remains the most sensible approach for a PHA to address its backlog.

EPC has financed \$500 million in energy-related improvements using anticipated operating cost savings, and should continue to generate funding. A restored and updated HOPE VI program is needed where large-scale neighborhood revitalization is called for and key community investments can be leveraged. HUD's practice of allowing additional operating subsidy for replacement units produced with leveraged capital funds must be continued.

Another current, but dormant, capital-raising mechanism is the ability of PHAs to mortgage their developments to raise funds on a property-specific basis. Even though few PHAs may use this mechanism because use of CFFP is easier, it could be used in some situations CFFP cannot, and thus HUD should activate the mechanism. HUD expeditiously should provide guidance how to pledge public housing rents, operating subsidy and capital funds along with mortgages on individual developments and ability to make annual replacement reserve commitments, subject to continuing long-term use restrictions ensuring availability for extremely low-income families.

While these mechanisms would be retained to contribute to the elimination of the capital backlog, as developments are renovated or replaced they should be provided greater assurance of adequate financial support, through the mechanism outlined above in connection with the renovation initiative for senior/disabled developments (individual contracts including inflation-related operating cost adjustments and capital replacement reserves). PHAs could be allowed to "opt in" to this system for developments that do not or no longer need extraordinary capital work, perhaps with a triggering mechanism linked to a development's acceptable physical condition and management performance.

D. Match of needs and resource mechanisms; appropriations

Estimates are needed of the amount of funds each of the mechanisms discussed above could be expected to generate, followed by annual appropriations implications. Some rough numbers for potential capital funds generated might be the following:

- Capital Fund: \$4 billion (average \$20,000 per unit for 200,000 units (renovation))
- Capital Fund Financing Program (CFFP): \$3 billion (mix of renovation and replacement)
- Senior/disabled preservation: \$4 billion (200,000 units) (renovation)
- Energy Performance Contracts: \$1.5 billion (renovation)
- Project-based voucher (PBV) conversion: \$9.75 billion (325,000 units @ \$30,000 per unit) (mix of renovation and replacement)
- 4% credits: \$4 billion (100,000 units @ \$40,000/unit; substantial use in connection with CFFP and PBV) (mix of renovation and replacement)
- Public housing greening: \$5 billion (other funding) (mix of renovation and replacement)
- HOPE VI and 9% credits (separate initiatives): \$4.5 billion total (30,000 units @ \$150,000 per unit) (largely replacement)
- Capital Fund Replacement Housing Factor: \$1.5 billion (10,000 units @ \$150,000/unit) (replacement)

The above mix of initiatives is illustrative. Addressing more of the backlog with one mechanism would lessen the burden on the other mechanisms. These numbers add to considerably more than the Center estimate, thus providing some room for more extensive renovations than the estimate includes, further inflation in costs, and contingency.

While the annual appropriations need would be considerable initially, it would be mitigated over time to the extent renovated units could be provided ongoing capital replacement reserves substantially lower than the last HUD study's estimate of per-unit "accrual" needs. This appears possible, provided that the necessary recapitalization mechanisms are included in the proposal as discussed above. In addition, a number of the funding sources listed above do not require full direct annual appropriations.

Thus, the list of potential resources above must be analyzed further to determine direct appropriations demands. For example, funds that would have come from the Capital Fund in the past would include amounts listed above for the Capital Fund (\$4 billion), CFFP (annual debt service necessary to finance \$3 billion plus \$2.5 billion already outstanding, or roughly \$4 billion over ten years), senior/disabled preservation (\$4 billion), replacement housing factor (\$1.5 billion), and replacement reserves (\$7.5 billion if 750,000 units were covered for ten years at

\$1,000 per unit per year). If all of these expenses were incurred fully for all ten years, the annual total would be \$2.1 billion in this example, which is lower than recent annual Capital Fund appropriations and leaves some room for other necessary appropriations (project-based vouchers, HOPE VI). But these funding levels will not be needed at the same level for ten years—the need for the replacement reserves will increase during the decade, while the need for capital grants will decline as units are completed or transition to project-based vouchers.

[COMPLETE THE ANALYSIS OF IMPACT OF PROPOSALS ON APPROPRIATIONS]

Of course, any proposal for additional resources will be in competition with many urgent domestic and funding priorities. The case will have to be made why any such investments will be better than the perceived results of some of the previous public housing investments or alternative housing investments, and are critical to the Nation.

E. Federal entity—“Public Housing Investment Trust”

Although the public housing investment strategy must continue to be driven locally, and HUD has made positive efforts to encourage such investments, the required initiative demands a more proactive national role. A more concentrated effort is needed, with a mission to track and facilitate the reduction in the capital backlog and reinvestment in public housing, provide additional technical assistance, and issue helpful regulations and streamlined procedures. The entity would need more expertise in project-basing and tax credits than is present in HUD’s current public housing administrative apparatus, and should be substantially separated from it. HUD’s Office of Affordable Housing Preservation and its contractors have such expertise, and their initiatives may be a useful model to consider further. Entities outside HUD, including State Housing Finance Agencies and private contractors, should be used to a greater extent. Further discussion is needed regarding placement of the entity; whether the entity could have a relatively small amount of gap funding to invest, use as credit enhancement or use in other ways that would make individual transactions work; and whether the ability to purchase and sell PHA debt in a similar manner to GNMA is necessary.