Building an Even Stronger Low-Income Housing Tax Credit

BY EMILY CADIK

CONGRESSMAN Pat Tiberi (R-Ohio), the leading Low-Income Housing Tax Credit (Housing Credit) champion in the House of Representatives, speaks often about the profound impact that seeing Housing Credit properties in his district has had on him personally.

“I've seen first-hand the benefits of the Low-Income Housing Tax Credit during my visits to low-income housing developments in my district,” Tiberi said this February. “It's an effective, successful program.”

The many tours of Housing Credit properties in his district organized by local developers and
partners have not just converted Tiberi into a supporter. Similar tours in other districts have been instrumental in transforming many of his colleagues on both sides of the aisle into supporters of the program as well.

The affordable housing industry’s concerted efforts to show members of Congress Housing Credit developments in their home states and districts is one of the primary reasons that the program has enjoyed bipartisan success over the years. But with half of Congress newly elected since 2010, and with 13 new Senators and 58 new Representatives in this Congress alone, there is never a shortage of opportunities for education.

Threats to the Housing Credit—both from tax reform and from the increasingly difficult affordable housing financing environment—make education around the Housing Credit even more important now than ever before. And the compelling stories that affordable housing developers and partners can tell about the program are critical to its future.

A Brief History of the Housing Credit

The Housing Credit is a product of the last major tax reform effort, in 1986—a bipartisan initiative signed into law by President Reagan. Over the past three decades, it has financed virtually all affordable rental housing in the U.S., creating or preserving over 2.7 million affordable homes by leveraging over $100 billion in private capital. It is “pay for performance,” representing the best of public-private partnerships and ensuring a high degree of efficiency, accountability and results. It is an economic stimulator: in a typical year, the program supports roughly 96,000 jobs, mostly in the small business sector, and adds approximately $3.5 billion in taxes and other revenues to local economies, according to the National Association of Home Builders.

The Housing Credit is also essentially the only option for building new affordable housing. In order to develop housing that would require households earning the minimum wage to pay no more than 30 percent of their income in rent, constructions costs would have to be reduced by about three-fourths of the current average. It simply doesn’t work without a subsidy, and there are very limited options for developing new properties without the Housing Credit.

In addition to providing sorely needed new affordable housing, leveraging private capital through the Housing Credit has become increasingly important for the preservation of existing affordable and assisted housing in the absence of any new capital subsidy programs—and it does not appear that over $26 billion of public housing capital needs backlog will be replenished any time soon. The Housing Credit is expected to provide roughly one-third of the financing to recapitalize over 180,000 units of public housing converting under HUD’s Rental Assistance Demonstration, for example.

The Housing Credit also serves as a complement to the voucher program. While vouchers are the primary way to bring down the cost of existing rental housing, the Housing Credit is needed in order to expand or preserve the affordable housing stock for the long
term, to bring housing supply into tight rental markets, to build developments that have special features needed to serve the residents and to revitalize communities. Likewise, vouchers are often needed in order to make Housing Credit apartments affordable to the lowest income households. It is impossible to meet the housing needs of many communities without both of these programs.

As the nation's housing needs evolve, the Housing Credit has become increasingly interrelated with traditional rental assistance programs, meaning that its continued success will rely on some less traditional allies. The agencies and partners administering these rental assistance programs have important stories to tell about the role that the Housing Credit plays in the work that they do, stories Congress needs to hear as it considers tax reform.

Threats to the Housing Credit from Tax Reform

The House, the Senate and the White House are all interested in pursuing tax reform in this Congress. Even if it is unlikely that they ultimately agree upon and pass a tax reform bill, any draft legislation that emerges from this Congress is likely to be a starting place for future efforts—meaning it has to be taken seriously. If a tax reform proposal eliminates or weakens the Housing Credit in this Congress, it will be that much harder to preserve or strengthen it in the next. And all tax expenditures are on the chopping block in order to bring top corporate rates down from 35 to 28 or even 25 percent—even popular ones like the Housing Credit.

Tax reform legislation will likely come out of the Senate first. Throughout the spring, the Senate Finance Committee has been considering tax reform through five working groups examining different portions of the tax code. Now that they have completed the process of soliciting feedback from the public through written comments and a series of roundtable discussions, they will be providing recommendations to the full committee by the end of

May that will be incorporated into draft legislation to be released this summer.

The timeline for tax reform in the House is less clear. House Ways and Means Chairman Paul Ryan (R-Wisc.) is certainly committed to tax reform, but has not yet made any announcements about how he plans to proceed. He appears to be using previous Chairman Dave Camp’s tax reform discussion draft as a starting point, which has both its advantages and disadvantages for the Housing Credit.

The Housing Credit was one of only three corporate tax expenditures preserved in the Camp discussion draft while dozens of others were cut, demonstrating strong bipartisan support for the program. On the other hand, the Camp draft proposed very troubling changes that would severely undermine the Housing Credit’s ability to achieve its purpose. These included eliminating the acquisition credit (also known as the “4 percent” credit), which currently preserves close to 20,000 affordable apartments each year. It would completely eliminate private activity multifamily housing bonds (Housing Bonds). Housing Bonds paired with 4 percent Housing Credits are responsible for financing more than 40 percent of annual Housing Credit production, providing affordable homes to over 1 million families since 1986. It would also lengthen the credit period from 10 to 15 years, which would reduce investor demand in the program and limit the amount of private equity capital that could be raised.

Even without modifications to the Housing Credit program or Housing Bonds, tax reform could have negative impacts on the pro-
gram through changes to other parts of the code. For example, the draft proposes to lengthen the depreciation period for real estate from 27.5 to 40 years and to lower the corporate tax rate to 25 percent, both of which would reduce the benefit of Housing Credit investments to investors. Combined with the proposal to lengthen the credit period, these two changes would result in a cumulative loss of as much as 19 percent of the total Housing Credit equity—about $1.5 billion annually, or as many as 13,000 units—according to industry accounting firm Novogradac & Company LLP.

All told, the reforms proposed in the Camp discussion draft could reduce annual Housing Credit production by over 60 percent, or a loss of up to 54,000 affordable apartments. The fact that the draft protected the Housing Credit at all was a major achievement for the affordable housing industry, but it also underscored that simply preserving it is not enough, and that Congress may be willing to make harmful changes to the program in order to generate cost savings.

That’s why, in addition to advocating for our top priority of protecting the Housing Credit in tax reform generally, we are being clearer about the need to protect each fundamental component of the program: the 9 percent credit for new construction and substantial rehabilitation, the 4 percent acquisition credit and the 4 percent credit used in Housing Bond-financed properties, as well as the preservation of Housing Bonds. We are also calling on Congress to maintain the 27.5-year depreciation period for Housing Credit developments, and to make any adjustments needed to offset the impact of a lower corporate rate on the Housing Credit.

**Threats to Affordable Housing Financing**

Beyond the existential threat posed by tax reform, the Housing Credit faces more practical threats as a result of a variety of factors that have made affordable housing financing more difficult. Foremost among them are “floating” Housing Credit rates.

Housing Credit rates determine how much tax credit equity can go into any given development. The rates were originally set at...
9 and 4 percent (which is how the “9 percent” and “4 percent” Housing Credit programs got their names), but the rates now float according to a formula related to federal borrowing rates. Because borrowing rates are at historic lows, the Housing Credit rates in use today are 15—20 percent lower than when the program was created. Recognizing that the rates had sunk below what was needed for many projects to be viable, Congress enacted a temporary minimum 9 percent Housing Credit rate in 2008, which was extended twice. However, it has now expired despite bipartisan support for its extension.

When less Housing Credit equity is available for each development, more gap funding sources are needed in order for the financing to pencil out. But as a result of budget cuts at the national, state and local levels, these programs are becoming increasingly scarce. The HOME Investment Partnerships Program, for instance, which has financed the construction of over 1.1 million affordable homes, has been cut by over 50 percent in recent years.

The combined effect of floating credit rates and cuts to gap financing sources is that some developments have simply become impossible to finance. This is especially true for developments that require more resources, including ones that serve lower-income tenants or provide additional building amenities (like accessibility features or community spaces) to assist the populations that they serve.

A Proactive Agenda to Protect, Strengthen and Expand the Housing Credit

Facing these challenges to the Housing Credit requires a comprehensive advocacy strategy. To meet this need, the affordable housing industry formed a broad, grassroots coalition known as the Affordable Rental Housing ACTION (A Call To Invest in Our Neighborhoods) Campaign, which now boasts nearly 900 national, state and local organizations focused on ensuring that low-income households throughout the nation have access to decent, safe, affordable rental housing by supporting the Housing Credit.

(Disclosure: NAHRO serves on the Steering Committee of the ACTION Campaign, which is responsible for leading the development and implementation of the campaign’s strategic agenda.)

The ACTION Campaign’s strategy involves traditional legislative advocacy, research to help make our case, and local outreach and targeted media to reach members of Congress in their home states and districts. NAHRO’s members have been especially invaluable in engaging in the local outreach needed to transform members of Congress into supporters of the program. Public housing authorities in particular are excellent ambassadors of the program, given the interconnectedness of the Housing Credit and other rental assistance programs as they are used together to meet local needs.

For the past several years, the ACTION Campaign has primarily been focused on protecting the Housing Credit in tax reform and strengthening the program through minimum Housing Credit rates—priorities that will continue going forward. But we also recognize that tax reform is an opportunity—and so in 2015 we are taking on a more proactive, expanded agenda to build an even stronger program.

Expanding the Housing Credit

In addition to defending the program, the ACTION Campaign is beginning to lay the groundwork for more Housing Credit resources by citing the data showing the vast and growing gap between what low-income renters can afford and the number of affordable homes available. An astonishing 11 million renter households—more than one in four of all renters in the U.S.—
spend more than half of their monthly income on rent, according to the Harvard University’s Joint Center for Housing Studies, meaning too many households have to choose between paying rent or buying food, paying medical bills or repairing their cars. The crisis is expected to worsen, as hundreds of thousands of new renter households—many of them low-income—enter the market and existing public and affordable housing is lost from the stock.

Meanwhile, state Housing Credit allocating agencies are forced to turn down viable affordable housing developments each year because there simply are not enough credits. States typically receive applications requesting two to three times as many Housing Credit resources as they have available, meaning they are unable to finance critically needed projects year after year.

Increasing the annual Housing Credit allocation is virtually the only way to increase the supply of affordable rental housing in order to begin closing the gap.

Giving States the Tools They Need

One of the features that has made the Housing Credit so successful is that state allocating agencies administer the program with significant flexibility to allocate the credits in ways that meet local needs and priorities. With additional flexibilities, states could do even more to finance the types of developments needed, with sufficient resources to ensure their viability.

Establishing minimum Housing Credit rates would allow states to increase the amount of equity in any given Housing Credit development in order to ensure viability. The temporary minimum 9 percent rate created in 2008 was extended twice in “tax extender” legislation. But the last tax extenders bill passed so late in 2014 that it provided no practical benefit for the Housing Credit, and the rate is once again expired. Further congressional action is needed in order to reinstate the 9 percent rate, and to create a minimum 4 percent rate for both acquisition Housing Credits and Housing Credits paired with Housing Bonds.

Representatives Tiberi and Richard Neal (D-Mass.) reintroduced legislation in the House to create minimum 9 and 4 percent rates (H.R. 1142) in February, and Senators Maria Cantwell (D-Wash.) and Pat Roberts (R-Kan.) introduced their companion legislation in April. Gaining extensive bipartisan support for these bills is the best way to making the case that minimum credit rates should be extended again in tax extenders, and even made permanent in tax reform.

The ACTION Campaign is also urging Congress to give states the ability to allow “income averaging” within Housing Credit developments. Currently, most Housing Credit properties have an income limit of 60 percent of area median income, which can limit the ability of developers to create mixed-income communities. We recommend that, instead, developers have the flexibility to serve households with income up to 80 percent of the area median, so long as the average income limit for the property is no higher than 60 percent of the area median. This would allow for Housing Credit developments to serve a broader range of low-income households. Depending on market conditions, it could even help bring down rents for lower-income households without additional subsidy by bringing in tenants who are able to pay slightly higher rents.

Making the Case for Our Priorities

Protecting, strengthening and expanding the Housing Credit will require continued education around the Housing Credit—how it works, how it impacts communities and how it could even better serve low-income households. NAHRO members have played an important role in building the support that we have to date, and will be needed even more as we cultivate more champions in the new Congress to support our expanded set of priorities.

Emily Cadik is a Senior Analyst/Project Director at Enterprise Community Partners, where she oversees tax policy related to the Low-Income Housing Tax Credit and the New Markets Tax Credit, as well as numerous public housing and rental assistance policy issues. Prior to joining Enterprise, she was a program coordinator for HUD’s Moving to Work public housing demonstration, where she was involved in developing recommendations for public housing and voucher reforms. As a Presidential Management Fellow at HUD, she also worked in HUD’s Office of Intergovernmental Affairs and Public Engagement, as well as for Bread for the City, a local comprehensive service agency for low-income families. She earned a Master in Public Policy degree from the Harvard Kennedy School of Government and a Bachelor of Arts degree from the University of Texas at Austin.