



ACTION Campaign Comments for the Senate Finance Committee Community Development and Infrastructure Working Group

The Affordable Rental Housing ACTION (A Call To Invest in Our Neighborhoods) Campaign is a national, grassroots coalition focused on supporting investment in affordable rental housing. The campaign represents a broad cross-section of nearly 900 organizations and businesses dedicated to creating and preserving affordable homes for low-income families using the Low-Income Housing Tax Credit (Housing Credit) and multifamily tax-exempt private activity housing bonds (Housing Bonds). A full list of ACTION Campaign members is attached.

The ACTION Campaign appreciates the thoughtful consideration that the Senate Finance Committee is devoting to tax reform and the opportunity to provide our recommendations related to the Housing Credit, our nation's most successful affordable rental housing production tool. The Housing Credit was established as part of the Tax Reform Act of 1986, and is now a permanent program in Section 42 of the Internal Revenue Code. Since its creation, 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. The Housing Credit is "pay for performance," representing the best of public-private partnerships and ensuring a high degree of efficiency, accountability and results, which is why it has always experienced bipartisan support. 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.

In summary, we recommend that Congress:

- Protect existing Housing Credit and Housing Bond resources:
 - Preserve the "9 percent" and "4 percent" Housing Credits,
 - Retain the multifamily housing private activity bonds tax exemption,
 - Maintain the current 27.5 year depreciation period for Housing Credit properties, and
 - Make adjustments to offset the impact a lower corporate tax rate would have on the Housing Credit should Congress reduce the corporate tax rate.
- Expand Housing Credit resources by an amount that makes significant progress towards meeting the affordable housing needs of low-income families.
- Provide states with flexibility to maximize Housing Credit resources:
 - Enact permanent minimum Housing Credit rates, and
 - Allow broader income mixing within developments.

These proposals are described in depth below.



Growing Affordable Housing Need

Though the Housing Credit has provided affordable homes for millions of low-income households, the unmet need for affordable rental housing continues to far outstrip the available resources. The Housing Credit is essentially the only way to increase the supply of affordable rental housing to meet our nation's vast and growing need.

An unprecedented 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 (JCHS), leaving too little for other expenses like food, medical bills and transportation. The affordable housing crisis is especially acute among those with the lowest incomes. According to JCHS, in 2012 there were 11.5 million extremely low-income families (those with incomes below 30 percent of area median income (AMI)), but only 3.3 million housing units that were both available and affordable to them. This has created an affordable housing supply gap of 8.2 million homes just for the lowest income households, marking a 55 percent increase in this gap since 2000.

Analysts expect an average of over 400,000 new renter households to enter the market each year for the next decade, many of whom will be low-income. The rental housing industry as a whole produces far fewer than this number of units each year, meaning that the gap in overall rental housing supply versus demand will only worsen. This factor alone will make it even more difficult in the immediate future and beyond for low-income renters to find suitable and affordable places to live as the competition for scarce rental housing becomes more acute. Meanwhile, we continue to lose affordable housing each year. Nearly 13 percent of the nation's supply of affordable housing – roughly 650,000 units – have been permanently lost from the stock of available housing since 2001 due to conversion to market rate rentals or condominiums, demolition or obsolescence. The net effect is that, according to JCHS, “the number of affordable units has stagnated over the past decade.” Though the affordable housing industry develops nearly 100,000 new affordable rental units each year, it cannot keep up with the growing demand and the loss of supply for housing for low-income households.

Protect Existing Housing Credit and Housing Bond Resources

It is critical that Congress preserve the Housing Credit in tax reform. Developing and preserving affordable homes for the growing population of cost-burdened low-income renters is not feasible without the Housing Credit, since the rents low-income households can afford are not high enough to cover the costs of building and maintaining properties. According to JCHS, to develop new apartments affordable to renter households working full-time and earning the minimum wage without the Housing Credit, construction costs would have to be reduced by 72 percent of the current construction cost average.

Unlike traditional direct spending housing programs, Congress designed the Housing Credit to operate through the tax code as a public-private partnership. Private sector investors provide upfront equity capital into a property in exchange for a credit against their tax liability in future years. Credits can be claimed only after properties are built and occupied by income-eligible residents at affordable rents. This unique structure transfers the real estate risk from the taxpayer to the private sector investor. State agencies select developments to receive Housing Credits based on a competition to meet



local priorities and monitor properties for compliance with program rules. In the rare event that a property falls out of compliance anytime during the first 15 years after it is placed in service, the state issues a finding to the Internal Revenue Service, which will trigger a recapture of the Housing Credits from the investor. Therefore, it is in the interest of the private sector investor to ensure that properties adhere to all program rules, including income eligibility, rent limits and high quality standards. This rigorous private sector oversight is a hallmark of the program, and has contributed to its unparalleled record of achievement. In fact, only 0.62 percent of all properties during the Housing Credit's nearly 30-year history have gone into foreclosure, a record far better than any other real estate class.

In addition to the need to preserve the Housing Credit generally, it is important to protect the fundamental components of the program and not impose new limitations on eligible activities. There are two types of Housing Credits: the 70 percent present value credit (referred to as the "9 percent credit") for new construction and substantial rehabilitation of properties that are not financed with the proceeds of Housing Bonds, and the 30 percent present value credit (referred to as the "4 percent credit") for the acquisition of existing buildings and for newly constructed or substantially rehabilitated properties which receive Housing Bond financing, discussed below in greater detail. While there is a clear need to build new affordable units, acquisition and rehabilitation of existing properties to preserve affordable housing is also a crucial use of the Housing Credit, including preventing existing federally assisted housing from being lost to obsolescence or decay or converted to market rate housing.

Given the unique housing markets and needs of each state, each of these components of the Housing Credit program – the 9 percent allocated credit, the 4 percent allocated acquisition credit and the 4 percent credit used in Housing Bond-financed properties – are critical to addressing states' affordable housing needs.

- [Preserve Multifamily Housing Private Activity Bonds Tax Exemption](#)

As noted, in addition to the Housing Credit authority subject to each state's per capita Housing Credit cap, states also may use tax-exempt Housing Bonds coupled with 4 percent Housing Credit equity to finance affordable rental housing. These 4 percent Housing Credit developments do not compete for credit authority with the 9 percent Housing Credit developments because the bonds with which they are paired are already limited by the state's annual bond volume cap. However, they must still comply with the state's allocation plan and with all other applicable Housing Credit rules.

Housing Bonds used in conjunction 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. Without these tax-exempt bonds, the Housing Credit's annual production potential would be cut almost in half. It is thus critical that Congress preserve the tax exemption on Housing Bonds in tax reform.

- [Maintain the Current 27.5 year Depreciation Period for Housing Credit Properties](#)

Today, approximately 30 percent of the value of a Housing Credit investment is based on the tax deductions from the investment, largely arising from depreciation. For Housing Credit developments financed using Housing Bonds, the tax deductions are an even greater proportion of the return on the investment. Though the rate of return on Housing Credit investments is dictated by market conditions, extending the depreciation period would cause the tax benefits associated



with an investment in Housing Credit property to decline, driving down Housing Credit pricing and resulting in less equity available for properties.

- **Make Adjustments to Offset the Impact of a Lower Corporate Tax Rate on the Housing Credit**

The amount of equity the Housing Credit raises for affordable housing is based on a number of tax-related factors, including the corporate tax rate. Should Congress lower the corporate income tax rate, we encourage Congress to consider making adjustments to the Housing Credit to ensure that at least as much affordable housing production is supported after tax reform changes are enacted as the Credit supports currently.

Today, the Housing Credit has a thriving equity market that generates more than \$10 billion per year in capital from investors. Affordable housing industry accounting firm Novogradac & Company LLP estimates that the combination of lengthening the depreciation period to 43 years, as proposed previously by the Senate Finance Committee, and a reduction in the corporate tax rate to 25 percent, would reduce Housing Credit investment by as much as \$1 billion annually. This reduction in investment would have the same economic consequences as cutting the Housing Credit itself by 10 percent, resulting in a potential loss of near 10,000 affordable apartments and 9,500 jobs each year.

Expand Housing Credit Resources

In addition to preserving current resources and important program features, the ACTION Campaign calls on Congress to increase Housing Credit resources by an amount that makes significant progress towards meeting the unmet affordable housing needs of low-income families.

Additional Housing Credit resources would make financing available for many critically needed affordable housing developments that are not built each year because of the scarcity of Housing Credits. State Housing Credit allocating agencies typically receive applications requesting two to three times as many Housing Credit resources as the agencies have to allocate, and many more developers with worthwhile development proposals do not even apply because the competition for Housing Credits is so great.

Because of insufficient resources to meet their local needs, state Housing Credit allocating agencies face difficult choices – whether to award Housing Credits for preservation or new construction, rural or urban areas, developments that revitalize neighborhoods or developments in higher opportunity areas with access to better schools. They balance whether to finance supportive housing for the homeless, assisted living for the elderly, homes for families with children or affordable apartments for veterans. New resources are the only way to begin to meet all of these needs.

Provide States with Flexibility to Maximize Housing Credit Resources

The Housing Credit and Housing Bond programs are administered by the states under broad federal guidelines set forth in the tax code which allow states substantial discretion as to how best to use these resources. State administration has made



these programs uniquely responsive to local needs. States provide sophisticated finance, underwriting and asset management capacity, as well as a multi-decade record of responsibility, effectiveness, transparency, public accountability and experience in administering tens of billions of dollars in federal housing assistance. An important component of state discretion is the ability to award Housing Credits and Housing Bonds to the developments that are of the highest priority to the communities they serve, in an amount that makes them financially feasible but which does not exceed the amount required for feasibility. The following program modifications would provide states with new flexibility to better respond to their needs and make the program even more effective than it currently is.

- **Enact Permanent Minimum Housing Credit Rates**

Although the overall Housing Credit program is a permanent part of the tax code, Housing Credit rates, which are an important component in the formula that determines how much Housing Credit equity is available for any given property, have been subject to annual “extenders” legislation since 2013. When the Housing Credit was created, Congress set the credit rates at 9 percent for new construction and substantial rehabilitation and 4 percent for the acquisition of affordable housing and for federally subsidized properties, which is how the “9 percent” and “4 percent” credits got their names. However, in practice Housing Credit rates fluctuate according to a formula related to federal borrowing rates, which now yields much lower credit rates (approximately 7.5 and 3.2 percent, respectively) as a result of historically low interest rates. As a result, in today’s interest rate environment there is 15 to 20 percent less Housing Credit equity available for any given affordable housing development than the original rates provided.

Recognizing the impact of declining rates on the program, Congress temporarily enacted a minimum 9 percent credit rate in 2008, which is now expired as of the end of 2014 despite strong bipartisan support for its extension. Congressional action is needed in order to create permanent minimum credit rates that allow states to allocate credits more effectively and enable more worthy developments to be financially feasible.

To fill the financing gap that results from use of the floating rate, states have limited options. They can attempt to fill some of the gap with other financing sources, such as the HOME Investment Partnerships Program or Community Development Block Grants. Alternatively, they can underwrite the property assuming owners will charge rents at levels that allow for higher levels of debt service, meaning the apartments must be targeted to the higher end of the eligible income spectrum and are less affordable to the lowest income households. Because gap financing sources are becoming increasingly scarce as a result of federal budget cuts, developers are finding it increasingly difficult to reach very- and extremely-low income families while making projects financially feasible. This unfortunate outcome conflicts with the congressionally mandated preference for properties which serve the lowest income residents for the longest period.

The ACTION Campaign urges Congress to create a permanent minimum 9 percent credit rate for new construction and substantial rehabilitation, as well as a minimum 4 percent rate for acquisition and for credits used in Housing Bond-financed developments. This virtually cost-neutral program modification would allow states to provide more Housing Credit equity to properties, allowing developers to target more units to very- and extremely-low income households at rents they could afford.



- Promote Broader Income-Mixing within Developments

Under current law, most Housing Credit properties serve renters with incomes up to 60 percent of AMI and rents are comparably restricted. However, this requirement has made it hard to support developments serving a mix of low income levels. The challenges are especially acute in: (1) sparsely populated rural areas where the effective market range is too narrow under current law; (2) economically depressed communities pursuing mixed-income revitalization strategies; and (3) high-cost markets, where it is extremely difficult to target apartments to the lowest-income tenants without significant additional subsidy.

The ACTION Campaign recommends allowing the 60 percent of AMI ceiling to apply to the average of all apartments within a property rather than to every individual Housing Credit apartment. The maximum income for any Housing Credit apartment would be limited to 80 percent of AMI, consistent with long-standing federal affordable housing policies. For example, a unit restricted to households earning 40 percent of AMI could be paired with another for a household earning 80 percent of AMI. Income averaging would preserve rigorous targeting while providing more flexibility and responsiveness to local needs. Depending on market conditions, the higher rents that households with incomes above 60 percent of AMI could afford also have the potential to offset the lower rents that households below 40 or 30 percent of AMI could afford, allowing developments to maintain financial feasibility while providing a deeper level of affordability.

We look forward to working with the Community Development and Infrastructure Working Group and the full Senate Finance Committee to promote an even stronger Housing Credit through tax reform. If you have any questions, please contact:

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