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Affordable Rental Housing and Public Policy

TOWARD GREATER HOUSING SECURITY AND STABILITY

MBA Affordable Rental Housing Task Force
December 2015

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Executive Summary

"I see one-third of a nation ill-housed, ill-clad, ill-nourished... The test of our progress is not whether we add more to the abundance of those who have much; it is whether we provide enough for those who have too little..."

—President Franklin Delano Roosevelt, Second Inaugural Address, January 20, 1937

"These policies are thoroughly consistent with American ideals and traditions. They recognize and preserve local responsibility, and the primary role of private enterprise, in meeting the Nation's housing needs. But they also recognize clearly the necessity for appropriate Federal aid to supplement the resources of communities and private enterprise."

—President Harry Truman on the Signing of the Housing Act of 1949, July 15, 1949

The number of American households who rent their homes stands at an all-time high. Most individuals have rented their home at various stages of life, and many seniors do or plan to rent during their retirement years. Our Nation's rental housing policies will continue to grow in importance due to the increase in rental demand, the need to safely and affordably house an aging population, and the fundamental desire to provide greater economic opportunity to a broader cross-section of American households.

Multifamily rental housing, by its very nature, tends to be affordable to low- and moderate-income families. Most multifamily rental properties, including market rate housing, are affordable to households of modest incomes. Rental housing that benefits from public subsidies — a component of the broader multifamily housing market — meets the needs of millions of low- to moderate-income families. Until recently, however, the pace of new construction since the financial crisis has lagged relative to demand and incomes have largely remained stagnant, especially among low- and moderate-income households. And much of our rental housing stock, particularly units that are affordable to households with modest incomes, is aging.

Significant numbers of American households are cost burdened — and for renters, the numbers are at a historic high, with 21.3 million renter households — almost half of all renter households — paying more than 30 percent of their incomes in rent.[1] More than a quarter of renter households spend more than half of their income on rent. Given the growing body of research supporting the importance of affordable and quality housing as a conveyor belt for better educational, health and economic outcomes, our public policies must keep pace with demographic and societal shifts — leading to holistic housing policy that addresses the critical importance of rental housing and a housing system that supports greater affordability and quality.

It is vital that policymakers and stakeholders understand the nature and scope of the affordable rental housing market and explore ways to effectively address the supply-demand gap. The **Mortgage Bankers Association,** as the leading association of the real estate finance industry, convened a Task Force to review the range of issues that surround the growing concern around the availability of affordable rental housing. The members of the **MBA Task Force** bring perspectives and expertise as practitioners in multifamily lending, working with a range of capital sources to finance diverse rental property types in virtually all geographic markets.

The Task Force sought to: (1) highlight the extent and impact of the current shortage of affordable rental housing, drawing on data and research; (2) be a catalyst for a holistic public discussion on affordable rental housing; (3) recognize the

1 Joint Center for Housing Studies of Harvard University, *America's Rental Housing — Expanding Options for Diverse and Growing Demand* (2015).

nature of the challenges and complexities associated with finding solutions to address affordable housing concerns; and (4) recommend principles that should shape how we think about affordable rental housing and improvements to existing programs that have supported the availability of affordable rental housing.

Toward these ends, the Task Force examined the importance of rental housing, the history and efficacy of existing federal programs designed to support it, and developed a framework for both general and specific policy recommendations. In summary, those *recommendations* are as follows:

- **Affordable rental housing must be an essential policy goal,** recognized as vital to our nation's well-being and future.
- **Housing policy should support new construction, preservation of existing housing stock, and demand-side assistance** — all of which play a vital role in ensuring access to quality, affordable housing.
- **Private capital should be used and attracted wherever and whenever possible** to increase the supply of housing, while recognizing that subsidies are necessary in more "targeted" affordable rental housing.
- **A broad and long-term approach is necessary** to address multifamily rental housing needs.
- **Existing proven programs should be enhanced where they have been effective,** rather than having a preference for inventing new ones. In this regard, enhancements to programs must take a holistic approach that addresses:
  + **Development of new and the rehabilitation of existing affordable rental housing,** primarily through attracting equity investments to rental housing development, including through the low-income housing tax credit program,
  + **Debt financing** available for affordable rental housing where GSE, FHA and other capital sources can play greater roles, and
  + **Demand** for rental housing on the part of households of modest means, but especially for low- and very low-income families who rely or would substantially benefit from housing choice and project-based voucher programs.

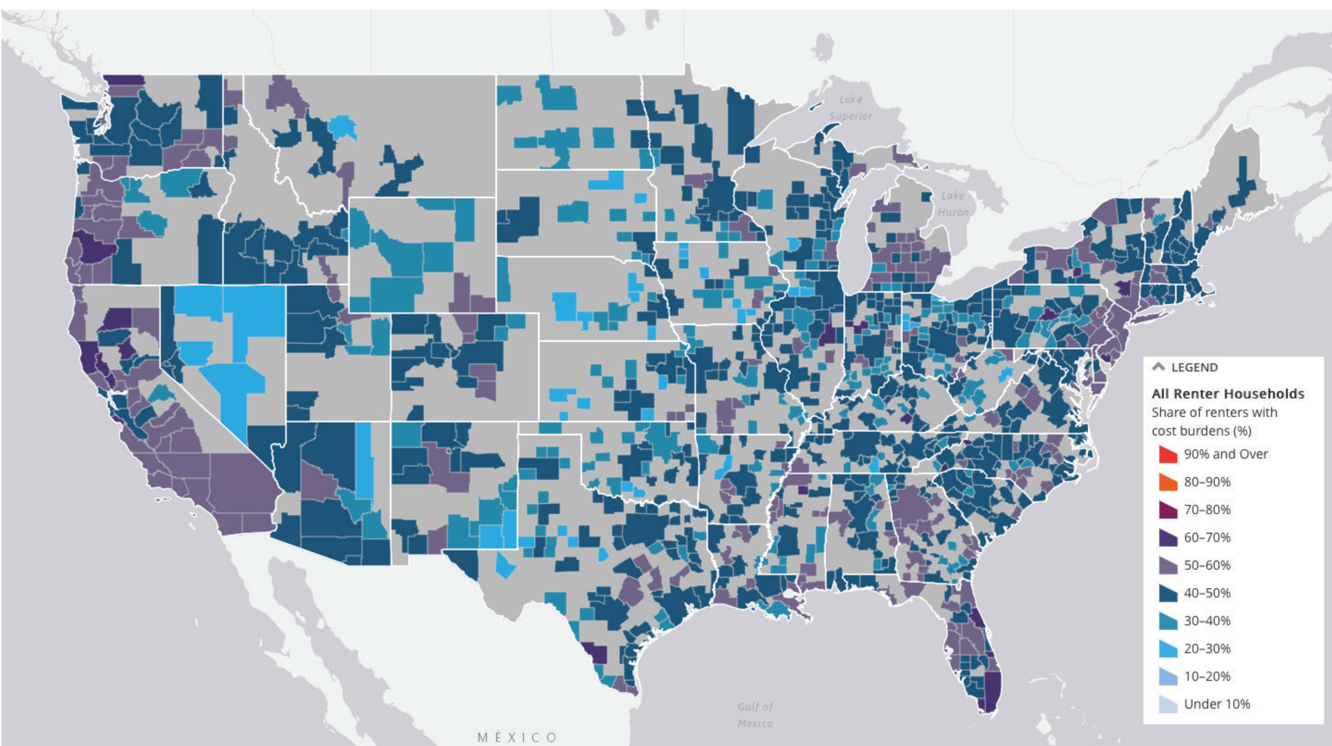
The paper is organized as follows:

- First, we discuss the current rental affordability landscape.
- Second, we describe the importance of affordable rental housing — the sense of housing security and stability that it provides to households and the impact that safe, decent and affordable housing can offer.
- Third, we survey the gap that exists between the supply and demand of affordable rental housing.
- Fourth, we discuss the challenges and complexities of addressing the affordable rental housing crisis — that do not lend themselves to simple solutions — and emphasize that policymakers must recognize the realities of these obstacles and maintain a multi-pronged approach to addressing them.
- Lastly, we provide recommendations — both principles for policy change and enhancements to programs — to generate a holistic policy dialogue, enhance affordability for renting households, and promote long-term housing security.

Where We Are Today

As the home ownership rate has dropped and more households have become renters since the financial crisis, the need for affordable rental housing has grown dramatically. Incomes fell significantly during the recession, and with limited growth in the supply of rental housing stock, rents have increased at several times the rate of inflation. Today, about half of the 43 million American households who rent their homes spend at least 30 percent of their income on housing. And almost a quarter of all renters — more than 11 million renter households — spend at least 50 percent of their income on housing, the highest total recorded. These are levels which we believe have not been seen since the Great Depression when the core of our nation's housing policies was originally developed.

SHARE OF RENTER HOUSEHOLDS SPENDING MORE THAN 30 PERCENT OF THEIR INCOMES FOR RENT



Source: Joint Center for Housing Studies of Harvard University, Tabulations of U.S. Census Bureau 2014 American Community Survey Data.

As real household incomes and net worth for many households declined to the levels of *20 years ago,* the cost of constructing rental properties and real rents have increased. The combination of stagnant incomes and rising rents has resulted in an almost 40 percent increase in the number of renter households that spend more than 30, 40 or even 50 percent of their incomes on housing. Not surprisingly, this impact is falling on those low-income and working households earning less than median income who can least afford it and are forced to make difficult trade-offs with other necessities. The average rent for rental units constructed since 2010 is more than $12,000 per year which accounts for over 35 percent of income for a renter earning the *median* renter income of $34,000 (compared to the median income of a homeowner of approximately $67,000).

Existing housing programs and capital sources, as discussed below, have been vital in serving the housing needs of many renters, but they often have not had the resources to fill the gap for those renters with median or lower incomes. Much of the stock that is affordable to most rental households today was constructed in the 1970s or earlier; with a median age of 38 years, the rental housing stock is likely older on average than it has ever been. While apartment starts have increased significantly in the last couple of years, much of this supply is not currently affordable to very low-income families.

The development and construction of new rental units, market rate and otherwise, will over time increase the supply of housing units affordable to those groups. This process, however, is gradual, especially in higher cost urban markets where, given increasing land and construction costs, rents on newly constructed dwellings may not be affordable to low- or moderate-income renters. Filling this gap for working or very low-income families will be ever more challenging unless our policies promote development and preservation of stock affordable to these groups.

Given that most renters earn less than the national median income, the concern over affordable and available rental housing will persist for years to come. On the supply side, although 300,000 to 400,000 new multifamily rental units per year are being constructed at this time (among the highest levels since the 1970s), a subset of these units will be affordable to lower-income households. And an estimated 100,000 units per year are lost to obsolescence.

Units delivered each year under the Low-Income Housing Tax Credit program offset a significant portion of units that go offline, but a potential gap of hundreds of thousands of affordable units per year remains — a gap that must be filled by additional multifamily or single family rental supply. And MBA research on the increase in renter households over the coming decade ranges from a low of 3.1 million to a high of 5.6 million new renter households.[2] Recent research also suggests that a significant percentage of these new renter households will be rent burdened and in many cases severely at current and projected rent levels based upon a modest level of income growth.[3] The need for supporting the development and maintenance of the affordable housing stock with both supply and demand side policies has rarely been greater.

POLICY AND POLITICAL CONTEXT

Affordable housing concerns have gained increasing attention in public policy discussions, particularly surrounding housing finance reform and the future of Fannie Mae and Freddie Mac, as well as the role of the Federal Housing Administration. While there is increasing acknowledgement among policymakers of the importance of rental housing and the need for continuous liquidity in all market cycles, we anticipate that the debate with regard to the role of the federal government in housing finance will continue without definitive resolution in the near term.

At the same time, housing advocates have proposed initiatives that would lead to greater development and credit support for affordable housing. A number of current regulatory initiatives, including those proposed by regulators at the Federal Housing Finance Agency and the Federal Housing Administration, are aimed at increasing the capital availability in the targeted affordable housing sector. Such initiatives have been and will continue to be debated and met with a range of reactions from both sides of the aisle.

What is often lost in the public policy discussion is that there has been a persistent subsidy bias towards home ownership rather than home rental. The typical renter household earns about 70 to 80 percent of median household income, which is in turn below that of the median owner household. If an objective of federal housing policy is to direct resources toward housing affordability and stability for households of modest means, then a more holistic evaluation of these policies and their purposes may be in order.

2 Fisher and Woodwell, MBA Research Report, *Housing Demand: Demographics and the Numbers Behind the Coming Multi-Million Increase in Households* (July 2015).

3 Enterprise Community Partners and Joint Center for Housing Studies, *Projecting Trends in Severely Cost-Burdened Renters: 2015–2025* (September 2015).

Why Housing Matters: The Importance of Affordable Rental Housing

The scarcity of affordable housing has negative ripple effects. There is a large and growing body of research indicating that housing cost burden and instability have significant health, educational and economic consequences to households and the communities in which they live. Housing instability can lead to poor health and nutrition, lower educational attainment, and stagnant economic mobility. These public concerns are complex and associated with multifaceted causal factors, but the correlation of these negative outcomes to the lack of safe, decent and affordable housing is clearly evident. Conversely, stable, secure and affordable housing has been shown to be a platform or conveyor belt for positive societal and economic outcomes for both renters and the communities in which they live.

HOUSING SECURITY

Affordable, stable housing contributes to a sense of housing security that benefits households and their communities. As observed by Enterprise Community Partners, "Nearly 19 million U.S. households pay over half their income on housing, and hundreds of thousands more have no home at all. Access to decent, affordable housing would provide critical stability for these families, and lower the risk that vulnerable families become homeless."[4]

Whether and to what extent housing is affordable has far reaching impacts, both direct and indirect, on households and communities. Where there is scarcity of affordable housing, families experience cost pressures on necessary expenses, such as food and education. Housing affordability has multifaceted impacts on renter households and the communities in which they live — from household stability to economic security to education, health, neighborhood and energy efficiency benefits.[5]

As a case study, Princeton Sociologist Douglas Massey studied the impact that stable, affordable rental housing had on low-income tenants of the 140-unit multifamily complex in Laurel, NJ, an affluent suburb outside of Philadelphia. Compared to prospective tenants who were on the property's waiting list, the study found that residents of the development experienced significantly lower exposure to neighborhood disorder and violence, far fewer negative life events, improved mental health, higher rates of employment, wages, family incomes, and lower levels of public dependency.[6]

Broader studies published by sources as diverse as the Journal of Cognitive Neuroscience and the Journal of Housing Economics show that children of families receiving income assistance in various forms, including housing vouchers, score higher on cognitive tests, perform better

4 Enterprise Community Partners, Inc., *Impact of Affordable Housing on Families and Communities: A Review of the Evidence Base* (2014), p. 2.

5 Id.

6 Douglas S. Massey, et al., *Climbing Mount Laurel: The Struggle for Affordable Housing and Social Mobility in an American Suburb* (2013). Children were also more likely to report having a quiet place to study and spent an average 6 more hours per week on homework in comparison to those children on the waiting list.

in school and likely earn more as adults as compared to children in rent-burdened housing.[7]

The MacArthur Foundation has observed that "Affordable housing may be an essential 'platform' that promotes a wide array of positive human outcomes in education, employment, and physical and mental health, among other areas."[8] Households who have to spend a higher percentage of their budget towards rent have less resources to spend on other necessary and discretionary expenses such as food, medication, health insurance, and savings for retirement or children's education. Lack of affordable housing also has long lasting indirect costs to society. Housing that is affordable may reduce the frequency of disruptive moves that can have detrimental impacts on school-age children.[9]

Similarly, the impact of frequent moves — often correlated with the lack of affordable housing — can have a negative impact on household stability and, in particular, children's social and educational development.[10] Studies have assessed the outcome of participants in HUD's Moving to Opportunity program who were provided rental subsidy and housing counseling to locate in more affluent communities compared to other similar low-income households who either received or did not receive rental assistance and were not geographically restricted. These participants and their children had statistically significant better health than the non-participants.[11]

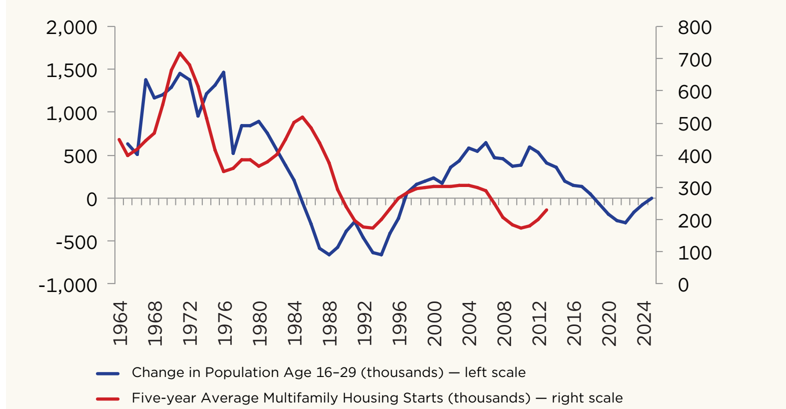
In sum, there is clear evidence that housing affordability, along with education, is a highly effective mechanism for improving economic outcomes for lower-income families and their children.

HOUSEHOLD FORMATION AND RENTER DEMOGRAPHIC TRENDS

The renting population is expected to continue to grow over the next decade. As noted above, MBA estimates an increase in renter households over the coming decade ranging from a low of 3.1 million to a high of 5.6 million new households.[12]

The aging of America's population and ethnic diversity in household growth will be primary drivers for change in rental demand. The aging of the baby boom generation will lift the number of renters over age 65 by 2.2 million in the next ten years. Minorities will contribute to the net increase in renters over the decade as well. Assuming today's renting rates, minority groups will add between 1.8 million to 2.2 million renter households.[13] The demand for affordable rental housing is clearly expected to remain strong, and a significant portion of the growing renter population is anticipated to have low and moderate incomes, underscoring the affordability concern. Based on demographic forecasts, it is estimated that the country will see an increase of over 5 million Hispanic and over 2 million African American households in the next decade. While many of these households will be homeowners, many will also be renters.[14] Adding to this demographic trend is a continued movement towards urbanization, which almost by definition means higher housing development costs due to land values and construction costs.

CHANGE IN POPULATION AGE 16–29 AND MULTIFAMILY HOUSING STARTS (THOUSANDS)



Source: MBA and Census

7 See, e.g., Jack P. Shonkoff, et al., *The Lifelong Effects of Early Childhood Adversity and Toxic Stress,* Pediatrics, volume 129, number 1, pp. e232 -e246, 2012; Mark M. Kishiyama et al., *Socioeconomic Disparities Affect Prefrontal Function in Children,* Journal of Cognitive Neuroscience, 21(6), pp. 1106–15, 2009; Greg J. Duncan and Katherine Magnuson, *The Long Reach of Early Childhood Poverty,* Pathways, Winter 2011; Joint Center for Housing Studies, *America's Rental Housing: Evolving Markets and Needs,* December 2013, p. 32; Sandra Newman and Scott Holupka, *Housing Affordability and Child Well-Being,* Center on Housing, Neighborhoods, and Communities working paper, August 2013; Sandra J. Newman and C. Scott Holupka, *Housing Affordability and Investments in Children,* Journal of Housing Economics, December 2013; Elizabeth March et al., *Behind Closed Doors: The Hidden Health Impacts of Being Behind on Rent,* Children's HealthWatch, January 2011.

8 MacArthur Foundation, *How Housing Matters to Families and Communities Research Initiative* (ongoing).

9 Center for Housing Policy, Insights, *The Impacts of Affordable Housing on Education: A Research* (Nov. 2014) Summary, p. 22.

10 Jeffrey R. Kling, at al., *Experimental Analysis of Neighborhood Effects* (June 2006); and Tama Leventhal, PhD and Jeanne Brooks-Gunn, PhD, *Moving to Opportunity: An Experimental Study of Neighborhood Effects on Mental Health* (2003).

11 See also MacArthur Foundation, *Linking Affordable Housing to Greater Spending on Child Enrichment and Stronger Cognitive Development.*

12 Fisher and Woodwell, MBA Research Report, *Housing Demand: Demographics and the Numbers Behind the Coming Multi-Million Increase in Households* (July 2015).

13 Joint Center for Housing Studies, *The State of Nation's Housing* (2014).

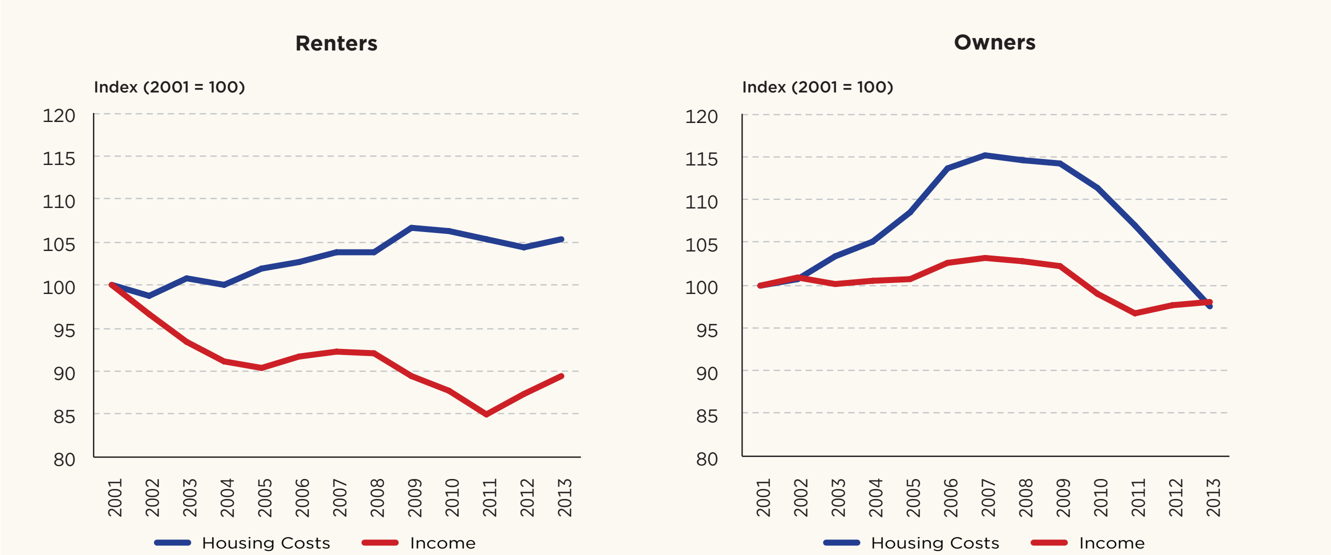
14 Id.

Gap Between Affordable Rental Housing Supply and Demand

As previously noted, about half of all U.S. renters are cost burdened and about a quarter of renter households are severely cost burdened, paying more than half of their income on rent.[15] As the Joint Center for Housing Studies observed, "the number of cost-burdened renters… set a new high in 2014 of 21.3 million. The number of households paying more than half of their income in housing jumped to 11.4 million."[16] Minorities and single-parent households have been particularly hit hard in this regard.[17]

Affordable rental housing can be viewed as both a supply-demand issue and the outcome of a mismatch between incomes and the cost to build and maintain such housing. Gaps will differ across property types and market segments, as well as across household profiles. While new construction activity for multifamily housing has been improving over the past several years, the demand is expected to remain strong, particularly in light of demographic changes and pressures on income growth.

INCOME LEVELS, WHILE RECENTLY IMPROVING, WERE TREMENDOUSLY IMPACTED BY THE GREAT RECESSION



Notes: Median costs and incomes are real values adjusted using the CPI-U for All Items. Owner housing costs are first and second mortgage payments, property taxes, insurance, homeowner association fees, and utilities. Renter housing costs are cash rent and utilities.

Source: JCHS tabulations of US Census Bureau, American Community Surveys.

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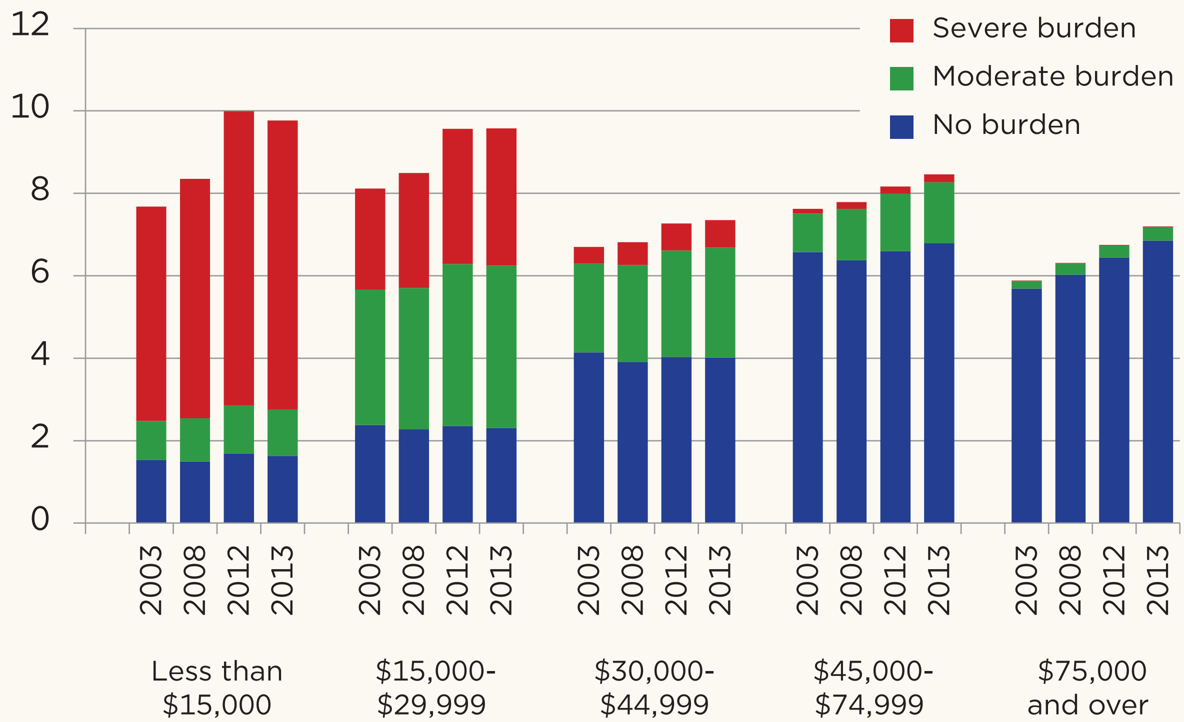
15 Joint Center for Housing Studies, *The State of Nation's Housing* (2015), p. 30.

16 Joint Center for Housing Studies, *America's Rental Housing: Expanding Options for Diverse and Growing Demand* (2015).

17 Joint Center for Housing Studies, *The State of Nation's Housing* (2015), p. 30.

NUMBER OF RENTER HOUSEHOLDS, BY INCOME AND LEVEL OF HOUSING COST BURDEN (MILLIONS)



Source: MBA and Harvard's Joint Center for Housing Studies.

The needs of very low-income multifamily renters are particularly acute. One study found that between 2007 and 2011, the number of very low-income multifamily renters increased from 7.6 million to 8.7 million (a 14 percent increase). The number of very low-income multifamily renters spending more than 50% of their income on housing increased from 2.5 million to 3.4 million (a 36 percent increase). The study also found that the number of adequate and available multifamily rental units affordable to very low-income households increased from 4.5 million to 4.6 million (a 4 percent increase).

Because of the faster growth in demand than supply, the supply gap increased from 3.2 million units to 4.0 million units (a 28 percent increase) over the period.[18]

The targeted affordable rental housing stock — housing that has historically benefited from government subsidies — is at increasing risk due to expiring restrictions. Privately-owned rental housing units that are government-subsidized were built specifically to provide affordable rental housing. Under government subsidy programs such as the Low-Income Housing Tax Credit program, "owners agree to maintain affordable rents for a set period, usually 15 to 30 years, in exchange for federal subsidies. When those agreements expire, owners can either re-enroll in the affordability programs or convert their properties to market-rate units."[19] The Joint Center for Housing Studies observed that "nearly 2.2 million assisted units are at risk of removal over the coming decade."[20] Public housing, for example, serves extremely low-income households but this inventory faces a mounting capital needs backlog that jeopardizes its long-term sustainability. Without the preservation of many of these units (much of which require substantial rehabilitation and capital improvements), the availability of the current affordable housing stock will contract further — potentially at a precipitous pace.

18 Freddie Mac, *Multifamily Affordability: Market Conditions and Policy Perspectives* (2013).

19 HUD, *Preserving Affordable Rental Housing: A Snapshot of Growing Need, Current Threats, and Innovative Solutions* (Summer 2013).

20 Joint Center for Housing Studies, *The State of Nation's Housing* (2015), pp. 33-34.

Complexities and Challenges in Expanding the Availability of Affordable Rental Housing

Although the extent and depth of the cost burden on renter households are evident, formulating public policy to increase the supply of affordable rental housing presents significant challenges and complexities. These realities must be acknowledged in efforts toward expanding the availability of affordable rental housing.

Affordability Mismatch. Affordability concerns with regard to rental housing fundamentally result from a gap between the cost of renting and the incomes of households seeking available units. The well-documented limits in income growth among moderate to low-income households has exacerbated the degree to which households are rent burdened. Housing finance policy does not impact household income levels. While a long-standing idea dating back to the 1930s, direct income subsidies in the form of rental vouchers have since the 1970s been the principal mechanism for addressing 'lack of income.'

Capital Source Characteristics. The federal government largely exited the business of building housing in the 1970s and relied instead on private capital to create supply. Private capital, by its nature, looks for a return on investment and flows to where that return may be higher. Private capital does not naturally flow into the targeted affordable segment of the housing market, given the lower returns anticipated. Some form of subsidy — federal, state, local, public-private partnership-based, or through the tax code — has been and will continue to be necessary to ensure an adequate supply of housing for low- and very low-income households. This reality must be acknowledged to the extent that affordable, safe rental housing is viewed as a policy priority. At the same time, the budget-constrained environment in which the federal government and most state and local governments operate limits the critically important resources that are necessary to support the broad availability of affordable rental housing.

Trade-off between Affordability and Quality. The cost drivers of developing affordable rental housing align in many ways with other multifamily projects, but also present unique challenges. Land price and construction costs are largely dictated by local market conditions and regulatory requirements. Because affordable rental housing needs often emerge in more densely populated areas, land prices and development costs may be higher. A 2014 study by Enterprise and ULI's Terwilliger Center for Housing describes, among other things, the added costs associated with affordable housing developments because of multiple funding streams, varying requirements and compliance costs, and the costs of providing a variety of amenities for the residents served.[21]

Rental housing that is affordable also may not necessarily mean it is safe and habitable. Properties that are very affordable could lack quality and present hazards to residents. As the Joint Center for Housing Studies observed, "Paying large shares of income for housing does not guarantee the units will be adequate or safe. Housing deficiencies related to plumbing, electrical, and heating systems or to structural integrity affect a much larger share of renters (9 percent) than owners (3 percent)."[22] Safety and quality should not be shortchanged for affordability, but these are trade-offs that some households are forced to make and represent an ongoing challenge to policy makers as development and operating costs continue to rise faster than incomes.

21 ULI, Terwilliger Center for Housing, Enterprise, *Bending the Cost Curve* (2014), pp. 8-9.

22 Joint Center for Housing Studies, *The State of Nation's Housing* (2015).

State and Local Regulatory Considerations. State and local rules and regulations can have a significant impact on the development of affordable rental housing. Permit fees, land use regulations and building codes are examples of locally-imposed frameworks that can significantly impact the cost and availability of rental housing. ULI and Enterprise observed, "As a result of these higher baseline costs, the ability of market-rate housing to reach lower income levels is limited and affordable housing subsidies result in fewer units."[23] While beyond the scope of this paper, we see significant opportunity for reform in the state and local regulatory sphere.

Multi-faceted Capital Needs. The development of affordable rental housing typically involves multiple sources of capital — a combination of equity, debt, grants and other subsidies. Policies that encourage or mandate debt financing alone cannot, by themselves, increase the production of affordable housing, and in fact, can lead to market distortions that are harmful in the long run. Where mortgage debt is provided by taxpayer-backed sources, credit quality and prudent risk management are particularly important considerations. While public policy objectives could lead to more flexible credit and underwriting standards, they must be balanced with the need for diversification of risk and safeguarding of taxpayer interests.

Single-Family Rental Housing. While not the focus of this paper, we believe that single-family rental housing can play a greater role in providing affordable housing to American households. The single-family rental stock is large and diverse and in fact represents fully half of all rental stock. This is a rapidly evolving market with maturing business and financing plans. The tools and regulatory framework for this sector could be enhanced further to expand housing options for these renting households. A range of capital sources could have a role to play in providing liquidity to this market.

23 ULI, Terwilliger Center for Housing, Enterprise, *Bending the Cost Curve* (2014), pp. 18-19.

Recommendations

RECOMMENDED PRINCIPLES

The breadth of challenges confronting the state of affordable rental housing does not lend itself to simple, clear cut solutions. We believe that a broad array of approaches is necessary to address the concern. The following principles, in our view, should guide policy efforts to support the availability and affordability of rental housing.

Affordable rental housing is an essential policy goal that is vital to our nation's well-being and future

There may be a tendency to view affordable housing — and affordable rental housing in particular — as a niche concern with a limited constituency. This is belied by the simple fact that a third of all American households rent their homes, and 18 million families live in multifamily rental housing. Most individuals have rented their home at various stages of life, and many seniors do or plan to rent during their retirement years. And as MBA's recent study on household formation shows, the dynamism and dependencies between owning and renting one's home are inextricably intertwined. Over the coming decade, affordable housing policy will grow in importance due to the increase in rental demand, the need to safely and affordably house an aging population, and the fundamental desire to provide via reduced cost-burdens greater economic opportunity to a broader cross-section of American households.

New construction, preservation of existing stock and demand-side assistance all play a vital role in ensuring access to quality, affordable housing

The availability of affordable rental housing, at its core, is driven by supply and demand in geographic markets. As a general matter, both construction and rehabilitation/preservation of affordable housing should be encouraged. Increasing the supply of new or rehabilitated housing stock is the best long term economic mechanism for promoting affordability. Indeed, much of the affordable rental housing today was the newly-constructed rental housing in the 1970s and 80s. Regulatory capital rules on construction lending at depository institutions, for example, should refrain from imposing rigid requirements that stifle the development of multifamily rental housing and other commercial real estate that supports the sustainability of communities. Federal finance programs should be oriented towards financing both construction and rehabilitation of multifamily housing. Preservation of aging affordable housing stock and those with expiring regulatory subsidies and restrictions should be a focus for policymakers, as "nearly 2.2 million assisted units are at risk of removal over the coming decade."[24] Without continued policy emphasis on both new construction and rehabilitation, the problem could get worse not better.

Use and attract private capital wherever and whenever possible to increase the supply of housing, but recognize that subsidies are necessary in more targeted affordable rental housing

The role of subsidies, whether formal or implicit, tax-driven or not, or at the level of the capital provider, investor or tenant, is simply necessary for housing that is targeted toward low- and very low-income families. As the Joint Center for Housing Studies states, "Since the private sector cannot profitably supply very low-cost units, the government must play a critical role in ensuring that the nation's most disadvantaged families and individuals have good-quality, affordable housing."[25] While being mindful of the budgetary impact of various programs, policymakers must be willing to invest in the availability and affordability of rental housing to both support the current and foreseeable need and to affect positive outcomes for low- to moderate-income households. Ongoing studies measuring the benefits of housing affordability will be key to better calibrating housing policy over time. Sources and the relative economic efficiency of equity, debt, and other components of the capital stack should be considered to ensure a holistic view of the liquidity needs of affordable rental housing.

A broad and long-term approach is necessary to address multifamily rental housing needs

Multifamily rental housing is, by its very nature, affordable to low- and moderate-income families. Most multifamily rental properties, including non-subsidized market rate housing, are nonetheless affordable to households of modest incomes. Apartments with affordable regulatory restrictions (e.g., inclusionary zoning requirements) are a subset of the broader multifamily housing market that meets the needs of millions of low- to moderate-income families. And as the industry has witnessed from the existing affordable rental housing stock — much of which was built 30 or more years ago — properties that may not necessarily be viewed as affordable today will likely be

24 Joint Center for Housing Studies, *The State of Nation's Housing* (2015), p. 33.

25 Joint Center for Housing Studies, *The State of Nation's Housing* (2015), p. 32.

the naturally occurring affordable rental housing in the future. Policymakers should continue to ensure liquidity in all market cycles to the broad multifamily finance market, while examining ways to expand the targeted affordable market. And finally, it is important to acknowledge that income subsidies in the form of vouchers are necessary to provide the means needed for the lowest-income families to live in higher quality housing and in mixed-income neighborhoods where it is increasingly evident that the children of these families are more likely to find a path out of poverty.

MEDIAN MONTHLY GROSS RENT AND NUMBER OF RENTAL UNITS, BY YEAR STRUCTURE BUILT, 2013

	MEDIAN RENT	# UNITS
Total:	$905	42,447,172
Built 2010 or later	$1,023	701,327
Built 2000 to 2009	$1,075	5,353,377
Built 1990 to 1999	$930	5,331,233
Built 1980 to 1989	$880	6,000,590
Built 1970 to 1979	$842	7,389,484
Built 1960 to 1969	$872	4,886,292
Built 1950 to 1959	$900	4,232,520
Built 1940 to 1949	$870	2,387,125
Built 1930 to 1939	$894	6,156,224

Source: 2013 American Community Survey, 1 Year Estimates.

Enhance and expand existing proven programs rather than invent new ones

There are numerous federal, state and local programs along with those of the nonprofit and for-profit sectors that support affordable rental housing. MBA's January 2015 *Research Datanote*[26] provides a high-level survey of programs that have sought to address affordable rental housing. Programs that have proven to be effective should be leveraged, replicated where possible, and/or built upon to develop public policy reforms. In doing so, lending and underwriting standards should be reasonable in order to support a sustainable real estate finance system.

Specific recommendations regarding a number of such programs are discussed in the following pages.

PROGRAMMATIC RECOMMENDATIONS

Building upon the foregoing principles, we believe that policymakers should adopt a holistic approach that addresses the three vital facets of expanding and preserving affordable rental housing:

- ***Development and rehabilitation*** of affordable rental housing, including attracting equity investments to rental housing development, including through the low-income housing tax credit program,
- ***Debt*** financing available for affordable rental housing where GSE, FHA and other programs can play greater roles, and
- ***Demand*** for rental housing on the part of households of modest means, but especially for low- and very low-income families who rely on or would substantially benefit from housing choice and project-based voucher programs.

These recommendations are discussed below.

Support and expand the Low Income Housing Tax Credit (LIHTC)

BACKGROUND. The LIHTC program is often described as the most successful affordable rental housing production program in American history. As a public-private partnership, LIHTC is a source of equity financing for the development of affordable housing that serves households earning 60 percent or less of AMI with rents restricted to keep the units affordable. Since it was established in the mid-1980s, the program has supported more than 2.5 million affordable rental units representing almost 15 percent of total apartment stock in the nation and between 1995 and 2012, LIHTC has placed nearly 2 million units in service.[27] A 2012 HUD study found that approximately 60 percent of households nationwide in LIHTC units earned less than $20,000 annually.[28] In addition to the direct impact of providing affordable housing, the LIHTC program provides a multiplier effect in the form of construction and then ongoing consumption effects. The LIHTC program provides approximately $6 to $7 billion of tax credits to equity investors in affordable housing, which is a relatively modest cost in the overall context of federal housing subsidies.

As the Joint Center for Housing Studies writes, "the competing demand — for new construction as well as for preservation — have put the tax credit program under extreme pressure and raised the question of whether it ought to be expanded."[29] We believe that it should.

RECOMMENDATIONS. Continuation and prudent expansion of the LIHTC program are critically important to affordable rental housing. Given both its proven success and reliance on private capital placed at risk, we strongly support expansion of LIHTC and oppose efforts to cut

26 MBA Research Datanote, *Mind the Gap: A High-level Review of the Need for — and Supply of — Affordable Multifamily Rental Housing* (2015).

27 MBA Research Datanote, *Mind the Gap: A High-level Review of the Need for — and Supply of — Affordable Multifamily Rental Housing* (2015), p. 6.

28 U.S. Department of Housing and Urban Development, Office of Policy Development and Research, *Understanding Whom the LIHTC Program Serves: Tenants in LIHTC Units as of Dec. 31, 2012.*

29 Joint Center for Housing Studies, *The State of Nation's Housing* (2015), p. 34.

back its scope, funding or productivity. In particular, we recognize the following programmatic components of the LIHTC program that have contributed to its success and urge their continuation. These elements include: the 10 year credit period; the 4 percent credit and use of private activity tax exempt bonds to generate the 4 percent credit; the allocation of credits rather than allocating basis; the basis "boost" for projects located in high cost and difficult to develop areas; the national pool for unused credits; and the occupancy preferences that state allocating agencies can use to tailor to local needs.

We support enhancements and expansion of this vital program. Several of the following specific proposals have been proposed by the Obama Administration, as well as industry and advocacy groups.

- **Modify the 9 percent and 4 percent credits to truly yield a minimum 9 percent and 4 percent credit.** Under current law, these rates float according to the federal government's cost of borrowing. With today's historically low borrowing rates, the 9 percent and 4 percent yield significantly lower credits to investors. Their floating rate nature also adds uncertainty to the development process and has created financing gaps that have rendered projects financially infeasible.

  We support legislation proposed in both the House and the Senate to fix the rate at a minimum of 9 percent and 4 percent. Alternatively, the Administration has proposed to alter the rates used in determining the credits by using the average of the federal government's mid-term and long-term borrowing rate plus 2 percent. While this would yield less than the fixed 9 percent and 4 percent rate suggested above in the current interest rate environment, this proposal could provide a higher credit rate under different market conditions.

- **Convert unused private activity volume cap to an equivalent 9 percent credit.** Many states have not used their allocation of private activity tax exempt bond volume cap. And the 9 percent tax credit program is perennially over-subscribed. The Administration has proposed allowing States to convert up to 18 percent of their volume cap which could effectively increase their 9 percent credits by 50 percent or more. We support this proposal.

- **Use income averaging within properties.** Currently, developers must agree to reserve a minimum of 40 percent of the units for occupancy by tenants whose incomes are at or below 60 percent of the area median or 20 percent of the units for occupancy by tenants whose incomes are at or below 50 percent of the area median. The Administration's proposal would allow projects to average 60 percent of the area median income within the overall project so long as none of the units are occupied by households whose incomes are greater than 80 percent of area median. Given that a mix of incomes is demonstrated to provide social benefits to the residents this increased flexibility would not only facilitate development but represent a positive policy enhancement.

  The goal of this proposal is to help lower-income tenants without additional subsidies and to provide more flexibility in using the tax credit program to acquire and rehabilitate existing properties where there likely is a mix of incomes. We strongly support this proposal.

- **Remove the Qualified Census Tract population cap.** Under current law, HUD can designate up to 20 percent of a metropolitan area as meeting the definition of a Qualified Census Track based on poverty and median income. Some communities, however, have significantly more than 20 percent of their census tracks meeting this definition. Projects located in QCT's can qualify for a boost in its project basis and generate additional tax credit equity for that project.

Leverage the Capabilities of the Government-Sponsored Enterprises

BACKGROUND. Fannie Mae and Freddie Mac serve an important role in the financing of affordable rental housing. While less well known than their single-family credit guarantee businesses, these two GSEs, working with their lender partners, have been a significant source of debt capital in the multifamily housing finance market providing on average approximately a third of the overall term financing for multifamily housing. Both prior to and during their conservatorships, the GSEs are governed by statutory charters, affordable housing goals, and other mission-related mandates that direct them toward workforce and other affordable housing activities. In the multifamily market, the GSEs primarily support the acquisition and refinancing of housing that is affordable to households at or below the median income, often termed the workforce housing segment, but have long had active targeted affordable programs, which their regulator has encouraged them to expand. In almost all agency financing models, there is private sector capital at risk before or pari passu with federally-backed dollars.

RECOMMENDATIONS. The role of the GSEs in providing ongoing liquidity to the workforce rental housing market through different market cycles has been critical. The vast majority of the rental units financed by the GSEs were affordable to families at area median income or below, which make them distinct from other sources of debt capital. Whether in conservatorship or in the future state of housing finance, we believe the GSEs (or successor entities) should continue to support workforce and affordable rental housing.

In the context of broader housing finance reform, we believe that the GSEs that benefit from a government guarantee should be subject to mission-oriented guidelines that direct them to provide liquidity to the workforce rental housing market. We believe that new or successor issuing entities should have a focus on the workforce multifamily housing market that includes the targeted affordable segment of the market.

Support for the targeted affordable housing market is essential. Targeted affordable rental housing, which typically benefits from government subsidies and/or regulatory restrictions, is intended for families with low- to very low-incomes, as well as housing in underserved areas. The economics of developing this housing does not produce the returns that private capital typically seeks; a mix of public and private capital and government subsidies is often necessary to initiate and complete projects. We believe that the GSEs are in a position to enhance their activities in this market. We encourage the GSEs and FHFA as their regulator to leverage their scale and intellectual capital to innovate and support this market.

A key means to effectuate this objective is through FHFA's recently re-proposed "duty to serve underserved markets" rulemaking. Rather than impose rigid, numerical objectives, the duty to serve rules required by the Housing and Economic Recovery Act of 2008 are intended to encourage secondary market innovation to support housing for very low-, low- and moderate-income housing. Structured properly, we see strong potential with the statutorily-mandated Affordable Housing Preservation prong of this regime. We urge that this particular duty be interpreted in a flexible manner that is not constrained to specific programs. Moreover, we recommend that the GSEs be incentivized to innovate in the preservation and rehabilitation of affordable rental housing and take some additional market risk in the rehabilitation stage. Finally, given that almost half of the rental product in the nation is single-family rental, where appropriate, we recommend that the potential role of the GSEs in financing such product be reviewed, subject to the consistency of that product with the GSEs' overall housing mission.

Explore Opportunities to Increase Affordable Housing Stock through Housing Trust Fund Allocations

Congress established the Housing Trust Fund and the Capital Magnet Fund as part of the Housing and Economic Recovery Act of 2008. Each GSE is to set aside 4.2 basis points of each dollar of unpaid principal balance of new business purchases toward these funds. These allocations were suspended in November 2008, but were recently allowed by FHFA. Contributions will be made under specific conditions set by FHFA.

While not without controversy, if the Funds are provided allocations, we believe that they could be deployed to increase affordable rental housing stock. By statute and due to the fact that the Funds are to focus on extremely low (30 percent of area median income) and very low-income (50 percent of area median income) households, the majority of resources should be devoted to the production and preservation of affordable rental housing.

Should the Funds receive allocations, we strongly recommend that HUD and Treasury Department regulations build in coordination among the Housing Trust Fund, Capital Magnet Fund, and existing programs that target very low-income housing and services to their residents. As a general principle, we believe these dollars should not compete with but rather facilitate the deployment of private capital while providing the taxpayers with a fair return for risk. We look forward to offering further thoughts as the parameters of the Trust Funds are developed.

Strengthen FHA Multifamily and Residential Healthcare Finance Programs

BACKGROUND. HUD, through FHA, has been a stable, counter-cyclical and prudent source of financing for multifamily and residential healthcare properties. FHA has a wide range of loan guarantee programs that promote the development and financing of multifamily rental properties and healthcare facilities, such as nursing homes, assisted living and hospitals. FHA insured loans provide long term (35-40 years), self-amortizing, fixed rate construction and permanent financing for such projects. The borrower's private capital in the form of equity in cash or value is the first loss position junior to the federally-insured financing.

FHA insured loans can be securitized through the Government National Mortgage Association (GNMA) and sold in the secondary market to institutional investors. With the government guarantee, investors are assured of the timely payment of principal and interest. Investors are further assured that should the loan go into default and be assigned back to HUD, the insurance claim will pay 100% of the outstanding balance. HUD/FHA works with lenders who propose projects that meet the various loan programs' criteria to process the loans and monitor the asset following loan closings. Borrowers pay a mortgage insurance premium with their monthly mortgage payments. There are over 14,000 multifamily and healthcare projects financed with FHA-insured loans.

HUD-insured loans for multifamily facilities have performed exceedingly well with a delinquency rate of 0.15 percent as of August 2015. Even during the Great Recession and the sluggish economy following it, claims on the insurance fund have been less than one percent. In fact, the multifamily and healthcare insured loan programs have consistently generated net revenue to the U.S. Treasury and serve as an accordion for mortgage capital. The program expands when capital markets are constrained and decreases when capital markets are more robust. Recently HUD has begun a process of consolidating its multifamily program offices (known as its Transformation Initiative) to better align its staffing with budgetary resources and an aging workforce.

RECOMMENDATIONS. ***Continue support for federally-insured mortgages.*** Policy discussions and draft legislation regarding the future of housing finance have proposed curtailing the federal guarantee and other programmatic changes that would reduce the effectiveness and viability of the insured loan program. Given its performance, even in the most dire of economic circumstances, this program has proven it is well run and provides market liquidity when other sources are unavailable.

Support HUD's Business Process Transformation Initiative. In order for this initiative to be successful over the long term, HUD must work with its industry partners and stakeholders to refine its implementation and consider further streamlining program policies and procedures that inhibit the program's effectiveness, especially when used in combination with other affordable housing programs. Lenders with proven capabilities should be offered the ability to assume more responsibilities where appropriate such as approving construction change orders, releasing reserve escrows, and approving changes in ownership interests — activities that most lenders are able to perform already. Furthermore, HUD will need sufficient budgetary resources to train staff, invest in technology, and to maintain robust oversight.

Preservation of Affordable Housing Stock. Equally important to developing new affordable housing units is preserving the current stock of affordable housing, including public housing that can be maintained. Public housing has documented needs acknowledged by HUD and Congress of $25 billion in deferred maintenance and required capital improvements which averages $25,000 in rehabilitation needs per unit. HUD's Rental Assistance Demonstration (RAD) program helps to recapitalize public housing properties and streamlines the provision of rental assistance needed for residents. Many RAD transactions include FHA-insured financing and HUD has recently incorporated some streamlined procedures that will help support more production. Through the RAD transactions, improvements to units have averaged $25,000 per unit. Congress has authorized HUD to continue with the program up to 185,000 units, and the program has seen success already.

While the number of improved units is sizeable, scalability in the program is necessary. With appropriate safeguards, we recommend that the cap on the number of units be lifted from the RAD program.

Reduce Regulatory Barriers. We believe that certain regulatory barriers should be reduced to enhance HUD's role in financing affordable properties. For example, revised project condition reserve requirements (e.g., "PCNA") that are being considered are excessive. While prudent risk management is a key priority, requirements that govern FHA's multifamily insurance program should be reasonable and refrain from imposing onerous requirements that could make FHA (and the U.S. taxpayer) a guarantor of last resort. This, in turn, would damage, rather than strengthen, the credit profile of the FHA multifamily and healthcare insurance programs, while inhibiting the financing of affordable rental housing.

Fund and Support Housing Choice and Project-Based Programs

BACKGROUND. The previously described programs all rely on private sector capital as equity level risk or as a layer of insurance to protect the taxpayer. The housing choice and project-based voucher programs are direct *demand side* subsidies that have been in place since the 1970s as an alternative to direct federal construction of public housing. Programs under section 8 directly subsidize the low-income renter and is the major federal program for assisting very low-income families, the elderly, and the disabled to provide affordable safe and decent private housing. The Housing Choice program provided housing to more than 5.3 million people in 2.1 million units in 2013, 91 percent of them earning less than 50 percent of the area median income.[30] A large portion of voucher recipients are disabled, elderly and working families with children.

In addition, HUD oversees project-based programs where a subsidy is provided for assisted units of a specific property for a contractually-determined period. The rents of such units are subsidized by HUD under the Section 8 New Construction, Substantial Rehabilitation and/or Loan Management Set-Aside programs.

As rents have increased in most metropolitan markets coupled with budget sequestration, the Section 8 program is under immense budgetary pressure. In the federal FY2015 budget, Section 8 was funded at $17.5 billion for vouchers and $9.73 billion for project based rental assistance. In FY2016, project based rental assistance will be funded on a calendar year basis rather than a Federal fiscal year cycle and require $1.2 billion for the added three months. Overall, when comparing federal housing expenditures, the portion devoted to renter households relative to homeowners is significantly smaller. Estimates by the Bipartisan Policy Center show that federal tax expenditures and federal appropriations for owner-occupied housing are about twice that of renter-occupied housing.[31]

RECOMMENDATIONS. Housing choice vouchers and the project-based program are critically important federal programs that have demonstrated efficacy, and are significantly oversubscribed and underfunded. Having been halved during the 1980s and under threat ever since, they should be fully funded as Congress originally intended. As the Joint Center for Housing Studies observed, "as of 2013, the average annual income of a HUD-assisted household was about $12,900, while that of a USDA-assisted household was $12,000."[32] While acknowledging the fiscal constraints under which the federal government is currently operating, we echo the views of the Bipartisan Policy Center's Housing Commission in this regard: "We do not believe our nation's most impoverished families should be subject to a lottery system or spend years on a waiting list to obtain access to federal rental assistance."[33]

Expansion of these programs would be warranted subject to the outcome of necessary research in the areas of increasing employment among voucher holders and a continuing measurement of the differential economic and education outcomes for families using vouchers in mixed-income neighborhoods versus areas of concentrated poverty. Expansion of the voucher program should be considered in concert with policy recommendations on the Low-Income Housing Tax Credit program and the GSE and FHA financing programs in order to ensure that vouchers provide benefits and reduced risk for the federally insured or subsidized financing programs. Analysis of whether project–based or individual vouchers are more effective in terms of promoting and maintaining the supply of affordable housing should be considered as part of program design going forward. The voucher programs should also incorporate scoring of the total economic benefit to communities and society as well as provide recommendations on equitable sources of funding for such vouchers from within the existing housing ecosystem.

30 HUD Data; MBA Research Datanote, *Mind the Gap: A High-level Review of the Need for — and Supply of — Affordable Multifamily Rental Housing* (2015).

31 For the 2012 fiscal year, federal tax expenditures and appropriations associated with owner-occupied housing was estimated at $120 billion and that for renters was about $62 billion. Bipartisan Policy Center Housing Commission, *Housing America's Future: New Directions for National Policy* (February 2013), p. 107.

32 Joint Center for Housing Studies, *The State of Nation's Housing* (2015), p. 32.

33 Bipartisan Policy Center Housing Commission, *Housing America's Future: New Directions for National Policy* (February 2013).

Conclusion

Since the financial crisis, the homeownership rate dropped and the population of renters increased accordingly. Given both the perennial and newer constraints to creating new affordable rental housing supply, rents have risen dramatically faster than incomes — thereby increasing the number of cost-burdened households to the highest levels seen in twenty years. And the number of cost-burdened renter households is expected to rise in the coming decade.

The financial crisis and the aftermath have increased the gap between low-moderate households and high-income households, and in particular, has highlighted the shortage of affordable rental housing. During this time, the subsidies available that directly impact the creation or preservation of new affordable supply (such as LIHTC) or directly subsidize rent payments (such as section 8) for lower-income households have remained essentially unchanged, even though the need has increased dramatically.

Support for workforce rental housing that is so vital to moderate-income families must be strengthened by the continued availability of a liquid finance market that encourages private capital and government-backed sources to build or rehabilitate new housing that can meet the growing demand for rental housing. Given the future demographic paths of more senior, minority and urban-oriented millennial households, this is a challenge that faces us for decades to come.

There is no single, effective policy solution. Meeting the nation's shortage of affordable rental housing, however, must be elevated as a policy priority that leads to actionable paths. Initial steps can be taken by expanding and improving programs that are known to work and, which in the majority of instances, places private capital at risk before taxpayer resources. It is our hope that legislators and regulators at all levels of government will be able to place our nation's housing policy on a holistic, coherent and sustainable path to meet the fundamental human need of a safe and secure home.

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