CITIZENS HOUSING AND PLANNING COUNCIL

THE URBAN PROSPECT

Housing, Planning and Economic Development in New York

September/October 1996 Volume 2, Number 5

Credits Crunch

With direct government subsidies for affordable housing evaporating, the importance of tax-based programs has correspondingly grown. Predictably, developers of affordable housing have recently found access to financing through those programs tightening.

The two mainstays of the tax-incentive approach to housing production, the Low Income Housing Tax Credit (LIHTC) and tax-exempt bond financing, are both subject to caps intended to limit the losses to the federal treasury. Just a few years ago limitations on those techniques were not serious constraints on housing production in New York City. Local developers could acquire LIHTCs from an underutilized national pool, while the city's massive housing program was financed directly through its capital budget. But as developers elsewhere in the state and country become more adroit at utilizing the tax credits and the city approaches its constitutional debt ceiling, the limitations on tax-incentive financing have begun to bite.

Learning Curves

The LIHTC, created as part of the federal tax reforms of 1986, provides valuable federal income tax credits to private investors who provide equity capital to affordable housing. Through the National Equity Fund, an affiliate of the Local Initiatives Support Corporation (LISC) and the largest syndicator of federal housing tax credits, over $1.6 billion, more than one-third of which has been used in New York City, has been raised from corporations and individuals. The program survived a bitter legislative battle during the FY1996 federal budget showdown.

LISC and the Enterprise Foundation honed techniques for utilizing the complex program in New York City during the late 1980s, using it to rehabilitate almost 10,000 units of vacant housing. Partially through the efforts of those organizations, the techniques have been disseminated throughout the country, increasing competition for the limited amount of tax credits available.

Federal law limits the new tax credits that may be allocated within each state annually to an amount equal to $1.25 per capita, which in New York represents over $23 million. That sum, multiplied over the 10-year life of the credits and properly discounted, represents about $140 million in capital for affordable housing development. Moreover, allocations not utilized after two years go into a national pool administered by the Treasury Department, and can be claimed by states that have utilized their regular allocation (in proportion to their population among states that are seeking to draw from the pool). In 1992, New York State received over $9 million in credit allocation from the national pool. As other states began to more fully utilize their per capita allocations, New York's ability to draw from the national pool declined. In 1995 the state got only $1.4 million additional from the pool, and in 1996 only $0.5 million. Consequently, the availability of tax credits within the state has declined dramatically at the very time the need for them has surged.

Housing developers in the city are also being squeezed by a growing demand for tax credit financing elsewhere in New York State. Federal law gives states the authority to allocate the credits within their boundaries; they may allocate them to projects directly or sub-allocate them to other agencies. In New York, the state Division of Housing and Community Renewal (DHCR) is the primary allocating authority. It, in turn, sub-allocates a portion of the state allocation to the state Housing Financing Agency (HFA), to the city's Department of Housing Preservation and Development (HPD) and to one upstate agency. The tax credits are crucial financial elements of the city's in rem disposition, SRO Loan, and other programs. In 1991, DHCR sub-allocated about $10.4 million to HPD out of the $35 million available. About 80 percent of DHCR's direct allocation, totaling over $15 million, also went to projects within New York City. In 1996, by contrast, HPD received a sub-allocation of $9.6 million, and only about 50 percent of the total directly allocated by DHCR went to projects in New York City.

QAP Flap

The need to ration a reduced supply of tax credits in the face of rising demand for them has prompted DHCR to establish new allocation criteria by revising its federally-mandated Qualified Allocation Plan (QAP, pronounced "quap"). The state agency halted its tax credit allocations in May and issued its proposed QAP revisions on August 1. The final, revised criteria are expected to go into effect on November 1.

The new allocation plan will apply twelve threshold eligibility criteria and then rank projects according to eleven

Continued on Page 2

Crunch

Continued from Page 1

scoring criteria. State housing officials hope that these standards will dissuade some national developers, who scour the country for available tax credits and quickly sell their interests in the resulting projects, from entering the state. One of the threshold criteria, for example, is that the proposed number of units in the project can be readily absorbed by the existing demand in the local area.

Other provisions of the QAP, however, have evoked criticism in New York City housing circles. Critics say that while the scoring system favors projects that give preference to very-low income or special needs populations, other criteria are biased against projects that have heavy service components. They see these criteria as contradictory, as the need for on-site services generally increases with the proportion of tenants that have very low incomes or special needs. Moreover, a clause which would permit DHCR to allocate credits to a project irrespective of its score ranking if it is determined "to be in the interests of the citizens of the State of New York" has raised fears that constituency politics will play a greater role in future allocation decisions.

New York State Share Of National Tax Credit Pool Re-allocation 1992 - 1996 (Dollars)

Year	National	New York State
1992	65,811,985	9,089,975
1993	29,677,166	7,780,310
1994	61,047,550	8,979,782
1995	16,587,142	1,352,225
1996	5,819,487	505,712

Source: National Council of State Housing Agencies

Also of concern to housing professionals in the city is DHCR's intention to implement a "fair share" formula for allocating credits around the state. State officials say that the fair share plan will be based on a strict per capita formula. Local housing professionals argue that that approach is biased against New York City, since the city contains only 40 percent of the state's population but almost 70 percent of the households in poverty.

Once the new allocation plan is in effect, DHCR intends to impose a January filing date for projects seeking tax credits during each year, with a second round later in the year only in the unlikely event that the qualified applications do not exhaust the full state allocation. There will be no carry-over from year-to-year; projects on the waiting list from one January will have to re-apply, and will be re-scored, the following year.

Tax Exempts Tight

One way housing producers can access additional tax credit benefits is through tax exempt bond financing. Low-income housing units financed with tax exempt bonds issued by a state housing finance agency automatically receive low income housing tax credits that are not subject to the federal caps (this type of tax credit provides shallower subsidies than the state-allocated type). However, the 1986 tax reform that created the LIHTC also placed stringent limits on the amount of tax-exempt "private activity" bonds that can issued by a state or its localities. With more affordable housing developers needing tax-exempt financing to make projects work, they are running into stiff competition from other priority uses of the bonds.

Bonds exempt from federal income taxation are usually issued by state or local agencies to finance housing at interest rates one to two percentage points lower than those on comparable taxable bonds. The New York State Housing Finance Agency (HFA), the State of New York Mortgage Agency (SONYMA), and the New York City Housing Development Corporation (HDC) are all issuers of tax-exempt mortgage revenue bonds.

The 1986 federal tax laws limited the amount of tax exempt private activity bonds a state may issue annually to $50 per capita, which in New York State amounts to a little over $900 million (government purpose bonds for facilities owned by public agencies are not capped). Any unused portion of the ceiling can be "carried forward" for up to three years, providing the state can certify to the IRS a specific purpose for which it will be used. States are responsible for allocating the authority to issue private activity bonds, within some limits prescribed by federal law.

The allocation formula in New York State is set forth through annual legislation (for 1996, Chapter 104). Each year, the law has required that one-third of the state ceiling be set-aside for the use of state agencies. In the past, SONYMA and HFA got the majority of that portion, but they have met with more competition for it of late. Another one-third is distributed among local agencies according to the share of the state's population contained in each agency's jurisdiction. The final third is held as a statewide reserve, allocation from which both state and local agencies may apply.

Continued on Page 4

CITIZENS HOUSING AND PLANNING COUNCIL

50 East 42nd Street Suite 407 New York NY 10017
Please call (212) 286-9211 for membership information.

Officers
Frances W. Magee, *President*
David A. Gardner, *Chairman*
Sander Lehrer, *Secretary*
Robert Berne, *Treasurer*

Staff
Frank P. Braconi, *Executive Director*
Marian Sameth, *Associate Director*
Paul Nolan, *Peter Joseph Fellow*
Micah Berul, *Staff Associate*

CHPC is a nonprofit, non-partisan membership organization founded in 1937. Contributions are tax deductible.
THE URBAN PROSPECT is free of charge to members.

CONGRESSIONAL WATCH

HUD in Holding Pattern

A HUD appropriations bill was enacted on time this year, providing for slight increases in funding for federal housing programs. In contrast to last year, when HUD was forced to operate on temporary spending authority for months, Congressional appropriations committees made few major budget changes and attempted to legislate no sweeping program revisions.

While the budget bill moved quickly through Congress with little controversy, Senate and House negotiators were unable to reach agreement on public housing reform legislation. House Republicans blamed Senate Democrats for sabotaging the negotiations, and were in turn criticized for their insistence on repealing the United States Housing Act of 1937. Some members of both parties feared repeal of the act would create a morass of legal complications. The failure of the reform efforts disappointed lobby groups for public housing authorities, who seek relief from federal income-targeting and rent-setting rules. The next Congress is not expected to be as favorable toward public housing deregulation, especially if Democrats gain control of either or both houses in November's elections.

Redefining Austerity

With Congress wanting to avoid the budget spectacle of last year and eager to hit the campaign trail, few significant budget changes were made. In fact, the most dramatic departure from previous budgets came in the way federal housing assistance expenditures are categorized. The new system reorganizes major budget lines to facilitate year-to-year comparability among HUD's functions.

Overall, HUD's budget was increased by about 1.7 percent to $19.45 billion still about 20 percent less than three years ago. Most major programs were funded at last year's levels, including Community Development Block Grants ($4.6 billion), HOME ($1.4 billion) and public housing modernization ($2.5 billion). Funding for public housing operating subsidies and for revitalization or demolition of severely distressed public housing was increased slightly. Special needs housing continues to fare relatively well, with the Section 202 program for the elderly receiving $645 million, Section 811 housing for the disabled $194 million, and Housing For Persons With AIDS $196 million. Homeless programs under the McKinney Act, including the Supportive Housing, the Section 8 Moderate Rehabilitation SRO, and the Shelter Plus Care programs were increased by about 8 percent to $823 million.

As in the past two years, no appropriations for general incremental Section 8 vouchers and certificates were made. About $190 million is provided, however, for Section 8 certificates for an assortment of special purposes, such as for families displaced through HUD property sales or because of discontinued project-based assistance. A small amount was also earmarked for a demonstration program tying Section 8 tenant-based subsidies to welfare-to-work initiatives. While Congress criticized HUD in its conference report for its tendency to initiate programs without Congressional approval, it nevertheless appropriated funds for the demonstration. Some observers believe that linking Section 8 to workfare is the most promising route to restoring funding for incremental Section 8 subsidies. Meanwhile, for the second consecutive year, the funding bill mandates a three-month waiting period before local agencies may reissue recaptured certificates; the delay provisions are a means of gradually shrinking the pool of certificates in use.

Stopgaps

Because the public housing reform legislation was not enacted, the budget bill contained additional one-year suspensions of some program provisions that would otherwise have been altered permanently. Those provisions included the one-for-one replacement rule for public housing demolition, the "take one, take all" rule for Section 8 housing, and federal preferences for tenant selection in public and assisted housing. The temporary minimum rent provisions for public housing were also extended, with new language to allow minimum rents of up to $50 per month.

For project-based Section 8, the funding legislation continues the basic approach established in last year's budget legislation. HUD is required to renew expiring Section 8 contracts for one year at rent levels equal to those in effect on the date of the contract expiration, provided that those rent levels do not exceed 120 percent of the local FMR. If they exceed 120 percent and the project is FHA-insured, the owner may elect to have the contract renewed for one year at the 120 percent of FMR level. For projects not FHA-insured but for which public agency financing remains outstanding, HUD is required to renew assistance contracts for one year at the rent levels in effect at contract expiration. An additional $10 million was also budgeted for the mark-to-market demonstration program that pertains to projects with expiring contracts, FHA insurance and rents that exceed 120 percent of the local FMR. Participation in the demonstration program remains voluntary.

House Republicans' least-favorite housing program, the Low Income Housing Preservation and Resident Homeownership Act (LIHPRHA) was funded at $350 million, more than $240 million above that provided in the House budget bill. That sum can only be used for tenant-based assistance for residents of projects leaving the Section 236 program, for "plans of actions" for sales to non-profits, tenant organizations and other priority purchasers, for projects for which a repayment or settlement agreement was executed before September 1, 1995, and for certain other special cases. The budget legislation also requires HUD to suspend further processing of preservation applications which have not already received approval of a plan of action. ■

Crunch

Continued from Page 2

New York City receives about $122 million annually in bond authority through the local agency set-aside. That allocation is controlled by the city's Industrial Development Administration (IDA), a unit of the Economic Development Corporation, which decides how much is needed for various economic development projects and how much can be allotted to HDC for the purpose of financing housing. In 1996, HDC will get about $65 million of that total. The IDA reportedly intends to carry forward most of the rest in anticipation of the second phase of a recycling plant on Staten Island, which will require about $120 million in tax exempt financing. Another recycling project in the Bronx would utilize an even larger amount of private activity bond financing, but the future of that project is now in doubt.

Because the city's share is controlled by IDA, the amount of bond cap available to HDC in future years is not known with certainty. This makes it difficult for the agency and housing developers to plan projects that would be dependent on tax-exempt financing. This year, HDC's $65 million will be spread over three projects, and those will receive only half of their financing through tax exempt bonds.

The city can apply for additional allocation from the state reserve, but under the allocation law that reserve's use is entirely at the discretion of the state's Department of Economic Development (in the case of state agencies, the decision is made by the Division of the Budget). The law mandates a Bond Allocation Policy Advisory Panel, comprised of five members, appointed by the governor, the president of the Senate, the speaker of the Assembly, the minority leader of the Senate and the minority leader of the Assembly. That panel is empowered to monitor the allocation process and to provide policy advice regarding the priorities for distribution of the cap, but it has only advisory powers.

Competition for a share of the state bond cap has grown more intense for several reasons. As federal and city capital grants for new housing diminish, more developers are exploring ways to structure projects utilizing tax exempt financing and the uncapped tax credits that go with it. At the same time, there has been a resurgence in private market rental housing development, which is eligible for tax exempt financing if 20 percent of the units are reserved for families with incomes less than 50 percent of the area median. Developer interest in such 80-20 projects has been heightened by recent changes in the city's 421-a tax abatement program, which extended the term of benefits from 10 to 20 years in marketable sections of Manhattan. Eligibility for those 421-a benefits also requires a 20 percent low-income component. Furthermore, there has been a shift in emphasis at the state and city levels, paralleling that elsewhere around the country, in favor of "economic development" over housing development uses.

Responding to this heightened competition, some housing finance professionals have been exploring 501(c)(3) tax exempt bond financing, which is available to non-profit institutions and is not subject to state volume caps. This approach has major shortcomings, however, as it precludes the use of tax credits without which few not-for-profit housing developers can raise the necessary equity. Furthermore, without tax credits, significant government grants, or a substantial market-rate component, tax exempt financing alone is not sufficient to permit rents affordable to low- and moderate-income families.

Debating Priorities

The sudden tightening in the availability of tax exempt financing has raised new questions about the state's allocation process and the setting of its economic development priorities.

Finance professionals familiar with the process argue that it is too ad hoc and sensitive to political pressures, and that allocation decisions are made in the absence of a coherent economic development strategy. Others suggest that the distinction between housing and economic development uses is artificial, and that a local or state-wide strategy should recognize the close inter-relationship of the two. There is some consensus that the state's year-by-year allocation legislation should be modified, making an individual agency's future allocations legally set in advance. That would facilitate "forward commitments," enabling long-term projects to proceed with other elements of the development process.

Competition for financing has also revealed a rift within the housing development community. Some housing professionals argue that 80-20 projects are an inefficient use of volume cap authority, as only one-fifth of the financing is actually used to create low-income units. Others counter that such projects are critical to retaining the city's middle class and job base, and to encouraging mixed-income communities. This rift was highlighted when The Trump Organization recently sought a reported $350 million in tax exempt financing from the HFA for its Riverside South project. A relatively routine bill to raise HFA's statutory debt ceiling was subsequently torpedoed, apparently by legislators opposed to the project or to its financing request.

Many experts in the housing and financial fields express misgivings that worthwhile housing and job-creation projects are forced to compete for arbitrarily limited financing. They point out that inflation has eroded the value of the $50 per capita volume cap by over 40 percent since 1986, while the federal government has slashed its direct funding for housing, environmental and urban development programs. Furthermore, they point out that tax exempt bonds are not a direct loss to the federal treasury, as projects created with them generate jobs and tax revenues that may more than offset their direct costs. Few, however, see any momentum in Congress to ease the volume restrictions on private activity bonds. ■

Publication of THE URBAN PROSPECT was made possible by a grant from The Community Preservation Corporation.