What Happens to Low-Income Housing Tax Credit Properties after 15 Years?

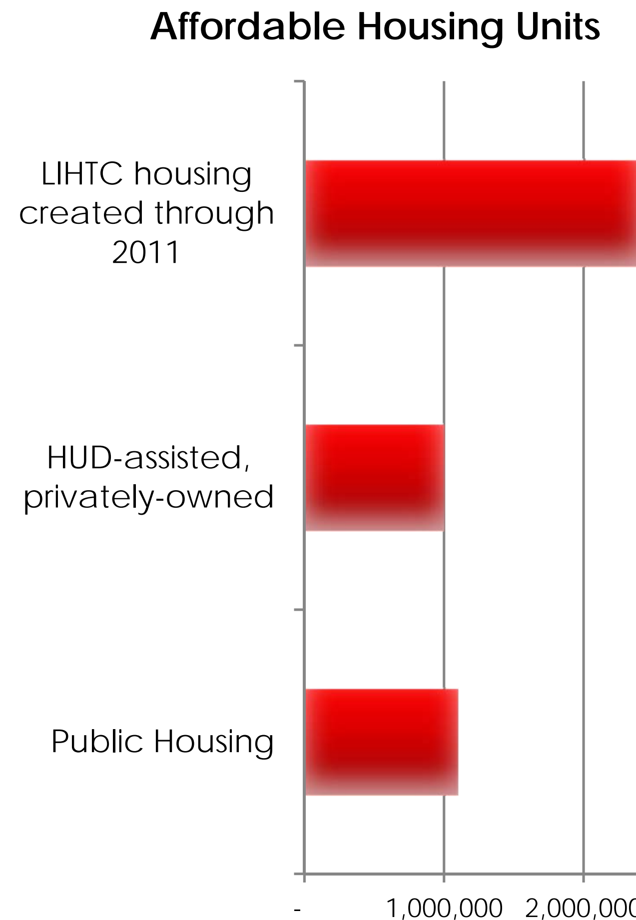
September 12, 2012

Study Team and Project Timeline

- Abt Associates
- VIVA Consulting
- HUD commissioned study in Fall 2009
  - Preliminary Report - January 2012
  - Final Report - March 2012
  - Report Released - August 2012

Overview of LIHTC Portfolio

- 2.2 million units of rental housing developed from start of LIHTC Program in 1986 through 2009 (Estimated 2.4 million units through 2011)
- Largest housing production program in U.S. history
- Since 1990, only production program of any scale
- One-third of all new multi-family construction, 1987-2006
- 6 percent of renter-occupied housing units nationally



Research Questions

- How many properties leave the LIHTC program after reaching year 15?
- What types of properties leave? What types remain under monitoring by HFAs for compliance with program rules?
- What are owners' motivations for staying or leaving?
- What are the implications of properties leaving the LIHTC program for the rental market? To what extent do properties that leave the LIHTC program continue to provide affordable housing?
- How do ownership changes and financing affect whether LIHTC properties continue to provide affordable rental housing and whether they perform well?

Study Approach

- Focus on earliest properties, placed in service 1987-1994
  - All would have reached Year 15 by 2009
  - Without Rural Housing Service Section 515 loans or project-based Section 8
- Syndicators, Investors, and Brokers
  - Discussions and interviews with 14 firms
  - Site visits and in-depth interviews with 5 of 14 firms
- State Tax Credit Allocating Agency/HFA Data
  - Analysis using HUD LIHTC Database
- Owners
  - OMB-approved survey with 37 property owners
- Industry experts
  - Discussions with 13 industry experts

Year 15 Events

Changes in LIHTC Use Restrictions at Year 15

- LIHTC properties have an initial, 15-year compliance period
- Extended use period (30 years total) began nationally for properties with allocations in 1990 or later
- Properties may have other affordability restrictions:
  – Some states, especially those with strongest markets, instituted extended use restrictions earlier than 1990
  – Mortgage financing from HFAs and other mission-oriented lenders
  – Subordinate grant and debt from state or federal sources (for example, HOME, CDBG)
- “Qualified Contract” process provides an option for owners to leave the program after 15 years

Changes in Ownership

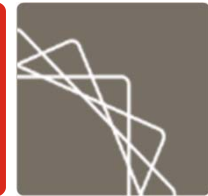
- Ownership change can happen at any time, but likely around Year 15
- Most limited partners (LPs) and investors want a quick exit after Year 15
  - Bulk of the tax benefits of ownership have been exhausted
  - Compliance/recapture risk is over
  - Reporting is a burden
  - Continued ownership involves continued risk
  - LPs can either sell their interest in the ownership entity, or they can sell the property and dissolve the partnership

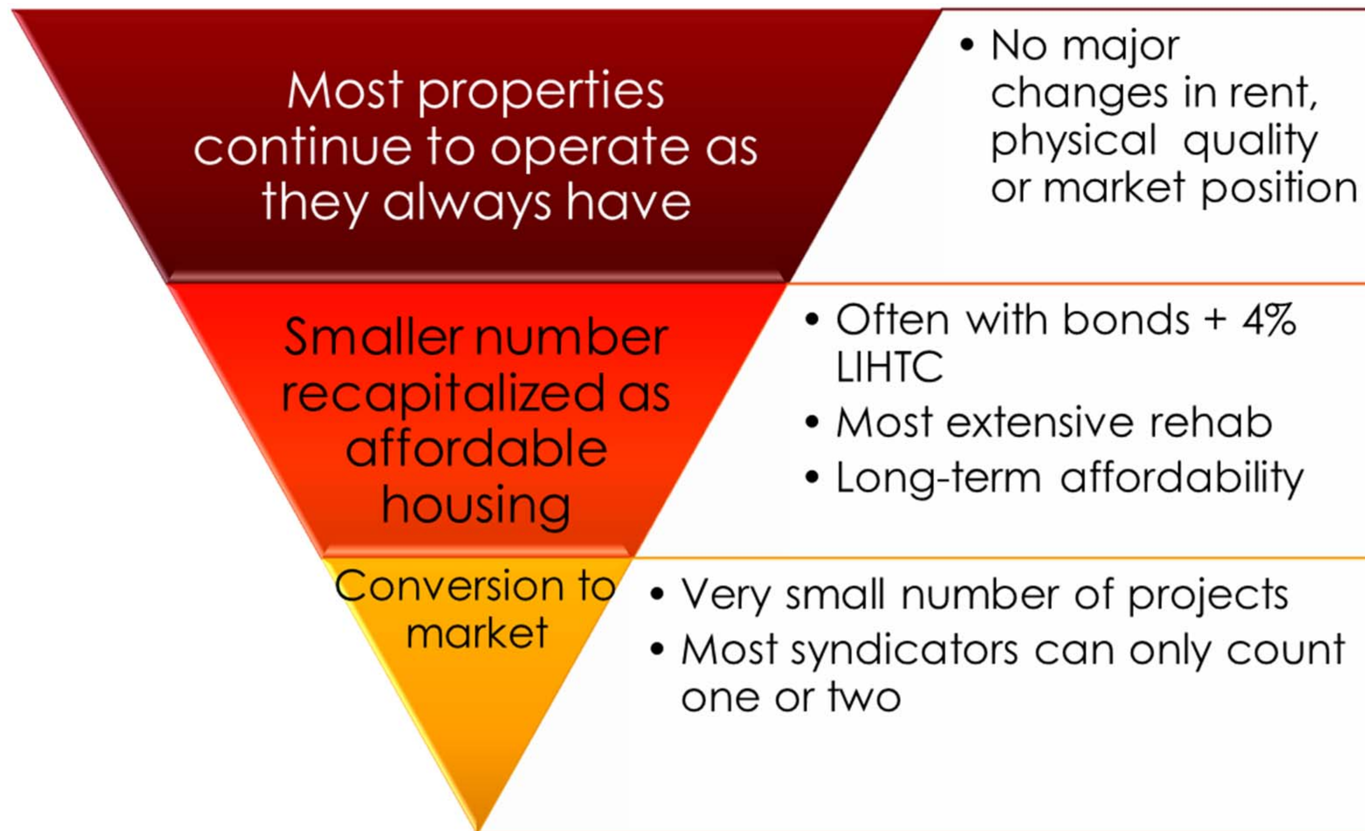
Financial Distress and Capital Needs

- Extent and nature of physical and financial distress will shape Year 15 outcomes
- LIHTC properties tend to operate on tight margins
  - Competition for initial subsidies
  - Awarded minimum amount of subsidy to make deal feasible
- Replacement reserves may be insufficient
  - We found no consensus on extent of renovation and repair needs at Year 15
- Strong markets with maximum rents and high occupancy can generate more operating funds for maintenance and repairs

Property Outcomes

Three Possible Outcomes





Remain Affordable Without Recapitalization

- Occurs even without use restrictions
- Some owners have mission of long-term affordability
- Many properties have market rents no higher than tax-credit rents
- Rehab without major new public subsidy
  - Typical level of rehab: $1,000-$5,000 per unit around Year 15
  - May be financed with new first mortgage or new owner equity
  - Some developments get modest soft loans or support new debt via property tax abatement

Remain Affordable with New Sources of Subsidy

- Properties with substantial capital needs
- Availability of new sources of subsidy depends on state LIHTC policies
- Re-syndication with tax credits
  - Large properties may be able to use tax exempt bonds and 4% credits
  - For a new allocation of tax credits, rehab costs need to be the greater of $6,000/unit or 20% of adjusted basis
  - Use of re-syndication has varied and appears tied to favorability of tax credit pricing
- Recapitalization sometimes with other public subsidy

Repositioned as Market Rate

- Primarily in low-poverty locations
- May result from QC process if no QC sale
  - Affordability restrictions are lifted, owners get regulatory relief, remove compliance and reporting burden
  - In weak housing markets, rents can be raised slightly above the LIHTC maximum, expanding pool of potential tenants
- May result from financial failure

Projected Outcomes at Year 30

- Most will remain affordable
  - Some will remain subject to use restrictions
  - Many will have mission-driven owners
- Some will be recapitalized with new tax credits
  - Competition for HFA resources will limit this, despite unmet capital needs
- Some will be converted to market rate
  - Most likely those in tracts with low poverty in suburbs and central cities with a for-profit sponsor (roughly 43,000 properties)
- Most will have large unmet capital needs

How Are Post 1994 Properties Different?

- **Bigger**: average 75 units compared with 36 units
- **Fewer Section 515**: 9% compared with 31%
- **Similar rates of project-based assistance**: 32% in later-year portfolio
- **More new construction**: 63% compared with 57%
  - Rehab on older properties more extensive
- **More nonprofit sponsors**: 28% compared with 10%
- **More in low-poverty census tracts**: 30% compared with 25%
- **More 4% deals**: 24% compared with 3%
- **Deeper income targeting**

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