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anhd
ASSOCIATION FOR
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AND HOUSING
DEVELOPMENT INC.

BACKGROUND

Over the past several decades, it has been evident that the development of new affordable housing would not occur without public subsidy given the private market's reluctance to build without these incentives. Since the Koch Administration in the late-1970s, New York City government has committed to investing substantially in the creation and preservation of affordable housing due to the wide held belief that the city's economic and civic health depends on having a dynamic, diverse workforce and citizenry. Assuming this commitment of public investment in affordable housing is secure going forward, ANHD has focused much of our efforts on pushing the city to adopt a policy of permanent affordability so as to maximize the return on this investment and ensure these important resources remain affordable to future generations.

Permanent affordability is not only good public policy, it is also good financial policy. As the city faces multi-billion dollar deficits, it is particularly important that public resources generate the maximum public benefit. One way to achieve this return for affordable housing is to maximize the number of years a given project will remain affordable per dollar of city subsidy, including both direct capital expenditures and unrealized income through tax abatements.

Indeed, in the majority of affordable housing deals, property tax exemptions and abatements are powerful incentives for developers. ANHD believes a viable approach to achieve a stronger return on the city's investment would be to require a project's initial affordability term mandatorily be extended for a similar length of time should the state or city continue to abate some portion of the project's property taxes. Currently, however, the city is reluctant to extend tax abatements to further the goal of permanent affordability unless it is certain that a large public benefit will be realized. The case studies detailed below offer compelling evidence that abating taxes in exchange for ongoing affordability is a cost effective approach.

Given these findings, it is evident that the city must either create a new tax abatement authority or modify the use of existing ones in order to match the longer affordability periods. For several reasons, chief among them being the ability to extend affordability restrictions past the current 60 year limit, creating a new abatement authority is the ideal approach. A new abatement could provide a catch-all, partial abatement that would run for the life of an extended regulatory agreement or be renewed at regular intervals for affordable housing projects that would not otherwise qualify for more generous abatements. Developers would sign an initial 60-year regulatory agreement with the city to be eligible for this abatement. However, a city opt-out could be inserted after 30 years or some other period of time to authorize the city to unilaterally cancel the regulatory agreement and withdraw the abatement if the extended affordability were determined to not be worth the potential lost tax-revenue. This approach would establish an expectation that affordability restrictions are expected to be permanent while giving the city the flexibility to make these decisions on a case-by-case basis if necessary.

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Another option would be to modify an existing tax abatement. The city currently has several abatements at its disposal that cover non-profits, for-profits, tax-credit developments, and moderate-income construction. Some of these, such as 420c, could already be utilized with regulatory agreements with extended affordability terms. Whether a new tax abatement authority is created or an existing abatement is amended, a complimentary action to extend the mortgage authority is also necessary.

While matching the regulatory agreement, tax abatement length, and mortgage length is optimal from a programmatic standpoint, the tax abatement must also be underwritten correctly to ensure both a sufficient incentive for development and a wise use of taxpayer money. Currently, several developers, both for-profit and not-for-profit, voluntarily sign regulatory agreements for longer – sometimes decades longer – than their tax abatement (most notably in DHCR tax credit projects where 50-year regulatory agreements have become prevalent). If abatement lengths are going to be matched to regulatory agreements, it does not necessarily follow that these should be full abatements, but instead should be tailored to reflect an appropriate cash flow for the building.

METHODOLOGY

ANHD conducted an analysis, based on financial models developed for our 2008 “Roadmap to Permanent Affordability” report, to determine the cost to the city of extending a full tax abatement to affordable units compared to replacing units when affordability restrictions expired. In terms of dollar-per-year of affordability, we found that given responsible management and a well-maintained building, comprehensive preservation programs mandating an additional extension of affordability is always a much more effective use of public subsidy – in some cases more than twice as efficient.

ANHD’s analysis compared the total city subsidy – including unrealized tax income – needed to build and preserve comparable affordable housing projects 30 years from now. To do this, we analyzed three different programs – a Low-Income Affordable Marketplace Program (LAMP) deal, a New Housing Opportunities (New-HOP) deal, and a standard 9% Tax Credit deal. New construction costs were assumed to be the same as today, indexed for inflation. Under the preservation scenario, the main costs to the city were the unrealized tax income, extension of the original mortgage, city subsidy needed for capital improvements, and soft costs and fees.

Unrealized Tax Income

The original models in the “Roadmap” report assumed that both preservation and new construction would have comparable tax abatements from 2037 on, i.e., a preserved New-HOP would have the same 421-a benefits as a newly-built New-HOP. However, there is an additional cost for preservation.
We revised the models to account for the likelihood that the original phase-out of 421a benefits would have to be abated as part of any comprehensive preservation program. We indexed that cost to 2037 dollars, and added it to the total city subsidy needed for preservation. There are, however, many projects which obtain a full tax abatement through the 420c program, which has no phase out and lasts for the life of the regulatory agreement or 60 years, whichever is shorter. In these cases, there would be no additional revenue lost to the city, because there would be no phase-out to be abated. Thus, the true cost to the city for preserving many projects would be less than the revised models estimate.

Unrealized Mortgage Recovery

With most affordable housing programs, one or more city agencies hold a balloon-mortgage with below-market interest rates. Under any preservation scenario, this mortgage will have to be extended to match the extended affordability terms. Currently, this mortgage authority is only allowed to extend mortgage terms for 30 years. However, a legislative fix to extend this mortgage authority for 60 years has been introduced in Albany.

Subsidy for Rehabilitations Costs

After 30 years, many of these developments will need substantial capital maintenance items, such as new roofs and boilers. Under any preservation scenario, these developments will likely utilize city subsidy for these capital needs and repairs. While it is difficult to estimate the amount of maintenance work needed on a building 30 years in the future, we have developed both a high and low estimate based on current HPD programmatic standers. Our low estimate of $15,000 per Dwelling Unit is based on the Year 15 preservation program, which is designed as moderate, in-tenant rehab for 15-20 year old tax-credit buildings. Our high estimate of $35,000 per Dwelling Unit is based on the Article 8A program, which is designed to correct substandard dwelling conditions brought on by poor management or neglect.

Developer Fees and Soft Costs

We are estimating soft costs and fees (engineering, legal, financing fees, and developer fees) as 15% of the total hard cost of construction. Again, since we based these three models off of pro-formas developed for our 2008 “Roadmap” report, “Year 1” is considered to be 2008 and “Year 30” is 2037. Current programs may have slightly different terms.

The majority of the financing is equity from the sale of 9% Tax Credits. The main debt financing is an amortizing loan from the State Mortgage Finance Agency (SONYMA), with an HPD PLP loan as subordinate debt. The SONYMA mortgage is amortized over 30 years, while the HPD PLP loan is a balloon, which would cost $3,500,000 to extend. Again, there are the two different tax abatements to take into consideration. If the project is majority owned by a not-for-profit, it will be eligible for an as-of-right full 420c tax abatement. If it is majority owned by a for-profit, it will most likely utilize a 25-year 421a tax abatement. From these assumptions, we have again determined both a high preservation estimate (421a abatement and heavy rehab costs) and a low preservation estimate (420c abatement and moderate rehab costs).

LAMP PROJECT

Our first deal is a standard Low-Income Affordable Housing Marketplace Program (LAMP) project. 80% of the 75 units are affordable to those making 60% of the Area Median Income, and 20% are affordable to those making 30% of the AMI. The financing is a first mortgage financed with Tax-Exempt bonds, a 1% balloon HDC second mortgage, an HPD PLP mortgage, and NYC Housing Trust Fund subsidy. Equity comes in the form of as-of-right 4% Tax Credits. Since the bond financing is amortized over 30 years, the cost to extend this mortgage is zero. The HDC balloon mortgage, HPD PLP mortgage, and Housing Trust Fund money are all balloons, and the cost to extend them would be $13,125,000.

There are two different tax abatements to take into consideration - if the project is majority owned by a not-for-profit, it will be eligible for an as-of-right full 420c tax abatement. If it is not, it will most likely utilize a 25-year 421a abatement. From these assumptions, we have determined both a high preservation estimate (421a abatement and heavy rehab costs) and a low preservation estimate (420c abatement and moderate rehab costs). There are other possible scenarios between these two preservation estimates detailed in the charts below, including a 421a abatement and moderate rehab costs as well as a 420c abatement and heavy rehab costs.

LAMP (60% and 30% AMI) 75 units	**Costs in year 2037**		**Notes**
	Preservation Costs	New Construction Costs	
Unrealized Tax Income			
421a Tax Abatement Lost Revenue (Y23 - Y30) in 2037 dollars	$2,366,330	None	3% inflation trending
421a Tax Abatement Lost Revenue (Y23 - Y30) in 2008 dollars	$1,004,127	None	3% inflation trending
Unrealized Mortgage Recovery			
HDC Mortgage Extension	$4,125,000	None	
HPD Mortgage Extension	$9,000,000	None	
Rehabilitation Costs			
Maximum Moderate Rehab Costs	$2,651,625	None	Y15 maximum ($15,000 per d/u) with 3% inflation
Maximum Heavy Rehab Costs	$6,187,125	None	8A maximum ($35,000 per d/u) with 3% inflation
Developer Fees and Soft Costs			
Fees and Soft Costs (w/ Mod Rehab)	$2,366,494	Factored into TDC	15% of development cost
Fees and Soft Costs (w/ Heavy Rehab)	$2,896,819	Factored into TDC	15% of development cost
New Construction Subsidy			
Subsidy needed for New Construction	None	$36,279,326	2008 subsidy+3% inflation
			of cost of New Construction
Total low cost estimate (mod rehab + 420c)	$18,143,119	$36,279,326	50%
Total high cost estimate (heavy rehab + 421a)	$24,575,274	$36,279,326	68%
Low cost estimate in 2008 dollars	$7,698,125	$15,395,000	50%
High cost estimate in 2008 dollars	$10,427,382	$15,395,000	68%

NEW HOP

Our second deal is a standard New Housing Opportunities Marketplace (New-HOP) moderate-income project. 80% of the 75 units are affordable to those making 80% of the Area Median Income, and 20% are affordable to those making 100% of the AMI. The financing is a first mortgage financed with Taxable bonds, a 1% balloon HDC second mortgage, an HPD PLP mortgage, and NYC Housing Trust Fund subsidy. Equity comes in the form a 15% contribution from the developer. Since the bond financing is amortized over 30 years, the cost to extend this mortgage is zero. The HDC balloon mortgage, HPD PLP mortgage, and Housing Trust Fund money are all balloons, and the cost to extend them would be $14,250,000.

Since this is a moderate-income project, the development is not eligible for a 420c exemption, but is eligible for the 25-year 421a tax abatement. From these assumptions, we have again determined both a high preservation estimate with heavy rehab costs, and a low preservation estimate with moderate rehab costs.

New HOP (80% and 100% AMI) 75 units	**Costs in year 2037**		**Notes**
	Preservation Costs	New Construction Costs	
Unrealized Tax Income			
421a Tax Abatement Lost Revenue (Y23 - Y30) in 2037 dollars	$2,366,330	None	3% inflation trending
421a Tax Abatement Lost Revenue (Y23 - Y30) in 2008 dollars	$1,004,127	None	3% inflation trending
Unrealized Mortgage Recovery			
HDC Mortgage Extension	$4,875,000	None	
HPD Mortgage Extension	$9,375,000	None	
Rehabilitation Costs			
Maximum Moderate Rehab Costs	$2,651,625	None	Y15 maximum ($15,000 per d/u) with 3% inflation
Maximum Heavy Rehab Costs	$6,187,125	None	8A maximum ($35,000 per d/u) with 3% inflation
Developer Fees and Soft Costs			
Fees and Soft Costs (w/ Mod Rehab)	$1,690,163	Factored into TDC	15% of development cost
Fees and Soft Costs (w/ Heavy Rehab)	$2,043,713	Factored into TDC	15% of development cost
New Construction Subsidy			
Subsidy needed for New Construction	None	$46,235,815	2008 subsidy+3% inflation
			of cost of New Construction
Total low cost estimate (mod rehab + 420c)	$18,591,788	$46,235,815	40%
Total high cost estimate (heavy rehab + 421a)	$24,847,167	$46,235,815	54%
Low cost estimate in 2008 dollars	$7,888,495	$19,620,000	40%
High cost estimate in 2008 dollars	$10,542,746	$19,620,000	54%

9% TAX-CREDIT PROJECT

Our last project, a 9% tax credit project, is the only one in which the city subsidy needed for preservation has the potential to outweigh that of new construction, which the model projects in cases involving a high amount of rehabilitation costs resulting from poor physical maintenance. It is extremely important to note, however, that this is only because of the large amount of equity available from the Federal Government in the form of Tax Credits. Even under the high cost estimate, an additional 4 million dollars of city money to preserve a project would free up 21 million dollars of Federal Tax Credits to construct additional affordable housing.

In our 9% Tax Credit deal, half of the 50 units are affordable to those making 50% of the Area Median Income, 30% are affordable to those making 60% of the AMI, and 20% are affordable to those making 80% of the AMI. The majority of the financing is equity from the sale of 9% Tax Credits. The main debt financing is an amortizing loan from the State Mortgage Finance Agency (SONYMA), with an HPD PLP loan as subordinate debt. The SONYMA mortgage is amortized over 30 years, while the HPD PLP loan is a balloon, which would cost $3,500,000 to extend. Again, there are the two different tax abatements to take into consideration. If the project is majority owned by a not-for-profit, it will be eligible for an as-of-right full 420c tax abatement. If it is majority owned by a for-profit, it will most likely utilize a 25-year 421a tax abatement. From these assumptions, we have again determined both a high preservation estimate (421a abatement and heavy rehab costs) and a low preservation estimate (420c abatement and moderate rehab costs).

9% Tax Credit (50%, 60% and 80% AMI) 50 units	**Costs in year 2037**		**Notes**
	Preservation Costs	New Construction Costs	
Unrealized Tax Income			
421a Tax Abatement Lost Revenue (Y23 - Y30) in 2037 dollars	$1,325,456	None	3% inflation trending
421a Tax Abatement Lost Revenue (Y23 - Y30) in 2008 dollars	$562,453	None	3% inflation trending
Unrealized Mortgage Recovery			
HDC Mortgage Extension	$3,500,000	None	
HPD Mortgage Extension	$9,375,000	None	
Rehabilitation Costs			
Maximum Moderate Rehab Costs	$2,651,625	None	Y15 maximum ($15,000 per d/u) with 3% inflation
Maximum Heavy Rehab Costs	$6,187,125	None	8A maximum ($35,000 per d/u) with 3% inflation
Developer Fees and Soft Costs			
Fees and Soft Costs (w/ Mod Rehab)	$1,690,163	Factored into TDC	15% of development cost
Fees and Soft Costs (w/ Heavy Rehab)	$2,043,713	Factored into TDC	15% of development cost
New Construction Subsidy			
Subsidy needed for New Construction	None	$8,247,979	2008 subsidy+3% inflation
			of cost of New Construction
Total low cost estimate (mod rehab + 420c)	$7,047,369	$8,247,979	86%
Total high cost estimate (heavy rehab + 421a)	$12,465,650	$8,247,979	151%
Low cost estimate in 2008 dollars	$3,001,655	$3,499,618	86%
High cost estimate in 2008 dollars	$5,289,237	$3,499,618	151%

ADDITIONAL AFFORDABILITY CONSIDERATIONS

In addition to a dollar-for-dollar analysis of New York City money, there are other considerations that should be taken into account – the availability of Federal and State funds to develop affordable housing today versus in 30 years, and the cost and availability of land.

The original affordable housing developments were done mostly on City-owned land, which was transferred to developers for nominal amounts. This model has served New York well since the 1980s; however, as land becomes more valuable and city-owned sites become scarce, affordable housing development will increasingly rely on other means of acquisition.

This model relies on city-owned land for the LAMP and 9% Tax-Credit deals. While we don't know the availability of land in the future, if current trends continue it is quite likely that acquisition costs for affordable housing development will be significantly higher than today. As such, an additional, un-numerated cost in 2037 – land – should be considered in this analysis.

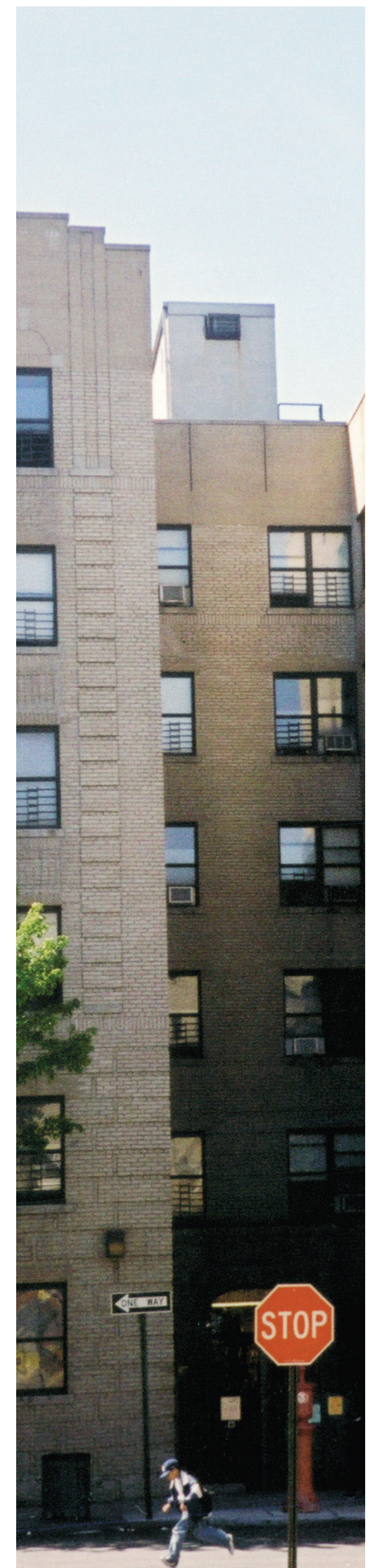
This analysis is also dedicated only to quantifying the cost of subsidy that comes directly from New York City agencies. Federal and State funding also factors into affordable housing development. There are many instances – such as the 9% tax credit project above – where small amounts of city subsidy dedicated to preservation allow for levering of larger amounts of Federal and State subsidy for construction of new units.

CONCLUSION

Affordable housing remains one of the foremost challenges here in New York City. Ever since Mayor Koch's first ten-year housing plan, we have recognized the important role the city, state, and federal government play in ensuring New York remains a vibrant and economically diverse city, and affordable to people from all income levels and walks of life.
Since 1987, we have had an amazing record of success – developing almost 300,000 affordable housing units and revitalizing entire neighborhoods.

Today, however, we confront a new problem: how to ensure this success does not slip away. Slowly but surely, we are starting to move backward as we lose affordable housing units at a higher rate than we are gaining them. Unaddressed, this trickle will soon turn into a flood.

Now is the time to start moving forward on a permanent solution to this permanent problem. Our own experiences, as well as those of other cities, have taught us this is a problem that can be solved. As the State and City of New York develop their strategies for permanent affordability, it is important to acknowledge that property tax incentives are one of the most powerful tools local government has, providing substantial leverage to ensure affordability.



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