MAJOR GOVERNMENT HOUSING PROGRAMS

AN OVERVIEW

04-16-2008

The following is a brief overview of the most common government housing programs applied to multi-family rental property. It is intended to provide only the most basic information about the most common components of these programs.

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Most of us deal with subsidized and government program multifamily housing properties on a limited basis. We don't have the time or desire to become experts in such a complicated area. There are at least 175 loan/insurance or grant programs available through HUD and this does not even include programs administered by Rural Housing or other government agencies. Unless you choose to make these types of properties a focus of your appraisal education, it is almost impossible to have a full understanding of the financing and restrictions in place for these properties. But I've discovered that many of us don't have a basic understanding of the major programs that create and define these properties. This lack of understanding can even be seen in some PVD documentation and suggested procedures.

We tend to lump any properties called "subsidized" into one big group and assume they have similar characteristics and therefore present a similar appraisal problem. But there are vast differences not only in the major types of programs but also in the available mix of programs for which a property may be eligible.

I hope to provide sufficient background information to clarify some of the issues and differences in types of subsidized properties. This is a basic overview intended to provide a general understanding of these properties and as a starting point for access to more detailed information. After a brief history of government housing programs, I will provide a very limited overview of four basic programs that are most common as applied to "For-Profit" owners. I will also list some documents and web sites that provided source material and that the reader can refer to for more detailed information.

HISTORY

It is easy to see why subsidized housing is hard to understand when you consider that current programs have their start in a federal program that is over seventy years old. The idea of government housing assistance has its roots in the Great Depression with the creation of the Federal Housing Administration. In reality, this program had as much to do with job creation as it did in providing housing for the poor.

The program soon led to the establishment of local housing authorities (LHA's) that directed these projects and carried tax exempt bonds to pay for the capital write down of these projects.

After WWII, the increased demand for housing increased government's involvement but by the 1960's, many projects were in disrepair and represented some of the worst living conditions in the USA. In response, the 1968 Housing Act was passed. This act called for the construction or major renovation of 26 million housing units in a ten year period.

The enormity of this goal led to the many programs, governmental departments, and private and non-profit sector involvement that we have today. Government looked for creative ways to construct and finance these projects and began to encourage private investors and non-profit organizations to participate. Along the way, the system was tweaked to deal with problems encountered. The Section 8 program was created to increase revenue to the projects when inflation outpaced operating budgets. Low Income Housing Tax Credits were introduced in the 1980's as an incentive to investors after tax law changes made ownership of these properties less desirable.

Today we have a tangle of government agencies from the IRS, Dept of Agriculture and HUD to state agencies and local housing authorities that oversee participation in a single or a complex ever-changing multitude of programs by quasi-governmental, non-profit, for-profit and limited dividend organizations.

PROGRAMS

There are a multitude of programs administered or funded by various entities for a significant number of specified uses: from low income housing for the elderly or disabled to preservation projects. A specific project may participate in a specific program but more often than not, it may be involved in a number of programs. For example, a specific housing project may have a HUD insured mortgage, receive a 70% tax credit over a ten year period for income tax purposes and receive Section 8 revenue for qualified tenants.

Because of the complexity of the programs, I will limit this article to the major programs that often apply to multi-family housing projects and that as appraisers, we should understand and consider:

RURAL RENTAL HOUSING LOANS (known as section 515)

MORTGAGE INSURANCE FOR RENTAL/COOP HOUSING (Sections 221(d)(3)& 221(d)(4)

LOW INCOME HOUSING TAX CREDITS (LIHTC)

SECTION 8 PROGRAM (Rental subsidies)

RURAL RENTAL HOUSING LOANS (SECTION 515): This is a direct mortgage program administered by the Rural Housing Service (RHS). RHS is a part of Rural Development (RD) which is within the U. S. Department of Agriculture (USDA).

To qualify for these loans a property must be located in a rural defined area – under 20,000 population and not near urban areas. It must serve "very low – low and moderate income"[1] individuals and families and it must meet agency standards for construction, maintenance and need.

The benefits of participation in 515 housing includes; A direct loan for up to 30 years at an effective rate of 1% interest and amortized over 50 years. (While a market interest rate is stated on the note – it is only used to establish the maximum rent payments allowed.)

RHS rental subsidies can be provided to limit tenant payments to 30% of their income. This provides the owner with some income stability.

By participating in 515, For-Profit owners must agree to operate on a limited profit basis. This is currently set at an 8% annual return on the initial investment. In addition, any 515 loans made after 1989 cannot be prepaid except under very specific circumstances.

MORTGAGE INSURANCE FOR RENTAL/COOP HOUSING (Sections 221(d)(3)& 221(d)(4) & 207/223(f) This is an insurance program administered by the U.S. Department of Housing & Urban Development. It provides mortgage insurance for HUD approved lenders. In effect, HUD guarantees payment to the lender if the borrower defaults on the loan. The intent of the insurance is to encourage the private sector to build and renovate rental housing by making capital more available. There are no low income requirements for this insurance.

To qualify a project must be for new construction, substantial rehabilitation of existing multifamily rental or for the purchase or refinance of an existing property. The property must provide housing for moderate-income families, elderly or handicapped. It must also meet HUD standards for community need, capabilities of the borrower, etc.

The benefits of participation vary somewhat by owner or type of project. Non-Profits under section 221(d)(3) can receive an insured mortgage up to 100% of the HUD estimated replacement cost of the project. For-Profits under section 221(d)(4) can receive up to 90% of the HUD estimated replacement cost estimate. Refinancing or purchase of existing properties under section 207/223(f) can receive mortgages up to 35 years and up to 85% of acquisition cost, HUD appraised value or a mortgage amount supported by 85% of net income.

The existence of the mortgage insurance allows for long term mortgages up to 40 years, more availability of funds and permits more favorable interest rates to borrowers.

RESTRICTIONS:
Eligibility is limited to properties containing 5 units or more and there are some statutory mortgage limits based upon size, type and location.

NOTE: HUD specifically indicates that there are **no** income requirements on tenants due to the mortgage insurance programs.

LOW INCOME HOUSING TAX CREDITS (LIHTC): are administered in Kansas by KANSAS HOUSING RESOURCE CORPORATION (KHRC)under provisions established by The Tax Reform Act of 1986 to conform to the regulations of Section 42 of the Internal Revenue Code.

How It Works: Each state is allocated a fixed amount of credits based upon its population. A state agency such as KHRC administers the program and based upon each individual project proposal and its merits awards the tax credits upon a competitive basis until the credits are exhausted for that period.

QUALIFICATION: Eligible developments must set aside a minimum of 20% of its units for persons whose incomes are at or below 50% of the area median gross income, or 40% of its units for persons whose incomes are at or below 60% of the area median gross income. Many properties reserve 100% of their units for low-income use to be eligible for 100% of the tax credits. Units designated for low-income use must be rent restricted with maximum rents. There are no tenant restrictions on other units that are not set aside for low income.

BENEFITS: The development receives a ten year tax credit based upon a percentage of its eligible basis. (There are numerous variables in establishing basis but in general it is the cost of the project and/or renovation cost less land value). Tax credits are usually 9% or 4% depending on the amount of the project set aside for low income and other factors.
EX: a property eligible for a 100% tax credit with an eligible basis of $1,000,000 would receive a $90,000 tax credit each year for ten years. These credits are usually sold to investors (often corporations) for $0.75-0.80 on the dollar. This provides equity funding for the development and the initial partner manages the property as a for-profit given the above qualifications.

RESTRICTIONS: Rents on low income portions of the property are set based upon tenant's income (30% including a utility allowance).
Properties must remain in compliance with the original agreement for a minimum of fifteen years.
There are various restrictions and requirements on the sale of these properties.
Properties must maintain additional records and be subject to inspection of the property and its records by the state governing authority.

SECTION 8 (HAP); is the largest public housing program in the country. It is federally funded and administrated either by HUD or more likely by local Public Housing Authorities (PHA's). Housing assistance payments (HAP) are made to landlords on behalf of qualified tenants based on low income, age or disability.

Section 8 is either tenant-based or project-based. Tenant based HAP vouchers are attached to the tenant not the property. Families who qualify for the rent subsidy are not limited to specific housing but may "carry" the voucher and live in any rental property that accepts such vouchers.

Project base HAP payments require a contract between a property owner and HUD or the PHA. The property owner agrees to set aside a specific number of units for low income tenants for a specific period of time. (These can be the same units as defined for qualification of the LIHTC program) The contract can be reviewed and updated on a periodic basis – at least every five years and specified rents are reviewed more frequently. In exchange, the property owner receives direct HAP payments for qualified tenants housed in these units.

HAP payments are basically figured at the difference between 30% of the tenant's monthly income and FAIR MARKET RENT[ii]. For example; if local FMR for a two bedroom apartment was established at $500/month and the tenant's monthly income was $1000/month, the tenant would pay $300/month and the property owner would receive a monthly HAP payment of $200.

Property owners must abide by the HAP contract, screen tenants for eligibility and are subject to periodic inspections. It is interesting to note that in case of vacancies, the property owner may continue to receive HAP payments for sixty days or longer.

As can be seen, government housing programs can be extremely complex. We have only referenced the most basic aspects of these programs. It is not realistic to assume that all "subsidized" housing can be valued by a single specified method or that participation in any or all government programs is categorically detrimental to its fair market value.

While 515 Rural Housing does have limits on profitability, many owners are non-profit organizations and there has been extremely limited construction of 515 housing since the 1980's.

Most For-profit ownerships enter into agreements that limit their ownership rights based upon the idea that they are receiving benefits of greater or at least equal value as the rights assigned. While participation in some programs restricts the right to sell the property or use it without restrictions, access to long term favorable loans, mortgage insurance, significant tax credits and stable rental income reducing risk at least balances these restrictions in the minds of these investors.

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The following references are to web sites or web pages/documents that provide further information that is pertinent.

http://www.huduser.org/datasets/fmr.html HUD site for Fair Market Rents

http://www.rihomeless.com/landlord_faq.htm Rhode Island Coalition for the Homeless frequent questions about section 8

http://www.usa-federal-forms.com/usa-fedforms-usda-rd/usda-rd-1930-7-nonfillable-k.pdf 1930-7 budget form required of section 515 housing

http://www.huduser.org/resources/hudprgs/ProgOfHUD06.pdf 136 page pdf file outlining HUD programs

http://www.kshousingcorp.org/display/htc_man/htc_02_tax_credit_program.pdf a 19 page pdf file from Kansas Housing Resource Corporation outlining tax credit overview

http://www.kshousingcorp.org/programs/htcmanual.shtml KHRC web site http://www.rurdev.usda.gov/ USDA Rural Development web site

http://www.hud.gov/ HUD web site

Further note: HUD maintains data bases of properties involved in HUD programs. The HUD website is quite large and sometimes confusing. McCully & Associates has downloaded some of these data bases, limited them to Kansas properties and designed report forms to summarize data. We can produce reports on participation in:

The HUD insured mortgage program
Low Income Housing Tax Credit
Section 8 Participation

We will be more than happy to provide these reports by fax to a specific county by request. *The user should be aware that some information has not been maintained or updated in the last few years by HUD – particularly the LIHTC data base. This limits its usefulness.*

i Very low income is defined as below 50% of the area median income: low income is between 50-80% of area median income; moderate income is capped at $5500 above the low income limit: rdinit.usda.gov/regs
ii FMRs are gross rent estimates. They include the shelter rent plus the cost of all tenant-paid utilities, except telephones, cable or satellite television service, and internet service. Fair Market Rents (FMRs) are primarily used to determine payment standard amounts for the Housing Choice Voucher program, to determine initial renewal rents for some expiring project-based Section 8 contracts, to determine initial rents for housing assistance payment (HAP) contracts in the Moderate Rehabilitation Single Room Occupancy program (Mod Rehab), and to serve as a rent ceiling in the HOME rental assistance program.