



## State of the Market 55: A year in the *Guru*, 2013



By David A. Smith

Alongside *State of the Market* for the broad multifamily residential audience, I write a monthly *Tax Credit Advisor* column, *The Guru is In*, consisting of shorter pieces in more technical (usually LIHTC-related) subjects. In these essays (full text appended for greater insight, grasshopper), protracted study of the micro often yields insights into the macro – so herewith, highlights from a year of the *Guru*.

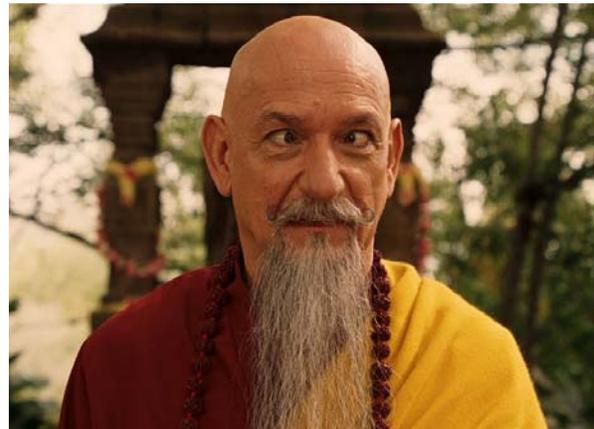
### January: Bring health care into housing

America's health care system has become so place-based that we signal someone's well-being by using locations as code words. We're moving her to assisted living (we say with sorrow); to a nursing home; to a hospital; to a hospice.

Place-basing our high-tech health care depersonalizes treatment and takes the person out of the process. She is a "patient" (a

#### David Smith receives NAHMA President's Award

David A. Smith has received the 2013 President's Award from the National Affordable Housing Management Association (NAHMA) for "an unparalleled commitment to advancing quality affordable housing in the United States and abroad, and innovative leadership that has inspired and contributed to success within federal agencies, Congressional committees, academia, the industry, and communities everywhere. We sincerely appreciate your commitment of time, energy and leadership on behalf of affordable housing worldwide."



*In the country of the confused, the cross-eyed man is king.*

demeaning term connoting passivity and dependency) who can't heal herself and must therefore be trundled from one location to another for the convenience of the "health care professionals" (a pompous neologism) who speak in a dual arcana – first medical and then Medicaid/Medicare. The result is a health care system that no one defends because no one understands it, its costs are soaring (and going higher under Obamacare), and it cannot show progress by any common-sense measure.

### February: Eliminate the MID

Once one realizes that the Mortgage Interest Deduction is harmful, one is imbued with an urgency to kill it when the opportunity arises – and this is our best chance in forty years.

Support for housing prices today is not coming from an explosion of mortgage credit; if anything, it's equity-based entrants who are the home buyers. At 4.25% or so, today's interest rates cost less, even if we ignore the MID entirely, than the 6.50% rates of five years ago would cost even with a full MID. And our



nation's current, staggering budget deficits are imperiling the country's economic future.

The MID must go. Let's do it now.

### **March: When the markets lead**

*When the people lead, the leaders will follow.*  
– Mahatma Gandhi

When it comes to green retrofits of existing multifamily affordable housing properties, over little more than half a decade, what once was hypothetical has become the next best thing to mandatory – at least for acquisition/ rehab transactions. That is a market-led revolution, caused by four parallel and reinforcing trends: (1) the emergence of standards, (2) state-level policy innovation, (3) the "next available opportunity" approach to green, and (4) the ability to calibrate "just enough marginal subsidy." When the markets lead, the policy eventually follows.

### **April: RIP, as-of-right zoning**

*Don't it always seem to go, that you don't know what you've got 'til it's gone.*  
– Joni Mitchell, Big Yellow Taxi

A loved one's passing should always be mourned, the more so when that death happened slowly, silently, through inattention. So it is with as-of-right zoning, an aspect of development that over roughly three decades has softly and suddenly vanished away, taking with it our control over affordable housing costs and our ability to execute a national housing policy – and raising preservation from afterthought to national imperative.

It's the affordable housing production paradox: the same communities that will fight you for years to *prevent* a developer from bringing new affordable housing *in* to a community will similarly fight to prevent that same developer

from taking *existing* affordable housing *out* of that community.

### **May: QAP is DNA**

Competition was a long time coming to affordable housing, arriving serendipitously in the Low-Income Housing Tax Credit (LIHTC) program, which mandates a trifecta of ring-fenced individual-state autonomous allocations, annual award cycles, and Qualification Allocation Plans (QAPs) as modifiable DNA.

Together this trio of imperatives replicates the forces of evolution: scarcity, selection, and rules. Without scarcity, there is no selection, and without rules, selection is random and does not progress. LIHTC's evolution advances through intelligent design: its rulemakers are manifest and conscious.

### **June: The folly of 'perpetuity'**

Because our financing and regulatory structures are tightly strung and comprehensively interconnected, any big capital expenditure requires opening up everything – physical, operational, financial, ownership, affordability. Thus I've long believed that properties should be comprehensively revitalized every 10 to 15 years. The longer a portfolio goes beyond this natural revitalization half-life, the more obsolete, market-disconnected, and cost-*inefficient* it becomes.

Want to kill a property slowly? Lock it up in perpetuity. Want to keep the property, financing, and owner on their games? Give it a reset option every 10-15 years.

### **July: Economic human shields**

In affordable housing appropriated programs, the use of economic human shields is easy, because a classical regulatory agreement is always a two-way street: while the owner is obligated to provide quality affordable housing,



the regulator is obligated to give the owner enough resources (rents or subsidy) to maintain economic viability.

The maestro of such malfeasance was the late A. Bruce Rozet, who at his peak controlled over 25,000 HUD apartments, and who routinely deployed economic human shields to frustrate several HUD secretaries' campaigns to oust him. Rozet stymied HUD because he knew that all of HUD's enforcement remedies (like abating the Section 8) would punish the property and the residents long before they punished the owner, so he repeatedly thrust the residents into economic harm's way and dared HUD to attack.

### August: The trap of caring

When owners and managers get paid to provide quality affordable housing units, and then go beyond that to provide quality resident-centric life services *for free*, residents and government agencies come to believe this will go on indefinitely, because the owner and manager *must* be getting something out of it. For owners and managers, this is the trap.

I don't want our industry to stop caring: we cannot be in the business of simply warehousing the poor. We must build the ladder upwards, providing a boost up to those residents with genuine needs. While helping those who do need our assistance, to get people into independence also requires *not* helping those who will not help themselves; that too is caring.

Caring about residents is a trap *if* we let our caring silence us. If budget cuts occur because we are silent, the trap will be sprung upon us.

### September: The unannounced revolution

**We all want to change the world.** While some revolutions are announced, others arrive with so little fanfare that by the time they seep into the

public consciousness they're all but inescapable. Such a revolution is quietly overtaking public housing: while the legacy program of HOPE VI remains on the books but zero-funded (except for occasional Choice Neighborhoods grants), the whole structure of public housing is being reinvented via HUD's Rental Assistance Demonstration (RAD).

Every HUD program, I once told a laughing LIHPRHA audience, goes through six stages: Conceptualization, Enactment, Chaos, Codification, Scandal and Shutdown. And the best time to enter a program is in Chaos; it maximizes opportunity for the smart and decisive.

Three years later, many of those same folks were no longer laughing – LIHPRHA's application window had closed and the program was defunded.

**You better free your mind instead.** RAD remains open for business: HUD still has 40,000 apartments' worth of demonstration authority (and funding for it). [*Since obligated – Ed.*]

Here is a HUD program that not only allows deregulation and innovation, but also accepts walk-in service by people who *want* to make the transaction work.

You say you want a revolution?

### October: Struldbrug buildings

To the visitor from a land where a Greyhound bus terminal carries a proud plaque attesting to its pedigree, England abounds in spectacular historic, often ancient structures. Many are the nation's treasures and wonders, sites lovingly maintained with public funds that bring past centuries alive.

But one also finds another kind of historic structure – England's struldbrugs. Much like Jonathan Swift's struldbrugs in *Gulliver's Travels*



(otherwise normal humans who can never die), Britain's struldbrugs are buildings that although legally designated historic (and therefore protected) neither disappear nor revive, because no funding is allotted to renovate or preserve them. Instead they sit empty, unimproved and often ringed by concertina wire, aging, derelict, and scarred by graffiti and broken windows, doomed to perpetual structural decline.

### November: Above the invisible ceiling

Blue-voting cities that need workforce or key-worker housing – health care workers, city teachers, police/fire, EMTs – cannot use LIHTC to help these people, as they are usually classified as “over-income”.

This is grossly unfair. These workforce customers – above 60% but below the income level needed to rent a market apartment in their supply-restricted blue cities – are the *only* income/tenure configuration in America whose housing costs aren't subsidized or supported. When everyone else is advantaged, not being advantaged means being discriminated against.

If you live in a low-ceilinged house long enough you gradually adapt your posture and forget about standing up straight. But once you remove the impediment, you suddenly discover how cramped you've been and remember your previous pain. In the LIHTC program, it's time to

allow high-rent locales to raise their local ceilings so states can serve that neglected niche.

### December: Fiat LIHTC

In 1887, theoretical physics faced an epochal crisis: is light a particle or a wave?

In 2012, LIHTC investing faced a similar paradox: is LIHTC investment economic, or tax?

After Michelson and Morley's exhaustive experiments, light could not be a particle, nor could it be a wave. According to 1887 theoretical physics, light was impossible.

Light is light; there it is. It is both at once: a particle when it needs to be, a wave when it needs to be. That physicists cannot pigeonhole it neatly into a pre-existing framework makes no difference. For proving this negative, Michelson and Morley won the Nobel Prize.

In accounting terms, LIHTC is LIHTC, and there it is. Is LIHTC economically motivated, or tax motivated? It is both at once: the tax considerations *are* the economics, and these are righteous because the federal government has deemed them righteous.

On November 14, the EITF saw the light, unanimously recommending classifying LIHTC as a thing unto itself.

*Fiat LIHTC.*

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