



State of the Market 51: "I've got a little list"



By David A. Smith

*As some day it may happen that a victim must be found, I've got a little list – the Lord High Executioner, *The Mikado*, Gilbert and Sullivan*

The current sequester is merely the first of a series of cost crunches that will dominate American domestic politics for the next several years. With economizing inevitable and urgent, five affordable housing expert practitioners – a CDC director, a non-profit acquirer, a public housing authority CEO, a quasi-public affordable lender, and a guru – participated in a brainstorming Harvard Graduate School of Design class whose topic was, *What should we change about America's affordable housing delivery system?*

Among the many provocative ideas surfaced – and presented for your consideration, as Rod Serling used to say, and without implied endorsement – were these:

Subsidy and incentives

Inescapable principles of land-use economics make subsidy an essential ingredient in modern urban affordable housing, and over the last four decades the temptation has been great to customize ever more particular forms of subsidy, with resulting perverse incentives, program inefficiency, and mushrooming compliance requirements. Our inventors offered multiple ways to streamline it:



*Misguided housing policies might well be underground
And that never would be missed, would surely not be missed*

1. **Make income subsidy an entitlement and time-limit it.** Time-limit Section 8 and step down its benefit levels (say, over five years) except for populations that are recognized as "permanently poor" (elderly, irremediably disabled).
2. **Create unitary consolidated eligibility.** Right now millions of hours are wasted on multiple certifications that are then multiply rechecked. For each individual eligible for any federal government benefit, establish a single government record (a unique number that for privacy isn't your social security number) which connects to a consolidated annual household certification (income, assets, household composition, work status, and so on). Tie said eligibility to a biometric



card (fingerprint or retinal scan) of the type being rolled out for India's billion-plus people. Standardize definitions across multiple programs – public housing, affordable housing, elderly care – and use standard formulas for income definitions, income exclusions, income from assets, and deductions.

- 3. Convert all social benefits, including housing assistance, into a cafeteria plan.** In a cafeteria plan, each household has a finite amount to spend on a set of permissible social benefits – health care, housing, food, and so on – up to a cap. So provide each beneficiary household with a calculated allowance based on consolidated eligibility criteria (see preceding point), include co-payment requirements from the beneficiary, and let the beneficiary choose which to consume when.
- 4. Shift Federal priorities away from homeownership.** Eliminate the mortgage interest deduction (MID) and repurpose that money. Though the MID is enormous (over \$100 billion of tax expenditure annually) and has grown well beyond affordability principles (a yacht can qualify if it has 'sleeping, cooking, and toilet facilities'), it has done little to boost homeownership. (Our homeownership rates are no higher than Canada and Australia, both of which have no MID, and lower than the UK which phased out its MID under Margaret Thatcher).

Laws

With increasing American urbanization and the cities' revival has come a proliferation of barriers to residential development, covered at length in *State of the Market 37: More's the laws*, April 2011. These increase the cost of affordable housing and widen the cost-value gap that subsidy must cover. Per-apartment costs will be dramatically lowered and production boosted if we scythe through the development thicket with these possibilities:

- 1. Enact a federal inclusionary-zoning statute or incentive system** whereby states that lack a certain percentage of affordable housing either have their local zoning trumped by higher-density properties with a stipulated minimum (say, 25% of the units) of affordable housing, or have their Federal revenue-sharing formulas reduced.
- 2. Eliminate exclusionary zoning, both explicit and implicit.** Enact metropolitan-plus safe-harbor as-of-right zoning overrides for areas with residential density above a threshold (dynamically adjusted from year to year to reflect increasing American urbanization), where basic affordable-housing developments are fast-tracked through all entitlements and approvals (e.g. wetlands, traffic, environmental) and override existing NIMBYite individualized reviews that now create potentially endless processes.
- 3. Revamp the national building code** that recognizes the technological and social revolutions of the last sixty years. Allow smaller apartments, multi-bedroom



roommate-oriented apartments with shared kitchens, higher-tech analogs of the historical RBK (room, bath, kitchen) that served as starter apartments for single people. Modify zoning to authorize live-work spaces as either residential or commercial to encourage creation of adaptable spaces.

4. **Waive exit taxes for any owner that sells its property to a permanent-affordability buyer.** This will enable owners of uneconomic smaller properties, such as RHS §515's, to exit from ownership and will encourage transfer to better owners and property revitalization.

Innovations and entities

Recessions and budget cutbacks mean shrinkage and consolidation. Government's increasing scale has taken it beyond the limits of its ability to provide localized touch (analyzed in *State of the Market 35: The Last-mile counterparty*, February, 2011). Combine these ideas and they imply that government must outsource implementation of delivery (into responsible private hands, whether for-profit or non-profit) and encourage mixing and matching of resources, in ways consistent with these ideas:

1. **Enact a reinvented CRA 2.0 reflecting the totality and complexity of current financial markets.** Bring in more financial institutions, including insurance companies, pension funds, securitizers and investment banks, credit card companies, banks-in-retail (e.g. WalMart, McDonalds), even cellphone providers if they operate mobile-money services. Expand the universe of financial products

that qualify for either debt or equity-type consideration to include secondary-market transactions, derivatives, guarantees and other instruments that facilitate the flow of capital into housing and urban development. Discard the antiquated approach of 'assessment area' (predicated on deposit-taking in physical locations) and use an income-based (e.g., poverty census tracts or income limits) definition of qualifying loans and investments.

2. **Move to having affordable housing properties owned solely by regulated affordable landlords (RALs).** Analogous to Britain's system of Housing Associations, define an RAL as a non-profit entity that is accredited, licensed, and controlled as to its economics (e.g. caps on director and executive compensation). Prohibit anyone but a RAL from owning affordable housing. Require RALs to be fully transparent as to financial and operational results. Then deregulate individual properties and regulate the RAL entity's entire portfolio, which is financed in a manner similar to REITs.
3. **Convert all public housing properties from the current subsidy to a property-based financeable approach.** This entails several steps at the same time. (a) Cancel the operating subsidy and modernization fund approach and replace it with property-based assistance akin to Section 8. (b) Cancel the current anachronistic regulatory covenant between HUD and the housing authority, which blocks all forms of financing, and allow housing



authorities to finance, reposition, or even sell existing public housing. (c) Deregulate housing authority operations and allow them to keep excess proceeds from property transactions. This effectively transforms the Rental Assistance Demonstration (RAD) from a voluntary pilot to the dominant method of funding legacy public housing.

4. **Replace current housing authority regulation with an accreditation system.**

Create a certification or minimum capacity standard (PHMAP or otherwise) for all owners (either using the Registered Affordable Landlord idea or for all owners regardless of profit status). Quantitatively score such owners annually by independent and disinterested reviewers, and publish the results. Mandate that all authorities that fall below a competency/capacity standard) divest themselves of operational and management control over their properties. The UK does this now for all its housing associations.

5. **Fund a national pilot/ study to test the long-term health benefits of better affordable housing.**

Create a longitudinal study to test whether quality affordable housing leads to better long-term health for the elderly through illness reduction and wellness improvements (i.e. decreased obesity, better nutrition, better mobility, less depression and isolation, fewer prescription medicines) that are predictors of reduced rates of falls, emergency room visits, hospitalizations, and nursing home admissions. Develop the evidentiary basis

to prove or disprove that preventive activities save money over an elderly person's lifespan, and which mix of wellness interventions maximizes an elderly person's long-term healthspan.

6. **Enable Medicaid to pay for health-related wellness services in elderly housing using a pay-for-success model.**

Expand the current §1115 Medicaid waiver program to pay for health-related interventions in existing properties (whether public housing or regulated affordable housing). These costs can include (a) common-area retrofits (light meals, home-health-aide offices and work stations), (b) interior retrofits (corridors, elevators), (c) in-apartment retrofits (stove knobs, bathtubs, door handles, lights), (d) wellness amenities both physical (light exercise equipment) and mental (in-building free wi-fi), and (e) in-building services (of the kind now arranged by service coordinators and provided by outside providers at no cost to the property). Use these to develop longitudinal aging and wellness studies.

7. **Create metropolitan or state-level consolidator owners** (deregulated at the individual property level) that can own legacy public housing, former §202's, old FmHA §515s, post-Year-15 LIHTC properties, and so on. Facilitate their acquisition of such properties with tax incentives, entity-level financing, and discretionary resources.



Eliminations

Though precision is desirable, complication is entropic, and our anonymous thinkers were unanimous that the pendulum has gone way too far toward theoretical precision and away from efficiency, so they want life to be simpler:

1. **Simplify all programs**, and accept there will be some programmatic collateral damage from that simplification. To do this, create a blue-ribbon commission, akin to the military's Base Realignment and Closure (BRAC) panels, that can propose a package of laws to eliminate – not modify, eliminate – which are then subject to an up-or-down vote.
2. **Drive consolidation among smaller owners** through a combination of minimum capacity standards, certifications, grant-maker priorities, and allocation scoring systems.

Commentary

Although each idea was independently generated and from an individual perspective, aside from the thematic clustering they show striking consistency around three big ideas:

- **Simplify.** America's affordable housing system is massively over-complex, because each new program created is an addition; no programs are ever eliminated (though a few are zero-funded), and there is no principle of hierarchy in rule administration (these supersede those). Complication for its own sake has run rampant when the largest single component of property management costs is compliance with

government regulations.

- **Consolidate**, both in entities (fewer more sophisticated ones are better than too many under-capacity entities), and in portfolios. As affordable housing has become more complicated, both in development and in ownership/management, the sophistication required of affordable housing entities has likewise increased. Sophistication requires scale and scale requires consolidation.
- **Develop cheaper and faster.** In highly urbanized environments – exactly the places where we have the greatest need for additional housing – we also have the most obstructive barriers to creating any new forms of affordable housing, and thus the longest lead times for the highest-cost new affordable homes and apartments. This self-defeating approach chokes off economic development, reduces labor mobility, enhances place-based economic discrimination, and raises housing prices.

Conclusion

As the Lord High Executioner (almost) commented, *If I should ever be called upon to act professionally, I am happy to think that there will be no difficulty in finding plenty of policies and programs whose loss will be a distinct gain to society at large.*

Politics may be the art of the possible; leadership is the art of making the right thing possible. Our industry needs less politics and more leadership.



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