PROPERTY TAXES

Property Tax Relief for Maintaining Affordable Rents

Strategy description

Property tax relief for current and potential owners of affordable multifamily rental properties can encourage its preservation as affordable housing. In exchange for property tax relief, owners make a long-term commitment to maintain units at affordable rent levels and/or to renovate affordable rental units. The tax relief can be in the form of reduced valuation of the property or a reduced tax rate.

Target population

The direct beneficiaries of this strategy are the owners of rental properties that experience a tax reduction.

The ultimate beneficiaries are the low- and moderate-income renters who are be able to pay lower rents because the owner's operating costs are reduced thanks to the reduced tax burdens.

How the strategy is administered

Property owners apply to the taxing agencies for the reduced property valuation and/or a reduced tax rate.

How the strategy is funded

Property taxes are generally administered at the local level, but may be subject to state laws (such as in Minnesota) that provide property tax relief. State legislative action is required to implement property tax relief that will apply to affordable housing statewide; local jurisdictions apply the appropriate assessed value or tax rate and collect the property taxes.

Extent of use of the strategy

Limited use.

Examples of locations where the strategy is being used

Minnesota[80] has a "4d" tax classification that provides a reduced tax rate of .75 percent for landlords who agreed to keep rents affordable to households at or below 60 percent of area median income (40 percent lower than the rate for market rate rental property).[81]

In several states including Alaska and Iowa, tax assessors value LIHTC properties using the statutorily mandated limited rents, rather than at market rents, thereby lowering the assessed value of the property and reducing the tax burden.

Pros and cons to using the strategy

Pros:

- Promotes the preservation of affordable rental housing.

Cons:

- Reduces tax revenues for the administering localities.

Sources of information about the strategy

- "Relief Found for Increasing Property Tax Burdens" Regulatory Barriers Clearinghouse website, updated October 2004: www.huduser.org/rbc/newsletter/vol2iss3more.html
- "Assessment and Classification Practices Report: Class 4d Low-Income Rental Housing," Property Tax Division, Minnesota Department of Revenue, February 26, 2007. Available at: www.taxes.state.mn.us/property/other_supporting_content/4d_report_final.pdf
- City of New York Department of Housing Preservation and Development website, Mayor's Office press release #307-03: www.nyc.gov/html/hpd/html/pr2003/mayors-release307-03-pr.shtml

Contact information

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Property Tax Relief for Developing Affordable Rental Housing

Strategy description

Tax abatements are used as incentives for constructing or rehabilitating affordable rental housing. For example, some jurisdictions encourage rehabilitation of older affordable properties by offering property tax abatement over a specific period (often 10 years) to owners who improve their properties and, in some cases, also agree to rent them at affordable levels. The abatement may freeze the property's assessed value at the current level for a period, tax the property at a lower rate during that time, or exempt the property entirely from property taxes. Similarly, some jurisdictions encourage affordable housing construction by providing tax abatements for a period of time on new apartments.

History of the strategy

New York City has been offering property tax abatements for newly constructed apartment buildings since 1971.

Target population

The strategy targets low- and moderate-income renters.

How the strategy is administered

This strategy can be administered in a number of ways. California provides property tax abatement for specific types of affordable housing projects; New York City issues negotiable tax-abatement certificates that can be bought and sold. Tax abatements can be applied city- or county-wide, or in a particular district.

How the strategy is funded

Property taxes are generally administered at the local level, but may be subject to state laws (such as in California) that provide property tax relief. State legislative action is required to implement property tax relief that will apply to affordable housing statewide. For local efforts to provide property tax relief, local government action (such as by the board of commissioners in Cook County) is required to pass an ordinance. In either case, local jurisdictions apply the appropriate assessed value or tax rate and collect the property taxes.

Extent of use of the strategy

Limited use.

Examples of locations where the strategy is being used

- Portland, OR has several tax abatement programs designed to promote transit-oriented development, rehabilitation of rental homes, construction or rehabilitation of owner-occupied homes in "opportunity areas," and nonprofit ownership of affordable rental units.
- Chicago has a special property tax classification designed to stimulate the construction and rehabilitation of affordable rental homes.[82]
- New York City's 421a program provides developers a partial tax exemption for new apartment buildings. In "exclusion zones," the units must meet an affordability standard to qualify for the tax abatement.
- In Richmond, VA owners of small multifamily residential properties undergoing substantial rehabilitation can request a partial tax exemption for the value of the rehabilitation.
- Many types of affordable housing developments in California qualify for property tax abatement under the Welfare Exemption of the California Revenue & Taxation Code Section 214(g).

Strategy results

- In Portland, OR, as of fiscal year 2004-2005, about 12,725 homes were receiving tax abatement under one of the city's various abatement programs.[83]
- More than 110,000 apartments – both affordable and market-rate – have been built under New York City's 421-a program over the last 36 years.[84]

Pros and cons to using the strategy

Pros:
- Provides strong incentives to developers and property owners to create or preserve maintain affordable housing.

Cons:
- Reduces tax revenues for the administering localities.

Sources of information about the strategy

- New York City website on the 421a program: www.nyc.gov/html/dof/html/property/property_tax_reduc_421_a.shtml
- Scott, Janny, "In Overhaul, City Seeks To Expand Lower-Cost Units," *New York Times*, December 21, 2006.
- Lubell, Jeffrey, "Increasing the Availability of Affordable Homes: A Handbook of High-Impact State and Local Solutions," prepared by the Center for Housing Policy, 2006. Available at: www.nhc.org/pdf/pub_hwf_solutions_01_07.pdf

- Lee, Randy. "421a tax abatement certificates: key financial resources for developers of affordable housing – Spotlight on Residential Real Estate." Real Estate Weekly, Feb. 24, 1999. Available at: http://findarticles.com/p/articles/mi_m3601/is_30_45/ai_54195260
- Hobson, Jason. "Significant Changes to California Property Tax Abatement Law for Affordable Housing Developments to be Considered by California Board of Equalization." Pillsbury Winthrop LLC Client Alert, Jan. 27, 2005. Available at: www.pwsp.com/content/portal/publications/2005/1/000051EE/Affordable%20Housing%20Vol%201801%20No%201801%2001-27-05.pdf
- Real Property Assessment Classification Ordinance, Cook County Assessor's Office, available at: http://www.cookcountyassessor.com/forms/ordinance2006.pdf

Contact information

City of New York
Department of Housing Preservation and Development
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New York, NY 10038
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Special Taxing Districts

Strategy description

Tax districts are quasi-governmental entities with distinct boundaries that may provide one or more public services, including funding for infrastructure projects. Funding for the districts typically comes from an annual tax surcharge applied to property owners within the district's boundaries.

Several types of tax districts provide public services that can reduce the cost of developing new housing. These include community development districts, real estate improvement districts, community facilities districts, and special improvement districts. Real estate improvement districts, in particular, are designed specifically for infrastructure development intended to lower directly the costs of developing housing.

History of the strategy

- Iowa, the only state to allow real estate improvement districts, passed its Special Districts statute in 2005.
- Other types of special districts have been in use much longer. For example, in 1976, the Hawaii state legislature created the Hawaii Community Development Authority to revitalize urban areas in the state in need of redevelopment and also designated the Kaka'ako area of Honolulu as the Authority's first community development district.

Target population

All residents of special districts benefit from the enhanced public services. Residents of real estate improvement districts benefit from reduced infrastructure costs for new residential construction; affordable units built using revenues from these districts provide additional benefits to low-income homebuyers and renters.

How the strategy is administered

- In order to form a real estate improvement or other special taxing district, owners of property in a geographic area to be designated as a district must file a petition requesting that the issue be put before the area's voters.
- Community development districts typically are administered by a community development authority composed of voting members from the private and public sectors who oversee the authority's operations and establish policies to implement its legislative objectives.

How the strategy is funded

Funding for infrastructure improvements and affordable housing development may come from a tax surcharge or a bond issuance to be repaid from future property tax assessments.

Extent of use of the strategy

Moderate use.

Examples of locations where the strategy is being used

- Iowa is the only state to have authorized real estate improvement districts, although it appears that no districts have been established.
- At least 11 states have authorized community development districts, including Hawaii and Arizona.
- Five states allow special districts to provide for infrastructure finance and development, including Iowa, Arizona, Florida, Colorado, and Texas.

Strategy results

In the community development district in the Kaka'ako area of Honolulu, the Hawaii Community Development Authority (HCDA) has created 1,388 affordable housing units.

Pros and cons to using the strategy

Pros:

- Reduces reliance on impact fees for new residential construction, improving affordability of housing generally.
- Increases accountability in public spending by tying activities to an explicit revenue source.

Cons:

- Requires the approval of the area's voters.
- May impose tax and other burdens on residents who might not be directly affected by the additional affordable housing or improvements.

Sources of information about the strategy

- Hawaii Community Development Authority Homepage. Available at: http://hcdaweb.org/
- *Infrastructure Solutions: Best Practices from Results-Oriented States*, National Association of Home Builders, 2007, p.4.
- *Land Development,* National Association of Home Builders, 2007, v20, n2, p. 9.

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Taxing Land and Buildings at Different Rates

Strategy description

A two-rate (or split-rate) property tax structure taxes land at a higher rate than buildings. Most U.S. localities currently apply one tax rate to both buildings and structures, leading to what some consider to be under-taxation of land and therefore speculation, private land banking, and sprawl. Higher land taxes and lower (or no) taxes on improvements encourage property maintenance and may reduce speculation and therefore land prices, improving the economic feasibility of affordable housing development.

History of the strategy

In the 19th century, political economist Henry George proposed a land value tax to eliminate land speculation and make more land available for production. The use of land value tax structures in the U.S. has been limited until the last few decades, when a number of Pennsylvania towns and cities began adopting two-rate or split-rate property tax structures, which are a version of a land value tax.[85]

Target population

Two-rate property taxes benefit homebuyers and renters generally, as these tax structures are intended to stabilize and reduce housing costs.

How the strategy is administered

State-level enabling legislation is necessary in most states to give municipalities the option to institute a two-rate property tax. Then municipalities can pass an ordinance adopting a two-rate property tax. For most homeowners, the change will result in a decrease in property taxes.

How the strategy is funded

If implementation of a two-rate property tax is designed to be revenue neutral, no funding is necessary.

Extent of use of the strategy

Limited use of two-rate property taxes; no pure land value tax systems in the U.S.

Examples of locations where the strategy is being used

- The Pittsburgh Improvement District uses a pure land value taxation as a surcharge on the regular property tax.
- 20 jurisdictions in Pennsylvania use a two-rate tax.

Strategy results

- Harrisburg, Penn. has taxed land at a rate six times that on improvements since 1975, and this policy is credited with reducing the number of vacant structures in downtown Harrisburg from about 4,200 in 1982 to less than 500.[86]
- Many small towns in Pennsylvania that use split-rate structures saw increased construction in their centers after implementing the tax.

Pros and cons to using the strategy

Pros:

- Under a revenue neutral change to a land value tax, homeowners and owners of rental housing would get a tax cut.
- Discourages land banking and speculation and encourages efficient and productive use of land.
- Encourages increased building in urban centers.[87]
- Reduces disincentives to revitalize marginal areas, helping to revive declining downtowns.

Cons:

- Difficult to persuade voters to adopt a change to a property tax system that may be difficult to explain.
- Likely to lower the value of undeveloped property because the higher property taxes will be capitalized into the value of the property.

Sources of information about the strategy

- Maryland Land Value Tax Project website: www.marylandlandtax.org/
- New Rules Project website, a project of the Institute for Local Self-Reliance: www.newrules.org/environment/landtax.html
- Center for the Study of Economics website, www.urbantools.org/.

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PENNSYLVANIA

TAXING LAND AND BUILDINGS AT DIFFERENT RATES

✓ Taxing land and buildings at different rates

In Pennsylvania, an arcane property tax structure is credited with helping revitalize communities, put vacant and underutilized land to use, and improve housing affordability, for both renters and homeowners.

The land value tax, also called a two-rate property tax and a split-rate property tax, is currently in use in 16 municipalities in Pennsylvania. A typical property tax assesses taxes on land and the improvements on the land at the same rate. In contrast, land value taxation places a higher tax on land while reducing or eliminating the tax on improvements.

Henry George, a late-19th century economist, advocated the idea of taxing land in the interest of fairness. He believed that an increase in the "natural value" of land (or the unimproved value) is unearned, making landowners speculators. Therefore, he believed taxing this value would not affect productivity. Similarly, proponents of the land value tax today believe that taxes on the improvements on land place the tax burden on those who generate economic growth.

Land value taxes may improve housing affordability and revitalize declining cities

The Center for the Study of Economics, a Philadelphia-based nonprofit started in 1980, advocates for land value taxes in communities around the country. Joshua Vincent, the Center's executive director, explained that a land value tax implemented to be revenue neutral (to leave overall property tax revenues unaffected) improves housing affordability in two ways.

First, it reduces property taxes for most homeowners. "Most people getting a first house don't take advantage of benefits to homeownership, like the mortgage deduction, because their incomes aren't high enough [to itemize and claim the mortgage deduction]," Vincent said. In contrast to the mortgage deduction, reducing property taxes for homeowners improves affordability regardless of income.

Second, Vincent describes a land value tax as a "stick" that encourages development by increasing the expense of holding vacant or underutilized land. The land value tax encourages denser development, because unlike a property tax that assesses land and improvements at the same rate, there is no disincentive to develop the property. This includes denser residential development, which can be more affordable than new construction on large lots.

"This flips the script by punishing disinvestment and rewarding investment," said Vincent. However, for a land value tax to have an impact on development in a community, Vincent says the tax on land must be at least five times higher than the tax on buildings.

> ***"This flips the script by punishing disinvestment and rewarding investment."***
>
> -Joshua Vincent

For example, Harrisburg, PA, had a moribund downtown when the land value tax was first implemented in 1975. The tax on land was about twice the rate of the tax on buildings until 1982, when one observer ranked Harrisburg the second most distressed city in the country. The tax on land was increased incrementally until it was six times the tax on buildings, where it remains. Since then, there has been an 85 percent reduction in the number of vacant properties, and there were 3.5 times the number of businesses on Harrisburg's tax rolls in 2003 as there had been in the early 1980s.[88]

Vincent cautions that a land value tax does not work quickly: "It generally takes five to ten years to see results," he said.

Communities with vacant and underutilized property are ideal candidates for a land value tax

The Center for the Study of Economics conducts research on the land value tax and assists communities interested in implementing the tax. Once the tax is in place, the land value tax is not administratively complicated. "Towns of 6,000 people – they manage to implement it," he said.

According to Vincent, the best candidates for a land value tax are communities with high numbers of substandard housing units and buildings and vacant or underutilized lots. "If there's an abundance of these, that's an indicator that we should implement a land value tax," he said. In addition, the tax should result in property tax savings for most residential parcel owners.

Savings to homeowners on property tax bills vary widely by community. Vincent says the highest savings to homeowners are in communities with high building values relative to land values. In general, he said homeowners can expect to save about 25 to 40 percent annually on their property taxes.

Of course not every property owner is better off under a land value tax. In Philadelphia, Vincent says opposition to the tax is led by parking lot owners. Other types of commercial property, such as gas stations and convenience stores, which are more land intensive than building intensive, also pay higher taxes.

Adopting a land value tax can be controversial

A typical approach to evaluating whether a land value tax will work in a community involves calculating the change in property taxes for each parcel in the community and providing an assessment of the revenue impact for the city and each parcel. "The city looks at the implications: if they see that our productive citizens, those keeping up their property, will be rewarded, they adjust the property tax ordinance," said Vincent.

Vincent says adoption of a land value tax is often done quietly, without much community outreach or involvement. Although voters aren't typically involved in adoption of the land value tax, Allentown, PA, provides evidence that voters can enthusiastically support an issue that can be difficult to explain. In Allentown, after contentious debate and a great deal of lobbying by opponents, a land value tax ordinance on the ballot passed with 60 percent of the vote in 1996. An effort to repeal the tax about a year later, led by a small number of commercial landowners including owners of a large fairground in the city center, was overturned.[89]

However, a significant challenge to organizing support for a land value tax is that the relatively few property owners who will face substantially higher bills as a result of the tax are typically better organized than individual homeowners, who do not have as much at stake financially.

To date, the Center for the Study of Economics has focused its efforts in Pennsylvania. "Now we're trying to spread the word elsewhere," said Vincent. The big island of Hawaii also uses a land value tax, but most states do not have enabling legislation authorizing municipalities to implement a land value tax.

Vincent expects state enabling legislation to be introduced in Connecticut, New York, Minnesota, and possibly Indiana during the next legislative year.

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OTHER TAXES

Land Gain Taxes

Strategy description

A land gain (or speculation) tax is a graduated tax on the profit between the sale and resale of the same house or building. The tax rate depends on the period of time that the land is held, with shorter holding periods and higher profits subject to higher tax rates. The strategy is intended to prevent the rapid "flipping" of real estate for a quick profit and instead to encourage long-term ownership. The tax also is intended to return to the community a significant portion of the short-term gains made by the rapid turnover of real estate. By discouraging speculation, these graduated taxes may reduce the land costs of affordable housing.[90]

History of the strategy

In the 1970s, the state of Vermont adopted a graduated tax on the profits from land sold within six years of purchase in response to concern raised about the effects of rapid increases in land prices, particularly in rural areas. The tax applies to the value of land, not buildings.

Target population

Direct Impact:

- The tax creates a funding stream that can be used to fund low-income housing.

Indirect Impact:

- Discouraging speculation benefits buyers and renters generally by making increases in property prices steadier and more likely to reflect current local economic conditions.

How the strategy is administered

State legislation is required to adopt a land gain tax, which is collected by the state tax department.

How the strategy is funded

No need for funding other than ensuring proper enforcement of the tax.

Extent of use of the strategy

Limited use

Examples of locations where the strategy is being used

- While considered in a number of states (Rhode Island, Hawaii, and Virginia), a land gain tax is currently only used in Vermont.
- A bill was proposed in the Hawaii state Legislature in the spring of 2007 that would add a new tax to the existing capital gains tax on sales of real estate. Homeowners selling their property within 6 months of its purchase would be taxed 60 percent on capital gains; 30

percent on capital gains between 6 and 12 months of ownership; and 15 percent on capital gains between one and two years of ownership. The bill would go into effect in January 2008 if passed.

Strategy results

As of 2005, the tax in Vermont was raising nearly $4 million annually, a significant increase from the $500,000 it had been generating only a few years prior.

Pros and cons to using the strategy

Pros:

- Decreased fluctuation in rents may reduce displacement of renters.
- The housing market will better reflect current incomes of the local population.
- Provides a possible dedicated source of funding for affordable housing.
- May slow inflation of housing prices.

Cons:

- Legislation must be written carefully to avoid unintended consequences for affordable housing developers, owner-occupants, and others.

Sources of information about the strategy

- Text of Vermont Statute Title 32, Chapter 236: Tax on Gains from the Sale or Exchange of Land: http://michie.lexisnexis.com/vermont/lpext.dll?f=templates&fn=main-h.htm&cp=
- *Institute of Community Economics* publication, Harmon, Tasha, "Integrating Social Equity and Smart Growth: An Overview of Tools," 2004. Available at: http://content.knowledgeplex.org/kp2/cache/documents/98054.pdf
- *Star Bulletin* news item about proposed bill in Hawaii state legislature: http://starbulletin.com/2007/03/17/business/story01.html
- Discussion of proposal to implement tax in Rhode Island and descriptions of Vermont's law in the *Rhode Island Policy Reporter*, http://whatcheer.net/ripr/ripr23.pdf and http://whatcheer.net/index.cgi/2005/11/

Contact information

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Demolition Taxes

Strategy description

A tax is levied upon demolition in order to promote the preservation or creation of affordable housing. The demolition tax only applies to residential demolitions, and is only in effect with the removal of more than 50 percent of an existing structure.

Target population

Demolition taxes are sometimes used to provide revenue to a housing trust fund that creates housing targeted to low- and moderate-income renters and homebuyers. It may also help preserve the diversity of a community's housing stock, benefiting the community generally.

How the strategy is administered

Typically administered by the city's Building Division; payment is required prior to issuance of a demolition permit. Exceptions may be granted to property owners who are replacing their house if they occupy it for a specified length of time (often three years).

How the strategy is funded

No funding is necessary.

Extent of use of the strategy

Limited use.

Examples of locations where the strategy is being used

- The city of Highland Park, IL levies a $10,000 demolition tax on residential property; exceptions include property owners who have resided in the property for five years or who sign covenants agreeing to remain in the property for five years after the new house is built. Revenues are largely dedicated to the city's housing trust fund (see case study).
- Lake Forest, IL enacted a $10,000 demolition tax on residential property in February 2006. Half of the revenue is dedicated to an affordable housing trust fund; the other half is allocated to the city's general fund.
- Evanston, IL also has a $10,000 demolition tax on residential property that has been in effect since 1998. The tax generates about $60,000 per year for the city's affordable housing initiatives.

Strategy results

Highland Park's demolition tax raised about $1 million for the city's affordable housing trust fund over the last four years.

Pros and cons to using the strategy and/or types of markets where the strategy is more or less effective

Demolition taxes are effective primarily in strong and gentrifying markets, where modest homes are being torn down and replaced with larger homes. They are less effective in distressed areas, because the tax is a disincentive to revitalization.

Pros:

- Provides a source of revenue for the city and/or a housing trust fund.
- May help maintain a diverse housing stock in a gentrifying area.

Cons:

- Likely to face opposition by property owners.

Sources of information about the strategy

- City of Highland Park Affordable Housing Demolition Tax, June 2006, available at: www.cityhpil.com/pdf/commissions/housing_demoTax.pdf
- "Affordable Housing Toolkit for Communities in the Chicago Region," Business and Professional People for the Public Interest, undated. Available at: www.bpichicago.org/documents/RegionalToolKit.pdf
- Lake Forest Demolition Tax, available at: http://metroplanning.org/homegrown/fin_lf_demotax.pdf
- Evanston Affordable Housing Demolition Tax, available at: http://metroplanning.org/homegrown/fin_ev_demoTax.pdf

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HIGHLAND PARK, ILLINOIS

- ✓ Housing trust funds
- ✓ Community land trust
- ✓ Inclusionary zoning
- ✓ Demolition taxes
- ✓ Profit-nonprofit partnerships
- ✓ Creative public-private collaborations

Highland Park, IL is one of the more expensive and high-income areas in the country, and might seem an unlikely candidate to encourage and implement affordable housing strategies. The median home price for new single family homes is about $1.2 million.

Nevertheless, years of commitment to maintaining a stock of affordable housing have enabled Highland Park to emerge as leader in the affordable housing arena. The city's accomplishments have been achieved through an array of strategies including demolition taxes, employer-assisted housing, green building, a flexible inclusionary zoning ordinance, and the establishment of a housing trust fund and a community land trust.

Highland Park has a long history of promoting affordable housing

Highland Park's focus on creating a diverse community that includes affordable housing dates to the 1870s, when the Highland Park Building Company began constructing homes of varied sizes and affordable rental units near the central business district. The establishment of the city's Housing Commission in 1973, which remains one of the city's strongest affordable housing proponents, sought to further address the need for affordable housing in the community. With input from the Housing Commission, the 1976 and 1997 city master plans both committed to promoting and increasing affordable housing opportunities, in a large part through early inclusionary zoning ordinances.[91]

Despite the city's initial efforts to prioritize affordable housing, an assessment in the late 1990s demonstrated a clear loss in affordable units over the previous two decades as a result of teardowns, the increased cost of new housing, and a depleted supply of developable land.[92] In response, the city initiated a joint task force in 1998, which, through significant community outreach and input from developers and other stakeholders, developed a solution. The four cornerstones of the most recent Affordable Housing Plan include:

- Revised inclusionary zoning ordinances;
- Establishing a housing trust fund to be funded in part by a demolition tax;
- Creation of the Highland Park Community Land Trust; and
- An employer assisted housing component.

Flexibility is key to the success of Highland Park's inclusionary zoning ordinance

The city's inclusionary zoning ordinance is both flexible and caters to the needs of developers to the extent possible. Michael Blue, director of community development for the City of Highland Park, emphasizes that flexibility has been the ordinance's greatest asset, as no two developers ever approach a project in the same way. "If [inclusionary zoning] is always black and white, it makes it much more difficult for a plan to work," he said.

> ***"If [inclusionary zoning] is always black and white, it makes it much more difficult for a plan to work."***
>
> -Michael Blue

Regulated developments with five or more units are required to set aside 20 percent of units as affordable, and the ordinance applies to new construction projects, renovations of multi-family developments that increase the number of dwelling units, and changes in the use of property from non-residential to residential or condo conversion.[93] Developers are rewarded for such developments with a one for one density bonus. An additional density bonus is offered for planned unit development (PUD), of up to 0.5 market rate units for each affordable unit to a maximum of 1.5 bonus units.

The flexibility of the ordinance comes in the construction of the affordable and market-rate units. The market rate and affordable units need not be identical, but they must be visually indistinguishable, contain the same number of bedrooms, possess gross floor areas within 75 percent of each other, and meet the same energy efficiency standards.[94]

Developers are also offered alternatives to on-site construction of affordable units. Developers of single-family projects with fewer than 20 units can make an in-lieu development cash payment of $100,000 per affordable unit by right; developers of projects with more than 20 units may appeal to the City Council for approval of an in-lieu payment, may dedicate land to the Housing Commission, or may provide off-site units. The in-lieu revenue is dedicated to the city's Housing Trust Fund, although only one developer so far has elected the in-lieu option, having opted to build two affordable units and pay the fee for the third required unit.

Incentives offered by the city to help offset the cost of the affordable units include a $10,000 impact fee waiver for these units as well as demolition permit fee and demolition tax waivers.

One of the largest developments the city has seen in a long time is currently underway, consisting of 42 units, including 30 townhomes and 12 condos. The 20 percent inclusionary requirement will generate seven affordable units, including five condos and two townhomes. The relatively high share of condos that are affordable relative to townhomes is one way the city provided the developer some flexibility in satisfying the requirement.

Housing trust fund provides key financing element

The city's housing trust fund (HTF), established in 2002, has also been a key element in providing affordable housing opportunities. The Fund's primary funding sources come from a $10,000 per teardown demolition tax, a $550 demolition permit fee, and other city sources such as a recent $1 million refinance of a local senior housing property. According to Blue, Highland Park averages about 50 teardowns per year, which have generated over $1 million over last four years in demolition tax revenue for the HTF.

Since its inception, the HTF has spent between $1.8 and $2 million for affordable housing purposes, the majority ($1.3 million) going to the community land trust (described below) to help it purchase land for the eventual development of affordable homes. An additional $50,000 has been set aside as matching funds for the city's still developing employer-assisted housing program.

CLT's multi-functional role is crucial to Highland Park's affordable housing success

Highland Park's community land trust was also established in 2001 to provide a long-term solution to the city's affordable housing needs. The CLT's initial role was to assist in the management of the newly implemented inclusionary zoning ordinance, including finding buyers for affordable inclusionary units.

Its primary functions now include providing technical capacity to builders, nonprofits, and other key affordable housing stakeholders; developing inventories of homes to remain affordable over the long term; and maximizing public investment. The CLT purchases and rehabilitates properties to sell as affordable units. It also uses grants to write down the price of properties on which it maintains deed restrictions. The maximum household income for buyers of CLT-financed properties is 115 percent of the area median income (AMI), although former CLT executive director Mary Ellen Tamasy notes that this can vary from project to project, and that the average is closer to 100 percent AMI. For rental properties, qualified renters have incomes closer to 80 percent of AMI. While anyone can apply who meets income qualifications, the CLT gives priority to those who live or work in Highland Park.

Laurel Court is a new 15-unit development that includes two affordable units.

The CLT's operational funding comes primarily from the HTF; however, it also receives direct donations and foundation grants. Funding for specific projects comes from a much greater variety of sources, including the HTF, bank loans, the Lake

County affordable housing fund, the Illinois Development Authority, the state donation tax credit, and the Federal Home Loan Bank.

To date, the CLT has created 13 affordable units, including six townhomes, five single- family detached homes, and two condos.

Partnerships are essential to the CLT's success

Some of the units created by the CLT were the result of a partnership between the CLT and a for-profit builder who initially acquired a foreclosed site. The CLT pieced together the financing for the Temple Unit Townhomes project, which included grants from the city and the county, money from the community development block grant, and a number of other sources. Appraised at $292,000 per unit, the CLT was able to subsidize $132,000 of the price and sell each unit for $160,000.

The CLT's current focus is a 14-unit townhome/apartment development at 500 Hyacinth Place, which includes both rental and for sale properties, all of which will be affordable.

The Hyacinth project also highlights the key role that partnerships play in the community's ability to generate affordable housing. The property was originally acquired by the HTF and donated to the CLT. Since then, the CLT has been working on the project with Brinshore Development, a local for-profit development company, and a nonprofit, the Housing Opportunity Development Corporation. Brinshore Development is guaranteeing loans and providing technical expertise; the Housing Opportunity Development Corporation is applying for public funding sources and managing the property

Highland Park's agenda for the road ahead

Highland Park's employer-assisted housing (EAH) component is still very much a work in progress, but the city is hopeful that it will both further expand affordable housing opportunities and build a stronger local workforce that is more connected to the community. The plan was devised from research done by the Housing Commission subcommittee on existing local and national EAH models. When the program is launched, eligible EAH activities will include downpayment and closing cost assistance, reduced interest mortgages, rental subsidies, and security deposit assistance.

Although green building is not directly tied to affordable housing in Highland Park, it is nevertheless a significant piece of their overall approach and has the potential to play an increasingly important role in improving long term affordability for Highland Park residents. The Hyacinth project currently underway will be powered in part by a wind turbine and geothermal heating, among other green features.

Lessons learned: "There is no silver bullet"

According to Blue, one of the most important lessons he and the rest of the community have learned through this process is the importance of customizing any affordable housing approach to meet the needs of the community. "There is no silver bullet," says Blue.

> *"There is no silver bullet."*
>
> -Michael Blue

One crucial component in devising a housing plan is obtaining input from the people affected by it. Before approving the Affordable Housing Plan, the Highland Park Commission conducted outreach to developers and other key community members. Their input was incorporated into all of the plan's strategic components. Blue says maintaining flexibility in the plan is also important, and it must be adapted to the inevitable changes the community will face over time.

The success of Highland Park's Affordable Housing Plan has received substantial recognition, having won various National APA and state awards. Locally, its adoption is being considered in a number of neighboring communities, paving the way for potential subregional implementation. "We are evangelizing this plan all over the country," Blue said.

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STATE TAX CREDITS

Tax Credits for Donations to Affordable Rental Housing Projects

Strategy description

State charitable tax credits provide tax credits to charitable donors (individuals or corporations) that donate money to affordable rental housing projects that are developed by non-profit developers. The donor receives an approved, one-time credit and the donation provides equity for the project. While there is some variation in the specific tax credit percentage allocated between different state programs, a tax credit valued at 50 percent of the contribution is most commonly used. In some states the program is limited to properties that also receive LIHTC allocations.

Target population

The direct beneficiaries are the non-profit developers of affordable housing projects that receive the donations. The ultimate beneficiaries are low-income renters who have access to the additional affordable units developed through the program. In some cases the target population is households with incomes below 80 percent of area median, and in others the target is households with incomes below 60 percent of area median.

How the strategy is administered

The state tax credits typically are administered by the state housing finance agencies. Donors apply for credits, which are capped at different levels in each state (ranging from abut $1 million to $13 million per year per state).

How the strategy is funded

The strategy is a state tax credit, which means that the state forgoes revenue in order to promote affordable housing.

Extent of use of the strategy

The strategy is being used by a number of states.

Examples of locations where the strategy is being used

- Illinois' Affordable Housing Tax Credit allows individuals or organizations to give donations to non-profit housing developers. The tax credit is worth 50 cents per dollar donated.
- Missouri's Affordable Housing Assistance Program provides about $11 million in tax credits annually. Of this, $10 million is allocated for Production credits for donations to construction, rehabilitation, and rental assistance activities. The remaining $1 million is for donations that help fund the operating costs of the non-profit organization.

- Maryland's Community Investment Tax Credit Program allows businesses to support a wide range of community projects including affordable housing. Businesses donating to qualified nonprofits receive state tax credits equal to 50 percent of the value of their contributions. The state authorizes $1 million in tax credits annually for the program.

Strategy results

Missouri's Charitable Tax Credit funded about 1,250 affordable housing units in 2002.

Pros and cons to using the strategy

Pros:

- Brings in private contributions for affordable housing.
- Can be combined with existing housing programs to reduce the debt and, therefore, the rent levels needed to support the project (federal LIHTC, or state-financed programs).
- Flexible in terms of the types of contributions that can be made (can be cash or in-kind contributions such as land).
- Donations also generally qualify for federal income tax deductions, providing an additional incentive to donors.

Cons:

- The state forgoes some tax revenues.

Sources of information about the strategy

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- "Missouri Affordable Housing Assistance Program," Missouri Housing Development Commission website, http://www.mhdc.com/rental_production/ahap/

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State Tax Credits for Investments in Affordable Rental Housing

Strategy description

Tax-based incentives from local and state governments include tax credits for state tax liability to developers of affordable rental housing. The developer sells the credits, usually through a syndicator, to an investor who gains an ownership stake in the project. The sales value of the credits provides equity for the project. State tax credits are sometimes used with federal Low Income Housing Tax Credits.

History of the strategy

Most state tax credits for affordable housing are modeled after the federal Low Income Housing Tax Credit, which was created by the Tax Reform Act of 1986.

Target population

Investment tax credits are generally targeted to rental housing for households with incomes below 80 percent of the area median income. In some states, part or all of the credits are reserved for housing affordable to households with incomes below 60 percent or 50 percent.

How the strategy is administered

Administration is often identical to administration for the federal Low Income Housing Tax Credit program. In general, developers apply to a state agency for an allocation of the available tax credits for that year. Successful applicants must obtain the additional financing needed, meet milestones for placing the units into service, and comply with rules governing maximum rents that may be charged for the units and the income levels of the families and individuals who move into the units.

How the strategy is funded

Tax credits represent foregone revenue for the state and as such either constraint other spending or must be made up with higher fees or taxes from other sources.

Extent of use of the strategy

Moderate use: at least eight states have a housing investment tax credit.

Examples of locations where the strategy is being used95

- Under California's Investment Tax Credit, projects approved for the federal Low Income Housing Tax Credit are also allocated state tax credits. In 2005, California had $70 million in state tax credits available, more than the $67 million in federal tax credits available that year.

- Massachusetts' Low Income Housing Tax Credit program has provides about $20 million in tax credits each year since 2001. State credits generally reduce the amount of federal Low Income Housing Tax Credits awarded to a project.
- Tennessee has a community investment tax credit for the promotion of affordable housing opportunities and small business lending.
- Other states include Hawaii, New Jersey, Oregon, Utah, and Missouri

Strategy results

- Massachusetts' credits have been used to create more than 1,800 housing units since 2000, more than 1,100 of which are affordable.
- Missouri's State Low Income Housing Tax Credits funded 1,256 units in 2002, at a cost to the state of about $78,000 per unit.[96]

Pros and cons to using the strategy

Pros:

- An indirect method of funding affordable housing investment can be more politically palatable than making direct expenditures.

Cons:

- State tax credits are not an entirely efficient mechanism for funding affordable housing because of their impact on the recipients' federal taxes. Because state taxes reduce federally taxed income, reducing state tax liability increases federal tax liability, typically by 35 percent for corporations. As a result, $1 in foregone state revenue results in less than $1 (and no more than about $.65) in affordable housing investment.
- The ability to transfer credits by selling equity to investors other than the housing developer increases their flexibility and value. However, state tax credits that can be sold sell for significantly less than federal tax credits, probably because the market is thinner and credits must be sold to another taxpayer in the same state.
- The process of obtaining tax credits typically is lengthy and bureaucratic. .
- The fixed expenses of obtaining and selling the tax credits can be high, precluding small projects from using them.

Sources of information about the strategy

- Listoken, David, and Kristen Crossney, "Best Practices for Effecting the Rehabilitation of Affordable Housing," Volume 1 Part 3: Resource Guide and Literature Guide, September 2006, available at: www.huduser.org/publications/affhsg/bestpractices.html
- Tennessee Housing Development Agency, Community Investment Tax Credit website: www.thda.org/Programs/commpro/citc/citccvr.html
- The Massachusetts Low Income Housing Tax Credit Program regulations, www.mass.gov/dhcd/components/housdev/want/dvlper_r/StateCredit.pdf

- Oregon Affordable Housing Tax Credit Program: Program Factsheet, available at: www.oregon.gov/OHCS/HD/HRS/pdfs/HRS_Factsheet_Oregon_Affordable_Housing_Tax_Credit_Program.pdf

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State Historic Tax Credits

Strategy description

Historic tax credits are provided to developers who rehabilitate historic buildings, complying with standards of historic preservation. Historic tax credits are not necessarily linked with affordable housing, but some states reserve a portion of historic tax credits for projects containing affordable housing. In addition, state historic tax credits are also sometimes used in combination with the federal Low Income Housing Tax Credit program. Even in states where tax credits are not explicitly linked to affordable housing, historic tax credits are often an important source of subsidy for rehabilitating affordable housing.

History of the strategy

State historic tax credit programs generally are modeled after federal Historic Preservation Tax Incentives, which were enacted in 1976. States began implementing similar programs in the early 1990s.

Target population

State tax credits for historic preservation generally are targeted to historically significant buildings and sometimes are limited to targeted areas.

How the strategy is administered

A state agency, such as the Massachusetts Historical Commission, administers selection criteria for projects applying for tax credits, allocating the credits available annually among qualifying projects that provide the most public benefit. Projects must be certified and overseen to ensure that tax credits are used for qualified rehabilitation expenditures.

How the strategy is funded

Tax credits represent foregone revenue for the state and as such either constrain other spending or must be made up with higher fees or taxes from other sources.

Extent of use of the strategy

State historic tax credits are widely used; those directly linked with affordable housing are in limited use.

Examples of locations where the strategy is being used

- About 25 states have a state historic tax credit. In general, states that award tax credits to income-producing properties (such as multifamily rental property) are more likely to improve the affordability of housing than those that are intended primarily for owners of private residences.

- In Massachusetts, at least 25 percent of tax credits must be awarded to projects that contain affordable housing.
- The Rhode Island Historic Preservation Investment Tax Credit Program provides a credit for 30 percent of the "qualified rehabilitation expenses," and can be combined with the federal Historic Rehabilitation Tax Credit, which covers 20 percent of expenses.

Strategy results

Although the tax credit is not directly linked to affordable housing, a study of the economic impacts of Rhode Island's Historic Tax Credit found that, of 1,699 residential units created in the 111 projects analyzed, 409 are designated as affordable to people of modest means. The state cost of the tax credit is about $1.3 million per project.[97]

Pros and cons to using the strategy

Pros:

- State historic tax credits can often be used with other tax credits, such as the federal Low Income Housing Tax Credit and the federal Historic Tax Credit. The combination of subsidies may allow units created to be affordable to low-income households at lower rents than would have been possible with only one source of subsidy.

Cons:

- Most state historic tax credits are used for purposes other than affordable housing.

Sources of information about the strategy

- Listoken, David, and Kristen Crossney, "Best Practices for Effecting the Rehabilitation of Affordable Housing," Volume 1 Part 3: Resource Guide and Literature Guide, September 2006, available at: www.huduser.org/publications/affhsg/bestpractices.html
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- Massachusetts regulations for the State Historic Tax Credit, available at; www.sec.state.ma.us/mhc/mhcpdf/830%20CMR%2063.pdf

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www.sec.state.ma.us/mhc/mhcidx.htm

Tax-Linked Bonuses

Strategy description

Tax-linked bonuses are one-time grants from a state to a non-profit affordable housing developer seeking gap funding for a specific project. As the project has no tax liability, the bonus provides the project with a grant to be used for equity. Funding is direct from the state to the project, but the bonus is implemented through the state income tax system.

History of the strategy

See below.

Target population

This strategy is ultimately targeted at those seeking affordable rental housing, particularly in the lower income neighborhoods, as a higher bonus is given to developments in those communities. The direct beneficiaries of the strategy are the developers whose projects receive the bonuses from the state.

How the strategy is administered

This strategy is administered through the State Housing Agency in exactly the same way as the LIHTC, and is calculated using the same financial process. The State Department of Revenue gives a check to the project, which may be used as a grant or is transferred to the State Housing Finance Agency to be administered as a loan.

How the strategy is funded

This strategy is funded through federal and state funds.

Extent of use of the strategy

Very limited use

Examples of locations where the strategy is being used

- This strategy is currently only being used in North Carolina, where it is only applicable to projects that are LIHTC-sponsored. The State provides eligible projects with a bonus check that can be claimed directly by the project or transferred to the NC Housing Finance Agency, which then lends it to the project. The value of the credit is 10, 20, or 30% of the developer's eligible base, which includes the sum of all depreciable construction costs. The percentage given depends on whether the location of the project is in a High, Moderate, or Low Income county.
- Minnesota has done research on this strategy and has considered its implementation.

Strategy results

In 2003, the first year of the strategy's implementation in North Carolina, the state funded 2,441 units, totaling $35,451,241. The average expenditure per unit was $14,500 in 2003. Overall, this strategy provides the majority of state affordable housing funding.

Pros and cons to using the strategy

Pros:

- Very easily administered and legally simple because it does not involve outside investors.
- Highly efficient, in that every $1 of public money spent under the program is used for affordable housing.
- Projects are held to strict levels of financial feasibility, project design, developer capacity, and monitoring.

Cons:

- Legal costs do exist, although they are minimal.
- Use is currently restricted to LIHTC-eligible projects.

Sources of information about the strategy

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- North Carolina Housing Finance Agency homepage: www.nchfa.com
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NORTH CAROLINA

- ✓ Tax-linked bonuses
- ✓ Housing trust funds

A number of states, including Minnesota, Oregon, California, North Carolina, Missouri, and New Jersey, offer state tax credits for affordable housing. Of these, North Carolina's goes the farthest in the amount of affordable housing per state dollar of tax expenditure.

A typical state tax credit is very similar to the federal Low Income Housing Tax Credit. Developers of affordable housing receive an allocation of tax credits, which are sold through a syndicator to investors who want to reduce their tax liability. The money raised through the sale of the tax credits is used as the developers' equity in the project. Inefficiency arises through the administrative costs of selling the tax credits, the impact of changes in state tax liability on federal taxes, and in the level of demand for state tax credits.

Although federal tax credits sell to investors for almost $1 for each $1 of the government's foregone tax revenue, these typical state tax credits sell for much less. In addition to limited demand for the credits, the price of state tax credits reflects the fact that they increase federal fax liability. State taxes reduce federally taxed income, so reducing state tax liability increases federal tax liability, typically by 35 percent for corporations. As a result, $1 in foregone state revenue results in $.65 in affordable housing investment at best, and in some states much less.[98]

North Carolina's tax credit (called a tax-linked bonus) is structured in a way that avoids these inefficiencies. Similar to the federal Earned Income Tax Credit, the program provides a subsidy through a refundable tax credit that returns funds to taxpayers, even if they do not have any tax liability. The owner of a tax-credit project, either a limited liability company or a limited partnership, claims the credit. Since these pass-through entities inherently have no income tax liability, the full amount of the credit is refunded. Owners transfer the right to this refund to the North Carolina Housing Finance Agency (NCHFA), which then makes a loan to the project in the same amount.[99]

North Carolina's state tax credits can only be used for projects that are allocated federal Low Income Housing Tax Credits. Almost all LIHTC projects (over 90 percent) also use the state tax credit, which is set at 10, 20, or 30 percent of the development's eligible basis, depending on whether it is in a high-, moderate, or low-income county. On average, state tax credits contribute about $16,000 per affordable unit.

Because state tax credits must be used with the federal LIHTC, the amount of state tax credits in any year is limited by the state's federal tax credit ceiling. As a tax credit, however, it is not subject to the state's annual appropriation process.

According to Mark Shelburne, NCHFA's counsel and policy coordinator, the state tax credit is very well distributed across high-, medium-, and low-income areas of the state. In addition to the LIHTC, the state tax credit is also often used in combination with federal HOME funds or money from the state's housing trust fund.

Shelburne says legislative approval of North Carolina's tax-linked bonus in 2002 was the result of an unusual alignment of political will in favor of affordable housing. He said the affordable housing community "Had the 'perfect storm' of an alignment of forces in our favor."

Like other states, North Carolina's affordable housing tax credit was initially also very similar to the federal LIHTC. The original state tax credit, implemented in 1999, was initially successful, but the pool of investors was extremely limited—they had to have both significant state tax liability and familiarity with affordable housing and tax shelter investing.[100] After two years, these institutions had reached the limit of their need to offset state taxes, and according to Shelburne, the value of the state tax credits would have been reduced to zero. As a result, most LIHTC projects in the works, which also relied on the state tax credit, would have unexpected large financing gaps, making them financially infeasible, and future projects would have more debt and higher rents.

Shelburne says this funding crisis was one critical component of getting a more efficient affordable housing funding mechanism. The second was determination and a close working relationship between the NCHFA, the Department of Revenue, and key legislators, and the third was a good argument.

"We were able to show how to save money and increase the subsidy [to affordable housing projects]," said Shelburne. The relationships were equally important: "Just having a compelling case isn't enough to make something happen legislatively," cautions Shelburne.

According to Shelburne, the tax-linked bonus does three things. First, it allows properties to be funded in rural areas, which was one of the initial goals of the tax credit. "Otherwise, it's hard to make federal tax credit projects work – [rural areas] have such low rents," said Shelburne.

Second, in urban areas, the tax credit allows deeper subsidies than would otherwise be possible. Because of the state tax credit, about one-quarter of units in high-income counties are affordable to households with incomes of 30 percent of the area median income.

Third, the tax credit allows 10 percent of units to be set aside for people with disabilities, who often have extremely low incomes. These units are given an operating subsidy by the state through the Key Program, which makes up the difference between what disabled residents can afford and the operating costs of the unit. In addition, owners partner with local human services agencies to provide placement, supportive, and other services to disabled tenants.[101]

In all of these situations the result is housing that is more affordable for low-income renters.

Although a number of other states have investigated North Carolina's tax-linked bonus, none has adopted it. One reason is that states with an existing affordable housing tax credit risk the possibility that their state legislature might eliminate the credit altogether rather than passing the legislation necessary to switch to a tax-linked bonus. North Carolina had an existing affordable housing tax credit before converting to a tax-linked bonus, but was fortunate during the legislative approval process that essential stakeholders did not advocate for its elimination. Importantly, the state's Department of Revenue was convinced that the tax credit was valuable, and supported the switch to the tax-linked bonus.

> ***"We might not have made the change if we were not backed into a corner."***
>
> -Mark Shelburne

Still, "We might not have made the change if we were not backed into a corner," said Shelburne. "We wouldn't have done it but we had nothing to lose. Other states still have something to lose, even if it's $.20 on the dollar."

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IMPACT FEES

Impact Fee Waivers and Reductions

Strategy description

Impact fees can make affordable housing development economically infeasible. To address this obstacle, some municipalities provide impact fee waivers for affordable housing units. Developers typically are required to apply for an impact fee waiver prior to construction. In some places, impact fees are deferred until the property changes ownership or no longer qualifies as affordable, at which point the fees must be paid. Alternatively, some jurisdictions change the full impact fee but allocate funds for forgivable second mortgages to cover the costs of impact fees for qualifying households.

Many municipalities charge impact fees that disadvantage multifamily housing, which tends to be more affordable than single-family housing. Lower impact fees for multifamily housing may be justified because this type of development often uses public services more efficiently than other types of development.

History of the strategy

Impact fees were first used in the 1950s and 1960s to fund water and wastewater facilities. As federal and state grants to local governments declined, use expanded in the 1970s to non-utilities such as roads, parks and schools. By the 1980s, when court cases in several states had validated their use, impact fees were being levied for a broad range of public services, including fire, police, and libraries.

Texas adopted the first state impact fee enabling act in 1986. About half the state acts that provide local jurisdictions with explicit authority to charge impact fees allow waivers for certain types of projects, most often affordable housing.102

Target population

Impact fee waivers are offered to developers who construct affordable housing; ultimately, these benefits are intended to be passed on to low- and moderate-income homebuyers and renters.

How the strategy is administered

If state enabling legislation for impact fees allows local governments to waive these fees for affordable housing, a local government action (such as a city council or county commission vote) implements the waiver in the local area. The local planning department or other government agency may administer the program.

How the strategy is funded

Five of the state enabling acts that allow local governments to waive impact fees require that the impact fee fund be reimbursed by another source of revenue.[103]

Extent of use of the strategy

Widely used.

Examples of locations where the strategy is being used

- At least 14 state impact fee enabling acts specifically allow local governments to waive impact fees for affordable housing: Colorado, Florida, Georgia, Idaho, Indiana, New Jersey, New Mexico, Pennsylvania, South Carolina, Texas, Vermont, Utah, Washington, West Virginia, and Wisconsin.
- Atlanta, Georgia offers a 100 percent reduction in the impact fee if the housing unit rents for less than 60 percent of the regional median rent or sells for less than 1.5 times the regional new home sale price. Impact fees are reduced by 50 percent if the unit rents for between 60 and 80 percent of the regional median rent or sells for 1.5 to 2.5 times the regional new home sale price.[104]
- Polk County, Florida provides partial impact-fee waivers for workforce housing (see case study).
- In Santa Fe, New Mexico, all impact fees for a development are waived if at least 25 percent of the units are affordable to low-income households.

Pros and cons to using the strategy and/or types of markets where the strategy is more or less effective

In high-cost housing markets, impact fee waivers may have little impact on the affordability of new homes. In these markets, impact fee waivers need to be combined with other strategies, such as density bonuses and downpayment assistance programs, in order to close the gap between incomes and house prices.

Pros:

- Although impact fees in some areas are modest, in others they can reach tens of thousands of dollars. In places with high impact fees, an impact fee waiver can make an important contribution to improving affordability of housing.
- Impact fee waivers may encourage developers to build more affordable housing units.
- Impact fees that are proportional to the actual impact of the housing type (multifamily versus single family) tend to encourage lower-cost multifamily development.

Cons:

- Impact fee waivers may need to be combined with other subsidies to achieve affordability of new housing.
- In states that require waived impact fees to be reimbursed with other revenues, impact fee waivers can increase other fees and taxes, such as property taxes.

Sources of information about the strategy

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POLK COUNTY, FLORIDA

- ✓ Impact fee waivers and reductions
- ✓ Housing trust funds
- ✓ Workforce housing
- ✓ Expedited permitting processes

Polk County, Florida, has found that a combination of strategies is the most effective solution to house prices that have recently become unaffordable even for moderate-income households.

One of these strategies is an impact fee waiver. Although Polk County has used impact fee waivers to encourage affordable housing for nearly two decades, growing evidence that moderate-income households also face affordability problems led Polk County to pass a workforce housing ordinance in the spring of 2007 that provides partial impact fee waivers to moderate-income households.

The new workforce housing ordinance targets those with incomes between 80 percent and 120 percent of area median income (AMI). It waives 50 percent of all impact fees for workforce housing units as long as the buyer stays in the home at least seven years. With impact fees in Polk County totaling almost $12,000, the partial fee waiver means a savings of almost $6,000 for workforce housing units.

Fee waivers 101

The logistics of the fee waiver are complicated. First, the developer pays the full impact fee when applying for a permit. Upon sale of the house to a qualified moderate-income buyer, the developer is reimbursed by the county. The impact fee portion of the price is "paid" by the county, reducing the price to the borrower. To enforce required repayment of the waived impact fees if the house is sold within seven years, the county places a lien on the property.

Take, for example, a house purchased by a moderate-income buyer for $150,000. The buyer is responsible for financing $144,000 of the price ($150,000 minus $6,000 in waived impact fees); the remaining $6,000 is "paid for" by the county and secured by the lien. If the owner chooses to sell the house before the end of seven years, he or she must pay the county back the $6,000. If the owner stays in the house for seven years, the lien is forgiven, and the owner realizes the additional $6,000 in equity.

Fee waivers also apply to rental housing, although the administration of the waiver is slightly different. The fee waiver on rental housing requires an annual certification of eligibility from the property owner. When the fee waiver is granted, a percentage of the units are set aside as workforce housing units, to be rented to families with incomes between 80 percent and 120 percent AMI. For the next seven years, the owner must certify annually that these units are occupied by households that were verified to be workforce housing-eligible when they rented the unit. If the units have been rented to households that are not eligible, the lien on the property is due to the county.

Impact fee waivers nothing new for Polk County

Polk County first introduced impact fee waivers in 1990, when it passed an ordinance that waives all impact fees for affordable housing development. Affordable housing developments that qualify for the waiver must contain units that are designated for households with incomes at or below 80 percent of AMI. This ordinance also includes the seven-year provisional period, in which the ownership and affordability status must be maintained, or the fee applies.

To limit the financial impact that the fee waivers might have on the county budget, the county sets a maximum annual waiver cap of $250,000 across all projects in the county. If the cap is reached, a developer may appeal to the appropriate commission for fee waivers that would exceed the cap.

> ***"You have to look at the big picture. You'll get 20 times as much as you're giving up."***
> -Scott Coulombe

Fee waivers granted are funded from general revenues, gas taxes, and other county sources of revenue. However, Scott Coulombe of the Polk County Builders Association believes the revenue generated from new residents through property taxes and an overall more diversified and vibrant community will more than offset the impact fee losses. "You have to look at the big picture. You'll get 20 times as much as you're giving up," he said.

Impact fee waiver has been slow to produce results

Despite the county's good intentions, only nonprofit organizations including the Keystone Challenge Fund, Habitat for Humanity, and Rural Development have thus far taken advantage of the impact fee waiver ordinance.

Keystone CHALLENGE FUND

The impact fee waiver alone is not enough to make homeownership affordable for moderate-income families in Polk County, according to Jeff Bagwell. Bagwell is director of the Keystone Challenge Fund, a local affordable housing nonprofit that provides homebuyer education, constructs community housing developments, and has helped over 3,000 low to moderate-income households obtain downpayment and closing cost assistance.

Bagwell notes that despite both the healthy buyer's market that currently exists in Polk County and the recently passed impact fee waiver ordinance, qualified buyers need deeper subsidies to purchase a home. He believes that funding for downpayment assistance to be used in combination with the waiver would solve the problem.

"This is the best time in five to six years to buy a home in Florida, but without downpayment assistance to help them out, the waived impact fees have yet to do much good," Bagwell said. "If I [as a nonprofit lender] had both downpayment assistance and impact fee waivers, I could close loans all day long."

In addition, Bagwell notes that an impact fee waiver must be well publicized and fully understood by the building community before a county or other municipality can expect it to yield results. Up until recently, many of the details about the waiver had yet to be worked out, which may have kept builders from building homes that would, with the impact fee waiver, be affordable to moderate-income families.

Florida's HTF heads list of additional affordable housing strategies

In addition to the impact fee waiver ordinance, Polk County expedites permitting procedures for affordable housing projects, and is considering adopting voluntary inclusionary zoning that would include density bonuses.

Bagwell, also the chairman-elect of the Board of the Florida Affordable Housing Commission, says that the key to affordable housing production in Polk County and throughout Florida, however, is the state's housing trust fund. The fund generates between $400 and $600 million a year, primarily from documentary stamp revenue.[105] A substantial percentage of the revenue goes directly into the fund.

HTF money is used to fund the State Housing Initiatives Partnership (SHIP) Program. SHIP is the nation's first permanently funded state housing program to provide funds directly to local governments to produce and preserve affordable housing opportunities. This is accomplished through the creation of partnerships between local public and private stakeholders. Using SHIP funds, these partnerships offer very low-, low-, and moderate-income families with assistance to purchase a home, funding to repair or replace a home, and other types of housing assistance.[106]

Not all money collected for the state's housing trust fund is dedicated for affordable housing, however. Substantial portions of the money have been used to pay for hurricane damage relief in 2002 and to help balance the state's budget. Currently, the amount collected by the fund that can be used for affordable housing is capped at $243 million annually; the remainder has been left unappropriated. Bagwell notes that were the cap removed, these funds plus the impact fee waiver would provide more than enough in subsidies (such as downpayment assistance) to generate significant affordable housing production.

Bagwell has joined others in Polk County in a committee formed in 2006 called Polk Vision. The committee will re-examine ways to promote and generate affordable housing for the long term.

In the meantime, Bagwell is optimistic that with the right combination of strategies, Polk County can increase opportunities for affordable and workforce housing for its residents.

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Graduated Impact Fee Schedules for Infill Development

Strategy description

To improve the economic feasibility of infill development, some jurisdictions use a graduated impact fee schedule for small infill projects for which infrastructure already exists.

Target population

Direct impact: Developers of infill areas pay lower impact fees, which reduces the cost of the housing being produced. In addition, some governments waive impact fees altogether for affordable housing in infill areas.

Indirect impact: Areas with opportunities for infill development are likely to be in urban centers, and more likely to be lower-income than other areas. Impact fees that encourage development in these neighborhoods may increase housing options and revitalize the community.

How the strategy is administered

State enabling legislation is required for a local government to be able to charge impact fees. In states with this enabling legislation, local government action (such as a city council or county commission vote) implements waivers or reductions for infill development. The local planning department or other government agency may administer the program.

How the strategy is funded

The strategy can be self-funding; if infill areas are adequately served by existing infrastructure, or if minor improvements are needed, then impact fee reductions or waivers reflect the true impact of infill development. If infill areas need more extensive infrastructure improvements to accommodate new development, then impact fees may be higher in other areas.

Extent of use of the strategy

Moderate use.

Examples of locations where the strategy is being used

- Florida’s Impact Fee Act (the state enabling act for impact fees) allows local governments to offer incentives for redevelopment within urban infill and redevelopment areas.
- Albuquerque, NM developed a tiered system of impact fees for areas that are “fully served,” “partially served,” which have most or all of the infrastructure already in place for new development, and “unserved,” which do not. Impact fees are lower in “fully served” areas, which are more likely to have infill and redevelopment opportunities, as well as to encourage

more efficient development patterns and use of resources. Impact fees for designated "Infill Development Zones" are waived completely.[107]

- The Sacramento Regional County Sanitation District implemented impact fees that varied based on whether areas were "infill" (at least 70 percent built out) and "new growth" in 2002 to encourage infill development. Based on analysis of the costs of providing services, fees in infill areas were set at 15 percent of the fees in new growth areas.[108]

Pros and cons to using the strategy

Pros:

- Impact fee reductions encourage infill development, promoting more efficient development patterns and making better use of already-existing infrastructure.

Cons:

- Reduced impact fees for infill development may be poorly targeted for encouraging affordable housing production, as reductions benefit both affordable and market-rate housing.
- Savings to developers in impact fees may not be passed on to renters or homebuyers.

Sources of information about the strategy

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- "State Impact Fee Enabling Acts," Duncan Associates, updated by Clancy Mullen, July 2006, available at: www.impactfees.com/publications%20pdf/summary%20of%20state%20acts.pdf

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This document is a portion of NAHB's report
Research on State and Local Means of Increasing Affordable Housing.

Click here to view the full report.

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January, 2008

Prepared for the
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