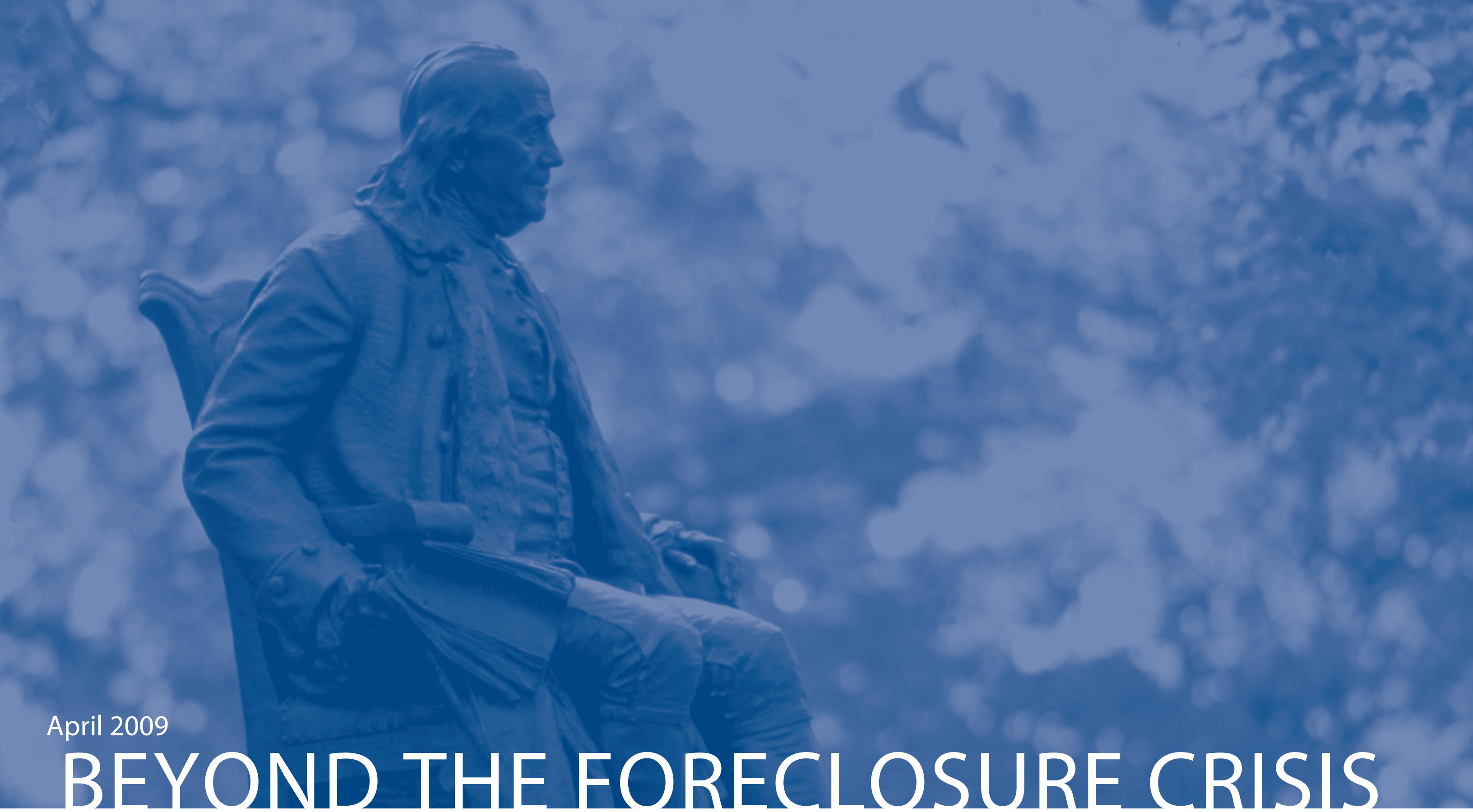

April 2009

BEYOND THE FORECLOSURE CRISIS

Reconstituting the Rental Housing Market in Pennsylvania

Fels Institute of Government

Fels Institute of Government
Penn Arts & Sciences

ABOUT THE FELS INSTITUTE OF GOVERNMENT

The Fels Institute of Government is the University of Pennsylvania's graduate program in public policy and public management. Fels was founded in 1937 by entrepreneur and philanthropist Samuel Simeon Fels of the Fels Naptha Soap Company in response to a wave of corruption and mismanagement in Pennsylvania government. Originally established for the purpose of training local government officials, over time Fels broadened its mission; it now prepares its students for public leadership positions in city, state, and Federal agencies, elective politics, nonprofit organizations, and private firms with close connections to the public sector. Its 1,800 living alumni work in leadership roles across the US and around the world.

Complementing the Fels academic program is Fels Research & Consulting, first established in 1946 as a "think and do" tank to work with governments and nonprofit organizations in five different policy areas: urban revitalization, K-12 education, economic and environmental sustainability, regional competitiveness, and human services. Within these policy areas, Fels works with its clients and partners to help them a) Get Better Results b) Move Ideas into Action and c) Pay for Results that Matter.

To find out more about Fels visit http://www.fels.upenn.edu.

“If anything, our government policies should encourage renting, not buying. … A bigger, healthier rental market, with more choices, would make renting a more attractive option for many people; it would also make the economy as a whole more flexible and responsive. “

Richard Florida
“How the Crash Will Reshape America”
The Atlantic, March 2009

PREFACE

Never has the connection between the economy and the housing market been clearer. The utter failure of a one-dimensional focus on homeownership to the exclusion of all other types of home opportunities has been a major contributing factor in leading our nation and, in fact, the global economy, to the brink of collapse.

The question is, will we learn our lesson and alter these disastrous housing policies to recognize and cultivate a more balanced approach? Or will we continue to simply ignore the need for a balance between housing types that will meet the full variety of housing needs in our communities?

It is time to create a Pennsylvania housing market that offers people a range of choices in housing type, size, cost and location. Such a market does not currently exist in most areas of the state. Instead, the statewide housing market has come to resemble a grocery store that sells only steak and caviar, offering few products that make sense for a working family on a meatloaf budget. Growth in the supply of homes has been lopsided, overemphasizing the construction of large single-family houses, and this overemphasis has created an imbalance in local and regional real estate markets. Pennsylvania lacks enough variety and enough reasonably-priced housing supply to meet the needs of many consumers.

Going forward, our housing policies must emphasize the development and preservation of homes that match the salaries of working people and the locations of their jobs, that provide smaller as well as larger homes, and that can be sustained over the long haul. It is time to embrace a sensible approach to housing and to take actions needed in order to bring the market in line with reality.

Simply put, there must be decent homes within reach of all Pennsylvanians. Working parents should be able to spend more time at home with their children rather than having to put up with long commutes. Retired persons and empty nesters should be able to move to smaller-sized housing units in places with excellent access to shopping, entertainment, and services. People with disabilities should be able to live with dignity in communities that keep them connected with friends and family. If we are to right the balance in supply and address the weaknesses of the market, we must respond in a more organized fashion to the demand for well-located, well-designed, and well–managed apartments and rental townhouses. Rental housing supply must be regarded as a valued economic asset-- not a liability--and strategies to develop and preserve attractive rental housing should be designed and implemented accordingly..

This report by John Kromer of the Fels Institute of Government jump-starts a needed dialogue about rental housing policy and strategies by exploring models of rental housing that are already proving successful here in Pennsylvania. Leading by example, he shows us, as consumers, providers, and policy makers, the benefits that a strong, viable rental market brings to communities of every size and type.

We are at a critical juncture. The housing crisis provides an opportunity for us to learn from what went wrong, and to understand how a realignment of our housing market to include more variety and options will benefit every community, both economically and socially.

This report gives us a good start at a better future.

Elizabeth G. Hersh, Executive Director
Housing Alliance of Pennsylvania

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INTRODUCTION

The lack of reasonable rental options for households in the turn-of-the-century real estate market was a contributing factor to the current housing crisis. Future crises can be avoided and long-term economic stability can be promoted through the creation of healthy rental housing markets. As steps are being taken to assist families who have lost their homes or are threatened with foreclosure, now is the time for action to reconstitute healthy rental housing markets as an economic development priority for Pennsylvania cities and towns.

Rental housing that is well-located, well-designed, and well-maintained is not a community problem—it is a community solution. The best rental housing

- Reduces travel time and expense for working families;
- Promotes vibrant downtowns and neighborhood commercial corridors by increasing housing density (and associated consumer buying power) in nearby residential areas;
- Provides market-rate retirement living options for singles and couples who would otherwise consider moving out of state; and
- Serves as a housing resource for young families and others seeking high-quality, reasonably-priced rental housing rather than homeownership.

The need to address rental housing issues in a strategic manner is especially great at this time, for several reasons.

- More people are experiencing income loss due to layoffs and downsizing, and they need lower-priced rental housing in order to make ends meet.
- As a result of the effects of the nationwide foreclosure crisis on Pennsylvania communities, many families that had been homebuyers during the earlier years of this decade will be renters in the foreseeable future.
- As a by-product of the economic meltdown that began in 2008, the level of investment equity that can be generated through the state-administered Low Income Housing Tax Credit, Pennsylvania's largest development financing resource for affordable rental housing, has shrunk substantially, significantly reducing the prospects for additional rental housing production financed through this resource.

During the past decade, individuals and families who had previously lived in the suburbs and out of state have become interested in Pennsylvania downtowns, many of which offer well-designed, reasonably priced housing in an attractive, pedestrian-friendly environment. In order to respond to this interest, downtown supporters need to find ways to expand the number of high-quality housing options that can be made available for these prospective downtown residents and to remove impediments to investment in market-rate and mixed-income housing development.

RENTAL HOUSING AFFORDABILITY FOR MINIMUM WAGE EARNERS IN SELECTED PENNSYLVANIA REGIONS					
HUD 2008 Fair Market Rents					
	Renter households (2000)	Rent afford-able with FT job paying minimum wage	Zero-BR	1-BR	2-BR
Allentown-Bethle-hem-Easton HMFA*	70,276	$372	$566	$690	$816
Altoona MSA	13,957	$372	$439	$480	$581
Armstrong County HMFA*	6,588	$372	$454	$494	$546
Erie MSA	32,799	$372	$433	$489	$631
Harrisburg-Carlisle MSA	61,341	$372	$502	$573	$722
Johnstown MSA	15,289	$372	$437	$444	$546
Lancaster MSA	50,296	$372	$489	$581	$715
Lebanon MSA	12,688	$372	$418	$499	$643
Philadelphia-Cam-den-Wilmington MSA	461,261	$372	$682	$781	$932
Pike County HMFA	2,646	$372	$766	$797	$923
Pittsburgh HMFA	277,579	$372	$507	$557	$666
Reading MSA	36,877	$372	$519	$580	$715
Scranton--Wilkes-Barre MSA	69,004	$372	$438	$522	$627
Sharon HMFA	11,099	$372	$457	$478	$583
State College MSA	19,650	$372	$600	$669	$788
Williamsport MSA	14,350	$372	$424	$487	$587
York-Hanover MSA	35,403	$372	$489	$562	$713
Source: National Low-Income Housing Coalition					
* HMFA = HUD Metro Fair Market Rent Area					

Rental housing that is affordable to individuals and families at all income levels—both below and above median income—is a critical economic development issue that is closely linked to the future prospects of Pennsylvania's residential communities. Rental housing for people earning salaries at or just above the minimum wage continues to be needed statewide—but the issue involves much more than the production of subsidized housing. Well-designed, well-located rental housing, both new or upgraded, can broaden economic opportunity and encourage further investment and development in Pennsylvania cities and towns, to the benefit of residents at all income levels.

- The City of Allentown is implementing a rental housing asset management strategy that is producing property improvements citywide and generating licensing and fee income that exceeds the City's program costs.
- The City of York has adopted an ambitious tax abatement incentive that helped attract a major investment in upscale rental housing, drawing new residents to the city's downtown core.
- Conservatorship legislation was recently enacted by the Pennsylvania General Assembly, in part to prevent the recurrence of problems such as that experienced by Carlisle Borough, where vacant properties controlled by a negligent investor impeded investment in a historic district where several high-quality historic restoration ventures had previously been completed. Conservatorship can be used to return neglected properties back to downtown and neighborhood real estate markets, stabilize residential or mixed-use blocks, and generate tax ratables to local and county government.

This report consists of a series of summaries of strategies and illustrative case studies that together are intended to stimulate creative thinking, dialogue, and action about rental housing opportunities for Pennsylvania. During the coming years, Pennsylvania and every other state will face major economic challenges. The manner in which we organize available resources to address these challenges will influence our economic prospects for many years to come. The production, preservation, and maintenance of rental housing for individuals and families at all income levels is one of the most important of these challenges.

The Fels Institute of Government and the Housing Alliance of Pennsylvania welcome comments on this publication and suggestions on next steps to be taken in support of these and other rental housing strategies.

ALLENTOWN, PA
PRE-SALE INSPECTION ORDINANCE

One strategy for ensuring that existing rental properties are maintained in safe and habitable condition is to require that residential property sales be preceded by a City inspection, to be followed by the correction of any significant code violations as a condition of sale.

In November, 2007, Allentown's City Council approved Bill No. 109-2007, which requires "the inspection of all residential properties…prior to the transfer of title for compliance with standards found in the City of Allentown, Property Rehabilitation and Maintenance Code and the allowable use designation according to the City of Allentown Zoning Ordinance." The ordinance calls for a seller of a property to contact the Bureau of Building Standards and Safety and request an inspection within three days of the listing date or offer to sell. Following the inspection, the Bureau's inspector completes a Buyer Notification Report, which lists any code violations that must be corrected by the seller or buyer as a condition of sale.

Compliance – that is, the resolution of issues identified in the Buyer Notification Report – is monitored by the same Bureau inspector who conducted the initial inspection and completed the report. Rental properties are subject to compliance terms spelled out in the Allentown Property Rehabilitation and Maintenance Code.

Other significant features of the ordinance:

- A requirement that sellers notify the City of the property buyer's name and address within three days of the transfer. This requirement puts an end to the practice by some absentee-owners of falsely listing the property address as their address; and
- City verification of a property's allowable use prior to sale. This verification assures the buyer that the property has no zoning code use violations, such as the illegal conversion of a single-family home to a multi-family property or the development of a property for more dwelling units than zoning allows.

RENTAL HOUSING ASSET MANAGEMENT STRATEGY

A well-managed code enforcement and housing preservation strategy can pay for itself (through revenue generated by fees, fines, and penalties) and upgrade the quality of rental housing citywide.

To preserve existing rental housing resources and to prevent the occurrence of crises requiring extreme measures such as a conservatorship assignment, local and county governments need to organize and implement their own rental housing asset management strategies. An effective asset management strategy addresses housing conditions on a citywide basis and imposes penalties on noncompliant property owners without creating regulatory barriers that make it difficult for responsible owners to operate profitably.

In November 2007, City of Allentown Mayor Ed Pawlowski released a report by the University of Pennsylvania's Fels Institute of Government, entitled A Housing Strategy for Allentown's Central-City Neighborhoods (the report may be viewed at http://www.fels.upenn.edu/neighborhoodrecovery/reports/allentown_report_07.pdf). The Fels Institute report identified the older residential neighborhoods located in the vicinity of the downtown area as "an extraordinary resource" that had become "one of the region's biggest problem areas." The report attributed the problems of these neighborhoods to speculation by absentee owners, inflated real estate values, a lack of suitable housing options for employees of companies located downtown, and a proliferation of housing code violations.

Consistent with the strategy summarized in the Fels Institute report, Allentown has instituted or strengthened the following measures.

- Enacting a requirement for a *pre-sale inspection of all residential properties* as a condition of sale. .
- Instituting a *citywide rental property inspection cycle*, so that all rental units are inspected within a five-year period.
- *Enforcing a strict "responsible agent" requirement* that calls for absentee owners to be represented by a local agent with legal exposure for problems associated with property maintenance.
- Collecting rental licensing fees in a timely manner and using the threat of license revocation in the event of non-payment.
- *Reinvigorating the Blighted Property Review Committee process*, so that vacant properties that are not code-compliant can be acquired and conveyed to developers for rehabilitation

READING, PA
MODERATE REHABILITATION MODEL

Neighborhood Housing Services (NHS) of Greater Berks has specialized in the rehabilitation of long-term vacant houses through a "gut rehab" approach involving a clean-out of the abandoned property, the replacement of all major systems, and the installation of all-new finish work. This relatively high-cost approach is the only feasible one for long-term vacant houses that are located on blocks where preservation and reoccupancy of the property is preferable to demolition that will produce a "gap tooth" vacant lot.

Although gut rehab will continue to be needed in order to return strategically located long-term vacant houses to the real estate market, many short-term vacant houses in better condition can be found within NHS' service area as well. If the acquisition and rehabilitation of these houses were to become a higher priority, then a lower-cost moderate rehabilitation approach could be pursued, emphasizing preservation and repair rather than tear-out and replacement.

Based on its experience in Reading and nearby communities, NHS has developed the following model development budgets for two identical 2 1/2-story, 3-bedroom houses, one requiring gut rehab treatment and the other suitable for moderate rehabilitation.

Development Budgets for Two Single-Unit Houses of Comparable Size in Reading

Zip Code	Gut Rehab	Moderate Rehab
No. Stories	2 1/2	2 1/2
No. Bedrooms	3	3
No. Square Feet	1,200	1,200
Acquisition	$10,000	$20,000
Rehabilitation	81,000*	20,000**
Soft Costs	2,000	2,000
Total Development Budget	**$93,000**	**$42,000**

* Gut rehab treatment includes lead risk assessment and remediation, rough and finished plumbing and electrical, replacement windows and doors, new cabinets, kitchen fixtures, bath fixtures, new roof, heater, hot water heater, carpentry, insulation, drywall, and painting,

** Moderate rehab treatment includes roof, repair of plumbing and electrical systems, interior painting, plywood underlayment, vinyl in kitchen and bath, heater, replacement windows (6), door locks, and plumbing fixtures (no lead testing and remediation).

MODERATE REHABILITATION

Using a small subsidy to upgrade existing unoccupied rental units, including upstairs units above storefront properties, can complement Main Street and Elm Street program strategies and generate higher occupancy levels at a low per-unit cost.

Many well-populated areas of Pennsylvania do not have a shortage of housing units—often the problem is that the existing housing is in need of major repairs or is vacant and uninhabitable. This problem is particularly evident in cities and older suburbs that have experienced late-twentieth century depopulation, as population decline has been accompanied by the proliferation of vacant houses. Many of these houses are located on otherwise stable blocks and are in reasonably good condition, with no severe structural flaws, water damage, or fire damage.

A moderate rehabilitation financing program provides a relatively small subsidy that is combined with private rehabilitation financing to support property rehabilitation for rental reuse. The properties that are improved and put back into service through such a program are located in stable, attractive neighborhoods that will attract good tenants. The rehabilitation involves the repair or replacement of at least one major system, but is not an extensive "gut" rehab project; highly deteriorated buildings require more subsidy than is available under a moderate-rehab program.

Some cities have used Community Development Block Grant or HOME funds to provide development subsidy financing for moderate rehabilitation of properties that are subsequently sold for homeowner occupancy. This model could be adapted to provide a rehabilitation financing resource for small rental properties as well.

During the 1980s, the U.S. Department of Housing and Urban Development (HUD) offered a rental rehabilitation financing program based on a model similar to that described above. Despite its success in cities in Pennsylvania and elsewhere, the program was discontinued toward the end of the decade. In this HUD program model, a relatively low development subsidy to support bricks-and-mortar expenses was accompanied by a rental assistance subsidy, enabling the property owner to offer the completed rental units to prospective tenants at a range of income levels (the rental assistance subsidy was awarded to the municipal government that administered the rehabilitation financing, not to the public housing authority). A revival of this program model could include a development subsidy along with rental assistance provided by the local housing authority (in the form of "project-based" Section 8 certificates) or through a non-government rental assistance fund. Although this combination would amount to a double subsidy, the total subsidy amount would be far lower than existing double-subsidy financing, such as the use of CDBG or HOME funds to supplement Low Income Housing Tax Credit Financing.

The value of this strategy is that it could finance a large number of rental units in good locations at rent levels that would be affordable to households at or below median income.

YORK, PA

CODO 241

Address:	241 North George Street, York, PA
Property:	Three-story, 26,661 square foot vacant building on a 1.33 acre lot at a key intersection at the northern entry into downtown York.
Developer:	Wagman Construction, Inc.
Development Plan:	35 rental apartments, a commercial office suite, and a street front restaurant. The existing building is married with approximately 25,000 square feet of new construction. Completed in early 2009, the project is the largest market-rate apartment development opened in downtown York in the past twenty years
Market Potential:	A market study completed in January, 2007 by Real Property Research Group verified a strong demand for high-quality apartments in the Greater York area. To respond to this demand, the Codo units range from several 600 square foot studio apartments to ten loft apartments of 1,000 to nearly 1,400 square feet. Renting from $595 to $1,295 per month, the apartments provide a range of new living options for professionals in downtown York and will push rental rates for other quality downtown housing upward. These 35 new upscale rental units are attracting new residents whose spending will contribute to the economic success of restaurants and retailers in downtown.
Development Budget:	$10,000,000
Tax Abatement Impact:	At the time of purchase in March of 2007, the assessed value of the property was $343,790. The estimated assessed value of the project upon completion is $3,000,000. At this assessed value, the total value of abated taxes over 10 years would be $773,000.

TAX ABATEMENT

A tax abatement incentive can attract quality rental housing development without government cash subsidies.

Under the tax structure that exists in most cities, investors and developers are, in effect, penalized for rehabilitating older buildings for rental housing; when the rehabilitation work is completed, the property is reassessed at a substantial higher value, and taxes go up. This and other disincentives--which may include a longer zoning and permitting process, higher labor costs, and environmental remediation or lead paint abatement expenses--cause many conventional developers to avoid undertaking rehabilitation and adaptive reuse projects in urban areas.

These impediments limit opportunities to develop market-rate rental housing in newly revived urban downtowns and in stronger neighborhood real estate markets, despite evidence of market demand for high-quality rental housing in such locations. A long-term, one hundred percent tax abatement is a strategy designed to offset these disadvantages and to help older cities more fully realize their market potential.

The most generous tax abatements involve a full exemption from property taxes associated with the value of the completed improvements for ten years, During the abatement term, the property owner is taxed only on the value of the land and the building in its pre-existing condition—its condition prior to the start of rehabilitation. At the end of the ten-year period, the owner pays taxes based on the full, current assessed value of the land and the building in its improved state.

Cities that have adopted generous tax abatement incentives, such as York, do so in part to stimulate interest in the rehabilitation and reuse of older buildings that have remained vacant or under-used for years (in York, city and county property taxes are fully abated, while school taxes are subject to a graduated abatement). The rationale for offering the abatement is the fact that, since a building of this kind has generated no developer or investor interest for an extended period, government has little or nothing to lose by offering a tax exemption; the level of tax revenue currently being collected will not be reduced, whether or not development takes place. If this incentive attracts interest and ultimately produces a fully rehabilitated, occupied building, the associated benefits for the surrounding area and the city can be substantial.

CARLISLE, PA
A CONSERVATORSHIP PRECURSOR

The following chronology describes the efforts of officials in Carlisle to resolve a case of property neglect, which ultimately resulted in the demolition of three buildings that had been highly suitable for preservation. This case illustrates the need for the conservatorship legislation that was approved by the Pennsylvania General Assembly in November 2008.

February 1998	A total of 158 citations for property maintenance code violations are issued for two vacant properties located on East High Street in Carlisle's historic district, on a block where several preservation projects had recently been completed. The owner holds title to eleven properties in the historic district, most of which are vacant.
January 2000	A Cumberland County judge places the East High Street properties and eight others under the management of the Cumberland County Housing and Redevelopment Authority and orders the owner to pay Carlisle Borough $12,000 in compensation for legal expenses associated with code enforcement actions. The Housing and Redevelopment Authority plans to repair the properties and make them suitable for rental occupancy.
March 26, 2001	The U.S. Supreme Court rejects an appeal by the owner of the properties, seeking to block implementation of the conservatorship ruling.
March 28, 2001	The three East High Street houses are severely damaged in a fire ruled as arson.
March 31, 2001	A Cumberland County judge determines that conservatorship is no longer possible due to the extent of the fire damage. The East High Street houses are demolished.
2004	The property owner is convicted of arson.

CONSERVATORSHIP

Conservatorship, a housing reclamation strategy which was legislatively approved in 2008, can be used to restore neglected investor-owned properties to full occupancy, with economic benefits for the blocks they occupy and the city as a whole.

Legislation authorizing Abandoned and Blighted Property Conservatorship (also known as receivership) was enacted in November 2008, as a result of joint planning, organizing, and advocacy by the Housing Alliance of Pennsylvania, members and staff of the Pennsylvania General Assembly, and numerous supporters across the commonwealth. Conservatorship enables a court to remedy a chronic case of rental property neglect by assigning a responsible party to take control of the property, repair it to comply with health and safety codes, and retenant and manage it.

Conservatorship is an action that is taken only as a last resort, when all reasonable efforts to achieve code compliance have been pursued without success; it is not a redevelopment strategy to be used on a large scale, but an intervention to be used selectively to address conditions that pose a threat to residents of a neglected property and the surrounding community. HB 2188 was designed to provide an opportunity to fast-track such cases in order to preserve endangered properties and maintain public safety. With this legislation, it is hoped that distressed properties can be repaired and returned to service quickly so that continued deterioration leading to demolition can be avoided. The Carlisle Borough case described on the facing page is an illustration of how, prior to the enactment of the conservatorship bill, it was possible for a negligent property owner to retain control while engaging in court appeals of code enforcement actions and the attempted assignment of a conservator.

The Housing Alliance has identified the following next steps toward implementing the conservatorship legislation.

- Educate officials and community groups about the new law and how to use it.
- Identify qualified conservators and make them available for court appointment as the first properties enter the system.
- Make the new law fully operational within the next one to two years.

More information about conservatorship is available through the Housing Alliance at http://www.housingalliancepa.org/news/view.php?news_id=455.

STATE COLLEGE, PA
LAND TRUST COST COMPARISON

Traditional Purchase and a Purchase with the Assistance of the Land Trust

Example #1		
Item	Traditional Purchase	Purchase with Land Trust
Price of Home	$85,000	$85,000
Cash Required (Down Payment & Closing Costs)	$7,650	$0
Land Trust Contribution	N/A	$25,500
Mortgage Amount	$80,750	$59,500
Monthly Payment	$741.58	$550.38

Example #1		
Item	Traditional Purchase	Purchase with Land Trust
Price of Home	$95,000	$95,000
Cash Required (Down Payment & Closing Costs)	$8,550	$0
Land Trust Contribution	N/A	$28,500
Mortgage Amount	$90,250	$66,500
Monthly Payment	$812.07	$613.36

Source: State College Community Land Trust at http://www.scclandtrust.org/scenarios/.

COMMUNITY LAND TRUSTS

A community land trust can sustain long-term residency in a community experiencing rapid increases in property values.

The Institute for Community Economics (ICE) defines a community land trust as "a private non-profit corporation created to acquire and hold land for the benefit of a community and provide secure affordable access to land and housing for community residents" ("What is a CLT?" Institute for Community Economics at http://www.iceclt.org/clt/index.html). In its index of land trusts around the country, ICE lists two Pennsylvania sites: the State College Community Land Trust in State College and Brightside Development and Land Trust in Lancaster.

Community land trusts preserve housing affordability by holding down the cost of land. Land trusts acquire real property—a group of scattered or consolidated properties or a single building—and lease it to individuals and families seeking affordable housing (land trusts may also own non-residential properties such as parks and community facilities). Land trust-owned properties are exempt from real estate taxes, and the cost of maintaining their assets is not affected by changes in property tax assessments.

Two major issues that must be addressed in connection with the organization of a land trust are financing for land assembly and organizational operations and management.

- In the most desirable real estate markets, land acquisition costs are high; alternatively the places where land costs are relatively low are isolated or deteriorated sites that would not be attractive to prospective residents. Given these constraints, the best prospects for starting a new land trust might be the acquisition of a single building or a small number of properties already owned by a government agency or local institution that might contribute the property or sell at a reduced price.
- Because management inexperience is a cause of land trust failure, starting an organization in collaboration with an experienced property manager (possibly in partnership with a local academic or health care institution) may address this potential problem.

Land trusts are more often used to promote affordable homeownership than as a rental housing resource. However, many land trusts offer both owner and rental housing opportunities (see, for example, Central Vermont Community Land Trust Rental Properties at http://www.cvclt.org/apartments.html).The two examples shown on the facing page could be adjusted to create an affordable rental housing scenario.

PHILADELPHIA, PA

RENTAL ASSISTANCE

Selected Rents and Rental Assistance Amounts by ZIP Code				
Zip Code	No. bedrooms	Monthly Rent Amount*	Monthly Rental Assistance Amount*	Utilities Included In rent? (Y?N)
19124	2	$625	$542	N
19144	2	$650	$598	N
19139	3	$775	$509	N
19140	4	$850	$802	N
* Does not include utility reimbursement.				

Source: City of Philadelphia, Office of Housing and Community Development.

Note: Philadelphia's program provides rental assistance for formerly homeless individuals and families, persons disabled by AIDS-related illnesses, and others with combined affordable housing and supportive service needs. The level of rental assistance required to support a working household would therefore be significantly lower.

RENTAL ASSISTANCE

A rental assistance strategy is the most direct and cost-effective way to close the housing cost gap and make more rental housing accessible to working families and others.

Providing a household with rental assistance—funding to make up the difference between the "fair market" cost of a rental apartment and the amount that is affordable (i.e., not more than thirty percent of household income)—costs much less than developing rental housing through new construction or vacant property rehabilitation. As development subsidy funding becomes scarcer and construction costs increase, more consideration should be given to using rental assistance more extensively and to funding rental assistance from sources other than traditional public housing authority-administered Section 8 rent subsidy programs.

The table on the facing page shows rental assistance funding being made available to four households living in different Philadelphia zip codes. The total cost of supporting the housing needs of these four households is about $30,000 a year. For the same amount of funding as the total required to develop a single rental unit with financing through the Low Income Housing Tax Credit program, rent assistance could be provided to these four households for most of a decade.

The following rental assistance options are worth further consideration..

- *Short-term rental assistance.* Funding available through the federal HOME program can be used to provide short-term (less than two years) rental assistance, and some cities use a portion of the HOME funding they receive to provide rental assistance to formerly homeless families who do not need to remain in emergency shelter and are seeking housing in a community environment. The City of Camden, New Jersey, with Camden's STRIVE program and other workforce development service providers, is exploring the opportunity to provide short-term rental assistance to work-readiness program graduates who have found employment, in order to provide housing support as they transition into the workforce.
- *Nongovernment rental assistance.* Rental assistance is a low-cost resource for preserving housing diversity in changing neighborhoods where property values are rising rapidly. An annual commitment to rental assistance in the form of matching funds made available by corporate, charitable, and/or institutional funders could capitalize a fund that could be privately managed and would not be subject to the limitations and restrictions associated with Section or HOME rental assistance.

NAP SUPPORT FOR AFFORDABLE RENTAL HOUSING

The General NAP Guidelines state that Affordable Housing Programs are an eligible activity for NAP projects….Accordingly, it is possible for a business firm to contribute to an Affordable Housing Program via a nonprofit organization and obtain state tax credits. Affordable Housing Programs are defined as : "projects that renovate, repair, construct, or preserve rental or ownership housing for individuals with low and moderate incomes in areas deemed unaffordable to these individuals"….

…[O]wners sometimes establish rent subsidy reserve accounts…in order to be able to set aside additional units in the building for very low income tenants….Developments that commit to providing enhanced services to residents, including but not limited to special needs and elderly populations, may capitalize a separate reserve account for the ongoing expenses associated with such services.

The NAP offers an opportunity for business firms to contribute to such reserve accounts and, in return, receive state tax credits….A business firm could make a monetary contribution to [a] nonprofit which would either (1) establish an escrow account with a third party and draw down on the funds as needed to provide rent subsidies to eligible tenants or provide supportive services or, (2) …use the donated funds to make a capital contribution to the…development for the purposes specified by the business firm, e.g., as a rent subsidy, to provide special needs services or meet an operating deficit.

"Coordinating the utilization of state NAP credits with federal Low Income Housing Tax Credits,"
memorandum to Interested Parties from Mark Schwartz and Laura Schwartz
September 2008

NEIGHBORHOOD ASSISTANCE PROGRAM

The Neighborhood Assistance Program, approved by the state legislature in 1967 and revised in 2007, enables a business that makes a contribution to a nonprofit community organization to obtain a credit on state corporate taxes, in an amount of up to fifty percent of the contributed sum, which may not exceed $250,000 annually.

"Neighborhood Assistance" is one of five activity categories that may be eligible for the NAP tax credit incentive. For the purposes of the program, "neighborhood assistance" is defined as "financial aid, labor, materials or technical advice that can provide physical improvement to any part of a distressed neighborhood" (the other four activity categories are Community Services, Education, Job Training, and Crime Prevention). NAP is administered by the Pennsylvania Department of Community and Economic Development (DCED), and any activities proposed for NAP support must be approved in advance by DCED (more information about NAP may be obtained at http://www.thepafoundation.org/docs/Nap-Programs-brochure.pdf).

According to program information published by DCED, the overall objective of NAP is to "help improve the lives of low-income people in distressed neighborhoods and communities through the creation of an effective partnership between community-based organizations and the business and corporate community." NAP activities "must serve clients who are either low income or residents of economically distressed neighborhoods."

Although NAP originated as a program that provided support for human service activities, the revision of the program in 2007 created an opportunity for NAP to be used as a source of support for affordable housing ventures as well. The memorandum by Mark Schwartz and Laura Schwartz that is excerpted on the facing page indicates that NAP-related contributions may be used to support housing construction and preservation projects, as well as the creation of operating reserve funds to finance reduced rents for lower-income tenants. Both forms of support would be especially relevant to older existing subsidized rental development sites that need physical upgrading or supplemental operating support in order to sustain themselves as resources for affordable housing.

Because these uses of NAP vary from NAP's traditional focus on human-service activities, it is important that any proposed use of this incentive be reviewed with DCED in advance of substantive planning. With DCED approval and the involvement of a qualified business partner, NAP could be a valuable resource for the development and preservation of affordable rental housing.

OWN-TO-RENT ADVANTAGES

*"**Overextended borrowers** would gain the right to rent for a period of time at market rate. This right in itself would provide an incentive for the new owner (the bank) to agree to renegotiate the mortgage instead of facing…rental….The distressed owners would be free to move if they prefer to live in another house….*

*"**The new owner (the bank)** would also benefit from this proposal. The substantial rental deposit and clear eviction rights in cases of abuse of a property should protect [the bank] against distressed former owners who mistreat the property or who fail to pay rent.*

*"For **the broader society**, this plan would provide new options to …citizens who are stuck with mortgages worth more than the homes they live in….It pushes both lenders and borrowers toward one of three resolutions: either renegotiate such mortgages on more favorable terms, shift the resident families and properties from the ownership market into the rental market in the same residence, or help the families move into other rental units they can afford in places they want to be."*

Bernard Wasow
"A Safety Net for Bubble Buyers: Rescuing Homeowners from Collapsing Home Values,
The Century Foundation
2008.

OWN TO RENT

Giving homeowners threatened with foreclosure the option to remain in their properties as renters is a low-cost strategy for preventing displacement, housing vacancy, and neighborhood destabilization.

Many families have been displaced and many occupied houses have been vacated--and have remained vacant--as a result of the mortgage foreclosure crisis. The problems associated with this crisis are expected to worsen. As many as 19 million households are estimated to have mortgage debt exceeding the value of their homes by 2010 (David Leonhardt, "The Trouble With A Homeowner Bailout," The New York Times October 21, 2008).

Mortgage loan modification strategies have not significantly improved this situation. In December 2008, the Associated Press reported that more than half of all homeowners who had their loans modified to make the payments more affordable in the first half of the year already are in default and cited experts' claims that most loan modifications do not actually provide much financial relief for borrowers (Allen Zibel, "Despite relief, more than half default on home loans," Associated Press, December 9, 2008).

Offering homeowners in default the option of remaining in their homes as renters would reduce displacement and housing vacancy and the threat of vandalism. As important, this approach would focus attention on a central issue: the need for housing asset management to stabilize neighborhoods that have experienced mortgage foreclosure on a significant scale.

Although own-to-rent strategies are not being pursued as an option by most of the parties involved in seeking to address the foreclosure crisis, this option should studied further, and lenders should be asked to test it on a trial basis with qualified households.

The excerpt on the facing page describes some benefits of an own-to-rent approach. Other analysis and commentary on this issue include Dean Baker, "The Key to Stabilizing House Prices: Bring Them Down" (Center for Economic and Policy Research, December 2008) and Daniel Alpert, "The Freedom Recovery Plan for Distressed Borrowers and Impaired Lenders" (Westwood Capital LLC).

In January 2009, New Jersey Governor Jon S. Corzine signed legislation authorizing the Housing Assistance and Recovery Program (HARP), which permits eligible homeowners faced with imminent foreclosure to remain in their homes as renters, paying an affordable rent, with an option to buy back the property at a later time. Based on experience gained through the implementation of the New Jersey program and other models, this option should also be made available in Pennsylvania.

PHILADELPHIA, PA
APARTMENT-BUILDING UPGRADE

Address:	4800 Block Pine Street, Philadelphia
Property:	116-unit apartment in a three-building complex 125,000 square feet of gross building area 92,500 square feet of gross living area
Purchase Price:	$4.5 million (approx. $38,800 per-unit acquisition cost)

Major Improvements:

- Removal of underground storage Tank
- Addition of lighting
- Installation of new fire alarms and smoke detectors
- Installation of new or rebuilt boilers
- Completion of extensive plumbing work
- Sanding and refinishing of hardwood floors
- Installation of modern cabinets and appliances
- Upgrading of hallways and common areas

Improvement Cost: $600,000

Rent Structure after Improvement (2004):	Studios (370 to 385 SF)	$585
	One-Bedroom (435 to 735 SF)	$660
	Two-Bedroom (1,000 to 1,300 SF)	$725

EQUITY FUND

Academic and health care "anchor" institutions interested in promoting or sustaining housing diversity or in developing or upgrading workforce housing in neighborhoods adjacent to their campuses can benefit from the University of Pennsylvania's experience in organizing an equity fund known as the Neighborhood Preservation and Development Fund. Formed in 1999, the fund's primary goal was to upgrade and improve rental housing within a residential target area extending nine blocks west of the University campus and, in doing so, to serve all members of the community, not just students.

At the time of its formation, Penn's commitment to the fund leveraged the participation of Fannie Mae, the University of the Sciences in Philadelphia (a nearby West Philadelphia institution), Commerce Bank, and Trammel Crow (the fund's structure and participants have changed since that time). The participants planned to acquire and renovate a portfolio of up to 1,200 rental units within the target area, focusing on highly visible, deteriorated or poorly managed properties. Through financing property improvements and improving property management and maintenance, the fund participants expected to stabilize and enhance the neighborhoods where they were located and generate a reasonable return on investment.

Some apartments in the fund portfolio are rented to students, while others are rented by community members who have no connection to the University. For example, according to a recent report, 39 of the 116 units at the Cornerstone (described on the facing page) were occupied by students.

Through experience to date, fund participants found that:

- Delegating operational responsibilities to a private property management firm was preferable to handling these tasks in-house.
- Economies of scale were best suited to a portfolio of 450 units or more (portfolio growth had been targeted to a maximum of 1,000 units).
- Rents in some units could be set at about $50 per month below market, providing workforce housing opportunities for lower-wage employees at area institutions.

ABOUT THIS REPORT

This report was completed as a project of Fels Institute of Government Research & Consulting. More information about the Fels Institute and other projects can be found at http://www.fels.upenn.edu/.

The report was written by John Kromer, Senior Consultant at the Fels Institute, with the assistance of Justin Evilsizor, Research Associate. Mr. Evilsizor's participation in this project was funded by a grant from the Samuel S. Fels Fund as part of the Fels Fund's Summer 2008 Internships in Community Service Program.

The Housing Alliance of Pennsylvania (http://www.housingalliancepa.org/
is currently working with the Fels Institute in developing education and training materials to support the implementation of conservatorship legislation approved by the Pennsylvania General Assembly in November 2008, which took effect in February 2009.

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