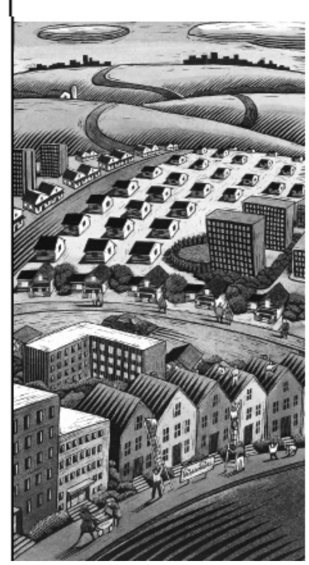
Long-Term Affordable Housing Strategies in Hot Housing Markets

Jesse Mintz-Roth

Fellowship Program for Emerging Leaders in Community and Economic Development

May 2008

Joint Center for Housing Studies
of Harvard University



NEIGHBORWORKS® AMERICA

Neighborhood Reinvestment Corporation dba NeighborWorks America was established by an Act of Congress in 1978 (Public Law 95-557). A primary objective of the Corporation is to increase the capacity of local, community-based organizations to revitalize their communities, particularly by expanding and improving housing opportunities.

These local organizations, known as NeighborWorks organizations, are independent, resident-led, nonprofit partnerships that include business leaders and government officials. All together they make up the NeighborWorks network.

JOINT CENTER FOR HOUSING STUDIES OF HARVARD UNIVERSITY

The Joint Center for Housing Studies analyzes the ways in which housing policy and practices are shaped by economic and demographic trends, and provides leaders in government, business and the nonprofit sector with knowledge and tools for formulating effective policies and strategies.

Established in 1959, the Joint Center is a collaborative unit affiliated with the Harvard Design School and the Kennedy School of Government at Harvard. The Center's programs of research, education and public outreach inform debate on critical housing issues and illuminate the role of housing in shaping communities. The Policy Advisory Board, a diverse group of business leaders in the housing sector, provides support and guidance for the Center and its activities. The Joint Center also receives input from its Faculty Committee, which draws on the expertise of a university-wide group of scholars.

This paper was written with the support of the NeighborWorks America's Emerging Leaders in Community and Economic Development Fellowship, which provides opportunities for highly qualified professional students at Harvard University to research and publish applied analytical projects of interest to the community-development field.

This analysis was performed with the support of NeighborWorks America, with editing and production by Amy Christian, Ampersand Editing & Production Services. The Corporation has full rights to use and distribute this document.

Harvard Joint Center for Housing Studies
Harvard University
1033 Massachusetts Avenue, 5th Floor
Cambridge, MA 02138
(617) 495-7908
www.jchs.harvard.edu

NeighborWorks® America
1325 G Street, NW, Suite 800
Washington, DC 20005
(202) 220-2300
www.nw.org

About the Author

Jesse Mintz-Roth received his master's degree in urban planning, with a concentration in real estate and urban development, from the Harvard Graduate School of Design in 2008, where he was head of the student group Housing GSD. He has worked as a policy analyst for the city of New York and as a project coordinator for the Woodrow Wilson School of Public and International Affairs at Princeton University. He received his bachelor of arts degree from the University of Chicago in public policy and geography in 2001.

Acknowledgements

I would like to thank my advisors, Nic Retsinas at the Harvard University Joint Center for Housing Studies, and Lindley Higgins at NeighborWorks America; my reader, Conrad Egan at the National Housing Coalition; and Keith Getter, at the NeighborWorks America Northeast district office in New York City, where I was based. I would also like to thank Karen Phillips, a commissioner of the New York City Planning Commission, for first introducing me to the need for greater coverage of this topic.

Abstract

This paper inventories strategies for maintaining affordable housing toward perpetuity in hot markets in an increasing number of locales. Long-term affordable housing strategies answer the call to make affordable housing resources last longer as federal funding for affordable housing diminishes, rental affordability programs expire, and owners prematurely buy their way out of affordable mortgages. The need is especially acute in hot-market cities, like New York City, that have seen large development programs end without any adequate replacements. The strategies span rental and homeownership delivery mechanisms, subsidy and equity sharing, cooperatives and community governance, land regulation, extending existing termed programs, and amassing funds to sustain affordable housing, with a focus on producing long-term affordable units through inclusionary zoning. Interviews with national policymakers and experienced affordable and mixed-income housing developers bring new light to the success of these mechanisms.

This study finds that neither relying on inclusionary zoning nor extending affordable housing programs should be considered a replacement for federal subsidies. Innovating new programs means setting numbers of units produced against longevity, affordability and occupants' capacity to generate equity. Recommendations are given first in terms of challenges, tensions, trade-offs and new questions that these strategies create, and then to specific actors in the policymaking arena. Nonprofits should focus on monitoring long-term affordability and accountability. Municipalities and local governments should better regulate sources and uses of housing trust funds, focus on helping fund first-time homebuyers, consider input from local developers, consider long-term inclusionary zoning regulation, and monitor productivity and long-term regulation. Policymakers and researchers should consider why potential homebuyers have selected riskier subprime mortgage products over more secure equity-sharing products and might want to better advertise equity-sharing options. Finally, New York City should expand its voluntary inclusionary program to more neighborhoods and better track its production and longevity.

Table of Contents

Table of Figures

I. Study Aims and Goals

This paper aims to describe policies for long-term affordable housing in an accessible form, compare long-term policy options both for creating long-term programs and extending existing programs, and focus on the increasingly significant issues of homeownership and inclusionary zoning in hot markets. Inclusionary Zoning (IZ) is a supply-side strategy for hot markets in which a specified percentage of a development is produced as affordable housing, usually as part of a density bonus. Municipalities are increasingly exploring the strategy as a means to regulate affordable housing tenures for 30 years to perpetuity.

II. Introduction

As federal funding for affordable housing has diminished since the 1980s, cities and states are vigorously seeking ways to stretch the tenure of their affordable-housing investments. This increasing interest in “long-term affordable housing” echoes the ongoing changes in housing funding and the shortcomings of existing affordable programs in hot-market locations. Displacement is a growing problem, as many of the 10-, 15-, 20-, and 25-year rental affordability programs that were created in the 1980s expire or as owners prematurely buy their way out of affordable mortgages in order to take advantage of the hot real estate market. With federal funding from the Department of Housing and Urban Development (HUD) decreasing, and multiyear waitlists for voucher-based Section 8 subsidies, supply-side place-based units have become the growing sector of affordable housing development. States and municipalities have fewer resources to build affordable housing and greater interest in sustaining it. This paper will inventory policy mechanisms, with a focus on homeownership, that exist for longer terms than traditional programs, discuss their inherent tensions, and consider input from national policymakers and housing developers on how to productively structure long-term and inclusionary affordable housing policies.

Context and Relevance

As funding for development and preservation dwindles and as for-profit developers buy themselves out of affordability agreements to take advantage of hot real estate markets, local government housing authorities seek opportunities to make lasting investments in affordable housing. HUD-funded municipal affordable-housing investments are replacing traditionally sponsored housing development for individuals of moderate income (80% area median income), low income (60% AMI) and very-low incomes (30% AMI). The public housing and Section 8 programs were conceived in perpetuity, but the last decade has found city housing authorities converting some public housing properties to the market while funds for Section 8 continue to shrink per capita. The most formidable funding source today for new affordable housing on the national level is the Low Income Housing Tax Credit (LIHTC), which funds affordable rental properties. Most states use a Housing Finance Agency (HFA) to set the guidelines for bidding on their scarce supply of tax credits. The federally regulated LIHTC tenure is 15 years; however, some states have imposed longer regulation requirements. Long-term affordable-housing programs are particularly relevant to investigate because they answer the call for an affordable housing source to supplement or replace the insufficient supply of expiring federally- and locally-financed affordable housing with new mechanisms capable of stretching the tenure of new affordable housing and sustaining mixed-income communities. Two policy vehicles for long-term local affordability of particular growing interest today are inclusionary zoning ordinances and community land trusts, both of which more communities are using to regulate affordability toward perpetuity.

Declining Supplies of Affordable Housing in Hot Markets

Despite the efforts of many cities, affordable units are being lost at a rate far faster than they can be created. New York City provides a good example when discussing affordability, given its broad array of expiring affordable programs and lack of affordability at nearly every income stratum. Many affordable housing buildings were erected since the 1960s, and most buildings built before 1974 are likely to contain rent-regulated units. For the first time in decades, since 2000 New York City has many record years of new residential construction. Despite this growth in the overall stock, increases in the luxury housing supply has led to a decrease in the affordable housing supply, defined as units affordable to households spending 30 percent or less of their income on housing. New York City lost over 32,340 units of privately owned rental-subsidized housing between 1990 and 2005,[1] at a rate of 2,000 to 6,000 units nearly every year since 1997.[2] The loss includes the sale of Manhattan's biggest affordable developments in 2006, Stuyvesant Town and Peter Cooper Village, together making up 11,232 units. MetLife, which built and sold these complexes to Tishman Speyer for $5.4 billion, estimated that by 2018, 70 percent of its units would be deregulated from rent stabilization, compared with 30 percent in 2006.[3] Rent stabilization, New York state's successor to New York City's nearly defunct rent control policies, governs rent increases until individual units crest at a $2,000 per month ceiling or a household's income exceeds $175,000. In 2006 Starrett City Associates also tried to sell Starrett City, a 5,881-unit development in Brooklyn, the largest Mitchell-Lama project. The New York City and state affordable-housing programs lost 24,000 units before 2004, and 26,000 more since as buildings leave the program.[4] Real estate values escalating faster than incomes rendered an additional 205,000 units unaffordable to households making 80 percent of AMI ($50,000 for a family of four) between 2002 and 2005.[5] New York's statistics are representative of the national scene, where 1.2 million rental units with monthly rents below $400 were lost between 1993 and 2003.[6]

New York City can provide lessons for all hot markets. It has far more robust subsidized affordable-housing development programs than any other American city, and precedent-setting experience tracking expiring units and monitoring displacement problems. Today the

[1] Community Service Society of New York, May 22, 2007; www.cssny.org/news/releases/2007_0522.html.
[2] Community Service Society of New York, "Policy Brief: Closing the Door," Figure 1, May 2006.
[3] New York *Times*, "Complexes' Seller Pushes Profits, as Critics Fear High Rents," Sept. 23, 2006.
[4] New York City Comptroller, "Affordable No More: An Update," May 26, 2006.
[5] Association for Neighborhood and Housing Development, "Housing Preservation as Important as New Construction," in Public Advocate for the City of New York, *Twelve for 2030: Responses to PlaNYC*, April 2007; www.pubadvocate.nyc.gov/policy/documents/Gotbaum_2030_response.pdf.
[6] Harvard Joint Center for Housing Studies, State *of the Nation's Housing 2005*, "Measuring the Nation's Rental Housing Affordability Problems," June 2005, p. 41.

city is striving to add 165,000 new units to its affordable supply by 2013 as part of its PlaNYC initiative. As municipalities work to develop affordable housing stock nationwide, they can learn from New York City's dilemmas involving expiring units.

The Daunting Task of Preservation

The task of preserving units building by building is a heroic undertaking, one that requires convincing a developer to give up the higher rents they speculated they would obtain in a hot market. Over the last decade, many affordable housing developers bought themselves out of affordable mortgages early so that they could take advantage of the market. Rather than only pursue preservation efforts, advocates are looking to long-term affordability mechanisms, such as extending affordability tenure guidelines under inclusionary zoning. This paper investigates the policies and ideas that have been suggested to implement this housing mechanism, and finds that they may be more complicated than advocates would prefer.

The Search for Affordable Housing: Gentrification, Displacement, Migration

The search for affordable housing today is the probable cause of the "greatest population redistribution since the dust bowl…'more significant than the migrations of the 1950s or 1970s.'"[7] The Harvard *State of the Nation's Housing 2007* report states that "affordability problems remain the nation's fastest-growing and most pervasive housing challenge."[8] Current typical searches for affordable housing take lower-income households from gentrified urban neighborhoods to the exurban fringe, and from foreclosed homes generally to rental or regulated affordable housing. In 2006, outer suburbs of hot market cities — notably in California, home of most of the nation's hottest housing markets — saw the fastest rates of population growth.[9] (In 2007, analysts predict a slowdown in migration to California.[10]) Housing can still sometimes be built at prices affordable to those with moderate incomes in exurban locations where land is cheaper, but exurban locations have the drawback of having the highest average commuting costs. However, for most moderate-income Americans, finding affordable housing is becoming an economic impossibility for the simple reason that "slow growth in wages for households in the bottom three-quarters of the income distribution is not keeping pace with escalating housing costs."[11] Creating "workforce housing" for "working families," meaning affordable housing for teachers, police, and other residents who make cities function is receiving political, real estate, and policy backing.[12]

---

[7] *Forbes*, "The Great American Migration," 7/16/07, www.forbes.com/2007/07/16/suburbs-growth-housing-forbeslife-cx_mw_0716migration.html; *USA Today*, "Pennsylvania Officials Concerned about Migration from New Jersey," July 15, 2007, www.usatoday.com/news/nation/2007-07-15-altoona_N.htm.

[8] Harvard Joint Center for Housing Studies, *State of the Nation's Housing 2007*, press release at the National Low Income Housing Coalition, www.nlihc.org/detail/article.cfm?article_id=4261&id=61.

[9] *Forbes*, "America's Fastest Growing Suburbs," July 16, 2007, www.forbes.com/forbeslife/2007/07/16/suburbs-growth-housing-forbeslife-cx_mw_0716realestate_2.html.

[10] Bruce Norris Group, June 21, 2007, www.rismedia.com/wp/2007-06-21/expert-says-californias-real-estate-crisis-will-be-worse-than-most-analysts-realize.

[11] Harvard Joint Center for Housing Studies, "Affordability Problems Escalate Even as Housing Market Cools," June 13, 2006, www.ksg.harvard.edu/ksgnews/PressReleases/061306_sonh.htm.

[12] The Urban Land Institute founded its initiative on Workforce Housing in summer 2007: www.uli.org/Content/NavigationMenu/Research/Initiatives/WorkforceHousing/Workforce_Housing.htm;

Many housing policymakers have taken great note of today's domestic migrations. What is clear today is that in hot markets, subsidies have become necessary for low-income and workforce households to be able to live near their workplaces.

Progressively minded jurisdictions, many of which are in coastal hot markets, have been tending to adopt housing policies with the intention of building mixed-income communities. Many of these mixed-income communities have also adopted inclusionary zoning or other long-term affordability measures.

III. Methodology

Research informing this study include the following:

- Literature search
- Interviews housing policy professionals
- Interviews national developers with experience building affordable housing

Definitions

Long Term: For the purposes of this paper, 30 years or more will be considered “long term,” taking as precedents expiring rental Low Income Housing Tax Credit (LIHTC) projects built by private, for-profit developers with regulated tenures of 10, 15, 20, and 25 years. Rhetorically, goal-oriented definitions are more useful; for example, “homeownership programs that keep units affordable to subsequent buyers,” or “subsidized-unit programs that avoid displacement,” potentially in perpetuity. These definitions allow many more types and durations of programs to fit under the rubric of long-term affordability and to inventory comprehensively their sets of workable policies.

Shared Equity: Long-term homeownership programs are based on equity-recapture or equity-retention provisions, which either recapture the initial subsidy amount or grow the subsidy to keep the unit affordable to subsequent buyers without new additional gap financing. Subsidy retention, pioneered by researcher Rick Jacobus of the Burlington (VT) Community Land Trust in 2001, is the focus of many of the shared-equity policy reports written by national housing policy organizations in 2006 and 2007.[13] (Following a merger with Lake Champlain Housing Development Corporation in October 2006, the Burlington Community Land Trust is now known as the Champlain Housing Trust.)

Shared-appreciation mortgages, shared-equity mortgages, limited-equity cooperatives and community land trusts are the best examples of programs based on shared-equity models. They assign homeowners an equity cap, or tie equity to a market index like area median income (AMI). They aim to give homebuyers a home that they could not otherwise afford, and with reasonable potential for equity growth, in exchange for avoiding the risk of potentially dangerous or potentially risky subprime mortgages.[14]

Inclusionary Zoning (or **Inclusionary Housing):** This involves policies on a neighborhood, municipal, or state scale that require or use incentives to encourage a percentage of set-aside affordable development for housing projects above a minimum threshold size. These policies are described in greater length below.

[13] John Emmeus Davis, “Shared Equity Homeownership: The Changing Landscape of Resale-Restricted, Owner-Occupied Housing,” NHI 2006; Rick Jacobus and Jeffrey Lubbell, “Shared Equity, Transformative Wealth,” NHC 2007; Caplin et al., “Shared-Equity Mortgages, Housing Affordability and Ownership,” Fannie Mae Foundation, 2007.
[14] Interview with Jim Gray, National Cooperative Bank: Capital Impacts, Washington, DC, August 24, 2007.

Mortgage-Interest Tax Deduction: By far the nation's largest housing subsidy is the mortgage-interest tax deduction, administered by the Internal Revenue Service. Designed to encourage investment in homes, the program has no cap. In 2006, deductions worth an estimated $76 billion were claimed by homeowners of all income strata,[15] roughly 120 times the amount spent on the LIHTC program. Over half of the deductions went to the 12 percent of taxpayers with incomes over $100,000. This program is not usually thought of an affordable housing subsidy, but the federal tax structure does clearly reward homeownership. The result is the unquestioned goal of increasing the homeownership rate. One recent unfortunate consequence of that policy has been the rise of predatory lenders targeting people who do not understand or cannot afford the financial products they are purchasing.

Hot Housing Markets: Affordable-housing developments, and their long-term affordable-housing regulation systems, are most common in hot housing markets, where housing affordable for households making at or less than the local AMI is not available. Table 1 shows the least affordable housing markets in 2006, as determined by comparing median house price to median household income.[16] Los Angeles leads many California Metropolitan Statistical Area (MSA) markets as the least affordable. New York City, the source of the above statistics, is not nearly the least affordable MSA. Notably, most of the 29 MSAs (among the 105 MSAs tracked) that are above the national average affordability ratio of 4.6 are on the East or West Coast, or in growing Sun Belt regions.

Figure 1: Least Affordable Hot Housing Markets, 2006

Los Angeles–Long Beach–Santa Ana CA MSA	10
San Francisco–Oakland-Fremont CA MSA	9.8
San Diego–Carlsbad–San Marcos CA MSA	9.5
San Jose–Sunnyvale–Santa Clara CA MSA	8.9
Honolulu HI MSA	8.6
Riverside–San Bernardino–Ontario CA MSA	7.6
Miami–Fort Lauderdale–Miami Beach FL MSA	7.2
New York–Northern New Jersey–Long Island NY-NJ-PA MSA	7.1
Sarasota-Bradenton-Venice FL MSA	6.7
Sacramento-Arden-Arcade-Roseville CA MSA	6.5
Reno-Sparks NV MSA	6.3
Bridgeport-Stamford-Norwalk CT MSA	6.3
Seattle-Tacoma-Bellevue WA MSA	6.1
Las Vegas–Paradise NV MSA	5.9
Boulder CO MSA	5.9
Washington-Arlington-Alexandria DC-VA-MD-WV MSA	5.7
Eugene-Springfield OR MSA	5.5

[15] *New York Times Magazine*, "Who Needs the Mortgage-Interest Deduction?" March 5, 2006.
[16] Harvard Joint Center for Housing Studies, *State of the Nation's Housing 2007,* May 2007.

Boston-Cambridge-Quincy, MA-NH MSA	5.4
Providence-New Bedford–Fall River RI-MA MSA	5.3
Portland-Vancouver-Beaverton OR-WA MSA	5.3
Tucson AZ MSA	5.3
Cape Coral–Fort Myers FL MSA	5.2
Orlando FL MSA	5.2
New Haven–Milford CT MSA	5
Chicago-Naperville-Joliet IL-IN-WI MSA	4.9
Milwaukee-Waukesha–West Allis WI MSA	4.8
Tampa–St. Petersburg–Clearwater FL MSA	4.8
Portland–South Portland–Biddeford ME MSA	4.7
Phoenix-Mesa-Scottsdale AZ MSA	4.7
National Average	*4.6*

Notes: Median House Price/Median Household Income Ratio;, metropolitan affordability table, ranked (29 MSAs above national average of 4.6, among 105 MSAs)

Source: 2006 statistics, reported in Joint Center for Housing Studies' *State of the Nation's Housing 2007.*

III. Policy Inventory

Affordable and long-term housing policies use three major types of delivery vehicles: (1) financial mechanisms (e.g., subsidies, grants, deductions, abatements, credits, below-market financing), (2) deed restrictions, and (3) land use regulations (i.e., zoning). Most programs use combinations of the three vehicles. Units can be rental (R) or homeownership (HO) in nature, depending on the municipality. A number of reports look at these strategies in greater detail.[17] A matrix of these policies can be found in the appendix.

Delivery Mechanisms for Affordable Housing Policy

Operating Subsidies and Financing (R, HO)

Below-market financing or a subsidy is generally what makes affordable housing affordable. The financing package subsidizes construction and/or operation. Conventional affordable-housing programs provide operating subsidies or financing for a fixed term. Long-term programs extend conventional terms or are built to operate for longer tenures. Homeownership programs subsidize units up front. Programs with the goal of long-term homeownership use equity sharing to cap owner equity and to recapture or retain affordability for subsequent buyers.

Deed Restrictions, Restrictive Covenants (R, HO)

Deed restrictions are the legal restrictions placed on affordable units of all kinds that mandate occupant income restrictions, affordability tenures, and other regulations. Restrictive covenants must be followed in order to gain and retain title to a restricted unit. Because deed restrictions must be closely monitored, especially for long-term programs, it is best to fund a monitoring agency in conjunction with the program, and even a title agency as well.

Within a deed restriction, a sponsoring agency can reserve the legal right to object to a sale. Rights of First Refusal (ROFR) grant the local housing agency (or other contracted non-profit) the right to oversee each transaction and approve both parties, throughout the tenure of a unit's regulated life. This condition — that a transaction can be challenged if the new owner does not fit the target population — implicitly strengthens the restriction. Little data exists on how frequently ROFRs are exercised in practice.

Land Regulation (R, HO)

Most broadly, zoning (and, more commonly, inclusionary zoning) specifies what land can be used for residential development and can contain mandates and incentives for affordable

[17] Rick Jacobus and Jeffrey Lubbell, "Preservation of Affordable Homeownership: A Continuum of Strategies," NHC April 2007; John Emmeus Davis, "Shared Equity Homeownership: The Changing Landscape of Resale-Restricted, Owner-Occupied Housing," NHI 2006; Brad Lander, "Concept Paper: Creating Permanently Affordable Homeownership from New York City's Inclusionary Zoning Program," Pratt Center for Community Development, August 2006; Greg deGiere, "Permanently Affordable Housing," California State Senate Office of Research, January 2003; Association for Neighborhood and Housing Development, "Moving Toward Permanent Affordability," April 2007.

housing. Detailed zoning is a mechanism used in hot markets that increases land value by limiting development densities.[18]

Subsidies and Equity Sharing

Rent Subsidies (R)

Although outside the focus of this paper, Section 8 rental vouchers deserve mention as the archetypal rent subsidy program, utilized nationwide, that many housing policymakers consider the best source of long-term affordable housing. The vouchers are made available through all levels of housing agencies. Some municipalities have developed other local voucher programs modeled on Section 8 for more specific populations, such as the homeless. As the cost of subsidizing vouchers to fill the gap between occupants' very-low or low income and the market is costly, Section 8 is losing funding per capita.

Shared Equity (HO)

Shared-appreciation mortgages and shared-equity mortgages are the main financial products that deliver shared equity to an individual homebuyer while keeping the unit affordable to a subsequent buyer and preserving continuing affordability in perpetuity. New advancements in shared equity extend to preferring subsidy retention over subsidy recapture, in order to make the original subsidy grow with housing cost increases while also earning appreciation for the homeowner. Traditional housing value appreciates and builds the homeowner's equity, whereas in a shared-equity partnership, the buyer's capacity for appreciation is limited. In the recapture model, the exact amount of the public funds used to initially make the unit affordable is recaptured when the unit is sold. In hot markets, the initial funds may not be enough to keep the unit affordable to subsequent buyers. Subsidy retention solves the recapture model fund shortage by allowing the public funds to appreciate with the property, to keep the unit affordable to future buyers.

Nonetheless, shared equity is contentious as some policymakers argue that limiting equity requires taking part in a complex program for little more return than a rental. Shared equity caps and indices have been a prolific area of policy research in 2006 and 2007. Rather than picking a fixed cap rate, many reports suggest the merit of tying equity caps to AMI growth, which has grown at least 3.35 percent in every seven-year period since the 1950s.[19] Shared equity can also help troubled borrowers provide returns for curative gap capital. Shared-equity mechanisms are a growing area of interest today.

[18] Edward Glaeser and Joseph Gyourko, "The Impact of Building Restrictions on Housing Affordability," *Economic Policy Review*, June 2003.
[19] Brad Lander, "Concept Paper: Creating Permanently Affordable Homeownership from New York City's Inclusionary Zoning Program," Pratt Center for Community Development, August 2006; "Preservation of Affordable Homeownership: A Continuum of Strategies," NHC April 2007, p. 40.

Cooperatives and Community Governance

Limited-Equity Cooperatives (HO)

Limited-equity coops (LECs) are generally the least costly form of homeownership. Market-rate coops and LECs are most common in Washington, DC, and New York City. In a coop, residents join to form a property tax–paying cooperative. Each resident owns a share of the building and land (or the building on long-term leased land) and pays a proportional share of its mortgage and taxes. In this way each member receives the homeownership mortgage-interest tax deduction. Because the share is personal property and not real property, there are no real estate transaction fees when a resident leaves the coop and ownership shares change hands. LEC residents recover their initial share of the investment plus simple interest (capped at 10 percent annually). While they prevent subsidized homeowners from capturing great increases in the value of their homes when the market goes up, LECs also shield members from great losses if the market goes down. Also, by keeping housing prices low, they allow some low-income homeowners to diversify their holdings with other investments. Despite their complexity, LECs lose their affordability unless the limited-equity provisions are structured for perpetuity and monitored. Coops have also lost popularity in recent years, LEC formation having peaked in the 1980s and 1990s. Single-family houses and condos have become more common typologies for both market-rate and affordable housing.

Mutual Housing Associations (HO, R)

Subsidized, affordable Mutual Housing Associations (MHAs) are nonprofit associations that govern initial subsidies and determine income qualifications and terms of affordability. An association's board is made up of tenants, lenders and local government representatives. As with an LEC, members enjoy the benefits of homeownership through personal investment in the association, but without the use of shares. In practice, initial subsidies are sometimes insufficient for maintenance and replacement reserves sufficient for long-term affordability.

Community Land Trusts (HO, R)

In a community land trust (CLT), a tax-exempt, nonprofit membership organization owns the land, and residents and other community members can invest as members. Residents, housing coops or mutual housing associations own the buildings separately and have the rights to use the land. As in an MHA, governance is through a board composed of residents, community members, public agency representatives and business professionals. As in an LEC, these require ongoing monitoring and technical assistance; unlike LECs they are usually used to make owner-occupied, single-family homes permanently affordable to homeowners, and can also be structured as rentals. CLTs are similar to other land trusts, which use land for conservation and recreational functions.

Land Regulation

Inclusionary Zoning (HO, R)

Inclusionary zoning (or inclusionary housing) is a land use regulation that requires or incentivizes developers to build an affordable percentage (generally five to 25 percent) for projects above a minimum size threshold. Ordinances can be mandatory or voluntary, on-site or off-site, and vary considerably in required affordability tenures. Voluntary programs frequently offer a density bonus, more rapid permitting, or additional financing options. Some states (e.g., Massachusetts, California and New Jersey) require localities to fulfill inclusionary measures, which are intended to create and sustain mixed-income communities or buildings, or to keep workforce employees near the schools or precincts where they work. However, many ordinances offer off-site provisions or let developers opt instead to contribute to a local housing trust fund. Inclusionary policies have existed since the late 1970s in California and Maryland, but have become more effective since 2000 at producing tens of thousands of units nationwide. Growing interest in inclusionary zoning in scale and long-term provisions constitute the policy focus of this paper, as discussed in the next section.

Extending Existing Termed Programs

Use Agreement Options (HO, R)

Exemptions from the real estate or income taxes that a developer usually pays are among the existing ways that conventional affordable housing is made affordable. These restricted "use agreement" options allow a municipality to opt out of taxes or market financing on to fulfill its policy choice to forgo a tax in exchange in order to encourage development of affordable housing.[20] Real estate tax exemptions are a common and conventional mechanism to support affordable housing. Long-term use agreement options continue these arrangements in perpetuity. Advocates of long-term exemptions would like to see them zoned around transit hubs, as with inclusionary zoning, to create mixed-use, affordable "old urbanism" districts. As with exemptions today, they could be delivered in the form of tax exemptions to form the basis for eligible units through abatements, tax credits, subsidized loans, extended financing to limit debt service payments, impact fee exemptions, or nonamortizing loans.

Amassing Funds to Sustain Affordable Housing

Impact Fees, Exactions, and Housing Trust Funds (HO, R)

A final topic to note is the use of housing trust funds to fund long-term affordable housing. Unlike the aforementioned strategies that directly maintain housing affordability, creating a long-term housing trust fund is a means for collecting funds and then distributing or redistributing them for specific projects or uses. The funds generally come from impact fees and exactions per square foot of development, and can then be directed to keep affordable housing affordable for the long term, provide gap financing between unit occupants or for low- or very-low-income occupants, or even to recapitalize existing projects in need of improvements.

[20] Interview with Aileen Gribbin, Forsyth Street Advisors, New York City, May 10, 2007.

IV. Policy Focus: Inclusionary Zoning

Inclusionary zoning has become a popular vehicle for providing regulated affordable housing for terms of upwards of 40 years or permanently. A supply-side, hot-market strategy, a specified percentage of the development (usually five to 25 percent) is developed as affordable. These affordable set-asides may be mandated or part of a voluntary bonus. IZ has precedents in land-use regulation (zoning), deed restrictions, public-private partnerships, mixed-income communities, impact fees, exactions and housing trust funds. By tailoring combinations of these provisions in localities and states, inclusionary ordinances produce public-private partnerships on a large scale, wherein developers get development rights and sometimes extra density, more rapid permitting, or more attractive financing in exchange for building affordable housing.

Inclusionary zoning has attracted a good deal of attention. Physically, it is attractive to planners, and it works in both suburbs and major cities. Rather than designating individual sites as affordable, zoning a percentage of parcels for partial affordability appears seamless and invisible, as well as providing a means to generate mixed-income communities. Unlike other housing policies, IZ uses a cheap municipal resource that is hypothetically in great supply: additional density floor area ratio (FAR). Additional development rights are an incentive to developers to continue giving in perpetuity, and are a good exchange for affordable building in perpetuity. But housing policymakers warn that IZ is not the panacea that advocates presume, as the discussion below indicates.

Literature on Inclusionary Zoning

Inclusionary zoning regained the attention of the policy community between 2001 and 2004, when many large cities were considering ordinances. Boston, Denver and San Francisco already had mandatory inclusionary provisions. In 2006 and 2007, state and national think tanks wrote more papers extolling the productivity of inclusionary zoning, especially in California and the suburbs of Washington, DC.[21] Developers and realty organizations responded with warnings that IZ taxes developers, raises surrounding housing prices, and in some cases excludes housing development.[22] In 2007, the Furman Center for Real Estate and Urban Policy at New York University published the first nonpartisan, empirical study of inclusionary policies, which noted that inclusionary policies are a disparate group despite nominal similarities. In addition, while the number of inclusionary units produced has been steadily increasing, the ordinances that bring them about have also been regularly revised, on

[21] Non-Profit Housing Association of Northern California, *Affordable By Choice: Trends in California's Inclusionary Housing Programs*, August 14, 2007; Earlier IZ bibliography at PolicyLink, www.policylink.org/EDTK/IZ/resources.html and BPI www.bpichicago.org/rah/rihi_pubs.html.
[22] National Association of Home Builders, *The Myths and Facts about Inclusionary Zoning*, September 2006, www.nahb.org/fileUpload_details.aspx?contentTypeID=3&contentID=63298&subContentID=81857; National Association of Realtors Resources, www.realtor.org/libweb.nsf/pages/fg806.

average every five years, in order to harness the level of productivity in the local housing market more effectively.[23]

Housing policy professionals and developers both laud and criticize inclusionary zoning. On the plus side, IZ policies allow neighborhoods, cities and states to begin to think of or sell themselves as affordable to a certain extent, although few cities know precisely what percentage of their housing can be so designated. Inclusionary zoning clearly needs oversight, as well as frequent injections of additional financing to attract development and sustain affordability.

Models of Inclusionary Zoning

As the Furman study finds, an important point to make about inclusionary ordinances is that they appear to have very little in common. The most basic distinction is whether a designated affordable percentage is mandatory or voluntary. There are five basic models of inclusionary zoning:

- Mandatory with no exemptions, buyouts or offset options
- Mandatory with exemptions (e.g., projects with over 50 units)
- Mandatory with cost offsets (e.g., extra market-rate density bonus)
- Mandatory with buyout options (e.g., paying into a housing trust fund)
- Voluntary with cost offsets

The first case, in which mandatory inclusionary zoning functions as a tax on development, is extremely uncommon. An example would be a municipality building its affordability requirement into its existing height and massing restrictions, effectively charging an affordable housing FAR "tax" on developers. Most inclusionary policies instead employ some incentive system, frequently a density bonus greater than the required or optional affordable housing, or provide alternatives, such as a minimum project threshold size.

Unlike subsidy and finance packages used with older affordable housing, density bonuses are municipal resources that provide a valuable incentive in perpetuity in exchange for providing permanent affordable housing. Off-site options to develop affordable housing, exactions per square foot going into a housing trust fund, or donating land for future affordable housing are the most common buyout alternatives.

Scale Production

Inclusionary ordinances were first created in the mid-1970s, but have just begun producing in scale during the last few years. Mandatory programs produced 11,000 units nationwide

[23] Jenny Schuetz, et al., "The Effects of Inclusionary Zoning on Local Housing Markets," NYU Furman Center for Real Estate and Urban Policy, 2007.

between 2003 and 2006, out of a total of 45,800 units created since inclusionary programs began.[24]

Advocates Prefer Mandatory Programs

By 2003, California had created 34,000 units of affordable housing through 101 mandatory IZ programs,[25] while 105 voluntary programs in Massachusetts had created only 1,000 units. This disparity has led housing advocates to favor mandatory programs, and several cities have switched to mandatory IZ as a result, including Cambridge, MA, Boulder, CO, and Pleasanton and Irvine, CA.[26]

Developers Prefer Voluntary Programs

Mandatory IZ is effectively a tax on developers, while an incentive program provides a greater density bonus (subsidy) than does an affordability requirement (tax). In both models, market units cross-subsidize affordable units and the density bonus functions as a subsidy that is directly calculable in rent per square foot. Voluntary programs generally yield a larger bonus than an affordability requirement, giving developers a net subsidy. Frequently mandatory programs have no financial incentive besides allowing a developer to enter a very hot housing market such as the San Francisco Bay area or suburban Washington, DC. Lowering the barrier to entry, however, can be a valuable benefit to many smaller developers.

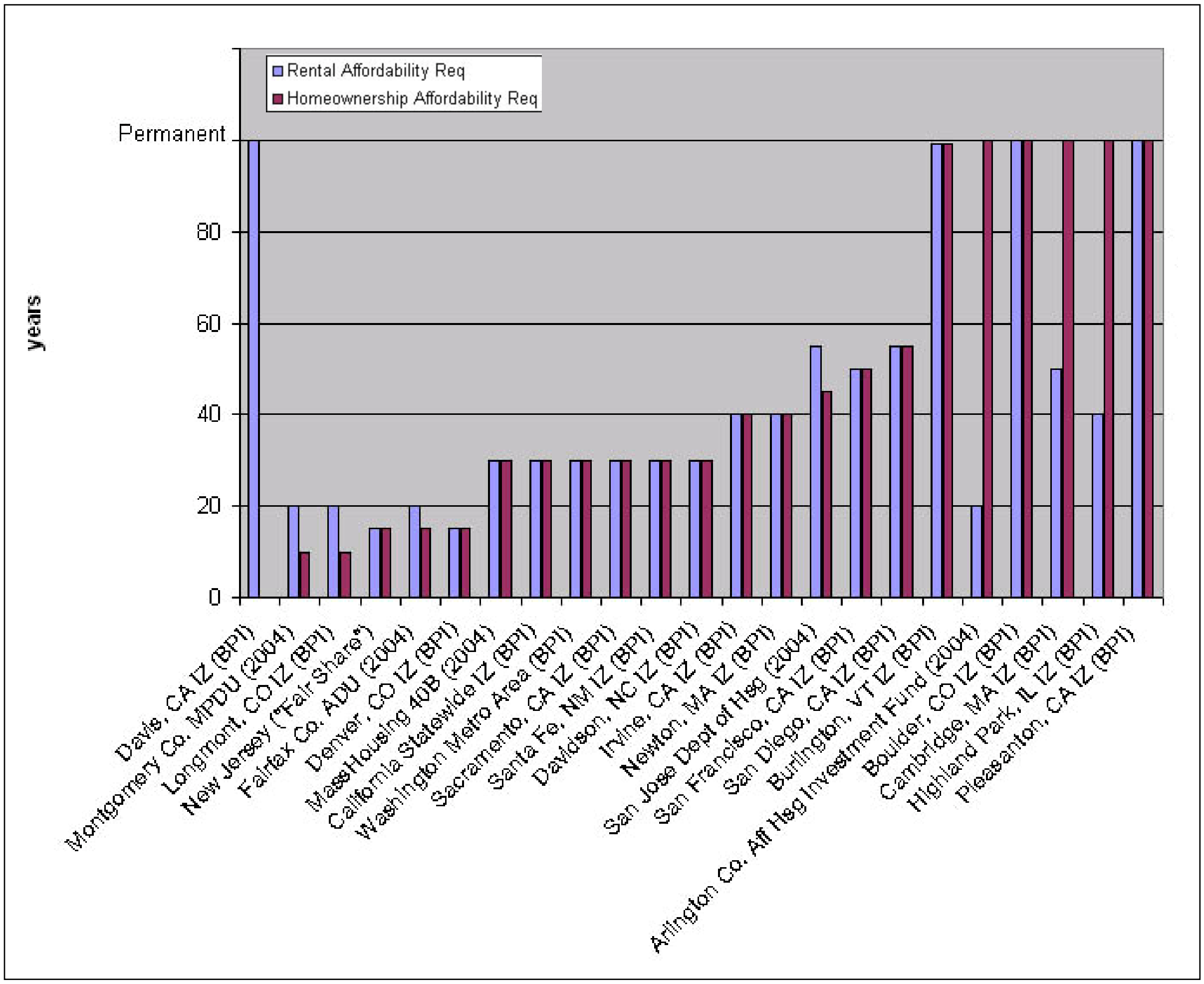
Regulated Tenure

Tenure under IZ moves the responsibility for legal regulation of affordable housing to zoning commissions rather than housing or financing agencies. In the case of Washington, DC, its commission chose to extend the whole program tenure to a permanent basis rather than have to revisit individual projects in the future.[27] Washington's precedent was the Moderately Priced Dwelling Unit (MPDU) program in suburban Montgomery County, MD, which extended its required regulated affordability in 2005 after most units had been sold out of the program at market prices. Tenures vary with local politics, but are increasingly being amended and extended. Washington, DC, and New York City use the word "permanence" in their ordinances, but define it as income restrictions for the life of the building. Other jurisdictions mandate specific tenures. Figure 2 shows tenures from around the country in 2004.

---

[24] Association of Neighborhood Housing Developers (NYC), "Moving Toward Permanent Affordability," April 25, 2007.
[25] Non-Profit Housing of Northern California and the California Coalition for Rural Housing, 2003.
[26] Fannie Mae Foundation, "Easing the Affordability Crunch: The Inclusionary Housing Option," August 2006, www.fanniemaefoundation.org/programs/hff/v8i1-inclusionary.shtml.
[27] Interview with Ellen McCarthy, former director of the Office of Planning, Washington, DC, August 25, 2007.

Figure 2: Required Affordability Tenure for Inclusionary Policies (State and Local), 2004



Source: Business and Professional People for the Public Interest, 2003, 2004.

Arguments Against Inclusionary Programs

A 2006 National Association of Home Builders (NAHB) report makes the case that all forms of inclusionary zoning essentially tax developers or neighboring residents in order to subsidize the lucky few.[28] Most of the subjects of the developer interviews conducted for this paper, however, are in favor of well-structured voluntary inclusionary programs that give incentives to developers, such as that of New York City. Economically, the NAHB argument is valid, in that mandatory IZ functions like a tithing. If a developer opts not to build in a jurisdiction because the market there is slow, then mandatory IZ is effectively exclusionary and counterproductive.

Both for-profit developer leaders with experience building affordable housing and national housing policy directors were interviewed for this paper. Input from developers, as from policymakers, falls across the spectrum of support. Some are against shared-equity arrange-

[28] National Association of Home Builders, "The Myths and Facts about Inclusionary Zoning," 2006.

ments, which homeownership through inclusionary zoning frequently involves, and believe that current policies have lost sight of the mission of affordable housing to build equity. More frequently, developers welcome the opportunity to build affordable housing whenever and wherever it can break even.

Input from Developers

On Inclusionary Zoning

Despite the NAHB argument against IZ, the Urban Land Institute (ULI), an influential national real estate development organization, started a new initiative for workforce housing in 2007. The ULI Terwilliger Center for Workforce Housing's benefactor and former ULI chairman, J. Ronald Terwilliger (CEO of Trammell Crow Residential, one of the nation's largest housing developers) actually advocated for mandatory inclusionary zoning as "one of the most effective tools to get affordable housing built" in a speech announcing the new ULI center and initiative.[29] This is an unprecedented statement from such a large developer to an organizational constituency of other large, for-profit developers. His $5 million donation, the largest ever made to the ULI, will be used to educate regional members and to spur development of 3,500 units of workforce housing, for households between 60 and 120 percent of AMI, in Atlanta, Southeast Florida and Washington, DC.

In general, developers tend to favor voluntary IZ. One described mandatory IZ as an unfair, industry-specific tax, pointing out that car manufacturers are not required to build extra cars and sell them below market to people with low incomes. Others felt that mandatory IZ could be a worthwhile entry ticket into certain profitable housing markets that would otherwise be difficult to enter.

On Long-Term Affordability

In California, long-term affordability is the norm: as projects financed with LIHTC bonds require a minimum of 55 years of affordability. California, enabled by its extremely hot housing market, is clearly a national leader in affordable longevity. The state is also a leader in adopting local inclusionary ordinances and producing units. A recent report found that by June 2006, 170 California jurisdictions with inclusionary policies had produced 29,281 units in the seven-year period since 1999.[30] Many municipalities have also recently amended their regulations to adopt permanent affordability.

California may be a role model for the rest of the country, but the state also has the significant advantage of being able to harness one of the most consistently hot markets of the last decade. The country's hottest housing markets are also the country's least affordable, as shown in Figure 1. Inclusionary zoning is an attractive tool for communities and local

---

[29] Urban Land Institute, "Former ULI Chairman J. Ronald Terwilliger Provides $5 Million to Fund ULI Terwilliger Center For Workforce Housing," February 1, 2007, www.uli.org/AM/Template.cfm?Section=Home&CONTENTID=81968&TEMPLATE=/CM/HTMLDisplay.cfm.

[30] NPH, August 14, 2007. It also reports that 80,000 people have been housed in California inclusionary programs to date, though not distinctly between 1999 and 2006.

governments in hot housing markets to promote social equity through the strength of the market.

On the East Coast, where long-term programs are less common and geographically smaller, some developers claim that long-term shared equity homeownership is a bad deal for unsophisticated homeowners. One developer suggested that homebuyers invest in certificates of deposit (CDs) instead, since they would yield a higher return.

Example: Inclusionary Zoning in New York City

New York City's improved 2004 IZ revision now involves five neighborhoods. Developers and housing advocates laud Commissioner Shaun Donovan for skillfully tapping the knowledge of area developers and nonprofits with an ordinance that attracts profitable affordable housing development. The New York City voluntary IZ ordinance gives a 33 percent density bonus as-of-right in exchange for requiring 20 percent affordability for the life of a project. The result is a 13 percent bonus of market-rate density in exchange for participating in the city's inclusionary program. The ordinance was written with the realization that in the city's hot market of the last several decades, this bonus space will make it more profitable to develop inclusionary housing. In New York City, inclusionary housing is one of several bonuses associated with the city's intricate and extensive zoning resolutions. Other precedents include community facilities, privately built public parks, plazas and arcades, and even theater preservation.

Voluntary Density Bonus Structuring

New York City housing policymakers have contentions with several areas of the ordinance despite the enthusiasm of developers. In the rezoning of Greenpoint-Williamsburg, the first outer-borough neighborhood to be zoned on an inclusionary basis (in 2004), advocates charge that the inclusionary ordinance gives away density bonuses rather than calculating for density profitability; that is, that the city simply decided how much extra density was suitable for the inclusionary parcels, rather than picking a target internal rate of return (IRR) and calculating backwards, using prevailing prices per square foot, to determine how much extra density bonus to award. Advocates claim that modeling proposed densities, particularly for the yet-finalized Hudson Yards midtown Manhattan business district extension, yields extreme densities while giving developers excessive profits. Had the city built from profitability upward, advocates claim, it could have given away much less density based on home sales rates per square foot since 2004.[31]

[31] Aaron Yowell, et al., "Inclusionary Zoning for New York City: Predictions and Recommendations for Hudson Yards, Greenpoint-Williamsburg, and Beyond," *Wagner Policy Review*, vol. 14, 2007.

Considering Homeownership

New York City's inclusionary zoning resolution notably includes no homeownership provision, although one has been under development unofficially for years. Local nonprofits, particularly the Pratt Institute Center for Community and Economic Development, which previously partnered with PolicyLink to write influential inclusionary zoning studies that influenced Washington, DC's, ordinance development in 2004,[32] have suggested adopting Jacobus's community land trust model and pegging equity appreciation to area median income growth.[33] However, the City Department of Housing Preservation and Development (HPD), rather than producing a public answer or an official equity-sharing arrangement, so far has permanent income restrictions for rental units produced under inclusionary zoning.

Tracking Performance

At this time New York City's inclusionary zoning program has been considered too new to track. HPD does know that the program produced 300 units in 2006; however, it does not know the number or percentage of developers on eligible sites that opt in or out of inclusionary affordable housing.[34] Despite having produced a small number of the 18,000 units that HPD built in 2006, IZ is an exception in the context of the city's New Housing Marketplace Plan (set to build 165,000 affordable units by 2013), which is assembling aggressive unit production quotas for a number of other housing production programs. The IZ program does seem promising: 300 units in five neighborhoods is more than Washington, DC's, annual goal of 170 units.[35]

Example: Chicago Community Land Trust

In 2006, Chicago became the first city government in a large, hot market to start and run a community land trust. As of 2008, it has 250 units in the pipeline, and a plan for 1,000 total units. If it reaches its projection, it would be larger than the Champlain Housing Trust (formerly the Burlington Community Land Trust), the most well known in the nation, which has 650 units. The Chicago municipal CLT is the first sign that the CLT model is ready for mass production in a hot urban market and can be run feasibly through the collaboration of city housing agency staff and a nonprofit board, rather than a municipally funded nonprofit. Through this initiative, the Chicago CLT was able to forgo nonprofit setup and administration hurdles, as well as unit construction, since it is taking affordable units already being built by other city programs and adding them to the community land trust.

There is excitement about CLTs in the housing world for two main reasons: (1) they have separated landownership from homeownership (owned by separate community organizations), thus (2) making single-family homeownership units that will sustain

32 Interview with Ellen McCarthy.
33 Brad Lander, Pratt Center for Community and Economic Development, August 2006.
34 Interview with Arden Sokolow, director of Inclusionary Zoning, NYC HPD, July 2007.
35 Washington, DC, Office of Planning, "Initial Impact Analysis of IZ Mapping," September 25, 2006.

affordability through successive owners using initial subsidies for perpetuity. CLT innovators, primarily Rick Jacobus, deserve credit for championing the long-term, shared-equity homeownership model that other delivery systems, such as homeownership inclusionary zoning in Washington, DC, are now implementing though other mechanisms in addition to CLTs.[36]

CLTs are increasing today. The number of CLTs in the U.S. has doubled since 2001 to over 200. As of late 2006, however, they have only produced about 6,500 units of housing nationwide since 1968.[37] Most CLTs involve about 50 units, composed of single-family houses, and in medium to hot northeastern markets.[38] The Chicago CLT is an anomaly in administration and scale. Success in Chicago, or Westchester County, NY (which began in 2007), could make this model more attractive to hotter market cities. Scale and location is central in evaluating CLTs. Local governments should take note of Chicago's CLT to see if operating one on a larger scale is feasible for municipalities in the hottest urban markets.

[36] Interview with Ellen McCarthy.
[37] Gregory Ingram, "Report from the President: Community Land Trusts," Lincoln Institute of Land Policy: *Land Lines*, October 2007.
[38] Yesim Sungu-Eryilmax and Rosalind Greenstein, "A National Study of Community Land Trusts," Lincoln Institute of Land Policy, 2007.

V. Findings: Inherent Challenges, Tensions and Trade-Offs

Expert Innovation vs. Expert Skepticism

Developers' skepticism of shared-equity homeownership leads to a stalemate similar to policy professionals' applause for Section 8. Housing policymakers have spent the past decade coming up with new and unorthodox funding sources: density bonuses, advanced legal restrictions, partnerships with developers, and equity from new homeowners. Despite the promise of these creative funding streams, these innovations do not equitably replace the present dearth of federal affordable-housing subsidies.

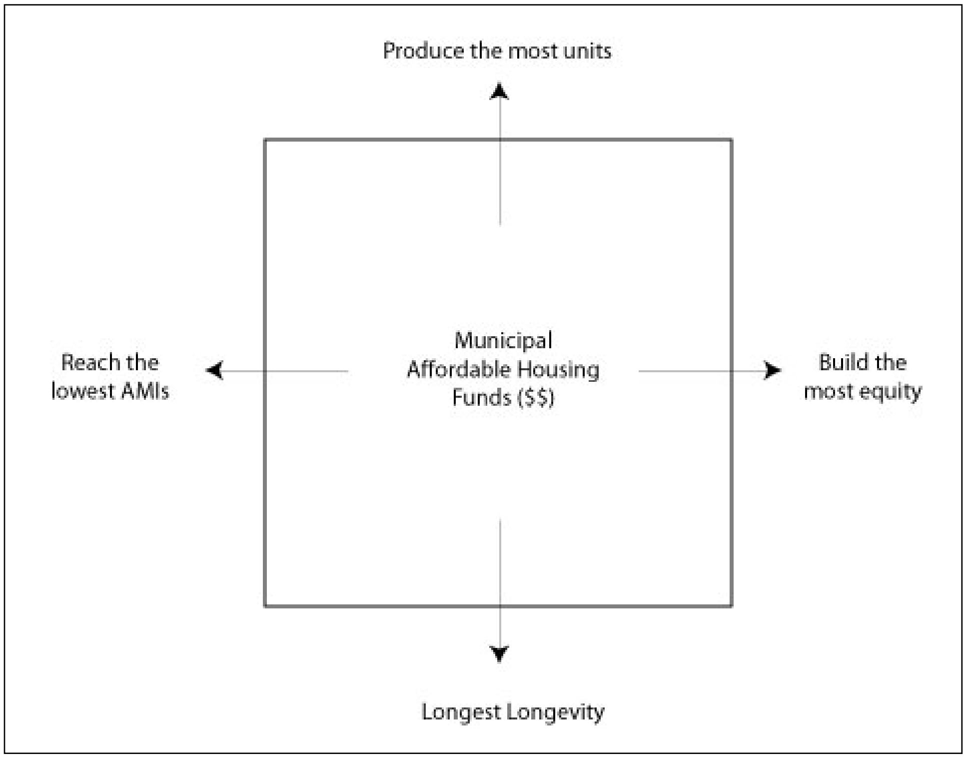
Lacking federal support, housing policymakers have worked to find the best balance between equity building, subsidy retention and financial mortgage products that are safe and desirable for unsophisticated homebuyers and investors alike. Despite these advances, with more sophisticated aspirations and less financial backing per capita, today's tools for providing affordable housing remain a set of "pragmatic approach[es]… to a set of utopian aspirations,"[39] a critique also made of LECs in the past. It is easy to be skeptical of today's prospects for long-term affordable homeownership. One developer blamed the "me generation" for fewer housing subsidies and blamed policymakers for losing sight of HUD's original goals. But with fewer subsidies for affordable housing today, and longer-regulated longevities sought, there is no perfect balance. Homeownership usually offers shelter, stability and equity. Long-term affordable options seem destined to offer fewer benefits, given less equity.

Unit Production vs. Target Affordability vs. Regulated Term vs. Equity Building

Like increases in the homeownership rate, high unit production tends to get the best press. Policy reports that laud high unit creation in their findings, however, do not register other equitable affordable-housing production outcomes. Creating a large number of units may come at the expense of reaching households with lower incomes and creating units with longer-regulated tenures, and may also render housing trust funds smaller for future financing or recapitalization, or may lack adequate program oversight, as depicted in Figure 3.

[39] Duncan Kennedy, "The Limited Equity Cooperative as a Vehicle for Affordable Housing in a Race and Class Divided Society," *Howard Law Journal*, vol. 46, 2002, p. 86.

Figure 3: Local Affordable Housing Expenditure Tensions



To illustrate these trade-offs, consider a municipality that is comparing IZ to CLTs in order to produce long-term affordable homeownership. To date, municipalities have found IZ much more flexible. It doesn't require buying land, and the Furman Center has found that most municipalities alter their ordinance about every five years. The outcome of many of these inclusionary alterations is longer affordable tenures, but perhaps these changes come at the expense of reaching lower-income households or of building equity for new homeowners. Long-term affordability policies seek to stretch limited resources. The most full-featured policies require municipalities to make significant investments.

Political Saliency

While long-term affordable housing mechanisms certainly go beyond the scope of a political term and can leave a salient legacy, the long-term aspect of a local program may be less salient for some politicians than creating more units, increasing overall levels of home-ownership, or helping constituents with the greatest financial need. Given that long tenure may be in financial conflict with other housing needs that can be accomplished immediately — and taken credit for, long-term programs are likely to continue to find difficulty garnering political backing.

Ensuring Housing Trust Fund Results

The Furman Center has found that many cities require less money to be given to housing trust funds than would ordinarily be required to build a new unit.[40] This complicates arguments for inclusionary zoning. The public sector needs more transparent accountability regarding housing trust funds. Their expenditures are also more complicated because units may be more costly overall than the developer may have anticipated, due to factors such as provision of a longer tenure, a greater subsidy to meet lower income requirements, or provision of gap financing to keep an existing unit affordable. This is especially important to consider as Congress considers legislation to create a national housing trust fund.

Homeownership Issues

Consequences of Emphasis on Homeownership

Because the IRS awards homeownership with one of its biggest tax deductions, encouraging homeownership investment encourages liquidity in the economy. Individuals and politicians alike see it as an unquestioned American goal. The predatory-lending crisis clearly raises flags that this goal should be questioned, especially for low-income buyers.

Shared equity for low-income buyers, however, is stable and sustainable. As an added perk, shared-equity homeowners also qualify for the homeownership tax deduction. This may not be worth much to them, but they do get most of the advantages of homeownership, including a safe investment with stable appreciation.

Homeownership Trends: Condominiums and Houses Favored Over Co-ops

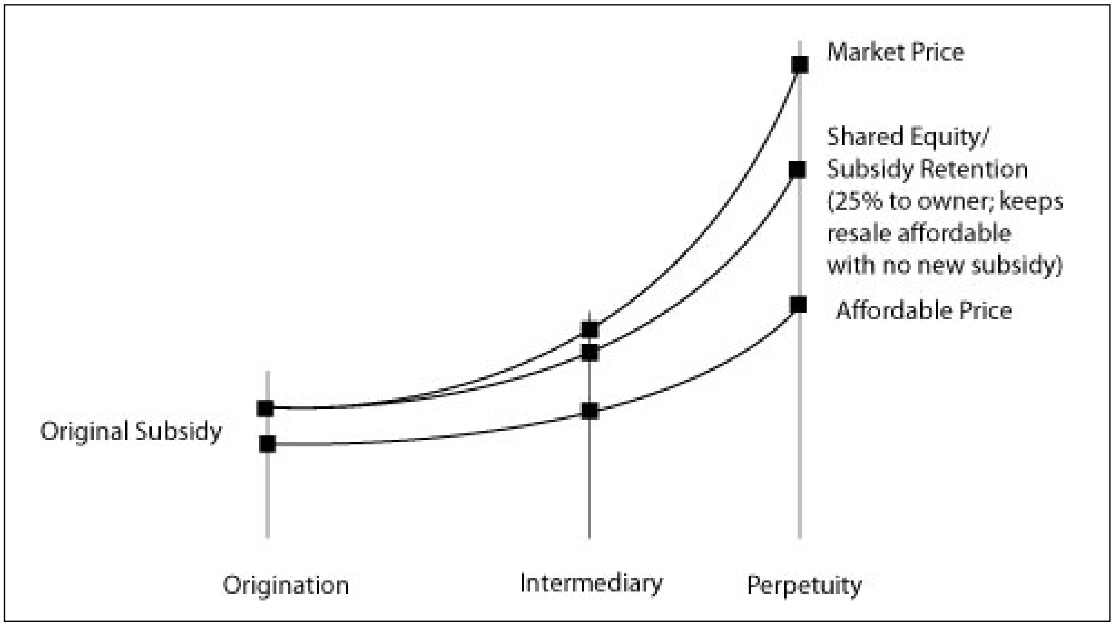
Homeowners want the equity and asset of a mortgage that enables them to refinance and “use their house like an ATM.” This is a big reason that condos have much greater market share in multifamily buildings than coops, both in the present and the probable future. Given the decreasing market preference for coops, IZ and CLTs are replacing LECs.[41]

Finding the Right Amount of Shared Equity for Homeownership Mechanisms

Shared equity is the current hot-button homeownership issue. Policymakers who make use of it need to decide how much appreciation is enough to maintain the unit for the next buyer, and how much is enough to make it a good investment by the homeowner. Ultimately, not all goals can be addressed at the same time. The National Housing Conference papers on shared equity (2007) recommend subsidy retention wherein the original subsidy is recaptured plus a share of the appreciation, as in Figure 4 (below).

[40] Shuetz, et al. 2007, p. 9, citing California Coalition 2003, Brown 2001, Rubin, et al. 1990, Hughes and McGuire 1991.
[41] Interview with Jim Gray.

Figure 4: Shared Equity Maintains Unit Affordability and Builds Limited Wealth



Note: Image based on Rick Jacobus and Jeffrey Lubbell, "Preservation of Affordable Homeownership: A Continuum of Strategies," National Housing Conference/Center for Housing Policy: April 2007.

To consider a case of how to choose an equity-sharing model, New York City housing advocates have been suggesting various models to the city's HPD in the hope that it will introduce an IZ homeownership program. In 2006 the Pratt Center for Community Development recommended using Rick Jacobus's CLT model and tying appreciation to AMI growth (rather than 5 percent per year on equity), and to share 25 percent of appreciation with the homeowner.[42] The model favors sustainability over substantial asset building for homebuyers, but offers them a house that is larger or has a better location than they would otherwise have been able to afford. This reflects the city housing agency's concerns about what could happen if AMI decreases.[43]

Redesigning a Framework for Upwardly Mobile Homeownership

Creating a shared-equity program to match the politics and market of any locality that adopts the goal of long-term homeownership is a big undertaking. The lengths of many recent reports on shared equity attest to how challenging it can be to sell the concept of shared equity to homeowners, builders and leaders.

What are the ultimate goals and how much equity is necessary to:

…attract homebuyers?
…create upwardly mobile homebuyers?

[42] Brad Lander, "IZ Homeownership Concept Paper for NYC HPD," Pratt Center for Community and Economic Development: August 2006.
[43] Interview with Arden Sokolow, July 2007.

…sustain affordability between owners?
…convince homebuyers to maintain and improve their homes?

Hypothetically, any share would help a responsible investor who lacks existing assets. But how much is necessary to make a good investment compared to other nonrisky investments, such as certificates of deposit?

Increased Regulated Tenures

Lengthening affordability creates some new questions for administering bodies about the most equitable uses of a limited number of affordable housing units. Should one occupant be able to keep a unit for his or her whole life, or should there be time limits for individual occupants in order to share a unit among many occupants? If a unit will eventually expire after an extended term, is the extension beneficial or is it just postponing the inevitable expiration — and pushing the search for replacement units to future administrators? Is extending tenure a good use of resources when those resources might be able to make a unit affordable to tenants with lower AMIs for a shorter period?

Limits on Tenant Tenure?

Whereas conventional affordability measures expire, long-term affordable housing allows municipalities to preserve their housing stocks potentially forever, while also enabling individual households to avoid displacement. Municipalities may not want to give individual households permanent benefits, or may want to limit their ability (as with rent control) to pass the unit on to others. In the long term, some municipalities may rethink their affordable housing philosophies.

The "Year 99" Problem

Postponing displacement under a long-term program does not avoid it. However, postponement does give municipalities time to establish more stable affordable-housing stocks. Localities can also decide whether to disallow developers from buying their way out of affordability terms prematurely. Nonetheless, some housing policymakers who were interviewed are skeptical of longer-term programs, perceiving them as only delaying inevitable displacement. They see the program term as being arbitrary if residents know about it in advance.

Deepest Affordability vs. Longest Affordability

For every ten units of public housing, a city could create 170 units of Section 8 housing.[44] For long-term programs, municipalities can choose subsidy sizes to reach households on lower to higher levels of the AMI scale that will make the affordability period longer or shorter. In localities with the hottest housing markets, such as California, these goals may not necessarily be in conflict with each other.

[44] Interview with Jim Stockard, Commissioner, Cambridge (MA) Housing Authority, June 2007.

Shared Equity and Upward Mobility

Learning About Limited-Equity Homeowners

Researchers know less about affordability issues that involve homebuyers than those that involve renters. How do municipalities test how limited-equity homeownership and appreciation sharing affect asset building and upward mobility? Does the percentage of equity cap correlate with the upward mobility of low-income homeowners? How do municipalities judge the efficacy of limited-equity homeownership as an asset-building tool for low-AMI households? Researchers could work with municipalities to see how these particular homeowners invest, refinance, or even buy other real estate.

Hypothetically, municipalities could prohibit refinancing and let limited-equity homeowners realize gains only upon selling, thus making it possible for other households to take advantage of the unit. Opting to move is different from displacement. Given a nonexpiring homeownership unit with no individual tenure limit, homeowners would not be displaced. But would housing agencies want to create time limits for individual tenants?

Flipping vs. Long-Term Affordability

While “flipping” — fixing up a home and selling it for more in a short time span — is practically a professional sport in the normal market (even the focus of a reality television show)[45], many housing policymakers and developers believe that it is a good way for new homebuyers to learn to build equity. Flipping yields appreciation for low-income homebuyers. However, flipping cost Montgomery County thousands of the affordable housing units that it had successfully created during the first 25 years of the its Moderately Priced Dwelling Unit (MPDU) program, which is considered the first productive precursor to IZ policies. Its early-deed restrictions were set to five years in 1974, which was then revised to 10 years in 1981 when few affordable units remained in the program. In 1999, only 3,500 of the 10,600 units that had been created were still affordable. In 2005, the county raised tenure to its present regulated status: 30 years for homeownership and 99 years for rental.[46]

A third option is policies that incentivize ownership for five or 10 years. In most jurisdictions, using a long-term regulated tenure as a deed restriction is the best way to retain and sustain affordability. When banks make loans or owners get titles, a nonprofit monitoring agency can also be contracted to approve the sale or exercise a right of first refusal. Using an equity escalator, which limits a house’s equity appreciation rate until a specified year of ownership, e.g., year five, a municipality can discourage flipping while still building equity appreciation. Resale data for long-term homeownership is limited, although a 2007 CLT

[45] *Flipping Out*, with the subheader “Drama for Sale,” airs Tuesdays at 10 pm ET on Bravo, www.bravotv.com/Flipping_Out.

[46] John Emmeus Davis, “Shared Equity Homeownership,” NHI, 2006, quoting Karen Destorel Brown, “Expanding Affordable Housing Through Inclusionary Zoning: Lessons from the Washington Metropolitan Area,” Brookings, 2001.

study looks at home price resale calculations nationwide.[47] Future studies could determine more information about owner tenures, equity building, and why owners leave.

Designing an Inclusionary Ordinance

Long-Term IZ: Mandatory vs. Voluntary

Policy reports frequently recommend mandatory inclusionary policies over voluntary ordinances for their success in creating the most units. Mandatory policies have been more productive, but new research shows that there are so many other variables in inclusionary policies that generalizing about inclusionary policy is rarely useful.[48] Voluntary policies, such as those of New York City, if zoned in on a larger scale, may be productive in bringing a long-term inclusionary policy to a city which is politically and economically less disposed to mandatory inclusionary ordinances. Following the trend of other municipalities that have started with voluntary and moved to mandatory policies in order to boost production of affordable units, a voluntary inclusionary policy is a productive way for a municipality to test-drive inclusionary zoning on a small scale, before choosing to implement it more aggressively.

Structuring Density Bonus IRRs

Structuring voluntary inclusionary ordinances is rarely a public process, yet the density bonus is the operative part of making a voluntary ordinance successful. Voluntary ordinances work in sophisticated markets despite the preference expressed in policy reports for a mandatory approach. Determining the amount of extra market-rate floor area to offer as a cost offset is best done by determining internal rates of return (IRRs) first, and then solving for the necessary density bonus. New York City offers 12 percent to 20 percent,[49] while Seattle offers 14 percent.[50] Developers tend to be more focused on IRRs, while city agencies focus more on costs.[51]

Do Density Bonuses Lower Quality of Life?

The primary negative aspect of inducing development of affordable housing through a density bonus is that, arguably, density can increase too much. In a suburban area this may be less notable, but in cities where tall buildings lining individual streets can form peaks and valleys in the urban streetscape, adding more density may harm historic context or lower the quality of life.

[47] Sungu-Eryilmaz and Greenstein 2007.
[48] Shuetz 2007.
[49] Interview with Arden Sokolow of the NYC Housing Preservation and Development IZ unit, July 10, 2007.
[50] Bay Area Economics report, 2005.
[51] Interview with Ellen McCarthy.

VI. Conclusions and Recommendations

There is no simple answer to the efficacy or success of long-term affordable housing programs. "Affordable housing" is still an unfamiliar term to most Americans eligible for it. So too is common terminology for longer regulation periods. Beyond simply raising the visibility of these programs, their application procedures and their limited tenures, housing providers and advocates want to know how to follow and implement leads like that of California elsewhere in the country. Current attempts to stretch municipal resources in hot housing markets to produce units that will survive decades of affordable homeownership meet both praise and skepticism. More cities are trying shared-equity strategies. Extended affordable-housing innovations have great promise to create sustainable affordable-housing products that will remain affordable for successive owners in hot markets. As greater numbers of these units go online, the next few years will show how low-income homebuyers, neighbors and developers react to these new housing options.

Recommendations for Nonprofits

Monitor To Ensure Long-Term Affordability and Accountability

In order to maintain quality affordable housing through long tenures, nonprofits should advocate and work with municipalities to oversee that deed restrictions are met and that local housing trust funds are used to maintain or finance gaps. Ordinances that incorporate housing trust funds should also develop methods that ensure that exaction payments are made in amounts equal to the cost of building a physical unit.

Recommendations for Municipalities and Local Governments

Critical responsibilities for the local public sector include educating constituents about affordable housing and how to apply for it (and about concepts such as expiring affordability and use), determining the municipality's percentage of affordability, and setting new citywide goals. Addressing these concerns will make the municipality more attractive to existing and potential residents, and more competitive with neighboring cities.

Better Regulate Sources and Uses of Housing Trust Funds

The amounts that developers put in housing trust funds should be the same as the amounts they would spend building units. There are, however, many other uses for the funds. To use them for gap financing or recapitalizing later in the tenure of affordable housing is recommended for all municipalities, particularly those intending to sustain affordable units longer than 20 years. Reaching tenants with lower incomes, making physical improvements, and sustaining units for longer terms are all marks of healthy ordinances that may "cost" building fewer units upfront, a point lost in many policy reports.

Increase the Safety, Success and Longevity of First-Time Homeownership

Politicians are celebrated for raising homeownership rates, but receive little blame for encouraging the factors which lead to foreclosures. Becoming a new homeowner is a great achievement, but it is not suited to all buyers. The mortgage-interest tax deduction is a boon for homeowners with large incomes, but n empty promise for low earners. Regulated affordable-homeownership programs are a safer way to increase homeownership among lower- and moderate-income homeowners.

Consider Input from Local Developers

For-profit affordable housing developers build most of the affordable housing in the United States, yet they are infrequently consulted for input on ordinances, particularly local inclusionary zoning, that affect the way they build affordable housing. Developers interviewed for this paper unanimously agree that planning agencies should seek developer input when structuring inclusionary ordinances. Two main problems are that in public forums and task forces developers are frequently vilified, thus losing interest in participation[52]; and developers may be the object of backlash in their own communities for being perceived as contributing to an unpopular or mandatory inclusionary ordinance.[53] To resolve these issues, and receive input from the developers likely to build under their ordinances, municipalities should convene a separate developer task force, led by a nonpartisan chairperson.

Evaluate Long-Term Inclusionary Zoning

Zoning commissions in large cities may prefer the idea of making inclusionary housing permanently affordable so as to simplify the need to review individual applications for regulated tenure revisions or extensions. The simplicity of using long-term blanket zoning is seductive for planners and policymakers. Such a decision should be made with close supervision from the city housing department regarding economic concerns, however. Such concerns as calculating whether the local market is hot enough to continue encouraging development, determining the costs of extended mechanisms to developers at present and in the future, and offering subsidies or financing to ease those barriers are as important as considering the policy itself.

Monitor Inclusionary Effectiveness, Productivity and Longevity

It is vital to track the success of inclusionary program and the efficacy of restrictive covenants. It often takes years to create an ordinance, rewrite a city’s code, enable underlying legislation, and rezone neighborhoods with inclusionary zoning. All cities using voluntary programs should track the percentage of developers that opt in or out of inclusionary housing. At a later date they should use this information to re-examine the ordinance. It is equally important to see that affordable units are being filled by eligible people, in order to ensure that the appropriate income groups are being targeted.

[52] Interview with Thomas Bozzuto, executive vice president of The Bozzuto Group, Greenbelt, MD, August 25, 2007.
[53] Interview with Ellen McCarthy.

Evaluate More Long-Term Affordable Housing Programs at More Levels of Government

States interested in lobbying to adopt long-term, affordable rent-based programs such as California's 55-year regulation period (up from 15 years in most states) on bond-financed LIHTC projects, New York State's rent stabilization program for rentals under $2,000 per month, and Montgomery County, MD's, 30-year affordable inclusionary homeownership program should evaluate the barriers to developing affordable housing in local markets. Competition for limited resources such as the state's annual allocation of federal LIHTCs and the supply of parcels zoned for inclusionary programs should be compared to the financial benefits that the developer receives versus the tenure desired. For developers, advantages such as more rapid permitting, access to more subsidies, and parcels that make it easier to break into the housing development market can be necessary commodities. If the market is hot enough, decision-makers should determine the geographical regions where they can assemble the political will to extend existing resources, add new subsidies, or extend regulated tenure most productively.

Recommendations for Policymakers and Researchers

In order to help policymakers and affordable housing developers better structure their products and compete with potentially harmful market products such as subprime mortgages, it is important to determine what motivates homebuyers to choose long-term affordable-housing options.

Study Wealth-Building and Upward Mobility

Comparing equity built among different categories of investments for low-income families over time — e.g., rental (the null case), certificates of deposit, long-term shared-equity affordable homeownership, Section 8 homeownership vouchers, limited-equity cooperatives, subprime and prime homeownership — facilitates determining the thresholds of the useful amount of equity for low-income families to start building. It would be helpful as well to determine the importance of other factors, such as education about approaches to building wealth and becoming a homeowner.

Further research could investigate optimal tenures in affordable housing stays, from the standpoint of both homeowners and municipalities. Long-term affordable housing challenges the paradigm that families are forced out when the building's regulated affordability expires. Instead, given a potentially infinite tenure, municipalities may choose to limit the amount of time that an individual family can benefit from the resource. In order for both families and municipalities to gain optimum benefit, researchers should study the time value of upward mobility in affordable housing.

Recommendations for New York City

Some recommendations follow based on interviews conducted in New York City for this paper.

Expand Voluntary Inclusionary Zoning

New York City's voluntary inclusionary ordinance is a model for other hot urban markets. It harnesses the sophistication of the city's developers and housing policymakers, while not being as aggressive as inclusionary policies in several less hot urban markets. Developers around the country praise New York City's IZ ordinance. Nevertheless, the ordinance should be rezoned into more city neighborhoods that are able to support it. Washington, DC's, new IZ will cover the entire city. New York City has had IZ since the 1980s, but only the 2004 revision is proving productive. It applies IZ to neighborhoods of varied densities in more diverse parts of the city and makes more financing available to developers. Unfortunately, the city HPD does not monitor it closely enough to track the policy's performance. If most developers are opting in to build affordable housing — and at least some of them are doing it onsite — the ordinance will be more worthy of its praise.

Track Success of Inclusionary Zoning

The New York City HPD should track the percentage of eligible developers who opt in or out of IZ. It should also watch where those units are built, how far off-site, and whether they cluster. Under the current resolution, most will be built off-site on the cheapest sites within applicable community districts. Advocates charge, correctly, that this does not create the mixed-income communities that inclusionary zoning intends to promote, but instead creates pockets of lower wealth. As more neighborhoods are zoned according to IZ, the HPD should track longevity to see how long the "permanence" in the zoning code actually lasts.

Appendix: Long-Term Affordability Mechanism Matrix

	Type				Mechanism			Longevity	
	Demand-Side	Supply-Side							
	Individual	Community	City/State	Federal	Subsidy	Legal	Restriction	Tested long-term?	Example Locale(s)
HOT MARKET									
Macro									
Operating Subsidies and Financing (R, HO)	Yes	Yes	Yes	Yes	Yes		Yes	Yes	National, state HFAs, cities
Deed Restrictions, Restrictive Covenants (R, HO)		Yes	Yes	Yes		Yes	Yes	Yes	CLTs, IZ, LECs, MHAs, etc.
Land Regulation (R, HO)			Yes		Maybe	Yes	Yes	Yes	All levels of jurisdictions
Mechanisms									
Rent Subsidies (R)	Yes		Yes	Yes	Yes			Yes	Section 8, NYC HSP
Shared Equity (HO)		Yes	Yes		Yes		Yes	Yes	Burlington (VT), Chicago, etc.
Limited-Equity Cooperatives (HO)		Yes	Yes		Maybe		Yes	Yes	NYC, DC, NH
Community Land Trusts (HO, R)		Yes	Yes		Maybe	Yes	Maybe	Yes	Burlington (VT), Chicago, etc.
Inclusionary Zoning (HO, R)			Yes		Maybe	Yes	Yes	Yes	CA, DC, NJ, MA, NYC
Mutual Housing Associations (HO, R)		Yes			Maybe		Yes	Yes	CT
Extending Existing Termed Programs									
Use Agreement Options (HO, R)			Yes		Yes	Yes		No	Short-term, extension possible
Amassing Funds to Sustain Affordable Housing									
Impact Fees, Exactions and Housing Trust Funds (HO, R)		Yes	Yes		Yes	Yes	Maybe	Yes	Short-term, extension possible
COLD MARKET									
Market Homeownership	Yes	Yes					No	Variable	
Market Rental	Yes	Yes					No	No	

Note: Units can be rental (R) or homeownership (HO) in nature, depending on the municipality.

Interviews

Dena Al-Khatib
Executive Director
Chicago Community Land Trust, Chicago Department of Housing

Eric Belsky
Executive Director
Harvard University Joint Center for Housing Studies

Deborah Boatright
District Director, Northeast District
NeighborWorks America

Toby Buzzoto
Executive Vice President
Buzzoto Development Company
Greenbelt, MD

Donald Capoccia
Principal
BFC Partners
New York, NY

Kate Collignon
Senior Vice President, Special Projects
New York City Economic Development Corporation

Sarah Gerecke
Chief Executive Officer
Neighborhood Housing Services of New York City

Keith Getter
Management Consultant
NeighborWorks America, Northeast District.

Jim Gray
Vice President
National Cooperative Bank Development Corporation

Doug Guthrie
President
Kimball Hill Urban Centers
Chicago, IL

Dave Hanzel
Policy Director
Association for Neighborhood and Housing Development
New York, NY

Lindley Higgins
Applied Research Manager
NeighborWorks America

Kevin Kelly
President
Leon N. Weiner & Associates
Wilmington, DE

Duncan Kennedy
Carter Professor of General Jurisprudence
Harvard Law School

Brad Lander
Director
Pratt Center for Community Development

Jeffrey Lubell
Executive Director
Center for Housing Policy, National Housing Conference

Jay Marcus
Director of New York Programs
NCB Development Corporation

Ellen McCarthy
Director of Planning and Land Use
Nixon Peabody (formerly D.C. Office of Planning)

Danilo Pelletiere
Research Director
National Low Income Housing Coalition

Nicolas P. Retsinas
Director
Harvard University Joint Center for Housing Studies

Jenny Schuetz
Economist
Furman Center for Real Estate and Urban Policy, New York University.

David Smith
Recapitalization Advisors, Inc.
Boston, MA

Arden Sokolow
Director
Inclusionary Housing Program, New York City Department of Housing, Preservation, and Development

John Stewart
Chairman
John Stewart Company
San Francisco, CA

James Stockard
Commissioner
Cambridge Housing Authority and Loeb Fellowship Curator, Harvard Graduate School of Design

John Wall
President
Mid City Financial Corporation
Silver Spring, MD

Aaron Yowell
Attorney
Simpson Thacher & Bartlett

Bibliography

Articles

Bruce Norris Group. "Expert Says California's Real Estate Crisis Will be Worse than Most Analysts Realize." 6/21/07.

Forbes. "The Great American Migration." July 16, 2007.

Forbes. "America's Fastest Growing Suburbs." July 16, 2007.

USA Today. "Pennsylvania Officials Concerned about Migration from New Jersey." July 15, 2007.

New York Times. "Complexes' Seller Pushes Profits, as Critics Fear High Rents." September 23, 2006.

New York Times Magazine. "Who Needs the Mortgage-Interest Deduction?" March 5, 2006.

Press Releases

Community Service Society of New York, press release. "Closing the Door on Housing: New York's Affordable Housing is Under Siege." May 22, 2007.

Urban Land Institute, press release. "Former ULI Chairman J. Ronald Terwilliger Provides $5 Million to Fund ULI Terwilliger Center For Workforce Housing." February 1, 2007.

Harvard Joint Center for Housing Studies, press release. "Affordability Problems Escalate Even as Housing Market Cools." June 13, 2006.

Policy Reports

Association for Neighborhood and Housing Development. "Moving Toward Permanent Affordability." April 2007.

Bay Area Economics, 2005.

Fannie Mae Foundation. "Easing the Affordability Crunch: The Inclusionary Housing Option." August 2006.

New York City Comptroller. "Affordable No More: An Update." May 26, 2006.

Harvard University Joint Center for Housing Studies. *State of the Nation's Housing 2005.*

———. *State of the Nation's Housing 2007.*

National Association of Home Builders. *The Myths and Facts about Inclusionary Zoning*. September 2006.

National Housing Conference/Center for Housing Policy. "Housing America's Working Families." Series 2003–2006.

Non-Profit Housing Association of Northern California. *Affordable By Choice: Trends in California's Inclusionary Housing Programs.* August 2007.

Non-Profit Housing of Northern California and the California Coalition for Rural Housing. *Inclusionary Housing in California: 30 Years of Innovation.* 2003.

Public Advocate for the City of New York. *Twelve for 2030: Responses to PlaNYC*. April 2007.

Office of Planning. "Initial Impact Analysis of IZ Mapping." Washington, DC, September 25, 2006.

Works

Brown, Karen Destorel. "Expanding Affordable Housing Through Inclusionary Zoning: Lessons from the Washington Metropolitan Area," Brookings, 2001.

Brunick, Nicholas J. "Inclusionary Zoning: A Policy for the City that Works." Business and Professional People for the Public Interest, 2003.

Brunick, Nicholas J. "Opening the Door to Inclusionary Zoning." Business and Professional People for the Public Interest, 2004.

Caplin, Andrew, et al. "Shared-Equity Mortgages, Housing Affordability and Ownership." Fannie Mae Foundation, Special Report, 2007.

Davis, John Emmeus. "Shared Equity Homeownership: The Changing Landscape of Resale-Restricted, Owner-Occupied Housing." National Housing Institute, 2006.

deGiere, Greg. "Permanently Affordable Housing." California State Senate Office of Research, January 2003.

Glaeser, Edward and Joseph Gyourko. "The Impact of Building Restrictions on Housing Affordability." *Economic Policy Review*, June 2003.

Ingram, Gregory. "Report from the President: Community Land Trusts." Lincoln Institute of Land Policy: *Land Lines*, October 2007.

Jacobus, Rick and Jeffrey Lubbell. "Shared Equity, Transformative Wealth." National Housing Conference: Center for Housing Policy, 2007.

———. "Preservation of Affordable Homeownership: A Continuum of Strategies." National Housing Conference: Center for Housing Policy, April 2007.

Lander, Brad. "Concept Paper: Creating Permanently Affordable Homeownership from New York City's Inclusionary Zoning Program." Pratt Center for Community Development, August 2006.

Kennedy, Duncan. "The Limited Equity Cooperative as a Vehicle for Affordable Housing in a Race and Class Divided Society." *Howard Law Journal*, vol. 46, 2002.

Schuetz, Jenny, Rachel Meltzer and Vicki Been. *The Effects of Inclusionary Zoning on Local Housing Markets: Lessons from the San Francisco, Washington, DC, and Suburban Boston Areas*. Furman Center for Real Estate and Urban Policy (New York University): Working Paper 07-05, 2007.

Sungu-Eryilmax, Yesim and Rosalind Greenstein. "A National Study of Community Land Trusts." Lincoln Institute of Land Policy, 2007.

Waters, Tom and Victor Bach. "Policy Brief: Closing the Door: Accelerating Losses of New York City Subsidized Housing." Community Service Society of New York, May 2006.

Yowell, Aaron, et al. "Inclusionary Zoning for New York City: Predictions and Recommendations for Hudson Yards, Greenpoint-Williamsburg, and Beyond." *Wagner Policy Review*, vol. 14, 2007.