An Extreme Oversimplification of Affordable Housing Programs

Part 1: The History of the Four Main Federal Housing Programs

By Paul Malinowski

July, 2021

Draft

Introduction

You've probably all heard the terms: "low-income housing", "low-rent housing", "public housing", "subsidized housing", "affordable housing", "Section 8 housing", "tax credits" and on and on. Sure, people who work in that industry know exactly what each of those terms mean, but those terms are either Greek or word spaghetti to the rest of us. Should we learn them or can we just use them interchangeably? Well, the answer is "sort of" to both questions. Don't worry, it's not as intimidating as you might think.

In this paper I will attempt to bring some understanding of this complex industry to the rest of us. For now, we will call that industry "affordable housing" as a convenient generic label going forward. And we will assume "affordable housing" means any kind of rental housing that receives some form of government funding assistance that allows the rents to be less than market rents for people who would not have the financial means otherwise to afford market rents. I know that's a really broad definition, but it will work – for now.

I have written this paper for an audience of persons with developmental disabilities including families of loved ones with developmental disabilities in Colorado but obviously I hope this can benefit anyone who is confused about these terms and just wants to learn more.

We will need to take a brief history lesson first to help understand how those terms came to mean different concepts at the time each was in vogue. Of course, many of those terms are just phrases "du jour" likely to be replaced by something not yet created. But understanding terms can help alleviate misunderstanding when looking for "affordable housing" and maybe even avoid wasting time applying for housing programs that might not suit you or your loved one's needs.

I will be simplifying terms and details of housing programs as much as possible in this paper, to the extent of even oversimplification (thus the clever title of this paper!). If someone in this industry reads this, they may have a pompous reaction to that fact. That's okay. Tell them to just take two aspirin and call you in the morning. In the meantime, this should work just fine for everyone else.

I worked (and continue to work) in this industry for 45 years and understand that these programs are complex with twists and turns all of which are really irrelevant to most of us. Again, if you're in the industry I don't mean to offend as there are all kinds of spinoffs and sequels and niche programs. I'm also excluding rural housing programs such as those run by the old Farm Home Administration and now the Rural Housing Development Corporation as they are simply versions of these urban programs that preceded them. Those are not a focus here. And although I cover it below, one of those programs is almost extinct which leaves three. And of those three two are actually siblings of each other but since they are not "identical twins" I've given each a separate treatment here.

Thus, there are really only four main federal affordable housing programs in existence today so that is all I will cover in this paper. In Part 2 of this paper, I will go more into the details of how these programs work and how to apply.

Public Housing

Let's start all the way back in 1937. That was when Congress passed the first "affordable housing" law. That law, known as the United States Housing Act of 1937, created an affordable housing program called "public housing". More formally it was also called "*low-rent* public housing" or "low-income housing". When I was working in the industry, some people even called it "low housing" which is an incorrect term, even as slang, unless you are referring to homes with ceiling heights of four feet or less.

Public Housing provided a mechanism to fund the construction and then ongoing operation of affordable housing for people considered "low-income".[1] Funding for public housing went directly from the federal government to local *Public Housing Authorities* (PHA is the common acronym), also known as *Local Housing Authorities* (LHA is the common acronym). Over the years most cities in Colorado, from urban communities such as Denver, Pueblo, Boulder, etc., to rural ones like Burlington and

[1] The definition of "low income" has been a moving target over the years depending on what housing programs are involved and what period of time we are talking about. It is always best to stay away from this term unless used in a very generic sense rather than any quantifiable measure.

Center, for example, set up these local public housing authorities initially for the express purpose of developing and operating public housing. These public housing authorities were unique entities in that State law allowed cities and counties to create these public housing authorities as mostly semi-independent agencies from the city or county that created them to serve the same geographic jurisdiction. For many years all PHAs looked alike. The City Council or County Commissioners would appoint five citizens to the boards of the PHA as the governing board. Most communities appointed one member of the City Council or County Commissioners to the governing board who could serve as a liaison back to the Council or Commission. It was the PHA itself, not the City or County that would apply for, and if successful, then build, own, and operate public housing.

Thousands of public housing apartments were built over the years, helping low-income families, elderly or people with disabilities live in a community that had substantially reduced rents. Residents only paid 25% of their monthly income as rent, no matter how little their income was.

But there were issues that cropped up with this program because of the way the federal government set overall policy and funded the program. The first major issue was the federal policy of requiring a high amount of density in cities, especially for large families. Did you ever hear of a high-rise building in St. Louis called Pruitt-Igoe? It was a public housing development built in the 1950s that consisted of thirty-three 11-story buildings. It became a prototype of the now pejorative term, “the projects”. Social issues there multiplied and eventually the Public Housing Authority determined the buildings were no longer safe, decent or sanitary and ordered their evacuation. If it still doesn’t ring a bell, you might remember seeing the Pruitt-Igoe buildings being demolished wholesale starting in 1972. Videos of the demolition can be seen on YouTube.

Less dramatic, but equally prevalent, were other public housing properties that suffered from a constant, annual lack of proper funding from Congress to sustain these properties. Residents only paid 25% of their income as rent and since they had to be at a very low income level to even qualify, these public housing properties typically had very little revenue generated by rents. For example, a resident earning say only $400/month in income from public benefits paid $100/month as rent. The Public Housing Authority had to rely on additional funding from Congress and antiquated methodologies developed by the United States Department of Housing and Urban Development (HUD) to determine that funding. This was consistently inadequate to

cover expenses and maintenance upkeep. Thus, many public housing properties became “the projects” and were often a physical blight in their communities.

By the 1980s funding for new public housing was practically nonexistent. There remains relatively very little public housing left because public housing authorities were allowed to convert the public housing program to newer programs of affordable housing. A good example here locally in the Denver metro area is the old Lincoln Park Townhomes developed and owned by the Denver Housing Authority. They helped countless households financially but the property itself had a reputation as a “project” and eventually the Denver Housing Authority tore it all down and replaced it with more “mixed-income” affordable (and some not so affordable) rental housing. A public housing property could only be owned by a Public Housing Authority and not by a non-profit organization or a private landlord so only a Public Housing Authority has a public housing property in its portfolio of properties, if it even does.

Section 8

About forty years after the start of the public housing program, the program was for all intents and purposes being phased out as the main form of federally assisted affordable housing. In its stead came the “Section 8” program. “Section 8” referred to a section of the same US Housing Act of 1937 (Section 8, in fact!) that created the public housing program. Until the 1970s it was never invoked. When Congress then started funding that section of the Act to create this new affordable housing program it inadvertently created some confusion and some head-scratching. For until that time the term “Section 8” meant something totally different, i.e., the process of getting a discharge from the United State military being judged mentally “unfit” to serve. Despite the somewhat pejorative connotation, “Section 8” became the standard name of this new program.

Section 8 housing differed from its predecessor, public housing, in three ways:

1. Buildings could now be owned by non-profit agencies and private developers in addition to public housing authorities;
2. There was a much more effective mechanism of funding operating shortfalls than the public housing methodology since the buildings had to have some form of subsidy to be affordable to lower income households; and
3. The Section 8 subsidy could be tied to the household and not just the building.

Let’s focus on this last point. When the Section 8 subsidy provided by the federal government was tied to a specific building, it was referred to as “project-based” Section 8. When the Section 8 subsidy provided by the federal government was tied to a

household, it was referred to as "tenant-based" Section 8. The two forms of Section 8 both were funded by Congress at about the same time, and both ran as somewhat companion programs for many years. But there are very key differences. A very brief and simplistic version of how the two programs work follows.

Project-Based Section 8

In "Project-based" Section 8 developments, a private owner, non-profit organization, or PHA applied to HUD for subsidy to build or acquire and rehab a property that would have a Section 8 subsidy tied to the rental complex. If they were fortunate to get funding in this highly competitive program, they did everything a private developer would do for a conventional market-rate rental property on the development and construction side but then they could only lease to households that were under a specified income level, often referred to as an AMI (this stands for Area Median Income – more on this in Part 2). It's not important to know what those regulations were over the years (spoiler alert: they changed) but just know there are income limits and they may not be the same for all properties. A key feature, though, is that each household that qualified for an apartment would pay 30% of their "adjusted" (leaving the definition of this term for later) monthly gross income as their portion for rent. The federal government would then make up the difference between what the property owner would charge as "normal" rent in the form of a Section 8 subsidy. This is also called a "Housing Assistance Payment (HAP)". Same thing.

Well, how in the world would a property sustain a mortgage payment, utilities, taxes, insurance, repairs, staff, etc. on, say, an average of $1,000/month per unit rental income if all those other expenses I mentioned ran about $4,000 per month? It wouldn't. So, the federal government, through the US Department of Housing and Urban Development (HUD) sent the owner of a Section 8 building a subsidy to pay for that $3,000 difference. Of course, that is an oversimplification because the amount of the subsidy is based on some semi-mythical "market rent" (what a private owner would get renting to "market-rate" tenants), not the actual expenses. But the point is the gap is the Section 8 subsidy. Again, it is paid directly to the building's owner and not the tenant. All that means is that when a tenant moved out and another moved in, the property owner still received the Section 8 subsidy. The tenant that moved out loses the subsidy (again, it was the building's, not the tenant's). Hopefully, they would have found another Section 8 building or qualified for another affordable housing program. If not, they would have had to find "market-rate" housing or find alternative forms of affordability such as moving in with family or friends or a roommate.

In the 1970s and 1980s, Section 8 project-based housing was a very popular form of providing affordable housing. The building owner entered into a contract with HUD for Section 8 subsidies for various time periods that typically ranged from 20 to 40 years initially. Some had 5-year renewal increments with the property owner deciding if they wanted to renew each time.

Eventually, this funding mechanism fell out of favor. Congress deemed it too "expensive" and many building owners of Section 8 found it too restrictive and realized they could make more money with conventional, market-rate properties. Although many project-based Section 8 buildings remain in use today throughout the country, many building owners, especially in the early 2000s, opted out of the Section 8 contracts, effectively ending that building's affordability. Those owner "opt-outs", as they were called, displaced thousands of lower income households nationwide. Today, most (but not all) project-based section 8 properties are owned by either non-profit organizations or public housing authorities since those organizations are mission-driven rather than profit-driven.

Tenant-Based Section 8

The other form of the Section 8 program from the 1970s that still exists today is an even more popular version than the project-based Section 8 program. It is called "tenant-based" Section 8. It works very similarly to project-based Section 8 in that if the tenant household qualifies by being under a prescribed income limit, they will pay only 30% of their income as rent, regardless of the amount of their income. The difference of what the landlord normally charges, and the tenant portion is again the Section 8 subsidy and is paid directly to the building owner. But here are two key differences in the tenant-based Section 8 program as opposed to the project-based Section 8 program.

1. The tenant finds their own market-rate rental housing. Project-based Section 8 buildings are excluded because obviously they already have a Section 8 subsidy tied to the building itself. Unfortunately, not all landlords choose to participate in this program as the "red tape" can scare off landlords who may have misconceptions to begin with;
2. The subsidy stays with the tenant. If the tenant moves out of the rental unit they are in the subsidy stays with them assuming: a) they weren't evicted; and b) the next rental landlord also accepts participating in the Section 8 program.

In the early days of this program, which started in the 1970s, there were two versions of the same program with very minute differences. One program was called the Section 8

Certificate program and qualified households were said to have a "certificate". The other was called the "Section 8 Voucher" program and qualified households were said to have a "voucher". Eventually the Voucher program "won out" so it's all vouchers now. To confuse matters more, this Voucher program then began being called the "Tenant-Based Choice" program. Don't be confused. They are all the same thing and by now you should realize government programs love having multiple names – it helps to confuse us all!

Whatever the "nom du jour", this program remains a popular one today, generally garnering bipartisan support in Congress for annual funding levels. Republicans like that it uses private, market-rate rental housing spread out in a community while for Democrats it's a social program that helps people in need pay their rent also throughout a community. Regardless of why it's popular, it helps a lot of people but if funding were increased even more a *lot* more lower-income households would likely take advantage of this program as it suffers from long waiting lists in most communities.

The drawback to tenant-based Section 8 is that it does nothing to add to the *supply* of affordable rental units. Thus enters the fourth and last of the major federal affordable housing programs, the Tax Credit Program.

Tax Credits

First, let's get all the monikers of this program out of the way. There is the Low-Income Housing Tax Credit program, LIHTC (acronym of Low-Income Housing Tax Credits, actually pronounced Lie-tec), "Section 42 Housing" (of course there would be a number in a government housing program!), "Workforce Housing" and whatever gets invented tomorrow. I will simply use the term "tax credit housing" to refer to this program.

The tax credit program got off to a very slow start initially with legislation by Congress getting it going in the 1980s. It wasn't until the start of the 21st century that it really began to take off due to three factors:

1. Congress started to end the funding for the Public Housing program;
2. Congress started to drastically reduce funding for new Section 8 projects;
3. Real estate developers, both private and public, began to figure out how the program worked. It's not that the program is so incredibly complex (although it is – hey, it's a government program after all!), it's more that this was the first housing program administered by the Internal Revenue Service (IRS) and not HUD. Yikes! Who wants to experiment with the IRS? No one at first. But then it became wildly popular – with Congress, private developers, non-profit

organizations, and the good old PHAs who saw this program as a way to become relevant again.

Instead of pouring a lot of money into construction of housing like the public housing program did or paying large operating subsidies in the form of Section 8 subsidies to building owners as the Section 8 program did, this program simply gave tax credits to multifamily rental property owners who agreed to rent apartments to income-qualified households. That's a zero cash outlay because only tax credits that could be taken annually for a period of ten years were used to lure developers to build tax credit housing. That may be lost revenue to the federal coffers but if that property had never been built there would be no revenue "lost" anyway. That concept of no cash outlay and allowing private real estate developers to develop these types of properties has made tax credit housing a relatively popular bipartisan program in Congress.

Not all developers of tax credit properties are private developers. Non-profit agencies and PHAs both figured out that this was rapidly becoming the #1 affordable housing program around and could actually supply new housing units, so they also latched on to the program. What made this program unique from the others, though, is in the almost ideally forced partnership of private-public entities. For example, a PHA's or non-profit organization's mission might be to provide new affordable housing units in their community but since they are both tax-exempt, what good is getting tax credits off of non-existent income taxes? Answer: there is no benefit. So those groups began to form new ownership entities to own the actual property where they would own a very small portion of the property (think 1 percent or less) and sell the rest of the ownership rights to wealthy private organizations that need tax breaks. This is the proverbial win-win solution whereby the PHA or non-profit organization meets its mission of providing affordable housing in the community while private organizations meet their mission of reducing their tax liability for a period of ten years. I've seen many a tax credit property that has all three types of entities involved because per Colorado law, a property can also be exempt from real estate taxes if even partially owned by a PHA. Thus, you might have a private developer, non-profit organization, and PHA all be part owners in a tax credit building, all getting something out of it. And one last winner is the tenant and here's why.

If a property is a tax credit building the property owner must charge rents that are under market rate to be able to take those credits. There are rent "levels" as opposed to the public housing and Section 8 concept of paying a percent of income no matter what your qualified income is. Tax Credit housing tenants pay a flat amount of rent

depending on their annual income. I'll go into this more in Part 2 but generally most, if not all, apartments in a tax credit building will be under the market rate for a similar type of apartment but a key takeaway is that there are multiple fixed rent amounts.

Conclusion

So, to recap, there have been three or four primary affordable housing programs in the United State:

1. **Public Housing** – started in 1937. It allowed Public Housing Authorities to construct housing for low-income households. Not a lot of properties built under this program remain;
2. **Section 8** – This program has two components:
    a. **Project-Based Section 8** – started in the 1970s. It allowed private developers, non-profit organizations and Public Housing Authorities to receive Section 8 subsidies for ongoing operating costs so that tenants can pay only 30% of their income as rent regardless of their income. The subsidy stays with the building;
    b. **Tenant-Based Section 8** – started in the 1970s. It allows tenants to go out on the private market and find suitable housing and pay only 30% of their income as rent regardless of their income while the owner of the rental unit receives a section 8 subsidy. The subsidy stays with the tenant;
3. **Tax Credit Housing** – started in the 1990s. It allows private developers, non-profit organizations, and Public Housing Authorities to construct or renovate multifamily rental housing. Tenants get to pay a reduced rent compared to a comparable market-rate rental property and in exchange the property owner gets to take significant tax credits off of their federal income taxes.

In Part 2 of this White Paper oversimplifying federal housing programs, I'll go into a bit more depth on each program and where and how to apply.

(The author has worked continuously since 1977 in the affordable housing industry. He has served as Executive Director of two Public Housing Authorities, Executive Vice President of a housing non-profit organization, Property Manager at a private property management company, Owner of a property management company specializing in affordable housing, and Consultant to affordable housing organizations. He has been unsuccessful in his attempts to retire since 2015.)