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Should We Foster the Nonprofit Housing Sector as Developers and Owners of Subsidized Rental Housing?

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Abstract

The strengths and weaknesses of nonprofit organizations in developing and owning subsidized rental housing are examined. In the course of this study, a number of comparisons are made between for-profit and nonprofit developers.

The nonprofit housing sector, including both community development corporations as well as the larger regional and national nonprofit housing organizations, are credited with having produced or rehabilitated more than 1,252,000 units of housing and more than 295,000 units, respectively. Taken together, these organizations have produced about one-third of the units in the social housing sector, which totals about 4.6 million units.

Since the 1960s nonprofits have been the beneficiaries of a number of federal programs and, more recently, they have been singled out for preferential treatment in several initiatives.

The unassisted private housing market generally does not provide sufficient profit for for-profit developers to build or maintain decent quality housing that is affordable to lower income households. In comparison with for-profits involved with subsidized housing, nonprofits typically focus on more distressed areas and their developments are typically targeted to harder-to-house populations.

For-profit developers typically have important attributes that make them attractive developers and owners of housing that is affordable to low income households. In particular, they generally bring significant financial and technical resources to a given deal. The ability of for-profit developers to cover the costs of acquiring land or buildings, as well as the up-front development costs, often allows them to move more quickly and efficiently than nonprofit organizations. Perhaps the major criticism of for-profit developers relates to the inherent contradiction in their need to make a profit and the potential for this to come into conflict with the long term affordability needs of low income residents, as well as the public purpose implicit in subsidy programs, as demonstrated in the "expiring use" crisis.

Supporters of nonprofits point to their commitment to produce housing that is affordable to lower income people over the long-term, as well as to stimulating investment in neighborhoods in need of revitalization, discussed above. In addition, nonprofit housing providers are credited for their connections to community and residents, their commitment to providing services for residents, and their potential for accessing affordable land and buildings.

Two central questions relate to the relative strengths and weaknesses of for-profit and nonprofit sponsorship of housing that is affordable to low income households. The first question asks whether it is more cost-effective to pursue one strategy or the other. The second questions the long-term viability of projects developed by each type of sponsor. The answers to both questions, however, are far from conclusive. But when nonprofit costs are found to be higher, researchers invariably note that this needs to be considered carefully, in the context of the other benefits that are typically associated with nonprofit-produced and owned housing.

The answer to the question about whether we should foster the nonprofit housing sector as developers and owners of subsidized rental housing is an unequivocal "yes."

For any developer or organization to be an effective housing producer and long-term owner, a number of competencies are necessary. In addition, the context in which development is taking place should be conducive to this activity. Nonprofits and for-profits may be differentially able to take advantage of these conditions. Twelve of the most important requirements—both organizational and contextual— for the successful development of subsidized housing are presented. Of course, it does not have to be either-or. There is fertile ground and a significant

amount of experience with nonprofits and for-profits joining together in partnership arrangements and some of the key requirements for such efforts are discussed.

Introduction

In view of the ongoing need for rental housing that is affordable to households earning 80 percent of median income, or less, policy makers, academics, government officials, and foundation personnel often question the type of entity that is in the best position to develop and own this housing. There are three broad types of options: the public sector through local housing authorities; the private for-profit sector; and nonprofit organizations.

While it is beyond the scope of this paper to examine the relative advantages and disadvantages of the public housing approach, suffice to say that one of its greatest drawbacks is the persistent negative public image. Although the stereotypical "project" exists more as a myth than a reality, and the overall record of the public housing program is far more positive than is generally acknowledged, there is an ongoing perception that public housing represents a glaring governmental failure. Garnering public support for public housing, even with efforts to clarify the true contributions of this strategy, would likely be difficult, at best.

This paper focuses on the strengths and weaknesses of the third major approach: the role of nonprofit organizations in developing and owning subsidized rental housing. Nonprofit developers of housing are tax-exempt organizations. They may make a profit on their activities, so long as this income is used to further the purposes of the organization. Nonprofit organizations are limited on how distributions of income can be made to those in control of the organization and other private parties: charitable corporations cannot distribute any gains, profits or dividends to its members, directors, or officers (National Housing Law Project, 1982, 3-4; Steinberg, 1998).

In contrast, for-profit entities have an explicit responsibility to their shareholders to maximize earnings. In fact, a corporation's failure to fulfill this duty can result in shareholders suing members of the board of directors or the corporation's officers (Hinkley, 2002).

In the course of this investigation, a number of comparisons are made between for-profit and nonprofit developers. Specifically, this paper:

- examines the growth of the nonprofit housing sector, focusing both on community development corporations as well as on the larger regional nonprofit housing developers and owners;

- discusses the special preferences nonprofits receive in government programs and provides an overview of other key sources of support including the nonprofit intermediaries that provide funding and technical assistance for nonprofit producers;
- explores the types of properties owned, target populations served, and other services provided by nonprofit developers, as well as for-profits involved with subsidized housing;
- presents the arguments in favor and against fostering the nonprofit and for-profit sectors as long-term owners of subsidized housing; and
- offers recommendations concerning optimum roles for nonprofit, as well as for-profit, producers and owners of subsidized rental housing.

Growth of the Nonprofit Housing Sector[1]

A Brief History

Nonprofit involvement in housing can be traced to the reform movement of the early 20th century. These early efforts—which involved limiting the profit that private entrepreneurs could realize from building model tenements—are not viewed as having been successful:

> In some cases, "model" tenements turned into slums as bad as ordinary free-enterprise tenements. The movement failed to generate enough capital to make a real impact on the slum problems…Either model housing had to be abandoned as a solution, or some further incentive had to be provided. Some subsidy—or at least cost reduction—was necessary (Friedman, 1968, 81-82, 87).

The next major initiative involving nonprofits arose about a half-century later, in 1959, in the form of the federal Section 202 program. Aimed at developing subsidized housing for the elderly and handicapped, it was modeled after the College Housing Program. While the latter relied on a specific type of nonprofit entity—colleges and universities—the Section 202 program invited participation by a diverse array of nonprofit organizations—religious, fraternal, trade, or civic.

The motivation for the Section 202 program's reliance on nonprofits was partially related to the perception that this broad range of groups would be good developers and owners of

[1] Portions of the first two sections of this paper are drawn from Bratt (2006a) and Bratt (1998).

housing. Nonprofits were typically viewed as good as "motherhood and apple pie." A Colorado congressman offered that the nonprofit is an organization "whose interest is the well-being of the members and the persons whom it serves…There is no desire to profiteer, there is no desire to cheat. There is a desire only to give the maximum service for the money available" (U.S. House of Representatives, 1959, 567). While there was certainly this kind of "pull" toward nonprofits, important, too, was the "push" away from public housing and the already prevailing negative image of local housing authorities.

The Section 202 program has always been viewed as a success, and it still operates today. Nonprofits have contributed to the positive assessment of this program due to their well-established positions in their communities, their ability to raise funds from their members, and their commitment to the projects both during their early phases and in overseeing management functions.[2]

In the 1960s, there were three sets of federal housing initiatives that included roles for nonprofits. First, with the creation of the Section 221(d) (3) and 236 below-market-interest-rate programs, nonprofit sponsors were given prominent, although not exclusive, roles as development sponsors. As of 1970 only about 28 percent of all units built under these two programs had been developed by nonprofits (Keyes, 1971). Second, the Office of Economic Opportunity and the Model Cities program supported the creation of housing development corporations, although a lack of sufficient resources, as well as grass-roots support, limited their effectiveness (Keyes, 1971).

Finally, the most significant federal initiative of the 1960s that was aimed at nonprofits came in the form of the 1966 Special Impact Amendment to the Economic Opportunity Act.[3] The nonprofits that were created through this program comprised the first generation of community development corporations (CDCs). Eight years later, Title VII of the Community Services Act authorized significant additional funding for these groups. In the fifteen years

[2] Other factors also contributed to the success of the Section 202 program. First, it served a relatively easy-to-house clientele; the predominantly white, moderate-income elderly female residents posed few management problems in terms of rent arrearages and property damage. And, second, HUD provided technical assistance to the nonprofits and developed a specialized staff to administer the program. HUD staff stringently enforced sponsors' qualifications as well as the design, siting, and financial feasibility of the proposed projects, and they intervened if a development ran into difficulty (Bratt, 1989, 184-185).

[3] Preceding the federal program aimed at supporting the development of CDCs, the Ford Foundation piloted its "Gray Areas" program, which was a new model aimed at providing operating and programmatic subsidies to community development organizations whose mission was focused on poor communities.

spanning 1966 to 1981, more than $500 million in federal funds were allocated to 63 CDCs through these two programs. While more than 10 percent of this original group of CDCs was never able to move beyond the planning stages, some groups are still operating today and have produced hundreds of housing units, jobs, and business ventures (National Center for Economic Alternatives, 1982, 25, 27, 49; see also Abt Associates, 1973).

With CDCs gaining new popularity, and with some groups receiving federal funds from the 1966 or 1974 legislative initiatives, scores of organizations were created, often in response to bank redlining, arson, urban renewal or abandoned properties. A survey of CDCs revealed that fifty-three percent had been created between 1973 and 1980; another 20 percent were created between 1981 and 1988 (Vidal, 1992, 35-36).[4]

Another important federal initiative that directly supported the growth of CDCs came in the form of the Neighborhood Self-Help Development program. Two rounds of funding, in 1979 and 1980, provided $15 million in federal grants to neighborhood development organizations (Mayer 1984). Abolished as a freestanding program in 1981, this type of funding became an eligible activity under the Community Development Block Grant program. CDCs have typically fared well under the CDBG program. Based on her early 1990s survey of CDCs, Vidal (1992) noted that CDBG is the most widely used funding source for these organizations.

The Nehemiah program was another federal initiative targeted solely to nonprofits. Following the well-publicized success of local programs in Brooklyn and the South Bronx, Congress authorized the Nehemiah Housing Opportunity Grants Program as part of the Housing and Community Development Act of 1987. Before the program was canceled in 1991 and folded into the CDBG program, there were three rounds of funding, with 54 grantees designated to receive a total of over $60 million to support the development of some 4,100 units.[5] Funding was provided to nonprofit organizations that, in turn, offered interest free second mortgage loans of up to $15,000 to purchasers of homes built under local Nehemiah projects. At present, there

[4] This is roughly consistent with data published by Stoutland (1999, 198). She reported that 435 CDCs (81 percent), out of the total number of groups incorporated between 1909 and 1993 (534), were formed in the decades of the 1970s and 1980s. In California, however, there has been a different pattern, with only one third of the nonprofit housing organizations in that state forming before 1980; 39 percent were incorporated in the 1980s (Christensen, 2000).

[5] Not all the units were actually developed. For example, in the first round, three projects dropped out of the program and two other projects needed to lower the number of units planned for the sites, reducing construction totals from 1,305 to about 1,170 units (Phipps, Heintz, and Franke, 1994, 2-13).

are scores of Nehemiah programs operating across the country—some have received federal funding, others have not. But many of the key characteristics of the original model are incorporated into these local initiatives.

To conclude this section, two additional observations should be made. First, although the major phases of nonprofit involvement with housing can be told in a fairly linear manner, as above, successive programs did not, for the most part, build on the experiences or lessons learned from their predecessors. Instead, each successive set of nonprofit-based housing initiatives grew from the particular set of political, economic and social needs and priorities that prevailed at a given time (Bratt, 1998).

Second, the view that nonprofits should receive special treatment is not universally shared. Among the most vigorous critics, Howard Husock has noted that CDCs undermine market operations and result in target neighborhoods being sustained by government resources and "potentially impeding the new, spontaneous development that is the hallmark of urban vitality." And, further, that the CDC movement is based on the assumption that "private market forces would never be drawn to restore poor urban neighborhoods or to create jobs in them, and that therefore government must provide both income support and housing for the poor trapped in cities" (2003, 80-81; 82). Instead, Husock's solution is to rely on the market. "Cities bounce back," he says, "when decline makes their land so cheap that it becomes economic for business to buy (2003, 90).

Most practitioners, policy makers, and analysts of urban housing and city planning disagree.[6] The most widely held view is that it is unconscionable to allow decade after decade of deterioration with the enormous physical and social costs that such conditions create. As a result, there have been a number of public interventions aimed at revitalizing cities, in general, and at assisting CDCs, in particular. Several of these have been noted above; additional interventions are discussed in a subsequent section of the paper.[7]

[6] Even Nicholas Lemann (1994), who lodged a pointed attack on federal community development initiatives, praised the work of CDCs, particularly their efforts to develop housing for low income residents.
[7] Several major urban revitalization programs are not discussed, notably the Urban Renewal and Model Cities programs. Particularly in the case of Urban Renewal, vigorous lobbying on the part of the private real estate market helped fuel the public intervention. Indeed, this non-market based initiative proved to be a significant boon to the private real estate market.

The Current View

The contemporary nonprofit housing sector is comprised of two major types of developers and owners: community development corporations and larger national and regional nonprofit organizations.[8] CDCs are nonprofit organizations that are:

> characterized by their community based leadership and their work primarily in housing production and/or job creation…CDCs are formed by residents, small business owners, congregations and other local stakeholders to revitalize a low and/or moderate income community. CDCs typically produce affordable housing and create jobs for community residents. Jobs are often created through small or micro business lending or commercial development projects. Some CDCs also provide a variety of social services to their target area (National Congress for Community Economic Development, 2005a).

CDCs are typically small organizations, committed to the revitalization of relatively small geographic areas, with a median staff size of ten employees, seven of whom are full-time (National Congress for Community Economic Development, 2005b).[9]

During the 1970s, 1980s and 1990s the National Congress for Community Economic Development tracked the growth of CDCs and presented an image of uninterrupted growth, from some 200 groups in the mid-1970s, to about 1,500-2,000 groups in 1988 to 3,600 in 1999 and 4,600 in 2005 (National Congress for Community Economic Development, 1989, 1999, 2005b). However, anecdotal evidence, as well as recent research, has revealed that CDCs not only get created, but they also go out of business (Rohe, Bratt, and Biswas, 2003).

The second broad category of nonprofit housing developers is sometimes referred to as "national or regional nonprofits." Many of these organizations have become members of the Housing Partnership Network (HPN), which is a peer network and business cooperative of 87 of some of the most accomplished affordable housing nonprofits in the country.[10] Its members

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[8] These two groups are not inclusive of all nonprofit housing producers. Some housing is built by religious institutions, trade unions, or other organizations with a particular constituency or mission. Other nonprofit organizations are committed to assisting the homeless or other groups with special needs, such as HIV/AIDS. Still other nonprofit organizations are tenant cooperatives. However, a focus on these types of groups is beyond the scope of this paper.

[9] Current figures on CDC operating budgets are not available. The 1999 census by the National Congress for Community Economic Development reported that the median annual budget was in the $200,000-399,000 range; only 20 percent of the groups had budgets exceeding $600,000.

[10] While affordable housing development is the most prevalent activity of Housing Partnership Network members, 32 (38 percent) of these organizations identify themselves primarily as lenders (Mayer and Temkin, 2006).

operate on a citywide or regional basis and share a similar public/private business model that forges entrepreneurial partnerships among the business, community, and government sectors to create and sustain affordable housing. The founding members formed the HPN in 1990 “to share knowledge and spread innovation among peer organizations, to shape policy, and to create new social enterprises to strengthen their businesses and achieve their missions” (The Housing Partnership Network, 2006).

HPN member organizations are typically considerably larger, in terms of staff size and operating budgets, than CDCs. Based on a recent study of these groups, researchers found that the FTE median staff size is 60; the median operating budget is $4.1 million (Mayer and Temkin, 2006).

Among the group of large nonprofit housing organizations, seven that work at a national level have coalesced under another, relatively new organization, Stewards of Affordable Housing for the Future (SAHF), which was launched in 2003. Member organizations own properties in multiple states and, taken together, they operate in 49 states, plus the District of Columbia, Puerto Rico, and the Virgin Islands. Similar to other nonprofit housing organizations, these groups also share a commitment to preserving rental housing as affordable to low-income families, seniors, and disabled individuals.

While CDCs often emerged as a result of a community group protesting poor conditions in their neighborhood, HPN organizations were typically created through cooperative arrangements on the part of local civic leaders, bankers, other leading businessmen, as well as public and nonprofit organizations. Despite the local prominence of HPN members,[11] as a group these nonprofits have enjoyed considerably less visibility than the much more prevalent, but significantly smaller CDCs.

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[11] During site visits conducted by a team of researchers under contract to the Urban Institute, interviewees frequently commented that the local Housing Partnership Network organization was viewed as the “go-to” organization in their area. In a number of cases, Housing Partnership Network members have considerable national reputations throughout the nonprofit community (e.g. ACTION-Housing, Bridge Housing Corporation, and the Cleveland Housing Network).

Production Record

CDCs are credited with having produced or rehabilitated more than 1,252,000 units of housing (National Congress for Community Economic Development, 2005b) and, in general, nonprofits have been responsible for a significant percentage of the lower income housing that has been developed over the past two decades. In 1990, nonprofits produced approximately 17.2 percent of the total number of federally assisted housing units and in the thirty year period, 1960-1990, the cumulative nonprofit share of all federally subsidized production and preservation units was about 15.7 percent (Walker et al., 1995, 22). As of 1995, nonprofit organizations owned 35 percent of the older assisted stock of housing (which included subsidies under the Section 221(d) (3), 236, and various Section 8 programs) (Finkel et al., 1999). Based on a sample of about one quarter of the Low Income Housing Tax Credit units developed between 1987 and 1996, just under one-third were developed by nonprofits either working alone or in partnership with for-profits (Cummings and DiPasquale, 1999, 255).

Housing owned by CDCs and other nonprofit organizations are important components of the social housing sector in the U.S., which comprises about 4.6 million units.[12] Included in this total are the units produced by non-CDC nonprofit producers of housing, notably the members of the HPN and SAHF, discussed above. These organizations have developed about 295,000 units (HPN = 225,000;[13] SAHF = 70,000[14]). This level of production – from only 94 groups—

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[12] This estimate draws on Stone's analysis (2006, 244, 246 and 257). However, Stone's estimate did not include the most recent number of CDC-produced units, based on the 2005 NCCED census—1,252,000 units (2005b). Thus, his estimate of 4 million units in the social housing sector has been increased by some 600,000 units, which, according to the National Congress for Community Economic Development, is the number of units produced by CDCs between 1999 and 2005.
Stone breaks down the size of the social housing sector as follows: First, he delineates three forms of publicly owned housing: federally-funded public housing—1.3 million units; state and local-funded public housing—700,000 units; and Department of Defense owned and operated housing—400,000 units. This totals about 2.4 million units. Second, he breaks down the various forms of nonprofit ownership: CDC produced housing that has remained in the social sector —450,000 units; other nonprofit-owned housing—250,000 units; neighborhood-reinvestment corporation sponsored mutual housing associations—8,300 units; limited equity cooperatives—425,000 units; community land trusts—6,000 units; rental units owned by nonprofits that have not received government subsidies or possibly just capital assistance from nonfederal public or private sources—200,000 to 400,000 units; Section 202 housing for the elderly—200,000; housing that was built under the below market interest rate programs of the 1960s (Section 221(d)(3) and Section 236) that continue to be owned by nonprofits—150,000 units; unsubsidized FHA-insured units that later received federal Section subsidies—150,000 units. Totaling all the units in the nonprofit category comes to a conservative estimate of about 1.7 million units.
[13] This figure is based on an estimate of the most recent production figures of Housing Partnership members. Personal email communication from Manuel Muelle, Director of Network Development, Housing Partnership Network. October 31, 2006. As noted in n.12, Stone (2006, 257) estimates that the size of the portfolio of "other nonprofit-owned" housing is about 250,000 units, which is roughly consistent with the figure of 285,000 units cited in the text. However, it is also important to point out that not all large regional housing producers are members of

equals about 23 percent of the number of units produced by CDCs.

Thus, taken together, CDCs and the other nonprofit producers of housing have played a major role in providing affordable housing opportunities to nearly 1.5 million households, almost one-third of the social housing sector. As a point of comparison, the total production by nonprofits has now surpassed by more than 25 percent the current number of federally subsidized public housing units, which stands at about 1.2 million (more than 1,252,000 CDC-produced units and about 295,000 HPN and SAHF-produced units, as well as other units not counted in either category).

The productivity of CDCs appears to have increased over time. The 245,000 units produced during the four calendar years spanning 1994-1997 represented 45 percent of all housing ever produced by CDCs (National Congress for Community Economic Development, 1999, 11). And the 600,000 units added between 1998 and 2005, when the most recent census was completed; represent nearly 50 percent of CDC housing production. Mean annual production has also increased from 27,000 units (1991-1994) to 86,000 units (1998-2005) (National Congress for Community Economic Development, 2005b). However, most CDCs (56 percent) have produced fewer than 100 units over the lifetime of the organization (National Congress for Community Economic Development, 2005b).

Productivity has similarly increased among HPN members. Mayer and Temkin (2006) report that annual housing production increased during 2000-2004 compared with earlier years and that, moreover, production was especially high in FY 2004. More specifically, the mean number of units produced by member organizations in 2004 was almost twice as great as the mean annual production per organization in the period spanning 2000-2004. HPN members typically have much higher production levels than the great majority of CDCs. A recent survey revealed a median aggregate production of 1,884 units and a mean of 2,654 units (Mayer and Temkin, 2006).

Another way of looking at the production record of nonprofits is to compare their output with that of for-profit developers. Walker et al. note that very few CDCs or for-profits produce

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the Housing Partnership Network or SAHF. The Community Builders, based in Boston (but with offices in 9 other cities in the Northeast and Midwest) is a good example of a large organization that is neither a CDC nor a member of the Housing Partnership Network. Its website claims that it is "the largest nonprofit urban housing developer in the United States" with over 20,000 housing units produced and with 7,000 units currently under management, located in 90 developments (The Community Builders, 2006).

[14] This estimate comes from Bill Kelly, President, Stewards of Affordable Housing for the Future, private email communication, December 11, 2006.

more than 100 units per year (4.4 percent of CDCs and 16.4 percent of for-profit developers reached this threshold during 1988-1990). Members of the HPN, however, have a considerably higher mean annual production of multifamily units compared with the for-profit members of the National Association of Home Builders—124 and 57 units, respectively. (Mayer and Temkin, 2006). Moreover, since for-profits are more likely to engage in single-family development, and nonprofits are more likely to take on the difficult set of tasks involved with financing and renovating multifamily projects, there is likely a "degree of sophistication among nonprofits that equals or exceeds that of [their] for-profit comparison group" (1995, 26).

All nonprofit housing producers strive to cover the costs of developing and managing their projects through developers' fees, management fees, and through the cash flow generated from the property. Increasingly, too, nonprofit housing groups are focusing on asset management, which involves viewing each property in terms of its long-range costs and revenue-generating potential. While the goal of all such organizations is to become financially independent, the costs involved in building and managing housing targeted to low-income households require an infusion of resources and assistance.

Government Preferences and Support Systems for Nonprofits

Additional Federal Programs

In addition to the various federal programs that have directly supported the development and growth of CDCs and other nonprofits, discussed above, starting in the 1980s, there have also been a number of federal initiatives that have given some type of preferential treatment to nonprofits. The net result is that for CDCs, the federal government is by far the most important source of grants, loans, or investments, with some 88 percent of all organizations reporting that they had received over $50,000 from federal sources, particularly HUD. Other key revenue sources include state and local governments, banks, national intermediaries, foundations and corporations (National Congress for Community Economic Development, 2005b). HPN members rely on a similar list of investors and donors (Mayer and Temkin, 2006).

First, the federal government looked to nonprofits to help bring back into use properties that had been owned by distressed and failed savings and loan associations and commercial banks. Specifically, in the Financial Institutions Reform, Recovery and Enforcement Act of

1989, nonprofits were given the right of first refusal to purchase properties from the Resolution Trust Company that had been in the portfolios of distressed S & Ls. Two years later, a similar provision was contained in the Comprehensive Deposit Insurance Reform Act of 1991, aimed at properties owned by failed commercial banks.

Second, nonprofits have been given a priority status in the “expiring use” crisis. Title VI of the Cranston-Gonzalez National Affordable Housing Act of 1990 gives these organizations and other “priority purchasers” the first right to make a bona fide offer to purchase a federally subsidized development whose owner has announced an interest in pre-paying the mortgage.

Third, and also in the Cranston-Gonzalez National Affordable Housing Act of 1990 (Title II—the HOME Investment Partnership Program), Congress mandated that at least 15 percent of each participating jurisdiction’s HOME funds be earmarked for use by qualified nonprofit housing organizations, which were termed CHDOs (Community Housing Development Organizations). This allocation, called the Community Housing Partnership set-aside, was strengthened in the Housing and Community Development Act of 1992, which permitted 5 percent of each jurisdiction’s overall HOME allocation to be spent on nonprofits’ operating expenses. Even before this change went into effect, as of FY 1992 nearly 28 percent of all HOME dollars went to nonprofit sponsors. And just looking at HOME funds committed to rental housing, nonprofits were the recipients of 40.6 percent of the allocation. However, the overall percentage of HOME funds going to CHDOs (or CDCs) was significantly less—roughly 15 percent as mandated by Congress (Walker et al., 1995).

Fourth and also contained in the Housing and Community Development Act of 1992, nonprofits are listed as one of the eligible entities to which public housing residents may choose to transfer management of their developments, instead of management being done by troubled public housing authorities.

A fifth critical set aside is stipulated in the Low-Income Housing Tax Credit program, which requires that at least 10 percent of each state’s annual tax credit allocation be earmarked for projects that are at least partially owned by a qualified nonprofit organization. However, the LIHTC allocation to nonprofits has been significantly higher than this amount. Between 1987 (the start of the tax credit program) and 2002, nearly 22 percent of all LIHTC projects were sponsored by nonprofits (HUD 2004). The all-time peak was reached in 1998 with nonprofits sponsoring 36.6 percent of all LIHTC properties. However, since then, there has been a decline in nonprofit sponsorship of these properties, with the rate falling to 25 percent, but still far above the 10 percent minimum threshold (Climaco et al., 2006, 23).

Concluding their study of nonprofit participation in LIHTC and HOME programs, O'Regan and Quigley observed that: "nonprofits do, in fact, receive a larger portion of funding in these programs than they have in other historically important sources of low-income housing production" (2000, 313).

A sixth example of how federal programs single out nonprofits to assume important roles is found in the New Markets Tax Credit Program,[15] which is operated by the Community Development Financial Institutions fund.[16] Designed to generate private sector equity investments in low income communities, the NMTC requires that all investments be made through certified Community Development Entities, which are domestic corporations whose primary mission is serving or providing investment capital to low income communities or low income persons. Tax credits are channeled to these entities, which, in turn, sell the credits to corporate investors. The cash proceeds are then invested in the earmarked project. Community Development Entities must be accountable to residents of their communities through representation on either a governing or advisory board (Community Development Financial Institutions Fund, 2003). While for-profit entities may qualify as a Community Development Entity, the requirements are geared to the basic characteristics of CDCs and other nonprofits.

Finally, nonprofits have also played a central role in supporting programs targeted to homeless people, both in terms of providing emergency shelters and in helping to fund transitional or permanent housing. Between 1987 and 1991, more than 87 percent of total federal spending for these programs was provided to nonprofit organizations (Walker et al., 1995).

Despite the important role that nonprofits have been playing in this significant array of federal initiatives, there is still nothing approaching a "nonprofit-centric" system of support for nonprofit organizations (Bratt, 1998), which would involve a comprehensive array of funding for operations, pre-development costs, construction and permanent financing, and long-term

[15] Enacted as part of the Community Renewal Tax Relief Act of 2000, the program may be used to finance retail centers, small businesses, charter schools, child care centers and other community facilities.

[16] This fund is aimed at increasing the capacity of financial institutions to provide credit, capital, and financial services in distressed urban and rural communities. Created in 1994, the fund receives annual Congressional appropriations; in FY 2006, $55 million was approved. These monies, in turn, are invested in Community Development Financial Institutions, which serve markets typically underserved by conventional financial institutions.

subsidies, as well as technical assistance. The piece-meal approach to supporting nonprofits notwithstanding, it is noteworthy that there have been many efforts to sustain and enhance the work of these organizations as they go about the task of providing decent, affordable housing.

Other Sources of Support

CDCs and other nonprofit organizations receive substantial support from a number of other sources, in addition to the federal government. The 1980s saw the beginning of federal devolution to state and local governments. No longer was the federal government to be seen as the sole source of funding and support for low-income housing initiatives. Instead, lower levels of government were expected to fill in the gaps both in program development as well as funding.

For example, prior to 1980 there were only 44 state-funded housing programs and the bulk of these were operating in three states: California, Connecticut, and Massachusetts. But between 1983 and 1987, 92 new state programs were established and this proliferation was accompanied by significant increases in state spending for housing. With this growth in state-based housing activity, nonprofits were often given central positions; in 1988, a survey revealed that state housing programs were typically oriented toward nonprofit developers (data reported in Goetz, 1993, 77-78).[17]

Financial institutions comprise another group of entities that support the work of nonprofit organizations. As noted previously, Community Development Financial Institutions have become enormously important in providing financing for development projects that would, perhaps, otherwise have difficulty locating resources.

The Affordable Housing Program and the Community Investment Program, both operated by Federal Home Loan Bank System, are also significant. The AHP is funded with 10 percent of the Federal Home Loan Bank System's net income each year. Under the program, grants are provided to member banks in partnership with developers and community organizations to finance the purchase, construction, or rehabilitation of owner-occupied or rental housing targeted to low- or moderate-income households. Grants can also be used to lower the interest rate on loans or cover down payment and closing costs. The CIP is restricted to providing below-market-rate loans that enable banks to extend long-term financing for housing

[17] Goetz provides further evidence of the pervasiveness of state and local funding for nonprofits (1993, 122-125). See also Bratt (1989) for an examination of Massachusetts' efforts to develop a comprehensive system of supports for nonprofit housing organizations.

and economic development that benefits low and moderate income families and neighborhoods (Federal Home Loan Banks, 2006).

Private foundations have also emerged as critical partners in supporting the work of nonprofit housing organizations. As far back as 1991, over 500 independent, corporate, and community foundations were providing funds in support of community-based development. And, in just four years, between 1987 and 1991, foundation support more than doubled —from $74 to $179 million (Council for Community-Based Development 1993).

The final major category of supports for nonprofits is comprised of the national nonprofit intermediaries, notably the Local Initiatives Support Corporation (LISC), Enterprise Community Partners (formerly known as the Enterprise Foundation) and NeighborWorks America (formerly known as the Neighborhood Reinvestment Corporation).[18]

The national intermediaries play an important role in influencing and supporting the work of CDCs. Both LISC and Enterprise Community Partners raise funds primarily through private corporate and foundation donations, while NeighborWorks America also receives annual Congressional appropriations. These three organizations disseminate funds to local chapters that, in turn, provide funds directly to affiliate organizations working in urban neighborhoods or rural locations.

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[18] NeighborWorks America's institutional origins can be dated to 1975, when the Federal Home Loan Bank created an office dedicated to neighborhood reinvestment. Three years later, Congress enacted the Neighborhood Reinvestment Corporation Act, which transformed the office into a free-standing federally-funded agency whose mission is "to revitalize older urban neighborhoods by mobilizing public, private, and community resources at the neighborhood level" (NeighborWorks, 2006). The NeighborWorks network, which was created and supported by the Neighborhood Reinvestment Corporation, consists of more than 240 local nonprofit organizations whose goal is to create affordable housing and to promote community revitalization (NeighborWorks, 2006). In FY 2005, $168 million in NeighborWorks revolving loan fund investments leveraged $2.8 billion in other direct investments in neighborhoods served by affiliate organizations (NeighborWorks, 2005).
Enterprise Community Partners was created in 1982 with the assistance of real estate developer James Rouse. Since then, the organization has secured and made $7 billion in investments and contributions. Through their network of more than 2,500 organizations, more than 190,000 homes affordable to low income families have been built or rehabilitated (The Enterprise Foundation, 2006).
The Local Initiatives Support Corporation (LISC) was created in 1980 and is committed to working with CDCs to rebuild communities. Technical assistance and financial support is provided to local programs operating in more than three dozen cities. LISC raises money from private investors, lenders, and donors (over $7 billion), which, in turn, leverages additional public and private sector funds. Since its inception, the organization has provided assistance to thousands of CDCs, which have built or rehabilitated 196,000 affordable homes and created over 27 million square feet of commercial, community and educational space (Local Initiatives Support Corporation, 2006a).
A fourth intermediary, the Center for Community Change, was created in 1967, years before the other groups, and is unique in its overriding concern with advocacy and in serving as a link between activist CDCs and technical assistance and in its commitment to grassroots empowerment (Rubin, 2000).

In addition, both LISC and Enterprise have subsidiaries that serve as intermediaries for tax credit investments. LISC's affiliate, The National Equity Fund, Inc., and Enterprise's subsidiary, Enterprise Community Investment, Inc., both provide a critical link between CDCs (as well as other nonprofit and for-profit developers) and community-focused investors. Both seek strong real estate investments that provide solid returns and risk protection for investors who include many of the top banks, insurance companies, and corporations in the country. By providing both technical assistance to the local development entity, as well as solid underwriting services, equity is funneled to projects, while assuring investors that the deal is financially sound and that the investment will be profitable (Local Initiatives Support Corporation 2006a; Enterprise Community Investment, Inc. 2006).

Another national intermediary, The National Housing Trust, serves as a consultant and development partner to mostly large nonprofit organizations, as well as to HUD, state and local housing agencies, and to low income residents that are working to preserve and improve affordable multifamily housing. Since 1996 the Trust has been involved in the acquisition and rehabilitation of over 12,000 apartments that have required a combined commitment of over $750 million. The National Housing Trust Community Development Fund, an affiliate of the National Housing Trust, provides predevelopment and bridge financing to preserve and improve affordable multifamily housing properties. And, in partnership with Enterprise Community Partners, a separate affiliated entity, NHT/Enterprise Preservation, acts as an owner/developer, purchasing and renovating existing, affordable housing. To date, NHT/Enterprise has preserved and operated over 3,000 affordable apartments, the vast majority of which are affordable to very low income households (National Housing Trust 2006).

In recent years, the role of intermediaries has grown significantly due, in part, to the substantial investments that these organizations have received from major funding efforts such as the National Community Development Initiative, which is now known as LivingCities. In fact, Walker (2002) has noted that:

> The number one accomplishment of the community development leadership system in the 1990s was the creation or strengthening of strong intermediary institutions—the collaborations, partnerships, coalitions and alliances, and other bodies that help engage leaders from multiple sectors as contributors to community development (48).

There is a prevailing view that CDCs are better able to deliver services with the assistance of intermediaries than without them. Specifically, intermediaries and local collaborations facilitate multiyear funding for CDC operations; they tend to increase the level of investment; they establish performance standards and monitor CDC progress; and they shift administrative burdens for grant-making and management away from the grantor to the intermediary (Walker, 2002, 40).[19]

Taken together, the support for nonprofits is extensive, albeit piecemeal. And, as financial and technical assistance for nonprofits has increased so, too, has the competition for these resources become more intense. One of the down-sides of the increase in the number of nonprofits over the past several decades is that more groups are pursing the available funds.

Properties and People Served by Nonprofits

Nonprofit housing developers are typically willing to enter into market situations and to serve populations that the unassisted private for-profit sector cannot or will not serve. In addition, when compared with for-profit developers utilizing some kind of subsidy, nonprofits still emerge as the group that is most likely to work in the most distressed areas and to serve the hardest-to-house residents. A number of studies and types of data underscore these observations. However, in presenting the various research findings, it is also important to note that the data comparing nonprofit and for-profits do not differentiate between the small, neighborhood-based organizations and the large, regional or national nonprofits. Therefore, when comparing the experiences of nonprofit and for-profit organizations, it should be remembered that we do not yet have intra-sectoral information on outcome measures (e.g. large nonprofits vs. small nonprofits and large for-profits vs. small for-profits).

Early Studies—1970s and 1980s

Given that CDCs can trace their roots to the Special Impact program of the 1970s, it is not surprising that that early initiative's focus on deteriorated areas has been a steady theme and basic orientation of CDCs. The Special Impact regulations noted that the program was geared to areas that "face severe shortages of income, jobs, skilled human resources…" And, further that,

[19] However, there is also some question about the extent to which intermediaries interfere with the agendas of CDCs. For a fuller discussion see Bratt, 2006a.

"the ultimate goal of the Special Impact Program [was] "to achieve parity between the impact areas and the areas surrounding them" (National Center for Economic Alternatives, 1981, 22).[20]

In a study of 15 impact areas included in this program, researchers noted that all the "sites have been subjected to the deleterious effects of social and economic changes. In every case these communities had substantially higher portions of their populations living in poverty than was the case in general for the United States in the selected comparison year of 1970" (National Center for Economic Alternatives, 1981, 36). And, further:

> The impact areas are not just poor. They are physically deteriorated. The urban neighborhoods typically include large blocks of abandoned housing and commercial space. The rural regions lack adequate public utilities like water, sewer and transportations systems. Investors are reluctant to put money into such places without guarantees and other help from responsible local institutions—and the impact areas lack such institutions (National Center for Economic Alternatives, 1981, 38).

Mayer's Study of 30 nonprofit organizations, that had received funding from the Neighborhood Self-Help Development program, revealed that: "the most consistent geographic pattern is that NDOs (Neighborhood Development Organizations) function in very troubled neighborhoods." Moreover, these neighborhoods are likely to present problems for "anyone trying to carry out development projects, and especially projects designed to benefit low- and moderate-income residents" (1984, 13, 53). Specifically among the NDOs in the study sample,

> about half operate in neighborhoods where conditions for residents and businesses are clearly as trying as, or often substantially more trying than, anywhere else in the same city. Poverty, unemployment, deteriorated and abandoned housing, a diminishing population often of advancing age, and declining or vacated commercial strips all characterize these neighborhoods. Many buildings would require major investment to be returned even to a safe, usable condition. Vandalism, theft, and, in a smaller number of cases, arson are serious threats to people and property. Social

[20] The Special Impact program was not focused on housing. The four major project areas included community business and commercial development; community physical development programs; training and public service employment programs; and social service programs. Housing rehabilitation or new construction was included as a permitted activity under the second category—community physical development. Other activities in this category included rehabilitation or new construction of commercial space; development of industrial facilities and parks; land banking; and the formation of construction companies. In a study of CDCs participating in this program, of the total number of business ventures launched within the first two categories above (287), only 44, or 15 percent, involved residential development. Support for business enterprises was the most dominant economic development activity of Title VII CDCs (National Center for Economic Alternatives, 1981, 104, 84, 85).

> problems—including alcoholism, drug abuse, and mental illness—are common. A significant share of these neighborhoods are likely among the most troubled in the nation. [In addition,] Many of the remaining half of the organizations work in areas that most Americans would describe as seriously troubled as well… [Finally,] In some neighborhoods little or no other investment was taking place; in others, there were no projects of the type the NDO chose (Mayer, 1984, 53-54).

The seminal study of CDCs, undertaken by Vidal in the late 1980s, reported similar findings:

> Census tracts in the neighborhoods served by sampled CDCs show a substantially lower median income than do other census tracts in the same cities…these neighborhoods include a considerably greater proportion of families with children that have incomes below the poverty line and of families on public assistance…If census tracts in each city are ranked according to their median incomes, those served by the sampled CDCs are clearly clustered in the more distressed parts of their cities (Vidal, 1992, 80).

Qualitative information collected by field researchers also confirmed that CDCs are serving needy populations: 82 percent of CDC neighborhoods were judged to be more distressed than their cities as a whole (Vidal, 1992, 81).

Research from the 1990s and 2000s

The National Congress for Community Economic Development has carried out five surveys of CDCs; the most recent one was completed in 2005. Based on their data, researchers concluded that: "these groups continue to share a guiding philosophy from the field's earliest days. Four decades after CDCs began; they're still targeting their initiatives to help the people who need it most. In this census, CDCs reported that 87 percent of the residents they serve are low income; 22 percent are poor" (National Congress for Community Economic Development, 2005b, 3). Similarly, in a survey of California's nonprofit housing developers conducted in 1997, 90 percent of these groups noted that very low income households were their target population (Christensen, 2000).

A survey that reported on income levels of occupants of units produced by members of the Housing Partnership Network revealed a similar pattern: "By design [member] organizations develop housing affordable in substantial part to low- and very low-income people. Their actual performance is highly consistent with such goals" (Mayer and Temkin, 2006, 34).

HUD's Low Income Housing Tax Credit database is a good source of information on the types of properties developed by nonprofits. Between 1995 and 2003 nonprofit sponsors located their properties in more difficult neighborhoods than the total universe of low income housing tax credit properties, the bulk of which were developed by for-profit sponsors. Climaco et al. (2006, 45) report the following:

- 27.3 percent of LIHTC units in properties owned by nonprofits were located in census tracts where over 30 percent of the population was below the poverty level, compared with only 19.8 percent of all LIHTC units;
- 45.3 percent of LIHTC units in properties owned by nonprofits were located in census tracts where over 50 percent of the population was minority, compared with 41.8 percent of all LIHTC units;
- 22.0 percent of LIHTC units in properties owned by nonprofits were located in census tracts comprised of households that were over 20 percent were female-headed, compared with 17.2 percent for all LIHTC units;
- and 51.6 percent of LIHTC units in properties owned by nonprofits were located in census tracts where over 50 percent of the units were renter-occupied, compared with 45.1 percent for all LIHTC units.

Data on tax credit properties also reveal that nonprofits were more likely to serve groups with special needs than for-profit developers. And, in keeping with the mission of many nonprofits to house large families, these groups were more likely to build units of over 1,000 square feet than for-profit developers (U.S. General Accounting Office, 1999).

To sum up: the results of the various analyses are consistent and clear. Nonprofit organizations tend to work in some of the most troubled geographic areas and they tend to serve some of our most difficult-to-house populations.

The Debate on the Role of Nonprofits

Should governments and foundations foster the growth of nonprofits as developers and long-term owners of subsidized rental housing? For both nonprofit and for-profit developers there are a number of positive and negative arguments, which are summarized below.

As a background to this discussion, however, it is important to underscore a basic observation: the unassisted private housing market generally does not provide sufficient profit for for-profit developers to build or maintain decent quality housing that is affordable to lower income households. This point has been made by numerous times and by various observers. Statements in the final reports of two Congressionally-mandated studies on future directions for U.S. housing policy are particularly noteworthy. The Report of the National Housing Task Force observed that [there is a] “clear understanding that housing for poor people cannot be produced by the private sector acting alone” (1988, 9). And, more than a decade later, the Millennial Housing Commission stated that one of the lessons learned from the 70-year history of federal housing programs is that: “The private sector needs the proper incentives to be an effective partner in the federal government’s efforts to address the nation’s housing challenges” (2002, 26).

If the private market, acting on its own, were able to meet the housing needs of residents at the full range of the income distribution, there likely would be little debate. Nonprofit organizations, rather than serving as developers and managers of housing could, instead, be called upon to play various social service functions—to support the non-housing roles that low income or special needs populations may require. Nonprofits could also serve as partners to for-profit developers, bringing their unique attributes to specific projects, including their connections to residents and the community at large. For the time being and for the foreseeable future, however, we are left with the question of which type of developer of housing affordable for low income households is preferable: nonprofits or for-profits? This section explores the benefits and drawbacks of for-profit and nonprofit developers and then presents a comparison of how each performs using two key variables: production costs and long-term viability of the developments.

For-Profits: **Benefits and Drawbacks**

For-profit developers typically have important attributes that make them attractive developers and owners of housing that is affordable to low income households. In particular, they generally bring significant financial and technical resources to a given deal. The ability of for-profit developers to cover the costs of acquiring land or buildings, as well as the up-front development costs, often allows them to move more quickly and efficiently than nonprofit organizations.

On the other hand, as noted above, for-profit developers using the LIHTC program are somewhat less likely than nonprofit organizations to develop projects in areas with higher percentages of very low income households. For-profits may be avoiding properties targeted to the neediest populations since they require additional services that are difficult and unprofitable to arrange, but are essential for residents.

Perhaps the major criticism of for-profit developers relates to the inherent contradiction in their need to make a profit and the potential for this to come into conflict with the long term affordability needs of low income residents, as well as the public purpose implicit in subsidy programs. A case study based in Massachusetts articulated this conflict:

> …it is not surprising that tax incentives to develop subsidized housing generate conflicts between public goals and private interests… The carefully argued and clear-cut positions that emerged during the resyndication[21] discussions present a sharp view of the conflicting program needs that arise between the profit aims of private developers and the public's objectives for subsidized housing (Bratt, 1987, 334).

The "expiring use" crisis provides an important example of how the needs of residents and the profit-motivated orientation of private developers come into conflict. This problem arose during the 1980s, as privately owned publicly subsidized developments reached the point at which owners were no longer bound by the regulatory agreements that they has signed with HUD to rent their units to low and moderate income households. It has been difficult and costly for the public sector to design incentives to keep for-profit owners from exiting subsidy programs when contracts expire in places where market conditions favor conversion to market rate rentals or conversions to condominiums. In 1987 and 1990, Congress passed two pieces of legislation aimed at providing first an "emergency" response to the expiring use issue, and then what was viewed as a "permanent" response.[22] By guaranteeing owners fair market value incentives to keep the housing affordable for at least 50 years, owners could either continue to own the housing themselves or sell to nonprofit groups that made the same commitment to long-term affordability. "Not surprisingly," Achtenberg notes, "most owners preferred to secure the

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[21] Syndication refers to the sale of shares of a given development to investors. Resyndication occurs when a property is bought by a new owner who, in turn, sells shares of that property to other investors. In both syndication and resyndication deals, investors reap tax benefits that are generated from the property, such as through depreciation losses or tax credits. Virtually all of the subsidized housing that has been produced by private for-profit developers over the past four decades has depended on investors buying into projects through syndication arrangements.

[22] The two laws were the Emergency Low Income Housing Preservation Act, Title II of the Housing and Community Development Act of 1987, P.L. 100-242, February 5, 1988, as amended and the Low Income Housing Preservation and Resident Homeownership Act, Title II of the Cranston-Gonzalez National Affordable Housing Act, P.L. 101-625, November 28, 1990, as amended.

incentives for themselves rather than sell their properties to nonprofits, and reports of lucrative equity takeouts with little or no funds reinvested in the property created the appearance of yet another boondoggle for the subsidized housing industry" (2006, 164). By 1997, under significant attack by the Republican Congress, and with little support from the Democratic administration, the federal government abandoned preservation funding.

With particular reference to the expiring use problem associated with Section 8 contracts, the mark-up-to-market preservation strategy will end up costing twice as much as capital grants that could have been used to permanently preserve the affordability of the property. Again, according to Achtenberg:

> …while preservation capital grants provided permanently affordable housing through social ownership, units marked up to market remain at risk every five years, despite the continued public investment in the housing. In effect, the current market-based strategy retains all of the costs of socially oriented preservation with none of the benefits…With 30-year hindsight, the failure of federal efforts to provide and preserve housing for low- and moderate-income families through the private sectors is readily apparent. The conflict between private property rights and social housing needs, inherent in the original structure of the federally-assisted housing programs, has never very been resolved but only managed in ways that have ultimately served to exacerbate the conflict. Preservation has been possible only when private interests are served as well; when this is not expedient or becomes too costly, social needs are sacrificed (2006, 168-69).

Another key point at which the needs of the private for-profit sector and those of the public may come into conflict is in the later years of property ownership, when for-profit owners may be looking to sell their property. However, it has proven challenging (to say the least) to anticipate and manage the tax consequences involved with for-profit owners exiting from their properties. This has been particularly problematic for pre-1986 investors in subsidized housing; in 1986 the tax code changed the incentive structure for investment in subsidized housing. In brief, these investors have found themselves unable to defer certain taxes, yet they are still responsible for income that was on paper only, also known as "phantom income." As the Millennial Housing Commission noted:

> Clearly, investor economic interest in such properties was substantially diminished and, as a consequence, necessary maintenance was in many cased reduced or eliminated…

> Even if an investor is no longer interested in owning a property (from which s/he has gained no significant economic benefit since 1986 and will gain none in the future), the investor is discouraged from transferring the property, because s/he will … be subject to a tax …(the “exit tax”) (2002, 34).

Attempting to resolve this disincentive for owners to sell their properties, or to maintain them at an adequate level, the Millennial Housing Commission proposed a new mechanism that would provide “exit tax relief” in such situations. The proposal has found its way into a bill, H.R. 3715, The Affordable Housing Tax Relief Act of 2005, but it has not been enacted. In short, the federal government would forgive taxes owed in exchange for a commitment that the property remains affordable for an additional thirty years.

Overall, the history of for-profit involvement with housing has been complex. In exchange for the significant investment capital that the for-profit sector brings, various intricate and costly tax incentives have been put into place. But each of these incentives has spawned the need for additional programs, in an attempt to secure the properties for long-term use by low income households. Each time a program is put into place with a limit on the length of time the development must remain affordable; the government has needed to step in to try to safeguard the affordability of the units with another incentive that, again, typically only provides another short-term resolution. Moreover, the costs of salvaging the housing for low income use are substantial, and tend to fuel public images of government waste and unnecessary spending.

Nonprofits: Benefits and Drawbacks

Nonprofit housing organizations have been criticized for the small scale of their activities and the perception that, despite their good efforts, nonprofit-produced units rarely amount to much more than the proverbial “drop in the bucket.” Indeed, data on nonprofit production presented earlier supports the view that most nonprofits have amassed modest production records.

Some of the other most frequently heard criticisms point to the difficulty that nonprofits often have in pulling deals together in a timely and efficient manner. On the other hand, in their defense, the development context in which nonprofits work is complex, and the need for them to line up multiple subsidy and funding sources, along with the typically skimpy working capital that they have available, serves to explain at least some of these concerns.

Supporters of nonprofits also point to their willingness to work in neighborhoods in need of revitalization, discussed above. On this latter point, however, not all observers see this as a positive attribute. For example, in their paper prepared for this symposium, Khadduri and Wilkins assert that developing housing in high poverty areas may not be a desirable approach, unless the new development is "part of a comprehensive revitalization effort with a realistic chance of success" (2006, 29). On the other hand, the ability of nonprofits to take risks that other developers are unwilling to take, and to invest in deteriorated neighborhoods, is often a key factor in the area's eventual revitalization. In fact, one of the ironies of community development is that the more nonprofits invest in neighborhoods that others are bypassing, and that this, in turn, stimulates other public and private investment, the more likely that the nonprofit will run into difficulties at some point in the future. Specifically, the nonprofit's own viability may be threatened as land and buildings that are affordable to the organization become scarce (Rohe, Bratt, and Biswas, 2003).

Nonprofits are also typically praised for their commitment to produce housing that is affordable to lower income people over the long-term. However, despite their good intentions to maintain these units in perpetuity, some nonprofits may already be finding it impossible to maintain all their units as affordable to low income households, due either to difficulty doing development deals as opportunities become scarcer in gentrifying areas or because some buildings may require more resources than the nonprofit can access. Indeed, all owners of housing affordable to low income households have to deal with the restrictions imposed by the various subsidy programs they are utilizing. In particular, with the exception of the old Section 8 New Construction/Substantial Rehabilitation program (as well as the public housing program following the creation of operating subsidies), federal subsidized housing programs have not included operating subsidies, to deal with maintenance and repairs, as well as unforeseen increases in costs.

While most nonprofits typically have difficulty accessing capital with which to secure land and buildings (see, for example, Mayer and Temkin, 2006), some groups are managing to overcome this obstacle by developing partnerships with land-rich entities.[23] In addition to such a

[23] This strategy is being used by a number of nonprofit organizations. For example, The Wisconsin Partnership for Housing Development Inc, located in Madison, sees partnerships with local churches that own land as a viable strategy for becoming more engaged with the inner city housing market in Milwaukee. According to field notes based on a site visit to the organization: "The approach involves giving technical assistance to the churches to

collaboration providing the nonprofit with access to land for its own development work, it could also enhance a for-profit developer's interest in participating with the nonprofit. This could, in turn, make a project more feasible, due to the financial support that the for-profit would likely bring to the deal. For example, a student affiliated with Harvard's Joint Center for Housing Studies noted the following:

> Private developers in urban areas partner for another indirect financial reason: access to land they could not otherwise purchase. Urban developers in areas such as New York City face a growing shortage of affordable, developable land and, subsequently, rising land costs. In recent years, New York City has begun aggressively foreclosing properties of owners who are negligent in paying their property taxes. This land has then been transferred to nonprofits through a much easier disposition process than to for-profits, sometimes at costs as low as one dollar. Since land is a key reason to partner, some urban developers investigate which nonprofits own or have access to land as the first step in the partnering process (Chung, 2004, 13-14).

In addition to nonprofits working hard to create innovative mechanisms to acquire land and buildings, other frequently noted attributes of nonprofit housing providers include their connections to their communities and residents and their desire to provide services that go beyond housing.

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consider development on their sites and potentially co-developing with them or marrying them with a for-profit developer" (Mayer and Weber, 2005, 6).

The Columbus Housing Partnership, in Columbus, Ohio, has followed a similar approach. The organization provides homeownership counseling for church members and, in the process, staff members connect with church leaders and build trusting relationships. With affordable parcels of land being scarce, the organization is aware that many of these faith-based groups may have land and may be willing to partner with the nonprofit at some point in the future, thereby making additional development possible (Bratt, 2006b).

In California, a field visit to the Mid-Peninsula Housing Coalition revealed that the organization relies heavily on good relationships with local governments, particularly in terms of locating buildable land: "With the limited set of sites available for building affordable housing (and zoned appropriately), many in public ownership or control, and [the organization's] desire for substantial volume, the local government support that yields site opportunities and funds to deal with high Bay Area project costs are critical" (Mayer, 2005, 4). While this is being recognized as an important part of the organization's activities, staff members acknowledged that they "may have missed out on some opportunities in localities in which they had not nurtured 'social' relations" (Mayer, 2005, 4).

Connections to Community and Residents

Despite the complexities of any single entity trying to understand and represent the "community,"[24] there is a widespread view that community-based organizations "are particularly effective at delivering services" (HUD, 1996, 22). This is due, in part, because CDCs are assumed to be connected to their local communities and to be good representatives of community interests. And it is these connections that help them understand and appropriately respond to local needs. Although community involvement in CDC activities typically goes well beyond board membership, more than one-half of the members of CDC boards are generally drawn from the local community (Vidal, 1992).

Empirical evidence suggests that community-based development organizations (which include CDCs) work to empower the poor and respond to community concerns. In particular, these organizations have demonstrated that local decision-making processes can become more open and accessible to community members, who, in turn are able to set a neighborhood development agenda, rather than this being done by the business community (Rubin, 1993, 106). In addition, researchers at the Urban Institute have found compelling evidence of community leadership and strong alliances both inside and outside CDCs' neighborhoods (Walker, 2002, 35).[25]

Holistic Approach to Housing--"Housing Plus"

Given the standing of CDCs and other nonprofits in their local communities, it is not surprising that these organizations typically focus significant effort and resources on the social needs of residents, as well on their communities as a whole.

In terms of the community orientation of CDCs, these groups may focus on crime watch programs, park and open space beautification, commercial redevelopment, small business assistance or some combination, as described in a number of studies (e.g., Vidal, 1992;

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[24] "Community" is not a monolithic entity (Heskin, 1991; Bratt, 1996). Any given "community" is likely comprised of tenants and homeowners of varying income levels, residents as well as absentee landlords, small businesses and larger commercial outlets. And there is no reason to assume that all these various groups—"the community"—will agree on all issues.

[25] Another area of research has explored the extent to which developments built by nonprofit and for-profits have differential neighborhood effects. Ellen and Voicu (2006) have found that both types of developments generate significant, positive spillover effects. Moreover, these effects may be more sustained over time in rehabilitation projects sponsored by nonprofits. The authors posit that "nonprofits are likely to invest more in developing and maintaining features that benefit the broader community than their for-profit counterparts" (49). However, they add that "in the case of small projects, nonprofit organizations delivered significantly lesser neighborhood benefits than their for-profit counterparts" (49). This finding further emphasizes the great variation in nonprofit organizations, in terms of size and capacity.

Leiterman and Stillman, 1993; Sullivan, 1993; Robinson, 1996; Bratt and Keyes, 1997; Grogan and Proscio, 2000; Von Hoffman, 2003).[26] Briggs and Mueller note that theirs was "perhaps the first-ever attempt to analyze rigorously collected data on a wide range of effects of CDC practices on the lives and attitudes of neighborhood residents." Among their many findings was that two of the three organizations studied "had measurable effects on the social fabric of their neighborhoods..." (1997, 1, 7–8).[27]

While housing is the foundation of most CDC activity and is usually viewed as part of a wider-scale community development agenda, many CDCs also, explicitly or implicitly, strive to promote resident "self-sufficiency."[28] Such activities include personal responsibility-building; skill-building for work (e.g. employment counseling, job training); service delivery; economic development; community-building through organizing, advocacy and political consciousness-raising; and homeownership (Bratt and Keyes, 1997).

Recent evidence about the importance of resident-oriented programs to the large nonprofit housing providers comes from a study of members of the Housing Partnership Network. A common theme among respondents to an Urban Institute-administered survey was that their organization's commitment to providing programs constituted a key difference between them and the for-profit developers in their area. Among the top two organizational missions cited by the groups responding to the survey, 24 percent noted community revitalization and 22 percent noted the creation of service-enriched communities (Mayer and Temkin, 2006).

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[26] Over the past decade, a growing movement, known as Comprehensive Community Initiatives (CCIs), has incorporated and expanded upon the community-building mission of CDCs. Funded by a number of foundations, CCIs generally have one or more CDCs as central actors in broad-based, community development initiatives (Eisen, 1992; Connell et al., 1995; Roundtable on Comprehensive Community Initiatives for Children and Families, 1997; Fulbright-Anderson et al., 1998).

[27] Another related area of inquiry has explored the neighborhood spillover effects of housing built or rehabilitated by nonprofit and for-profit developers. For example, Ellen and Voicu (2006) examine increases in neighborhood property values and find positive spillover effects of both nonprofit and for-profit projects. In addition, "while the spillover benefits generated by nonprofit housing are sustained over time, the benefits generated by for-profit housing appear to diminish somewhat in the years after completion. [Further], while large development deliver similar benefits regardless of sector, we find that in the case of small projects, for-profit developments generate greater impacts than their nonprofit counterparts, perhaps as a result of capacity constraints faced by nonprofits" (2006, p. 32).

[28] "Self-sufficiency" is a frequently used term that generally refers to a household's ability to provide for itself without government subsidies. However, it is a problematic term, since virtually no one in society is truly "self-sufficient"; virtually everyone receives one or more forms of direct or indirect public assistance (Bratt and Keyes, 1997).

The surveys also included many detailed statements about the extent to which programs are integral with organizational mission. This was confirmed repeatedly in a series of in-depth phone interviews with 12 nonprofit groups, as noted in the following examples:

> For many groups, programs are so central, that some of those interviewed indicated that housing, through a housing-based services program, is a means to help move people out of poverty. According to staff members at the Columbus Housing Partnership, Inc., the organization was producing good housing developments, or communities as they are called, but they felt that there was a piece missing. In order to move people out of poverty, they needed a more holistic approach, which included providing programs to families. Similarly, ACTION-Housing Inc.'s foreclosure prevention program is viewed as a 24-month process that involves both helping to stabilize their clients' mortgage payments as well as other aspects of their lives. And Assistant Director Kate Monter Durban of the Cleveland Housing Network summed up their approach this way: "You can't succeed in working with low-income families without offering at least some level of services. They have too many needs; our goal is to provide a basic safety net, but we are aware that we are not able to cover all the bases." This was echoed by Trudy McFall, Chairman and co-founder of Homes for America: "Right from the beginning we felt that housing needed to be coupled with on-site services. We were not interested in a service delivery model without staff; you need people to do the job. We always have had a strong service mission, with a commitment to adequate on-site space to go with it."
>
> Carol Lamberg, Executive Director of the Settlement Housing Fund offered that, from the outset, they could see that housing and programs go together. Even when they did not own the buildings that they helped to develop, they pushed the services agenda. They shared developers' fees with the neighborhood organization in the hope that services would be included. She further observed: "housing is important without services but it is better with. America is supposed to provide opportunities for upward mobility, to equal the playing field, to attain the American vision. Mixed-income housing is a great way to pull people in and offer them something. Community programs for a mixed-income population encourage upward mobility for the lower income groups" (Bratt, 2006b).

As CDCs and other nonprofits have gone beyond producing "housing alone" (no small achievement in itself), they have emerged as leaders in providing—or in many cases helping to coordinate—housing plus services. The particular mix of initiatives that a group selects depends on its mission, the community's needs, staff capacity, and the availability of funds and other types of assistance (Leiterman and Stillman 1993; Vidal 1997).

Comparative Production Costs and Long-Term Viability

Two central questions relate to the relative strengths and weaknesses of for-profit and nonprofit sponsorship of housing that is affordable to low income households. The first question pertains to the "bottom line." Is it more cost-effective to pursue one strategy or the other? Second, what is the long-term viability of projects developed by each type of sponsor? The answers to both questions, however, are far from conclusive.

Production Costs

One of the first studies comparing production costs of housing built by nonprofit compared to for-profit developers was completed in 1993 by a team of researchers at Abt Associates, under contract to HUD. Despite some serious methodological flaws, which the researchers enumerated,[29] a "***rough comparison*** with industry standards" of development hard costs for the six new nonprofit-constructed projects included in their study revealed that:

> ***The actual per-square foot construction costs for the new construction study projects ranged from 20 percent above to 20 percent below the nominal industry costs for the specified location, type and size of building.*** This variability relative to construction costs is not unlike what one might expect to see from a similar sample of for-profit projects (Hebert et al. 1993, ES-18; emphasis in original).

To the extent that nonprofits' costs of construction were higher than those of the for-profits, some of the reasons were attributed to the essential characteristics of nonprofits, particularly their need to depend on multiple funding sources and the delays that result by having to work with so

[29] In addition to the sample being very small and non-random, there were other important limitations: "The study made no provision for correspondingly comprehensive data collection for similar actual for-profit projects;…the study did not have the resources for the extensive data on building specifications, construction techniques, and materials that would be necessary to do a ***precise*** build-up of estimated costs using industry standards…; aside from direct construction costs, reconnaissance indicated no industry standards generally applicable to total development cost or its components, such as for pre-development costs, legal and organizational costs, and marketing, for example; [and further] metropolitan-wide construction cost averages may not reflect typical construction costs for difficult urban affordable housing sites" (Hebert, et al., 1993, ES 17-18).

many different funders (an average of 7.8 per development included in the study). The report went on to state that:

> The overall pattern of costs among the 15 projects suggests that the variance among the nonprofit project costs might be at least as large as any variance in costs between nonprofit and for-profit projects….[I]n Boston, the range of costs for nonprofit and for-profit projects may be similar. Therefore some of the higher cost levels observed in our study may be more a function of local development conditions and requirements rather than systematic differences in nonprofit versus for-profit comparative efficiencies (Hebert et al., 1993, ES-20).

In a subsequent study undertaken by the U.S. General Accounting Office (GAO, now known as the U.S. Government Accountability Office), researchers found that the average cost of units built by nonprofit developers was about $18,000 higher than the average cost of for-profit developers' units (1999, 1). However, when key differences in the units' characteristics were taken into account, most of the reason for the higher costs among nonprofits was explained and the cost differences were substantially less, from $1,600 less per unit to $12,700 more per unit for units built by nonprofit compared with for-profit developers. The researchers concluded that the difference in estimated per-unit costs for nonprofit and for-profit developers was not statistically significant and, for the most part, could be explained by the following:

- although unit costs were not found to vary significantly with the economic condition of the neighborhood, nonprofits were more likely than for-profits to build in economically distressed areas;
- nonprofits were more likely than for-profits to build units eligible for additional tax credits (additional tax credits are available in areas where development costs are high relative to incomes—such units were more costly to develop than those not eligible for additional credits);
- nonprofits were less likely to develop garden style units and more likely to build mixed developments than for-profit developers—the latter are more costly to build than garden style units;
- nonprofits were more likely to develop larger units than for-profit developers—and these units are more costly to develop than smaller units;

- nonprofits were more likely to be working in the Pacific and Northeast regions than for-profits—and these are areas with higher costs.

In another major comparative study of costs of development done at about the same time as the GAO analysis, Cummings and DiPasquale found that, on average, projects developed by nonprofits tended to have higher total development costs per unit than for-profit developers—$90,268 compared with $63,778. Even after controlling for project size, unit type, and location, nonprofit-developed units, on average, cost 20.3 percent more than those developed by for-profits (1999, 259, 304).

As noted at the outset of this section, the data about the relative costs of nonprofits and for-profits developing housing that is affordable to low-income households are not conclusive. But when costs are found to be higher, as in the Cummings and DiPasquale study, for example, researchers invariably note that the higher costs need to be considered carefully, in the context of the other benefits that are typically associated with this housing. This view is summarized well by O'Regan and Quigley:

> Arguments are seldom put forward that nonprofits will provide the same affordable housing at the same cost as for-profit firms, but rather that nonprofits will supply the housing that is the most difficult to induce from for-profit firms. Thus, to the extent that federal housing goals emphasize harder-to-serve populations or those with particularly low incomes, this rationale suggests a greater involvement of nonprofit providers (2000, 300).

The various benefits of nonprofit development, including their focus on those groups that are typically difficult to serve, have been noted previously.

Long-Term Viability

Very little data is available concerning the comparative long-term viability of developments produced by nonprofit and for-profit sponsors, using the same programs. In an early report by the GAO on the Section 236 program, 47 percent of the developments sponsored by nonprofits were found to have failed (e.g. mortgage default resulting in a claim on the FHA insurance fund), although they accounted for only 23 percent of these developments. In brief, "nonprofit sponsored [Section] 236 projects failed at four times the rate of limited dividend sponsored projects" (1978, 93). The GAO report explained this finding by observing that nonprofits have little resources to weather adversity; they are probably less experienced; they tend to admit the lowest income people who are eligible for the subsidy program; and they tend to serve needier families than limited dividend sponsors (1978).

The comparative cash flow generated from properties developed by nonprofit and for-profit developers of LIHTC properties was explored by Cummings and DiPasquale (1999). They found that nearly 83 percent of the developments owned by for-profits had positive cash flows, compared with only 60 percent of the developments owned by nonprofits. They concluded their discussion on this point with the following observation: “Despite incentives to keep net income close to zero, no project can continue indefinitely with expenses exceeding revenues. Syndicators and investors indicate that as projects increasingly are structured to provide no positive cash flow, funding reserves becomes very important.” And, with only 11 years of experience with the program at the time of their analysis, they observed that “there is no evidence on how these projects will fare when they need substantial capital infusions for renovations or systems replacement. How well these projects clear such hurdles will be a major determinant of long-term viability (1999, 278).

In another study of FHA insured multifamily properties, researchers found that “distressed and stressed properties were more likely than sound properties to have nonprofit/cooperative or limited dividend owners and were less likely to have for-profit owners.” However, since for-profit owners predominate as sponsors of the less problem-laden newer assisted properties and nonprofits are more prevalent as sponsors of the generally more troubled older, assisted properties, these findings would be expected (Finkel, et al., 1999, 4-11).[30]

Additional information revealing concerns about the long-term financial viability of housing owned by nonprofits comes from a study by Bratt et al. (1994). Although they did not undertake comparative analyses, their research revealed some significant financial problems facing the developments they studied.[31] The following are their most important findings on this issue:

[30] Older assisted properties were insured by HUD and receive either mortgage interest subsidies under the Section 221(d) (3) or 236 programs or rental assistance under one of the Section 8 programs, except for the New Construction/Rehabilitation program. Newer assisted properties were insured by HUD and receive rental assistance through the Section 8 New Construction/Rehabilitation program. Distressed and stressed properties had what the author’s term “annual backlog-adjusted cash flow deficits” exceeding $250 per unit and less than $250 per unit, respectively. This refers to the adequacy of cash flow to cover unfunded backlogs. Distressed properties’ operating and physical needs would be far in excess of available revenues and reserves (Finkel, et al. 1999).

[31] Finkel et al. (1999) present extensive information on thousands of HUD-insured properties which reveals significant financial problems and physical backlogs of repairs.

- The properties examined displayed a problematic pattern in both capital and operating reserve balances. In 1992, only 6 of 23 developments for which data were available had capital reserves of more than 2 percent of the replacement value of the property, a commonly used industry guideline. Of the 23, 12 had some reserves, but less than the amount needed, and 5 had no capital reserves whatsoever. Given the importance of capital reserves, it is safe to day that 17 of the 23 developments examined are in a dangerous position.
- On the operating reserve side, the picture is even worse. In 1992, 14 of the 23 reporting developments had no operating reserves at all. Another 4 had operating reserves of less than 10 percent of their operating budget. Only 3 developments reported reserves over 20 percent of operating costs, the number that HUD considers the minimum for public housing authorities.
- More than one-half of the total number of the developments in their sample (15 out of 28) reported that they were spending more than they were taking in. And the overspending was serious. For 11 of these 15 developments, the deficit was more than 10 percent of annual operating expenditures, for 10 properties it was over 20 percent, and for 7 it was over 30 percent.
- The owners of these properties are dealing with their financial issues by allowing their accounts payable rise to a dangerous level, or they are using nonrecurring sources of income to balance the budget, neither of which is an acceptable solution (8-9).

While no effort was made to quantify how specific conditions created the above types of difficulties, a number of reasons were offered. For example, the quality of the initial rehabilitation was often found to be problematic, due to inadequate construction budgets or poor workmanship and dishonesty among contractors. In addition, small portfolios of properties made it difficult for organizations to cover the full costs of management operations from property management fees and neighborhood factors often created adverse conditions and increased management costs.

Among the most interesting findings was the array of reasons behind the first set of problems. While the poor quality of the initial rehabilitation may have been due to mundane errors on the part of the organization, particularly noteworthy were conscious decisions organizations made to undertake a project, despite their awareness that funds were not adequate. In those cases, organizations reported that their desire to respond to local pressures to improve a problem property or to provide some additional housing in the area became the dominant concern (Bratt et al., 1994, 11-12; 121-130).

The willingness of nonprofits to undertake projects in areas that other developers are more likely to by-pass appears to be a key factor in any differences in the viability of developments owned by nonprofit and for-profit developers. But if developments are not able to survive, there are obviously both short-term and long-term implications for residents, for organizations, and for the host communities.[32]

The remaining task involves an attempt at trying to resolve the question of how nonprofit and for-profit developers can best play their respective roles.

For-Profits and Nonprofits—Recommended Roles

This paper poses the question: Should we foster the nonprofit housing sector as developers and owners of subsidized rental housing? The answer is an unequivocal "yes."

Reflecting on this question, the Millennial Housing Commission offered that: "Effective delivery of affordable housing relies on enabling public sector, for-profit businesses, and nonprofit organizations to do what each does best" (2002, 28). Of course, the "devil is in the details." What, exactly, does each do best and in whose judgment? Some of the particular attributes of nonprofit and for-profit sponsorship of housing have been discussed. Yet, it is not a matter of deciding whether nonprofits or for-profits should be involved in housing production for low-income households. Instead, the challenge is to be as clear as possible about what the various roles should encompass.

Somewhat parenthetically, in addition to both nonprofits and for-profits having considerable responsibility for producing housing that is affordable to low income residents, I continue to be supportive of public housing authorities as developers and managers of subsidized housing. Despite the widespread negative impressions of this program, as well as the reality that many developments continue to be severely distressed, the logic of developing housing with up-front capital grants that is permanently held within the social sector makes a great deal of sense. While this paper has not explored the positive and negative attributes of this approach, suffice to

[32] Cummings and DiPasquale (1999) found that, after controlling for a number of variables, "nonprofits generate higher returns for equity investors, suggesting that for comparable projects nonprofit developers are perceived as riskier than for-profit ones" (296). Further study is needed on the reasons behind this difference, although there are many plausible explanations for ongoing differences in perceptions about the two types of developers.

say that it still remains a viable option. But the likelihood of creating a new, widely supported public housing program is not strong, at least for the present. What, then, should be the roles of nonprofit and for-profit developers? Both nonprofit and for-profit developers can be effective producers of subsidized rental housing, as discussed below.

Nonprofit and For-Profit Developers—Either/Or?

For any developer or organization to be an effective housing producer and long-term owner, a number of competencies are necessary. In addition, the context in which development is taking place should be conducive to this activity. Nonprofits and for-profits may be differentially able to take advantage of these conditions.

A critical issue that directly relates to the differences between nonprofit and for-profit developers was mentioned at the outset of this paper but warrants repetition: large for-profits have a legal obligation to maximize earnings for shareholders and, even small business developers are still committed to earning profits. On the other hand, nonprofits are explicitly prohibited from distributing any profits that are derived from their activities to individuals. An outgrowth of this fundamental difference in the legal structures of the two types of entities is that nonprofits tend to be more mission-driven and they are typically willing to accept lower levels of returns than for-profit developers. In addition, there are many types of developments that the latter would simply not be interested in pursuing, such as those with less than about 40 units and/or targeted to at-risk populations, such as the formerly homeless or to people with physical or mental disabilities. Many nonprofit groups also typically operate with limited cash reserves[33] and would likely have difficulty managing large, complex projects, such as HOPE VI developments. At the same time, if a project is extremely complex, for-profit developers may not be interested in participating. For example, a recent *New York Times* article noted that: “developers… tend to shy away from the complex financial packages and long lead times necessary for most affordable projects” (Sharoff, 2006).

Beyond the legal mandate and constraints of nonprofit and for-profit developers, the following represents the most important requirements—both organizational and contextual— for the successful development of subsidized housing.

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[33] See, for example, Bratt et al. (1994).

- **Staff capacity** to conceptualize the project, line up subsidies and financing, oversee construction, and manage the completed development (either in-house or contracted out).
- **Front-end capital** to cover initial costs including land/building acquisition, engineering, and architectural fees, as well as **financial capacity** to enable the project to survive during what can become long delays in permitting and construction.
- **Community support for the project** to assure that it is consistent with local needs and preferences.
- **Access to affordable land and/or buildings** is an essential need for any development, but particularly one that is focused on low income occupancy.
- **External supports, financing, and subsidies** must be available. External support may include local government approval, as well as assistance from local or national intermediaries. Assembling the needed financing, including sources of subsidies to assure that the units are affordable, is also essential.
- **Market conditions must be assessed** to assure that the completed units will be marketable at the projected rent levels. This may be particularly important in mixed-income developments. But even if the development is geared exclusively for low income occupancy, a weak market could create significant rent-up problems, thereby reducing projected income and threatening financial viability.
- **Capacity to manage the development and oversee its progress** is essential. This includes an ability to manage the entire development team, as well as to make sure that construction is consistent with the plans. Whether this role is performed by a development consultant or by in-house staff, all housing sponsors must be in full control of the “nuts and bolts” of a project’s development.
- **Capacity to manage the property,** again whether done in-house or contracted out, this is a critical role of long-term owners of any type of housing, including subsidized housing.
- **Organizational scale** may be important since entities with large portfolios can likely use income from their high-performing properties to subsidize those that are running at a deficit. In view of the risky nature of real estate, it is likely that any developer will have some of both types of properties. However, the larger the organization, the more likely that ailing properties can be kept afloat.

- **Interest and capacity to provide services to residents** is of critical importance in low income housing developments. Whether these services are provided directly by the owner of the housing, or through networking with other agencies, various types of programs should be available and easily accessed by residents.
- **Neighborhood revitalization** and community development are activities that are often thought to be inseparable from the production of subsidized housing. The importance of the housing that is built both fitting in with the existing neighborhood, as well as enhancing it, is another important factor to be considered.
- **Long-term affordability** is almost a *sine qua non* of subsidized housing development. Too often, programs have been devised that have not included mechanisms to make sure that the units that get built and that are occupied by low income households, will remain available both to the original tenants, as well as to future generations who need housing assistance.

As noted in the accompanying chart, some of these tasks are typically assumed to be better performed by nonprofits. In other areas, however, for-profits would generally be considered to have the advantage. In saying this, it is important to underscore that, as discussed earlier; there are a broad range of nonprofits and a broad range of for-profits. Either can have enormous sophistication, financial capacity, and technical expertise. Smaller and less well established organizations, whether for-profit or nonprofit, will likely be in less good positions to take on subsidized housing development, particularly large-scale complex projects. Therefore, in making the following generalizations, it must be emphasized that they are just that:

Development and Management of Housing for Low-Income Households:

Comparison of Nonprofit and For-Profit Strengths and Weaknesses

	Nonprofits	**For-profits**
Staff capacity	Highly variable	Generally assumed to have consistent and strong capacity.
Front-end capital and financial capacity	Often a problem, particularly for small organizations	Generally assumed that cash is available to launch developments as well as to see the project through to completion.
Community support	Viewed as a clear strength	Highly variable; may be lacking.
Access to affordable land/buildings	May be a problem, but public land may be more accessible and partnerships with land-rich entities may have been developed.	Given the presumed availability of cash to acquire properties, this may not present obstacles. However, in high cost areas, the costs of acquisition at market rates could make development unfeasible.
External supports, financing, subsidies	Nonprofits typically have access to a range of external supports and subsidy programs. Access to conventional financing may present more of a problem, particularly for small organizations.	These supports typically are neither available to for-profits, nor are they assumed to be needed. Access to subsidy programs, with the exception of LIHTC, may not be possible. However, access to conventional financing is typically not a problem.
Market assessment	May not always be carried out with adequate sophistication.	Usually considered a strength of for-profits.
Development oversight	May be variable, whether done in-house or contracted out.	Usually considered a strength of for-profits.
Property management capacity	May be variable, whether done in-house or contracted out.	May be variable, whether done in-house or contracted out.
Organizational scale	Most nonprofit housing developers are small. However, there are about 100 nonprofit organizations that operate at a regional or national scale.	Large variation. Many for-profit developers tend to be large.
Resident services	Important component of many nonprofits' orientations.	Usually not on their "radar screen."
Neighborhood revitalization	Often a major concern among nonprofits.	Typically of importance only as neighborhood factors may impact the development.
Long-term affordability	Typically an important focus.	Not a primary concern. In fact, for-profits typically look forward to the expiration of affordability restrictions.

generalizations, not backed by empirical evidence or hard data. But perhaps these observations provide insights into the ways that nonprofits and for-profits look in a head-to-head comparison.

This exploration into the relative strengths and weakness of for-profits and nonprofits reveals two additional important issues: the need for HUD to reconsider some of its guidelines concerning how nonprofits are required to treat any residual income that flows from the property and the need for both types of developers to be treated more similarly around key aspects of operating housing affordable to low income households.

First, HUD guidelines concerning its subsidized rental housing programs prohibit nonprofits from extracting residual income from properties either from cash flow or from refinancing that, in turn, could be used for other projects or for organization-related expenses. With specific reference to the Section 202 program, which is only available to nonprofit sponsors, residual receipts cannot be used for non-project related activities[34]—such as covering organizational costs, launching new initiatives, off-setting deficits that other projects may be encountering, or to cover service provision at other developments.

Second, in other HUD programs that are accessible to both nonprofit and for-profit sponsors, HUD is more restrictive about how the former is allowed to use any income that is derived from a specific project. A recent memorandum on this subject concluded the following:

> Three of HUD's central programs explicitly restrict non-profits' ability to retain and use excess project revenue in a way that they do not restrict for-profit owners. Section 8 New Construction/Substantial Rehabilitation programs maintain a blanket ban on such distributions with exceptions available only on an ad hoc basis. Section 221(d) (3) restricts the use of project income to meeting project expenses and prohibits distributions. The regulations regarding excess income for non-profits under Section 236 are similar to those for 221(d) (3). Furthermore, for programs where no explicit restrictions are found, HUD employs a general presumption against project income distribution to nonprofits, as stated in its handbook.[35] This restrictive treatment of distributions does not appear to be mandated by statute, but is simply a matter of policy (Stewards of Affordable Housing for the Future, 2005, p. 5).

However, the memorandum further points out that in several of HUD's other programs, a much greater degree of flexibility around the issue of nonprofits retaining project income is provided. For example, in the HOME program, the question of whether a nonprofit is able to retain project income depends on the local jurisdiction's rules, not HUD's. HUD's regulations "do not bar

[34] 12 U.S.C. 1701q(j)

[35] U.S. Department of Housing and Urban Development, Handbook No. 4350.1, Multifamily Asset Management and Project Servicing § 25-1.

nonprofit owners of rental housing from receiving and retaining program income" (Stewards of Affordable Housing for the Future, 2005, p. 4).[36] Such provisions, could therefore serve as a template for expanding a more lenient approach in all HUD's multifamily programs.

To the extent that any given development is providing excess revenues, nonprofits should be able to reap the benefits, so long as the funds continue to be used to advance the mission of the parent organization. Until this type of change occurs, nonprofits will continue to be placed at a significant disadvantage in relation to their for-profit counterparts who are able to extract equity or excess cash flow from a successful project.

According to Michael Bodaken, President of the National Housing Trust, "sustainability—whether one is a for or nonprofit—can only be achieved through sufficient reserves and cash flow. Cash flow can only be achieved by good underwriting at the inception of ownership or, later, via refinancing. Nonprofits and for-profits don't differ at all with respect to these fundamental rules of real estate development. So why treat them differently?"[37] And, similarly, "in order to maximize long term affordability for our existing and future affordable housing stock, why not impose the same long term affordability terms and restrictions on back end residual gain—on nonprofit and for-profit developers alike?"[38] If the goal is long term affordability, it would make sense for all types of sponsors to be held accountable to this standard, operating under the same set of rules.

Ellen and Voicu further offer that "government officials will be well served by contacting housing rehabilitation dollars out to either nonprofit or for-profit organizations…there is ultimately a value in maintaining a mixed organizational environment in which both nonprofit and for-profit providers can compete" (2006, 50).

Nonprofit – For-Profit Partnerships

Of course, it does not have to be either-or. There is fertile ground and a significant amount of experience with nonprofits and for-profits joining together in partnership arrangements. In 2002 The Urban Land Institute hosted a two-day meeting at which specific experiences with collaborative relationships were presented. To sum up:

[36] See 24 C.F.R. §§ 92.503, 92.504 (2005).
[37] Private email communication, November 17, 2006.
[38] Private email communication, November 12, 2006.

> Participants discussed the strengths that both CDCs and for-profit partners bring to joint venture development projects, stressing that each partner can bring knowledge, expertise, and resources that meet the needs of the other partner. CDCs can provide expert knowledge of the community and an understanding of the local market, and can boost local credibility for a project. A for-profit developer can provide development expertise, resources and credibility with lending sources (Myerson, 2002, 9).

Commenting on the need for for-profits to work with local partners, the president of a large development firm observed: "The deals we've been involved in usually have long histories with lots of politics. We can't just go in and announce we're going to build 1,200 units. We need our local partners who are engaged in the community" (Sharoff, 2006). Thus, while the nonprofit may be seeking a for-profit partner with more expertise or resources, the for-profit may need the nonprofit both for its community connections and in order to take advantage of the variety of special programs targeted specifically to nonprofit sponsors. There are a number of specific attributes of a strong collaborative arrangement between a nonprofit and a for-profit developer. Most of the following are based on suggestions offered by Myerson (2002, 9-10) and Chung (2004):

- Each partner should have development experience and knowledge;
- Nonprofits should be able to clearly articulate and even quantify the contributions that they will bring to the deal so that the for-profit developers can understand their value;
- But to the extent that the nonprofit may be lacking either development experience or an ability to clarify the value of its role, third parties (e.g. housing lawyer or more experienced nonprofit) may be brought into the negotiations to advocate on behalf of the nonprofit. In short, each party should work to understand each other's perspective. The benefits to each partner should be articulated, including how profits will be shared, the anticipated social and economic benefits to the community, the goals of the for-profit partner in terms of increased visibility in the community, and the potential for increasing nonprofit capacity;
- The roles for each partner should be clearly defined and a project manager identified;
- There should be a willingness on the part of the for-profit partner to share its expertise with the nonprofit on issues pertaining to organizational sustainability, succession, and future leadership; and

- The legal details of the partnership must be carefully crafted and understood by all parties and they must be consistent with the Internal Revenue Code.

Concerning this last point, there is a considerable body of legal precedent related to the structuring of nonprofit/for-profit partnerships, particularly as they relate to LIHTC deals. A few points are important to consider, as suggested by Rubin and Klein (2006):

- The nonprofit sponsor must typically provide a variety of guarantees and indemnities to investors (e.g., including environmental indemnifications, guarantees of construction completion, operating deficit guarantees, and tax credit recapture guarantees);
- The IRS and the Courts have determined that some commitments made by a nonprofit organization as part of a partnership with a for-profit entity violated its charitable purpose, thereby threatening its tax-exempt status. A key question relates to whether the structure of the deal effectively forces the sponsor to act in a manner inconsistent with its charitable goals or to jeopardize its charitable mission by exposing charitable assets to excessive risk;
- On April 25, 2006, an internal IRS memorandum set forth new criteria for evaluating the involvement of tax-exempt entities engaged with LIHTC transactions. Although this does not carry the weight of law, it provides some guidance for how the IRS might view partnerships that enable nonprofit organizations to access equity under LIHTC, while not jeopardizing their tax-exempt status. Specifically, the memorandum requires that the nonprofit take certain steps to limit its financial exposure, it outlines caps on the guarantees provided by the nonprofit entity, and it states that the partnership documents must contain a provision specifying that, in the event that a conflict of interest exists between the charitable purpose of the nonprofit and the obligation, under the partnership, to maximize profits for investors, the charitable purposes will prevail.

Rubin and Klein conclude their analysis by stating that:

> the April 25 Memorandum represents a reasoned, practical approach to the issues of risk and control in an LIHTC partnership, largely reflecting business practices that already prevail in many partnership arrangement between seasoned investors and well-represented nonprofit organizations…[It] is a step in the right direction. It is to be hoped that the IRS will ultimately create a legal safe harbor through a formal rulemaking process, so that

> charitable entities engaging in the critical mission of developing and operating affordable housing may access much-needed equity under the LIHTC program without jeopardizing their tax-exempt status (2006, 8, 10).

An essential component of a nonprofit/for-profit partnership involves assuring the long-term affordability (preferably in perpetuity) for low-income households. As noted earlier, one of the major drawbacks of involving for-profit developers in subsidized housing programs is that once the affordability requirements expire, these developers have little incentive to maintain the units for low-income occupancy. Although the Low Income Housing Tax Credit's time limit has been extended to 30 years (up from the original 15 years), even this period is not long enough. Unless housing is secured for low income occupancy in perpetuity, experience has shown that what seems like a long use restriction when a development is first built passes very quickly.

Of course, nonprofit developers are subject to the same time limits, in terms of guaranteeing the affordability of their units as for-profit developers. But the mission of nonprofits typically provides a strong motivation for them to continue to maintain the units for their target population. Nevertheless, the ability of nonprofits to achieve this goal is dependent on there being adequate financing and capital available.

In LIHTC partnerships, the Internal Revenue Code now allows a nonprofit the right of first refusal to purchase the property (at the end of the initial 15 year compliance period) for an amount essentially equal to $1.00, plus accumulated debt on the property (which could be assumed if the lenders are willing), plus the investor's exit tax liability.[39] This, then, makes it possible for the partnership to be dissolved and for the housing to remain in the social housing sector, over the long-term.[40] However, as just noted, the ability of nonprofits to do this will likely be dependent on the availability of additional subsidies. A possible area of further inquiry could explore the extent to which nonprofits are, in fact, facing serious dilemmas about how to maintain their units for low income residents, once term limitations expire. Also important is a better understanding of how this challenge is being addressed and the types of public assistance needed to help them achieve their goals.

[39] This is based on a summary of the Internal Revenue Code [42(i) (7)], offered by Roberta Rubin. She further states that although the title of the section "refers to a tenant's right of first refusal, the text itself refers to a right of first refusal on the part of a qualified nonprofit organization as well." Personal email communication, July 28, 2006.
[40] Among the other stipulations of the April 25, 2006 IRS memorandum was a restatement of the right of first refusal given to nonprofit organizations. As noted by Rubin and Klein, this "represents an exit strategy for investors as well as a path to ultimate nonprofit control of housing" (2006, 8).

Concluding Note

In view of the continuing need for increased housing production that is affordable to low income households, it is essential to draw on the resources and capabilities of all types of developers—for-profit, nonprofit, as well as public housing authorities. While each type of developer can be successful on its own, partnership arrangements are extremely important. The various strengths that each party brings to a development can result in projects that are well connected to community needs, while also having the financial backing to assure viability.

Aside from the housing development's financial "bottom line," also to be considered are the societal contributions that this housing makes. Whether the developer is for-profit, nonprofit, or a partnership between the two, the goal should be to meet the requirements of the "double bottom line." Bratt et al. (1994) may have been the first to use this phrase, which is defined as the simultaneous need for financial accountability *and* a commitment to social goals. They further observed that most of the groups analyzed in their study were aware of this need, striving

> to meet their social mission while maintaining the financial stability of a complex business. The organizations have come to recognize that it is not enough to be caring landlord with roots in the community. Rents must be collected (and raised when expenses rise), necessary evictions carried out, buildings cleaned and maintained in good order, and vacancies filled in a timely fashion. Recognition of the financial imperative of running a tight ship has come with difficulty to some owners—and then only after peering over the edge of financial and organizational disaster (Bratt et al., 1994, 70).

Since housing needs are not abating, all low income housing must serve as a long-term community resource and partnerships must be structured accordingly. Beyond the type of development entity, adequate financial resources—subsidy dollars—are essential to enable projects to meet the needs of our most vulnerable residents. And, as always, this is a matter of political will.

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