



# PRESERVING THE AFFORDABLE INVENTORY

**Federal resources are increasingly dedicated to preserving rather than to expanding the stock of assisted rentals. At the same time, hundreds of thousands of privately owned, unsubsidized units are at risk of loss from the affordable stock, whether through deterioration and removal or upgrading. Since about two-thirds of the nation's lowest-income households live in unsubsidized rentals, preserving privately owned low-cost units is an urgent priority.**

## FEDERAL PROGRAMS

In the past, the federal government provided affordable rental housing for low- and moderate-income households by subsidizing production of both publicly and privately owned units. Under the traditional public program, local housing agencies received operating and capital grants to rent units to the nation's poorest families. Under the various private production programs, project-based subsidies—either in the form of reduced mortgage payments or other operating support—allowed tenants to pay lower rents.

The Housing and Community Development Act of 1974 then refocused federal assistance by taking a new tenant-based approach, now known as the Housing Choice Voucher Program. Under this system, renters receive certificates to lease housing in the private market. More recently, the 1986 Tax Reform Act created the Low Income Housing Tax Credit (LIHTC) program, an initiative that has since become the primary source of new affordable housing construction.

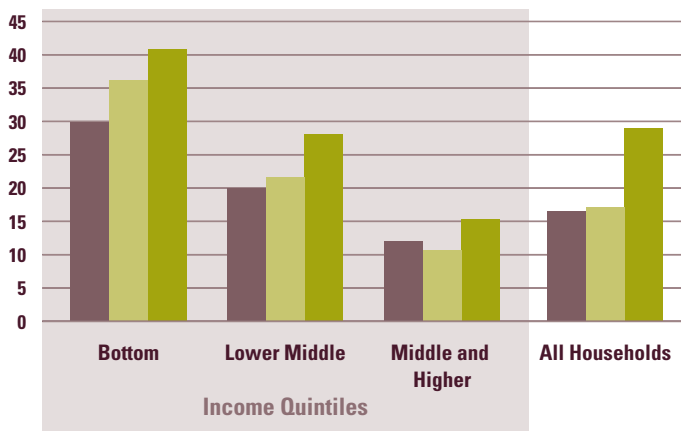
Recognizing that housing assistance is not an entitlement program, Congress has attempted to target funds to the neediest families. But at current funding levels, government housing programs serve just over a third of lowest-income renters (Figure 24). What is more, only four in ten lowest-income elderly renters—a segment consistently targeted for preferential treatment—receive housing assistance.

Pressures to limit federal domestic spending have hit housing programs particularly hard. Although precise statistics are difficult to assemble, the American Housing Survey estimates that only 6.2 million households receive rental assistance. Included in this total are the nearly 1.5 million households living in units built under the LIHTC program, which annually adds some nearly 90,000 units to the nation's assisted housing inventory.

Unfortunately, other components of the subsidized rental inventory have shown little growth in recent years.

**FIGURE 24** Assisted Housing Covers But a Fraction of Renter Families in Need

Share of Renters Receiving Assistance in 2003

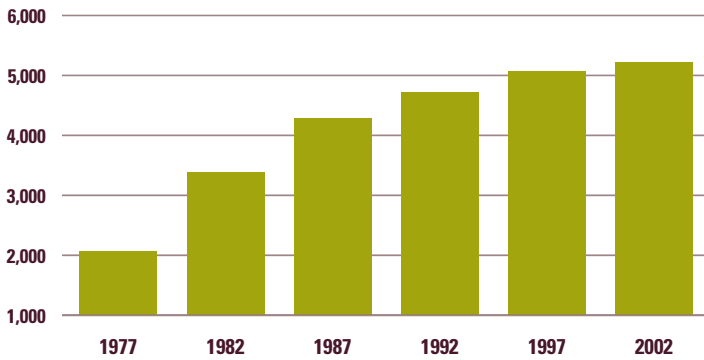


Legend: ■ Under Age 35 ■ Age 35 to 64 ■ Age 65 and Over

Source: Table A-6.

**FIGURE 25** Growth in Rental Assistance Has Slowed in Recent Years

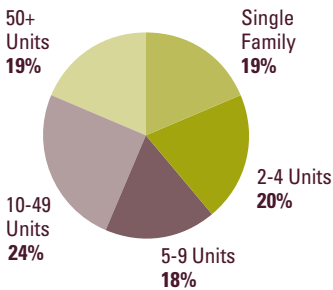
Assisted Households (Thousands)



Source: U.S. House of Representatives, Committee on Ways and Means, 2000 and 2004 Green Books.

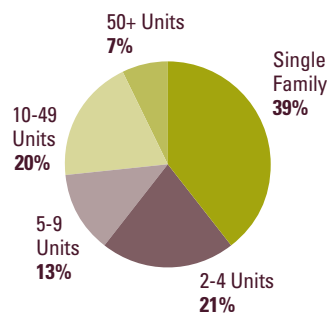
**FIGURE 26** Most Renters Live in Single-Family Homes or Small Multifamily Apartment Buildings

Shares of Renters Living in Subsidized Structures



Total = 6.2 Million

Shares of Renters Living in Unsubsidized Structures



Total = 27.4 Million

Note: Single-family units includes manufactured housing.  
Source: JCHS tabulations of the 2003 American Housing Survey.

Congressional sources estimate that the number of households receiving direct assistance (public housing, housing choice vouchers, or project-based rental assistance) has increased only 2 percent since 1999, to just over 5.2 million. This represents a sharp slowdown from the rapid gains made between 1977 and 1987, when the number of directly assisted renters more than doubled (Figure 25).

Contrary to popular perceptions, over half of the assisted housing inventory is made up of single-family homes or small multifamily apartment buildings (Figure 26). These include units rented by voucher holders as well as public housing and

project-based developments located in smaller metropolitan and non-metropolitan areas. Only one-fifth of assisted rentals are in buildings with 50 or more units. These larger properties are typically older public housing and project-based developments, as well as newly built LIHTC projects.

### LOSSES OF ASSISTED RENTALS

At the same time that the LIHTC program and incremental funding for housing vouchers have managed to add to the affordable stock, other subsidized rentals are dropping out of the inventory. Beginning in the late 1980s, private owners of subsidized housing became eligible to “opt out” of programs by prepaying their mortgages. By the mid-1990s, the trickle of opt-outs became a flow as more and more project-based Section 8 contracts expired. According to the National Low Income Housing Coalition, more than 200,000 units with project-based assistance have been lost from the affordable inventory over the past ten years.

Opting out of project-based subsidies is particularly common among owners of properties located in prosperous neighborhoods, given that they can charge higher market rents and/or convert the units to condos. In either case, these opt-outs have removed some of the most desirable units from the affordable housing inventory.

In 1999, HUD attempted to stem the tide of losses by raising the subsidies for project-based units to be more in line with market rents. In another effort to preserve project-based units, HUD also began to provide additional subsidies to encourage owners to transfer their assisted properties to non-profit entities and to help fund needed capital improvements on properties already owned by nonprofits.

The success of these efforts of course depends largely on the willingness of Congress to appropriate sufficient funds to renew expiring project-based contracts. Failure to fully fund these renewals means that losses of subsidized units will continue. Of most immediate concern are HUD-insured projects nearing the end of their 40-year mortgages, when their use restrictions are set to expire. According to the GAO, mortgages on 1,800 subsidized properties—comprising more than 196,000 units—are at risk of loss over the next 10 years.

### SMALLER PROPERTIES AT RISK

While much of the housing preservation debate focuses on the subsidized inventory, of equal concern is the fate of the privately owned, unsubsidized rental stock that serves the vast

majority of low-income renter households. This affordable inventory consists primarily of single-family and small multi-family units that filtered down to the rental housing market when their original owner-occupants traded up to bigger and more modern homes.

More than half of the low-cost, privately owned rental stock was built at least 30 years ago when construction techniques and capital markets were less sophisticated and households were less affluent. As a result, much of this inventory is now in need of substantial repair. According to the American Housing Survey, 3 million private market rental units have severe structural deficiencies and are at risk of removal. Given their limited choices in the marketplace, one in seven lowest-income renters live in such housing.

Over the ten years beginning in 1993, an estimated 2.3 million rental units (6 percent) were demolished or otherwise permanently removed from the inventory. Over half of these rentals were in older (built before 1960) one- to four-family buildings located in the nation’s most distressed neighborhoods (Table A-10). As might be expected, loss rates are higher for properties with such additional risk factors as low rent, long-term vacancies, and structural deficiencies. For older, smaller multifamily units, these added risk factors push the loss rate to 13 percent. Combining all the risk factors, including structural inadequacy, pushes the loss rate to over 20 percent (Figure 27).

## FRAGMENTED OWNERSHIP STRUCTURE

Loss of approximately 200,000 rental units each year vastly exceeds net additions of subsidized housing through the LIHTC or voucher programs. Little wonder, then, that the number of units renting for less than \$400 a month in inflation-adjusted terms has dropped by nearly one million in the last 10 years.

Among other things, losses of this magnitude reflect the fragmented ownership of the older, low-cost rental inventory. Information on the characteristics of rental property owners is limited, but recently released data from the 2001 Residential Finance Survey (RFS) suggest that many owners—and especially those with only a few units—are ill-equipped to operate and maintain their properties profitably.

Overall, the RFS data indicate that close to two-thirds of the nation’s nearly 26 million unsubsidized rental units are owned by individuals or couples (Figure 28). The rest are owned by a variety of corporations and other entities, ranging from limited partnerships to churches and nonprofit organizations to real estate investment trusts.

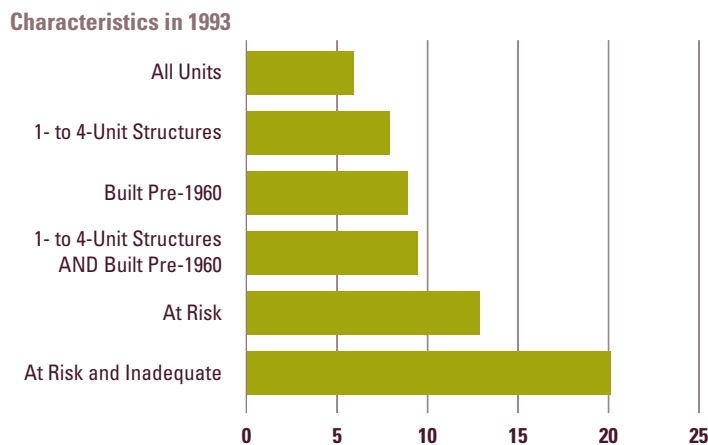
According to the Property Owners and Managers Survey (POMS)—perhaps the most comprehensive look at owner characteristics—most individuals have fewer than ten rental units, and many have just one. This is consistent with the RFS report that individuals own more than 80 percent of the nation’s single-family and two- to four-family rentals, and more than 70 percent of rentals located in buildings with five to nine units. Moreover, individuals own disproportionately larger shares of older, lower-rent units and are more likely than other owners to be financially distressed.

For many, the rental business is a part-time activity that at best provides supplemental income or housing for friends and relatives. Many individual owners bought their properties as a place to live and then became landlords because they were unable to sell when they moved. The POMS data reveal that almost a third of nonresident owners with fewer than ten rental units are themselves poor, with incomes of \$30,000 or less from all sources. Only one in ten can afford the services of a third-party manager. It is therefore unsurprising that over a third of nonresident owners report no profit from their rentals, and over 60 percent say that, given the choice, they would not buy their properties again.

For financially pressured owners, it makes sense to abandon the properties if the rents do not meet operating expenses or the selling price would not cover outstanding debt or property

**FIGURE 27** Smaller, Older Rental Properties Are Particularly at Risk of Removal

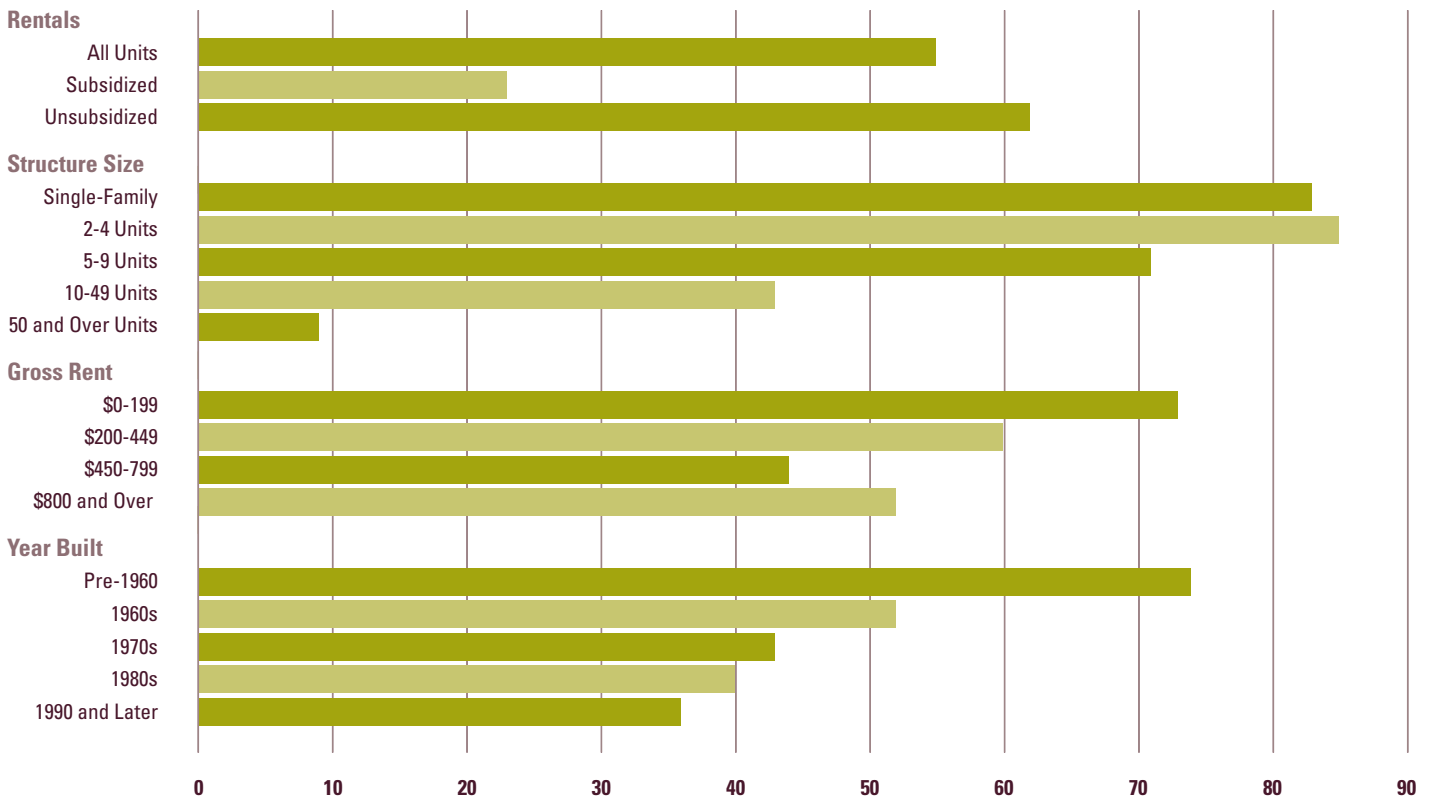
Loss Rates 1993-2003



Notes: Loss rates defined as share of all units in 1993 that were reported as permanently removed from the inventory by 2003. At-risk units are those in 1- to 4-unit structures, built prior to 1960, and renting for under \$300, vacant for more than 6 months, and/or reported as severely inadequate. Single-family structures include manufactured housing. Source: Table A-10.

**FIGURE 28** Individuals Own Much of the Smaller, Older Rental Stock

Shares of Units Owned by Individuals (Percent)



Notes: Single-family units include one-unit detached and attached structures and condominium units for rent. They do not include manufactured homes.  
Source: JCHS tabulations of the 2001 Residential Finance Survey.

tax liens. Unfortunately, abandonment leads first to structural deterioration, which not only threatens the safety and well-being of any remaining tenants, but also degrades the general attractiveness of the surrounding neighborhood. Abandoned buildings in turn bring down rents in the area, spreading the financial distress to nearby property owners.

The absence of suitable financing options only makes matters worse for small rental property owners. Loans for acquiring and improving smaller, nonresident-owned rental properties are poor candidates for securitization and sale into the secondary mortgage market. The limited availability and higher costs of financing thus prevent many small property owners from investing in needed capital improvements or selling to more financially stable owners. In addition, high administrative costs keep tax credits and other project-based assistance flowing primarily into the production and preservation of larger rental properties, allowing smaller multifamily units to drop out of the bottom of the market.

### THE OUTLOOK

At the same time that federal funding restrictions prevent expansion of subsidized housing, efforts to stem losses of the rapidly deteriorating stock of privately owned, low-cost rental apartments have gained little attention. Unfortunately, capital markets have been slow to discover ways to meet the requirements of this most “at risk” portion of the housing. Without new policies to address these barriers to preservation, both subsidized and unsubsidized units will continue to disappear from the inventory of affordable rental housing.