Financing Affordable Rental Housing:

Defining Success
Five Case Studies

Bessy M. Kong and Derek Hsiang

Wilson Center

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Introduction

Financing Affordable Rental Housing in the United States: Defining Success Five Case Studies

The challenges facing the development of affordable housing across the United States are growing as rent burdens increase, as existing affordable housing ages and is in need of repair, and as neighborhoods gentrify and citizens compete for prime real estate. The five case studies that follow examine a particular aspect of the development process and showcase the different ways affordable housing eventually gets built. In particular, we will take a look at the financial incentives used and how different players are positioned to take advantage of the tools that are available.

The following case studies examine affordable rental housing projects used by three different types of housing providers: public housing authorities, non-profit housing developers, and private for-profit developers. For each case we analyze the circumstances that led to the development of the particular project and the financial picture that made the project work.

Details of the projects vary greatly, whether it is a project for the elderly in Los Angeles, California or a mixed income development in Alexandria, Virginia. However, though the reasons for the development differ, the actual financing structure for construction and completion of the project is limited to a narrow range of financial options. Therefore, we see the federal low income housing tax credit being used time and again in projects across

the United States, as detailed in the cases studies from California, Massachusetts, Florida, and Virginia that are presented in this report. When local governments get involved in building affordable housing, they can also use the power of the local tax code to incentivize the development that is most suited to their communities. Therefore, in New York, a tax abatement program spurs targeted affordable housing development in communities in need of investment.

In addition, the primary actors in affordable housing–government agencies, non-profit housing organizations and private developers–often work closely together on a single project. In fact, without a certain amount of public/private cooperation, many projects would be infeasible. There can be overt partnerships to develop a project such as the one at Collins Park in Miami-Dade, Florida. More often than not, however, partnerships provide the necessary financial contribution at a crucial time in the life of a project. Thomas Safran would probably not have developed Skyline Village in Los Angeles without the loans from the city and county. Similarly, Chatham Square in Alexandria, Virginia relied on the mutually beneficial arrangement between a private developer and the city that held title to the property being developed.

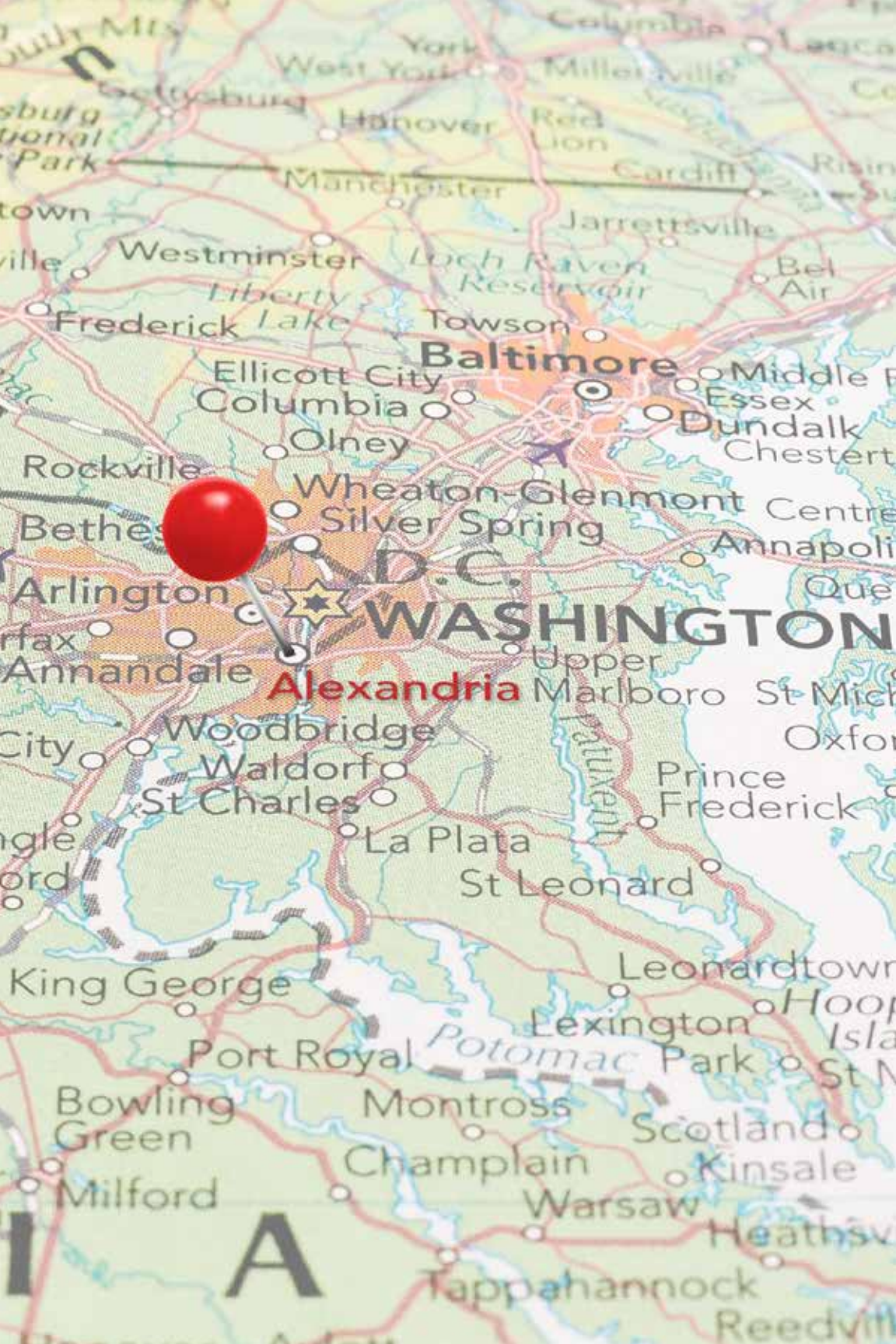
In all our case studies, we see that the success of the project depends on the developer being able to piece together various parts of the financial arrangement. This involves using the ubiquitous low income housing tax credits for affordable housing, but it also involves using federal and local grants, loans from multiple sources, bond financing and deferred fees. The exact combination will depend on funding that is available locally as well as at the federal level but it is almost always true that not just one source will provide all the funding necessary.

Finally, the case studies have certain "soft" qualities in common. These are not generally evident when a project is first being developed and financed but it becomes more apparent as the project proceeds and begins to take shape. These commonalities

include the importance of design in any project. Each of the developers highlighted in the case studies emphasizes the importance of good design to enhance the lives of their tenants whether it is the addition of thoughtful open space or the inclusion of common amenities. Good design helps generate interest in the project and ensures tenant interest in living in and caring for the property.

Given the intersection of public and private interest, it is also important that the developers of affordable housing are trusted partners in the process. Usually the developers are known to the city or county in which they work and often they have a track record of similar housing projects in the area. While there are large for-profit firms that have affordable housing divisions, such as Related Urban Development Group in Florida, many players in this arena are non-profits or were first established as faith-based organizations such as Caleb Foundation in Massachusetts. In either case, effective developers tend to have a good local knowledge base and a solid history of successful housing development. When private, for-profit developers are enticed to enter the affordable housing realm, it is usually to ensure that the more profitable market rate apartments are built. Sometimes we see unintended consequences such as the use of a "poor door" (Navarro 2014) which separates affordable tenants from market-rate tenants, and the use of early tax abatements for market rate housing, illustrated in this report by the New York City cases.

The case studies that follow are not intended to provide a definitive answer to the question of how we can foster the production of more affordable housing. Instead, they can only show how some projects succeeded and what was important in making that success possible. If they offer an overarching argument, it is this: 1) there must be a firm commitment to creating affordable housing that benefits low-income households by the government; and, 2) government cannot do it alone and needs the assistance of players in the private and non-profit sectors in order to succeed.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Hanover
Red Lion
Manchester
Cardiff
Jarrettsville
Westminster
Loch Raven Reservoir
Bel Air
Liberty Lake
Frederick
Towson
Baltimore
Middle
Ellicott City
Columbia
Essex
Dundalk
Olney
Chestert
Rockville
Wheaton-Glenmont
Silver Spring
Centre
Annapoli
D.C.
Arlington
WASHINGTON
Annandale
Alexandria
Upper Marlboro
St Mich
Woodbridge
Oxfor
Waldorf
Prince Frederick
St Charles
La Plata
St Leonard
King George
Leonardtown
Lexington Park
Port Royal
Potomac
Bowling Green
Montross
Scotland
Champlain
Kinsale
Milford
Warsaw
Tappahannock

Alexandria Redevelopment and Housing Authority

Chatham Square and the Use of HOPE VI

INTRODUCTION

In this case study, we examine the use of a federal grant program and how it can be used in conjunction with other financing to redevelop and construct both affordable and market rate housing. Here the Public Housing Authority (PHA) and developer unite to create both affordable and market rate housing to realize profit for the developer and to provide revenue for the housing authority. The Chatham Square case study also shows us how affordable housing can be built when market conditions are exactly right and the location of the public housing asset is desirable.

THE COMMUNITY

The City of Alexandria lies within sight of the U.S. Capitol Building in downtown Washington. Its proximity to the larger city has always made it attractive for people who work in Washington and its history as a bedroom community dates to the advent of commuter rail lines in the region. However, the historical roots of Alexandria predate those of Washington, having been established in 1749 as a "tobacco trading post and site of the largest slave-trading firm in the country" (City of Alexandria 2016). But it was also home to a large free African American population who continued to settle in the city after the Civil War. From its beginnings as a thriving town of about 2,700 peo-

ple in the 18th century, it is today, after two annexations, a city of about 150,000. About 22% of the population is black/African American, 16% Hispanic, and 53% white. These percentages have remained stable for much of the last decade.

Economically, the median income of residents in Alexandria was about $89,134 in 2015, much higher than the national median income, yet slightly lower than the regional median (City of Alexandria 2015). Income is derived primarily from administrative, managerial, or scientific fields with a concentration in government services. About 10.7% of the population in Alexandria lives below the federal poverty line (City of Alexandria 2015) or $11,700 for a single member household in 2015 (U.S. Department of Health and Human Services 2015). By household type and size, Alexandria has a higher poverty rate than its neighbor, Washington, DC, largely due to Alexandria's smaller household size. However, poverty in the city is not evenly distributed, with low-income families lodged in older, multi-family structures scattered throughout the city. While some tracts exhibit generally lower incomes, it is also true that high income neighborhoods may have older housing that is home to low- and very low-income families. This was certainly true of the Berg, which became the site of Chatham Square Apartments, the subject of this case study.

THE PROJECT: AN EXCELLENT LOCATION FOR CHATHAM SQUARE

Chatham Square is located within the historic area of Alexandria known as Old Town. The Berg is a neighborhood that lies within Old Town and was established by slaves who had fled Petersburg (thus the name) at the time of the Civil War. It continued to be a predominantly African American neighborhood well into the 20th century. The historic boundaries of the Berg originally encompassed about 15 city blocks but at the time of Chatham Square's construction in 2004, the Berg had shrunk so that its ties to the black community rested largely in the Samuel Madden Homes, a public housing project of 100

units built in 1945. By then the Berg was no more than two city blocks bounded by Pendleton, North Pitt, Princess and North Royal streets. Though diminished, it continued to occupy a prime location within walking distance of the commercial activity along King Street and only a few blocks from the green space and recreational activities along the river.

Old Town, itself, after undergoing a period of decay in the 1960s and 70s was revitalized, largely through the efforts of residents who sought to restore the historic character of the community and renovate the many 18th and 19th century rowhouses that comprise such an important part of its housing stock. By the 1990s, when the first plans for Chatham Square were discussed, Old Town had outstripped other communities in Alexandria in terms of the income and educational attainment of its residents, as well as the rents charged for its housing units. In other words, it had become highly desirable as a place to live and the change from largely African American to largely white, non-Hispanic neighborhoods was already well established.

Chatham Square built on the site of the Samuel Madden Homes public housing project, is made up of market-rate townhomes and public housing units, situated around a central courtyard of shared green space and play areas. It was completed in 2005 with 100 market-rate home ownership units and 52 public housing rental units. The remaining 48 former residents of Samuel Madden Homes were relocated to other newly renovated projects in Alexandria. At the time it was one of the more unusual mixes of market rate and affordable units in the country because of the wide disparity between the value of the homes for sale and those for rent. The project was recognized for its sensitive design and successful execution in the many building and development awards it received.

Figure 1. Samuel Madden Homes, Downtown Alexandria

Source: Virginia Housing Development

Figure 2. Chatham Square Today

Source: Virginia Housing Development

THE PLAYERS

The Owner/Operator: Alexandria Redevelopment and Housing Authority (ARHA)

ARHA administers and maintains the city's public and assisted housing and oversees the tenant-based voucher program as well as the Moderate Rehabilitation Program (Mod Rehab) and Low Income Housing Tax Credit (LIHTC) Program. ARHA was created by state charter but gets most of its operating and development funds from the federal government. While ARHA does not receive funding from the city of Alexandria, the board of commissioners that governs the housing authority is appointed by the city. Currently there are nine commissioners on the Board including a public housing resident and a member of the Alexandria Landlord-Tenant Relations Board. An Executive Director manages the operations of the authority at the direction of the Board.

ARHA's mission is to "maintain, preserve and provide safe, decent, sanitary and affordable housing for low-income and low-moderate income families, through the reorganization, alteration, reconstruction and/or redevelopment of areas in which unsanitary and unsafe conditions exist." (ARHA History). In light of its mission, ARHA has been restricted from enacting any policies that would reduce the number of affordable and/or assisted housing units in the city. At the same time, it is restricted from relocating more than 50% of tenants already living in assisted housing to off-site locations. The one-for-one replacement policy was ultimately made official as City Council Resolution 830 adopted in 1982. Since that time, no publicly assisted housing has been eliminated, yet neither has the resolution encouraged additional public or assisted housing to be built. All activities including both redevelopment and new construction have been within the numbers that existed since 1972. ARHA continues to oversee 1,150 affordable units. It is responsible for the administration of about 1,722 vouchers and receives about $33.5M annually from the Department of Housing and Urban Development (HUD) for all its programs.

Because so much of the affordable housing stock in the city was built in the 1940s much of it is entering the end of its useful life. Efforts at modernization and redevelopment have included an effort, within its policy limitations, to redistribute affordable units throughout Alexandria and not concentrate so much of it in the Old Town district. Proponents of redistribution argue that the location of so much of the affordable units in highly valued Old Town reflects Alexandria's historic roots and not a well-conceived response to changing needs. In addition, redistributionists say, concentrating low-income families in contiguous projects reduces opportunities for these families to improve both educational and economic attainment. Opponents of redistribution believe that moving low-income families away from their traditional neighborhoods is intended not so much to foster integration but to free up valuable real estate for higher income households. These arguments continued not only during the development of Chatham Square but even after the project was completed and occupied.

The Developer: EYA (formerly Eakin/Youngentab Associates)

EYA is a prominent and frequent participant in Alexandria's development projects. Established in 1992, the firm specializes in urban neighborhoods that are transit-oriented, walkable, and sustainable. Since its founding EYA has been responsible for the development of more than 4,000 homes in more than 30 neighborhoods across the Washington metro area. Its imprint on the Alexandria landscape is perhaps more pronounced than in any other community as it currently has completed or under development at least 18 residential and or mixed-use projects.

EYA prides itself on choosing projects that fulfill its mission of creating "lifestyle friendly residential neighborhoods (EYA)." It specializes in projects that are transit-oriented, build on private-public partnerships, promote mixed-use, mixed-income communities and, often capitalize on in-fill residential designs. EYA submitted its qualifications to ARHA when a Request for Qualifications (RFQ), Phase I was issued in 2001. EYA was among

five developers who submitted applications but was one of only two who were then asked to submit project proposals under RFQ, Phase II. Project proposals had to conform to criteria chosen by various stakeholders in a public process that took over a year. A 198-unit high rise project had previously been rejected by the city for the site. EYA's plan for Chatham Square showed a concern for maintaining open space for the residents; it did not maximize the developable units but opted for a plan that was in keeping with the lower density character of the neighborhood; it wanted to create a community where before there had been a project. The plan EYA presented unanimously won the approval of all six members of the selection committee and it was awarded the development contract in 2002.

The Investor: Fannie Mae

The Federal National Mortgage Association, commonly known as Fannie Mae, was the sole investor in the housing credits that funded the affordable units in Chatham Square. Fannie Mae is a government-sponsored enterprise (GSE) and since 1968 a publicly traded company. It was established in 1938 following the Great Depression in order to bolster the housing sector by increasing the lending of local banks. Fannie did this by securitizing mortgages in the form of mortgage-backed instruments, in the process creating the secondary mortgage market.

In the early 2000s, at the time of the project's development, Fannie Mae was operating under explicit guidelines to meet affordable housing goals. Anti-predatory lending practices which had been stringently enforced prohibited the GSE from engaging in high-risk, high-cost projects to satisfy those goals. As the financing for the affordable units at Chatham Square was being put in place, these rules still applied. In 2004 the rules were dropped and Fannie could once again engage in riskier projects to meet affordable housing goals.

PROJECT DELAYS

Chatham Square is one of the few examples of mixed-finance development where the market rate housing far exceeded the values of the affordable housing. Given the location of the project in the heart of Old Town, ARHA wanted to maximize the development potential of the site but it still had to provide, by law, replacement housing for at least half the residents of Samuel Madden Homes in any new project that emerged. From the start, ARHA knew that it was developing not just one project but at least three: first, there were the 100 market rate townhomes; then, on the same site, there were the 52 public housing rental units; and finally, there were three scattered site projects in other parts of the city that would house the remaining 48 families dislocated by the demolition of Samuel Madden Homes.

While plans were being considered as early as 1989, it took another dozen years before demolition work could actually begin. Opposition by the surrounding community as well as the public housing residents delayed construction until 2002. During that time, the project was fought over in the courts as both the Resident Council representing tenants of Samuel Madden Homes and the Old Town Civic Association filed suit against the housing authority. When a federal HOPE VI grant was awarded to ARHA for the project in 1998, a suit was also brought against HUD, the funding agency. It was only when a faction of the residents lost their case in the Supreme Court for a right of first refusal to develop the project that ARHA's plans for Chatham Square could proceed.

PROJECT FINANCE

After persevering through the court process, and suffering through years of delays, ARHA was determined to strike the best deal it could to make the wait worthwhile. In a complex arrangement, EYA agreed to purchase the land from ARHA at 150% of its assessed value. The cash from the sale was promptly placed in escrow until construction on the project was completed and units sold or leased. ARHA would also receive bonuses upon the sale of

the market rate units if the value increased beyond a certain point. Earlier, ARHA had been awarded a HOPE VI grant of $6.7 million for its proposed mixed-income development at Chatham Square. It now used that award to bolster its application for low income housing tax credits to fund public housing at both Chatham Square and the three other relocation sites collectively known as Braddock Whiting Reynolds (BWR) Apartments. The Virginia State Housing Finance Agency awarded ARHA the credits in 2003. The equity generated by the credits combined with proceeds from the sale of the land was sufficient to fund the entire cost of the public housing without additional capital subsidy from HUD. Fannie Mae stepped in to purchase all the tax credits and because the funds for the entire development had been escrowed until project completion, there was minimal risk to the investor and ARHA was rewarded with a higher rate for its credits. The HOPE VI funds were used to cover administrative costs, tenant relocation costs, resident support services and some construction costs at BWR. The city assisted as well with a $3.5 million loan which helped bridge costs during the development process (ULI 2007). As for the market-rate units, EYA was able to obtain straightforward equity and debt financing from its long time banking partner Wachovia Bank. The relative ease of that financing contrasted sharply with the complexity involved in financing affordable housing.

Chatham Square Project Details

PROJECT DATA	
LAND USE INFORMATION	
Site area (acres):	4.16
Percentage complete:	100
Gross density (units per acre):	34
Number of off-street parking spaces:	272

LAND USE PLAN	
Area (Acres)/ Percentage of Site	
Buildings	2.24/ 54%
Streets/surface parking	1/ 24%
Landscaping/open space	0.92/ 22%*
Total	4.16/ 100%

**Does not include rooftop terraces and decks.*

Source: ULI 2007

Chatham Square Finance Details

DEVELOPMENT COST INFORMATION	
Site Acquisition Cost:	$8,117,219
Site Improvement Costs:	$8,799,485
Excavation/grading:	$1,233,281
Sewer/water/drainage:	$2,554,773
Paving/curbs/sidewalks:	$1,179,014
Landscaping/irrigation:	$162,306
Fees/general conditions:	$3,670,111
Construction Costs:	$28,161,000
Soft Costs:	$10,418,646
Architecture/engineering:	$1,199,444
Project management:	$1,015,520
Marketing:	$770,083

Legal/accounting:	$555,208
Taxes/insurance:	$758,276
Title fees:	$3,933,330
Construction interest and fees:	$3,933,330
Other:	$1,425,034
Total Development Cost:	$55,496,350

DEVELOPMENT SCHEDULE	
Planning started:	July 2002
Construction started:	November 2003
Site purchased:	January 2004
Sales/leasing started:	February 2004
Project completed:	December 2005

Source: ULI 2007

PROJECT DESIGN AND OUTCOME

The design of Chatham Square was more important to the success of the project than is usually the case in public housing developments. Not only did the public housing units have to conform to quality housing standards set forth by HUD but it also had to do so within the total development cost limits that were attached to the grant. This had to be done while satisfying the expectations of market rate homeowners that would be paying luxury townhouse prices yet living alongside lower-income families. The architect, Lessard Group, met the challenge and created a design that seamlessly combined both types of housing and provided the requisite garage parking while reflecting the 18th and 19th century facades of the surrounding neighborhood. Viewing the project from the street there would be no way of distinguishing between the market rate townhouses and the public housing. In fact, false facades make the rental units appear to be townhomes when they are actually grouped together as single units next to actual 3-4 story townhouses.

Demand for affordable housing is so great that in Alexandria, as in many other cities, the waiting time for an affordable unit is estimated to be 3-5 years.

In addition to the design challenges, the requirements of the LIHTC allocation called for a very restricted construction schedule. All public housing units had to be delivered within two years of receiving the funding. The fully integrated design as well as the financing arrangements meant that the market rate units had to be completed along the same schedule. Luckily the delays caused by the controversy of the project and the resulting law suits allowed ARHA to spend more time on project planning and testing of different design models with the community. When the litigation was finally resolved, both EYA and ARHA were ready to begin.

EYA served as the general contractor for the entire project and, in its contract with ARHA, guaranteed a maximum unit cost for the public housing of $217,000 each (ULI 2007). The considerable site development costs were prorated and shared between EYA and ARHA. Given that part of the site was located directly across from the municipal bus depot and given the inherent riskiness of valuing a mixed-income property, EYA set the initial price of the market rate units slightly below those of surrounding properties. But when the first units were completed, the demand was surprising. Interested buyers waited in line to view the townhomes. "The sales office opened on a Saturday, and folks started camping out to buy on Wednesday," said Jack McLaurin, principal architect with Lessard Group (Oliver 2006). The last townhomes sold for a high of $1.4 million in January 2006 while the average cost of a Chatham Square unit was $870,000. Ultimately the value of a Chatham Square unit exceeded the value of surrounding commensurate property on a per square foot basis. With the increase from anticipated value, ARHA received an added bonus of about $3 million based on the original purchase agreement with EYA (ULI 2007).

The 52 public housing units were also in great demand. Many tenants who had previously lived in Samuel Madden Homes wished to return and if they met the income and work requirements for residency they were granted a preferred status. Those who could not be accommodated at Chatham Square could choose one of the three scatter sites. Tenants who held vouchers or lived in other sites were put on another waiting list and as vacancies occurred they would move forward. Demand for affordable housing is so great that in Alexandria, as in many other cities, the waiting time for an affordable unit is estimated to be 3-5 years.

The agreement to retain an ownership interest in the market rate units caused a great deal of suspicion in the community especially regarding the fate of the public housing tenants. There is no doubt that maximizing profits from the redevelopment of Samuel Madden Homes was a key consideration for ARHA, but it also extracted social benefits in the interests of its tenants from EYA. Thus, there was an agreement that EYA would participate in job training programs and hire local residents for the project. The fact that Chatham Square became such an economic success meant that the revenue generated could be used for redevelopment of other public housing projects in the city. More than that the public housing units retained in ARHA's portfolio have increased in value and add equity which can be leveraged to finance additional housing. That ARHA had a stake in the project that was in some ways no different than EYA's meant that both were equal partners in ensuring the project's success. For a developer working with a difficult site, with tight time constraints, and vocal neighbors, that was an invaluable asset. ARHA continues that relationship with EYA as it is today one of the prime developers of real estate projects in Alexandria. The model set forth by Chatham Square is not one that is easy to repeat but the financial rewards have been so great that ARHA has used the mixed income model in several other projects including most recently, Old Town Commons, to modernize its public housing.

HOPE VI

The HOPE VI grant awarded to Chatham Square, though small, was instrumental in how the project took shape and impacted both the public housing tenants and the housing authority. It is therefore worthwhile to examine HOPE VI's achievements as well as failures.

HOPE VI, which stands for Housing Opportunities for People Everywhere, was launched in 1992 in the wake of the National Commission on Severely Distressed Housing's finding that about 6% or 86,000 units of the nation's 1.3 million units of public housing were in critical need of rehabilitation or reconstruction. The program was originally directed to provide for the demolition and rebuilding of the most dilapidated housing and to champion resident empowerment through job training and other supportive services. It was estimated that HOPE VI should be funded at $7.5 billion over a ten-year period. However, through the first half of its life, HOPE VI never received more than an annual appropriation of $625 million. HOPE VI dispensed grants to public housing authorities of up to $50 million per grant with about 5-6 such grants each year. Over the course of about 20 years from the time of HOPE VI's inception to 2012 when its last appropriation amounted to only $28 million, the program reflected a long discourse on how America should address housing its poor.

By 1996, HOPE VI had become a vehicle for urban experimentation. With that year's Notice of Funding Availability (NOFA), applicants for HOPE VI grants were encouraged to use the funding for mixed-finance, mixed-income projects that reflected many of the design standards of New Urbanism. Housing Authorities were also exhorted to leverage the grants through use of tax credits and to partner with private-sector developers and other lending institutions. In 1998, the Quality Housing and Work Responsibility Act (QHWRA) allowed housing authorities more leeway to select tenants based on local preferences. There was a new emphasis on rewarding work and under QHWRA the requirement for PHAs to house 75% of the lowest income families was reduced. These important poli-

cy changes were echoed in the HOPE VI NOFA for that year (Popkin et al. 2004).

That Chatham Square incorporated many of the incentives of HOPE VI into its development is certainly no coincidence. The application submitted by ARHA for its grant in 1998 was almost a verbatim list of the elements that now constituted the government's efforts to "fix" public housing.[1] This is not surprising as any PHA would want to adjust its application to meet the requirements in order to secure funding. More to the point is how the requirements of HOPE VI affected the development it helped fund.

In EYA, ARHA found a partner that embraced many of the principles of New Urbanist design. The project they developed was a low-rise, less dense project rather than the high-rise tower that had once been proposed. With its interior pathways, individual entrances that faced the street, and attractive exterior elements such as variable rooflines, the design embodied many of the concepts of both new urbanism and defensible space. The Chatham Square design has won many architectural and building awards and based on resale values, buyers continue to be attracted to the project. The chief criticism of this aspect of HOPE VI was that in order to achieve the lower densities dictated by New Urbanist design, more units had to be demolished than necessary. Debate about whether or not they should have been rebuilt on site or elsewhere is relevant to projects across the country. During HOPE VI's first ten years, it is estimated that of the 95,000 units funded for demolition, less than half would be replaced as public housing. In addition, a chief criticism of the program is that the time it takes to actually get a HOPE VI project built is far too long. While Chatham Square was built on time with the start of construction to completion taking two years, the HOPE VI grant had actually been

Debate about whether or not they should have been rebuilt on site or elsewhere is relevant to projects across the country.

awarded in 1998 when litigation was on-going and plans were not yet finalized. The approximately seven years between award and project completion is not unusual for a HOPE VI project with some, especially in the early years, taking far longer.

Tax credits which financed Chatham Square, were now being touted by housing experts as the best way to fund the huge backlog of reconstruction that public housing needed. HOPE VI was the lever that would move other sources of capital to invest in affordable housing. In the case of Chatham Square, this seemed to work as ARHA did receive both LIHTC and city funding as well as a single private sector investor in Fannie Mae. Furthermore, the market rate units including the shared amenities were financed with a private bank loan. An argument against HOPE VI is that it has not been able to attract sufficient non-federal funds into the financing mix (LIHTC is considered a tax expenditure and therefore federal). While this was not the case with Chatham Square, this criticism often applies to much larger projects where the capital needed is far greater and the real estate values can't approximate those in Alexandria. A greater issue in the case of Chatham Square is whether or not the HOPE VI award was needed in the first place. In "hot" markets, the private sector is eager to participate with or without the added federal benefit (Popkin et al. 2004). Although the degree of interest in Chatham Square may not have been accurately predicted, there was no doubt at the start of the project that market rate units would be well received in the heart of Old Town. The sale of the land plus the tax credit equity was sufficient to cover all ARHA's costs in the development without the need for ARHA to expend any additional capital resources of its own. The award of the HOPE VI grant may have been useful as a signal to the state finance agency responsible for dispensing LIHTC that Chatham Square had the support of HUD.

The HOPE VI program has strongly favored mixed income development and Chatham Square certainly reflects that. Having tenants of varying income levels

serves multiple purposes: these projects are more likely to be better maintained and have higher level amenities than if all tenants were very low or extremely low income; mixed-income projects deconcentrate poverty and allow socioeconomic integration which might bring benefits to all parties; having higher income tenants can be a safeguard against the risk of fluctuating federal funds for operations and debt financing. In choosing to develop Chatham Square as a mixed income project, ARHA was responding more to market conditions than to the other potential benefits. The value generated by developing market rate homes was simply too much to leave on the table. That the city required at least 50% of demolished units be replaced on site and that HUD favored this kind of development, helped determine the exact mix for the project.

Deconcentrating poverty was an ARHA objective despite the fact that many residents were suspicious of this effort. Chatham Square contrasts sharply with the low-income housing that still exists across the street in both appearance and general upkeep. Crime statistics indicate that there has been an overall benefit to the neighborhood: according to the police, both violent crime rates and nuisance crime rates have declined although some community residents dispute the statistics for nuisance crime (Branch 2011). Since funding for the market rate and public housing units were kept separate and costs for shared infrastructure improvements prorated, there was no added benefit in terms of cross subsidizing project operating costs. Furthermore, research shows that "mixed-income development rarely reduces the per-unit subsidies needed to serve households at a particular income level" (Popkin et al. 2004). However, the greater hope that there would be socioeconomic benefits through increased interactions, especially for affordable housing tenants, has proven elusive. To-

The value generated by developing market rate homes was simply too much to leave on the table.

day, years after the last unit was sold, tensions among tenants at Chatham Square are still the subject of city council discussions and community meetings. The designation of a special liaison to report to the City Manager about issues at Chatham Square indicates the magnitude of the problem.

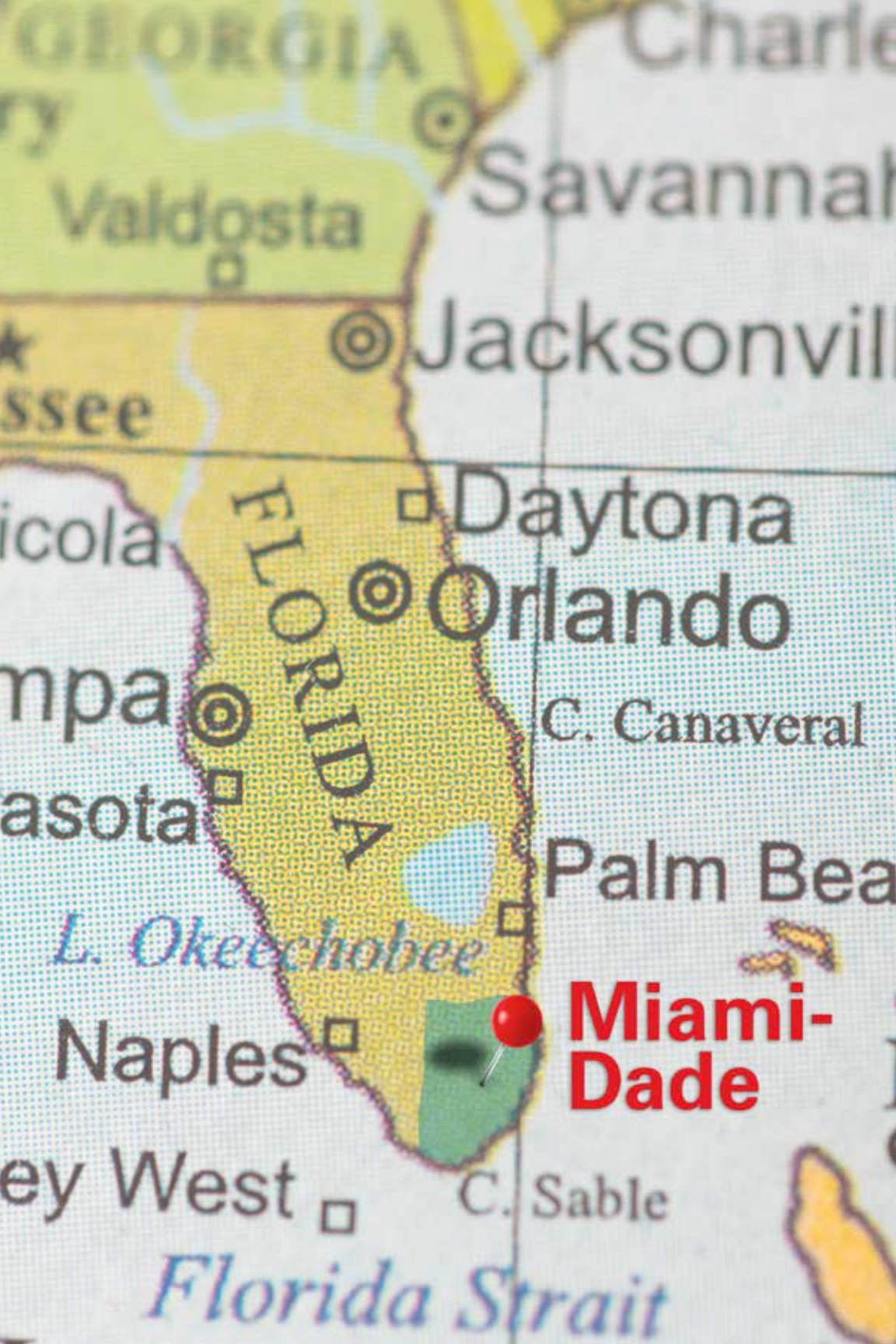
The other major goal of HOPE VI was to improve the lives of public housing tenants through supportive and community services. Chatham Square did require that EYA set up job training programs and employ members of the project in appropriate jobs. The idea was that these tenants would learn a trade by helping to build their own housing. Today some of those trainees are still working for EYA or a subcontractor although because of the lack of tracking, it is hard to quantify the actual benefits. This remains true with other HOPE VI projects because the kind and level of supportive services varies so much from project to project. In addition, the original intent to allocate 20% of HOPE VI funds for supportive services was seldom realized and was reduced each year.

CHOICE NEIGHBORHOODS (CHOICE)

In its last ten years, HOPE VI was seldom funded at its earlier levels and each year saw diminishing allocations. By 2011, it only received $28 million. By then, the conversation about public housing focused not simply on demolition and revitalization of the worst-case housing, but on how entire communities could benefit from some of the lessons learned from HOPE VI.

In response to some of these criticisms of HOPE VI, the Obama Administration funded in 2010, Choice Neighborhoods, a neighborhood revitalization program, with an initial allocation of $90 million. There were several similarities to HOPE VI, including Choice's emphasis on developing mixed-income communities through partnerships with a variety of financial institutions; having a diversity of financing models so that reliance was not on single stream of financing; and, a continued interest in providing relocation and supportive services to those being displaced. Impor-

tantly, Choice expanded the field of applicants who could apply for Choice grants to include not just PHAs but also owners of private and other federally subsidized developments. Improvements not just of the decaying public housing project but of the entire neighborhood were sought. In support of an early mantra that proclaimed poverty was determined by one's zip code (Kaufman 2015), Choice deliberately set out to layer federal funding to targeted neighborhoods. Choice applicants were scored higher if they also had been awarded the Department of Education's Promise Neighborhoods grant or were part of the Department of Justice's juvenile crime prevention program. This is perhaps a natural evolution of what HOPE VI first set out to accomplish, which the Commission on Severely Distressed Housing did not fully recognize: namely the nation's housing problem is too large for one program to address in all its complexity. It will take an expansion of the original vision to test the limits of what is possible.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Miami-Dade Public Housing and Community Development and the Related Urban Development Group

Collins Park, Private-Public Cooperation

INTRODUCTION

As we will see in greater detail later in the case of Skyline Village, Los Angeles, the ability to develop affordable housing is greatly aided by federal incentives that encourage the participation of non-profits in the marketplace. But sometimes, as in the case that follows, private developers are more than willing partners with public agencies for reasons unique to the project or property being developed. Such public-private partnerships are the very kind of relationships that are sought after across all sectors of government. The difficulty is recognizing the opportunities for such partnerships when they arise and then facilitating the processes that will allow the partners to achieve the mutual benefits they all desire.[2]

MIAMI-DADE COUNTY PUBLIC HOUSING AND COMMUNITY DEVELOPMENT (PHCD)

Miami-Dade County in the southern tip of the state of Florida sprawls across vast tracts of urbanized as well as agricultural and undeveloped lands. Within its boundaries are included 34 incorporated cities of which the largest is the city of Miami. The county works in tandem with its incorporated localities to provide a complete array of services. While police and fire protection, zoning and code enforcement

are provided at the local level, other services including affordable housing and housing development are administered by the county. Miami-Dade Public Housing and Community Development (PHCD), a department of Miami-Dade County, serves both the larger county as well as city populations. As of 2013, the population of Miami-Dade was 2.6 million with much of that concentrated within Miami's metro area.

PHCD is the sixth largest public housing agency (PHA) in the nation. It administers federal funds that support almost 10,000 units of public and other assisted housing serving more than 30,000 residents distributed over 100 separate projects. An additional 16,000 residents receive Section 8 vouchers which are payments to private landlords funded by the federal government and administered by PHCD. Other federal grant programs such as the Community Development Block Grants (CDBG), HOME, the Emergency Shelter Grant (ESG) and Neighborhood Stabilization program are also administered by PHCD. In addition to its federal responsibilities, PHCD oversees the Documentary Stamp Surtax Program and State Housing Initiatives Partnership (SHIP), both state funded programs that promote and provide competitive funding for affordable housing development.

Leading PHCD is Michael Liu, former Assistant Secretary of Public and Indian Housing at the Department of Housing and Urban Development (HUD). He was selected as PHCD director in 2014 by County Mayor Carlos A. Gimenez who said upon announcing his choice, "Michael Liu brings a wealth of experience to the position of director with more than 25 years of being actively engaged in transforming communities at the local, state and national levels" (Miami-Dade County 2014b). As director, Mr. Liu leads a workforce of 430 and manages a budget of over $450 million. Under the county governing structure, the director of PHCD reports to the Mayor of Miami-Dade County and the 13-member Board of Commissioners. At the same time, the director must be responsive to both the state and federal entities that provide funding for affordable housing programs in Miami-Dade.

PHCD is engaged in an active redevelopment program intended to modernize and upgrade available units. Based on its most recent 5-Year Plan, PHCD intends to move forward in the next few years with construction activity on over 3,000 units of housing currently in its portfolio.

PHCD's Mission Statement

There is no doubt that the need for affordable housing in the Miami area is great. According to a 2013 University of Florida rental housing study, an increasing number of low-income households are rent burdened, meaning they pay more than 40% of income on rent. At the time of the study there were about 250,000 cost burdened families in the metro area. This number had increased substantially among all lower income families including elderly families over a 10-year period. In Miami-Dade, which accounts for approximately half of all low-income families in the area, the rent burden is even greater with at least 50,000 families paying more than 50% of their income on rent (Affordable Housing for All 2015).

In the face of this pressing need, PHCD identified in its mission statement the objective of serving low and moderate-income families by providing affordable housing in stable neighborhoods with economic opportunities for self-sufficiency. More importantly PHCD's mission statement highlights the importance of "partnerships with private and public entities to optimize resources through innovative programs" (Miami-Dade County 2014a).

With a myriad of programs to administer and millions of dollars of funding to oversee, PHCD relies on an in-house project management team and successful partnerships to implement its development plan and ensure the necessary expertise to complete often complex and difficult projects. Its development partners can be either private for-profit companies or non-profits. Collins Park was developed in a unique arrangement with Related Urban Development Group.

RELATED URBAN DEVELOPMENT GROUP

Related Urban Development Group (RUDG) headed by Jorge Perez, its chairman and chief executive officer, is a private for-profit real estate company with projects throughout Florida. It was founded by Perez in 1979, drawing on his background with public housing development in Miami to focus on affordable housing in South Florida. Since then it has grown to encompass luxury condominiums and workforce housing as well. In the Florida marketplace, RUDG has led in the construction, redevelopment or management of over 10,000 affordable units with the goal "to create affordable housing opportunities in a variety of geographically, economically and socially diverse neighborhoods" (Related Group 2011). Part of its success can be attributed to the years of relationship building it has had with local government, financial institutions and community groups. In the numerous independently awarded development contracts that RUDG has won from Miami-Dade it has shown itself to be a reliable partner that can deliver on its commitments with skill and efficiency.

The Collins Park project was overseen by RUDG's senior vice president Alberto Milo, Jr. who brought to this project and to RUDG's corporate leadership his own extensive experience in affordable housing, and in particular his work providing affordable homeownership opportunities in underserved communities. Milo's familiarity with the county organization and requirements no doubt contributed to the success of the Collins Park partnership.

RUDG is an arm of Related Companies, a private corporation with diverse interests in real estate development and financing and associated service industries. Related Companies has an ownership interest in RUDG and the CEO of RUDG is part of the senior management team at Related Companies. The $30 billion Related Companies was founded by Stephen Ross in 1972 and is headquartered in New York.

COLLINS PARK: THE NEIGHBORHOOD

The Collins Park project is located at 3625 NW 20 Avenue in the community identified as Allapattah. Allapattah is a name derived from the Seminole Indian word meaning alligator, but it is hard to imagine that this densely populated urban neighborhood was ever a marshy habitat for such creatures. The neighborhood is otherwise known as Little Santo Domingo, a more recent nickname that also identifies it as home to a large proportion of Miami's Dominican population. Today, it is a diverse urban community that supports a mix of Caribbean, Central American and Latin American cultures.

Today, it is a diverse urban community that supports a mix of Caribbean, Central American and Latin American cultures.

Roughly 5 square miles and one of Miami's oldest neighborhoods it is predominately working class with a large number of residents who are low-income and eligible for housing assistance. The median household income based on census information was only slightly above $19,000. Recent data shows that the median price of a single-family house in Allapattah was $123,000, the second lowest in the city. Allapattah is bounded by State Road 112 and the Miami River to the north and south, and Interstate 95 and Northwest 27th Avenue on the east and west. The Collins Park project is located near the northern boundary of Allapattah which is also its boundary with the Liberty City community, the neighborhood with the lowest home prices in the city.

Once a vibrant commercial and residential district, small businesses fled with the middle class families they serviced in the 1950s and '60s. Today, the commercial strip along 36th St. is occupied with pawn shops, bodegas, car mechanics and bare-bones restaurants. Along its border with the Civic Center neighborhood to the south, there exists healthy industrial activity

characterized by clothing manufacturers, auto repair, carpentry and upholstery shops. Additionally there are several shipyards and drydocks along the banks of the Miami River towards the southwest. Together with the Produce Market, the largest open-air food distribution center in Miami, these enterprises provide jobs to many of the more than 45,000 residents of the neighborhood.

There is today in Allapattah the potential for neighborhood transformation and gentrification. The Miami Herald noted that it has the fastest increasing home prices in all of Miami. With abundant housing stock, investors are taking another look at the neighborhood and those willing to risk its current high crime rates are starting to buy up single family homes and convert them into duplexes or renovate them for rent (Nehamas 2015).

Into this changing environment, the Collins Park project represents a positive step toward continuing the transformation that is occurring while also considering the residents that live there and call it home.

THE PROJECT

When Collins Park was officially opened in January 2015, it was proclaimed by Miami-Dade County Mayor Carlos Gimenez as a "model to address aging public housing throughout the country." County Commissioner Audrey Edmonson declared that the project "demonstrates what we can accomplish when the public and private sector work together to address our pressing housing needs in our community." PHCD Director, Michael Liu, hailed it as an example of a "one-of-a-kind public approach to private partnerships that will greatly improve the quality of the living conditions for our public housing communities" (Miami-Dade County 2015).

Collins Park was built on land originally assembled by RUDG from various individual property owners. Like much of the surrounding neighborhood, these parcels were once occupied by small industrial businesses, auto repair and tire shops. Collins Park was not initially conceived as public housing; that came later as ideas for the development of two other projects were being discussed and the construction of Collins

Park was underway. RUDG had recently won contracts from PHCD to redevelop two public housing developments; Three Round Towers, about six blocks from Collins Park Apartments, and Harry Cain Towers, located in downtown Miami close to another ongoing RUDG project. Both were developments for the elderly. As plans to redevelop Harry Cain Towers progressed, PHCD and RUDG agreed upon the idea of using Collins Park as a building for relocation of the Harry Cain Towers residents. Harry Cain Towers would then be redeveloped as a mixed-income project that would include market rate units to increase revenues to PHCD for use in maintaining Harry Cain Towers. However, Harry Cain residents voted to keep the project in its all-public housing configuration by only a slim margin. At this point, the attention turned to Three Round Towers and the possibility that Three Round Tower residents might be given the option of moving to Collins Park.

Three Round Towers had been completed in 1974 and was spread over almost 7 acres. It comprised 391 units in three 14-story structures which were in need of repair and modernization. In fact, the entire site was to be reimagined with a medical facility and additional mixed uses and housing to maximize the vacant land that was part of the project and to bring existing units up to standard. As part of the first phase of the project, it was now RUDG's intention to complete the Collins Park Apartments so that tenants from Three Round Tower C, who wished to do so, could be moved permanently into the new Collins Park units so that their current substandard apartments could be redeveloped. This would permit construction to proceed at the Towers and relocation of existing elderly tenants to occur with minimum disruption. The arrangement would benefit RUDG for two reasons: they would eliminate the need to market the property and residents would not need to be temporarily relocated off-site during construction of the Towers.

Collins Park as built consists of 124 new 1-bedroom units for the elderly in a modernistic, 7-story elevator building.

Figure 3. Collins Park Today

Source: Miami-Dade County

The project was praised for including the latest environmentally sensitive amenities such as porcelain flooring, hurricane impact windows and doors, and energy efficient appliances. It included high-end features generally found in market rate buildings and common space to unite tenants typically living alone. When you walk into the Collins Park Apartments you will find a computer center, a library, a fitness center and a community room. Additionally, each unit boasts stylish finishes that include wood cabinets and granite countertops. It is not, however, the design of Collins Park that sets it apart from other affordable rental projects. Instead, the manner in which this project came together is what makes it unique.

Collins Park Apartments, LLC, (the owner) is the entity created by RUDG to own and develop the project. It was charged with obtaining all the necessary financing to build the project, to develop the

site plan and undertake construction, and to relocate tenants. The owner, once the project was completed, would donate the land to PHCD so that it would have an ownership interest in the project and thus be eligible for federal operating subsidy under the public housing program. A private entity related to the developer, TRG Management (TRG), would be responsible for maintaining and operating the project in accordance with all applicable public housing and state housing finance requirements. In turn, PHCD would execute a ground lease back to Collins Park Apartments, LLC. PHCD would also turn over all federal funds it received for the operation of Collins Park Apartments to TRG less a fee for oversight and administrative costs. The regulatory and operating agreement would be in effect for an anticipated period of 75 years. The county thus gained 124 new units of elderly housing and the developer was able to manage a larger project with relative ease while adding to his development portfolio. The project was completed as a private development, thus it did not come at a cost for the county to build, yet it eliminated the need for procurement processes that would have added time and complexity to the project.

The Collins Park Apartments project exemplifies all that the county hoped to gain through a public-private approach to development. However, the details of the project are challenging to replicate; thus it will be interesting to see whether or not future projects can be developed in a similar fashion. An essential prerequisite for successful public-private partnerships is the establishment of mutual trust between the public and private entities. Trust grows and is strengthened when the developer and the government agency have worked together in the past and are comfortable with each other's organization and staff. Each partner must have a commitment to the mission which in this case was the provision of affordable housing. Importantly, the project must contain specific winning elements for each partner. Collins Park was a success first because it was located close to another project which RUDG was in the process of developing. Second, because

the timing was right, it was available to be developed when it would serve the developer's purpose and would not exceed the maximum public housing units allowed to PHCD by law. Finally, each partner brought to the table important financial aspects of the deal, a key aspect of private-public partnerships.

PROJECT FINANCING

In 2012 RUDG was awarded 9% Low Income Housing Tax Credits (LIHTC) by the Florida Housing Finance Corporation for the Collins Park Apartments project. The developer through Boston Financial Collins Park, LLC was the equity investor in the credits raising $26.3M in permanent financing. This was based on a cost, at the time, of $1.044 per credit over the 10-year allocation period. In addition, Low-Income Housing Development (LIHD) proceeds provided up to $1.8M of Miami-Dade county funding. The cost to the developer of purchasing the land on which the project sits was $4.03M. As noted earlier, the property was donated to the county as a HUD requirement in order to obtain federal funding for its operations. The donation was executed as a warranty deed approved by the County Board of Commissioners which in turn ground leased it back to the owner, Collins Park Apartments, LLC, for a leasehold fee of $1 per year for a period of 75 years. As a bridge construction loan, $21.5M was obtained. An affiliate of the developer, Fortune Construction Company, was the general contractor. Both the developer and the contractor took fees out of the project amounting to $5.14 million of the total costs of the project. All predevelopment costs of about $500,000 for the project were borne by the developer.

Given the private development aspect of the project, financing the Collins Park Apartments was relatively straight forward. While the fees charged by the project were higher than typically seen in mixed finance projects, at 13.75% rather than the standard 9-12%, the unique arrangement between the developer and the local government entity, which resulted in an additional 124 new units to PHCD's public housing inventory, more than made up for

the slightly higher fees. More important was the savings in time. From the award of the LIHTC allocation in December 2012 to the completion of construction in October 2014, the entire project took slightly more than 22 months. This compares favorably to the completion record for other federally funded development projects which typically take six years or longer.

Collins Park Financing

Construction Financing			
Source	Type	Amount ($mm)	Structure
Boston Financial	Equity	3,996,051	
CitiBank	Construction loan	21, 500,000	1st mortgage
GP Capital	Deferred developer's fees	2,657,437	
Permanent Financing			
Source	Type	Amount ($mm)	Structure
LIHTC	Equity	26,328,488	
Miami-Dade LIHD	Loan	1,825,000	
Total Development Cost		28,153,488	

Much of this effort was concentrated on ensuring compliance with federally mandated regulations regarding the admissions of low-income tenants and the establishment of management practices...

Perhaps the most complicated aspect of this project was the donation of the property to the county and the effort to ensure a stable funding source for operations and maintenance. Numerous approvals and sign-offs by state and county officials, PHCD officials, and officials from various offices of the Department of Housing and Urban Development (HUD) were required. Much of this effort was concentrated on ensuring compliance with federally mandated regulations regarding the admissions of low-income tenants and the establishment of management practices in keeping with public housing operations guidelines. It was with these requirements that the experience and the willingness of all parties to work together became most evident. Staff from PHCD, RUDG, HUD and FHFC had to coordinate numerous contracts and agreements to make the deal work.

LOW INCOME HOUSING DEVELOPMENT PROCEEDS AND THE STATE DOCUMENTARY SURTAX PROGRAM

The only direct public contribution in Collins Park Apartments was the Low-Income Housing Development proceeds. Other funding that is generally used for development projects, although not used at Collins Park, is the State Documentary Surtax Program. This program, established by the Florida state legislature in 1984, allowed certain counties to levy a tax on real property transactions within their jurisdictions. Money collected from approved transactions is used to address affordable housing needs and funding is targeted for programs that assist very low to moderate income families.[3] In Miami-Dade,

the Surtax Program funds interest-assisted mortgages for eligible families to buy their first home. It provides housing counseling services and low-cost construction financing for non-profit and for-profit developers of affordable housing. The program has been credited for helping to produce over 15,000 units of affordable housing in Miami-Dade since its inception. In 2013, the program generated $27 M to fund affordable housing programs.

State surtaxes on real estate transactions are not new and have been employed in various jurisdictions around the country. Currently, 37 states and the District of Columbia employ documentary transfer taxes to fund various programs, not just affordable housing. How they are levied and how the funds are used distinguish one program from another. Though many localities use them, they are not always well received as they are an obvious form of additional taxation and can have a regressive impact on the economy. Therefore, some localities, Miami-Dade being one, provide exemptions from the tax for transfers of single family real property. At the same time, the county's representatives have argued vigorously for an extension of the tax as it provides direct funding for their affordable housing projects while also providing local flexibility over how those funds can be used. Despite deeply divided arguments about the benefits of a documentary surtax, the Miami-Dade Surtax Program continues to be a big part of PHCD's responsibilities.

OPERATING AND CAPITAL SUBSIDY

In this public-private partnership, RUDG, through its various affiliates, provided the development expertise and the financing. PHCD, once the transfer of ownership to the county was accomplished, then stepped in to provide the operating and capital subsidy for the life of the project. Because of the relocation of public housing tenants from Three Round Towers, it had been reasonable to convert Collins Park Apartments to public housing to provide the level of subsidy necessary. TRG Management, a developer entity, provided property management with oversight from PHCD.

Other factors that can influence costs at individual PHAs included the extent of recent modernization efforts, the amount of elderly housing compared to family housing, the age of the existing housing stock...

Funding of public housing is based on a formula calculated annually and then distributed to each of the nation's 3200 public housing authorities as a grant. The money appropriated each year by Congress is stipulated in law under Section 9 of the US Housing Act of 1937. PHAs receive both capital funds and operating funds under separate formulas. The operating fund covers day-to-day operations and normal maintenance activities while the capital fund covers major repairs and long-term upkeep. The funding is intended to cover the difference between rents collected from tenants (no more than 30% of tenant income in most cases) and the actual costs of maintaining and operating public housing in "decent, safe, and sanitary" (Housing Act of 1937) conditions. Since both funds are subject to annual budget appropriations by Congress, the monies provided can be less than requested by either the PHAs or the administration. In those cases, the formula amounts for each PHA are then prorated against the total allocated. The shortfall in the operating budget leads to greater pressure on the capital budget even though for many PHAs these funding pots are distinct and accounts for each are kept separate. The 2010 Capital Needs Report estimated an existing need of $21 billion to bring all PHAs up to a decent and economically sustainable condition. In order to maintain that condition, an accrual need, assuming all existing needs are met, of $3.4 billion would be necessary each year (Finkel 2010).

The report sampled over 1 million units to obtain cost data. It concluded that accrual needs at the

lower end of the spectrum were about $2,400 per unit per year, ranging upwards to about $3,200 per unit per year. On the other hand, existing needs were conditioned by project size, location and kind of development. For very large housing authorities such as PHCD, the existing needs were greatest, averaging $28,553 per unit. Other factors that can influence costs at individual PHAs included the extent of recent modernization efforts, the amount of elderly housing compared to family housing, the age of the existing housing stock relative to the age of their systems and the type of housing. Thus developments located in the Western United States, with newer housing that had not yet been modernized but with relatively older housing systems; with a greater percentage of townhouse/row house developments that are more costly to operate; and with fewer modernization grants awarded in this region, have an average existing need of $39,221 per unit. At the lower end of the scale, housing in the Midwest has an average existing need of only $9,500 per unit based in part on its higher share of elderly housing that is less costly to operate.

PHCD estimated an annual subsidy need of $402,442 when the project opened. This represents the amount needed to operate Collins Park Apartments after income from rent is deducted. Income from rent was initially calculated at an average of $175 per unit per month for an annual rental income of $260,400. Increases were built into the revenue and expense calculations for inflation as well as other fees. The project operates under a Management Plan that conforms to all operating procedures applicable to public housing units in the county. Because it is a mixed finance project, which includes tax credit funding, it has additional rent regulations to meet; specifically, 10% of its units can only be rented to residents with income below 28% of area median income. This was not a difficult condition to meet as many elderly tenants on fixed incomes easily met that requirement.

CONCLUSION

Public-private partnerships can work as they encompass a wide range of models. However, the model presented by Collins Park Apartments would be difficult to replicate as it demands very specific players and project characteristics, as well as location and timing. The plan for relocating Harry Cain Towers' residents failed due to the objections of the tenants. If Three Round Towers had not been available, the partnership might never have occurred. However, once the idea to partner is accepted with obvious benefits and good faith on all sides, then it is possible that no administrative hurdles in and of themselves, can jeopardize the agreement.

The unique aspect of Collins Park is the donation of property to the county. Often, affordable housing programs have relied on subsidy in the form of reduced land costs to the developer. While this is ultimately what happened, the extra step of the transfer in ownership to the county makes this case unusual. The more common partnership that exists today between the federal government and affordable housing developers is the one that funds affordable housing development with low income housing tax credits. This is a partnership that has gained in importance over the last decades and will continue to play an important role in the affordable housing market.

COLLINS PARK

Boise
Salt Lake
Reno
Carson City
NEVADA
UTA
Fresno
CALIFORNIA
Las Vegas
ARIZON
Barbara
s Angeles
San Diego
Ensenada

Thomas Safran and Associates

Skyline Village: Using Low Income Housing Tax Credits and Tax Exempt Bonds

INTRODUCTION

In this case study, we examine the use of Low Income Housing Tax Credits (LIHTC) in the financing of an apartment project for the elderly. LIHTC has become the key to whether or not new affordable housing gets built. As the case studies in this paper explore, almost all affordable projects today use some form of LIHTC often combined with other forms of financing.

BACKGROUND

Thomas Safran and Associates (TSA), led by its energetic founder and chairman Thomas Safran, is a well-known presence in the affordable housing markets of southern California. Since its founding in the late 1970s, TSA has developed and managed over 6,000 units of housing in the Los Angeles region. With the exception of 31 market rate units, all are affordable rental units for seniors and families. A TSA project is marked by its regard for architectural design, its sensitivity to site and locational considerations, and, perhaps above all, its meticulous attention to tenant management and day-to-day operating details.

When Safran began his career in the development of affordable housing more than 40 years ago, he took advantage of new financing instruments and housing programs that the federal government was then beginning to promote. After decades of build-

ing housing through mortgage rate or other interest reduction programs aimed at developers and home buyers, as well as setting massive affordable housing goals for its own agencies, the federal government began to explore alternative ways of meeting the demand for more low-cost housing (Miles et al. 2015, 105). In that era, the Section 8 program which gave vouchers to income-qualified tenants to subsidize housing found in the private market, was born. Incentives began to explore ways that tenants themselves could be involved in their housing choices rather than merely creating more fixed place, federally subsidized and government controlled housing. It was in that time that disturbing stories about the alienating effects of the forbidding and institutional-looking high-rise blocks the government had been building began to surface. Critics of this kind of federal architecture cited the Robert Taylor Homes in Chicago and, most famously, Pruitt-Igoe in St. Louis.

As the federal government explored new ways of meeting the demand for housing through the introduction of the Section 8 program, it also began to discuss incentivizing the supply-side of the market in much broader ways than had previously been done. This discussion eventually led to the creation of the LIHTC program which was introduced as part of the Tax Reform Act of 1986.

In this fervent and challenging time, individuals like Safran decided they could enter the housing development field with a more humanistic approach to housing for low-income tenants. Non-profit and limited-profit developers, such as TSA, were able to maneuver in the development arena with financing tools that made it possible to build affordable housing, rent out projects and then reinvest in the next project. Safran had been informed by the five years he spent working at the Department of Housing and Urban Development before he moved to southern California and began his first project. He managed to obtain development rights to a property with only $1,000 and a partnership deal with the owner. Since that first project, he has continued to develop high-qual-

ity and well-designed projects throughout Los Angeles and the surrounding communities.

TSA: THE FIRM

Today, TSA is a thriving limited-profit development company with more than 50 projects under management. With a growing team of development finance and management professionals including his co-presidents, Andrew Gross and Jordan Pynes, Safran continues to develop a variety of affordable, market rate and mixed-use rental housing (residential plus retail). A TSA project is often characterized by its moderate size, generally between 75-125 units, and its thoughtful design. Safran contends that the attention to "superior design helps him attract high quality low-income residents as well as 'sell' affordable housing, especially family developments, to communities that would not otherwise accept them" (Miles et al. 2007, 372). Good design should not be limited only to luxury developments for high-income residents. Good design can be built into affordable housing when care and consideration go into the development. That affordable housing need not be unattractive is a major tenet of TSA's development philosophy. As a result, TSA has won numerous awards for design, including the 1978 Exceptional Design Award from the Inglewood Planning Commission for his first project, the 1980 Honor Award for Project Design from HUD for Ponderosa Village and the 1993 National Award of Merit in Project Design for the Strathern Park Apartments. In addition TSA has been inducted into the 2016 California Housing Hall of Fame by the California Housing Consortium.

TSA is as concerned with the on-going management of a project once it has been completed as it is with the front-end details of acquisition, finance, design and construction.

> Safran's group puts great stock in good management. Resident managers are hired during project construction so that they will develop a commitment to a given project. As a result, they go the extra step

> in selecting good residents. And good residents are critical to a project's success (Miles et al. 2007, 372).

Tenants, who are often chosen from a long waiting list of applicants, must also be committed to the rules established to live in a TSA project. These include strict limits on the number of occupants in a unit, rules forbidding any kind of drug use, cooperation for units to be inspected regularly and cooperation with annual income re-certifications to ensure tenants continue to meet eligibility requirements. Because of the attention to tenant selection and occupancy issues, TSA projects are able to operate and maintain their properties at a high level while meeting projected revenues. As a result, TSA projects have a low delinquency collection rate–less than half of 1%–and an equally low vacancy rate.

With a development philosophy that focuses on the physical and design details at the beginning of the process and the management and occupancy issues at project completion, the actual financing of the project may seem to be only a means to an end. However, it goes without saying that without the hard work of putting the financial pieces of a project together, there often would be no project and no affordable units for low-income families or the elderly.

SKYLINE VILLAGE

"Probably the hardest thing about this type of development is coordinating the endless varieties of approvals and financing. It can be numbing to put a deal together because of the inconsistencies from one group to the other." Thomas Safran (Miles et al. 2007, 373)

Safran believes this statement applies to all of his affordable projects, but was particularly applicable to Skyline Village, a 73-unit affordable housing complex built within sight of downtown Los Angeles. It is what made this project more challenging but ultimately more satisfying when the pieces did come together according to Andrew Gross, President of Development at Thomas Safran and Associates. This project

was first discussed with the city of Los Angeles in 2000 and was brought into service in 2004. Despite the short timeline, the financing deal was complex and ultimately involved more than 7 different agencies and 6 separate deeds of trust.

Skyline Village is located at 444 Lucas Ave, Los Angeles in a part of the city now identified as Center City West. It lies between the parallel arteries of W. 3rd Street to the north and W. 6th Street to the south. Two blocks to the east is the Hollywood Freeway, a major thoroughfare that traverses the city in a north-south diagonal. Surrounding the site are a major hospital center, two elementary schools, low-rise apartment complexes, and numerous commercial and retail enterprises. Importantly, the high rise office towers of downtown Los Angeles are just on the other side of the Hollywood Freeway. Bus routes exist along 3rd Street and also Wilshire Boulevard to the south, taking passengers to the Westside or to Downtown.

Figure 4. Skyline Village Courtyard

Source: Thomas Safran and Associates

Figure 5. Skyline Village Common Area

Source: Thomas Safran and Associates

The project itself, built on 1.67 acres, is arranged in groupings of apartments and townhomes. It is composed of a total of 73 units, in a mix of 1-4 bedroom units ranging from 600 to 1400 sf. The majority are 2 and 3 bedroom units, comprising 80% of the total units and reflecting the family orientation of its residents. Twenty percent of the units are reserved for seniors. All units have either patio or balcony space with views of downtown or the landscaped interior courtyards of the property. A portion of the project is devoted to common space with amenities such as a community room with library and ping pong table, an exercise room with gym equipment, a computer lab with free internet access, two playgrounds, a basketball court and a gas barbecue picnic area. The grounds are extensively landscaped distinguishing the project from the surrounding two story apartment buildings. A central courtyard built over the underground garage takes advantage of the sloping nature of the property and is entirely at grade level. A nondescript and rundown apartment block similar to some still standing in the area had occupied the site prior to its redevelopment as Skyline Village.

While Skyline does not limit its rents based on the Section 8 voucher restrictions, it does conform to affordable housing rents set forth by the tax credit financing rules. Therefore, rents have been set at 35%, 50% and 60% of Area Median Income (AMI). With AMI in Los Angeles currently $60,600, rents, which are generally calculated at 30% of income, range from $568 for one- bedrooms to $909 for 4-bedrooms. Two-bedrooms and 3-bedrooms are about $682 and $795 respectively. Tenants with higher incomes pay slightly more while those at the lower end of AMI pay slightly less. When Skyline Village opened, the project's amenities, its location, and its affordable rents attracted more than 2,600 applicants for the 72 affordable units.

SKYLINE VILLAGE FINANCING

When TSA first conceived the project, it had planned for an allocation of 9% tax credits from the state. At that time in early 2000s, well before the financial crisis, the housing market was getting heated and investment in residential construction projects abounded. The competition for financing at the affordable level through the LIHTC program was particularly competitive and Skyline Village did not win a reservation of LIHTC funds. Instead of abandoning or even shelving the project for a time, TSA felt strongly enough about Skyline Village to adjust its financing expectations. The location of the project and the strong commitment of local officials eased concerns about a more difficult financing arrangement. TSA restructured the deal to use 4% LIHTC which also required the use of tax-exempt bonds. This generated about $5.4 million in tax credit equity rather than the approximately $13.2 million that 9% credits might have generated. Given the disparity in the expected equity between a straight construction loan and the tax-exempt bond approach, TSA needed to scramble to fill in the financing gap. "They pieced together the remaining financing by obtaining five permanent loans, each secured by deeds of trust. The California Housing Finance Agency also provided about $9 million in bond funds for a loan-to-lender deal with Bank of America. The bank then used the funds to provide the project with a construction loan" (Miles et al. 2007, 374).

Skyline Village Financing

Construction Financing			Total $10.966 M
Los Angeles Housing Dept.	Residual Receipts	$ 2.872	
Alliant Capital	Equity Investment		
Bank of America	Construction Loan	$ 9.0	Via CAHFA
City of Industry Funds	Residual Receipts		Loan
AHP – Federal Home Loan Bank of San Francisco	Grant		
TSA and Housing Corporation of America	General Partners/ Equity/Deferred Fees		

Interim Financing			
Century Housing	Bridge Loan	$ .550	

Permanent Financing			Total $17.98 M
Los Angeles Housing Dept.	Residual Receipts	$ 2.872/3.26	Loan
City of Industry Funds	Residual Receipts	$ .600	Loan
AHP - Federal Home Loan Bank of San Francisco	Grant	$ .300	
Multifamily Housing Program (CA Dept of Housing & Comm. Devel.)	Loan	$ 4.00	55 yrs/3%
California Housing Finance Agency	Bonds	$ 3.75	40 yrs/5.35%
Alliant Capital	Equity Investment		
Tax Credit Allocation Committee	Tax Credit Equity (4%)	$ 5.40	

Source: Thomas Safran and Associates

The award of the 4% LIHTC funds, though limited, allowed TSA to move forward to secure the remainder of the necessary construction financing. The LIHTC funding indicated to other potential financing institutions that the California State Housing Finance Agency had reviewed this project and that it met very stringent guidelines for viability and for meeting the state's public purposes. In meeting LIHTC requirements, it further defined the nature of the project for primarily low-income working families.

The property had been purchased for $2.1M in cash with $1M advanced by TSA. There was no owner financing but the purchase price was supplemented by other sources including Century Housing. It was evident to the TSA partners early on that multiple sources would need to be used. As each transaction presented itself, TSA worked through the requirements, adding new transactions to fill the gaps until there was enough financing to complete the project.

The state Department of Housing and Community Development provided a 55-year $4 million soft second loan at 3%. The Los Angeles Housing Department agreed to a 45-year $3.3 million third loan at 5%. Funds from the City of Industry program provided an approximately $600,000 fourth loan, and the Federal Home Loan Bank of San Francisco provided a $300,000 Affordable Housing Program loan through Broadway Federal Bank, which counts as the fifth loan. The formula for the repayment of the soft second, third, fourth and fifth loans is complicated. It is based on a pro rata share of a percentage of total residual receipts, applied first toward accrued interest and then to unpaid principal of each loan.

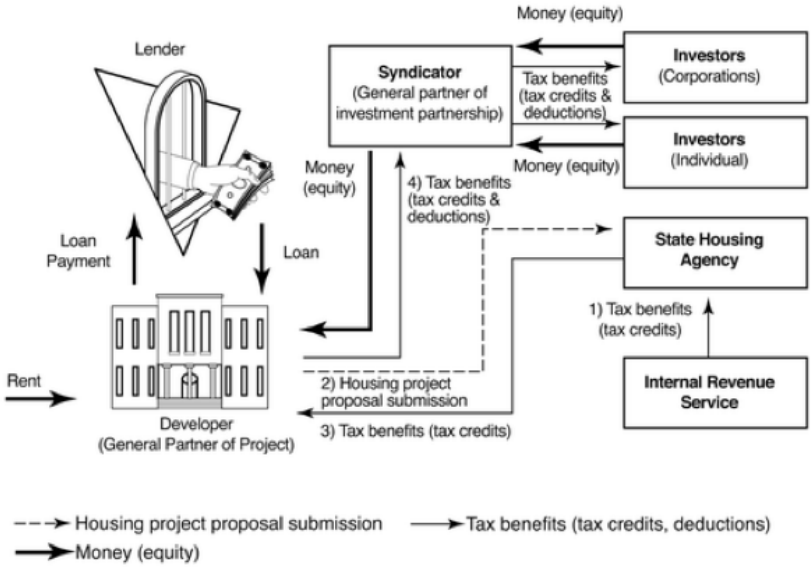
In another move, CalHFA also provided about $9 million in bond funds for a loan-to-lender deal with Bank of America. The bank then used the funds to provide the project with a construction loan. Century Housing provided a $550,000 bridge loan (Kimura 2006).

LOW INCOME HOUSING TAX CREDITS

The LIHTC program, written into law as Section 42 of the US Tax Code as part of the Tax Reform Act of 1986, is today the primary means of funding affordable housing for construction and redevelopment in the country. It does this by providing tax incentives to investors who in exchange for tax credits over a ten year period, provide the equity funding that is used to build and/or rehabilitate affordable housing projects. While LIHTC was never intended to provide all the financing a developer needs, the equity investments reduce the overall debt burden of otherwise risky, below market projects. Today, LIHTC has made possible the acquisition, development and/or modernization of close to 3 million rental homes between 1987 and 2014 (HUD). It wasn't until the early 1990s that LIHTC really took off, yet today it accounts for an average of 1,400 projects and more than 104,000 units annually (HUD).

As a federal program, LIHTC is distributed among all 50 states on a per capita basis. In 2015, each state received $2.30 per capita with a minimum of $2.68 million for small states. These funds are channeled through the state's Housing Finance Agency (HFA) which is charged with administering the program, allocating the funds and ensuring they are spent for the intended purpose. The HFA does that by issuing their state's qualified allocation plan (QAP) which puts forth the state's affordable housing priorities and eligibility requirements. QAPs can also be used to award tax exempt bonds and other state-level tax credit programs. Based on QAP submissions, the HFA awards their LIHTC funds in a highly competitive process. The only federal requirement imposed on the states with regard to LIHTC awards is that at least 10% of these funds have to be reserved for non-profits.

Figure 6. How the LITHC Program Works



Source: Desai et al. 2010

Once awarded a LIHTC allocation, the developer must conform to the rent restrictions for affordability that the program imposes. At the outset, developers decide if their projects will be targeted to tenants at 50% or 60% of AMI. Since rents are pegged to 30% of the target AMI, of course, some developers would prefer to receive higher rents from slightly higher income tenants. However, at 60% of AMI, the project would have to devote 40% of its units to this low income group, while at 50% of AMI, only 20% of all units would be devoted to the very low income group. The trade-offs are up to the developer and ultimately depend on the financials for the project as well as the neighborhood characteristics of the project. Since the guidelines only set minimums there is still leeway for developers to create mixed-income projects or to go beyond the minimums and serve even lower income families or more low income families. At Skyline, 100% of the rentals serve

the compliance period imposed was for a total of 55 years and was deemed appropriate given the need for affordable housing, particularly housing so close to downtown...

low income families including those at the very low (50% AMI) and extremely low (30% of AMI) levels. The more restrictive rents were required by the City of Los Angeles which provided some of the permanent financing.

In addition to meeting income limits, projects that receive LIHTC allocations must also meet requirements for how long units stay affordable. Usually, this is for a minimum of 15 years and an extension of an additional 15 years for a total of 30 years. The second 15-year period can be relinquished and the original developer bought out or the units converted to market rate. In that case tenants are given vouchers to make up the difference between the affordable and the market rate rents. The state therefore likes to deal with developers that they trust to continue operating the project as affordable housing. Because states vary widely in the degree of their need for affordable housing and the type of housing necessary, compliance periods are kept flexible and largely determined by state requirements. At Skyline, the compliance period imposed was for a total of 55 years and was deemed appropriate given the need for affordable housing, particularly housing so close to downtown. The HFA compliance requirements even exceeded those of the City of Los Angeles which typically requires only 45 years. TSA considers its primary role as a developer of affordable housing so did not balk at the more stringent compliance requirements, regarding it as necessary for obtaining the financing that would get the project built.

Since the credits are stretched out over a ten-year period, the responsibility is on the HFA to en-

sure that units remain affordable by monitoring income and rent restrictions. Credits can be recaptured if the developer fails to comply or violates other requirements such as housing code or fair housing mandates. Syndicators who package the credits and sell them to investors therefore have an interest in dealing with only credible and experienced affordable housing developers. TSA was already well established in the Los Angeles housing community when it first proposed the Skyline Village project to city officials. "It's a top quality project from a top-quality developer," said Carl Wise, senior vice president at Alliant which has invested in several Safran developments and was the syndicator for Skyline (Kimura 2006).

There are two types of tax credits: 9% and 4%, formally known as "applicable percentages." Projects can combine these credits during the development process thus magnifying the government support and potential equity. Yields from 9% and 4% tax credits are either 70% or 30%; or, in other words, over the lifetime of the credits the expected value today should equal 70% or 30% of eligible development costs.

Skyline failed to win an allocation of the 9% credits which are much more popular with housing developers and therefore more competitive. The project was not located in a Qualified Census Tract (QCT) which, if it were, might have made it more attractive to the HFA and given it an edge in the competition. Qualified Census Tracts or Difficult to Develop Areas (DDAs) as they are also known, were added to the LIHTC legislation in 1989 to further target the use of credits to lower income neighborhoods. DDAs added a 30% bonus to the usual credits for projects within the tract. This credit "boost" is used to incentivize development in areas with a poverty rate of at least 25% or in areas where at least half the population has an income no greater than 60% of the area median.

Four percent credits are more widely available but are limited by certain conditions. For example, 4% credits can only be used for acquisition of a building for substantial rehab; it can be

used for new construction only in combination with other federal funds; and finally, the provision TSA used, 4% credits can only be used with projects which also employ tax exempt bonds. If a project can qualify for tax exempt bond financing, it automatically is awarded the 4% LIHTC. The bond financing helps fill the gap in the 4% yield but because of the extra step in applying and qualifying for the bonds, 4% tax credits are considered both cumbersome and costly by developers, and unlike the popular 9% credits, had for years been left unused in a state's volume cap allocation. As housing developers have become more familiar with the intricacies of bond financing combined with tax credits, there has been greater use of the 4% LIHTC so that today they have become a staple in the developers' financing tool box.

The amount of tax credit a project receives is based on a calculation known as the "eligible basis." This is the cost of the project, less land acquisition and permanent financing costs. Any federal funds used in the project are also deducted from the eligible basis. The additional 30% credit boost is also calculated on the eligible basis after the 9% credit has been applied. 4% credits cannot be granted a credit boost even if located in a DDA.

Finally, how tax rates are determined affects the amount of equity investment that will be generated. While the terms 9% and 4% imply fixed rates, at the time of the Skyline project they were, in fact, determined on a monthly basis and seldom fell exactly as described. For example in December 2004, when Skyline was placed in service, the tax credit percentage was actually 7.96% for 9% credits and 3.41% for 4% credits. Housing advocates have perennially argued for a fixed rate minimum LIHTC program as a way of providing some certainty to affordable housing subsidies. Such an adjustment was introduced in 2008 during the recession and was made permanent in 2015 for 9% credits only.

While certain provisions of the LIHTC program can vary from state to state and some aspects of the program can be adjusted to respond to market conditions or to

meet national policy needs, the attraction of LIHTC to the development community is that they are a tax expenditure and not subject to budget appropriations each year. As a tax expenditure, the Treasury Department exerts primary control over how changes are made in a formalized manner and seldom varies from year to year. In 2016, the total cost of LIHTC is $7.9 billion. This compares to the $6.5 billion for Public Housing Operating and Capital Funds (supply side) and $21.1 billion for the Housing Choice Voucher program (demand side).

There is no doubt that LIHTC in both its forms, has become the primary means of financing affordable housing in this country. Both advocates and developers favor the tax credit approach as it provides financing for all the major components of project development, construction and rehabilitation. By incentivizing outside investors it brings together a savvy pool of expertise through syndicators, investment bankers, and tax attorneys who act as a filter for project viability and continued affordability. Most importantly, tax credits leverage limited public resources for a public benefit which by some estimates would require another 20-40% of local contribution.

TAX-EXEMPT BONDS

As discussed above, tax-exempt bonds are the first step in gaining an automatic award for 4% tax credits. Even so, such bonds are subject to a state's volume cap which means that affordable housing projects must compete with all other private activity projects that serve a public interest and that the state wishes to fund. (Per Sec. 142(d) of the Tax Code). These can include other kinds of

Both advocates and developers favor the tax credit approach as it provides financing for all the major components of project development, construction and rehabilitation.

housing projects, student loans and industrial development as well as other privately developed enterprises. Given the tax benefits of such bonds, interest rates paid for the bonds are also lower allowing for a higher loan amount. The California Housing Finance Agency awarded TSA bond funds worth $3.75 million for Skyline Village. Together with the tax credits of $5.40 million, the total of approximately $9 million was the cornerstone on which the rest of the financing package for Skyline was built. TSA entered into a partnership with the California Housing Finance Agency as the issuer of these bonds and Alliant Capital as the equity investor.

Unlike 9% tax credits, the 4% credits are allied to the tax-exempt bonds by what is called the 50% test. Where tax credits do not allow funding of land costs, tax-exempt bonds do. The 50% test is applied to the "aggregate basis" of a project's cost which includes land and depreciable costs. This rule requires that at least 50% of the project costs be financed with bonds otherwise there is the potential that anything more than 50% of the project's costs would not be considered for the non-competitive credits. That could mean a forfeiture of some part of the maximum potential allocation. In addition, very specific rules govern how much funding must be used for a project once bonds are awarded.

Where tax credits do not allow funding of land costs, tax-exempt bonds do.

These rules for tax-exempt bond financing under the tax code are complicated and the number of participants necessary to complete a 4% deal are numerous, making the cumulative fees for these deals high. It is estimated that affordable housing developers can pay 5-6% of project costs in administrative fees for bond financing (Novogradac 1999). But as in the case of Skyline Village, it can often be the only source for low-interest loans and equity financing of affordable rental housing. Higher costs do demand even more layers of financing and makes even more important a strong and attractive project.

Skyline met the criteria and was able to piece together multiple financing programs to get the project built.

Since 1998, the use of bond finance together with LIHTC has steadily increased. This has been due to the increasing sophistication of both non-profit and public agencies that apply for and distribute these funds. As familiarity with use of bond financing coupled with tax credits has spread, more affordable housing developers are willing to use this tool. Public agencies are also finding that this approach can leverage a greater share of public dollars, especially in localities where there are limited capital resources and a highly competitive 9% tax credit market. Use of bonds and 4% credits frees up more availability for 9% credits and does not affect the cap on tax credits imposed by the federal government, another attractive feature of bond plus LIHTC funding.

VERMONT
NEW HAMPSHIRE
MASSACHUSETTS
CONNECTICUT
RHODE ISLAND
Auburn
Bridgton
Sebago
Portland
Biddeford
Sanford
Laconia
Rochester
Dover
Concord
Manchester
Portsmouth
Hampton
Lawrence
Gloucester
Salem
Boston
Baia del Massachusetts
Baia di Capo Cod
Plymouth
Barnstable
Nantucket Sound
Martha's Vineyard
Nantucket
Lowell
Nashua
Worcester
Milford
Woonsocket
Providence
Fall River
New Bedford
Newport
Rhode Island Sound
Block Island
Montauk
East Hampton
Southampton
Long Island
New London
Greenport
Stratton
Brattleboro
North Adams
Athol
Pittsfield
Holyoke
Southbridge
Enfield
Hartford
Warwick
Meriden
Norwich
Newport
Claremont
Springfield
Manchester
Lebanon
Conway
White Mountains
Mount Washington

Pond View Village, Gloucester, MA:

Mixed-Income Development on an Historic Site– Failure and Success in the Same Project

INTRODUCTION

This case study takes another look at a mixed-income development but one where the market conditions were not as fortunate as those at Chatham Square, Alexandria. We also consider the impact of outside forces in the development of affordable housing and how federal and local grants can be used to target affordable housing development even in the worst of times.

BACKGROUND

The Pond View project sits on a 20-acre site located at 147 Essex Avenue in the city of Gloucester, Massachusetts (Shotwell 2006, 35). The property includes a 7-acre pond, hence its name, and was the site of a manufacturing plant that produced glue from 1876 until 1951 when the factory moved elsewhere. The land and its buildings remained under the ownership of the LePage Co. and continued to be used for its operations until 2001, when it became available for sale. At about the same time, the City of Gloucester had identified a critical need for affordable housing within its limits especially for working people with moderate incomes. A non-profit organization, Wellspring House, Inc., composed of Gloucester citizens, some of whom also sat on the Mayor's Task Force on Housing, was encouraged to come up with ideas that could promote more affordable housing in the area. Wellspring, whose experience was primarily with housing for the homeless, decided to create a non-profit dedicated

to the construction of affordable housing for Gloucester workers. Its executive director was to be Nancy Schwoyer, a housing advocate and founder of Wellspring House. Its first project would be the purchase of the former glue factory and the development of a mixed income, mixed use community. Thus, Cape Ann Housing Opportunity (CAHO) was born with many members from Wellspring serving on its volunteer board. It immediately set about raising money to purchase the old LePage Co. glue factory for the future Pond View Village site. Within a year, in August 2002, CAHO had raised sufficient funds to accomplish the first step of its goal. However, a condition of the purchase had been to limit the time allowed to perform its due diligence of the site, a factor that later led to difficulties.

Figure 7. Le Page Co. 1887

Source: MAPC

Figure 8. Pond View Today

Source: The Caleb Group

POND VIEW VILLAGE, PHASE I AND II

Due to its roots in social service development and community organizing, CAHO spent a good part of the following year gathering input and meeting with the community to come up with a plan that would satisfy both community needs and the concerns of surrounding neighbors. CAHO, founded on a commitment to affordable housing and environmentally responsible development, was particularly interested in a project that would respect Gloucester's past and reflect the tightly knit small village that it had once been. The village concept was transferred to Pond View with plans that called for a series of buildings to be clustered together with most of the rest of the property devoted to open space. Pond View would offer housing plans to satisfy a range of incomes with homeownership units at both the affordable and market rate levels but it would also have affordable rental units for families that were not yet able to buy or did not wish to own. In all there would be 118 units, 75 for sale and 43 for rental. The project would serve not just the residents but it would also have a large community center with a kitchen and room for a public gallery and other communal events. To conform to CAHO's commitment to sustainable development, the project would be built with improved window glazing, a central heating and air conditioning system, Energy Star compliant appliances, and a higher rated building insulation (Shotwell 2006, 39). More cutting-edge techniques, such as thermal heat or solar energy, proved infeasible and were not cost effective for a project of this size. The vision for Pond View also inspired CAHO to obtain a rezoning of the property from "Industrial" to "Village Business District (VBD)." The new zoning allowed it greater design flexibilities but it also allowed for home businesses that would minimize the need for long commutes or inject more traffic onto local streets. The new zoning also harkened back to a more crafts-oriented era and was in keeping with the bucolic ideal that Pond View represented to its non-profit developer.

Of the 11 buildings originally on the site, 7 were retained and rehabilitated for residential use. Three others were demolished and new structures were built in their place while one other building was razed to allow more room for open space. The units varied in size from one to three bedroom configurations. They also varied in style ranging from single level apartment units to multi-level duplexes. The separate structures are knit together by a walkway which connects buildings to each other and to the shared facilities. Phase I consisted of the 43 affordable rental units. Phase II was the mix of affordable and market rate homeownership units. While Phase III was originally slated for condos, it was ultimately developed as affordable rentals.

Pond View Project Mix

	Rentals*	Condos	1 bdrm	2 bdrm	3 bdrm	PBV**
Phase I	43		10	19	6	8
Phase II		41				
--Market rate		--26				
--Affordable		--15				

**All rentals are affordable*

***Project Based units use federally subsidized tenant vouchers*

PHASE I AND II FINANCING

Working with its financial advisor, VIVA Consulting, CAHO devised a business plan for financing the project in pieces. The phasing of the project was a deliberate strategy to secure funding that would allow CAHO to complete all three segments of the project without the need to obtain financing for the entire project at once. Phase I consisted en-

tirely of rental units because tax credit equity was only available for affordable rental units. Also there were more funding sources for affordable units than for market rate units and successfully completing the first phase would make the second phase more attractive to traditional lenders. The business plan relied on revenue from the rental units to help finance and complete the second phase. In turn the sale of the market rate units would finance the third phase of affordable ownership units which would not be eligible for LIHTC.

Equity from LIHTC was put together by a nonprofit investment syndicator, the Massachusetts Housing Investment Corporation (MHIC). Since Pond View was part of a designated Difficult to Develop Area, it also benefited from the additional credit boost. Still tax credit funding met slightly less than half of the projected development costs. The remainder was pieced together from multiple sources. Chief among these was the Massachusetts Housing Partnership (MHP) which provided an additional $2.8M. Of that, $2.4M was a direct loan and the remaining $450,000 was provided through another arm of MHP, Home Funders (MHP). The low interest loan from Home Funders in combination with other sources of low-interest loans, served to write down the long-term interest rate on its permanent debt. The total amount of debt provided by mission oriented funders such as Housing Stabilization Funds and the MA Affordable Housing Trust amounted to $3.86 million in funding. In addition to grants that helped fund site development costs, the total development cost of Phase I was $12,952,897.

Pond View Sources of Funding – Phase I Rental

Tax Credit Equity	**$6, 121,975**
Facilities Consolidation Funds and Philanthropy	$721,922
MHP/Bank of America	$2,425,000
Home Funders	$450,000
Subordinate Debt (Federal Home Loan Bank, City of Gloucester, North Shore Housing Consortium, CDBG + HOME, Department of Housing and Community Development)	$3,234,000
Total Development Costs	**$12,952,897**

Source: Shotwell 2006

Phase II financing for the ownership units, in comparison, was less complex as it relied primarily on ownership equity. Some of this would have included rental revenue as well as presale of the units but a large part came from a consortium of bank loans put together by MHIC. The remainder of the funding came primarily from mission oriented debt that included Community Development Block Grant funds, the MA Housing Trust Fund and DHCD Housing Stabilization Funds.

Pond View Sources of Funding – Phase I Ownership

Developer's Cash Equity (MHIC)	$9,653,365
Grants	$59,315
Mass Development	$216,344
Energy grants and rebates	$38,375
Subordinate Debt (Affordable Housing Trust, City of Gloucester CDBG, DHCD Housing Stabilization Funds)	$2,175,000
Total Development Cost	**$12,142,399**

Source: Shotwell 2006

MASSACHUSETTS HOUSING PARTNERSHIP (MHP)

As we see above, MHP stepped in to provide a sizeable share of the development financing for the rental units. State and local players are a crucial element of funding for affordable housing but many communities do not have the resources to devote to this. Even if it is identified as a critical need it often falls below other pressing priorities including education and infrastructure. This is especially true for smaller communities such as Gloucester whose share of federally distributed formula grants, such as Community Development Block Grants, are often not enough to provide the funding needed. It is worth looking at how the state of Massachusetts addressed this problem. MHP was established in 1985 as a public non-profit that works closely with the Governor and the Department of Housing and Community Development (the state housing finance agency) to identify and assist in affordable housing development. Its mandate is to work with cities and towns across the state to increase housing production and to explore new ways of doing so. In 1990, Massachusetts became the first and only state to pass an interstate banking act aimed at benefiting housing. The act requires companies that acquire

Massachusetts banks to make funds available to MHP. With access to credit, MHP created a bank funded loan pool for affordable housing uses. Between 1990 and 2014, MHP has extended more than $1 billion in loans and is responsible for the development of more than 22,000 units of housing. A separate arm of MHP is Home Funders which was established in 2003. Home Funders' loan pool is established solely from local philanthropies and in its first year of operation it raised about $19 million. Home Funders is often used to supplement the more significant loans extended by MHP.

PROJECT DEVELOPMENT: PROBLEMS AND PITFALLS

CAHO, as evidenced by its founding, was well connected to city officials and other leaders in Gloucester and the surrounding communities. It easily obtained the permit it needed to proceed with development of up to 118 units of housing and by the end of 2003 it was ready to break ground. Unfortunately, CAHO's original general contractor resigned from the project in early 2004 citing the rising materials costs that would make it difficult for him to realize any profit from the deal. It took CAHO almost a full year to find another general contractor, Cutler Associates, and construction successfully began in April 2005. Construction proceeded rapidly and Phase I and Phase II were completed in 2006. While the affordable rental units were fully occupied soon after completion, the condos suffered from poor timing and a mistaken pricing strategy. The pitfalls of the project's early slow pace of development, its agreement to shortcut the due diligence process and its prolonged consultative process, aided in the unfortunate timing. By the summer of 2006, the condo market had begun to drag. "It was about the perfectly wrong time to go to market" said Bob Gilles, one of CAHO's board members (Anderson 2008). As construction continued, the first condos were being put on the market. In the course of two months more than 400 potential buyers viewed the for-sale units. Not a single market rate unit sold and CAHO finally decided to take

them off the market in the spring for repricing.

Nevertheless, problems only seemed to accelerate. While Phase II units were being shown, work had continued to prepare the site for Phase III, the 34 affordable rate condos. CAHO sought and was granted a height amendment for its Phase III building which involved removing another building and replacing it. As a result, the 276 neighbors bordering Pond View filed suit. Despite more than a year of open meetings and public previews prior to the start of construction, the neighbors feared that the change in design would obstruct their views. To settle the lawsuit, the owner agreed that Phase III would not begin until a certain number of Phase II condo units had been sold. This litigation delayed the completion of Pond View Village considerably and added additional costs that CAHO could ill afford.

Costs had been rising in unexpected ways throughout the project's construction. Most notably, the site had difficult drainage problems that were expensive to resolve. The sharp grade differences between buildings and access roads added to design and construction costs. Labor and materials costs also rose. CAHO's contractors sued for payment of cost overruns adding to financing problems. At least 8 of the 15 affordable units sold but the project relied on sales from the market rate units to meet their loan obligations and to fund the subsequent Phase III. With needed sales at a standstill, CAHO sought an additional $1.5 million from the state so they could make all the condo units affordable for tenants at 110% of area median income. They were turned down but if the plan had worked CAHO and its investors would have had to write off $1 million.

In any event, CAHO had already defaulted on a payment and was about to be foreclosed upon by its major investment partner, Massachusetts Housing Investment Corporation (MHIC). The condos went back on the market in September 2007 with new prices considerably lower than the original pricing. Still, investors and CAHO under this pricing scheme

had to take a $2 million write off. The first market-rate unit finally sold in November 2007 below the asking price and after that, units would sell slowly and intermittently. Too slowly, as it would take several more years before all the market rate units were sold, and by then CAHO could no longer hold on. It filed for bankruptcy in January 2009. At that time the nation's housing crisis was in full force and CAHO was not alone in facing foreclosure, even though many of CAHO's problems preceded the crisis. MHIC, the major investor, took over Pond View Village and experienced its first major loss in 18 years of lending across the state.

Pricing Pond View Condos

	Affordable 2-bdrm	Market 2-bdrm	Market 1-bdrm
Scheme 1 (2006)	$265,000	$359,000	
Scheme 2 (2007)	$175,000	$225,000	
Scheme 3 (2009)	$154,000	$195,000-235,000	$159,000

Source: Anderson 2008, The Caleb Group

THE HOUSING CRISIS OF 2007-2010

There is an old adage that says location is the most important component of any real estate transaction. But those people are forgetting the importance of timing. CAHO could not have picked a worse time to market its units. While the Phase II units were completed when they could still have been sold with credit available to extend financing, the window was rapidly closing for both those activities to occur. What had fueled the crisis, easy credit and over-confidence in steadily rising home prices, led to a spectacular bubble that burst in 2007-2008. Pond View itself had been prompted by the double digit increase in home values of the early to mid-2000s. By 2006, when Phase II came

on the market, some estimated that housing prices were already at their peak and possibly overvalued by as much as 70% (Williams 2017). When prices plunged and foreclosures became widespread, uncertainty became rampant. With uncertainty, the financial markets dried up and lenders were reluctant to lend even to other financial institutions. By 2008 multiple failures or impending failures of some of the biggest players in the mortgage lending markets led to a housing crisis which was a leading cause of the economic downturn that has come to be known as The Great Recession.

PHASE III: NEW DEVELOPMENT PLANS

Since construction had never been completed on Phase III due to the lawsuit filed by the neighbors and subsequent settlement, the property went through foreclosure proceedings to transfer ownership rights to MHIC. The Community Economic Development Assistance Corporation (CEDAC) had been a secondary lender to CAHO, and reached an agreement with MHIC to purchase the ground lease on Phase III and sell the development rights to an experienced affordable housing developer.

CEDAC is a nonprofit community development finance institution which provides seed capital, bridge financing and predevelopment financing to developers of affordable housing. It also provides technical assistance and consulting services to affordable housing developers. With about $20 million a year in investment funds, CEDAC provides loans to 50 affordable housing developers to generate approximately 2,400 units of housing a year (CEDAC).

The original plan to develop the final phase as affordable home ownership units was abandoned in favor of affordable rental. The enormity of the 2008 housing crash had depressed any hopes of a quick turnaround in the housing market. Condos especially, as Phase II showed, did not appeal to buyers in the area. Also abandoned were remnants of the building that CAHO had intended to redevelop. Instead, new construction would take its place. The five-story structure that would be built would include a ground level garage and four levels of apartments.

THE CALEB GROUP: A NEW DEVELOPER STEPS IN

The Caleb Group was founded in 1992 by Warren and Joan Sawyer and Debra Nutter. After years of experience in developing market rate and senior housing, Warren Sawyer saw a need for high quality, affordable housing in the communities in and around Boston, MA where he both lived and had many of his for-profit projects. The Caleb Group is a non-profit organization and its founders drew from fellow members of their church to serve on its first Board. While today, Caleb no longer identifies as a faith-based organization, the role of these organizations in establishing and leading community development efforts is a critical one.

The Caleb Group was a well-respected and known developer of affordable housing when it was selected to assume management of Pond View Village and completion of Phase III. In addition, Caleb's mission "to provide secure, affordable homes and build stable communities that offer diverse populations the tools and resources to empower individuals to make positive changes in their lives"(The Caleb Group) was in keeping with the original vision for Pond View Village. By the time of its selection Caleb had an extensive portfolio of affordable housing projects to its name in Maine, New Hampshire, Massachusetts and Connecticut. It owned or managed more than 16,000 units throughout New England. What made it an especially good choice to complete Pond View was its affinity

Faith-based organizations are more numerous and diverse than is commonly recognized. Current public conversations about the possible role of faith-based organization in community life often assume that these organizations are local worship communities. In fact, many other types of organizations are faith-based. One useful typology (Castelli and McCarthy 1997) divides faith-based groups into three sets: (1) congregations; (2) national networks, which include national denominations, their social service arms (e.g., Catholic Charities, Lutheran Social Services), and networks of related organizations (such as YMCA and YWCA); and (3) freestanding religious organizations which are incorporated separately from congregations and national networks but have a religious basis. Freestanding organizations can be as simple as an independent nonprofit organization spun off by a congregation to pursue a particular social purpose such as affordable housing (Vidal 2001).

for the tenant development aspects of its projects. Each Caleb property also included a Resident Services coordinator to assist tenants of affordable units with locating the social services they needed. Moreover, with its years of experience in the affordable housing field, Caleb had a trusted and proven group of partners for the project. From its general contractor, Keith Construction, to its legal representative at Nixon, Peabody, Caleb could rely on a professional network that had been developed over time and numerous projects.

Caleb broke ground on the Pond View Village site in July 2010 in a ceremony attended by previous supporters of CAHO. The project was not an easy one for Caleb or any other developer to assume. There were legal issues associated with reviving a failed project and a number of environmental concerns to resolve. However, the project was well supported by the city, which wanted a potential eyesore removed and continued to support efforts to provide more affordable housing in Gloucester.

PHASE III FINANCING

Caleb acquired the leasehold development rights to the property from CEDAC which had purchased the ground lease in a settlement arrangement with MHIC. The lease which was for a period of 99 years worked to the benefit of Caleb as it involved only the building footprint and allowed them to be absolved from the environmental issues on parts of the remaining property. Controlling the new project through leasehold also did not affect their eligibility for LIHTC funding which was critical to the project.

The primary sources of funding were $4.6 million of 9% LIHTC and $5 million of Tax Credit Exchange (TC-X) under the American Recovery and Reinvestment Act of 2009 (ARRA). Additional funding came from HOME administered by DHCD, state funding, deferred developer fees, and MHP permanent debt.

Sources of Funding - Phase III
Rental

Tax Credit Equity	$4,634,260
Deferred Developer Fee	$173,470
Tax Credit Exchange	$5,000,000
HOME (DHCD)	$550,000
Affordable House Trust (Mass Housing)	$765,000
MHP Permanent Loan	$740,000
Total Development Cost	**$11,862,730**

Source: The Caleb Group

The LIHTC award of 9% credits came at a time when the housing crisis was most intense. Private finance had all but dried up and housing construction was at a virtual standstill. As Rob Bernardin, Director of Acquisitions for Caleb recalls, "After months of searching, the highest pricing we could attract for the LIHTC was only 68 cents per dollar of Award…Today's pricing would be closer to 92 cents for each dollar of award" (Bernardin). As a result the need for additional funding was acute.

In response to the housing crisis, HUD received $13.61 billion under the American Recovery and Reinvestment Act of 2009 (ARRA) for programs that would help stimulate the economy. The largest part of that money, about 75%, was distributed among the states and localities through a formula process. The remaining 25% was awarded through competitive grants. Because of the intensity of the housing crisis and the impact to the economy as a whole, funding was allocated to projects which could be quickly implemented and would have immediate positive impacts on populations and communities that were most in need. Thus, more than $4 billion was allocated to "shovel ready" projects; projects which had been stalled due to lack of financing resulting from the crisis. Of that allocation, $2.25 billion was designated for the Tax Credit Assistance Program (TCAP).

TCAP was conceived as a response to the reduced funding from LIHTC. It was aimed specifically at projects that had already met LIHTC qualifications but still fell short of needed financing. Similar to LIHTC, TCAP was distributed to states to administer and distribute according to local criteria. It substantially differed from LIHTC in the basis of its statutory authority. While LIHTC was created within the Tax Code, TCAP was a grant program governed by the federal Home Investment Partnerships Program (HOME) regulations. Instead of receiving funding based on a per capita allocation, Massachusetts would ultimately receive $31 million dollars of TCAP based on its 2008 HOME allocation. In the process it became known as the tax credit exchange program (TCX) throughout the state.

Pond View III met all the criteria for TCX since it had already qualified for LIHTC and met the state's QAP requirements. According to Rob Bernardin, "This community could not have been completed without the timely introduction of the much needed ARRA funds" (Bernardin). The full $5 million grant was provided to Caleb as a 30-year, non-interest bearing loan. In return, Caleb agreed that Pond View III's 34 units would be affordable to tenants whose income is 60% or less of area median income (AMI). Four of the units would be reserved for tenants with income less than 30% of AMI.

Today, Pond View Village is complete and fully rented. Rents established for the newest units range from $348 to $758 for a one-bedroom and $402 to $901 for a two-bedroom, based on the income of the tenant. Caleb manages the entire complex. Despite the many setbacks in getting this project to completion, Pond View has finally met the objectives of its earliest supporters. It is providing a high quality living environment to working households at affordable rents. With its mix of unit types and income qualifications it presents a model for communal living.

Figure 9. Pond Village

Source: The Caleb Group

CONNEC
Poughkeepsie
Middletown
Bridgeport
Stamford
Norwalk
Fairfield
Peekskill
Milford
Ringwood
Greenwich
Hamburg
White Plains
Hopatcong
Yonkers
New Rochelle
Mount Vernon
Paterson
Hicksville
Morristown
Newark
Levittown
Garden City
Bay shore
Long Beach
Elizabeth
NEW YORK
Edison
STATEN I.
Philipsburg
New Brunswick
Long Branch
Princeton
East Windsor
Asbury Park
Trenton
Point Pleasant
Lakewood
Levittown
NEW
JERSEY
Atlantic City
Ocean City

New York City

The Effectiveness of 421-a Midtown West, Manhattan

INTRODUCTION

In this case study, we will track the evolution of New York City's 421-a program through the lens of six apartment buildings developed by private, for-profit developers in a single district, Midtown West. Although the 421-a program was created to spur development, it was modified to become a vehicle for for-profit developers to create affordable housing. While it was undoubtedly successful in incentivizing development, its effectiveness as an affordable housing program is the subject of contentious debate.

A BRIEF HISTORY OF MIDTOWN WEST

Since its colonization by Europeans in the 17th century, New York City has been a destination for immigrants. Millions of immigrants were processed in Manhattan and later through Ellis Island. Many chose to settle in the port city, evolving it into a dense and diverse economic powerhouse.

Midtown West, the area from 34th to 59th Street between Eighth Avenue and the Hudson River, was once New York City's worst slum. In the 19th century, it was an industrial area populated by mostly German and Irish immigrants living in overcrowded tenements and working in factories, lumber yards, and slaughterhouses.

After the Civil War, gangs ruled the streets, with The Hell's Kitchen Gang at the top of the hierarchy. As a result, Midtown West has to this day been referred to as "Hell's Kitchen." The industrial landscape coupled with organized crime made Hell's Kitchen a hotbed for bootleg distilleries and speakeasies during the Prohibition Era.

New York City continued to rise on the global stage, though, and there was a severe housing shortage in the 1920s with vacancy rates falling below 1%. To combat the problem, the City exempted all new housing developments from property tax between 1920 and 1926. Hundreds of thousands of new apartments were built within the decade, raising the vacancy rate to 8%, and the exemption was gradually phased out by 1929. The success of this tax measure is often credited as the precursor to the 421-a tax abatement program.

Midtown West was largely left behind in the development boom, however, because a number of factors worked against the gentrification of the neighborhood. Besides the rampant criminal activity, the development of public transportation infrastructure created a less desirable living environment. The Lincoln Tunnel was built in three phases between 1937 and 1939 to service traffic coming in and out of the City from New Jersey. It became one of the most highly trafficked underground roadways in the world, but it also cut off the area below 39th Street from the rest of the neighborhood. Additionally, the Port Authority Bus Station was opened in 1950 to service an increasing need for public transportation. However, dissenting political opinions resulted in a series of costly renovations that lacked a cohesive vision. And despite the accessibility via car and bus, the subway system did not extend into Midtown West at all.

HISTORY AND ENACTMENT OF 421-A

By the late 1960s, New York City was a metropolis in decline, characterized by soaring crime rates, labor union strikes, racial tensions, civil unrest, corruption, economic stagnation and a fleeing popula-

tion. The City lost nearly a million residents to the suburbs between the late 1960s and late 70s.

Falling from a 1962 peak of 70,686 permits issued for new housing units to only 3,810 in 1975 (Wu 2012, 21), real estate investment and development nearly came to a standstill in New York City. Many had written off the City due to its near bankruptcy.

Using the tax exemption program from the 1920s as a precedent, Mayor John Lindsay sought to combat disinvestment and population decline through changes to New York's tax law. Working with legislators in Albany, Lindsay surmised that a dramatic reduction in property taxes for developers would jump-start residential development in an otherwise speculative investment environment.

On July 1, 1971, Albany enacted Section 421-a of the New York State Real Property Tax Law. This tax reform provided building owners and developers a ten-year exemption from the increase in property tax resulting from the development of new multifamily housing on otherwise underutilized or vacant land in New York City. Over the ten-year exemption period, the exemption decreased 20% every two years with up to a three-year tax-free construction period. The owners were still obligated to pay the prior tax assessment throughout the exemption period.

The legislation proved to be successful in spurring development and creating employment opportunities. And with 90% of new residential development capitalizing on the 421-a exemption (The Municipal Art Society "The History of 421a"), New York State renewed the program in 1977.

421-A'S FIRST REFORM: GEOGRAPHIC EXCLUSION AREAS, AFFORDABLE HOUSING AND CERTIFICATES

As real estate development rebounded, legislators and city officials began to view 421-a as an excessive windfall for developers of luxury condominiums and sought to impose restrictions on the scope of the exemptions. The first reform to 421-a emerged from a landmark court battle be-

tween Donald Trump and Anthony Gliedman, the head of the NYC Department of Housing & Preservation under Ed Koch's mayoral administration in 1981.

Trump sought a ten-year tax break through 421-a for Trump Tower, his 58-story replacement of the Bonwit Teller department store at 725 Fifth Avenue. The City rejected his request for the tax abatement, arguing that as it was generating $30 million in annual revenues, the Bonwit Teller building did not meet the definition of an "underutilized property." Trump sued, and despite lower court's ruling in his favor, the Appellate Division of the Supreme Court sided with the City. Trump appealed to the New York Court of Appeals.

On July 5, 1984, the Court of Appeals concluded that NYC-DHP "impermissibly erected a barrier to the benefit provided by the Legislature" given that "no definition of the key phrase 'underutilized land' is set forth in the statute." Furthermore, the court found that "the Legislature did not choose to restrict availability of this exemption to construction of low- and middle-income housing. Thus, it is immaterial that luxury housing is an issue." In fact, "the New York City Legislative Representative explained, 'Under this bill, the City would not actually lose tax revenues since the owner would continue to pay during the period of the exemption the amount of prior taxes on the property, and future tax yields would be greatly enhanced by the improvements.'" (Trump Equitable Fifth Ave. Co. v. Gliedman, 62 N.Y2d 539) Trump was awarded a ten-year tax break worth $50 million.

Three months after the ruling, the City reformed 421-a to exclude market-rate developments in "Geographic Exclusion Areas" (GEAs) from receiving the tax breaks. The first GEA included 14th through 96th streets in Manhattan along with Greenpoint and Williamsburg in Brooklyn, as the City determined that sufficient market demand in these areas made the incentives unnecessary.

In addition to creating GEAs, the City added an affordable housing component to the 421-a program.

In order to be eligible for the tax exemptions, all new developments within the GEAs were required to include affordable housing either on or off site. Developments outside of the GEAs that included affordable housing would receive an extended 15-25-year tax break.

Sites within the GEA with no on-site affordable units were allowed to take advantage of 421-a with the introduction of a negotiable certificate program. For each affordable housing unit built anywhere in New York City without government subsidy, the developer would receive four to six tradable tax abatement certificates. Each certificate entitled a market rate unit to a10-year tax abatement. These certificates have historically traded on average between $12,000-$15,000 each on the open market.

Table 1 illustrates the phasing of the exemptions based on location and affordable components.

Figure 10. Midtown West

Photo by Derek Hsiang

Table 1. 421-a Exemption Schedule After 1985 Reform

Location	Manhattan between 14-96th, Greenpoint & Williamsburg waterfront (GEA)	Manhattan between 14-96th, Greenpoint & Williamsburg waterfront (GEA)	Rest of Manhattan below 110th	Rest of Manhattan below 110th	Outer Boroughs or Above 110th St	Outer Boroughs or Above 110th St
Affordable Component	Purchase certificates for off-site affordable units.	20% affordable units on-site	As of right for market- rate units	5% affordable for middle income	As of right for market-rate units	As-of-right for Neighborhood Preservation Area
Length of Exemption	10-year exemption	20-year exemption	10-year exemption	20-year exemption	15-year exemption	25-year exemption
Year	Amount of Exemption					
Construction 1	100%	100%	100%	100%	100%	100%
Construction 2	100%	100%	100%	100%	100%	100%
Construction 3	100%	100%	100%	100%	100%	100%
1	100%	100%	100%	100%	100%	100%
2	100%	100%	100%	100%	100%	100%
3	80%	100%	80%	100%	100%	100%
4	80%	100%	80%	100%	100%	100%
5	60%	100%	60%	100%	100%	100%
6	60%	100%	60%	100%	100%	100%
7	40%	100%	40%	100%	100%	100%
8	40%	100%	40%	100%	100%	100%
9	20%	100%	20%	100%	100%	100%
10	20%	100%	20%	100%	100%	100%
11	0%	100%	0%	100%	100%	100%
12		100%		100%	80%	100%

13		80%		80%	60%	100%		
14		80%		80%	40%	100%		
15		60%		60%	20%	100%		
16		60%		60%	0%	100%		
17		40%		40%		100%		
18		40%		40%		100%		
19		20%		20%		100%		
20		20%		20%		100%		
21		0%		0%		100%		
22						80%		
23						60%		
24						40%		
25						20%		
26						0%		

FROM LAWLESSNESS TO LUXURY: THE RISE OF HELL'S KITCHEN

Despite a redubbing of Hell's Kitchen to the more genteel name of Clinton (after former Mayor and Governor DeWitt Clinton), the neighborhood still largely missed out on the wave of new 421-a development and gentrification. Organized crime persisted throughout the 1970s, and the lack of subway transportation made it unattractive to developers and residents alike. Furthermore, there was a strong effort by the community to preserve the residential core of the neighborhood. The local council met with the City Planning Commission to create The Special Clinton District in November 1974:

> **The Special Clinton District (CL),** generally between West 41st and West 59th Streets west of Eighth Avenue, was created to preserve and strengthen the residential character of a community bordering Midtown, maintain a broad mix of incomes and ensure that the community is not adversely affected by new development. Special regulations for designated perimeter areas provide appropriate transitions between the lower-scale side streets, and the Special

Hudson Yards District to the south and the Special Midtown District to the east (Special Purpose Districts).

Critical points of the special zoning included a height limit of 66 feet with no more than six stories. Additionally, structurally sound buildings could not be demolished without a special permit approved by the City Planning Commission. Appendix 1 visualizes the effect of this special zoning.

As the saying goes, good things come to those who wait, and Hell's Kitchen finally began a gradual metamorphosis in the 1980s. Organized crime phased out with several key convictions of mob bosses, clearing the way for Broadway's theater culture, with many actors and artists taking residence in the neighborhood. Old speakeasies and bars along Eighth and Ninth Avenues turned into "Restaurant Row," featuring a diverse selection of ethnic cuisines.

Along with the gentrification, the City approved the development of the Jacob Javits Convention Center as part of a larger master plan for the area. Several zoning changes were made on the outskirts of Hell's Kitchen, opening the doors for the largest apartment buildings in New York City to be developed under 421-a program. The first development we'll examine is just above the northern border of Hell's Kitchen.

75 WEST END AVENUE: MANHATTAN WEST

The father and son team of Nathan and Daniel Brodsky had established the Brodsky Organization as masters of moderate-income rentals by 1991. Having just finished the 248-unit, 36-story "Concerto" at 200 W 60th St, they were positioning to develop their largest rental building yet as their encore.

They had acquired a 4-acre property located between 61st and 64th Streets on West End Avenue and planned to construct a 38 story, 1000-unit rental building geared towards the middle market. Unlike Trump, who was

pursuing super-luxury finishes in his multi-building complex a few blocks northwest, Brodsky went for lower finishes and more efficient common spaces to cater to moderate income renters. 75 West End Avenue, dubbed Manhattan West, included a 24-hour attended lobby, complimentary shuttle service to Columbus Circle, a 350-car parking garage, 5,000 sf of community facilities, a 12,500 sf New York Sports Club with swimming pool and 38,000 sf of retail space. The project also provided a 1.25-acre public park between 63rd and 64th Streets. Total project cost was approximately $180 million, of which about a third went towards acquisition.

As part of the 421-a program, rent on all units are stabilized during the abatement period. Landlords may collect an annual surcharge on top of the stabilized rent increases equaling 2.2% of the rent in order to offset the gradual diminution of tax abatements. However, with lower inflation rates projected into the mid-1990s, the forecasted rise in rents created an environment where the 10-year 421-a abatement coupled with the 2.2% surcharge was still not enough to offset rising operating costs for a mid-market rental development with typical 75% LTV financing. "It worked fine when you had the inflation rates of the early 1980s," Mr. Brodsky said. "It doesn't work in a noninflationary environment" (Bagli 2016).

Therefore, the Brodsky Organization pursued a 20-year abatement by building 200 (20%) affordable units on site. After public review, the State Legislature under Governor Mario Cuomo approved the plan, and 75 West End became the first 80/20 development to receive the 20-year tax abatement. The affordable units were made available to renters with household incomes at 50% Area Median Income (AMI), which was $20,000 at the time. The abatement also helped reduce the pricing for the 800 mid-market units, which were targeted towards young professionals with incomes ranging from $40-90,000.

Figure 11. 75 West End Avenue

Source: The Brodsky Organization

75 West End Avenue

Address	75 West End Avenue
Developer	The Brodsky Organization
Year Built	1994
Type	Rental
Total Units	1000
On-site Affordable Units	200
Building area (SF)	978,985
Floors	37
Zoning	C4-7
Exemption Period	20 years
Beginning of Exemption	1996/97
Development Cost	$180 million
Tax Class/2016 Rate	2 (11+ units) – 12.892%
2014/15 Abatement (20%)	-$1,471,738
2014/15 Taxes	$6,593,976
2016 Taxes (Abatement expires)	$9,386,594
2015/16 Average Rent/sf	$54

2016 AVAILABLE MIDDLE INCOME UNITS				
Unit Size	Monthly Rent	Units Available	Household Size	Annual Household Earnings
Studio	$2,024	32	1	$70,732-82,550
1 bedroom	$2,170	15	1	$75,772-82,250
			2	$75,772-94,250
2 bedroom	$2,611	3	2	$90,926-94,250
			3	$90,926-106,080
			4	$90,926-117,780

Appendix 2 illustrates a very rough estimate of the difference in potential cash flows if the project had been done with 421-a versus without 421-a. The calculation is performed using available public data from the perspective of Brodsky back in 1994 (and some from 2016), as this may have been a very similar approach they would have taken in evaluating whether to use 421-a at the time. Keep in mind, there was a lot of uncertainty in the market in the early 1990s, and interest rates were significantly higher.

The calculation is made under the assumption that there are three streams of cash flow that are most affected:

- Taxes: The primary argument from rental developers is that without the tax abatement, many projects are not feasible.
- Rental Revenue: Without 421-a, 100% of the units would be market rate, increasing rental revenue.
- Debt Service: Without 421-a, all units would have the same fixtures and appliances, so development cost would be slightly higher. This in turn affects the construction loan amount.

For simplicity, all other figures (other expenses, other income, vacancy, etc) in the calculation

are assumed to be equal in both scenarios and therefore left out of this comparison.

The net difference comes out to approximately $30-40 million in benefits in 1994 dollars using 421-a (the range is based on sensitivity analysis not shown). On a project with a total budget of $180 million, this is clearly significant and can make a substantial difference in feasibility.

However, note that the option with 421-a generates less cash flow than the 100% market rate scenario after the expiration of the abatement. Even if Brodsky's models showed better cash flows beyond 20 years without 421-a, it would have been very difficult to secure financing since few investors and lenders would rely on such a long-term prediction. The 421-a option was clearly less risky and easier to build.

As we'll see with the next property, 75 West End helped set a precedent for 421-a mega-apartments at the south end of Hell's Kitchen.

LARRY SILVERSTEIN PIONEERS W 42ND STREET DEVELOPMENT

Midtown West is often labeled the final frontier for real estate developers in Manhattan. While the Brodsky Organization would eventually develop rentals on West 42nd Street, it was Larry Silverstein who pioneered luxury residential development on the far west end of the street. The owner of Silverstein Properties is primarily known for his investment in the World Trade Center and other commercial office projects. He is also distinguished for recognizing the value created by plans for Class A office towers just west of Times Square. To complement the commercial development, he envisioned a highly luxurious mega-apartment primed with amenities three blocks west on 42nd Street's Hudson River waterfront.

During the construction of Javits Center in 1984, Mr. Silverstein purchased a block-through lot between 11th and 12th Avenues on 42nd St for $20 million (financed with a $25m loan from Bankers Trust Company). Although he had

luxury residential in mind, the area was still zoned M1-5 (industrial/manufacturing). And so, the waiting game began.

The City had planned for ambitious office, residential and hotel expansions as part of the greater master plan surrounding Javits Center. A small cluster of blocks directly to the north was eventually rezoned to C6-4 (commercial/retail), paving the way for potential mixed-use development. But a recession followed by political debate over the expansion plans prevented anything from materializing. The City intended to purchase Mr. Silverstein's property and develop a hotel, but the plans fell through. Sixteen years after he purchased the property, Mr. Silverstein was able go forward with his own plans. He financed the $225 million development with a mix of his own equity and lenders led by Bank of New York.

Like Brodsky's 75 West End project, Mr. Silverstein opted to participate in the 80/20 program for River Place I. The 40-story rental tower had 921 units, of which 184 were affordable. The unit mix was comprised of mostly studios, one-bedrooms and two-bedrooms. River Place was intended for the luxury market with high-end finishes and a long list of amenities. The building features a 24-hour concierge, complimentary shuttle service along 42nd Street, valet parking at a 200-space garage and (for a monthly fee) access to a 34,000 sf residents-only gym with a 75-foot swimming pool, two tennis courts, and basketball court.

Figure 12. River Place

Photo by Derek Hsiang

Table 3. 1 **River Place**

Address	1 River Place / 650 W 42nd St
Developer	Silverstein Properties
Architect	Costas Kondylis & Partners
Year Built	1999
Type	Rental
Total Units	921
On-site Affordable Units	184
Building area (SF)	887,879
Floors	40
Zoning	C6-4
Exemption Period	20 years
Beginning of Exemption	2002/03
Development Cost	$225 million
Tax Class/2016 Rate	2 (11+ units) – 12.892%
2014/15 Abatement (80%)	-$6,316,336
2014/15 Taxes	$2,172,990
2016 Average Rent/sf	$51

2016 WAITING LIST FOR LOW INCOME UNITS			
Unit Size	Monthly Rent	Household Size	Annual Household Earnings
Studio	$562	1	$18,060-24,080
1 bedroom	$604	1-2	$19,350-27,520
2 bedroom	$733	2-4	$23,220-34,360

MOINIAN GROUP JOINS THE 42ND STREET PARTY

Joseph Moinian, founder and CEO of Moinian Group, built a reputation as one of New York's top real estate developers and investors. Before venturing into Manhattan's West Side, he accumulated a portfolio of 20 million square feet of office and luxury residential buildings in Manhattan, Long Island and New Jersey. He certainly saw the potential in Midtown West, having con-

verted The Biltmore on W 47th Street into luxury apartments in 2003, and completing another luxury rental, The Marc, on W 54th Street in 2004. In 2005, Mr. Moinian purchased a six-story Verizon office building at 563-569 11th Avenue for $120 million—directly across the street from River Place I.

Mr. Moinian shared Mr. Silverstein's vision for West 42nd Street. He even recruited the same architect, Costas Kondylis, to maintain a consistent design on the rapidly transforming block. But instead of an 80/20 rental building, The Atelier was a luxury condo subsidized with 421-a certificates from 96 off-site units, thus only making it eligible for a 10-year exemption period. Like River Place I, The Atelier was loaded with amenities: 24-hour concierge, valet parking, roof deck with an outdoor sports court, gym with swimming pool, children's playroom and common lounges.

Table 4. The Atelier

Address	635 W 42nd St
Developer	Moinian
Architect	Costas Kondylis & Partners
Construction Period	2005-2007
Type	Condo
Total Units	478
Affordable Units	96 off-site units (certificates)
Building area (SF)	434,119
Floors	46
Zoning	C6-4
Exemption Period	10 years
Beginning of Exemption	2008/09
Development Cost	
Tax Class/2016 Rate	2 (11+ units) – 12.892%
2016 Average Price	$1.6 million/unit
2016 Average Price/sf	$1,682

421-A'S SECOND REFORM

As evidenced by River Place I and the Atelier, developers were capable of creating luxury condos and rentals with the help of 421-a benefits. A study by the Independent Budget Office found that of 192,000 apartments units built between 1985-2002, 69,000 (36%) of them received 421-a abatements. However, only 5,500 (8%) of those units were affordable.

Lawmakers took notice that owners of new luxury units under 421-a were paying a disproportionate amount of tax compared to owners of older units. Although 421-a was creating affordable units, lower to middle income families were not actually receiving the bulk of the benefits.

As Section 421-a approached another expiration date, the Bloomberg Administration paired its renewal with a series of changes that went into effect on July 1, 2008:

- The GEA was expanded to include all of Manhattan, portions of the Bronx, more neighborhoods in Brooklyn, portions of Queens and portions of Staten Island. In addition, the GEA became subject to review by Boundary Review Commission every two years.
- Within the GEA, new affordability requirements were introduced. All affordable units were subject to rent stabilization for 35 years. Tenants in occupancy through the end of the period would remain rent stabilized for the duration of their tenancy.
- New requirements based on AMI were also introduced. Within the GEA, 20% onsite affordable units were required to be affordable for tenants at or below 60% AMI. Outside the GEA, affordability was set at 80% AMI.
- Outside the GEA, a cap of $65,000 of assessed value (AV) per unit was placed on the amount eligible for tax exemption.
- Negotiable certificates were eliminated. Existing certificates could still be used to

receive partial benefits, but the last certificate was issued July 1, 2008.

- As-of-right 25-year benefits for developments in Neighborhood Preservation Programs (NPP) or Rehabilitation Mortgage Insurance Corporation (REMIC) areas were eliminated. Instead, these developments now required 20% affordable units on site.
- Buildings receiving 421-a benefits were required to have an affordable unit mix proportional to the market rate units. At least 50% of the affordable units must have 2 or more bedrooms.
- A new requirement was added for certain building employees of projects with 50+ units to be paid the prevailing wage.

Table 5 illustrates the updated exemption schedule based on the reform. In the following development examples, we will examine how the reform affected new developments.

Table 5. 421-a Exemption Schedule after 2008 Reform

Location	All of Manhattan, Portions of Brooklyn, Queens, Bronx, Staten Island (GEA)	All of Manhattan, Portions of Brooklyn, Queens, Bronx, Staten Island (GEA)	Outside GEA	Outside GEA	Outer Boroughs or Above 110th St	Outer Boroughs or Above 110th St
Affordable Component	Purchase certificates for off-site affordable units.	20% affordable units on-site. Rent Stabilization for 35 years.	As of right for market-rate units	5% affordable for middle income	As of right for market-rate units	20% affordable units on-site within a Neighborhood Preservation Area
Length of Exemption	10-year exemption	20-year exemption	10-year exemption	20-year exemption	15-year exemption	25-year exemption

MANHATTAN'S TALLEST RENTAL

As Moinian Group was completing the Atelier, Larry Silverstein was nearly breaking ground on the rest of his parcel on 42nd Street with plans to build River Place II. The World Trade Center investor once again collaborated with architect Costas Kondylis to design twin towers of his own. The towers literally mirrored design elements of the Atelier with a reflective all-glass facade, and it was appropriately named Silver Towers. This was the most ambitious and largest rental development in Manhattan to date, with 1,359 luxury rental units across one million square feet. Each tower is 61 stories and at the time, it was Manhattan's tallest rental building.

Continuing the trend that he started, Mr. Silverstein addressed the far west side's transportation problem by creating a living environment that residents wouldn't have to leave. As he and Mr. Moinian proved with River Place I and the Atelier, large apartment communities could absorb the expense of maintaining an exorbitant list of amenities. Silver Towers features two 24-hour attended lobbies (one for each tower), a circular driveway, parking garage, a complimentary shuttle down 42nd Street, gym, swimming pool, public park and yoga lawn.

As of 2016, Silver Towers commands market rate rents between $2,690 for a studio and up to $8,600 for a 2-bedroom.

Figure 13. Silver Towers

Photo courtesy of Wikimedia.org

Table 6. **Silver Towers**

Address	600 W 42nd St
Developer	Silverstein Properties
Architect	Costas Kondylis
Construction Period	2006-2009
Type	Rental
Total Units	1359
Affordable Units	272
Building area (SF)	1,049,441
Floors	61
Zoning	C6-4
Exemption Period	20 years
Beginning of Exemption	2010/11/12
Development Cost	
Tax Class/2016 Rate	2 (11+ units) – 12.892%
2014/15 Abatement	
2014/15 Taxes	
2016 Average Rent/sf	$82

EXTELL CREATES THE FIRST AND LAST "POOR DOOR"

Back uptown next to 75 West End Ave, Gary Barnett of Extell Development sparked a new debate with his liberal interpretation of the 421-a requirement in his development at 50 Riverside Blvd (also marketed as One Riverside Park). Mr. Barnett was not a stranger to pushing the limits of 421-a, having taken advantage of the negotiable certificate program to help finance One57, a 1,004-foot ultra-luxury condominium tower overlooking Central Park. Units at One57 were the antithesis of affordable housing, breaking price per sf and sales price records in Manhattan (one unit sold for $100.5 million).

At 50 Riverside Blvd, Mr. Barnett opted to use the 80/20 program, creating 216 condo units and 55 rental units in one building. However, he created two very different, segregated products with two separate entrances under one roof. At 50 Riverside Blvd, condo owners have access to 24-hour concierge in a lavishly appointed lobby, a 40,000 sf La Palestra gym with two pools, rock climbing wall, basketball court, squash court, a movie theater, bowling alley and a private garden. At 40 Riverside Drive, tenants enter via an unadorned side door on 62nd Street. In lieu of a doorman is an intercom and buzzer. River views are replaced with views of the garden that they are restricted from accessing. Fixtures and appliances are much lower quality, and living rooms and bedrooms are not adorned with preinstalled lighting.

The announcement of the separate entrance immediately sparked controversy for two reasons. First, as Assemblywoman Linda B. Rosenthal stated, "No landlord should be allowed to tell a child that they are not able to walk through the same doors, or play in the same areas, as their neighbor" (Licea 2016). Second, it was perfectly legal to have the separate entrance. The press labeled the second entrance a "Poor Door" and politicians moved swiftly to ban the practice henceforth in New York City.

Despite the controversy, 50/40 Riverside was a financial success for Extell. The parcel was located in an Inclusionary Housing Bonus zone which awarded an additional FAR (floor area ratio) bonus for building 20% affordable on-site. Although Extell did not use the extra air rights on this project, the company intends to sell them to the eventual developer of the southern parcel. The market rate condos have sold for an average of $2250/sf and $4.6 million per unit.

Table 7. **40 & 50 Riverside Blvd**

Address	40 & 50 Riverside Blvd
Developer	Extell Development Company
Architect	Goldstein, Hill, & West Architects
Construction Period	2012-2015
Type	Condos & Rentals
Market Rate	216 Condos
Affordable Units	55 Rentals
Building area (SF)	541,114
Floors	33
Zoning	R10
Exemption Period	20 years
Beginning of Exemption	2015/16
Tax Class/2016 Rate	2 (11+ units) – 12.892%
2014/15 Abatement	-$695,549 (Rental portion only)
2014/15 Taxes	$1,053,136 (Rental portion only)
2016 Average Price/sf	$2,250

2016 Available Affordable Units				
Unit Size	Monthly Rent	Units Available	House-hold Size	Annual Household Earnings
Studio	$833	10	1	$30,240-35,280
1 bedroom	$895	15	1	$32,400-35,280
			2	$32,400-40,320
2 bedroom	$1,082	30	2	$38,880-40,320
			3	$38.880-45,360
			4	$38,880-50,340

In the face of the negative feedback from the press and City Council pushing for equality in the affordable units, Barnett noted, "If you say that in any project getting an inclusionary bonus zoning, the affordable units would have to take up some of our best views and units, nobody would build them" (Cuozzo 2013).

Moinian Reaches for the Sky
In what appeared to be a game of one-upmanship with Mr. Silverstein, Mr. Moinian (this time working with his son, Mitchell Moinian) also planned a sequel to his development on 42nd Street. He had acquired the adjacent parcel in 2005 (a gas station at the time) with the intention of topping the Atelier in scope. Excavation did not begin until 2008, and the project hit substantial delays after the recession.

Earlier in 2016, Sky became Manhattan's largest apartment building with 1,175 units (including 235 affordable units mixed in with units below the 31st floor) in a single, 71 story tower. Mr. Moinian hypothesized that an unparalleled level of luxury and amenities could yield unparalleled rents for Midtown West. Sky features a lobby adorned in marble and wood paneling with triple-height ceilings (equally accessible to all tenants) with a lifestyle concierge and valet service. The circular car port showcases a sculpture by renowned Japanese artist Yayoi Kusama. Lifetime Fitness occupies three of the lower floors, and includes a 15,000 sf fitness center, two outdoor pools, one indoor lap pool, a basketball court designed by Knicks star Carmelo Anthony, a water club with a hot tub, sauna, a hammam, or Turkish bath and daily fitness classes/training included in membership. Also located on the premises are a children's playroom, billiards lounge, café (offering free breakfast to residents), private resident's park and pet spa.

Market rate apartments are ornamented with higher-end finishes and Miele appliances, while the affordable rate units have lower end finishes. On the upper half of the building, units feature higher ceilings, with the top five floors reserved for Penthouses with ultra-luxury finishes such as solid wood doors and marble flooring. As of the end of 2016, Sky is approximately 50% occupied with average market rate rents at $4,300/month.

Table 8. **Sky**

Address	605 W 42nd St
Developer	Moinian
Architect	Rockwell Group
Year Built	2008-2016
Type	Rental
Total Units	1,175
Affordable Units	235
Building area (SF)	1.2 million
Floors	71
Zoning	C6-4
Exemption Period	Pending
Beginning of Exemption	2015/16
Development Cost	$850 million
Tax Class/2016 Rate	2 (11+ units) – 12.892%
2016 Abatement	Pending
2016 Taxes	$7,967,764
2016 Average Rent/sf	$90+

2016 Available Affordable Units				
Unit Size	Monthly Rent	Units Available	Household Size	Annual Household Earnings
Studio	$868	70	1	$31,132-36,300
1 bedroom	$931	120	1	$33,326-36,300
			2	$33,326-41,460
2 bedroom	$1,124	45	2	$39,978-41,460
			3	$39,978-46,620
			4	$39,978-51,780

The project cost approximately $850 million, and was partially financed with $539 million in 4-year low interest bonds provided by Bank of China. SL Green also provided $50 million in mezzanine debt which included an option (which they exercised after open) to acquire a 20% ownership interest.

As of November 2016, Moinian has filed a suit against the City for starting the 421-a benefits in 2008 (when excavation began). Moinian is seeking to have the benefits begin from when construction began on revised plans in 2014. As shown in Table 1, developers receive a 100% exemption for up to a three-year construction before the exemption period commences. Therefore, the way the City interprets the start date will have significant impact on the project's financials.

AFFORDABLE HOUSING: A LOW-INCOME RENTER'S PERSPECTIVE

As one might expect, there's steep competition for affordable housing units–so much that it's officially called a "housing lottery." For 40/50 Riverside Blvd, 88,000 applications were submitted for the 55 available units. Similarly, Sky attracted 91,000 applicants for 235 units. Given the tremendous number of applicants, the chances of getting an affordable unit are extremely slim, with odds hitting 1000 to 1 in 2016.

For 80/20 developments, the process for applying begins with filling out a form on the NYC Housing Connect website. New buildings post advertisements (following an NYCHC format) listing available units, rents and required household size and income ranges and an application deadline.

Applicants must prove their eligibility by first meeting the household and income criteria. Applicants may apply for as many different buildings as they want, but they may apply to each building only once. If selected, the applicant is interviewed in person anywhere from 2 to 10 months after the application deadline. If approved, they are assigned a unit based on their household size.

Once approved, income levels do not affect the level of rent (although tenants must recertify incomes annually). Instead, the units are subject to rent stabilization.

THE EXPIRATION OF 421-A AND ONGOING DEBATE

Today's New York City real estate environment is markedly different from when 421-a was first passed in 1971. Over the last several decades, many neighborhoods in New York City have gentrified due to declining crime rates and a strong, resilient economy. New York City bounced back from the recession in 2009 to create one of the strongest real estate markets in its history, with luxury condo development leading the way.

Midtown West has made huge strides since the Hell's Kitchen gang ruled the neighborhood. It still has some catching up to do, but is poised to do so in an unprecedented manner with the rezoning of the Hudson Yards District south of 42nd Street. The developments by Silverstein and Moinian on W 42nd Street are a taste of what's to come as almost every major private developer has a stake in the district. Related Companies is anchoring the district with the nation's largest private real estate development project— a 22 million square foot mixed use master plan— and it will surely be one of Manhattan's most desirable neighborhoods upon completion.

With record numbers of luxury condos in the pipeline, a new problem has emerged. Apartments are fetching astronomical prices, widening the divide between income classes and pushing lower income residents further out from Manhattan. In stark contrast to the fleeing population of the 1970s, New York City now faces an affordability problem. To combat this, one of Mayor de Blasio's primary goals under his administration is to create or preserve 200,000 affordable housing units within 10 years (beginning in 2014).

Section 421-a approached expiration in June, 2015, and while it was responsible for 110,000 affordable housing units since its inception, it was also padding the

profits on luxury condo developments and lowering the tax bills for their wealthy foreign or celebrity buyers. Thus, the program has become the center of an intense debate.

The City authorized a record 33,910 permits for 421-a units in the quarter before expiration (see Appendix 3), as Governor Andrew Cuomo attempted to work out a fair proposal between all sides. He issued a temporary extension through January 15, 2016 while the debate raged on.

From the developer perspective, many proponents of 421-a asserted that rental development wasn't possible in certain market conditions without the subsidy. Furthermore, taxes are the largest operating expense for a rental building, and imposing taxes based on the full assessment value from inception would be infeasible in many cases. And finally, many developers claim that the City doesn't actually lose any income if the buildings aren't built in the first place because the base taxes are still billed.

From the City's perspective, 421-a represents one of the largest subsidies, which makes it one of the City's largest "expenses." It's not a true expense in the sense that City funds are being spent, but rather potential tax revenue is foregone when it could be collected and spent directly on government-sponsored housing projects instead.

The issue of a prevailing wage also became a part of the discussion, as it did in the 2008 reform. This time, the Building and Construction Trades Council of New York (BCTCNY) clashed with the Real Estate Board of New York (REBNY). BCTCNY is representing unions seeking higher minimum wages for construction workers in order to allow the renewal of 421a, while REBNY is pushing for the renewal of the program.

The program has officially expired since January 2016 with the debate locked in a stalemate. New construction permits have fallen significantly since its expiration.

CONCLUSIONS

We have seen examples of six different development projects that successfully utilized the 421-a tax abatement to generate a profit. The developers in this case study were all driven by the financials, and as such, they interpreted the law in what they perceived to be the most economically efficient manner to achieve their goals. The Brodksy Organization believed in the moderate-income niche and created a product to cater to it. Next door, Extell believed that segregating the market rate condos from the affordable rentals would yield the best returns. Silverstein Properties and Moinian Group consistently raised the bar on each other in the luxury rental market on 42nd Street, and will continue their rivalry in Hudson Yards.

While all of these developers were wildly creative in achieving profitability, we've also seen that profits do not necessarily align development with the intention of legislation. Lawmakers cannot expect developers to follow the spirit and intention of affordable housing laws if the economics don't work. 421-a certainly succeeded in spurring development when in slow periods, but the affordable housing component was tacked on and modified over time. The program wasn't designed to adapt to market conditions, making it appear unnecessarily generous towards developers in strong markets, and absolutely necessary in weak markets.

For large developments like the ones in this case study, developers meticulously calculate a project's risk and determine if it's an appropriate fit for their risk appetite. With proper market timing, the results can be overwhelmingly in their favor. Or it can also wipe them out. Rental developers are exposed to significant market risk once they commit to a multi-year construction timeline with a long-term payback period, and programs like 421-a offer a much needed cushion in the event of a downturn.

City treasuries on the other hand rely on a much more predictable and stable cash flow through taxation, and when developers take advantage of policies such as 421-a in a strong economy, the public cries foul for handing out

unnecessary subsidies. The concerns are certainly valid, as tax subsidies are one of New York City's largest expenses. Policymakers must seek to find a better middle ground that mitigates both market risk and outsized developer returns.

Appendix 1. Aerial of Midtown West

Note the lower building heights as a result of the Special Clinton Zoning District

Source: Google Earth

Appendix 2. Comparison of profitability on 75 West End Ave With 421-a Vs. Without 421-a

Assumptions		
Total SF	979,985	Actual figure
Retail & Amenity SF	55,500	Actual figure
SF After Loss factor + Vacancy	738,788	Assume 85% rentable SF and 5% vacancy
80% Market Rate SF	591,030	
20% Affordable SF	147,758	
Debt interest rate	7%	Based on interest rates in 1994
Term of Loan	20	For simplicity, we'll assume the loan ends during the abatement period

With 421a	1994	1995	1996	1997	1998	1999
Up front cost	$ (180,000,000)					
Equity (25%)	$ (45,000,000)					
Debt (75%)	$ (135,000,000)					
Debt service		$ (12,559,843)	$ (12,559,843)	$ (12,559,843)	$ (12,559,843)	$ (12,559,843)
Rental/SF (assume stable 3.3% annual increase. 1996 & 2016 figures are actual)			$ 28	$ 29	$ 30	$ 31
Market Rate income			$ 16,548,851	$ 17,139,882	$ 17,705,498	$ 18,289,779
Affordable Income (assume 1/3 of market rate pricing)			$ 1,379,071	$ 1,428,323	$ 1,475,458	$ 1,524,148
Combined Income			$ 17,927,922	$ 18,568,205	$ 19,180,956	$ 19,813,927
421-a abatement %	100%	100%	100%	100%	100%	100%
Market Value (based on actual tax bill data)			$ 78,425,294	$ 81,964,432	$ 85,642,382	$ 89,496,289
Estimated Assessed Value (based on actual tax bill data)			$ 35,291,382	$ 36,879,495	$ 38,539,072	$ 40,273,330
Estimated Taxes (based on 13% tax rate)			$ -	$ -	$ -	$ -

Without 421a	1994	1995	1996	1997	1998	1999
Up front cost (assume additional costs for 100% market rate)	$ (190,000,000)					
Equity (25%)	$ (47,500,000)					
Debt (75%)	$ (142,500,000)					
Debt service		$ (13,257,612)	$ (13,257,612)	$ (13,257,612)	$ (13,257,612)	$ (13,257,612)
Rental/SF (assume stable 3.3% annual increase. 1996 & 2016 figures are actual)			$ 28	$ 29	$ 30	$ 31
Market Rate income			$ 20,686,064	$ 21,424,852	$ 22,131,872	$ 22,862,224
Market Value (based on actual tax bill data)	$ 78,998,030	$ 82,552,941	$ 86,267,823	$ 90,149,875	$ 94,206,620	$ 98,445,918
Estimated Assessed Value (based on actual tax bill data)	$ 35,549,113	$ 37,148,823	$ 38,820,521	$ 40,567,444	$ 42,392,979	$ 44,300,663
Estimated Taxes (based on 13% tax rate)	$ (4,621,385)	$ (4,829,347)	$ (5,046,668)	$ (5,273,768)	$ (5,511,087)	$ (5,759,086)

Net difference in cash flow (with - without)	Net Present Value	1994	1995	1996	1997	1998	1999
Rent	$ (38,125,964)	$ -	$ -	$ (2,758,142)	$ (2,856,647)	$ (2,950,916)	$ (3,048,297)
Taxes	$68,644,865	$ 4,621,385	$ 4,829,347	$ 5,046,668	$ 5,273,768	$ 5,511,087	$ 5,759,086
Debt Service	$7,550,336	$ -	$ 697,769	$ 697,769	$ 697,769	$ 697,769	$ 697,769
Savings from 421-a	**$38,069,237**	**$ 4,621,385**	**$ 5,527,116**	**$ 2,986,295**	**$ 3,114,890**	**$ 3,257,940**	**$ 3,408,559**

With 421a	2000	2001	2002	2003	2004	2005	2006	2007
Up front cost								
Equity (25%)								
Debt (75%)								
Debt service	$ (12,559,843)	$ (12,559,843)	$ (12,559,843)	$ (12,559,843)	$ (12,559,843)	$ (12,559,843)	$ (12,559,843)	$ (12,559,843)
Rental/SF	$ 32	$ 33	$ 34	$ 35	$ 36	$ 38	$ 39	$ 40
Market Rate income	$ 18,893,342	$ 19,516,822	$ 20,160,877	$ 20,826,186	$ 21,513,450	$ 22,223,394	$ 22,956,766	$ 23,714,339
Affordable Income	$ 1,574,445	$ 1,626,402	$ 1,680,073	$ 1,735,516	$ 1,792,788	$ 1,851,950	$ 1,913,064	$ 1,976,195
Combined Income	$ 20,467,787	$ 21,143,224	$ 21,840,950	$ 22,561,702	$ 23,306,238	$ 24,075,344	$ 24,869,830	$ 25,690,534
421-a abatement %	100%	100%	100%	100%	100%	100%	100%	100%
Market Value	$ 93,523,622	$ 97,732,185	$ 102,130,133	$ 106,725,989	$ 111,528,659	$ 116,547,448	$ 121,792,084	$ 127,272,727
Estimated Assessed Value	$ 42,085,630	$ 43,979,483	$ 45,958,560	$ 48,026,695	$ 50,187,896	$ 52,446,352	$ 54,806,438	$ 57,272,727
Estimated Taxes	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -

Without 421a	2000	2001	2002	2003	2004	2005	2006	2007
Up front cost								
Equity (25%)								
Debt (75%)								
Debt service	$ (13,257,612)	$ (13,257,612)	$ (13,257,612)	$ (13,257,612)	$ (13,257,612)	$ (13,257,612)	$ (13,257,612)	$ (13,257,612)
Rental/SF	$ 32	$ 33	$ 34	$ 35	$ 36	$ 38	$ 39	$ 40
Market Rate income	$ 23,616,677	$ 24,396,028	$ 25,201,097	$ 26,032,733	$ 26,891,813	$ 27,779,243	$ 28,695,958	$ 29,642,924
Market Value	$ 102,875,984	$ 107,505,403	$ 112,343,147	$ 117,398,588	$ 122,681,525	$ 128,202,193	$ 133,971,292	$ 140,000,000
Estimated Assessed Value	$ 46,294,193	$ 48,377,432	$ 50,554,416	$ 52,829,365	$ 55,206,686	$ 57,690,987	$ 60,287,081	$ 63,000,000
Estimated Taxes	$ (6,018,245)	$ (6,289,066)	$ (6,572,074)	$ (6,867,817)	$ (7,176,869)	$ (7,499,828)	$ (7,837,321)	$ (8,190,000)

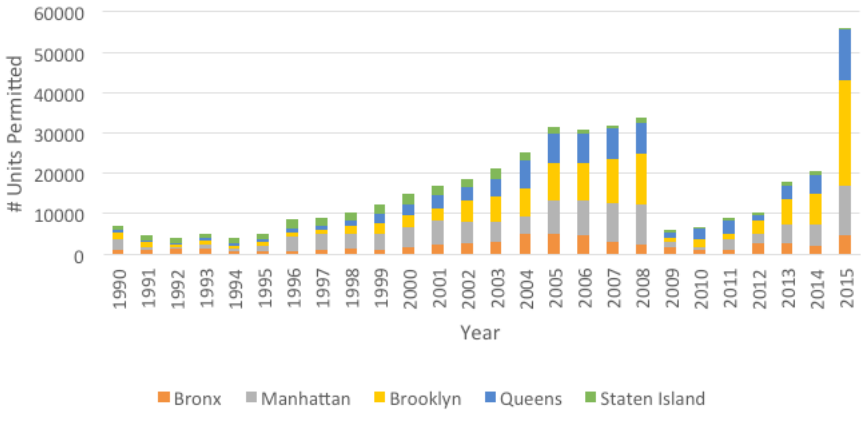
Net difference in cash flow	2000	2001	2002	2003	2004	2005	2006	2007
Rent	$ (3,148,890)	$ (3,252,804)	$ (3,360,146)	$ (3,471,031)	$ (3,585,575)	$ (3,703,899)	$ (3,826,128)	$ (3,952,390)
Taxes	$ 6,018,245	$ 6,289,066	$ 6,572,074	$ 6,867,817	$ 7,176,869	$ 7,499,828	$ 7,837,321	$ 8,190,000
Debt Service	$ 697,769	$ 697,769	$ 697,769	$ 697,769	$ 697,769	$ 697,769	$ 697,769	$ 697,769
Savings from 421-a	**$ 3,567,124**	**$ 3,734,031**	**$ 3,909,697**	**$ 4,094,555**	**$ 4,289,063**	**$ 4,493,698**	**$ 4,708,962**	**$ 4,935,379**

With 421a	2008	2009	2010	2011	2012	2013	2014	2015	2016
Up front cost									
Equity (25%)									
Debt (75%)									
Debt service	$ (12,559,843)	$ (12,559,843)	$ (12,559,843)	$ (12,559,843)	$ (12,559,843)	$ (12,559,843)	$ (12,559,843)		
Rental/SF	$ 41	$ 43	$ 44	$ 46	$ 47	$ 49	$ 50	$ 52	$ 54
Market Rate Income	$ 24,486,913	$ 25,305,311	$ 26,140,388	$ 27,003,019	$ 27,894,118	$ 28,814,624	$ 29,765,507	$ 30,747,769	$ 31,762,445
Affordable Income	$ 2,041,409	$ 2,108,776	$ 2,178,366	$ 2,250,252	$ 2,324,510	$ 2,401,219	$ 2,480,459	$ 2,562,314	$ 2,646,870
Combined Income	$ 26,528,322	$ 27,414,087	$ 28,318,752	$ 29,253,270	$ 30,218,628	$ 31,215,843	$ 32,245,966	$ 33,310,083	$ 34,409,315
421-a abatement %	80%	80%	60%	60%	40%	40%	20%	20%	0%
Market Value	$ 133,000,000	$ 138,985,000	$ 145,239,325	$ 151,775,095	$ 158,604,974	$ 165,742,198	$ 173,200,597	$ 180,994,623	$ 187,000,000
Estimated Assessed Value	$ 50,540,000	$ 52,814,300	$ 55,190,944	$ 57,674,536	$ 60,269,890	$ 62,982,035	$ 65,816,227	$ 68,777,957	$ 71,060,000
Estimated Taxes	$ (1,314,040)	$ (1,373,172)	$ (2,869,929)	$ (2,999,076)	$ (4,701,051)	$ (4,912,599)	$ (6,844,888)	$ (7,152,908)	$ (9,237,800)

Without 421a	2008	2009	2010	2011	2012	2013	2014	2015	2016
Up front cost									
Equity (25%)									
Debt (75%)									
Debt service	$ (13,257,612)	$ (13,257,612)	$ (13,257,612)	$ (13,257,612)	$ (13,257,612)	$ (13,257,612)	$ (13,257,612)		
Rental/SF	$ 41	$ 43	$ 44	$ 46	$ 47	$ 49	$ 50	$ 52	$ 54
Market Rate Income	$ 30,621,141	$ 31,631,639	$ 32,675,483	$ 33,753,774	$ 34,867,648	$ 36,018,280	$ 37,206,884	$ 38,434,711	$ 39,703,056
Market Value	$ 146,300,000	$ 152,883,500	$ 159,763,258	$ 166,952,604	$ 174,465,471	$ 182,316,417	$ 190,520,656	$ 199,094,086	$ 205,700,000
Estimated Assessed Value	$ 55,594,000	$ 58,095,730	$ 60,710,018	$ 63,441,990	$ 66,296,879	$ 69,280,239	$ 72,397,849	$ 75,655,793	$ 78,166,000
Estimated Taxes	$ (7,227,220)	$ (7,552,445)	$ (7,892,305)	$ (8,247,459)	$ (8,618,594)	$ (9,006,431)	$ (9,411,720)	$ (9,835,248)	$ (10,161,580)

Net difference in cash flow	2008	2009	2010	2011	2012	2013	2014	2015	2016
Rent	$ (4,082,819)	$ (4,717,552)	$ (4,356,731)	$ (4,500,503)	$ (4,649,020)	$ (4,802,437)	$ (4,960,918)	$ (5,124,628)	$ (5,293,741)
Taxes	$ 5,913,180	$ 6,179,273	$ 5,022,376	$ 5,248,583	$ 3,917,543	$ 4,093,832	$ 2,566,833	$ 2,682,340	$ 923,780
Debt Service	$ 697,769	$ 697,769	$ 697,769	$ 697,769	$ 697,769	$ 697,769	$ 697,769	$ -	$ -
Savings from 421-a	**$ 2,528,130**	**$ 2,659,490**	**$ 1,363,414**	**$ 1,445,649**	**$ (33,708)**	**$ (10,836)**	**$ (1,696,316)**	**$ (2,442,288)**	**$ (4,369,961)**

Appendix 3: Residential Permits Issued in NYC

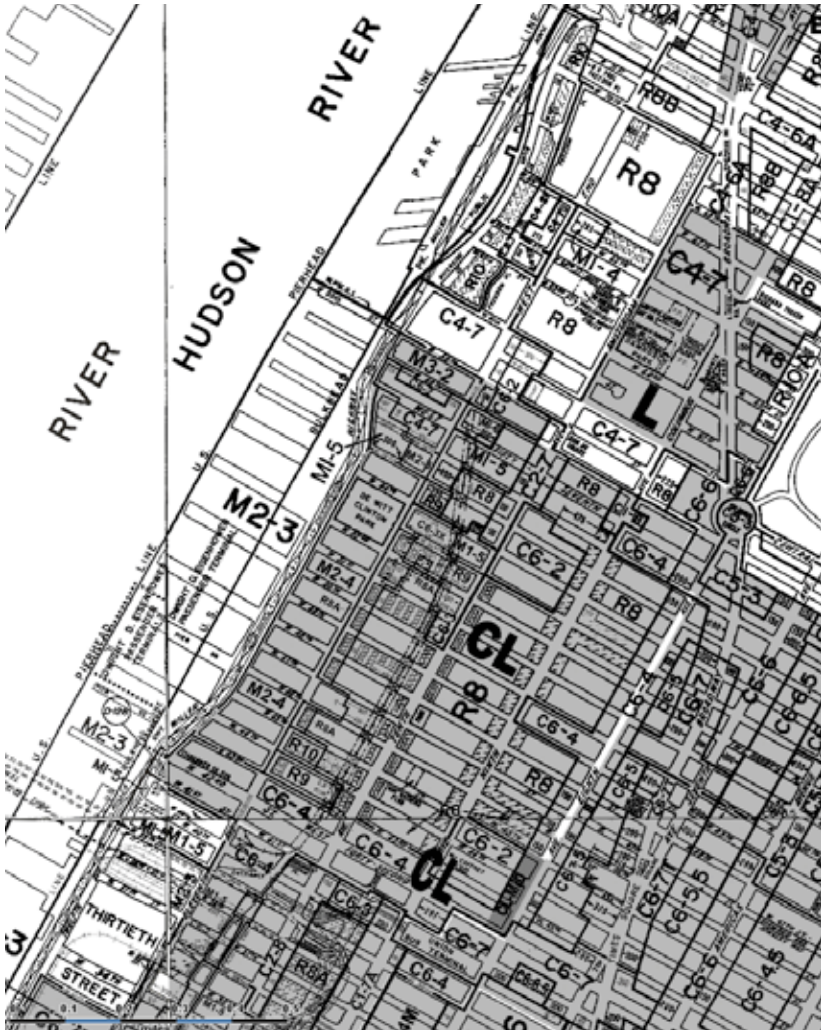


Source: United States Census Bureau

Appendix 4: 421-a Development Map

Source: The Municipal Art Society "421-a: Tax Exemption"

Appendix 5: Zoning Map



Source: NYC Planning "Zoning Maps"

ENDNOTES

1 See Popkin et al. (2004) for a full discussion of policy elements of HOPE VI."

2 It is important to make sure that we distinguish what is meant by "public-private partnerships." In a sense, the public sector engages the non-profit and private sectors in many forms of such partnerships on an on-going basis: when the Treasury grants tax credits to private investors for public priorities; when private companies are funded to provide federal prisons; when religious organizations provide schools. In the case study here, we are defining such partnerships to be primarily a "long-term contract between a private party and a government entity" (World Bank). The case presented is but one along a continuum of possible "partnerships."

3 Very low-income families are those with incomes below 50% of area median income (AMI). Moderate income families have income greater than 80% but less than 140% of AMI.

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ABOUT THE AUTHORS

Bessy Kong has over 35 years of experience in the affordable housing field both domestically and internationally. She was a project manager in the first US Housing Guarantee Program for international development working on projects in Africa and Asia. She has also worked in the private sector as a land use planner with both private and non-profit housing developers in California. From there she went on to successfully develop her own land use consulting firm specializing in medium size non-profit developments. Most recently and for the last 18 years she has worked at the Department of Housing and Urban Development (HUD) in the Office of Public and Indian Housing (PIH). She has served HUD as a Deputy Assistant Secretary for Policy, Planning and Legislative Affairs as well as a senior advisor to the Assistant Secretary of PIH. She has been the HUD representative to the White House, serving as a senior policy analyst on the Domestic Policy Council, Office of Urban Policy. Ms. Kong has also been a Policy Scholar at the Woodrow Wilson International Center for Scholars where she first developed an understanding of South Korean housing programs. Bessy Kong graduated from Smith College with a BA in History and from Columbia University with an MS in Urban Planning.

Derek Hsiang has been working in New York real estate since 2011 as an investor, developer and consultant. He specializes in Real Estate Technology and Data Science, and his clients include Gale International (developer of Songdo IBD in South Korea) and Common Living (a co-living startup). In his spare time he enjoys playing classical music and reading about sociology. Derek obtained his BS in Industrial Engineering from Cornell University and is a Licensed Real Estate Salesperson in New York.

One Woodrow Wilson Plaza
1300 Pennsylvania Avenue, N.W.
Washington, DC 20004-3027

www.wilsoncenter.org/usl
usl@wilsoncenter.org
Facebook.com/urbansustainabilitylab
@Urban_WilsonCtr
202.691.4137

Wilson Center