



U.S. Department of Housing and Urban Development  
Office of Policy Development and Research



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# **Barriers to the Rehabilitation of Affordable Housing**

## **Volume II Case Studies**

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**Barriers to the Rehabilitation of Affordable Housing**  
**Volume II of II**  
**Case Studies**

PREPARED FOR:

U.S. Department of Housing and Urban Development  
Office of Policy Development and Research

AUTHORED BY:

David Listokin  
Barbara Listokin  
Center for Urban Policy Research (CUPR)  
Edward J. Bloustein School of Planning and Public Policy  
Rutgers—The State University of New Jersey

RESEARCH ASSISTANCE PROVIDED BY:

National Trust for Historic Preservation  
Department of Law and Public Policy  
Tamar Osterman  
Bridget Hartman

The Enterprise Foundation  
Planning, Design, and Development  
William Duncan  
Peter Werwath

and

Bradford J. White, Project Management Advisors  
Robert Kuehn, Keen Development Corporation  
Stephen Turgeon, Consultant  
Ioan Voicu, CUPR

MAY 2001

## ACKNOWLEDGMENTS

We would like to acknowledge the critical assistance of the National Rehab Study Housing Resource Group:

Robert Adams, VMH, Inc.  
Randall P. Alexander, The Alexander Company  
DeWayne H. Anderson, Anderson Development Company  
Alfred Arezzo, Hoboken, New Jersey  
William Asdal, Asdal Builders  
James E. Babbitt, Flagstaff, Arizona  
Richard Baron, McCormack Baron & Associates  
Eddie Belk, Belk Architects  
Peter Bell, National Housing & Rehabilitation Association (NHRA)  
Bruce Block, Milwaukee, Wisconsin  
Jim Bonar, Skid Row Housing Trust  
William Brenner, National Institute of Building Sciences (NIBS)  
Thurman Burnette, Rural Development  
Andrew Chaban, Princeton Properties  
William Connolly, New Jersey Department of Community Affairs, Division of Codes and Standards  
Karen A. Danielsen, Director of Housing Policy and Practice, Urban Land Institute (ULI)  
William F. Delvac, Latham & Watkins  
Linda Dishman, LA Conservancy  
Dan Dole, Scottsdale, Arizona  
Carl Dranoff, Dranoff Properties  
David Engel, Office of Policy Development and Research  
Dan Falcone, New Economics for Women  
Mario Fonda-Bonardi, Fonda-Bonardi & Hohman, Architects  
Joan Galleger, Garsten Management Corporation  
Terry Goddard, Law Offices of Terry Goddard  
Tony Goldman, Goldman Properties, Inc.  
Dean Graves, FAIA  
Frank Green, Chattanooga Neighborhood Enterprise (CNE)  
Cissy Gross, Kansas City, Missouri  
George Haecker, Bahr Vermeer & Haecker, Architects  
David Harder, Executive Director, Little Haiti Housing Association (LHHA)  
James Harger, Winn Management  
David Hattis, Building Technology, Inc.  
Curt Heidt, Federal Home Loan Bank  
Michael Hervey, Jackson, Mississippi  
Kitty Higgins, National Trust for Historic Preservation  
Bill Huang, Community Partners (National Trust)  
Lawrence Jacobsen, Mortgage Bankers Association  
Marty Johnson, Isles, Inc.  
Anthony Jones, Clearwater, Florida  
Will Jones, Research Officer, National Association of Housing and Redevelopment Officials (NAHRO)  
Wendall C. Kalsow, McGinley Hart & Associates  
Kevin Kelley, Leon Weiner Associates  
C. Theodore Koebel, Center for Housing Research, Virginia Tech  
Karl K. Komatsu, AIA Komatsu Architecture  
Richard Kuchnicki, International Code Council  
Robert Kuehn, Keen Development Corporation

Michael Lappin, The Community Preservation Corporation (CPC)  
John Leith-Tetrault, Community Partners (National Trust)  
Aaron Lewit, Enterprise Foundation  
Kelley Lindquist, Artspace Projects, Inc.  
Stanley Listokin, Executive Director, Masada Construction  
Stanley Lowe, Executive Director, Pittsburgh Housing Authority  
Weiming Lu, Lowertown Redevelopment Corporation  
Alan Mallach, City of Trenton, New Jersey, Department of Housing and Development  
Christy McAvoy, Historic Resources Group  
Bob McLoughlin and Helen Lopez, Albuquerque Housing Services  
Michael Mills, Ford Farewell Mills & Gatsch Architects  
D. Thomas Mistick, Mistick Construction  
William Mosher, Mile High Development  
Ronald F. Murphy, Stickney Murphy Romine Architects  
Jerry Myers, Pocatello, Idaho  
James Paley, Executive Director, Neighborhood Housing Services of New Haven  
Bryan Park, Northwest Housing Resources (NHR)  
Sharon Park, Heritage Preservation Services, National Park Service  
Brian Patchan, National Association of Home Builders (NAHB)  
Perry Poyner Alley, Poyner Architects  
Jonathan F. P. Rose, Affordable Housing Construction Corp.  
Donovan Rypkema, Washington, D.C.  
Clark Schoettle, Providence Preservation Society Revolving Fund  
Howard B. Slaughter, Jr., Pittsburgh, Pennsylvania  
Kennedy Smith, National Main Street Center (National Trust)  
Robin Snyder, U.S. Environmental Protection Agency  
Gary Stenson, MetroPlains Properties, Inc.  
Kathleen Taylor, Owner, Taylor Construction Services  
Pat Tiller, National Park Service  
Stephen Turgeon, Memphis, Tennessee  
Mike Turner, Professional Remodeler  
George Vallone, West Bank Realty  
Emily Wadhams, Burlington, Vermont  
Ronald Wells, Spokane, Washington  
Kathleen H. Wendler, Southwest Detroit Business Association  
Peter Werwath, The Enterprise Foundation  
Jim Wheaton, Chicago Neighborhood Housing Services (NHS)  
Bradford J. White, Esq., Project Management Advisors, Inc.  
David Wood, Professional Remodeler

We also gratefully acknowledge the patience and critical assistance provided by Edwin Stromberg, GTR at the U.S. Department of Housing and Urban Policy Development, Office of Policy Development and Research. Mr. Stromberg is a consummate professional. Importance assistance was also provided by Tamar Osterman of the National Trust for Historic Preservation; William Duncan and Peter Werwath of the Enterprise Foundation; as well as other consultants to the study (Bradford J. White, Robert Kuehn, Stephen Turgeon, and Ioan Voicu). We also thank numerous unnamed professionals who attended two national review panels held in conjunction with the annual conference of the National Trust for Historic Preservation.

Lastly, we thank those working in the case study organizations for participating in this study. They gave generously of their time and expertise.

Final responsibility for the contents of this report, however, rests with the authors alone.

The contents of this report are the views of the contractor and do not necessarily reflect the views or policies of the Department of Housing and Urban Development of the U.S. Government.

## Foreword

The rehabilitation of the country's aging housing stock is a major resource for meeting the Nation's affordable housing needs. Large numbers of communities recognize this and use HUD, as well as other public and private resources, to address their affordable housing needs. These communities do this because of the demonstrated economic and social benefits of rehabilitation.

Despite the demonstrated benefits of rehabilitation, there is potential for even greater use of the existing stock, not only to address affordable housing needs, but also to promote broader community revitalization goals. However, heretofore there has been a lack of in-depth research on the factors that act as barriers to rehabilitation of affordable housing. Gaining a sound understanding of the issue is difficult because barriers vary from project to project and from community to community.

To address these concerns, HUD entered into a cooperative agreement with the National Trust for Historic Preservation to examine the major barriers to urban rehabilitation. The result of this collaboration is this study, *Barriers to the Rehabilitation of Affordable Housing*, which is intended to fill this information gap and, in doing so, empower decision-makers and housing professionals to begin work to eliminate these barriers.

The project's research team reviewed relevant literature, conducted case studies, and convened study groups of highly-qualified real estate developers, nonprofit leaders, architects and other professionals who face barriers to affordable housing rehabilitation in their "real world" experiences. Volume I provide the context of the study as well as a synthesis of findings and technical analysis. Volume II presents the case studies in detail.

The rehabilitation needs of our cities will continue to grow. The comparative advantages of housing made available through the rehabilitation of existing buildings will enhance the character of our housing stock in the years to come. Through this report and other activities, HUD will continue to encourage rehabilitation as a way to renew our cities and as a way to increase homeownership opportunities for all Americans.



Lawrence L. Thompson  
General Deputy Assistant Secretary for  
Policy Development and Research

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## INTRODUCTION TO THE CASE STUDIES

Our study of the barriers to the rehabilitation of affordable housing relied on multiple sources of information and data. These included the existing literature; the study's resource group, often contacted by telephone; and technical analyses, such as a review the low-income housing tax credit's (LIHTC) qualified allocation plan (QAP) criteria. Our analysis also drew from the research team's considerable rehab experience.

The multiple sources provided an extensive base of information on the barriers to affordable-housing renovation; however, the sources had limits as to the amount and nature of information that could be covered. For example, because of time and other constraints, the telephone discussions with the resource group were not suitable for ascertaining the numerous modifications to, or evolution of, a specific rehab program. In addition, the telephone discussions did not allow for the face-to-face rapport that encourages a rehab developer or lender to give a candid, introspective evaluation of the problems encountered. Accordingly, the study included a series of case studies to assess the experiences of those doing rehab on a day-to-day basis. This volume describes the purpose of the case studies, details the case study organization, and provides, in Chapters 6 through 11, an account of each investigation.

### PURPOSE OF THE CASE STUDIES

The purpose of the case studies is to add qualitatively to our understanding of the barriers to affordable-housing rehab. Over and above the information obtained from the telephone discussions, literature, and other sources, the case studies provide an in-depth and "real world" look at the hurdles faced by rehab projects.

The resource group nominated many candidates for the case study investigations. The 11 programs chosen for study were selected on the basis of the following considerations:

1. *Problems.* The cases chosen all achieved considerable measures of success in their renovation activities, but they also had to overcome myriad problems. We focus on the hurdles that were encountered.
2. *Strategic range.* As described in volume 1, barriers to affordable-housing rehab can be grouped substantively into economic, development, construction, and occupancy hurdles. The 11 cases selected for the in-depth examination were chosen so that there was a representation of examples of a majority of the types of barriers. We also sought variety in the types of specific major issues encountered. Thus, some case studies predominately involve the building code, others historic preservation issues, and yet others lead-paint challenges.
3. *Range of institutions.* In selecting institutions for investigation the research team sought variety in type, size, and geographic location.
4. *Availability.* The candidates were asked whether they would be willing to participate in the on-site case studies.



Although we sought a variety of case studies, there is still a limited range. Only one investigation involved a local, private remodeler. The cases also lack rural representation. Study resources inhibited the ability to expand the case study range.

The 11 case studies are listed below by location, name of organization, and the major barriers considered.

<b>Case Study Location</b>	<b>Topic/Organization</b>	<b>Barriers Considered</b>
State of Massachusetts	Article 34	Progress and limitations of statewide rehab-sensitive building code; issues concerning historic preservation, seismic, and accessibility provisions
New Haven, CT	NHNHS	Secretary of Interior Standards; pilot program for flexible standards
Trenton, NJ	Isles	Barriers confronting nonprofit, including building code issues ("old" New Jersey building code)
Trenton, NJ	Capital City Redevelopment Area	Rehab issues ("old" code) involving reuse of upper-story space
Chester, NJ	Asdal, Inc.	Rehab issues confronting remodeler and benefits of New Jersey's new, rehab-sensitive building code
South Brunswick, NJ	Rural farmhouse conversion to cultural center	Rehab issues confronting reuse; highlights sensitive administration of New Jersey's "old" code
Miami, FL	Little Haiti Housing Association (LHHA)	Many issues confronting a nonprofit rehabilitating houses in Little Haiti
Chicago, IL	Varied	Issues confronting adaptive mixed use
Memphis, TN	Varied	Survey of range of issues confronting adaptive reuse and mixed-use rehabilitation
Seattle, WA	Varied	Barriers to rehabilitation in a "hot" real estate market, including analysis of the impact of growth management
Los Angeles, CA	Varied	Issues confronting rehabilitation of masonry buildings; benefits and limitations of moderate rehabilitation

## **CASE STUDIES: FIELD PROTOCOL AND ORGANIZATION**

All of the 11 case studies were prepared or overseen by the research team. Two of the case studies were commissioned by the National Trust for Historic Preservation. Bradford White conducted the Chicago case study for the Trust, and Stephen Turgeon conducted the Memphis investigation. The Los Angeles analysis was commissioned by the Enterprise Foundation. The remaining eight case studies were conducted by Rutgers University (with Robert Kuehn assisting Rutgers in the Massachusetts analysis). All of the Rutgers case studies were prepared by Dr. David Listokin and/or Dr. Barbara Listokin of the Center for Urban Policy Research.

To ensure a consistency, a field protocol was developed that would be followed by all those administering the case studies. The protocol also specified the following organizational framework for the case study write-ups:

1. *Summary of findings.* This opening section provides a synopsis of each case study's major findings.
2. *Background.* This section sets the context for each case study and includes such considerations as the history of the organizations (e.g., Isles or LHHA) or legislation (e.g., Massachusetts's Article 34 or New Jersey's new rehab code) studied and an overview of the city or state setting.
3. *Rehab description.* Where applicable, information is provided on the scale and nature of the rehab activity.
4. *Barriers to housing rehab.* This section presents the barriers as illustrated in the case studies. The hurdles are presented following the analytic framework shown in summary exhibit 1 in the executive summary in volume 1: the economic barriers are presented first, followed by the hurdles to effecting renovation at the development, construction, and occupancy phases.

## **CASE STUDY FINDINGS**

Although we conducted 11 case studies, only six are presented in this volume because of space limitations. The six, which are geographically dispersed, are Article 34 (Massachusetts), NHNHS (Connecticut), Isles (New Jersey), LHHA (Florida), Chicago (Illinois), and Seattle (Washington). All eleven case studies, however, are drawn from in the synthesis chapter (Chapter 2). The findings from the 11 case studies are also summarized in exhibit I.1.

**EXHIBIT I.1**  
**Case Study Examples of the Barriers to Affordable-Housing Rehab**

**DEVELOPMENT PHASE BARRIERS**

<b>Case Study</b>	<b>Acquisition Strategies</b>			
	<b>Banks</b>	<b>Property Liens</b>	<b>Private Purchase</b>	<b>FHA</b>
<i>NHNHS</i>	Sale in bulk unfeasible for NHNHS's smaller scale, and they are unwilling to outbid speculators	Liens are sold in bulk often to investors and speculators—they are not suitable for NHNHS's needs	Impractical because of thousands of dollars owed on such properties. Also have trouble locating owners and getting them to sell, or owners overvalue their property	High appraisal values are often above NHNHS's budget for property acquisition
<i>Isles</i>		City does not foreclose where there is a tax-rate certificate. Also, foreclosure is a lengthy process and the city does not properly secure properties against vandals and further deterioration	Owners have to be located and often refuse to sell or overvalue their property. Liens must often be paid on properties as well	FHA sale prices are too high above Isles's budget, and the sites are typically scattered
<i>LHHA</i>		Acquiring property through foreclosure is a lengthy process, exacerbating deterioration. More important, the title conveyed through this method is unrecognized	Difficult to identify legal owners or to get realistic prices for the homes, considering the back taxes owed. Private owners rarely give options to buy, and they want to close quickly. The long turnaround time for public subsidies makes these high up-front costs difficult to cover	As a result of recent changes to FHA fore-closures, LHHA is now competing against many others for homes, including high-bidding speculators, and is no longer receiving a 30 percent discount previously given to nonprofits.
<i>Memphis</i>	Banks are unwilling to use existing, unfinished buildings as collateral			
<i>Asdal &amp; Co.</i>			Difficult to find owners, clear title, and assemble properties	

*Continued on next page*

**EXHIBIT I.1 (continued)**

**DEVELOPMENT PHASE BARRIERS**

<b>Case Study</b>	<b>Acquisition Strategies</b>		
	<b>Eminent Domain</b>	<b>Donation</b>	<b>Other Acquisition Strategies</b>
<i>Isles</i>	Requirement for property valuation at the time an area is designated as blighted means values are often too high	Rare; owners usually want compensation, or too much money is owned in liens	
<i>LHHA</i>	City does not use eminent domain to acquire property for rehab		
<i>Chicago</i>			Competing with market-rate developers for the same properties. Finding affordable properties in areas with sufficient residential support services is difficult. Difficult to convert nonresidential properties, and hard to find buildings suitable for 100 +/- units
<i>Memphis</i>			Speculation is a problem, especially once renovation has begun in an area; owners are hoping for much more than buildings are worth and prices are high. Absentee landlords are happy to do nothing
<i>Asdal &amp; Co.</i>			Properties available for sale or rehab are often not in desirable areas. Price is another issue
<i>Seattle</i>			The “hot” market in Seattle has effectively driven up housing prices. It is often necessary to pay cash at closing and property owners want to close quickly. Attempts to assemble properties have also driven up prices

*Continued on next page*

**EXHIBIT I.1 (continued)**

**DEVELOPMENT PHASE BARRIERS**

Case Study	Acquisition Strategies		
	Estimating Costs	Insurance	Land Use
<i>NHNHS</i>	A problem in 95 percent of homes. Adds to the difficulties of rehab		
<i>Isles</i>	Challenging because every property is different, hidden construction needs add to costs, and there is often a delay between the original estimate and the onset of renovation		
<i>LHHA</i>	Uncertainties in estimation arise from the fact that major systems (e.g., heat and plumbing) are often turned off, or from other unknowns, (e.g., termite damage)	“Greater risk” with rehab translates to higher liability and hazard insurance. Hurricane Andrew drove up prices and made insurance difficult to obtain	
<i>Chicago</i>	Architect fees are generally higher for rehab		Parking requirements are difficult to meet in some places, as are other requirements in the local zoning code. Obtaining zoning approval for adaptive reuse was difficult in one instance because of community opposition
<i>Los Angeles</i>	Los Angeles is in an inflationary spiral (at least at the time of this study). As prices began to increase during the construction boom that began in 1996, general contractors received higher and higher bids, which forced them to farm the work out to more subcontractors. The subcontractors were experiencing a labor shortage; they had to raise their prices and be more selective about the jobs they accepted. This increased the amount of the bids, since the bids were based on what the subcontractors hoped to make, and, thus, market estimates went up. Remodeling projects are complicated by constraints and asbestos/lead conditions. Builders typically prefer new construction	Because some buildings are located in high-crime neighborhoods, full-time security guards, dogs, and razor-wire fencing may be required	
<i>Memphis</i>	Many contractors fear surprises like lead pipes or asbestos and hesitate to give numbers. The Fudge factor for unknowns is high, and pricing is coming in 50 percent higher than what was estimated	Insurance is expensive, but not difficult to obtain	Need to provide parking is a serious issue, especially in downtown rehab. Acceptable means of providing close parking, such as an underground facility or in a garage, are prohibitively expensive
<i>Asdal &amp; Co.</i>	It is common to underestimate expenses, often because of problems that arise once rehab has begun, e.g., unanticipated termite damage		Difficulty in obtaining variances in adaptive reuse and NIMBY-ism for in-fill rehab projects in general
<i>Seattle</i>	Inherent uncertainties in estimating rehab make it difficult, as does the practice of estimating on comparable jobs, since every building is different. But the speed with which estimating has to be done in many cases makes working with “comps” necessary. Access is sometimes limited, plans are typically absent and hazardous materials are often a factor		Parking requirements have been a detriment to doing rehab in Seattle: space is at a premium and adding parking in existing structures is difficult. Another barrier is the mandate that all construction must include 20 percent open space. Retrofitting an existing structure with 20 percent more space is a challenge

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**EXHIBIT I.1 (continued)**

**DEVELOPMENT PHASE BARRIERS**

<b>Case Study</b>	<b>Financing</b>	<b>Historic Tax Credits (HTC)</b>	<b>Low-Income Housing Tax Credit (LIHTC)</b>
<i>NHNHS</i>			LIHTC is limited statewide, and NHNHS has kept their annual request constant, despite rising rehab costs, for fear of losing it outright
<i>Isles</i>	A “reasonable cost limit penalty” places a ceiling on the amount of money allowed per unit to be eligible for some subsidies. This can work to the disadvantage of Isles because the smaller construction scale, historic nature, variability and higher amenity of rehab, community infrastructure, and general urban mission make the cost per unit exceed that ceiling	Use of HTCs requires certain trade-offs between preservation and practicality. Preservation is usually more expensive	Meeting the scoring criteria for LIHTCs (including scoring additional points for more bedrooms, energy efficiency, larger units, or other amenities) is increasingly necessary to gain the subsidy; however, meeting the criteria is more difficult when dealing with a rehab project
<i>LHHA</i>	Subsidies are necessary but competitive, have ancillary costs, and pose timing difficulties. LHHA projects are contingent upon the Miami-Dade Co. surtax program, CDBG, HOME, HOPE, AHP from FHLB, and tax credits. Low appraisals are often a hardship for LHHA’s financing		The smaller scale of units in an LHHA project does not reach the critical scale of 100 units typically funded by LIHTCs
<i>Chicago</i>	Most financing barriers pertained to the amount of time the application and approval process takes and the need to have control of a building to apply for financing. A developer may have to control a building for 12 to 18 months or more before financing is closed and construction can begin. This is especially difficult for nonprofits because of the general lack of predevelopment funds. Only a limited number of banks meet CIP (Community Investment Program) requirements. There is a lack of coordination between city and state processes	The availability of many other sources of funds and the subsequent reduction of state and local funds when using HTC reduces its use. Applicability is limited by “economic substance” requirements under the IRS code. The need to preserve interior partitions, ceilings, plaster, and trim is a significant challenge when using HTC for adaptive reuse	The city of Chicago has LIHTC funds allocated by statute, application is typically made to the city rather than to the state. TC investor will sometimes not put money into a rehab project because of the uncertainty of certification until after the building is placed in service. Some investors discount the pricing of the LIHTC because of certification risks
<i>Memphis</i>	Many of the rehab projects in this study are in mixed-use buildings with ground floor retail. Finding retail tenants has proven to be difficult, but necessary, especially in the smaller buildings where the space makes up a significant portion of the floor area and constitutes a significant portion of the building’s revenue. Banks are reluctant to finance both buildings downtown and older buildings. Appraisals are not high enough for the amount of work going into the building		
<i>Asdal &amp; Co.</i>	Low loan-to-value ratios and higher fees and interest rates increase financing costs. Appraisers have difficulty finding comparable properties and do not understand many of the environmental costs		
<i>Seattle</i>	Because of the uncertainties and challenges that accompany rehab, lenders typically demand a higher project contingency factor, higher hard- and soft-costs estimates, and a construction team with greater expertise	A tension between qualifying for HTCs and satisfying the market often arises, making the use of HTCs difficult or impossible	

*Continued on next page*

**EXHIBIT I.1 (continued)**

**CONSTRUCTION PHASE BARRIERS**

<b>Case Study</b>	<b>Building Code</b>	<b>Access</b>	<b>Seismic/Lead/Asbestos</b>	<b>Historic</b>	<b>Davis-Bacon</b>	<b>Trades</b>	<b>Relocation</b>
<i>NHNHS</i>		Can add to the costs	Environmental issues are sometimes confronted, but NHNHS manages to deal relatively painlessly with lead and asbestos	NHNHS needs more flexibility in meeting historic preservation requirements as they often delay the rehab or add to the costs. Mandating such things as wooden window replacements, as opposed to vinyl, significantly impacts the costs of rehab	Can add to costs	Construction jobs above a certain dollar threshold must be publicly bid, so NHNHS sometimes cannot ensure that they are working with the most experienced and competent urban rehab company	
<i>Isles</i>	The “25–50 percent rule” (i.e., more rehab increases requirements) in the New Jersey code adds to costs; however, recent changes that affect existing buildings help to alleviate the problem		Lead-paint abatement forces higher costs substantial rehab	Isles is sensitive to historic preservation needs, but it needs greater flexibility in historic preservation controls to keep rehab affordable, especially when working on a building’s interior. Historic preservation compliance and lead-paint abatement have also been at odds		Difficulty in securing medium-sized contracting firms	
<i>LHHA</i>	LHHA has experienced long delays in applying for electrical, plumbing, and other permits. Use of some public subsidies requires full compliance with minimum housing standards, leading to costly replacement of still-usable items, such as a ceramic-tile roof			The use of federal funds for acquisition-rehab purposes evokes the Section 106 process to determine historical significance. This process can be lengthy and has sometimes left LHHA in a “costly limbo”	Were LHHA to use federal monies for rehab, they would have to pay prevailing wages—more than they currently pay	The scale of LHHA’s jobs is usually too small for subcontractors, but they often have trouble keeping their in-house crew sufficiently at work. Also, the small scale often means higher material and delivery costs	If HOME money is used for rehab construction, then relocation expenses must be paid for both legal and illegal tenants
<i>Chicago</i>	Sprinkler requirements are costly in anything but substantial rehab, and the installation of fire alarms adds to costs. Loft conversions over four stories must meet high-rise codes, which adds significantly to costs	Handicap access (elevators and stairwells) can be difficult to provide and costly	In moderate rehab, encapsulation, lead-paint abatement, and removal of storage tanks can significantly increase the budget		Can increase rehab costs 30 percent to 40 percent	Bringing contractors into compliance and helping them complete paperwork can unexpectedly add to costs	
<i>Capital City Redevelopment (Trenton)</i>	Because their level of rehab required compliance with new-construction code standards, the building in question needed two means of egress. Compliance was difficult because of costs, historic requirements, and reconfiguration constraints						

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**EXHIBIT I.1 (continued)**

**CONSTRUCTION PHASE BARRIERS**

<b>Case Study</b>	<b>Building Code</b>	<b>Access</b>	<b>Seismic/Lead/Asbestos</b>	<b>Historic</b>	<b>Davis-Bacon</b>	<b>Trades</b>	<b>Relocation</b>
<i>Los Angeles</i>	Requires compliance with substantial rehab requirements	Upgrades not required of the low- or mid-cost options. Necessary for the high-cost option	Some of the buildings have seismic reinforcement, but for those without it, this expense adds considerably to the cost for rehab, often making it unfeasible. Asbestos is an issue in many of these buildings		If the guidelines apply to the project, cost is estimated to rise 15 percent to 30 percent		Becomes an issue if a mid- to high-cost option is used since many of the buildings are inhabited
<i>Memphis</i>	Difficult to acquire a variance for operable windows. Another obstacle is the requirement for two stairways to achieve fire ratings	Requires more imagination	Difficult to make old buildings conform to the current seismic requirements			The limited availability of contractors, especially for small jobs, in a tight construction market was a general barrier and drove up costs significantly in recent years	
<i>Asdal &amp; Co.</i>	Restrictive codes drive up rehab costs, often significantly		Asdal has encountered complications due to seismic and nuclear testing and lead-paint requirements			Higher skill levels necessary for quality rehab. There is a paucity of training	
<i>Seattle</i>	Despite a fairly flexible building code and general support for rehab, the threshold for meeting new-construction standards is often imposed. New-construction fire and safety standards can drastically increase the cost of rehab. Also a factor is the requirement that an entire mixed-use building meet the code if the residential rehab on upper floors triggers the substantial alteration standard	Creativity of design and flexibility are often necessary to meet access requirements	Retrofitting existing buildings to strict seismic protections is a challenge. Often, residents must vacate for the rehab to be completed. Asbestos containment can be expensive if ceiling layouts have to be altered	Review time for projects can be lengthy		The “hot” construction market makes it difficult to hire competent contractors, who are generally spoken for by larger companies. Smaller companies “are less sophisticated and encounter such issues as difficulty in getting bonding”	



## **CASE STUDIES**



## **CHAPTER 6**

### **Rehab Barrier Case Study: State of Massachusetts—Article 34**

#### **SUMMARY OF FINDINGS**

Massachusetts is regarded as a leader in adopting regulations that foster rehab of existing buildings (Pierlert 1981). A prime example of this is Article 34 of the Massachusetts State Code. Article 34 replaced the rigid “25–50 percent rule” (i.e., new-building standards are mandated by rehab investment exceeding 50 percent of the building’s value) with a much more flexible standard. This case study focuses on the accomplishments and limitations of Article 34 and other regulations governing rehab in Massachusetts.

Regulation of additions to and repair, alteration, and change of use of existing buildings under Article 34 is proceeding with relative success in Massachusetts. Following are some of the comments made by experts interviewed by the authors: “Article 34 provides an effective framework for looking at each project and an avenue to work out solutions.” “Article 34 generally works well, especially compared to the “25–50 percent rule” that was absolutely wrong.” and “Article 34 provides latitude in making decisions.” (Persons interviewed are included in the references section.)

While Article 34 and its accomplishments are to be lauded, the article does have limitations. These are described below.

#### **Lack of Awareness/Need for Training**

One problem regarding the use of Article 34 is that building officials are frequently not fully aware of its provisions and how it works. Coupled with this is the overall need for more training for building officials at the local level and more staff at state and local levels. When Article 34 was first adopted, an outreach program provided some information and training for local building officials. This training has been cut back, however, and what is currently not well understood is the intent of the code and the details of its regulations.

#### **Unnecessary Requirements**

When an extensive rehab project (in terms of expense) is contemplated, code officials sometimes demand building improvements that go beyond the standards specified in Article 34. Thus, the “25–50 percent rule” in effect sometimes lingers. The building owner and the architect will often comply with more than the code requires so as to “move the project along” and not antagonize code officials. This situation of building officials demanding more than what is required by the code is aggravated by inadequate training.

#### **Coordination with Fire Protection Regulations**

Better coordination with fire officials and linkage of the fire code requirements and Article 34 would result in an improved system in Massachusetts. As things stand now, there is some conflict. Also, as the fire protection requirements have increased (e.g., making sprinklers

mandatory with substantial rehab), the flexibility of responding to Article 34 through compliance alternatives (e.g., installing sprinklers as an alternative to enclosing a stairway) has diminished for the rehab of existing properties.

### **Issues beyond Article 34—Access and Historic Preservation Provisions**

Massachusetts General Law, chapter 22, section 13A, mandates rules and regulations for accessibility and establishes the Architectural Access Board (AAB). The fact that the AAB's standards are different from and more restrictive than the requirements of ANSI A-117.1, the Americans with Disabilities Act, and the Fair Housing Amendment adds considerable complexity to rehab projects. Furthermore, it has been reported that bringing matters before the AAB tends to add significant delays (90 days minimum). Involvement with the accessibility regulations may be preventing some rehab projects from proceeding. It is clear that greater coordination between the Architectural Access Board and the Board of Building Regulations and Standards, Article 34, is needed.

Historic rehab in Massachusetts is fostered by section 635, which establishes building code requirements for historic properties in the state. The Secretary of the Interior's Standards for Historic Preservation (SISHP) also can affect the rehab of historic buildings (e.g., when federal historic rehab tax credits are used). Overall, the SISHP have been flexibly administered in Massachusetts, but there are instances in which the application of these standards raises issues with respect to effecting affordable-housing rehab and adaptive reuse.

### **BACKGROUND TO ARTICLE 34 OF THE MASSACHUSETTS STATE BUILDING CODE**

In 1972, the Massachusetts state legislature decided that there should be a statewide uniform building code instead of separate regulations set by each community. Chapter 802 of the Acts of 1972 authorized a statewide code that would apply uniformly throughout the Commonwealth. The statewide code included a "25–50 percent rule": if the rehab expense exceeded one-half the value of the building being renovated, the entire building would have to be brought up to the standards for new construction.

The 1970s saw an increase of rehab and reuse activity in Massachusetts. (This state has the nation's oldest housing stock and is a leader in adaptive reuse). The "25–50 percent rule," however, became increasingly problematical to renovation investment in this state. The following example is illustrative (Ferro 1993). In 1974, a six-unit Cambridge apartment building was slated for rehab. The renovation budget of \$38,000 (in 1974 dollars) would modernize the building and remove hazards by converting the building's heating system from space heaters to modern central heat; rehabilitating all bathrooms, kitchens, plumbing, and wiring; installing a new roof; and removing hazardous lead paint. Yet, this plan was thwarted by the building code.

Enter now the building inspector. Having determined that the proposed investment, under the "25–50 percent rule," required full compliance with the new-building code, the inspector had no choice but to make additional demands. First, since the building contained two halves, each with three apartments, the

inspector asked that the wall between them be rebuilt to provide two-hour fire protection and further requested that a full complement of smoke and fire detectors be installed in each rental unit. Second, the inspector noted that some tenants were using the intended dining room as a bedroom. Therefore, new hallways would have to be installed between it and the kitchen. Finally, all ceilings and wall surfaces would have to be brought into compliance with required fire ratings. Because the additional cost of the inspector's specified changes was conservatively estimated at \$15,000 (1974 dollars)—a 40 percent addition to the original budget—both the owner and his tenants agreed that such added costs would entail unacceptable increases in mortgage debt and rents, and the project was abandoned. (Ferro 1994)

There were repeated problems in Massachusetts with respect to the building code in adaptive reuse situations. For instance, in the 1970s, the Atlas Stores warehouse—a New England mill-type building of six stories—was converted into Boston's Children's Museum. As the rehab cost exceeded 50 percent of the building's value, the "25–50 percent rule" required that the museum meet all code standards for new museum buildings—an impossible retrofit of the 100-year-old structure. Ultimately, the reuse to the Children's Museum was accomplished only through the granting of variances in the many situations where new-code compliance was infeasible. To depend on variances was problematical, however. The variances required that the code official constantly grant waivers from the nominal standard. In addition, the variances were time-consuming, added to processing costs, and raised the issue of the wisdom of keeping a rule ("25–50 percent" standard) if it had to be constantly administratively circumvented.

It was recognized by the latter part of the 1970s that the Massachusetts state code would have to be modified to eliminate the "25–50 percent rule." Rethinking of the "25–50 percent rule" was occurring nationwide at the same time (United States Senate 1978; Gross, Pierlet, and Cooke 1979; Berry 1979). After much committee work and consensus building, a draft Massachusetts rehab code was approved by the State Building Code Commission late in the fall of 1978 (Dinezio 1980). The document was incorporated as Article 22 of the Third Edition of the Massachusetts State Building Code and became effective in June 1979. Article 22 was revised in 1980 to include energy conservation provisions, recognition of various types of construction, and the extension of the time limit from two to five years for a building to qualify under Article 22 (i.e., buildings would have to have been occupied/used for five years to fall under Article 22's provisions).

In 1990, Article 22 was renumbered as Article 32, and in June 1992, minor editorial corrections were introduced. In a subsequent reshuffling of regulations, Article 32 was renumbered Article 34.

In the mid-1990s, seismic regulations for the upgrading of existing buildings were incorporated into Article 34.<sup>1</sup> Some background is in order. While Massachusetts is popularly considered to be an area of "moderate" seismic risk, because of the geology of the region, the effects of an earthquake would be felt over an area up to 40 times greater than the area affected by an earthquake of similar magnitude in California (Massachusetts Board of Building Regulations and

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<sup>1</sup>Seismic is a concern for rehab in other jurisdictions as well (see Morton 1991).

Standards [MBBRS] 1994b). Additionally, Massachusetts has a large stock of older buildings, constructed prior to the adoption of the first state building code in the early 1970s, and many of these buildings are constructed of unreinforced masonry—a known poor performer in earthquakes.

Recognizing the potential for serious damage to existing buildings and major loss of life and personal injury during an earthquake, a Massachusetts Seismic Advisory Committee spent four years (1988 to 1992) developing seismic regulations for the upgrading of existing buildings (MBBRS 1994b). The efforts of the committee culminated in amendments to Article 34 that were adopted in 1995.

The following sections focus on the overall provisions and application of Article 34. There is then a brief description of some of its specialized applications—namely, those dealing with historic properties and seismic requirements.<sup>2</sup>

## **ARTICLE 34: PROVISIONS**

Article 34 encompasses a chapter on provisions (the “Article”) and a technical appendix (Appendix F), which contains four parts:

Part One—Guidelines for Application

Part Two—Suggested Compliance Alternatives

Part Three—Detailed Classification of Occupancy by Hazard Index Number and Use Group

Part Four—Archaic Construction Systems

In brief, the intent of Article 34 is to foster rehab that “delivers” safe buildings while not requiring full adherence to the standards for new construction. This approach is reflected in the purpose section of Appendix F to Article 34 (F-101.1)

The purpose is to allow additions to and the repair, alteration, and change of use of existing buildings without requiring that the entire building be brought up to new construction requirements, and to still provide for the public health, safety, and general welfare. Conceptually, it is the intent of Article 34 to allow repair, alteration, addition, or change of use without meeting all new-construction requirements under the following general conditions:

1. All hazardous conditions must be corrected.
2. The existing building becomes the minimum performance standard.
3. The degree of compliance after the changes must not be below that existing before the changes.

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<sup>2</sup>While technically it is Massachusetts General Law, section 635, rather than Article 34 of the Massachusetts State Building Code, that governs historic properties, the section 635 historic code provisions are included here as an important code regulation of existing buildings.

In other words, Article 34 attempts to balance the desire to improve the condition of a building and the need to remove hazards—while not mandating that the property being renovated be totally retrofitted to a new building standard. An example of a hazardous condition to be addressed is a “hazardous exitway,” which Article 34 defines (3200.4) as a building with less than two acceptable exitways serving every story—one- and two-family and other types of buildings exempted—and with insufficiently wide egress with respect to doors, aisles, stairways, and so on. Other than hazardous conditions and certain improvements that will be specified shortly, the standard (as provided for by Article 34) to be maintained by the rehab is, by and large, the prevailing condition of the existing building.

Article 34 presents a number of critical concepts and provisions:

1. *Applicability* to existing buildings.
2. *Identification of building-use groups and, correspondingly, a hazard index scale.* Depending on how rehab affects the use groups/hazard index scale, more- or less-stringent requirements must be met. (These are described in detail shortly.)
3. *Requirements to be met.* These are on a sliding scale basis, as noted above.
4. *Compliance alternatives.* When a provision under Article 34 is impractical (e.g., because of the difficulty and expense of retrofitting an existing building), a reasonable alternative may be accepted.

Following is a description of each of these items.

### **Applicability**

Article 34 pertains to existing buildings. Section 3200.3.1 defines an existing building as one that has “. . . been legally occupied and/or used for a period of at least five (5) years.” (As originally adopted in Article 22, there was a two-year requirement.) The section also states that “No building for which there exists an outstanding notice of violation or other order of the building official shall qualify to use this article unless such proposed work includes correction of all outstanding orders of the building official.” If a building does not satisfy both of these conditions, it does not qualify as an existing building under the provisions of Article 34, and, therefore, it does not benefit from its provisions (MBBRS 1994a, 13)—in other words, it must comply fully with the code for new construction.

Article 34 applies to rehab. Ordinary repairs do *not* have to comply with Article 34 and, in fact, can be performed without a building permit (3200.3.6).

A further note with respect to applicability concerns the rehab of historic properties. Historic buildings in Massachusetts are regulated by a separate section (section 635 of the Massachusetts General Law), which is summarized later in our discussion. Section 635 generally has less-stringent requirements than does section 34.

## Building-Use Groups/Hazard Index Scale

Article 34 rates each building by use group and a corresponding hazard index scale from one (1) to eight (8), with one indicating the least hazardous use and eight indicating the most hazardous (see exhibit 6.1). For example, a storage facility (use group S-2) that stores items that do not tend to burn (e.g., glass or metal) is assigned a hazard index of one (1). Conversely, a very hazardous use (use group H)—for example, a place where combustible and potentially explosive liquids or gases are processed—is assigned a hazard index of eight (8).

### EXHIBIT 6.1 Hazard Index

USE GROUP <sup>a</sup>	DESCRIPTION	INDEX NO. <sup>b</sup>
A-1	Theater with stage	6
A-1	Theater without stage	5
A-2	Night club	7
A-3	Restaurant	
	Lecture halls, recreation centers, museums, libraries, similar	5
	assembly buildings	4
A-4	Churches	4
A-5	Outdoor assembly	4
B	Business	2
E	Education	4
F-1 & F-2	Factory and industrial	3
H	High hazard	8
I-3	Institutional restrained	5
I-2	Institutional incapacitated	4
M	Mercantile	3
R-1	Hotels, motels	2
R-2	Multifamily	2
R-3	One- and two-family	2
S-1	Storage, moderate hazard	3
S-2	Storage, low hazard	1

*Note:*

Each building is rated by use group and on a hazard-index scale from one (1) to eight (8). One indicates the least hazardous use; eight indicates the most hazardous use.

<sup>a</sup>See Section 203.0 through 212.0 and appendix F.

<sup>b</sup>Hazard Index Modifier for selected construction types.

When a building is classified in Construction Type 1A, 1B, 2A, or 2B, subtract one (1) from the Hazard Index number shown in Table 3204 of Article 34 for the applicable proposed new use group only.

The other uses fall somewhere between these two extremes. For example, a night club (use group A-2) is assigned a hazard index of seven (7); a restaurant (use group A-3) is assigned a hazard index of five (5); mercantile (use group M) is assigned a hazard index of three (3); and business (use group B) and multifamily (use group R-2) and one- and two-family housing (use group R-3) are assigned a hazard index of two (2). (See exhibit 6.1 for details.) Part three of appendix F to Article 34 has more detailed breakout of uses and hazard levels.



Of critical concern are the building's present use group (before rehab) and its intended use group (after rehab) and the corresponding hazard index ratings of the present and intended uses.

The *present* use group and corresponding hazard index are compared with the *intended* use group and hazard level, and the difference (in hazard use index) is calculated. Article 34 describes three declensions of this “before and after comparison”:

1. “The use group remains the same or there is a change in use group of equal or lesser hazard index.”
2. “There is a change in use group to one hazard index greater.”
3. “There is a change in use group to two or more hazard indices greater.”

Condition 1 above is governed by section 3203.0 of Article 34; condition 2 is governed by section 3204.0; and condition 3 is governed by section 3205.0. As shall be detailed shortly, building requirements increase from condition 1 to condition 3. First, however, the application of the use groups and hazard indices—the starting basis for the three levels of building requirements as specified by sections 3203, 3204, and 3205—are illustrated below from research by Boston Building Consultants (1994).

Thayer Hall is one of the Victorian brick buildings surrounding the quadrangle at Harvard Yard. Thayer Hall has been a student dormitory since its construction in 1869 (Boston Building Consultants 1994). An extensive renovation was designed in early 1993, the notable features of which were to introduce habitable space in the attics and to improve access and egress. In this instance, there is no change in use or shift in hazard level. The present use group is multifamily (R-2) with a hazard index of 2, and the intended use group is multifamily (R-2) with a hazard index of 2; since there is no change, section 3203.0 would govern the new use.

Bixby Crossing in Haverhill, Massachusetts, was constructed circa 1930 for a shoe factory; its last use was for a box company (Boston Building Consultants 1994). A 1988 remodeling involved an adaptive reuse of the structure for residential apartments. The building's present use group (before rehab) is factory (F-1), with a hazard index of 3; the intended use group (after rehab) is multifamily (R-2), with a hazard index of 2. The hazard level is reduced, so Section 3203.0 would be applied to the new use.

Student Crossing involved the reuse of an office building for a retail establishment in Cambridge. The present use group (before rehab) is business (B), with a hazard index of 2; the intended use group (after rehab) is mercantile (M), with a hazard index of 3. Because of an increase of one hazard level, Section 3204.0 would govern the new use.

Flint Memorial Hall in North Reading, Massachusetts, had been used as offices. In 1990, it was converted to the town library (Boston Building Consultants 1994). The present use group (before rehab) is business (B), with a hazard index of 2; the intended use group (after rehab) is library (A-3), with a hazard index of 4. Due to an increase of two hazard levels, Section 3205.0 would regulate the renovation.

## Requirements to Be Met

The standards to be met by Article 34 are detailed in sections 3203, 3204, and 3205. These, as noted, have increasingly stringent requirements.

Least demanding is section 3203, which applies if there is no change in use or if a change in use reduces the hazard index. Alterations and repairs that maintain or improve the performance of the building do not require full compliance with this section if there is no change of use (3203.4). Section 3203 requirements include the following:

- *Hazardous conditions*: Hazards must be removed (for example, the hazardous exitways previously described).
- *Loads*: Floor and structural loads must be determined to be adequate to support the proposed specific floor loads, which may be reduced from the new-construction load schedule. Other structural loads specified in the code for new construction must be safely supported.
- *New systems*: Newly installed systems (e.g., electrical or plumbing) must conform to the new-construction standard to “the fullest extent practical” (3203.3); individual components of an existing system may be repaired/replaced without requiring the system to comply to the new-construction standard.
- *Stairway enclosures*: Open stairways are prohibited except in one- and two-family dwellings, but no minimum fire-resistance rating is required for an existing enclosure. New stairway-enclosure construction should provide at least a one-hour fire-resistance rating (compared with two-hour fire resistance in most new construction).
- *Energy*: Energy standards must be met only by the building element that is altered (e.g., new walls or doors) or by equivalent energy savings elsewhere in the building, but the entire building need not comply with new-construction requirements.

There are a number of other requirements pertaining to fire hazards presented to adjacent buildings (the hazard should not be increased) and the provision of exit signs and lights, means-of-egress lighting, fire alarm systems, and other issues. In short, section 3203 requires that a building be safe in a number of critical characteristics (e.g., loads and fire safety), but, by and large, basic existing building conditions can remain. For instance, building area and height requirements in the code for new construction do not have to be met.

Standards are more stringent in section 3204, which is applicable when there is a change in use that increases the hazard index by one. In this case, the existing building is required to conform to the requirements of the new-construction code, with the following exceptions:

- Area and height limitations may be exceeded.
- Mixed-use fire separation requirements are reduced.

- Accessibility for the physically handicapped need not be provided.
- Exit stairway enclosure requirements are reduced in some cases.
- Fire- and party-wall requirements need not be complied with.
- Fire separation requirements for adjacent buildings need be complied with only when fire loading is increased.

Thus, even with the more stringent requirements of Section 3204, many characteristics of the existing property undergoing rehab do not have to be fully brought up to new-building code standards. For instance, a change in use is allowed in an existing building even if the structure exceeds the area and height limits.

Finally, if a change in use raises the hazard index by two or more, then section 3205 governs. Such a change is considered to be so significant that the rehabilitated building is mandated by section 3205 to “conform to the requirements for new construction” (3205.1). This same mandate is applicable to any change in use to an institutional use group, even when the hazard index is equal or reduced (3203.16).

### **Compliance Alternatives**

At the heart of Article 34 are the sliding scales of standards detailed above and the increased flexibility in meeting requirements offered by “compliance alternatives.” As stated in Section 3206.0:

Where compliance with the provisions of the code for new construction, required by this article, is impractical because of structural or construction difficulties or regulatory conflicts, compliance alternatives may be accepted by the building official.

Any decision about the adequacy of a compliance alternative is left to the local building official. Article 34 requires, however, that the official provide the Massachusetts Board of Building Regulations and Standards with “information regarding the compliance alternatives adopted or rejected by him” (3206.2).

The above is a technical outline of Article 34. As with all codes, further clarification is offered by examining its application in practice. We present one example below.

### **EXAMPLE OF A COMPLIANCE ALTERNATIVE**

#### **Background**

The property in question is the Old Reading Schoolhouse Condominiums located at 52 Sanborn Street, Reading, Massachusetts. This almost-100-year-old Georgian–Colonial style building is designated as a local historic landmark. It was originally designed and used as a high school and,

in more recent years, as a town community center. The building was then converted and approved for 40 residential condominium units. This involved a substantial rehab and adaptive reuse and raised numerous building code issues (Macartney 1992).

The building's existing (prerehab) use group as a recreation center was A-3, with a hazard index of 4. The after-rehab use was multifamily (R-2) with a hazard index number of 2. The change of use thus involved a lesser hazard index, and, as such, the rehab was governed by Section 3203.

Although section 3203 entails the least-stringent rehab requirements, compared with sections 3204 and 3205, the renovation of the Old Reading Schoolhouse was restricted by existing structural conditions as well as by historical commission constraints. As a result of these constraints, various code-related issues required compliance alternatives as described below. (Illustrative examples of the many compliance alternatives are presented.)

### **Code Issue—Stairwell Enclosures**

#### *Code Requirement*

- Construction to complete stairwell enclosures should be one-hour rated, per MSBC section 3203.12.

#### *Constraints to Meeting the Code Requirement*

- The historic significance of the existing building, including specific interior components.
- Developer's desire to promote use of the stairs by the occupants, since the stairs are large and inviting.
- No natural light available to the interior corridors if the stairwells on each floor level are solid walls.

#### *Compliance Alternative*

- Automatic sprinklers are provided in the path of egress from each unit into the stairwell.
- In addition, the interior, nonrated glass-pane wall is protected through the sprinkler system by a water curtain on both sides of the enclosure.
- Sprinkler heads are included within the stair tower at each floor level for added protection.

#### *Supporting Considerations for the Compliance Alternative*

- Occupancy load per floor is less than 40 persons.
- There are two emergency stairways per floor, with a maximum travel distance of 46 feet.
- Glass is tempered with self-closing door hinges; an existing push plate is acceptable.

## **Code Issue—Stairwell Guards and Continuous Handrail**

### *Code Requirement*

- If the space between the stringers exceeds 12 inches, guard height should be 42 inches.

### *Constraints to Meeting the Code Requirement*

- The mandate to maintain the historic significance of interior building design and components.
- The existing handrail construction is set between 30 and 32 inches and is connected to a post at each change in direction.

### *Compliance Alternative*

- No change from the existing construction is required.

### *Supporting Considerations for the Compliance Alternative*

- The stairs and landings are much wider than required by code (five feet).
- The corner posts are higher than the rails (40 to 42 inches), which tends to route users away from the inside.
- The occupant load per floor is less than 40 persons.
- The existing condition has worked well without accidents for many years. With the reduced occupant load resulting from the change to residential use, the current situation is less hazardous than the former arrangement. (Macartney 1992)

These (and other) compliance alternatives were allowed and fostered the reuse of this property.

## **ANALYSIS OF ARTICLE 34**

As previously described in detail, the key to the application of Article 34 is the degree to which the building will move up or down a hazard index scale based on its continuation of or change in use group. There are three primary categories (sections 3203, 3204, and 3205) for which specific requirements are spelled out. A key feature is that compliance alternatives may be proposed in all categories.

In practice, Article 34 operates in a somewhat more complicated manner (Adams 1995). Where an extensive rehab project (in terms of expense) is contemplated, building code officials may demand a building improvement that goes beyond the standards specified. The building owner and architect will often comply to “move the project along” and to not antagonize the code official. In effect, building code officials are still applying the old “25–50 percent rule,” irrespective of Article 34, that required new-construction standards for existing buildings. In short, there is an official three-tier specification of requirements in Article 34 (e.g., sections 3203 to 3205) and a “gray area” of rehab requirements (expensive rehab equals added demands), but both the official and gray-area improvements may be met by compliance alternatives.

## **Preliminary Meeting**

The key to initiating compliance under Article 34 is described in subsection 3202.1, “Investigation and Evaluation,” which states the following: “For any proposed work covered by this article, the building owner shall cause the existing building to be investigated and evaluated in accordance with the provisions of this Article.”

It is this investigation and evaluation, coupled with the early schematic design for the proposed use and alteration of the building, that triggers how Article 34 is to be applied to the project. In short, it is up to the owner (and the owner’s design professionals and consultants) to provide the building department with the information necessary to determine the present condition of the building and the types of changes desired and anticipated as part of the rehab project. The building department may choose to visit the existing building to confirm the conditions noted in the investigation and evaluation report, but a site visit is unusual.

The presentation of this investigation and evaluation by the owner is often done as part of a preliminary meeting with the building department. At the preliminary meeting, issues are discussed informally. It is recognized that such meetings are an important first step in the process. Despite this, not all building departments are routinely available for such preliminary meetings to examine existing conditions and compliance alternatives (McBain 1995).

Whether or not a meeting is held and/or compliance alternatives are considered by a given building department is typically as much a matter of happenstance as it is formal procedure. In this regard, it is important to step back and look at the capacities and character of the local building officials. There are 351 cities and towns in Massachusetts and the circumstances vary widely.

In municipalities like Boston, Worcester, Springfield, and other large cities, the inspection services departments have professional staffs more capable of processing compliance alternatives. Few, however, employ rehab specialists who are trained to deal with the particular nuances of Article 34. These departments are also often very busy with routine matters like inspecting code violations, processing repair orders, and handling more ordinary building permit requests. Some rise to the occasion and are readily engaged in thinking through compliance alternatives, but others tend to avoid these requests. The success of the process therefore often depends on the current workload of a department or the personality and interest of the assigned code official rather than on the merits of a particular Article 34 case.

In many smaller cities and towns, these conditions are compounded by the lack of depth and experience of the local building department. These offices are often staffed by part-time employees who do not necessarily have extensive professional training. (In one small Massachusetts town, the building official worked on code matters in the morning and managed the transfer station—town dump—in the afternoon.) Their routine activities run more to single-family home construction and remodeling. A request to consider a compliance alternative for an existing building of any scope is likely to be a very infrequent circumstance. Consequently, requests for waiving or modifying the strict application of the code are often viewed suspiciously and are not readily accommodated.

This last point speaks to the underlying problem of implementing Article 34. Building code officials properly view themselves as protecting the public interest and public safety. The building code is generally prescriptive in defining what constitutes safe practice; e.g., an exit stairway must be 42 inches in width. It is therefore a considerable departure for a code official to take it upon him- or herself to decide that some alternative approach is just as safe; e.g., an exitway may be 36 inches wide if a sprinkler system is installed. Such a compliance alternative also requires a value judgment, which could expose the building official to criticism for compromising the public interest or, worse yet, for showing favoritism to a particular applicant. Thus, the very nature of Article 34 requires a leap of faith by code administrators—a leap that cuts against the conservative tendencies of officialdom.

### **Training of Building Code Officials**

Training is a major issue. The state law requires continuing education for building code officials under the auspices of the Massachusetts Board of Building Regulations and Standards (MBBRS). MBBRS currently offers only four professional training seminars a year in different state locations; each local building official is required to attend one seminar each year. In addition, there are speakers at local and regional building-official association meetings. The training program for building officials is ad hoc, however, and more could be done in this area. When Article 34 was first adopted, there was an extensive outreach program that provided information and training for local building officials. This outreach has since stopped and neither the intent of the code nor its details are well understood in the field.

The MBBRS is generally viewed by the building industry as a positive influence. However, the agency has only a few staff members and its budget is quite modest. Notwithstanding its limited staffing, it is able to promulgate new regulations and process code appeals in an expeditious manner. In an ideal world, the budget of the MBBRS would be expanded to build upon these successes. One could imagine a monthly or quarterly newsletter that publicized new code issues or summarized cases that provide precedent for code compliance. The training seminars could also be expanded to ensure that all local officials were up to speed on current code issues and reasonably knowledgeable about their prerogatives under special code provisions, such as Article 34.

The building industry could also do more to support the MBBRS—developers, architects, engineers, contractors, and other professionals often privately complain about the vagaries of the code and its administration, but they seldom take public action. The industry could, at a minimum, lobby to expand the scope and budget of the MBBRS. A few hundred thousand dollars per year in extra budget could save tens of millions of dollars squandered on unnecessary code compliance if the system worked better and local officials were better informed. The industry could also partner with the MBBRS to cohost seminars for building officials on a more regular basis, perhaps creating a series of mini-topics like alternative compliance, accessibility, seismic design, historic preservation, or related issues. The historic community in particular has been remiss in not taking the initiative to better define its unique problems in reusing significant buildings within the confines of the code.

## Coordination with the Fire Marshall

The interrelationship of the building department and the fire department is a critical factor in the regulation of any rehab project. This interrelationship is defined differently in each Massachusetts community. In some jurisdictions, like Boston, the fire department has a representative located in the building department, while in other communities, like Newton, the fire department is located in a separate building, perhaps across town. In some communities, the building department and the fire department work is parallel through the informal and formal review and evaluation processes, while in other communities they work in series with little coordination. As a Boston architectural firm noted:

The fire laws have removed the ability to negotiate. There is no flexibility. The building department and fire department are generally not together, either physically or in interest. The fire department is looking out for the safety of the firefighters first and foremost. (Kaslow and Alexander 1995)

Coordination between the building official and the fire official is critical because each is enforcing important health and safety requirements. These requirements overlap and, in some cases, may conflict. An inherent source of potential conflict exists because building officials and fire officials have overlapping authority. The Massachusetts State Building Code is a regulation under a state law that requires that all local jurisdictions enforce it. Referenced in the state code is the National Fire Protection Association (NFPA) which is also locally administered, typically by the municipality's fire department. While NFPA is technically part of the building code, it is generally viewed as being "owned" by the fire marshal who takes full authority for its administration. Since fire code issues are literally a matter of life and death, few participants inside or outside of the local building department are willing to challenge this authority. In effect, both code officials and private professionals are often intimidated by these circumstances, and the fire marshal sometimes expands his or her authority beyond the code—at times quite arbitrarily.

This situation is exacerbated by the limited capacities of the local fire department to review and evaluate proposed architectural and engineering plans for compliance. A frequent complaint in this regard is that the fire department's plan reviewers cannot read plans.<sup>3</sup> Unlike minimal requirements for building code officials, the fire marshal's designee need not have any particular professional background or training for the task at hand. Often the marshal's plan reviewer is an older firefighter who needs a desk job until retirement or a firefighter who has been injured in the line of duty. This is not to say that these are not good, hardworking, committed people, but only that the professional background for code review is often lacking or likely to require on-the-job training.

The process of submitting construction drawings and specifications to the building department results in code review and the issuance of a building permit. Once a permit is issued, these construction documents become the record set that is essentially signed-off as to code

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<sup>3</sup>This observation was offered unsolicited in one form or another by at least half a dozen professionals interviewed in the course of this research. However, none wished to be quoted directly, citing their ongoing relationship with fire department personnel whose capacities are being called into question.



compliance. However, the same set of documents submitted to the fire department is not typically considered binding and more often than not is subject to additional review and change once the building is completed. This circumstance creates great consternation among building professionals who thought they were in full compliance after preconstruction reviews, only to find at the end of construction that there is a long list of additional or changed requirements being imposed by the fire marshal. The fire marshal also often does not feel bound by the codes in effect at the time the building permit was issued (a standard assumption for code compliance) and frequently will require the building to be brought up to current standards, including code requirements adopted during the period of construction. Over a two-year construction period, this can result in extensive and costly changes.

Savvy architects and contractors recognize this reality and spend extra time talking through the fire compliance issues with the fire marshal before construction begins. This process does not necessarily ensure that there will be no changes down the line, but at least issues can be flagged that otherwise would not come to light because the reviewer probably does not understand the documents. The other step taken, assuming the fire marshal cooperates, is to ask the marshal to walk through the building when it is two-thirds complete—at a time before the walls are closed up and changes can still be made easily. At this juncture, the electrical and plumbing code inspectors make such a walk-through and sign-off, so it is also a good time for fire marshals to inspect the project (although they are not compelled to do so).

This “talk-through” and “walk-through” approach tends to minimize surprises at the time of completion and certificate of occupancy, but success is not guaranteed. Fire marshals are perfectly capable of changing their minds if, in their judgment, some assembly or system can be made safer. No one disagrees with the ultimate concept of safety, but there needs to be a reasonable limit since nothing is ever 100 percent safe. Of course, the owner, the architect, and the contractor are most vulnerable at the end of construction when deadlines for completion and occupancy are looming, so there is usually little choice but to comply with even excessive or erroneous directives from the fire marshal. At best, the development team attempts to negotiate some reasonable compromises and/or to plead for a temporary certificate of occupancy until the issues can be sorted out or appealed.

There are also a number of Massachusetts fire prevention laws (e.g., MGL I48 sec. 26) that, because they are laws and not regulations, take precedence over the building code. Some of these laws are in effect throughout the state and others require local adoption. An example of a type of potential conflict and the need for coordination is apparent in looking at one of the local options, section 26 I, which states the following:

In a city, town or district which accepts the provisions of this section, any building hereafter constructed or hereafter *substantially rehabilitated so as to constitute the equivalent of new construction* and occupied in whole or in part for residential purposes and containing not less than four dwelling units... *shall be equipped with an approved system of automatic sprinklers* in accordance with the provisions of the state building code.... (emphasis added)

This local option was enacted after a particularly serious fire in Boston when it was determined that a sprinkler system could have prevented loss of life. Previously, only high-rise buildings (buildings over 70 feet), required sprinkler systems, but the new law, if adopted by the locality, requires systems in all newly constructed or substantially rehabilitated buildings.

This law is relatively new and its requirements are still going through the process of being defined by local jurisdictions that have adopted it. Like many laws enacted in response to a single tragic event, it was not thought through. For example, the term “substantially rehabilitated” harkens back to the old definition of rehab used when the “25–50 percent rule” applied rather than the more flexible standards of Article 34.

The interpretation of the highlighted portion of the excerpt above also has significant implications as to the use of a sprinkler system as a component of a compliance alternative in residential buildings. The fear is that if code officials take a position that sprinklers are now required, no compliance alternative credit can be taken under Article 34 (DeMarco 1995). The law or its regulations should be clarified to continue the relief allowed for compliance alternatives in conjunction with the installation of sprinkler systems, notwithstanding the new general mandates for such systems.

Other anomalies have resulted from the new sprinkler law. Since it applies to any residential building of four or more units, code officials are applying the law to row houses. Such dwellings are usually designed with fire-wall separations, making these structures the functional equivalents of one- or two-family homes. The law was so poorly conceived and drafted, however, that code officials also believe that sprinklers are mandated for this common building type. Here again, the law should be clarified or row houses (new or rehabilitated) may become cost prohibitive.

One additional comment about the interplay between the building code and fire code is that the extensive systems being required for public safety (e.g., alarms) may start to become counterproductive. The cost implications are considerable and often make the difference between whether or not a building can be built or rehabilitated. An existing building is usually less safe than once renovated to updated standards, so the net level of public safety may be actually compromised if rehab is postponed. In addition to first costs, the systems are also very expensive to maintain, given annual or more frequent testing. There also is evidence that these systems have become so complicated that neither the public nor private parties charged with operating them have the expertise to do so, resulting in false alarms and other malfunctions that could actually compromise safety. There is anecdotal evidence that even firefighters responding to an emergency have thrown the wrong switches in a complex fire-safety electronics panel, actually exacerbating the problem at hand. Fire-safety systems need to be user-friendly.

Another type of project that requires effective coordination between the fire and building departments is construction of and addition to an existing building and modifications to the existing building. The extent of code compliance for new construction related to the existing portion of the project often needs definition.

## **Building Code Appeals**

The decisions of a local code official may be appealed to the MBBRS, but the appeals process is often misunderstood. While only a few jurisdictions have a local appeals board, it is not necessary to go before the local board prior to appealing before the state board. It is also assumed by many that the process is lengthy, but the MBBRS believes that it can handle appeals in a relatively short time frame (usually in less than 30 days). Furthermore, design professionals frequently express a concern that appeals will be viewed as adversarial actions and political capital will be expended in pursuing an appeal.

In fact, the appeals process can be handled both expeditiously and noncontroversially. As previously explained, local officials understandably tend to be conservative in their administration of the code; they do not wish to exceed their authority or to compromise public safety, and they prefer prescriptive rules over value judgments. Nonetheless, they also tend to be practical people who recognize that it may not be possible to exactly comply with all code requirements, especially when a project involves an existing building. Therefore, the official may be open to compliance alternatives under Article 34, but may be looking for secondary support for such a decision.

In this context, it is often helpful to approach the issues in a matter-of-fact way, documenting current conditions and compliance alternatives. Reference to other successful interpretations (e.g., priorly approved compliance alternatives) that support the pending case are helpful to build confidence. If the local official is willing to sign off on the compliance alternatives, terrific. But, if not, the next step should be to suggest that the matter be referred to the MBBRS on appeal to clarify the situation. If the discussions have been properly handled on a nonconfrontational basis, the official should welcome this step and be willing to take a positive or at least neutral position; i.e., he or she should not be opposed to the appeal.

Once appealed to the MBBRS, the compliance alternative can be resolved on its merits. If the alternative suggested is common, this process sometimes will not even require a hearing. This appeal process becomes a win-win: the proponent is relieved of a strict code compliance that would unduly burden the undertaking, and the code official can accommodate reasonable requests for compliance alternatives without risking a potentially controversial code interpretation. However, the key for the development team is to avoid adversarial actions that could cause the local official to be opposed to the appeal; the MBBRS is likely to err on the side of its code constituents in the event of a dispute.

Although less frequently employed, decisions of the fire marshal may also be appealed to the MBBRS under the NFPA regulations, which are part of the state building code. Such appeals are less frequent because the fire marshal is less prone to compromise—again waving the pre-eminent banner of public safety. In this case, the process is more likely to be adversarial and end in failure. Nonetheless, appeals of NFPA issues are possible, with the support of local marshals, in the case of narrower code interpretations where, perhaps, there is a conflict in the code or some acceptable alternative that is not clearly prescriptive. (For example, NFPA calls for standpipe systems to be equipped with a testing system that, if literally interpreted, requires a second redundant system for semiannual tests where, in fact, a reduction valve and garden hose

will often suffice.) In these cases, the fire marshal will sometimes accede to an appeal without prejudice. Again, such appeals for purpose of clarification are viewed as healthy for all parties.

### **Seismic Requirements of Article 34**

In Massachusetts, Article 34 (section 3208 and cross-referenced sections from 1113.0—Earthquake Loads) governs seismic requirements for existing buildings undergoing rehab. It is instructive to compare the original seismic requirements with the new standards incorporated into Article 34 in 1995.

The original seismic standards follow the scale related to change in use and the hazard index of Article 34:

1. If there is no change in use and no increase (or decrease) in the building's hazard index, there are no specific seismic requirements.
2. If there is a change in use and the hazard index increases by one, the original Article 34 requires only that the building's lateral load resistance not be reduced.
3. If there is a change in use and the hazard index increases by two or more, the original Article 34 requires that the existing building meet the seismic requirements for new construction.

As noted in one report, there were problems with all three of the above scenarios:

Scenario 1—Where there was no increase (or decrease) in the hazard index, it was permissible to *reduce* the building's lateral load resistance. Walls, for example, could be removed. While these walls were not designed to provide lateral load resistance, they had some capacity to do so. Was it, therefore, wise to allow the removal of such a building element?

Scenario 2—Where a change of use increased the hazard index by one, the original Article 34 merely stated that the building's lateral load should be kept at the status quo. In reality, this standard was liberally interpreted and there was some question whether "liberal" equates with safe.

Scenario 3—Where a change in use increased the hazard index by two, the original Article 34 required that the property meet new construction seismic standards. This was impractical, or, at best, difficult to achieve. For instance, section 1113.4 of the Massachusetts Building Code, which covered seismic design, was specifically limited to structures meeting certain ductility requirements set out in section 1113.5 (Boston. With specific requirements for reinforced concrete, and the requirement for masonry to be reinforced, these provisions were rarely met on structures designed prior to the introduction of seismic standards into the Code in 1975. In these instances, a variance was sought—but relying on a variance was far from an optimal approach. (Boston Building Consultants 1994)

The new seismic design provisions of section 3208 attempt to correct these problems by considering a building's seismic hazard *separately* from its fire hazard and by providing detailed guidelines for buildings that do not meet the ductility requirements of section 1113.5.

The major difference between the original and new Article 34 with respect to seismic standards is that the design decision process is now based on *factors specifically relevant to seismic design* rather than on factors relevant to fire hazard. The severity of the seismic requirements under the new Article 34 depends on several considerations (Boston Building Consultants 1994):

- Whether the cost of alterations exceeds 50 percent of the building's assessed value.
- Whether the occupancy is increased by more than 25 percent. This is considered only if the new occupancy is more than 100.
- Change of use of the building, based on the hazard index. This was previously the only deciding factor. It is now much reduced in importance and, in effect, applies only when a building changes to assembly-type use.
- Buildings with additions are subject to rules based on the addition's scale relative to the existing building. Allowing structurally separate additions to be considered as separate buildings both simplifies the design work and encourages sound seismic design.
- Whatever other considerations apply, alterations to elements of a lateral load system must be justified by analysis.

The new provisions still require the design to conform with the code for new construction in many cases, but they usually allow a modified K value to be used for buildings that do not meet the ductility requirements. A lower-level requirement is to correct special earthquake hazards—parapets, unrestrained masonry walls, and connections of structural, precast concrete elements.

It is worth noting that the only circumstance in which full compliance with the code for new construction, including ductility, is required is for a structurally attached addition larger (in weight or area) than the original building.

A study that examined the original and the new seismic requirements and conducted five case studies concluded the following (MBBRS 1994b):

- The new provisions effectively achieve the aim of reducing the risk of loss of life by concentrating on specific areas of high risk due to seismic weakness or specific occupancy.
- The new provisions for most applications remove the unreasonable requirement to design (existing) buildings to meet the code for new construction.
- The new provisions are clearer and much more specific than the original provisions.
- The new provisions will increase both design and construction costs by a small amount.

- In four of the five buildings studied, the total cost of lateral-load retrofit work under the new provisions was 3 percent or less of the total construction cost. In the fifth building, 12 percent of the total construction cost was associated with lateral load retrofit, but this work was already required by existing code provisions. Additionally, this fifth building was seismically very weak.
- The majority of buildings will incur additional construction costs of 1 percent over present costs without the new regulations in place.
- Design fees will increase between 10 percent and 25 percent under the new provisions, depending on the project's overall size.

### *Seismic Peer Review*

Note also that, under the building code, seismic requirements may help to trigger a structural peer review. Such reviews are required by section 110.11 of the code (sixth edition) under the circumstances described below:

As a condition for the issuance of a building permit, the structural design of the following described structures shall be reviewed by an independent structural engineer to verify that the design of the primary structure is conceptually correct and that there are no major errors in the design:

1. Buildings that are five stories or more in *height* above the lowest floor, including stories below grade.
2. Buildings that enclose a total volume of 400,000 cubic feet, including stories below grade. The volume shall be measured using the outside dimensions of the *building*.
2. Structures in *Use Group A*, or structures that are partially in *Use Group A*, which will be used for public assembly of 300 or more persons.
4. Structures of unusual complexity or design shall be determined by the MBBRS. A building official may apply to the MBBRS for such a determination on a specific structure. (MBBRS 1994b)

None of these thresholds are specific to seismic design issues. In practice, however, the new seismic standards have building officials worried: the new standards are relatively complex, so peer reviews are sometimes called for when similar situations resulted in routine waivers in the past. Test #2, for example, establishes a threshold of 400,000 cubic feet—roughly, a building footprint of 100 feet x 100 feet and 40 feet high. Such a building might be four stories of new construction but only three stories (or less) with higher floor-to-floor heights in an existing building. In the past, peer reviews were waived for larger existing buildings if they were not substantially altered or enlarged, but now seismic requirements have more frequently triggered reviews.

The above said, peer reviews add only modest costs and delays (although each extra cost for code compliance adds up). If a review is required for an existing or historic building, it is essential to select a structural engineering peer who is experienced with adaptive reuse. If the peer attempts to apply new construction standards to the existing structure, chances are it will not comply. Particularly troublesome in states like Massachusetts are issues regarding masonry walls, both bearing and nonbearing, which cannot fully meet ductility requirements without prohibitively costly retrofits.

This completes our analysis of Article 34. We now briefly examine other provisions (access and historic preservation) that bear on rehab in Massachusetts. While these provisions are distinct from Article 34, they sometimes affect its implementation.

### **ACCESS REGULATIONS**

Massachusetts General Law, chapter 22, section 13A, mandates rules and regulations for handicapped accessibility and establishes the Architectural Access Board (AB). The state's rules and regulations are also different and more restrictive than the requirements of ANSI A-117.1, the Americans with Disabilities Act, and the Fair Housing Amendment. Exhibit 6.2 compares the federal and Massachusetts state requirements for selected components (primarily aimed at residential occupancy).

**EXHIBIT 6.2**  
**Comparison of Accessibility Regulations:**  
**Federal Guidelines Compared with Massachusetts State Guidelines**

<b>Building Component</b>	<b>Federal Guidelines</b>	<b>Massachusetts State Guidelines</b>
(1) Enforcement		
-Regulations	Guidelines or “safe harbor” only; alternatives allowable by builders	Absolute requirements; advance variances required for any deviations
-Compliance	“After the fact” upon action by the aggrieved party	“Before the fact” by a building official or the AAB; also after completion by any party
(2) Applicability		
-General	4 or more units	3 or more units
-Existing buildings	Exempt	Exempt (except for Group 2 units)
-Elevator buildings	All units	All units
-Walk-up buildings	Ground floor (or at least 20 percent if otherwise impractical)	Ground floor (no exceptions, including second floor if commercial/parking on the ground floor)
-Townhouses	Exempt	Reserved (no regulations except Group 2A compliance)
-Duplexes/lofts	Exempt (provided the entry level complies)	Not specified
(3) Public Spaces		
-Entrances	At least one accessible entrance (unless impractical due to terrain)	All primary public entrances must be accessible and on an accessible route (no impracticability exceptions)
-Common areas	All common spaces and facilities accessible (except only a reasonable selection if otherwise impractical)	All common spaces and facilities accessible (no exceptions)
-Laundries	No restrictions (provided assistive devices are available)	No front-loading machines; no stacked washers/dryers unless capable of replacement
(4) Passageways		
-Public areas	ANSI standards (typically 3' 0" clear)	3'-0" door providing 34" nominal opening
-Dwelling units	2' 10" door providing 32" nominal opening	3'-0" door providing 34" nominal opening
-Thresholds	3/4" maximum threshold; 1/2" maximum drop from interior floor level to exterior grade (except 4" if impervious or as required by local code)	1/2" maximum threshold; 1/2" maximum drop from interior floor level to exterior grade (except 4" if impervious and capable of retrofitting)
(5) Controls		
-Switches and outlets	15" to 48" above floor (reduced if overhang)	15" to 48" above floor
-Thermostats and intercoms	Same as switches (but with flexibility to relocate)	36" to 48" above floor (or relocatable)
-Circuit breakers	Not applicable	36" to 48" above floor
(6) Bedrooms		
-Primary	No requirements	Minimum of 10' x 13' for furnishing and maneuvering
-Secondary	No requirements	Minimum of 10' x 11' for furnishing and maneuvering



Note in particular that federal rules provide “safe harbor” guidelines but also allow compliance alternatives; the state rules and regulations prescribe absolute requirements. The federal rules also provide enforcement in the event of a specific complaint; the state rules require an affirmative sign-off in advance by building code officials as well as enforcement due to subsequent complaints.

Although the local building official is responsible for enforcement under the AAB, the state accessibility rules and regulations constitute a wholly separate code that is not otherwise part of the state building code. Hence, Article 34 alternative compliance procedures do not apply. Furthermore, there is no regular appeals process to the MBBRS; any requests for variances must be made to the AAB. Considerable delays are reported in bringing matters before the AAB and in receiving their official response. One official stated:

Triggering involvement with the Architectural Access Board will generate a minimum of three months delay in a project. There is little room to negotiate and this is preventing some rehab from proceeding. (Fanning 1995)

Part of the problem is that each case has to be heard, even though similar cases may have established a clear precedent; i.e., there are no administrative waivers or clarifications, even for drafting errors in the AAB code. Clearly, the process should be streamlined, or the code should be updated for clarifications and standard practice more frequently.

Thus, the local building inspector is charged with enforcing the AAB code, but he or she has little discretion in its administration. Moreover, there are requirements of the building code that conflict with the requirements of the accessibility regulations. There are also triggers in the accessibility regulations that relate to the amount of money being spent on the project (\$100,000 threshold) and rehab expense related to the value of the building (30 percent threshold). Article 34 specifically eliminated such value triggers with respect to standards to be met for rehab. There are, however, activities (e.g., ordinary repairs) exempt from the access requirements, and historic properties receive at least passing mention as deserving of special attention.

The overriding issue with the AAB is the extent to which access should be mandated, especially in the context of existing or historic buildings. The current perspective is one of entitlement, namely that handicapped and disabled people are due redress and are absolutely entitled to all of the prescriptions in the code. This single-issue focus also provides little room for compromise when the AAB code conflicts with other building code provisions or with existing conditions in older or historic buildings. If the AAB calls for clear passageways of 36 inches but an existing hallway is only 35 inches wide and bounded by a structural wall, the access mandate may be to tear out the wall and widen the passage by 1 inch. If a three-story building has a ground floor storefront with two apartments on the floors above, then an elevator may be required, even though the \$50,000 cost is prohibitive and means that the building is not likely to be rehabilitated. Or, if a decorative light fixture is less than seven feet off the access path but projects more than 4 inches, the historic fixture may be required to be moved, even though it presents no real obstruction or hazard.

This attitude is further exacerbated by the means by which alleged infractions of the AAB code are enforced. A number of “code spotters” have been trained (or self-appointed) to ferret out even the most minor of technical lapses. These people, while well-intentioned, exhibit no practical sense of what it takes to build or, especially, to rehabilitate a building. Rather, they measure each detail down to the fraction of an inch and then file voluminous complaints with the AAB, all of which have to be answered. They also intimidate local building officials and threaten action for allowing code violations. Code officials are often sympathetic with the position of the owner or architect, but they also feel they cannot give any leeway in the face of potentially adverse publicity that their department appears not to support the letter-of-the-law as to handicapped accessibility.

The result is that existing buildings that could be rehabilitated are not because the AAB regulations cannot be reasonably met. (The example, give above, of the main street retail stores with residential apartments provides a classic case in point.) While providing access is an important social goal and has been long overdue, its implementation in Massachusetts has sometimes turned into a nightmare of compliance, which many now address by the most literal means possible—even where better compliance alternatives could be considered. Since the AAB is relatively unapproachable and uncompromising, many professionals do not seek variances in advance, but rather design to their best understanding of the regulations and then seek appeals after the fact if required, knowing that there will be complaints filed anyway.

In the best of all worlds, the AAB rules and regulations should be incorporated as a subset into the state building code. The political reality, however, is that no one is likely to take on this emotional issue of the access mandate. In the least, however, the concept of compliance alternatives provided by Article 34 should be allowed under the AAB process, and any requests for variances or appeals of advance decisions should be accelerated to reduce the currently unacceptable 90-day wait.

## **HISTORIC BUILDINGS**

In Massachusetts, the building code regulations effected on the historic stock is separately governed by section 635 of the Massachusetts Building Code.<sup>4</sup>

In brief, section 635, as it was enforced from the late 1970s to 1994, applied to properties individually listed on the National Register of Historic Places or “contributing buildings” in a National Register district. (A “contributing building” is a property significant to the fabric and integrity of the district.) Historic properties under Article 635 were further classified into one of two groups: totally preserved and partially preserved. The totally preserved properties were of museum quality and had to be open to the public for a given minimum number of days (12) per year. Additional uses, original or ancillary to the principal use, were permitted, and the property still qualified as totally preserved if the additional use did not exceed 25 percent of the total gross floor area. The buildings that qualified as totally preserved were individually listed in an appendix to the Massachusetts State Code and numbered about 125 properties statewide. All other historic buildings that were not totally preserved were considered partially preserved.

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<sup>4</sup>As originally adopted, the historic standards in the Massachusetts State Code were found in section 436. This was renumbered to section 635 in 1987.

In parallel to the sliding-scale requirements of Article 34, section 635 had different standards for different categories of historic properties. Rehab of a totally preserved building had to meet *minimal* requirements, including the following:

1. Installation of manual fire extinguishers and automatic fire warning systems.
2. Installation of exit signs and emergency lights.
3. Limitation of occupancy to the level that could be accommodated by the structural floor level with a further consideration of limiting occupancy for properties with just one means of egress.

Other than these very basic requirements, other provisions were not required when the museum-like, totally preserved buildings were rehabilitated. For the partially preserved buildings, however, the full provisions of Article 34 governed. That is, the historic, partially preserved properties had to meet the same requirements imposed on all existing buildings under Article 34.

That was section 635 as it existed for almost two decades (1977 to 1994). That original section 635 was changed with the new section 635 provisions (Holtz 1995).

### **Section 635 Eligibility**

As described above, historic properties under the original section 635 were limited to the following:

1. Properties individually listed in the National Register of Historic Places
2. Contributing buildings in National Register Districts

Under the new section 635, the definition of historic is expanded to include the following:

3. Properties in *locally* designated historic districts—if these districts meet National Register District criteria
4. Any building not yet on the National Register but *individually eligible* for inclusion in the National Register

These additions to eligibility are quite significant. Group 3 above encompasses the historic identification of local districts, since many historic properties are not suitable for federal designation on the National Register yet qualify as local landmarks. Group 4 includes as historic the many properties that have not gone through the official process of nomination or acceptance to the National Register yet have features that make them *eligible* for such listing.

The inclusion of groups 3 and 4 significantly adds to the building stock considered historic under section 635. The Massachusetts State Historic Preservation Office (SHPO) estimates that groups 1 and 2 above—the historic stock encompassed in the original section 635—amount to about

50,000 buildings. The SHPO estimates that groups 3 and 4 together add almost 500,000 more buildings statewide to the historic stock for the purposes of the new section 635—a tenfold increase (Holtz 1995).

As with the original section 635, the new Section 635 continues the two-tier declension of totally preserved and partially preserved buildings. Thus, the totally preserved buildings are the museum-quality properties open to the public for at least 12 days each year. One change, however, is that additional uses up to 40 percent, as opposed to the old 25 percent, of gross floor area are permitted in the totally preserved buildings. All other historic buildings not classified as totally preserved fall into the partially preserved category.

### **Section 635 Standards**

The building rehab requirements for the totally preserved group remain as before. As described earlier, these are limited to such basic items as installing fire exit signs, emergency lights and manual extinguishers, and limiting occupancy to safe levels.

There is a change, however, with respect to the partially preserved stock. Under the original section 635, the full requirements of Article 34 governed. Under the new section 635, exceptions to the state building code are allowed for certain features that contribute to the property's historic distinctiveness. These are noted in a new section 635.5.2, as follows:

635.5.2 State Building Code exceptions: A partially preserved building shall be subject to the following exceptions: Repairs or in-kind replacement of the following features will be allowed on partially preserved buildings so as not to compromise the architectural integrity of the historical characteristics and qualities which contributed to the eligibility for listing in the National Register of Historic Places.

1. Roofing—repair or in-kind replacement of an existing historic roof system (i.e., slate, wood, clay tile, metal) shall be permitted without requiring structural compliance for equivalent new construction as long as dead and live loading requirements have not changed.
2. Windows—repair or in-kind replacement of existing historic windows (i.e., frames, sash, muntins, glazing, sills, molding, shutters) shall be permitted without requiring energy code compliance. (See Section 32.07.)
3. Entries/Porches—repair or in-kind replacement of existing individual decorative features of an existing system (i.e., columns, balustrades, stairs, pilasters, doors, sidelights) shall be permitted. (See Section 635.1; 1,2.)
4. Wood Siding/Decorative Elements—Repair or in-kind replacement of an existing system including such items as clapboards, shingles, cornices, brackets, and window and door surrounds shall be permitted. (See Section 635.5.1; 1,2.)

5. Masonry—repair or in-kind replacement of masonry units as part of an existing system (i.e., brick, stone, terra cotta, concrete, and stucco) shall be permitted. (See Section 635.1; 1,2.)
6. Metals—repair or in-kind replacement of existing architectural metals (i.e., cast and wrought iron, steel, tin, copper and copper alloys, aluminum, zinc) shall be permitted. (See Section 635.1; 1,2.)
7. Interior features—repair or in-kind replacement of nonstructural interior features that are important in defining the overall historic character of a building (i.e., columns, cornices, baseboards, fireplace mantels, paneling, window trim, doors, moldings, railings, flooring, plasterwork) shall be permitted. (See Section 635.5.1; 1,2.)

An example of the application of the original compared with the new section 635 follows.

On Commonwealth Avenue in Oak Bluffs, Massachusetts, there is a camp meeting property built in 1871. The property has classic period features such as double northern gothic doors, cut shingles, and decorative railings. This building was not on the National Register, so under the original section 635, it was not considered historic. The property was being rehabilitated and an issue arose concerning its second-story porch railings. These railings were 20 inches in height; 40 inches were required for new construction. The owner was able to drop the floor in the second-story porch, thus mitigating the issue of the low railing. This approach was approved through a variance granted by the code official.

Under the new section 635, there would be direct support for allowing the low railing. This camp building was on a local historic register, so it would qualify as a partially preserved building. Section 635.5.2 would exempt the property from meeting the standard railing height since this was an “existing individual decorative feature of an existing (porch) system” (Section 635.5.2.3.) in a partially preserved building.

The Oak Bluffs example shows how the new section 635 can facilitate the rehab of Massachusetts historic properties.

### **Secretary of the Interior’s Standards**

Historic properties are sometimes bound by design requirements that are independent of the state building code. Examples include properties that are subject to various historic covenants or controls and/or that may use state or federal funding sources (e.g., properties using federal historic rehab tax credits [HRTC]). Properties utilizing the HRTC, for instance, must also meet the Secretary of the Interior’s Standards for Rehabilitation (hereinafter the Standards). The Standards comprise very useful guidelines which are aimed at ensuring that the historic integrity of the building components are properly preserved.

1. A property shall be used for its historic purpose or be placed in a new use that requires minimal change to the defining characteristics of the building and its site and environment.

2. The historic character of a property shall be retained and preserved. The removal of historic materials or alteration of features and spaces that characterize a property shall be avoided.
3. Each property shall be recognized as a physical record of its time, place, and use. Changes that create a false sense of historical development, such as adding conjectural features or architectural elements from other buildings, shall not be undertaken.
4. Most properties change over time; those changes that have acquired historic significance in their own right shall be retained and preserved.
5. Distinctive features, finishes, and construction techniques or examples of craftsmanship that characterize a historic property shall be preserved.
6. Deteriorated historic features shall be repaired rather than replaced. Where the severity of deterioration requires replacement of a distinctive feature, the new feature shall match the old in design, color, texture, and other visual qualities and, where possible, materials. Replacement of missing features shall be substantiated by documentary, physical, or pictorial evidence.
7. Chemical or physical treatments, such as sandblasting, that cause damage to historic materials shall not be used. The surface cleaning of structures, if appropriate, shall be undertaken using the gentlest means possible.
8. Significant archeological resources affected by a project shall be protected and preserved. If such resources must be disturbed, mitigation measures shall be undertaken.
9. New additions, exterior alterations, or related new construction shall not destroy historic materials that characterize the property. The new work shall be differentiated from the old and shall be compatible with the massing, size, scale, and architectural features to protect the historic integrity of the property and its environment.
10. New additions and adjacent or related new construction shall be undertaken in such a manner that if removed in the future, the essential form and integrity of the historic property and its environment would be unimpaired.

Note that the above Standards apply to rehab. The SISHP differentiates between recommended treatments for rehab and slightly different and more exacting standards for preservation, restoration, or reconstruction.

The Standards are enforced by the Massachusetts Historical Commission (MHC) and the National Park Service (NPS) on a case-by-case basis. In the overwhelming majority of cases this enforcement has consistently struck a reasonable balance between the perfect and the practical, resulting in a steady volume of preservation and adaptive reuse in the Commonwealth. Yet there

have been issues concerning how flexible versus how “purist” the Standards should be interpreted. Examples of touchstone issues include the following:<sup>5</sup>

- Windows have been an ongoing issue. Few would deny that fenestration is a key component of the historic character of the building. However, the Standards review has sometimes adopted hard and fast positions that do not easily admit to advances in technology. An example is the development of the new low-e glass, which is only marginally different in its appearance from regular glass but which has significantly improved energy performance. The NPS will sometimes disallow low-e glass windows in rehabilitating historic properties.
- Penthouses are often necessary to accommodate equipment for contemporary HVAC requirements of economic reuses. Arguably, placing such equipment in a “temporary” structure on the roof is far preferable to inserting the HVAC within the structure itself, which in turn requires grills or other intake and exhaust devices. However, the Standards review sometimes prohibits such penthouses for buildings of three stories or less and discourages any rooftop additions on most buildings.
- Atria are frequently required to adapt buildings with a larger footprint. For example, an existing retail building might cover an entire city block with dimensions of 150 feet by 300 feet (45,000 square feet per floor). That footprint is not adaptable for housing offices, or for most other uses, without creating an internal courtyard or atrium to introduce light and ventilation on internal facings. Such courtyards and atriums are, by their nature, not visible from the street and when carefully designed otherwise minimize any impact on the historic character of the building. However, the Standards review has all but prohibited the use of atria unless they are covered, which typically eliminates any reuse, such as housing, that requires natural light and ventilation.
- Assembly spaces include auditoriums, church halls, and other places of assembly within larger structures. There is frequently no current use for these spaces as part of an overall adaptive reuse plan. However, the Standards review has been insisting that these assembly spaces be restored to their original purpose, notwithstanding the lack of any demand for such space. Hence, not only are significant extra costs involved but there are also no offsetting revenues. This burden could tip the balance of an economic reuse and discourage rehab of the building.

The MHC and NPS are mandated to carefully consider the Standards in their historic tax credit and other deliberations in order to protect historic resources. These agencies must also be credited for helping foster historic rehab generally. Specifically, these agencies fostered preservation involving affordable housing throughout the United States, as well as in Massachusetts. Furthermore, the NPS is currently taking steps to further the ability of historic preservation to deliver low-income housing, to foster adaptive reuse, and to achieve other

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<sup>5</sup>In each of these categories—windows, rooftop additions, atria, and assembly spaces/auditoriums—there are examples where these treatments have been approved by the National Park Service. Each project has to be seen as individual in style, form, condition, significance, etc. There are also better energy types of glass with lighter tints that the NPS has approved. The NPS maintains that it is generally consistent in its review and discourages major changes to buildings.

socially desirable goals. Yet the NPS and the larger preservation community must be constantly vigilant in reexamining the preservation standards to be applied. If preservationists insist on purist positions or abstract one-size-fits-all directives, then provisions, such as the Standards, may serve as a disincentive and preservation will be discouraged. Significant structures might not be renovated, or they may be renovated to no standard at all. Worse yet, important buildings could be demolished or destroyed through neglect with the excuse that no practical solution was allowed under the interpretation of the Standards or other guidelines.



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## **CHAPTER 7**

### **Rehab Barrier Case Study: Neighborhood Housing Services of New Haven, Inc.**

#### **SUMMARY OF FINDINGS**

Neighborhood Housing Services (NHS) of New Haven, Inc. (hereinafter New Haven NHS, or NHNHS) is a nonprofit housing and community development organization active in New Haven, Connecticut. Since its founding in 1979, New Haven NHS has acquired and rehabilitated nearly 100 houses. This housing is offered for sale to low- and moderate-income (LMI) families. Many of the rehabilitated houses are historic. This feature is a positive market attraction, since distinctive homes with desirable architectural details (e.g., porches and wainscoting) are being made available. At the same time, the properties' historic character raises regulatory issues associated with the Secretary of the Interior's Standards for Rehabilitation. This case study focuses on this regulatory issue, briefly considering other barriers as well.

#### **Economic Constraints**

New Haven NHS's ability to deliver rehabilitated housing to economically disadvantaged households depends on subsidies, yet the subsidies are very competitive and only limited funds are available.

#### **Development Phase Barriers**

##### *Acquisition Properties*

Many NHNHS strategies for acquiring properties pose challenges. Banks often dispose of their mortgage-delinquent properties in bulk, and this volume acquisition is unsuitable to the property-by-property rehab strategy of New Haven NHS. Similarly, the city sells property-tax-delinquent liens in bulk; this potential property acquisition strategy (i.e., buying liens and then foreclosing on them) is also unsuitable for NHNHS. Direct NHNHS purchase of properties offered for sale for private owners is often impracticable because of the exorbitant liens frequently owed on such parcels.

#### **Construction Phase Barriers**

##### *Historic Preservation*

Historic preservation is important to NHNHS's mission of respecting neighborhood character and amenity. Yet NHNHS needs greater flexibility with respect to historic preservation controls in affordable-housing situations. This has sometimes proved problematic. As NHNHS utilizes federal monies, it must, in rehabilitating historic properties, abide by the Secretary of the Interior's Standards for Rehabilitation. Strict interpretation of these standards has sometimes delayed the rehab process or has added to renovation costs (e.g., requiring the installation of wooden windows rather than less expensive vinyl ones). This hurdle is currently being addressed through more flexible interpretation of the Secretary of the Interior's Standards.

### *Other Construction Phase Barriers*

While NHHNS praises the flexibility of New Haven's building code inspectors, it does sometimes encounter problems with requirements of the building code (e.g., required headroom in stairways). Similarly, although satisfying lead- and asbestos-abatement regulations typically is not an issue, there are exceptions.

## **BACKGROUND**

### **New Haven, Connecticut**

New Haven, Connecticut, is a historic city, dating to early colonial times. For the last half-century, it has confronted many socioeconomic and housing challenges. Once a prosperous regional center, the postindustrial economy has not been kind to the community. Its population declined from 152,048 in 1960 to 124,665 in 1996. New Haven's once largely white, middle-class population has long since fled to the suburbs. In 1950, only 6 percent of the city's population was nonwhite. Today the city is heavily minority; according to the 1990 census, 36.1 percent of its residents are black and 13.2 percent are Hispanic. Although it contains affluent neighborhoods, New Haven overall is far from affluent. Its 1989 household income was only \$25,811, and in 1990, 21.3 percent of its population were in poverty. In 1996, the city had an unemployment rate of 7.1 percent.

New Haven's socioeconomic challenges have affected its housing stock. According to the 1990 census, the city contained 48,996 housing units—32 percent ownership and 68 percent rental. The 1990 median value of the owner-occupied units was \$145,000 and median gross monthly rent on the rental units was \$568. By contrast, the respective parallel statistics in the more-advantaged Connecticut sister city of Stamford were \$295,700 and \$794. New Haven's housing stock was old, with almost half (46 percent) built before 1940. The 1990 census reported that 5 percent of the city's housing stock was substandard.

Socioeconomic and housing challenges are especially severe in some of New Haven's older neighborhoods. Illustrative is the Dwight neighborhood, where NHHNS is headquartered and where it has focused its activities.

### **Dwight Neighborhood**

For a period of 200 years, from the time of its settlement in the early 1600s, New Haven's growth was confined to areas immediately adjacent to its harbor (Grzywacz 1999, 13). By the 1820s, growing prosperity led to geographic expansion, with one locus of growth found in the area west of Park Street and north of Oak Street. This neighborhood was ultimately referred to as Dwight, named for its bisecting street which honors Timothy Dwight, a Yale University president from 1795 to 1817 (Grzywacz 1999, 13).

By the 1840s, most of the lots between Dwight's Howe and Park Streets were filled with buildings, most commonly Greek Revival structures. The initial spurt of development and economic activity in this neighborhood lasted till after the Civil War. The industrialization

rampant in New Haven at this time provided jobs in abundance. For instance, by 1860, more than 200 area residents were employed in the carriage trades; most were living on Dwight's Edgewood, Howe, Dwight, and Day Streets. Construction workers, both skilled and unskilled, were attracted to the neighborhood as well.

General population increase caused by New Haven's post-Civil War industrial growth led to increased population density in Dwight and other city neighborhoods. Many Dwight prewar single-family houses were subdivided, and a new type of house—two- (and later three-) family—became very common. The many style variations, from late Italianate through Queen Anne to Shingle, were built right up through the 1920s. The pattern of Dwight's development in this period was for an individual builder to erect two or three houses on adjacent lots, a pattern that explains the small groupings of nearly identical houses that characterize New Haven.

In the post-Civil War era, Dwight's residents spanned the economic spectrum. While small local tradesmen predominated, the neighborhood also attracted wealthier manufacturers and professionals. Dwight's housing stock ranged from modestly scaled homes with few decorative details to more substantial houses showing the characteristics of their Victorian era with elaborate size and decorative attachments. The earlier homes, in the Greek Revival style, tended to be smaller and more modest. The largest homes date from the late nineteenth century to the 1920s and were often Queen Anne and Neoclassic Revival in style. The whole range of Victorian "revival" styles can be found in Dwight, with some Gothic Revival structures, numerous French mansard buildings, and many with a combination of eclectic features.

Up until the later part of the nineteenth century, Dwight was ethnically almost totally "Yankee." The Jewish community was the first large ethnic group to live in Dwight; Polish and Italian immigrants started moving in after 1900. Blacks lived in this neighborhood from early in the nineteenth century, though as individuals rather than as a significant percentage of the population. The increased demands for housing by Dwight's ethnic groups led to the growth of triple-deckers, and ultimately to tenements with up to six units.

Despite the lengthy time period of its development, and the divergent styles emerging in Dwight, certain common characteristics were retained in many of the neighborhood's streets. Uniform building setbacks are typical throughout the Dwight neighborhood, providing a consistent and uninterrupted rhythm to the streetscape. The regularity of the neighborhood is accentuated by the small front yards and by the tree spacing that was utilized in this area. The unifying rhythm characteristic of both structures and landscaping is a recurring theme throughout Dwight, distinguishing the neighborhood from nearby areas that have not retained this harmonious streetscape and housing character. These amenities were recognized when the Dwight neighborhood was placed on the National Register of Historic Places in 1983.

Historic designation alone could not preserve Dwight. As New Haven's fortune waned in the post-World War II era, so did housing and social conditions in Dwight. Dwight's historic homes were often unappreciated and some were demolished. When repairs or alternations were made, many of the historic characteristics of the homes were done away with or obscured. The removal or revamping of porches and the re-siding of buildings with aluminum siding that obscured the wooden details in the structures were typical. Additionally, windows and doors were often

inappropriately replaced. The loss of these unique features had a negative visual impact on the community.

In part, these developments reflected social changes. The “white flight” to the suburbs of the postwar period drained Dwight of its most educated and affluent members. The large number of homes available for sale kept prices low. This discouraged investment, as people did not expect to recoup any investment in their properties. Additionally, the new home buyers were often financially strapped, unable to do the maintenance and repairs needed to keep up their homes.

The deteriorating housing attracted speculators, who turned many of the larger residences into illegal multifamily buildings, significantly increasing the population on many blocks and attracting people with even lesser incomes and many social problems into the area. The 1970s and 1980s saw a worsening drug situation and increased gang activity in the community.

A speculative increase in property values in the 1980s provided a short respite for New Haven and Dwight, but ultimately gave way to increased deterioration and neglect in the 1990s. Properties had been increasing in value about 15 percent annually from 1982 to 1987. This rise in appreciation attracted speculators, who often bought Dwight and other New Haven properties for capital gains purposes. When the real estate market crashed in the late 1980s and early 1990s, the speculators were unwilling to continue carrying the operating losses that were common for these houses and ceased maintaining their properties. Many historic and once attractive properties in Dwight (and elsewhere in New Haven) were abandoned.

Poorly maintained and abandoned properties had a chilling effect on Dwight. New homeowners were discouraged and existing owners disinvested. Crime and other social problems increased as the neighborhood began to take on the appearance of a slum. The mission of the New Haven NHS is to stem this cycle of deterioration and to encourage reinvestment.

### **New Haven NHS**

NHNHS is affiliated with the Neighborhood Reinvestment Corporation (NRC). In 1978, Congress enacted a law that created the NRC, a national nonprofit organization with a mandate to revitalize America’s older, distressed communities. NRC creates and supports local nonprofit organizations across the country through its Neighbor Works<sup>®</sup> network. Local Neighbor Works<sup>®</sup> affiliates are private, not-for-profit organizations governed by boards of directors that are chaired by neighborhood residents and include local government officials and private-sector representatives. Provision is also made for secondary market sale of Neighbor Works<sup>®</sup> loans.

Today there are almost 200 Neighbor Works<sup>®</sup> affiliates, located in large cities and rural communities. Each of these organizations, like NHNHS, is autonomous.

Because homeownership is so crucial in achieving stability in distressed areas, the NRC created a national campaign to make homeownership a reality for more lower-income people. Full-Cycle Lending<sup>™</sup> was developed as a part of this campaign. Full-Cycle Lending<sup>™</sup> encompasses multiple linked steps, including neighborhood organization partnership building (e.g., bringing together residents, businesses, and local government leaders), offering prepurchase home buyer

education, making available flexible loan products, and offering other services such as postpurchase counseling.

New Haven NHS, as an affiliate of NRC, implements Full-Cycle Lending™ and other strategies to help revitalize the city's neighborhoods, including Dwight and its environs (e.g., the adjoining Beaver Hill and Dixwell areas). NHHNS was founded in October 1979 as a private nonprofit organization through which neighborhood residents, property owners, and others could improve homes and the environment. Neighborhood residents serve on NHHNS's board of directors. The City of New Haven assists NHHNS by serving on the board of directors, providing code enforcement activities, and offering financial assistance. The private sector is represented through the participation of such lenders as Fleet Bank and the New Haven Savings Bank.

NHS of New Haven currently operates with a staff of five: an executive director, a project manager, a rehab specialist, an administrative assistant, and a community relations coordinator. It has an annual budget (total revenues) of about \$2.0 million. NHHNS implements numerous strategies to realize the goals of neighborhood social and physical improvement. Examples include community organizing and infill new construction. For instance, NHHNS has organized tenants in New Haven's public housing projects. Drawing upon federal urban development action grants (UDAG), Community Development Block Grants (CDGB), and assistance from the Connecticut Housing Finance Authority, the organization built infill new town houses in the Baldwin Court, Scranton Street, and other projects.

Another critical activity of NHHNS is the rehab and sale of the historic housing stock in Dwight and its sister neighborhoods. It has completed about 100 such rehabs. Illustrative is the historic restoration of 43 Beers Street, a property constructed in 1857. Over time, physical changes were made to the house. The tower was probably added in the 1870s, along with Italianate features which embellished the original Greek Revival design. The three bay windows on the south side and the north wing addition may have been added in the 1880s, providing Victorian stick elements. The rear of the house received a one-story addition around the turn of the century. By the mid-1980s, however, 43 Beers Street was totally dilapidated.

The rehab of 43 Beers Street by NHHNS respected the property's architectural history. Replicated brackets were installed; fish-scale shingles were set on the gable; and porch railing and trim work were carefully reproduced. The charming single-family home at 43 Beers Street restored by NHHNS saved a piece of history while strengthening the character and fabric of the Dwight neighborhood.

As illustrated in the above example, New Haven NHS has been sensitive to historic character in its rehab. Despite this, it ran afoul of historic preservation regulations—an issue we turn to after considering other barriers encountered by NHHNS in effecting affordable rehab.

**ECONOMIC CONSTRAINT BARRIERS  
TO AFFORDABLE-HOUSING REHAB**

At the current time, NHNHS typically (there are wide variations) incurs the following costs in acquiring and rehabilitating properties:

<u>Component</u>	<u>Cost Range</u>	<u>Cost Midpoint</u>
Property acquisition	\$15,000–\$20,000	\$17,500
Hard construction costs	\$115,000–\$135,000	\$125,000
Soft costs	<u>\$20,000–\$30,000</u>	<u>\$25,000</u>
	\$150,000–\$185,000	\$167,500

The costs cited above deliver a house containing, on average, 3,500 to 4,000 square feet. (By point of comparison, NHNHS notes that new construction of a similar-sized house would cost at least \$250,000.) The rehabilitated homes almost always include two units: a large (four- to six-bedroom) unit is available to the homeowner and a smaller unit is rented for approximately \$600 monthly.

NHNHS sells the rehabilitated homes to low- and moderate-income (LMI) families earning approximately \$30,000 to \$35,000 annually. Unaided, even with income from the rental apartment, there is no way households with such constrained earnings could afford a home costing about \$170,000. The gap between what can be afforded by the LMI family and the costs of property acquisition and rehab is made up through subsidies from various sources, including the following:

1. *State of Connecticut.* As an example, Connecticut offers state housing tax credits for LMI housing.
2. *Federal government.* NHNHS and its clientele have been aided by such federal programs as HOME and CDBG and, in the past, UDAG and other funds.
3. *City of New Haven* has assisted NHNHS by offering it monies from local and federal flow-through sources (e.g., UDAG).
4. *Lenders.* With the assistance of the Federal Home Loan Banks of Boston and San Francisco and local/regional lenders, LMI owner-occupants aided by NHNHS can obtain financing for the purchase of NHNHS homes at below-market interest rates. In addition, the prospective buyers’ income requirements are far lower than would be acceptable with traditional underwriting, and there are other underwriting flexibilities.

The above subsidies are often combined and “layered.” With the state housing tax credit, NHNHS may write down the sales price of the rehabilitated unit (costing around \$170,000) to \$135,000. Additionally, the purchaser often acquires a “soft” second mortgage (a mortgage with little or no payment obligations) of from \$15,000 to \$30,000. The effective cost to the purchaser is therefore not NHNHS’s expense of almost \$170,000, but as low as about \$100,000. The principal, interest, taxes, and insurance (PITI) cost on such a home is approximately \$1,000 to



\$1,200 monthly—an amount further reduced by the roughly \$600 monthly income from the rental apartment. Thus, many subsidies enable LMI families to acquire the homes rehabilitated by NHHNS.

The competition for housing subsidies, however, is very intense. Take, for instance, the Connecticut state housing tax credit that NHHNS utilizes to writedown about \$25,000 to \$30,000 per unit. In the entire state of Connecticut, only \$1 million annually is available for such credits. Nonprofits competitively apply for allocations from this modest statewide pool and few succeed. To date, NHHNS has been very successful in this area, securing about \$300,000 yearly from the \$1 million total, but there are limitations. First, the \$300,000 allocation limits the writedown to about ten houses per year. Second, NHHNS has kept its dollar request for tax credits constant, despite rising rehab costs. It has done this fearing that if it asked for more than \$300,000—already a large share of the \$1 million statewide total—its application could very well be rejected outright. (Requests for funds are either accepted or denied in totality.) Third, NHHNS acknowledges that while it has been successful in the past in garnering state housing tax credits, it surely has no lock on these funds. Were NHHNS cut off from state tax credits, and the many other subsidies enabling LMI homeownership, the organization’s rehab efforts would be in jeopardy.

## **DEVELOPMENT PHASE BARRIERS TO AFFORDABLE-HOUSING REHAB**

On a “typical” rehab project, NHHNS currently pays about \$10,000 to \$20,000 for property acquisition. In years past, property costs were even lower, about \$5,000 to \$10,000 of the roughly \$150,000 to \$170,000 total project expenditure. Because NHHNS can expend only a modest sum for property acquisition, its acquisition strategy is limited. In addition to its need to economize, other considerations color NHHNS’s selection of property acquisition approaches.

### **Obtaining Properties**

NHHNS’s options for property acquisition include purchase from banks, purchase of property tax liens, purchase from private owners, and FHA foreclosures. Each of these approaches offers advantages and disadvantages.

#### *Purchase from Banks*

After the collapse of the New Haven speculative real estate boom in the 1980s, many speculator purchasers ceased making regular mortgage payments. In theory, banks would foreclose on these properties and NHHNS could acquire the foreclosed parcels from the lenders. In a variation of this, NHHNS could purchase the “bad loans” from the banks at a discount and could initiate foreclosure proceedings on its own.

While NHHNS has acquired some properties in the manner described above, bank property acquisition is problematical. First, lenders sometimes hesitate to foreclose on even nonperforming loans because they fear the liability of owning marginal urban properties. Second, rather than foreclosing, lenders prefer to sell their nonperforming portfolio to investors. That sale, however, is often done in bulk, and the purchasers are typically speculators who buy a

package of loans. The bulk sale hurts NHHNS in two ways. As a small nonprofit, NHHNS is not prepared to buy in bulk, nor is it willing to outbid the speculators. Also, the speculators who make the wholesale purchase are often irresponsible landlords, so their disinvestment leads to further property deterioration in Dwight and its sister neighborhoods.

### *Purchase of Property Tax Liens*

When the real estate market softened in New Haven in the late 1980s, property tax delinquency rose in the city. If property taxes remain unpaid, the city ultimately sells property tax liens at auction. In theory, purchasing tax liens and foreclosing on them could provide NHHNS with a means to acquire properties, but this route is problematic in practice. Like the banks selling their bad loans, when New Haven sells tax liens it prefers selling them in packages. Speculators often do the bidding, and when they acquire a package of such liens they focus their attention on the better properties and disregard the rest. This process hurts NHHNS because: (1) buying tax liens in bulk is unsuitable to its needs; (2) speculators will typically outbid the nonprofit;<sup>1</sup> and (3) the virtual if not actual abandonment of the less-desirable properties by the speculators who buy the lien packages in bulk hurts NHHNS's neighborhood-upgrading objectives.

### *Purchase from Private Owners*

NHHNS could acquire properties by contacting private property owners directly and negotiating with them. In fact, NHHNS periodically uses this strategy, yet it has numerous drawbacks. The owners have to be located, and they have to be amenable to a sale. In practice, owners may be hard to locate, and/or may refuse to sell for various reasons (e.g., there may be estate complications), and/or may have unrealistic expectations of the worth of their holdings. Their asking price will often far exceed the \$10,000 to \$20,000 per unit ceiling imposed by NHHNS. When buying from property owners, one often runs headlong into the problem of unpaid liens. NHHNS recounted the example of one property it was negotiating for with private owners who owed \$10,000 in back taxes and \$20,000 in delinquent water/sewer bills. Thus, even if the owner donated the property (which was not likely), NHHNS would have been obligated to pay \$30,000 to clear the tax and utility liens—an amount above its budget for acquisition.

### *FHA Foreclosures*

There are numerous FHA foreclosures a year in New Haven, and NHHNS could obtain properties from this source. It has turned to this strategy in the past, capitalizing on some advantages the group had at such sales. First, nonprofits had priority access to bid on the FHA foreclosures (along with others, such as local law enforcement personnel who would reside in the property). Second, nonprofits were accorded a 30 percent discount off the posted price of the FHA-foreclosed properties.

These advantages remain today. However, NHHNS is encountering very high appraised values on the FHA foreclosures, reflecting what speculators who are only interested in flipping the

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<sup>1</sup>For example, NHHNS recently went to bid on property at 383 Sherman Avenue, prepared to make an offer of about \$20,000. A speculator bid \$50,000 and then attempted to “flip” it for \$90,000 to an unsophisticated buyer.

property or keeping it as a rental and “milking” it will pay.<sup>2</sup> Thus, even with the 30 percent discount, the price on the FHA foreclosure is above NHHNS’s budget for property acquisition.<sup>3</sup>

The upshot is that NHHNS is frustrated on many fronts in acquiring properties, impeding its rehab mission and limiting its ability to revitalize Dwight and sister neighborhoods. The long-term future of NHHNS-rehabilitated properties is clouded by the fact that the nonprofit cannot readily acquire adjacent, abandoned properties and rehabilitate it.

## **Other Development Phase Barriers**

### *Estimating Costs*

NHHNS found that accurately estimating costs is a problem, no matter how experienced its contractors and crew. NHHNS has encountered unforeseen problems in 95 percent of the homes it has worked on. While these problems are not insurmountable, they add to the difficulties of the rehab. By contrast, NHHNS does not find cost estimation to be as problematic in its new-construction jobs.

### *Obtaining Insurance and Financing*

NHHNS has not encountered problems in obtaining insurance and financing. It has a “fortunate relationship with a good insurance agency” (Paley 1999), so NHHNS has been able to secure hazard and other coverage at reasonable cost. NHHNS also has access to revolving lines of credit at three banks, which gives it access to working capital with “maximum flexibility” (Paley 1999).

Draws on the credit lines are secured by the properties being worked on by NHHNS. Thus, a \$250,000 line will be secured by three to four properties, a \$350,000 line by five to six properties, and so on.

To facilitate the financing process, NHHNS cultivates relationships with appraisers who have a good sense of the marketplace in Dwight and similar urban neighborhoods. These appraisers are careful in picking appropriate comparables (“comps”) to the properties being rehabilitated by NHHNS. The “comps” either should be similarly renovated or an adjustment should be made. Not all appraisers are so careful; NHHNS has encountered some who lump together all property sales in Dwight and do not differentiate between renovated properties, which NHHNS believes should be valued at the “high end of the market” (Paley 1999), and sales of unrenovated parcels.

With respect to valuations, NHHNS acknowledges that the distinction between the market price of deteriorated properties in Dwight and the value of its renovated units is nowhere near commensurate with its rehab investment. For example, the market value of 383 Sherman Avenue—a boarded-up foreclosed property—is \$50,000 because that is what a speculator will pay for it. If NHHNS bought 383 Sherman Avenue for \$50,000 and invested another \$150,000 in

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<sup>2</sup>Recall the \$50,000 purchase of 383 Sherman, described in an earlier note.

<sup>3</sup>In the past, NHHNS negotiated a price with HUD. NHHNS can now negotiate with HUD over price, but if it does, it forfeits its right of first access.

it between hard and soft costs, the property would still be valued in the marketplace at only about \$125,000. This caps the upward boundary of the market. Thus, if a buyer were willing to pay NHHNS's cost of purchasing and fixing up 383 Sherman Avenue—about \$200,000—the appraisal on this property would in no way support its full market purchase and rehab.

## **CONSTRUCTION PHASE BARRIERS TO AFFORDABLE-HOUSING REHAB**

### *Overview of Construction Phase Issues*

NHHNS encounters various difficulties in this area. Environmental issues are sometimes confronted in the process of rehabilitating older structures. Because of the federal involvement in the rehab (e.g., CDBG subsidies are utilized), environmental abatement rules are operative in regard to asbestos and lead paint. NHHNS has managed to work with New Haven health department officials in encapsulating asbestos where it has been found undisturbed so full asbestos removal is not required. Sometimes NHHNS has been forced to encapsulate asbestos even when it is unlikely that it will be disturbed (e.g., asbestos-wrapped pipes, high off the floor). By and large, however, asbestos containment is not a major issue. Lead paint issues have been accommodated as well. Houses have to be made “lead safe” as opposed to “lead free.” However, where there is an order for lead poisoning on a property (the property has a history of lead poisoning), a full abatement program must be utilized, adding significantly (up to \$20,000) to renovation costs.

NHHNS can draw on a cadre of experienced contractors, so obtaining qualified people to do the construction work is not a problem. Yet NHHNS cannot always guarantee that its most trusted contractors will be awarded the work. This is because of the requirement that construction jobs above a certain dollar threshold be publicly bid. Sometimes a less competent contractor must be awarded the job if that contractor submitted the low bid. NHHNS recognizes the merits of public bidding, but regrets that it is sometimes forced to work with a contractor who may not be the most experienced and competent in urban rehab.

Building codes rarely present a problem to NHHNS. The organization does a very thorough rehab job, typically replacing the plumbing, wiring, HVAC, windows, and so on. New Haven's building inspectors, recognizing the integrity of NHHNS's rehab program, are flexible with the nonprofit when it comes to complying with the building code. Yet sometimes the building code itself is an issue. In one instance, NHHNS combined the existing second and third floors of a property. The building code required more headroom in a stairway than could be readily provided. NHHNS in this case was forced to retrofit the additional headroom, which proved to be an expensive undertaking.

Regulatory issues concerning the historic nature of the housing stock rehabilitated by NHHNS are detailed below.

### *Historic Preservation Context*

One of the major attractions of the Dwight and sister neighborhoods in New Haven is the historic character of the homes. NHHNS recognizes this and is careful to respect the historic fabric in its

rehab work. This sensitivity was alluded to in the prior description of the renovation of 43 Beers Street. That same attention to historic character is evident in many other NHHNS rehabs. For example, 317 Edgewood Avenue is a late-Victorian home with many eclectic features, particularly Queen Anne and Neoclassical Revival elements. NHHNS's rehab preserved such character-defining details as the porch's decorative features. In a similar vein, the NHHNS rehab of 345 Winthrop Avenue, an example of a Neoclassical Revival-style residence built between 1910 and 1930, preserved such distinctive features as the curved windows.

Rehabbing houses in a way that maximizes their period details is a difficult and expensive process, but one which NHHNS sees as critical to its goal of providing desirable communities for LMI homeowners. NHHNS has restored structures to their historic condition even in situations where it was not required to do so by law, as in houses that have no district or individual historic designation. Similarly, NHHNS has restored features on historically designated properties that the historic regulators were willing to let go. For example, NHHNS recently rehabbed a property at 513-515 Sherman Parkway, a classic revival-style property dating from roughly the early 1890s, which was historically designated. This property contained a deteriorated porch that the Connecticut State History Preservation Office (SHPO) allowed to be removed since it was a later (twentieth century) addition. The SHPO requested only that after removing the deteriorated porch, NHHNS retain an outline of the porch's presence on the property. This "ghost" remnant would cost a nominal \$400. NHHNS, however, felt that more had to be done. Recognizing that the building's prominence and importance depended upon this porch feature, NHHNS rebuilt the porch with its original details (e.g., full canopy with pilasters) at a cost of \$7,000. NHHNS does not try to minimize costs by eliminating the architectural fabric of the community; instead, it seeks to give these elements new life so that they can continue to attest to the time and place of their construction.

Despite NHHNS's sensitivity in preserving the historic fabric in its rehab, it has sometimes encountered problems abiding by the Secretary of the Interior's Standards for Rehabilitation. To better understand this issue, some background must be presented.

#### *Secretary of the Interior's Standards for Rehabilitation*

The Secretary of the Interior's Standards for Rehabilitation (hereinafter the Standards) got its start with the 1976 Tax Reform Act. Its underlying themes, however, predated the 1976 tax incentives. In fact, the basic principles expressed in the Standards were derived from existing preservation documents, some going back to John Ruskin and William Morris in nineteenth-century England. The 1964 Venice Charter, adopted by the International Council on Monuments and Sites, was one of these important documents. Another was a publication titled *Administrative Policies for Historic Areas of the National Park Service*, which appeared in 1967.

The Standards as we know them were written in the mid-1970s and had two specific programs in mind:

- The Department of Housing and Urban Development's (HUD) Emergency Home Assistance Program, which got under way in 1974

- The Department of the Interior’s Historic Preservation Grants-in-Aid Program, which started funding preservation projects in the early 1970s

The Standards first appeared in print in 1977 in a document called Guidelines for Rehabilitating Old Buildings. The subtitle read “principles to consider when planning rehab and new construction projects in older neighborhoods.” The 1977 Standards was issued not by the Department of the Interior but by HUD. These guidelines did not consist of requirements at this point, but rather were a series of recommended and not-recommended work treatments. The 1977 publication of the Standards was designed to provide practical guidance on preserving historic properties—their materials, spaces, features, and finishes—and to ensure that significant components of the property were not inadvertently destroyed in the process of rehab.

With passage of the 1976 Tax Act, the ten Standards for Rehab became closely associated with the preservation tax incentives program. Tax certification regulations required that a project meet the Standards to be eligible for federal historic tax credits.

Section 106 review of federal undertakings, mandated by the 1966 Historic Preservation Act (NHPA), also considers the Standards. For example, if Community Development Block Grant (CDBG) funds are used for rehab (considered an “undertaking”), and if the rehab is done on a property either on or eligible for listing on the National Register of Historic Places (itself established by the NHPA), then the appropriateness of the rehab would be evaluated under the Section 106 process by consulting the Standards.

It is important to remember that the Standards for Rehab are just one component of a larger document: the Secretary of the Interior’s Standards for Historic Preservation Projects. This document contains separate standards for such treatments as restoration, reconstruction, stabilization, and preservation.

Of these various treatments, rehab is the one that allows the greatest amount of latitude and flexibility. The definition reads:

Rehab is the process of returning a property to a state of utility through repair or alteration which makes possible an efficient contemporary use while preserving those portions and features of the property which are significant to its historic, architectural, and cultural values.

In 1986 the National Park Service (NPS) began a review of the Standards for Rehab to determine whether they had remained valid principles of preservation and whether the language of the Standards should be revised. After consulting with developers, architects, federal, state, and local preservation officials, NPS determined that some modifications would be desirable. NPS then began a four-year process of writing, review for comment, and revising. What started out to be a six-month project ended up taking three and a half years. A period for public comment was provided in 1988; the comments received were incorporated into the final revisions that were published in the Federal Register in early 1990.

The preservation principles embodied in the 1990 revised Standards are simple and straightforward. Understand why a historic building is significant and identify its character-defining features. Minimize alterations: retain historic finishes, features, and spaces to the maximum extent possible. Repair existing features rather than replace them. Do not undertake treatments that irreversibly damage, alter, or destroy significant historic fabric. When constructing a new addition, distinguish between old and new. The Standards place a high premium on retaining and reusing significant historic fabric, on reusing existing materials rather than inserting new features and finishes.

What follows is a summary and brief discussion of the major concepts contained in the revised Standards for Rehab.

1. A property shall be used for its historic purpose or be placed in a new use that requires minimal change to the defining characteristics of the building and its site and environment.
2. The historic character of a property shall be retained and preserved. The removal of historic materials or alteration of features and spaces that characterize a property shall be avoided.
3. Each property shall be recognized as a physical record of its time, place, and use. Changes that create a false sense of historical development, such as adding conjectural features or architectural elements from other buildings, shall not be undertaken.
4. Most properties change over time; those changes that have acquired historic significance in their own right shall be retained and preserved.
5. Distinctive features, finishes, and construction techniques or examples of craftsmanship that characterize a historic property shall be preserved.
6. Deteriorated historic features shall be repaired rather than replaced. Where the severity of deterioration requires replacement of a distinctive feature, the new feature shall match the old in design, color, texture, and other visual qualities and, where possible, materials. Replacement of missing features shall be substantiated by documentary, physical, or pictorial evidence.
7. Chemical or physical treatments, such as sandblasting, that cause damage to historic materials shall not be used. The surface cleaning of structures, if appropriate, shall be undertaken using the gentlest means possible.
8. Significant archeological resources affected by a project shall be protected and preserved. If such resources must be disturbed, mitigation measures shall be undertaken.
9. New additions, exterior alterations, or related new construction shall not destroy historic materials that characterize the property. The new work shall be differentiated from the old and shall be compatible with the massing, size, scale, and architectural features to protect the historic integrity of the property and its environment.

10. New additions and adjacent or related new construction shall be undertaken in such a manner that if removed in the future, the essential form and integrity of the historic property and its environment would be unimpaired.

*Advisory Council on Historic Preservation's Affordable Housing and Historic Preservation Statement*

While few would dispute the historic preservation objective underlying the Standards, affordable-housing advocates decried that strict interpretation of the Standards impeded their mission. The following comments are reflective of that view:

In my work with The Enterprise Foundation, I have seen historic preservation requirements add as much as \$10,000 per dwelling unit, or up to about 15 percent extra, to rehab costs. The major cost drivers are requirements for new wooden windows versus vinyl or aluminum, expensive façade restorations, and preservation or restoration of interior features. The third area—interior features—can have a double impact on costs, by both adding to direct construction costs and diminishing the amount of usable space (for example, by not allowing reconfiguration of floor plans to create optimum room sizes and layouts and maximize usable, income-generating space). (Werwath 1998, 494)

To better enable affordable-housing construction that abided by the Standards, the Advisory Council on Historic Preservation (ACHP) formed a Committee on Affordable Housing and Historic Preservation. The task force included members from the National Trust for Historic Preservation, the National Conference of State Historic Preservation Officers, the U.S. Department of Housing and Urban Development, and other organizations. The task force's deliberations led to the ACHP's June 26, 1995 Policy Statement on Affordable Housing and Historic Preservation (hereinafter the Statement). The Statement underscored the need to better coordinate the objectives and activities of the preservation and housing communities.

Federal agencies that assist in the construction and rehab of housing, most notably HUD and the Department of Agriculture, are tasked with meeting Americans' basic needs for safe, decent, and affordable housing. Historic properties have played a vital role in fulfilling this objective; this must continue. It is, however, important that Federal and State agencies, local governments, housing providers, and the preservation community in general actively seek ways to reconcile national historic preservation goals with the special economic and social needs associated with affordable housing, given that this is now one of the Nation's most challenging and controversial issues.

To further the reconciliation, the Statement underscored that as a matter of policy, the ACHP "seeks to promote a new, flexible approach toward affordable housing and historic preservation." To that end, the Statement included ten principles (detailed below). State Historic Preservation Officers (SHPOs), federal and state agencies, and local governments involved in the administration of the Section 106 review process for affordable-housing projects funded or



assisted by federal agencies were encouraged in the Statement to use the principles as a framework for Section 106 consultation and local historic preservation planning.

The ten principles included the following:

1. Emphasize consensus building. Section 106 reviews for affordable-housing projects should place principal emphasis on broad-based consensus reflecting the interests, desires, and values of affected communities.
2. Elicit local views. Identification of historic properties and evaluation of their eligibility for the National Register for Historic Places should include discussions with the local community and neighborhood residents to ensure that their views concerning architectural and historic significance and traditional and cultural values receive full consideration by the SHPO and others.
3. Focus on the broader community. When assessing the effects of affordable-housing projects on historic properties, consultation should focus not just on individual buildings which may contribute to a historic district but on the overall historic preservation potentials of the broader community. Historic preservation issues should be related to social and economic development, housing, safety, and programmatic issues integral to community viability.
4. Adhere to the Secretary's Standards when feasible. Plans and specifications for rehab, new construction, and abatement of hazardous conditions associated with affordable-housing projects should adhere to the recommended approaches in the Secretary of the Interior's Standards for Rehabilitation and Guidelines for Rehabilitating Historic Buildings, when feasible (emphasis added). Where economic or design constraints preclude application of the Standards, consulting parties may develop alternative design guidelines tailored to the district or neighborhood to preserve historic materials and spaces.
5. Include adequate background documentation. Proposals for nonemergency demolitions of historic properties should include adequate background documentation.
6. Emphasize exterior treatments. The Section 106 review process for affordable-housing rehab projects and abatement of hazardous conditions should emphasize the treatment of *exteriors* (emphasis added) and be limited to significant interior features and spaces that contribute to the property's eligibility for the National Register.
7. Coordinate with other reviews. Where appropriate, Section 106 reviews for affordable-housing projects should be conducted in conjunction with the historic rehab tax credit and other state and local administrative reviews to ensure consistency of reviews and to minimize delays.
8. Avoid archaeological investigation. Archaeological investigations should not be required for affordable-housing projects, which are limited to rehab and require minimal ground disturbance activities.

9. Develop programmatic approaches. Governments are encouraged to develop programmatic agreements that promote creative solutions to implement affordable-housing projects and to streamline Section 106 reviews through the exemption of categories of routine activities; the adoption of “treatment and design protocols” for rehab and infill new construction; and the delegation of Section 106 reviews to qualified preservation professionals employed by the local community.
10. Empower local officials. Certified local governments and/or communities that employ qualified preservation professionals should be allowed to conduct Section 106 reviews on behalf of the Council and/or the SHPO for affordable-housing projects.

### *NHNHS Rehab and Historic Preservation Issues*

NHNHS construction is a federal “undertaking” since it is subsidized by CDBG and other federal monies. To satisfy the ensuing Section 106 review of the “undertaking,” the NHNHS renovation has to comport with the Standards’ mandate of sensitivity to the existing historic fabric. That compliance should be made even easier because of the flexibility encouraged in the 1995 Statement. Further, given our previous description of NHNHS’s attention to the historic character in its construction, one would think that abiding by the Standards would not be an issue to this nonprofit organization. That was generally the case, but the “devil” is always in the details.

Certain aspects of the Section 106 review of NHNHS’s rehab embodied a spirit of flexibility. For instance, reflecting principle 6 in the Statement, this review has focused on the exterior as opposed to the interior of the properties being renovated. The spirit of principle 9 in the Statement was implemented in the form of a “memorandum of understanding” attempting to expedite the historic review process by establishing broad programmatic guidelines. Similarly, the intent of principle 4 in the Statement was adhered to with respect to the “begrudging acceptance” (Paley 1999) of vinyl siding. NHNHS prefers restoring the existing clapboard, because this saves costs, and as important, the restoration preserves the historical character of the neighborhood. At times, however, the clapboard cannot be restored, or it can be saved only at tremendous cost. In these instances, NHNHS will install vinyl siding. The Section 106 reviewers generally have “grimaced but have accepted the NHNHS decision to opt for vinyl siding” (Paley 1999).

Section 106 review of NHNHS’s rehab plans has not always been favorable. The case of windows is illustrative. Many of the properties rehabilitated by NHNHS contain numerous windows, and these are a distinguishing property feature. NHNHS will try to repair existing windows when it can (e.g., it did this at considerable expense at 345 Winthrop Street), but often the original windows have been removed and/or are beyond repair. The question then is what replacement windows should be used. The Section 106 reviewers sometimes insist that NHNHS replace the original wooden windows with a similar wooden window. NHNHS, however, argues that in such cases, vinyl replacement windows should be allowed for multiple reasons.<sup>4</sup>

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<sup>4</sup>Section 106 can sometimes approve projects with vinyl windows, but vinyl windows would not be approved on a project requesting historic rehabilitation tax credits. Section 106 is supposed to balance competing benefits. The tax credits are for fully meeting the standards.

1. The vinyl windows are a stock item that can be readily purchased, while the wooden replacement windows, because of their archaic size and other features, are a custom order. Therefore, vinyl windows can be ordered and delivered within a two- to three-week period, while the lead time for wooden windows is as long as two months.
2. In part because of their custom-order nature, wooden windows are more expensive than vinyl windows.
3. Wooden windows are often more difficult to install (e.g., when the “opening was not square”) than their vinyl counterparts.
4. The wooden windows must be painted by NHHNS, a task unnecessary with the vinyl alternative. And the wooden windows require more future maintenance by the LMI homeowners for painting and the like.

Given these considerations, the purchase and installation of a single wooden window will cost NHHNS about \$450 to \$500—almost double the \$250 to \$300 cost per vinyl window. The \$200 to \$250 price differential per window adds up, given the large number of windows (25 to 50) typically found in the properties rehabilitated by NHHNS. Thus, vinyl windows cost the nonprofit \$5,000 to \$10,000 *less* per rehab job—a significant savings when trying to house LMI families.

It is not simply a matter of cost, for as noted, NHHNS often opts to spend extra to preserve the historic fabric (recall the porch reconstruction at 513-515 Sherman Parkway and the beautiful original windows restored at 345 Winthrop Street). NHHNS argues that vinyl windows are in fact compatible with historic rehab, because, when viewed from the street, it is hard to discern the difference between vinyl and wooden windows unless one is an expert.

Some examples are in order. The historically sensitive rehabs at 43 Beers Street and 317 Edgewood Avenue utilized vinyl window replacements. Similarly, the rehab at 513-515 Sherman Parkway did the same for windows on the first, second, and third floors. A close-up photograph shows not a jarringly inappropriate casement window, but rather a vinyl window purposely made to look as close to the original as possible. NHHNS estimates that using vinyl rather than wooden windows in 513-515 Sherman Parkway saved between \$5,000 and \$8,000. Furthermore, the purchaser of this property would have maintenance-free windows.

In sum, NHHNS argued that using vinyl replacement windows was the right strategy from an affordable-housing objective and was also appropriate from a historic preservation perspective, especially given the call for flexibility emphasized in the 1995 Statement. Would the Section 106 reviewer of NHHNS’s “undertakings” feel likewise? The answer was yes and no. At the Connecticut-level Section 106, NHHNS’s request to use the vinyl windows was typically *denied* on the basis that such windows violated the mandate of the Standards. After the initial rejection at the Connecticut-level 106 review, NHHNS would appeal the state decision to the ACHP in Washington, DC. The appeal to allow the vinyl windows would typically be approved, but the

process could take as long as four months, and in the interim the rehab job was in limbo. The appeal also added to costs for staff work, property holding costs, and the like.

The affordable housing–historic preservation tensions transpiring at NHHHS were happening elsewhere in the United States when Section 106 and other historic reviews were effected. To address this issue, a number of pilot programs are under way with the assistance of the Partners Program of the National Trust for Historic Preservation. Dwight is one of the pilot efforts. As part of the Dwight pilot, specially tailored guidelines were developed in 1999.

### *Dwight Historic District Design Guidelines*

The purpose of the Dwight Historic Design Guidelines is “to encourage preservation rehab strategies that are economical yet focus on preserving the most important historic architectural features of each house and those most important to defining the character of the neighborhood” (Grzywacz 1999, 9).

The guidelines are used for two purposes:

- For historic rehabs within the Dwight Historic District that are subject to Section 106 review.
- For homeowners undertaking privately financed rehabs, the guidelines provide *suggested priorities* for making repair or replacement decisions on their historic homes.

The guidelines attempt to synthesize affordable housing and preservation principles by asserting that (Grzywacz 1999, 9):

- Historic features should be preserved where possible.
- Some features are more central to defining the character of a house and the district, and the preservation of these features should be given priority.
- The costs of housing rehab often require making choices—most people can’t afford everything they want.
- Because of their impact on the neighborhood, the more important historic features are those seen from the street. These should be given the first priority in rehab.

The guidelines include recommendations for numerous historic features such as windows, porches, trim and ornament, and so on. For each feature, the guidelines provide three options. Option 1 calls for always repairing rather than replacing the historic feature or materials. This is the least intrusive rehab choice, and depending on existing conditions, often the least costly as well. Sometimes a historic building has already been altered or has been severely neglected so that Option 1 is not a viable choice. In that case, Option 2, replacing the feature and material to match, is preferred. Only when Option 1 and Option 2 are too costly should Option 3, replacement with comparable substitute material, be chosen (Grzywacz 1999).

This philosophy is embodied in the following three window options.

**Option 1. Retain and repair historic window sash and frames.** Wood windows require routine recaulking and repainting to prevent deterioration. Proper maintenance and weather-stripping can improve the energy efficiency of existing windows. Storm windows may be added to historic wood windows to increase energy efficiency. Today, for economy, many homeowners select aluminum or vinyl storm windows, which if made to a narrow or low profile in a compatible color with the rest of the house, sized to fit the full opening, and divided at the same point as the sash, can be fairly unobtrusive.

**Option 2. If all or parts of a historic window are missing or too deteriorated to repair, remove the severely deteriorated components and replace them with ones that match the original as closely as possible.** If a historic window is seriously deteriorated on a street facade, it is best to replace it with a wood window of the same size and with the same pane division. This may require obtaining a custom window if the proper size or pane divisions are not available off the shelf. Where possible, it is preferable to replace only the sash while retaining and restoring the existing casing, trim, and framing.

**Option 3. If Option 2 proves too costly, consider replacing the severely deteriorated historic window with a compatible substitute window that matches the overall size, mullion divisions, and as many of the other characteristics of the original as possible.** A stock wood window will often closely approximate the dimensions of the original historic window. A wood window will provide a profile and glasses setback visible from the outside which a vinyl window cannot match. However, as many windows face side and rear yards, and are not normally visible from the street, where severe deterioration of original windows exists, substitute materials replacement windows may provide cost savings while allowing more money to be allocated to retaining, repairing and/or replacing (to match) the original windows on the street face(s) of the house. While replacement wood windows are preferable from the standpoint of historic preservation, in affordable housing where there is particular concern over exposure to lead paint and dust, or where extreme deterioration precludes window rehab for economic reasons, complete window replacement with substitute materials units is acceptable. (Grzywacz 1999, 30–31).

NHNHS views the guidelines as aiding its mission of providing affordable housing while respecting the historic fabric. If an original wooden window can be repaired, NHNHS will do that for reasons of economy and aesthetics. That is the philosophy embodied in Options 1 and 2. For example, some of the boarded-up windows on one property it is rehabilitating will be retained because they are important to the character of the property (e.g., one is a beautiful stained glass window). Option 1 was also followed at 345 Winthrop Street because the original curved windows there could be repaired and these windows were integral to the distinctive appearance of that house. Option 3, however (especially the reference to “economic reasons”), should give NHNHS the leeway to install vinyl replacement windows if the original wooden

windows are too deteriorated and wooden replacement windows are too expensive, as was the case at 43 Beers Street, 317 Edgewood Avenue, and 513-515 Sherman Parkway. NHHHS hopes that the guidelines will be adhered to at the Connecticut-level Section 106 review of its rehab projects, thus ending the need to appeal to the ACHP in Washington, DC. We don't know if that will transpire; however, the Dwight Guidelines and similar pilot programs throughout the United States should further the objective of better integrating historic preservation and affordable housing.

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## **CHAPTER 8**

### **Rehab Barrier Case Study: Isles**

#### **SUMMARY OF FINDINGS**

Isles, short for “islands of redevelopment,” is a nonprofit community development and environmental organization active in Trenton, New Jersey, and its environs. Since its founding in 1981, Isles has completed 129 housing units and is currently involved in projects that will provide 198 additional units. This housing is offered for sale or rent to very low income households. Much of Isles’s housing stock has undergone substantial rehab, with the gut rehab of a Trenton row house prototypical.

Isles encounters numerous hurdles in its housing rehab that complicate its mission. These barriers include the following.

#### **Economic Constraints**

Isles’s ability to deliver rehabilitated housing to economically disadvantaged households depends on subsidies, yet

1. the subsidies in general are very competitive;
2. the subsidy providers’ preference for units with more bedrooms and other features works to the disadvantage of rehab projects;
3. the subsidies’ cost ceilings are problematical for the urban, infill rehab done by Isles, which because of its lesser scale and other characteristics is expensive;
4. even with the subsidies, resource gaps are encountered.

#### **Development Phase Barriers**

##### *Acquiring Properties*

Many strategies for acquiring properties pose challenges. For instance, because of the requirements of New Jersey law, acquisition through eminent domain is often expensive. And private owners may refuse to sell, or they may demand excessive prices, especially in light of their property’s expensive “lienfields” (e.g., outstanding tax certificate, mechanic, and other charges).

##### *Estimating Costs*

Isles finds it challenging to estimate rehab costs because each property is different, construction needs may be hidden (e.g., termite damage is not revealed until a wall is opened), and there is often considerable delay between the original cost estimate and the onset of the renovation.

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This case study is partially based on research originally conducted by Rutgers University for the New Jersey Department of Community Affairs.

### *Obtaining Financing*

While Isles is not facing difficulties in obtaining private financing today, that may change in the future. One reason for this is the low valuations assigned by appraisers to Isles' rehabilitated housing.

### **Construction Phase Barriers**

#### *Building Code*

Until recently, the 25–50 percent provision of the New Jersey building code had complicated Isles's rehab efforts by adding considerable costs. Recent (1998) adoption by New Jersey of separate building code provisions governing existing buildings has alleviated this regulatory problem.

#### *Historic Preservation*

Historic preservation is important to Isles's mission of respecting neighborhood character and amenity. Yet Isles needs greater flexibility with respect to historic preservation controls in affordable housing situations, especially regarding the regulation of a building's interior.

#### *Lead Paint*

Lead-paint abatement may force Isles to do more expensive substantial rehab (e.g., if original kitchen and bathroom cabinetry have to be taken down and then cannot be salvaged). Isles calls for more cost-effective lead-abatement solutions.

#### *Trades*

Isles has difficulty in securing moderate-size contractors—those larger than a single proprietor that can handle one or two houses, yet smaller than a larger company that does scores of units at a time.

### **BACKGROUND**

Trenton, the state capital of New Jersey, is a historical city, dating to colonial times. For the last half century, however, it has confronted many socioeconomic and housing challenges. Once an industrial giant, the city's slogan was "Trenton makes, the world takes." But the postindustrial economy has not been kind to the community. Its population declined from 128,000 in 1950 to 89,000 in 1990. Trenton's once largely white, middle-class population has long since fled to the suburbs. Today the city is predominantly minority; according to the 1990 census, about half of its residents are black, and one-seventh are Hispanic. Trenton is much poorer than its neighbors; its 1989 \$11,018 per capita income contrasted with a \$18,936 average in surrounding Mercer County. Trenton's official unemployment rate is 11.8 percent—more than double Mercer County's unemployment level. Trenton's 1997 per capita property valuation of \$22,141 is a fraction of the \$58,485 Mercer County average. Relatedly, Trenton's property tax rate is very

high; as of 1997, it stood at \$3.40 per \$100 of market value, compared with a \$2.58 average rate in Mercer County.

Trenton's socioeconomic challenges have affected its housing stock. According to the 1990 census, the city contained 33,578 housing units—71 percent ownership and 29 percent rental. The housing stock was old, with 60 percent built before 1940. The 1990 Census reported that 9 percent of the city's housing stock was vacant; the community has had a persistent abandonment problem. The average house cost \$59,468 in Trenton as of 1997, a much lower figure than the \$144,178 housing value average for Mercer County.

Socioeconomic and housing challenges are especially severe in some of Trenton's oldest neighborhoods. In the Old Trenton area, abandonment went unchecked for decades, and when abandoned houses were demolished by the city, the empty lots remaining would fill with garbage and vermin. Another hard-hit location was the "Battle Monument" area:

Time has not been kind to the Battle Monument section of this city. The five-block area, the hub of the Battle of Trenton in 1775 and of transportation in the 1950s, has in the last four decades suffered from abandonment and neglect.

With its streets pockmarked by empty lots and vacant buildings, "it has become a symbol of how bad things could become." (Garbarine 1997)

Isles was formed in 1981 to address the socioeconomic and housing challenges in Trenton's most impacted areas, such as Old Trenton and Battle Monument (Isles 1997). While it has focused primarily on Trenton, Isles is dedicated to improving distressed communities throughout central New Jersey. Isles's goals are to

1. address immediate challenges, such as hunger, homelessness, underemployment, and environmental decay, using long-term strategies that promote self-reliance and community empowerment;
2. build upon existing assets while creating wealth in distressed communities; and
3. broaden its impact by developing easily replicated programs, assisting other community groups and institutions, and improving community-related public policy. (Isles 1998)

Commensurate with its long-range goals are a broad array of Isles programs. A historical chronology, synopsis in exhibit 8.1, includes Isles starting a community gardening program (1981), an affordable-housing initiative (1990), and cleanup of a toxic industrial site (1994). This multifaceted intervention continues, as is evident in the listing below of Isles's current activities (Isles 1998):

1. *Urban agriculture*: Isles helps neighbors transform abandoned lots into gardens. Benefiting more than 3,000 Trenton residents annually, these gardens serve as outdoor activity centers, provide a vital source of nutritious food, and beautify neglected open space.

**EXHIBIT 8.1**  
**Isles—Milestones**

- 1981 Isles was founded by a group of Princeton University students and professors to provide technical assistance to groups interested in community gardening and nonprofit housing development.
- 1982 Isles started a community gardening program that today supports 65 sites throughout Trenton.
- 1984 Isles began planning, building, and preserving public parks and other open spaces. Isles encouraged the city of Trenton to form the Open Space Advisory Board, which today advises the Planning Board on policy.
- 1987 Isles created the Perry Street Children’s Garden, a specially designed nature laboratory for urban youth. Isles cofounded the New Jersey Community Loan Fund, which provides low-interest loans and technical assistance to homeowners and nonprofit housing organizations throughout the state. Isles is also a founding member of the New Jersey Affordable Housing Network and the Capitol Area Food Security Council.
- 1988 Isles organized the Open Space Coalition, a public–private partnership, which successfully redrafted and implemented a new Open Space Master Plan for Trenton.
- 1990 Isles initiated its in-house Affordable Housing Program.
- 1992 Isles successfully completed the first demonstration Trenton Neighborhood Tree project (TNT).
- 1993 Isles established the first central New Jersey urban environmental center, in Trenton's Cadwalader Park.
- 1994 Isles began a demonstration project to involve residents in the cleanup and reuse of an abandoned toxic industrial site in Trenton; the project has expanded to three additional communities.
- 1995 Isles completed construction of the \$5.2 million, 46-unit Wood Street Project, an innovative joint venture with a for-profit developer. Isles was awarded the contract to construct the 80+ unit Monument Crossing development. Isles began a job-training program that is teaching at-risk youth the construction trade while helping them pass the high school equivalency test and address life-skills issues.
- 1996 Isles formed a community outreach group to develop community leadership, involve residents in neighborhood planning and redevelopment, and inform them about available resources.
- 1998 Isles began two initiatives: the Environmental Health Project, to gather health information and help city residents create and enact responses to public health hazards; and a community farm, to train and employ city residents in the production of food to be distributed in low-income neighborhoods.

*Source:* Isles 1999.

2. *Environmental education*: This Isles urban-focused program helps children learn about and care for their environment through hands-on greening projects offered in schools, city parks, and neighborhoods. More than 7,000 urban youth—and hundreds of adults—participate in these programs each year.
3. *Community outreach and urban brownfields*: Isles involves residents in such issues as the cleanup and reuse of contaminated sites. More than 3,000 families annually benefit from Isles’s community outreach activities.
4. *Affordable housing*: Isles designs, builds, preserves, and markets affordable housing, primarily in Trenton. Isles provides counseling and training for its homeowners and requires a contribution of “sweat equity” from purchasers. To date, Isles has completed 129 housing units.
5. *YouthBuild jobtraining*: Isles trains at-risk young men and women (high school dropouts) in the construction trades while rehabilitating vacant, inner-city houses. More than 80 at-risk youths have graduated from or received training through this program.

Isles has an annual budget of about \$2.3 million, of which \$1.1 million is dedicated to housing construction, development, and training. Of its \$2.3 million budget, about \$1.3 million comes from government (including \$0.7 million of government funding for housing); foundation, corporate, and other donations provide about \$0.7 million; and the remainder comes from miscellaneous sources (e.g., fees). As is evident from the above figures, housing is a major Isles activity. The following section considers Isles’s shelter interventions, focusing on its housing rehab activities.

## **REHAB DESCRIPTION**

Isles’s Affordable Housing Program encompasses two production tracks: scattered-site rehab and project-unit production. Scattered-site rehab targets currently abandoned buildings, acquires and rehabilitates the houses, and then sells them to first-time buyers. Project-unit production works on larger-scale, more densely concentrated projects that are rehab and/or new construction. In both tracks, the primary end result is to foster homeownership. Where this is not possible, Isles produces affordable rental opportunities while fostering the path toward future homeownership.

Exhibit 8.2 tracks Isles’s housing production over time. As of 1999, Isles has completed 129 housing units, and is currently involved in projects encompassing 198 additional housing units. Of the latter, 140 units are under development and the remainder are in predevelopment.

Of the 129 completed units, 40 were homeownership and 89 were rental. In Isles’s current housing operations, this emphasis is reversed; of the 198 housing units, 112 units are homeownership and 86 units are rental. Of the 327 housing units either completed or current, all but three are oriented to families as opposed to seniors. The family homes typically have two to three bedrooms.

**EXHIBIT 8.2**  
**Isles Housing—Project Summary (1999)**

<b>Project Name</b>	<b>Date Completed (Expected)</b>	<b>Location</b>	<b>Construction Type</b>	<b>Tenancy</b>	<b>Market</b>	<b># Units</b>	<b>Total Project Cost</b>	<b>Cost Per Unit</b>	<b>Subsidies Utilized</b>
<b>I. Completed</b>									
Phase 1	1993	Trenton	SR	HO	FA	6	\$420,000	\$70,000	BHA/HOME
Phase 2	1994	Trenton	SR	HO	FA	6	\$480,000	\$80,000	BHA/HOME
Phase 3	1995	Trenton	SR	HO	FA	20	\$1,864,000	\$93,200	BHA/HOPE 3
HOPE3/VOA	1997	Trenton	SR	HO	FA	8	\$905,500	\$113,125	HOPE 3/HOME/AHP
Wood Street/Esperanza	1996	Trenton	SR	RE	FA	46	\$4,600,000	\$100,007	BHA/LIHTC/HTC/AHP/ICVF
Academy Place	1998	Trenton	SR	RE	FA	40	\$4,815,000	\$120,375	HTC/LIHTC/BHA/AHP
Monarch Housing	1997	Trenton	MR	RE	SN	3	\$78,000	\$26,000	NA
Tucker Street Facility	1995	Trenton	MR	OT		0	\$60,000	NA	NA
Shepherds Alley Storage	1996	Trenton	MR	OT		0	\$5,500	NA	NA
Princeton Comm. Center	1997	Princeton	NC	OT		0	\$220,000	NA	NA
<i>Subtotal</i>						129	\$13,448,000		
<b>II. Current</b>									
Phase 4	1998	Trenton	SR	HO	FA	10	\$958,000	\$95,800	BHA/RCA/LIHTC
Monument Crossing-1	1999	Trenton	NC	HO	FA	38	\$3,781,000	\$99,500	UHORP/AHP
Monument Crossing-2	1999	Trenton	NC	HO	FA	46	\$5,100,400	\$110,878	UHORP
Reservoir/Frazier	1998	Trenton	NC	HO	FA	17	\$1,650,200	\$97,071	UHORP/HOME
Bell Lofts (Artist Housing)	(2001)	Trenton	SR	RE	FA	50	\$7,190,730	\$143,815	LIHTC/BHA
East Hanover	1999	Trenton	SR	RE	FA	23	\$3,841,390	\$167,016	LIHTC/BHA
Chestnut/Monmouth	1998	Trenton	MR	RE		13	\$306,955	\$23,612	LIHTC/BHA/AHP
6 Chelsea	1998	Ewing	MR	HO	FA	1	\$75,000	\$75,000	NA
P.R. Comm. Day Care	1999	Trenton	SR	OT		0	\$600,000	NA	NA
<i>Subtotal</i>						198	\$23,503,675		
<b>III. Concept</b>									
Culinary Arts Institute	(2000)	Trenton	SR	OT		0		NA	NA
25 Units	(2000)	Trenton	MR	HO	FA	20-40		NA	NA
Sustainable Development	(2000)	Lawrence	NC	HO	FA	10-15		NA	NA

**Type Key**

NA = Information not available or not applicable.

Construction type—new construction (NC), substantial rehab (SR), moderate rehab (MR)

Tenancy—homeownership (HO), rental (RE), other (OT).

Market—family (FA), special needs (SN).

State subsidies—Balanced Housing Assistance (BHA), Urban Home Ownership Recovery Program (UHORP), Regional Contribution Agreement (RCA).

Federal subsidies—HOPE3, HOME, Low-Income Housing Tax Credit (LIHTC), Historic Tax Credit (HTC).

Other subsidies—Affordable Housing Program (AHP), Inner City Ventures Fund (ICVF)

Isles's housing production efforts emphasize rehab. Of the 129 completed units, all were rehabilitated, with the lion's share (98 percent) being substantially as opposed to moderately renovated. With the 198 housing units currently in production, about half (101) are new units and the remainder (96) rehab. Isles's emphasis on substantial improvement continues, as 85 percent of its current rehab is substantial rather than moderate.

Isles has produced one-floor apartment-style units. Its headquarters at Wood Street is a mixed-use building that also contains 40 apartment units ("flats") averaging about 900 square feet each. Most of the housing produced by Isles, however, comprises larger homes (about 1,200 square feet each) of a two-story, townhouse configuration. Prototypical are the Trenton row houses undergoing rehab. These row houses were built as modest dwellings during the period 1890 to 1910. They are typically 13 feet to 16 feet wide and 32 feet to 46 feet long, with two stories and a basement and attic. The buildings are of wood-frame construction with clapboard siding (original) or other siding (e.g., asphalt, asbestos, aluminum, imitation brick) and stone foundations. Originally constructed without interior bathrooms (outhouses were used), over time most had a "dogleg" addition containing a kitchen and indoor bathroom built to the rear of the structure. These doglegs were modest and substandard even by the minimal standards of the time. The row houses are challenging to rehabilitate, a point we will return to later.

All of Isles' housing production, both rehabilitated and new, is targeted to very low income families—that is, those earning less than 50 percent of the areawide median. In the Trenton area (i.e., Mercer County), the 50 percent of median cutoff for a family of four is currently \$32,500. The housing Isles has delivered to its very low income clientele costs the organization roughly \$100,000 to \$130,000 per unit. The 129 completed homes, which as noted were all rehabilitated, averaged \$102,032 in cost each. Of Isles' 198-unit current production, the rehabilitated homes are slated to average \$128,875 in cost per unit, the new construction, \$104,273 per unit.

As is evident from the above figures, in the Isles case, rehab is more costly than new construction. This is further evident if the comparison is extended to similarly sized, modest new housing in suburban communities located just outside Trenton (e.g., Hamilton Township). A new, comparably sized suburban townhouse costs about \$110,000 per unit—roughly \$20,000 less than Isles's rehab housing in Trenton. Despite the cost disadvantage, Isles emphasizes urban, infill rehab for the following reasons:

1. Suburban communities severely limit production of affordable housing through restrictive zoning and other means. While New Jersey's *Mount Laurel*<sup>1</sup> decision has relaxed some of those barriers, there is still very limited opportunity for low-income housing production in the suburbs as opposed to urban areas such as Trenton.
2. Isles's mission is community rebuilding. As the communities it targets for assistance are largely built-up and dominated by an existing housing stock in dire need of upgrading, Isles has little choice but to do rehab.

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<sup>1</sup>This refers to a New Jersey State Supreme Court decision mandating that all New Jersey municipalities provide for a fair share of affordable housing.

3. Related to the above point is Isles's belief that community rebuilding must respect the character of the area and should enhance, rather than destroy, a neighborhood's distinctive features. In the case of Trenton, that perspective translates into not only a rehab emphasis, but rehab sensitive to a neighborhood's stylistic and historic features; yet, preserving such amenities increases rehab costs.

## **ECONOMIC CONSTRAINT BARRIERS TO AFFORDABLE-HOUSING REHAB**

### **Subsidies Utilized**

There is no way that Isles can deliver rehabilitated housing currently costing about \$130,000 per unit to very low income families earning a maximum of about \$32,000 without subsidies. Isles has tapped a potpourri of federal housing aids, including HOME, HOPE3, the low-income housing tax credit (LIHTC), and the historic rehab tax credit (HRTC). It has also obtained Affordable Housing Program (AHP) funds from the Federal Home Loan Bank.

Additionally, Isles has utilized a variety of New Jersey-specific housing subsidies. One state program is Balanced Housing Assistance (BHA). The BHA, funded by the New Jersey Realty Transfer Tax, provides grants and loans on a competitive basis to foster low- and moderate-income (LMI) housing. BHA is always used in conjunction with the LIHTC. A second state aid, the Urban Home Ownership Recovery Program (UHORP), provides low-cost financing to developers of mixed-income urban for-sale homes. A third state program is referred to as a Regional Contribution Agreement (RCA). In brief, the New Jersey Fair Housing Act, promulgated in response to the *Mount Laurel* decision, permitted municipalities to transfer up to 50 percent of their fair share obligations to one or more municipalities within the applicable housing region.<sup>2</sup> The sending municipality must transfer a negotiated payment, the RCA, now established at \$20,000 per unit as the minimum. Funds may be used to subsidize new construction or to rehabilitate existing units for occupancy by LMI households. More than \$109 million in RCAs has been transferred into urban areas; Trenton has received \$10 million.

As is evident from exhibit 8.2, Isles's rehab projects have tapped a potpourri of both federal and state subsidies. The Academy Place rehab, providing 40 very low income housing units at a total project cost of \$4,815,000, was made possible by layering \$3,015,000<sup>3</sup> from the LIHTC and HRTC, \$1,560,000 from New Jersey's BHA monies, and \$240,000 in AHP funds from the Federal Home Loan Bank of New York. The \$4,600,000 Wood Street rehab layered LIHTC and historic tax credits, in BHA support, in AHP funds, and an Inner City Ventures Fund grant from the National Trust for Historic Preservation. Academy and Wood Street were both rentals, and the units' operating costs are paid from the tenants' rents. The \$958,000 Phase 4 rehab of 10 for-sale rehabilitated homes was made possible by aggregating \$219,000 from BHA, \$109,000 from AHP, \$202,000 from a Trenton Regional Contribution Agreement, and the remaining \$428,000 in the homebuyers' down payments and the mortgages they obtained.

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<sup>2</sup>The region within New Jersey for which the Mount Laurel fair share system calculates housing need, fair share responsibilities, and other matters, including RCA transfers.

<sup>3</sup>This equity amount received from selling the tax credits.



It is inherently difficult to garner subsidies from so many sources, and in Isles's experience the hurdles are compounded in a rehab setting.

### **Subsidy Criteria and Rehab Assistance**

As demand for subsidies exceeds supply, funders establish scoring criteria. The latter encompass various legitimate concerns, including need (e.g., targeting aid to the most impacted neighborhoods), economy (e.g., imposing housing unit cost ceilings), and leverage (e.g., favoring projects with higher ratios of private financing).

Some of these criteria will favor the urban infill rehab undertaken by Isles. For instance, when Isles applies for low-income housing tax credits from the New Jersey Housing and Mortgage Finance Agency (NJHMFA), it receives extra points on its applications for such project characteristics as "additional income restrictions" (all of Isles's units are set aside for the poor), "increase in compliance period" (Isles's provides a 45-year compliance period as opposed to the minimum 30 years), "tax abatement" (Isles's rental units have property tax abatement), "social services" (Isles offers social services on its projects), and the fact that it is a qualified nonprofit general partner.

Other NJHMFA criteria that appear on the surface to have merit are problematical in a rehab context (Swartz 1999). These are explained below:

#### *More Bedrooms*

LIHTC projects have a minimum requirement for units with a greater number of bedrooms. This is done so that the housing needs of larger families will be met. Thus, on low-rise buildings, 30 percent of the tax credit project's units must have three bedrooms, while on high-rise buildings, the minimum share of three-bedroom units is 15 percent. In doing new construction, it is easier to meet these bedroom requirements than it is on a rehab job, where existing apartment layouts, corridor widths, and many other existing dimensions constrain the ability to provide units with more bedrooms.

#### *Amenities*

LIHTC projects compete according to their amenities. NJHMFA awards points if projects contain such features as a larger unit size (e.g., 650 square feet for a one-bedroom, 800 square feet for a two-bedroom), parking, or have participated in a state-run energy efficiency program (e.g., "Energy Star"). Each amenity gains the project one point, up to a maximum of two points. LIHTC projects submitted to NJHMFA are at a severe competitive disadvantage if they don't secure these two points. With rehab projects, it is often harder to provide the amenities. For instance, on one project (Chestnut/Monmouth), Isles could not garner an extra point for energy efficiency because this moderate rehab did not realize a high enough energy savings. Isles was

ultimately able to provide two project amenities<sup>4</sup> on Chestnut/Monmouth so as to secure the maximum two-point rating, but it had to scramble to do so.

### *Land-Use Approval*

NJHMFA would award one point for those LIHTC-submitted projects that had already received preliminary and final site plan approval (PFSPA). Under New Jersey land use law, PFSPA is routinely required for new construction but not for the rehab of an existing building. Thus, awarding a point for PFSPA is sensible only for new construction. In order not to be at a competitive disadvantage (i.e., not to lose points) on one rehab job, Isles went to the Trenton Planning Board to obtain PFSPA—an unnecessary and costly process.

Fortunately, however, the awarding of points for PFSPA has been rescinded by NJHMFA. Now, projects simply must have the appropriate land-use approval, and as rehab typically does not need PFSPA, Isles can avoid having to get a “sham” PFSPA, as it did on the Trenton project cited above.

### *Cost Limits*

Many of the subsidy programs utilized by Isles have housing cost ceilings above which monies are not awarded.<sup>5</sup> For the LIHTC, the current NJHMFA cost ceilings are \$112,000, \$120,000, and \$129,000 for one-, two-, and three-bedroom apartments, respectively. These amounts are the maximum “cost basis” figures, from which the tax credit is calculated. State moneys, such as the BHA Program, have a similar “reasonable cost limit penalty.” The “penalty” is that a dollar of subsidy is subtracted for each dollar exceeding the “reasonable cost limit.” As Isles rehab projects often are near or exceed these federal and state ceilings, the programmatic cost limits are an issue.

On its face, a cost limit is sensible for it furthers the objective of programmatic economy. Isles argues, however, that as its costs are higher for rehab than new construction, a singular cost limit for both rehabilitated and newly constructed units works to the disadvantage of the former. Isles’s rehab tends to be more expensive because of the following.

SCALE. Rehab, targeted to individual houses on a per need basis, will tend to be a smaller-scale, costlier construction job. In contrast, Isles’s new construction has been done on a larger scale and has therefore garnered better prices for labor, materials, appliances, and other outlays.

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<sup>4</sup>Projects also compete on their “unit amenities,” such as whether they include central air-conditioning, garages, patios, and such details as the “linear feet of kitchen cabinets.” One point is awarded, up to a two-point maximum, for each of the unit amenities. Isles has not found it hard to provide these unit amenities, but other organizations involved in rehabilitation may not be as fortunate.

<sup>5</sup>To get around that problem, Isles recommends that cost ceilings should recognize a project’s location in an urban area and also variety of cost components related to acquisition, environmental remediation, site preparation, demolition, and high construction costs due to myriad factors (e.g., advanced deterioration, but attached to existing structures or in a historic district; historic property; or adaptive reuse of commercial properties).

NATURE OF THE WORK. Isles argues that the commonalities of new construction, as opposed to the variability of rehabilitating distinctive existing units, makes the latter inherently more expensive. Peter Kasabach, the nonprofit's director of housing explains:

With new townhouses, the roofing is all the same, as are the exteriors. With rehab one exterior can be wood and another brick; there are endless varieties. The same is true with the roofs being rehabilitated; one can be angled and another flat, one roof can be shingle and another, yet a different material.

Framing is very different. In Monument Square [new construction], the framing is done quickly as it is all alike. In rehab, the framing in every house is different; in fact, the framing on every floor in the same existing house can be different. All these differences add to [rehab's] costs. (1999)

Relatedly, the type of building being renovated can add to expenses. Isles's conversion of a multistory concrete building to housing is illustrative. This building once housed heavy electrical equipment and is being donated by Bell Telephone to Isles. The donation is a plus because it eliminates an acquisition cost. Yet converting a concrete, industrial building to 50 housing units is expensive. Construction and soft costs for the adaptive reuse will amount to \$7.1 million, or \$142,000 per unit. This figure exceeds the maximums allowed under the LIHTC and BHA Programs and that overage is clearly an issue for Isles.

UNIT AMENITIES. Isles claims that it, and other nonprofits, often rehabilitate a unit to a higher amenity level than that typically followed by for-profits. For example, Isles routinely replaces operational electric heating systems because of their higher utility operating costs. A for-profit developer might very well retain the existing electric system. Yet these differences are unrecognized in the cost ceilings.

HISTORIC PRESERVATION. Rehab is also costing Isles more because of the amenity of the existing stock that it preserves. Isles's preservation of such historic features as gingerbread, metal mansard roofs, wooden windows/doors, and other features helps retain the character of the older neighborhoods it is working in, yet can add thousand of dollars in costs per unit. The subsidy cost ceilings do not differentiate between new construction and rehab incorporating historic preservation, and as the latter is more costly, the undifferentiated cost ceiling is an issue for Isles.

COMMUNITY INFRASTRUCTURE. Included in Isles's costs are the expenses it incurs for such community improvements as redoing streets and sidewalks, providing tot lots, neighborhood gardens, job training, and the like. These neighborhood upgrades are necessary yet costly in an inner-city setting; they are *not* factored in the subsidy housing cost ceiling per unit. Related is the fact that contractors demand a premium for working in the city, and this geographic cost differential is unacknowledged in the cost limits.

In sum, many factors characterizing Isles's work, such as its smaller construction scale, the variability and higher amenity of its rehab, its community infrastructure and urban missions, all contribute to its relatively high rehab costs, which put it at a disadvantage with respect to the

subsidies’ cost ceilings. While it is hard to isolate these commingled characteristics of scale (urban), location, and nature of the rehab, the figures in exhibit 8.3 are instructive:

**EXHIBIT 8.3**  
**Isles Housing Costs**

<b>Housing Strategy</b>	<b>Estimated Cost Per Unit<sup>a</sup></b>
Isles effecting smaller-scale urban rehab <sup>b</sup>	\$130,000
Isles effecting larger-scale urban rehab <sup>c</sup>	\$120,000–\$130,000
Isles effecting larger-scale urban new construction <sup>d</sup>	\$110,000–\$115,000
Isles effecting larger-scale suburban new construction <sup>d</sup>	\$100,000–\$110,000

<sup>a</sup>In all instances, the housing unit is an attached two-story townhouse-style home of approximately 1,200 square feet.

<sup>b</sup>Dispersed unit-by-unit rehab.

<sup>c</sup>Concentrated renovation of a block front of Trenton row houses, comprising 20 to 30 homes.

<sup>d</sup>New construction of 30 units or more.

In short, ratcheting up the scale of urban rehab offers a modest savings (\$0 to \$10,000) off the \$130,000 it currently costs Isles to effect spot rehab on a unit-by-unit basis. Explains Kasabach (1999) explains: “The higher volume is welcome, yet it leaves the variability of renovation and the higher amenity we have to preserve vis-à-vis new construction.” New urban construction done by Isles in volume drops the cost to \$110,000 to \$115,000 per unit—Isles’s expense on its current Monument Crossing block of new townhouses<sup>6</sup> (exhibit 2). Were Isles to build the same new unit in the suburbs, lower contractor, security, and other costs would drop expenses to the \$100,000 to \$110,000 level. These cost differentials are largely ignored in the various programmatic cost ceilings, thus working to the disadvantage of Isles’s urban infill rehab projects.

*Rehab and Economic Gap*

Even when Isles obtains subsidies, the amounts tendered are often insufficient to fully make up the gap between what it costs the organization to produce the rehabilitated units and the amounts affordable by its very low income clientele. That gap is in part an outgrowth of the higher costs of Isles’s infill urban rehab, explained earlier. Yet other programmatic requirements contribute to the gap.

Take, for instance, New Jersey’s UHORP. This program requires a mixing of below-market and market-priced for-sale housing units. Isles figures that this mixing would yield an average sales price of \$80,000 per unit in a “better” Trenton neighborhood and \$60,000 per unit in a “worse” Trenton neighborhood. Given the way the UHORP formula works, the program would provide a \$25,000 per unit average subsidy in the former case and a higher \$35,000 average per unit subsidy in the latter neighborhood. In both instances, the subsidy falls short of being able to cover the resource gap, as shown below.

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<sup>6</sup>The full cost is actually \$115,000 on the latest Monument Crossing townhouses. Isles’s project expenses shown in exhibit 8.2, \$5,100,000 for the 46 units or \$110,878 per unit, excludes a \$200,000 outlay by the City of Trenton (or \$5,400 per unit) for demolishing existing housing and cleaning up the site.

	<b>“Better Trenton Neighborhood”</b>	<b>“Worse Trenton Neighborhood”</b>
1. Average proceeds from sale of units (market and subsidized)	\$85,000	\$60,000
2. UHORP subsidy	<u>\$25,000</u>	<u>\$35,000</u>
3. Total sales proceeds and subsidy	\$110,000	\$95,000
4. Cost of rehabilitated housing unit	<u>\$130,000</u>	<u>\$130,000</u>
5. Subsidy Gap (4-3)	\$20,000 short	\$35,000 short

## **DEVELOPMENT PHASE BARRIERS TO AFFORDABLE-HOUSING REHAB**

### **Obtaining Properties**

On a “typical” spot rehab of a Trenton row house, costing about \$130,000, Isles pays \$0 to \$5,000 for the property, about \$100,000 in “hard” construction costs, and the remaining \$20,000 to \$25,000 in soft costs and general contractor (GC) markup.<sup>7</sup>

As the above breakout connotes, Isles can expend only a modest sum for property acquisition so that limits its acquisition strategy. In addition to its need to economize, legal and other considerations color Isles’ selection of property acquisition approaches.

Isles could acquire properties through multiple means, including FHA foreclosures, eminent domain, purchase from private owners, donation from private owners, and property tax foreclosures. Each of these approaches offers advantages and disadvantages.

#### *FHA Foreclosures*

While there are hundreds of FHA foreclosures a year in Trenton, Isles rarely obtains properties from such sales. First, the FHA sale prices are far above the \$4,000 to \$5,000 per unit property price ceiling set by the nonprofit. Second, Isles finds that the properties offered at the auctions are typically scattered—“a property here and a property there” (Kasabach 1999); Isles prefers to cluster its rehab so as to achieve a critical mass.

#### *Eminent Domain*

Focused-scale property assemblage could be achieved through the city using its eminent domain powers. New Jersey law allows municipalities such as Trenton to acquire properties in this fashion in “blighted” areas suitable for redevelopment. The Old Trenton and Battle Monument neighborhoods where Isles operates readily satisfy the “blight” criteria; they have, in fact, been declared “blighted” since the mid-1980s. Consequently, the legal machinery is in place for Trenton to acquire and assemble properties in the areas where Isles is working.

In reality, public condemnation is not a viable property acquisition strategy for Isles. Under the New Jersey blight statute, the public acquirer must pay the market value *as of the time the blight designation was made* (e.g., 1986 in Old Trenton). This provision was added to protect against

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<sup>7</sup>As a general rule of thumb, soft costs and GC markup are equal to roughly 20 to 25 percent of hard costs.

municipalities declaring blight as a means to drive down property values so as to realize budget-priced property purchases. At the same time, this provision increases property acquisition costs in the case of Isles.

To illustrate, Isles was interested in a six-unit apartment building on East Hanover Street. This abandoned, run-down property had a 1999 market value of roughly \$25,000, or \$4,000 per unit—comfortably within Isles’ property acquisition range. If the city could acquire the property under the blight legislation, it would be a welcome addition to Isles’ rehab operations because East Hanover is in the heart of the nonprofit’s targeted area. Yet this potential property acquisition is thwarted by the requirement under the blight legislation that the parcel be valued “as of the time the area was blighted,” in this case 1986. In 1986, East Hanover was a fully occupied property with a market value of \$180,000, or \$30,000 per unit. The \$30,000 amount is not the market value today, and is six times Isles’ property cost acquisition ceiling. Consequently, condemnation of East Hanover under blight is not a practical solution for Isles; the East Hanover situation is repeated throughout the neighborhoods where Isles operates.

#### *Purchases from Private Owners*

Isles could pay current market prices for properties by directly contacting private property owners and negotiating with them. In fact, Isles periodically uses this strategy, yet it has numerous drawbacks. The owners have to be located, and they have to be amenable to a sale. While Isles finds the former less of a problem than the latter, owner intransigence is often an insurmountable problem. Isles cites numerous “situations where we have had to build a project around owners who refused to sell” (Kasabach 1999).

Owners refuse to sell for various reasons. These may be personal (e.g., estate) complications. Owners may have unrealistic expectations of the worth of their holdings, and their asking price will often far exceed the few-thousand-dollar-a-unit ceiling imposed by Isles. The latter’s offer is also tempered by the outstanding liens that typify many Trenton properties, as is illustrated below.

A small (three-unit) multifamily in Trenton needing rehab will often be at least two years property tax delinquent; as taxes are about \$5,000 annually, the back taxes owed are \$10,000. This property may also have had a prior two-year period of tax delinquency where the taxes had been paid by an investor; the investor now holds a \$10,000 tax certificate with an 18 percent interest rate. Unpaid water and other utility charges, and mechanic and related liens, will often represent a further amount owed of at least \$3,000 to \$5,000. The cumulative arrearage of the property is thus about \$25,000. That amount alone exceeds what Isles can pay for the building. In other words, even were Isles to receive the property at no cost, the back charges are so excessive that Isles cannot economically acquire and rehabilitate the housing.

#### *Donation from Private Owners*

Isles has received some buildings as outright donations. For instance, Bell Atlantic gave Isles an industrial property that will be adaptively converted to 50 apartments. The building had a market value of about \$250,000, so the utility’s largesse saved Isles that amount. In addition, Bell

Atlantic transferred the building in an environmentally clean state, thus saving Isles many thousands of dollars in cleanup costs.

Few private owners, however, share Bell Atlantic's charitable spirit; the private owners want to be compensated for their properties, and they surely will not incur expenses for environmental remediation. Further, even were an owner to donate a property to Isles, that still leaves the "lienfields" noted earlier—the outstanding property taxes, tax certificates, and utility and other charges that are often quite costly. One way of reducing that arrearage is through property tax foreclosure.

### *Property Tax Foreclosure*

The city of Trenton regularly moves to foreclose on properties delinquent in their taxes. To expedite the process it proceeds in an action *in rem* rather than *in personam* (an action against the property rather than against the property owner). The *in rem* process in New Jersey proceeds as follows:

*In rem* proceedings are initiated by a city council resolution authorizing proposed foreclosure of properties not redeemed after a one-year redemption period. The parcels are assembled into a single suit and filed with the Superior Court of New Jersey. Additional copies of the suit are filed with the county clerk and the state attorney general. A legal announcement of such a proceeding is published in local papers. Defendants have 45 days from the date of publication to respond to the complaint. An affirmative response takes the form of either repaying owed taxes in full or arranging for them to be repaid on the installment plan. Should the property owner not respond, the city files an affidavit of default with the court. Several days later, a final judgment is returned, wiping out all previous liens with a few exceptions (described shortly). The judgment is then certified by the Superior Court clerk and recorded in the county clerk's office. The recording acts as a deed to all property, temporarily granting the city absolute title. A final resolution is then adopted by city council, acknowledging receipt and indicating acceptance of the judgment. It is possible for a former owner to have the judgment set aside for up to 90 days by offering to pay the amount due on the tax sale certificate plus interest, court costs, and a reimbursement to the city for filing and recording fees. To postpone redemption beyond this period, the owner must provide a compelling reason. The city officially acquires title to the property after procedural compliance and certification is granted by a private title search company. The firm issues a Certificate of Regularity indicating that all the necessary steps for securing title have been followed.

Trenton applies this process and then makes available the properties so acquired to Isles and sister nonprofits (as well as private parties interested in redevelopment) at no or nominal cost. Isles has acquired most of its properties in this fashion. Besides no/low cost to those receiving the properties, foreclosure offers other advantages as an acquisition strategy. In New Jersey's case, it conveys strong, insurable title. In addition, the foreclosure wipes out many outstanding charges; in the example cited earlier, of the \$25,000 in "lienfields" (\$10,000 back taxes, \$10,000 in tax certificates, and \$5,000 in utility and mechanic liens), the tax foreclosure would wipe out the back taxes and utility–mechanic liens or \$15,000 of arrearage.

Yet the fact that the foreclosure does not eliminate the obligation of the tax sale certificate is one drawback of this approach. In fact, Trenton does not proceed on the tax foreclosure of a property that has an outstanding tax certificate. What this means is that the lienfield problem still lingers in the presence of a tax certificate. Ironically, as Trenton's fortunes have improved, in part due to the rehab activities of Isles and sister nonprofits, there is enhanced investor interest in tax sale certificates, and as more of these certificates are sold, tax foreclosure becomes less capable of delivering properties for rehab.

Another issue concerning foreclosure is the length of time involved. While in rem foreclosure is much faster than in personam, the former still takes years from initial delinquency till the time a property is available for rehab. A few years is an eternity in an urban setting such as Trenton, and in the interim, the property can so deteriorate that it is beyond rehab.

Isles also observes that city-owned properties are insufficiently stabilized. Once a parcel is foreclosed, Trenton may just lock the exterior doors rather than boarding all doors and windows. The latter stabilization is much better at thwarting vandals, squatters, drug-users, and others who can cause much harm in a short period of time.

### **Estimating Costs**

Isles is good at estimating rehab costs, and this prowess is due to numerous factors. The organization has experienced construction people on staff, these personnel have worked numerous years on Isles' rehab jobs, and there is an inherent simplicity in much of the housing stock (e.g., Trenton row houses) worked on by the organization.

Despite these factors, Isles admits to challenges in estimating costs. To that end, it builds generous contingencies. The contingencies are needed. Construction cost estimates are often 10 percent to 15 percent less than the expenses ultimately incurred, and sporadic larger errors are encountered.

Isles attributes the challenge of estimating costs to a variety of influences, including those described below:

#### *Nature of Rehab*

As each property is different, so are the requirements of each rehab, and these requirements may not be known until the job starts. A preconstruction estimate, consisting of a visual inspection of a wall, may anticipate only minor repairs, yet once the wall is opened, costly termite, water, and other damage may be revealed. Or, costs are estimated based on city-approved plans, but city building inspectors, working in the "field," do not adhere to these plans and require expensive modifications (see later discussion).

#### *Timing and Other Factors*

Because of subsidy funding deadlines and other considerations, estimates of the rehab expenditure are often done early on in the process. Isles has encountered gaps of up to two years



from its initial cost estimate until it actually begins the work. Costs go up over time, and while an inflation factor can be incorporated into the original estimate, it is hard to project precisely how much costs will rise. For example, in the last two years, the price of lumber and the cost for recycling building materials have risen at many times the general inflation rate. This period has also been one of strong economic times. In addition, construction contractors are in demand, so they can insist on top dollar, especially for urban infill rehab, which is not the most desirable work. The upshot is that Isles has been buffeted by rising construction costs for its work; these costs are difficult to predict over a multiyear period.

A further reason that estimates can be off is that when they are made early on, there is often an incomplete basis on which to forecast the work. Plans drawn to scale are rarely available, and the estimate may have to be done from a “walkthrough of the premises rather than from precise architectural and engineering calculations.”

Time also takes a toll on the condition of the property. A cost estimate made early on will not remain valid after a building has been vandalized. Other forces come into play. One Isles property at 221 Academy Street had an unnoticed leak. Over the two years that elapsed from the initial cost estimate on this project to the start of work, the front walls went through a cycle of leaks, freezes, and thaws that damaged the wall and caused structural damage. The result was an actual rehab cost which far exceeded the original estimate.

### **Obtaining Insurance and Financing**

Isles does not report problems with obtaining insurance for its needs, including hazard, builder’s risk, and other coverage. While some of the smaller contractors working on Isles projects have not been able to obtain surety bonding, “funders have recognized this problem” (Kasabach 1999) and have allowed the builders to work without payment for performance protection.

Obtaining private financing similarly has not been an issue for Isles. To start, the organization obtains much of its funding from publicly subsidized sources; it requires relatively modest private funding. For instance, the \$4,815,000 project cost of Academy Place was funded entirely from equity received from the low-income housing and historic tax credits (\$3,015,000), a \$1,560,000 Balanced Housing Grant, and \$240,000 from the Affordable Housing Program. On its rental projects such as Academy Place, Isles tries to avoid carrying any permanent mortgage. Financing is secured on the single-family rehabs but in modest draws. Isles’s Phase 4 rehab of Trenton row houses, a \$958,000 project, drew down only a \$321,000 construction loan. Once the Phase 4 row houses were rehabilitated, the purchasers secured mortgages. Some of these were granted by a public entity, the New Jersey Housing and Mortgage Finance Agency, and others by private lenders. In all instances, however, these purchase mortgages were for modest amounts—about 50 percent or less of the property acquisition and rehab expense—and therefore the permanent lenders, both public and private, were quite comfortable with the modest financing they extended.

In short, Isles has not confronted obstacles in obtaining private funding because so little of its funding comes from that sector. When banks extend financing to Isles, they are in a secure

position because of the modest amounts tendered, and lenders working with Isles benefit by securing credit for Community Reinvestment Act investments.

Isles, however, does foresee a possible future private financing issue. If subsidies are cut in the coming years, property appraisals, heretofore not a problem, may restrict the available bank lending. To illustrate, a prototypical rehabilitated row house costing Isles about \$130,000 is sold to the homeowner for \$50,000, with the remainder coming from a BHA grant (\$42,000) and Trenton RCA and other sources (\$38,000). When an appraisal is done on this property, the valuation assigned to the row house is typically \$50,000 to \$60,000. Despite the fact that the rehab cost \$130,000, the \$50,000 to \$60,000 value is based on neighborhood “comparables.” Currently, the \$50,000 to \$60,000 appraisal is not a hurdle to the financing because the homeowner is seeking a mortgage of only \$50,000. In the future, however, the dynamic may change. If subsidies on the row house are reduced, then purchasers may need a \$60,000, \$70,000, or \$80,000 mortgage. If appraisals remain in the \$50,000 to 60,000 range, these larger loans may very well not be forthcoming.

### **Land-Use Restrictions**

Isles encounters few land-use issues, and these are usually evoked only when it is adaptively reusing a property. In converting the Bell Telephone building to 50 apartments, Isles had to obtain various variances for parking (the building had eight spaces, and the 50 apartments required 30 spaces) and open space (the site had 2,000 square feet less open space than the amount required for such a scale residential project).

## **CONSTRUCTION STAGE OBSTACLES TO AFFORDABLE-HOUSING REHAB**

### **Building Code**

Initially, Isles encountered many problems with the New Jersey building code. Its problems, and those confronted by many others effecting rehab in the state, led New Jersey in 1998 to change its building regulations with respect to existing buildings. To better understand that reform, we begin by synopsising the New Jersey building code as it existed (before the 1998 reformulation), then we summarize the many code problems encountered by Isles, and we conclude the section by summarizing the current New Jersey building code.

#### *Former New Jersey Building Code Regulation*

Prior to 1976, the hundreds of municipalities in New Jersey mandated diverse local standards with respect to building code regulation. In 1976, however, the New Jersey Uniform Construction Code (UCC) was adopted. The UCC-BOCA addressed new structures, changes in the use of existing structures, and renovations and additions to existing structures. New Jersey did not write the technical provisions of the UCC-BOCA but instead adopted by reference model codes that then comprised numerous subcodes. The UCC’s building code provisions were based on the BOCA code, with the latest revision of BOCA released in 1993. In all instances, the UCC-1993 BOCA permitted code officials to grant “variations” when the literal application of the code would be impractical or prohibitively expensive.

There were two provisions in the UCC-1993 BOCA that most significantly affected the rehab of existing buildings. The first concerned change in use (5:23-2.6); the second concerned alterations (5.23-2.4). Under Section 5.23-2.6(b)1 a change in use had “met the intent of the provisions of the regulations for the proposed new use group.” In other words, if a building changed from one use to another—for example, from business to mercantile, or mercantile to residential—the UCC-1993 BOCA required that the entire building be brought up to the current UCC-1993 BOCA requirements for a new building of a given use (the use to which the building was converted).

For rehab that did not change a building’s use, the UCC-1993 BOCA provision governing alterations applied. The requirements for alterations varied depending on the value of the alterations relative to the value of the building. There were three ratios or thresholds in this regard—where the alteration’s value was (a) under 25 percent, (b) 25 percent to 50 percent, and (c) over 50 percent of the building’s value.

At the first threshold, where the alteration value was under 25 percent of the value of the structure, 5:23-2.4(a)5 required that the “subcode official shall determine to what degree the portion so altered” shall be made to conform. At the second threshold, where the alteration value was 25 to 50 percent of the structure value, 5:23-2.4(a)3 required that “only the altered or repaired portions need conform to the requirements for new structures.” At the last threshold, when alteration expenses exceed 50 percent of the structure’s value, 5:23-2.4(a)1 mandated that “requirements for new structures shall apply to the *entire structure* (emphasis added) including those portions not altered or repaired.”

In other words, at the lowest threshold, it was left to the subcode official’s discretion concerning the extent to which the work being done had to meet new building code standards. At the midlevel threshold, when the rehab outlays equaled one-quarter to one-half of the structure’s value, the code required that what is worked on had to meet new building specifications. At the last threshold, where rehab exceeded one-half of the structure’s value, not only the altered areas but the entire building had to be upgraded to the new code standard.

### *Building Code Issues Confronting Isles*

When the UCC-1993 BOCA prevailed, Isles found it was often ineffective in fostering cost-effective, uniform, and predictable regulation of rehab. Problems and issues could be broadly categorized as “administrative” or “technical,” albeit there is much overlap between the two. “Administrative” involves how the UCC-1993 BOCA was implemented, not the code itself per se, while “technical” involves the standards themselves.

The Isles experience illustrates numerous administrative problems.<sup>8</sup>

1. *Changing requirements.* At the start of its operations, Isles encountered numerous instances of the same official making different demands at different points in time and, even more frequently, differing requirements asked for by different officials. With respect to the latter, in many cases Isles had its plans approved by a reviewer in the subcode official’s office, only

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<sup>8</sup>Over time, Isles’s working relationship with local code officials *dramatically improved*. The incidents reported here reflect the early interactions.

to have these plans rejected by the field inspector. Thus, in 108 Passaic Street, the one-hour-rated exterior siding accepted in the “office” was rejected in the “field”; in 411 Lamberton Street, retaining the second-story stairway, a strategy accepted in the “office,” was rejected in the “field”; in 45 Delawareview the plan to convert to a two-unit building, accepted in the “office,” was rejected in the “field.” These many “field” changes proved chaotic and costly.

2. *Unwarranted requirements.* Isles encountered numerous instances of being asked to meet excessive requirements. In 31 Sheridan Avenue and numerous other properties, the 1.5-hour fire rating of existing materials (brick infill and undisturbed plaster) was simply not acknowledged. Therefore, rather than simply supplementing this existing protection with one layer of Sheetrock to obtain a total two-hour fire rating, Isles was forced to provide a much more extensive treatment that did not capitalize on the existing building’s starting fire protection.
3. *Inflexible requirements.* In many instances, slight deviations from code requirements could have been addressed by variances but were not. For instance, in 108 Passaic Street and 128 East Trenton, breezeways that were 4'10" rather than 5' resulted in expensive problems for Isles. Similarly, variations could have been granted to Isles on 411 Lamberton because the existing stairway was 30" versus a required 36", or at 51 Asbury and 32 Daymond because doors were 32" rather than 36" wide; in fact, strict code adherence was required in all those cases. In 45 Delawareview, the shortfall was even less—a stairway 3/4" too narrow and windows 5/8" too small. These should not have been code issues, but should have been routinely handled through variances; in fact, they were not.

More fundamentally, there were major application and conceptual problems with the “25–50 percent rule” and the “change-in-use rule.” Take, for instance, the “25–50 percent rule.” As described earlier, the “rehab value” was compared with the “structure value,” and depending on this ratio, various requirements followed. While seemingly a simple comparison, the Isles case studies illustrate numerous problems in applying the standard, and raise the issue of whether this standard is sensible.

Let’s consider “rehab value.” The New Jersey Department of Community Affairs had issued a bulletin (94-3) specifying that only permitted construction work (i.e., that receiving a building permit) should count in the enumeration of “rehab value.” Despite the publication of NJDCA Bulletin 94-3, there remained confusion in the field concerning whether the rehab cost included all outlays—all materials (including equipment and fixturing), bond and surety expenses, professional services (e.g., architect, engineer, planner), markup profit and contingency, demolition and cartage costs, and expenses for meeting asbestos, radon, access and other mandates. NJDCA Bulletin 94-3 in fact *excluded* all of these expenses, but in practice different inspectors varied in what items they would or would not tally in the “rehab value” calculation.

There were also “gray areas” of interpretations concerning what constituted “structure value.” Technically the latter was defined as replacement cost (from the BOCA tables), but the physical area to be included in measuring the building’s size (square footage) was not clear; for instance, did one measure to the inside or outside of walls? Did the total size of the building include basement and attic areas? If it did, should these areas count the same as

other space, since they were less expensive to construct (e.g., a square foot of basement space is less costly than the same amount of upstairs living area). In Isles's experience, the measurement of space for the purpose of ascertaining total building size and, hence, structure value was not done very carefully nor consistently.

A more fundamental shortcoming was the flawed logic of the "25–50 percent rule." The case studies illustrate how Isles would plan its rehab outlay to come under the 50 percent trigger. Was that sensible compared with doing the work on the basis of need? Also, did the basic concept of comparing the rehab outlay to structure value as a trigger for varying code standards to be met make sense? In Isles's case, rehab spending had little if any correlation with the risk and hazard level of a building; therefore, why did its spending trigger the building standard to be met? The "25–50 percent rule" added unnecessary costs to Isles's rehab work.

### *Current New Jersey Building Code and Isles Projects*

In 1998, New Jersey adopted a separate subchapter to the UCC (hereinafter NJ Subcode) to govern all construction work on existing buildings. The "25–50 percent rule" was dropped, and instead the New Jersey Subcode followed a "ladder system" progressing from the least to most in terms of the amount of changes to the building and the degree of code requirements. The ladder encompassed "repairs," "renovations," "alterations," "reconstruction," "change of use," and "additions." The New Jersey Subcode had the least requirements for repairs, renovations, and alterations, and more stringent requirements for reconstruction, change of use, and additions. As most of Isles's work would fall into the "renovations," "alterations," and "reconstruction" categories, depending on the particular Isles renovation, under the New Jersey Subcode, Isles would not be faced with the broad mandate of bringing the entire building up to a new code standard as it was under the "25–50 percent rule."

### **Historic Preservation**

The historic character of the neighborhoods where Isles is working contributes to their distinctiveness and appeal. Isles respects that ambience and tries to protect historic flavor in its rehab. Isles spent about \$15,000 extra for the rehab of 129 West Stockton Street in order to restore that building's distinctive metal mansard roof, stockade fence, and other features. Additionally, preservation offers the potential of drawing upon the historic tax credit (HTC). In fact, Isles has combined the LIHTC and the HTC in its Academy and Wood Street projects (exhibit 8.2).

Preservation has a price, however. A vinyl replacement window for a Trenton row house costs about \$115. A wooden replacement window, required in Trenton's historic districts, costs \$400, a difference of about \$300 per window. In addition, the wooden windows are harder to install than the vinyl, adding about \$50 more in expense for a \$350 differential. A Trenton row house has about six windows on its facade (the area regulated by historic preservation), so opting for the historically appropriate wooden windows over the vinyl results in \$2,100 in additional expenses. Isles wonders if that is money well spent "as the difference (in windows) may not be apparent from more than a few feet away" (Kasabach 1999). Also, the wooden windows have a higher long-term maintenance expense for painting.

Windows were also an issue in the Wood Street project. This project involved an adaptive reuse of a former industrial building into apartments and Isles headquarters. The building had once housed a prominent Trenton printer, and its age, style, and usage gave it historic character. As such, Isles secured a historic tax credit for the adaptive reuse of Wood Street, yet with that came debate over how the building's windows were to be treated. At first, the State Historic Preservation Office (SHPO) demanded that the original windows be kept, but as the original windows were in poor shape and were not insulated, this demand was rescinded. Next, the SHPO required that any replacement windows be an exact replica of the original. Isles argued against the need for, and practicality of, that request, as replicating the original would entail the custom crafting of oversized and uninsulated steel windows. Instead, Isles countered with a proposal for insulated aluminum windows that were half the price of the custom-crafted units. Isles' proposal was at first denied by the SHPO because the aluminum windows were one-eighth of an inch smaller than the original windows. Ultimately, after considerable negotiation, the SHPO accepted the installation of replacement aluminum double-pane insulated windows.

On Academy Street, Isles received a historic tax credit, which added about \$300,000 in equity. Yet there were certain trade-offs:

1. Isles had hoped to reconfigure the first floor from three small apartments into two more desirable larger units. However, the building had large open hallways and a staircase that had to be preserved, thus thwarting the apartment reconfiguration.
2. The building was found to have lead paint on much of its "ornamentation" (e.g., sills, ballasters, and windows). As these features contributed to the property's historic character, they could not be removed. Instead, Isles had to strip these features, an expensive proposition.
3. As a result of the building's historic character, utility lines were installed in the rear instead of the front, again adding costs.
4. Keeping historic exterior and interior doors interfered with security.
5. Other preservation work (e.g., repairing tiles) was also expensive.

Isles estimates that the preservation-related outlays amounted to \$200,000 to \$300,000, about equal to the historic tax credit received (net of the LIHTC). In short, there was an "economic wash" between the historic expense and benefit. Ultimately, Academy Place is a more desirable place to live because of the historic preservation. Isles acknowledges that and strongly supports attention to historic detail on the exterior of the buildings. At the same time, Isles calls for more flexibility in interpreting historic standards on the interior of a building, especially in the instance of historic preservation involving affordable housing. Indicative of its mixed reaction, Isles is declining to apply for a historic tax credit on a 22-unit project on East Hanover Street in Old Trenton. While Isles would like to emphasize historic preservation on this project and would welcome the tax credit equity, it is not applying for the historic tax credit (it is applying for a LIHTC) because of the anticipated added expense of satisfying the historic preservation mandate and, as important, the loss of flexibility in doing interior alterations.

## **Lead Paint**

To protect the future occupants of its rehabilitated units, Isles tests for lead paint and effects abatement as needed. For instance, on 326 Chestnut Street, Isles originally contemplated a moderate rehab of this building's units, estimated to cost \$230,000. Isles tested for lead and found a .9 reading where the legal limit was .1 (Isles hypothesizes that a prior owner likely used lead-based surplus naval paint). Given the high lead level, Isles had to: (1) strip all the trim, windows, framing, and other exposed and painted surfaces, and (2) laminate the walls with a one-quarter-inch drywall. To install the drywall, all cabinets in the kitchen and bathrooms had to be taken down. As these cabinets were original and were in fragile condition, removing them was tantamount to destroying them. Replacing the cabinets and other lead abatement-related work (e.g., dropping the ceilings) changed the nature of the job from moderate to near-gut costs; expenses escalated by \$100,000 to a total of \$330,000.

With the costs increased “the job changed to a new funding category” (Kasabach 1999). In the case of 326 Chestnut Street, Isles decided to apply for a LIHTC. With the tax credit, there is little incentive to do only selective rehab—that is, to save as much as possible and to replace only what is necessary. The upshot is that the lead abatement has changed what was once intended to a moderate rehab of 326 Chestnut Street into a much more extensive and expensive renovation. Isles does not question the wisdom of ridding units of lead paint. It wonders, however, if there are more cost-effective ways of accomplishing this goal.

Isles also observes that in some instances a historic preservation mandate may exacerbate lead-paint abatement. Preservation is often sensitive to retaining the existing trim and other decorative features that define a building's character. Yet these features often pose lead-paint hazards. The least expensive way of dealing with that is often to remove the decorative features, yet such removal may be disallowed by historic preservation controls or related mandates (e.g., if historic tax credits are utilized, certification that the rehab satisfies the Secretary of the Interior's standards). Isles is not arguing against the merits of historic preservation just as it is not disputing the need for lead-paint protection. Rather, Isles emphasizes that funders should acknowledge the high costs of satisfying environmental (e.g., historic and lead) mandates when rehab is undertaken.

## **Trades**

Isles does not encounter major difficulties in obtaining tradespersons to do rehab. It does, however, note pressures in securing contractors for midsized jobs.

Isles makes three rough cuts of job scale: (1) one to two units, (2) three to 29 units, and (3) 30 units or larger. The contractor for the one- to two-unit job is typically a single proprietor, and while these entities pose problems of their own (e.g., they require considerable Isles administrative oversight and have trouble securing bonding), the Trenton area has a ready supply of these small contractors. At the other end of the spectrum is the larger contractor capable of handling a 30-unit or larger job. These companies are better capitalized, can obtain performance bonding, require less Isles oversight, and also are in “reasonable supply” in the Trenton area—albeit, with construction booming, they prefer new construction jobs. Still, Isles can obtain the services of these larger contractors, as it has, for instance, on the Monument Crossing projects.

Most problematical for Isles is the intermediate-sized contractor—that is, companies able to work on the three- to 29-unit job. That job is too demanding for the single proprietor, and Isles finds that there are few competent intermediate-sized contractors available in the Trenton area.



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## **CHAPTER 9**

### **Rehab Barrier Case Study: Little Haiti Housing Association**

#### **SUMMARY OF FINDINGS**

Little Haiti Housing Association (LHHA), a nonprofit organization founded in 1987, uses housing as a primary vehicle to improve the physical and socioeconomic conditions of the Little Haiti neighborhood in Miami, Florida. LHHA has been lauded as “serving the poorest of families in one of the most impoverished communities in one of the poorest cities in the United States” (Fannie Mae 1997). As of February 1999, 180 families have received extensive homeownership counseling from LHHA. Fifty-seven of these families have purchased houses from LHHA. Fifty-two of the homes were rehabilitated and five were newly built. To date, not one of the 57 homeowners has experienced a foreclosure, and there is a zero percent delinquency rate. In addition, LHHA is in the process of rehabilitating about 70 multifamily units and is building a new 33-unit for-sale townhouse project. LHHA also provides an umbrella of social services such as youth and family programs.

The predominant share of the housing provided by LHHA has been rehabilitated, and improvement of the existing housing stock is viewed by LHHA as “fundamental to its mission of improving the quality of life in Little Haiti” (Harder 1999). LHHA has encountered a gamut of obstacles in its rehab efforts; the organization has risen to the challenge and has overcome the many hurdles. Rehab barriers confronted by LHHA are described below.

#### **Economic Constraints**

LHHA is able to house low-income Haitian families only by securing a potpourri of subsidies. These subsidies, however, are very competitive and often have ancillary costs (e.g., federally mandated relocation requirements) and problems pertaining to timing and other issues.

#### **Development Phase Barriers**

##### *Acquiring Properties*

LHHA buys properties from numerous sources, and all pose their own challenges. For instance, private property owners often are difficult to contact and demand unreasonable prices, and city tax foreclosure properties frequently are burdened with flawed titles.

##### *Obtaining Insurance*

LHHA pays an increased amount for the hazard and casualty insurance it carries because it is engaged in rehab. Its cost for surety bonding (i.e., payment for performance) is very expensive.

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This case study builds from research conducted by Rutgers University for the Fannie Mae Foundation.

### *Obtaining Financing*

LHHA sometimes encounters underappraisals of its rehabilitated housing. For instance, on a recent project costing the organization almost \$500,000 for acquisition and rehab, the appraisal of the property after rehab was only \$310,000.

### *Land-Use Restrictions*

These are rare. However, a new requirement that all past illegal work effected on a property (e.g., an addition that violated the zoning) must be remediated by present owners is of issue to LHHA because many properties it acquires are replete with illegal additions and alterations.

## **Construction Phase Barriers**

### *Building Code*

A pending change to the Miami building code, which would include the *cumulative* value of all work historically done on a property in the “25–50 percent” rule calculation, will be problematical to LHHA, because with the 50 percent threshold more readily triggered, LHHA will be forced to bring the entire building undergoing rehab up to a new building standard.

### *Minimum Housing Standards*

These are sometimes rigidly enforced, demanding wholesale replacement of systems rather than allowing more economical selective rehab. This differential can be quite expensive—for instance, replacing windows costs \$4,000 per single-family house; repairing existing windows costs \$1,000.

### *Environmental Clearance*

LHHA often encounters unnecessary delays in obtaining such clearance.

## **BACKGROUND**

Miami, Florida, has emerged as a city dominated by people who are either foreign-born or first-generation Americans. A mass migration of Cuban exiles to the city began in 1959, and since the 1970s, growing numbers of immigrants and refugees from other Caribbean and Latin American nations have come to Miami. As of 1995, Miami’s population was estimated at 366,000. Of that total, 66 percent were Hispanic, 21 percent were non-Hispanic black, 12 percent were non-Hispanic white, and one percent consisted of other groups. The city had a very large foreign-born population (59 percent); less than a quarter of its residents (24.1 percent) were born in Florida. City income lagged significantly behind that of its peers; the 1995 city median household income of \$19,900 was far below the near \$30,000 median of all Florida households.

The changes in Miami are reflected in dramatic shifts in many of its neighborhoods. The Edison-Little River area that ultimately became known as Little Haiti was largely developed in the post–

World War II period. The Edison-Little River housing reflected the middle-class orientation of the residents—predominantly single-family detached homes of about 1,000 to 1,200 square feet on 5,000-square-foot lots. There were scattered small multifamily buildings and one large multifamily complex, called Sable Palm, that in the 1950s was purportedly “the place to be” (Harder 1998). Starting in the mid-1960s, however, Edison-Little River experienced “white flight” and shortly became the locus of Haitian in-migration in Miami.

An estimated 150,000 people of Haitian ancestry live in Florida (Stepick 1998). Most live in the Miami-Dade County area. The most concentrated area of Haitian settlement in Florida is in the Edison-Little River (“Little Haiti”) section of Miami. The area is one of the oldest sections of the city, located north of the central business district.

According to the U.S. Census, the population of Little Haiti in 1990 was 39,243. Unofficial estimates, however, placed the number as high as 60,000 to 70,000. Of the total neighborhood population in 1990, 82 percent of the residents were black, 13 percent were Hispanic, and 5 percent were white. It is estimated that 85 percent to 90 percent of the neighborhood’s black population is Haitian (LHHA 1998a).

Living conditions in Little Haiti are deplorable (Stepick 1981, 1982a, 1982b, 1998). Little Haiti’s estimated 70,000 people are living in an area encompassing only three square miles. It is not uncommon for a family of eight to live in a two-bedroom apartment. Only 26 percent of housing units in Little Haiti are owner-occupied, compared with a county average of 48 percent (LHHA 1998a). Single-family homes constitute 75 percent of the housing stock in Little Haiti, but many of these homes have been illegally subdivided into as many as four apartments. The illegally converted units rent for roughly \$400 to \$500 monthly—a high rent for the Haitian families who average \$14,000 annual income. Code violations abound, and code enforcement is nearly nonexistent.

Little Haiti Housing Association (LHHA) was formed in response to these deplorable conditions. LHHA is a nonprofit organization working to revitalize the Little Haiti area, primarily by making adequate and affordable housing available to low-income residents. LHHA purchases and rehabilitates existing houses, and it also constructs some new affordable housing in Little Haiti and surrounding neighborhoods. Those homes are then sold, mainly to very low income families (those earning less than 50 percent of the areawide median). The organization provides a comprehensive range of financial and homeownership counseling and education services. LHHA also attempts to improve the lot of renters by informing them of their legal rights and directly providing sound, affordable rental units. These many shelter activities reflect the “integrated housing product concept” followed by LHHA (Harder 1998) in ensuring that a diversity of shelter opportunities are afforded to the Haitian community.

LHHA serves all of Little Haiti, which is bordered on the east by Biscayne Boulevard, on the west by Interstate 95, on the north by 86th Street, and on the south by Interstate 112. The organization is presently expanding its target area to include nearby neighborhoods with similar conditions. Approximately 90 percent of the people who use LHHA’s services are Haitian; almost all are very low income (i.e., earning less than 50 percent of the areawide median).

LHHA currently has an annual budget of approximately \$600,000 raised from various sources: program contracts (e.g., the City of Miami, the State of Florida, and Miami-Dade County HOME Program); corporate donations; foundation grants; and project-related income from development fees on construction projects. At present, LHHA has a staff of ten (LHHA 1998b).

LHHA provides a comprehensive range of social services, from after-school youth programs to economic betterment functions. Its shelter interventions are also extensive and involve the many steps necessary to qualify low-income Haitians for homeownership and to retain these families as successful long-term homeowners. To that end, LHHA provides extensive support, such as homeownership and credit counseling and a postpurchase homeowners' club.

While all of the above LHHA functions are important, the following discussion focuses on LHHA's major housing production vehicle, namely the rehab of the existing stock. Rehab is central to LHHA's mission, as noted by LHHA's executive director, David Harder:

We don't have a choice. We must do rehab if we are to improve Little Haiti, if we are to do community rebuilding. [Little Haiti] is where the people live and we have to improve their existing housing through rehab. . . . If we don't rehab, the area will be beset by abandoned buildings, which will fill with trash and will attract criminals. . . . We expect that our rehab efforts will encourage families to stay who might otherwise leave the neighborhood. By doing rehab, we give them a choice; they can stay in Little Haiti.

Harder further argues for the economic merits of rehab relative to new construction in an inner-city setting such as Little Haiti. While LHHA's acquisition-rehab of detached single-family homes saves only about \$10,000 per unit over comparable new construction (currently \$80,000 versus \$90,000), there is a significant cost advantage in LHHA's rehab of multifamily units, especially when it can do selective (as opposed to gut) rehab. An example is LHHA's recent acquisition of a 14-unit multifamily building. The building with selective rehab and soft expenses will cost \$35,000 per unit. By contrast, new construction of a similar modest-sized multifamily in Little Haiti<sup>1</sup> would cost at least \$60,000 to \$70,000 per unit—almost double the expense of rehab.

## **REHAB DESCRIPTION**

As of the summer of 1999, LHHA had rehabilitated and sold 52 single-family houses. To serve those families not immediately qualifying for homeownership, LHHA is also pursuing a number of projects to create decent and affordable rental units. A 56-unit rental apartment building (Harvard House) is currently being renovated, and the organization has just purchased and is beginning to rehabilitate a 14-unit multifamily rental property.

Once LHHA acquires a property, it undertakes extensive renovations to bring the unit up to (and beyond) code. In each unit, LHHA replaces the plumbing and electrical systems, paints, and installs new flooring, roofing, windows, and kitchen cabinets (Harder 1998).

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<sup>1</sup>Little Haiti is almost fully developed, so infill new construction would be modest-scaled.

## **LHHA Single-Family Rehab**

Exhibit 9.1 tracks the single-family homes rehabilitated and sold by the LHHA. These homes are listed in the chronological order in which they were sold from 1991 through 1997.

The median LHHA home purchase price during the 1991 through 1997 period was \$59,000. The current purchase price is about \$80,000. (New construction of single-family detached homes in Little Haiti would currently cost about \$80,000 to \$90,000 per unit.) Almost all of the purchases have been by black Haitians with large families. The median household income of LHHA clients has been \$18,000. Adjusting for household size, which in this instance is quite large, LHHA purchasers have an income only 40 percent of the county median income for comparably sized families.

The current cost of an FHA-foreclosed home acquired by LHHA (the most common source of the units) is about \$40,000. To that is added about \$28,000 for rehab outlays (for system repairs and replacement, painting, and other improvements as previously described). There is an additional \$10,000 or so for soft costs. The latter include casualty insurance of about \$1,000, the original closing cost on the FHA acquisition, amounting to roughly \$2,000, an anticipated \$2,800 in closing costs for the purchaser of an LHHA-rehabilitated unit (these are paid by LHHA in order to minimize the up-front capital needed by the purchaser), property taxes of about \$1,000, construction loan interest of about \$500, and miscellaneous other outlays.

The total LHHA outlay for delivering the unit is the sum of the \$40,000 acquisition expenditure, the \$28,000 construction outlay, and \$10,000 in soft costs, for a total of approximately \$80,000. These are figures as of 1997 to 1998; total costs were in the \$50,000 to \$60,000 range in the early 1990s. Individual prices differ by unit, depending on such variables as the price demanded by FHA (or other seller), the condition of the house and the attendant need for rehab, and other factors.

## **LHHA Multifamily Rehab**

For those households earning \$10,000 to \$15,000 annually, LHHA acquires and rehabilitates rental complexes and offers the renovated housing as sound and affordable rental units with the future potential of LHHA selling the units as low-cost (i.e., \$10,000 to \$15,000 ) homeownership dwellings.

One such venture is Harvard House (formerly Tiffany Square apartments), located in North Miami Beach, an area just north of Little Haiti where there has been significant Haitian in-migration. This complex was purchased by Greater Miami Neighborhoods (GMN) from the Resolution Trust Corporation, which had foreclosed on the complex's mortgage. Because Tiffany Square housed numerous Haitian families, GMN approached LHHA to collaborate on rehabilitating this complex, which had been operated as a slum. LHHA agreed, viewing this as a new opportunity to implement its "integrated housing" strategy. GMN-LHHA are effecting a gut rehab of the 56-unit complex.

**EXHIBIT 9.1**  
**LHHA Homeownership Financing and Purchaser Profile**

Property Purchase Date	Program <sup>b</sup>	Purchase Price	Mortgage Financing					Monthly Payment <sup>c</sup>	Purchaser Profile <sup>a</sup>			
			1st Mortgage Amount <sup>b</sup>	2nd Mortgage Amount <sup>b</sup>	2nd Mortgage Source <sup>b</sup>	3rd Mortgage Amount	3rd Mortgage Source <sup>b</sup>		Median Income	Family Size	Marital Status	Race
6/91	LHHA	\$47,000	\$20,000	\$25,500	Surtax	N/A	N/A	\$250	30%	5	M	BH
12/91	LHHA	\$50,000	\$21,000	\$26,500	Surtax	N/A	N/A	\$277	41%	5	M	BH
12/91	LHHA	\$55,000	\$13,250	\$33,000	Surtax	\$6,000	AHP	\$225	25%	5	S	BH
12/91	LHHA	\$43,000	\$16,425	\$20,425	Surtax	\$4,000	AHP	\$238	27%	4	M	BH
3/92	LHHA	\$50,000	\$34,000	\$13,500	Surtax	N/A	N/A	\$491	40%	2	S	BH
4/92	LHHA	\$47,500	\$26,125	\$19,000	Surtax	N/A	N/A	\$256	33%	7	UM	BH
6/92	LHHA	\$59,000	\$23,050	\$33,000	Surtax	N/A	N/A	\$269	38%	4	M	BH
12/92	LHHA	\$46,000	\$26,150	\$17,550	Surtax	N/A	N/A	\$322	46%	4	S	BH
6/93	Surtax/GMN	\$54,000	\$33,300	\$18,000	HOPE III/ GMN	N/A	N/A	\$353	36%	7	M	BH
6/93	HOPEIII/GMN	\$78,000	\$35,100	\$39,100	HOPE III/ GMN	N/A	N/A	\$500	45%	6	M	BH
9/93	HOPEIII/GMN	\$57,000	\$33,150	\$16,000	HOPE III/ GMN	\$5,000	AHP	\$368	41%	1	S	HI
9/93	LHHA	\$60,000	\$20,900	\$33,000	Surtax	\$5,000	AHP	\$299	33%	4	S	BH
9/93	LHHA	\$52,500	\$16,850	\$33,000	Surtax	N/A	N/A	\$230	29%	4	M	BH
11/93	HOPEIII/GMN	\$53,000	\$19,850	\$25,500	HOPE III/ GMN	N/A	N/A	\$381	30%	3	S	BH
12/93	LHHA	\$59,000	\$47,550	\$10,500	Surtax	N/A	N/A	\$460	51%	8	M	BH
1/94	Surtax/GMN	\$59,000	\$36,050	\$20,000	Surtax	N/A	N/A	\$419	59%	3	M	BH
1/94	LHHA	\$56,000	\$17,000	\$27,500	Surtax	\$5,000	AHP	\$320	33%	2	S	BH
4/94	HOPEIII/GMN	\$69,000	\$49,550	\$16,000	HOPE III/ GMN	N/A	N/A	\$560	48%	6	UM	BH
4/94	HOPEIII/GMN	\$56,000	\$25,600	\$24,000	Surtax	N/A	N/A	\$290	30%	4	M	BH
4/94	LHHA	\$55,000	\$19,250	\$33,000	Surtax	N/A	N/A	\$340	32%	3	S	BH
6/94	LHHA	\$67,000	\$46,000	\$18,650	Surtax	N/A	N/A	\$431	39%	7	M	BH
12/94	CDBG/LHHA	\$50,000	\$22,500	\$25,000	HOME	N/A	N/A	\$302	40%	3	S	BH
1/95	LHHA	\$73,500	\$33,050	\$36,750	HOME	N/A	N/A	\$397	48%	5	M	BH
1/95	CDBG/LHHA	\$50,000	\$25,500	\$22,000	HOME	N/A	N/A	\$328	38%	4	S	BH
4/95	HOPEIII/GMN	\$60,000	\$33,000	\$24,000	HOPE III	N/A	N/A	\$419	39%	5	UM	BH
5/95	CDBG/LHHA	\$50,000	\$17,500	\$25,000	HOME	\$5,000	AHP	\$314	24%	2	S	BH

N/A = Not applicable.

<sup>a</sup>S = single; M = married; UM = unmarried; BH = Black, Haitian; HI = Hispanic.

<sup>b</sup>AHP = Affordable Housing Program from the Federal Reserve Banks.

GMN = Greater Miami Neighborhoods.

HOPE, HOME = HUD housing programs.

LHHA = Little Haiti Housing Association.

Surtax = Miami, FL surtax program.

<sup>c</sup>Payments are for principal, interest, taxes, and insurance.

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**EXHIBIT 9.1 (continued)**

Property Purchase Date	Purchase Price	Down Payment	Mortgage Financing					Monthly Payment <sup>b</sup>	Purchaser Profile	
			1st Mortgage Amount	2nd Mortgage Amount	2nd Mortgage Source <sup>a</sup>	3rd Mortgage Amount	3rd Mortgage Source <sup>a</sup>		Household Income as Percentage of Area Median Income	Family Size
6/91	\$47,000	\$1,500	\$20,000	\$25,500	Surtax	N/A	N/A	\$250	30%	5
12/91	\$50,000	\$2,500	\$21,000	\$26,500	Surtax	N/A	N/A	\$277	41%	5
12/91	\$55,000	\$2,750	\$13,250	\$33,000	Surtax		AHP	\$225	25%	5
12/91	\$43,000	\$2,150	\$16,425	\$20,425	Surtax	\$4,000	AHP	\$238	27%	4
3/92	\$50,000	\$2,500	\$34,000	\$13,500	Surtax	N/A	N/A	\$491	40%	2
4/92	\$47,500	\$2,375	\$26,125	\$19,000	Surtax	N/A	N/A	\$256	33%	7
6/92	\$59,000	\$2,950	\$23,050	\$33,000	Surtax	N/A	N/A	\$269	38%	4
12/92	\$46,000	\$2,300	\$26,150	\$17,550	Surtax	N/A	N/A	\$322	46%	4
6/93	\$54,000	\$2,700	\$33,300	\$18,000	HOPE III/GMN	N/A	N/A	\$353	36%	7
6/93	\$78,000	\$3,800	\$35,100	\$39,100	HOPE III/GMN	N/A	N/A	\$500	45%	6
9/93	\$57,000	\$2,850	\$33,150	\$16,000	HOPE III/GMN	\$5,000	AHP	\$368	41%	1
9/93	\$60,000	\$1,600	\$20,400	\$33,000	Surtax	\$5,000	AHP	\$299	33%	4
9/93	\$52,500	\$2,650	\$16,850	\$33,000	Surtax	N/A	N/A	\$230	29%	4
11/93	\$53,000	\$2,650	\$19,850	\$25,500	HOPE III/GMN	\$5,000	AHP	\$381	30%	3
12/93	\$59,000	\$950	\$47,550	\$10,500	Surtax	N/A	N/A	\$460	51%	8
1/94	\$59,000	\$2,950	\$36,050	\$20,000	Surtax	N/A	N/A	\$419	59%	3
1/94	\$56,000	\$2,800	\$17,000	\$31,200	Surtax	\$5,000	AHP	\$320	33%	2
4/94	\$69,000	\$3,450	\$49,550	\$16,000	HOPE III/GMN	N/A	N/A	\$560	48%	6
4/94	\$56,000	\$1,500	\$25,600	\$23,900	Surtax	\$5,000	AHP	\$290	30%	4
4/94	\$55,000	\$2,750	\$19,250	\$33,000	Surtax	N/A	N/A	\$340	32%	3
6/94	\$67,000	\$2,350	\$46,000	\$18,650	Surtax	N/A	N/A	\$431	39%	7
12/94	\$50,000	\$2,500	\$22,500	\$25,000	HOME	N/A	N/A	\$302	40%	3
1/95	\$73,500	\$3,700	\$33,050	\$36,750	HOME	N/A	N/A	\$397	48%	5
1/95	\$50,000	\$2,500	\$25,500	\$22,000	HOME	N/A	N/A	\$328	38%	4
4/95	\$60,000	\$3,000	\$33,000	\$24,000	HOPE III	N/A	N/A	\$419	39%	5
5/95	\$50,000	\$2,500	\$17,500	\$25,000	HOME	\$5,000	AHP	\$314	24%	2

N/A = Not applicable or information not available.

<sup>a</sup>AHP = Affordable Housing Program from the Federal Reserve Banks.

GMN = Greater Miami Neighborhoods (umbrella community group which receives various subsidies).

CDBG, HOPE, HOME = HUD housing and community development programs.

LHHA = Little Haiti Housing Association.

Surtax = Miami, FL, surtax program.

<sup>b</sup>Payments are for principal, interest, taxes, and insurance.

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**EXHIBIT 9.1 (continued)**

Property Purchase Date	Purchase Price	Down Payment	Mortgage Financing					Monthly Payment <sup>b</sup>	Purchaser Profile	
			1st Mortgage Amount <sup>a</sup>	2nd Mortgage Amount <sup>a</sup>	2nd Mortgage Source <sup>a</sup>	3rd Mortgage Amount	3rd Mortgage Source <sup>a</sup>		Household Income as Percentage of Area Median Income	Family Size
4/95	\$75,000	\$3,750	\$43,500	\$27,750	HOME/GMN	N/A	N/A	\$506	50%	5
4/95	\$70,000	\$3,500	\$35,000	\$31,500	HOME	N/A	N/A	\$357	42%	6
4/95	\$75,000	\$3,750	\$41,250	\$30,000	HOPE III	N/A	N/A	\$464	37%	4
4/95	\$55,000	\$2,500	\$25,000	\$27,500	HOPE III	N/A	N/A	\$351	29%	2
4/95	\$59,000	\$2,950	\$26,550	\$29,500	HOPE III	N/A	N/A	\$398	36%	5
6/95	\$69,000	\$4,000	\$50,000	\$15,000	Surtax	N/A	N/A	N/A	69%	7
6/95	\$69,000	\$3,450	\$36,550	\$29,000	Surtax	N/A	N/A	N/A	59%	6
8/95	\$55,000	\$2,500	\$25,000	\$22,500	HOME	\$5,000	AHP	N/A	70%	2
4/96	\$78,000	\$3,900	\$30,100	\$39,000	HOME	\$5,000	AHP	N/A	42%	5
4/96	\$80,000	\$4,000	\$27,000	\$44,000	Surtax	\$5,000	AHP	N/A	33%	5
4/96	\$58,000	\$3,400	\$16,600	\$33,000	Surtax	\$5,000	AHP	N/A	32%	3
6/96	\$73,000	\$3,650	\$34,350	\$35,000	HOPE III	N/A	N/A	N/A	58%	2
6/96	\$73,000	\$3,650	\$28,350	\$36,000	HOME/GMN	\$5,000	AHP	N/A	33%	6
7/96	\$50,000	\$2,500	\$17,500	\$25,000		\$5,000	GMN	N/A	30%	5
8/96	\$50,000	\$2,500	\$27,600	\$19,900	HOME	N/A	N/A	N/A	45%	2
11/96	\$50,000	\$2,500	\$17,500	\$25,000	HOME	\$5,000	GMN	N/A	31%	5
12/96	\$82,000	\$4,100	\$31,900	\$41,000	Surtax	\$5,000	AHP	N/A	43%	7
3/97	\$66,000	\$3,300	\$29,700	\$33,000	HOME	N/A	N/A	N/A	40%	3
3/97	\$80,000	\$4,000	\$36,000	\$40,000	HOME	N/A	N/A	N/A	46%	5
4/97	\$50,000	\$2,500	\$22,500	\$25,000	HOME	N/A	N/A	N/A	34%	3
6/97	\$85,000	\$4,250	\$31,750	\$44,000	Surtax	\$5,000	AHP	N/A	44%	5
6/97	\$94,500	\$4,725	\$37,775	\$47,000	HOME	\$5,000	AHP	N/A	67%	6
7/97	\$87,000	\$5,500	\$37,500	\$44,000	Surtax	N/A	N/A	N/A	48%	6
7/97	\$73,000	\$3,500	\$26,000	\$38,500	Surtax	\$5,000	AHP	N/A	39%	3
Average	\$62,260	\$3,012	\$28,924	\$28,425	N/A	\$1,900	N/A	\$359	40.63%	4.4
Median	\$59,000	\$2,825	\$27,300	\$27,625	N/A	\$0	N/A	\$351	39.30%	5.0

N/A = Not applicable or information not available.

<sup>a</sup>AHP = Affordable Housing Program from the Federal Reserve Banks.

GMN = Greater Miami Neighborhoods.

HOPE, HOME = HUD housing programs.

LHHA = Little Haiti Housing Association.

Surtax = Miami, FL surtax program.

<sup>b</sup>Payments are for principal, interest, taxes, and insurance.

The financial pro forma is as follows: Tiffany Square was purchased for approximately \$450,000. It requires a gut rehab projected to cost \$2.7 million. With financing and other expenses, the total project cost is estimated at \$4.2 million, or \$75,000 per unit. To keep rentals affordable, a low-income housing tax credit (LIHTC) was applied for by LHHA and GMN.

As there are many more LIHTC project applications than a state has authorization for, obtaining LIHTC authorization is a very competitive process. In an initial competitive round, the Tiffany Square application did not score high enough to be approved; in subsequent rounds it was ranked higher and was approved. (The reason for Tiffany Square's initially low LIHTC scoring will be explained shortly.) For the affordable units in Tiffany Square—that is, those units cross-subsidized by the market-rate units—rentals will indeed be affordable. For households at 40 percent of the area median income, a one-bedroom rehabilitated unit will rent for \$334 monthly, while two- and three-bedroom units will rent for \$401 and \$463 a month, respectively.

LHHA has been conducting searches for small (two- to twenty-unit) apartment complexes, focusing on buildings near the single-family properties that LHHA already sold to families. As noted by LHHA (1998a), “Creating pocket neighborhoods of educated homeowners and tenants will advance LHHA’s goal to bring a greater stability to the Little Haiti community.” As an example, LHHA recently acquired a 14-unit multifamily building (5513 NE Miami Place). This building, despite being only 15 years old, had been operated as a slum property and was quite run-down at the time of LHHA’s acquisition. LHHA is just beginning to rehabilitate the property. It acquired the building for \$268,000, or about \$19,000 per unit; with rehab and soft costs, the total expense will be about \$35,000 per unit.

The largest multifamily complex in Little Haiti is Sable Palm. Once a showplace, this 500-unit complex is currently quite deteriorated and in need of extensive rehab. LHHA wishes to tackle this project’s renovation but has thus far been thwarted for reasons we shall detail later.

## **BARRIERS TO AFFORDABLE-HOUSING REHAB**

### **Economic Constraint**

#### *Subsidies Utilized*

For the acquisition–construction phase of its single-family rehabs, LHHA tries to avoid public subsidies because of cost, timing, and other issues that will be discussed shortly. On these smaller-scale single-family jobs, LHHA tries to use conventional bank financing. Thus, it sometimes avails itself of no-cost or very low cost funding for acquisition–rehab from a lender consortium, Community Reinvestment Group of Miami-Dade County (detailed later). Yet LHHA often does not have the luxury of private funding on the larger multifamily rehabs it tackles. And in all instances at takeout, when LHHA either sells the single- /multifamily units or finishes rehab and rents them, it can reach its intended low-income audience only with the help of public subsidies, as explained below.

LHHA faces a major problem in making its rehabilitated units affordable to its mainly low-income Haitian clientele. The Haitians’ average annual earnings of \$10,000 to \$25,000 would

appear to be insufficient for affording rehabilitated housing costing from \$35,000 to \$80,000 per unit. This financial gap is overcome only by LHHA acquiring many housing subsidies. For instance, the sale of single-family detached rehabilitated units to low-income households is realized through LHHA tapping a potpourri of sources as follows:

1. a 5 percent down payment by the purchaser;
2. a market-rate, no points, modest-sized first mortgage granted by a lender;
3. a large soft second mortgage (i.e., with minimal repayment requirements) funded from monies from Miami-Dade County or the federal government; and
4. a modest-sized soft third mortgage from a grant program (Affordable Housing Program, or AHP) from the Federal Home Loan System.

Exhibit 9.1 shows the financial structuring of the first, second, and third mortgages used by LHHA. Recall that the median-priced LHHA home over the course of its operations has been about \$60,000. First mortgages given by such lenders as Citibank, Barnett Banks, and First Nationwide Bank have ranged in size from \$20,000 to \$40,000. The median first mortgage has been \$27,000, and because of the extensive secondary financing, the loan-to-value ratio of the first mortgage is at a very low 25 percent to 50 percent. As noted by LHHA's executive director, David Harder, "Banks will make loans all day and night at such low LTVs with the icing on the cake that these loans are good CRA investments" (Harder 1998). Every home sold by the LHHA has had a second mortgage, and these range in size from \$20,000 to \$40,000; the median LHHA secondary mortgage over the term of its operation has been \$28,000. These soft second mortgages are funded from the Miami-Dade County surtax program and HUD HOME, CDBG, or other federal sources. Exhibit 9.2 details the terms and other characteristics of these subsidies for the soft second mortgages. Finally, roughly about a third of LHHA homes have used an AHP-based third mortgage, a source also detailed in exhibit 9.2. The AHP-derived third mortgages have ranged in size from \$4,000 to \$6,000 each, with a median of \$5,000.

The major reason for the tremendous variation between first and second mortgage amounts noted above is that every transaction differs with respect to the price of the unit, the purchaser's income, and other factors. To get a sense of that variation, exhibit 9.3 details two rehabilitated homes currently being sold by LHHA. Example home one (costing \$83,000) is slated for purchase by a very low income household of four earning \$16,673 (\$1,389 monthly), or 37 percent of the current Miami-Dade County \$44,604 median for comparably sized households. The property in question, newly rehabilitated and containing three bedrooms, is ideal for the purchaser. Yet, in most instances, it would be an impossible financial reach for a household earning less than \$17,000 to purchase an \$83,000 unit. LHHA realizes homeownership in this instance through the layering of mortgages and programs previously described. The household purchasing a home from LHHA is required to make a 5 percent down payment, which in this instance amounts to \$4,150 ( $\$83,000 \times .05$ ). The \$4,150 down payment leaves \$78,850 to be financed. Since the purchaser's income in this instance is so low, only a modest first mortgage

**EXHIBIT 9.2**  
**Subsidies Used by LHHA in Its Homeownership Projects**

<b>Subsidy</b>	<b>Description</b>	<b>Financial Assistance</b>
Miami-Dade County Surtax	The Miami-Dade County Documentary Surtax imposes a levy of \$0.45 per \$100 of assessed value on deed transfers relating to the sale of land, commercial buildings, and residential properties. The surtax moneys are used to finance the construction, rehabilitation, or purchase of housing for low- and very low income families. The moneys can be used for wide-ranging housing purposes, such as providing low-cost rehabilitation loans and second mortgages or financing new rental projects. Numerous housing development entities in Miami-Dade County apply for surtax funds, and there is a scoring system for granting these moneys. The LHHA has applied directly for surtax moneys to be used for second mortgages and has also received allocations of surtax funds from an umbrella community development entity in Miami-Dade County called Greater Miami Neighborhoods (GMN).	<p>The surtax funds can be used by households earning up to 120 percent of the Miami-Dade County median income. The repayment schedule for these funds differs depending on the income of the beneficiary household; the most liberal terms are offered for those households with the lowest incomes. For households earning less than 80 percent of the area median income—the target group served by LHHA—the surtax-based secondary mortgage has to be repaid over a 30-year period at a 3 percent interest rate. To make these already liberal terms even more affordable, the repayment schedule is staggered so that only small amounts must be repaid in the initial years of the mortgage, with rising payments to make up for the shortfall in the latter years. For the first five years of the 30-year term, only interest is repaid; for the next five to ten years, interest and some principal payments are made; and in the last 20 years of the mortgage, the loan is fully amortizing. Further staggering of the loan repayments to reduce the financial demands during the early years (e.g., requiring minimal or no interest payments) are also applied, as is illustrated in exhibit 9.3.</p> <p>If surtax moneys are used for a second mortgage by LHHA, the front-end ratio is capped at 28 percent, while the back-end ratio has a ceiling of 32 percent. These 28/32 ratios are relatively modest, so LHHA will often draw on HUD funds that allow for higher front- and back-end ratios (e.g., HOME program; see below).</p>
HUD programs	Various HUD programs are used by LHHA. A primary example is the CDBG program, under which Miami-Dade County receives a block grant from the federal government to be used for a variety of purposes benefiting low- and very low income families, such as LHHA secondary financing. Other HUD programs have been used for the same purpose. Miami-Dade County receives an allocation of HOME moneys and distributes these funds for different purposes (e.g., homeownership and rental production by nonprofit as well as profit-oriented entities). The distribution of the HOME funds is competitive. LHHA receives about 40 percent of the HOME moneys it applies for, which are then used for low-cost second mortgages. LHHA has used HOPE III funds from HUD in a similar fashion.	The HOME-based secondary mortgages have 30/36 front-/back-end ratios and are available to those earning less than 80 percent of the areawide median income. The HOME secondary loans used by LHHA are granted for a term of 30 years at a zero percent interest rate. For low-income households (earning 50 percent to 80 percent of the areawide median), only principal has to be repaid; for very low income households (earning less than 50 percent of the areawide median), the HOME-based secondary loan is due only upon the sale of the property. Further, that repayment must be made only if the household sells the unit in the first five years after its acquisition; if the house is sold subsequent to the five-year holding period, repayment is forgiven proportionately over the 30-year term of the loan.
Federal Home Loan System—Affordable Housing Program (AHP)	AHP is a competitive grant available from the Federal Home Loan System to foster affordable homeownership. AHP is applied for by member banks. For instance, Citibank in Florida received \$160,000 in AHP moneys and in turn made funds available to LHHA for low-cost secondary financing.	AHP moneys are used by the LHHA as a third mortgage over and above the second mortgages derived from the surtax, HOME, and other sources. The typical AHP third mortgage administered by the LHHA is about \$5,000. It is due only upon the sale of property, and is forgiven if the property is held for more than 10 years. For the first 10 years of ownership, the AHP repayment upon sale is forgiven at a rate of 10 percent annually.

**EXHIBIT 9.3**  
**LHHA Homeownership Affordability Case Examples**

<b>A. Borrower Profile</b>	<b>Example 1</b>	<b>Example 2</b>
Annual income	\$16,673	\$23,750
Monthly gross income	\$1,389	\$1,979
Family size	4	5
Area median income (adjusted for family size)	\$44,600	\$51,700
Percentage of median income	37.38	45.94
Income status	Very low	Very low
<b>B. Financing Structure</b>		
Purchase price	\$83,000	\$81,500
5% down payment	\$4,150	\$4,075
Required financing	\$78,850	\$77,425
First mortgage required	\$19,900	\$33,925
Maximum second mortgage (Surtax)	\$53,950	\$38,500
Third mortgage grant (AHP)	\$5,000	\$5,000
<b>C. Financing Terms</b>		
Amount of first mortgage	\$19,900	\$33,925
Interest rate	7.5	7.5
Length of term in years	30	30
Amount of second mortgage	\$53,950	\$38,500
Interest rate	0.0	3.0
Length of term in years	30	30
<b>D. Financing Amounts</b>		
	<i>Monthly Payment</i>	<i>Monthly Payment</i>
First mortgage payment (principal and interest)	\$139	\$239
Property taxes	\$120	\$102
Insurance (hazard/flood)	\$100	\$0
Total first mortgage payment	\$359	\$341
Debt-income ratio	25.9	17.2
Condo association fee (including insurance)	\$0	\$202
Second-mortgage payment <sup>1,2,3</sup>	\$0	\$25
Total first and second mortgage and condo payment	\$359	\$568
Debt-income ratio (%)	25.9	28.7
<b>E. Debits</b>		
Total payments (mortgage and debits)	\$359	\$568
Debt-income ratio (%)	25.9	28.7

**Monthly Payments Schedule for Second Mortgage**

	<b>Example 1</b>	<b>Example 2</b>
Years 1–5	\$0	\$25
Years 6–10	\$0	\$50
Years 11–30	Negotiable	\$216

can be carried, and consequently a first mortgage of under \$20,000 (\$19,900) is sought. That leaves \$58,950 (\$78,850-\$19,900) to be loaned, which is comprised of a \$53,950 second mortgage from the Miami-Dade County surtax program and a \$5,000 AHP third mortgage.

Ongoing repayment of the second and third mortgages is not required. That leaves only principal and interest payments from the first mortgage of \$19,900. That loan had a 30-year term and a 7.5 percent interest rate, thereby demanding modest principal and interest charges of \$139 monthly. The home in question had yearly property taxes of \$1,440, or \$120 monthly. There was a considerable hazard insurance premium of \$1,200 yearly, or \$100 monthly. (Hazard insurance was so steep because of the large insurance company losses in Florida from Hurricane Andrew.) Summing the principal, interest, taxes, and insurance (PITI), periodic costs for example property one amounts to \$359 monthly, or a modest 26 percent (front-end ratio) of the household's \$1,389 monthly income. The household had no debt, so the back-end ratio has an identical 26 percent load—a very affordable debt. Also of note is that the \$359 monthly cost for buying the unit is much less than the monthly rent in Little Haiti—and the rental units are often little better than hovels.

Example property two, also detailed in exhibit 9.3, has been made affordable to its low-income Haitian home buyers through a similar layering of modest down payments and first mortgages and generous subsidized secondary financing. If the latter were not forthcoming—and that is always a possibility because many Miami-Dade County nonprofit entities compete for the surtax, CDBG, HOME, and other subsidies—LHHA could not continue its current purchase, rehab, and sale of single-family homes.

The same is true with respect to LHHA's multifamily rehabs; absent deep subsidies, most of these projects would be financially infeasible. Take for instance the rehab of the 56-unit Tiffany Square. As noted earlier, the total project cost is estimated at \$4.2 million, or \$75,000 per unit. The apartments in this complex will have post-rehab rentals of an average of about \$500 per unit, or a total of roughly a \$336,000 annual gross rental roll. These rents do not financially support a \$75,000 unit or a \$4.2 million project, respectively. What bridges the gap is a low-income housing tax credit of about \$1.3 million.

Yet the LIHTC is very competitive. States have many more applications for tax credits than they can grant, so a worthwhile application may simply lose to the competition. As noted, Tiffany Square was not approved in the first round of competition, nor was it guaranteed that it would be approved in any subsequent round.

It is not simply a matter of competition—that is, many applicants attempting to obtain funding from a limited pool of resources. In numerous instances, the very scoring systems used to rank requests for funds work to the disadvantage of the type of rehab activity being attempted by LHHA. The LIHTC is, again, illustrative. In Florida, higher scores are accorded to LIHTC applications from larger projects, for housing with superior amenities (e.g., multiple bathrooms per unit), and for projects with greater private leverage—that is, those attracting more private financing relative to the tax credit requested. All this works to the disadvantage of projects such

as Tiffany Square, which was a smaller apartment complex, had lesser amenities (e.g., one bathroom per unit), and had relatively low leverage, since its limited market rents constrained the private financing obtainable relative to the requested tax credit.

Development scale also bears on the practicality of what types of projects are brought forth under the LIHTC. There are high fixed professional costs for tax attorneys, accountants, market studies, and the like. Since these do not vary much according to development scale, they are relatively more costly on smaller projects than larger ones. Knowledgeable syndicators in Florida have indicated to Rutgers that because of high fixed costs, as well as other factors, the practical minimum size of an LIHTC application is roughly 100 housing units.

This is a disadvantage to rehab, because rehabilitated housing projects tend to be smaller than new construction ventures. In the entire Little Haiti neighborhood, there are only three existing housing developments that reach the 100 housing unit minimum optimal scale noted above. In contrast, there are hundreds of smaller multifamily buildings in Little Haiti in dire need of rehab; these multifamilies contain anywhere from two to 20 units. Yet, these smaller complexes are below the financial critical scale for the LIHTC.

In sum, LHHA's single- and multifamily rehab operations are contingent on Miami-Dade County surtax; HUD CDBG, HOME, HOPE, and other monies; AHP funding from the Federal Home Loan Bank; and tax credits offered by the LIHTC. As all of these monies are competitive, and in the case of the LIHTC, there is a scoring point disadvantage in submitting a rehab application, the financial underpinning of LHHA's operations—a layering of subsidies—is tenuous at best.

### **The “Costs” of Subsidies from Ancillary Requirements**

While the availability of subsidies is central to LHHA's delivery of housing to financially limited households, LHHA's experience also points to certain ancillary costs of using public assistance. In fact, LHHA purposely tries to avoid using subsidies for the purchase–construction stage of its operations, as opposed to the “takeout” phase (e.g., the soft second and third mortgages used by the LHHA home purchasers) because of the former's cost requirements. These include at the purchase–acquisition stage:

1. Labor wage requirements. Were LHHA to use HOME or other federal monies for construction, for instance, it would have to pay prevailing wages—a much higher wage scale (about \$20 to \$25 hourly) than it currently tenders (about \$15 hourly).
2. Surety requirements. With public subsidy for construction, surety bonding is required, whereas with private financing such bonding may be waived. LHHA has used private (i.e., nonsubsidized) financing for its single-family rehab purposely to avoid obtaining surety bonding. For the more costly multifamily rehabs, it must turn to public subsidies, and on these jobs, it has been forced to pay high premiums for performance insurance (i.e., \$45,000 on Harvard House).



3. Other requirements. As an example, if HOME monies from Miami-Dade County are used for subsidizing the rehab construction, then the county requires that the full gamut of federally prescribed relocation benefits be accrued to any tenants, whether legal or illegal (e.g., squatters). This is particularly germane to rehab because it tends to involve relocation issues much more frequently than does new construction. Participating jurisdictions (PJs) involved in administering federal block programs, such as HOME, often prescribe many other requirements. An example involving minimum housing standards is detailed later. David Harder notes that “requirements proliferate through the PJs’ ‘filter’” and calls upon HUD to “give clearer guidance to PJs when its funds are being disbursed as to what standards are mandatory” (Harder 1999).

### **Timing of the Subsidies**

Even if subsidies were fully available to meet need, and the subsidies did not impose some of the costs noted above, there still would be issues of timing. LHHA confronts considerable costs “up front.” Because of competition for real estate from slum landlords in Little Haiti, and other factors (e.g., Miami-Dade County not foreclosing tax delinquent properties and making them available), LHHA must pay a premium for the housing units it acquires.

These units must be bought outright. Unlike the sellers of raw land, owners of the buildings that are candidates for rehab very rarely give an option to buy; they want an outright sale of the building and they demand to close quickly (i.e., in 30, 60, or 90 days). If LHHA balks at these terms, there are always slum landlords in Little Haiti who will quickly proffer all cash–no contingency deals for properties they will illegally convert to multiple units. After LHHA’s acquisition, which is costly (e.g., \$30,000 to \$45,000 per unit for single-family homes), LHHA must invest yet again for the renovation, thus cumulatively incurring a high “up-front” outlay. While LHHA confronts the immediacy of the considerable up-front investment, the public monies to subsidize the acquisition–rehab are much more slowly forthcoming. David Harder gives the following example of this discordance in timing:

The seller wanted a quick sale; he wanted to close by November 30 and was asking \$285,000. We were able to push the closing off a month and negotiated a \$268,000 price. . . . [However] the public money for acquisition–rehab works very slowly. For federal, county, or city funds, whether from HOME, CDBG, or the surtax, we would be locked into the funding cycle: apply in July, may hear back by November, final approval in March, and monies forthcoming in June. That is an eleven-month cycle to get the public funding when LHHA has to close in two months and then must do the rehab. (Harder 1999)

## **DEVELOPMENT PHASE BARRIERS TO AFFORDABLE-HOUSING REHAB**

### **Obtaining Properties**

LHHA acquires properties to be rehabilitated from multiple sources, including FHA foreclosure sales and independent property owners. Purchasing through each of these routes poses certain advantages and problems.

In years past, LHHA advantageously utilized sales of FHA-foreclosed homes as a means to acquire single-family detached units in Little Haiti that lent themselves to rehab. Numerous foreclosed properties were available at each of the FHA sales. Because of unscrupulous real estate practices in Little Haiti, Realtors and speculators commonly sold homes to Haitians who were ill-prepared for homeownership; these families could not keep up the payments so ultimately the FHA foreclosed the units and resold them.

Until recently, bidders at the FHA sales in the Miami area were classified in three priority tiers. Nonprofits and selected others (e.g., government agencies) were given the first opportunity to acquire the foreclosures. If the foreclosed homes were located in difficult-to-redevelop neighborhoods termed “revitalization areas,” the nonprofits could acquire the homes at a 30 percent discount from the appraised values assigned by the FHA. The remaining two priority categories were, first, bidders claiming they would use the properties as owner occupants, and then all other bidders. Neither the owner occupants nor all the other bidders were entitled to the 30 percent revitalization area discount.

The above system, in place for many years, worked well for LHHA. As a nonprofit, it could capitalize on the first priority access to the FHA foreclosures. Additionally, it could take advantage of the 30 percent discount because Little Haiti was classified as a revitalization area.<sup>2</sup>

Recently, however, the three tiers of priority access to the FHA-foreclosed homes has been restructured to a two-tier system. Nonprofits no longer have first access. Instead, nonprofits and owner occupants collectively have the first priority, followed by all other bidders. The 30 percent discount to nonprofits is also no longer being offered.

These changes reflect recent attempts to operate FHA in a more businesslike fashion—a laudable goal. Yet the revisions have made it more difficult for nonprofits, such as LHHA, to obtain properties at attractive prices. At the FHA foreclosure sales, LHHA is now competing against many others. It is first competing against potential owner occupants. If they were as they claimed, LHHA would welcome their interest, for the Little Haiti neighborhood would benefit from an increase in owner occupants. Unfortunately, however, many of these would-be owner occupants are in fact being duped by unscrupulous realtors interested only in making a sale. LHHA explains:

Realtors approach Haitian families and tell them we can get you into a home . . . just sign here. The realtors encourage the families to have the families’ relatives agree to be co-borrowers without fully explaining the obligations involved. More often than not, outlandish fees are tacked on, such as a \$8,000 closing cost on a \$40,000 home. The families have no idea what it means to be a homeowner and

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<sup>2</sup>The 30 percent discount was not so much a bonus but rather a useful complement to LHHA’s rehabilitation intentions. The 30 percent discount was applied to the appraised values of the homes, and these appraised values were often based on cursory “drive-by” appraisals, which typically did *not* factor in the deteriorated interior condition of the foreclosed homes in Little Haiti. The 30 percent discount, however, essentially mirrored the cost of the repairs needed on the foreclosed property, so with this discount, LHHA was essentially acquiring the FHA-foreclosed homes at their fair market value.

soon they, and their relatives, have been tarnished by a foreclosure. The property is let go and quickly becomes an eyesore. And this is a home that LHHA could have acquired, rehabilitated, and sold to a buyer fully prepared by our counseling and other programs. (Harder 1999)

Under the new FHA sales protocol, LHHA is also competing against speculators willing to bid high prices on the foreclosed units. The speculators are looking to flip the properties at a still-higher price to Haitian families who are novice buyers. Other bidders competing with LHHA include slum landlords. They are willing to pay a premium at the auction because they plan to illegally subdivide the single-family homes into multiple rental units, each of which will command high rents and profits.

In sum, in years past, the FHA auctions were a good source of properties for LHHA because as a nonprofit, it had privileged access to the units being offered. Today, however, that is no longer the case, and LHHA is often at a disadvantage in obtaining homes at the FHA sales.

LHHA also acquires properties by directly contacting the owners of strategically located parcels. If LHHA rehabilitates some houses on a given block, it might contact the owners of nearby homes that are not being maintained. This is done to realize a critical mass of upgrading in a given area and, relatedly, to protect the investment already made in the rehabilitated homes.

While directly contacting owners is an obvious strategy for property acquisition, it is an approach fraught with difficulty. To start, it is often problematical to identify the legal owners. LHHA finds that the ownership information on property tax records is frequently erroneous (e.g., it indicates a deceased person), outdated (e.g., the property owner is correctly listed but that person has moved from the address given), or is in other ways not very usable. For instance, ownership may be in the name of a shell corporation filed at an attorney's office. LHHA has attempted to track down owners through such means as going to the Florida motor vehicle bureau to ascertain the current address of a listed owner, but this is a time-consuming process that often comes to naught.

Further, even when the owner is contacted, that person may not be willing to sell, or if amenable to a sale, demands an unrealistic price. LHHA recounts that owners often demand the assessed value of the property, or even a premium to the assessed value, despite the fact that their properties often need many thousands of dollars in rehab and have other charges that have to be met. A prototypical case on a neglected property comprises the following:

\$3,500—for public charges for cleaning up a property (e.g., if trash had been dumped and the city had sent a clean-up crew), securing it, and for fines and penalties levied on the owner.

\$3,000-\$4,500—for back taxes; taxes are about \$1,500 annually and properties are often two to three years delinquent.

\$0-\$1,000—mechanic and other liens

\$6,500-\$9,000 total charges against the property

Owners selling Little Haiti properties often conveniently “ignore” the charges noted above, despite the fact that these charges represent an obligation that LHHA, or any other buyer, would have to meet. Similarly, they do not discount prices in light of the rehab needed. Owners hold firm to their asking prices, thinking that if LHHA is contacting them, it is a sellers’ market in Little Haiti. Reinforcing that view is the presence of a speculators’ market in the neighborhood, whereby investors are willing to pay a premium for the single-family homes because they flip them to gullible buyers or illegally convert the homes to multiple rental units. Thus, LHHA is often outbid by others. Given this litany of hurdles, it is no wonder that LHHA has only sparingly turned to direct owner contact as a strategy for property acquisition.

In other jurisdictions, some of the property acquisition barriers noted above, such as owner reluctance to sell and the presence of considerable back taxes and other liens (collectively referred to by Little Haiti as “lienfields”), are addressed through public intervention. This might include a city using its eminent domain powers to acquire strategically located properties suitable for rehab, thereby wiping out the “lienfields” blocking property acquisition. In LHHA’s case, however, neither the city of Miami nor Miami-Dade County is willing to use eminent domain to foster acquisition for rehab. There is a similar reluctance by government to even foreclose on tax-delinquent properties, because government does not want to be the property caretaker of last resort.

Private entities such as LHHA could try to acquire properties themselves through tax foreclosure, but this process is not very fruitful in the Miami context, as is explained below. Every year Miami-Dade County auctions off tax liens, that is liens on unpaid taxes, in an interest “bid-down” system. The county commences the auction by offering to sell the tax obligations at the maximum interest rate allowed by law (18 percent). Bidders can then offer to accept successively lower interest rates, with the winner being the bidder proffering the lowest rate. For example, if the last bid on a \$1,000 lien were 10 percent, the bidder would pay the city the \$1,000 owed and would then try to collect the \$1,000 with 10 percent interest from the delinquent taxpayer. If the latter refuses to pay the tax lien, the property can ultimately be foreclosed.

In theory, the tax foreclosure approach should be implementable by LHHA. This organization is seeking to rehabilitate deteriorated properties in Little Haiti, and many of these parcels are delinquent in their property taxes. LHHA could bid on these properties at the annual tax auctions, and if the owners are not willing to meet their obligations, LHHA could foreclose and obtain title. This title would wipe out many of the outstanding charges (e.g., fines and mechanic liens), which, as noted earlier, often amount to thousands of dollars.

In practice, however, this property acquisition approach has many shortcomings. First, the eventual foreclosure on the tax liens cannot be realized before a multiyear period of nonpayment. Thus, even if LHHA could acquire properties through foreclosure, it would be a lengthy process, and in the interim, the tax-delinquent parcels would likely be severely neglected, thereby making rehab difficult and expensive. Second, and more fundamental, is the frail title that results from the proceeding. As explained by an attorney who does work for LHHA:

The Miami-Dade County tax deed does not involve due process and title insurance companies don't recognize it; the companies will not stand behind the title which is conveyed. If LHHA invested in the tax certificates, it would be laying out money and would not have usable title. (Deutch 1999)

The attorney's cautionary note has been heeded by LHHA, and *not one* property rehabilitated by this organization has been acquired through tax foreclosure. This situation is not likely to change in the future without a radical reformulation of the foreclosure process in Miami-Dade County, allowing for the conveyance of a stronger title.

There are many buildings in Little Haiti crying out for rehab that LHHA cannot acquire. The largest example of this is Sable Palm, a 500-unit rental complex in Little Haiti. A Texas corporation bought Sable Palm's mortgage from FHA some years ago for \$3 million. The corporation then obtained Section 8 subsidies, but ran the complex so poorly that the Section 8 support was terminated. Today, the project is an eyesore, with many abandoned units and only a 50 percent occupancy rate.

Sable Palm would be an ideal candidate for rehab by LHHA, in alliance with the area's umbrella nonprofit organization, Greater Miami Neighborhoods (GMN). Yet LHHA-GMN overtures to acquire Sable Palm have come to naught. The Texas corporation is demanding \$9 million for the mortgage—three times what it paid. Despite the run-down condition of the project, neither the city nor any other governmental entity is forcing the issue through code enforcement, tax foreclosure, or other means. Since they are experiencing no governmental pressure, Sable Palm's owners are sitting tight; they likely calculate that someone will ultimately agree to a high asking price, so why negotiate with LHHA-GMN? Yet LHHA's inability to acquire and rehabilitate this keystone property in Little Haiti has greatly hindered efforts to improve the neighborhood.

### **Estimating Costs**

LHHA encounters uncertainties in estimating rehab expenditures. Frequently, when LHHA evaluates a property, the major systems (e.g., heat and plumbing) have been turned off and therefore cannot be tested. There are other unknowns. In one rehab job, when LHHA opened a wall, termite damage was observed; the building inspector then "red-tagged" the job and costly remediation not included in the original construction estimate was required (Allen 1999).

Despite encountering challenges in estimating construction costs, overall LHHA is remarkably proficient in accurately estimating rehab expenses. On most jobs, the organization comes within 5 percent of its construction estimate. LHHA attributes its success in this regard to the lengthy construction track record of its staff. Notes David Harder (1999), "We have two generations of rehab experience." Also contributing to the precision of estimation is the similarity of many of the properties rehabilitated by LHHA. For the most part, these consist of modest single-family detached homes of similar size, age, and layout. As such, the lessons learned from working on one property can be transferred to another. The fact that LHHA has the same staff involved in its cost estimation and construction further facilitates this institutional transfer and memory.

There is nothing esoteric about LHHA's cost estimation procedure. Software is not utilized; rather each property is carefully checked to ascertain the condition of the roof, foundation, and electric, heating, plumbing, and, where present, cooling systems. The building is checked for termites. LHHA uses its own checklist to determine what work is needed on each of the units. This system works well, given LHHA's construction experience and the housing unit similarity described above. LHHA acknowledges, however, that if in the future its rehab volume increases dramatically, it would consider incorporating rehab cost estimation software, such as that developed by the Enterprise Foundation.

## **Obtaining Insurance**

LHHA carries various lines of insurance, including general liability, directors and officers, fidelity, workmen's compensation, and hazard coverage. Of these lines, the most expensive are general liability and hazard insurance; both coverages are somewhat more expensive and in other ways slightly more problematical than usual because LHHA is involved in rehab.

The general liability coverage costs LHHA \$2,500 annually. This encompasses liability for such occurrences as someone injuring themselves in LHHA's office or in any of the houses it is rehabilitating. The \$2,500 premium covers up to four units of rehab undertaken at any one time; liability insurance on additional houses being rehabilitated costs an additional \$350 per unit. LHHA's insurance agent estimates that were LHHA working on new construction rather than rehab, the liability policy would cost roughly half as much, that is \$1,500, with a \$200 charge for each unit over the four-unit coverage (Gruntler 1999). The agent attributes the higher expenditure to insurance underwriters viewing rehab as "having a greater risk factor exposure" relative to new construction (Gruntler 1999).

Hazard coverage for the rehab work costs LHHA about \$650 per housing unit. This provides fire, wind storm, flood, and other protection. Hazard coverage for new construction in Little Haiti would cost LHHA about \$250 to \$300 per unit, or about one-half that of the rehab premium. This differential is again attributed to higher risk factors including the following:

1. *Greater value exposure.* Since the rehab starts with an existing unit, that entire improvement must be covered from the onset. With new construction, improvements are made in increments, so less value is outstanding at any one time and therefore the insurance cost is lower.
2. *Rehab conditions.* Insurance underwriters view rehab as inherently more risky because "whether or not it is justified, the rehab situation is perceived as an open invitation for vandals, squatters, and others who can damage a vacant unit. If the unit is occupied and rehab is being done around tenants, that triggers yet other risks. New construction has a cleaner exposure" (Gruntler 1999).

Compounding these rehab factors is an overall difficult insurance climate in South Florida. After the region was hit by Hurricane Andrew, a natural disaster that caused tremendous damage, almost all insurance companies stopped writing policies; coverage was only available from a joint underwriting (JU) program. Currently, insurance companies in Florida are reluctant JU

participants, and in this atmosphere, rehab insurance coverage, which even under optimal conditions is somewhat harder and more expensive to secure, is problematical. Asserts LHHA's insurance agent, "I have to shop for LHHA much more than I used to" (Gruntler 1999).

## **Obtaining Financing**

As public subsidy issues have already been discussed, we shall focus here on private-sector financing concerns as they pertain to rehab. These concerns involve both appraisers and lenders.

### *Appraisal Issues*

Mortgage financing is typically offered at a percentage of real estate value. Single-family financing is offered at the higher range of the loan-to-value (LTV) ratio, usually 80 percent LTV or greater; multifamily financing is proffered at lower LTVs, typically at a 60 percent to 70 percent ratio. Since financing is secured at a share of value, the appropriate determination of the value of properties being rehabilitated is a prerequisite for obtaining adequate-sized mortgage loans for rehab.

Professional valuations are done by appraisers who assign values to a given property ("subject property") by considering the cost to produce it ("cost approach"); what buyers have paid for comparable properties, typically referred to in an abbreviated fashion as "comps" ("sales approach"); and what the property is worth as an investment ("income approach").

Any valuation is challenging; the appraisal in a rehab context is even more so. The appraisal of infill urban rehab, such as that carried out by LHHA, constitutes one of the most demanding appraisal assignments of all.

Take, for instance, the concept of "neighborhood." As reflected in the adage "location, location, location," where a property is located has a significant influence on its value. For many years, neighborhoods such as Little Haiti were viewed deprecatingly by appraisers, and this perspective made rehab there harder because valuations were discounted accordingly. Recognizing the destructive influence of such a practice, the Government Sponsored Entities (GSEs)—Fannie Mae and Freddie Mac—have recommended that appraisers limit their neighborhood analysis to the immediate environs of the subjects; the GSEs have advised appraisers to take into account improvements being made in the neighborhoods. In theory, then, appraisers considering a Little Haiti property to be rehabilitated by LHHA on a block of other LHHA-renovated units should not negatively view the subject because of the abandonment in Sable Palm and other run-down buildings in the area, but instead should focus on the immediate environ of the subject (positive) and should acknowledge the rehab and other investment in the area by LHHA and sister organizations (a further positive). While that is the theory, in practice old prejudices against urban neighborhoods such as Little Haiti often linger.

Related to this is the divergence between cost and value (Wiedlich 1999). In Little Haiti, single-family homes may trend to a \$60,000 value but rehabilitated units cost more, in LHHA's case about \$80,000. One can understand why appraisers would lean to a \$60,000 valuation for homes in Little Haiti, even renovated ones, because that's where neighborhood values cluster. At the

same time, appraisers should recognize that a renovated unit is more desirable than its unrehabilitated peers, and as such may very well constitute a distinct, supportable submarket. The rehabilitated unit is the “apple” against the neighborhood’s “oranges,” which often have fewer amenities. This “apples to oranges” distinction is often not made, however, and the rehab outlay is labeled an “overimprovement” rather than an investment that proactively raises the neighborhood price threshold.

A similar difficulty exists with the identification and adjustment of comparable properties. In new construction it is easier to identify “comps,” because the new units sold tend to be more generically standard (e.g., a 1,200-square-foot, two-bedroom, two-bath townhouse), or may even be identical (e.g., if sales occurred in the same subdivision). With older units, dissimilarities increase, and when one is dealing with an older unit that has been rehabilitated, the issue of comps is even more complicated. Appraisers recognize the variability of real estate in the analysis of comps by factoring “adjustments.” Inherently, however, it is easier to make adjustments with newer units, which tend to an underlying standard yet differ in amenities, condition, and so on, as opposed to older units; it is especially problematical to make adjustments between the unrehabilitated older unit and older renovated housing.

Many of these issues are illustrated in the appraisal assigned to a 14-unit multifamily rental property at 5513 NE Miami Place in Miami. As noted earlier, this property was purchased by LHHA for \$268,000, and with rehab and soft costs, will comprise a total investment of \$490,000. LHHA had to obtain a professional appraisal of the project, and the appraiser assigned a value of \$310,000 *after the rehab investment*. The \$310,000 valuation was only slightly more than 60 percent of LHHA’s planned investment. Under normal circumstances, this much lower valuation would doom the project, because financing at yet a lower share of the appraised value would cover such a small amount of the cost (e.g., at a 70 percent LTV, a mortgage of only \$220,000 would be obtainable). While LHHA is proceeding with the job by deferring its soft costs and making other adjustments, the low appraisal is a hardship to LHHA.

The details of the \$310,000 valuation are found in exhibit 9.4 and reflect many of the rehab appraisal hurdles noted earlier. These include

- giving no credit for improving conditions in Little Haiti through rehab and other interventions;
- ignoring rehab in analyzing and adjusting comparables in the sales approach and in determining a capitalization rate for the income approach; and, in a similar vein,
- ignoring rehab’s impact on such real estate fundamentals as vacancy and operating costs (i.e., a renovated building would benefit from lower vacancies than its unrenovated peers and would also operate more efficiently, thus enhancing its value under the income approach).

As is detailed in exhibit 9.4, the appraisal compounded errors. For instance, the operating expense ratio of the rehabilitated building was *increased* rather than being *decreased*. Exhibit 9.4 also shows that a more appropriate appraisal would value this 14-unit multifamily at around \$430,000, much closer to LHHA’s project costs—but this is an after-the-fact academic exercise.



**EXHIBIT 9.4**  
**Valuation of 5513 NE Miami Place, Miami, Florida:**  
**Appraisal as Effected and Critique of Effected Appraisal**

<b>I. Effected Appraisal</b>	<b>II. Critique of Effected Appraisal</b>
<b>A. Subject Property Profile</b>	
Type: multifamily Size: 14 unit Age: 15 years Current Rent Roll: \$79,800 annually Property Condition: "Average to Fair" Neighborhood Description: e.g., "many neighborhood buildings are inadequately maintained and receive only basic maintenance"	<ul style="list-style-type: none"> <li>Profile information is factually accurate. However, negative neighborhood conditions are overstressed and do not incorporate Fannie Mae-Freddie Mac guidelines that appraisers limit the neighborhood analysis to the immediate environs of the subject and should note improvements and investments in the area (e.g., LHHA rehabs).</li> <li>In considering neighborhood conditions, appraiser does not factor rising property values (e.g., the costs of the FHA-foreclosed units acquired by LHHA have risen by \$10,000 per unit over the last few years).</li> </ul>
<b>B. Conditions–Timing of the Appraisal</b>	
"The present condition of the (subject) building is typical of most neighborhood apartment buildings. The property is being appraised <u>as renovated</u> " (emphasis added)	<ul style="list-style-type: none"> <li>Of major importance is the time and date of the appraisal: is it to be before or after the rehab? This consideration is crucial in comparing the subject to comparables and making valid adjustments. The effected appraisal was said to be after a substantial rehab yet the appraisal did <u>not</u> reflect the renovated condition of the subject. See details below.</li> </ul>
<b>C. Valuation of the Subject–Sales Approach</b>	
\$310,000 project value (\$22,143 per unit value based on sales of multifamily units ranging between \$15,000 and \$26,000 per unit)	<ul style="list-style-type: none"> <li>Both the rental comparables and the sales comparables used in the appraisal were of multifamily structures in "fair" condition in the general area of the subject. The prices paid for such complexes were low partly due to deferred maintenance. Yet these low values and multiples were seen as market issues and not as a consequence of the buildings needing considerable financial investment just to retain current income.</li> <li>Adjustments for the sales comparables are crucial. Usually the costs of deferred maintenance are subtracted from the price agreed to for a property, thus arriving at the final sales price and the Gross Income Multiplier (the latter affecting the Income Approach detailed shortly). The appraiser used the sales price (without adjusting for deferred maintenance) and used the multipliers for the subject without adjusting upward for the rehab that was to occur. These procedures negatively impacted the subject twofold by (1) using a multiplier that was less than the comparables were actually paying and (2) also not adjusting upward for the superior condition and marketability of the subject after rehab.</li> <li>No adjustment was made for the types of units in the subject. The subject contains mainly 2-bedroom units for which there is much greater demand. In comparison, all the comparables had a lesser percentage of 2-bedroom units and most were smaller in size (ft<sup>2</sup>) per unit. Comparable 3, which contained 2-bedroom units exclusively, in fact sold for appreciably more than the other comparables.</li> <li>All the value indicators used were within the range of the comparable sales, despite the fact that subject had a major rehab. Subject's multipliers should have been above the comparable sales by a significant amount because of said rehab and better competitive stance.</li> </ul>

*Continued on next page*

### EXHIBIT 9.4 (continued)

I. Effected Appraisal	II. Critique of Effected Appraisal
	<ul style="list-style-type: none"> <li>All the comparables were considered of average quality and condition and were in the same neighborhood as the subject property. The subject itself was considered to be above average in quality and condition, yet the Gross Income Multiplier (4x), or GIM, was nearer to the median than the high end of the comparables and perhaps should have been even higher. A valuation at the high end of GIM would have provided for a value of \$367,000 vs. \$321,000. A GIM of 5x the rent roll would have allowed a value of \$402,000, nearer the amount a property with no deferred maintenance would be worth. The comparable units were sold in a range of \$15,000 to \$26,000 per unit. The subject was given a value of \$22,000 per unit despite the fact that after rehab it was in significantly better condition than any of the comparables. If only the highest per unit value was used, a value of \$364,000 would be indicated instead of \$308,000. More aggressive multipliers for the subject are appropriate here as the subject is being considered after substantial rehab and with no deferred maintenance.</li> </ul>
D. Valuation of the Subject—Income Approach	
<p>\$303,000 project value (\$21,643 per unit value) based on the following:</p> <p>\$80,400—gross income after rehab</p> <p>less 10%—market vacancy loss factor</p> <p>\$72,360—effective gross income (EGI)</p> <p>less 41.3%—expense ratio</p> <p>\$29,939—expenses, leaving</p> <p>\$42,421—net operating income (NOI)</p> <p>divided by .14—capitalization ratio</p> <p>\$303,007—project value based on income approach</p>	<ul style="list-style-type: none"> <li>Gross income—Rehab of the subject may allow some increase from current \$80,400 rent roll.</li> <li>Vacancy factor—Even if rents can't be raised in the rehabilitated subject, the appraiser should acknowledge that the improved competitiveness of the rehabilitated units in the subject will provide for a more stable tenancy with substantially reduced vacancy and credit loss. If there is a 10 percent market level vacancy, it is appropriate to assume that the better quality and value housing, such as the renovated subject, will have more tenants wishing to rent apartments there since their rents will be the same as the inferior units they are competing against. At most, a vacancy and collection loss of 5 percent would have been acceptable for the subject with 3-4 percent even more appropriate.</li> <li>Expense ratio—Expense ratios for the comparables used in the appraisal were stabilized at 35 percent of EGI, as no expense information was available and this was considered to be typical in the market. The subject however was given a higher expense ratio because it was believed that the nonprofit owners would provide a higher level of maintenance and thus would spend substantially more than market owners. This is a fallacy on both an operational and a theoretical level. If the building is rehabilitated, operating expenses for at least the first few years should be lower than competing market rental units. Additionally, as a nonprofit owner, LHHA could very likely realize lower operating costs (e.g., LHHA was granted a property tax abatement on the subject and secured a below-market-interest-rate mortgage). These subsidies were totally ignored despite the fact that some may be transferable to new owners. Thus an argument could be made that the current expense ratio should be lowered to reflect the above-cited better-than-market operating condition for the subject.</li> </ul> <p>In sum, at worst, an equal-to-market expense ratio should have been applied (35 percent), and more correctly, the subject's expense ratio should have been lower than the comparables (less than 35 percent and surely not 41.3 percent).</p> <ul style="list-style-type: none"> <li>Expense ratio-vacancy factor—The combined effect of applying a more appropriate vacancy factor, say 5 percent, and even conservative expense ratio, say 35 percent, would be to increase NOI to \$49,647—more than 17 percent higher than the derived \$29,939 NOI.</li> <li>Capitalization rate—The appraiser used a capitalization rate (14 percent) derived from the market sales used in the sales comparison approach. The capitalization rates for these sales (ranging from 12.8 to 186 percent) were skewed because of the various degrees of disrepair and deferred maintenance in these sales. It was totally inappropriate to use a market-derived capitalization rate in this instance; it does, in effect, apply a prerehab analysis when, in fact, the subject is being valued after rehab.</li> <li>Capitalization ratio—The appraisal-applied capitalization rate of 14 percent assumes a blended rate for the mortgage financing used and a return on equity for the investment dollars of the owners. Given current market mortgage rates and terms (i.e., 70 percent LTV and 7 percent interest rate), the used cap rate of 14 percent infers an internal rate of return (IRR) of over 30 percent. This is an outrageously high premium and is not justified in the market. A capitalization rate of 10 percent would still have provided an IRR of 17 percent which is more typical in this market and more appropriate.</li> </ul>

*Continued on next page*

**EXHIBIT 9.4 (continued)**

I. Effected Appraisal	II. Critique of Effected Appraisal
<p><b>E. Valuation of the Subject—Cost Approach</b></p> <p>\$386,000 project value (\$27,571 per unit value) based on \$423,190 estimated costs for land, improvements, and renovation, less a 17 percent depreciation factor</p>	<ul style="list-style-type: none"> <li>Given the extensive renovation contemplated for the subject, the 17 percent depreciation factor is somewhat high.</li> </ul>
<p><b>F. Final Determination of Value</b></p> <p>Considering the sales, income, and cost approaches yields a value of \$310,000 (\$22,143 per unit)</p>	<p>Given the same basic information used in the appraisal with all the same comparables, a more reasoned (and correct) market value would be as follows:</p> <ul style="list-style-type: none"> <li>Sales approach—Compare subject to comparables at time of their sale. Comparables at that point are in significantly poorer condition than the subject after renovation. Significant upward adjustment to comparables should therefore be made. Comparables were \$15,000 to \$26,000 per unit; those figures should be adjusted to the highest point on the range taking into account condition. This calculation would indicate comparables at \$25,000 to \$30,000 per unit. The subject is therefore valued at \$385,000 (\$27,500 x 14 units).</li> <li>Income approach—              \$80,400—Gross income              less 5%—Vacancy factor              \$76,380—EGI   <u>\$26,733</u>—expenses—at 35% expense ratio,              leaves \$49,647—NOI  <u>divided by .11</u>—capitalization rate              \$451,336—subject value based on income approach</li> <li>Cost Approach—              \$386,000 determination of value by appraiser is reasonable</li> <li>Value Determination—              Consideration of sales approach (\$385,000), income approach (\$451,000), and cost approach (\$386,000) leads to a final subject value determination of \$430,000 (income approach is weighted more)</li> </ul>

LHHA had to work with a \$310,000 value and this severe discount to the actual project expense illustrates the appraisal hurdle faced by those attempting to do urban, infill rehab.

### *Private Lenders*

An appropriate appraisal is a good start toward, but does not guarantee, financing. LHHA has a good working relationship with private lenders. In fact, as noted, LHHA tries to use private rather than public monies for its up-front acquisition and rehab expenses because of the government subsidies' ancillary requirements and other drawbacks. The private financing utilized by LHHA has taken various forms. LHHA has obtained traditional construction loans from lenders, paying the prime rate plus additional basis points as dictated by the market, and has also availed itself of monies from the Community Reinvestment Group (CRG) whereby Miami-Dade County lenders extend to nonprofits up to 95 percent financing for acquisition–rehab at well below market interest rates. On some recent single-family acquisition–rehab involving a package of three homes financed by CRG, LHHA paid no interest, just principal, on the first two houses, and incurred a nominal charge (3 percent interest) for the acquisition–rehab loan on the third unit.

LHHA also draws on private-sector financing for the permanent first mortgages on the rehabilitated single-family homes it sells. These mortgages, as detailed earlier, have modest LTVs and pose low risk to lenders and, as a bonus, offer CRA benefits.

Rutgers researchers spoke to some of LHHA's lenders. The lenders applauded LHHA's construction and development savvy, its ability to garner multiple subsidies, and the nonprofit's homeownership counseling and other social support services (Powell 1999). At the same time, the lenders spoke of their misgivings—not in the case of LHHA, because this organization has proven itself—concerning affordable-housing rehab financing.

Affordable-housing rehab was viewed by the lenders as being “more difficult” and “harder to realize its goals” relative to affordable new construction (Powell 1999). As such, lenders, as prudent fiduciaries, would tend to demand more equity in the rehab case. This would manifest itself in such ways as tending to loan at lower LTVs on the affordable-housing rehab projects as opposed to the affordable new-construction jobs. Summarized one lender, “For nonprofits, new construction is simpler to do, and simpler to get financing on” (Anonymous 1999).

Lenders also spoke of a cost versus value dichotomy being of greater concern in a rehab setting, with the following example cited:

We can only lend on the basis of value not cost. In a neighborhood of existing \$100,000 homes, the \$120,000 rehab is a reach. We would be more comfortable lending on a \$120,000 new house because new is distinguishable and buyers will pay more for new. (Anonymous 1999)

Some lenders also acknowledged that they were not aggressively involved in government programs to foster rehab financing, such as Title I and Section 203(k). They attributed this to

myriad misgivings, including “the time it would take to learn about the programs” and concern whether “sufficient volume and quality returns could be realized” (Anonymous 1999).

## **CONSTRUCTION PHASE BARRIERS TO AFFORDABLE-HOUSING REHAB**

For the most part, building codes and related regulations do not pose very critical barriers to LHHA’s operations. But there are exceptions, and conditions may worsen in the future.

### **Building Code Issues**

Florida has a statewide building code to which local jurisdictions can add requirements. The statewide code has a “25-50 percent rule,” whereby if the rehab investment exceeds 50 percent of the value of the property, the entire building (not just the rehab work) must comply with new-building standards.

While the “25–50 percent rule” is problematical in many jurisdictions, that is *not* the case for LHHA, in part because of the way the rule is applied; Miami-Dade County excludes construction work not requiring a building permit from the rehab value calculation, so LHHA outlays for carpeting, painting, and other maintenance not requiring a permit do not factor in to the 50 percent trigger. Also mitigating the 50 percent activation is the fact that LHHA acts as its own developer–general contractor. That arrangement allows LHHA to generously count what is “maintenance,” and therefore not be included in the 50 percent trigger, and to parsimoniously value the permitted construction that is factored in to the 25–50 percent calculation. Given such accounting by LHHA, the “25–50 percent rule” has been triggered only a handful of times in this nonprofit’s rehab activities.

A pending rule change, however, will make the “25–50 percent rule” much more of an issue. The change would make the 50 percent mark a cumulative total, whereby all construction (other than unpermitted maintenance noted above), *going back in time over the life of the unit* would be counted. For instance, if LHHA was planning \$10,000 of rehab on a house valued at \$40,000, the “25–50 percent rule” would be triggered if over the course of time \$10,000 of previous permitted construction had been effected. As the properties LHHA is rehabilitating are typically many decades old, they are likely to have had considerable accumulated renovation, so that even modest LHHA construction would trigger the 50 percent rule.

Another pending regulatory change will pose additional problems for LHHA. Heretofore, property owners in Miami-Dade County were *not* held responsible for work done by prior owners that was not permitted or in other ways did not meet prevailing regulations. For instance, if LHHA bought a property that five years earlier had electrical work done by anyone other than a licensed electrician, and 10 years before that had an illegal addition put on, LHHA, as the new owner, would not under current rules have to correct these improperly effected changes. Under the new rule, however, LHHA would be responsible for bringing the structure entirely up to code, and thus would have to deal with the illegal electrical work and illegal addition noted in the above example. As the Little Haiti properties often have had decades of unpermitted and otherwise illegal alterations, the new rule, if applied to the letter of the law, would pose a considerable burden to LHHA.

The above discussion referred to the frequency of unpermitted construction work. LHHA acknowledges that even as a proficient and experienced contractor, it encounters long delays in applying for electrical, plumbing, and other permits; days if not weeks elapse before the permits are issued. This is even more daunting for the lay owners of Little Haiti's properties, and many owners/tenants elect to work outside the official system. LHHA also notes a catch-22 situation with respect to permitting. LHHA cannot apply for a permit until it officially owns a property; yet it cannot start construction until a permit is issued. Thus many weeks may elapse between the time LHHA acquires title and begins paying interest charges and its receiving all the permits necessary to begin rehab.

### **Minimum Housing Standards**

Regulatory issues are compounded when public monies are used for the acquisition-rehab; hence, the previously described reluctance of LHHA to use public subsidies up front. As an example, when county surtax assistance is used, or when HOME or other federal aids are drawn upon, the Participating Jurisdictions (PJs) make the acquisition-rehab funding contingent upon satisfying a host of building standards, including full compliance with a stringent interpretation of the Miami-Dade County Minimum Housing Standards (MHS). This leads to costly replacement of many items that still have a useful remaining economic life (REL). Illustrative situations include the following:

**REPLACING ROOFS.** A roof of a property being rehabilitated may have a REL of at least moderate duration (i.e., five to seven years). Many Little Haiti single-family detached homes retain their original tile roofs. These are attractive and can provide many years of service. Despite this, the PJs administering the public subsidies may interpret the MHS as requiring a new roof. The cost on a single-family detached home is about \$3,500, and the replacement roof of vinyl-asbestos is not as attractive as the original tile.

**REPLACING WINDOWS.** LHHA prefers to keep the existing windows and make only necessary repairs. In a house with jalousie windows, common in Little Haiti, LHHA would prefer to replace glazing and window operators as needed. For the 10 to 15 windows in a typical Little Haiti single-family detached home, the above-cited repairs would cost about \$1,000 in total. The PJs, however, frequently interpret the MHS as requiring new windows in an older home and make such replacement a condition of awarding acquisition-rehab subsidies.

Replacing windows in South Florida is no simple matter in the wake of Hurricane Andrew, where much window damage was sustained. In the aftermath of that storm, window standards were upgraded. The new requirements mandate that engineers must first do wind-load calculations, taking into account the building's footprint, peak, height of eaves, zones (e.g., windows at the corner of a house are more vulnerable to damage), and other measures. The wind-load calculation determines the type of window to be purchased with respect to its impact resistance, need for hurricane shutters, and other material characteristics. Further, before the windows are installed, a permit has to be pulled and the installation inspected. This gamut of window-replacement activities is quite costly. LHHA estimates that its expenses for the purchase and installation of the 10 to 15 windows in a typical Little Haiti single-family detached home are \$3,000 to \$4,500—as against the \$1,000 for the selective rehab of the existing windows.

REPLACING THE ELECTRICAL SYSTEM. Little Haiti homes acquired by LHHA frequently need to have their electric panels replaced, along with other electrical work. Yet instead of simply repairing/replacing what is necessary, the PJs, citing the MHS, will often mandate redoing the entire electrical system. This typically entails breaking through plaster walls, which then have to be repaired. One of the few times the 50 percent building code rule was triggered in Little Haiti's rehab was when an electrical replacement (and other factors) forced it to break through walls, increasing the rehab outlay to the 50 percent trigger.

Even without the escalating cost of construction work related to electrical replacement, LHHA's expense for redoing the electric system is \$5,000 to \$6,000 per single-family unit. By contrast, limiting the work to electric panel replacement and selective repair results in a price tag of about \$1,500.

OTHER SYSTEM REPLACEMENT. The theme noted above is repeated in other areas. Instead of simply replacing the main shutoff and doing plumbing repair, the redo of the entire plumbing system is mandated; septic systems are not repaired but instead are replaced at a cost of \$1,500 to \$2,000 per single-family unit; and rather than simply replacing the rotted floor joists in the bathroom, much more structural framing work is required by the PJs.

The mandate of replacement instead of repair is not only an issue when public subsidies are involved and disbursed by the PJs; a building inspector in an unsubsidized rehab job could also cite the MHS as a basis for system replacement. In practice, however, LHHA finds that the escalation from repair to replacement is much more common when surtax, HOME, and other subsidies are drawn upon. This more extensive intervention is prompted for two reasons. First, as the funding authorities, the PJs may mandate system replacement as an appropriate public policy for the sustainable improvement of deteriorated properties. Second, even when replacement is not a programmatic requirement, building inspectors on a subsidized rehab job will often require more extensive intervention, thinking that major work should be done when there are subsidized funds to pay for it.

LHHA is not unsympathetic to the position that systemic systems replacement at the time of rehab will reduce the need for repair and replacement in the future. LHHA is committed to the long-term success of its rehabilitated units, and to that end makes available counseling and other support programs. LHHA also recognizes that replacement of systems can lead to operational efficiencies (e.g., new windows will reduce heating/cooling costs).<sup>3</sup> Yet LHHA argues that by not taking advantage of the remaining economic life of major systems, when that life is at least of moderate duration (i.e., five to seven years), a significant benefit of rehab—capitalizing on what exists—is lost.

LHHA suggests that it would be possible to meet the goal of maximizing the utility of existing buildings through selective rehab (i.e., repairing where possible and replacing when necessary) while at the same time protecting against unaffordable major repairs/replacement by establishing a homeowners' replacement reserve. This would work as follows: LHHA would do selective rehab as opposed to total systems replacement, a strategy that could save perhaps \$5,000 to

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<sup>3</sup>Ironically, this does not have much practical import for LHHA's Haitian clientele. The major utility cost in Florida is for air-conditioning, and the Haitians tend to use minimal air-conditioning.

\$10,000 per unit in construction costs on its single-family rehabs<sup>4</sup> (LHHA currently spends a total of about \$30,000 in renovating these units). The \$5,000 to \$10,000 saving would allow LHHA to reach still lower income families and/or draw less in subsidies. Before the rehabilitated units would be transferred, LHHA would estimate the remaining economic life of the system it was not replacing and would calculate the present value of replacing these systems a stipulated number of years into the future. That amount could be set aside each month in a replacement reserve.

### *Environmental Clearance*

When LHHA utilizes subsidies upfront for its acquisition–rehab, it must obtain environmental clearance. The latter entails meeting a series of environmental regulations regarding lead paint, asbestos, historic preservation, archeological, and other matters. The process of satisfying environmental requirements is often time-consuming.

LHHA encounters the most delays when dealing with historic preservation. Since federal monies are often involved in the acquisition–rehab subsidies it acquires, the Section 106 process of the National Historic Preservation Act (NHPA) is evoked. Under Section 106, when there is a federal “undertaking” (and federal subsidy for acquisition–rehab constitutes an “undertaking”), an opportunity must be afforded for considering the impact of the undertaking on resources either listed on, or eligible for, the National Register of Historic Places, itself instituted by the NHPA. Thus, each property to be rehabilitated by LHHA utilizing federal funds is evaluated as to whether it is historic register listed or eligible, and if so, the compatibility of the intended rehab with the property’s historic character.

While there are some historic buildings in Little Haiti, the houses LHHA works on are generally not strong candidates for historic designation; in fact, not one has thus far been deemed historic. Nonetheless, each house to be rehabilitated is evaluated as to its historic candidacy. This review is administered by the Miami-Dade County Office of Community and Economic Development (OCED), which forwards each file to Florida’s State Historic Preservation Office (SHPO) for its input. OCED, however, waits until it has a number of properties to be reviewed before it forwards the files to the SHPO, and hence, time is lost.<sup>5</sup>

This process has sometimes left LHHA in a costly limbo. In the instances where it is using subsidized funds for the acquisition–rehab, it cannot begin the work until environmental clearance has been secured. Yet clearance is frequently delayed for weeks while the historic review is undertaken. In the meantime LHHA is incurring costs (typically \$25 to \$50 daily) for the housing unit it has purchased and has slated for rehab (St. Louis and Francois 1998). LHHA does not have the luxury of delaying closings until after the environmental clearance has been secured, because sellers demand an outright sale with a quick closing, not a contingency sale or

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<sup>4</sup>The single-family homes tend to be in better shape than the multifamily units rehabilitated by LHHA, and as such the former have more systems lending themselves to repair as opposed to replacement.

<sup>5</sup>It is likely there was not adequate staff or budget by those doing the historic preservation review. If LHHA filed a master plan to the city preservation officer it is possible the historic reviews could have been done in bulk. It is questionable, however, which one would be faster. If the entire area was surveyed and LHHA waited for that survey, it may be waiting for research on a lot of buildings that are irrelevant to LHHA’s goals.



one with a delayed closing. The result of these entanglements is weeks of delay and many hundreds of dollars of extra holding costs.

LHHA suggests that a better way would be for public authorities to survey the entire Little Haiti neighborhood and summarily identify which properties are historic. That would satisfy the historic preservation protection mandate while avoiding the property-by-property review that contributes to the delay in the environmental clearance.

### **Tradespersons and Other Construction Issues**

In doing new construction, where jobs tend to be larger, or in effecting a large renovation job, subcontractors are often hired. As LHHA's rehab volume is modest-scaled, it cannot afford a subcontractor. Notes LHHA, "We can't find subs because we are not large enough, or if we find a sub, he would charge an arm and a leg because of our small jobs" (Allen 1999). Consequently, LHHA has opted for an in-house work crew. Another reason for this approach is perceived quality-control benefits. LHHA's construction manager explains:

With new construction, work quality is less open to debate. With rehab, that is not the case. A sub will say, "It is the best I can do given that the floors are uneven or the walls are out of plumb." With your own crew, you know your men and can better control quality. (Allen 1999)

The downside of an in-house crew is the pressure of maintaining a steady flow of work to keep the crew occupied. Given the ebbs and flows of LHHA's housing activity, during which delays in property acquisition, closings, and the like can lessen the immediate demand for construction, keeping LHHA's construction crew efficiently at work is often challenging.

LHHA has not found it problematical to secure skilled workers; many Haitians have construction experience. LHHA has capitalized on this by predominantly hiring skilled locals. LHHA has, however, made efforts to improve construction productivity. For instance, the organization is currently contemplating making the rehab of each house the responsibility of a designated worker. This approach would clarify lines of authority and would also encourage that worker to operate more responsibly and efficiently (e.g., the designated worker would plan ahead and order materials on Friday for Monday delivery and installation).

LHHA acknowledges the construction challenges of its work. Despite trying to keep a constant flow of work, the vicissitudes of property acquisitions, closings, and the like have led it to vary its in-house construction crew from 5 to 13 members. LHHA also speaks of inherent inefficiencies in its rehab efforts. These include the following:

1. *Minimum charge requirements.* A concrete truck may have a five-yard minimum charge at \$45 per yard. LHHA will have to pay the \$225 cost despite often needing only a yard or two on a rehab job at any one time. As another example, the smallest dumpster may have more capacity than LHHA needs yet nonetheless it must pay the \$350 dumpster fee. Also, proportional to the amount of construction, such temporary construction provisions as a

fence, toilet, and temporary power and water are more costly in rehab than in new-construction jobs.

2. *Material delivery in small quantities is costly and time-consuming.* A lumberyard may charge the same \$50 delivery fee for \$500 or \$2,000 worth of materials. Rehab often requires smaller amounts of materials, so the proportional delivery cost is higher. Also, determining the materials needed is harder with rehab than new construction jobs since the latter allow a more standard, predictable calculation. If on the rehab job construction materials run short, work may have to stop to await resupply.
3. *Security.* Security tends to be more expensive for rehab versus new construction. It is less expensive to put one fence around, say, five contiguous houses being newly constructed on one block than to install five separate fences around five scattered houses being rehabilitated in a neighborhood.

A fence is not always installed on a rehab job. Because of the adverse impact it will have on adjacent occupied houses, LHHA often forgoes a security fence. While it may be a neighborly gesture, an unfenced site is a security challenge.

4. *Other.* LHHA must do certain construction jobs that are unique to its rehab focus. Many properties in Little Haiti have had illegal structures built on their properties that were then illegally rented as dwellings. Also common is the illegal conversion of a garage to a rental unit. When LHHA acquires such properties, it must gut the illegal units to bring them up to code, a process involving labor, removal of materials, and other expenses. Such costs would not be evoked in new construction.

To be certain, some of the costs noted in this section, such as minimum charge requirements, do not loom large in the entire construction budget. Yet they do add expenses, and in linked ways can add to the aggravations of the job. For instance, lumber ordered for replacing joists in a bathroom may be lost due to theft at an unfenced house being rehabilitated. This situation may require another delivery, at a proportionately high charge, and in the interim, the carpenters on the job slotted to do the joist replacement are underutilized.

## **CONCLUSION: BARRIERS TO AFFORDABLE-HOUSING REHAB**

The rehab obstacles encountered by LHHA are especially poignant in a state such as Florida, where new construction faces far fewer barriers. About one hour from Little Haiti, in places such as Homestead and Florida City, there is a mushrooming of inexpensive new construction. In these places, approved unimproved land for single-family homes can be had for \$7,000 a lot—about one-sixth what Little Haiti pays for its FHA single-family foreclosures. This raw land can often be tied up at low cost by option; in contrast, LHHA does not have this luxury, but must purchase properties outright. New construction, starting with a clean slate, will tend to have fewer permitting issues than rehab. Further, the new construction done in places such as Homestead and Florida City is done en masse, and as such realizes economies of scale in labor, materials, and appliances; Little Haiti, by contrast, suffers from diseconomies of scale. It is no

wonder that the path of least resistance is to new construction rather than rehab, much less the infill, urban rehab practiced by LHHA.

LHHA is committed to improving conditions in Little Haiti. To that end, it has no option other than to do infill, urban rehab. It is doing this renovation despite the myriad obstacles discussed earlier—a tribute to its perseverance. Yet LHHA’s executive director has reservations about the organization’s current scale of operations:

LHHA is doing about 15 single-family rehabbed units a year and every so often a small multifamily. At this pace, we will be permanently relegated to mediocrity and co-dependency with our funders. To have a critical impact, we should be doing at least 50 to 75 units annually and that volume will also make our operations more efficient. . . . Funders must also recognize that rehab is its own method of housing delivery and has to be nurtured. (Harder 1999)

Achieving a higher level of housing rehab activity and “nurturing” will require addressing the many obstacles noted in this study. While a detailed blueprint to that end is beyond the mandate of the current case analysis, we close by noting that LHHA is working on resolutions to its many obstacles. It is putting together a financial plan to raise about \$500,000 in private capital. This would allow LHHA to effect a much higher volume of acquisition–rehab without being constrained by the protracted timing cycle and programmatic requirements of public subsidies. Other strategic responses being considered include the following:

1. LHHA would be appointed a receiver of neglected properties. This would curb the further deterioration of these homes and, ultimately, by foreclosing on its receiver repair liens, LHHA would acquire the properties and rehabilitate them.
2. The PJs would permit selective rehab as opposed to requiring blanket replacement of systems. In addition, homeownership maintenance reserve accounts would be established on the properties being selectively rehabilitated.
3. Processing bottlenecks would be reduced, such as supplanting the property-by-property historical review being done in Little Haiti with an areawide historical inventory. Also, applications for building permits could be submitted even before title to a property has been transferred in order to expedite the permitting process.

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## **CHAPTER 10**

### **Rehab Barrier Case Study: Chicago, Illinois**

#### **SUMMARY OF FINDINGS**

Interviews with key developers, city officials, an architect involved in the design of affordable housing, and syndication firms were undertaken to identify barriers to affordable-housing rehab at various stages in the development process: development (acquisition, financing, and zoning, etc.), construction, and occupancy. The research revealed that there have been few projects involving the rehab of nonresidential buildings for conversion to affordable housing. Based on our discussions with affordable-housing providers, this is likely attributable to a variety of factors including the lack of nonresidential buildings in areas with services necessary to support residential uses (e.g. grocery stores, public transportation, and other retail stores) and the difficulty of conversion of some nonresidential buildings to residential use. Adaptive reuse has been most common in the conversion of industrial loft buildings. Many of these buildings are more easily convertible to residential use than other non-residential buildings because of the flexibility offered by an open floor plate and expansive floor-to-ceiling heights.

Based on our interviews, the barriers at each stage of the development process are as follows:

#### **Economic Constraints**

Based on the information revealed in the Chicago case study, the cost of rehab does not limit or impede rehab and the production of affordable housing any more than the cost of new construction. In both instances, the cost of production exceeds the property owners' or tenants' ability to pay.

#### **Development Phase Barriers**

Development barriers generally revolve around acquisition and financing, and are often intertwined. Acquisition barriers usually are associated with the difficulty of finding appropriate buildings, at a reasonable price, in neighborhoods with sufficient residential support services.

Interestingly, we did not find that the typical financing barrier related to the ability to obtain financing (at least with the experienced developers we interviewed). Instead, the financing barriers related to the extended time frames in the application and approval process. We found that such time frames can result in a developer having to hold or control a property for 12 months to 18 months or more before financing is closed and construction can begin. This is especially onerous for not-for-profit developers because of the general lack of predevelopment funds and financing.

Other development barriers concerned parking and other requirements in the local zoning code.

## **Construction Phase Barriers**

The construction barriers focused on some building code issues, accessibility requirements, and increased costs resulting from compliance with Davis-Bacon requirements. The only barriers identified associated with compliance with the Secretary of Interior's Standards for Rehabilitation revolved around the necessity of keeping some interior features. These were reported to be minor issues.

This case study revealed that the primary barriers to affordable-housing rehab concerned acquisition and financing. None of those interviewed expressed frustration with the application or administration of the Secretary of Interior Standards. Few of the developers we interviewed regularly use the historic tax credit in conjunction with an affordable-housing rehab. This appears to be due to the availability of other financing tools (low-income housing tax credits, the Affordable Housing Trust Fund, and other public and private lending sources) rather than to any difficulty with the application and review standards. In fact, when a developer wants to use the historic tax credit, state and local funding awards are often reduced by the amount of the historic tax credit, thus reducing the value of the incentive. When the historic tax credit is used, it is typically as a source of gap financing (see interview with Jack Markowski related to the rehab of the Hilliard Homes).

The applicability of the historic tax credit is further limited by the "economic substance" requirements under the IRS code. Relaxation of the economic substance requirements in connection with affordable-housing rehab would likely increase the use of the historic tax credit. In addition, expansion of the 10 percent credit (historic tax credit for buildings built prior to 1936) to allow its use for housing rehab, would increase the use of the historic tax credit.

## **BACKGROUND**

### **Chicago, Illinois**

The city of Chicago, the third most populous city in the United States, was chosen as a case study because of its large inventory of buildings used for housing or convertible to housing, substantial activity in rehab, significant activities in the use of the low-income housing tax credit (LIHTC) and rehab tax credit (RTC) programs, and its size and location in the Midwest. The purpose of the Chicago case study is to highlight issues of barriers to affordable housing in adaptive reuse.

Since 1994, the city of Chicago has experienced a housing renaissance. In the central area, more than 16,700 residential units have been created, including approximately 5,600 condominium conversions, 5,100 loft redevelopments, and more than 6,000 newly built condominiums and townhomes. Many neighborhoods outside of the traditional lake-front locations have also experienced significant gains in new and rehabilitated housing units. Large public housing projects are being demolished and replaced with low-rise town homes, and detached single-family mixed-income housing units. Still, the need for affordable housing is enormous. As housing prices and rental rates increase, the pressure to provide affordable housing mounts. The housing renaissance simply puts more pressure on private developers and not-for-profit

organizations seeking to provide affordable housing: prices escalate for buildings suitable for rehab and conversion to affordable housing, buildings cannot be found in desirable locations, and the cost of production continues to climb.

## **REHABILITATION DESCRIPTION**

This study reveals that, compared to new construction, rehab in Chicago is often nonstandard, less predictable, smaller in scale, burdened by more stakeholders, and requires more administration. Many of the materials used in rehab must be specially milled or adapted to the particular project, unlike new construction where buildings are designed to be standardized. However, when dealing with residential rehab many of the mechanical, electrical, and plumbing systems that are standard in the industry can be used with relatively little adaptation to rehab.

Rehab in Chicago is undoubtedly less predictable than new construction. Only after demolition has been completed can the developer and contractor accurately predict the scope of the rehab project, structural needs, and, in some cases, room and mechanical configurations. Experienced developers, contractors, and architects do an excellent job of reducing the risks resulting from the less than optimal predictability; nevertheless, uncertainty is the norm until the rehab project is well under way.

This case study reveals that, generally, rehab projects are of a smaller scale than new construction. Many factors can impact the size of the project. There is an economy of scale of management—in other words, the project has to be of a certain size to make management costs reasonable. In addition, the typical old or historic building that is being converted to residential or simply being rehabilitated for residential reuse is smaller than is typically constructed in today's marketplace. However, some projects, such as the rehab of the 700-unit Hilliard Homes (public housing) are as large or larger than new-construction projects currently under consideration. Size can impact the type of developer or investor that will get involved in a particular project. Some developers will not undertake projects and some investors will not invest in projects that are smaller than a certain size because of internal hurdle rates and administrative costs of dealing with smaller projects.

It is common to find more stakeholders involved in a rehab project compared with a new-construction project. However, unless the rehab involves a historic building, the stakeholders usually arise from the layers of investors and lending agencies that it takes to make an affordable-housing rehab work. There are a few cases where neighborhood opposition to a particular housing type (e.g., supportive housing) may impact the rehab of a building for housing, but these cases seem to be limited. Instead the stakeholders are a wide variety of private lenders, and local and state government agencies that provide the numerous layers of financing for a project.

Administration of rehab projects appears to be somewhat more intensive than for new construction. While funding sources require compliance with Davis-Bacon and require intensive “financial” management, this is not different for new construction or rehab. However, construction administration by the architect and the project manager is likely to be more

intensive with rehab because of the variety of unknown conditions and changes that are necessary after beginning construction.

## **ECONOMIC CONSTRAINT BARRIERS TO AFFORDABLE-HOUSING REHAB**

A gap exists between the cost of producing affordable residential units through rehab or new construction. The state and local government funding programs, low-income housing tax credits, historic tax credits, and private lending programs bridge these gaps to allow the private sector to attempt to meet affordable-housing needs. According to those interviewed, the HTC more than offsets the cost of historic rehab; the HTC is used where a financing gap exists even after taking advantage of the other government financing programs.

## **DEVELOPMENT PHASE BARRIERS TO AFFORDABLE-HOUSING REHAB**

A number of potential barriers have been identified during the different stages of the development process. We have investigated the following as part of our case study.

### **Obtaining Properties**

The acquisition of properties that are appropriate for rehab for residential use is difficult. First, there are fewer and fewer properties located in desirable neighborhoods (those with good public transportation service, shopping districts, etc.) that can be acquired at a price that makes rehab for affordable housing economically feasible, even with significant government incentives. Second, in the case of adaptive reuse, the most adaptable buildings for conversion to residential uses are typically industrial loft buildings. These are not frequently located in areas where there are significant services. In addition, many loft buildings close to the downtown or in other desirable locations have already been converted to meet the demands of the higher end housing market. Third, the most significant issue relating to acquiring properties is the length of time necessary between entering into a purchase contract and closing as a result of the significant application period for financing from the low-income housing tax credits, state trust fund, and other city programs.

The difficulty in finding appropriate buildings in desirable neighborhoods is best illustrated by our interviews with representatives from LR Development and Lakefront SRO. LR Development is a private, for-profit developer that focuses part of its energies on developing affordable housing using the low-income housing tax credit. Until recently, LR Development had a geographic focus on the North Side of Chicago. However, due to increasing real estate prices and the lack of buildings suitable for affordable housing, LR has expanded its reach beyond the North Side. LR's most recent affordable-housing project, which is planned for rehab in 2000, is located in the South Shore neighborhood south of Hyde Park. LR Development has recognized that it must move beyond its traditional geographic boundaries to continue to develop affordable housing.

Lakefront SRO, a not-for-profit organization, is focused on the development of supportive housing. Lakefront focuses on the rehab of existing buildings that were originally designed as residential hotels. However, Lakefront is undertaking its first new-construction project on the



Near South Side; this will be its largest project to date. The difficulties for Lakefront relating to acquisition concern the length of time that the organization must have control of the property before it is awarded and closes on low-income housing tax credits and other financing. The “holding” period can range from 12 months to 18 months or more. This is a lengthy period that hinders Lakefront, and other not-for-profits, from acquiring properties; this is a significant problem since most not-for-profits do not have significant predevelopment funds available to self-finance options and earnest money.

### **Estimating Costs and Obtaining Insurance**

Those interviewed for the Chicago case study reported few, if any, problems with estimating rehab costs. Most admitted that development pro-formas for rehab projects require a higher construction contingency than for new construction; however, all were experienced in dealing with such cost issues.

Those interviewed, however, admitted that rehabilitation is undoubtedly less predictable than new construction. Only after demolition has been completed can the developer and contractor accurately predict the scope of the rehabilitation project, structural needs, and, in some cases, room and mechanical configurations. Experienced developers, contractors, and architects do an excellent job of reducing the risks resulting from the less than optimal predictability; nevertheless, uncertainty is the norm until the rehabilitation project is well under way.

There were no reports with problems or excessive costs related to insurance.

### **Obtaining Financing**

The representatives of the organizations we interviewed focused on projects that require allocation of low-income housing tax credits from the state of Illinois or the city of Chicago. In fact, none of these organizations reported that they have ever been denied an allocation from the state or city. We found that, in most cases, the financing available through state and city programs is sufficient to make the proposed projects financially feasible, though in some cases a small private first mortgage may be necessary to fill the financing gap. For example, LR Development has obtained a \$400,000 first mortgage from a private institution for its \$5 million rehab project on Chicago’s South Side (Cregier Apartments).

We found that few of the projects that were described to us had a financing gap after awards from state and city programs. The Chicago Housing Commissioner, Jack Markowski, described the most significant gap. The project involves the rehab of 700-unit Hilliard Homes for affordable housing. The estimated rehab costs of \$75 million to \$80 million could not be financed completely through low-income housing tax credits and other affordable-housing programs. As a result, the developer will take advantage of the historic tax credits, which will generate equity of about \$10 million.

As discussed above, the most often reported problem with financing is the length of time a developer has to hold a property before financing is awarded. This is an issue for not-for-profit and for-profit developers.

## **Land-Use Restrictions**

The most significant land-use restrictions that impacted the development of affordable housing related to parking requirements. Representatives of Lakefront SRO reported that single-room occupancy zoning requires fairly insubstantial off-street parking—one parking space per 10 units. However, if family housing is included in the SRO mix, parking requirements can increase to one space per unit. Little consideration is given to the important fact that these buildings are typically located in areas well serviced by public transportation, nor does it consider the income levels of the individual tenants. It is very difficult for many to own and maintain an automobile; this makes even nominal parking requirements somewhat excessive particularly when considering the costs of purchasing “extra” land for parking.

An architect also reported that parking requirements are excessive. He pointed out one project targeted to the elderly that was required to provide one off street parking space per unit. He believed that this was far in excess of actual needs.

Hispanic Housing Development reported that changing zoning to residential use in a conversion project was somewhat difficult because neighborhood residents were reluctant to allow more affordable-housing development into the area. Some of the opposition was a result of a bad experience with a previous developer.

## **Other Development Phase Barriers**

Few other issues were identified as problems. The representative of American Housing LLC suggested that soft costs (architect’s fees) are somewhat higher for rehab than new construction. However, this is limited when dealing with architects that are experienced with rehab issues.

## **CONSTRUCTION PHASE BARRIERS TO AFFORDABLE-HOUSING REHAB**

Construction issues typically relate to codes and regulations and trades. The following issues were identified in our case study.

### **Building Codes/Regulations**

We found that the code and regulatory issues that were most significant concerned sprinklers and accessibility. The representative from LR Development and Dennis Langley, an architect interviewed for the case study, reported that sprinkler requirements can be overly restrictive. While sprinkler requirements can add significant costs to a project, the requirements are most difficult to deal with when the project requires only a moderate rehab as compared to a substantial rehab. Tearing out ceilings and walls to create space for piping, risers, and sprinkler heads can add substantial costs to an otherwise moderately scaled project.

Langley identified other code issues that have impacted projects that he has undertaken. For example, in the conversion of a four-story loft building to residential use, interior roof access was required to comply with the city’s high-rise codes. Also, he suggested that the BOCA code

allow propping open of fire doors for purposes of providing ventilation while the Chicago code does not. Both of these code issues increase the costs of providing affordable housing.

Accessibility issues were frequently identified as the most significant regulatory issue. Creating areas of safe refuge, expanding existing elevator shafts and replacing elevator cabs have a significant cost impact. In addition, Langley reported that accessibility requirements can, at times, be difficult and somewhat costly to comply with depending on the type of residential housing (e.g. supportive housing units tend to be small, requiring increasing the unit size and bathrooms size to accommodate wheelchair accessibility). Also, Langley suggested that there are buildings, such as smaller walk-ups, that cannot accommodate elevators.

The Secretary of Interior's Standards for Rehabilitation and local historic landmarks review were not identified as significant issues in the rehab of buildings for affordable housing. The representative of Hispanic Housing Development Corporation reported that a Section 106 review went very well. Langley reported that while window issues are a big part of the historic review process, windows have not posed a significant challenge on the projects that he has undertaken. From his perspective, the more significant issue is accommodating interior elements such as unit trim and ceilings when trying to design new mechanical, electrical, and plumbing systems. Saving existing plaster or replicating plaster details can add significant costs to the rehab project.

### **Environmental Regulations**

We found that environmental regulations were not a significant barrier when undertaking a substantial rehab. More issues arose when a moderate renovation was contemplated. The representative of Hispanic Housing reported that when converting a nonresidential building to residential there was more of a likelihood of facing environmental issues. For example, Hispanic Housing spent \$70,000 to remove an underground storage tank from the basement of an industrial building. This is less likely to be an issue in a building historically in residential use.

### **Trades**

We found no information related to the difficulty of finding or training qualified trades people. However, the construction industry is under significant pressure because of the large amount of construction and rehab taking place in the city.

The representative of Hispanic Housing reported that the more significant issue relating to the trades is educating and training the contractors and subcontractors complying with the regulations concerning Davis-Bacon. A significant amount of paperwork must be completed and maintained to ensure compliance with the regulations; there is a hidden cost in the educating, training, and compliance issues related to the regulations that go beyond the more measurable cost of "prevailing wages."

We found that all of those interviewed agreed with the purposes of Davis-Bacon but many found that the regulation increased costs unnecessarily in smaller projects where local, nonunion tradespeople would traditionally be employed. Some reported that in some cases prevailing wage rates exceeded union rates.

## **Occupancy Phase Barriers to Affordable-Housing Rehab**

Occupancy issues were not a major concern of those interviewed. The representative of American Housing LLC reported that ongoing maintenance costs are likely to be higher for a rehabilitated building as compared to new construction. However, he had no evidence of this. Ongoing maintenance costs are likely to be impacted by the level of rehab. For example, in a moderate rehab where little work is undertaken on the exterior shell, maintenance issues are likely to arise faster than those buildings that undergo more significant rehab or buildings that have been newly constructed.

In sum, there are substantial barriers to affordable housing during the development and construction process. Most of these barriers concern acquisition, lining up financing, zoning regulations, and building codes. There is little evidence, based upon our work, that regulations relating to historic preservation and design are barriers to the affordable-housing rehab.

## **CHAPTER 11**

### **Rehab Barrier Case Study: Seattle, Washington**

#### **SUMMARY OF FINDINGS**

Compared with many sister cities, Seattle is growing in population and is enjoying economic prosperity. These forces are helping support rehab and adaptive reuse in Seattle, but, as elsewhere, rehab in this city confronts numerous hurdles.

#### **Economic Constraints**

There is a gap between the costs of rehab and the ability to afford these expenses by income-constrained households. The gap is addressed through tapping layered subsidies, such as combining the low-income housing tax credit and the historic rehab investment tax credit.

#### **Development Phase Barriers**

##### *Acquiring Properties and Estimating Costs*

“Hot” real estate market complicates property acquisition for affordable rehab. Experienced parties doing rehab are adept at estimating costs. Nonetheless, this task is challenged by the inherent uncertainties of rehab and the inadequate time and resources typically afforded to architects and other professionals asked to do the estimating.

##### *Land-Use Restrictions*

Seattle’s off-street parking and open space requirements, especially the former, are a rehab barrier. For instances, it is very hard to retrofit into existing buildings a Seattle requirements that 1.3 off-site parking spaces be provided per housing unit.

#### **Construction Phase Barriers**

##### *Building Code*

Unlike other jurisdictions where the building code is governed by an archaic “25–50 percent rule” and code administration is often “by the book,” the building code situation is much more positive in Seattle. Nonetheless, building code issues are found in this city (e.g., when substantial alterations are done), and they are exacerbated in adaptive-reuse situations.

##### *Historic Preservation*

Historic preservation is an important theme for Seattle’s rehab activity, and the city offers special incentives for landmarks. Nonetheless, issues arise concerning such matters as interpreting the standards to be applied for the historic investment tax credit.

### *Access Requirements*

While the state of Washington access code allows flexibility in satisfying access requirements, the city's topography (e.g., sloped streets) and historic pattern of development (full lot coverage), as well as the inherent difficulty of retrofitting access, make it challenging to meet the access mandate.

### *Other Issues*

Adaptive reuse of nonresidential to residential applications sometimes encounters "brownfields" issues.

By strengthening an in-city Seattle housing market, growth management is a positive rehab force. At the same time, the strength of the city market sometimes encourages demolition of existing properties for redevelopment to more intense purposes. Thus, instead of renovating an existing single-family or two-family home, the building might be demolished in order to construct an apartment house.

## **BACKGROUND**

The city of Seattle, a community of 84 square miles, is located in King County, in the state of Washington. Seattle's 1990 population was 516,259. Of that total, 388,858, or 75 percent, were white, and 51,948, or 10 percent, were black. As of 1990, the city contained 246,476 households. There were 236,202 occupied housing units, with roughly an even mix of owner-occupied and renter-occupied homes.

In recent years, Seattle has enjoyed a measure of prosperity. Certainly not everyone was doing well; as of 1990, 12.4 percent of Seattle's residents were in poverty. Overall, however, there were many positive signs. Seattle's median family income in 1989 was \$38,860—almost 10 percent higher than the Washington statewide median family income in that year of \$36,705. Adjusted for inflation, average income for Seattle residents has increased approximately 5.8 percent since 1990, a gain greater than the national average. A relatively well educated population has contributed to the city's good economic times. Whereas only about a tenth of the U.S. population has more than four years of college, in Seattle that share is one-quarter (City of Seattle 1998).

Seattle has been experiencing rapid growth. Between 1990 and 1996, population grew from 516,259 to 536,600, households from 245,476 to 258,433, and employment from 419,800 to 467,000. This growth has fueled housing costs increases. From 1970 to 1997, average Seattle house values increased by about 850 percent and average rents rose over this period by about 400 percent, the latter roughly the same percentage as the 1970 to 1997 gain in the average city household income (City of Seattle 1998).

Population growth is anticipated to continue in the future. Seattle is expected to grow by 72,000 to about 600,000 people by 2014. The rest of King County is expected to grow at an even faster

pace. Over the next 20 years, Seattle expects to add about 140,000 new jobs (City of Seattle 1999).

In contrast to the city settings of many of our other case studies, such as Trenton, New Jersey, and New Haven, Connecticut, which have lost population and are disadvantaged economically, Seattle is growing in residents and is doing well economically. Thus, by studying Seattle we get a glimpse of the barriers to affordable-housing rehab in a “hot” real estate market. Not coincidentally, Seattle is our only case study city where growth management is being actively pursued, so we shall also examine some of the influences of growth management on affordable-housing rehab.

In our other case studies, we typically focused on a specific organization, building, or regulation (e.g., New Haven NHS in Connecticut, Wetherhill-Mount House in South Brunswick, New Jersey, and Section 34 in Massachusetts). In the Seattle case study, we have a more generalized orientation on the subject of barriers to affordable-housing rehab. To that end, we spoke to a variety of experts on housing rehab in Seattle, including: Mr. Ronald F. Murphy, an architect-partner at the firm of Stickney, Murphy, Romine; real estate consultants-developers Ms. Maria Barrientos (Real Estate Development Services), Mr. Scott Norland (Kauri Investments, Ltd.), and Mr. Val Thomas (Val Thomas Inc.); Seattle City officials Ms. Karen Gordon (Seattle’s Historic Preservation Officer) and Mr. Rick Hooper (Seattle’s Office of Housing); and individuals working in Seattle nonprofit organizations, Mr. Chuck Weinstock (Capitol Hill Housing Improvement Program) and Ms. Sharon Lee and Mr. Matthew Flickinger (Low Income Housing Institute). What follows is a summary of the barriers to affordable-housing rehab observed by the individuals cited above.

### **ECONOMIC CONSTRAINT BARRIERS TO AFFORDABLE-HOUSING REHAB**

Although Seattle is home to many well-educated and well-paid residents, there are exceptions. Homeless people are seen in front of coffee shops and microbreweries catering to the affluent. Others, while not homeless, are facing severe housing affordability problems. One such individual is a college student with multiple sclerosis who relies on a \$450-a-month subsistence check (Angelos 1992). When his landlord raised the rent to \$375 per month, the student clearly was challenged to pay for shelter. That problem was solved when the student rented an apartment for \$185 a month in the Larned, a building rehabilitated by the Capitol Hill Housing Improvement Program (CHHIP).

The Larned is a 33-unit project rehabilitated by CHHIP at a 1992 cost of \$2.8 million, or about \$84,000 per unit. The post-rehab monthly rents ranged from \$175 to \$375 per unit, with most rents between \$175 and \$210 per month (Angelos 1992). Those rents do not support a \$84,000-per-unit outlay. A similar gap between rehab costs and rents is found in other CHHIP rehab projects (CHHIP does new construction as well), as shown below.

Example CHHIP Rehab Project	Year Completed	Building Size (Units)	Project Cost		Monthly Rents
			Total (in \$million)	Per Unit	
Brewster	1994–95	35	\$2.6	\$75,254	\$325–\$500
Fleming	1998	36	\$2.7	\$75,000	\$290–\$519
Centennial	1999	30	\$2.6	\$86,067	\$275–\$485

Source: CHHIP 1999.

Rents are modest in the CHHIP rehabs because this organization aids households earning between 30 percent and 60 percent of the areawide median income (AMI). In Seattle, the current median annual income for households of two members (Seattle's 1990 average household size was 2.0) is \$50,100. Those at 30 percent to 60 percent AMI earn a maximum of \$15,030 to \$30,060 yearly, or \$1,253 to \$2,506 monthly. If rent is capped at 30 percent of income, then the households aided by CHHIP can pay between \$375 and \$750 a month in rent. Those are roughly the rents in the CHHIP rehab projects noted above. That monthly rent-paying capacity, however, does not support a CHHIP rehab cost of about \$80,000 per unit.

The rehab cost-rent gap is bridged by CHHIP securing a variety of subsidies (Weinstock 1999). On its rehab (and new construction) projects, CHHIP has used such aids as: low-income housing tax credits (LIHTC); Affordable Housing Program (AHP) monies from the Federal Home Loan Bank; Local Initiatives Support Corporation (LISC) investment; assistance from the Washington State Housing Trust Fund, the city of Seattle, and the U.S. Department of Housing and Urban Development (HUD) (e.g., HUD Neighborhood Development Demonstration Project, Section 8, and Section 241 (f) programs); Community Reinvestment Act (CRA)-inspired low-cost loans from Washington Mutual Savings Bank, First Interstate Bank, Pacific First Bank, Sea First Bank, and other lenders; "creative financing" (e.g., sale of development rights); and foundation support (e.g., from the Merrill and Skinner Foundations).

CHHIP has also tapped a variety of creative financing mechanisms, including (Capitol Hill Housing Improvement Program 1999, 4) the following:

*Bargain sales:* Sellers of real estate can make a partial donation of equity to a nonprofit buyer such as CHHIP, with the seller then claiming a charitable contribution to reduce tax liabilities. CHHIP has negotiated transactions including nearly \$1 million in such donations over the past five years.

*Tax-exempt financing:* Due to its unique status as a nonprofit development authority, CHHIP can offer tax-free interest to its lenders, thus securing below-market interest rates for loans to CHHIP.

*Partnerships:* CHHIP has crafted and entered into productive relationships with private parties to achieve production and reduce rents. The nature of these partnerships varies from project to project. Examples include leasing relationships, tax-advantaged investments, and "linkages" with commercial developers desiring site bonuses available from promoting low-income housing.

*Property tax exemption:* In 1987, CHHIP organized the effort to change state law so that properties owned by public development authorities serving low-income households are now exempt from property taxes. This enables CHHIP to either reduce rents or increase the amount of conventional debt the property can support.

CHHIP's sister organizations work in similar ways to secure aid from a variety of sources. Seattle's Low Income Housing Institute (LIHI) has developed about 1,400 affordable-housing units; more than half have involved rehab and/or adaptive reuse (Lee 1999). For example, the Frye Hotel, a historically prominent property in Seattle that had come on hard times, was



rehabilitated by LIHI to provide housing for 234 LMI families. As the Frye's LMI residents could not afford the cost of the renovation, LIHI had to secure a layering of subsidies. Frye and other LIHI projects have tapped such aids as the LIHTC; the historic rehab tax credit (HRTC); the Community Development Block Grant (CDBG), Section 8, McKinney and other HUD programs; AHP grants from the FHLB; and Washington and Seattle government supports.

The HRTC is often combined with the LIHTC to create a powerful subsidy for low-income historic rehab. Seattle's Plymouth Housing Group (PHG) acquired the Pacific Hotel located in the downtown area. Built in 1916, this property traditionally had provided transient housing; it had closed by the 1980s. PHG, a homeless-advocacy group, acquired the abandoned hotel and rehabilitated it to provide 112 units. All of the units served low-income residents; there were 75 single-room-occupancy (SRO) units in one wing and 37 studio and one-bedroom apartments in another (Sullivan 1998).

The Pacific Hotel's total project cost was \$8,534,694 (\$2,113,092 acquisition and \$6,421,602 rehab), or about \$76,000 per unit. PHG's clientele could not afford the rents to amortize a \$76,000 unit, but rents were brought down to an affordable level through multiple sources. The \$8,534,694 project expense was met through \$3,656,085 in equity—raised from combining the LIHTC and HRTC (see exhibit 11.1 for details)—and \$4,878,609 in debt financing. The debt's cost was reduced from subsidies received from the FHLB, the Washington State Housing Trust Fund, and the City of Seattle. The project's operating costs were further subsidized from HUD's McKinney SRO MOD REHAB program (Sullivan 1998).

While layering aids is the practical way to deliver affordable rehab in today's subsidy climate, there is a price to pay for such grantmanship. There is a learning curve for each program, and staff time and other expenses are involved in the application process. Each funder has its own requirements, ranging from the type and wording of real estate closing documents to the priorities and nature of the rehab (Williams 1999). When the Seattle Housing Levy<sup>1</sup> is used, the building's systems have to be rehabilitated to a 20-year life, whereas state/federal funders have other requirements or are silent on the matter (Williams 1999). Ancillary programmatic requirements can be expensive in their own right. CHHIP tries to avoid using CDBG funds for rehab because such funding requires Davis-Bacon construction wages and adhering to federal relocation mandates (Weinstock 1999).<sup>2</sup> Programmatic requirements can exacerbate regulatory tensions. When Housing Levy funds are used, Seattle housing officials understandably encourage extensive rehab to avoid future maintenance problems. The same is true when the LIHTC is secured. Syndicators involved in the program push "substantial" rehab as a preferred strategy that will better ensure the long-term use of the renovated housing units by income-

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<sup>1</sup>The 1995 Seattle Housing Levy is a \$59.211 million program designed to produce and preserve a minimum of 1,360 units for low- and extremely low income households. Levy programs include homeowner rehabilitation, home buyer assistance, rental production, and an operating and maintenance trust fund. The levy was approved by Seattle voters in November 1995 as a program funded by property tax levies for seven years, from 1996 through 2002. The Department of Housing and Human Services (DHHS) administers all Seattle Housing Levy programs.

<sup>2</sup>CHHIP is sympathetic to relocation needs and adheres to city of Seattle relocation requirements. The latter are viewed by CHHIP as being less onerous to a nonprofit than the federal requirements. The federal mandate, codified in lengthy, formal regulations, is seen by CHHIP as more appropriate for massive federal interventions (e.g., dam or highway construction) than for the small-scale rehabilitation work effected by nonprofits.

constrained families. Yet the inclination toward more extensive rehab by the Housing Levy, LIHTC, and sister programs triggers building code problems, as detailed later.

**EXHIBIT 11.1**  
**Example of Combining the HRTC and the LIHTC**  
**in the Rehab of the Pacific Hotel, Seattle, Washington**

TAX CREDIT ANALYSIS:	
<i>Historic Rehab Tax Credit (HRTC)</i>	Project
Total development costs	\$8,534,694
Total qualifying expenditures	\$5,925,041
Rehab tax credit %	x20%
Total rehab tax credit	\$1,185,008
Equity yield for rehab credit	\$0.80 per \$1.00
Equity raised from rehab credit	\$948,006
<i>Low-Income Housing Tax Credit Analysis (LIHTC)</i>	
Total developing costs (should be the same as above)	\$8,534,694
Total qualifying expenditures	\$6,234,742
Less rehab tax credit	[\$1,185,008]
Eligible basis	\$5,049,734
Low-income proportion <sup>a</sup>	130%
Qualifying basis	\$6,564,654
Annual credit %	9%
Annual credit amount	\$590,819
Total low-income housing tax credit	\$5,908,190
Equity yield for low-income credit <sup>b</sup>	45.84 cents per \$1.00
Total equity raised from low-income credit	\$2,708,079
<b>Total Combined Equity:</b>	<b>\$3,656,085</b>

Source: Sullivan 1998, 5.

<sup>a</sup>Project consists of 100% low-income units and is located in a “qualified census tract.” Therefore, a 30% boost/increase in credit amount is allowed.

<sup>b</sup>Yield low due to the following: (a) at that time the LIHTC was not yet a permanent program, resulting in few investors/little competition; and (b) 100% of HRTC and LIHTC equity was invested up front, at the start of construction.

The interplay of the benefit of a subsidy against the need to abide by the subsidy’s regulatory mandate is also illustrated with respect to the HRTC. As was evident with the Pacific Hotel case, the HRTC is a deep subsidy, crucial for making rehab affordable. Yet when the HRTC is used, the rehab must abide by historic preservation standards; sometimes this conflicts with the goal of providing affordable housing. (We detail this particular tension later in the case study.)

Sometimes the funding requirements are a particular disadvantage because of the nature of Seattle’s housing stock. Many Seattle residential properties have commercial uses on the first floor. In renovating the property, the first floor cannot be ignored; yet many subsidies drawn upon by those doing rehab (e.g., LIHTC and the Housing Levy) can be used for housing purposes *only*. (The HRTC can be used for nonresidential historic rehab.)

Given the multiple applications and many programmatic requirements and “sign-offs” inherent in layering subsidies, it is time-consuming to “package the deal.” The Pacific Hotel project is a

notable example of successfully combining the LIHTC and the HRTC. In order to secure these subsidies, the building had to be shown to be eligible for the National Register of Historic Places (“Part 1—Evaluation of Significance”), the rehab plans had to be approved by the Washington state historic preservation officer (SHPO) and the National Park Service (NPS) (Part 2 of the historic rehab tax credit; there is a Part 3 when the completed rehab work is approved by the SHPO-NPS), and the LIHTC had to be applied for. In the case of the Pacific Hotel, these negotiations went quite smoothly, and there was cooperation and constructive communication among the developer, architect, SHPO, NPS, and others. Nonetheless, all this effort takes time, shown in exhibit 11.2, prepared by the NPS (Sullivan 1998, 2).<sup>3</sup>

**EXHIBIT 11.2**  
**The Pacific Hotel Development Schedule**

<b>Event</b>	<b>Date</b>
Project initiated	Oct. 1, 1992 <sup>a</sup>
Architect hired	Oct. 1, 1992
Initial contact with SHPO	Jun. 14, 1993
Part 1 approval (HRTC)	Nov. 9, 1993
Low-income tax credit approved	Dec. 3, 1993
Part 2 approval (HRTC)	Oct. 17, 1994
Ownership structure organized	Oct. 21, 1994 <sup>b</sup>
Financing approved	Oct. 25, 1994
Construction initiated	Oct. 26, 1994
Construction completed	Oct. 23, 1995
Leasing begun	Oct. 11, 1995
Final Certification for HRTC (Part 3 approval)	Jan. 19, 1996

*Source:* Sullivan 1998, 2.

*Notes:*

SHPO: State Historic Preservation Officer

HRTC: Historic Rehab Tax Credit

<sup>a</sup>Initial feasibility study.

<sup>b</sup>Organized some time earlier, but not officially finalized until HRTC Part 2 approved Oct. 17, 1994.

Difficulty in securing support for affordable-housing rehab is an even more fundamental hurdle than the programmatic demands of the subsidies. Housing subsidies are in short supply. LIHI’s Frye Hotel LIHTC was so large (relative to the available statewide LIHTC pool) that it was drawn down in two separate LIHTC allocations. Given the modest sums available, housing subsidies are very competitive—and the competition does not always favor rehab. Again, the LIHTC is illustrative. In Washington, as in other states, far more projects apply for LIHTCs than credits are available statewide. Consequently, there is a “beauty contest” competition for the tax credits. The LIHTC “beauty contest” in Washington incorporates the following scoring system:

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<sup>3</sup>In considering the Pacific Hotel’s development schedule, it is important to note that all development projects take time—whether they are rehabilitation or new construction. The Part 2 HRTC approval is often delayed by other design details in the project. The financial planning and design work was all completed within regular time frames on the Pacific Hotel project.

1. Lowest-income tenants—50 points
2. Extend (Low-Income) use period—44 points
3. Serves greatest housing needs—15 points
4. Project location—10 points
5. Family housing—10 points
6. Elderly housing—10 points
7. Housing for the disabled—10 points
8. Preservation of existing affordable housing—10 points
9. Transitional housing—10 points
10. Maximum efficient use of credit—10 points
11. Rehab projects—10 points
12. Small-scale project size—10 points
13. Low developer's fees—10 points
14. Rural housing service projects—5 points
15. Participation of nonprofit organizations—5 points
16. Historic property—5 points
17. Targeted areas—5 points
18. Leveraging of public resources—5 points
19. Local support—5 points
20. Readiness to proceed—5 points

Some of the above criteria “favor” rehab projects, either directly or indirectly. These include criterion 8 (preservation of existing affordable housing), 11 (rehab projects), 12 (small-scale project size), and 16 (historic properties). However, other criteria may have the opposite effect, such as awarding points for rural projects, for ready-to-proceed projects (because of their complexity, rehab projects may be less ready-to-proceed than their new counterparts), and for applications with low developer fees (because of their complexity and risk, developers of rehab projects may demand a premium rather than a lower fee).<sup>4</sup> A further complication for rehab is the LIHTC's cost ceilings. The ceilings are established by the state of Washington at \$72,916 per unit in nonelevator buildings and \$76,200 per unit in elevator properties; these amounts are “tight” for rehab. (Recall CHHIP's near \$80,000 rehab cost per unit.)

CUPR has analyzed LIHTC data for Washington. For the 1992 to 1995 period, about three-quarters of all the LIHTC projects in this state were new construction, and one-quarter were rehab. The national break out is roughly two-thirds new-construction projects, one-third rehab. Thus, Washington leans somewhat more toward new LIHTC projects. This may or may not be due to the scoring criteria noted earlier.<sup>5</sup>

In summary, when CHHIP, LIHI, or equivalent organizations attempt to effect affordable-housing rehab, they confront the barrier of a fundamental resource gap: the rehab cost exceeds what their income-constrained clientele can afford. The gap is made up by securing a variety of

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<sup>4</sup>This was not the case for CHHIP and LIHI.

<sup>5</sup>We do not have data on the *applications* for state LIHTCs, just information on the outcome of the “beauty contests”—that is, the actual projects successful in securing the LIHTCs.

housing subsidies. Yet the very layering of subsidies creates issues. Furthermore, the subsidies are very competitive and the competition *may* be somewhat more perilous for rehab applications.

## **DEVELOPMENT PHASE BARRIERS TO AFFORDABLE-HOUSING REHAB**

### **Obtaining Properties**

Acquiring properties for rehab in Seattle means confronting issues noted in other jurisdictions, such as difficulties in contacting owners and having to deal with estate legal complications. Yet in contrast to other jurisdictions' typically "soft" real estate markets, Seattle's "hot" market has driven up property prices. Affordable-housing rehab—indeed, affordable housing in Seattle, in general—is being thwarted by escalating property values. As noted in Seattle's *Daily Journal of Commerce*:

Changes for saving other buildings like the Pacific Hotel are slipping away as the economy booms. Some have long-time absentee owners who have seen a big jump in the value of their land. Others have . . . affordable-housing subsidies that have now expired. One by one, they are going on the market to be remodeled or replaced, and long-time tenants are going on the street (Enlow 1999).

Our fieldwork found numerous instances of escalating property values. CHHIP acquired the Villa apartment building for renovation in 1998 for \$1.2 million; today, the fair market price would be \$2 million or more. The Pacific Hotel was acquired in the early 1990s and converted to housing. The acquisition cost then was \$2.1 million. Today, this downtown property would likely cost \$3 million to \$4 million.

It is not only the high prices that must be paid for Seattle real estate, it is the terms of sale. When the LIHI acquired the Frye Hotel, the nonprofit had to pay cash at closing (Lee 1999). Property sellers don't want to take back "paper" (i.e., seller financing) and want quick closings without contingencies—conditions nonprofit housing groups find hard to abide by.

Groups attempting to acquire properties for rehab encounter stiff competition from other parties. CHHIP looked into buying a "rickety property" in Capitol Hill to renovate. The nonprofit was outbid, however, by an investor looking to acquire the property "as is"—because Capitol Hill is increasingly sought after as an in-town neighborhood, even unrenovated apartments would rent for \$600 and up per month (Weinstock 1999).

Rehabilitators also face competition from parties interested in acquiring properties for assemblage purposes. This is especially true when the property's current use is far below the highest and best use. In downtown Seattle, properties are commonly built on lots 60 feet wide and 120 feet deep. Numerous lots this size contain three- to four-story buildings yet are zoned for an FAR about twice as great (Murphy 1999). If two such properties can be assembled, they are worth about \$2 million dollars; three such properties have a value of \$3 million to \$4 million. Affordable-housing groups such as CHHIP and LIHI find it difficult to afford such prices. LIHI, for instance, recently had to pay \$2.1 million for a vacant 47-unit property (an acquisition cost of

almost \$45,000 per unit) because the property was located in an area zoned for a high-rise (Lee 1999).

## **Estimating Costs**

Groups doing rehab in Seattle speak of the task of estimating costs as being “part of the job” (Barrientos 1999), and for the most part they are reasonably accurate. Yet they recognize the challenges of estimating rehab expenses, especially when compared with “more straightforward new construction” (Murphy 1999). “Substantial” rehab was deemed easier to estimate accurately than a more moderate renovation because in the latter there were more judgment calls concerning items that could be retained as is, those that need to be repaired, and finally, systems that must be replaced. With substantial rehab, almost everything is replaced; thus, estimating that type of job is more akin to new construction.

The groups we spoke to in Seattle explained that rehab cost estimating was challenging because of the following:

1. *Inherent uncertainties of the work.* For instance, could a wall be patched or would it have to be “opened up,” and if the latter, would new-building energy efficiency requirements have to be met? “Gray areas” of the building code (explained shortly) add to the uncertainty.
2. *Timing and compensation of the cost estimating.* Architects and other professionals asked to do the estimating are typically given a very short time to complete the job (Murphy 1999). Time may be of the essence because sellers are anxious and want a quick decision. Sellers often want to sell the property “as is,” and if they allow an inspection and rehab cost estimation, they demand that it be done expeditiously. The fee to the architect or other individual for estimating the job is usually a token amount, typically in the \$5,000 to \$10,000 range. This compensation does not pay for a thorough, item-by-item cost estimation. The estimation is therefore done in large part by relating the job at hand to other comparable work done in the past. It is good to build on professional experience, and for the most part that does give a sense of cost, yet every building is different, so estimating based on “comps” is perilous.
3. *Difficulties of cost estimating.* Even were more time and resources available for cost estimation, it would be difficult. If properties are occupied, tenants may deny or limit entry by those doing the cost estimating. Even if access is not an issue, estimating is made that much harder because floor and other architectural plans are typically absent, hazardous materials are frequently present, and so on (Murphy 1999).

The difficulty of doing rehab, in part reflected in the issues of estimating, are acknowledged in suggested professional fees. In the state of Washington, the suggested fees for architects are 2 percent *higher* for rehab than for new-construction assignments.

## **Obtaining Insurance**

This was not an area of major concern. Hazard and other coverage on the properties being rehabilitated was readily obtainable at what has been deemed a reasonable cost, though CHHIP mentioned that the carriers were always changing (i.e., a company would extend coverage and would then elect to “get out of the business”) and one had to shop to secure the best rates (Weinstock 1999). Surety coverage for contractors doing rehab was available at reasonable cost for experienced companies. Those with less of a track record had more difficulty in securing such bonding. Interestingly, professional firms involved in rehab (e.g., architects) paid roughly a 10 percent surcharge for their “errors and omissions” (E and O) protection compared to E and O coverage on new construction (Murphy 1999).

## **Obtaining Financing**

Years ago, some Seattle lenders were uncomfortable financing rehab jobs; currently, such loans are routinely extended. Because of the uncertainties and challenges of rehab, however, lenders demand a “tighter” proforma (Barrientos 1999). These include a higher project contingency factor with rehab; a contingency of 8 percent to 10 percent is demanded by lenders on renovation jobs, a factor roughly 2 percent to 3 percent higher than with new construction (Barrientos 1999). Lenders expect “soft” costs to be about 5 percent more on rehab work relative to new construction. (Hard construction costs are about \$60 to \$75 per square foot for rehab compared with \$50 to \$55 per square foot for new construction.) Lenders also demand greater development-construction expertise on a rehab job team relative to their expectation for a new-construction project because the former has more uncertainties. Yet sometimes lenders will cut the rehab job some slack with respect to the acceptable project financial pro forma. Because of its more distinct amenities and hence unique market attraction, a rehabilitated residential property in Seattle can expect to have a 1 percent to 3 percent lower vacancy rate than its new-construction counterpart (Barrientos 1999).

## **Land-Use Restrictions**

Seattle’s parking and open space requirements—especially the former—were viewed by many as adding to the difficulty of doing rehab in the city.

The employment and population boom in Seattle has exacerbated an already difficult parking situation. There are simply not enough on-street spaces for Seattle’s residents and workers. Consequently, the city requires that 1.3 on-site parking spaces be provided per housing unit. That requirement applies to all properties—both new construction and rehab—yet the parking mandate is typically easier to satisfy when building anew than when trying to retrofit spaces. It is obviously difficult to provide parking where it did not exist before, as described by one developer contacted by CUPR who told of the machinations of excavating and building an underground garage (Nodland 1999). This parking retrofit required the shoring of foundations (itself made more complicated because of seismic requirements), rerouting of HVAC systems, and other major work that added about \$15,000 to \$20,000 in cost per housing unit (Nodland 1999).

Seattle allows some exceptions to the parking mandate. Properties in the downtown are exempt, as are historic properties throughout the city. That still leaves many existing properties subject to the city parking statute. And even without a public parking requirement, the market for middle-income and more costly housing demands a parking amenity (Barrientos 1999; Thomas 1999). A Seattle developer noted that “Parking drives everything. I often look at a building’s potential for rehab by examining the parking situation” (Nodland 1999). This developer asserted that “the parking requirement is a terrible detriment to existing housing.”

Residential developments in Seattle must include 20 percent open space. As with the parking mandate, that requirement applies to both new construction and rehab projects. In new construction, open space can be provided in a more straight forward fashion through the design the buildings footprint. It is much more challenging to retrofit one-fifth open space into an existing property, and creative solutions have to be sought. One developer proposed that the open space requirement be met in a property he was rehabilitating by building a large rooftop deck (Nodland 1999). But no retrofit is easy. Constructing a rooftop deck affected the live loads throughout the structure, and this in turn required that footings be shored up against columns and that other structural work be done. The cost of that work amounted to about \$250,000.

The developer doing the rooftop deck further noted that his proposal required approval in the Master Use Permit (MUP) for the rehab project. The requirement for open space is just that—that one-fifth of the property be “open.” The rooftop deck had to be agreed upon as an open space amenity in the MUP process, but any such discussion or variance delays the MUP deliberations. In the rooftop example, it took six months to complete the MUP negotiations, and fees for planners, attorneys, and other professionals amounted to \$45,000.

Even when there are no parking, open space, or other variance issues, it is expensive to secure a MUP. It is not unusual to spend tens of thousands of dollars for attorney and other costs to obtain this permit. This high fixed cost discourages smaller projects, since the MUP processing outlay has to be amortized over fewer units. As many rehab jobs tend to be smaller in size, the MUP processing cost serves as a greater barrier to rehab than to the typically larger new-construction job.

## **CONSTRUCTION PHASE BARRIERS TO AFFORDABLE-HOUSING REHAB**

### **Building Code**

#### *Background to the Seattle Building Code*

Seattle’s Building Code (SBC) incorporates certain flexibilities pertaining to renovation. Particular flexibility is encouraged in the instance of historic properties.

**Section 3403.8: Historic Buildings and Structures.** The building official may modify the specific requirements of this building code as it applies to buildings and structures designated as landmarks of historical or cultural importance and require in lieu thereof alternate requirements which, in the opinion of the building



official, will result in a reasonable degree of safety to the public and the occupants of those buildings.

A historic building or structure is one which has been designated for preservation by the city council or state of Washington, has been listed, or has been determined eligible to be listed, in the National Register of Historic Places, has been officially nominated for such status or is a structure contributing to the character of a landmark or special review district.

Historic preservationists report that building officials do in fact modify the nominal requirements of the building code to further the rehab of landmark buildings (Gordon 1999). Thus, the spirit of Section 3403.8 is, in fact, being upheld.

Section 3403.8 of the SBC applies only in the instance of landmarks. The general rule—that is, the mandate for all buildings—is that if a property is rehabilitated in Seattle, it has to be brought up to a new-building standard only if “substantial alteration” has been made. Section 3403.11 of the SBC defines five “triggers” of “substantial alteration:”

1. Extensive structural repair
2. Remodeling or additions which substantially extend the useful physical and/or economic life of the building or significant portion of the building, such as remodeling a complete floor other than typical remodeling
3. A change of a significant portion of a building to an occupancy that is more hazardous than the existing occupancy, based on the combined life and fire risk as determined by the building official. A change of tenant does not necessarily constitute a change of occupancy
4. Reoccupancy of a building that has been substantially vacant for more than 12 months (with some exceptions)
5. A significant increase in the occupant load of an unreinforced masonry building

Of the five definitions of “substantial alterations,” the second (“extending the useful physical and/or economic life of a building”) is the most frequently used, and code officials acknowledge it is one of the most difficult triggers to determine (Seattle Department of Construction and Land Use 1996). For example, routine maintenance of a building, by itself, will not trigger a “substantial alternation.” Routine maintenance typically includes items such as painting, reroofing, or replacement of plumbing fixtures. When routine maintenance has been delayed to the point where the building has suffered significant deterioration and requires expensive restoration, however, it may be considered substantial. Routine maintenance combined with some improvement work may also be considered substantial.

Since “extending the useful physical and/or economic life of a building” is a gray area, the SBC notes three criteria that guide this second trigger of substantial alteration. The three criteria include the following (Seattle Department of Construction and Land Use 1996):

1. *Cost of project.* For the typical project, if the cost is high relative to the value of the building, it will be considered substantial. For example, if a project consists of new carpet, paint, upgrade of light fixtures, new toilets and sinks, a new roof, and patching of plaster, and the cost is more than half the value of the building, it would probably be considered a substantial alteration. Even though most of these items alone would be considered maintenance, the total amount of work would be great enough to justify a conclusion that the project is a substantial alteration. The 50 percent figure used here is not intended to be a fixed percentage, but only an example.
2. *Existing conditions.* A careful review of existing conditions is important in determining whether a given proposal will trigger substantial alteration requirements. A relatively new building may undergo a face-lift, with expensive new finish work and some minor alterations and yet not trigger special requirements, while a very old and poorly maintained building that undergoes similar improvements may be viewed as a substantial alteration.
3. *Size of project relative to building size and extent of use.* Alteration projects vary considerably from total building renovation to renovation of a portion of a floor; building use varies from fully occupied to completely vacant. It is the particular combination of these two items that becomes important in evaluating whether a project is substantial. For example, many older downtown buildings have very limited, if any, use of their upper floors. Renovation of the tenant spaces on the lower floors of such a building, even though of moderate size and scope relative to building size, may trigger the substantial alteration requirements.

If there is a substantial alteration, however triggered, then the SBC requires that the new building undergoing rehab conform to critical new-building standards. These include conformance to the requirements of Section 403 (high-rise buildings, when applicable), Section 713.10 (smoke dampers), 713.11 (fire dampers), 801 through 805, 808 (interior finishes), 904 (fire-extinguishing systems), Chapter 10 (means of egress), Chapter 3 (fire alarm requirements), and Section 3403.11.3 (evaluation and mitigation of seismic deficiencies) (Seattle Department of Construction and Land Use 1996).

### *Evaluation of the Impact of the Seattle Housing Code on Rehab*

Unlike other jurisdictions where the building code is governed by an archaic “25–50 percent rule”<sup>6</sup> and code administration is often “by the book,” the situation is much more positive in Seattle. “Modifications” to requirements are expressly permitted in the case of historic properties. More generally, the SBC’s “substantial alteration” rule, provided for in Section 3403.11, has many reasonable features, such as requiring more stringent standards in the cases of rehab increasing the hazard level (trigger 2) or occupant load (trigger 5) of a property.

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<sup>6</sup>A provision that links code requirements to the extent to which rehab adds to the property’s value. For instance, if the rehab exceeds one half of the property’s pre-renovated value, then the entire existing building, and not just the renovation, would have to meet the standards for new construction. See Chapter 5 for details.

Helping matters is the philosophy behind the SBC's administration.<sup>7</sup> That philosophy historically has been supportive of rehab, especially in affordable-housing situations. A current city administration, which is particularly pro-housing, has encouraged municipal officials to flexibly administer the SBC (Hooper 1999).

Yet even flexible administration ultimately is guided by the regulations and there are elements of the SBC that can frustrate rehab. Seattle is not governed by a strict "25–50 percent rule," but that long-criticized standard does have an impact. The second definition of "substantial alteration" (extending the useful physical and/or economic life of a building) is the most common trigger, and that trigger, in turn, is most often influenced by the "cost of project" criteria. Groups knowledgeable about rehab in Seattle describe the following negotiations (Murphy 1999; Thomas 1999). Developers and architects will argue that their proposed rehab is actually "deferred maintenance," and as such should not trigger the "substantial alteration" requirements. Building code officials, however, will often be guided by the hard costs of the rehab job and will scale up their requirements accordingly. As a rough rule, if the rehab expenses amount to less than one-third of the property's assessed improvement value—that is, the assessed value of the structure but not including the land—then the rehab will, in fact, be considered "deferred maintenance." If expenses exceed two-thirds of the assessed improvement value, then the job is counted as a substantial alteration. Rehab jobs costing between roughly one-third and two-thirds of the assessed improvement value are a gray area, and depending on other factors (e.g., existing conditions and/or size of the project relative to building size and extent of use), will be treated as either deferred maintenance or a substantial alteration.

Ironically, funders of rehab subsidies often "push" a job into the substantial alteration category. Knowing how the rehab cost can influence its building code treatment, sponsors of affordable-housing renovation may decide to improve less or to stagger the work over time in order to prevent the substantial alteration trigger. Funders, however, often have a different perspective. For instance, when Housing Levy funds are tapped for rehab, program administrators often encourage "doing the job right" by effecting a substantial rehab in "one fell swoop," as described by one nonprofit developer (Weinstock 1999). Yet doing rehab in such a fashion means it will be considered a substantial alteration, and thus will have to meet stringent code requirements.

It is often difficult and expensive to retrofit the substantial alteration requirements, which can involve such work (unless a variance is granted) as modifying a stairway's riser, altering the door swing, enclosing stairways, installing sprinklering, and in other ways meeting new-building fire safety standards (Murphy 1999).

Further complicating matters is having to meet new-building standards in a mixed-use structure (Lee 1999). As noted earlier, many Seattle properties have a commercial use (e.g., restaurant) on the first floor and residential apartments on the upper floors. If the apartments are rehabilitated,

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<sup>7</sup>The generally rehabilitation-supportive situation in Seattle with respect to the building code was contrasted to a more challenging environment in the suburbs and rural areas outside the city. Building officials in these outer locations were described as typically having less expertise than their Seattle counterparts and being less willing to negotiate. Compounding the problem were instances where a single person was both the fire and building official, thus controlling all critical regulatory matters. When that individual was not flexible, the building code could be a major hurdle to affordable-housing rehabilitation (Murphy 1999).

and if that work triggers the substantial alteration standard, then the *entire* building, including the first-floor commercial use, has to be upgraded to the new standard, and that can be particularly difficult for commercial uses. Retrofitting the new-building standards for a restaurant, for example, will often involve extensive work on smoke dampers, air changes, and the like (Flickinger 1999).

Retrofitting seismic protections is another challenge. Seattle is in a high seismic risk area and accordingly, the city has stringent seismic protection standards. (One notices that immediately by the extensive bracing evident in the Seattle airport.) It is not easy to satisfy these standards to the level required when the substantial alteration trigger is activated. The rehab must then include such work as bracing lower floors, installing “y” or “k” braces to support loads at ground level, taking down plaster walls and reinstalling a more seismic-resistant plywood-plaster wall combination, bracing parapets, and doing other extensive work (Murphy 1999).

The seismic retrofit is expensive, amounting to roughly \$10 to \$15 per square foot. Besides cost, there are other challenges. Installing braces or floor diaphragms and similar work is dusty and noisy construction, so if a building is occupied, tenants have to vacate while the seismic retrofit is done (Murphy 1999).

Given Seattle’s proximity to California and the eruption of nearby Mount Saint Helens, the affordable-housing community in this city recognizes the need for seismic protection. There are many instances where seismic protection has been quite easily added in affordable-housing rehab projects. That was the case with the Pacific Hotel, as we shall detail shortly. At the same time, affordable-housing advocates raise the issue of priorities. The Frye Hotel rehab cost LIHI \$6 million for construction; about \$2 million of that total was spent for seismic protection. As this project’s seismic cost was extreme, much desirable renovation could not be done. Thus, old medicine cabinets and other cabinets had to be kept because the budget did not allow for their replacement. LIHI rhetorically notes that the seismic mandate requires many such “terrible choices” in the rehab work that is done or left undone (Lee 1999).

## **Historic Regulations**

In Pioneer Square, Pike Place Market, the International District, and many other Seattle neighborhoods, historic preservation is an important theme for housing rehab. To that end, Seattle offers a number of incentives to owners of landmark properties. These include the following (City of Seattle 1997):

- *Zoning code relief.* For a designated landmark, Seattle may authorize a use not otherwise permitted in a certain zone. This provision provides flexibility of use to encourage the preservation and use of historic buildings.
- *Building code relief.* The SBC allows modifications to specific requirements of the building code for landmark buildings.
- *Special tax valuation for historic properties.* Special property tax breaks are accorded to landmarks undergoing rehab.

Seattle further offers special incentives for downtown landmarks. These include the following (City of Seattle 1997):

- *Transfer of development rights.* To encourage the preservation of landmarks, the property owner is able to sell unused development rights to other developers. The value of these development rights is negotiated between the owners of the sending and receiving lots.
- *Downtown residential zone.* Seattle landmarks in a downtown residential zone are exempted from any restriction on commercial density as long as the building is restored and committed for long-term preservation.
- *Demolition disincentive.* Development on a site that results in the destruction of a designated Seattle landmark is not allowed to acquire additional development rights through a floor area bonus.

Local preservation controls and incentives in Seattle, by almost all accounts, are an important support to housing rehab in that city (Barrientos 1999; Williams 1999). Yet there are costs associated with that regulation. One developer recounted the following example (Nodland 1999). He proposed the rehab of a residential property in a landmark historic district.<sup>8</sup> The work fell under the oversight of a neighborhood historic preservation board. As the board met only every two weeks and reviewed many applications, its review of the project in question took a long time, almost a year. There were often legitimate reasons for this delay, but the local Seattle historical oversight, however well intentioned and important to encourage rehab in the city, does exact a regulatory cost.

The same is true with respect to the historic rehab tax credit (HRTC). The 1986 Tax Reform Act (TRA) allows a 10 percent investment tax credit (ITC) for income-producing nonresidential properties. TRA provides for a 20 percent HRTC. To qualify for the 20 percent HRTC, the rehabilitated property has to be a “certified historic structure” (i.e., a building individually listed on the National Register or located in, and contributing to, the historic significance of a registered historic district);<sup>9</sup> the rehab must be “substantial” (i.e., more than \$5,000 or the adjusted basis of the renovated property, whichever is greater); and finally, the rehab has to be certified.

The HRTC is an important incentive to affordable-housing rehab in Seattle, especially since it can be combined with the LIHTC. This was previously illustrated in the Pacific Hotel example, which showed how the HRTC could be applied in a way that met the goals of providing affordable housing while abiding by the Secretary of the Interior’s Standards for Rehabilitation as well as the local building code and other requirements. The Pacific Hotel traditionally had been used for transient housing, so its rehab for SRO and other compact (e.g., studio and one-bedroom) apartments was very compatible. This compatibility allowed the Pacific Hotel rehab to “successfully use the historic floor plan with only minimal changes” (Sullivan 1998, 3), as is

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<sup>8</sup>The city of Seattle contains about 200 individual landmarks and about 800 to 1,000 properties in seven historic districts.

<sup>9</sup>A registered historic district includes both those districts listed on the National Register, and any state or local historic districts in which the district and enabling statute are certified by the Secretary of the Interior.

shown in the “before” and “after” plans of the project’s west wing (see exhibit 11.3, top). This theme of synthesis was carried forth in the project, satisfying historic, affordable housing, and building regulatory mandates as described in a 1998 study by the National Park Service (NPS).

Several code issues with a potential to impact the historic appearance of the structure also required creative solutions. Providing disabled accessibility to the building was a major challenge. Due to the sloping streets, all of the existing entries were located several steps up from the sidewalk. The only feasible option was to create a new, level entry at a point where the sidewalk most closely aligned with the floor. To accomplish this, a large window opening was carefully modified to become a doorway by cutting away the sill. Two apartments were then minimally reconfigured and a ramp (leading to an elevator) was inserted between them. As a result, eight units and all common areas were made fully accessible. Another code issue was caused by the balconets (i.e., pseudo-balconies), which blocked emergency egress from 36 bedroom windows. The balconets are integral to the historic integrity of the building’s façade. The solution in this case was to cut the guardrail from the frame and remount it as a hinged “gate” with a latch reachable from inside the unit.

Although constructed with a concrete frame, the building’s geographic location in an earthquake zone also mandated significant seismic improvements. The inside of all exterior walls received a grid work of two by four framing to which the existing clay tile infill was anchored using heavy-gauge copper wire. Structural shear walls were installed at selected interior locations and roof parapets braced. All exterior walls were covered on the inside with 3 ½” insulation added to the wall cavities created by the two by four framing. This approach allowed the original single-glazed windows to be retained while improving overall energy performance.

The east apartment wing contained two ornate exit stairs, one of which was extremely steep and non-code complying. After considerable study it was determined that the ground-floor portion of the stair met code and could be retained while the steep portion (2<sup>nd</sup> through 4<sup>th</sup> floor) required replacement with a modern, code-complying stair. Prior to any action being undertaken, the architects consulted with the National Park Service for guidance. The action was approved by NPS, out of consideration for safety issues and the fact that a similarly detailed stair remained in the building and was representative. (Sullivan 1998, 3–4)

Sometimes there are greater tensions in trying to harmonize the Secretary of the Interior Standards and other mandates; these tensions are often most acute where the interiors of the properties are being renovated. In the case of the Pacific Hotel, the functional compatibility of the historical and current use of the property allowed for rehab that essentially left intact the significant interior features of this building. But that is not always the case.

Take, for example, another SRO (not identified by name or address but referred to here as “other SRO”) shown in the bottom portion of exhibit 11.3. The original interior of the other SRO had

narrow hallways, reflecting the historical, modest housing amenity of the property. The original apartments were also “bare bones,” essentially single rooms off a corridor. To modernize the other SRO and to produce the kind of unsubsidized units that are sought after in today’s marketplace, a developer proposed altering its interior. The units would be enlarged and new corridors would be built. The exterior features of the property would be left intact, however.

The developer of the other SRO sought an HRTC, claiming that the proposal satisfied the spirit of the Secretary of the Interior Standards. The NPS rejected that argument. The developer then proposed leaving the interior of the first floor as is, thus preserving its historic character. The interiors of the upper floors, however, would be remodeled as earlier described. The exteriors of all floors would be left intact. This second proposal was considered by the NPS and discussions took place between the developer and the NPS during the next few months. Ultimately, the developer opted to cease negotiating over the historical appropriateness of the different rehab approaches. He dropped the HRTC application, made the interior changes he wanted, and kept the exterior largely as it had been.

Other developers described variations of the same theme. A historical school was being renovated to market-rate housing (Thomas 1999). The original corridors were too wide, so it was proposed that they be narrowed and the classrooms remodeled in order to provide market-attractive housing. The school’s distinctive original windows were kept intact, though they were made more energy-efficient through the installation of interior storm windows. This project was approved for historic tax credit, but not before months of deliberations.

There are often “tensions” in using the HRTC. The Samis Company, for example, has been very active in the revitalization of Seattle’s historic Pioneer Square. Samis has used the HRTC, but acknowledges the “costs” of this program, as is recounted in the following article in Seattle’s *Daily Journal of Programs*.

Federal tax credits are also available for some historic buildings. A case in point is the Corona Hotel. Samis is converting the six-story, single-room occupancy hotel into middle-to-upper-income apartments with four units of 800-1,000 square feet on each floor—a cost- and market-driven solution. Dating from 1903, the Corona is eligible for federal rehab tax credits of up to 20 percent on construction and other costs. . . AIA Samis has found, however, that advantages arising from the tax credits may be negated by the cost of completing interior rehab under current interpretation of the standards: each floor of the building interior must “reflect a sense and essence of the original.” This often increases the developer’s costs or reduces the building’s efficiency.

“A project has to be market- not tax-driven,” Samis said. (Murphy 1998)

**EXHIBIT 11.2**  
**Floor Plans and Historic Housing**

**Proposed Market Amenity Housing with Interior Changes  
Plans that Comport with Historic Floor Plan**

**Proposed Market Amenity Housing with Interior Changes  
That Conflict with Historic Floor Plan**



One developer raised a point regarding a processing issue with respect to the HRTC (Nodland 1999). This developer praised the HRTC as a valuable subsidy, yet he encountered a snag going from Part 2 HRTC approval (sign-off on plans) to Part 3 HRTC approval (sign-off on the completed rehab). In this developer's experience, as construction proceeded, inevitably there would be departures from the Part 2 plans. Since it would take too long to have these variations approved by the SHPO-NPS—a step that would stop construction—the variations would be effected and the developer would hope that they would be approved in the Part 3 review. This situation, however, created uncertainties. The developer recommended a review process that could provide expedited review of desired variations to Part 2 plans. This review would clarify whether the variation was acceptable as construction proceeded, rather than leaving the situation uncertain until the Part 3 review. To expedite matters, this review could be done at a state-regional level rather than having to forward applications to NPS in Washington, D.C.

These HRTC-market tensions may be exacerbated in adaptive reuse situations where the current use differs markedly from the original. With respect to the Pacific Hotel, the current use—modest housing—resembled its historic use as an SRO. In the Corona Hotel, Samis wanted to create apartments much larger than the original hotel units, making it difficult to retain the historic interior while satisfying current market dictates. Seattle's historic preservation officer, Karen Gordon, observes that historic preservation on the west coast more often than not involves adaptive reuse and notes that it is a challenge to the historic preservation and development communities to come to a meeting of minds in these situations (Gordon 1999). Is retaining one original interior floor of an adaptively converted hotel, SRO, or school sufficient? What about two floors? Must the original floor plan of the entire property be kept intact?

### **Access Requirements**

The state of Washington access code combines the most stringent requirements of the Fair Housing Act (FHA) and Americans with Disabilities Act (ADA). The state access requirement recognizes that it is often challenging to retrofit accessibility and therefore allows various flexibilities, including the following:

1. *Substantial rehab hardship.* The full access requirements have to be satisfied only in the case of substantial rehab, defined as rehab exceeding 60 percent of the property's appraised value (not the lower assessed value, which is the measure used in the "substantial alteration" test). In other words, if rehab amounts to less than 60 percent of the property's appraised value, the rehab project would be exempt from full-access requirements because they would constitute a "substantial hardship."
2. *Path of travel.* The path of travel has to be made accessible only if the cost of doing that does not exceed 20 percent of the cost of construction expended over 36 months.
3. *Historic properties.* Flexibility in meeting access requirements is encouraged in the case of historic properties.

These provisions allow flexibility in satisfying access requirements while effecting rehab in Seattle. Yet the city's topography (e.g., sloped streets), historical pattern of development (full lot

coverage), and other characteristics, as well as the inherent difficulty of retrofitting access, make it challenging to meet the access mandate. Satisfying the mandate requires creative responses. In the Pacific Hotel, as noted, a new level entry was provided and a window opening was modified to create a doorway (Sullivan 1998, 3–4). In the rehab of the Blive building, there was no way to provide a ramp because the lot was 100 percent covered. The solution was an accessible unit in the basement, which did have wheelchair access. Thus, the accessibility mandate is being satisfied in myriad ways but it is more difficult to do so when doing rehab as opposed to new construction.

## **Environmental Regulations**

Numerous parties knowledgeable about rehab in Seattle mentioned a brownfields constraint to rehab. This was the case especially in situations of adaptive reuse from industrial to housing. For example, one property being rehabilitated by CHHIP had been used for car repair, manufacturing, and several other applications. With the building now being adaptively reused for housing, CHHIP had to resolve brownfields contamination issues, and that resolution was time consuming and expensive (Weinstock 1999). Making the situation even more difficult was a lack of documentation; CHHIP could not obtain records on the historical legal uses of the property, let alone the illegal ones, which made it more difficult to come up with an environmental remediation plan.

Even when a building's use is not being changed, there can be environmental issues and oil tank contamination was cited frequently in this regard. CHHIP described the following situation concerning its rehab of the Finch Building (Weinstock 1999). As part of its due diligence, it found and capped an above ground oil tank. In the course of rehab, however, CHHIP's contractors "smelled petroleum," and they began to excavate to remove petroleum that had seeped into the ground and to find what they suspected was an underground tank. Extensive excavation was done, which was expensive in its own right and stopped the rehab job for weeks. The project's architect feared that any further digging would undermine the property. The underground oil tank was never found, and, in fact, it was unclear if the leaking oil tank was on CHHIP's property or its neighbor's.

Meeting lead and asbestos standards was also mentioned as sometimes challenging in Seattle rehab projects. As an example, many 1950s Seattle office buildings had asbestos "popcorn" insulation in their ceilings. When such properties are reused for housing, asbestos containment can be expensive if ceiling layouts have to be altered.

## **Trades**

The "hot" construction market in Seattle is making it more difficult to secure qualified tradespersons. One individual interviewed by CUPR stated that the bigger and most competent general contractors and tradespersons are "120 percent spoken for by commercial and high-end residential construction in Seattle. That leaves the smaller companies, but they are less sophisticated and encounter such issues as difficulty in getting bonding" (Williams 1999).

## **Other—Growth Management**

To understand how growth management affects affordable-housing rehab in Seattle requires some background on this topic.

### *State of Washington Growth Management*

Following a period of public alarm over the state’s “trending to California”—clogged freeways, disappearing farmland, leapfrog development pushing all the way out to the mountains—the Washington legislature enacted the Growth Management Act (GMA) in 1990 (Beaumont 1996, 295). “. . . [U]ncoordinated and unplanned growth,” declared the Washington legislature, “together with a lack of common goals expressing the public’s interest in the conservation and the wise use of our lands, pose a threat to the environment, sustainable economic development, and the health, safety, and high quality of life enjoyed by residents of this state.”

The Washington Growth Management Act (GMA) provides Washington communities with a number of tools to help them manage their growth (New Jersey Office of State Planning 1996). One of the major tools provided is the establishment of an Urban Growth Area (UGA), whereby the state’s fastest-growing counties draw a line that separates urban areas and rural or resource areas. As detailed in the GMA:

Each county . . . shall designate an urban growth area [UGA] . . . within which urban growth shall be encouraged and outside of which growth can occur only if it is not urban in nature . . . An urban growth area may include territory that is located outside of a city only if such territory already is characterized by urban growth or is adjacent to territory already characterized by urban growth.

The Washington GMA identifies 13 statewide planning goals addressing (1) urban growth, (2) sprawl, (3) transportation, (4) housing, (5) economic development, (6) property rights, (7) permits, (8) natural resource industries, (9) open space and recreation, (10) Environment, (11) citizen participation and coordination, (12) public facilities and services, and (13) historic preservation. Washington’s fastest-growing counties, and the cities within them, must prepare local comprehensive plans that address the state’s major planning goals. Plans must include discrete elements for land-use, transportation, capital facilities, and other needs (Beaumont 1996, 295). The Washington GMA is administered by the state’s Department of Community, Trade and Economic Development (CTED). CTED is responsible for establishing a program of technical and financial assistance and incentives for counties and cities to encourage the adoption and implementation of comprehensive plans and development regulations throughout the state (New Jersey Office of State Planning 1996).

### *Growth Management in King County/City of Seattle*

In 1992, the Growth Management Planning Council (a 12-member board of officials from King County government, Seattle, and the 34 suburban cities) developed the Countywide Planning Policies to address growth and change and to guide individual planning efforts. The King County

Comp Plan is guided by planning goals and by Vision 2020, a regional plan for the four-county central Puget Sound area developed by the Puget Sound Regional Council (City of Seattle 1999).

The Countywide Planning Policies outline how King County can accommodate an expected 293,000 more people over the next 20 years and still maintain a high quality of life and thriving economy (City of Seattle 1999). The policies establish an urban growth boundary that separates urban areas from rural areas. Most of the expected growth will be encouraged to occur within urban areas, especially Urban Centers, which are existing areas of concentrated employment and housing supported by many services. There are 13 designated Urban Centers within King County. Five are in Seattle; the remaining eight are in other concentrated growth nodes in the county (e.g., Bellevue).

The Seattle Comp Plan mirrors the orientation of the Countywide Planning Policies. As a guide for the future, the Seattle Comp Plan encourages growth to occur where the greatest concentrations of housing, jobs, public facilities, and services already exist, and where further growth could most easily be accommodated. Known as the Urban Village Strategy, the Comp Plan policies show these areas as Urban Centers and Urban Villages, in keeping with the direction established by the Countywide Planning Policies (City of Seattle 1999a).

Urban Centers and Villages are not being created by the Seattle Comp Plan. They already exist. The lively neighborhoods of Ballard, West Seattle Junction, Beacon Hill, International District, Capitol Hill, Greenwood, Columbia City, and Wallingford are all examples of Urban Villages as preliminarily designated in the Seattle Comp Plan. They all contain an active commercial center within easy walking distance of the surrounding residential area. Designation of these neighborhoods as Urban Centers or Villages enables Seattle to plan more effectively for future development, to encourage private investments, and to make decisions regarding investment of public resources in housing, transit, public facilities, and other services so that these neighborhoods can support their anticipated growth and remain attractive places to live and work (City of Seattle 1999).

To support the diversity of Seattle's employment base and the vitality of its manufacturing and industrial sector, the Seattle Comp Plan has further designated two Manufacturing/Industrial Centers—Ballard/Interbay and Duwamish—specifically for this type of activity. The Seattle Comp Plan protects Duwamish and Ballard/Interbay from incompatible development and encourages government action and partnerships with the private sector to reverse current trends toward declining numbers of jobs in manufacturing and industrial enterprises.

#### *Growth Management and Affordable-Housing Rehab*

Because the implementation of the King County/Seattle Comp Plans is taking place as of this moment, it is too early to determine how growth management is affecting affordable-housing rehab in Seattle. Also, events other than growth management are taking place, affecting the equation. These other influences range from a heated electronic-based regional economy to renewed efforts to limit pollution in the state's rivers in order to protect the salmon. (The latter activity might limit new construction in rural areas bordering these rivers.)

While recognizing the difficulty of isolating the influence of growth management on affordable-housing rehab in Seattle, we can report on the perceptions of the knowledgeable observers CUPR interviewed. Both positive (rehab-encouraging) and negative (rehab-discouraging) influences were perceived. On the positive side were the influence of the UGB and designation of Urban Villages and Centers in making older neighborhoods more attractive and hence more prominent candidates for rehab. That view was expressed in Seattle's *Daily Journal of Commerce*.

“Growth management is a key force behind what is happening,” says Andy Wilch, executive director of the Pioneer Square Community Development Organization. Growth management has renewed emphasis on housing in Pioneer Square. Seattle's comprehensive plan calls for an additional 2,100 households in the Pioneer Square Urban Village by the year 2014, and 4,800 additional jobs.

“People who have not been urban dwellers with an urban mind-set are being asked to change their mode of thinking,” Wilch says. “This is a new philosophy of living, more consistent with higher-density urban neighborhoods.” (Murphy 1999)

Capitol Hill, another designated Urban Village, may be experiencing greater housing demand and rehab of its housing stock because of growth management. Yet such a statement may be pure conjecture, for even without Washington's GMA, Capitol Hill would very likely interest rehab developers because of its proximity to Seattle's downtown and the historic character of its housing stock.

Growth management was viewed by some as possibly having a negative influence on affordable-housing rehab for a number of reasons. First, even if one accepts the linkage between growth management and the enhanced desirability of such areas as Capitol Hill and Pioneer Square, the very fact of this enhanced attraction can drive up property and rental prices in these neighborhoods. If rehab is effected in the Urban Centers and Villages, it may not be affordable, because property costs are so high.

Second, even if growth management enhances the draw to the Urban Centers and Villages, who is to say that housing there will be provided through rehab as opposed to infill new construction? An example is Malden Court in Capitol Hill. Malden Court, a development of ten homes (priced between \$150,000 to \$170,000), was built on the site of modest bungalows in Capitol Hill; the original bungalows were demolished to make way for the infill housing because the market and zoning supported a higher intensity of use. Malden Court has won awards, because while it increased the site's density, it sensitively matched the mass, height, building spacing, and “front-porch signature” typical of Capitol Hill's single-family housing. Malden Court is attractive infill housing, but it is new construction rather than rehab. Will growth management encourage more new Malden Courts at prices approaching \$200,000 rather than the affordable renovation of the existing housing stock?

A third negative influence of growth management on affordable-housing rehab in Seattle has to do with its possible curbing of adaptive reuse. In many areas of Seattle, housing has been delivered through the adaptive reuse of industrial properties. Regulations that protect industrial uses from such “encroachment” impede this housing delivery process. The Seattle Comp Plan designates two Manufacturing/Industrial Centers—Ballard/Interbay and Duwanish. Is such designation perhaps discouraging the reuse of industrial buildings in these neighborhoods to housing?

Many preservationists tout growth management as a support for retaining and upgrading the existing stock, whether historic or otherwise. That may be happening in Seattle. Yet there are instances, as described herein, where growth management may be making it harder to do affordable-housing rehab in that city.

### **COMBINED DEVELOPMENT AND CONSTRUCTION PHASE BARRIERS TO AFFORDABLE-HOUSING REHAB**

Thus far we have been describing the barriers discretely. Yet, it is the concatenation of the many hurdles that can discourage affordable-housing rehab. A declining supply of the most logical candidates for rehab (e.g., SROs in the downtown) and the many building code, access, and other barriers can dampen enthusiasm for renovation. This sentiment is echoed in the following remarks by Seattle’s Samis Company.

Economics is the biggest challenge in restoring very old buildings . . . In general, the amount of structural changes, as well as electrical upgrades, plumbing replacement, and asbestos removal, make it [rehab] much more costly than new construction. (Murphy 1998)

Many individuals interviewed by CUPR indicated they are doing a lot less rehab than they did in the past and more new construction (Thomas 1999; Nodland 1999). One architect asserted “It [new construction] is a lot easier; with rehab you have to jump through hoops” (Murphy 1999).

Another developer said, “I started small in rehab by getting surplus properties from the city, but now I have bootstrapped myself to new commercial work, which is easier and more profitable” (Anonymous).

What would it take to bring Seattle’s former rehabbers back to the field? Addressing the many hurdles described in this case study is a start. So, too, are enhanced incentives. For example, a proposed multifamily tax-abatement program in eight Seattle neighborhoods (including Pioneer Square) would waive property taxes for 10 years in new or remodeled residential buildings of four or more units. (This would make Seattle’s existing 10-year special property tax credit for historic buildings more widely applicable). While the multifamily tax-abatement program is not limited to rehab it would be a start to reinvigorating this activity in the city. It could be further tailored to affordable-housing rehab by offering a bonus (a higher credit or a longer-than-10-year qualifying period) for rehab as opposed to new construction and an added bonus when the rehab is affordable.

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