Preserving and Expanding Affordability in Neighborhoods Experiencing Rising Rents and Property Values

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Abstract

To ensure that low- and moderate-income households can continue to afford to live in neighborhoods experiencing rising rents and property values, local governments will need to adopt comprehensive strategies that make use of multiple policy levers. This article outlines a framework for thinking about the necessary local policies organized into six components: (1) preservation, (2) protection, (3) inclusion, (4) revenue generation, (5) incentives, and (6) property acquisition.

Introduction

Many urban neighborhoods are experiencing increases in rents and property values associated with an influx of higher-income households. This phenomenon (sometimes referred to as "gentrification") can be a double-edged sword. On the one hand, it may contribute to the revitalization of older deteriorated buildings; generate increased property taxes for cities, helping to shore up city finances; and contribute to greater diversity in terms of income, race, and ethnicity. On the other hand, many critics are concerned that the rent and property value increases may push out long-time residents of these neighborhoods, undermining the full potential of these changes to enhance community diversity, disrupting longstanding cultural traditions, and depriving long-term residents of the health, educational, and quality-of-life benefits of living in revitalized neighborhoods.

The ideal solution to the challenge of rapidly rising rents would preserve opportunities for low- and moderate-income households to continue to afford to live in these neighborhoods even as higher-income households move in, increasing income, expanding racial and ethnic diversity. To achieve this outcome, cities and counties will need to be proactive in adopting local housing strategies designed to preserve and expand the availability of affordable housing in these neighborhoods. A successful strategy generally will require the adoption of multiple policies or programs to address different aspects of the challenge and achieve a larger cumulative impact as well as advance planning to anticipate areas where rising rents and home prices are likely so the needed policies can be adopted early in the trajectory of neighborhood change. Communities will need to coordinate the actions of multiple local government agencies and build close working partnerships with many nongovernmental actors, including nonprofit organizations and for-profit developers, community development corporations, advocates, and others.

To address this challenge, local governments need to focus on six housing strategy components—

1. **Preservation.** Preserve existing affordable rental units.
2. **Protection.** Help long-time residents who wish to stay in the neighborhood.
3. **Inclusion.** Ensure that a share of new development is affordable.
4. **Revenue generation.** Harness growth to expand financial resources for affordable housing.
5. **Incentives.** Create incentives for developers of affordable housing.
6. **Property acquisition.** Facilitate the acquisition of sites for affordable housing.

In general, these policies will be most useful in cities and counties where strong regional economies are creating an increased demand for housing in urban areas that is driving up rents and home prices. Many of these high-cost communities are experiencing rent and home price increases throughout (or in large parts of) the city or county. These policies also may be useful, however, to address rising rents and home prices in particular neighborhoods within cities or counties that are otherwise considered to have a weak or stable housing market.

This article provides a broad overview of housing policies and programs that address each of these housing strategy components, followed by a brief discussion of cross-cutting issues that will need to be addressed as part of a comprehensive strategy for preserving and expanding affordability in these neighborhoods.

Housing Strategy Components

1. Preservation: Preserve Existing Affordable Rental Units

The first component of an overall strategy in this area aims to preserve the affordability of existing affordable rental units despite increases in surrounding property values and rents. These units fall into two main categories: (1) rent-restricted rental units and (2) unsubsidized but affordable units. Federal and state public housing units may also need preservation, although the challenges are somewhat different and so are addressed in the "Preserving Public Housing" section as a third category.

Preserving Rent-Restricted Rental Units

Most rental housing preservation efforts focus on units for which rents are legally restricted to affordable levels (rent-restricted units), usually because the owner receives one or more government housing subsidies. Federal rental subsidy programs include the Low-Income Housing Tax Credit (LIHTC) Program; a number of programs from the U.S. Department of Housing and Urban Development (HUD)—including the project-based Section 8 Program, the Section 202 Supportive

Housing for the Elderly Program, the Section 811 Supportive Housing for Persons with Disabilities program, and the Section 236 Mortgage Program—and programs from the U.S. Department of Agriculture (USDA) such as the Section 521 Rural Rental Assistance program. Two HUD block grant programs—the HOME Investments Partnership Program and the Community Development Block Grant (CDBG) program—also provide funding for housing subsidies. Some states and localities also have housing subsidy programs.

Preservation efforts tend to focus on units for which rents are restricted due to the receipt of government funding, in part, because these units are often easier to preserve than unsubsidized units and, in part, because some (though not all) of these housing units provide "deep" subsidies that base rents on 30 percent of household income. These deep subsidies are especially important for ensuring that poor households—including those living entirely on Social Security and the working poor—can afford to live in the community. The deep subsidy programs include project-based Section 8, project-based vouchers, Section 202, Section 811, and USDA's Section 521.

Preserving rent-restricted units presents three main challenges. The first challenge is that the subsidies giving rise to rent restrictions usually have a specific duration, after which the subsidy expires and the owner may choose to raise rents to market levels. In some programs, owners also have the choice of "opting out" during the normal term of the subsidy at various trigger points or time intervals. In neighborhoods that are experiencing or expecting to experience increases in market rents, owners usually have a financial incentive to exercise their rights to raise rents to market levels rather than agreeing to keep rents below market levels. Counteracting financial incentives will thus be needed in many cases to convince owners to keep rents below market.

The second challenge is that some subsidized developments have accrued sizable capital needs that need to be addressed, such as roofs or furnaces that need to be replaced and kitchens and bathrooms that need to be updated. One way to address these needs is to seek residents capable of paying higher rents, enabling the development to borrow money against the higher rental stream to pay for capital improvements. This approach, of course, defeats the goal of long-term affordability. To address this issue, owners will often need a grant or below-market-rate loan to pay for the needed improvements, which can itself be a quid pro quo for extending affordability periods.

The third and final challenge is that, in some cases, properties are no longer being managed actively by owners but rather are more in caretaker mode. This occurs, in particular, for older properties developed as tax shelters under pre-1986 tax law, in which the owners are at points in their lives or careers where they are mostly waiting for the subsidy to end so they can sell the property rather than actively managing the property as an ongoing endeavor. In these cases, it may be important to bring in new owners who are more mission driven and focused on actively managing the developments as affordable rental properties.

Approaches used to preserve the affordability of rent-restricted units include the following—

- **Creating preservation catalogs.** An important first step is to identify the units one is trying to preserve along with information about the type of subsidies and rent restrictions present in each development and the timing of when those subsidies are going to expire. Some of this information is already available through the National Housing Preservation Database (http://www.preservationdatabase.org), but other information—notably, regarding state and local subsidies—will need to be added to complete the picture. A policy brief by the Center for Housing Policy (n.d.) provides information on how preservation catalogs work, based on examples from Chicago, Illinois; Florida; New Jersey; New York City, New York; and Washington, D.C.

- **Prioritizing properties.** After the full range of potential properties has been identified, communities can determine their priority targets for preservation by reaching out to owners to learn more about their intentions and the physical and capital needs of the property and determining the likelihood that any given property will leave the subsidized housing inventory. In general, the properties at greatest risk are (1) located in neighborhoods with the highest market rents and (2) not owned by a mission-driven owner, such as a nonprofit organization; properties with high levels of accrued capital needs are also vulnerable. Where practicable, it is best to do a site-by-site analysis, because circumstances can vary from property to property. This analysis, in turn, can facilitate a determination of how properties' needs can be met in ways that encourage the preservation of long-term affordability.
- **Targeting resources.** Communities may elect to prioritize the highest priority preservation projects for the limited resources available for housing and community development activities, including HOME and CDBG funds, LIHTC, tax-exempt multifamily bonds, and 501(c)(3) bonds. The goal of such efforts generally is to develop a package of financial supports that can help properties meet any accrued capital needs and be in a position to continue to do so for as long of a period as possible. The quid pro quo for these efforts usually is a long-term extension of affordability.
- **Expanding resources for preservation.** In many cases, additional funding—above and beyond the amount normally available through federal funding streams—will be needed to preserve properties. The policies discussed later under the "revenue generation" component generate flexible funding that can be used to meet a wide range of affordable-housing needs, including preservation.
- **Facilitating transfers to new owners.** As noted previously, the preservation challenge sometimes extends beyond providing financial assistance to ensuring that properties are owned by mission-driven owners committed to actively managing the property and preserving long-term affordability. To achieve this objective, communities will often need to cultivate mission-driven owners (often nonprofit organizations) and to facilitate and finance their purchase of the properties.
- **Adopting other preservation-friendly policies.** Other policies that can help facilitate preservation of subsidized properties include (1) tax abatements to lower property taxes for owners that agree to preserve their properties as affordable, such as in the Class S incentive program in Chicago; (2) advance notice policies that give subsidized renters advance notice when an owner seeks to leave a subsidized housing program; and (3) right of first refusal policies that give either all renters or just subsidized renters (depending on the policy) a right of first refusal to match any offer to purchase a rental property that an owner seeks to convert to condominiums.[1]

Galen Terrace Apartments in Washington, D.C., provides an example of preservation policies at work. A troubled project-based Section 8 property facing physical deterioration and criminal activity, Galen Terrace came under new ownership as a result of Washington, D.C.'s policy that gave

[1] Condominium conversion protections are discussed in greater depth in the "Protection" strategy.

residents a right of first refusal in the event that a rental property was put up for sale. Members of the tenant association exercised this right in 2006 and worked with the National Housing Trust-Enterprise Preservation Corporation and Somerset Development Company to make long-needed renovations and preserve the property as affordable, using a mix of low-income housing tax credits, private activity bonds, a 20-year renewal of the property's Section 8 contract, and other financing sources (National Housing Trust, n.d.).

Preserving Unsubsidized but Affordable Housing

A large share of the nation's affordable rental housing stock consists of privately owned unsubsidized units—usually older units in which rents have filtered down over time as newer units with more amenities have come on line. Many of these rental units are single-family homes or homes that provide two or three units. Others are in small, midsize or larger multifamily buildings. In many neighborhoods with rents that are low compared with those in the city or metropolitan area as a whole, these units—sometimes called "market-rate affordable" units—significantly outnumber the number of subsidized rental units.

Given the large number of these unsubsidized but affordable units, it makes sense to at least consider efforts to preserve them as affordable as neighborhoods change. Doing so, however, is easier said than done. Absent the "hook" provided by a government housing subsidy or ownership by nonprofits or mission-driven for-profit organizations, few reasons exist for owners of these buildings to forgo the profit associated with higher rents or conversion to condominiums when the market conditions allow for these higher returns.

Options to consider for preserving strategically important unsubsidized properties include the following:

- **Facilitate the purchase by mission-driven owners committed to preserving the properties as affordable.** The pioneering Housing Partnership Equity Trust offers a model for preserving the affordability of market-rate rental housing that could be put to use in target neighborhoods. Organized as a real estate investment trust (REIT), the REIT raises funds to enable participating nonprofit organizations to purchase decent-quality, market-rate affordable properties for the purposes of maintaining them as affordable over time. Tenant protection laws represent another mechanism for facilitating the purchase of properties by mission-driven owners. In Washington, D.C., for example, owners of a rental property who wish to sell it or discontinue its use as a residential property must provide residents with the first opportunity to purchase the property and a right to match any legitimate offer. This policy helped to facilitate the preservation of Galen Terrace Apartments, noted previously.
- **Provide incentives for properties to stay affordable.** In Chicago, the Class 9 program provides a tax abatement for owners of market-rate properties that undergo substantial rehabilitation so long as they agree to maintain a certain percentage as affordable. Such programs can be helpful in maintaining market-rate units as affordable but, in general, have a limited duration—such as 10 or 15 years. In the context of changing neighborhoods, such policies might best be considered as a bridge to maintain affordability for a 10- or 15-year period to provide the community with time to develop and implement longer-term options for affordability, such as the construction of LIHTC developments paired with long-term affordability covenants.

- **Bring properties into a subsidy program.** Owners of market-rate properties with substantial capital needs may find it attractive to use the LIHTC Program as a vehicle for recapitalizing and upgrading the development. Because LIHTC units may be rented only to households with incomes that are less than 60 percent of the Area Median Income (AMI)—and many target even lower-income households—this process effectively preserves the affordability of these units and also improves their quality through the investment of additional equity. The project-based Housing Choice Voucher program is another option that has the added advantage of creating units affordable to households with extremely low incomes.

Preserving Public Housing

Although most discussions of rental housing preservation focus on either privately owned rent-restricted housing or unsubsidized but affordable housing, it is also important to focus on the preservation of any public housing units that may be located within the target neighborhoods. The preservation challenge for these units generally does not refer to the preservation of affordability but rather to maintenance of the units in good physical quality. Although, in some cases, these units may be in good condition, in other cases, they may have substantial accrued capital needs and will require new financing to bring them up to current standards.

The legal framework for public housing can make it difficult to use the LIHTC Program to recapitalize these properties. A new program called the Rental Assistance Demonstration (RAD), however, offers a solution that converts public housing subsidies into a form that can be married more easily with the LIHTC Program and other subsidy mechanisms. Congress currently caps the number of public housing units eligible to convert to RAD. See Costigan (2016) for an overview of the RAD program and its initial accomplishments.

2. Protection: Help Long-Time Residents Who Wish To Stay in the Neighborhood

In addition to taking steps to preserve affordable housing in target neighborhoods, communities can adopt a variety of policies to protect low-income households from being displaced by rising rents and home values and help them manage the relocation process. Because many of these policies involve providing legal protections to renters, legal services and marketing campaigns often will be needed in conjunction with these policies to ensure residents are aware of and have the ability to exercise their rights.

Policies to protect residents from displacement include—

- **Condominium conversion protections.** These policies protect residents of multifamily rental properties in a variety of ways from adverse impacts when the properties in which they live are converted to condominium ownership. In addition to rights of first refusal for the building as a whole—discussed previously as a preservation tool—some policies require that residents be offered the right to purchase individual units in the building before they are offered to new residents. Other policies provide residents with advance notice of the conversion (so they can plan for an orderly move) and provide relocation assistance to displaced households.

- **Rent stabilization.** These policies specify that, after an initial rent is set, it can rise by only a specified amount each year. Although these policies often allow for rents to float to market each time a new resident is admitted—and thus do not guarantee the housing is initially affordable to any particular income level—they do promote housing stability for existing residents by limiting rent increases. Most policies allow owners to raise rents to cover investments in capital improvements, so the policies cannot offer full protection from large rent increases in areas experiencing an influx of higher-income residents. They also often apply only to older buildings.

- **Good-cause eviction protections.** In some states, renters can be evicted for any reason whatsoever or no reason at all. Often, communities have the power to adopt laws that provide increased protection, providing, for example, that owners demonstrate "good cause" for eviction, such as nonpayment of rent or intentional damage to the unit. Although these protections will not help residents who simply can no longer afford the rents, they can reduce the incidence of indiscriminate evictions, giving residents more time to adjust to higher rents and, if needed, look for alternative housing arrangements. When paired with rent stabilization policies, they can promote stability for existing residents for many years.
- **Property tax protections.** Renters are not the only ones affected by higher housing costs in areas experiencing influxes of higher-income households. Homeowners with low or moderate incomes may also face higher housing costs—even if they own their homes outright—in the form of higher property taxes due to increases in assessed home values. To help protect existing owners from displacement, communities can cap the amount by which property taxes increase in a given year, set a maximum property tax level based on income, exempt a certain amount of assessed value from tax, or defer collection of increased property taxes until a property is transferred or the owner becomes deceased. By applying these policies to residents who have been in the homes for a certain period of time (for example, 5 years), these benefits can be targeted to existing residents. Some states adopt similar policies in the form of a credit against state taxes. (See Lincoln Institute of Land Policy [2012] for a compilation of residential property tax relief policies.)
- **Shared equity homeownership.** This term encompasses a range of affordable ownership policies—including community land trusts, limited equity cooperatives, and deed-restricted homeownership—that are designed to provide both initial and lasting affordability. The basic approach is to use a subsidy (or inclusionary zoning) to bring homes down to a level affordable to the target income group and then to limit resale prices according to a formula designed to balance long-term affordability to the target group with an opportunity for owners to build assets. (See Davis [2006] and Lubell [2014].) Done well, this approach can ensure that a single subsidy provides affordable-housing opportunities for one generation of homebuyers after another due to the long-term affordability of the subsidized homes. For this reason, it is well suited to changing neighborhoods that are experiencing an influx of higher-income households and can be used either as a protective mechanism to help residents continue to afford to live in a neighborhood or as a vehicle for expanding the stock of permanently affordable housing.
- **Housing Choice Voucher homeownership.** In the Housing Choice Voucher Homeownership Program, tenants with housing choice vouchers use them to pay for homeownership costs, such as mortgage payments and property taxes, rather than for rent. The family pays 30 percent of its adjusted income for housing costs and the public housing authority pays the difference between the family contribution and a locally determined voucher payment standard (Brennan and Lubell, 2012). Communities interested in using voucher homeownership as a protective

strategy for existing residents in a changing neighborhood could work with their local housing authority to ensure the option is available in the community and encourage its use in the target neighborhoods.

3. Inclusion: Ensure That a Share of New Development Is Affordable

In addition to preserving existing affordable housing within changing neighborhoods, local governments will also want to take steps to ensure that a share of new development is affordable. The most common mechanism for doing so is "inclusionary zoning," a land use policy that either requires or creates incentives for developers to make a share of newly developed units affordable. The related term "inclusionary housing strategy" or "inclusionary housing policies" encompasses inclusionary zoning and most of the other policies covered by this article that help ensure that affordable housing is available in areas experiencing new development.

Mandatory Inclusionary Zoning

Inclusionary zoning policies can be mandatory or voluntary. The classic mandatory inclusionary zoning ordinance specifies that a share of newly developed housing units—for example, 10 or 20 percent—must be affordable to households at a specified income level. In developing a mandatory inclusionary zoning policy, communities will need to determine—

- Which developments are covered by the mandate.
- The share of units required to be affordable.
- The target income level of the affordable units.
- The duration of required affordability.
- Whether to allow owners to pay a fee in lieu of providing units on site.
- Whether to allow owners to build units off site in lieu of building on site.
- What offsets, if any, to provide developers in compensation for the lost revenue associated with the affordable units.

Allbee, Johnson, and Lubell (2015) provided a summary of the considerations involved in making these determinations. Jacobus (2015) prepared an indepth guide to designing mandatory inclusionary zoning policies. Sturtevant (2016) summarized lessons learned from research on inclusionary zoning. Levy et al. (2012) reviewed the inclusionary zoning policies of Montgomery County, Maryland, and Fairfax County, Virginia—longstanding inclusionary policies that, together, have produced more than 16,000 affordable units.

In some states—notably California, Colorado, and Wisconsin—courts have interpreted mandatory inclusionary zoning policies as a form of rent control, which is not permitted under these states' laws, and thus restricted the ability to apply these policies to rental housing. To address this limitation, several California jurisdictions, including San Francisco, have instituted an affordable-housing fee on new rental development. Developers have the option of producing affordable housing units in lieu of paying the affordable-housing fee. (This approach is essentially the inverse of a traditional inclusionary zoning policy.) The high fee in San Francisco has made the affordable-housing development option more attractive to developers (Hickey, 2013).

Voluntary Inclusionary Policies/Density Bonuses

Although most successful inclusionary zoning policies are framed as requirements, some policies have succeeded in generating affordable units through policies that are voluntary rather than mandatory. The key to a voluntary policy is to have really strong incentives that make sense within the market context. For example, New York City rezoned formerly industrial land on the Brooklyn waterfront as residential land, providing a strong density bonus for developers that agreed to meet specified affordability targets (20 percent of units at rents affordable to households at or below 60 or 80 percent of AMI, depending on the use of other programs). Because greater density is highly valued in New York City, the program was able to generate about 2,700 permanently affordable rental units between 2005 and 2013. Some 949 affordable units were built on the Brooklyn waterfront, which accounted for about 13 percent of total units built in the area (Ullman, Freedman-Schnapp, and Lander, 2013). New York City ultimately determined, however, that it needed to produce a larger number of affordable-housing units and thus, in 2016, adopted a new mandatory inclusionary zoning policy applicable to all future upzonings that requires about 25 percent of newly developed units in covered areas to be affordable.

Some communities have policies that provide—either as a matter of formal policy or as a matter of practice—that a certain level of affordability will be required whenever an applicant seeks a variance from the standard zoning requirements. This approach has the advantage of making the nexus between the affordability requirement and the provision of a government benefit in the form of the zoning variance very clear. It is also a policy that can be adopted as a matter of practice even when insufficient political will exists to adopt a broadly applicable inclusionary zoning policy. It additionally gives policy officials a significant level of control over individual development approval decisions, which get made on a case-by-case basis. On the down side, the policy provides less predictability to developers and also increased costs associated with navigating variances or special use permits for virtually every project, which can potentially depress the overall level of supply and investment in the housing market and raise housing costs for residents living in unsubsidized rental units.

4. Revenue Generation: Harness Growth To Expand Financial Resources for Affordable Housing

The fourth component of a strategy for helping to ensure that families of all incomes can afford to live in areas experiencing an influx of higher-income households is to set up mechanisms for using the growth associated with new development or redevelopment to generate funding for affordable housing. The three principal policies within this component are (1) tax increment financing (TIF), (2) linkage fees, and (3) housing trust funds.

Tax Increment Financing and Related Tools

In general, TIF is a mechanism used for funding infrastructure and other public improvements through the future increases in property taxes expected to result from these investments. Consider, for example, a community that wanted to redevelop a distressed downtown neighborhood and needed funding for the necessary investments in roads, sidewalks, water/sewer, schools, parks, and so on. These investments would be expected to increase the value of property located in the neighborhood, generating increases in property taxes. By establishing a TIF district, with specific geographical boundaries and a specific duration, a community can capture some or all of the increased property taxes that are collected after these investments are made (the "increment") for the duration of the TIF. These funds can be used to reimburse the community for the original investment or to repay a loan that was made to finance the original improvements. Depending on state law, the property tax increment can be used for other purposes as well, including affordable housing within the TIF district.

The key to using a TIF for affordable housing is to enact a legally binding requirement at the time the TIF is established to use a portion of the funds for affordable housing. For many years, such a requirement was in place in California, where 20 percent of TIF revenues from TIFs established by redevelopment agencies were required to be spent on affordable housing. Several cities have similar requirements, including Madison, Wisconsin, which has a 10 percent set-aside of TIF funds for affordable or workforce housing, and Portland, Oregon, which has committed to invest a minimum of 30 percent of TIF funds in affordable-housing development. In other communities, no citywide requirement exists for an affordable-housing set-aside from all TIFs, but the requirement has been included in the authorization of a specific TIF when adopted by city council or other authorizing body.

One challenge with using TIFs in the context of areas with rising rents and home prices is that the enabling statutes often specify that TIFs be used only in blighted or distressed neighborhoods. In states that take a strict view of requiring blight or distress as a condition for establishing a TIF, it may make sense to seek statutory authorization for a new type of mechanism that works similarly to a TIF but can be applied equally to neighborhoods experiencing an influx of higher-income households, irrespective of whether the neighborhood starts out as blighted or distressed. Such a vehicle might conceivably tap only a portion of the "increment," as traditionally defined in TIFs, to minimize concerns of diverting funds from schools and could have limited uses—perhaps focused only on affordable housing or on a narrow range of activities that include affordable housing.

The Homestead Preservation Reinvestment Zones established by the Texas legislature to address concerns with gentrification in parts of Austin and Dallas provide a precedent for this approach. The 2005 legislation (updated in 2013) authorizes TIF-like vehicles and also other housing policy options within districts designated locally within Austin and Dallas to, among other things, "provide affordable housing for low-income and moderate-income residents in the community; . . . promote resident ownership and control of housing; . . . keep housing affordable for future residents; and capture the value of public investment for long-term community benefit."[2] Although the criteria for establishing the zones are still somewhat restrictive and the specific basket of policies included in the legislation may or may not make sense in every state, the legislation nevertheless provides a precedent for other states to set up specific zones designed to capture a portion of increased property tax values for purposes of helping to preserve and expand affordable housing in changing neighborhoods.

[2] Texas H.B. 525 (2005), relating to the creation of homestead preservation districts, reinvestment zones, and other programs to increase home ownership and provide affordable housing.

Linkage Fees

Linkage programs are another mechanism for generating funding for affordable housing in neighborhoods undergoing development or redevelopment. They generally are implemented as a fee, applied on a per-square-foot basis to new retail development.

A number of justifications exist for these fees. In areas where retail and residential developers are competing directly for land—as is often the case in changing urban neighborhoods that are characterized by mixed-use land patterns—the competition can drive up property values, aggravating affordable-housing challenges. In areas where retail and residential developers are not in *direct* competition, such as in designated retail areas, the addition of new retail can still reinforce the cycle of neighborhood change in nearby residential areas, providing amenities that attract additional higher-income households and also workers who want to live close to work, leading to increases in rents and home values.

Linkage fees are also sometimes explained as a remedy for a "jobs-housing imbalance" in a market where commercial development begins to outpace affordable-housing production. Some communities have found that commercial projects, such as the construction of offices, business parks, hotels, warehouses, and shopping centers, create a demand for housing affordable to the very low and low-income households that work there. This increased demand for a limited supply of affordable units can drive up rents and home prices that potentially jeopardize the ability of existing residents to afford to remain in the neighborhood.

In implementing a linkage program, communities need to strike a balance between raising funds for affordable housing and encouraging economic development and growth. Communities also need to meet a number of legal requirements. Local governments generally are required to show a reasonable nexus between the challenge the community is trying to address (in this case, the need for affordable housing created by commercial development) and the solution being adopted (the linkage fee). See David Paul Rosen & Associates (2001) and Local Progress and Cornerstone Partnership (2013).

Linkage fees have been used successfully in a number of communities around the country. Some localities like Fairfax County have implemented a linkage fee program in response to planned transit development. Others, like Boston, Massachusetts, apply the policy citywide.

Housing Trust Funds

Many cities, counties, and states have established housing trust funds to generate flexible revenue for affordable housing. These funds can be financed in a variety of ways, including through general revenue bonds, discretionary appropriations, document recording fees, real estate transfer taxes, linkage fees, and fees paid in lieu of providing affordable units under an inclusionary zoning policy.

Many of the funding mechanisms for housing trust funds are linked to new growth and thus represent a form of "value capture" similar to TIFs and linkage fees. In addition to linkage fees and in-lieu fees, these mechanisms include document recording fees and real estate transfer taxes. These "dedicated" fees rise and fall with the volume of new development and so represent a good way to generate funding when communities are experiencing new development. When growth slows down, however, these funding sources start to dry up, even if the need continues to be high for affordable housing. The Center for Community Change (n.d.) provides a hub for information on state and local housing trust funds.

5. Incentives: Create Incentives for Developers of Affordable Housing

Communities can offer a range of incentives to stimulate the development of affordable housing in targeted areas. Voluntary inclusionary housing policies are essentially structured as an incentive, generally offering increases in density or relief from other provisions of the zoning code in exchange for the inclusion of affordable units within new development. This section highlights additional incentives that communities can use to stimulate the production of additional affordable housing, including—

- Tax incentives.
- Parking incentives.
- Expedited permitting.
- Reduced impact fees.
- Transfers of development rights.
- Targeting of federal, state, and local housing subsidies.

To be effective, the incentives need to make a material difference in the bottom line for developers, which can be accomplished through a single large incentive or by combining smaller incentives together to achieve a larger collective impact.

Tax Incentives

Communities have used a range of tax incentives to encourage the development and rehabilitation of affordable housing. Common tax incentives include freezing a property's taxable assessed value after construction or rehabilitation for a period of time or providing a lower property tax rate. These policies are sometimes called tax abatements or exemptions. Some states also provide a credit against state income taxes.

Tax incentives can be used to achieve a number of different housing policy goals. In neighborhoods experiencing rapidly rising rents, communities will want to focus on incentivizing long-term affordability. In weaker markets or in neighborhoods with higher levels of distress, tax incentives can be used to stimulate rehabilitation and new development of market-rate homes.

Parking Incentives

Because of local zoning codes, developers often have to meet minimum off-street parking requirements meant to reduce traffic congestion and overcrowding. These parking spaces increase land acquisition costs, which often are passed on to the homebuyer or renter. By reducing parking requirements for developments that include affordable housing, localities can decrease production costs, allowing the developments to provide more affordable housing. This tool may be particularly useful in dense, high-cost cities where land prices are very high and account for a large proportion of a development's overall costs.

For example, in Denver, Colorado, developers of rental housing who voluntarily agree to set aside at least 10 percent of the units as affordable housing receive a reduction in parking requirements, among other incentives. In King County, Washington, developers receive a 50-percent reduction in onsite parking requirements for each affordable unit.

Expedited Permitting

Another incentive for affordable housing that some communities offer is an expedited permitting process that helps reduce development costs associated with delays in permit processing. For example, in 2009, Rhode Island passed a law, Expedited Affordable Housing Permitting, which granted state agencies the ability to expedite the approval process for affordable-housing developments that address critical housing needs. In Pinellas County, Florida, affordable-housing development receives priority in the permit review process with a 2-week turnaround.

Reduced Impact Fees

Impact fees are one-time charges for new development designed to cover the costs of developing infrastructure to support that unit, such as water, sewer, and schools. Court cases have established that impact fees must have a "rational nexus" in terms of the actual impact of development on public facilities or other infrastructure. By reducing or waiving fees for affordable housing below the levels that may otherwise be required, localities can provide incentives for developers to provide affordable housing.

Transfers of Development Rights

A transfer of development rights (TDR) program is meant to transfer development potential from one site to another. The "sending site" sells its development rights (for example, the right to build at all or above a certain height) to a "receiving area," where a developer can now build at a higher density or height than usually permitted by local zoning codes. Although often used to preserve open space, this approach has also been used to preserve affordable housing in dense, urban areas experiencing high levels of redevelopment. One approach is for existing affordable housing to serve as "sending sites" that can grant development rights to developers of other properties, raising funds to recapitalize and upgrade the units, preserving long-term affordability. This market-based tool has the ability to preserve certain areas and encourage development in other areas that can handle increased density. Rather than increasing overall density, TDR policies use the economic value of greater density to developers to generate funds for the development, rehabilitation, and preservation of affordable housing.

For example, a TDR program in Seattle has been used to preserve affordable housing since 1985. Seattle's TDR program focuses on preserving existing low-income housing in the city. Through the program, the city can transfer development rights from low-income housing sites to downtown developments that want more density. Nonprofit organizations that need to rehabilitate or preserve affordable-housing units sell the site's development rights to the city, which are then deposited into a TDR "bank" for developers to purchase.

Targeting of Federal, State, and Local Housing Subsidies

Other resources available to create incentives for the development of affordable housing in areas experiencing an influx of higher-income households are communities' bread-and-butter housing programs, funded by the HOME and CDBG funds and a diverse array of other funding sources, depending on the community, including general obligation bonds, general revenue, and state funding. In administering these programs, some communities give equal weight to applications from all parts of the community, but other communities give a preference for funding in certain priority neighborhoods. Because the resources for these programs are typically very limited, communities that wish to use their bread-and-butter programs as incentives for stimulating the preservation and expansion of affordable housing in particular neighborhoods will likely want to signal clearly in their requests for proposals and other funding plans that investments in specific target neighborhoods (or neighborhoods meeting certain criteria of need) will be prioritized for funding.

Federal funding for both HOME and CDBG has experienced cuts, leading to tight allocations that force communities to make difficult choices and reduce the scale of the impact that can be achieved directly with this funding. In considering the impact of these funding sources and decisions on how to target these funds, however, it is important to remember that these and other sources of local funding often leverage substantial additional funding through the LIHTC program. In many communities, LIHTC deals require some source of "gap funding" to cover the difference between what a project costs to develop and what the equity raised by the LIHTC and the debt supported by expected rent revenues will support. For this reason, a community's decision to focus a substantial portion of its allocation of HOME or other funds on specific geographical areas can have an outsized impact on the production of affordable housing in those neighborhoods.

6. Property Acquisition: Facilitate the Acquisition of Sites for Affordable Housing

One of the biggest challenges associated with preserving and expanding affordable housing in an area experiencing rising rents and home prices is gaining control of desirable sites for development or redevelopment at affordable prices. These challenges differ depending on where a neighborhood is on the spectrum of neighborhood change.

Early in the trajectory of neighborhood change—when an increase in demand is not yet apparent or has not yet expressed itself in higher rents or land prices—development sites generally are easier to acquire at comparatively affordable prices. The lower prices, however, generally reflect a heightened level of risk, at least from the perspective of market-rate developers, because the potential of the site to achieve full occupancy (or sell at prices that will generate a profit) is not yet clear. Because of this uncertainty, a lengthy holding period often is required between the time a property is acquired and the time a property is developed, which can add costs (interest on any loans taken out to purchase the property plus responsibility for property taxes) and, in some cases, make it more difficult to use federal funding for the acquisition.

At this stage in the cycle, developers interested in preserving or developing affordable housing may need access to capital for land acquisition that is more patient than federal block grant funding and, in some cases, may need assistance paying for property taxes while a property is in the holding period. They also may need some backstop for the risk that a neighborhood may not be ready to absorb the planned development for some period of time. Although the challenges associated with achieving full occupancy in an affordable property are different from those of a market-rate property, they are real and need to be addressed for a development to be successful.

By contrast, late in the trajectory of neighborhood change—after rents and home prices have risen substantially—the challenge is reversed. At this point, prices tend to be high but the risk that a property will not achieve full occupancy is much lower. Easy-to-develop sites often are hard to find and property prices generally assume that renters or purchasers will have much higher incomes than the low-income households affordable-housing developers seek to serve.

At this point, developers of affordable housing do not need long-term patient capital so much as they need flexible capital that can be deployed quickly to compete effectively with private developers offering all-cash purchases. They also need financing on attractive terms. To achieve affordable, flexible financing that is easy to deploy quickly, some form of credit enhancement often will be needed from the public or nonprofit sector.

Of course, many neighborhoods fall in between these two extremes. Communities that wish to maximize the availability of affordable housing in targeted neighborhoods can facilitate its development by working closely with developers of affordable housing to understand the property acquisition challenges they face and help them overcome them.

The following two approaches have been used to help developers acquire properties for affordable housing.

Property Acquisition Funds

Some communities have set up funds to facilitate the purchase and holding of properties for development as affordable housing. The most common model is a revolving loan fund that provides low-interest-rate loans to nonprofit organizations for the acquisition of property to be developed or redeveloped as affordable housing. A second approach is a direct acquisition model in which a single entity purchases and holds land for subsequent development by outside developers.

These funds address several factors that prevent nonprofit developers from competing on an equal footing with private developers in the private market. Unlike market-rate developers, developers of affordable housing typically have few sources of available flexible funds to purchase property. In addition, public-sector funds for affordable-housing development usually require a lengthy application and competition process. These factors constrain the ability of an affordable-housing developer to successfully compete for property acquisitions in the private real estate market.

Affordable-housing developers can access low-interest capital more quickly through acquisition funds than through many other public-sector funding sources. These funds are usually made possible by the collaboration of several investors, including the local government, community development financial institutions, and private banks.

The New York City Acquisition Fund provides an example of how an acquisition fund can provide support for affordable-housing development in a highly competitive housing market. To help level the playing field with market-rate developers, the fund makes up to $210 million in loans available for up to 3 years to developers of affordable housing for acquisition and predevelopment financing through major banks and financial institutions. These institutions are protected by a $40 million guarantee pool consisting of $8 million of City funding and $32 million in funding from philanthropic foundations (New York City Global Partners, 2013).

Two other funds focus more specifically on facilitating affordable-housing development near transit—

1. The Bay Area Transit-Oriented Affordable Housing Fund is a $50 million fund managed by the Low-Income Investment Fund, a Community Development Financial Institution. The fund focuses primarily on supporting the production and preservation of affordable housing in the San Francisco Bay Area, but 15 percent of the funds are set aside for the development of neighborhood amenities, including community facilities, health clinics, retail, and grocery stores. (Seifel Consulting Inc., 2013).

2. The Denver Transit-Oriented Development Fund is an example of the alternative model in which a single entity—the Urban Land Conservancy—purchases and holds property for subsequent development. It was established to purchase key sites for the creation and preservation of more than 1,000 affordable-housing units in "current and future transit corridors" in and around Denver (Urban Land Conservancy, n.d.)

Use of Publicly Owned Land

Another approach to addressing the challenges associated with acquiring properties for development of affordable housing in changing neighborhoods at reasonable prices is to focus on properties owned by public agencies within the city, including properties owned by public hospital corporations, police and fire departments, school boards, and a wide range of administrative entities. Some of these sites may have vacant or underutilized land that can be used for affordable housing, such as a parking lot that is rarely at capacity. In other cases, a property may have been developed at a density that is low compared with the higher densities emerging as the community changes. By redeveloping the property at a higher density, the original purpose can continue to be served while also making space available for affordable or mixed-income development.

In addition to developing affordable housing on land controlled by a range of city agencies, some communities also seek to use the inventory of tax-delinquent properties as a source of property for affordable housing. This approach works as long as an adequate number of tax-delinquent properties that are desirable development sites are within the target neighborhoods. As the market for housing in target neighborhoods begins to heat up, however, fewer tax-delinquent properties are likely to be within those neighborhoods as owners find buyers willing to purchase the properties and retire the tax debt. So this approach may work better toward the beginning of a neighborhood change cycle than toward the end.

A number of challenges are associated with using tax-delinquent properties for affordable housing or other development, including lengthy and complicated tax foreclosure processes and challenges assembling small parcels into development sites. An excellent manual about "land banks" by Frank Alexander (2011) provides a comprehensive overview of the challenges and approaches to addressing them.

Cross-Cutting Issues

In developing a comprehensive housing strategy for preserving and expanding affordable housing in target neighborhoods, it will be important for localities to address a number of cross-cutting issues.

Advance Planning

Advance planning is always a good idea, but it is particularly important in this area because of the impact of rising land prices on the overall costs of an affordable-housing strategy. The longer one waits to get serious about an affordable-housing strategy, the more difficult and expensive it will be to acquire attractive sites for development or redevelopment as affordable housing. In some cases, the higher-income households that move into a changing neighborhood also become the strongest critics of new development, again underscoring the importance of early and comprehensive planning. Finally, it often takes a period of years to put a strategy in place and begin creating affordable units, so it is best to start early.

It is not always easy to identify which neighborhoods are likely to experience influxes of higher-income households before it happens, and, as noted previously regarding land acquisition, it can be problematic to guess incorrectly. Despite the risks, it is essential to be looking ahead and paying attention to early warning signs, rather than waiting until after the change process has taken place and having to play catch-up.

Public and Private Capacity

The successful execution of a strategy to address rising rents and home prices will require a high level of capacity both within and outside government. Cities and counties can look to similar communities for models of ordinances and implementing practices, but, ultimately, policies will need to be customized to meet the needs of each locality. Members of the development community and advocates can help local government officials identify promising models and adapt these models to local market dynamics. A strong infrastructure of affordable-housing developers will also be needed to help implement many of the policies.

Long-Term Affordability

Many affordable-housing strategies aim to create housing that is affordable at the outset, and perhaps for the next 10 to 15 years, but do not focus sufficiently on what happens to housing prices or rents after that time period. This flaw can be fatal for neighborhoods where home prices and rents are rising, because the homes are unlikely to remain affordable after the initial affordability period ends.

Options for maintaining long-term affordability include shared equity homeownership (on the ownership side) and long-term covenants and nonprofit ownership (on the rental side). Well-designed policies can maintain affordability for 50 years or longer, helping to maximize and maintain the value of scarce public subsidy and ensure that efforts contribute to the overall stock of affordable homes, rather than simply replacing units exiting the affordability period. In many cases, these options will require local initiative because the affordability periods required by federal law are not long enough to preserve affordability in changing neighborhoods.

Increased Density

Rents and home prices are highly sensitive to the law of supply and demand. So long as demand for housing is low and supply is high, prices and rents will tend to be low relative to other locations, but, when demand for housing is high and supply is low, rents and home prices tend to go up, which is often the case in changing neighborhoods.

Allowing for density to increase is one way to make it easier to accommodate strong demand among incoming residents in a changing neighborhood without displacing existing residents and thus has a place as part of an overall housing strategy. In a neighborhood experiencing strong increases in demand for housing, it will seldom be possible to increase density sufficiently to keep housing prices and rents from rising at all; the best conceivable outcome is slower growth in rents and home prices. Policies to increase density can also be problematic if they accelerate the process of neighborhood change before a full-blow housing affordability strategy is in place, and, by themselves, these policies rarely produce housing in changing neighborhoods that is affordable to the very lowest incomes. If married with a comprehensive affordable-housing strategy, however, increased density can play an important role in providing ample space for both existing residents and newcomers and in generating new development that produces affordable units through an inclusionary zoning policy.

Reduction of Barriers to Development

Consistent with the discussion on density, communities may wish to consider overall reforms to their housing entitlement process that reduce barriers to new development, allowing for the supply of housing to better respond to increased demand. Density is one component of this reform process, as are the related concepts of minimum lot size and required set-backs. Parking requirements can also be a problem by increasing the amount of land needed per unit. Other barriers include lengthy permitting processes, complicated and lengthy zoning approval processes, and environmental requirements that do not effectively balance legitimate environmental goals with the need for an increased supply of housing. As with density limitations, it is unlikely that a barrier reduction strategy on its own will achieve a community's affordability goals, but it can be an important part of a broader strategy.

Targeted Versus Citywide Policies

Many of the strategies discussed in this article can be employed either in specific neighborhoods or in the city as a whole. Communities will need to decide which approach to take. Targeted policies can be more impactful than broader policies, given a limited amount of public subsidy to expend, but they may raise political issues among residents and representatives of other parts of the community. One way to avoid the appearance of singling out particular neighborhoods is to specify that policies apply wherever certain objective market conditions apply, such as median rents above a certain level or median rents increasing at a certain rate. Some of the policies, such as TIF, can be applied only to a targeted area. In practice, many communities will end up with a combination of targeted and citywide policies.

Building Community Support and Political Will

Political support will be needed both to pass the necessary public policies and to ensure that individual affordable-housing projects can be developed. Community opposition can make or break an affordable-housing project. To facilitate the necessary development and the preservation and expansion of affordable housing, communities will need to work proactively with residents and resident leaders and groups to build a trusting relationship and ensure that the city's plans for the neighborhoods respond to residents' needs and concerns.

Conclusion

The dynamic of neighborhood change brought about by increases in demand among higher-income households can be difficult to fine tune. At the outset, neighborhood change holds the possibility of increasing diversity, but, after rent and home price pressures build up, the promise of increased diversity can give way to displacement and resegregation. The local policy environment has the potential to be an important factor shaping the final outcome. A range of policy tools are available to local governments to preserve and expand housing opportunities affordable to low- and moderate-income households. Communities that wish to protect long-time residents and preserve diversity will need to act proactively to adopt a suite of complementary policy tools as early as possible in the cycle of neighborhood change.

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