HOUSING AND COMMUNITY DEVELOPMENT

## Affordable Rental Housing At Risk of Conversion[1]

One of California's foremost housing problems is the potential loss of affordability restrictions on a substantial portion of the government-assisted rental housing stock. As of mid-1998, there were more than 3,200 such privately-owned multifamily rental developments in California, which included more than 186,000 housing units.[2] This housing sheltered an estimated 375,000 to 450,000 people, many of whom are very low-income elderly individuals and families with children. Much of this housing is "at-risk" of conversion from affordable housing stock reserved predominantly for lower-income households, to market-rate housing (see Table 27).

Several government programs, with different regulatory standards, were used to finance these properties, and thus, the nature of the risk of conversion differs. The eligibility of these properties for conversion from low-income use is both immediate and continuing beyond 2010. The timing of the number of at-risk units peaks, however, in relation to the conversion eligibility of the Section 8-assisted portion of the stock. More than 80 percent (92,000) of these units have Section 8 contracts expiring by 2005.

### *HUD and FmHA-Assisted Housing*

Approximately 80 percent of the 186,000+ properties were federally assisted by mortgage insurance, low-interest loans, and project-based rental subsidies (Section 8). This housing resulted from the primary affordable rental housing production programs of the federal government from the late 1960s through the early 1980s. These properties constitute a substantial share of the State's existing government-assisted rental housing stock for lower-income households.[3]

Under these programs, the federal government (HUD and what was then the Farmer's Home Administration, or FmHA)[4] provided subsidies to developers that led to the production of approximately 150,000 units. These include Section 515 properties, and those created by the HUD 221(d)(3) and 236 programs (referred to as "older-assisted" properties), and other project-based Section 8 properties. The first phase of these properties began converting to market-rate in the late 1980s, prompting federal enactment of the Emergency Low-Income Housing Preservation Act (ELIHPA) in 1986. In 1990, ELIHPA was succeeded by the Low Income

Table 27

## AFFORDABLE PROJECTS AND UNITS AT RISK OF CONVERSION (FROM 1997)

| | PROJECT BASED SECTION 8 (a) | | OLDER-ASSISTED PP-ELIGIBLE (b) | | SECTION 8 MOD REHAB | | BMR UNITS - TAX EXEMPT BOND (c) | | SECTION 515 | | TOTAL PROJECTS (d) | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Projects | Units | Projects | Units | Projects | Units | Projects | Units | Projects | Units | Projects | Units |
| **Greater Los Angeles Metro** | | | | | | | | | | | | |
| Los Angeles | 723 | 39,374 | 112 | 8,090 | na | 1,630 | 201 | 8,154 | - | - | 980 | 53,203 |
| Orange | 56 | 4,406 | 3 | 441 | na | 508 | 60 | 3,667 | - | - | 118 | 8,802 |
| Riverside | 48 | 3,078 | 2 | 331 | na | 545 | 54 | 2,322 | 40 | 2,159 | 143 | 8,270 |
| San Bernardino | 41 | 3,299 | 6 | 771 | na | 156 | 70 | 3,227 | 16 | 716 | 130 | 7,784 |
| Ventura | 10 | 616 | 4 | 379 | na | 163 | 17 | 908 | - | - | 29 | 1,877 |
| Imperial* | 15 | 413 | - | - | na | 82 | - | - | 27 | 1,058 | 42 | 1,553 |
| **Greater Los Angeles Metro Total** | **893** | **51,186** | **127** | **10,012** | **-** | **3,084** | **402** | **18,278** | **83** | **3,933** | **1,442** | **81,487** |
| **Bay Area Region** | | | | | | | | | | | | |
| San Francisco | 89 | 8,042 | 4 | 394 | na | 544 | 11 | 976 | - | - | 102 | 9,759 |
| Marin | 21 | 742 | 1 | 56 | na | 33 | 8 | 486 | - | - | 30 | 1,289 |
| San Mateo | 50 | 1,465 | 1 | 102 | na | 131 | 5 | 305 | - | - | 56 | 1,952 |
| Santa Clara | 80 | 7,014 | 4 | 463 | na | 271 | 24 | 1,557 | - | - | 106 | 9,074 |
| Alameda | 91 | 6,626 | 5 | 451 | na | 879 | 31 | 1,420 | - | - | 125 | 9,151 |
| Contra Costa | 42 | 3,437 | - | - | na | 248 | 28 | 1,392 | - | - | 70 | 5,077 |
| Sonoma | 22 | 1,297 | - | - | na | 128 | 14 | 634 | 8 | 304 | 44 | 2,363 |
| Solano | 23 | 1,471 | 3 | 288 | na | 92 | 7 | 657 | 3 | 96 | 35 | 2,460 |
| Napa | 8 | 391 | - | - | na | 35 | 2 | 38 | - | - | 10 | 464 |
| **Bay Area Region Total** | **426** | **30,485** | **18** | **1,754** | **-** | **2,361** | **130** | **7,465** | **11** | **400** | **576** | **41,588** |
| **Sacramento Region** | | | | | | | | | | | | |
| Sacramento | 105 | 5,897 | 30 | 1,614 | na | 79 | 25 | 1,686 | - | - | 145 | 8,469 |
| Placer | 9 | 456 | 3 | 170 | - | - | 1 | 124 | 13 | 663 | 25 | 1,328 |
| El Dorado | 5 | 313 | - | - | - | - | - | - | 10 | 364 | 15 | 677 |
| Sutter | 4 | 165 | 2 | 144 | - | - | - | - | 5 | 148 | 10 | 385 |
| Yuba | 5 | 439 | 1 | 76 | - | - | 1 | 28 | 5 | 223 | 12 | 728 |
| Yolo | 21 | 880 | 1 | 95 | - | - | 9 | 466 | 4 | 148 | 35 | 1,542 |
| **Sacramento Region Total** | **149** | **8,150** | **37** | **2,099** | **-** | **79** | **36** | **2,304** | **37** | **1,546** | **241** | **13,129** |
| **Central Valley Region** | | | | | | | | | | | | |
| Fresno | 38 | 3,027 | 7 | 518 | na | 191 | 26 | 1,938 | 31 | 1,479 | 99 | 6,894 |
| Madera | 2 | 121 | - | - | - | - | 1 | 136 | 5 | 174 | 8 | 431 |
| Kern | 32 | 1,261 | 9 | 290 | na | 74 | 2 | 310 | 26 | 1,022 | 65 | 2,812 |
| San Joaquin | 19 | 1,399 | 3 | 240 | - | - | 3 | 272 | 1 | 42 | 25 | 1,833 |
| Stanislaus | 14 | 1,108 | 2 | 142 | na | 75 | 7 | 430 | 7 | 303 | 29 | 1,987 |
| Merced | 8 | 364 | 1 | 46 | - | - | 6 | 270 | 18 | 758 | 33 | 1,415 |
| Tulare | 10 | 658 | 2 | 105 | na | 106 | 4 | 173 | 34 | 1,561 | 49 | 2,551 |
| Kings* | 6 | 286 | - | - | - | - | 2 | 118 | 17 | 750 | 25 | 1,154 |
| **Central Valley Region Total** | **129** | **8,224** | **24** | **1,341** | **-** | **446** | **51** | **3,647** | **139** | **6,089** | **331** | **19,077** |
| **San Diego** | **94** | **9,818** | **5** | **138** | **na** | **948** | **39** | **2,574** | **1** | **32** | **137** | **13,441** |
| **Central Coast Region** | | | | | | | | | | | | |
| Monterey | 11 | 557 | 2 | 150 | na | 135 | 5 | 355 | 3 | 150 | 20 | 1,272 |
| San Luis Obispo | 8 | 305 | 1 | 44 | - | - | 1 | 25 | 8 | 371 | 18 | 723 |
| Santa Barbara | 10 | 570 | - | - | na | 21 | 15 | 176 | 1 | 28 | 26 | 795 |
| Santa Cruz | 18 | 1,477 | - | - | na | 348 | 6 | 501 | - | - | 24 | 2,326 |
| San Benito* | 1 | 48 | 1 | 115 | - | - | - | - | 6 | 188 | 8 | 294 |
| **Central Coast Region Total** | **48** | **2,957** | **4** | **309** | **-** | **504** | **27** | **1,057** | **18** | **737** | **95** | **5,410** |

Table 27 (continued)

**AFFORDABLE PROJECTS AND UNITS AT RISK OF CONVERSION (FROM 1997)**

| | PROJECT BASED SECTION 8 (a) | | OLDER-ASSISTED PP-ELIGIBLE (b) | | SECTION 8 MOD REHAB | | BMR UNITS - TAX EXEMPT BOND (c) | | SECTION 515 | | TOTAL PROJECTS (d) | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Projects | Units | Projects | Units | Projects | Units | Projects | Units | Projects | Units | Projects | Units |
| **Northern California Region** | | | | | | | | | | | | |
| Butte | 14 | 679 | 4 | 274 | na | 80 | 3 | 133 | 7 | 488 | 26 | 1,517 |
| Shasta | 7 | 336 | - | - | na | 228 | - | - | 11 | 529 | 18 | 1,093 |
| Tehama* | 6 | 295 | 2 | 94 | - | - | 1 | 46 | 9 | 390 | 17 | 778 |
| Glenn* | 2 | 114 | - | - | - | - | - | - | 7 | 279 | 9 | 393 |
| Colusa* | 3 | 102 | - | - | - | - | - | - | 6 | 259 | 9 | 361 |
| **Northern California Region Total** | **32** | **1,526** | **6** | **368** | **-** | **308** | **4** | **179** | **40** | **1,945** | **79** | **4,142** |
| **NON-METROPOLITAN AREAS** | | | | | | | | | | | | |
| **Northern California Non-metropolitan Region** | | | | | | | | | | | | |
| Del Norte* | - | - | - | - | - | - | 1 | 56 | 4 | 180 | 5 | 236 |
| Humboldt* | 7 | 488 | - | - | - | - | - | - | 8 | 337 | 15 | 825 |
| Mendocino* | 11 | 447 | - | - | na | 96 | - | - | 16 | 636 | 27 | 1,179 |
| Lake* | 5 | 208 | - | - | - | - | - | - | 10 | 382 | 15 | 590 |
| Siskiyou* | 12 | 365 | 3 | 108 | - | - | - | - | 8 | 325 | 22 | 744 |
| Modoc* | 2 | 111 | 1 | 64 | - | - | - | - | 2 | 60 | 5 | 203 |
| Trinity* | - | - | - | - | - | - | - | - | 2 | 64 | 2 | 64 |
| Lassen* | 2 | 61 | 1 | 64 | - | - | - | - | 7 | 294 | 10 | 387 |
| Plumas* | 1 | 47 | - | - | na | 49 | - | - | 8 | 271 | 9 | 367 |
| Sierra* | - | - | - | - | - | - | - | - | 1 | 50 | 1 | 50 |
| Nevada* | - | - | 1 | 80 | - | - | - | - | 10 | 515 | 11 | 555 |
| **Northern California Non-metropolitan Region Total** | **40** | **1,727** | **6** | **316** | **-** | **145** | **1** | **56** | **76** | **3,114** | **120** | **5,200** |
| **Central-Southern California** | | | | | | | | | | | | |
| Amador* | 2 | 112 | - | - | - | - | - | - | 5 | 196 | 7 | 308 |
| Alpine* | - | - | - | - | - | - | - | - | - | - | - | - |
| Calaveras* | 2 | 27 | - | - | - | - | - | - | 5 | 187 | 7 | 214 |
| Tuolumne* | 3 | 106 | - | - | - | - | 1 | 39 | 9 | 426 | 13 | 571 |
| Mariposa* | - | - | - | - | - | - | - | - | 4 | 126 | 4 | 126 |
| Mono* | - | - | - | - | - | - | - | - | - | - | - | - |
| Inyo* | 1 | 6 | - | - | - | - | - | - | 1 | 34 | 2 | 40 |
| **Central-Southern California Total** | **8** | **251** | **-** | **-** | **-** | **-** | **1** | **39** | **24** | **969** | **33** | **1,259** |
| **Other (e)** | | | | | | **87** | **32** | **1,438** | | | **32** | **1,438** |
| **Metropolitan Counties** | **1,738** | **111,088** | **218** | **15,812** | **na** | **7,648** | **686** | **35,340** | **257** | **11,758** | **2,790** | **173,740** |
| ***Non-metropolitan Counties** | **81** | **3,236** | **9** | **525** | **na** | **227** | **5** | **259** | **172** | **7,007** | **263** | **10,992** |
| **TOTAL CALIFORNIA** | **1,819** | **114,324** | **227** | **16,337** | **-** | **7,962** | **723** | **37,037** | **429** | **18,765** | **3,085** | **186,170** |

**Notes:**

(a) Project-based Section 8 data from 1997 HUD Inventory. Because many projects have more than one contract, there are actually more contracts than projects. Figures are subject to renewal activity since 1996.

(b) Approximately 50% of Older-Assisted Prepayment Eligible units are also Project Based Section 8 developments; thus, some of these units overlap, an exact number is unknown.

(c) This section represents below market-rate units in projects funded with tax exempt bonds, including CHFA regulated non Section 8 projects.

(d) Total columns represent all numbers from all funding sources. Only 50% of units are counted from the older-assisted prepayment eligible stock (see note "a" above).

(e) Other for Section 8 Moderate Rehab is: "California Non-specified; Other for targeted tax exempt bond financed units is: "Multiple Counties"

**Sources:**

1) Project Based Section 8: HUD Inventory, November 1996; entire universe expiring units starting in 1996.
2) Older-assisted Pre-Payment Eligible: California Housing Partnership Corporation Research; entire universe expiring units starting in 1996.
3) Section 8 Moderate Rehab: HUD Profile, total universe of Section 8 Moderate Rehab as of June 1996.
4) Tax-exempt Bond Financed projects with expiring below market rate (BMR) units: Table III-2 "Units in Occupied Projects: Multifamily Housing", 1996 Annual Summary: The Use of Housing Revenue Bond Proceeds, California Debt and Investment Advisory Commission; entire universe expiring units starting in 1996; source for CHFA-regulated units: California Housing Finance Agency 1996-1997 Statistical Supplement to Annual Report, Section IV-1 - Asset Management
5) Section 515: Department of Rural Housing Services

Housing Preservation and Resident Homeownership Act (LIHPRHA). Both programs prevented owners from converting properties to market-rate; instead these programs provided financial compensation in exchange for new 20-50 year affordability restrictions, thereby continuing federal responsibility for preserving the affordability of this housing. HUD provided well over half a billion dollars to California projects through the ELIHPA and LIHPRHA programs, covering nearly 100 percent of all preservation costs. Since 1996, however, the risk of conversion of the HUD-insured portion of the at-risk stock has increased markedly due to the loss of assistance from these programs and the restoration of a direct conversion option.

Between the spring of 1996 (when the prepayment rights of owners were restored by Congress) and late 1997, owners of nearly 6,300 of the remaining older-assisted, prepayment-eligible units in California prepaid mortgages and converted to market-rate use. As of spring of 1998, an additional 1,400 units were in the pipeline for doing so. Although tenant vouchers can be used for transition, one-third of the units from the older-assisted stock were converted within approximately 18 months of eligibility. As of May 1998, there were approximately 16,300 additional units of older-assisted stock still eligible to convert from restricted to market-rate use. In the absence of some preservation incentives to current owners or potential purchasers, it is likely that additional "older-assisted" units will be converted and will reduce the affordable housing stock.

Section 8 contracts, which were originally issued for 15-20 year terms, are now subject to annual renewal. Upon expiration of the Section 8 contract, owners are generally under no obligation to accept a contract renewal and maintain the affordability of the units to lower-income households. Section 8 assisted properties include both the HUD older-assisted properties (approximately half of these), and newer assisted properties which were generally financed by HUD under the Section 221(d)(4) program, or by the California Housing Finance Agency (CHFA).

In late 1997, Congress enacted the Multifamily Assisted Housing Reform and Affordability Act (MAHRAA), which substantially alters how Section 8 subsidies are provided. This new law, which took effect on October 1998, is intended to control costs and introduce reforms in the Section 8 program. Under this program, State and local government will assume newly delegated responsibilities, whereby the CHFA[5] plans to serve as a "participating administrative entity" (PAE) for the implementation of the MAHRAA program to restructure eligible Section 8 assisted properties.

California's experience with market-rate conversion of the older-assisted stock suggests that 15-20 percent of the owners of the Section 8 inventory are likely to opt-out of project-based Section 8 and terminate their relationship with HUD unless new incentives are created to retain the Section 8 assistance. While some owners will choose to opt-out, other owners may be ineligible to renew their contracts. Owners might be ineligible, if for example, the development is saddled with financial or physical problems, or is located in an area with high vacancies and high contract rents. Thus, a significant number of affordable units could be lost due to owners opting out of subsidy contracts and also because some properties will no longer be eligible for Section 8 assistance. Based on an analysis of Section 8 contracts scheduled to expire during 1998-2000 which are at or below Fair Market Rents, the counties which appear most likely to experience owners opting out of Section 8 contracts are: Alameda, Contra Costa, Los Angeles, Sacramento, San Diego, San Francisco, and Santa Clara.

As of mid-1998, there were approximately 430 projects in California receiving Section 515 funding, representing nearly 18,800 units. In the mid-1980s approximately 1,800 units in 45 projects had their mortgages prepaid. However, subsequent to enactment of ELIHPA in 1987, mortgage prepayment on these properties is only allowed if other subsidies such as Section 8 are available, or if there is sufficient affordable housing in the region. Consequently, in the last 10 years, less than 200 units have been prepaid and no tenants were relocated or otherwise adversely affected. Since these properties are generally not located within high rent areas of the State and as tenants may not be displaced, these units are much less likely to be lost from the affordable stock than the other at-risk properties.

### *Mortgage-Revenue Bond Assisted Properties*

While roughly 80 percent of the rental housing at-risk of conversion from low-income use received direct subsidies from HUD or FmHA, the remaining 20 percent of California's at-risk housing was assisted with (federally-authorized) State or locally-issued mortgage revenue bonds (MRBs). Beginning in the early 1980s, these properties were financed with below-market interest rate mortgages in exchange for restricting a portion of the units for lower-income households for a specified period of time. The rent level restrictions and use restriction period of these properties vary, depending on when they were constructed, and whether other use restrictions apply. Thus, moderate- and low-income tenants may reside in these properties, and the conversion of low-income use restrictions on these properties may affect only a portion of the tenants if a portion of the units already have market-rate rents.

Reliable figures on the portion of the MRB assisted units that are still subject to use restrictions are not currently available. According to the most recent tabulated information (1996), approximately 22,500 units had eligible conversion dates from 1998 until beyond 2010.[6] A large majority of below-market units financed with tax-exempt bonds will convert to market-rateupon expiration of the rent-targeting requirement. Unlike federally-assisted housing, there is no program or agency such as HUD to provide rental assistance vouchers or other transition assistance.

### *Summary of Conversion Risk*

The nature of the risk of conversion of these units to market-rate rents, and the prospective displacement of the low-income tenants, varies significantly. A number of factors affect the conversion risk of individual properties:

- the options afforded by the program(s) under which a property is financed and regulated (e.g., some properties are no longer eligible for assistance);
- the condition of the local rental housing market, including the relationship of the contract rents to local market rents;
- the physical condition of the property and its ability to command higher rents;
- the nature of its ownership and owner motives (for-profit vs. non-profit);
- the financial stability of the property and the ownership entity; and

- whether there is dedicated government assistance available to extend or preserve the property's low-income use restrictions or assist the tenants.

Due to the tight rental markets in many parts of the State, California has had a level of prepayment and conversion among older-assisted HUD properties that is triple the amount of any other State. Between mid-1998 and the year 2000, based on recent conversion activity, it is quite possible nearly 10,000 affordable units could be lost from the existing affordable federally-assisted housing stock, as well as very high proportion of the MRB-assisted units. A short-term forecast of the distribution of such loss of affordability restrictions might include the following:

- an additional quarter of prepayment-eligible older-assisted developments (approximately 4,000 units);

- 20 percent of the Section 8 assisted properties facing contract expiration (approximately 6,000 units); and

- an undetermined portion of the below-market units in tax-exempt bond projects (approximately 9,000 units are estimated to be eligible for conversion 1998-2000).

This affordable housing is generally most at-risk in the State's highest cost rental markets. While the actual number and location of conversions will depend on factors summarized above, the extent of the pending loss of this scarce housing resource would severely aggravate the State's affordable housing needs.

**Endnotes**

[1] Much of the information in this section is from a report prepared by the California Housing Partnership Corporation (CHPC) for the Department of Housing and Community Development, Spring 1998.

[2] The actual number of developments and units is difficult to estimate because the need to reconcile and update different reporting systems, and because some of the programs overlap. In the case of the Section 8-assisted units, for example, some of the properties are covered by multiple contracts, expiring at different times.

[3] This includes only privately-owned housing with project-based subsidies, and excludes the Section 8 certificate and voucher programs, which provide (portable) tenant-based subsidies.

[4] The Farmers Home Administration has been succeeded by Rural Housing Development.

[5] Local governments can also apply to be delegated as PAEs, although as of this writing there are none.

[6] The Use of Housing Revenue Bond Proceeds, California Debt and Investment Advisory Commission, 1997 report for FY 1995-96.