

Housing Programs in Weak Market Neighborhoods

Developing the Right Tools for Urban Revitalization



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Introduction

Since the mid-1990's, housing prices in many Massachusetts communities have risen much faster than incomes and construction costs. In the face of this dramatic price appreciation, most affordable homeownership programs have focused on building and/or rehabilitating housing units to be sold at below-market prices. While this strategy makes sense in many communities, it is not suited to all. Neighborhoods in cities such as Holyoke, Springfield, Fitchburg, Pittsfield, and others grapple with vacant properties, abandoned buildings, aging infrastructure, high crime rates, and concentrated poverty. In these distressed markets, ownership housing cannot be sold at a price sufficient to cover the cost of new construction or rehabilitation.

Currently, most of the state's housing programs are designed to address housing cost inflation in booming markets. This paper argues that strong-market policy tactics can actually be counterproductive in weak-market neighborhoods; these neighborhoods would benefit from appropriate incentives and regulatory flexibility.

The most problematic housing policy instrument for weak-markets is the deed restriction for long-term affordability. Currently, regardless of a neighborhood's economic condition, housing units built or rehabilitated with state subsidies (or state-administered federal subsidies) for sale to owner-occupants must be deed restricted for a period of years, limiting resale to buyers who qualify as low- or moderate-income. Resale prices are also limited to levels affordable to households deemed low- or moderate-income.

Long-term affordability restrictions and income limits make sense in the state's many heated housing markets. In high-cost markets, current policy tools ensure that public funds are appropriately targeted, preventing subsidies from turning into major gifts of equity to only a few lucky families. These policies promote economic diversity by making it possible for lower income people to live in areas that would otherwise be available only to the relatively well-to-do. In such cases, public funds fill the gap between the market price and the price that is affordable to people with low or moderate incomes.

In weak market neighborhoods, on the other hand, the market price for housing is already at or below the "affordable" level. Under these market conditions, the owner of a unit redeveloped with subsidies could not, in the short run, resell the unit for a windfall. Plenty of comparably priced homes may well be available in these neighborhoods. While these "affordably priced" units may be in very poor condition, they are also free of deed restrictions that limit the income of future buyers and that restrict resale prices. The effect of such restrictions is to reduce the attractiveness of new or redeveloped units, and to further concentrate low-income residents in these neighborhoods.

The revival of weak markets—which requires price appreciation and buyers with capital to invest in their properties—should be an important objective for state and local government. Vacant lots and boarded-up buildings harm residents' quality of life, and reduce the value of the entire community. Weak market neighborhoods cost government money due to lost taxes, increased policing needs, and arson and accidental fires. These areas could also relieve inflationary pressures throughout the state if they offered safer, more attractive homebuying options.

Deed restrictions on income eligibility and resale hamper revitalization by discouraging homebuyers in weak markets. These tools might help cool a hot market; we argue that

weak markets should be encouraged to warm up. Restrictions that might make sense in Cambridge should be relaxed for other Massachusetts communities where the market price is already “affordable”. When a market improves and prices rise, public policy could then turn from a revitalization strategy to a housing affordability strategy. More flexible housing policy tools could serve as a kind of thermostat, tailoring the state’s efforts to the climate of each market.

This paper will focus on programs that subsidize the building or rehabilitation of units for owner occupancy, as opposed to the development of rental properties. Most weak market neighborhoods already feature a high proportion of renters and high rates of vacancy. Many one- and two-family homes, once owner-occupied, have become investor-owned, often by default, and have suffered from deferred maintenance and poor property management practices. Increasing homeownership is a broadly shared goal for weak market neighborhoods, and our recommendations support these efforts.

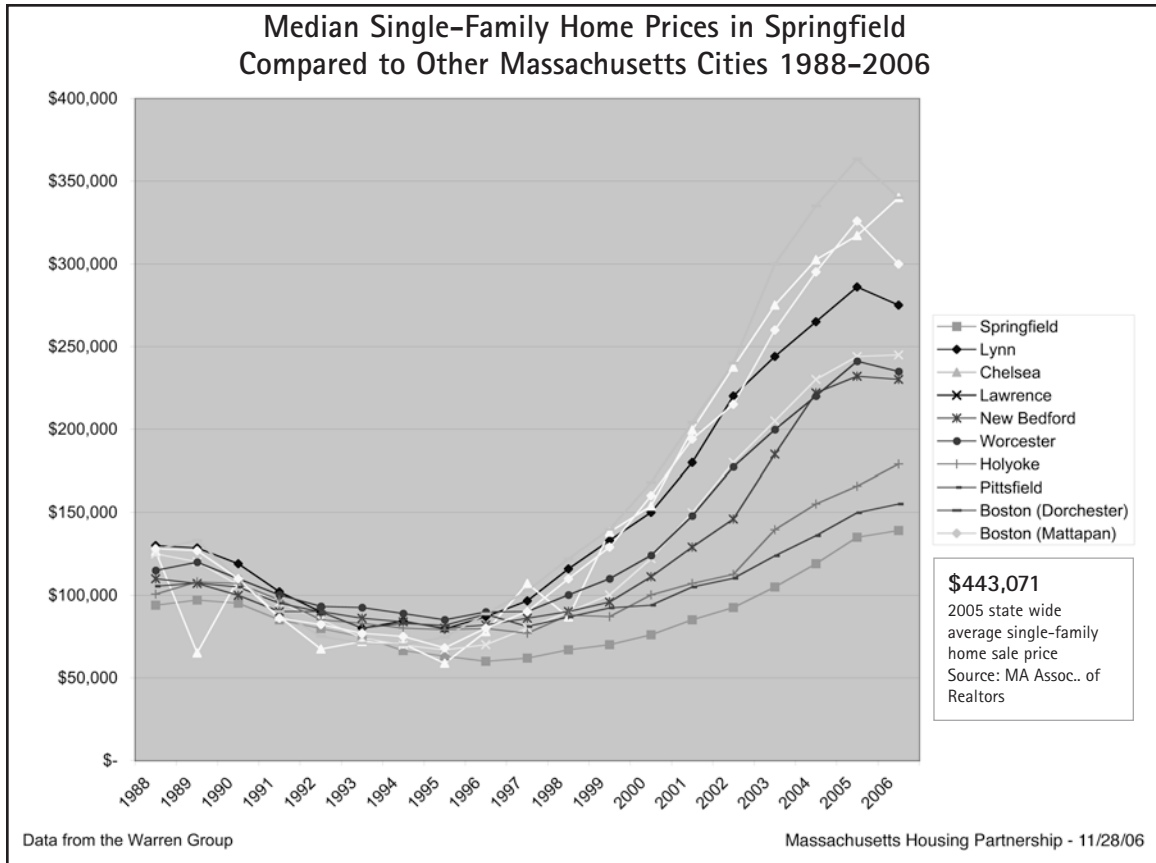
In section two, this paper will define and present examples of weak market neighborhoods; section three argues that revitalization of weak market neighborhoods should be a policy priority for the entire state; sections four and five explore the evolution and impact of housing subsidy programs and deed restrictions; section six outlines the inadequacy of current housing programs for weak markets; and section seven makes detailed policy recommendations to help revive the Commonwealth’s neediest neighborhoods.

Weak market neighborhoods

For the past decade, Massachusetts has experienced a heated housing economy. The average sale price of a single-family home increased from \$177,700 to \$443,071 from 1995 to 2005, according to the Massachusetts Association of Realtors.¹ A 2006 report released by the New England Public Policy Center of the Federal Reserve Bank of Boston finds that the lack of affordable owner-occupied housing is a problem for both middle-income and low-income households across much of New England.² While inflation has been the norm in most communities, there are still neighborhoods, particularly in older cities outside of Route 495, where the market price of housing remains affordable to those with lower-incomes (See chart on page V). Unfortunately, the prices in many of these neighborhoods are held down by concentrated poverty, high crime rates, high vacancy rates, the neglected condition of the housing stock, a pattern of abandoned buildings, and low levels of owner-occupancy.

Old Hill, one of Springfield’s seventeen neighborhoods, is representative of weak market neighborhoods. There are over 130 vacant lots and abandoned buildings in a neighborhood with only 4,700 residents and 1,660 residential units. The number of vacant lots or boarded-up buildings represents nearly 8% of Old Hill’s residential units. A growing number of abandoned properties are now city-owned due to tax delinquencies. Absentee landlords own many of the neighborhood’s residential structures.

In weak market neighborhoods such as Old Hill, rents do not cover the cost of operating an apartment building properly. Return on capital is not sufficient for the owner to justify further investment. Similarly, sale prices of ownership housing can be so low that it is not feasible to build a new home, or substantially renovate an existing structure, even if the site is donated. Data from the Multiple Listing Service shows a total of 22 single-family homes sold in Old Hill in the twelve months ending September, 2006. Sales prices



ranged from \$35,000 to \$159,000, with an average of \$86,400. Only one house sold for more than \$118,000 during this period. The return on investment in such a market is not sufficient to attract private builders and discourages investment in the neighborhood. When the cost of developing a single-family house can exceed \$175,000, but comparable properties are appraised at less than \$118,000, the market will produce no new housing.

Depressed housing values feed a downward spiral in weak market neighborhoods. Buildings are abandoned, fire-damaged structures are torn down and not replaced, and previously owner-occupied units are rented, often in substandard condition and without effective property management. Heirs walk away from properties. Lenders write off mortgages rather than foreclosing and reselling the property. The municipality itself, seeing no value, may choose not to pursue the collection of back taxes. Over time, the failure to collect back taxes means that accumulated taxes and interest on many parcels can greatly exceed their market value, making private transactions impossible. The challenge for Old Hill is to create a functioning market where none currently exists.

Some cities have managed to accomplish this daunting task. Several years ago, Taunton had many boarded-up buildings and vacant parcels. Market prices of real estate were too low to entice development. The city embarked upon a program of rehabilitation of vacant properties, creating affordable homeownership opportunities. Taunton also benefited from its close proximity to commuter rail service and to many major highways. As prices in Greater Boston skyrocketed in the late 90's, Taunton became an attractive alternative for tenants and homebuyers.

Between 1990 and 2000 the number of vacant housing units in Taunton dropped by 569.³ Between the 1990 and 2000 US Census, more than 2,600 new residential units were created – a 13% increase. The number of occupied ownership units increased by 2,611, or 24%, over the same period. Taunton now has an ownership vacancy rate of only .6%.

A local development agency in Taunton recently reported a long list of eligible buyers for four newly-completed affordable homes. The agency's director described the list as "longer than my arm." In this new market, over half of Taunton households could not afford to purchase the median priced single-family home. According to an analysis in 2004, a family at the median income of \$52,433 would qualify to purchase a house worth approximately \$161,196, assuming the then-current rate of 5.63% for a fixed-rate, thirty year mortgage.⁴ The result was an affordability gap of \$85,804 between the mortgage that could be supported at the median family income and the actual median single-family home price of \$247,000. With price escalation since 2004, and an increase in interest rates, there may be an even greater gap today. Clearly, Taunton's is no longer a weak housing market.

While Taunton benefited from its proximity to major commuting routes, public investment in neighborhood revitalization has also played a role. This investment can help set the stage for economic rejuvenation. When the market heats up, public policy should then turn from a revitalization strategy to a housing affordability strategy. One size does not fit all.

Many cities have experienced weak market conditions at various times in their history. Currently, as the graph depicts, markets continue to be weak in many cities outside of the Greater Boston region. While prices have climbed dramatically in Dorchester, Mattapan, Lynn, and Chelsea, prices have barely kept pace with inflation over an 18-year period in Springfield, Holyoke, and Pittsfield. Lawrence and Worcester have seen greater price appreciation, in part due to their proximity to Boston and its suburbs, but many of these cities' neighborhoods have lagged behind the city as a whole.

The importance of revitalizing weak market neighborhoods

Some might argue that governments need not act to revitalize weak market neighborhoods since the state of the market merely reflects a lack of demand. In this view, if people do not want to live in a certain neighborhood, so be it. Yet there are many compelling reasons why state and local government, as well as society as a whole, should have an interest in revitalizing neighborhoods in older cities. First, weak market neighborhoods consume tax dollars from every level of government. Second, they represent a missed opportunity for "smart growth", a framework that channels development into areas where there is existing infrastructure while protecting undeveloped land. Smart growth policies reduce commuting times and encourage use of public transit. Third, residents who can't afford to move out of weak market neighborhoods often find life there to be difficult, if not dangerous.

Weak market neighborhoods strain government budgets in a variety of ways. Local governments lose tax income due to both non-payment and reduced property values. Increased crime strains policing budgets. Arson and accidental fires are a burden on local fire departments. Governments pay for boarding, securing, demolishing or otherwise managing the inventory of abandoned property. Finally, the government also pays for trash clean up when

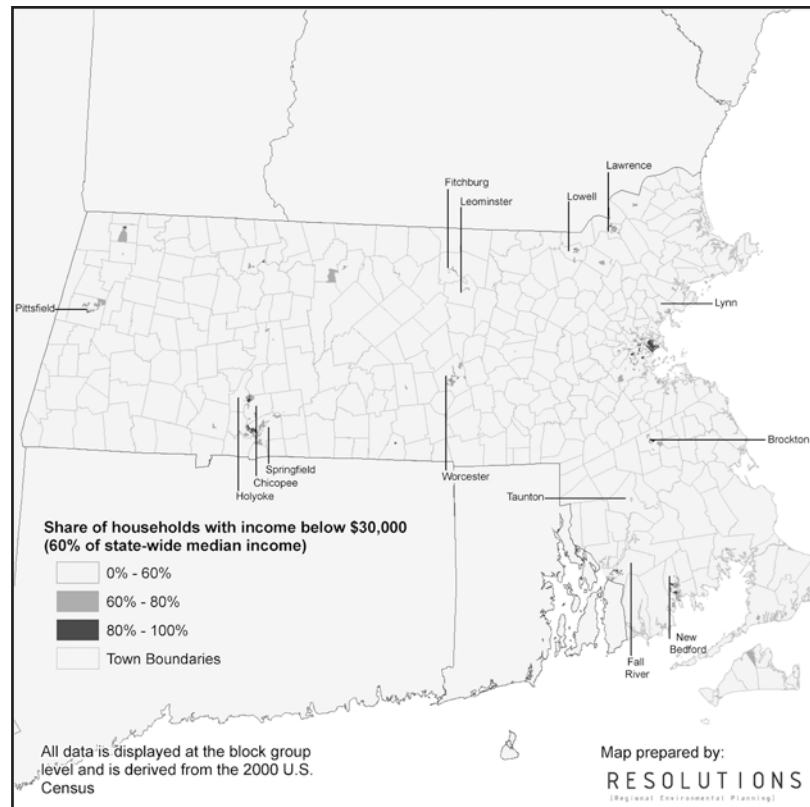
people illegally dump garbage on vacant lots. According to a Springfield official, the City has spent more than \$2 million on demolition in a single year, and spends hundreds of thousands of dollars annually to clean and secure blighted properties.

Massachusetts policy-makers, environmentalists, housing advocates, and business leaders have endorsed the principles of smart growth. Redevelopment of urban neighborhoods enables more people to live in close proximity to work, stores, schools and parks.

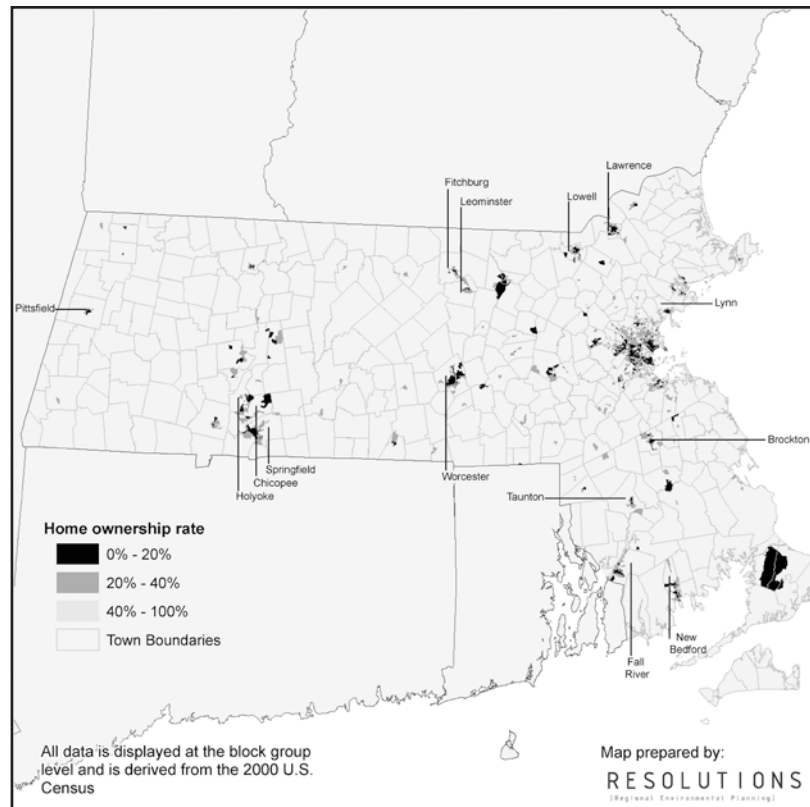
While “greenfield” development requires investment in new roads, sewer extensions, schools and more, such infrastructure already exists in urban areas. There are 65,000 jobs in Springfield; of these, Springfield residents hold only 35,000. Smart-growth public policies would encourage those 30,000 commuters to live closer to work. More of Springfield’s workforce might choose to live there if they could be assured that the neighborhoods are safe, the schools adequate and the housing options attractive.

Revitalization also contributes to the personal safety and financial security of current residents. Vacant buildings and lots are associated with higher rates of crime. Improvements in blighted neighborhoods also help existing homeowners financially. Homeowners in failing neighborhoods suffer from stagnant or declining home values, high property insurance premiums, and difficulty in financing home improvements. According to a 2001 study by the Temple University Center for Public Policy and Eastern Pennsylvania Organizing Project, “Blight Free Philadelphia: A Public-Private Strategy to Create and Enhance Neighborhood Value”, houses located within 150 feet of a vacant or abandoned property lost \$7,627 in value. Within 300-450 feet, properties lost \$3,542 in value. The study found “that all else being equal, houses on blocks with abandonment sold for \$6,715 less than houses on blocks with no abandonment.”

The revitalization of Massachusetts’ cities is not solely of benefit to those cities’ residents. Urban redevelopment is an important public policy task that benefits the governments, businesses, and citizens of the entire Commonwealth. The public policy rationale for government investment is multi-faceted:



- Elimination of vacant lots and boarded up buildings makes neighborhoods safer.
- Restoration of housing values encourages homeowners to buy, sell, refinance and make home improvements.
- Rising property values encourages heirs to not walk away from their inheritance, lenders from their mortgages or the city from back taxes.
- Creation of an attractive alternative to suburban and rural housing options provides more options to live near work and public transit.
- Promotion of economic diversity prevents a disenfranchised concentration of very low-income households with few options.
- Revitalization and investment will actually reduce other burdens on city resources.

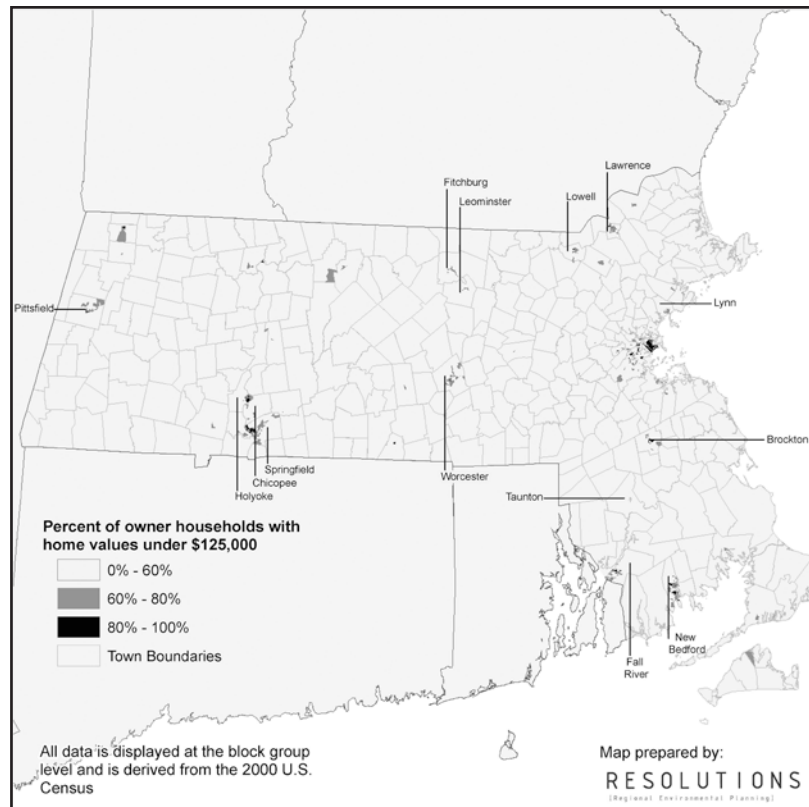


Current housing programs

Development of housing in areas where the attainable sales price will not cover construction costs requires resources to fill the gap. In the affordable housing arena, public resources are often used to make development financially feasible. Four of the most commonly used programs for subsidizing the capital cost of building and rehabilitating housing in Massachusetts are the federal HOME and Community Development Block Grant (CDBG) programs, and the state's Housing Stabilization Fund (HSF) and Affordable Housing Trust Fund (AHTF). Each program carries its own eligibility requirements and its own set of rules to preserve affordability. While the CDBG program was created as a revitalization tool, the other three were designed to increase the production of affordable housing.

When applied to ownership housing, the program restrictions generally consist of income eligibility limits for initial buyers and a specified period of time during which subsequent buyers must also be income-eligible. The federal programs are generally less restrictive and more flexible than the state programs, but communities that administer federal programs often add their own affordability restrictions.

A wide variety of provisions regulates the length of time that an owner-occupied home must remain affordable to income-eligible buyers. The federal HOME program requires that affordability restrictions be in place on subsidized units for 5 to 15 years, depending on the level of the subsidy. CDBG, the oldest of the current federal programs, has no requirements for deed restrictions or duration of affordability. In contrast, the state's Housing Stabilization Fund now requires 50 years of preserved affordability, and the Affordable Housing Trust Fund requires 30 years of affordability.



Each program has income eligibility restrictions. HOME requires that subsidized units be affordable to households earning no more than 80% of area median income (AMI). In theory, the HOME program does not require a mechanism for enforcement, such as a deed restriction, if a market analysis determines that the housing is likely to remain affordable. In practice, administering agencies in Massachusetts have generally opted for a deed restriction of some kind.

CDBG requires that 70% of its funds be targeted to households earning no more than 80% of AMI. Up to 30% of an administering agency's CDBG funds can be used for non-income restricted projects aimed at eliminating blight. In practice, most communities direct funds according to the income eligibility standard. Units subsidized by HSF funds can only be sold to households at 80% of AMI or less, and units subsidized with AHTF can be sold to households at 110% of AMI or less. For ownership housing, the sale of assisted units is also usually limited to households that qualify as first-time buyers.

HOME

The HOME program provides grants to states and local governments to implement local housing strategies that will increase homeownership and affordable housing opportunities for people with low- and very low-incomes. HOME funds can be used for assistance to homebuyers for down payments and closing costs, tenant-based rental assistance, housing rehabilitation, and new construction of housing. Nationally, 40% of HOME funds are allocated to states and the remaining 60% to local governments. In

Massachusetts, cities that have their own HOME allocations must match any state-administered HOME money with their own HOME funds.

HOME requires that subsidized properties remain affordable for specified periods of time based on the size of the grant, ranging from five years for small grants, such as those provided for down payment assistance, to fifteen years for larger grants typically associated with the development of housing. The local jurisdiction can impose longer terms. In practice, the Massachusetts Department of Housing and Community Development (DHCD) requires 30 years of affordability and some municipalities require longer periods, up to perpetuity.

All homeownership units subsidized with HOME funds must be affordable to households at or below 80% of AMI. For rental units, 90% must be affordable to households at or below 60% of AMI, and in projects of five or more units, 20% must be for households at or below 50% of AMI. The other 10% of rental units must be affordable for households under 80% of AMI.

Affordability must be enforced by some sort of mechanism such as a deed restriction, unless a market analysis documents that market conditions in the neighborhood are such that the housing is unlikely to become unaffordable to low income homebuyers. In practice, very few if any jurisdictions in Massachusetts have asserted and documented that the market conditions meet this requirement. Local participating jurisdictions may tighten eligibility requirements, but cannot set them below minimums required by statute.

CDBG

The federal Community Development Block Grant program provides annual grants on a formula basis for qualifying communities to carry out a wide range of community development activities. Communities develop their own programs. States receive grants to directly administer the program on behalf of communities that are deemed too small to qualify for their own direct allocation. All CDBG activities must meet one of the following national objectives: benefit low- and moderate-income persons; aid in the prevention or elimination of slums and blight; or meet certain community development needs. Funds can be used to acquire properties, rehabilitate residential and non-residential properties, provide public facilities and infrastructure, and assist homeowners or businesses.

While the CDBG statute requires that 70% of its funds be spent on projects that benefit households making 80% or less of AMI, the statute and regulations do not require any kind of deed restriction or enforcement mechanism on subsidized housing and therefore have no requirements for duration of restriction. While it is not required by statute, communities may choose to impose policies to restrict affordability for several years or even in perpetuity. The remaining 30% of CDBG funds can be used for projects that prevent or eliminate slums or blight or meet community development needs of special urgency.

Housing Stabilization Fund

In 2006, the Massachusetts legislature authorized the state to bond for \$29 million designated for the Housing Stabilization Fund. HSF can assist both rental and ownership developments. HSF-assisted ownership units are sold to income-eligible first-time homebuyers. The program currently requires that subsidized homeownership units come

with a deed rider restricting the use and subsequent resale of the unit for a period of at least 50 years. HSF-assisted rental units must also remain affordable for 50 years. With each successive bond issue, the legislature has increased the required period of years during which the property must remain affordable. Originally, the term was set at 20 years, but was increased to 40 years in the third bond issue and to 50 years in the current version of the program. All HSF-assisted rental units in homeownership properties must be affordable to people below 80% of area median income at the time of initial occupancy. The property must serve as the purchaser’s primary residence for the duration of the restriction.

Affordable Housing Trust Fund

The state Affordable Housing Trust Fund was created in 2000. It was intended that the program be funded at \$20,000,000 per year from appropriations. Subsequently, the legislature authorized \$70,000,000 in bond funding for the program. The fund is intended to provide resources to create or preserve affordable housing. For ownership housing, the program may assist households with incomes that do not exceed 110% of AMI. The minimum period of affordability for projects receiving AHTF funding is 30 years. The Affordable Housing Trust Fund is sited within the state’s Department of Housing and Community Development (DHCD) and is managed by the Massachusetts Housing Finance Agency (MassHousing) with guidance from a 15-member Advisory Committee comprised of local officials, housing advocates, lenders and developers.

Chart of programs – requirements for ownership units

| Program | Term Housing unit must remain affordable for x number of years | | | Affordability Participants must earn no more than xx% of Area Median Income | | |
|---------------------------|---|---|---|---|--|-------------------|
| | Statue | Regs | Policy | Statue | Regs | Policy |
| HOME (federal) | 15 years (if more than \$40K per unit. Could be as short as five years for smaller grants.) | | DHCD policy is 30 years - municipality can elect longer terms | 80% | | |
| CDBG (federal) | 0 | 0 | Up to 99 years | 80% | 80% | |
| HSF IV (state) | 40 years | Additional 10 year restriction after first 40 years | | 80% | 100% during additional 10 year period for rental | |
| AHTF (state) | 30 years | | | 110% | | 80% in many areas |

Types of resale formulas

A variety of formulas is used to calculate allowable resale prices of ownership units that are under long-term affordability restrictions. The formulas, like the restrictions, have been developed since the mid-1980s. Before then, most restrictions were intended only to prevent short-term speculation, rather than to ensure continued affordability over time. Often, these provisions, common in CDBG-funded work, were limited to five years.

We can use the case of a deed restricted affordable house in Springfield to illustrate how the resale formulas produce widely varying returns in outcome. In one particular project, \$115,612 in public subsidies was invested in the restoration of a two-family house in 2001. At the time of sale, the two-family home was appraised at \$77,000, although true comparable sales were difficult to find. The house was sold for that price, with affordability deed restrictions, in August 2001.

In early 2006, the family that had purchased the house needed to sell it or face foreclosure. In the five years since the purchase, the market had changed. In this particular neighborhood, the elimination of blight had been accomplished through the use of both public investment and privately donated labor and materials. Following the rehabilitation of several one- and two-family houses on a parallel block, construction of two new single family homes by Habitat for Humanity around the corner, and a major rental development that removed a substantial area of blight a few blocks away, market prices in the neighborhood began to rise. The neighborhood also benefited from a gradual citywide price appreciation after many years of stagnation. As a consequence of the changes, the two-family house was appraised in 2006 for \$180,000. (Some of the comparable prices used to determine this value likely came from other neighborhoods).

If the house had not appreciated during the time period, the family would have realized no return at all upon the sale of the house. Given that there was substantial appreciation, the resale value was limited below the market price by the deed rider's resale formula. If there had been no deed restriction on this property, the sellers could have realized a return of \$103,300 had they found a willing buyer. Under the terms of the deed rider, the family was entitled to walk away with \$7,036 including their initial down payment of \$2,310, their principal payments of \$3,456, and a calculation of return on equity (defined as down-payment plus one half of the their principal payments) based on the consumer price index.

DHCD recently implemented a new deed rider. If calculations had been made according to the new formula, the family would have been entitled to their initial down payment, their principal payments, and a calculation of return on equity, based on the purchase price of the house. Under the new rules, the same family could have realized \$13,564 from sale, perhaps enough to make a down payment on another house.

A third formula, used by a local community land trust, would have allowed them to keep \$23,956. In the land trust formula, the resale price is calculated by applying the percentage increase in the Area Median Income to the original purchase price. With this formula, the increase in sales price is directly proportional to the increase in the income eligibility limit.

The application of yet another typical land trust formula would have yielded \$31,517. In this fourth model, essentially an equity sharing provision, the seller's proceeds includes

the value of their down payment plus the total of their principal payments plus 25% of the value of the actual appreciation in the market.

In any of these instances, the family's returns would have been far less than the \$103,000 return that an unsubsidized owner might have realized from the same transactions.

The evolution of government assistance to homebuyers

The government's role in housing and community development has evolved over the past 70 years. During that period of time, there have been at least three major public policy goals addressed by a variety of programs and initiatives advanced by federal and state government. Throughout this history, homeownership has been promoted as a vehicle to stabilize communities and build family wealth; some would argue that this is the genius of the American economic system, the genesis of a large middle class and today's suburban America. Another common policy theme has been the revitalization of distressed urban neighborhoods, sometimes expressed as "the elimination of slums and blight." Finally, another set of programs promulgated over that period of time was created to provide affordable housing for families who could not afford what the market was able to produce.

Early programs focused on the production of rental units. Public efforts to promote homeownership began with the Housing Act of 1934, which, among other efforts, established the Federal Housing Administration. The introduction of mortgage insurance encouraged lenders to make mortgage loans with higher loan-to-value ratios and longer terms, helping to secure financing for a new class of homebuyers.

To address the needs of people living in urban slums or rural poverty, the federal government next moved to create public housing, generating thousands of apartments owned and managed by local housing authorities. The objective was to create decent, affordable units as an alternative to the crowded, substandard rental housing associated with troubled neighborhoods.

With the problem of urban slums and blight still unresolved, the 1949 creation of urban renewal programs focused on tearing down and rebuilding whole neighborhoods. This approach did not place a high priority on affordability, as many urban renewal areas became upscale housing, offices, or commercial developments.

In the 1960s, the federal government created programs designed to stimulate the production of privately owned housing for people of low- and moderate-incomes. This was seen as an alternative to long-term public housing tenancy as well as an opportunity to harness the productivity of the private real estate development and building industries.

In the 1970s, the Section 8 housing assistance payments program was created to allow people of low and moderate incomes to move to higher-priced neighborhoods and communities. It was intended as a clear alternative to both public housing and to large, privately developed housing projects. In addition to creating expanded housing opportunities by improving access to privately owned market-rate rental housing, the program hoped to bring about a "deconcentration" of very poor people. The 1970's also saw the creation of the "block grant" program, which allowed cities to chart their own renewal strategies. The Community Development Block Grant program embraced the twin goals of assisting people of low and moderate incomes and eliminating slums and blight.

The 1980s and 1990s saw housing programs tighten their focus on helping the poorest of the poor. The Section 8 program re-trenched. Having once served people with incomes up to 80% of AMI, the program was revised to give preference to households below 30% of AMI. The Low Income Housing Tax Credit program and the HOME program focused their rental programs on households below 60% of AMI while HOME's homeownership assistance was limited to households below 80% of AMI. While it may have been logical to target an increasingly scarce resource to the poorest of the poor, this targeting has been a hindrance to community revitalization. The consequence, intended or unintended, is to further concentrate the poorest people in blighted areas.

In 1986, Massachusetts created the Homeownership Opportunity Program, which included efforts to design deed restrictions to limit future sales prices over the long term. Properties funded under this program continue to come up for re-sale, often with unanticipated results arising from the application of the original formula.

Since the inception of the HOME program, many municipalities have created their own deed restrictions, while others have used the state's prescribed deed restrictions. State deed restrictions have gone through many revisions over the past 15 years with both minor and major modifications. The addition of the state-funded Housing Stabilization Fund and the Affordable Housing Trust Funds has resulted in further variations.

In addition, the state has seen affordable ownership housing developed in high-end markets that rely on internal price-skewing rather than actual public subsidies. In these projects, the developer often is able to use a "density bonus" under the Chapter 40B "comprehensive permit" process to create enough additional units to allow 25% of the units to be priced as affordable. More recently, thousands of affordable units have been created through the New England Fund program, while others have been built under the Local Initiatives Program (LIP). Each of these has utilized a variety of resale formulas.

In response to the problem of concentrated poverty, HUD's HOPE VI program was initiated in 1993. HOPE VI's aim is to "break the monoculture" of traditional public housing projects by replacing them with mixed-use development and mixed-income housing. By encouraging private capital to help build HOPE VI housing, HUD argues that federal money can act as a powerful lever for inner city reinvestment. According to HUD data presented by the Ash Institute at Harvard University, \$4 billion in federal money has attracted \$6.7 billion in private investment.⁵ Other housing programs could be leveraged in a similar fashion to encourage diversity and investment in old urban neighborhoods.

While the history of state and federal housing initiatives in the homeownership arena has included three public policy goals — building family wealth, revitalizing neighborhoods, and creating and preserving affordable housing — the implementation of these programs today has come to focus primarily upon affordability. Over time, we have begun to achieve greater participation in the "American Dream" of homeownership. An ironic consequence of this, however, is that many of the products that make homeownership possible also restrict the opportunity to build wealth and to follow previous generations on the path to the middle class. Efforts to revitalize long-neglected neighborhoods, many occupied by African American and Latino families, are hampered by disincentives inherent in deed restrictions. These restrictions are appropriate to affordability goals but counterproductive to revitalization.

The burden of deed restrictions on weak-market neighborhoods

As a matter of public policy, government should not promote gentrification that would force people out of their homes, nor should it aim to build enclaves of only the poorest of the poor. Unfortunately, government has tended to advance policies that have the effect of segregating people in neighborhoods according to income. Programs that build income-restricted housing in blighted areas have the effect of further concentrating poor people. In addition, local zoning policy often works to effectively exclude the poor or near-poor from many neighborhoods.

Neal McBride, the founding Executive Director of Springfield Neighborhood Housing Services, and subsequently a Vice President for community development with Fleet Bank for more than 15 years, commented that many efforts to revitalize downtowns and neighborhoods have contributed to the concentration of people living in poverty: “These high density pockets of poverty were not just the result of market forces or normal patterns of urban social evolution, but rather [the result of] well-intended but conceptually-truncated social policy.” He argues that the current tools for revitalization are overly simplistic and narrowly focused.

The challenge when revitalizing a weak market is to attract new people to the neighborhood, while giving current residents reason to stay. Existing homeowners should be encouraged to restore value to their properties, which means they should be able to profit from reinvestment – even if that investment includes some public money. Even with such improvements, attracting new people to the neighborhood is essential to the market’s revival. These new buyers are pioneers. They buy in the hope that public safety and schools will improve. They may ignore gunshots near their house during the day or night and look the other way when their children see a hypodermic needle or a used condom lying on the ground in the nearby park. The buyers are placing their life savings at risk to make a down payment on a house that might not even be worth its purchase price when the time comes to sell. Government policy should encourage these pioneers by allowing them to realize benefits commensurate with their risk.

These buyers also still face typical real estate risks. The house might need substantial repairs; taxes, insurance or utilities may increase costs beyond the point the buyer can afford to pay; the buyer might lose his or her job and be unable to pay the mortgage; the buyer might be subject to foreclosure and lose his/her credit standing; or the real estate market could decline, making it impossible to sell or refinance. For buyers to take these risks, they should be allowed to realize appreciation in the value of their home if the neighborhood improves.

Under the current regime of deed restrictions, buyers may not profit from the rising values that they help to stimulate. The city benefits. Their neighbors benefit. Financial institutions benefit. Fairness and equity require some consideration for these pioneers. Plain marketing savvy would argue that we need incentives, not obstacles, to attract potential homebuyers. Limiting sales to those who are both first time buyers and income-eligible serves to disqualify the potential buyers that an area needs most.

Community response to deed restrictions

As deed restrictions have become embedded in state housing programs, there is evidence that these restrictions have discouraged many potential homebuyers. Before the advent of

today's 30-year, 50-year, and perpetual deed restrictions, it was common for restrictions to decline proportionately annually to zero over a 5-15 year period, at which point the owner was entitled to the full proceeds at resale. A director of a non-profit dedicated to community redevelopment in one of Massachusetts' cities commented: "We were comfortable with having these units heavily restricted... during the first five years, and then [reducing restrictions] during years 6-15... With...restrictions of 30 years, we feel like these projects start to be more like long-term rental projects than homeownership, insofar as the owners will not be able to use the asset...to leverage other important assets, most notably college education for their children and retirement for themselves. They do have the benefit of secure, low-cost, healthy homes, but not the other benefits of homeownership."

The City of Fitchburg often chooses not to use state funding to subsidize ownership units because of the extended affordability terms and restrictions on equity. Instead, it relies on its own allocation of federal HOME and CDBG funds to support owner-occupied housing in targeted locations. The City imposes only the minimum level of restrictions required by the federal programs. "We do not want to segregate low income populations in our older neighborhoods," explains Larry Casassa, Deputy Planning Coordinator for Fitchburg.

In Lawrence, prices have been increasing in recent years. The director of a local community development organization reports that two family homes that sold at a market price of \$110,000 in 2000 are now selling for as much as \$300,000. Despite the fact that affordability is becoming an increasing problem for the city's low-income residents, the director reported that people are discouraged from applying by the restrictions on affordable units. "Demand is quite high for affordable units. We...always have enough demand for lotteries for our homeownership units. However, in our most recent lottery [in early 2006], we had a much smaller number of potential buyers—about 4 buyers for each home v. 10 buyers for each home a few years ago. We know from our marketing that the increased severity of the deed restrictions discouraged many families from applying."

Bob Landry, Director of the Fall River Affordable Housing Committee, explained that from the 1980s through the mid 1990s, Fall River had many boarded up and abandoned buildings. In those years, public programs for rehabilitating housing came with few affordability restrictions. Early deed restrictions typically had a term of five years and were intended primarily to prevent or delay speculation. Landry commented that the City would have not had the same interest in the housing if they had been required to place 30-year affordability restrictions on the rehabilitated units. Today, prices in Fall River have increased and there is much more demand for affordable units.

Local officials and affordable housing developers have also observed that some buyers may not fully understand the implications of the deed rider that they are required to sign. A family's strong desire to realize the dream of owning their own home can outweigh normal caution and judgment. There is a clear body of information indicating that some families are so desperate to own a house that they agree to predatory mortgage products and risk severe financial hardship. In the excitement of buying a first home, it is similarly easy for a buyer to accept a deed restriction without fully understanding the consequences. It is likely that eager first-time buyers are as susceptible to misunderstanding the deed restrictions as they are to failing to understand the details of a predatory mortgage.

While this risk is mitigated by homeownership education and counseling, it remains a concern of practitioners.

When buyers do understand the restrictions, they may be discouraged from purchasing a deed-restricted house. Several community development professionals have reported that prospective buyers have backed out of purchase agreements once they understood the restrictions. Some avoid resale restrictions by purchasing dilapidated properties that they can't afford to renovate. This encourages the further decline of the neighborhood and demonstrates the unintended consequences of misapplied policy tools

Recommendations

The Massachusetts legislature and the Department of Housing and Community Development should recognize that existing state housing programs do not adequately address the public policy goal of revitalizing weak market neighborhoods. Current state-administered programs are designed to create or preserve affordable housing in the state's expensive housing markets.

1. The state should modify requirements regarding the term, target populations and resale formulae that accompany funds for building or rehabilitating housing in weak market neighborhoods.
 - a. The state legislature should amend the statutory requirements for the Housing Stabilization Fund and the Affordable Housing Trust Fund such that housing built or rehabilitated in weak market neighborhoods with these funds do not have the same long-term affordability requirements as housing built or rehabilitated elsewhere in the state. In weak market neighborhoods, it should be possible to either waive the requirements for long-term affordability restrictions or to modify them so (1) the term of the restriction is limited to five years; (2) people earning more than 80% of area median income can buy the subsidized units; and/or (3) homebuyers of the subsidized units can accumulate equity in the property.
 - b. DHCD should amend regulations and change policies that exceed statutory affordability terms to ensure greater flexibility in the restrictions on units in weak market neighborhoods. The applicant for the funds, with approval of the administering agency, should determine the appropriate level of restriction, including the period of years and the re-sale formula.
 - c. The state should also make an effort to seek waivers from federal affordability restrictions to complement its efforts in this regard and should not impose restrictions in excess of that required under federal statute and regulation.
2. Applicants (localities and local housing agencies) looking for a waiver or modification of affordability restrictions would have to demonstrate that the given project is in a qualifying weak market neighborhood by meeting at least three of the following criteria:
 - a. More than 5% of units or parcels in a neighborhood are vacant as a result of demolition, or contain a vacant, abandoned building.
 - b. More than 30% of units in the neighborhood are already under long-term deed

- restrictions for affordability.
- c. The median household income in the neighborhood is below 50% of the Area Median Income.
 - d. Comparable sales prices for single-family homes or condominiums in the target neighborhood are less than 120% of the price that would be affordable to a buyer at 80% of Area Median Income, calculated on the basis of conventional underwriting standards at the 30 year, fixed interest rate.
 - e. Comparable sales prices for single-family homes or condominiums in the target neighborhood are less than the cost of construction plus land for a new unit of comparable size.
 - f. More than 5% of the properties in the neighborhood have been delinquent on their taxes for more than one year.
 - g. The number of sales of one and two family homes in the past twelve months, other than through foreclosure, is less than 5% of the existing units.
3. DHCD should simplify the resale restrictions to be better understood by homebuyers and housing professionals alike. Again, in doing so, the Department should design resale formulae that would allow homebuyers in weak market neighborhoods to accumulate equity.

Endnotes

1. <http://www.marealtor.com/content/upload/AssetMgmt/Documents/Member%20Resources/Research/SingleFamilyAvgPrices.pdf>
2. "The Lack of Affordable Housing in New England: How Big a Problem? Why Is It Growing? What are We Doing About It?" by Alicia Sasser, Bo Zhao, and Darcy Rollins, New England Public Policy Center at the Federal Reserve Bank of Boston. 2006.
3. Taunton Housing Needs Analysis June 2004 by Southeastern Regional Planning & Economic Development District, <http://www.srpedd.org/tauntonhousingna.pdf>
4. Taunton Housing Needs Analysis June 2004, p. 13
5. (<http://www.hinstitute.harvard.edu/Ash/hopevi.htm>)



Peter A. Gagliardi has been the Executive Director of HAP, Inc., a regional housing partnership serving the 43 cities and towns in Hampden and Hampshire counties, since 1991. Mr. Gagliardi is a past president of both the Massachusetts Non-Profit Housing Association and Citizens Housing & Planning Association; he continues to serve on both boards. In addition he currently serves on the Board of Directors of the Housing Partnership Network, National Rural Housing Coalition, and Western Massachusetts Enterprise Fund. He also serves as a member of the Community Development Advisory Committee of the Federal Reserve Bank of Boston, the City of Springfield's Community Advisory Committee, and the Steering Committee of the Human Service Forum, based in Springfield. Prior to coming to HAP, Mr. Gagliardi served as Director of Private Housing for the

Massachusetts Executive Office of Communities and Development and Director of Field Operations for the Massachusetts Housing Partnership. He also served as Associate Executive Director of Rural Housing Improvement, Inc. in Winchendon, MA from 1973 – 1986. Mr. Gagliardi holds a degree in Government from Harvard University and teacher certification from Fitchburg State College. He did graduate work in Politics at Brandeis University.

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