IDENTIFYING AFFORDABLE QUALITY HOUSING COMPONENTS FOR DEVELOPING A SMART GROWTH MODEL

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IDENTIFYING AFFORDABLE QUALITY HOUSING COMPONENTS FOR DEVELOPING A SMART GROWTH MODEL

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ABSTRACT

Smart growth development entails retracting the city, hence attempting to house low-income residents at new affordable housing facilities within a metropolitan area. Instead, the dense living conditions would cause the land price to surge due to the scarcity of available land. In such situation, housing developers would be more burdened by high land costs, and low-income families have no alternatives other than paying higher rental prices to building owners. This paper introduces the Low Income Housing Tax credit (LIHTC) as an alternative funding source for developing affordable housing projects. It has successfully enable smart growth development in high-density cities such as in the San Francisco Bay. In this article, we present the affordable housing and smart growth elements in two selected tax credit programs in the United States. We compared these elements with the Malaysian commitments in Agenda 21 and recommend how we could move forward in utilizing these elements to develop the Malaysian LIHTC point system that supports both affordable housing and smart growth requirements. We present the nine affordable housing and eleven smart growth elements that the proposed Malaysian LIHTC supports, and the additional elements that Malaysia has committed to fulfill its Agenda 21 the selected tax credit programs do not have. The proposed Malaysian LIHTC is limited to developing affordable housing in the urban areas, and more studies are required to develop detailed mechanisms of the financing programs. It is our hope that the model will become an alternative solution for housing developers in Malaysia who cannot rely on government subsidies to develop affordable quality housings for the growing nation.

Key words: Smart Growth, Affordable Quality Housing, Low Income Housing Tax Credit

INTRODUCTION

Many low-income people are trapped into paying high rental for low quality housing. It would even be farfetched for them to save enough to make any down payments on a home. With the need to house 709,400 units where 38.2% is for low- and low-medium houses in the Ninth Malaysian Plan (9MP), the growing and shifting population is creating demands for new housing in some areas while decreasing demands for new and existing housing in another. The state of Selangor and Kuala Lumpur require 23.7% of new housing units to cater to its growing population in the 9MP. Inflation and other factors have brought about a dramatic increase in the cost of new and existing housing. In addition, the trend for consumer awareness is reflected in housing alternatives, and improved construction method and materials. The need to provide affordable housing to people in growing metropolitan areas had long prompted the American public to develop alternative housing programs that are not degrading to the population in need. Hence, the birth of the Low Income Housing Tax Credit [1], Section 42 (1986) of the Code in the USA. It requires each state to prepare a Qualified Allocation Plan to determine housing priorities and to give preference to projects serving the lowest income tenants and projects obligated to serve qualified tenants for the longest periods. In this article, we review two programs, namely the Washington State Housing Finance Commission and California Tax Credit Allocation Committee. Both must incorporate selection criteria, which includes project location, housing need characteristics, sponsor characteristics, and tenant populations with special housing needs. With reference to the Malaysian Ninth Plan and Malaysian Vision 2020, we hope that any alternative Low Income Housing Tax Credit for Malaysia would also entail smart growth development. The purposes of using the Malaysian LIHTC are providing safe, affordable shelter of high quality to those in need; establishing stability and opportunity in the lives of residents; and fostering communities that allow people from all ethnic, social and economic backgrounds to live in dignity, harmony and mutual respect. Based on the two programs, we initiated an analysis towards developing critical elements for supporting a smart growth LIHTC program in Malaysia.

Smart growth development entails retracting the city, hence attempting to house low-income residents at new affordable housing facilities within a metropolitan area. On contrary, the dense living conditions would
cause the land price to surge upward due to the scarcity of available land. In USA, when the monthly carrying cost of housing exceeds 30-35% of a household income, housing is then considered unaffordable for that household [2]. For homeowners, an affordable mortgage payment is defined as 25 percent of household income, which allows 5 percent of income for other costs such as taxes, insurance, utilities and maintenance [1]. The American Planning Association (APA) outlines smart growth as a new method of metropolitan development leading to more compact regions, i.e., offering an alternative to sprawl [2]. Given that housing comprises a major share of the built environment, policies that promote denser residential development form a key component of smart growth. Although some of these policies may require new mechanisms, it provides long-term savings by eliminating inefficiencies caused by inconsistent and uncoordinated planning. There is growing awareness, too, that poorly planned development is a hidden tax on citizens and communities alike [3]. Danielson (1999) highlights about the different benefits that may result from housing developed at greater densities compared to subdivisions of single-family homes on large lots. Among them are financial savings on infrastructure such as water, roads, and utilities (Altshuler 1977; Burchell 1997b; Burchell et al. 1992; Frank 1989; Real Estate Research Corporation 1974a, 1974b; Windsor 1979); financial savings on schools due to economies of scale (Ladd 1992); financial savings on municipal and other service delivery (Altshuler and Gomez-Ibanez 1993); financial savings on land costs per dwelling unit (Burchell et al. 1992); and lower land consumption (Burchell et al. 1992; Landis 1995).

Smart growth also means investing in time, attention, and resources in restoring community and vitality to existing cities and older suburbs. Smart growth in new developments is more towns-centered, is auto-accessible but also accommodates transit and pedestrian activity, and has a greater mix of housing, commercial and retail uses. It also preserves open space and protects sensitive areas such as wetlands. Smart growth recognizes connections between development and quality of life. Smart growth advocates argue that, if done right, building more compact regions should not conflict with economic development (Ewing 1997). Perhaps the greatest challenge smart growth faces is community resistance to new development in already built-up areas. Enacting smart growth on a regional scale means that many existing lower density neighborhoods will receive new higher density housing. Suburbanites have a long history of resisting higher density housing for fear of what it might do to property values, and who may reside in such housing [5]. White suburbanites, in particular, associate higher density affordable housing with neighborhood racial succession (Black 1998; Downs 1994; Haar 1996). No matter how much current politics oppose sprawl, policies adding higher density housing to most neighborhoods remain a tough sell. The choices have always been between having higher density or going for sprawl [7].

The Low-Income Housing Tax Credit (LIHTC) has been the major federal program for producing affordable rental housing since its creation as part of the Tax Reform Act of 1986 (TRA). The LIHTC represents a partnership among a variety of public and private sector actors. The basic premise of the LIHTC is to offer federal tax credits to private investors in return for their providing equity for the development of affordable rental housing. The intent of the program is to provide enough incentives to ensure that there will be an adequate supply of low-income housing [8] by granting tax credits to the owners of selected rental housing developed for occupancy by low- or moderate-income households. The program is administered by the state (or, in a few cases, the local authority) housing policy makers who set goals for the program, review projects proposed by for-profit and nonprofit developers, monitor the reasonableness of project costs, and take responsibility for ensuring that projects stay in compliance and that approved projects receive only the tax credits necessary to make the project work. The Internal Revenue Service (IRS) is responsible for monitoring compliance and state performance [9]. The program has been viewed as both a success and a failure. It has been a success in that it has generated many rental-housing units that are now occupied by low- and moderate-income households. Although estimates vary, the program has contributed to the rehabilitation or construction of somewhere between 500,000 and 900,000 units [10]. This success has been attributed to the program’s flexibility. Units have been built across the country, in a variety of markets and serving a broad range of housing needs [11]. The tax credit program appears to have been absorbed into the rental housing development process, but market rate housing developers have not adopted it. Rather, it has been adopted by either nonprofit Community Development Corporations (CDC) or by specialized developers building projects entirely dedicated to low- or moderate-income occupancy. The units are going into largely metropolitan markets containing heavy concentrations of poor, minority households but rents are being charged that make the units affordable to only those poor households with the highest incomes in these areas [8].

This research provides an analytic review of the ways affordable housing can be used to support successful smart growth policies by using low-income housing tax credit. We compare two-tax credit point system in the United States (i.e., Washington State Housing Financing Committee and California Tax Credit Allocation Committee) and recommend key elements that we think Malaysia could benefit if incorporated. The main objective is identifying key criteria for developing the Malaysian LIHTC allocation that motivate housing developers to build more affordable housing development, ensuring dignified inclusion of tenants to such housing programs, and encouraging authorities to protect and preserve these kinds of products.
RESEARCH METHODOLOGY

The LIHTC provides favorable tax benefits as an incentive to invest in affordable housing. In most cases, the LIHTC investors are corporations rather than individual investors, as tax law in the US (since 1992) is more favorable to corporations than to individual investors (corporations can use passive losses (i.e., the investor is not directly involved in the business, he is a passive, versus active investor) against other income while individual investors cannot)[13]. In addition, the Qualified Allocation Plan must incorporate selection criteria, which includes project location, housing need characteristics, sponsor characteristics, and tenant populations with special housing needs. The Commission's Qualified Allocation Plan is included as part of this Application Package. California Tax Credit Allocation Committee’s “point system application LIHTC 2007 form” and Washington State Housing Finance Commission’s “point system application LIHTC 2007 form” are our case studies. Therefore, we hypothesize that we could extract the affordable housing and smart growth elements, which are embedded within the “Point System” for ranking and scoring of the Malaysian LIHTC. We then compare the affordable housing and smart growth elements in both programs before recommending key elements for smart growth principles within affordable housing requirements to be applied in the Malaysian context.

LIHTC POINT SYSTEM FOR RANKING AND SCORING APPLICATIONS

The United States’ housing authorities receive far more applications for tax credit than it can award. For that reason, in 1999, the United States implemented a point system by which to rank applications. The housing development applicant is responsible for demonstrating that the project qualifies for all selected Allocation Criteria and ensuring that all appropriate attachments are submitted. The Tax Credit Director will determine if a project qualifies to receive Allocation Criteria Points [12]. Although it is somewhat complicated by the overlay of statutory set-asides and geographical apportionments, the basic point structure advantages applications that show evidence of leveraging public and some private funds, projects for which the owner and management company have previous affordable housing experience, projects that have location amenities (for example, being located by a public transit stop), projects that will offer tenants various service amenities (for example, after school computer classes), projects serving the lowest income tenants, “mixed income” projects that have a non-tax credit component of renters, projects that are ready to proceed, projects that attain energy efficiencies, and projects that contribute to neighborhood revitalization.

CALIFORNIA TAX CREDIT ALLOCATION COMMITTEE (CALIFORNIA TCAC)

The “point system application LIHTC 2007 form” under the California TCAC program has 6 articles [14] with total possible points of 124. Refer to Table 1 on the allocation criteria listed below:

1. General Partner/Management Company Characteristics (maximum 9 points)
   (A) General Partner experience
   (B) Management Company experience
2. Housing Needs (maximum 10 points)
   Large Family Projects or Single Room Occupancy Projects or Special Needs Projects or Seniors Projects or At-Risk Projects
3. Amenities (A-Site) (maximum 15 points)
   Being part of a transit-oriented development strategy, public park, public library, full-scale grocery store/supermarket, for a large family development, for a senior development, for a special needs or SRO development, medical clinic or hospital, pharmacy.
   Amenities (B-Service) (maximum 10 points)
   High speed Internet service, after school programs of an ongoing nature for school age children, educational classes such as ESL, computer training, etc, Licensed child care providing 20 hours or more per week, Contracts for services.
4. Sustainable building methods (maximum 10 points)
   Attention to Title 24 energy, water-saving fixtures, one high efficiency toilet, use of fluorescent light fixtures, etc.
5. Lowest Income (maximum 52 points)
   In accordance with the table in appendix.
6. Readiness to Proceed (maximum 20 points)
WASHINGTON STATE HOUSING FINANCE COMMISSION (WASHINGTON SHFC)

The “point system application LIHTC 2007 form” under the Washington SHFC program has 20 articles [15] that a developer can earn maximum 277 points. Refer to Table 1 on the allocation criteria listed below:

1. **Additional low-income housing set-aside.** Points will be awarded to Projects based on the Applicant’s Commitment to provide selected percentages of the Total Low Income Units for occupancy by households at or below selected Area Median Gross Income levels (Maximum 50 points).

2. **Additional low-income housing use period.** Two points will be awarded (up to a maximum of 44 points) for every year of the Additional Low-Income Housing Use Period, up to 22 years (Maximum 44 points).

3. **Housing needs.** Points will be awarded based on the county in which the project is located. These points are not cumulative. If a Project is located in more than one county, the Project will be awarded points equal to the points applicable to the county that offers the least number of points (Maximum 10 points).

4. **Nonprofit sponsor.** In order to be considered for the Nonprofit Sponsor points (Maximum 5 points).

5. **Farm worker housing.** The applicant makes a commitment to provide X% of the Total Housing Units in the Project as low-income housing units for farm workers (Maximum 25 points).

6. **Housing using for large households.** The applicant makes a commitment to provide a minimum of 20% of the total housing units as low-income housing units with three bedrooms or more and to reserve such housing units for large households. (Maximum 10 points).

7. **Housing for persons who are elderly.** The applicant makes a commitment to maintain the project as an elderly housing project reserved and occupied by elderly persons, and as (Maximum 10 points).

8. **Housing for persons with disabilities.** The applicant makes a commitment to provide a minimum of 20% of the total housing units for persons with disabilities (Maximum 10 points).

9. **Housing for the homeless.** Provide a minimum of 20% of the total housing units as low-income housing units for transitional housing. A building must be 100% transitional housing if any housing unit in the building is used for transitional housing (Maximum 20 points).

10. **Preservation of federally assisted low-income housing.** Documentation that the project has a federally assisted building(s) with low-income housing units equal to at least 50% of the total housing units in the project that are at risk of being converted to market rate housing units within five years of the date of the application (Maximum 10 points).

11. **Maximize use of credit.** Projects that request the “4%” credit and that agree to limit the credit reservation and/or allocation to $4,050 or less per low-income housing unit or projects that request the “9%” credit and that agree to limit the credit reservation and/or allocation to $7,940 or less per low-income housing unit (Maximum 10 points).

12. **Rehabilitation projects.** Points will be awarded to projects consisting of one or more buildings, which will be rehabilitated and returned to, or converted to, residential use (Maximum 12 points).

13. **Project size.** Points will be awarded based on the greater (Maximum 10 points).

14. **Developer fees.** The applicant makes a commitment to limit the maximum developer fees for the project (Maximum 10 points).

15. **Historic property.** Percentage of housing units in building(s) designated as historic property (Maximum 5 points).

16. **Targeted areas.** A Difficult to Develop Area (DDA) or a Qualified Census Tract (QCT), additional points * may be scored if the entire project is located in a QCT and the Project’s development contribute to a Community Revitalization Plan (Maximum 7 points).

17. **Leveraging of public resources.** Supporting documentation that the project has received a substantial funding commitment(s) from a federal, state, and/or local government. (Maximum 10 points).

18. **Donation in support of local housing needs.** The applicant agrees to contribute to a local nonprofit organization an amount equal to the greater of: 25 basis points (0.0025) of total project cost; or $10,000 (Maximum 5 points).

19. **Eventual tenant ownership.** Points will be awarded to projects that are intended for eventual tenant ownership after the initial 15-year compliance period. (Maximum 2 points).
20. **Project readiness.** Projects financed with public resources: Binding loan commitments or projects not financed with public resources, all building permits ready and available to be paid for and picked up (Maximum 12 points).

Table 1: Comparison of inclusion of affordable housing and smart growth elements between the Washington State Financing Committee (2007) and the California Tax Credit Allocation Committee (2007) credit point system

<table>
<thead>
<tr>
<th>Elements</th>
<th>Washington SHFC</th>
<th>California TCAC</th>
<th>Proposed Malaysian LIHTC (urban area)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Location</td>
<td>Weight</td>
<td>Location</td>
</tr>
<tr>
<td>Affordable Housing Elements</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>1, 2, 7, 8, 9 &amp; 10</td>
</tr>
<tr>
<td>Based on sliding scale</td>
<td>LIHTC A%</td>
<td></td>
<td>LIHTC A%</td>
</tr>
<tr>
<td>Medical expenses should be deducted from housing cost</td>
<td></td>
<td></td>
<td>LIHTC A%</td>
</tr>
<tr>
<td>Housing size needs to be based on family need</td>
<td>6 3.9%</td>
<td>2 8%</td>
<td>2</td>
</tr>
<tr>
<td>Choice about location</td>
<td>*LIHTC A%</td>
<td>LIHTC A%</td>
<td>LIHTC A%</td>
</tr>
<tr>
<td>Needs to be stable in rent</td>
<td>LIHTC A%</td>
<td>LIHTC A%</td>
<td>LIHTC A%</td>
</tr>
<tr>
<td>Must meet stringent housing quality standards</td>
<td></td>
<td>4 8%</td>
<td>5</td>
</tr>
<tr>
<td>Based on the income</td>
<td>LIHTC A%</td>
<td>LIHTC A%</td>
<td>LIHTC A%</td>
</tr>
<tr>
<td>Should have the same rights, &amp; responsibilities</td>
<td>Management System A%</td>
<td>Management System A%</td>
<td>Management System A%</td>
</tr>
<tr>
<td>No additional fees</td>
<td></td>
<td>3(B)</td>
<td>10% LIHTC &amp; 4 A%</td>
</tr>
<tr>
<td>Smart Growth Elements</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(Adapted from metropolita n tenant organizer (2007))</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Preserve open space</td>
<td></td>
<td></td>
<td>4</td>
</tr>
<tr>
<td>Conservation of natural resources</td>
<td></td>
<td>4</td>
<td>5</td>
</tr>
<tr>
<td>Developing infill sites</td>
<td></td>
<td></td>
<td>3(A) &amp; 3(B)</td>
</tr>
<tr>
<td>Pedestrian-friendly architecture</td>
<td></td>
<td></td>
<td>3(A) &amp; 3(B)</td>
</tr>
<tr>
<td>Include citizens in land use decision-making ventures</td>
<td></td>
<td></td>
<td>1</td>
</tr>
<tr>
<td>Provision for creating widespread affordable housing</td>
<td>LIHTC</td>
<td></td>
<td>LIHTC</td>
</tr>
<tr>
<td>Encourage regional governing solutions to urban/suburban sprawl</td>
<td></td>
<td></td>
<td>3</td>
</tr>
<tr>
<td>Reduce automobile dependence</td>
<td></td>
<td>3(A)</td>
<td>12% 3, 4, 11 &amp; 12</td>
</tr>
<tr>
<td>Promote compact, high-density or mixed-use development</td>
<td></td>
<td>3(A) &amp; 3(B)</td>
<td>AA</td>
</tr>
<tr>
<td>Encourage cooperation from local/regional governments and planning organizations</td>
<td>4, 17 &amp; 18</td>
<td>7.9%</td>
<td>- --</td>
</tr>
<tr>
<td>Impose the social costs of new development onto real estate developers</td>
<td></td>
<td>3(B)</td>
<td>10% 3 &amp; 4</td>
</tr>
<tr>
<td>Proposed New Malaysian Scoring Elements</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Physical and social infrastructure</td>
<td></td>
<td></td>
<td>8</td>
</tr>
<tr>
<td>Female-headed as a target group</td>
<td></td>
<td></td>
<td>13</td>
</tr>
<tr>
<td>Attention to mix income housing</td>
<td></td>
<td></td>
<td>14</td>
</tr>
<tr>
<td>Concentrate on building for disadvantaged and the poor in urban area</td>
<td></td>
<td></td>
<td>8 &amp; 11</td>
</tr>
</tbody>
</table>

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NOTE: *Some percentages are common between some elements, for this reason cannot sum them and also some elements are involved in LIHTC aims and management system.

AA. Although developers would pay the costs for improving site amenities and services amenities, they may not directly involve pedestrian-friendly architecture.

BB. Applicable to mix-development projects only.

A%. Unaccountable.

From Table 1, we note the differences between two states in the United States. We have categorized all of the affordable housing elements and smart growth principles in two original group and try to show, which element has come in which point system. For example, both Washington’s and California’s point system give special attention to first affordable housing element as "Focused on families with minimum wage". However, when we refer to one of the smart growth principles as "Reduce automobile dependence", the reader can find this California point system in 3(A) had attention to this element but Washington did not attention to this. On contrary, the Washington point system has special attention to "Encourage cooperation from local/regional governments and planning organizations" but the reader would not find any article about this element in California point system. As the reader note, the ratings differ for each element between both states since both have differing number of articles and points for consideration. For instance, California focuses on the quality of life while Washington emphasizes on the human factors such as the elderly, farmers and homeless.

PROPOSED MALAYSIAN LOW INCOME HOUSING TAX CREDIT (MALAYSIAN LIHTC)

Housing has been promoted in the 7th Malaysian Plan (7MP) and the 8th Malaysian Plan (8MP). The 9MP is expected to see the government’s continuous effort to ensure that Malaysians of all income levels will have access to adequate, quality and affordable homes, particularly for those under the low-income group. In this regard, the private sector is expected to support the government’s initiative to build more low- and low-medium-cost houses in their mixed-development projects while the public sector will concentrate on building low-cost houses as well as houses for public sector employees, the disadvantaged and the poor in urban and rural areas. To enhance the quality of life of the urban population, the provision of more systematic and well organized urban services programs will emphasis on sustainable development, promoting greater community participation and social integration of the population [17], [18]. As a participant at the 25th special session of the general assembly for an overall review and appraisal of the implementation of the outcome of the United Nations Conference on Human Settlements (Habitat II) in New York in 2001, Malaysia has made a commitment to implement Agenda 21. We extracted the key elements in these documents and found that four of the items (as highlighted below) are missing from the combined affordable housing and smart growth elements requirements. Hence, we extended Table 1 to include the four Malaysian smart growth requirements:

1. Median income group beside the low income group (Seventh Malaysian plan)
2. Quality of life (Ninth Malaysian plan)
3. Development projects while the public sector (Ninth Malaysian plan)
4. Houses for public sector employees (Ninth Malaysian plan)
5. Concentrate on building for disadvantaged and the poor in urban and rural areas (Ninth Malaysian plan)
6. More systematic and well organized urban services programs (Ninth Malaysian plan)
7. Emphasize on sustainable development (Ninth Malaysian plan)
8. Promoting greater community participation (Ninth Malaysian plan)
9. Physical and social infrastructure (Malaysian statement at Habitat II)
10. Soft housing loan for target group (Malaysian statement at Habitat II)
11. Female-headed as a target group (Malaysian statement at Habitat II)
12. Attention to mix development and mix income housing (Malaysian vision 2020)

Additionally, we would also like to introduce three smart growth elements that are missing in both tax credit programs, which are preserving open space, developing infill sites, and encouraging regional governing solutions to urban/suburban sprawl.
CONCLUSIONS

In this paper, we attempt to develop a low-income housing tax credit program for Malaysia that includes smart growth elements while supporting the development of affordable housing units in Malaysia. The proposed Malaysian LIHTC supported nine affordable housing elements including focused on family with minimum wage, points based on sliding scale, housing sizes need to be based on family needs, choice of location, needs to be stable in rent, must meet stringent housing quality standards, based on the income, should have the same rights and responsibilities, and no additional fees. It also supports eleven smart growth elements including preserve open space, conservation of natural resources, developing in-fill sites, pedestrian-friendly architecture, include citizens in land use decision-making ventures, provision for creating widespread affordable housing, encourage regional solutions to urban/suburban sprawl, reduce automobile dependence, promote compact high density or mixed-used development, encourage corporation from local/regional governments and planning organizations, and impose the social costs of new development onto real estate developers. We are proposing additional elements based on the Malaysian commitments to Agenda 21 including physical and social infrastructure, female-headed as a target group, attention to mixed-income housing, and concentrate on building for disadvantaged and the poor in the urban area. It is our hope that our point system will become an alternative solution for housing developers in Malaysia to work together with government and corporations to finance the development of affordable quality housings for the whole nation. We also hope smart growth LIHTC become a common solution for urban problems in all over the world special developing countries.

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