

Testimony of Rafael Cestero
Senior Vice President for Field Operations and Program Support
Enterprise Community Partners, Inc.

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Field Hearing on Affordable Housing Preservation: Lessons from Starrett City
Brooklyn, New York
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Thank you, Chairwoman Waters and distinguished members of the Financial Services Housing and Community Development Subcommittee. My name is Rafael Cestero and I am senior vice president for Enterprise Community Partners. I appreciate the opportunity to share with you Enterprise's extensive on-the-ground affordable housing preservation activities and our analysis of Starrett City, as well as to outline our federal policy recommendations.

Enterprise is a leading provider of development capital and expertise needed to create decent, affordable homes and rebuild communities. For a quarter of a century, Enterprise has pioneered neighborhood solutions through private-public partnerships with community organizations, financial institutions, local governments and others who share our vision. Enterprise has raised and invested \$8 billion in equity, grants and loans to support the creation of 215,000 affordable homes, and is currently investing in communities at a rate of \$1 billion a year.

National Need for Preserving Affordable Housing

During the past decade, approximately 170,000 public housing units were lost to neglect and deterioration. Much of the remaining public housing stock has substantial renovation and rehabilitation needs. Without an infusion of new resources and policy changes, the remaining 1.2 million public housing units - nearly half of which are home to the elderly or seriously disabled - will continue to decline.

At the same time, 1.4 million units of privately owned, federally subsidized housing faces preservation challenges. Roughly 300,000 units were lost during the last 10 years, representing close to 15 percent of the national affordable housing stock. This loss can primarily be attributed to building owners choosing not to renew subsidized contracts.¹ Outside forces affecting these decisions include gentrifying markets, continued uncertainty over tenant and project based Section 8 appropriations and tax depreciation recapture issues faced by investors.

Through practical experience, we know that it costs less to preserve affordable housing units than to replace them. Enterprise estimates that the tax credit equity needed to rehabilitate an apartment is \$39,500, while the estimated tax credit equity needed to newly construct an apartment is \$65,500, a 66 percent cost premium.

¹ Center on Budget and Policy Priorities, "The Effects Of The Federal Budget Squeeze On Low-Income Housing Assistance," February 2007

Strategies for the Preservation of Affordable Housing

Enterprise is committed to preserving affordable housing nationwide, bringing our expertise and resources to bear through predevelopment loans, financial restructuring, tax credit equity investments and credit enhancements. In 2006, Enterprise refinanced more than 30 properties that had HUD financing or subsidies. Proceeds from refinancing allow additional capital investment, increased support services and create more affordable housing units. Additionally, the recapitalization will ensure that these units remain affordable for another 20 to 30 years.

State and Local Efforts

As efforts to preserve affordability at Starrett City have shown, preservation requires governmental involvement at local, state and federal levels. States are making strides toward addressing preservation issues. State and local finance agencies employ a variety of strategies to ensure preservation of affordable housing, such as providing private activity bonds and 4 percent Low Income Housing Tax Credits (LIHTCs), allocating state housing trust fund money and providing predevelopment and bridge loans. Six years ago, only six states set aside 9 percent Low Income Housing Tax Credits – a precious commodity – for affordable housing preservation. Today, 46 states have set aside credits dedicated to preserving affordable homes in their qualified allocation plans.² Enterprise works with these state programs, bringing a range of financing tools and approaches as well as unique understanding of non-profit and for-profit developer motivations, market knowledge and relationships. Both New York State and New York City have allocated significant amounts of their 9 percent tax credits and tax exempt bond volume cap to preservation of affordable housing. During the last several years, this has led to the preservation of 40,000 units in the City.

Enterprise Preservation Funds

To ensure that community organizations have access to much needed capital to acquire and preserve housing affordability, Enterprise has launched preservation funds in New York City and Washington, D.C.; we are exploring similar funds in Los Angeles and Atlanta. In the District of Columbia, Enterprise created the DC Preservation Fund as an acquisition loan product for preserving multifamily housing. Enterprise raised \$20 million of private capital, matched by \$8 million of public dollars from the District government to create a \$28 million preservation fund. This new fund provides acquisition and predevelopment financing for non-profit sponsors in the Washington, D.C. metropolitan area to acquire existing affordable multifamily properties threatened with conversion to for-sale housing or higher-rent use. To date, the fund has preserved more than 600 affordable units in D.C. and the surrounding suburbs.

NYC Billion Dollar Promise and Acquisition Fund

The affordable housing challenge has never been more severe in New York City. Mayor Michael Bloomberg's groundbreaking New Housing Marketplace Plan to create and preserve 165,000 units is the largest municipal housing effort in the country. Yet this Herculean effort is only part of the solution. With unsubsidized rents rising and affordability restrictions in programs like Mitchell-Lama ending, the housing stock is

² National Housing Trust State and Local Housing Initiatives Working Paper, June 2007. www.nhtinc.org

quickly trending up-market to rates only the wealthiest can afford. Developments such as Starrett City with its close to 6,000 apartments must be preserved as affordable housing. In 2004, Enterprise New York pledged to invest \$1 billion in 15,000 affordable homes by 2008 in support of New York City's efforts. . We are now more than halfway there, with \$610 million invested in grants, equity and loans to create or preserve almost 7,000 homes for low-income New Yorkers.

As part of our billion dollar promise, Enterprise and our partners created the NYC Acquisition Loan Fund. The goal of the New York City Acquisition Loan Fund is to create and preserve more than 30,000 units of affordable housing in 10 years. The Fund is a partnership among the public, private and non-profit sectors. It offers a new way for community-based developers to secure development capital to create a pipeline of affordable housing sites. Through the fund, loans are available to non-profit and for-profit developers for acquisition and pre-development costs only.

Just two weeks ago, Enterprise and the New York City Department of Housing Preservation and Development announced the acquisition and preservation of 283 low- and moderate-income apartments in the northwest Bronx. This sale is the first preservation agreement through the Acquisition Fund.

I'd like to share with you the story of the Rodriguez family, current residents of this particular development in the Bronx. Like many New Yorkers, the Rodriguez family struggled to find a safe and decent home in today's challenging housing market. Working at a day-care center during the day, Marisol Rodriguez seldom saw her husband, Wilmer, who works the night shift as a doorman in Manhattan. Marisol and Wilmer were barely making ends meet to afford a substandard apartment, and they knew they could not continue raising their children in a neighborhood where they constantly worried about their safety.

Marisol and Wilmer decided to move to this building in the Kings Bridge Heights area of the northwest Bronx in hope of finding a safer, more affordable apartment. The owners of this building decided to sell their portfolio of properties, but were committed to keeping the rents affordable for the buildings' tenants. With the help of Enterprise and the New York City Acquisition Fund, the Fordham Bedford Housing Corporation (FBHC), a non-profit affordable housing developer in the Bronx, acquired the Rodriguez's building and five others. This \$23 million loan to FBHC will help to ensure future affordability in a borough where 50 percent of residents pay half their income for rent.

For the Rodriguez family, being able to stay in their home in Kings Bridge Heights has made all the difference. It is the safest neighborhood in which they've lived, and they feel confident about letting their children out to play. With the combined efforts of the City, the Acquisition Fund, and Enterprise, the Rodriguez is among the 283 families that will keep their affordable and well-maintained homes far into the future.

Preservation of Starrett City

Preserving Starrett City as an affordable housing resource for low- and moderate-income families in New York City is and should be one of the highest priorities for all levels of government. Enterprise, in partnership with ACORN, has looked very carefully at the Clipper Equities bid for the Starrett City property. It is very clear that without significant new subsidies from the federal, state and local governments, this bid will lead to the loss of Starrett City as affordable housing.

I say this for several reasons: Clipper Equities has proposed to acquire Starrett City for \$1.3 billion and opt-out of the existing regulatory regime. Clipper’s proposal is dependent upon receipt of an additional \$30 million in annual government rent subsidies, retention of current real estate tax abatements at an estimated cost government of \$17 million and assumption of significant operating cost savings. Both of the financial conditions requested by Clipper require significant waivers of programs and policies that may not be statutorily possible. Without these deep government subsidies, the Clipper’s transaction is financially infeasible and the \$1.3 billion acquisition price cannot be supported.

	Clipper Proposal	Clipper Proposal, at Full Taxes without Waivers and Based on Actual Operating Costs
Effective Apartment Revenue	\$125 million	\$97.4 million
Commercial / Other Revenue	\$9.2 million	\$9.2 million
Effective Gross Income	\$134.2 million	\$106.6 million
Operating Expenses	(\$65 million)	(\$80 million)
Real Estate Taxes	(\$3.1 million)	(\$20 million)
Reserve Requirements	(\$0 million)	(\$3.3 million)
Net Operating Income	\$65.9 million	\$1.5 million
Proposed Debt Service	(\$59.9 million)	(\$59.9 million)
Net Cash Flow	\$5.9 million	(\$58.4 million)

Federal Policy Recommendations for Affordable Housing Preservation

Preserving affordable housing at the necessary scale will require commitment at the highest levels of federal, state and local government. I commend and thank the New York City House delegation as well as Senators Schumer and Clinton for their powerful advocacy on behalf of preserving affordable housing at Starrett City and elsewhere.

I would like to make the following policy recommendations as low-cost strategies that will provide much-needed flexibility and expand the available resources to preserve affordable housing for our nation’s most vulnerable:

Enact Exit Tax Legislation

Historically, the federal government has invested in creating affordable rental housing for millions of lower income individuals and families. Changes to the tax code have made owners of affordable housing properties reluctant to transfer their property to new owners because depreciation recapture taxes due at sale often exceed a reasonable sales price. Instead, owners often choose to hold the properties until death, at which point no taxes will be collected on the depreciated gain. As a result, lower valued affordable housing properties are often left to deteriorate while higher valued properties are sold and converted to market rate housing. Either scenario risks federally assisted affordable housing stock.

I urge congress to enact the Affordable Housing Preservation Tax Relief Act of 2007 (H.R. 1491/S. 1318), which would facilitate the transfer of federally assisted housing so that rental housing can be preserved as affordable. This bill would waive the seller's depreciation recapture tax liabilities if the purchaser agrees to keep the housing affordable for 30 years after the property transfer. This policy change would have enormous positive impact on preserving affordable rental housing for low-income people.

Create an Early Warning System

With minimal investment, HUD could create an Early Warning System to help preserve properties if owners prepay mortgages, opt out of HUD subsidy programs or encounter other circumstances which may lead to loss of the property's affordability restrictions. As part of this Early Warning System, HUD should be required to post Real Estate Assessment Center (REAC) scores, Section 8 opt out or renewal notices and Wellstone prepayment notices. Providing this information as soon as possible to tenants, community developers and state and local governments will allow localities to develop solutions before the ability to preserve the property is lost. There is no guarantee that an Early Warning System would have prevented the Starrett City situation. But creating such a system would provide the information necessary to safeguard housing affordability, building by building, community by community.

Strengthen Cities' Right of First Refusal

Local governments must be able to exercise their statutory right of first refusal to purchase HUD-owned buildings. Previously, sales price for buildings sold by HUD to local government housing agencies were based on a number of industry standards, including estimated repair and rehabilitation needs. However, HUD recently issued guidance stating that it will no longer consider repair or rehabilitation costs in determining an appropriate sales price. This new policy will undoubtedly raise preservation costs as purchasers must effectively pay twice for any repair costs. Such policies make it nearly impossible for government housing agencies and/or subsequent preservation developers to preserve the properties as affordable.

I strongly encourage Congress to enact Section 5 of the Stabilizing Affordable Housing for the Future Act (H.R.44), which provides that HUD must use industry standard appraisal practices, including consideration of repairs costs and maintenance of affordability, in determining the market value of all multifamily real property and multifamily loans. I commend Congresswoman Velázquez for introducing this

legislation, which when enacted will provide valuable tools and resources for the preservation of affordable housing.

Strengthen Protections for Troubled Properties

Congress should amend existing law to grant HUD's non-judicial foreclosure authority to local governments designated by HUD as part of the note and mortgage sale process. These local governments will then be able to more efficiently handle physically or financially distressed buildings. Local governments will also be able to manage these distressed properties to the benefit of eligible tenants. Congress should require HUD to maintain rental assistance to buildings during rehabilitation as part of a preservation transfer. This assistance should be escrowed until the building or units meet HUD's Housing Quality Standards, at which time the escrowed funds should be made available to the property.

Enact a Federal First Right of Purchase

Federal law establishes no protections for most federally assisted housing properties when owners seeks to prepay mortgages and convert properties to market rate use. Tenants may receive enhanced or other vouchers, but despite years of federal investment the physical housing units are lost to the community. Congress should require owners proposing to end participation in federal HUD and Rural Development housing programs to offer the properties for sale at fair market value to preservation purchasers.

Conclusion

I would again like to thank the Subcommittee for holding this important hearing and for their commitment to preserving affordable housing. The federal government plays an invaluable role preserving affordable housing and creating effective preservation policies. Enterprise stands committed to working with Congress to create policies that will preserve affordable homes, with the goal of creating healthy and sustainable communities of opportunity for families of all incomes.