



2020

TIPPING THE SCALE

PRESERVING THE AFFORDABILITY OF UNSUBSIDIZED
SMALL- TO MEDIUM-SCALE MULTIFAMILY HOUSING

ACKNOWLEDGMENTS



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INTRODUCTION

As the United States continues to see a shortfall in its housing supply, home prices and rents have continued to outpace household incomes and units with lower rents have continued to fall out of the supply. These dynamics have created a housing crunch, particularly for low- and moderate-income people.ⁱ To tackle this challenge, we must both build more homes and preserve the homes we already have.

SMMF properties—properties with 2 to 49 units—provide 54 percent of the nation’s rental housing and 21 percent of all housing in the United States.ⁱⁱ SMMF properties are a critical source of housing for lower-income households: Among the estimated 21 million rental units in SMMF buildings, 34 percent (7.1 million units) are affordable to households at 80 percent of median renter income; 57 percent (11.9 million units) to households at the median renter income, and 75 percent (15.7 million) to households at 20 percent of median renter income.ⁱⁱⁱ While these properties often accept tenant-based rental assistance, many of these affordable units are in buildings without property-level subsidies.^{iv} This portion of the SMMF stock—properties that do not receive project-level subsidies but are still affordable to lower-income households—is the focus of this toolkit.

Unsubsidized affordable SMMF housing not only represents a significant component of the affordable rental housing stock, but it can also offer a more cost-efficient way to address housing needs. Preservation efforts usually cost 30 to 50 percent less than new construction, with one study finding that new construction costs \$40,000 to \$71,000 more per unit than rehabilitating older units.^v

Preserving the affordability of these properties can provide a crucial source of housing that is otherwise in short supply while also yielding reasonable economic returns. But it represents new territory for many in the housing and community development field. This toolkit seeks to close the information gaps that may be preventing more developers from engaging in the preservation of unsubsidized affordable SMMF housing.



A NOTE ON TERMS

SMMF stands for small- to medium-multifamily, which this toolkit defines as properties with 2 to 49 units. This toolkit focuses on SMMF properties that are unsubsidized and affordable to lower-income households.ⁱⁱ This unsubsidized, yet affordable housing is sometimes referred to as “naturally occurring affordable housing” or “NOAH” in the affordable housing sector. Recognizing the social and economic forces (e.g. disinvestment and redlining), along with property and neighborhood conditions (e.g. age, physical condition, surrounding amenities), that contribute to the relative affordability of rents in these properties, we will instead use the term “unsubsidized affordable housing.”^{vii}



TOOLKIT OVERVIEW

This toolkit provides best practice recommendations and tips that will help you avoid common challenges when working on an unsubsidized affordable SMMF preservation project. The toolkit is organized into the following sections:

RELATIONSHIP BUILDING

The strength of your relationships will affect your success at each stage of the development process. While this is not unique to unsubsidized affordable SMMF preservation, it is especially important in these projects because they often represent new territory for many of the partners that will be necessary to bring a deal to life. In particular, strong relationships can help overcome common barriers found at the outset of unsubsidized affordable SMMF projects – finding the right property, acquiring it on favorable terms, and assembling sufficient financing to preserve it. This toolkit highlights the impact of several key relationships on the viability of your unsubsidized affordable SMMF preservation project, along with tips to build and strengthen those relationships.

PROPERTY IDENTIFICATION

There are fewer systems in place and less widespread understanding of the characteristics that make unsubsidized affordable SMMF properties strong candidates for preservation, which can create more work for you at the outset of a project. Tips in this toolkit are designed to make that property identification process easier.

SECURING FINANCING

Unsubsidized affordable SMMF preservation is often viewed by financiers as a niche market and many existing financing products for affordable housing are not designed for this property type. These factors can make it difficult to assemble sufficient financing for preservation. This toolkit provides an overview of financial products that can support your unsubsidized affordable SMMF preservation project.

NEGOTIATION AND DEAL CLOSING

Much of the negotiation and deal closing process for SMMF properties will be similar to other development projects. However, there are specific risks to be mindful of that may be more likely with this property type. These risks increase with the complexity of your project, particularly based on the financing and level of rehabilitation you pursue. This section of the toolkit outlines the common pitfalls that can disrupt or delay the closing process for unsubsidized affordable SMMF preservation, along with tips for addressing them, to help you better plan for and mitigate potential risks at this stage of a project.

REHABILITATION

Since unsubsidized affordable SMMF properties tend to be older, they often require some level of rehabilitation to bring them up to code or improve their habitability. The toolkit provides an overview of five topics that may uniquely impact an unsubsidized affordable SMMF project: 1) zoning and building codes; 2) health and safety needs; 3) energy efficiency; 4) disaster resilience; and 5) existing residents and community members.

PROPERTY MANAGEMENT

Effective and cost-efficient property management is critical to successfully preserving affordability after rehabilitation or refinancing. Since preservation may or may not include the use of subsidy to maintain the property's affordability, this section outlines the unique considerations you must account for when managing an unsubsidized affordable SMMF property or when managing a newly subsidized SMMF property. The toolkit also highlights several strategies you can use to minimize operating expenses through property management.



KEY TERMS



HOUSING AFFORDABILITY

Housing is considered affordable when the cost does not exceed 30 percent of a household's income. Affordability is tied to income; this toolkit focuses primarily on the preservation of housing that is affordable to low- and moderate-income households.



LOW-INCOME/MODERATE-INCOME

A household is considered low-income when their income is at or below 80 percent of the area median income. A household may be considered moderate-income if their income is between 80 percent and 120 percent of the area median income.



MEDIAN RENTER INCOME

The median household income for all renter households in an area. This metric is used to assess affordability throughout this toolkit to better capture demand for SMMF rentals. Median renter income is not adjusted for household size and is often lower than area median income (which includes both renters and homeowners). As such, median renter incomes do not correspond to HUD income limits or definitions of low-income, very low-income, or extremely low-income based on HUD income limits.



PRESERVATION

Preventing the loss of currently affordable units from the available and affordable housing stock. Preservation activities may include refinancing, improving or modernizing existing properties to ensure they remain affordable to households at specific income levels and livable.



SMALL- TO MEDIUM-SCALE MULTIFAMILY (SMMF) HOUSING

Residential buildings with 2 to 49 units.

RELATIONSHIP BUILDING

Any development project depends on strong partnerships and relationships to move from concept to reality. Unsubsidized affordable SMMF preservation is no exception. In fact, relationships are often more critical in these projects—particularly for purchasing the property and securing the financing needed to preserve it. Relationships are especially important since there are limited examples of successful projects at this scale, fewer established systems to support it than other preservation deals, and (sometimes) tighter financial margins.

These relationships will impact every stage of the preservation process. Tips related to relationship building for unsubsidized affordable SMMF preservation projects have been incorporated throughout the toolkit. These tips are highlighted with the following icon: . They focus on dynamics that may be unique to an unsubsidized affordable SMMF project relative to a larger-scale project or a project preserving subsidized housing.

KEY RELATIONSHIPS THROUGHOUT THE UNSUBSIDIZED AFFORDABLE SMMF PRESERVATION PROCESS



Stakeholders who may own unsubsidized affordable SMMF properties

- Public sellers – local government
- Private sellers – mom and pop owners, other local/regional owners, institutional owners and investors



Stakeholders who can help acquire unsubsidized affordable SMMF properties

- Brokers or real estate agents
- Local government
- Real estate attorneys



Stakeholders who can help finance unsubsidized affordable SMMF properties

- Community Development Financial Institutions (CDFIs)^{xii}
- Banks
- Local and state governments
- Housing finance agencies
- Real estate investment trusts (REITs)
- Government-sponsored enterprises (GSEs)
- Foundations
- Anchor institutions
- Other private investors



Other stakeholders that will influence the success of the project

- Development team – architects, engineers, construction managers and contractors
- Local, regional and state policymakers
- Local planning commissions
- Community members



Stakeholders that can help manage the property

- Property managers
- Asset managers

HOW DO RELATIONSHIPS FOR UNSUBSIDIZED AFFORDABLE SMMF PRESERVATION DIFFER FROM LARGER PROJECTS OR SUBSIDIZED HOUSING PRESERVATION?

OWNER PROFILE

You will likely be working with fewer institutional owners. Unsubsidized affordable SMMF property owners tend to have smaller portfolios and are more likely to live near their properties.

BROKERAGE EXPERTISE

There are fewer established frameworks for identification of unsubsidized affordable SMMF opportunities than with other property types. Fewer established practices means you or your broker partner will need more expertise about what makes a property a strong candidate for preservation. When brokers have this expertise, plus strong relationships with unsubsidized affordable SMMF property owners, they can help you identify opportunities for property acquisition before they are listed for sale. Off-market opportunities can help keep costs low and increase the financial feasibility of preserving unsubsidized affordable SMMF properties. Considerations related to identifying strong candidates for SMMF preservation are outlined in the Property Identification section.

EVALUATION BY LENDERS

Lenders tend to place a larger emphasis on their belief in the owner when evaluating affordable SMMF deals, as compared to other affordable housing deals.

BROAD COMMUNITY ENGAGEMENT

There will be fewer requirements (if any) for community participation in the preservation of an unsubsidized affordable SMMF property, unless subsidies are used or significant local land-use approvals are needed. In addition to obtaining approvals, community support and relationships can be critical when you are identifying properties for preservation, engaging existing owners, and finding tenants.



PROPERTY IDENTIFICATION

EVALUATING UNSUBSIDIZED AFFORDABLE SMMF PROPERTIES

Unlike subsidized housing, the affordability of unsubsidized affordable SMMF properties occurs in a largely unregulated environment, meaning there are few systems focused on this market segment to guide decision making. In terms of property identification, many national frameworks for affordable housing preservation do not focus on SMMF as a distinct market segment, even though they make up 54 percent of the national rental housing stock.^{vii} These gaps reinforce uncertainty about working with this property type, along with the inherent uncertainty associated with an affordable, yet unregulated property.

For many developers, opportunity tends to drive preservation of unsubsidized affordable SMMF properties, although what “opportunity” means varies by the developers’ experience in a given market and their overall mission or interest in preserving these properties. For instance, to some developers, “opportunity” means a willing seller in a rapidly changing neighborhood. To others, “opportunity” means a property where moderate improvements will extend the useful of a property without increasing rents significantly.

Four key factors should be used to evaluate opportunities for unsubsidized affordable SMMF preservation:^{xiv}

- 1. PROPERTY CHARACTERISTICS** – This factor focuses on the overall condition of the property, its size, and who the property serves today. Common criteria include building size, physical condition, reputation of current property management, and household income of existing tenants.
- 2. PROJECT FEASIBILITY** – This factor focuses on a project’s ability to meet basic regulatory requirements, including compliance with land-use standards and building codes. This factor also considers a project’s eligibility for financing and public subsidies. Common criteria include whether rezoning, variance, or other land-use exemption is required; ability to meet all applicable building codes; ability to meet all infrastructure requirements (e.g., water, sewer, road capacity); funding eligibility; and existing relationships.
- 3. NEIGHBORHOOD MARKET CONDITIONS** – This factor focuses on how neighborhood market conditions are changing or may change, based on indicators of market activity. Market activity serves as a proxy for financial feasibility and risk of displacement or loss of unsubsidized affordable SMMF properties. Common criteria for this factor include different dimensions of increased or anticipated market activity and neighborhood change.
- 4. NEIGHBORHOOD ACCESS** – This factor focuses on access to basic amenities and common destinations. This factor highlights surrounding conditions that may make the property appealing. Preserving properties in areas with stronger access to opportunity promotes economic mobility and addresses long-standing disparities. Common criteria include access to employment centers; access to transit service; access to healthy foods; and access to quality schools.



EVALUATING UNSUBSIDIZED AFFORDABLE SMMF OPPORTUNITIES IN STRONGER OR EMERGING MARKETS

In the national literature about unsubsidized affordable properties, the most commonly cited goal for preservation is to safeguard the property's inherent affordability before it is lost. Unsubsidized affordable SMMF properties in stronger or emerging real estate markets are typically seen as top preservation priorities since they are the most susceptible to market-rate conversion or demolition, and preserving their affordability can help to foster vibrant, mixed-income communities.^{ix}

In stronger or emerging markets, preserving unsubsidized affordable SMMF properties necessitates quick action and often faces fierce competition. For opportunities in this type of market, property identification factors such as project feasibility—relationships to pull together an offer quickly, access to nimble financing, and limited or no regulatory constraints—may be more important than in neighborhoods with stable or weaker housing markets.

EVALUATING UNSUBSIDIZED AFFORDABLE SMMF OPPORTUNITIES IN STABLE OR WEAKER MARKETS

It is equally important to consider the loss of unsubsidized affordable SMMF in stable or weaker markets, as it is in rapidly changing neighborhoods. In stable or weaker markets, maintaining or improving habitability staves off loss due to property deterioration and preserves affordability in lower-cost areas.

In stable or weaker markets, the calculus around unsubsidized affordable SMMF preservation is somewhat different than in stronger or emerging real estate markets. For instance, preserving unsubsidized affordable SMMF properties necessitates a longer commitment to the neighborhood. Due to neglect or age of the properties, the overall rehabilitation costs may be higher, resulting in the need for a larger per unit investment or higher contingency (although these costs are typically offset by lower land costs).

On the other hand, some barriers to entry may be lower. Due to less interest from outside investors, accessing properties in stable or weaker submarkets may be easier, avoiding the high upfront acquisition costs in stronger markets.

For opportunities in this type of market, property identification factors such as property characteristics—the building's age and condition—may be more important than in neighborhoods with stronger or emerging housing markets.

TIPS FOR IDENTIFYING AN UNSUBSIDIZED AFFORDABLE SMMF PROPERTY

CONSIDER UNSUBSIDIZED AFFORDABLE SMMF OPPORTUNITIES IN NEIGHBORHOODS WHERE YOU ALREADY WORK.

Avoid the need to create economies of scale in a new market or neighborhood by looking for unsubsidized affordable SMMF opportunities in neighborhoods where you already own or operate properties.

LOOK FOR OFF-MARKET OPPORTUNITIES.

Off-market opportunities do not face as much (if any) competition from other buyers helping to lower acquisition costs, especially in stronger markets with more interest in unsubsidized affordable SMMF properties from investors. To identify them, use real estate data, such as CoStar, that classifies property condition, experience working in a specific neighborhood, and relationships with property owners and brokers.

BUILD RELATIONSHIPS WITH LENDERS TO VET POTENTIAL OPPORTUNITIES.

Lenders can provide upfront advice about potential unsubsidized affordable SMMF opportunities and share their willingness or ability to be involved in a project, which assists with understanding broader project feasibility.

IDENTIFY ANY REGULATORY CONSTRAINTS.

In many places, unsubsidized affordable SMMF properties are a “nonconforming structure” (i.e., do not meet the current zoning requirements in their current area) and may require a rezoning or other land-use exemption before a sale can proceed. In other instances, unsubsidized affordable SMMF properties may not maximize the full development potential on their site, making them more valuable to competing buyers.





FINDING THE RIGHT BROKER-PARTNER

Your relationship with a broker (or brokers) affects your ability to identify off-market opportunities, quickly acquire properties, and the price you may pay.

Questions to consider when evaluating potential brokers for partnership:

- How well does their expertise align with my preservation goals?
- Do they understand the rehabilitation process for multifamily units?
- Do they have experience with SMMF properties?
- Do they have experience and relationships in the geography where the property is located?
- Are they comfortable with the financing sources I plan to use for acquisition?



DEALBREAKERS FOR UNSUBSIDIZED AFFORDABLE SMMF PROPERTIES

NEED FOR TENANT RELOCATION

The time, costs and requirements associated with tenant relocation may deter developers from unsubsidized affordable SMMF opportunities. Read more about the considerations around tenant relocation in the Rehabilitation section.

NEED FOR SIGNIFICANT REPAIRS

Preservation of unsubsidized affordable SMMF properties, especially without subsidy, require a “repair, not replace” type mindset. To ensure financial feasibility, focusing on properties with light or moderate capital needs is recommended. While choosing properties with light or moderate capital needs is ideal, more subsidy makes properties with more substantial rehabilitation needs feasible (albeit more complex). Some organizations conduct rigorous capital needs assessments to understand immediate needs, as well as to plan for medium- and long-term needs prior to purchase, while others conduct visual surveys of a property. To

ensure all capital needs are taken into consideration, a more detail capital needs assessment is recommended, as is having resources available to assist with these assessments either prior to preservation or on an ongoing basis.

LACK OF PUBLIC SUPPORT

Support among neighborhood residents, local decisionmakers and public-sector staff are all critical to the success of preserving an unsubsidized affordable SMMF property. Elected leaders and public-sector staff often need to make decisions about regulatory changes or funding quickly, as buyers are competing in the private market for these properties. Smaller, affordable properties may garner neighborhood support more easily than a large-scale affordable housing development.



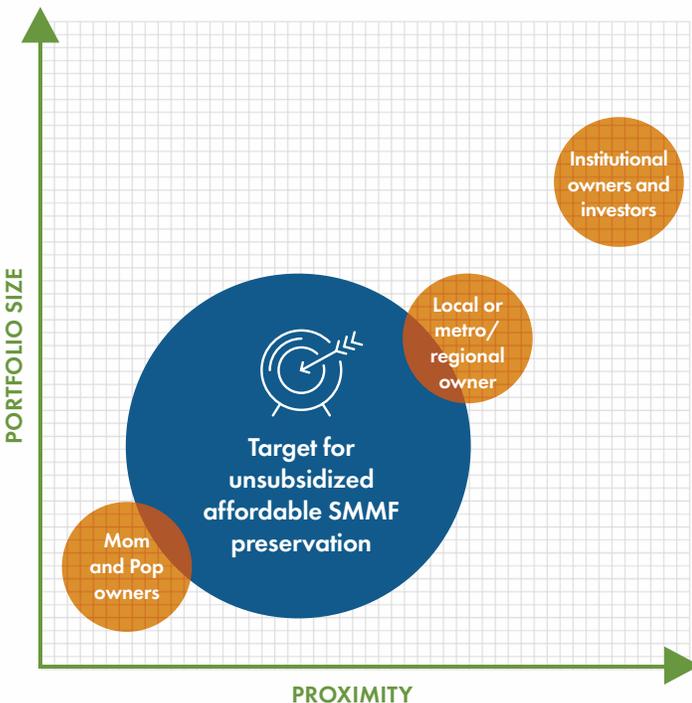
WORKING WITH PROPERTY OWNERS

Even when using a commercial real estate brokerage, having a strong relationship with property owners can help increase your access to potential deals and the deal's success.

Two key dimensions that may affect sellers' behavior are:

- Portfolio size (i.e., how many properties do they own?)
- Proximity (i.e., how far from the property is the owner based?)

Generally, an owner is less likely to engage in affordable housing preservation activities when they own a large portfolio of properties and those properties are located farther away from them, unless there is a strong economic case or if they have a distinct focus on mission over profit.



Potential seller motivations^{xvii}

- Increasing and maintaining a steady cash flow
- Maximizing return on investment
- Alleviating the burden of property maintenance
- Inability to access capital for necessary rehabilitation
- Alleviating the cost of rising property taxes
- Retirement or estate planning

Mission or public benefits may motivate a property owner, but the extent will vary. Research has found that part-time or smaller-scale owners with local interests are the most willing to prioritize mission and community investment over other motivations, particularly when they are not tied to a larger organization's bottom-line.^x

Considerations for building and maintaining strong relationships with sellers

- **Demonstrating sufficient capital**, or an expedient timeline for assembling the necessary capital, is important for successfully engaging sellers. In such situations, bridge financing or a line of credit can be critical, particularly when competing with cash offers. See page 23 for tips on relationship building with financial institutions, who can help assemble these resources.
- **Agreeing on project goals and terms upfront**, including the long-term relationship between both parties and the property. This agreement is particularly important if sellers plan to stay involved with the property after its preservation. For instance, mission-oriented sellers may want to be involved with property operations, such as resident services or other onsite activities.^{xii}

SECURING FINANCING

Financing unsubsidized affordable SMMF depends on a range of factors: a property's capital needs; its size; and its location, to name a few. To many lenders, deals for unsubsidized affordable SMMF represent a niche financing market. Financing, like other aspects of the preservation process, benefit from economies of scale. Few national products are designed specifically for SMMF properties, making it an under-resourced inventory.

Many traditional tools for affordable housing development, such as the Low-Income Housing Tax Credit, favor larger properties and new construction. Depending on a property conditions, four percent tax credits may not be enough to fund capital needs and typically require a larger deal to be financially feasible. Building a portfolio of unsubsidized affordable SMMF properties or preserving unsubsidized affordable SMMF properties as part of a larger development are two ways to build economies of scale, and in turn, expand eligibility for financing.^{xii}

Meeting a lender's loan-to-value requirement can pose another barrier for underwriting purposes, when capping rents at affordable levels. Some financial products on the West Coast, such as the New Generation Fund in Los Angeles, offer higher loan-to-value ratios to address this barrier (but as of now these products are only available regionally).^{xiii}

The preservation of some unsubsidized affordable SMMF properties can be financed using conventional lending products. If an unsubsidized affordable SMMF property needs to be more heavily subsidized to maintain affordability, additional sources of capital or direct subsidy will be needed.



THE FINANCIAL MODELING TOOL

Use the financial modeling tool to understand these dynamics and evaluate the feasibility of real-world unsubsidized affordable SMMF opportunities.

Developers and lenders with experience working with unsubsidized affordable SMMF stressed that financing these properties requires a market-oriented mindset, especially if no subsidy is being used. They agreed that a lean approach (and set of financing assumptions) is critical when trying to balance cash flow with nominal rent increases to maintain affordability.

NATIONWIDE CAPITAL SOURCES AND SUBSIDIES FOR SMMF PRESERVATION

Table 1 below provides a snapshot of nationally available capital and subsidy sources that could support the preservation of affordable SMMF properties.

TABLE 1. RESOURCES AVAILABLE FOR PRESERVATION OF SMMF PROPERTIES

Program	Resource type	Considerations for unsubsidized affordable small- and medium-scale multifamily properties
U.S. Department of Housing and Urban Development FHA 223(f) Multifamily Loan Insurance Program	Hard debt	<ul style="list-style-type: none"> • Designed for properties with 5+ units • Lower-interest rate • Non-recourse financing • Substantial rehabilitation ineligible
Freddie Mac Small Balance Loan Program	Hard debt	<ul style="list-style-type: none"> • Simplified capital stack • Streamlined underwriting • Pricing breaks • Designed for properties with 5+ units and portfolios (2+ loans) • Non-recourse financing
Fannie Mae Small Balance Loan Program	Hard debt	<ul style="list-style-type: none"> • Simplified capital stack • Streamlined underwriting • Pricing breaks • Designed for properties with 5+ units • Non-recourse financing
Freddie Mac Value-Add Program	Hard debt	<ul style="list-style-type: none"> • More feasible for larger unsubsidized affordable SMMF properties (25+ units)
Freddie Mac NOAH Preservation Loan	Hard debt	<ul style="list-style-type: none"> • Minimum affordability requirements • Minimum equity requirements • Full underwriting process
Freddie Mac Impact Gap Loan	Hard debt	<ul style="list-style-type: none"> • Need to find an outside impact investor
U.S. Department of Housing and Urban Development Project-based vouchers (administered by local housing authorities)	Operating subsidy	<ul style="list-style-type: none"> • Stable resource • Pre-screened tenants • Competing local programmatic priorities • Ongoing administration costs • Limit on project-based vouchers per project

TABLE 1. RESOURCES AVAILABLE FOR PRESERVATION OF SMMF PROPERTIES (CONTINUED)

Program	Resource type	Considerations for unsubsidized affordable small- and medium-scale multifamily properties
U.S. Department of Housing and Urban Development HOME Investment Partnerships Program (administered by local jurisdictions and states)	Soft debt Grant Hard debt	<ul style="list-style-type: none"> • Stable resource • Flexible (can fill multiple capital needs) • Maximum affordability • Subsidy limits • Competing local programmatic priorities • Alignment with funding cycles • Compliance with federal requirements • Prevailing wage requirements (12+ assisted units) • Rules when combining HOME and tax credits
U.S. Department of Housing and Urban Development Community Development Block Grant (administered by local jurisdictions and states)	Soft debt Grant Hard debt	<ul style="list-style-type: none"> • Stable resource • Flexible (can fill multiple capital needs) • Maximize affordability • Competing local programmatic priorities • Alignment with funding cycles • Compliance with federal requirements • Prevailing wage requirements (8+ assisted units)
Enterprise Community Loan Fund Acquisition Loan	Hard debt	<ul style="list-style-type: none"> • Developers' experience • Full-time development staff to offset experience
Enterprise Community Loan Fund Pre-Development Loan	Hard debt	<ul style="list-style-type: none"> • Developers' experience • Full-time development staff to offset experience





Fannie Mae’s and Freddie Mac’s Small Balance Loan programs offer two of the most viable financial products for preserving unsubsidized affordable SMMF properties. Both programs offer financing for properties with 5 to 50 units. These programs can assist relative newcomers to the unsubsidized affordable SMMF market. As non-recourse financing (i.e., the property’s operations secures the loan), strong property management is critical. However, the programs’ size thresholds leave out the smallest multifamily products (those properties with 2 to 4 units).

While federal resources for affordable housing have been declining, they still represent a long-standing resource for preserving unsubsidized affordable SMMF. The HOME Investment Partnerships (HOME) and Community Development Block Grant (CDBG) programs are two federal programs that can support unsubsidized affordable SMMF. These federal programs are available to entitlement communities (cities and counties) directly and through state agencies to non-entitlement communities, which both set more specific priorities for their use.^{xiv}

One of HOME and CDBG’s advantages is their flexibility. Both programs can be used to fill a range of capital needs. For instance, both acquisition and rehabilitation are eligible activities under these programs. HOME funds can also be used to refinance a project’s existing debt in conjunction with rehabilitation.

An important consideration when using either program is a developer’s ability to comply with all federal requirements, including paying local prevailing wages. The smallest unsubsidized affordable SMMF projects may avoid this requirement entirely. The prevailing wage requirement is triggered for properties with eight or more assisted units when using CDBG dollars and 12 or more assisted units when using HOME dollars. Prevailing wages may add significant cost to the project (as much as 20 to 40 percent by one national estimate).

Rental assistance available through local public housing authorities is another federal resource—in this case, to support ongoing operations of unsubsidized affordable SMMF properties rather than capital needs. Project-based vouchers, a component of the federal Housing Choice Voucher program, keep individual units affordable for tenants and generate consistent rents for a property owner. However, public housing authorities have their own policies guiding the use of these vouchers and typically award them through a competitive process. Developers can also accept rental assistance directly from tenants as another way to assist with their cash flow.

CONSIDERATIONS BEYOND CAPITAL

Lenders evaluate deals for unsubsidized affordable SMMF through a different lens than more traditional affordable housing deals. In unsubsidized affordable SMMF deals, lenders place a larger emphasis on their belief in the owner, including the owner's capacity for property and asset management and past development experience.

Why is this the case? Unsubsidized affordable SMMF properties are viable investments only if they can maintain a steady cash flow (in contrast to subsidized properties where compliance with affordability requirements is an added consideration). These properties are especially sensitive to vacancy. A strong track record of property management demonstrates the ability to control expenses, retain tenants, and effectively asset-manage.

Ways to support this property type include:^{xxv}

- *Creating a lending or banking consortium^{xv}*
- *Creating an SMMF equity pool funded by government and/or philanthropy*
- *Expanding existing national preservation funds to properties with 50 or fewer units*
- *Expanding existing capital products to properties with 5 or fewer units*
- *Working with philanthropic organizations to provide the following:*
 - *Credit enhancements*
 - *Program-related investments*
 - *Unfunded guarantees to financial institutions*



BUILDING STRONG RELATIONSHIPS WITH LENDERS



Assume more of the risk

(compared with other affordable housing financing models, like the Low-Income Housing Tax Credit).

For instance, one national lender said they would require at least 5 percent equity to consider underwriting an unsubsidized affordable SMMF project.



Possess strong development and/or property management expertise

A developer should be able to demonstrate familiarity with property management and leasing laws, including a successful history of property ownership and management. If a developer does not have this expertise in-house, they can demonstrate how they will fill any capacity gaps, such as partnering with a large management company for the first few years of operations or hiring an accountant and lawyer to assist them. This expertise can vary based on the property's condition and phases of the project. For instance, you may benefit from a property management partner with expertise in addressing troubled properties during the rehabilitation process but may need a different long-term manager once the property is preserved.



Make a strong first impression

For national lenders, up-to-date, professionally packaged financial information bolsters confidence.

NEGOTIATION AND DEAL CLOSING

Understanding the aspects of an affordable SMMF preservation deal presents an opportunity to strengthen your negotiation and closing with your project partners. For instance, a financial partner may have fewer projects or deal structures to reference when doing an affordable SMMF preservation deal, and it can be helpful to demonstrate how you see the deal coming together.

A practical financial modeling tool can help established nonprofit and for-profit developers become more active players in the unsubsidized affordable SMMF market. It can demonstrate the key aspects of your preservation deal to lenders or local decisionmakers to help build support for your project and long-term capacity to assist with a smoother closing. And it can quickly assess ways to fill any financing gaps that may arise during this stage of preservation.

COMMON PITFALLS THAT CAN DISRUPT THE CLOSING PROCESS FOR AFFORDABLE SMMF PRESERVATION

In addition to the common financial hurdles that can disrupt closing (e.g., obtaining consent of subordinate lenders in refinancing; conditions of the construction lender relative to the permanent lender; disagreement about different debt sources' positions in the capital stack), there are a variety of property-related hurdles to be aware of during the closing process for affordable SMMF preservation projects:

ISSUES FOUND DURING A TITLE SEARCH THAT MAY PREVENT A TITLE COMMITMENT

This may be especially relevant for SMMF properties that have unreleased liens or have been informally sold or transferred in the past (including heirs' properties). Research by the Center for Community Progress has shown these murky title situations are more likely to occur in low-income communities and neighborhoods with many senior households, which are also areas where preservation efforts can be particularly impactful (e.g., addressing blight or preventing displacement).

EVIDENCE OF CONTAMINATION OR HAZARDOUS MATERIALS

This pitfall is most relevant to properties that have been vacant and/or are located in older, predominantly low-income communities.^{xvi} Contamination can result from things like leaking pipes running under the property, neighboring industrial buildings, leaching from a nearby waterway and illegal dumping. These issues can present even if there is a previous environmental study on the property, reinforcing the need for updated environmental studies at the outset of your preservation project.

APPRAISAL GAPS

Appraisal gaps can occur due to inadequate market analysis, poorly estimated cash flow projection or simply a very strong real estate market. This can be a particular risk with unsubsidized affordable SMMF preservation, since it may be hard to find appropriate comparables, especially in strong markets, where a property's selling price may be determined by rents in newly constructed buildings or a different use. If the appraisal comes back less than anticipated, you may need to find additional equity or financing to cover the gap. One potential solution would be to seek a guarantee from a philanthropic funder, which may enable a Community Development Financial Institution or bank to offer a higher loan-to-value ratio.

TIPS FOR NAVIGATING NEGOTIATION AND DEAL CLOSING

Team capacity – To close a preservation deal for unsubsidized affordable SMMF properties, the following capacities are needed:

- **Knowledge of:**
 - Local land-use and permitting processes
 - Financial resources and how to structure deals
 - Comparable projects and their terms and conditions
- **Expertise:**
 - Technical expertise – Surveying, environmental assessment (if needed), architecture and/or engineering (if needed), construction, property management
 - Financial expertise – Accounting; private sector lending; public sector financing
 - Legal expertise – Land-use, affordable housing, real estate/tax law^{xxviii}
 - Regulatory compliance expertise related to using specific financing resources



RELATIONSHIPS WITH FINANCIAL PARTNERS

It also helps to have good relationships with and knowledge of your financial partners. Even if you don't have an existing relationship with your financial partner, understanding their interests in your deal (e.g., exit terms, sponsor guarantees, investor's expected return) will support a stronger negotiation.

NEGOTIATE DEAL POINTS EARLY

Ideally, all major deal points should be negotiated as early as possible. Major deal points include (but are not limited to): guarantees; credit delivery; pay-ins and conversion requirements; permit status; dates for final investment approval; lien position; and discrepancies in lease-ups and legal leases compared with current cash flow statements.

With fewer precedents for unsubsidized affordable SMMF projects, financial partners may need to negotiate waivers or alternative terms on a case-by-case basis, adding time and uncertainty to the closing process. For instance, during the underwriting process, identify any deviations from a lender's programmatic requirements and understand options for waivers as soon as possible. Proactively identify issues that could derail the deal and propose solutions that will help compensate the lender for added risk (e.g., adjustments to term and interest rates or extra reserves).

REHABILITATION

Since unsubsidized affordable SMMF properties tend to be older or have deferred maintenance, they often require some level of rehabilitation to bring them up to code or improve their quality.

This section provides an overview of how the following factors affect the rehabilitation of unsubsidized affordable SMMF properties:

- Zoning and building codes
- Health and safety needs
- Energy efficiency
- Disaster resilience
- Existing residents and community members

It also provides tips and examples of how to address these factors while maintaining the property's affordability.



ZONING AND BUILDING CODE REQUIREMENTS

PARKING REQUIREMENTS

Meeting minimum parking requirements can be a challenge when preserving unsubsidized affordable SMMF properties, particularly for older properties that have less parking than is now required. In some instances, these requirements may mean you need a larger site to create an efficient parking arrangement.

PERMITTED DENSITY

More substantial rehabilitation of unsubsidized affordable SMMF properties may experience issues with allowable density. For instance, if part of the preservation strategy includes creating more units to increase cash flow without raising rents, that may trigger issues with allowable units per acre (or even allowable building height, if the rehabilitation plan would expand the building envelope).

NONCONFORMING STRUCTURES

Given the age of unsubsidized affordable SMMF properties, they may no longer conform to current zoning regulations. In other words, these properties may be a nonconforming structure, meaning the structure may have met zoning requirements when it was built, but subsequent changes to zoning requirements include new standards that the lot and/or structure do not meet. Nonconformance can be the result of wholesale updates to the zoning code or adoption of zoning overlays for specific areas. Rehabilitation of nonconforming structures often triggers a requirement to bring the property into conformance, which can be costly.

Recognizing this requirement can be a disincentive to rehabilitate deteriorating housing, some local governments have offered regulatory relief for certain types of preservation projects.

BUILDING CODES

While building codes are often cited as a key barrier to rehabilitation of existing buildings, particularly older buildings, trends in building code reform have been favorable for unsubsidized affordable SMMF preservation. It is increasingly recognized that having the same building code standards for rehabilitation and new construction projects has prevented quality rehabilitation from taking place (or at least made them more costly). This recognition has resulted in an increasing number of specific rehabilitation codes across the country. Research has shown these differentiated code requirements have resulted in significant cost savings in rehabilitation projects, particularly for smaller projects.^{xix}

Despite positive reforms, some building code requirements still create hurdles to the preservation of unsubsidized affordable SMMF properties, particularly when they trigger the same requirements as new construction. On the other hand, more resilient buildings can result in lower insurance premiums and significant cost-savings when disasters occur, despite the higher upfront cost. *See below for more discussion about resilience and unsubsidized affordable SMMF preservation.*

It is important to be aware of any building code requirements during the property identification phase of your project and adjust assumptions about your costs accordingly. For instance, some developers noted the surprising cost of new fire sprinkler systems, which often need to be added to unsubsidized affordable SMMF properties but may not be accounted for during property identification.



HEALTH AND SAFETY NEEDS

ASBESTOS AND LEAD-BASED PAINT REMOVAL

Two of the most common health and safety concerns when rehabilitating a property involve asbestos and lead-based paint removal. If the property in question was built before 1978, it is likely that one or both of these will need to be remediated.

The level of rehabilitation may inform what level of mitigation to pursue. For instance, if a property has been relatively well-maintained and requires little more than refinancing to maintain affordability, encapsulation may be a suitable (albeit temporary) solution. Meanwhile, substantial internal renovations may require the complete removal of hazardous materials.

INCORPORATING ACCESSIBILITY

Nationally, one-quarter of SMMF buildings were built in the 1970s and 1980s, and some are much older.^{xx} Older properties may not offer accessibility features for persons living with disabilities or others, such as seniors, that would benefit from more accessible features.

Creating more accessible homes is important in and of itself. But when older properties use public funding, they are subject to federal accessibility requirements through the *Americans with Disabilities Act (ADA) of 1990* and Section 504 under the *Rehabilitation Act of 1973*.

Developers using federal funding and undertaking more significant rehabilitation of unsubsidized affordable SMMF properties with 15 units or more need to provide accessible units under Section 504. Developers who receive funds from federal, state or private sources will need to comply with ADA requirements in public areas of their multifamily property (parking lots, rental office and laundry and community rooms).^{xxi}

ENERGY EFFICIENCY

SELECTION OF THE RIGHT PRODUCTS

Some energy efficiency measures can be incorporated into small-scale rehabilitation efforts with little to no additional cost, if you know the right products to use (e.g., which lighting fixtures reduce energy consumption). These products are generally comparably priced to other less efficient products and reduce your operating costs over time. This can be especially important if you want to use Housing Choice Vouchers, since public housing payment standards are based on both rent and utilities.

TEAM EXPERTISE

Certain energy efficiency or green building measures may require specialized expertise to implement. To help you find qualified technical assistance providers, Enterprise Community Partners, Inc. has compiled a [Technical Assistance Providers Database](#) of qualified experts in topics related to the design, development, and construction of energy-efficient, environmentally friendly, and safe affordable housing.

TRANSACTION COSTS

While energy-efficient measures are not costly to incorporate, the transaction costs, such as the cost and time to conduct energy audits or measure and verify cost-savings, do not scale.^{xxii} You may also lose some volume efficiency when buying energy-efficient products in smaller quantities. Pursuing a portfolio of unsubsidized affordable SMMF rehabilitation projects at the same time can address this barrier.

ENERGY EFFICIENCY FUNDING

You can obtain free energy audits and grants for implementation through existing programs. It is also important to note that some local jurisdictions require energy audits on a regular basis.

Energy efficiency can be more costly in older SMMF properties if they require broader systems updates (either to meet existing codes or extend the property's lifecycle). In these instances, green rebate programs and other financing (like Property Assessed Clean Energy programs) may be available to cover the upfront capital costs. For the latest information on resources available to finance energy efficiency improvements, consult the [Database of State Incentives for Renewables & Efficiency](#). When pursuing these resources, be aware of any requirements that may impact your broader project (e.g., caps on total preservation cost or cost-per-unit).

DISASTER RESILIENCE MEASURES

Resilience means "the capacity of individuals, communities, housing, infrastructure, institutions and businesses within a community to survive, adapt and grow as they confront a variety of extreme and chronic stresses."^{xxviii} As the number and severity of disaster events increases across the United States,^{xxix} resilience is not only key to maintaining the fabric of our communities; it is also a smart financial investment which can save property owners money, by promoting efficiencies, eliminating building deficiencies, and potentially reducing insurance premiums.^{xxiii}

VULNERABILITY OF UNSUBSIDIZED AFFORDABLE SMMF PROPERTIES

The size and age of unsubsidized affordable SMMF properties mean they are particularly vulnerable to disasters:

- **Age** – Unsubsidized affordable SMMF buildings tend to be older and inconsistently maintained. As a result, properties may not meet the latest standards for disaster preparedness
- **Size** – Since construction materials and methods may differ based on property size, unsubsidized affordable SMMF properties can have different risks to hazards than larger properties. Strategies for increasing the resilience of SMMF properties through rehabilitation are discussed in more detail below and in Appendix 2.

UNDERSTANDING YOUR RISK

It is important to understand the local hazards surrounding your preservation project, because different areas of a community are vulnerable to different types of disasters. The context around your project will affect how you incorporate resilience into your rehabilitation efforts, which disaster-related requirements apply to your project, and which resources are available. Appendix 2 provides a framework for assessing your project's hazard risk. Enterprise Community Partners, Inc. is also creating a resilience portfolio assessment tool to help you understand the specific exposure rating of your building. Based on your inputs, it will create a risk score based on social vulnerability and climate risk. The tool covers those hazards most common to the United States and territories.^{xxiv}

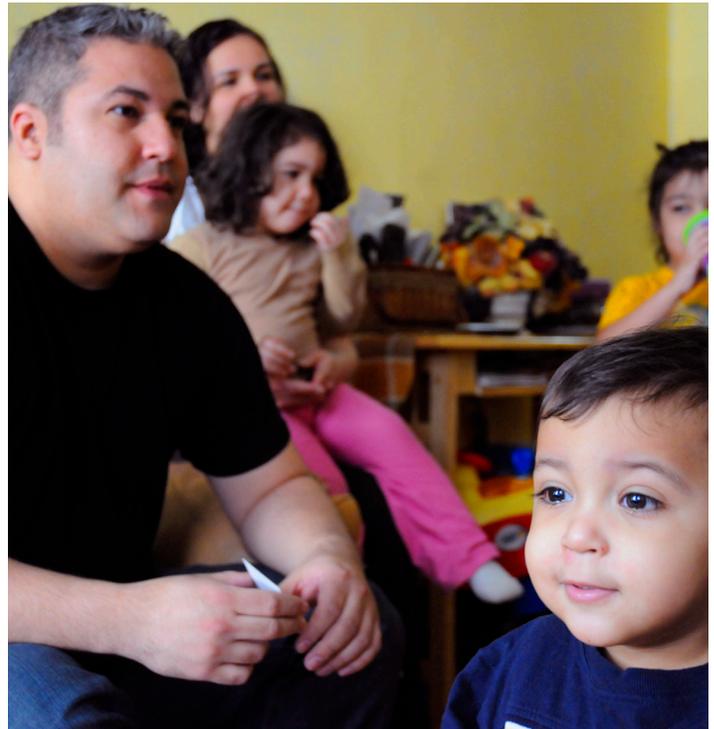
REDUCING DISASTER RISK AND MAINTAINING AFFORDABILITY IN REHABILITATION

The following strategies can help keep costs low and improve resilience during rehabilitation:

- **Investing in resilience and energy efficiency** – Making these improvements can reduce your operating costs, making it financially feasible to keep rents lower. These improvements can range from simpler measures like weatherization up to the replacement of full systems. The average payback on these investments is seen in less than three years, depending on the project scale.^{xxv} There are a variety of funding and rebates available to support the upfront investment in these measures.

For example, Property Assessed Clean Energy (PACE) financing is available in many markets around the country and provides low-interest loans to cover 100 percent of the hard and soft costs of energy efficiency, renewable energy or other resilience projects that you repay via assessments on your property tax bill.

- **Investing in preventative maintenance** – Sealing leaks and cracks not only prevents longer term problems that protect the structure from deteriorating, such as mold, but also reduces your long-term financial exposure.
- **Having redundant building systems** – Having back-up systems, such as electrical and heating systems, helps a property maintain habitability and property owners repair systems with greater speed.
- **Selecting materials with co-benefits** – Certain materials have multiple benefits (or “co-benefits”) when used. For instance, light-colored materials, including finishings and paint, reduce heat intrusion to keep rooms cool and withstand moisture.



EXISTING RESIDENTS AND COMMUNITY MEMBERS

There are a variety of points in the preservation process where residents and community members can influence the success of your rehabilitation project:

- **Identifying unsubsidized affordable properties for preservation** – Existing community members are a vital source of information on the local demand for different types of housing, which can inform your assessment of different properties. They may also be aware of key risks associated with properties in their neighborhood, including potential code violations or hazards, which can also inform your rehabilitation plan.
- **Acquiring the property** – Since many unsubsidized affordable SMMF owners live near the properties they own community members are likely both aware of good candidates for preservation in their neighborhood and know the owner directly. With this knowledge and relationship, community members can help you formulate an owner-engagement strategy to acquire the building.
- **Obtaining approvals from local government** – As with any development, a small group of vocal community members can have a great impact on the likelihood of obtaining approvals from local decisionmakers. Critical approvals for unsubsidized affordable SMMF preservation may include land acquisition (if the property is publicly owned), financing awards, and land-use approvals.
- **Finding tenants** – Marketing the units once they come online will require strong communications with surrounding community members, who may be prospective tenants or who may be able to recruit tenants.

COMMUNITY ENGAGEMENT FOR UNSUBSIDIZED AFFORDABLE SMMF PROJECTS

Unsubsidized affordable SMMF preservation projects tend to have fewer requirements and less time for community engagement, relative to larger scale preservation efforts, new construction or preservation of subsidized units. However, it is still critical to build trust and communicate regularly with the surrounding community, given the many ways they can impact your preservation process and outcomes.



BUILDING AND MAINTAINING STRONG COMMUNITY RELATIONSHIPS



Regularly attend community meetings

These events may include town halls, council meetings, neighborhood meetings, or stakeholder meetings to support public planning processes.



Research the historic context

Community experiences from past development projects can greatly influence expectations for future projects. Prepare to acknowledge this history and explain how your project will be consistent with or different from that experience. Local newspaper archives and community outreach can help you understand this context.



Identify resident leaders

Establish a regular feedback loop with resident leaders. These leaders may come from schools, community centers, social service agencies, faith-based institutions and other groups that are embedded in a community.



Have an easily accessible online presence

Ensure your website is easily search-able and leverage social media. Pair this with clear and consistent messaging before, during and after rehabilitation.



Communicate the community benefit of your project

This may include key health and safety needs that will be addressed through rehabilitation. Consider messages that uplift existing assets in the community and/or are grounded in expressed community goals.



SPECIAL CONSIDERATIONS FOR ALREADY OCCUPIED PROPERTIES

If your unsubsidized affordable SMMF property is already occupied, there are several additional considerations to keep in mind (each of which underscores the importance of strong engagement with residents and community members):

- Tenant-based voucher use** – While unsubsidized affordable SMMF properties do not have project-based subsidies prior to preservation, current tenants may be using Housing Choice Vouchers to pay rent. In fact, early research on unsubsidized affordable SMMF properties suggests they are often home to voucher recipients.^{xxvi} If current residents are using vouchers, this will trigger federal relocation requirements.
- Demographics** – Depending on how you are financing your preservation effort, you may have restrictions on who can live in the units after the project is complete (e.g., subsidies that require a share of units serve low-income households). You should carefully consider how funding requirements align with the demographics of current tenants before adding restricted funding or financing to your capital stack. If there is a mismatch between funding or financing requirements and existing residents, you risk displacing them, which will not only damage the community and your reputation but also your bottom line (e.g., relocation costs, legal issues, or significant push-back from community members that delays or stops your project).
- Tenant opportunity to purchase** – In some municipalities, tenants have the right to collectively purchase the property they live in before it is sold. If that is a possibility, it is even more important that you build trust with the existing tenants and their neighbors and that you clearly communicate the value of your rehabilitation plan to them, including how it meets core community needs and goals.



RELOCATION TIPS

- Work with property managers who have experience with the current residents and relocation processes. They can help inform and coordinate moving timetables and other logistics.
- Bring on an experienced compliance specialist who has experience with tenant relocation regulations and can manage the entire process.
- Create a clear way to prioritize who gets to move back first, if at all. Use lease terms and impact on housing subsidies to help inform this prioritization.

PROPERTY MANAGEMENT

The management of unsubsidized affordable SMMF properties ensures the viability and livability of these properties once preserved. The key challenges associated with managing this property type are creating economies of scale for professional property management services and managing operating expenses. Unlike newly constructed housing, preserved unsubsidized affordable SMMF properties need ongoing attention to their expenses to keep cash flow consistent.

There are some key differences between managing an unsubsidized affordable SMMF property that was preserved using significant public resources and one preserved with limited or no public resources. For unsubsidized affordable SMMF properties preserved with limited or no subsidy, property managers need to focus on maintaining stable occupancy; ensuring on-time rent payments; and marketing and leasing these properties to prospective tenants who may be weighing various alternatives. For unsubsidized affordable SMMF properties preserved with significant subsidies, property managers' largest focus should be on meeting all the requirements associated with them. Compliance at these properties creates a need for specialized experience and staff as part of the property management team.



CHALLENGES MANAGING PRESERVED SMMF PROPERTIES

CREATING ECONOMIES OF SCALE

Unsubsidized affordable SMMF properties often do not generate enough cash flow to hire a full-time property manager or maintenance person. One of the largest challenges associated with operating preserved SMMF properties are achieving economies of scale, without which there is little interest from professional management companies and higher indirect costs when an owner performs management functions in-house. Economies of scale for owning and operating affordable housing properties is typically reached by portfolios with 100 units or more and when properties in that portfolio are near one another. At this size, portfolios should be able to attract a third party to assist with operations.^{xxvii}

INDIRECT COSTS ASSOCIATED WITH PROPERTY SELF-MANAGEMENT

Due to SMMF properties' small size (2 to 49 units), many nonprofit or mission-driven property owners may choose to self-manage. Self-management enables the property owner to focus on meeting residents' needs and use management fees from the project budget to support property management functions. However, one of the most significant challenges associated with self-management is covering indirect costs (e.g., overhead, supervisory, and other "back office" costs).^{xxviii}

MEETING COMPLIANCE REQUIREMENTS

SMMF properties preserved using public subsidies, such as HOME or the Low-Income Housing Tax Credit, requires reporting and compliance with all regulatory requirements and federal fair housing laws, in addition to more traditional property management functions. While requirements vary by funder, meeting them requires a strong administrative infrastructure. Property owners will need the expertise, staff capacity and systems to effectively administer and comply with these requirements.

MANAGING EXPENSES

Managing expenses is one of the most important aspects of managing preserved SMMF properties. SMMF properties preserved through light or modest rehabilitation often need ongoing investment to maintain their livability. Typically, SMMF properties preserved through light or modest rehabilitation have limited operating reserves to cover escalating expenses, such as higher utility costs and property taxes (this may be a particular issue in stronger or emerging housing markets where these properties are at risk of losing their affordability). They also may or may not have enough replacement reserves to cover large-scale needs, making "repair, not replace" an important strategy when managing expenses.

PROPERTY INSURANCE IN AREAS PRONE TO ENVIRONMENTAL DISASTERS

As disasters become increasingly common, insurance costs are also rising. Often, these cost increases are passed onto building tenants. Property owners will need to anticipate any changes and ensure they have enough cash flow to cover an increase in insurance costs while keeping rents stable for tenants. Alternatively, incorporating resilience measures into your rehabilitation plan can help lower insurance premiums, helping you both maintain affordability and protect your property and the people that live there from future disasters. See the Rehabilitation section of the toolkit for additional information about disaster resilience for this property type.



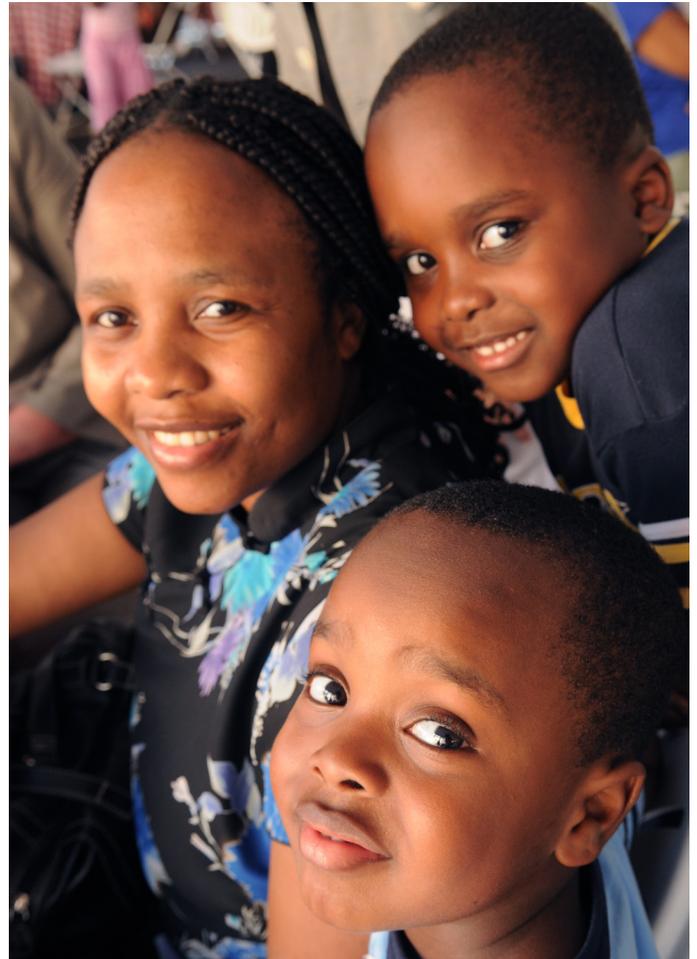
Ways to minimize operating expenses

- **Work with funders to develop a “compliance light” approach.** Many developers and lenders with experience preserving unsubsidized affordable SMMF properties recommend looking for opportunities to fit compliance requirements into owners’ existing property management practices and minimize overall requirements when possible.
- **Invest in materials that will be cost-efficient over the project lifecycle, including energy efficiency, green building and disaster resilience measures where possible.**^{xxix} Using more durable materials that need to be replaced less often and upgrading the building structure and systems to improve energy efficiency are two ways to lower operating and maintenance costs and increase affordability. In many cases these measures can also support the building’s resilience to natural disasters, which further helps lower operating costs by reducing insurance premiums.
- **Build capacity to scale key operating functions in-house.** Owners of smaller portfolios would benefit from building their capacity to perform key property management functions. Owners can seek out property and asset management trainings to build their in-house capacity or solicit for assistance to understand different approaches and clarify the roles they should play. They can also explore lighter service models, such as the resident/circuit-rider model offered by Community Housing Improvement Systems and Planning Association (CHISPA) in Salinas, CA. In this model, a manager oversees multiple, clustered properties and visits a property during set office hours to address residents’ needs.^{xxx}
- **Centralize key operating functions with nearby property owners.** Owners of smaller properties can work with other small-scale or mission-driven property owners located in the same neighborhood to create a larger portfolio and advertise it to professional management companies. These owners could also explore partnerships with larger property owners located in the same neighborhood to understand opportunities for shared management services, including a la carte assistance with specific functions such as tenant screening.



OPERATING COSTS

- The physical structure is in good condition.
- Systems improvements lower utility costs (e.g., water and energy).
- Property taxes are manageable.
- Developers have the right capacity and skillset for property management.
- Paperwork associated with compliance is minimal.



CONCLUSION

The preservation of unsubsidized affordable SMMF properties can be a powerful method for addressing our nation's housing affordability crisis, spurring investment in neighborhoods and strengthening local economies. A variety of strategies can increase the success of these projects, including:

PORTFOLIO-BASED APPROACHES FOR ECONOMIES OF SCALE – Pursuing the preservation of multiple unsubsidized affordable SMMF properties at the same time (particularly multiple properties that are located near one another) can help you achieve greater economies of scale, increasing your access to financial products, improving the feasibility of various rehabilitation expanding efficient options for your property management operations.

STRATEGIC ACQUISITION – Choices made during property identification and acquisition have far-reaching effects on other stages of the preservation process and the project's long-term viability. Calibrating your property choices to the surrounding market conditions is critical. Key considerations include whether the property can be acquired off-market; it is in a neighborhood where you already work; it does not need major repairs; and it does not require tenant relocation.

FINANCING RIGHT-SIZED TO MARKET CONDITIONS AND PROPERTY NEEDS – To right-size financing, you will need to assess if subsidy is appropriate and available and if so, how much subsidy is needed to cover the property's capital needs while keeping rents affordable to tenants. From there, it is critical that your financing terms are tailored to your anticipated cash flow, accounting for projected market conditions and property needs. For instance, in markets that have experienced disinvestment, shorter loan periods may be beneficial because you can refinance again more quickly. Meanwhile, in markets experiencing price increases, longer amortization periods may allow you to maintain lower rents, by providing more time to recoup costs before paying back debts.

REDUCING TRANSACTION COSTS – While the project may be smaller, transaction costs are not smaller for SMMF properties. But they can be reduced through more efficient processes that reduce time and administrative burdens, such as increasing the amount and reducing the frequency of draws during construction. Strong relationships, particularly with your lender, and transparent communication systems (e.g., accounting software, project management plans) are key to reducing these costs, especially if you or members of your project team have not completed an SMMF preservation project before.

FOCUS ON MATERIALS THAT WEAR WELL OVER THE PROPERTY'S LIFECYCLE – It will be cheaper to invest once in materials that can withstand the test of time, rather than replace materials repeatedly. Identify opportunities to negotiate lower costs on quality building materials that will have longer life spans. These opportunities may include purchasing materials that will reduce energy consumption or improve resilience to natural disasters, since these can also lower operating costs.

More examples of successful SMMF preservation, along with more systems designed to support these types of projects are needed to increase the scale of these efforts across the United States. The first step is increased attention to this important segment of our affordable housing supply, followed by a commitment to its affordability. We hope you will join us in taking up this challenge to *tip the scale* in favor of preserving small and medium multifamily properties.

NOTES AND REFERENCES

ⁱ New housing construction has barely kept pace with household growth for the past eight years. According to the Joint Center for Housing Studies, annual construction should be producing 260,000 units more than were produced in 2018 to keep up with demand while maintaining slack for normal vacancies. And while cost-burden rates have been improving among homeowners, renter cost-burdens are rising among most income groups. Nearly one-half of renter households (47 percent) experienced cost-burdens in 2018, and this figure is much higher in some areas of the country. Meanwhile, the United States' lower-cost housing stock shrunk by four million units since 2011. For more information, see the Joint Center for Housing Studies' State of the Nation's Housing (2019): www.jchs.harvard.edu/sites/default/files/Harvard_JCHS_State_of_the_Nations_Housing_2019.pdf.

^{iv} An, B. et al. (2017). Understanding the Small and Medium Multifamily Housing Stock. Report prepared by Enterprise Community Partners, Inc. and USC Price School of Public Policy. Available at <https://www.enterprisecommunity.org/resources/understanding-small-and-medium-multifamily-housing-stock-19423>.

^v Enterprise Community Partners, Inc. tabulation of 2017 American Community Survey (ACS) 1-year microdata. Median renter income was used instead of area median income to focus on the accessibility of rental units for renters.

^{vi} There are about 1.7 million units actively subsidized at the property level in SMMF buildings nationally, which accounts for less than one-quarter of the total SMMF units affordable to households at 80 percent or less of median renter income. Enterprise Community Partners, Inc. tabulation of 2017 ACS 1-year microdata and National Housing Preservation Database.

^{vii} Brennan, M. et al. (2013). Comparing the Costs of New Construction and Acquisition-Rehab In Affordable Multifamily Rental Housing: Applying a New Methodology for Estimating Lifecycle Costs. Center for Housing Policy Working Paper. Available at <https://pdfs.semanticscholar.org/5337/abc2544ae5820a1bc92e52ce3d8f6d5fb8f9.pdf>. and HUD. (2013). "Preserving Affordable Rental Housing: A Snapshot of Growing Need, Current Threats, and Innovative Solutions." Evidence Matters. Available at www.huduser.gov/portal/periodicals/em/summer13/highlight1.html.

^{xii} Community Development Financial Institutions (CDFIs) are mission-driven financial institutions dedicated to expanding economic opportunity through lending and financial services in underserved communities, such as low- and moderate-income neighborhoods.

^{xiii} Enterprise Community Partners, Inc. tabulation of 2017 ACS 1-year microdata.

^{xiv} These factors were derived from a literature review of national frameworks for identifying, evaluating, and prioritizing preservation projects and public policy priorities for preserving housing affordability.

^{xv} This is particularly true for unsubsidized affordable SMMF properties, as research conducted by the National Trust for Historic Preservation has demonstrated that neighborhoods with a mix of older, smaller buildings also tend to contain more age diversity, woman and minority-owned small businesses, and have greater walkability than areas with newer, larger structures. See Older, Smaller, Better: Measuring How the Character of Buildings and Block Influence Urban Vitality: https://dillonm.io/articles/NTHP_PGL_OlderSmallerBetter_ReportOnly.pdf.

^{xvii} Minnesota Preservation Plus Initiative. (2013). The Space Between: Realities and Possibilities in Preserving Unsubsidized Affordable Rental Housing. Available at <https://noahimpacifund.com/wp-content/uploads/2016/08/gmhf-space-between.pdf>.

^{xviii} Abdelgany, S. (2017). Catching Affordability Where It's At: Acquisition/Rehab of Oakland's Unsubsidized Affordable Housing. Available at www.urbandisplacement.org/sites/default/files/images/pr_somayaabdelgany_5.25.pdf.

^{xix} Treskon, M. and Sara McTarnaghan. (2016). Anatomy of a Preservation Deal: Innovations in Preserving Affordable Housing from around the United States. Report prepared for the Urban Institute. Available at www.urban.org/research/publication/anatomy-preservation-deal-innovations-preserving-affordable-housing-around-united-states.

^{xxi} For a detailed discussion of the challenges of financing SMMF properties, see *Small Multifamily Rental Property Financing* by the Office of the Comptroller of the Currency, U.S. Treasury Department: www.occ.treas.gov/publications-and-resources/publications/community-affairs/community-developments-investments/pub-cdi-may-2015.pdf.

^{xxii} For instance, the New Generation Fund, a revolving loan fund for acquisition and predevelopment, offers up to 120 percent loan-to-value for nonprofit sponsors and up to 95 percent loan-to-value for for-profit sponsors.

^{xxiv} Visit HUD's [Community Development Block Grant](http://www.hud.gov/CommunityDevelopmentBlockGrant) and [HOME Investment Partnerships](http://www.hud.gov/HOMEInvestmentPartnerships) program sites, respectively, for more information about how entitlement communities are determined.

^{xxvi} In a lending consortium, bankers "pool their risks and resources to address areas of need." For a detailed discussion of the challenges of financing SMMF properties, see *Small Multifamily Rental Property Financing* by the Office of the Comptroller of the Currency, U.S. Treasury Department: www.occ.treas.gov/publications-and-resources/publications/community-affairs/community-developments-investments/pub-cdi-may-2015.pdf.

^{xxvii} Ha, H. et al. (2016). "Analysis of Pollution Hazard Intensity: A Spatial Epidemiology Case Study of Soil Pb Contamination." *International Journal of Environmental Research and Public Health*, 13(9). Available at www.ncbi.nlm.nih.gov/pmc/articles/PMC5036748/.

^{xxviii} It is important to have your own attorney (separate from that of the seller or lender) when title issues are identified.

^{xxxiii} Mattera, P. (2006). Breaking the Codes: How State and Local Governments are Reforming Building Codes to Encourage Rehabilitation of Existing Structures. Available at www.goodjobsfirst.org/sites/default/files/docs/pdf/breaking_the_codes.pdf.

^{xxxv} An, B. et al. (2017). Understanding the Small and Medium Multifamily Housing Stock. Report prepared by Enterprise Community Partners, Inc. and USC Price School of Public Policy. Available at <https://www.enterprisecommunity.org/resources/understanding-small-and-medium-multifamily-housing-stock-19423>.

^{xxxvi} Section 504 requirements apply to developers that receive federal financial assistance, such as Community Development Block Grant or HOME funds, for substantial rehabilitation (a project that has 15 or more units and the cost of the alterations is 75 percent or more of the replacement cost of the completed facility). Under these circumstances, a developer needs to make a minimum of 5 percent of units, or at least one unit, whichever is greater, accessible to persons with mobility disabilities and an additional 2 percent of units, or at least one unit, whichever is greater, accessible to persons with hearing or visual disabilities.

^{xxxvii} ICAST. Multifamily Green Rehabilitation Resource Guide. Available at www.icastusa.org/wp-content/uploads/2017/01/ICAST-Multifamily-Green-Rehab-Resource-Guide-Old.pdf.

^{xl} A national study conducted by FEMA noted that each dollar invested in pre-disaster mitigation leads to an average of \$4 in savings from avoided damages. These investments can also help lower energy use, reduce operational expenses, and lower insurance premiums.

^{xli} This tool will be made available on Enterprise Community Partners, Inc.'s website in Spring 2020.

^{xlii} Bay Area LISC and Build It Green. Green Rehabilitation of Multifamily Rental Properties: A Resource Guide. Available at www.novoco.com/sites/default/files/atoms/files/greenrehabmultifamilyrentals.pdf.

^{xliii} Jakobovics, A. et al. (2017). Small and Medium Multifamily Housing Units: Affordability, Distribution, and Trends. Report prepared by Enterprise Community Partners, Inc. and USC Price School of Public Policy. Available at www.enterprisecommunity.org/resources/small-and-medium-multifamily-housing-units-affordability-distribution-and-trends-19323.

^{xliv} Diaz, M. (2004). Assessing Property Management for Affordable Housing. Paper prepared for the Joint Center for Housing Studies of Harvard University. Available at www.jchs.harvard.edu/sites/default/files/w04-9_diaz.pdf.

^{xlv} LISC. (2001). Managing Small and Scattered Site Portfolios Workbook. Available at www.lisc.org/our-resources/resource/asset-and-property-management-workbooks.

^{xlvii} For more information about how to account for the full costs of maintaining a property over its lifecycle (i.e., a "lifecycle cost analysis" or "lifecycle underwriting") see The Lifecycle Cost Adjustment Methodology: An Exploration of the Baseline and Alternative Assumptions by the National Housing Conference: www.nhc.org/publication/the-lifecycle-cost-adjustment-methodology-an-exploration-of-the-baseline-and-alternative-assumptions/

^{xlviii} Diaz, M. (2004). Assessing Property Management for Affordable Housing. Paper prepared for the Joint Center for Housing Studies of Harvard University. Available at www.jchs.harvard.edu/sites/default/files/w04-9_diaz.pdf.

