LOW INCOME RENTAL

PRIORITIES

The overarching goal for the low-income rental market is to **ensure that non-student households are not paying more than 50% of their income in rent**, preferably not even paying 30%. The first priority in achieving this goal is to ensure that there is a sufficient supply of rental housing in the market to allow the market to properly function through moderate vacancy. **The priority must then be to substantially increase the number of units in the market that are affordable to households making less than $50,000 per year** (80% of median household income).

1. **For all new multifamily rental buildings proposed in the City of Madison that are well sited** for low-income populations (good access to transportation, schools, grocery), **integration of some affordable units should be encouraged**. As market rate projects begin the approval process, developers should be encouraged to include affordable units as part of their unit mix.
    a. Dedicate a larger portion of City of Madison funds to subsidize low-income rental units
        i. Further enhance TIF policy to subsidize the development of low-income rental units
        ii. **Strengthen, revise, and permanently fund the Affordable Housing Trust Fund**
    b. Explore ways to **give a preference in the development approval process to rental developments that include affordable units**
        i. Discount or exempt affordable units from density limits
        ii. Identify areas and zoning districts to encourage low-income rental development
        iii. Wave or reduce fees on affordable units
2. For the existing supply in the rental market, affordable subsidized units should be preserved and additional **units should be converted to affordable housing by purchasing land use restrictions**. Converting existing units is that fastest way to add affordable units to the market.
    a. Explore programs to subsidize landlords to designate existing units as affordable
        i. Place a land use restriction on units
        ii. Commit to affordable rents for 15 years
        iii. List units for rent on WIHousingSearch.org
3. **For new multifamily developments pursuing Section 42 tax credits, City funding programs should be aligned** to maximize the likelihood of tax credits being awarded. Coordinating these programs leverages City subsidy, making subsidy go farther or reach deeper down the income spectrum.
    a. Coordinate HOME, CDBG, TIF, Affordable Housing Trust Fund, and Project-based Voucher award timelines to ensure that projects have awards in place in time to apply for Section 42 tax credits in January
    b. Coordinate HOME, CDBG, TIF, Affordable Housing Trust Fund, and Project-based Voucher award criteria and processes so that projects that meet a common set of criteria that is in line with City and WHEDA priorities (good access to transportation, 3 bedroom units, walkability) get funded by the City and therefore score higher on their tax credit application
    c. Annually release the coordinated funding priorities to drive development that meets the criteria
    d. Actively recruit developers to apply for Section 42 tax credits in the City of Madison
4. **Pursue demonstration projects to test the viability of alternative housing forms** (Accessory Dwelling Units, Micro housing, Cottage Housing)
    a. Allow exceptions to existing funding programs and zoning rules to allow for demonstration projects
    b. Recruit developers with experience constructing alternate forms of housing
    c. Recruit financial institutions to create portfolio loan products that would allow for housing types that might not conform with currently lending rules

OVERVIEW

Since the beginning of the recession in 2007, the City of **Madison has experienced a continued rise in population and households that has outpaced its production of housing**. The resulting housing problem can be defined as an **undersupply of rental housing that is affordable to a range of household incomes, particularly to lower and moderate income wage earners** who get squeezed out of the market.

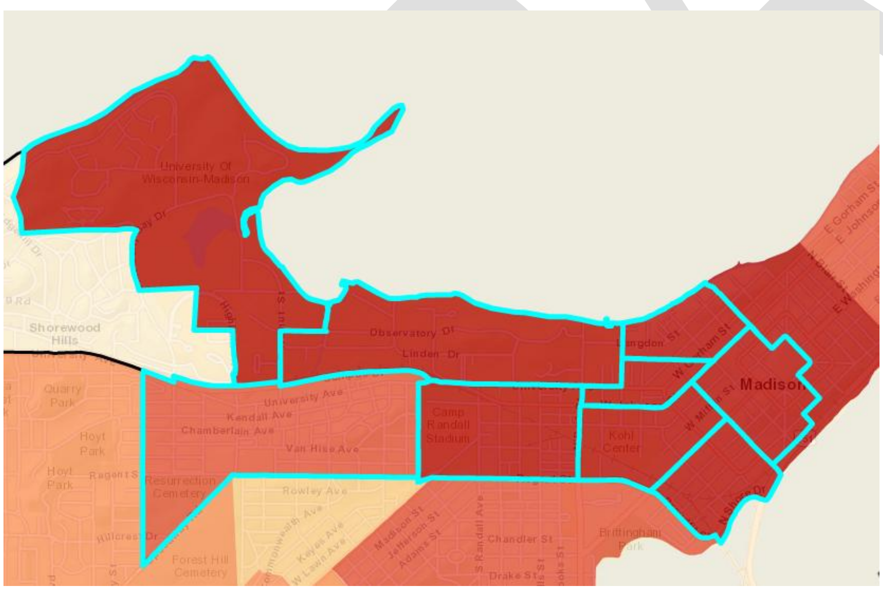
In response to this undersupply of residential rental housing, **the market has seen rents rise and vacancy rates fall**. Large affordability gaps exist between the rental payments a low-income household can afford and median rent price:

- A household must earn $35,000 annually in order to afford median monthly rents while allocating 30 percent of income to housing payments
- 35% of Madison households are unable to afford this payment
- Roughly 50% of Madison renters are housing cost burdened

As rents rise and vacancy rates fall, low-income households are increasingly priced out of Madison's rental market.

This gap must be examined with the understanding that Madison is home to a large population of college students, particularly in areas surrounding the UW Madison campus. Because their housing preference and income is substantially different from the general market, students are not included in this segment. To achieve this, renters from nine Census tracts have been removed from the data. These tracts were selected based on their proximity to the UW Madison campus, high concentrations of renters with incomes under 30% of AMI, and anecdotal evidence from landlords and UW Madison staff. For the purpose of this report, low-income rental exclude those nine Census tracts.

NOTE – These tracts have not yet been removed from the data



These tracts represent

- 12,000 Households
- 10,700 are renters
- 8,000 make less than 30% of AMI
- 6,500 are housing cost burdened renter making less than 50% of AMI
- 5,200 are severely housing cost burdened renters making less than 50% of AMI

Likely
Students

DEMAND

Typically for City of Madison programs, low income is defined as 80% of Area Median Income based on the number of persons per household. However because households rent in a market, competing against households of different sizes, for the purposes of this report demand for low-income rental housing is defined as household income of less than 80% of Area Median Household Income or roughly $50,000.

The most common professions with average incomes in this range include:

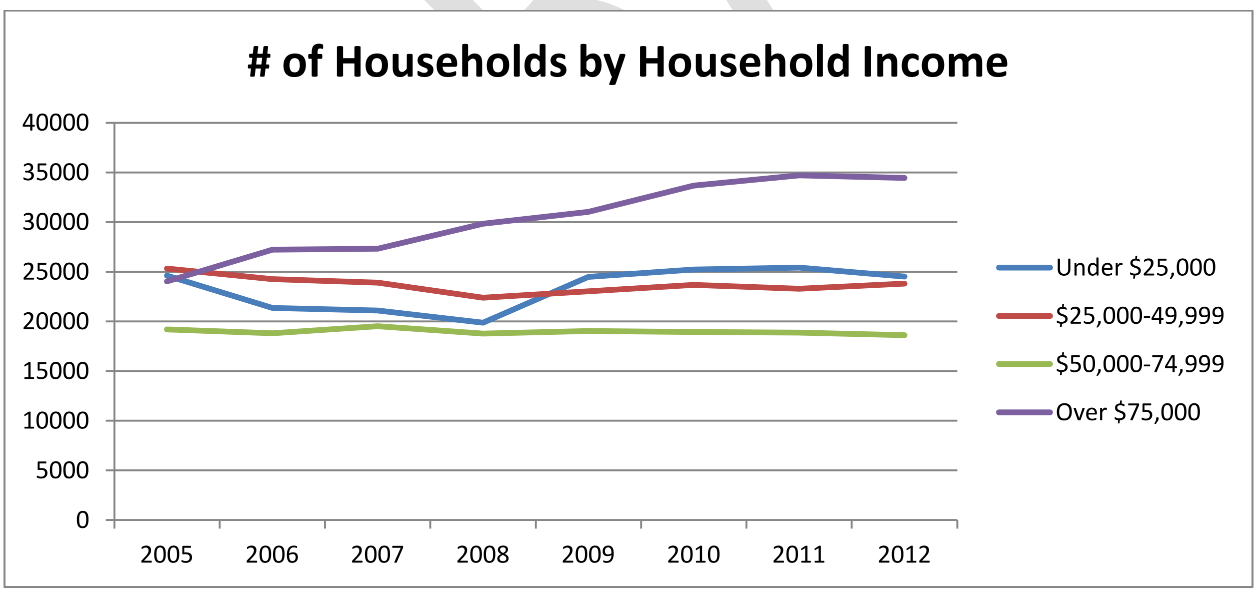
- Customer Service Representative - $33,940
- Cashier - $19,830
- Janitor - $25,800
- Laborer - $26,730
- Waiter/Waitress - $20,600
- Administrative Assistant - $35,340

Demand for this segment is also defined by the preference for rental rather than ownership. For this population, demand factors are strongly influenced by impediments to ownership including down payment and credit requirements.

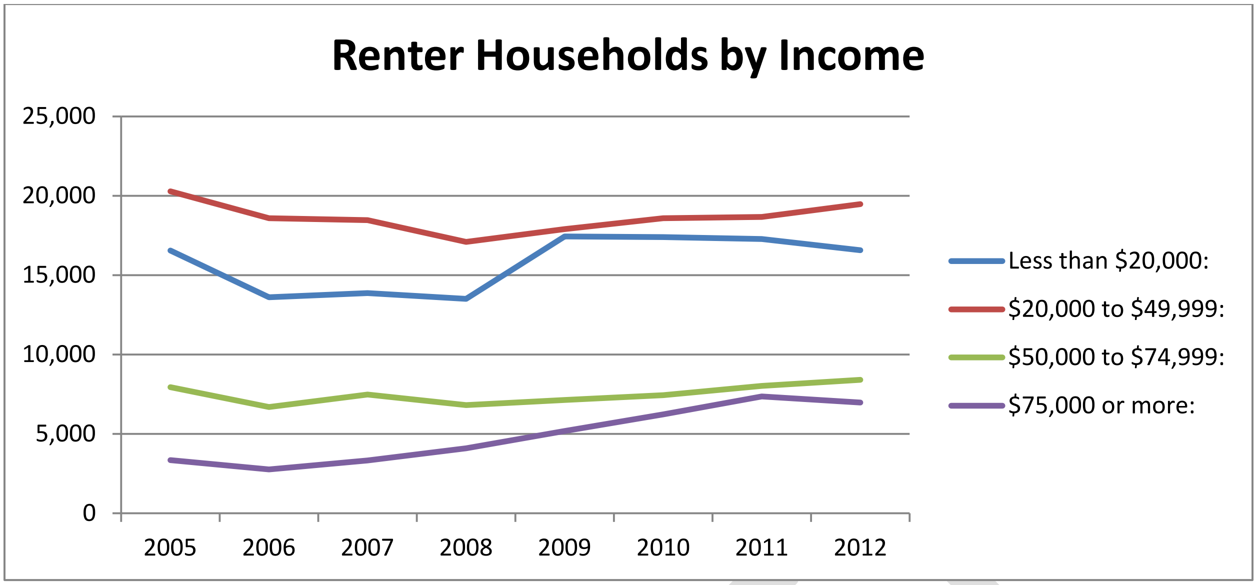
DEMOGRAPHICS

Since 2007, the City of Madison has added approximately:

- 9,500 new households
- **3,400 households with incomes below $25,000 (~40% of Median Household Income)**
- **-100 household with incomes below $50,000 (~80% of Median Household Income)**
- -900 households with incomes below $75,000 (~120% of Median Household Income)
- 7,100 households with incomes above $75,000 (~120% of Median Household Income)



Source: 2012 3-Year American Community Survey



Source: 3-year American Community Survey

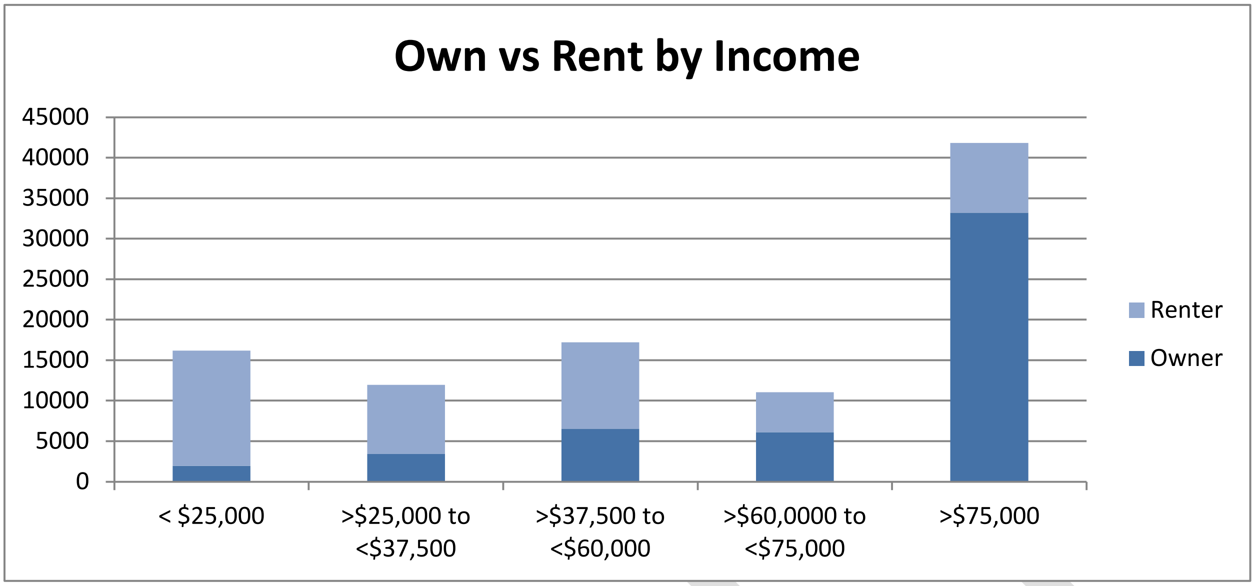
The income pattern of renter household in the City of Madison shows that almost all growth comes from renters with low incomes (under 80% of Area Median Household Income) and high incomes (over 120% of Area Median Household Income).

Since 2007, the City of Madison has added approximately:

- 8,300 new renter households
- **2,700 households with incomes below $20,000 (~30% of Median Household Income)**
- **1,000 household with incomes below $50,000 (~80% of Median Household Income)**
- 1,000 households with incomes below $75,000 (~120% of Median Household Income)
- 3,600 households with incomes above $75,000 (~120% of Median Household Income)

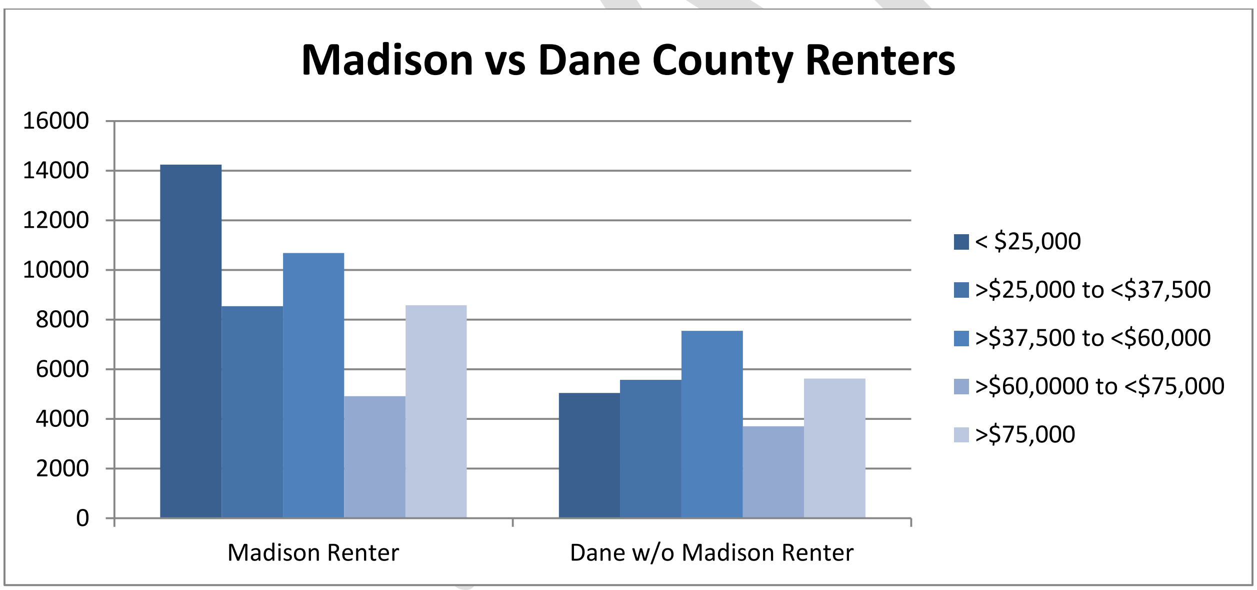
The rental market has absorbed almost 90% of households added to the city since 2007.

A snapshot of the Madison market shows that **the majority of low-income households rent rather than own their housing.** At the same time**, over half of renters are low to moderate income households**.



Source: 2006-2010 CHAS – HUD

The income pattern of renters in Madison is virtually identical to that of Dane County, with the largest block at $37,500 - $60,000 (60-100% of Median Household Income). (When students are removed)



Source: 2006-2010 CHAS - HUD

TRENDS

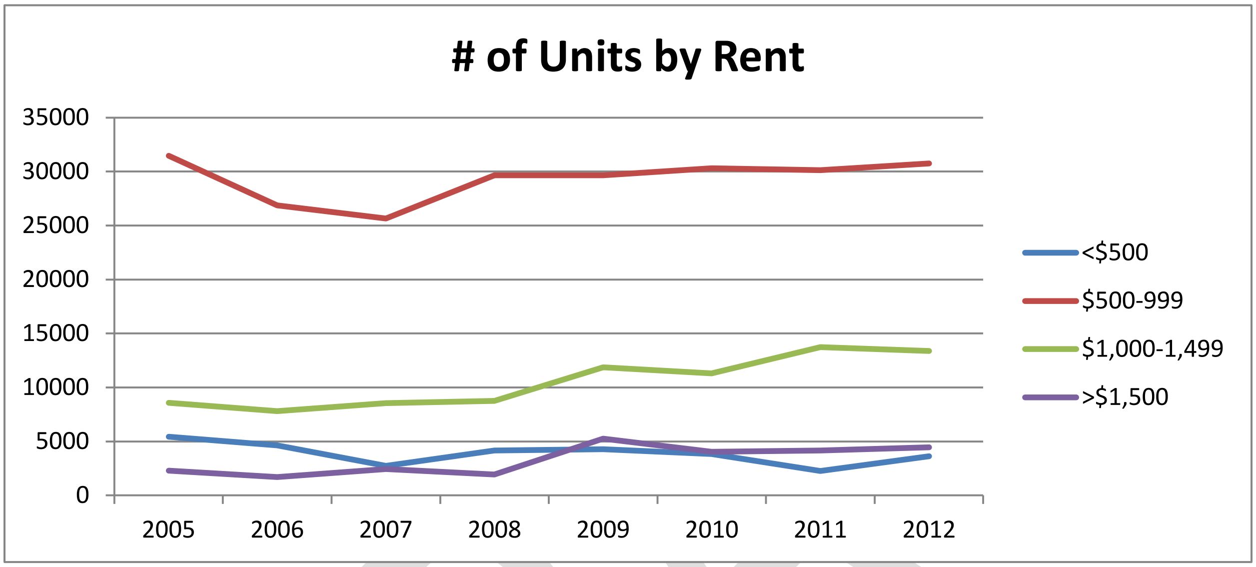
- Madison's population **growth is fueled by households on the bottom (<$25,000) and top (>$75,000) of the income spectrum**
- **Madison's rental market is currently dominated by households at the lower half of the income spectrum**

SUPPLY

The supply of rental housing in the City of Madison has seen a sizable increase in recent years with much more in the pipeline, however only a fraction of that is targeted towards low-income households.

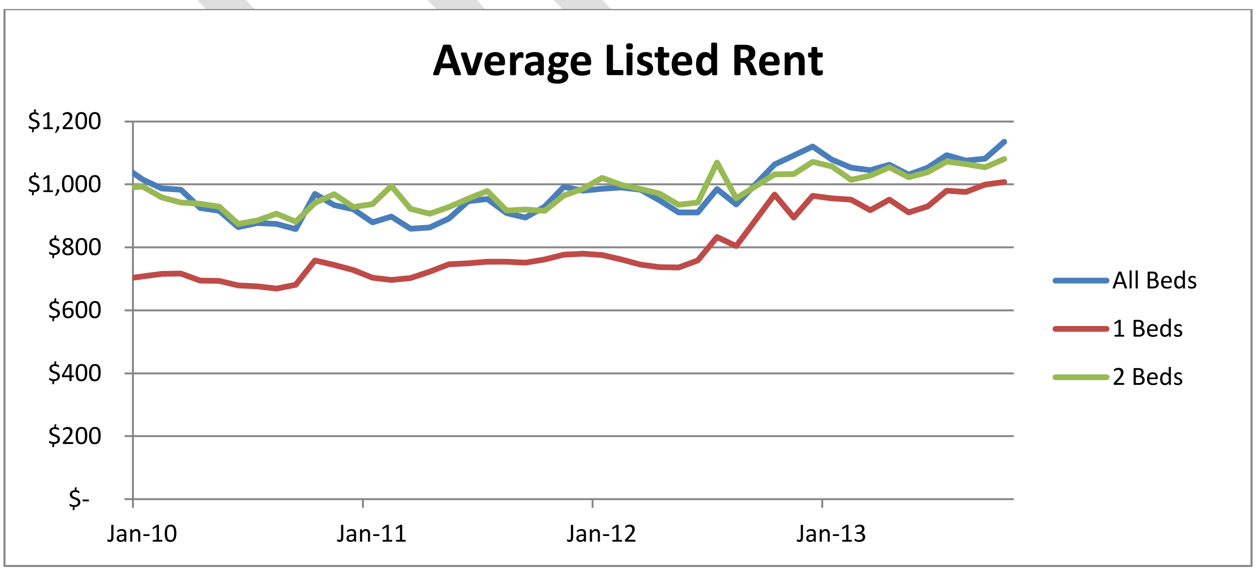
RENTS

A household with income of $40,000 (80% of Household Median Income) can afford rent of roughly $1,000 per month and a household at $25,000 (40% of Household Median Income) can only afford $600 per month. Since 2007, **virtually all increase in supply has been in units unaffordable to households making less than $40,000 (~60% of Household Median Income).**



Source: 1 Year American Community Survey

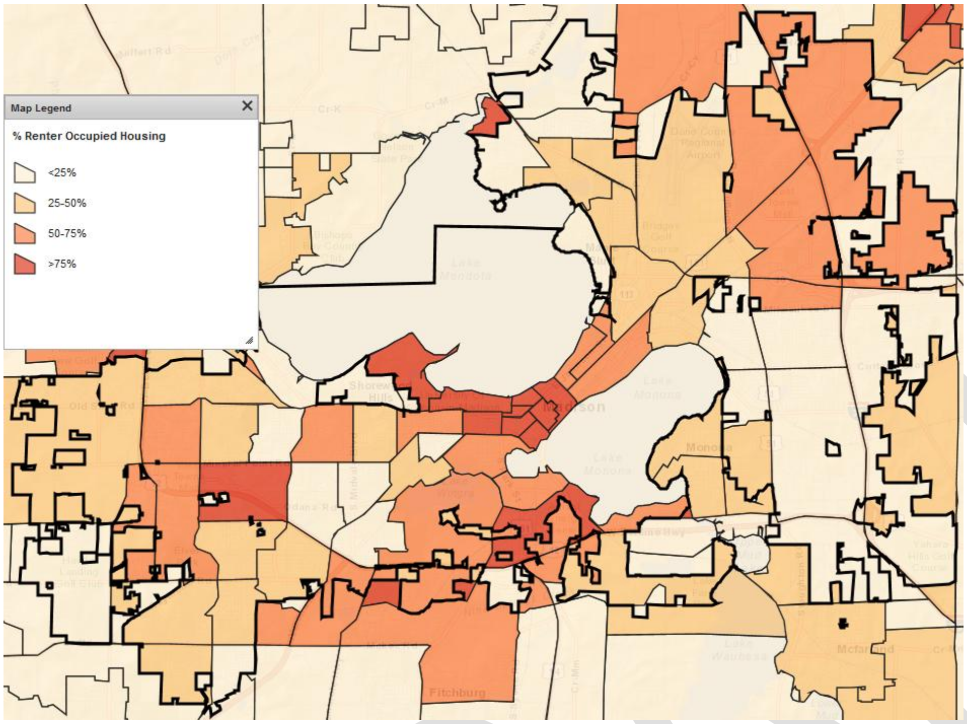
Market rents for one and two bedroom apartments have increased significantly in recent years, particularly since mid-2012 according to data from rentjungle.com an aggregator of online rental listings. This increase is especially apparent in **the market for one bedroom units, which has seen a 30% increase in average list price since the beginning of 2012**.



Source: rentjungle.com

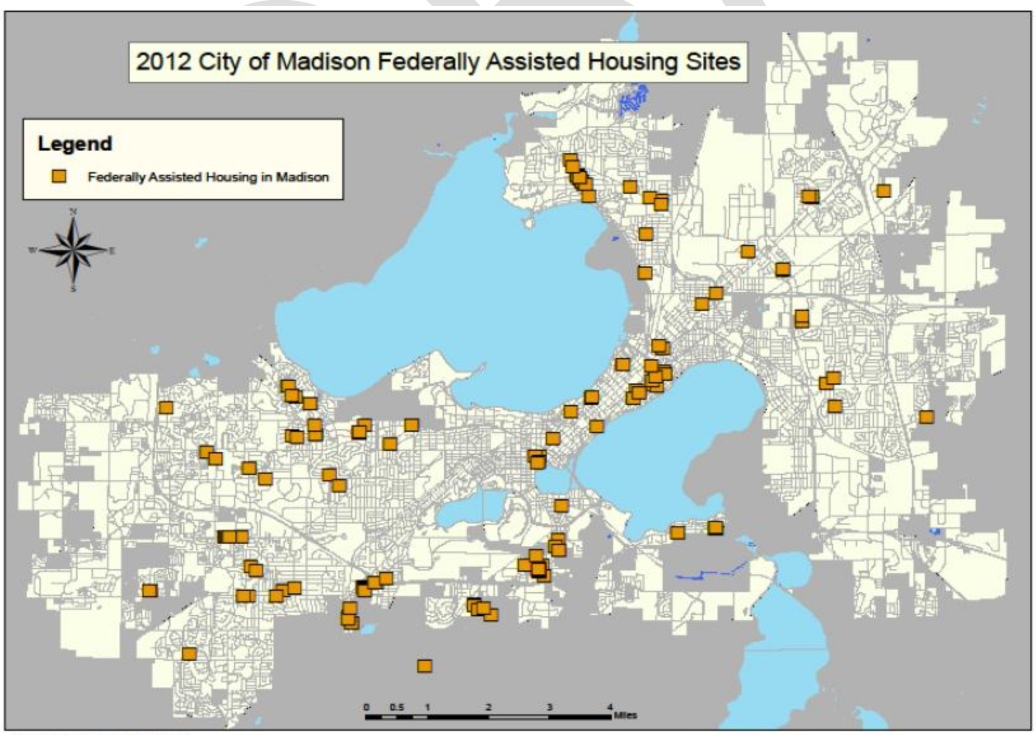
LOCATION

In the City of Madison, rental housing is concentrated in the downtown core, campus, south side, north east, and west sides of the city.



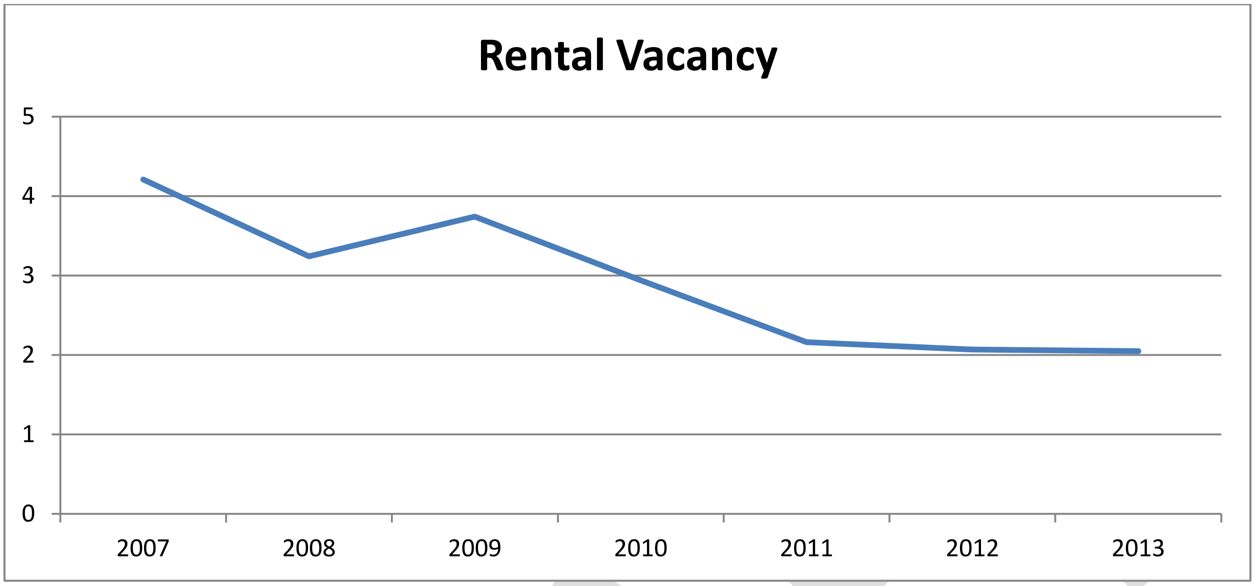
Source: HUD CPD Maps

Federally subsidized low-income housing is more evenly dispersed across the city. However, individual sites can contain dramatically different numbers of subsidized units.

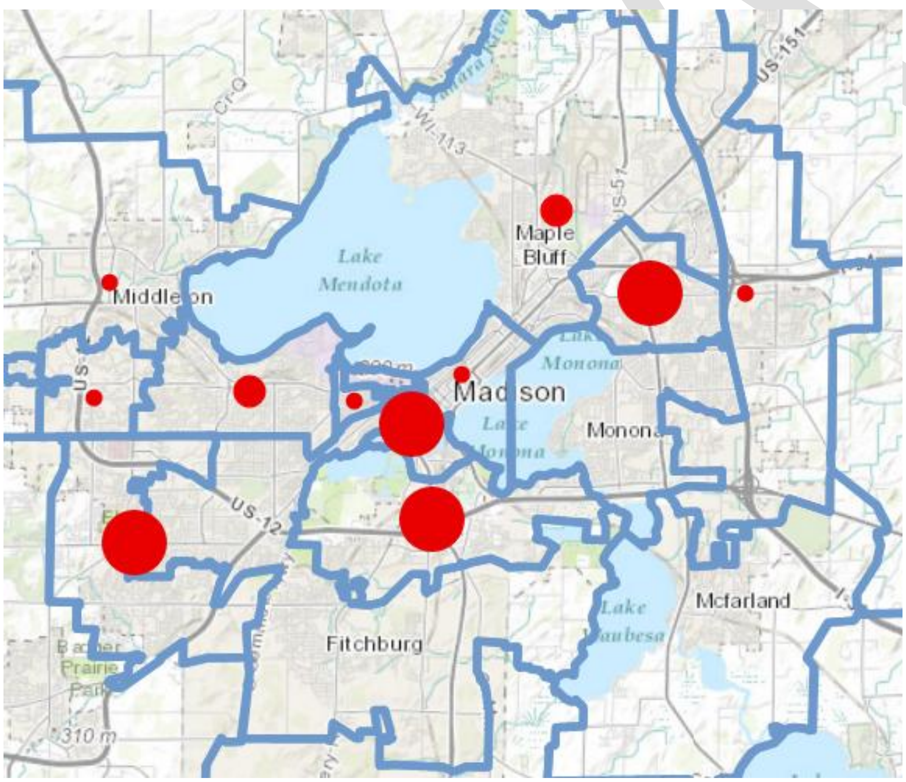


VACANCY

Vacancy in the Madison rental market has been at or near historic lows for a number of years, implying that **the market is undersupplied.** In the United States, the typical rule of thumb is that a 5% vacancy rate is needed to maintain stable prices.



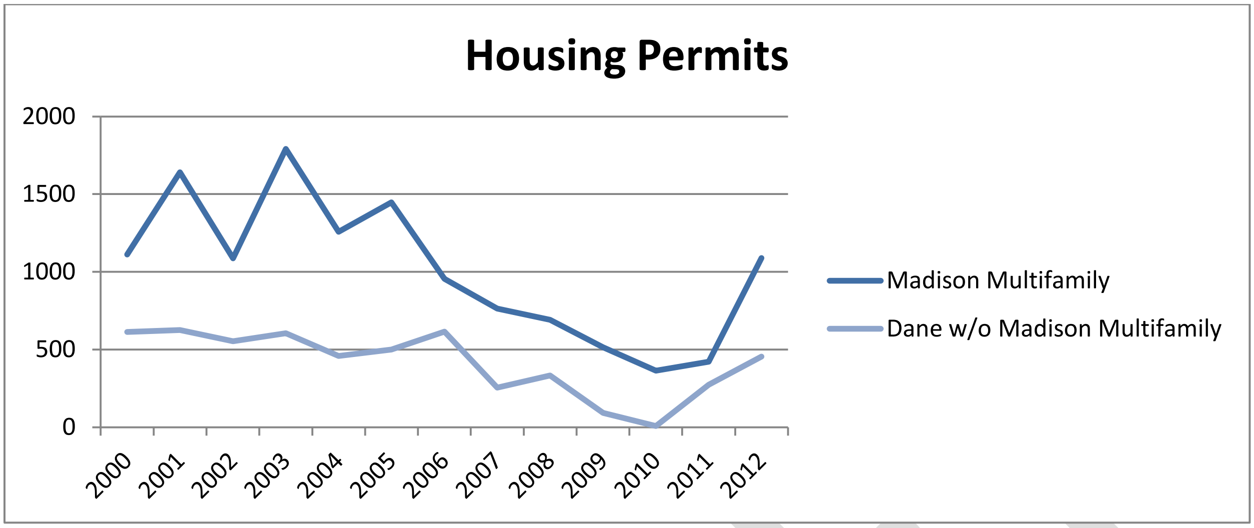
Vacancy is not evenly dispersed in the Madison market. The southwest, south, and east side have moderate vacancy of 3-4%. The west, far east, and downtown markets have vacancy rates as low as .5%.



Source: MGE Multifamily Vacancy

NEW SUPPLY

The market has responded to the forces of rising rents and lower vacancy with a return to 2000-2005 levels of permits for multifamily units for both Madison and Dane County.

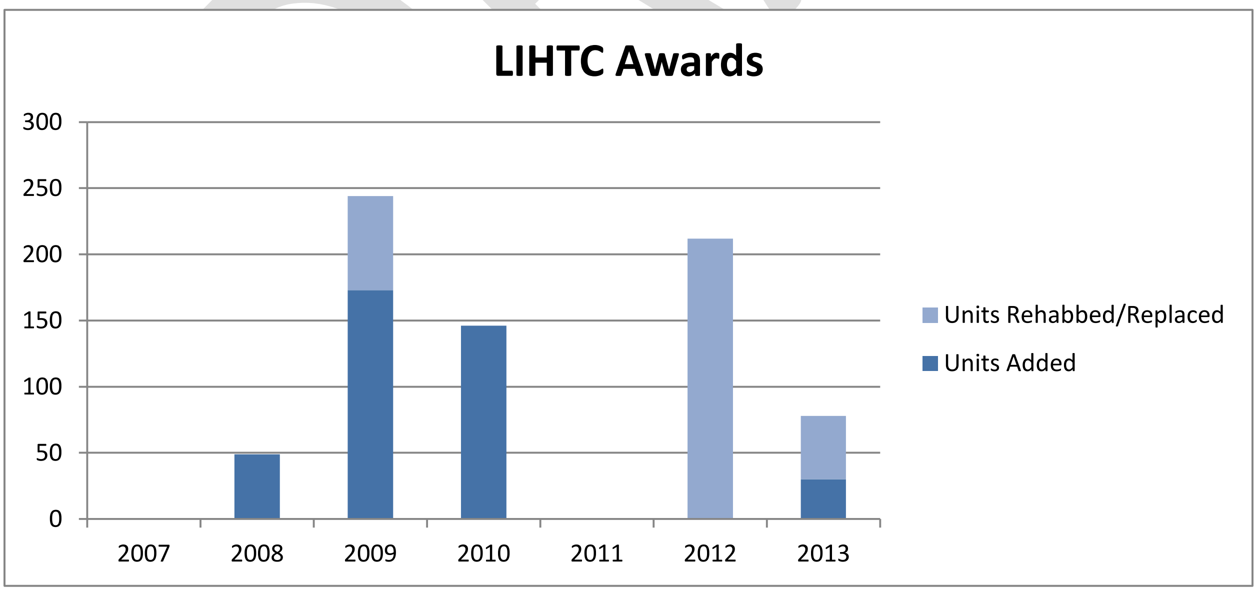


Source: Census Building Permits Survey

The City of Madison saw a significant increase in multifamily rental units in 2013 with:

- Projects Complete: 647 residential units
- Under Construction: 814 residential units
- Approved: 1287 residential units
- Major Pipeline Projects: 899 residential units
- TOTALS: 3,647 residential units

These units have yet to have a significant effect on the vacancy rate or median rent price.



Section 42 tax credits have been a large, but inconsistent, driver of new affordable supply added to the market.

FINANCE/FUNDING

NATIONAL

The majority of funding for low-income rental is in the form of traditional commercial mortgages and investor equity, while the majority of subsidy comes from the US tax code and the US Department of Housing and Urban Development (HUD).

CONSTRUCTION/REHAB

Because low-income housing inherently has reduced income streams, new construction is typically financed with relatively high levels of subsidy and equity rather than debt. New supply is funded by a combination of debt, investor equity and:

- Low Income Housing Tax Credits (LIHTC)
  - In Wisconsin credits are awarded by WHEDA according to its Qualified Allocation Plan which is updated on a biennial basis
  - Credits are converted to cash equity by a direct buyer or syndicating partner
  - After syndication, funds typically cover 70% of building cost
  - Annual competitive process to secure, very complicated
  - While small of amounts of LIHTC (4% credits) are available on a non-competitive basis to project financed with tax-exempt bonds, more units are created with the more robust competitively awarded 9% credits
  - The maximum award per development $8,500,000 in credit, with no limit on the maximum number of units
  - Can be used for permanent or transitional housing, typically not shelter
  - Can be used in new construction and acquisition/renovation
  - Requires occupants to earn less than 50% or 60% AMI with incentives to reach lower income populations
  - Requires property to stay affordable for 30 years
  - Requires property to pay property taxes
- HOME Funds
  - The City of Madison received $991,841 in FY2013
  - HUD funds awarded to state and cities for the creation of affordable housing
  - Deferred loan product
  - Administered by the City of Madison Community Development Division
  - Can be used in new construction and acquisition/renovation
  - Requires 90% of benefiting families have incomes under 60% AMI and in rental projects with five or more assisted units, at least 20% of the units must be under 50% AMI
  - Requires a match every dollar of HOME funds used (except for administrative costs) with 25 percent from nonfederal sources, which may include donated materials or labor, the value of donated property, proceeds from bond financing, and other resources
  - Requires units stay affordable for 20 years for new construction of rental housing
- Freddie Mac
  - Offers securitized debt products to the multifamily market
  - Goal of reducing interest rates and increasing housing supply through providing stability and liquidity to the multifamily loan market
- Federal Home Loan Bank AHP
  - Typically $18,000 per unit
  - Competitively awarded forgivable loan
  - Can be used for apartments, SROs, and transitional housing
  - Requires at least 20% of building occupants to earn less than 50% AMI

OPERATIONS & RENT SUBSIDY

When there are federal and city programs that subsidize the cost to build low-income housing, rents are often locked at lower than market rates and owners are required rental to income qualified tenants. Alternately, federal programs can directly subsidize units by providing rent subsidy programs where tenant pays what they can afford and the federal program pays the difference between market rent and the tenant's portion.

- Housing Choice and Project Based Vouchers
    - Serves low-income families, the elderly, and persons with disabilities
    - Participants rent from private landlords
    - 1,816 vouchers are allocated to the CDA
    - Because of HUD funding constraints 1,594 in use
    - Tenants pay 30% of their income
    - HUD funded
- HUD - VASH
    - Serves chronically homeless veterans
    - Participants rent from private landlords
    - 110 vouchers are allocated
    - Tenants pay 30% of their income
    - HUD funded rent subsidy and VA funded services
- Public Housing
    - Federal contract administered by CDA
    - Approximately 800 apartments owned and managed by CDA
    - Tenant pays 30% of income and the federal government provides the difference between estimated operating costs and the tenant paid portion

LOCAL SOURCES

- Affordable Housing Trust Fund
    - City of Madison funded endowment for the creation of affordable rental and owner-occupied housing administered by the Community Development Division
    - Balance of over $3 million with disbursements limited to 25% of the balance
    - Provides installment loans and grants to for-profit and non-profit housing developers for acquisition/rehab, new construction, and up to 15% for soft costs
    - Requires at least 60% of the funds eligible for disbursement annually be used to create units for occupants who earn less than 60% AMI
    - Requires occupants to pay no more than 30% of gross household income at 60% AMI in rent
    - Requires units stay affordable for 30 years
- Tax Incremental Financing (TIF)
    - City of Madison funded program that uses projected future increases in the property taxes from a defined area (TID) to subsidize redevelopment in that TID
    - Project must be located in a TID with a "generator" property that is sufficient to increase the tax base
    - Project must prove that "but for" the subsidy the development would not occur
    - Affordable housing for renters under 80% AMI is an allowable use of funds
    - Can be used for capital costs but not for operating expenses
    - Project must pay property taxes
    - Recent changes in state law allow for the Tax Incremental Districts to be extended for one year for the purpose of use the funds for affordable housing within a municipality

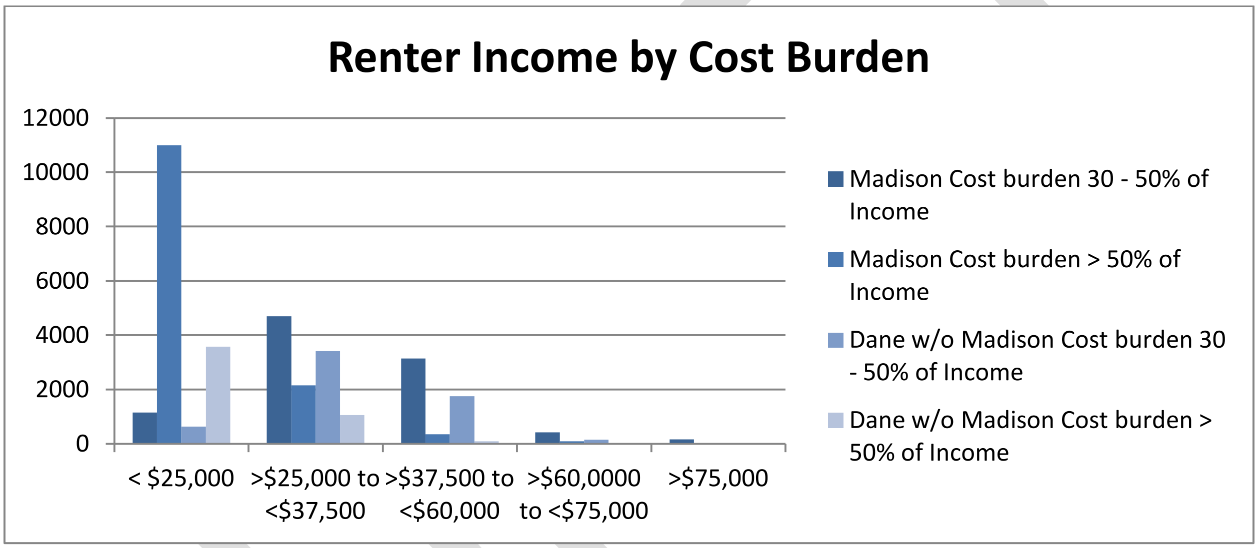
CHALLENGES

The supply of rental units affordable to low-income households and the demand for these units does not align. **There is a large persistent gap in the number units that are affordable to low income residents, as shown by the large number of low-income renters that are housing cost burdened**. This problem is further exacerbated by the low vacancy rate, which puts additional pressure on the low end of the market.

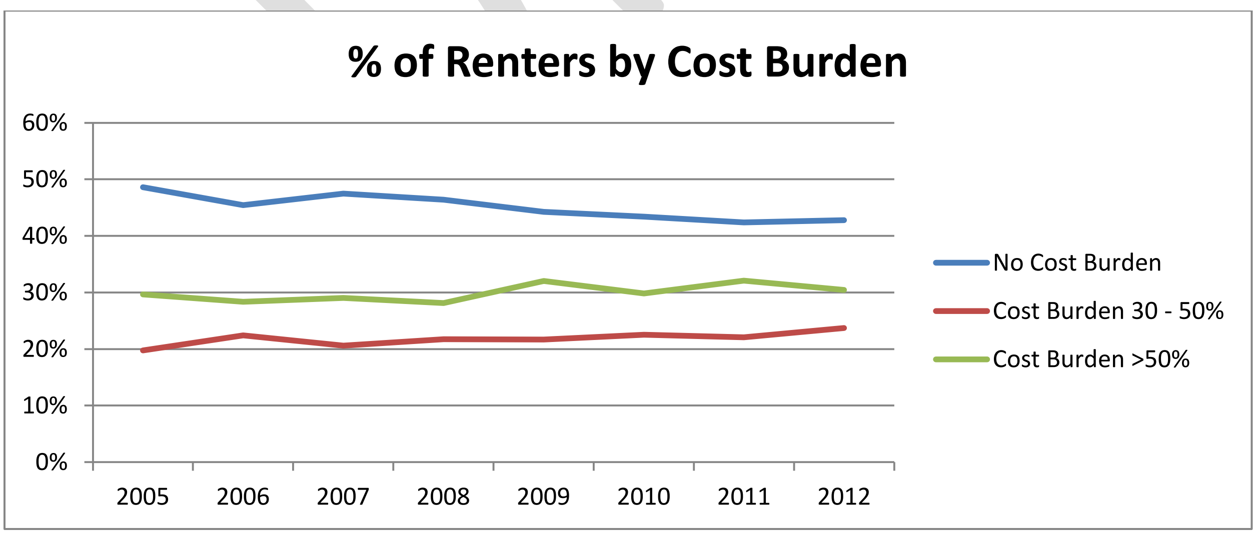
HOUSING COST BURDEN

The percentage of cost burdened renters has slowly risen since 2005.

- **A slight majority of renters pay more than 30% of household income in rent (cost burdened)**
- **Cost burden is particularly prevalent amongst renters with income of less than $37,500 (~60% of Household Median Income)**
- **Households with income of less than $25,000 (~40% of Household Median Income) often pay more than 50% of household income in rent**



Source: 2006-2010 CHAS - HUD



Source: 3 Year American Community Survey

MARKET FORCES

The main challenge to creating additional units of rental housing affordable to low income households is that in our market **it costs more to build a unit than can be covered by rents that would be considered affordable to low income renters.**

For example for a typical one-bedroom unit:

Construction and Land Cost	$125,000

Loan-to-Cost Ratio	20.00%	Loan-to-Cost Ratio	80.00%
Required Equity	$25,000	Mortgage Loan	$100,000
Annual Pre-Tax Distribution Rate	10.00%	Mortgage Interest Rate	5%
Cash Payments for Equity	$2,500	Cash Required for Debt Service	$6,250

Net Operating Income	$8,750
Operating Expenses	$2,500
Real Estate Taxes	$2,000
Replacement Reserve	$300
Effective Gross Revenues	$13,550
Vacancy Loss (5%)	$675
Gross Potential Income	$14,225

Breakeven: Annual Rent Per Unit	$14,225
Breakeven: Monthly Rent	$1,185

The cost to build a one-bedroom unit without subsidy would requires rents of $1,185 per month to cover expenses, debt service, and a modest return on equity, which is unaffordable to single person below 80% of AMI.

Household Size	100% of AMI	Affordable Monthly Rent by Household Income						
		90% of AMI	80% of AMI	70% of AMI	60% of AMI	50% of AMI	40% of AMI	30% of AMI
1 person	$1,418	$1,276	$1,128	$992	$851	$709	$567	$425
2 persons	$1,620	$1,458	$1,289	$1,134	$972	$810	$648	$485
3 persons	$1,823	$1,640	$1,450	$1,276	$1,094	$911	$729	$546
4 persons	$2,023	$1,820	$1,610	$1,416	$1,214	$1,011	$809	$606
5 persons	$2,185	$1,967	$1,740	$1,530	$1,311	$1,093	$874	$655
6 persons	$2,348	$2,113	$1,869	$1,643	$1,409	$1,174	$939	$704
7 persons	$2,510	$2,259	$1,998	$1,757	$1,506	$1,255	$1,004	$753
8 persons	$2,670	$2,403	$2,126	$1,869	$1,602	$1,335	$1,068	$801

SOLUTIONS

LOCAL

- Large increase in apartment construction
  - Since 2012, the Madison rental market has seen a boom in construction of new units
  - While most projects are not targeted at low income renters, the volume of units in the pipeline should provide relief from the historically low vacancy rate which pushes rents up
  - 2013 Projects
    - Projects Complete: 647 residential units
    - Under Construction: 814 residential units
    - Approved: 1287 residential units
    - Major Pipeline Projects: 899 residential units
    - TOTALS: 3,647 residential units
- City of Madison Community Development Block Grant Funding
  - The CDBG committee funds a number of new apartment developments targeted towards low-income renters every year with the goal of improving and expanding affordable housing options throughout the city
  - 2013 funding created 18 rental units and 154 households received rental assistance
  - 2014 Commitments
    - Tennyson Ridge
      - To be developed by Lutheran Social Services
      - 72 affordable units including 1,2, and 3 bedrooms
      - $500,000 from the Community Development Division Housing Development Reserve Fund
      - $295,000 from the Affordable Housing Trust Fund
      - Applying for Section 42 tax credits
    - Pinney Lane Apartment - Royster Clark
      - To be developed by Stonehouse and Movin' Out
      - 59 Affordable unit including 1,2, and 3 bedrooms
      - 25% of the units will be affirmatively marketed for people with disabilities
      - $128,318 2012 HOME rental development funds
      - $265,841 in Housing Development Reserve funds
      - $265,841 from the Affordable Housing Trust Fund
      - Applying for Section 42 tax credits
      - Also receiving $400,000 in TIF funds
- City of Madison Community Development Authority
  - The CDA is currently working to add 8 new units and replace 40 units at its Truax location
- TIF Policy Changes
  - The City of Madison is revising its TIF policy to specifically assist projects that target low-income residents. The guidelines allow funding of residential real estate projects in which no less than 40% of the units are affordable to households making less than or equal to 40% of Area Median Income (AMI). Underwriting will be based on the WHEDA Low Income Housing Tax Credit application criteria

NATIONAL MODELS

Communities across the nation have applied different policies, funding models, and processes to increase the supply of low-income rental housing. Some models are less effective, would not apply well to the Madison market, or may not be permitted under current state law.

INCREASE SUPPLY

To address the needs of low-income renters, most communities rely on programs and policies that focus on increasing the supply of housing that is affordable for them. Most common is to focus on creating units specifically targeted at low-income households, which can be done through:

- Construction Subsidy
    - At its core, this strategy involves making Section 42 tax credits, Affordable Housing Trust Funds CDBG, HOME, TIF, and other local funds available to assist developers in construction of low-income units.
    - Communities can go a step further and coordinate internal processes, eligibility criteria, timelines, and approvals in a one-stop-shop to maximize the potential of projects to stack subsidies.
- Inclusionary zoning
    - Require a given share of units in new construction developments to be affordable to people with low to moderate incomes
    - A portion of the City of Madison's Inclusionary Zoning Ordinance was struck down by the courts in 2006 and a portion was repealed years later.
- Reduce Fees
    - Communities can reduce or waive the host of fees charged to low income housing developments as part of the development process which can add up to tens of thousands of dollars
    - The City of Longmont, California waives up to 14 fees for low income units averaging $2,283 per apartment
    - In the City of Madison, typical fees include:
        - Plan Examination Fee $ .03/sqft
        - Permits
            - Demolition $600
            - Plumbing - Based on floor area
            - Electrical – Based on floor area
            - Erosion Control $100
        - Inspection Fee $ .32/sqft
        - Conditional Use $950
        - Parks Fees up to $2,461.95 per unit
- Density Bonuses
    - Projects are allowed to exceed density or height limits normally allowed by zoning if the units are designated as low-income
    - For example zoning that normally allows for 24 units could be granted an additional 6 units if they are designated affordable without having to seek conditional use allowances
    - King County, WA allows projects to discount affordable units against density limits up to 150% of the normal unit limit
- Geographic Targeting
    - As part of the comprehensive and neighborhood planning process, zoning districts and areas within each neighborhood could be designated as appropriate for low-income housing development to drive low-income development to these areas
    - Zoning rules can be modified to facilitate low-income rental development in designated districts and subsidy can be targeted at projects that fall within the designated areas
    - The Wisconsin Housing and Economic Development Authority awards bonus points on Low-Income Housing Tax Credit applications to projects that are in Census tracts that they have designated as in high need of affordable rental housing

- Vancouver Model
    - The City of Vancouver has one of the tightest rental markets in Canada with less than a 1% vacancy as a result the City has implemented two policies to increase rental housing supply
        - A required 1-for1 replacement policy for any demolition of rental housing
        - Fast track city approvals for development that are 100% rental housing with relaxed zoning requirements and density bonuses
- Micro Housing Units
    - Densely configured very small studio units designed to serve single adults
    - The density and small size allows developers to build units in markets with high land costs at a lower cost than traditional apartments
    - Gaining popularity in New York, San Francisco, and Seattle where land costs are very high
    - Typically defined as studio units under 400 square feet, but can be as small as 150 square feet
    - Difficult to build in Madison because of restrictions on unit density (not minimum square footage requirements) in the zoning code
- Accessory Dwelling Units
    - A housing unit created within a building or as a separate structure that's use is clearly incidental to that of the main building and which is located on the same lot as the principal building, and is subordinate to the principal building in height and floor area.
    - Can come in the form or a basement apartment, carriage house, or garage apartment.
    - The increased density on the parcel allows for reduced housing cost
    - The State of Florida requires by statute that ADU's be rented at rates affordable to low-income households
    - Allowed in select zoning designations within Madison
    - Challenge in financing their creation because they are not allowed by many common mortgage products

Supply can also be created within existing buildings by reducing rent rates through direct subsidy or by reducing building operating costs.

- Conversion
    - Units located in a multifamily rental or ownership housing complex are converted from market rate non-affordable to affordable rental through the purchase of affordability restrictions.
    - The State of California allows public funds to be used by local governments to fund the conversion of existing units to meet housing targets.
        - Converted units must result in a net increase in the stock of housing affordable to low- and very low-income households
        - Converted units must be made available for rent at affordable housing costs, not be currently occupied by low- or very low-income households, and in decent, safe and sanitary condition when occupied
        - Long-term affordability covenants apply to these units
- Rent Subsidy
    - Like the Housing Choice and Project Based Voucher program, state and local governments can choose to directly subsidize rent in units for low-income households
    - Minnesota has a program to directly subsidize rent for those at risk of homelessness
- Reduce Property Taxes
    - Property taxes are the most direct cost that local governments impose on the operation of buildings including low-income housing
    - Depending on state law, local governments can adjust assessments or reduce property taxes for housing contingent on the affordability of rents charged
    - Cook County Illinois systematically phased in property tax reductions for multifamily rental properties by roughly 10% to bring assessments more in line with other residential buildings
    - Wisconsin's rules on equalized values limit the amount that assessments can be adjusted
- Rent Control and Rent Stabilization
    - Laws which limit the changes that can be made to rents in a building functioning as a price ceiling
    - Goal of limiting the price that would result from market forces, where inequality of bargaining power between landlords and tenants produces continually escalating prices
    - Can have the effect of creating shortages and exacerbate scarcity in the housing market
    - Illegal in Wisconsin

REDUCE DEMAND

- Increase Household Income
  - Rather than increase the number of rental units affordable to low-income households, reducing the number of low-income households by raising incomes or the number of wage earners per household would have similar results.
  - For example, raising income from minimum wage of $7.25 to $12.00 would bring a two-income household from 50% of median area household income to 80% of median area household income and increase the amount of rent they can afford to pay from $750 per month to $1,250 per month.
  - The Wisconsin Housing and Economic Development Authority awards bonus points on Section 42 tax credit applications for projects that are located in census tracts that are near employment centers to tie housing to employment opportunities.