Income Limits WORKING GROUP™
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March 25, 2022

Secretary Marcia L. Fudge
U.S. Department of Housing and Urban Development
451 7th Street, S.W.
Washington, DC 20410

Re: Comments on the Effects of 2020 American Community Survey Data Issues

Dear Secretary Fudge:

On behalf of the members of the Income Limits Working Group, and four national affordable housing organizations, we appreciate the opportunity to comment on the impact to the 2023 income limits due to the data issues with the 2020 American Community Survey (ACS). The members of the Income Limits Working Group are stakeholders in the affordable housing community who work together to help resolve technical issues involving HUD's income limit policies. Our group includes nonprofit and for-profit developers, syndicators, investors, lenders, lawyers and other affordable housing professionals. Income limits are a critical part of the low- income housing tax credit (LIHTC) and residential rental tax-exempt private activity bond programs. U.S.Department of Housing and Urban Development (HUD) income limits are used both for determining who qualifies to live in LIHTC housing and how much tenants pay to rent that home.

Due to collection and data issues related to COVID-19, the U.S. Census Bureau did not release one-year ACS data for 2020. The 2020 ACS data would typically be used by HUD to calculate Fiscal Year (FY) 2023 income limits for areas that have a reliable one-year ACS estimate.

Historically, when a reliable one-year ACS is not available, a five-year ACS is used in its place. However, research conducted by the Income Limits Working Group shows that shifting from a one-year ACS to a five-year ACS will result in a large decrease in income limits for many areas.[1] In addition, the shift back from the five-year to a one-year ACS will result in a large jump in income limits the following year.

Similar to why HUD implemented caps and floors on income limit changes in 2010, it is in the best interest of tenants and landlords to avoid large swings in income limits from year to year.

Impact to Prospective Tenants

A lower income limit would have a negative impact on residents trying to qualify for affordable housing. Using 2019 as our reference year, the one-year ACS median family income estimate for the United States was $65,712, which HUD considers a four-person household. The five-year ACS median family income estimate for the United States was $62,843. The majority of the LIHTC units are restricted at 60% of median income, so if we adjust these estimates to 60% median incomes, we would arrive at a

[1] Stagg, Thomas. (2021, October 25). Income Limits Could Be 3.5% Lower in 2023. Notes from Novogradac. https://www.novoco.com/notes-from-novogradac/income-limits-could-be-35-lower-2023

60% national income limit of $39,420 for a family of four based on the one-year ACS and a 60% national income limit of $37,680 for a family of four based on the five-year ACS.If we assume an even population distribution, the Current Population Survey (CPS) for 2019 estimates that 1.27% of households would fall between these two income limits. If we extrapolate that out to the entire U.S. population, there would be approximately 1.5 million households that would no longer qualify for housing using the five-year ACS data.

One member of the working group analyzed its portfolio using the 5-year ACS median income instead of the 1 year and determined the following:

Out of a portfolio of 25,701, 2,370 households, current lease holders (or 9.2%) would not have been able to qualify for residency in their home based on their income at move-in. Additionally, 1,763 dependents of these leaseholders would be affected, resulting in a total impact of 5,100 residents, or 19.8%, without affordable housing.

Not surprisingly, the impact of change disproportionately affects people of color and women as follows:

- 90% are Female or BIPOC,
- 67% are BIPOC,
- 66% are Female,
- 40% are Female and BIPOC,
- 26% are Senior (55+)

What this means prospectively is that access to affordable housing, which is already in short supply, willlikely be even more difficult to obtain for almost 10% of the population that currently qualifies for residency in LIHTC properties. Furthermore, those impacted are likely to be women and BIPOC populations, further exacerbating already challenging equity issues facing the nation.

Impact to Property Owners

LIHTC and tax-exempt private activity bond properties are unique compared to other federal programs as their rent limits are directly impacted by the income limits for the area. Once a property is placed in service, their gross rents are held harmless from decreases. However, income and rent limits are not held harmless for properties that are not placed in service. A decrease in rents, in contrast to actual income increases, will impact each property type differently.

<u>Existing Properties</u>

Existing properties are held harmless for decreases in gross rent under Internal Revenue Code Section 142.However, flat rents are still detrimental to a property's ability to cover operating expenses and debt service, especially in high inflationary times like we are currently experiencing. Furthermore, some expenses, such as insurance, are increasing in exponential ways. For 2021, inflation was 7% and Income Limits Working Group members are reporting that they have seen increases in operating expenses across their portfolios.

One working group member provided the following analysis of cost increases across their portfolio:

Total average expenses per unit have increased by compound 6.6% between 2018 and 2021. Moreover, the single year annual growth in expenses between 2020 and 2021 is 11%. Over the same 4-year period, utility costs (which represent 20% of overall costs) increased 5% and insurance costs (which represent 18% of the overall cost per unit) have increased 18.5%. Owners have little choice other than to control the costs they can control, like payroll, which in this case increased 3.8% over the same time frame and represents 24% of the total per unit costs. The ability of property managers to compete in the current constrained labor force continues to put pressure on that cost as well. In addition, owners can only constrain costs for so long before the cost constrains lead to deferring critical maintenance that lessens the quality of the affordable homes.

In addition, it is only the gross rent limit that is held harmless. The rents collected from tenants are reduced by a utility allowance. As noted above, inflation is impacting utilities, and therefore utility allowances, and that, in turn, will put even more pressure on a property's ability to cover operating expenses.

Finally, as outlined above, the properties would have a harder time finding qualified tenants if income limits are held flat when actual incomes are increasing.

<u>New Properties Placed in Service in FY 2023</u>

Of significant concern is the impact of an abnormally depressed rent level on the critical affordable housing units currently in the development process. Properties placed in service in FY 2023 will be most impacted. In addition to the rising operating costs mentioned above, new properties will not be eligible forthe hold harmless policy, and therefore, will see a corresponding decrease in their gross rent limits. This will impact a property's ability to underwrite debt *permanently* over the course of the financing. Put simply, properties that would have been feasible on initial analysis will no longer be feasible.

Furthermore, depressed rent levels will cool development work under consideration precisely as the nation faces a growing crisis in LIHTC unit development.

Here is an example of the impact on a sample property in Austin, TX:

5.00%	Interest Rate
30	Amortization
6.51%	Debt Constant

Austin, Texas - General Occupancy New Construction (192 Units)

Supportable Mortgage with 1 Year ACS Data:		*Total*		*Per Unit*
Rental Income	$	3,069,545	$	15,987
Operating Expenses		1,252,702		6,524
Net Operating Income	**$**	**1,816,844**	**$**	**9,463**
Supportable Debt	**$**	**24,280,000**	**$**	**126,458**

Austin, Texas - General Occupancy New Construction (192 Units)

Sources of Funds:		*Total*		*Per Unit*
Freddie Mac Forward Loan	$	24,280,000	$	126,458
Low Income Tax Credit Equity		22,393,254		116,632
Total Source of Funds	**$**	**46,673,254**	**$**	**243,090**
Uses of Funds:		*Total*		*Per Unit*
Acquisition Costs	$	3,750,000	$	19,531
Construction Costs		35,500,000		184,896
Lender or Investor Cash Reserves		3,630,203		18,907
Professional Services		2,214,500		11,534
Financing Costs		1,542,047		8,031
Funding Excess (Gap)		36,504		190
Total Use of Funds	**$**	**46,673,254**	**$**	**243,090**

-3.71%	Impact of Five Year

Austin, Texas - General Occupancy New Construction (192 Units)

Supportable Mortgage with 5 Year ACS Data:		*Total*		*Per Unit*
Rental Income	$	2,955,665	$	15,394
Operating Expenses		1,252,702		6,524
Net Operating Income	**$**	**1,702,963**	**$**	**8,870**
Supportable Debt	**$**	**22,760,000**	**$**	**118,542**

Austin, Texas - General Occupancy New Construction (192 Units)

Sources of Funds:		*Total*		*Per Unit*
Freddie Mac Forward Loan	$	22,760,000	$	118,542
Low Income Tax Credit Equity		22,393,254		116,632
Total Source of Funds	**$**	**45,153,254**	**$**	**235,173**
Uses of Funds:		*Total*		*Per Unit*
Acquisition Costs	$	3,750,000	$	19,531
Construction Costs		35,500,000		184,896
Lender or Investor Cash Reserves		3,630,203		18,907
Professional Services		2,214,500		11,534
Financing Costs		1,542,047		8,031
Funding Excess (Gap)		(1,483,496)		(7,727)
Total Use of Funds	**$**	**45,153,254**	**$**	**235,173**

As demonstrated in the above sample property, assuming a 5% interest rate and a 30-year loan amortization, a new construction property in Austin, Texas would experience an estimated $8,000 decrease in supportable mortgage proceeds per unit if the 5-year ACS data is used as the basis of 2023 income limits. Under this scenario, to remain financially viable, the property must reduce the costs by the corresponding reduction in sources of funds. Controllable uses of funds are primarily tied to construction costs and land acquisition costs. Since land purchase prices are set by the full market, with competition from developers that do not have rent restrictions, that significant factor is also not controllable. The only option to make such developments work, is to lower construction costs for affordable properties by reducing unit quality through less durable appliances, smaller unit sizes, and diminished common spaces. In addition to tenants potentially living in smaller, less desirable units, social programs that benefit tenants will potentially be cut to keep a property financially solvent.

While paring construction costs to the bone may be possible in some cases, in many others, the incentive for investment is lost and overall production of affordable housing will suffer. In the states where LIHTC development is already limited, this change would render such developments next to impossible.

Deriving an alternate methodology for determining 2023 income limits would result in a sustained quality of life for residents of low-income housing and an increased property tax base for local municipalities at no cost to the Department of Housing and Urban Development.

Suggested Remedies

The Income Limits Working Group suggests three alternative approaches to using the five-year data to calculate median income for HUD FY 2023:

1. Use Census Bureau 2020 Experimental Data
2. Average the 2019 and 2021 ACS Data
3. Trend the 2019 ACS to 2023 using the Consumer Price Index (CPI)

<u>Use Census Bureau 2020 Experimental Data</u>

Although the Census Bureau has only made the 2020 Experimental Data available publicly for states and Private Use Microdata Sample, we would encourage HUD to continue to work with the Census Bureau to be provided access to the experimental data on a county basis.

This approach would yield calculations that are most in line with how HUD has previously calculated income limits and would more closely reflect the change in incomes at the metropolitan statistical area, HUD Metropolitan Fair Market Rent Area, and county level.

<u>Average 2019 and 2021 ACS</u>

If HUD is unable to access the Census Bureau 2020 Experimental Data, another alternative would be to use an average of the 2019 ACS and the 2021 ACS. This would serve to still tie the 2023 income limits to ACS data for the specific area. It would also help avoid an estimate that does not match the underlying economics of the area that may result in large corrections in 2024.

The Income Limits Working Group, understands that due to the timing of the release of the 2021 ACS data that the 2023 income limits may be delayed while the average is calculated. However, any potential delay in the release of income limits could be mitigated by the fact that only those areas that rely on theone-year ACS will need to have this adjustment. The one-year ACS is typically released in September.

HUD would not need to wait for the 2021 five-year ACS that is generally released in December as they could use the 2020 five-year ACS data that is anticipated to be released in March 2022.

The calculation of area median income would be as follows:

(20219 ACS +2021 ACS)/2 = Imputed 2020 ACS

Imputed 2020 ACS * (2023 CPI/2020 CPI)

<u>Trend the 2019 ACS to 2023 using CPI</u>

If the previous two suggestions are not possible, the income limits should be based on the last year thatone-year ACS data was available and trended forward to 2023 using a CPI trend factor. This will help avoid the up and down of shifting to a five-year ACS, will reflect the changes in inflation between the 2019 estimate and the 2023 limit and is in line with how HUD currently trends ACS data.

The calculation of area median income would be as follows:

2019 ACS * (2023 CPI/2019 CPI)

Conclusion

We thank you for your time in reviewing this letter and considering our proposals. We would be happy to discuss these proposals and any questions or concerns you may have. Income limits are a critical component of the LIHTC and tax-exempt bond programs. If the lack of data would result in an artificial decrease in the income limits, the burden would be felt by both tenants and property owners.

Yours very truly,
Novogradac & Company LLP

By: Thomas Stagg, Partner

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