

## **Losses Stall Affordable-Housing Projects**

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Affordable housing is the latest victim of the credit crunch that is reverberating through financial markets.

Projects are being canceled because some of the nation's largest financial companies, including Fannie Mae, Freddie Mac and Bank of America, have scaled back their participation in the federal government's largest and most prolific affordable housing tax-credit program, designed to boost construction of below-market-rent apartments.

Carlisle Development Group, a developer that manages 6,000 government-subsidized units in Florida, recently shelved the first phase of a \$100 million project it was planning in Miami with the local YMCA. It would have provided 355 affordable housing units. The housing authority in Pueblo, Colo., delayed a 25-unit project for senior citizens this week. Developers report similar tales around the country.

Reeling from losses in the housing and credit markets, U.S. financial giants are without profits that need shielding from taxes and therefore don't need tax credits. With few buyers, the value of tax credits has declined sharply, leaving a funding gap for developers.

The low-income housing tax-credit program was created in 1986 and has financed the construction of more than a million below-market rate apartments. It is considered one of the most successful federal housing programs that melds aspects of government subsidy with free-market enterprise. Both for-profit and nonprofit developers receive between 30% and 65% of a project's cost via tax credits in return for agreeing to keep rents within reach of residents who earn below 60% of an area's median income. Projects serve the homeless and mentally ill, as well as low-income professionals. The rent restrictions last from 15 to 40 years. Projects under the program have had a very low default rate.

The credits are allocated to states based on population and are distributed to developers by state housing finance agencies. The developers sell the credits to middlemen called syndicators, who in turn sell the credits to investors. Most investors are typically financial institutions looking to shield profit from taxes and to comply with federal requirements to invest in communities that banks had shunned in the past.

"Fannie and Freddie and a number of the major banks are either not in the market or are reassessing" how much they will invest, says Richard Richman, founder of the Richman Group, a tax-credit syndicator and developer of low-income housing. He says the lack of equity has "caused a shock to the marketplace. Now it's not even a matter of the pricing. It's even the availability of equity."

Also depressing Fannie Mae's appetite for the credits is that its financial condition could make it subject to the corporate alternative minimum tax, a provision of the tax code that blunts the effectiveness of tax credits. "Because of the net loss we recorded in 2007, there is an increased risk that we may not be able to fully utilize these tax credits" it said in Feb 27 federal filing.

Ed Neill, a Fannie Mae senior vice president says: "As with other investors in this market, we periodically adjust our levels of new investments and our levels of sales of [tax credits] to correspond to our current corporate tax liability."

Elizabeth Hersch, executive director of the Housing Alliance of Pennsylvania, says the tumult comes as the slack economy and foreclosure crisis dumps folks into the low end of the rental market. "The tax-credit program has been the one production program that has increased supply at the low end. If we see decline now, it's piling disaster on top of disaster."

Fred Copeman, national director of Ernst & Young's tax-credit practice in Boston, estimates 40% of the equity in what annually is usually an \$8 billion market went away in the past six months. Developers across the country, he says, are "twisting on the vine."

"I've got a lot of screwed up tax-credit deals," says Matthew Greer, chief executive of Carlisle. On the YMCA project, he qualified for \$74 million in tax credits but the investor who had committed to taking the credits walked away. "There's lack of liquidity," says Mr. Greer.

Frank Pacheco, executive director of the Pueblo Housing Authority put a senior-citizen development on hold this week after pricing on tax credits came in 8% lower than expected. He had planned to start construction in April. "It would have been great," he said.

Like other groups, his only hope now is to secure gap financing, such as grants from local governments or private foundations. In his case, he's looking to make the projects qualify for a separate federal rent subsidy program. Meanwhile, his group put another project that's in an earlier stage of development on the shelf. "We won't even talk about that until this thing straightens out," he says.

In recent years, investors would pay upward of 95 cents per dollar of tax credit, in some cases even paying above par value.

Now credits are being priced as low as 79 cents per dollar of credit. For example, last year a developer who was awarded \$1 million in tax credits could expect to get an investor to pay 95 cents per dollar of credit, yielding \$950,000 for the project. Today, an investor might pay 79 cents, yielding just \$790,000.

Fannie Mae and Freddie Mac were the largest investors in the credits, together snatching up 40% of the available credits in recent years, according to syndicators. Fannie Mae had \$8.1 billion worth of unused credits stockpiled according to a Feb. 27 company filing. When the companies pulled back from the market last year, the moves sent prices tumbling and created a situation where some projects are having trouble attracting investors at all.

The logjam in tax-credit investing is similar to the crunch in the debt markets. "If I'm an investor there's nothing really compelling me to come into the market when pricing is unsettled," says Mr. Copeman of Ernst & Young. "Why shouldn't I sit back and wait for some clarity. When will there be clarity? Who knows."

New Orleans, which received a special allocation of credits following Hurricane Katrina, will be particularly hard-hit by the drop in the value of credits. High construction costs and relatively low rents already made it difficult for tax-credit-driven developments to pencil out. Now that the tax credits are worth less, deals are even harder to accomplish.

NHP Foundation, a Washington, D.C., nonprofit developer recently received a \$1 million grant from a state-chartered organization in Louisiana to fill the gap on two projects in New Orleans. "What New Orleans was counting on was that the credits would be highly sought," and have high value, says Ghebre Mehreteab, NHP's chief executive. With values of the credits having dropped, "the only way to meet that gap is through other sources," he says.

Congress has already begun to tackle the issue. The House Ways and Means Committee is considering a bill that would change the governing legislation and could unleash supplemental resources.

#### Corrections & Amplifications

Carlisle Development Group and Biscayne Housing Group will proceed with the first part of a multiphase affordable-housing project in Miami. The later phases were put in danger -- but not canceled -- when investors withdrew earlier commitments to fund the project. This article incorrectly said the first phase had been shelved.