JLARC
JOINT LEGISLATIVE AUDIT AND REVIEW COMMISSION

December 13, 2021

Affordable Housing in Virginia

Commission Briefing

Study resolution

- Review of Virginia's affordable housing needs, including:
  - rent and cost burden across the state
  - demand for affordable housing versus supply
  - impacts of lack of affordable housing
  - factors that may constrain housing supply
  - effectiveness of existing affordable housing programs
  - coordination of state and local entities on housing policy

Commission resolution (November 2020)

Primary research activities

- Analyzed data on housing cost burden, housing demand versus supply, and housing loan programs
- Interviews
  - Staff at Virginia Housing, DHCD, and other state agencies
  - Local planning staff and public housing agency staff
  - Other Virginia housing stakeholders, including developers
  - State and national academic experts and U.S. Department of Housing and Urban Development
- Surveyed local government planning departments
- Contracted with consultant, CSG Advisors, for financial analysis of Virginia Housing's REACH program

In brief

Nearly 30% of VA households are cost burdened.

VA has a shortage of at least 200K affordable rental units, mostly in the "urban crescent" but also in rural areas.

Virginia Housing could contribute more to its affordable housing fund, better support increasing state's rental housing inventory, and improve assistance with homebuyers' upfront mortgage costs.

Not enough land is zoned to allow or encourage development of affordable housing, particularly in fast-growing localities.

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Background

Virginia's affordable housing needs

Resources to address affordable housing needs

Affordable rental housing

Affordable homeownership

Impact of local zoning on availability of affordable housing

Housing stability can affect health, education, and economic outcomes

- Housing stable households have affordable, safe, quality housing that meets their needs
- Housing unstable households have worse health and educational outcomes and spend less on food, transportation, and healthcare
- Housing affordability is important for housing stability
  - Cost burdened households spend more than 30% of their income on housing
  - Severely cost burdened households spend more than 50% of their income on housing
  - Households renting their home more likely to be cost burdened than households owning their home

DHCD is lead state agency for housing programs

- Reports to secretary of commerce and trade
- Administers several programs that receive federal funds
  - e.g., National Housing Trust Fund, HOME Investment Partnerships, and Community Development Block Grant
- Administers the Virginia Rent Relief Program, which has distributed over $506 million to over 60,000 households (since June 2020)
  - Provides subsidies for renters struggling to pay rent as a result of the pandemic
  - Virginia Housing launched mortgage relief program

*DHCD: Department of Housing and Community Development

DHCD administers the Virginia Housing Trust Fund

- General Assembly created in 2012 to facilitate affordable housing development
- Largest ever appropriation ($71M) to VHTF in FY21
  - Between FY14 and FY20, VHTF received $63M
- Finances affordable housing development (80%) and provides services to households experiencing homelessness (up to 20%)
  - Over 2,800 affordable housing units produced in FY21 ($24M)
  - Provided $6.4M for Homeless Reduction Grants in FY21 for services to 859 households experiencing homelessness

Virginia Housing is state's housing finance agency

- Independent authority created in 1972 to expand quality affordable housing to low and middle income Virginians
- Acts as a bank for affordable housing financing
  - Funds programs through sale of bonds and mortgage-backed securities
  - Provided $2.2 billion in financing in FY21
- Finances affordable multi-family rental developments and administers Low Income Housing Tax Credit (LIHTC)
  - Financed over 32,000 affordable units since 2013
- Helps low and middle income Virginians afford homeownership (8,500 mortgages in FY21)

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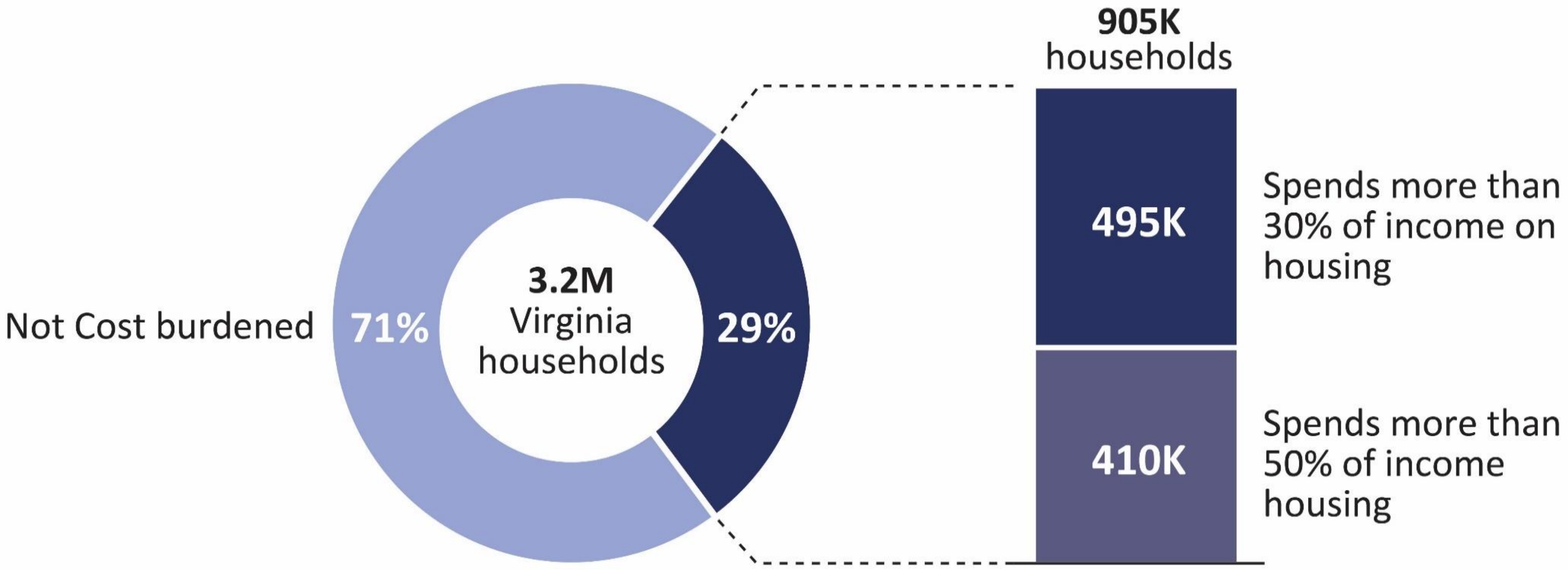
Finding

Nearly 30 percent of Virginians are cost burdened by their housing.

Almost 30 percent of Virginia households are housing cost burdened



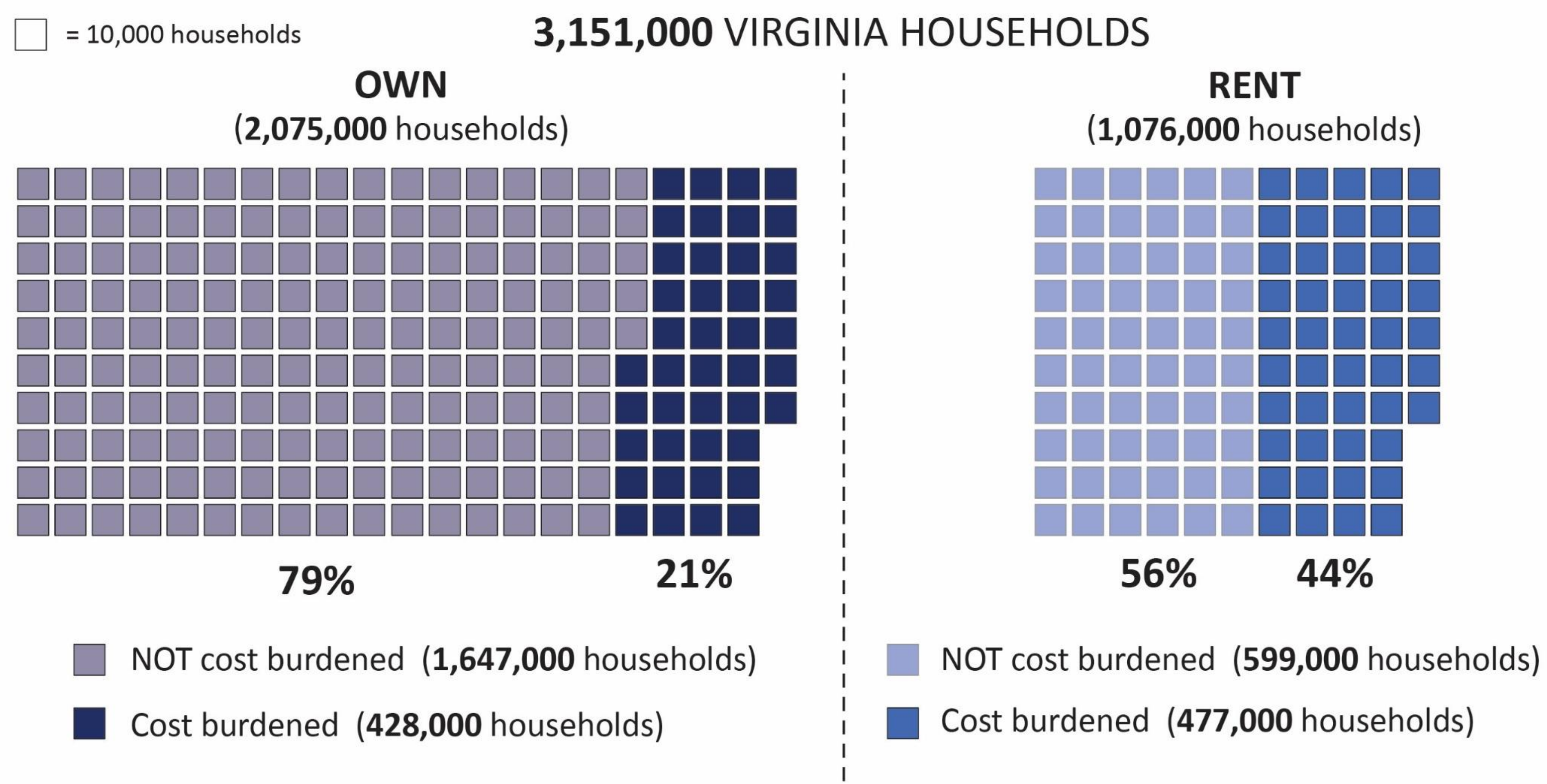
Source: JLARC analysis of American Community Survey, 5-year data, 2015-2019.

Many common occupations have low incomes that increase likelihood of cost burden

	% of AMI	Max income for 1 person	Max income for 4 people	Common occupations
Extremely low income	Up to 30%	$19K	$28K	Hourly part-time workers
Very low income	31% to 50%	$32K	$46K	Custodians, teaching assistants, home health aides, waiters, cashiers (assumes full-time work)
Low income	51% to 80%	$51K	$73K	Licensed practical nurses, bus drivers, auto mechanics, paramedics
Middle income	81% to 100%	$64K	$92K	Police officers, firefighters, electricians

Source: JLARC analysis of Bureau of Labor Statistics Wage Data by Area and Occupation for Virginia in 2020 and HUD FY20 Income Limits Summary.
Note: Incomes and Area Median Income (AMI) are the statewide median, actual limits vary by locality.

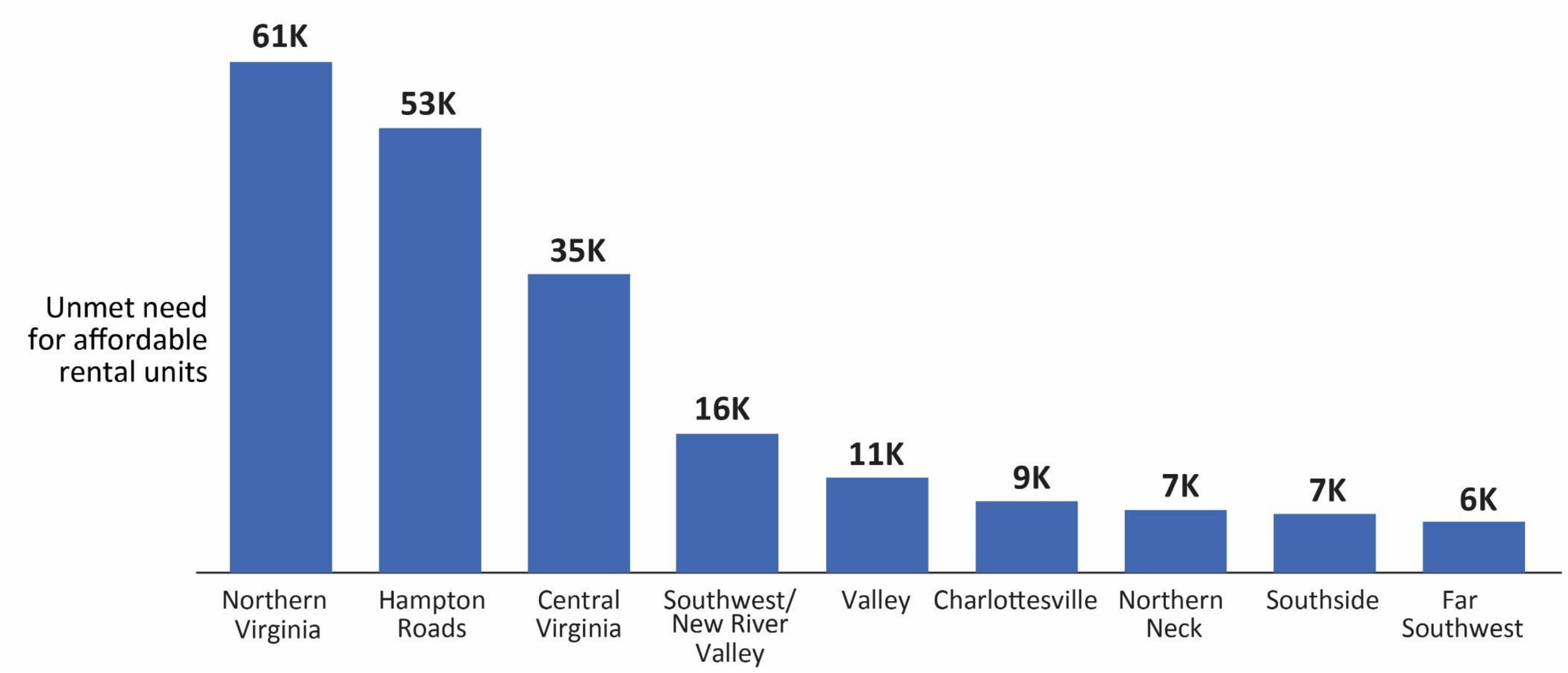
Higher proportion of renter households are cost burdened than owner households



Finding

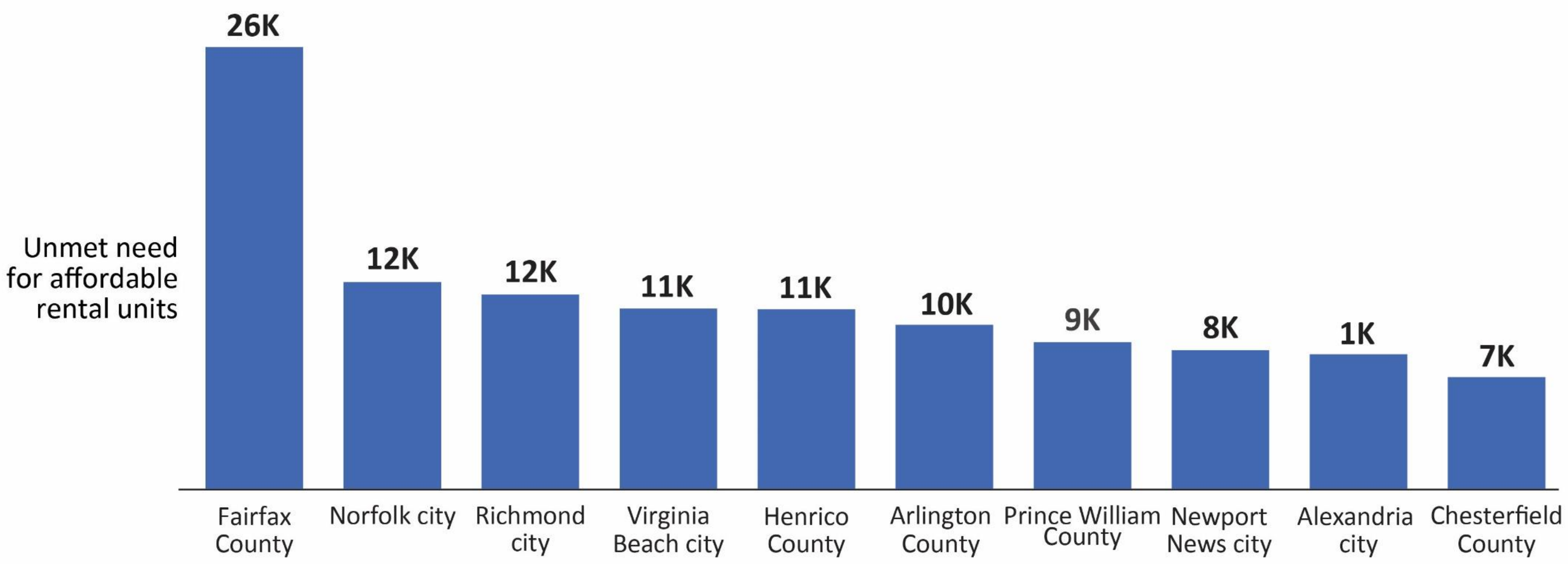
Virginia has a shortage of housing available for lower income households.

Shortage of at least 200,000 affordable rental units statewide



Source: JLARC analysis of American Community Survey, 5-year data, 2015–2019.

Over 50 percent of needed affordable rental units are in 10 localities



Source: JLARC analysis of American Community Survey, 5-year data, 2015–2019.

Rising home prices have put homeownership out of reach for some Virginians

- Homeowners are less likely to be cost burdened than renters, even at the same income levels
- Home prices have increased sharply, especially in the past year
  - Median home price increased 32% between 2016 and 2021, from $204,000 to $270,000
  - Prices have increased 15% in the past year alone from $234,000 to $270,000
- Percentage of Virginia renters who could afford to purchase a home declined from 28% in 2016 to 19% in 2021

Note: Home prices are adjusted for inflation.

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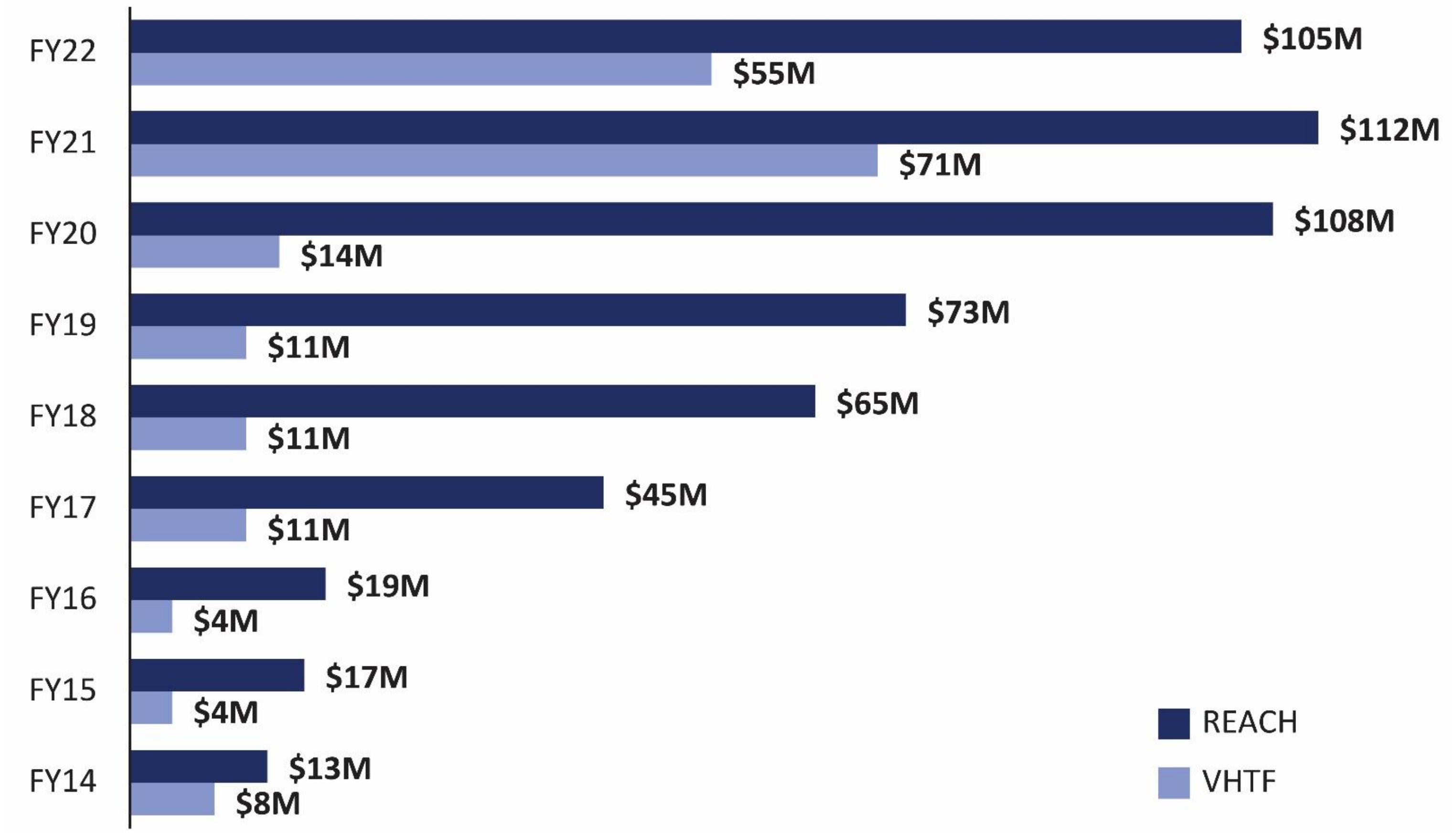
Two state-level discretionary funds are available to expand affordable housing

- Virginia Housing Trust Fund (VHTF)
  - Administered by DHCD
  - Receives annual contribution from general funds
  - Provides (i) financing for affordable housing development (80%) and (ii) grants for homelessness services (20%)
- Resources to Enable Affordable Community Housing (REACH)
  - Administered by Virginia Housing
  - Funded with a portion of the authority's average annual net income
  - Used to promote homeownership, affordable rental housing development, and community outreach projects

REACH is a larger resource for affordable housing than the VHTF



Note: Amounts are annual contributions to each fund, not balances. REACH amounts include additional amounts associated with the Amazon HQ2 project in FY20–22.

Virginia Housing has considerable financial strength

- Virginia Housing's purpose is to finance affordable housing and address the state's housing needs
- Virginia Housing has considerable financial strength
  - One of the largest net asset balances, $3.7 billion, of any state housing finance agency
  - One of the highest producing housing finance agencies in the country for both single-family loans & multifamily rental loans
- JLARC hired CSG Advisors, a national expert in housing finance, to help determine whether Virginia Housing could afford to contribute more funds to affordable housing through REACH

Finding

Virginia Housing can afford to contribute more to the REACH program.

Virginia Housing's REACH allocation formula unnecessarily lowers contributions to the program

CURRENT REACH FORMULA	PROPOSED REACH FORMULA
$100M Total revenue	**$100M** Total revenue
− **$8M** Programmatic and administrative expenses	− **$8M** Programmatic and administrative expenses
− **$20M** REACH grant awards	
$72M Net income (after grants)	**$92M** Net income (before grants)
X **60%** = **$43M** REACH allocation	X **60%** = **$55M** REACH allocation

- Virginia Housing could commit an additional $230 million to REACH by FY31 by not counting grants as an expense in its formula

Note: Hypothetical example for illustration purposes only. REACH grant amounts must be counted as an expense for accounting purposes and in financial documents, but accounting rules do not apply to the formula.

Virginia Housing could afford to contribute a higher percentage of net income to REACH

- Virginia Housing has enough financial strength to contribute 75 percent of its net income, *before grants*, to REACH
- Virginia Housing's net assets would continue to grow under the proposed formula
- CSG Advisors recommends that Virginia Housing first change its formula to use net income before grants in FY23 and then change its contribution percentage to 75% in FY25
- Increasing the contribution percentage to 75% would result in an additional $102 million allocated to REACH by FY31

Recommendations

Virginia Housing should adjust its methodology for calculating annual allocations to REACH so that the net income used as the basis for the annual allocation is not reduced by REACH grants awarded in a previous year.

Virginia Housing should increase from 60 to 75 percent the proportion of its net income allocated to REACH.

Finding

Virginia does not consistently assess or plan for statewide housing needs, inhibiting strategic investment of state resources.

Affordable housing strategy is piecemeal, inefficient compared to some other states

- Current approach to identifying and planning for housing needs is decentralized and reliant on local governments
- Most local governments limit affordable housing planning to content required in comprehensive plans
  - Only a handful have conducted more comprehensive housing assessments
- Other states conduct periodic statewide assessments of housing needs and outline specific strategies and measurable goals for addressing them
  - Maryland and Oregon

Recommendations

General Assembly may wish to consider requiring DHCD to

- conduct a comprehensive housing needs assessment every 5 years,
- develop a statewide housing plan with measurable goals,
- provide annual updates to the General Assembly on progress, and
- update the plan at least every 5 years.

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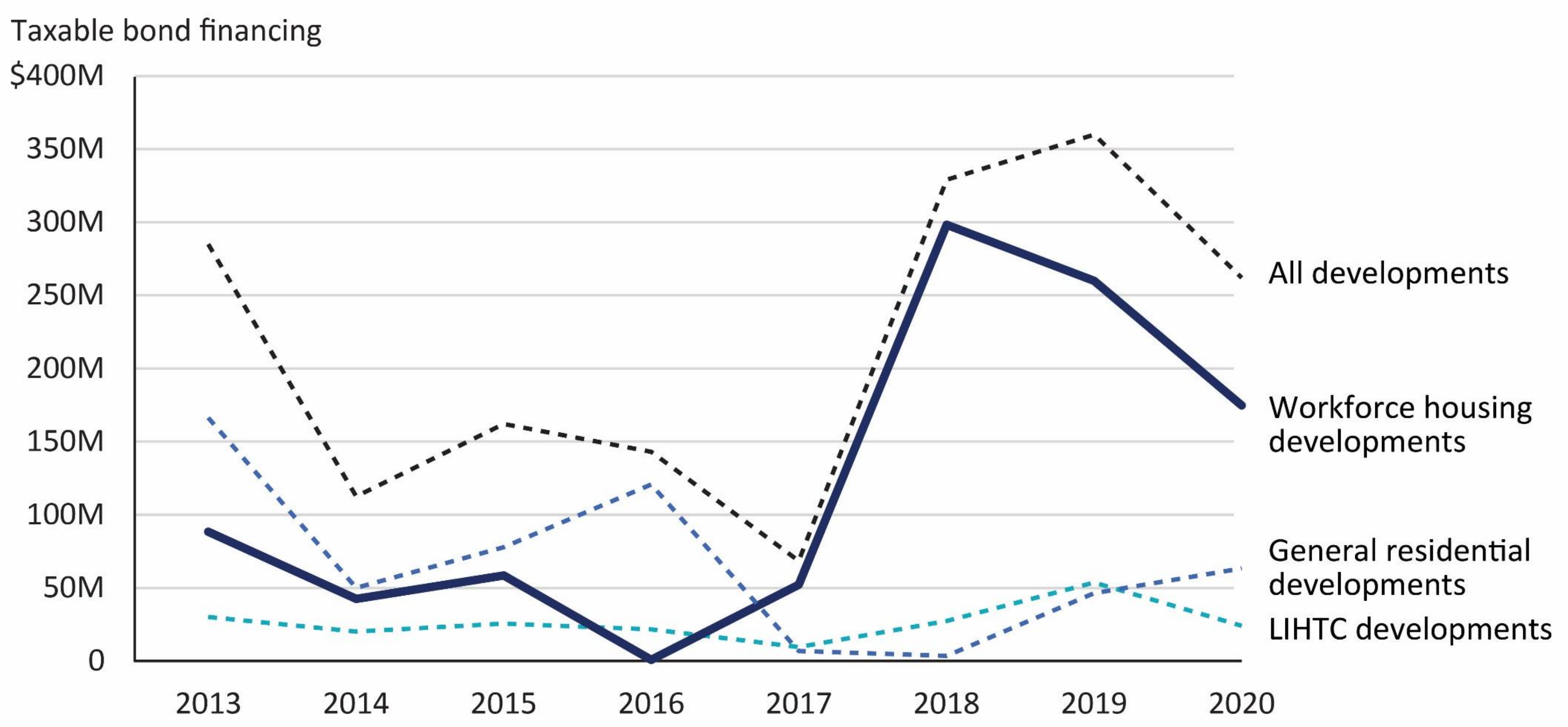
Virginia Housing's financing programs use a mix of funds to create a range of affordable units

	LIHTC credits	Tax-exempt bond financing	Taxable bond financing	REACH subsidy	Affordability requirements
9% LIHTC projects	✓		✓	✓	**20%** of units — Households at or below **50%** of AMI or **40%** of units — Households at or below **60%** of AMI
4% LIHTC projects	✓	✓		✓	
Workforce housing projects			✓	✓	**20%** of units — Households at or below **80%** of AMI
General residential projects			✓		**100%** of units — Households at or below **150%** of AMI

Finding

Virginia Housing's "workforce housing" program units are not affordable to all lower income residents for whom units are reserved.

Virginia Housing has substantially increased its investments in workforce housing development



Not all workforce housing units are affordable to the households they are reserved for

- Workforce housing program requires developers to set aside *income*-restricted units, not *rent*-restricted units
- Income-restricted units had only slightly lower average rents
  - $15 less per month for one-bedroom units
  - $40 less per month for two-bedroom
- Median rent burden for residents in income-restricted units is no lower than the statewide median (32 percent)

Recommendations

General Assembly may wish to consider requiring that 20 percent of units in workforce housing developments be reserved for and have rents that are affordable to households earning 80 percent and below area median income.

Virginia Housing should increase its REACH subsidy for workforce housing developments to ensure they remain financially feasible under a rent restriction requirement.

Finding

Virginia Housing does not maximize use of private activity bonds or the REACH program to increase inventory of affordable rental units.

Using private activity bonds for affordable rental housing draws down additional federal funds

- Private activity bonds are federally regulated, tax-exempt bonds issued by state and local governments
  - Lower borrowing cost for developers
  - Federal government caps the dollar amount of private activity bonds that can be issued in each state annually
- Affordable rental housing developments financed with private activity bonds are eligible for 4% LIHTC credits
- Majority of Virginia's private activity bonds are used for mortgage credit certificates, not expanding rental housing inventory

REACH funds could facilitate use of private activity bonds for rental development

- Developers and Virginia Housing staff reported that more private activity bond rental projects would be feasible with funding from other sources
  - Pairing with 4-percent tax credit funding is insufficient
- Virginia Housing could use REACH as additional funding
  - $49 million in unspent REACH rental funds since 2016
- Would be a more strategic use of private activity bonds than mortgage credit certificates: addresses lack of affordable rentals and draws down federal funding

Recommendation

Virginia Housing should:

- use REACH funds to help finance affordable rental housing projects that use tax-exempt private activity bonds and 4 percent LIHTC credits and
- report REACH use on these projects and units created to its Board of Commissioners.

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Finding

Virginia Housing effectively helps low- and middle-income Virginians qualify for and afford a mortgage and effectively prevents foreclosure against its borrowers.

Virginia Housing issues mortgages to Virginians less likely to qualify in the commercial market

	Virginia Housing	Commercial market
Income	$62,000	$88,100
Combined loan-to-value ratio	100%	95%
Percentage of borrowers with high debt-to-income ratio	71%	59%
Percentage of first-time home buyers	90%	50–55%
Median credit score	688	729

Note: Income, combined loan-to-value, and debt-to-income are compared to VA market. First-time homebuyer and credit score are compared to national market.

Virginia Housing has a lower foreclosure rate compared to the commercial market

- Virginia Housing's delinquency rate has been higher than the national average
  - In line with Virginia Housing's riskier borrower pool
- However, Virginia Housing's foreclosure rate averaged 0.14% since 2015
  - Virginia Housing's foreclosure rate is lower than the state (0.56%) and national (1.24%) average foreclosure rates

Finding

State law requires Virginia Housing to establish interest rates as low as possible, but its interest rates are slightly higher than rates offered through the commercial market.

Majority of Virginia Housing's borrowers have higher interest rates than commercial borrowers

- 75% of Virginia Housing borrowers have slightly higher interest rates than comparable borrowers from other institutions*
- Amounts to $20–$30 more on average per month or $7K to $11K over 30 years
  - Average of 8 basis points higher per loan
- State law requires Virginia Housing to set interest rates at the lowest possible level

*Controlled for income, debt-to-income ratio, loan-to-value ratio, other relevant demographic factors

Virginia Housing's Plus mortgage pricing policy increases interest rates

- Virginia Housing offers "Plus mortgages" to homebuyers who need help affording upfront costs
  - Provides up to 5% of the purchase price in the form of a second mortgage
  - Used to pay for down payments and/or closing costs
- Virginia Housing adds between 12.5 and 25 basis points to the interest rates for borrowers who receive a Plus mortgage
- According to Virginia Housing staff, the upward interest rate adjustment is meant to cover the risk and expense of originating and servicing the Plus mortgage

Recommendations

Virginia Housing should

- determine whether Plus mortgage pricing adjustment policy is necessary, and, if so, what the minimum basis point adjustment should be and
- provide annual reports to the Board of Commissioners comparing its interest rates to commercial interest rates, & present options to lower rates when its rates are higher than comparable commercial market rate.

The General Assembly may wish to direct Virginia Housing to conduct a financial analysis to determine whether it could offer lower interest rates than commercial market.

Finding

Virginia Housing Plus mortgages cover borrowers' upfront home purchase costs but increase borrowers' debt.

Plus mortgages are more attractive for homebuyers than grants but increase debt

- Down payments and closing costs combined are at least 5% of the cost of a mortgage
- Plus mortgages cover more or all of these costs
- Plus mortgage adds about $17,000 to a borrower’s loan cost over 30 years
- Virginia Housing offers grants as an alternative to Plus mortgages for lower income borrowers, but they don’t fully cover upfront costs

Replacing the down payment assistance program could reduce costs for borrowers

- Virginia Housing could offer larger grants, OR
- Virginia Housing could replace the Plus mortgage with a 0% interest deferred second mortgage
- Both offer considerable savings for low-income borrowers compared to the Plus mortgage
  - Between $12K and $22K over a 30-year mortgage
- Plus mortgages appear to generate relatively modest revenue for Virginia Housing
  - 10-year impact on REACH would be less than 2%

Note: Current down payment assistance grants cover up to 2.5% of the purchase price. A larger grant would cover up to 5% of the purchase price, like the current Plus mortgage.

Recommendation

Virginia Housing should modify its down payment assistance program so that upfront costs are more fully covered for lower income borrowers.

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Zoning sets standards for new development

ZONING PURPOSE	CONSIDERATIONS FOR LOCALITIES		DEVELOPMENT CONSIDERATIONS
Designate what can and cannot be built in each zone	Localities may set a rural growth boundary.	Localities decide how much single-family and multifamily housing development they will allow.	Zoning determines whether multiple types of housing at multiple price points can be built in the same area.
Set standards and limits for construction by structure type and zone	Localities determine the maximum allowable building height in different zones.	Localities determine how far buildings must be set back from the street.	Zoning determines how many housing units can be built on a given piece of land.
Lay out the process by which local governments approve new development	Localities decide what type of development will be allowed by right in different zones.	Localities decide what type of development will require special exceptions or rezoning before it is approved.	Zoning determines what type of development is most likely to be approved by a locality.

Finding

Existing zoning ordinances constrain development of new affordable housing, especially in Virginia's fastest-growing localities.

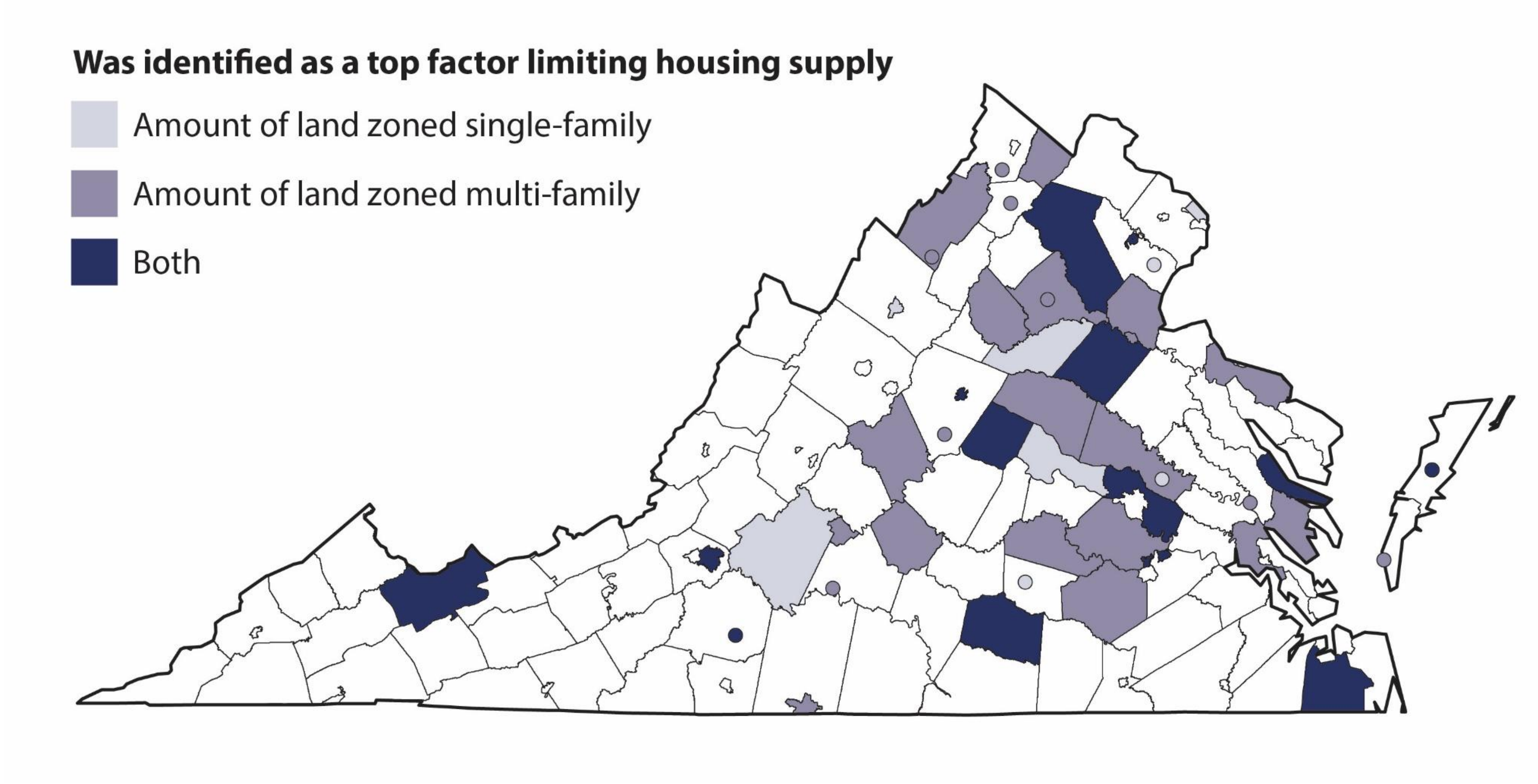
Proposed developments that require rezoning cost more and are riskier for developers

- Developments that comply with zoning ordinances ("by right" developments) are easily approved by localities
- Expanding a locality's affordable housing may require rezoning if existing zoning ordinances are too restrictive
  - Requirements that may prevent affordable housing development include requiring certain lot sizes or set-backs, prohibiting multifamily development, or restricting building heights
- Rezoning requires developers to take on additional costs (legal or consultant fees, prolonged payment of property taxes while rezoning is considered)
  - Estimated to range from $250K to $1M per development

Virginia stakeholders report that zoning is a barrier to housing development

- Developers, local planners, and national experts report that restrictive zoning prevents needed development
- There is not enough land already zoned to meet localities' affordable housing development needs
  - 62% of local planners said existing by-right development would meet only a portion of housing needs
  - 19% said it would meet none of their housing needs

Thirty percent of localities reported that zoning was a top factor constraining housing supply



Localities with more population growth, higher housing costs reported zoning constraints

	Average population growth rate	Average median home sale price	Average median rent payment
Reported zoning constraint	7.0%	$313,850	$1,083
Did not report zoning constraint	0.8	237,100	921
Statewide	3.0	261,727	984

Small amount of land zoned for multifamily development in most localities

- Most localities reported that 25% or less of the land in their locality was zoned for multifamily
  - This included localities with a large unmet need for affordable rental units

Proportion of developable land zoned for multifamily developments	Percentage of cities and counties
25% or less	77%
26% to 50%	15
51% to 75%	5
More than 75%	3

Increasing the amount of land developable by right is discouraged by proffer structure

- Any housing development brings costs to the locality—costs include transportation, roads, schools, public safety, and parks
- Developers can voluntarily offer fees, “proffers,” to the locality during the rezoning process
  - Proffers are intended to offset localities’ costs from development, specifically for transportation facilities, public safety facilities, public school facilities, and public parks
- Proffers can only be offered if rezoning occurs

Recommendation

General Assembly may wish to consider directing DHCD to evaluate how to structure, administer, and fund an incentive program to encourage localities to adopt zoning policies to facilitate affordable housing development.

Inclusionary zoning policies can be effective tools for increasing affordable housing supply

- Inclusionary zoning policies either require or allow developers to include a certain number of affordable units in any new development
- In exchange for including affordable units, developers receive an incentive
  - Ability to build more units, parking requirement waivers
- Other states and some Virginia localities have implemented inclusionary zoning policies

Seven Virginia localities authorized to implement mandatory inclusionary zoning policies

- All Virginia localities have authority to implement inclusionary zoning policies, called "affordable dwelling unit ordinances"
  - Voluntary for developers to participate, unless locality is given authority in state law to mandate participation
- Seven localities have authority to implement mandatory inclusionary zoning policies
  - Research shows that mandatory inclusionary zoning policies are most effective

High-cost, high-growth localities could benefit from mandatory inclusionary zoning

- Inclusionary zoning policies work best in high-cost, high-growth housing markets
- Localities currently with authority to implement mandatory inclusionary zoning are high-cost and high-growth
- Some other localities have equally high housing costs and population growth rates
- High-cost and high-growth localities were most likely to report zoning constraints

Policy option to consider

General Assembly could grant localities with population growth rates, median home sales prices, and median rents in the top quartile of state the authority to adopt mandatory inclusionary zoning policies.

Key findings

Nearly 30% of VA households are cost burdened.

VA has a shortage of at least 200K affordable rental units, mostly in the "urban crescent" but also in rural areas.

Virginia Housing could contribute more to its affordable housing fund, better support increasing state's rental housing inventory, and improve assistance with homebuyers' upfront mortgage costs.

Not enough land is zoned to allow or encourage development of affordable housing, particularly in fast-growing localities.

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